Presentation on :

Types of cost

- Mahesh.Patil


Costs

A **cost** is the value of money that has been used up to produce something.

Definition of cost

The expenses faced by the business in the process of supplying goods and services to consumer

Types of costs

- Opportunity cost and actual cost
- Direct and indirect cost
- Explicit and implicit cost
- Historical and replacement cost
- Fixed cost and variable cost
- Real and prime cost
- Total,average,and marginal cost

Opportunity cost and actual cost

Opportunity cost : Cost incurred for loosing next best alternative

Actual cost : An actual amount paid or incurred, as opposed to estimated cost or standard cost.

Explicit and implicit cost

Explicit cost refers to the money expended to buy or hire resources from outside the organization for the process of production

Implicit cost refers to the cost of use of the self owned resources of organization that are used in production

Direct and Indirect cost

Direct cost is a cost.

Direct Cost: Direct costs are those cost that have directly accountable to specific cost object such as a process or product

Ex:wages paid ,salary paid labor, material…etc

Indirect cost:

Indirect cost are those costs which are not directly accountable to specific cost object or not directly related to production

Ex: insurance, mentainence ,telecom, ….etc

Historical and replacement cost

Historical cost refers to the original (actual) cost incurred at the time the asset was acquired

The **replacement cost** is the price that an entity would pay to replace an existing assets at current market price that may not be market value of that asset.

Fixed and variable cost

Fixed cost is the cost that remains unchanged irrespective of the output level or sales revenue such as intrest,rent,salaries etc

Variable cost are thoese costs that vary depending on a company's production volume; they raise as production increases and fall as production decreases

Real cost and Prime cost

Real cost of a production refers to the physical quantities of various factors used in producing commodity

Ex: Real cost of a table composes of a carpenter's labor to cubic feet of a wood ,a dozen of nails, half a bottle of varnish…..etc

" *Real cost thus signifies the aggregate of real productive resources absorbed in the production*"

Prime cost

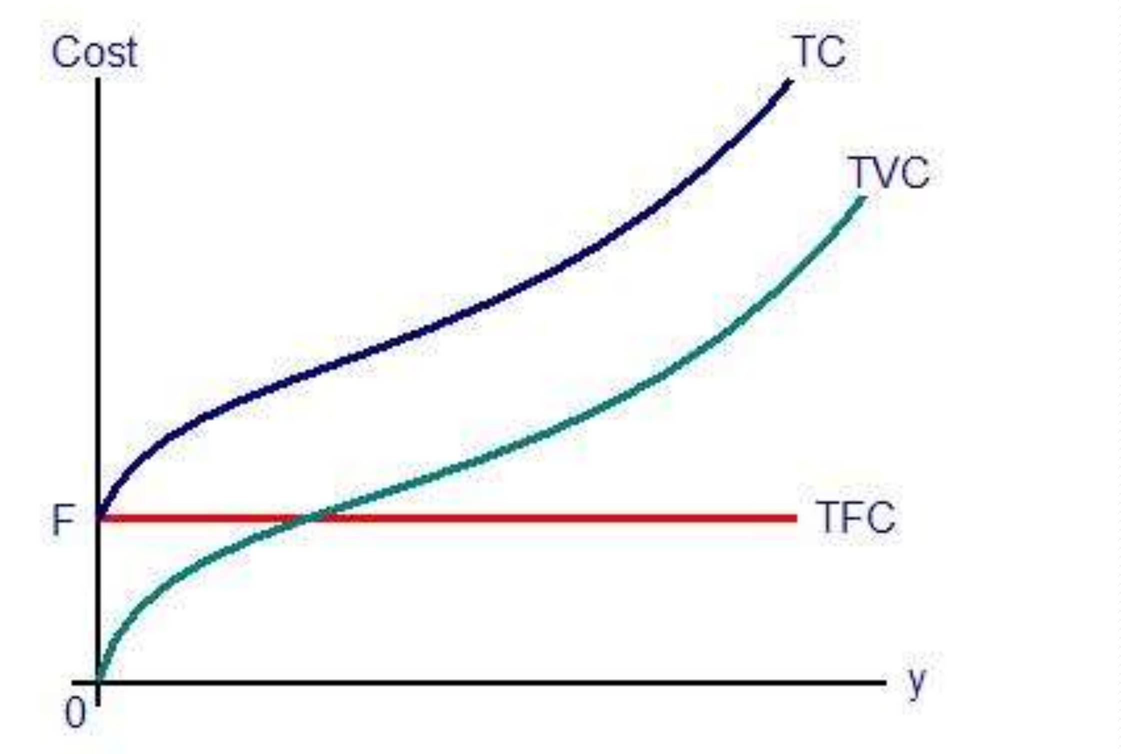
The direct cost of commodity in terms of the materials and labor involved in its production excluding fixed cost

By calculating prime cost the firm can decide how much should be their selling price to earn profit

Total cost

Total cost : it is the cost refers to the total expenses incurred in reaching a particular level of output

TC = TVC + TFC



Marginal cost

The marginal cost is also per unit cost of production. It is the addition made to the total cost by producing one more unit of output

$$MC_n = TC_n - TC_{n-1}$$

i.e the marginal cost of the unit of output is the total cost of producing n units minus the total cost of producing n-1 (i.e ...one less in the total) units of output

Average cost

Average cost is the total cost divided by total units of output Thus,

$$AC = \frac{TC}{Q}$$

Where Q is the quantity produced

Average fixed cost (AFC)

Average fixed cost is the total fixed cost divided by total units of output

$$AFC = \frac{TFC}{Q}$$

Where Q is the number of units produced

Average Variable cost

Average variable cost is total variable cost divided by quantity produced

$$AVC = \frac{TVC}{Q}$$

Where Q is the quantity produced

Managerial uses of cost analysis

- To find most profitable rate of operation of the firm
- To determine in advance the cost of business operations
- To fix the price of the product
- To decide what sales channel to use
- To have clarity about the various cost concepts