Business

Begoña López

1. The organization of economic activity
2. The firm
3. Environment and firm strategy
4. Management
5. Finance
6. Operations
7. Marketing

Begoña López

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Contact hours	Tuesday 9 00-10 00, 11 00-12 00 Wednesday 10 00-12 00 Thursday 9 00-10 00, 11 00-12 00

Assessment	Activities	Weight in final grade
Controlled assessment	Mid-term exam of the first three lessons to be held in week 9 approximately. Two assignments that will be scheduled in weeks 5 and 12 approximately and they will be announced in advance, after finishing lessons 2 and 5 .	30% 15% 15%
Final exam	Exam of the four last lessons at the end of the semester.	40%

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The organization of economic activity

At a glance

1.1. Economic activity and markets
1.2. Analysis of economic variables
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Lesson 1 is a short introduction to Economics, the social science that studies how wealth is created and distributed

- Macroeconomics (study of a country's overall economic dynamics)
  - Gross domestic product, employment rate, …
- Microeconomics (the functioning of individual markets or smaller economic units)
  - Individual businesses, individual consumers, …

1.1. Economic activity and markets

- Economic systems
- How does a market work? Demand and supply
- How are markets organized? Market structures

Economic systems

Hypothesis: self-sufficient person

Advantage: no need of coordination
Disadvantage: inefficiency

But we live in societies

Advantage: specialization (efficiency)
Disadvantage: need for coordination

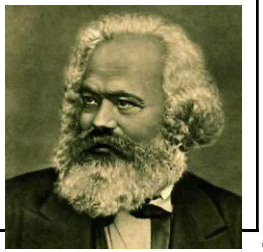
Economic systems

Economic systems

Market economy

Planned economy

Decentralised	Decision making	Centralised
Private	Ownership of production factors	Public
Prices	Coordinating device	Commands
Capitalism *Adam Smith*		Socialism *Karl Marx*



Economic systems

Market economy

Mixed economy

Planned economy

Market coordination + Government intervention by regulations

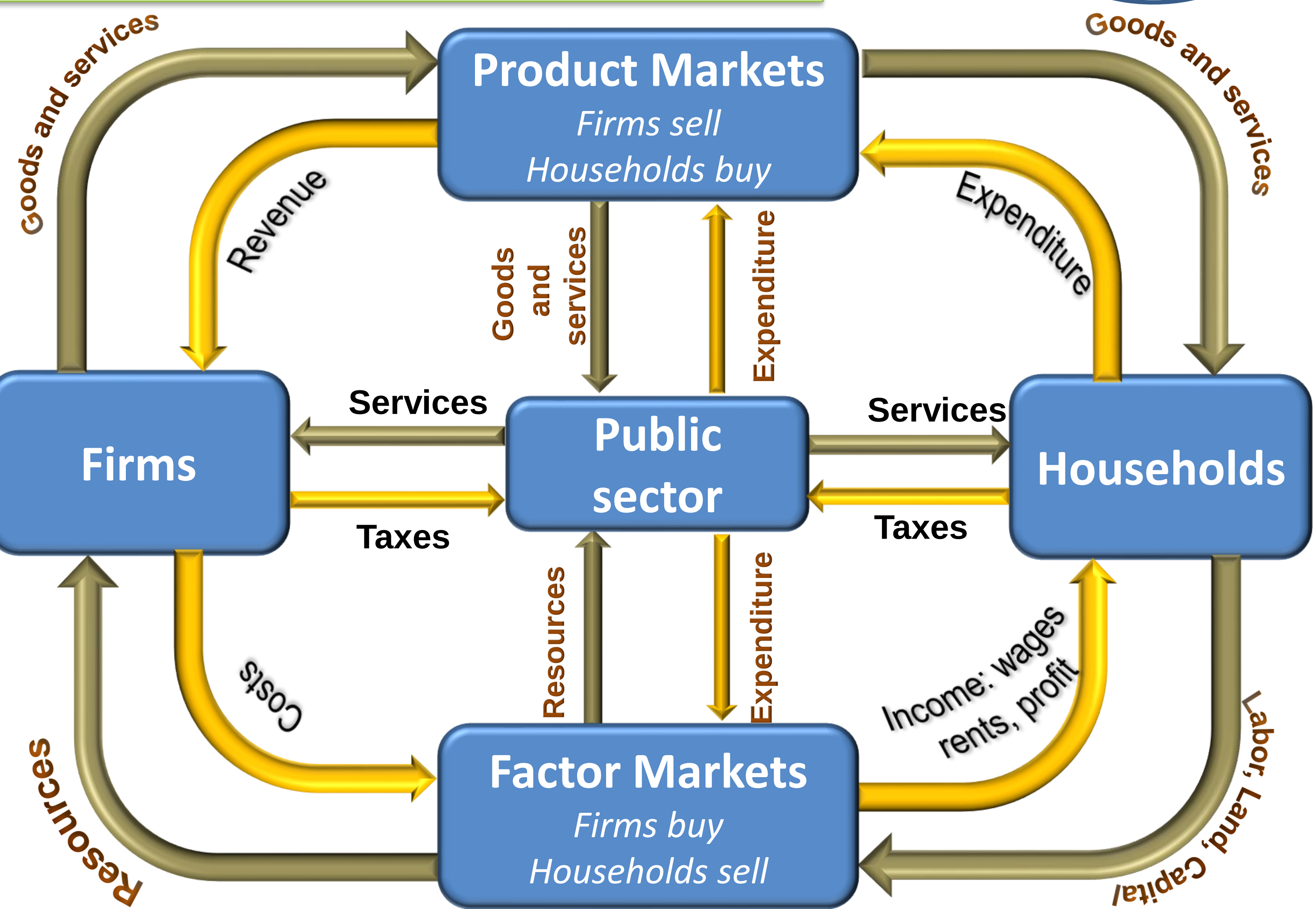
USA Western Europe China Cuba North Korea

