ECONOMICS 101 IN-CLASS ACTIVITY FALL 2017 – 10 MINUTES

PLEASE COMPLETE THIS ACTIVITY ON OUR OWN.

In Class Activity 6 - Nov 14

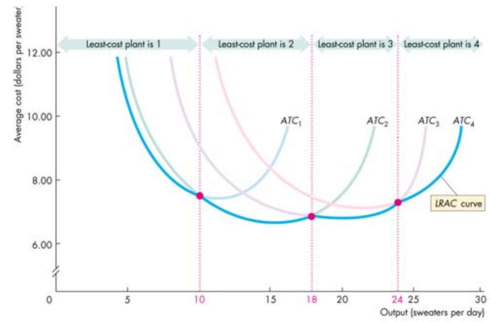
1. Explain the link between short run cost, long run cost and scale of plants.

Short Run: Average Total Cost Curve is U-Shaped basis influence of two opposing forces:

- **Spreading total fixed cost over a larger output**—*AFC* curve slopes downward as output increases.
- **Diminishing Marginal Returns**—the *AVC* curve slopes upward and *AVC* increases more quickly than *AFC* is decreasing.

Long-run average cost curve is made up from the lowest ATC for each output level.

- To decide plant size or scale select lowest cost for producing each output level and the corresponding plant size. This will mean we get the least-cost way of producing a given output level.



The LRAC curve is a planning curve that tells the firm the plant size or scale that minimizes the cost of producing a given output range.

2. Based on information from part 1, how do you know what size of plant to have in the long run?

- As a firm you want to take advantage of economies of scale to decrease LRAC … so if in section I, increase scale to increase Q to get decrease LRAC
- Do not enter into diseconomies of scale