

Economies of scale and minimum efficiency scale

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Economies of scale are a term used to refer to the advantages related to cost which a company gets or realizes as result of expansion. It's mostly enjoyed by companies that are planning to enlarge their scale of operations. Some of the operations that a company should expand to fully realize the economies of scale are buying materials in large quantities and mostly this should be through long term contracts. Through advertising, a company can too realize economies of scale since it can spread the cost of carrying out advertising over a great range of output in the market media.

Minimum efficiency of scale on the other hand is a term used to refer to the smallest output that a company can produce in a way that its long run average costs are minimized. These two factors have been put into practice by most companies in America that produce carbonated soft drinks like the coca-cola and Pepsi as well as other small companies. The large companies like coca-cola and Pepsi have been able to apply the concept of economies of scale effectively and this has made them to be the biggest players in their field.

Since these two companies are well established they are able to purchase raw materials in large quantities . Whenever purchases are done in large quantities, a lot of money is saved since discounts are given and other services. But when other small companies who have little spending power buy raw materials, they buy in small quantities. In such a case, the bigger companies get advantage over the small companies when it comes to purchasing of raw materials and this has impact also on the overall cost of production.

At certain times, any business faces hard times financially and ends up borrowing money from financial institutions like banks and they need to feel secure that their money will be repaid. This satisfaction comes from knowing that the company they are lending money to be well established and so this works in favor of large companies other than for the small ones. The small companies that produce carbonated soft drinks (CSD's) still survive in the market despite this big advantage their competitors have over them.

Minimum efficiency of scale has made co-existence of these two players in the beverage industry possible. The scale states that there is a certain quantity of production which a company should produce so that its long run average costs are minimized. This means that even the small companies can minimize their cost of production if they apply this scale efficiently. In America, the minimum efficient scale is small compared to the overall market for carbonated soft drinks and this makes it possible for many companies to coexist. It's also under this that the rule of perfect competition is enforced.

Perfect competition is a description of rules that are intended to ensure fair play business transactions. This law forbids any producer or consumer from having direct influence on the prices of the products. This protects small companies from exploitation from big ones through controlling the prices in the market and this has led to an efficient outcome for the small and large companies in America. If this was not applied, then big firms like coca-cola would set prices that would force the small beverage companies walk out the market.

This kind of balance in which the market price is established through the amount of goods produced by producers and the amount that's sought for by buyers or consumers is equal is known as economic equilibrium. Economic equilibrium dictates that no producer should be left to control the prices in the market but on the contrary, the prices should be not change unless in cases where the change comes accompanied by a change in demand for the products or a change in the supplies.

Good and effective of application of the economies of scale as well as the minimum efficient scale can be said to be the two major factors that have enabled small beverage companies be able to compete with large ones or multinationals effectively.

References

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