

BUSINESS EXPANSION

ECONOMIES OF SCALE

Business expansion by employing more of a few or all the factors of production is referred to as an increase in the scale of operation / production.

The advantages that a business achieves by producing at a large scale are known as economies of scale. They are the reductions in a firm's average cost of production (unit costs)

TYPES

1. Internal Economies of scale
2. External Economies of scale

INTERNAL ECONOMIES OF SCALE

They are the benefits of growth that arise when a business grows from within. They are:

1. Purchasing economies
2. Production or technical economies
3. Financial economies
4. Marketing economies
5. Risk – bearing economies
6. Information economies
7. Managerial economies

EXTERNAL ECONOMIES OF SCALE

They are the benefits or the reduction in costs which any business in an industry might enjoy as the industry as a whole grows in size. They are:

1. Emergence of skilled labour force
 - supply of labour is high – low wage rates
 - less need to train
 - efficient and productive labour – less avg. costs
2. Training courses in local educational institution
3. Co-operation among the firms
4. Government support
5. Ancillary or supportive business emerge
6. More specialization can take place (Disintegration) – focus on core activities

DISECONOMIES OF SCALE

The factors that increase the average costs as a firms scale of operation increases beyond a certain size are known as diseconomies of scale.

TYPES

1. Internal Diseconomies of scale
2. External Diseconomies of scale

INTERNAL DISECONOMIES OF SCALE

They are the disadvantages of expansion that arise when a business grows from within. They are:

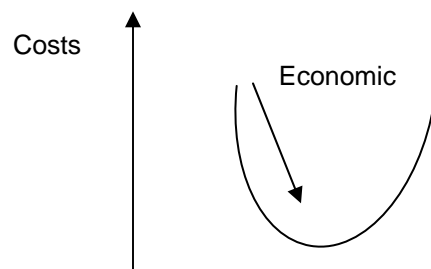
1. Communication problems
2. Managerial problems
3. Co-ordination problems
4. Control problems
5. Alienation of the workforce
6. Technical or efficiency related diseconomies

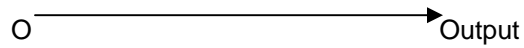
EXTERNAL DISECONOMIES OF SCALE

They are the disadvantages or increases in costs which any business in an industry might face as the industry as a whole grows in size. They are:

1. Overcrowding in industrial problems
 - Traffic congestion
2. Price of the factors of production might rise as firms compete for a limited amount of resources.
3. Firms can pressurize the government policies for their own benefit
4. Inflation increases
 - demand increases
 - salaries high – purchasing power high
5. Overcrowding
 - pollution increases
 - skilled labour shortages due to high competition

Average Costs Curve





APPROACHES TO AVOID DISECONOMIES OF SCALE

1. Management by Objectives
2. Decentralisation
3. Reduced diversification to control co-ordination and communication problems

Mega Lecture