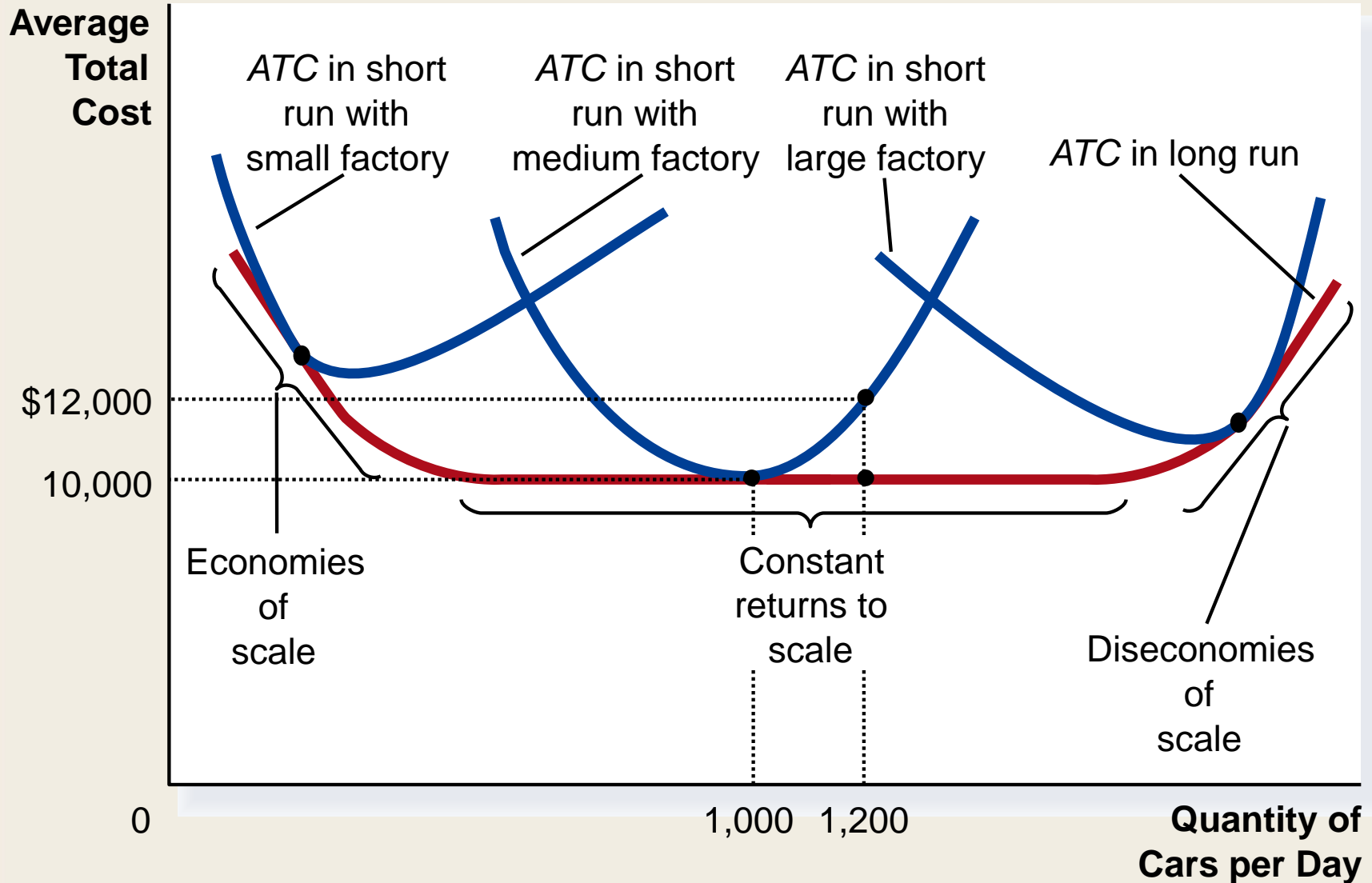


# Economies and Diseconomies of Scale

- *Economies of scale* refer to the property whereby long-run average total cost falls as the quantity of output increases.
- *Diseconomies of scale* refer to the property whereby long-run average total cost rises as the quantity of output increases.
- *Constant returns to scale* refers to the property whereby long-run average total cost stays the same as the quantity of output increases.

# Figure 6 Average Total Cost in the Short and Long Run



# Summary

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- The goal of firms is to maximize profit, which equals total revenue minus total cost.
- When analyzing a firm's behavior, it is important to include all the opportunity costs of production.
- Some opportunity costs are explicit while other opportunity costs are implicit.

# Summary

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- A firm's costs reflect its production process.
  - A typical firm's production function gets flatter as the quantity of input increases, displaying the property of diminishing marginal product.
  - A firm's total costs are divided between fixed and variable costs. Fixed costs do not change when the firm alters the quantity of output produced; variable costs do change as the firm alters quantity of output produced.

# Summary

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- Average total cost is total cost divided by the quantity of output.
- Marginal cost is the amount by which total cost would rise if output were increased by one unit.
- The marginal cost always rises with the quantity of output.
- Average cost first falls as output increases and then rises.

# Summary

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- The average-total-cost curve is U-shaped.
- The marginal-cost curve always crosses the average-total-cost curve at the minimum of ATC.
- A firm's costs often depend on the time horizon being considered.
- In particular, many costs are fixed in the short run but variable in the long run.