Microeconomics

Introduction to Economics

Scarcity is the driving force of Economics.

It is a study of how a society manages its scarce resources. It deals with constrained optimization i.e. maximization (best possible solution) when face with restriction.

It studies how people make decisions -how much to work.what to buy;how much to save.

It studies how people interact in the market in buying a selling of goods and services.

Why is Economics so relevant?

Because……………

Some basic principles of Economics

Uno) People face trade-off i.e there is always something that we let go.

“The ain’t such a thing a free lunch.

At a macro level , we deal with Efficiency (getting most from scarce resources) v/s Equity (Distributing Economic Prosperity)

Dos) The cost (opportunity cost) of something is what we give up to get it.

Tres) Rational people think at the margin.

Rational people are those who systematically and purposefully do best they can to achieve their objectives.

Margin is a small incremental adjustment to a plan of action.

To be continued…………

Some basic principles of Economics

A person’s willingness to pay for a goods depends on the marginal benefit that the extra unit of that good yields. The marginal benefit on the other hand depends on how much person usually has.

Cuatro) People respond to incentives.

Incentives induces a person to act.

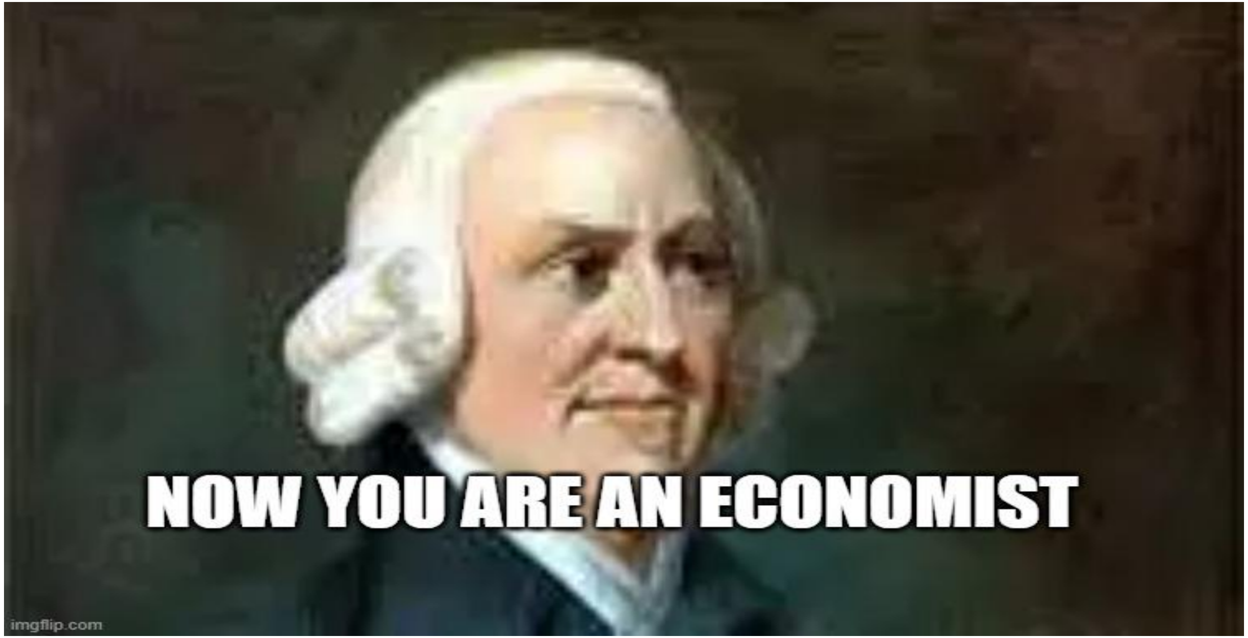
Cincho) Trade makes everyone better off. It leads to specialisation.

Seis) Markets are usually a good way to organize economic activity.

Lasseiz Faire economy or Market economy that allocates resources through decentralized decisions of households and firms as the interact.

Some basic principles of Economics

Siete) Government can sometimes improve market outcomes by addressing the issues of property rights,market failures, externalities, market power (monopolies , cartels).



Two Sector Economy

Households - Responsible for consumption

and provides land, labor, capital

Firms- Responsible for production

and provides incomes/ compensation

to the inputs/factors used.

