

# MICROECONOMICS

Course no. 1

Assist.Prof. Alin Artene PhD

The evolution of economic  
thinking

Fundamental economic problems

Utility - the optimum of the  
consumer

# Economic thinking

- 1. Mercantilism
- Events that took place during that period



Martin Luther



Mihai Viteazul

Machiavelli elaborate the Principles



Galileo Galilei  
inventor of the pendulum and thermometer



Miguel de Cervantes



# Mercantilism



William Petty

Jean Bodin



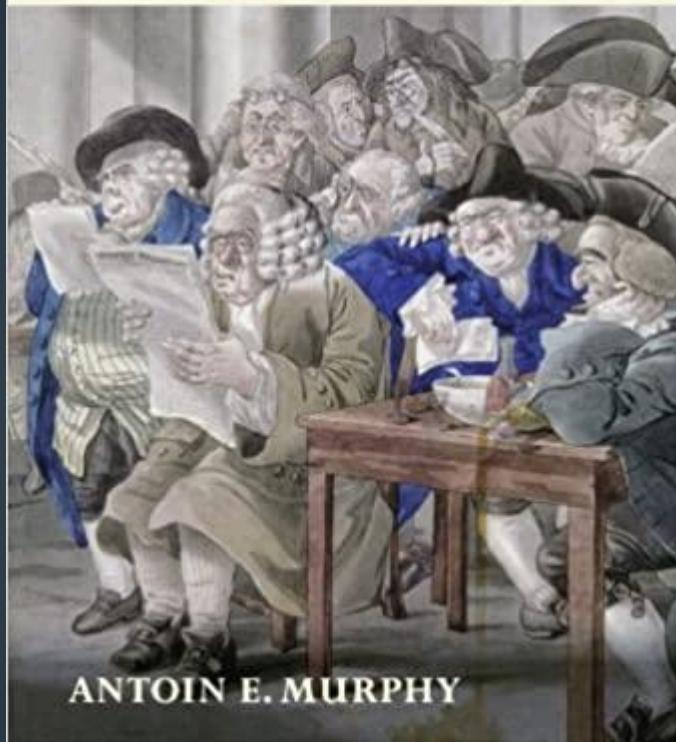
- It appears against the backdrop of the formation of national states and the desire to assert national power
- Precious metals were the main form of wealth that allowed the economic development of a society
- The economy focused on getting vast quantities of gold
  - Through exports greater than imports



OXFORD

# THE GENESIS OF MACROECONOMICS

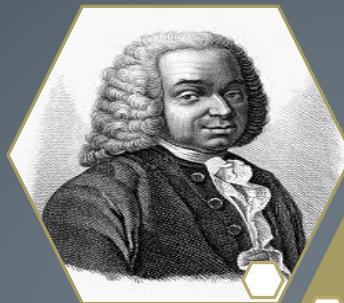
NEW IDEAS FROM SIR WILLIAM PETTY  
TO HENRY THORNTON



- 2. The physiocratic current
- Events that took place during that period



# Physiocracy



François  
Quesnay

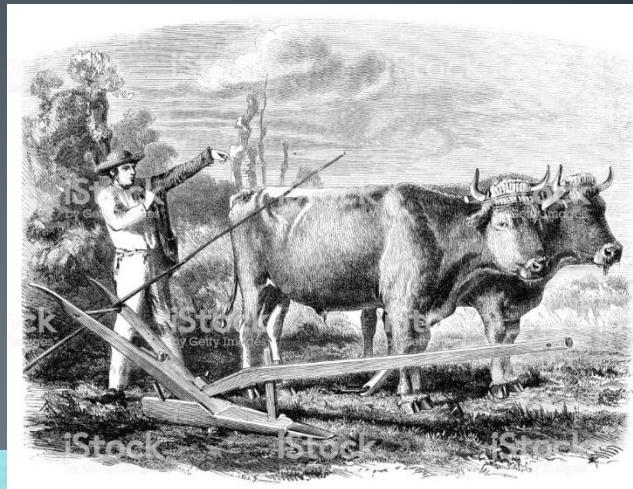
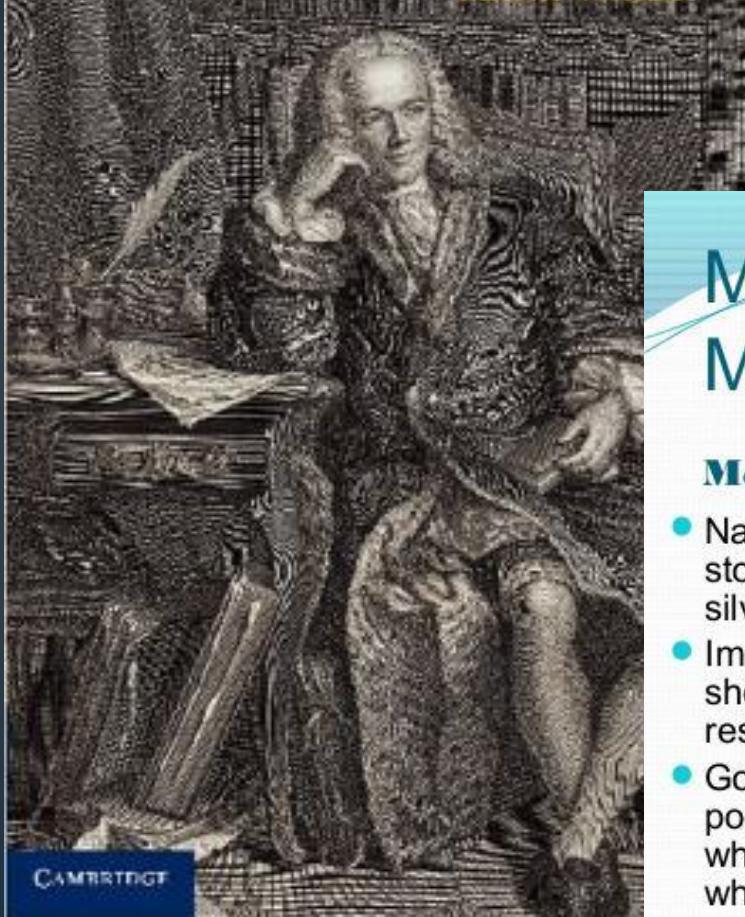
Jacques  
Turgot



- The idea of natural order appears
- Agriculture is the only productive branch that adds value, not commerce

## THE PHYSIOCRATS AND THE WORLD OF THE ENLIGHTENMENT

LIANA VARDI



## Main Differences Between Mercantilists & Physiocrats

### Mercantilist

- Nations wealth determined by store of precious metals (gold & silver)
- Importation of foreign goods should be limited through restrictions/high tariffs
- Government needed to control population patterns by dictating where people can live and where they may work in order to ensure productivity

### Physiocrats

- Nations real wealth derived from land & natural resources
- Free trade should be encouraged among nations through the absence of excessive laws & taxes
- Government should allow people to make own choices
- Because free labor is more productive

- 3. Economic classicism

- Events that took place during that period

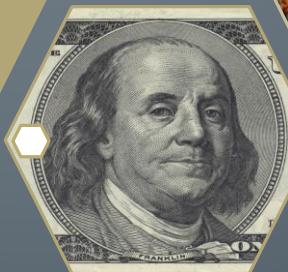


USA -  
Declaration of  
Independence



Wolfgang  
Amadeus  
Mozart

Benjamin  
Franklin



The Fanariot  
regime in the  
Romanian  
Countries



James Cook



# Classical economics



Thomas  
Robert  
Malthus



Adam  
Smith

David  
Ricardo



- "The wealth of nations" (Adam Smith) marks the emergence of a new stream of economic thinking
- In the economy there are different automatic adjustment mechanisms
- Economic activity must be allowed to run freely, with as few interventions as possible.
- The industrial production process is analyzed
- New concepts appear: productivity, objective value of goods