How does a mixed economy work?

Economic systems

Circular flow of income in a mixed economy

Market is an actual or nominal place where buyers and sellers (demand and supply) interact to trade goods and services.



How does a market work?

- What we produce?
- How we produce?
- What price to charge?
- How much to produce?
- Whom to hire?

How does a market work?

Scarcity

The essential economic problem

Wants are *unlimited*...

but

…resources are *limited*!

So

we all must make choices!


Nothing comes free

How does a market work?

The nature of economic choice

Example

The allocation of a truly scarce resource-

your time!

How do you allocate your daily 24 hours?

- Maintenance of self, family, household
- Learning
- Working
- Other

What might change *your* allocation?

How does a market work?

The nature of opportunity costs

- Choices involve trade-offs
  - play video games or study for an exam
  - spend a vacation at the beach or in the mountains
- The value of the foregone option is the opportunity cost of the option selected

How does a market work? **Demand and supply**

DEMAND

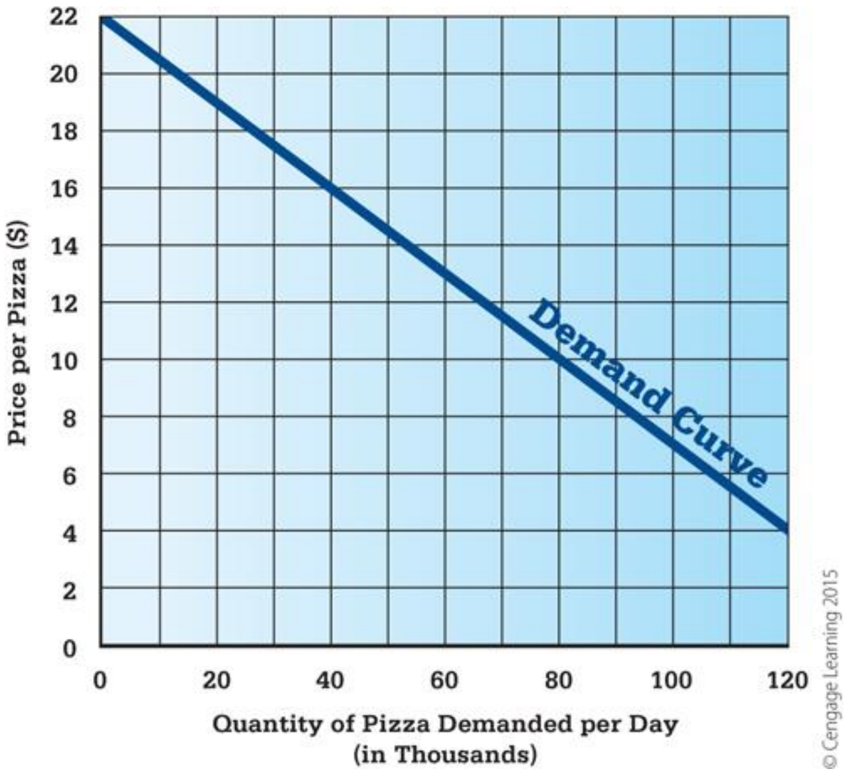
Quantity of products that consumers are willing and able to buy at different market prices