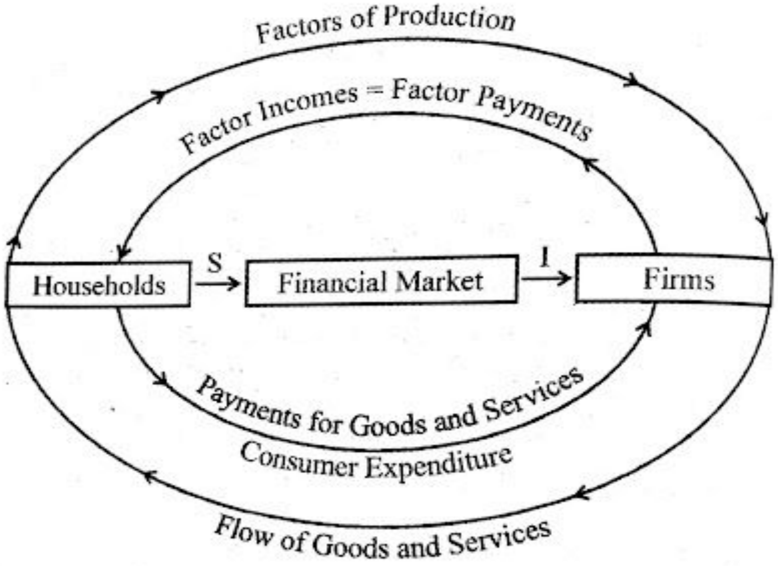


Fig. 2.2

Utility

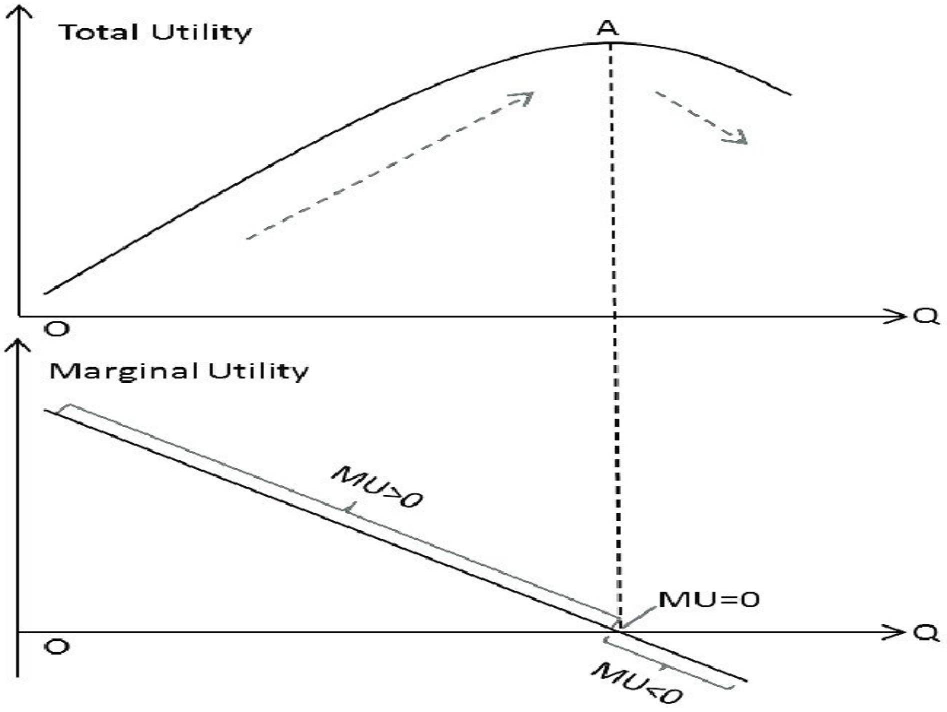
Satisfaction after consumption.

1. Cardinal Utility - Utility is quantified.

a.Total Utility

b. Marginal Utility

c. Law of Diminishing Marginal Utility



Utility

2.Ordinal Utility- Utility is not quantified .It is ranked.Utility is measured using Indifference Curve.

Demand.

Law of Demand.

Exceptions.

Production

Production Functions- explains the relation between physical output and inputs.

Inputs are also called the factors of production.

Two types of factors of production- a. Fixed factor b. Variable Factor

Fixed factor does not change regardless of the output.

Q=f(k,l); K= Capital, l=Labour

Types of production function.

Long run - All the factors varies with time.

Short run - Only one factor (labor) varies.

Production

Short Run Production Functions - relates between specific variable input and quantity of output.

Law of Variable Proportion

As the quantity of one input increases the total output first rises at an increasing rate then at a decreasing rate and finally the total ends up falling .

Assumptions

a. One input.
b. Short Run
c. Fixed Technology

Total Product, Marginal Product, Average Product