## THE MARKET

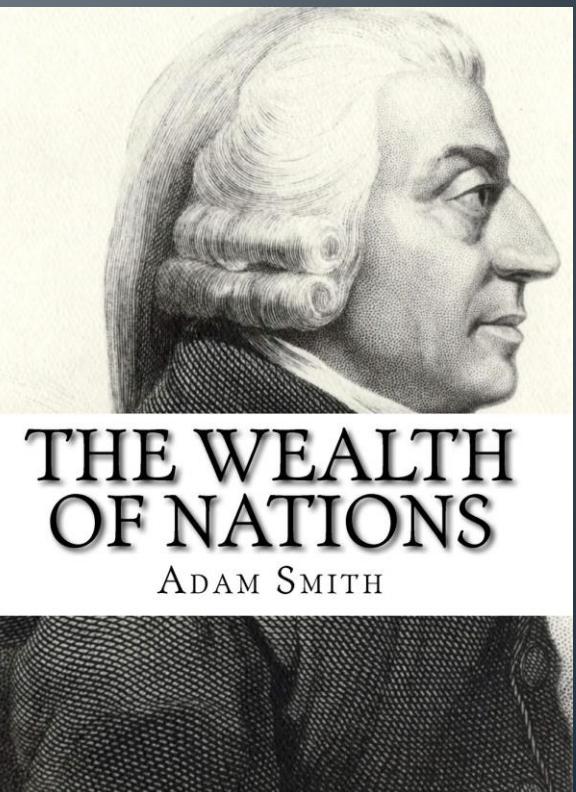
- ❖ Society can depend on unregulated capitalist markets rather than tradition or authoritarianism
- ❖ Self interest (guided by profit) motivates people to perform tasks required by society (what people are willing to pay for)
- ❖ Competition regulates greed i.e. over chargers lose to those that charge cheaper, even for wages
- ❖ Thus pursuit of self interest leads to communal prosperity
- ❖ Depends on freedom to pursue self interest and compete

## THE INVISIBLE HAND

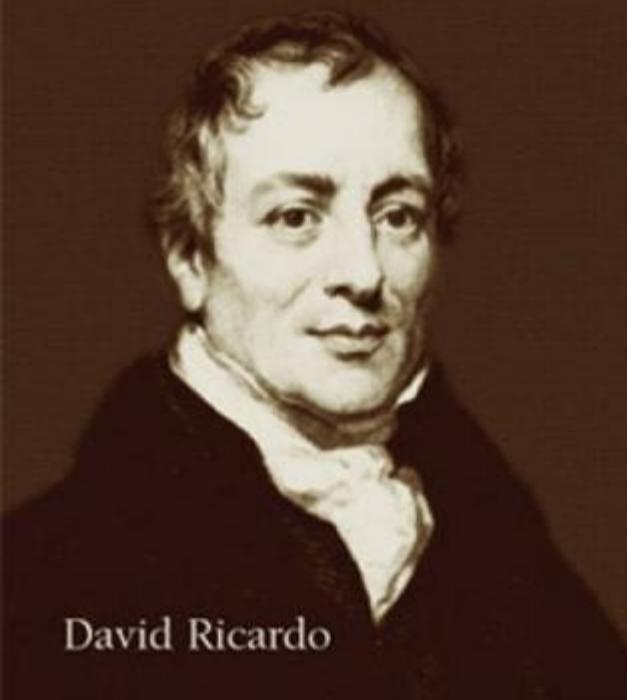
- ❖ Supply and demand always uses prices and profits to signal to producers that society required. Thus producers, in search of profits, produce what society requires - in the correct quantity and at a competitive price.
- ❖ Too little of a good produced for society - high demand for low supply leads to high profit from high prices so attracts more effort into production and vice versa until at 'equilibrium'

## LEGACY

- ❖ Formalized economic thinking - presented both sides whilst giving evaluative factors, then argued for his opinion on the best means for prosperity
- ❖ Optimism in dynamic progression of society
- ❖ Long discussions and digressions on prominent economic themes of his day



THE PRINCIPLES OF  
POLITICAL ECONOMY  
AND TAXATION



David Ricardo

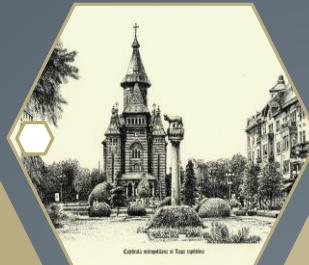
## What Is Ricardo's Theory Of Comparative Advantage?

- ❖ David Ricardo asked what might happen when one country has an absolute advantage in the production of all goods
- ❖ Ricardo's theory of **comparative advantage** suggests that countries should specialize in the production of those goods they produce most efficiently and buy goods that they produce less efficiently from other countries, even if this means buying goods from other countries that they could produce more efficiently at home

- 4. Marxism
- 5. Neoclassicism



Antiviral  
vaccine  
appears in  
Europe

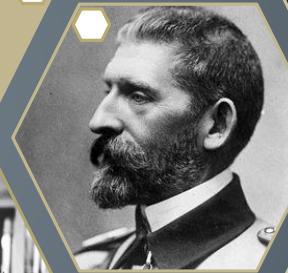


Spain sells  
Florida to the  
United States

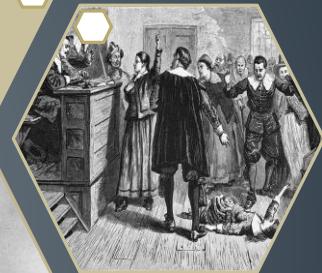
George Enescu  
enters the  
Conservatory



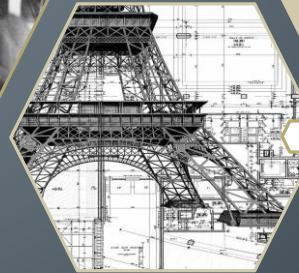
King Ferdinand  
becomes an  
inheriting  
prince



The last trial of  
a witch's  
conviction

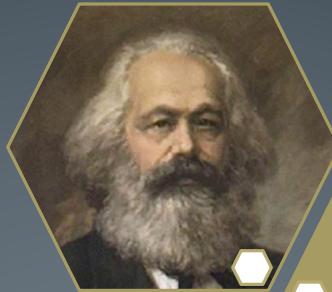


Construction of  
the Eifel Tower



Events that took place during that period

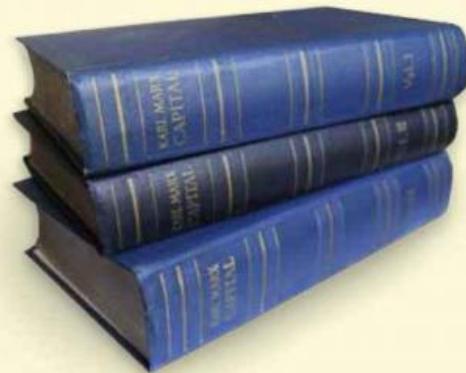
# Marxism



Karl  
Marx

- It is characterized by a pessimistic, catastrophic vision of the evolution of the capitalist system
- The market cannot function satisfactorily, and in the absence of state intervention, the natural evolution of the economy will inevitably lead to failure
- The state must regulate the details of economic life
- Only the fair development of the members of the society can ensure well-being
- Capitalism leads to unequal accumulation of wealth that will cause social tensions and the collapse of this system

