Marginal revenue and profit

? In order for a company to be able to reach its full potential financial management must be in place. This management needs to be aware of at least the basics of financial plans which are revenue, cost and profit. These three things can make or break a company. Each of these things must be understood and considered before plans can be laid to create or better a company. Revenue is the amount a company receives (Marginal Revenue, 2009). If a company is in the business of sales, revenue is the amount ofmoneythe company receives per unit sold. Marginal revenue is the amount of money a company receives for the last unit sold.

This is found by dividing the change in revenue by the change in quantity sold. For companies that compete with one another marginal revenue is not very important. This is because in a competitiveenvironmentmost products are sold at a set price so that marginal revenue is equal to the set sales price of the product. For a monopoly on the other hand, marginal revenue is very important. Monopolies have a decreasing marginal revenue curve (marginal Revenue, 2009); for a monopoly the marginal revenue is less than the sales price. This is because a monopoly must have a lower sales price in order to increase the amount of product sold.

Total cost is the amount of money it costs to operate at a particular rate of production (Baker, 2000). There are two types of cost: variable and fixed. Fixed costs are those that remain the same regardless of production and variable costs are those that change with production. Marginal cost is the addition either to total cost or total variable cost resulting from one more unit of output (McConnall & Brue, 2008). Usually this is found by dividing the change in total cost by the change in quantity. Profit is the positive gain from

an investment or business operation after subtracting expenses (Profit, 2009).

Profit maximization is the idea that people will try to create as high a profit as possible given the circumstances. Since marginal revenue is the amount of revenue an additional unit will bring in and marginal cost is the amount the additional unit will cost to produce, then profit maximization is the point where marginal cost and marginal revenue are equal (Profit Maximization, 2009). So as long as marginal cost is lower than marginal revenue there is profit, but if marginal cost ever exceeds marginal revenue the last unit should not be produced. If the marginal revenue is higher than the marginal cost, the company can produce more units.

Business owners and managers need to be able to make a profit. Whenever people think of profit, they are aware that profit is the amount of money left after the expenses are paid and most people know the greater the profit the better off they will be. Most people do not know that profit maximization requires the knowledge of marginal cost and marginal revenue. In order to determine when a company is no longer profiting from production of extra units, one must know that profit maximization is the point where marginal revenue equals marginal cost. Refernces (2009). Marginal revenue: Fundamentalfinance.

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