Principles of Microeconomics

Mr. Spence

July 9, 2025

Contents

Chapter 1

Supply and Demand

1.1 Introduction

- An economy is a system of producing, distributing, and consuming goods and services.

- Economics is the study of economies.

- Microeconomics is the study of how individuals, households, and firms make decisions and how they interact in specific markets.

- Macroeconomics is the study of society's overall system of production, distribution, and consumption.

1.2 Markets and Competition

- A market is a group of buyers and sellers of a particular good or service.

- A competitive market is a market with so many buyers and sellers that each has a negligible impact on the market price.

- A market is perfectly competitive if:

    1. The goods/services offered for sale are all exactly the same.
    2. The buyers and sellers are so numerous that no single buyer/seller has any influence on the market price.

- Buyers and sellers in perfectly competitive markets are called price takers because they must accept the market price.

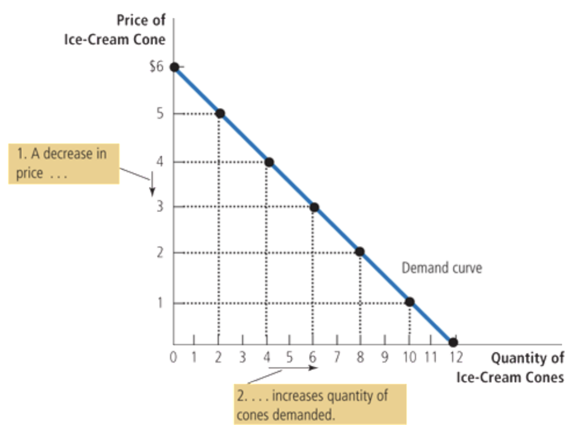
1.3 Demand

1.3.1 The Demand Curve

- The quantity demanded of a good is the amount that buyers are willing and able to purchase.
  - There are many determinants of quantity demanded, but the most important is the good's price.
- Law of Demand: Holding everything else constant, when the price of a good rises, the quantity demanded falls. When the price falls, the quantity demanded rises.
- A demand schedule is a table that shows the relationship between the price of a good and the quantity demanded (holding every other determinant of quantity demanded constant).
- The demand curve is the curve relating price and quantity demanded (holding everything else constant).
  - By convention, price is plotted on the y-axis and quantity demanded is plotted on the x-axis.

Ex. Catherine's Demand Schedule and Curve

Price of Ice-Cream Cone	Quantity of Cones Demanded
$0	12 cones
1	10
2	8
3	6
4	4
5	2
6	0

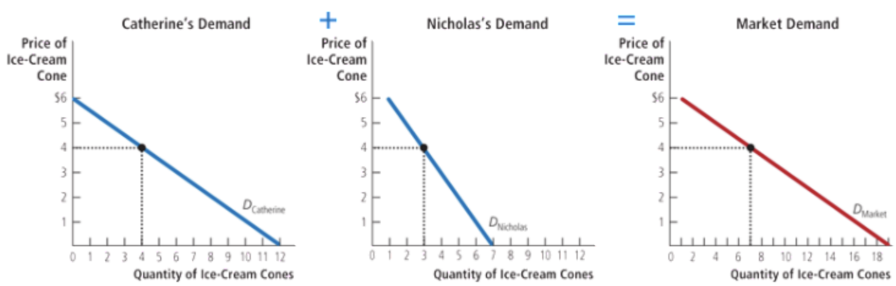


1.3.2 Market Demand

- The quantity demanded in a market is the sum of every individuals' quantity demanded at each price

Ex. Market Demand Schedule and Demand Curve

Price of Ice-Cream Cone	Catherine		Nicholas		Market
$0	12	+	7	=	19 cones
1	10		6		16
2	8		5		13
3	6		4		10
4	4		3		7
5	2		2		4
6	0		1		1



1.3.3 Shifts in the Demand Curve

- If a determinant of quantity demanded other than price changes, the demand curve shifts.

Variables That Shift the Demand Curve:

1. Income:
   - Typically, when people's income falls, their demand for a good falls. If demand for a good falls when income falls, the good is called a normal good.
   - If the demand for a good rises when income falls, the good is called an inferior good.
2. Price of Related Goods:
   - When a fall in the price of one good reduces the demand for another good, the two goods are called substitutes.
     - Substitutes are often goods that are used in place of each other, e.g. ice cream and frozen yogurt
   - When a fall in the price of one good increases the demand for another good, the two goods are called complements

  - Complements are often goods that are used together, e.g. ice cream and ice cream cones.

3. Tastes:

   - If people's tastes (a.k.a. preferences) change, their quantity demanded will change, and the demand curve will shift.

