

Winthrop University
College of Business Administration

Principles of Microeconomics
Econ 215

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General Outline for exam 1

General Definitions

Opportunity cost, economics, microeconomics, macroeconomics, positive economics, normative economics, marginal analysis

History of micro economics.

How was price determined?

(1) Church influence in pricing: In early western history, the church had a significant social influence on the business world. If businesses charged more for a product than what the church thought it should, the church looked down upon them. So, churches kept prices down because of guilt. The church was also very powerful politically. Profit margins were set. Therefore, prices were determined by cost of production plus a small profit margin. Prices should not solely be determined by cost of production.

(2) Mercantile influence in pricing: Price were based on competitor's prices around the world. But this concept causes problems for the countries that made products for lower prices. The only way to keep prices low was to pay workers less. So the country that treated the workers the worst and paid them the lowest amount, charged the lowest prices; But if workers are paid low wages, they cannot buy anything. Economy is hurt overall.

(3) labor theory of value: the cost of production is the greatest determinant of price. Labor costs should be consistent across occupations.

(4) Marshall said the interaction of the suppliers (producers) and demand (consumers) together determine the price.

This natural process of producers and consumers determining prices and quantities results in a free market economy. Free markets are the most efficient economic system, they coincide with capitalism.

Types of economic systems

Command – governments determines prices and quantities produced

Capitalistic - free market interaction between buyers and sells determines prices and quantities produced

Mixed – a mix where in some markets the government is a buyer, regulator, or producer.

Even with a free market capitalist system there are times when the system does not operate in a manner that best suits the overall population. These occurrences are known as free market breakdowns. Some of these free market breakdowns are listed below.

firms with market power –
monopolies
cartels – collusion
monopsonies

externalities
positive – subsidize or encourage
negative – tax, regulate discourage

public goods

distribution of income
know some of the facts

When should the government be involved with setting prices and specifying production?
When should the government not be involved with price setting and product determination?

Trade is another way to advance an economy and move it to a level it otherwise could not reach.
Make sure you know

the pros and cons of trade – handout

What is better for the U.S., to buy a Ford built in Mexico or a Honda built in Ohio?

Theory of Comparative Advantage - handout

Some basic information about the U.S.'s trading partners – page of numbers

Understand trade deficits, trade surpluses, imports, and exports – notes definitions

Consumer Theory - Demand

Why is the demand curve downward sloping

substitution effect

income effect

Shift factors:

Income

Normal goods includes luxuries and necessities

Inferior Goods

taste and preferences,

advertising

fads

new information or reports

price of related goods,

compliments

substitutes

number of buyers

Supply

Reason why the supply curve is upward sloping.

Shift factors

Look on your supply handout

Equilibrium

Static analysis (shifts in the supply and/or demand curve).

Single shifts

Double shifts

Price floors and price ceilings – demand and supply applications

Section 1: Expect about 50 multiple choice questions

Section 2: 1. A supply and demand application question

2. Most likely a question on trade

3. Most likely a question on a free market breakdown