Factors affecting the demand of a particular good:
good's own price; prices of related goods; income; tastes...

$$Q_x = f\,(\,P_x\,;\,\underbrace{P_1\,...\,P_{x-1}\,;\,I\,;\,T\,...}_{}\,)$$

ceteris paribus = remain constant

Demand curve:
Graphed relationship between price and quantity from a demand standpoint



How does a market work? **Demand and supply**

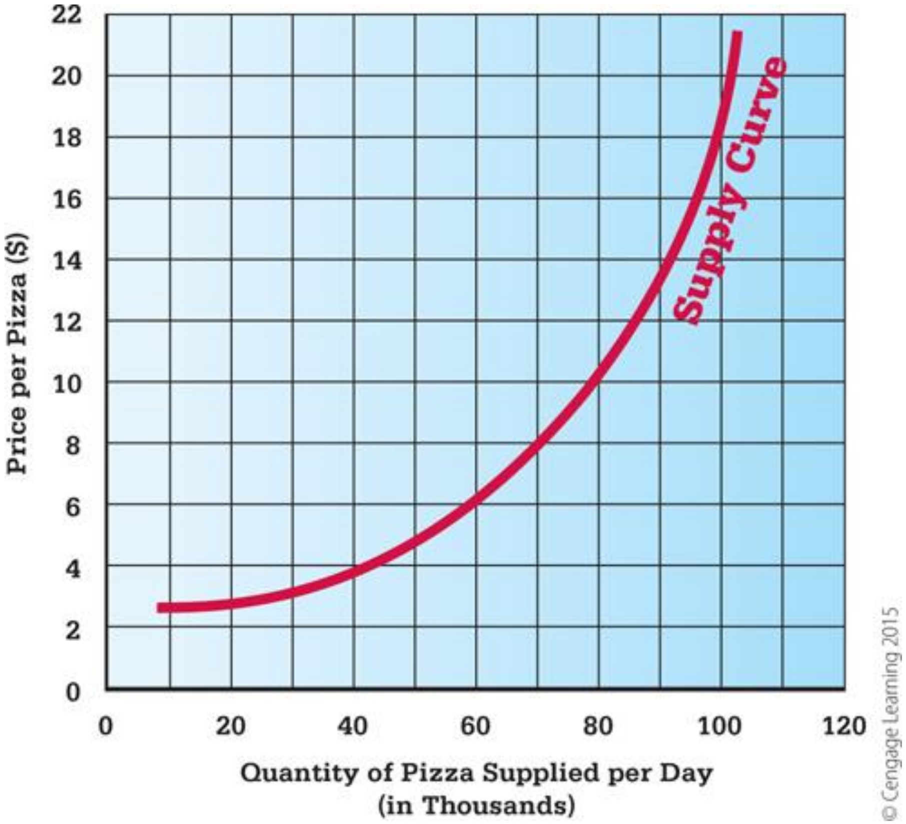
SUPPLY

Quantity of products that producers are willing and able to offer for sale at different market prices

Factors affecting the supply of a particular good:
good's own price; prices of inputs; technology...

$$Q_x = f\ (\ P_x\ ;\ \underbrace{F_1\ ...\ F_z\ ;\ Tech\ ...}_{\textit{ceteris paribus} = \text{remain constant}})$$

