

## McLeod Econ 102 Final Exam Study Guide

*(numbers refer to how many questions on the exam will pertain to that subject)*

### 1) What is economics?

- a. Economics is the study of how people allocate their scarce resources to satisfy their unlimited wants.
- b. Positive vs. normative economics
  - i. Positive: makes statements about what is or what will be. They are **testable** statements.
  - ii. Normative: makes statements about what we **should** or we ought to do.
- c. Microeconomics vs. Macroeconomics
  - i. Micro: the study of decision making by **individual** economic agents (firms, households, government)
    1. 3 main questions
      - a. what to produce
      - b. how to produce
      - c. for whom to produce
  - ii. Macro: the study of the economy as a **whole**
    1. Main topics
      - a. Unemployment
      - b. Output
      - c. Overall prices
      - d. Economic growth

### 2) Production Possibilities Curve: a graph showing all possible combinations of goods and services that can be produced with a given amount of resources and a given technology.

- a. Downward slope (represents Opportunity Costs)
  - i. Law of Increasing Marginal Opportunity Costs:
    1. Resources are not equally well-suited to the production of different goods. As you produce more and more of one type of good, you have to use resources that are less and less well-suited to the production of that type of good. So you have to use more and more resources to produce additional units of that type of good.
    2. PPC is drawn assuming a society is using all of its resources and using the resources efficiently.
  - ii. Shifts of the PPC

1. Increase in our resources and increase in technology cause an outward shift
2. Economic growth
- iii. Points inside the curve
  1. Represent unemployment or inefficiency
  2. Not using all our resources or not using them efficiently
- iv. Points outside the curve
  1. Cannot be produced with the amount of resources given

## 2) Absolute/Comparative Advantage

- b. Absolute advantage:
  - i. one country has an absolute advantage in the production of a good over another country if it can produce a given amount of the good using fewer resources than the other country can.
- c. Comparative advantage:
  - i. one country has a comparative advantage in the production of a good over another country if it can produce a given amount of that good at a lower opportunity cost than the other country.
- d. Opportunity Cost:
  - i. The value of the next best alternative that we give up/forego when we make a choice.

## 5) Supply and Demand

### 1) Demand:

- a. Law of Demand: There is an inverse relationship between price and quantity demanded. When one of those things goes up, the other goes down.
- b. Quantity Demanded: the amount of a good or service that a person would buy during a given period of time at a given price
- c. Change in Qd vs. Change in D:
  - i. A change in Qd is represented by a movement along the demand curve (point A to point B). It occurs because of a change in the price of a good.
  - ii. A change in demand is represented by a shift of the demand curve. It is caused by a change in something other than the price of a good.
    1. Change in preferences
    2. Change in income
      - a. Normal goods: increase in income causes an increase in demand

- b. Inferior goods: increase in income causes a decrease in demand
- 3. Change in price of a related good
  - a. Compliments: increase in price of 1 good causes a decrease in demand for the other
  - b. Substitutes: increase in the price of 1 good causes an increase in demand for the other
- 4. Changes in expectations (future prices & income)
- 5. Change in the number of consumers

## 2) Supply

- a. Law of Supply: there is a positive, or direct, relationship between Price and  $Q_s$ , ceteris paribus.
- b. Quantity Supplied: the amount of a good/service that a firm will produce and offer for sale in a given period of time at a given price.
- c. Change in  $Q_s$  vs. Change in Supply
  - i. A change in  $Q_s$  is represented by a movement along a given supply curve (pt A to pt B). It occurs because of a change in price of a good.
  - ii. Change in Supply is represented by a shift of the entire supply curve. It occurs because of a change in something other than price.
    - 1. a change in the cost of production
    - 2. a change in the price of inputs
    - 3. a change in technology
    - 4. a change in the number of firms in the market
    - 5. Gov't policies (taxes and subsidies)
    - 6. Weather/natural disasters

## 3) Equilibrium

- a. A situation where there is no tendency for change
- b. Equilibrium price= the price @ which  $Q_d=Q_s$ 
  - i. Suppose  $Q_d>Q_s$  = "excess demand" or shortage
    - 1. If  $Q_d>Q_s$ , there is a tendency for price to rise
  - ii. Suppose  $Q_d<Q_s$  = "excess supply" or surplus
    - 1. If  $Q_d<Q_s$ , there is a tendency for price to fall
  - iii. Only if  $Q_d=Q_s$  is there no tendency for price to change

## 4) Price Floor

- a. A minimum price, set by the gov't, that buyers have to pay for a good or service