## Week 1

## Week 2

## Economics and Scracity

| | | | |
|---|---|---|---|
| economics | the study of how society manages its scarce, or limited, resources. | Economics studies all of these forces – decision making by individuals, by firms, by government institutions | Focus is on how markets operate to allocate scarce resources |
| Scarcity | **Dictators** (since they might not know much about economics, it would likely fail) and **government** (have advisors to help plan) decide allocation | allocations work through the interactions of all these people through markets | |

from Week 1

## Basic Principles of Microeconomics

| | | | |
|---|---|---|---|
| Microeconomics | The study of how households and firms make decisions and interact in markets. | | |
| Macroeconomics | The study of how economy wide phenomena including inflation, unemployment and economic growth. | | |
| **Principles of Microeconomics** | | | |
| *How People Make Decisions* | | | |
| | Principle 1 | People face trade-offs | |
| | Principle 2 | Opportunity Cost | the cost of something is what you give up to get |
| | Principle 3 | People think at the margin | |
| | Principle 4 | People respond to incentives | Government policies have incentives, sometimes unintended. Sometimes don't work as intended. |
| *How People Interact* | | | |
| | Principle 5 | Trade can make everyone better off | |
| | Principle 6 | Markets are usually a good way to organize economic activity | |
| | Principle 7 | Sometimes governments can improve market outcomes | |
| *How the Economy Works* | | | |
| | Principle 8 | A country's standard of living depends on its ability to produce goods and services | |

## Basic Principles of Microeconomics (cont)

| | | |
|---|---|---|
| Principle 9 | Prices rise when the government prints too much money | **inflation**: an increase in the overall level of prices in the economy |
| Principle 10 | Society faces a short-run trade-off between inflation and unemployment | |

## Questions

What exactly do people gain when they trade with each other?

Why do people choose to be interdependent?

## Important Concepts

| | | |
|---|---|---|
| Absolute Advantage | ability to produce more of a good, given inputs, then another producer | |
| Comparative Advantage | the ability to produce a good at a lower opportunity cost than another producer | better to specialize in whatever makes makes your opportunity cost the least |

## Demand, Supply, and Market Equilibrium

| | | |
|---|---|---|
| **Market Demand** | | |
| *Quantity demanded* | amount of good buyers are willing and able to purchase | |
| *Law of Demand* | all else equal, as the price rises its quantity demanded decreases | |
| *Demand Curve* | a graph of the relationship between the price of a good and quantity demanded | |
| | Causes of shifts | |
| | **Income** | |
| | *normal good* | if demand for a good **increases** when income increases |
| | *inferior good* | if demand for a good **decreases** when income increases |
| | **Prices of related good** | |
| | substitutes | if price of sunstitute goes down, the demand goes down |
| | complements | if price of complement goes down, the demand goes up |
| | **tastes/preferences** | |
| | **expectations** | |
| **Market Supply** | | |

## Demand, Supply, and Market Equilibrium (cont)

| | |
|---|---|
| *Quantity supplied* | amount of a good that sellers are willing and able to sell |
| *Law of Supply* | all else equal, when the price of a good rises the quantity supplied rises |
| *Supply Curve* | relationship between price of a good and quantity supplied |

Remember to notice what makes that demand relationship change, i.e. the forces that would make someone want more of a good at any given price.

## Market Equilibrium

a situation in which the market price has reached the level at which quantity supplied = quantity demanded

## Changes in Supply and Demand

**Steps**

| | |
|---|---|
| 1 | Decide whether it is: supply, demand, or both. |
| 2 | Decide in which direction curve shifts |
| 3 | Use demand-supply graph to evaluate change. |

**Scenarios**

| | |
|---|---|
| - | An increase in demand. |
| - | An increase in supply. |
| - | An increase in both demand and supply |

## Week 3

## Elasticity

| | | | |
|---|---|---|---|
| Elasticity | a measure of the responsiveness of quantity demanded or quantity supplied to a change in one of its determinants | | |
| | *Elastic Demand* | if the quantity demanded responds *substantially* to a *price change* | steeper demand curve |
| | *Inelastic Demand* | if the quantity demanded responds *only slightly* to a *price change* | flatter demand curve |

**Types of Elasticity**

## Elasticity (cont)

| | | | |
|---|---|---|---|
| *Price Elasticity* | measures how much quantity demanded responds to a change in price. | Price Elasticity of Demand= %Δ in Quantity Demanded / %Δ in Price | [Q2−Q1 (Q1+Q2)/2] / [P2−P1 (P1+P2)/2] |
| *Supply Elasticity* | measures how much the *quantity supplied* responds to a change in the *price* | | |

**What factors affect elasticity?**

| | |
|---|---|
| *close substitutes* | *elastic* since easier for consumer to switch to a substitute good |
| *necessities* | *inelastic* because need to survive |
| *luxuries* | *elastic* because don't need |
| *time horizon* | more *elastic* over long horizons because necessities can become luxuries |