

Hello students. Welcome to yet

another module. Of managerial

economics in your semester 2.

Today we're going to study under Unit 2.

That is profit analysis.

The topic profit.

That is, what is the meaning nature

of profit and what are the various

concepts and types of profits?

Which economics are classified?

This is your model number 9.

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Outline of this module

includes the meaning of profit,

the nature of profit concerns,

or kinds of profit,

and the role or importance

of profit for a businessman.

Students. After going through this module,

you will be able to understand

the meaning and nature of profit.

The various concepts and kinds of profit.

And the role of profit

in a business decision.

Profit. We all know profit is the

revenue or business pulls in after

paying all expenses and costs.

Whether it is a lemonade and bhel puri

stand or a multinational company,

the primary goal of any business is

to earn money there for a business

performance is based on profitability.

Well then what is profit?

Profit is a return to an entrepreneur

who brings together land,

labor, capital and enterprise,

organizes and manage them to get

the desired output efficiently.

Profit is a reward for the

businessmen or entrepreneur,
who bears the risk of uncertainty
of return of such investment.

What is uncertainty then?

See for a businessmen,
there is no certainty that the output
generated will always be sold in the
market at a price higher than its cost,
as the future is uncertain.

We saw also during the COVID-19 times
and lock down period how businessmen,
many of them, lost their businesses
and went into heavy losses.

Profits is a reward for
uncertainty and risk.

Hence, while rent interest wages
are certain they are paid 1st and
are positive streams of income.

Profit, on the other hand,
is an uncertain source of income.

It is a residual income which

are businessmen has to be happy
with after he pays wages,
interest,
rent to the other factor of production.

And profit therefore can be negative
if the business goes in a loss.

Profit is also a reward for
entrepreneur for undertaking research,
invention innovation and trying to
cut down various costs of production.

Let us try to understand then the various
concepts and kinds of profits which
economists accountants normally use.

Let us first see the meaning of accounting,
profits and economic profits,
and then see how they are different.

Profit of a firm as we all know,
is the excess of sales revenue
over its current costs.

Cost carries different meanings
with economists and accountants.

In the accounting sense of the term,

profit is equal to total

revenue minus the explicit costs.

What are explicit costs in?

Accounting profit is a concept

used by accountants to determine

or forms taxable income.

Explicit costs then, on the actual

costs or cash payments for inputs.

Resources purchased like rent paid.

Wages paid to labor interest on capital.

Cost of raw material,

transport charges, etc.

When all these explicit costs are

subtracted from the forms total revenue,

what we get is the accounting profit.

The formula for counting profit.

As you can see in green accounting

profit therefore is simple.

It's total revenue minus explicit costs.

But then what is?

Economic profit.

Economic profit is slightly
different from accounting profit.

Accounting profit ignores opportunity
cost of firms own resources used
in production of goods.

Economists catch just this.

The Economist includes these costs,
which are also called as hidden,
implicit or imputed costs.

And this is used while calculating
the total cost of production.

If a firm's total revenue
exceeds all its economic costs,
both explicit and implicit.

Then the residual which goes
to the entrepreneur is called
an economic or pure profit.

Does economic profit equals
total revenue less all costs,
both explicit and implicit?

What is implicit cost then?

Let us, try to understand with the help

of an example. Implicit costs are.

If a firm uses or a businessman uses

his own building in his business,

he uses his own funds, the capital.

Or the business owner gives his own time

for the production of his business.

Then all these are called as self

owned or self employed resources.

for which actually payments are not made.

But while calculating economic

profits we give them some monetary

value or monetary costs.

And these are also deducted from the total

revenue to arrive at the economic profits.

Economic profits, therefore,

are like normal profits.

That is there the minimum amount

required to keep the ENTERPRENEUR

engaged in the present business.

As you can see, the formula highlighted in green shows economic profit is equal to total revenue minus explicit cost plus implicit cost.

This is the difference between accounting profit and economic profit.

Let's see economic profit.

An accounting profit very easily with the help of an example.

Suppose a firm has an accounting profit of ₹55,000.

The firm also has implicit costs of the following nature.

Entrepreneurs own forgone salary. 40,000. Foregone interest on capital.

Let us say it is rupees 1000.

Foregone rent equal to rupees 4000.

Forgotten means these are the incomes which the owner forgoes because he owns them or he owns these resources.

Had he not owned them he would have

had to incur all these costs and therefore economic profit calculation is nothing but you take the accounting profit here that is ₹55,000.

You subtract from that the implicit costs that is 40,000 plus 1000 + 4000 that is 45,000 and 55,000 -- 45,000 will give you a pure economic profit of rupees 10,000, so this is easily understandable how economic profits are calculated.

Another very simple classification and category of.

Profit is gross and net profits.

What is gross profit?

The first level of profitability of a business is gross profits.

It is nothing but your simple sales, minus the cost of goods sold.

Sales are the first line item on the income statement and cost of goods sold

is generally listed just below it.

Let's take an example.

If a company has rupees one Lac

as sales revenue and its cost

of goods sold is rupees 60,000,

then it is very easy for us to know

that the gross profit is nothing

but the total sales revenue that

is 100000 minus of cost of

goods sold at is rupees 60,000.

Which gives us a gross profit of

rupees 40,000. For the company.

Net profit, on the other hand,

is beyond gross profit.

It is gross profit minus indirect expenses

plus indirect receipts of the firm.

And a very important classification

of profits is. Super Normal,

normal and subnormal profits.

We have already seen what are explicit

and what are implicit costs based on

that super normal profits are defined
as a situation a firm lends itself in
or earns as super normal profits when
its total revenue is greater than its
total explicit plus implicit costs.

Well, normal profit is like a
break even situation,
where total revenue just equals the
total explicit and implicit costs,
and finally,

subnormal profit is an indicator that
the form is not doing well or it is
going to land in losses in the future,
and that this is when the total revenue
is much lower than the total costs,
both explicit as well as implicit.

I hope you followed all the
three classifications of profit
and also what is profit?

These are the references.

Thank you for watching the video.