3.3.4 Normal Profit, Supernormal Profit and Subnormal Profit (Loss)

- Profit is reward for risk taking
- Profit maximisation is explained in previous sections
- At a lower output MR>MC, there are profits to be claimed
- At a higher output MC>MR, the cost of another unit is more than the revenue from selling it, firm needs to reduce profit
- Use marginal analysis

Normal Profit

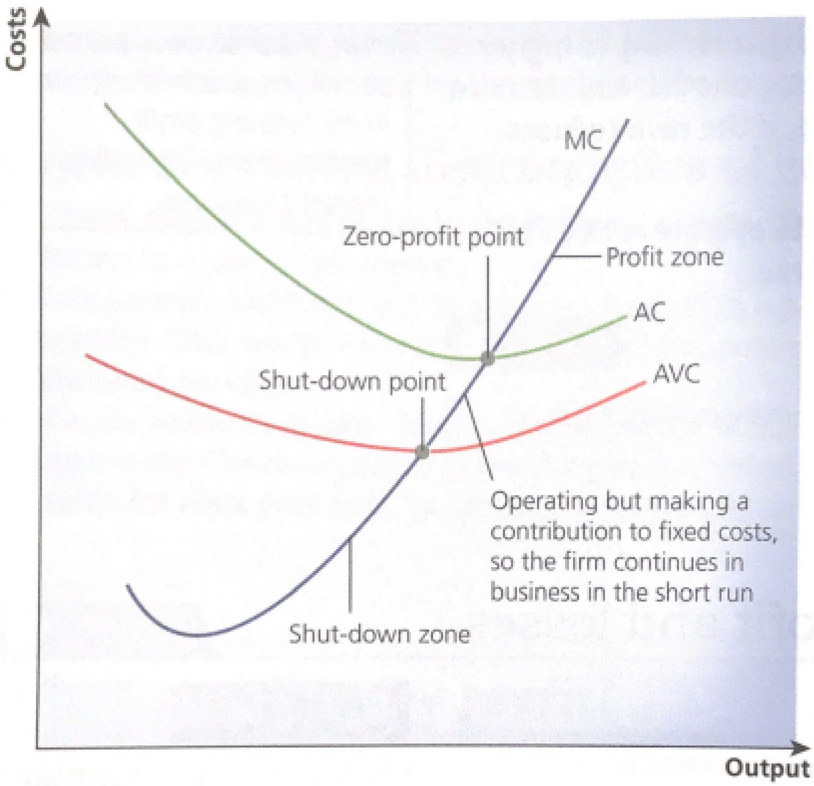
- Minimum profit neccesary to keep firm in business and resources in current use, represents opportunity cost
- Built into AC curve, represents cost of use of entreprenurship
- Size of norm profit varies according to level of risk. If risks are higher, normal profit must be higher also

Supernormal Profit

- Profit above the minimum required to stay in business, any extra profit. Difference between TR and TC or AR and AC

Subnormal Profit/ Loss

- Occurs when total costs are greater than total revenues or when average production costs are higher than price per unit
- Break even level of output is AC=AR or TC=TR
- Break even is when no super/subnormal profit is made
- Shutdown point is where price is equal to AVC. If AVC isn't covered then firm will close in short run
- If firm covers AVC in SR it can still make a loss but stay in business. Any point below and including P=AVC is where the shut down point occurs.


Costs
MC
Zero-profit point
Profit zone
AC
AVC
Shut-down point
Operating but making a contribution to fixed costs, so the firm continues in business in the short run
Shut-down zone
Output