

ECONOMICS DICTIONARY

Syllabus 1.5

Terms: 42

Submariner Dictionary: Unit 1 (1.1, 1.2, 1.3 + 3.2)

Term	Definition note the use of key terms to explain the term	Diagram. Probably better to add by hand!	Example. Add examples as appropriate.
Term	Definition:	Diagram to use:	Example:
diseconomies of scale	key efficiency indicator in the long run to highlight higher average unit costs due to inefficiencies		1) managerial
economies of scale	key efficiency indicator in the long run whereby firm gains efficiency in the long run as the firm grows. Efficiency is indicated through lower average unit cost.	LRAC	1) bulk buying 2) marketing 3) financial
law of diminishing returns	DMR(diminishing marginal returns) relates to how output changes (marginal product) as a result of adding one extra unit of input e.g. labour	Total and marginal product diagram.	best explained with a numerical example but you must explain that while total output may still be increasing the marginal output is falling so inefficiency has set in. Note that it is a short run concept as at least 1 fop is fixed.
long run costs	long run is often a period of time (usually more than 1 year but it could be as much as 3 years depending on the industry.		
production function	In economics, a production function relates physical output of a production process to physical inputs or factors of production.		The production function relates the quantity of output of a good/service to a quantity of inputs
short run costs	short run is often a period between 0 and 12 months and is a period when at least ONE of the factors of production is fixed.		typical short run costs are total/average variable costs such as labour and raw materials that clearly increase as o/p increases
production function	In economics, a production function relates physical output of a production process to physical inputs or factors of production.		Essentially the production function relates a quantity of inputs to a specific quantity of output

Term +Explanation**Diagram + Example**

increasing /decreasing returns to scale	Returns to scale is a size of the business concept that looks at the quantity of inputs and outputs resulting from those inputs. If a firm increases inputs it will be keen to measure the growth in outputs and this will partially inform the decision to grow the business or not.		For example if a firm increases its inputs of land, labour and capital by 100% and its outputs increase by 150% then the firm will enjoy increasing returns to scale. The decision to increase the size of the firm is justified. Decreasing returns would result in a 80% increase in output. Constant returns would result in a 100% increase in output.
average cost	average is a key concept in calculating the costs or output of a firm. The formula is $\text{total} / \text{quantity}$. AC is a key concept in the course and can be referred to in the short run and the long run. (Remember the short run in microeconomics is when at least 1 factor of production is fixed.)		AC is typically 'u' shaped. Why? Short run: AC is 'u' shaped because of falling afc (average fixed costs) and rising avc (average variable costs). Remember rising avc are caused by diminishing marginal returns which causes costs to rise in the short run. See Law of Diminishing Returns
total cost	total cost is the addition of all costs/ outputs for a firm. It is the addition of tvc (total variable costs) and tfc (total fixed costs).		Note that the total number is critical as the average and marginal cost is calculated from the total cost
marginal cost	key concept in theory of the firm and marginal cost is the change in total cost as a result of producing one extra of output.		
average output	average output is the total output of units / quantity of units produced		
total output	total output is the total number of goods produced		
marginal output	marginal output is the change in total output as a result of adding one extra unit of input		

Term +Explanation**Diagram + Example**

profit maximisation output	profit maximisation output is a key objective of firms and it occurs where mr (marginal revenue) = mc (marginal cost). Output greater than where $mr=mc$ is a situation where $mr<mc$ i.e. firm is making a loss on each additional unit of output as the cost of producing it is greater than the revenue of that unit.		
supernormal profit	supernormal profit occurs where ar (average revenue) $>$ ac (average cost).		Note that this is sometimes referred to as abnormal profit or excess profit.
normal profit	normal profit is that level of profit sufficient to keep the firm in the industry i.e. $ar = ac$. The firm is covering all of its average costs with its average revenue. The firm is able to pay for all of the factors of production including a level of profit necessary to keep the firm from leaving the industry		
barriers to entry	barriers refer to entry and exit into an industry. Entry barriers reduce levels of competition and therefore can result in higher prices. Exit barriers (e.g. high exit costs where a firm may not be able to sell its assets easily) can also influence the level of entry into the industry.		Large entry costs such as ship or aircraft production can have a significant deterrent effect on the level of competition resulting in a small number of producers e.g. Boeing and Airbus
kinked demand curve	kinked demand curve is a theory that explains why prices may be 'sticky' in an oligopoly because either higher or lower prices in relation to the 'kink' will result in the firm losing total revenue and therefore firms will look to other non price methods to compete in the industry		Firms can use special offers or 'loyalty' campaign to attract customers or advertising campaigns build up customer loyalty and attempt to make demand more inelastic for the product or service.

Term +Explanation**Diagram + Example**

price discrimination	firms can practice price discrimination by selling the same product or service to consumers for a different price		Note that this is common practice with firms as they use a knowledge of elasticity to charge different prices to customers based on their 'need' for the product or service. Off peak use of trains and public transport can favour certain consumer groups such as old age pensioners
natural monopoly	natural monopoly is a situation where the industry is best suited to a single producer due to large structural costs and the existence of two or more producers could lead to inefficient use of resources		railway systems are a typical example where the set up costs are high and a second parallel railway system would be cost inefficient
price taker	price taker' is an interesting concept where the firms has no price power and due to high levels of competition the firm will take the industry price. Consumer demand is elastic here as there are numerous alternative products/services available		
price maker	price maker' is a less competitive situation where the firm is facing inelastic demand and can charge higher prices resulting in higher total revenue		

Term +Explanation

Diagram + Example

[illegible]