

COST

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What is cost?

- Total expenditure incurred in producing a commodity.
- Sum of explicit cost and implicit cost
- Explicit cost- Actual money expenditure on inputs or payment made to outsiders for hiring their factor services
- Example- Wages paid to the employees, rent paid for hired premises, payment for raw materials
- Implicit cost- The estimated value of the inputs supplied by the owners
- Example- Interest on own capital, rent of own land, salary for the services of entrepreneurs

What is cost?

- Cost in economics includes actual expenditure on inputs and the imputed value of the inputs supplied by the owners
- Cost
 - Short-run cost functions
 - Long- run cost functions

Short-run Cost Functions

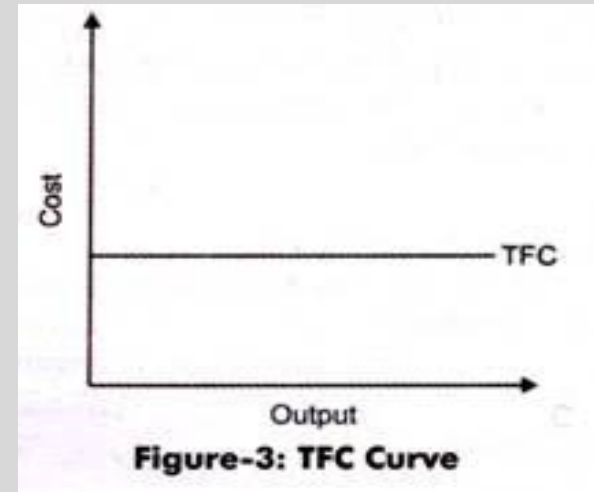
- Some factors are fixed while others are variable
- Short-run costs are divided into two kinds of costs
 - Fixed Costs
 - Variable Costs

Total Fixed Costs (TFC)

- Fixed costs- those costs which do not vary directly with the level of output
- Incurred on fixed factors like machinery, land, building etc. which cannot be changed in the short run
- Payment of these factors remain fixed irrespective of the level output
- Example-Rent of premises, Interest on loans, salary of permanent staff, insurance premium etc.

Total Fixed Costs Schedule and Curve

Output	TFC
0	12
1	12
2	12
3	12
4	12
5	12

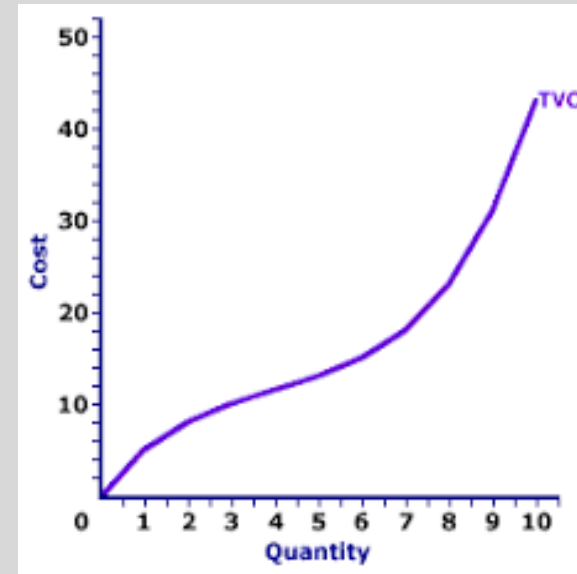


Total Variable Cost (TVC) or Variable Cost (VC)

- Variable Costs- Which vary directly with the level of output
- Incurred till there is production and becomes zero at zero level of output
- Example- Payment for raw material, power, fuel, wages of casual labour etc.

Total Variable Cost Schedule and Curve

Output	TVC
0	0
1	6
2	10
3	15
4	24
5	35



Total Variable Cost Curve

- TVC curve is inversely S-shaped
- Initially increases at decreasing rate and later it increased at increasing rate
- TVC is zero at zero level of output
- This is due to law of variable proportion

Difference between TVC and TFC

TVC

- Can be changed in the short-run
- Zero when there is no production
- TVC is inversely S-shaped
- Incurred in variable factors

TFC

- Cannot be changed in the short run
- Can never be zero even if there is no production
- Horizontal straight line
- Incurred on fixed factors

Total Costs (TC)

- Total expenditure incurred by a firm on the factors of production required for the production of a commodity
- TC is the sum of TFC and TVC at various levels of output
- $TC = TFC + TVC$
- As TFC remains same at all levels of output, the change in TC is entirely due to TVC

Total Cost Schedule and TC Curve

Output	TFC	TVC	TC
0	12	0	12
1	12	6	18
2	12	10	22
3	12	15	27
4	12	24	36
5	12	35	47