AN INTRODUCTION  
*to the*  
THREE VOLUMES of  
**KARL MARX'S  
CAPITAL**

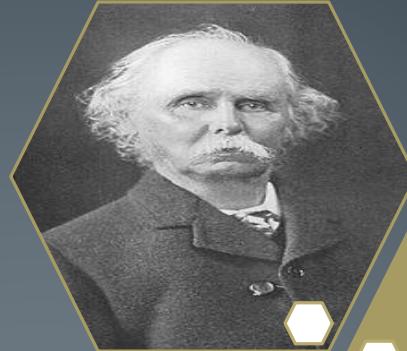


Michael Heinrich

Translated by Alexander Locascio



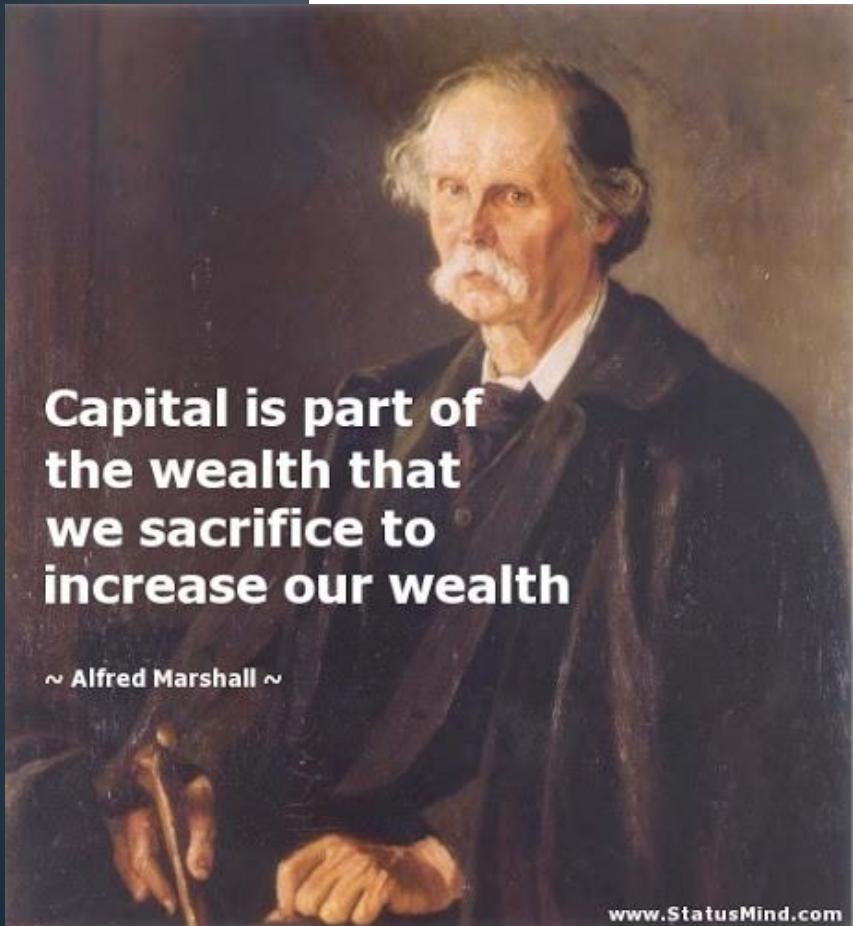
# Neoclassicism



Alfred  
Marshall

- The ideas of liberalism continue
- Emphasis is placed on the microeconomic aspects
- The behavior of the individual economic agent is analyzed
- The marginal analysis is introduced

# ALFRED MARSHALL (1842-1924)



**Capital is part of  
the wealth that  
we sacrifice to  
increase our wealth**

~ Alfred Marshall ~

[www.StatusMind.com](http://www.StatusMind.com)

The Father of Neoclassical Economics (along with Leon Walras)

The Originator of the Principles of Microeconomics

Wrote "The Principles of Economics" (1890)

The Stereotypical Economists ("It depends")

Marshall is a very careful thinker. His thoughts on marginal analysis pre-date Stanley Jevons and Carl Menger, yet his publication of this idea was twenty years after the other two rushed onto the economics landscape.

Perhaps influenced, to some extent, by Mill's hasty conclusion to value theory.

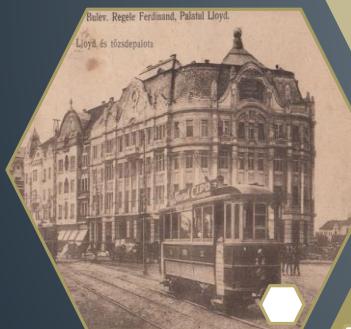
Marshall rarely attempted a statement or took a position without expressing countless qualifications, exceptions, and footnotes. He showed himself to be an astute mathematician—he studied math at St. John's College, Cambridge—but limited his quantitative expressions so that he might appeal to the layman.

<http://www.econlib.org/library/Enc/bios/Marshall.html>



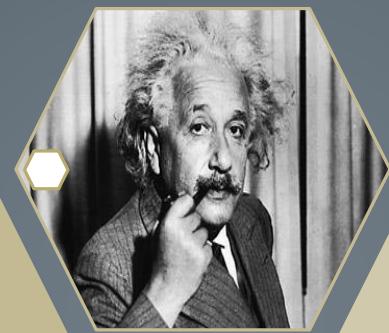
## • 6. Keynesism

Events that took place during that period

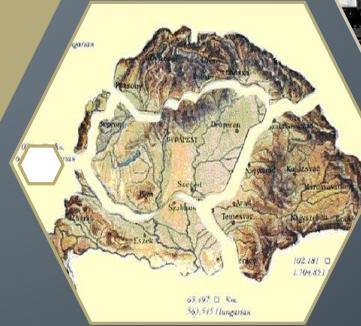


◆ Polytechnic  
University  
of Timisoara

Albert  
Einstein –  
Nobel prize  
in physics



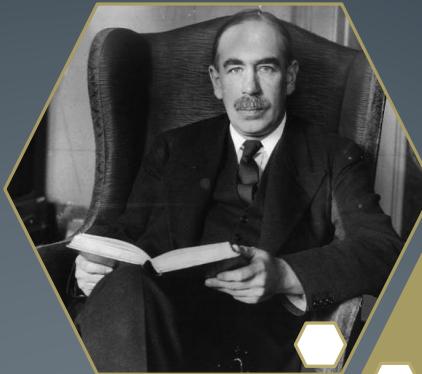
Treaty of  
Trianon



Chrysler is  
established

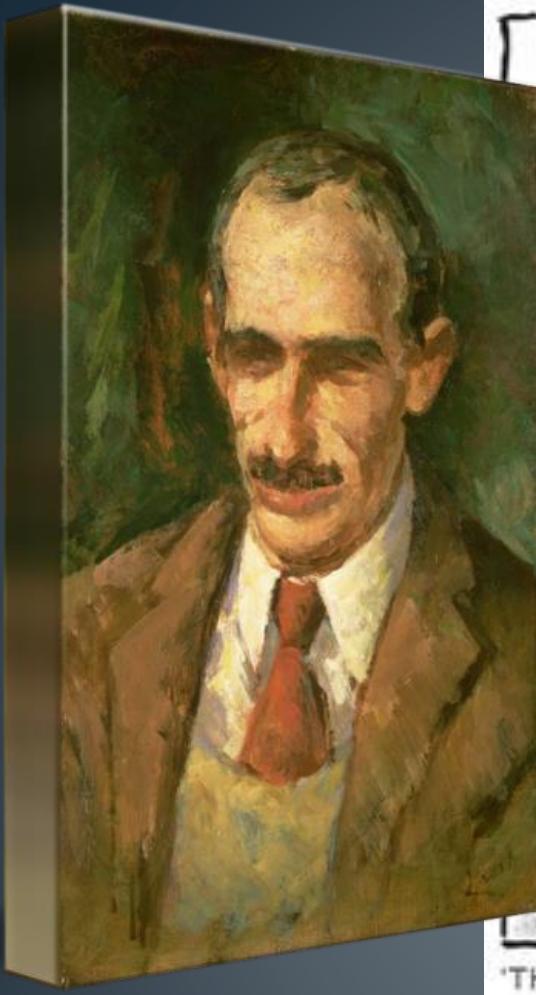


# Keynesism



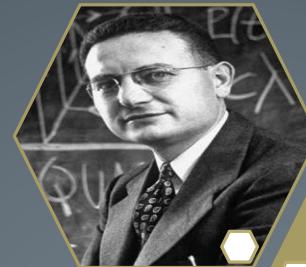
John  
Keynes

- The economic crisis that followed the First World War showed that liberal principles do not work in practice as well as in theory.
- Keynes proposes a theory based on state intervention in the economy
  - The market works well under normal conditions - but sometimes anomalies occur and the state has to intervene to correct them
  - The state intervenes only to provide a framework for economic activities, leaving the market to operate freely



- Keynes developed his theories in response to the Great Depression, and was highly critical of classical economic arguments that natural economic forces and incentives would be sufficient to help the economy recover.
- Activist fiscal and monetary policy are the primary tools recommended by Keynesian economists to manage the economy and fight unemployment.

# Neokeynesism



Paul  
Samuelson

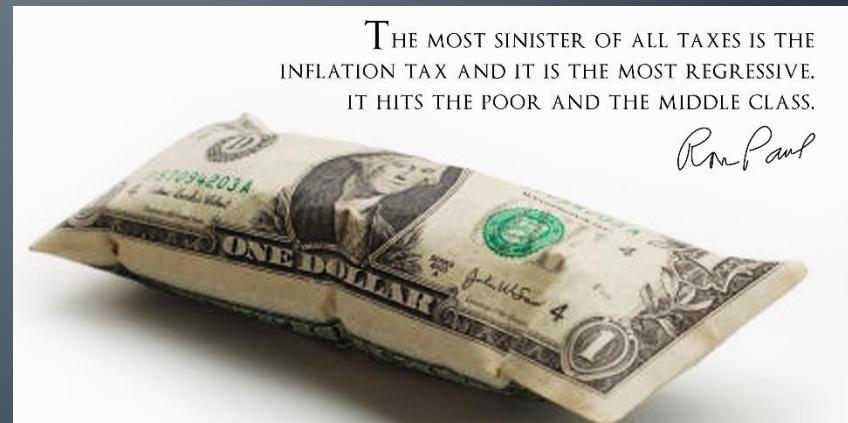


J.K.  
Galbraith

- The idea of state intervention in the economy by other means is maintained
  - State investments
  - State loans
  - Fiscal policies



The **Phillips curve** is a single-equation [economic model](#), named after [William Phillips](#), describing an inverse relationship between rates of [unemployment](#) and corresponding rates of rises in wages that result within an economy. Stated simply, decreased unemployment, (i.e., increased levels of employment) in an economy will correlate with higher rates of wage rises.



