

MBA- I semester, paper- Managerial Economics, MB 102, TOPIC-Cost-Output Relationship

A proper understanding of the nature and behaviour of costs is a must for regulation and control of cost of production. The cost of production depends on money forces and an understanding of the functional relationship of cost to various forces will help us to take various decisions. Output is an important factor, which influences the cost.

The **cost-output relationship** plays an important role in determining the optimum level of production. Knowledge of the **cost-output relation** helps the manager in cost control, profit prediction, pricing, promotion etc. The relation between cost and its determinants is technically described as the cost function.

$$C = f(S, O, P, T \dots)$$

Where;

- C= Cost (Unit or total cost)
- S= Size of plant/scale of production
- O= Output level
- P= Prices of inputs
- T= Technology

Considering the period, the cost function can be classified as

(1) short-run cost function and

(2) long-run cost function.

In economics theory, the short-run is defined as that period during which the physical capacity of the firm is fixed and the output can be increased only by using the existing capacity allows to bring changes in output by physical capacity of the firm.