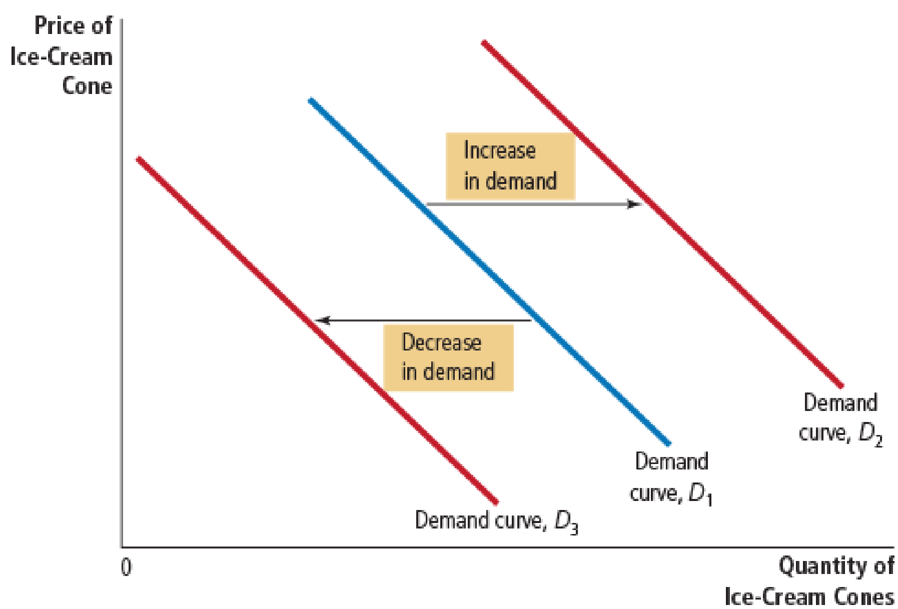
4. Expectations:

   - If people expect a higher price in the future, they will demand more at today's price.
   - If people expect a higher income in the future, they will demand more today.

5. Number of Buyers:

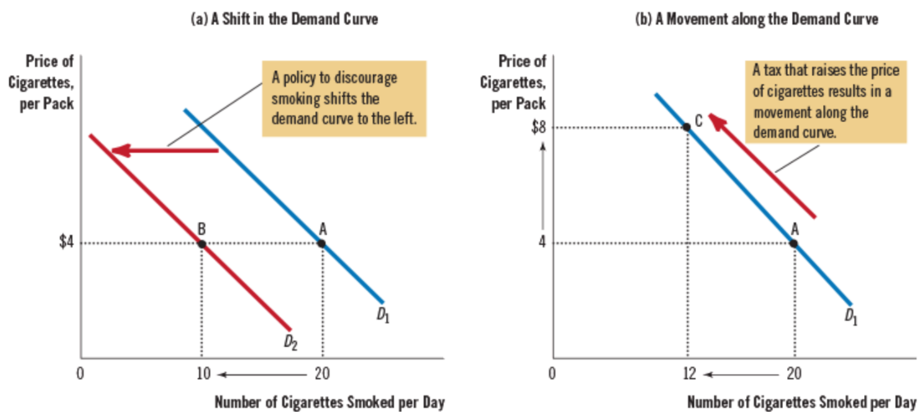
   - An increase in the number of buyers increases demand.
   - A decrease in the number of buyers decreases demand.

Ex. Shifts in the Demand Curve



Warning:

- A change in the price of a good does *not* shift the demand curve for the good.
- A change in the price of a good represents a movement along the demand curve.



