

Economies of Scale:

- As a firm increases its production capacity, the efficiency of production also increases.
- As a result the firm is able to get more output per unit of input, leading to low average total costs.
- This state is termed as **economies of scale**.
- There are two types of economies of scale: internal economies of scale and external economies of scale.

Internal economies of scale: achieved by a firm due to its internal efficiency and management.

- **Technical Economies** – superior technique and high quality machines and equipments.
- **Specialization Economies** – Division of labour and specialization.
- **Managerial Economies** – Professional management and functional specialization.
- **Marketing Economies** – Sale and purchase in large quantities and market research benefits.
- **Financial Economies** – Finance available at lower interest rates.
- **Risk Bearing Economies** – Distribution of risk.

External economies of scale: achieved by all firms or whole industry due to improved infrastructure in an area.

- **Transport and communication:** Improvement in transport and communication network
- **Training and education:** Focus on training and education within the industry
- **Allied industries:** Support of other industries

Diseconomies of Scale:

- After a certain point, as the scale of operation further increases, it becomes more difficult to manage the firm effectively and coordinate the various operations and divisions of the firm, and thus it results in diseconomies of scale.
- Total average cost of production starts increasing.
- Similar to the economies of scale, diseconomies of scale can also be categorized into internal and external diseconomies of scale.

Internal diseconomies of scale:

- **Managerial inefficiency** - challenge of managing a bigger firm

- **Labour inefficiency** - labour absenteeism, lethargy, discontinuation of services, etc., become common

External diseconomies of scale:

- **Prices of raw materials:** increase in the prices of raw materials
- **Demand for skilled labour:** increase in the demand for skilled labour
- **Waste disposal:** expensive waste disposal or recycling methods
- **Advertising and promotion:** excessive need for advertising and promotion

Real and Pecuniary Economies to Scale:

- ✚ Real economies to scale refers to economies due to technical, managerial, infrastructural benefits.
- ✚ Pecuniary economies to scale refers to economies due to reduction of input and factor prices.

Real and Pecuniary Diseconomies to Scale:

- ✚ Real diseconomies to scale refers to diseconomies due to technical, managerial, infrastructural limitations.
- ✚ Pecuniary diseconomies to scale refers to diseconomies due to increase of input and factor prices.