THE MOST SINISTER OF ALL TAXES IS THE INFLATION TAX AND IT IS THE MOST REGRESSIVE. IT HITS THE POOR AND THE MIDDLE CLASS.

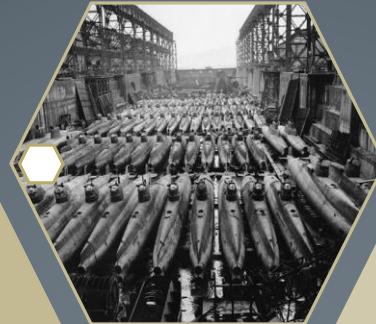
Ron Paul

- 7. Monetarismul



UNICEF is set up

The end of the Second World War



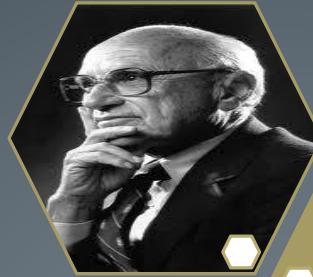
The UN is set up

58/5000  
The Timisoara Opera is set up

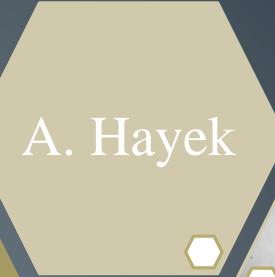


Events that took place during that period

# Monetarism



Milton  
Friedman



A. Hayek

- It is a current that addresses macroeconomic issues
- The role of money in the economy is neutral
  - Increasing the amount of money can only be achieved by raising prices and implicitly inflation
  - By increasing the amount of money in a modern economy, economic activity is not stimulated
  - The idea of an independent monetary policy focused on the objective of price stability appears

# MILTON FRIEDMAN

## ECONOMICS IN THEORY *and* PRACTICE

ABRAHAM HIRSCH NEIL de MARCHI

## Milton Friedman Quantity Theory of Money

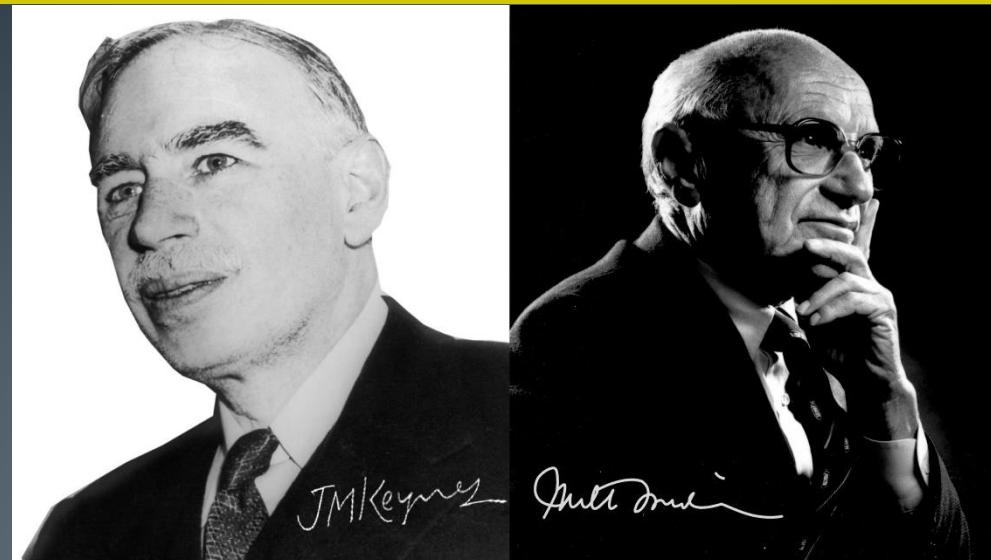
- Quantity Theory of Money-published in 1956
- Descends from Copernicus
- Defied Keynes' theories from the 1930's
- Most noted for his Monetarist argument against Keynesian-Quantity Theory of Money, and Policy Lag
- Friedman presented evidence to resurrect the quantity theory of money

If you put the **federal government**  
in charge of the **Sahara Desert**, in  
5 years there'd be  
a **shortage of sand**.

