Average total cost the firm

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Notice that marginal costs fall for production up to 3 units, the region of increasing marginal product of labor. Marginal cost rise thereafter, the region of decreasing marginal product of labor. The short run marginal cost will increase because of decrease in productivity. Average fixed cost will decrease fast in the beginning and slowdown but the decrease will continue because fixed cost will not change with output. The short-run marginal cost curve shout pass through the lowest point of both short-run average total cost and short-run average variable cost.

The optimal point of input is in this example: ‘’3’’, that is when short run marginal cost is in its lowest point. After that the value of added labor starts to decrease. As we can see Average Fixed Costs falls steadily because TFC is spread over larger output levels and thus, reducing the Average Fixed Cost. The Average total cost is decreasing until unit 5 which is the lower Average Total Cost the firm has ($21, 80). After that the Average Total Cost starts to increases again.

AVERAGE COST IN LONG- RUN PERIOD

On the contrary, the time period into which the enterprise can alter the quantity of all factors of production is called long-term or Long-Run. At Long-Run period the company can alter all its factors, even the capital goods. This means that in the long-run the firm can: vary its factor size, switch techniques of production, hire new workers or train them, negotiate new contracts with suppliers of Raw Materials if we believe that the costs are too high or the firm has the opportunity to change its suppliers if the situation is bad (high cost, bad delivery etc).

Long-Run Total Cost is the minimum cost of producing each output level when the firm can adjust all inputs. In the Long-Run, because the firm can change/alter all its factors, the firm can succeed Economies of Scale. The state of Economies of Scale is defined when the Long-Run Average Cost falls as output rises.

The reasons of Economies of Scale are 3: 1st: Indivisibilities in the production process. (A firm needs a minimum quantity of inputs like rent, telephone, electricity, manager, accountant whether or not output is produced.

But the costs are fixed costs so they do not vary with the output level, as a result the bigger the output the lesser will be the Fixed Cost. 2nd: Specialization. A firm in the long-run can train their workers and make them specialists in some departments or works of the business in order for the firm to have better production from the workers. 3rd: higher amount and better quality of machinery and better quality oftechnology. This clearly means higher productivity in the future. Even though, the scale of economies are at low output levels and at high output levels, we have diseconomies of scale which is the opposite.

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This is caused due to the fact that, when having more workers there is more confusion because the vast number of workers involves less machines and less space and this can reduce the productivity. We can see this from the M. P. L (marginal product of labour) Consequently, in the long-run, the firm can vary all factors freely. As output expands the firm enjoys some scale economies, then diseconomies of scale set in and marginal costs of further

output increases start to rise again. In the short-run period we suppose that the all factors are constant (as capital K) apart from the work.

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