**KEY CONCEPTS AND SKILLS Theory of the Firm 2 – Revenue, Profits and the Goals of Firms**

**Definitions:**

* **Profit** = revenue – total costs
	+ **Accounting profit** = revenue - explicit costs
	+ **Economic profit** = revenue – economic costs = revenue – (explicit costs + implicit costs)
	+ **Normal profit** = the amount of profit necessary for a company to keep producing; this occurs when revenues are just equal to explicit plus implicit costs (i.e., economic profit = 0)
	+ **Abnormal profit** = profits in excess of economic costs = revenue – economic costs (if positive)
	+ **Loss** = revenue – economic costs (if a negative number)
* **Profit Maximization**: Determining a level of output that the firm should produce to make its profit as large as possible (or its loss as small as possible)
* **Corporate Social Responsibility**: the practice of avoiding socially undesirable business activities

**Concepts and Applications:**

***Revenues***

* Define *total revenue,* *marginal revenue* and *average revenue*.
* Plot the TR, MR and AR curves assuming a perfectly competitive market, and explain any relationships among the curves.
* Given data sets and/or diagrams, calculate total, average, and marginal revenue.

***Profit***

* Distinguish among *accounting profit*, *economic profit*, *normal profit*, and *abnormal profit.*
* Describe a firm’s levels of *economic profit*, *normal profit*, and *abnormal profit* in a competitive market.
* Describe the levels of *economic profit*, *normal profit*, and *abnormal profit* of a firm that is making a loss.

***Goals of Firms***

* Explain, with reference to diagrams, two rules that a firm could use to maximize its profit.
* Describe the following alternative firm goals: revenue maximization, manager utility maximization, satisficing, and corporate social responsibility.
* Outline, with reference to a diagram, how a firm in a competitive market would set its output level if it were guided by the following goals:
	+ Maximizing profit
	+ Maximizing revenue
	+ Maximizing revenue without incurring a loss