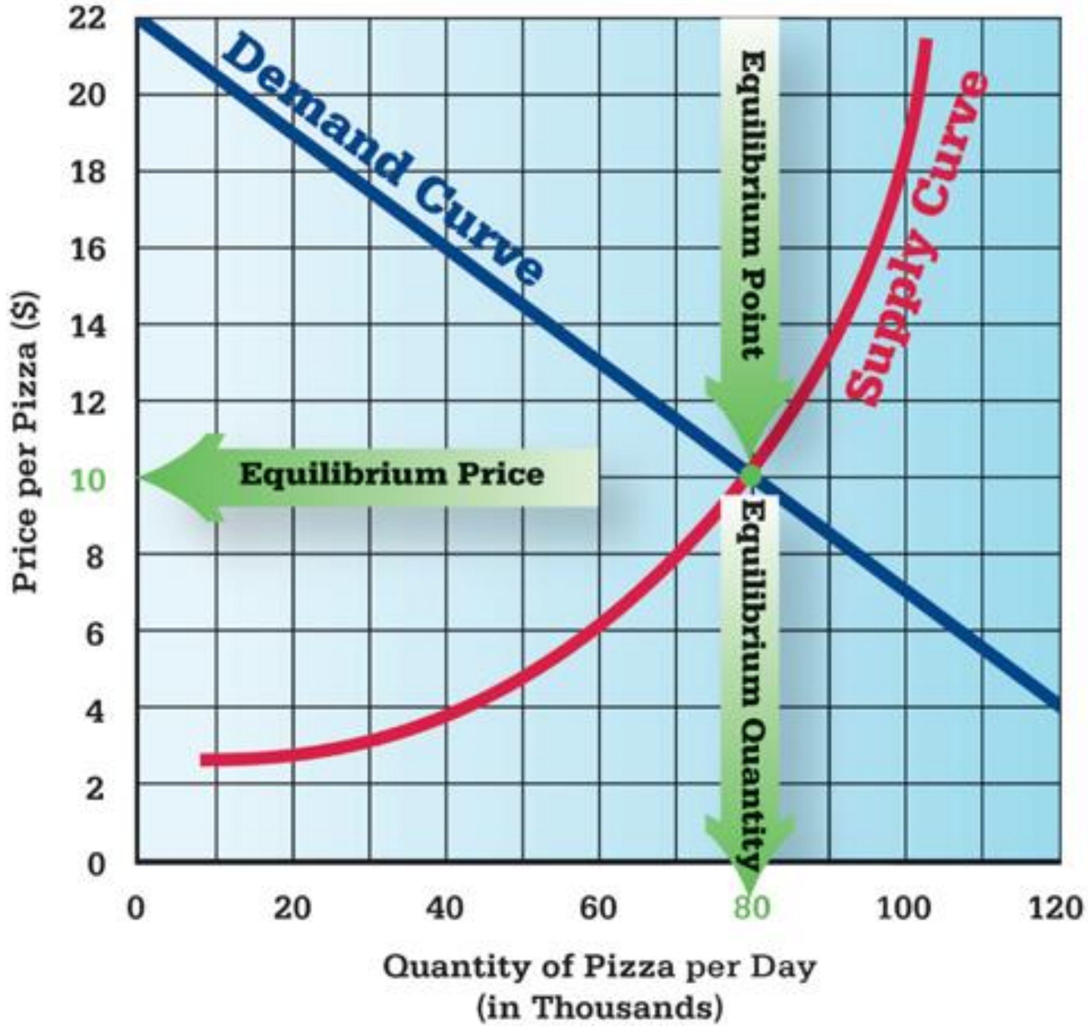
Supply curve:
Graphed relationship between price and quantity from a supplier standpoint



How does a market work? **Demand and supply**

DEMAND AND SUPPLY

The interaction of demand and supply ("invisible hand") establishes the market equilibrium price



