

Cost analysis

Scale of output

- Constant return to scale: output increases at same level as input
- Increasing return to scale: output rises quicker than input
- Decreasing return to scale: input rises quicker than output

Economies of scale



Internal economies of scale (under companies control)

- Labour: expertise, better staff
- Investment
- Procurement: bargaining power over suppliers (monopsony)
- R&D
- Capital
- Diversification
- Product promotion
- Transport & Distribution
- By-products



External economies of scale

- Labour force: firms in an industry group together
- specialised ancillary firms open up (e.g. in Finance districts --> Accountancies etc.)
- Social infrastructure: development of facilities etc...

Diseconomies of scale



Internal diseconomies

- Management: the bigger the more complex --> unresponsive
- Labour: gap between management & staff
- Other inputs



External diseconomies

- e.g. renting prices go up as more companies come into market etc...

X-inefficiency

The relationship between long and short run costs --> envelope curve, short run extrapolates long run

Product and process innovation can lead to cost reduction

Experience curve

costs fall over time when people get experienced (learn curve effect) --> leads to virtuous circle (Lower unit cost --> competitive advantage --> Growing market share)

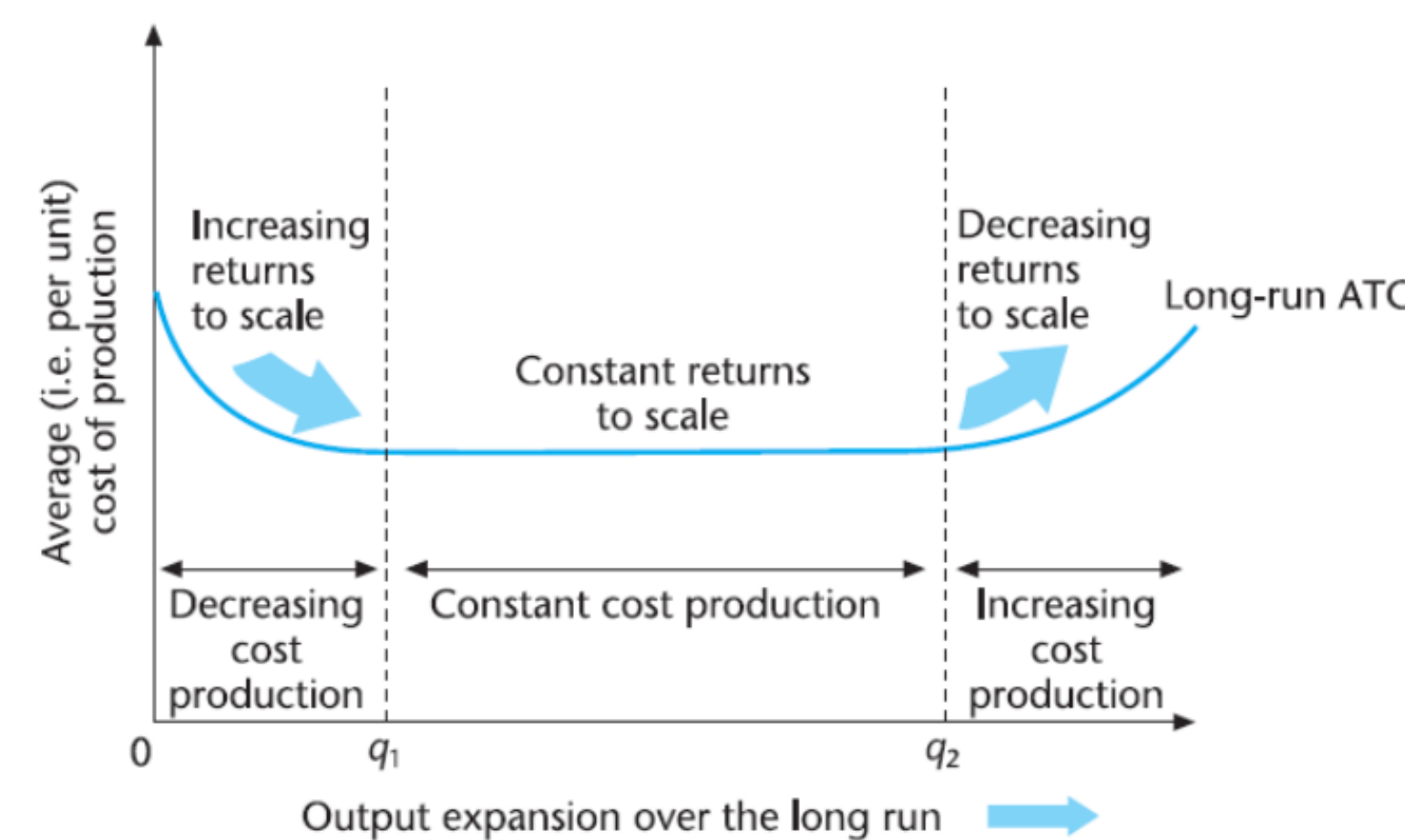
Economies of scope (Verbundvorteil)

when the costs of producing 2 or more different outputs by one firm are lower than would be the case if each output was produced in separate firms

Sharing common inputs over a range of activities

Jointly promoting its range of products and services

Jointly distributing its range of products and services



long run average cost

MES = Minimum efficient scale = where the Long run ATC comes to constant cost production