

SYLLABUS REFERENCE 2.2 HL EXTENSION: Cost Curves:
Short Run and Long Run Average Total Cost

What is the relationship in Economics between the following:

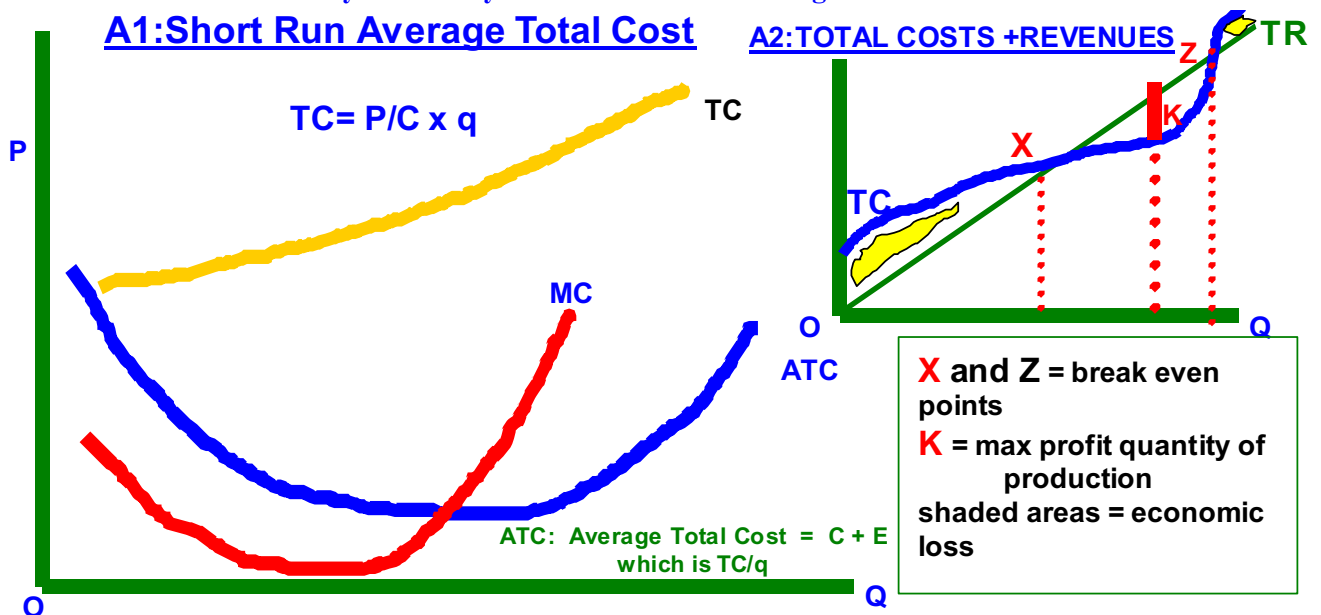
- Total
- Average
- Marginal

Note: marginal applies to revenue, cost and output etc

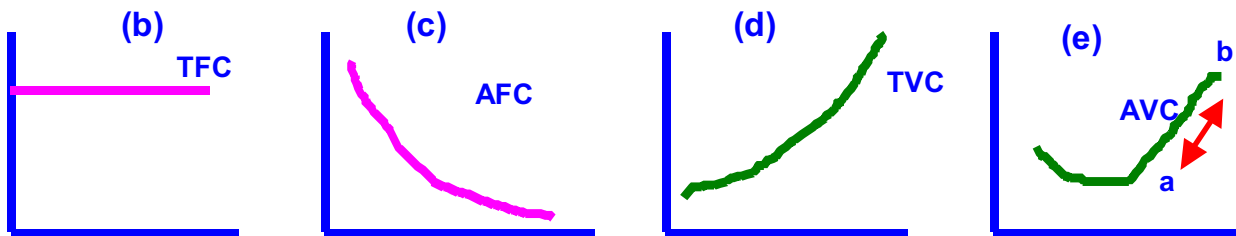
SHORT RUN AND LONG RUN

- Short run = at least one FoP is fixed. This allows for the existence of diminishing marginal returns of scale – see webnote 211 on diminishing marginal returns.
- Long run = all factors variable and therefore the firm can plan the ideal scale/size of operation

Note: the rise from a to b on diagram (e) is caused by diminishing marginal returns. This indicates inefficiency. Too many variable factors are being used with one fixed



X and Z = break even points
K = max profit quantity of production
shaded areas = economic loss

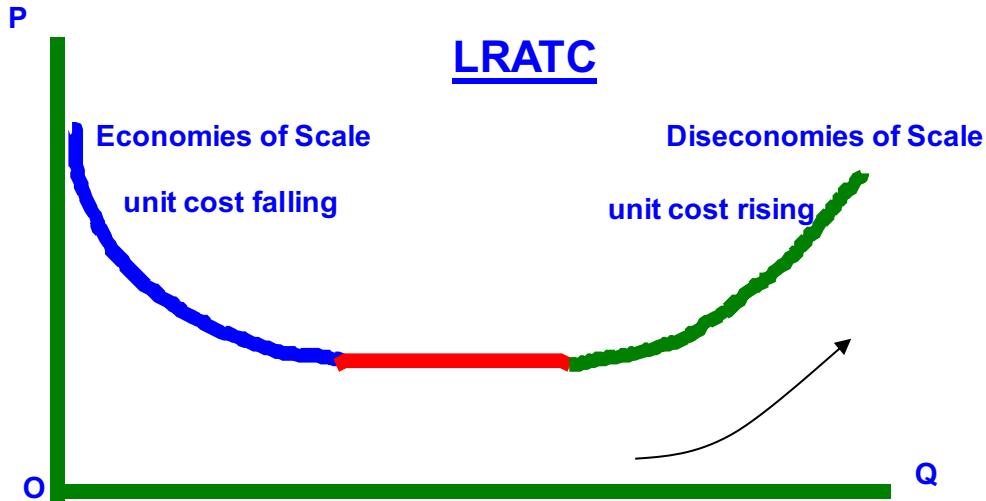


Every Firm must cover its AVC in the Short Run or it must shut down

Note:
 The rise from a to b on diagram (e) above is caused by diminishing marginal returns. See webnote 211. This indicates inefficiency in the short run. Too many variable factors are being used with one fixed factor likely to be capital.

AC in the long run is labelled as LRAC and it has a different set of

F: Long Run ATC Depends on Internal + External (DIS) Economies of Scale



influences known as 'economies of scale'. NB long run in microeconomics is when all factors of production are variable. (no fixed factors as exists in the short run- take a look at the 'Toy Truck' video from welker on the 2.11 webpage.

Note: Growth does not necessarily bring lower cost

Note: no D.M.R. as all FoP's are variable in the long run

Note: see webnote 211 re increasing and decreasing returns to scale

Internal Economies of Scale

1. Technical
2. Marketing
3. Managerial
4. Financial
5. R and D

Max
 efficiency
 =
 productive
 efficiency

Internal Diseconomies of Scale

1. Managerial
2. Technological
3. Labour

External Economies of Scale

1. Education and training
2. Infrastructure
3. Trade Journals/
 publications / seminars
4. R and D
5. Supply firms may relocate

External Diseconomies of Scale

1. Labour shortages
2. Raw material shortages
3. Poor infrastructure
4. Government regulation /
 legislation