How does a market work? **Demand and supply**

DEMAND AND SUPPLY

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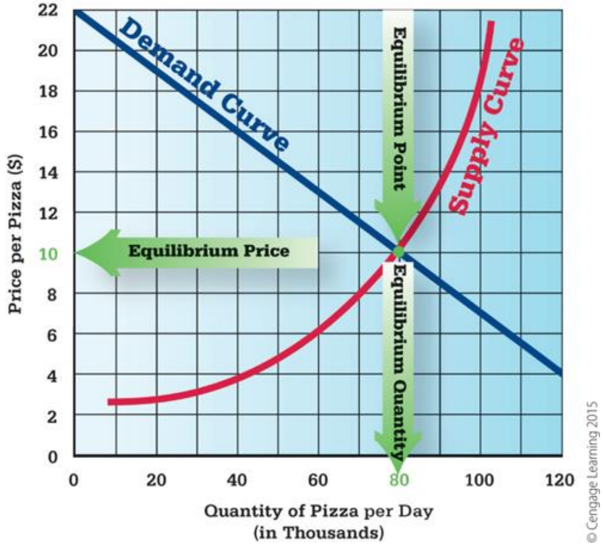
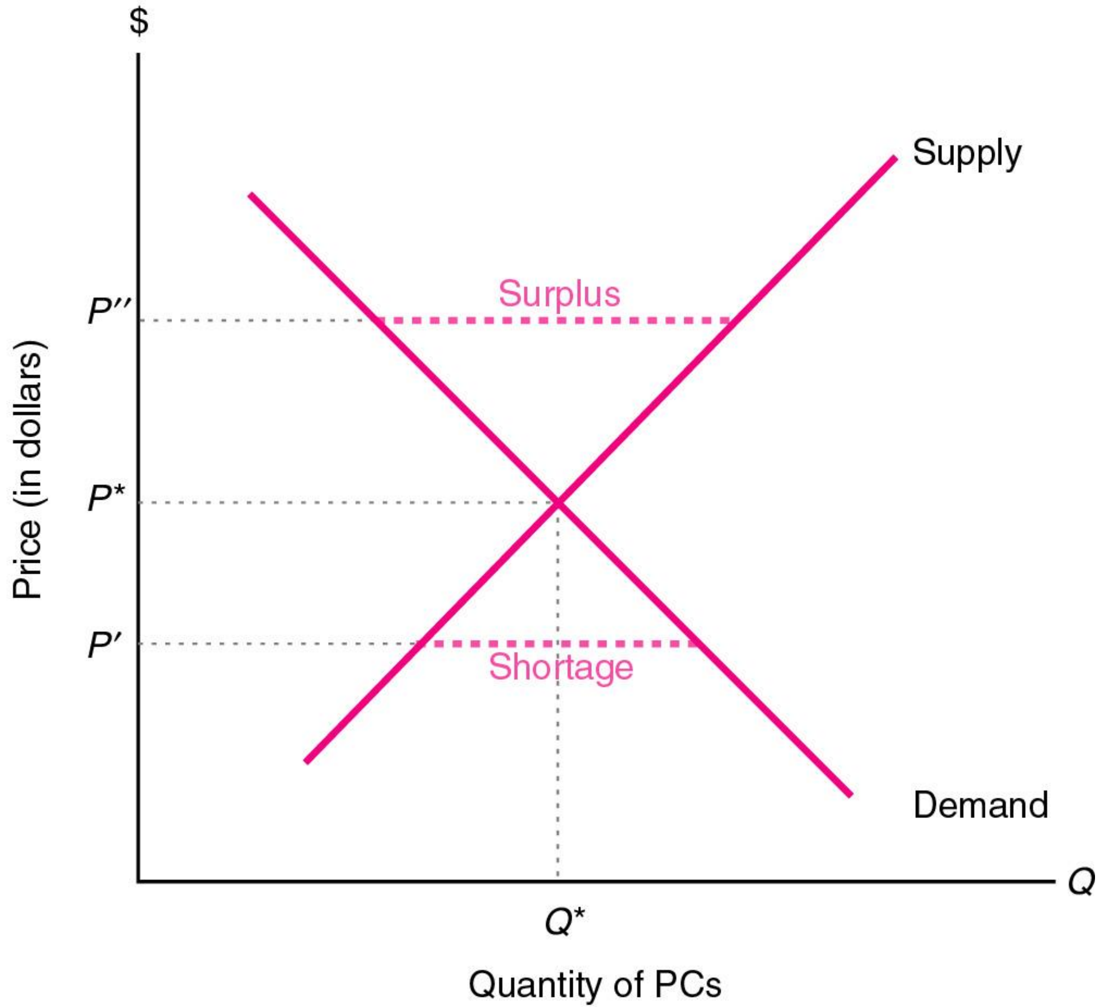


