MONEY COST, REAL COST. IMPLICIT COST , EXPLICIT COST AND OPPORTUNITY COST

Money cost or nominal cost is the total money expenses incurred by a firm in producing a commodity. It includes the following elements:

1. Cost of raw materials
2. Wages and salaries of labour
3. Expenditure on machinery and equipment
4. Depreciation on machines, buildings and such other capital goods
5. Interest on capital
6. Other expenses like advertisement, insurance premium and taxes.
7. Normal profits of the entrepreneur.

Real cost

Real cost is a subjective concept. It expresses the pains and sacrifices involved in producing a commodity.

Marshall defined real cost as follows, " The exertions of all the different kinds of labour that are directly or indirectly involved in marking it together with the abstinence s or rather the waiting s required for saving the capital used in marking it.

But real costs are not amenable to precise measurement. Modern economists therefore prefer the concept of opportunity cost.

Implicit cost and explicit cost

Explicit cost are those costs which are actually paid by the firm. To put it in other words, explicit costs are paid out costs. Explicit costs include wages and salaries, prices of raw materials, amounts paid on fuel, power, advertisement, transportation, taxes and depreciation charges. Explicit costs are recorded in the firms books of account.

Implicit costs are imputed value of the entrepreneur's own resources and services. In other words, implicit costs are costs which self - owned and self - employed resources could have earned in their best alternative uses. It refers to the highest income which might have been received by him if he has let his labour, building and money to someone else. These costs are frequently ignored in calculating the expenses of production.

Opportunity cost

Modern economists have rejected the labour and sacrifices nexus to represent real cost. Rather, in its place they have substituted opportunity or alternative cost.

The concept of opportunity cost occupies an important place in economic theory. The concept was first developed by an Austrian economists, Wieser. The other notable contributors are Daven Prof, Knight, Wicksteed and Robbins. The concept is based on the fundamental fact that factors of production are scarce and versatile.

The opportunity cost of anything is the alternative that has been foregone. This implies that one commodity can be produced only at the cost of foregoing the production of another commodity. As Adam Smith observed, if a hunter can bag a deer or a beaver in the course of a single day, the cost of a deer is a beaver and the cost of a beaver is a deer. A man who marries a girl is foregoing the opportunity of marrying another girl. A film actress can either act in films or do modelling work. She cannot do both the jobs at the same time. Her acting in film results in the loss of an opportunity of doing modelling work.

In the words of Professors Byrns and stone " opportunity cost is the value of the best alternative surrendered when a choice is made.

In the words of John A. Perrow " Opportunity cost is the amount of the next best produce that must be given up (using the same resources) in order to produce a commodity.