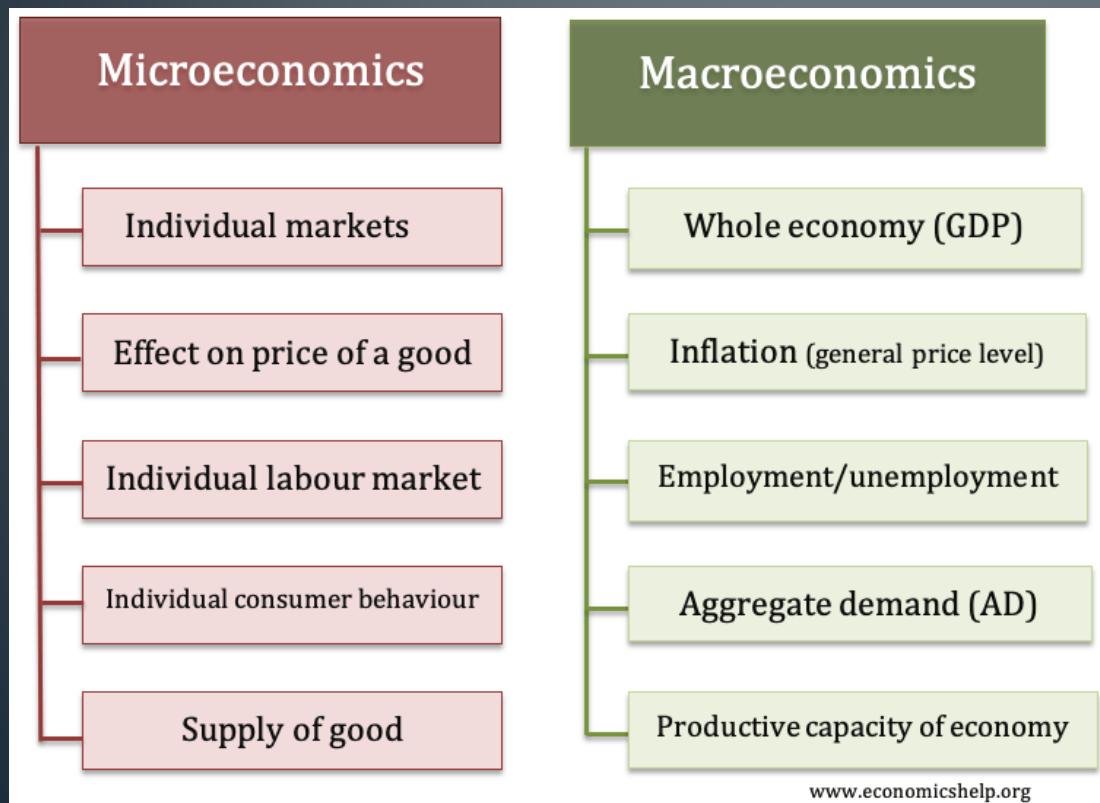
- Milton Friedman

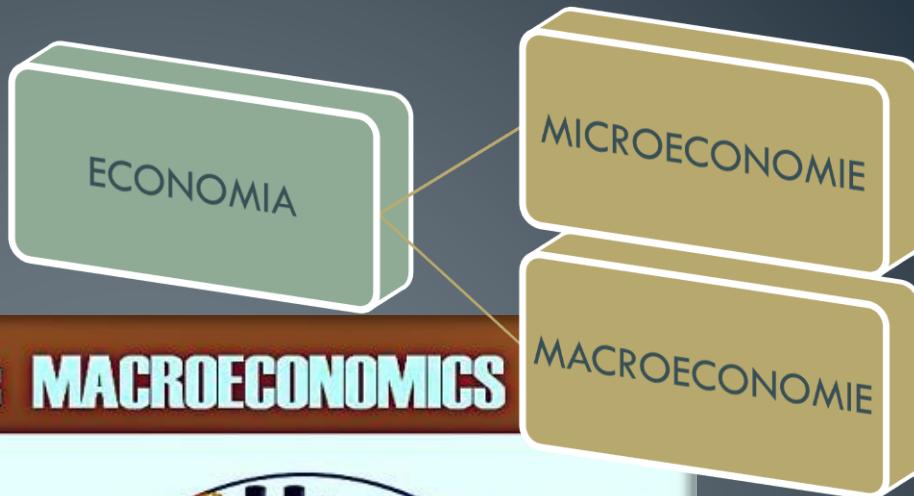
AZQUOTES





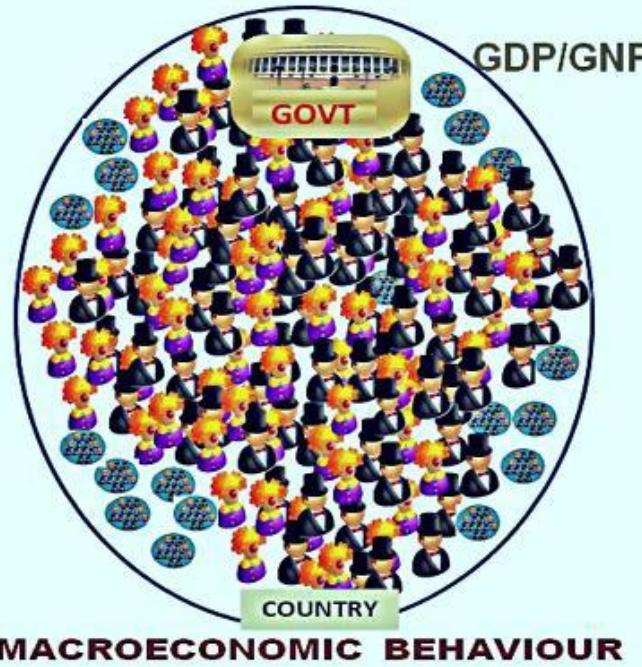
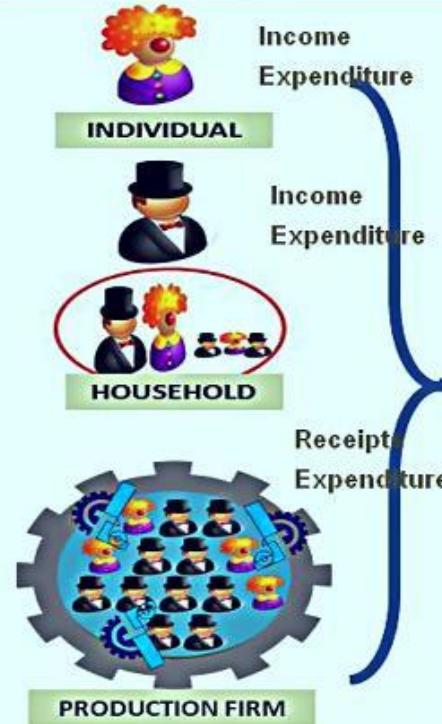
	<b>Keynesian view</b>	<b>Monetarist view</b>
<b>Fiscal policy</b>	In recession, expansionary fiscal policy can stimulate economic activity	Fiscal policy causes no long-term increase in real output
<b>Wage rigidity</b>	Wages can be sticky downwards causing unemployment	In absence of min wages/ trade unions wages flexible.
<b>Unemployment</b>	Demand-deficient unemployment big causes	Tend to emphasize supply-side unemployment (natural rate)
<b>Phillips Curve</b>	There is a trade off between unemployment and inflation	Only a trade-off in the short-term.
<b>Government borrowing</b>	In recession, governments should borrow more to offset fall in private spending	Government should seek to run balanced budget
<b>Crowding out</b>	No crowding out in recession	Government borrowing causes more crowding out





## MICROECONOMICS Vs MACROECONOMICS

### MICROECONOMIC BEHAVIOUR





The economic activity :  
the set of actions by which  
people meet their needs  
through the production and  
exchange of goods and  
services



What happens in the  
economy?

Goods and services that are  
the subject of transactions  
between economic agents

What should be produced?

How much should be produced?

Questions

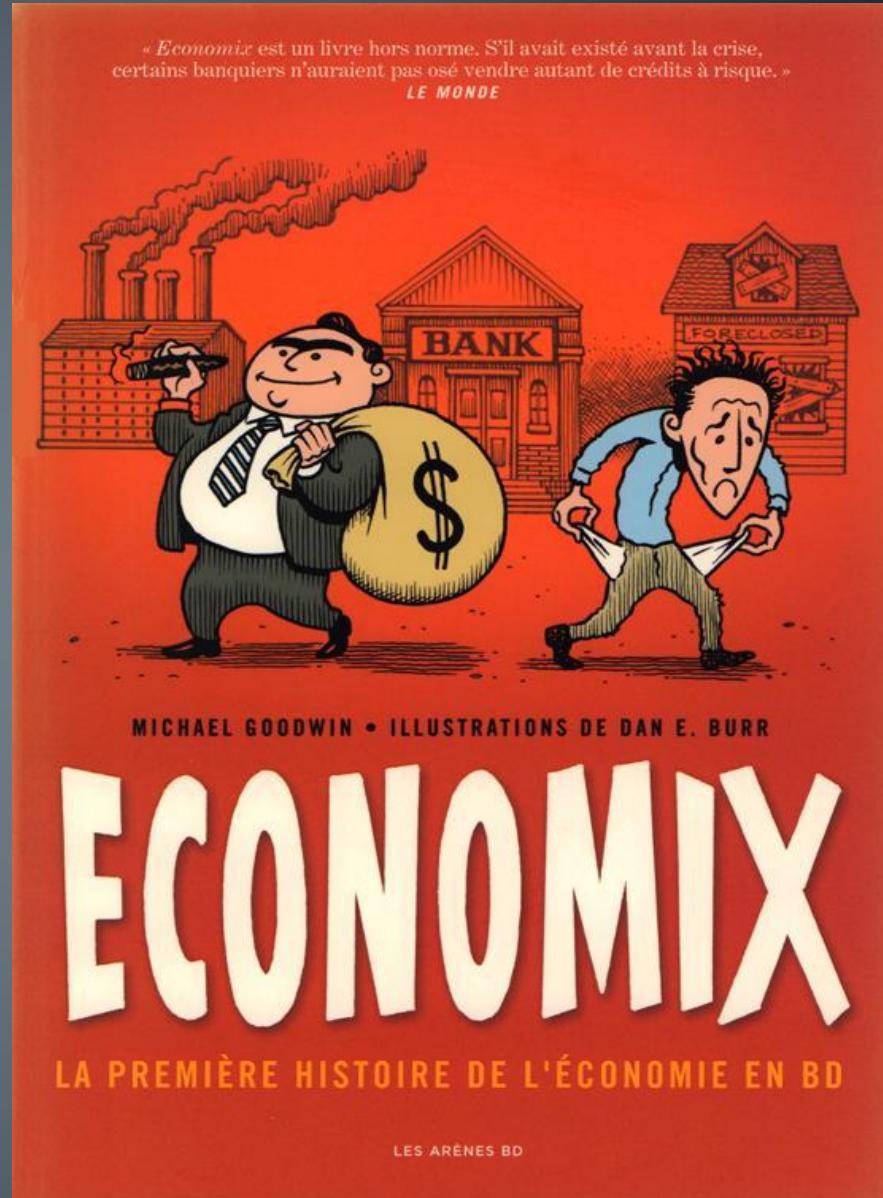
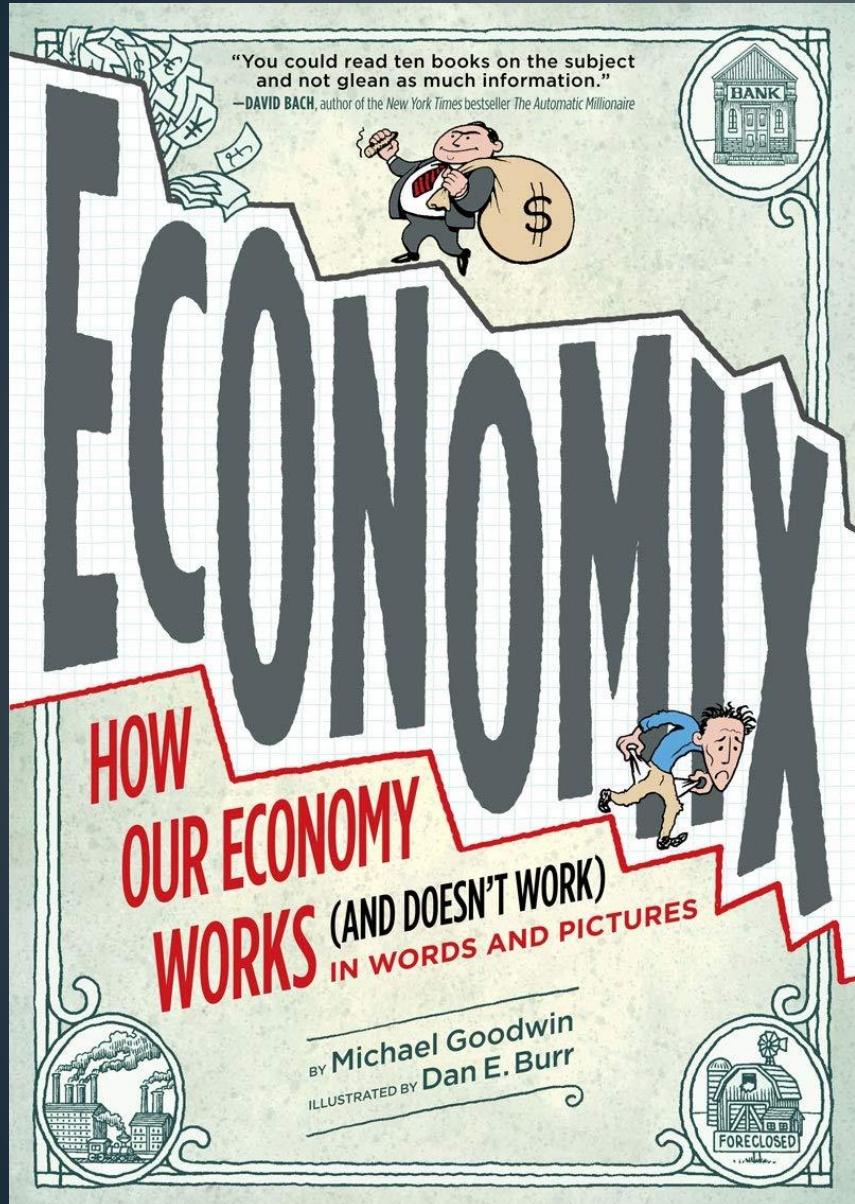
How should it be produced?