What happens if the price changes? Movement <u>along</u> the curve

What happens if any other factor changes? Movement <u>of</u> the curve

Supply and demand in the PC industry

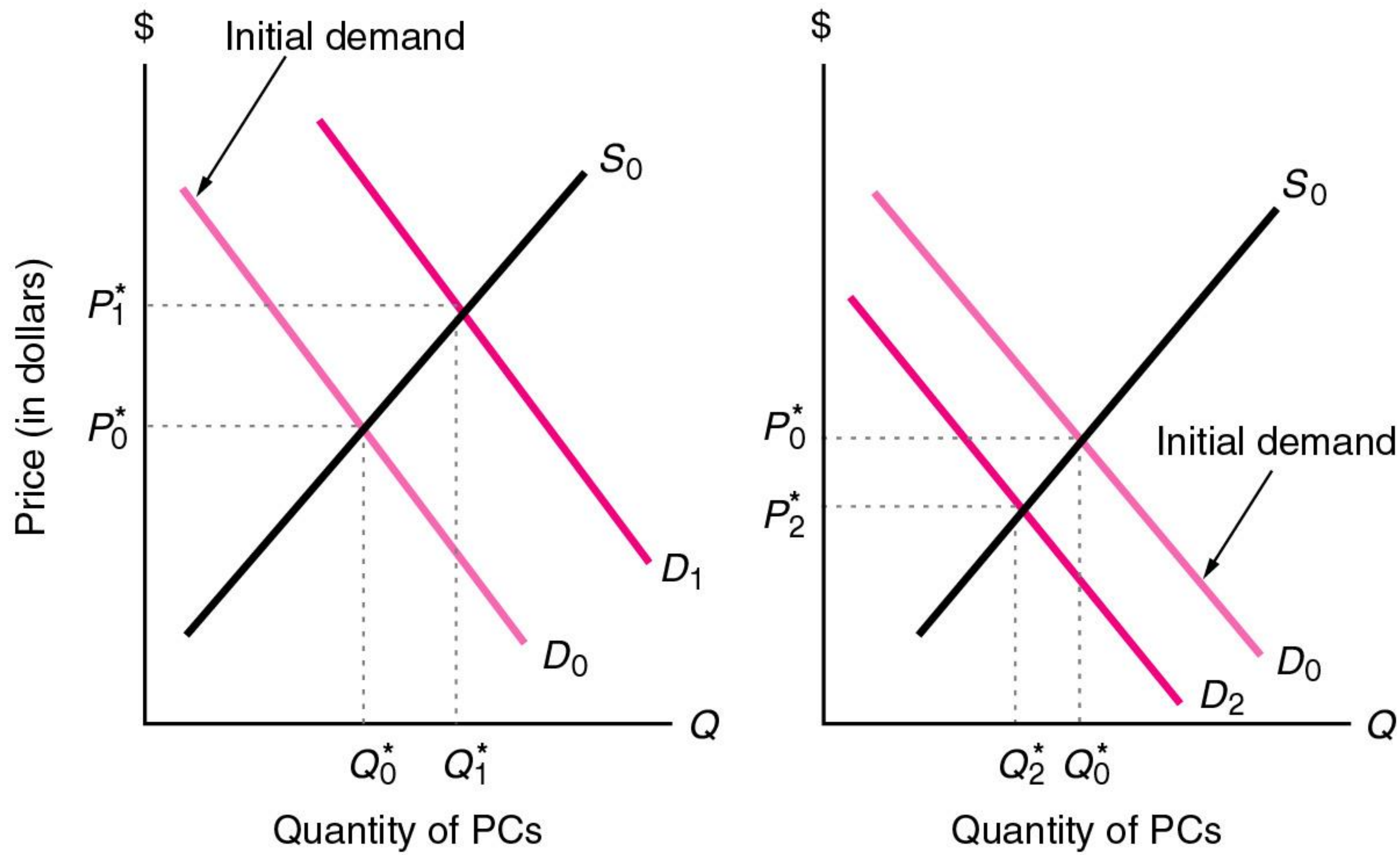
What happens if the price changes? Movement along the curve



