ECONOMICS- FIRST YEAR, SEMESTER ONE

WEEK ONE- INTRODUCTION TO ECONOMICS (MICROECONOMICS)

HOW PEOPLE MAKE DECISIONS

- ***Scarcity-*** *society has limited resources and cannot produce all the goods and services that people require- has less to offer than people desire*
    - Economics is the study of how society manages these scare resources
    - For scarcity to exist, there must be more people that want a resource than is available
    - Combination of it being finite and a desire for it
- People face trade- offs → to get something, we have to give up something else that we like
    - ***Efficiency-*** *getting the most we can from our scarce resources*
    - ***Equity-*** *benefits of the resources are distributed fairly among society's members*
    - E.g. how big the pie is vs how much each person gets → economics is more concerned with efficiency rather than equity
- ***Opportunity cost-*** *cost of the best alternative you give up to get that item*
    - Opportunity costs arise because of resource scarcity; based on trade- offs
    - What you give up vs what you gain → includes both monetary amount (explicit cost) and monetary value of any other sacrifices made (implicit cost)
- Normal assumption is that people are rational → they do the best they can to achieve their objectives, given the opportunities that they are presented with
    - Rational people know that decisions are not usually black or white
    - ***Marginal change-*** *small incremental adjustment to a plan of action*
    - Historical costs are irrelevant → money's already gone, it's about what you can do from here
- Rational people make decisions by comparing marginal change and marginal cost → only takes action if the marginal benefit exceeds the marginal cost; people are mostly rational most of the time
    - A person's willingness to pay for a good is based on the marginal benefit that an extra unit of the good would yield
- Incentives → a higher price in a market provides an incentive for buyers to consume less, and incentive for sellers to produce more
    - The law also affects behaviour by changing incentives → if a policy changes incentives, it will cause people to alter their behaviour
    - By comparing costs and benefits, people respond to incentives
    - Many policies can change the costs or benefits that people face
- When both cost and quality increase, we can't be certain of the effect on demand

HOW PEOPLE INTERACT

- Many of our decisions in life affect not only us, but others as well
- Trade can make everyone better off
    - It allows everyone to specialise in the activities they do best → by trading, people can buy a greater variety of goods and services at a lower cost
    - Trade can be mutually beneficial and the government can improve market outcomes

- Markets are a good way to organise economic activity
    - In communist countries, only the government can organise economic activity to promote economic wellbeing for the whole country

- ***Market economy-*** *allocates resources through the decentralised decisions of firms and households as they interact in markets for goods and services*
  - Firms and households make their own decisions through interacting in the marketplace
- Prices reflect the value of a good to society, and the cost of the making the product → affected by supply and demand
  - Subjective value → an item holds different value to different people
- Concept that individuals are usually best left to their own devices, free from government intervention → an individual can best determine the value of a product

- Governments **can** improve market outcomes sometimes
- People rely on police to enforce rights over what we produce
- ***Market failure-*** *when a market is left on its own and it fails to allocate resources efficiently*
- ***Externality-*** *impact of one person's actions on the wellbeing of a bystander e.g. pollution*
- ***Market power-*** *ability of a single person to disproportionately influence market prices e.g. monopolistic*
  - Regulating monopolistic prices may improve economic efficiency
- Market economy rewards people according to their ability to produce things that people are willing to pay for → economic policies don't try to achieve the **same** for everyone, but rather to ensure a more equitable distribution of economic wellbeing

HOW THE ECONOMY AS A WHOLE WORKS

- A country's standard of living depends on its ability to produce goods and services → in countries where workers produce large quantities, most people enjoy a high standard of living
- When thinking about how policy affects living standards, think about how it will effect ability to produce goods/ services
  - Policy makers need to raise productivity, ensuring workers are well- educated, and have the right materials to be most efficient
- Prices rise when the government prints too much money
  - ***Inflation-*** *increase in the overall level of prices in the economy*
  - Keeping inflation at a low level is the economic goal of policy makers globally
  - Relies on the quantity of money
- Society faces a short- term trade-off between inflation and unemployment (Phillips curve)
  - Reducing inflation causes a temporary rise in unemployment
  - Some prices are said to be sticky in the short- term → slow to adjust, leading to unemployment
  - Lower spending leads to reduce quantity of goods and services, with lower sales causing firms to lay off workers, rising unemployment temporarily

WEEK TWO- DEMAND AND SUPPLY

- The theory of supply and demand:
  - Considers how buyers and sellers behave and interact with each other in competitive markets
  - Shows how the interaction between buyers and sellers determines quantity of product and price at which it is sold in a competitive market
  - A market is a group of buyers/ sellers in a physical or virtual place
- Whenever you have a group of sellers/ buyers interacting to trade, you have a market

- A market is amoral → not about what is right/ wrong, but about a network of markets
- ***Competitive market-*** *market in which there are so many buyers and sellers that each has a negligible impact on the market price*
    - In a highly competitive market, each buyer knows there are several sellers, and each seller knows they must compete
    - The smaller the ability of each buyer/ seller to affect the market price, the more competitive the market
- ***Perfectly competitive-*** *the goods offered for sale are all exactly the same (homogenous), and the buyers/ sellers are so numerous that nobody has an impact on market price*
    - As soon as there are no barriers to entry, it is a competitive market
    - As buyers and sellers accept the market price as given, they are ***price takers***
    - Opposite is monopoly e.g. Sydney Water, where the seller is a ***price setter***
- Can be a legal monopoly, or economies- of scale (e.g. Toyota)- no technical barrier, but can't compete

DEMAND

THE DEMAND CURVE- RELATIONSHIP BETWEEN PRICE AND QUANTITY DEMANDED

- ***Quantity demanded-*** *amount of a good that buyers are willing and able to purchase*
    - Demand depends on many factors e.g. price of the good, tastes, income etc.
- ***Law of demand-*** *claim that other things being equal* ***(ceteris paribus)*** *the quantity and price demanded has an inverse relationship- meaning that demand falls when prices rise*
    - Shown through a **demand schedule** (table) or **demand curve** (graph)
- ***Market demand-*** *horizontal sum of all individual demands for a particular good/ service*

SHIFTS IN THE DEMAND CURVE

- **Shifts** to the right (increase) or left (decrease) are cause by **'other' factors**
    - A curve shifts whenever there is a change in a variable that does not appear on either axis
- **Movements along the curve** are caused by a change in the price of good

- 'Other" factors:
- Income → lower income means you have less to spend on most goods
    - ***Normal good-*** *when income goes down, demand goes down e.g. handbags*
    - ***Inferior good-*** *when income goes down, demand up e.g. bus rides*
- Prices of related goods → if the price of a good falls, you are more likely to buy it
    - Relationship between the price of a related good and demand depends on what type of goods the products are
    - ***Substitutes-*** *two goods where a decrease in the price of one leads to decrease in demand for another e.g. ice cream and frozen yoghurt*
    - ***Complements-*** *two goods where decrease in price of one leads to increase in demand of the other e.g. chocolate topping and ice- cream*
- Tastes → based on what you like/ personal preference
- Expectations → expectations for the future affect your demand today e.g. wait for price drop
- Number of buyers → if there are more buyers, demand curve will shift right
- Two ways for policymakers (e.g. reducing smoking):
    - Implement a policy to shift the curve
    - Increase the price e.g. through taxes to move the curve