

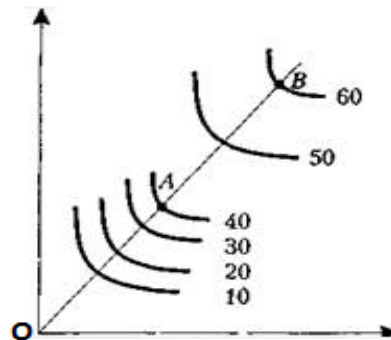
Answer on Question #65415, Economics / Microeconomics

With the aid of graph of total product, identify and explain increasing and decreasing return to scale.

Answer:

Increasing returns to scale - a situation in which a proportional increase in all factors of production leads to ever-greater increase in the volume of product release. Assume that all factors of production are doubled, and the volume of the product has increased three times. Increasing returns to scale due to two main reasons. Firstly, an increase in productivity because of factors of specialization and division of labor with an increase in the scale of production. Secondly, the increase in the scale of production often requires a proportional increase of all inputs. For example, a doubling of the production of the cylindrical equipment (such as pipes) would require an increase of metal less than twice.

When increasing returns to scale (segment OA) characterize the production process of the company, the isoquant closer to each other. This means that if the proportional increase in labor (5, 10, 15, etc.) and capital (1, 2, 3) output increases at an accelerating rate.



Decreasing returns to scale is a situation in which balanced growth of all factors of production leads to a smaller increase in the volume of product release. In other words, the volume of production increases to a lesser extent than the cost of production factors. For example, all factors of production increased three times, and the volume of production - only two times.

Under the decreasing returns to scale (segment AB), on the contrary, the isoquant placed further apart, as it takes more and more factors of production to increase production volumes.

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