1.4 Supply

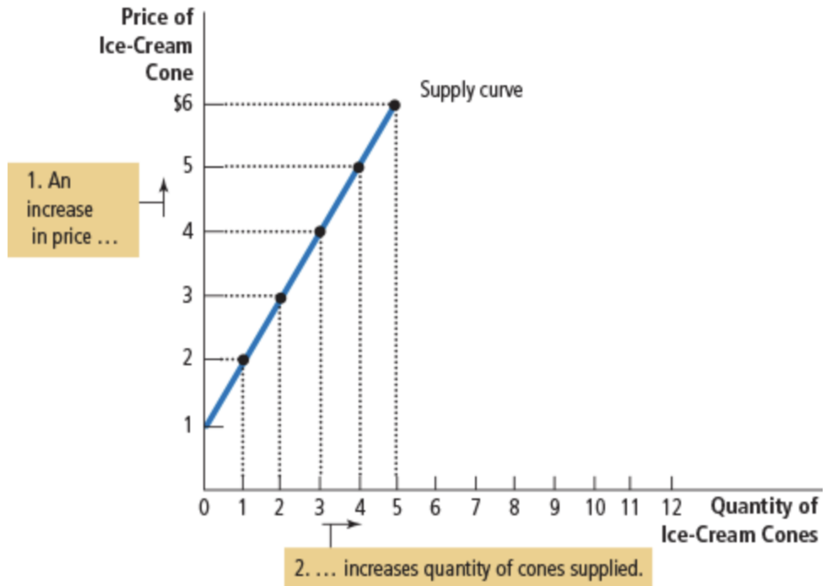
1.4.1 The Supply Curve

- The quantity supplied of a good is the amount that sellers are willing and able to sell.
  - The most important determinant of the quantity supplied of a good is the price of the good.
- Law of Supply: Holding everything else constant, when the price of a good rises, the quantity supplied rises. When the price falls, the quantity supplied falls.
- A supply schedule is a table that shows the relationship between the price of a good and the quantity supplied (holding every other determinant of quantity supplied constant).
- A supply curve is the curve relating price and quantity supplied (holding everything else constant).

1.4.2 Market Supply

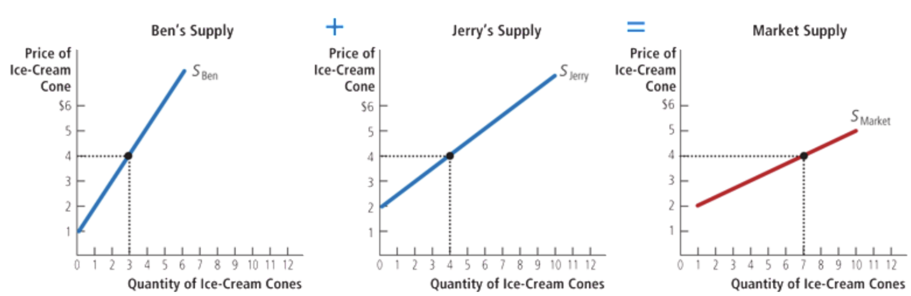
- The quantity supplied in a market is the sum of every individual's quantity supplied at each price.

<u>Ex.</u> Ben's Supply Curve



<u>Ex.</u> Market Supply Schedule and Supply Curve

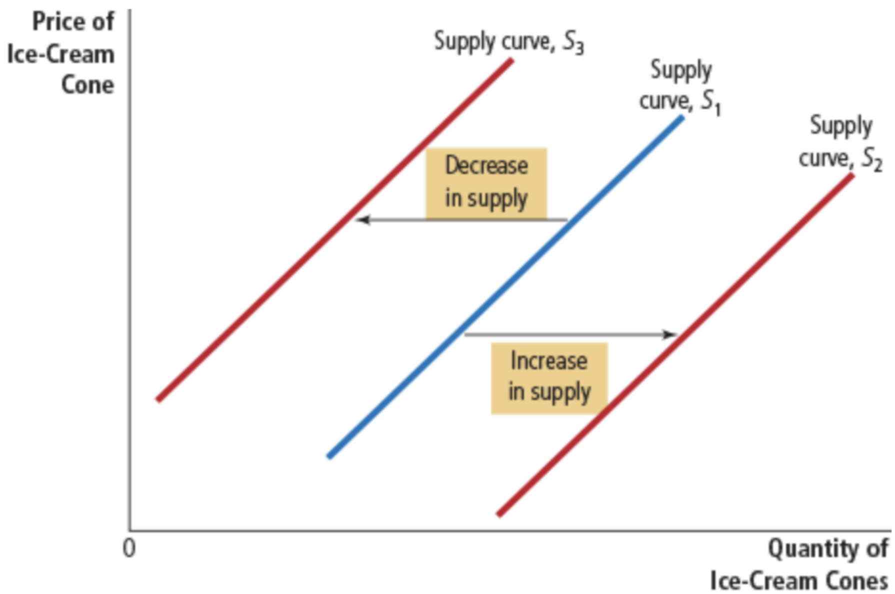
Price of Ice-Cream Cone	Ben		Jerry		Market
$0	0	+	0	=	0 cones
1	0		0		0
2	1		0		1
3	2		2		4
4	3		4		7
5	4		6		10
6	5		8		13



1.4.3 Shifts in the Supply Curve

- If a determinant of quantity supplied other than price changes, the supply curve shifts.

Ex. Shifts in the Supply Curve



Variables That Shift the Supply Curve

1. Input Prices:
   - An input is any good or service that's used to produce another good or service.
   - An increase in input prices makes production less profitable, so fewer producers are willing to supply at a given price and supply decreases.
   - Similarly, a decrease in input prices will increase supply.
2. Technology:
   - Advancement in production technology reduces costs which increases profits, so firms supply more and supply increases.
   - Similarly, a decline in production technology will decrease supply.
3. Expectations:
   - If firms expect higher prices in the future, they will postpone some production, and supply in the present will decrease.

- If firms expect lower prices in the future, they will fast forward its production, so supply in the present will increase.

4. Number of Sellers
5. An increase in the number of sellers increases supply.
6. A decrease in the number of sellers decreases supply.