Economic & Accounting profit

Found this simple read:

Accounting profit is the profit used by accountants to determine a firm's net income.

Accounting profit = Total revenue - Total accounting costs

Economic profit equals a firm's total revenue minus its total economic costs.

Economic profit = Total revenue - Total economic costs

Economic cost takes into account the total opportunity cost of all factors of production. **Opportunity cost** is the next best alternative forgone in making a decision. It is the unearned or nominal profit that the resource-owner did not make from investing in the next best alternative. As a result, you can have a significant accounting profit with little to no economic profit.

Example

Suppose a person uses his own resources, land, capital, and time in the production of goods. The opportunity costs of these resources are shown below:

Accounting Profit = $55,000
Entrepreneur's own forgone salary = $40,000
Foregone interest on capital = $1,000
Foregone rent = $2,000
Economic Profit = 55,000 - 40,000 - 1,000 - 2,000 = $12,000

For publicly traded corporations, economic profit is accounting profit - required return on equity capital.

When economic profit is zero, a firm's accounting profit becomes **normal profit**, which is effectively the total implicit opportunity cost.

Accounting profit = Economic profit + Normal profit

When a firm's total revenues are just equal to its total costs, its economic profit is zero, but it still makes accounting profit. Zero economic profit does not mean that the firm is about to go out of business. Instead, it just indicates that the owners are receiving exactly the market (normal) rate of return on their investment.