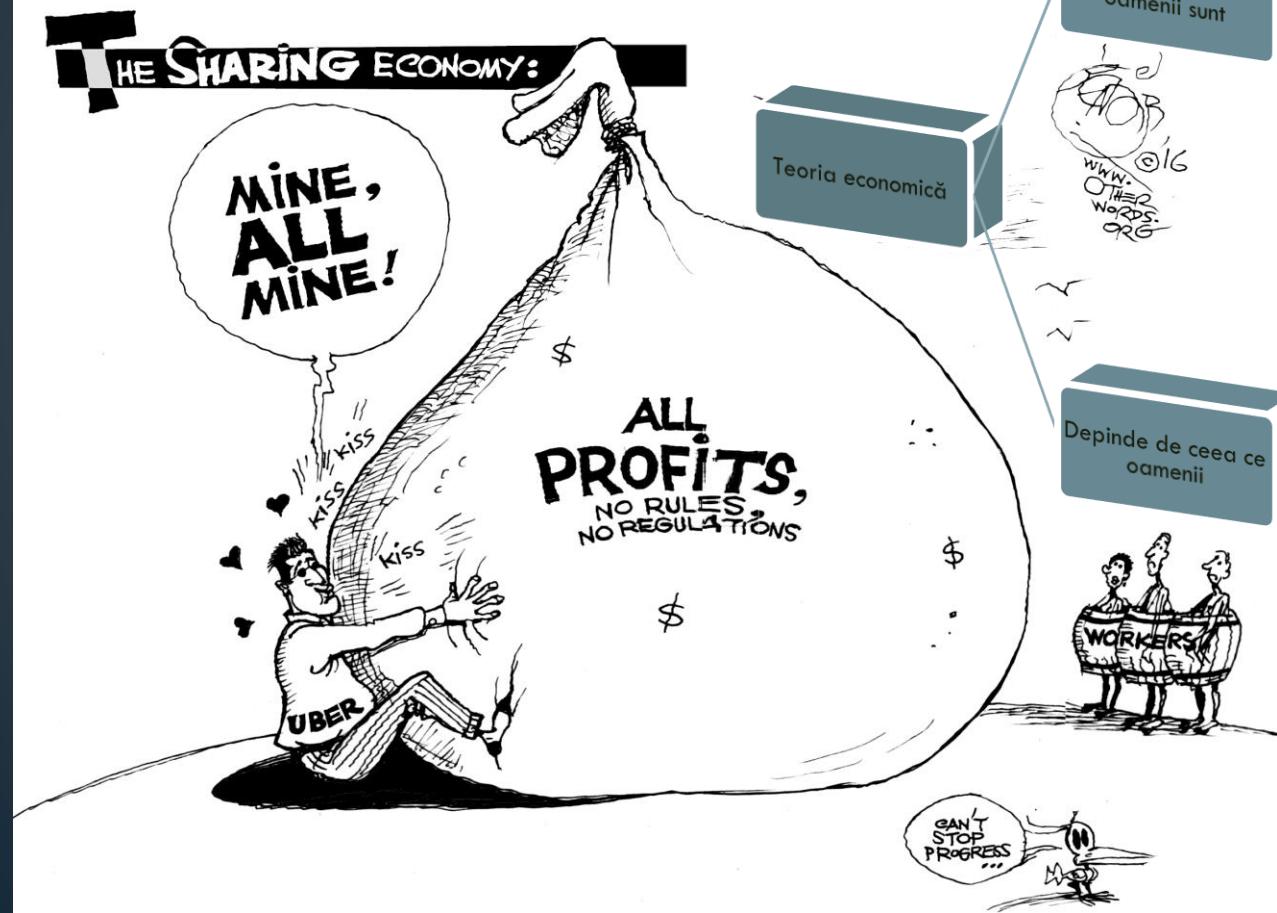
Who is the recipient of the product?

Economic thinking researches all types of choices as well as unintended consequences - unanticipated side effects



- A social group is made up of individuals who choose based on the benefits and costs they expect





# Utility and consumer

- Utility generally means the ability of a good to meet a need (need).
- The utility in the economic sense represents the satisfaction that a consumer feels by using a quantity determined by a good obtained on the market, through the process of sale-purchase.
- Goods represents any element of reality that satisfies a need (personal consumption or productive consumption)

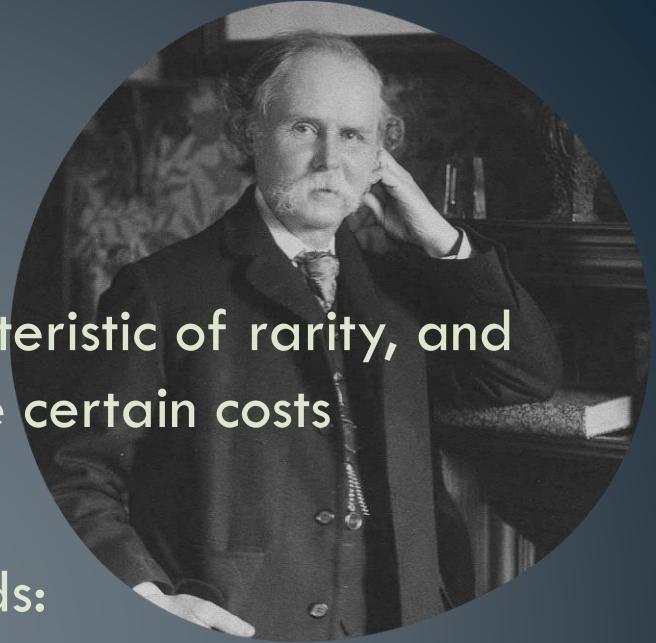
# Classification of goods

By their provenance :

