CONCEPTS OF COST

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- **Characteristics of the long run AC curves**
- **1. Tangent curve**
- The LAC is tangential to the various SAC curves . The SAC curve can never cut a LAC curve though they are tangential to each other. This implies that for any given level of output, no SAC curve can ever be below the LAC curve. Hence, SAC cannot be lower than the LAC in the long run.

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- **2. Envelope curve**
- It is known as Envelope curve because it envelopes a group of SAC curves appropriate to different levels of output.
- **3. Flatter U-shaped or dish-shaped curve**
- The LAC curve is also U shaped or dish shaped cost curve. But It is less pronounced and much flatter in nature. This shape of the LAC curve implies that there are important scale economies as a firm grows in size at first and these economies are overshadowed by scale diseconomies after a point . The U –shape of the SAC curve is more pronounced than that of an LAC curve simply because 'diminishing returns' to increase in proportion of variable factors set in very early as the volume of output is expanded in the short run. Scale economies are not exhausted so easily and early with expansion in scale.

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- **4. Planning curve**
- The LAC curve is described as the Planning Curve of the firm because it represents the least cost of producing each possible level of output. This helps in producing optimum level of output at the minimum LAC. This is possible when the entrepreneur is selecting the **optimum scale plant**. Optimum scale plant is that size where the minimum point of SAC is tangent to the minimum point of LAC.

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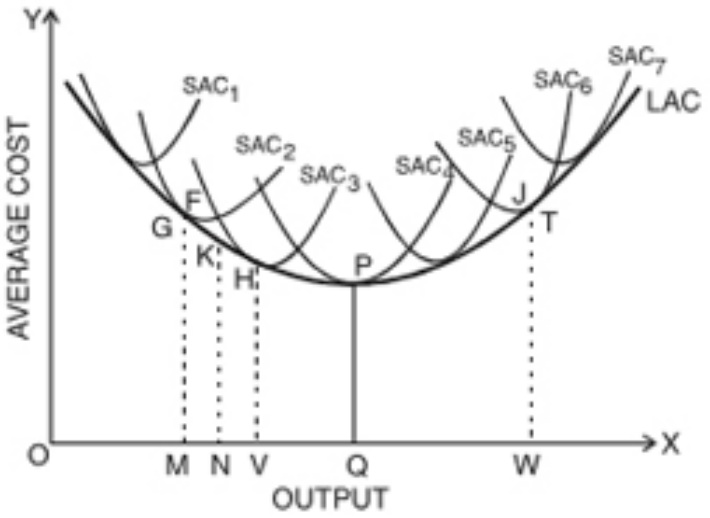
- In the diagram, OQ is regarded as the optimum scale of output, as it has the least per unit cost. At Q output LAC = SAC. And point P shows the optimum size or scale of the plant .



CONCEPTS OF COST

- 5.The LAC Curve can never cut a SAC curve . This implies that for any given output , LAC can never be higher than the SAC .
- 6.The LAC curve will touch only the optimum plant SAC curve at its minimum point. All other SAC curves will be touched by the LAC curve either to the left or to the right of their minimum points.

- To be continued…….