2.6 Production

Key Words

Total Revenue	The total income of a firm from the sale of its goods and services
Average revenue	The revenue per unit sold
Total cost	All the costs of the firm added together
Average cost	The cost of producing a unit
Profit	The amount of money a producer has left after all the costs have been paid ie when total revenue is greater than total costs
Loss	When a firm's revenue is less than its costs
Productivity	One measure of the degree of efficiency in the use of factors of production in the production process. It is measured in terms of output per unit of input
Production	The total output of goods and services produced by a firm or an industry in a period of time

	Calculations
Revenue	Quantity sold x selling price
Average Revenue	$\frac{\text{Revenue}}{\text{output}}$
Total costs	Fixed costs + variable costs
Average Costs	$\frac{\text{Total costs}}{\text{Output}}$
Profit/ Loss	Revenue - costs

Production and its importance for the economy

Production and productivity are not the same thing. Production is about total output while productivity is output per unit of input.

Producers can be individuals, firms or the government (government is the producer of defence, police, education and health for example)

The level of production is important to the economy because it will impact on the number of people with jobs, the level of output and therefore ultimately the amount of economic growth the economy experiences. For a firm it will impact on the costs structure and economies of scale for example. The benefits of production are summarised here:

- Increased employment
- Increased profits
- Economies of scale
- Economic growth

The importance of productivity for the economy

Productivity is the **main determinant of living standards** – it quantifies how an economy uses the resources it has available, by relating the quantity of inputs to output.

Productivity increases can be due to:

- Workers specialising
- Through improving the skills of workers through education and training
- Through greater investment in new technology
- By increasing the amount of capital equipment

Higher productivity can lead to the following benefits:

- Lower average costs
- Improved competitiveness
- Higher profits
- Economic growth
- Higher wages

BUT

- May lead to unemployment if more capital rather than labour is used
- May lead to other countries retaliating

Exam Questions

Quizizz

Video

Specification

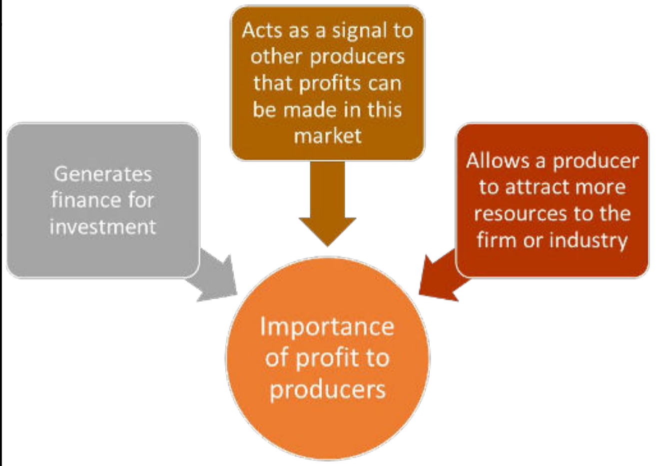
BOHUNT EDUCATION TRUST

2.6 Production

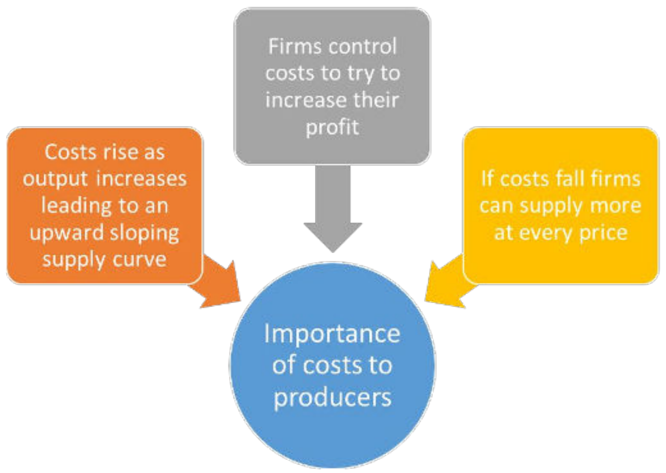
Key Words

Economies of scale	As the firm gets bigger, its average costs of production begin to fall
Technical economies	Larger firms are able to purchase expensive specialist equipment. This is possible because the costs can be spread across a large output.
Economies of increased dimensions	Doubling the size of a shipping container will increase its costs four times (ie area increases by four times). The volume increases by eight times as much, leading to lower unit costs of production
Purchasing economies	Buying goods in bulk results in the purchaser being able to buy at a lower cost of production
Financial economies	Larger firms are able to borrow money from banks more easily and at a lower rate of interest.
Managerial economies	Larger firms can afford to employ specialist staff for functions such as finance and marketing.
Marketing economies	Larger firms are able to use more expensive marketing methods that reach more potential customers. The costs of marketing per unit of output are lower as they are spread over a greater output.
Risk bearing economies	Larger firms are able to spread the risk by offering a range of goods and services. If one product loses sales then it can still rely on others.
External economies of scale	External economies are the benefits gained by the firm as a member of a particular industry or because of its location

The importance of costs, revenue and profit to producers



The importance of revenue and costs to producers	
Importance of revenue to producers	Improves profitability Encourages investors Helps to gain finance
Importance of costs to producers	Lower costs improve profitability Lower costs improve competitiveness



Internal and External economies of scale

Internal economies of scale of scale refer to the fall in average costs as the firm itself grows. External economies are the benefits gained by the firm as a member of a particular industry or because of its location.

Type of external economy of scale	Explanation
Concentration of firms	Suppliers of parts may locate near the main producer. For example, there is a cluster of formula one firms in the Woking area and this attracts suppliers to these firms to locate nearby.
Education and training facilities	With a concentration of similar firms in an area a local university may run courses to suit the needs of the firms
Location	An area with a good reputation may attract more firms
Transport	Better transport links will help to reduce costs of all the firms in that area

An example of external economies of scale:

Silicon valley in California is famous for the number of big technology companies who have their headquarters there.	With the abundance of tech companies in the area, there is no shortage of talent to headhunt.	Many young and talented software engineers move to the area in the hope of securing their dream job. This makes recruiting new workers not only easier but also much cheaper.

Exam Questions

Quizizz

Video

Specification

BOHUNT
EDUCATION TRUST