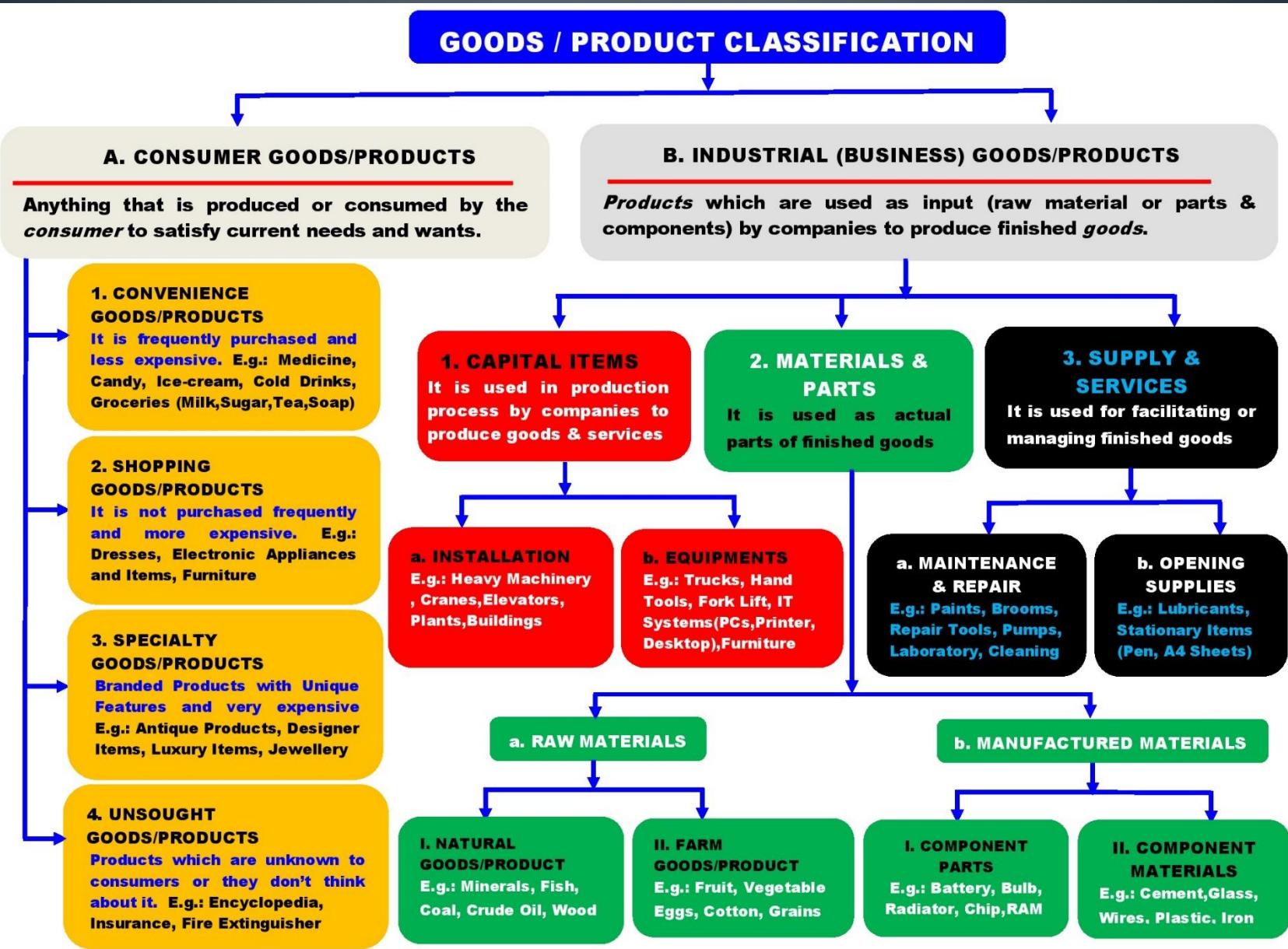
- **Free goods** - are available in unlimited quantities and anyone can use them as needed
- resources that are abundantly found in nature in such a way that anyone can benefit from them: air, sun, water, etc
- intellectual work, ideas, except copyright, Google, Wikipedia, etc.

# Classification of goods

- Economic goods – they have the characteristic of rarity, and their obtaining and consumption require certain costs
- Alfred Marshall – about economic goods:  
*„Economic goods include all those goods - external to man - that belong to him and do not belong to his neighbors in the same degree. Therefore, they are their own and can be measured directly through monetary unity, a measure that expresses, on the one hand, the efforts and sacrifices necessary for them to appear in the world and, on the other, the needs that are met through them.”*

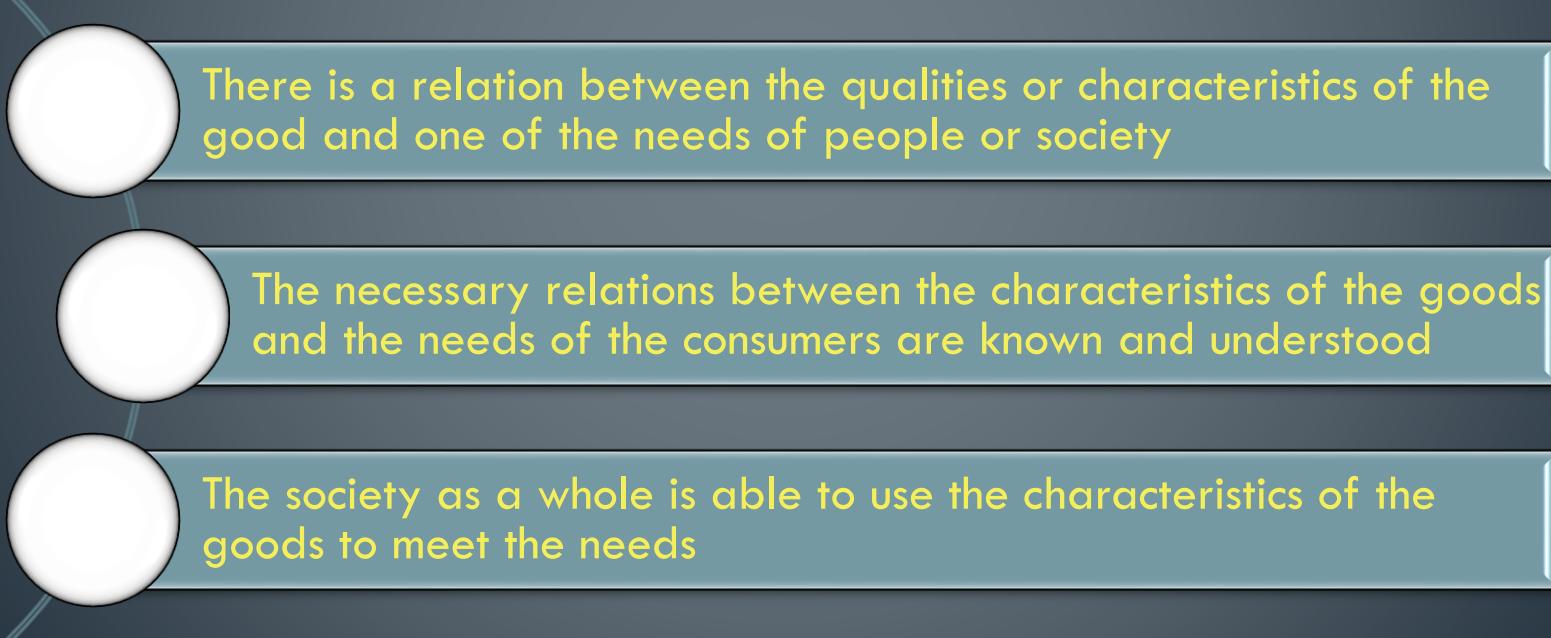


# Typology of economic goods



The economic goods must enjoy the appreciation of the consumers so that they have utility.

## Utility gains economic meaning



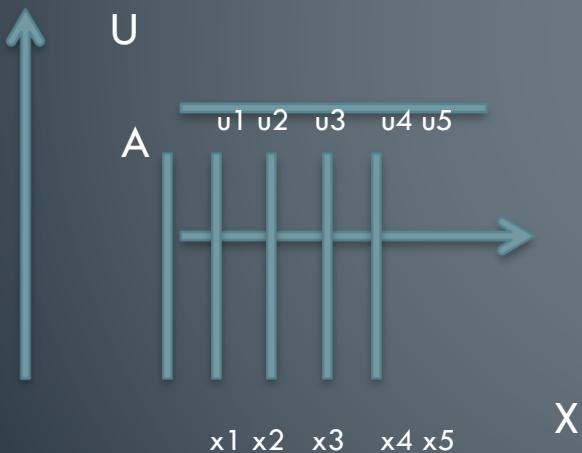
There is a relation between the qualities or characteristics of the good and one of the needs of people or society

The necessary relations between the characteristics of the goods and the needs of the consumers are known and understood

The society as a whole is able to use the characteristics of the goods to meet the needs

# Unitary utility

- **Unitary utility** – satisfaction of the intensity of desire, of the need brought by a dose of a good X consumed by an individual
- The consumer - is able to measure the usefulness of each good, expressing it in a number of abstract (useful) units

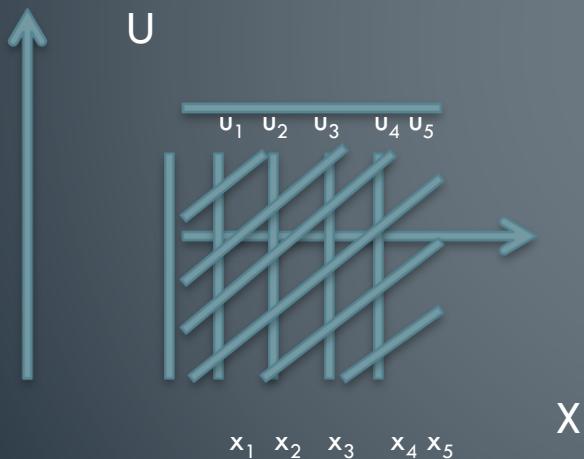


The elements  $x_1, x_2, x_3, x_4, x_5 \dots x_X$  belonging to the set X have identical utilities  $u_1, u_2, u_3, u_4, u_5 \dots u$

$$A = u_1(x_1) = u_2(x_2) = u_3(x_3) = u_4(x_4) = u_5(x_5)$$

# Total utility

- **Total utility** – the satisfaction felt by an individual after consuming all doses of a good, in a given period



