## Key Terms

accounting profit

total revenues minus explicit costs, including depreciation

average profit

profit divided by the quantity of output produced; also known as profit margin

average total cost

total cost divided by the quantity of output

average variable cost

variable cost divided by the quantity of output

constant returns to scale

expanding all inputs proportionately does not change the average cost of production

diminishing marginal productivity

general rule that as a firm employs more labor, eventually the amount of additional output produced declines

diseconomies of scale

the long-run average cost of producing output increases as total output increases

economic profit

total revenues minus total costs (explicit plus implicit costs)

economies of scale

the long-run average cost of producing output decreases as total output increases

economies of scale

the long-run average cost of producing output decreases as total output increases

explicit costs

out-of-pocket costs for a firm, for example, payments for wages and salaries, rent, or materials

factors of production (or inputs)

resources that firms use to produce their products, for example, labor and capital

firm

an organization that combines inputs of labor, capital, land, and raw or finished component materials to produce outputs.

fixed cost

cost of the fixed inputs; expenditure that a firm must make before production starts and that does not change regardless of the production level

fixed inputs

factors of production that can’t be easily increased or decreased in a short period of time

implicit costs

opportunity cost of resources already owned by the firm and used in business, for example, expanding a factory onto land already owned

long run

period of time during which all of a firm’s inputs are variable

long-run average cost (LRAC) curve

shows the lowest possible average cost of production, allowing all the inputs to production to vary so that the firm is choosing its production technology

marginal cost

the additional cost of producing one more unit; mathematically,

marginal product

change in a firm’s output when it employees more labor; mathematically,

private enterprise

the ownership of businesses by private individuals

production

the process of combining inputs to produce outputs, ideally of a value greater than the value of the inputs

production function

mathematical equation that tells how much output a firm can produce with given amounts of the inputs

production technologies

alternative methods of combining inputs to produce output

revenue

income from selling a firm’s product; defined as price times quantity sold

short run

period of time during which at least one or more of the firm’s inputs is fixed

short-run average cost (SRAC) curve

the average total cost curve in the short term; shows the total of the average fixed costs and the average variable costs

total cost

the sum of fixed and variable costs of production

total product

synonym for a firm’s output

variable cost

cost of production that increases with the quantity produced; the cost of the variable inputs

variable inputs

factors of production that a firm can easily increase or decrease in a short period of time