Midterm – Topics for Review

- Economists interested in marginal changes in status quo
  - Key equation: MC=MB
- Economics – definition
- Unlimited wants vs. scarce resources
- Resources:
  1. Land – includes other natural resources
  2. Capital – definition (NOT MONEY)
  3. Labor
  4. Entrepreneurial ability (what is an entrepreneur)
- Production possibilities and production possibilities curve
  - Assumptions made when drawing curve – point in time; resources and technology fixed.
- Productive vs. allocative efficiency
- Points inside, outside, and on PPC
- Overalllocation and underallocation of resources
- Opportunity cost
- Law of increasing opportunity costs and shape of PPC
- Rationality
- Economic models
- Ceteris paribus
- Positive and normative analysis
- Microeconomics and macroeconomics
- Laissez faire
- “Invisible hand”
- Market mechanism
- Mixed economies
- Market vs. government failure
- Markets
- Demand – definition
- Law of demand
- Individual and market demand relationship
- Demand vs. quantity demanded
- Determinants of demand (factors that change demand):
  1. Tastes
  2. Related goods – substitutes and complements
  3. Income – normal and inferior goods
  4. Expectations
  5. Number of buyers – affects market but not individual demand curves
- Supply – definition
- Law of supply
- Individual and market supply relationship
- Supply vs. quantity supplied
• Determinants of supply (factors that change supply):
  1. Technology
  2. Cost of inputs
  3. Prices of related good – substitutes in production
  4. Expectations
  5. Taxes and subsidies
  6. Number of sellers – affects market but not individual supply curves

• Equilibrium

• Shortages and surpluses

• Shifts of supply and demand – will need to graph for short answer

• Market failure – allocative efficiency
  • Public goods – underproduced
    • Free rider problem
  • Externalities – positive and negative
    • Social demand
    • Negative – overproduced
    • Positive -- underproduced
  • Market power
    • Monopoly
    • Less output/higher price
    • Antitrust law
  • Inequity
    • Transfer payments

• Government failure
  • Waste and productive inefficiency
  • Allocative inefficiency
  • Cost/benefit analysis

• Public choice

• Price elasticity of demand
  • Elastic
  • Inelastic
  • Unit elastic
  • Varies along straight line demand curve
  • Relationship to total revenue
  • Total revenue = Price * quantity
  • Perfectly elastic (∞) and perfectly inelastic (0) demand

• Determinants of price elasticity of demand
  • Number of substitutes
  • Price to income ratio
  • Luxuries vs. necessities
  • Time

• Income elasticity of demand – normal and inferior goods

• Cross-price elasticity of demand – substitutes and complements

• Utility
• Total utility
• Marginal utility
• Law of diminishing marginal utility
• Utility maximization rule – MU_A/P_A = MU_B/P_B …
• Indifference curves – what are they?
  • Slope = MRS (marginal rate of substitution)
  • Higher indifference curves better
• MRS – what it means in general and how it is represented (in general terms, not specifically)
• Budget constraint – What does it represent?
  • Slope (again, generally)
  • Determine income and price from a budget constraint given other pieces of information
  • What happens when income or price changes
• Consumer equilibrium – graphically
  • Slope of budget constraint equal to slope of indifference curve
  • Point on demand curve
• Deriving a demand curve from indifference curve and budget constraints – note this will only be two points on the exam, so focus on other problem areas first