How does a market work? **Demand and supply**

Effects of demand shifts

What happens if any other factor changes? Movement <u>of</u> the curve

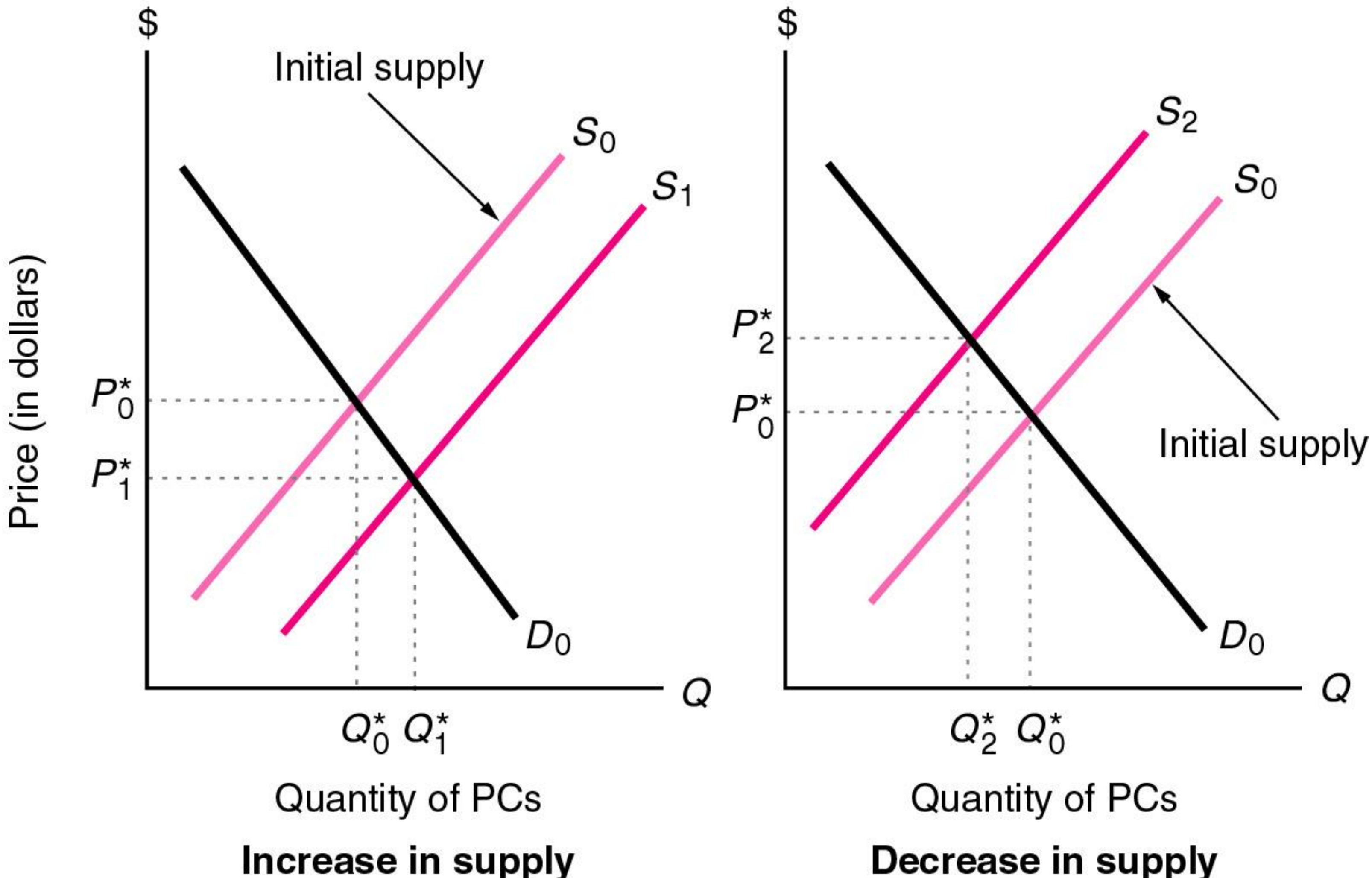


Increase in demand

Decrease in demand

How does a market work? **Demand and supply**

Effects of supply shifts



Determinants of demand shifts to the right (increase)

More fashionable good
Income increase (normal goods) or income decrease (inferior goods)
Price increase of substitute goods
Price decrease of complementary goods

Determinants of supply shifts to the right (increase)

Technology innovation
Inputs price decrease
Inputs surplus

Shifts coming from changes in income

- When income increases, the demand for a normal good will also increase.

- When income increases, the demand for an inferior good will decrease.

How are markets organized? Market structures

Important features of the structure of a market:

- The degree of concentration: number of buyers and sellers
- The degree of product differentiation
- Information

How are markets organized? Market structures

Pure competition	Wheat, peanuts
Monopolistic competition	Clothing, shoes
Oligopoly	Automobiles
Monopoly	Software protected by copyright, many local public utilities

How are markets organized? Market structures

Pure competition

Assumptions:

- **Large number of buyers and sellers**
- No entry and exit barriers
- **Perfect information**
- **Homogeneous products**

Outcomes:

- **No long term abnormal profits**
- **A paradise for buyers, a hell for sellers**

Pure competition serves as **a benchmark** against which to measure real-life imperfectly competitive markets

How are markets organized? Market structures

Assumptions:

- **Single seller**
- High entry barriers
- **No close substitutes for the product**

Outcomes:

- **Long term abnormal profits**
- **A paradise for the seller, a hell for consumers**

Sources of monopoly power:

- Nature of that product makes a single supplier more efficient
- Government sanctioned and regulated