A good X consists of n doses:  $x_1, x_2, x_3, x_4, x_5, \dots, x_n$ , having as individual utility  $u_1, u_2, u_3, u_4, u_5, \dots, a$

The total utility is determined by the formula:

$$UT = U_1 + U_2 + U_3 + \dots + U_n = \sum U_x$$

The total utility is represented by the hatched surface

# Marginal utility

Marginal utility quantifies the added satisfaction that a [consumer](#) garners from consuming additional units of goods or services. The concept of marginal utility is used by economists to determine how much of an item consumers are willing to purchase. Positive marginal utility occurs when the consumption of an additional item increases the total utility, while negative marginal utility occurs when the consumption of an additional item decreases the total utility.

$$\text{marginal utility} = \frac{\text{Change in Total Utility}}{\text{Change in number of Units consumed}}$$

# The Law Of Diminishing Marginal Utility

## Law of diminishing marginal utility

- **Assumptions:**

- 1. Tastes, preferences, etc of the customer remain constant.
- 2. Income of the consumer also remain constant
- 3. Units of the goods are identical or similar
- 4. The process of consumption is continuous.
- 5. Units of the goods are not very small in size.

- **Importance:**

- 1. Framing taxation policy by the government.
- 2. Useful to consumer to regulate his expenditure.
- 3. Useful to monopolist producer in fixing the prices of his products.
- 4. Basis for law of demand.
- 5. Differentiate value-in-use and value-in-exchange.

„**The Law Of Diminishing Marginal Utility** states that all else equal as consumption increases the marginal utility derived from each additional unit declines. Marginal utility is derived as the change in utility as an additional unit is consumed. Utility is an economic term used to represent satisfaction or happiness. Marginal utility is the incremental increase in utility that results from consumption of one additional unit.”

Mc. Konnell și Brue

# LAW OF DIMINISHING MARGINAL UTILITY:

Burger 1



You are hungry! Eating the burger gives lots of instant satisfaction!



Utility

Burger 2



You are still sort of hungry. Eating another burger gives some satisfaction.

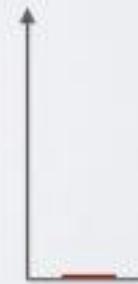


Utility

Burger 3



You are full! Eating the burger gives very little satisfaction.

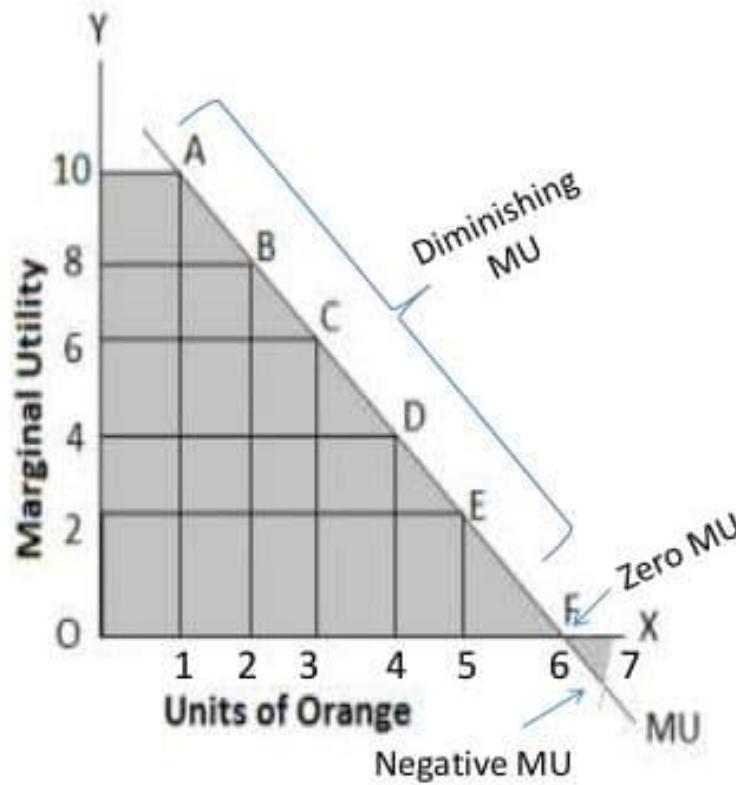


Utility

# Law of Diminishing Marginal Utility

Units	Total Utility	Marginal Utility
1	10	10
2	18	8
3	24	6
4	28	4
5	30	2
6	30	0
7	28	-2

MU curve is downward sloping because of the fact that consumption of successive units gives less satisfaction.

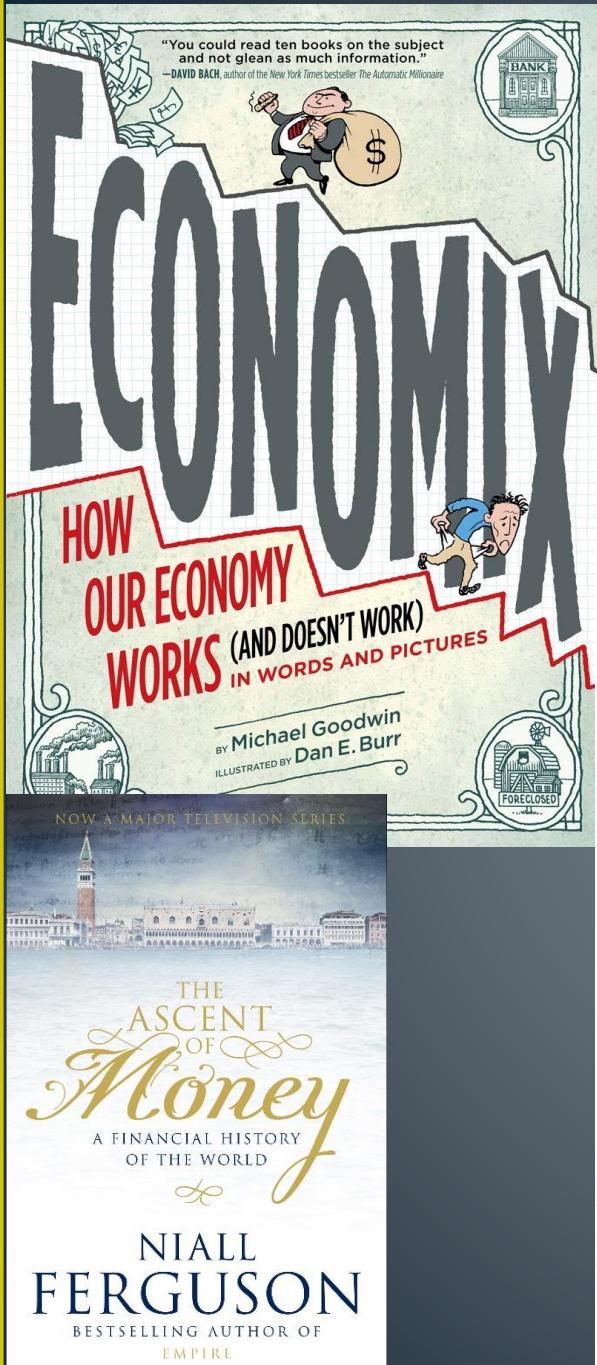


# Consumer optimum

- A **consumer optimum** represents a solution to a problem facing all individuals -- maximizing the satisfaction (utility) from consuming different goods and services subject to the constraint of household income and product prices.
- Now we assume that a consumer consumes only one good and we are looking for optimal quantity of this good, i.e. quantity which consumption will maximize utility of consumer. Finding of the consumer's optimum is based on the assumption that consumer will be willing to pay the asked price for the good only as long as he/she will attribute greater or equal utility to each unit of consumed good (i.e. until  $MU \geq p$ ). He/she will stop his/her consumption (will buy the last good) when the utility of the good will be equal to the price
- If the consumer consumes more goods, we will get the marginal utility function from consumption of each of them by the partial derivation of the total utility function according to amount of the corresponding good. If, for example, a consumer consumes two goods, amount of these two goods must enter even the total utility function. Total utility is therefor the function of the consumed quantity of both goods X and Y:  $TU = f(X, Y)$ .

# The Consumer's Optimal Choice

- ◆ The point at which the indifference curve and the budget constraint touch (i.e. its tangent) is called the optimum.
- ◆ The consumer chooses consumption of the two goods so that the marginal rate of substitution equals the relative price.



# BIBLIOGRAPHY

