

Week 1

Week 2

Economics and Scarcity

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
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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, than 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



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Demand, Supply, and Market Equilibrium (cont)

<i>Quantity supplied</i>	amount of a good that sellers are willing and able to sell
<i>Law of Supply</i>	all else equal, when the price of a good rises the quantity supplied rises
<i>Supply Curve</i>	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	
<i>Elastic Demand</i>	if the quantity demanded responds <i>substantially</i> to a <i>price change</i>	steeper demand curve
<i>Inelastic Demand</i>	if the quantity demanded responds <i>only slightly</i> to a <i>price change</i>	flatter demand curve

Types of Elasticity



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Elasticity (cont)

<i>Price Elasticity</i>	measures how much quantity demanded responds to a change in price.	Price Elasticity of Demand= $\frac{\% \Delta \text{ in Quantity Demanded}}{\% \Delta \text{ in Price}}$	$\frac{[Q2-Q1 (Q1+Q2)/2]}{[P2-P1 (P1+P2)/2]}$
<i>Supply Elasticity</i>	measures how much the <i>quantity supplied</i> responds to a change in the <i>price</i>		

What factors affect elasticity?

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



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