Subject: micro economics

Topic: Midterm paper

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Q1:[a].Explain the low of demand?

Ans: Demand is the relationship between the quantity of a good or service consumers will

purchase and the price charged for that good. The law of demand states that the quantity

demanded for a good rises as the price falls, with all other things staying the same. The 'all

other things staying the same' part is really important.

There are other things that can affect demand besides price. They are prices of related goods

or services, income, tastes or preferences, and expectations. For example, if you really like

Apple products, you might not mind paying a higher price for the new phone that just came

out. If you get a new job and your income goes up, you might not mind paying higher prices

for certain goods because of your newfound wealth.

Downward sloping of demand curve-The demand of a production refers to the desire of

acquiring it by the consumer but backed by his purchasing power and willingness to pay the

price. The law of demand states that there is an inverse proportional relationship between

price and demand of a commodity. When the price of commodity increases, its demand

decreases.

Similarly, when the price of a commodity decreases its demend increases. The law of

demand assumes that the other factors affecting the demand of a commodity remain the same.

Market demand carve derived from individual demand curves To derive a market

demand curve, simply add the quantities that each consumer buys at each price. The prices on

the vertical axis do not change, but the quantities on the horizontal axis are the sums of the

consumers' demand. This group of quantities is called horizontal summation. Continue to

find points on the market demand curves that are the sums of the individual quantities.

Connect the points to get the market demand curve. The market demand curve on the left is

labeled D. Any factor that shifts any of the individual demand curves will shift the market

demand curve. In the example on the left, only Bob's income changed. The change shifts

Bob's individual demand curve and the market demand curve outward because a larger

quantity is demanded at each price.

[b].What are the determinants of demand? What happens to the demand

curve when any of these determinants change? Distinguish between a

change in demand and a change in in the quantity demanded noting the

cause of each.

Ans: Determinants of Demand

When price changes, quantity demanded will change. That is a movement along the same demand

curve. When factors other than price changes, demand curve will shift. These are the determinants

of the demand curve.

1. Income: A rise in a person's income will lead to an increase in demand (shift demand curve to the

right), a fall will lead to a decrease in demand for normal goods. Goods whose demand varies

inversely with income are called inferior goods (e.g. Hamburger Helper).

2. Consumer Preferences: Favourable change leads to an increase in demand, unfavourable change

lead to a decrease.

3. Number of Buyers: the more buyers lead to an increase in demand; fewer buyers lead to

decrease.

4. Price of related goods:

a. Substitute goods (those that can be used to replace each other): price of substitute and demand

for the other good are directly related.

Example: If the price of coffee rises, the demand for tea should increase.

The determinants of demand, as defined in the reading, are: consumers' tastes (preferences),

the number of buyers in the market, consumer incomes, the prices of related goods and

consumer expectations. Additionally, it seems that the actual price of the good itself is a

primary consideration but it affects the curve up and down rather than side to side. As a price

increases the curve leads to movement up the curve and as it decreases it leads to movement

down the curve. When any of the determinants of demand change a change in the demand of

the item will change. An increase in demand can be shown as a shift of the demand curve to

the right and a decrease in demand will be shown as a shift in the curve to the left. If there is

increased demand from an increased market, increased desire for a good, higher competitor

prices or the fear of a price increase the curve will shift to the right. If the reverse is true, the

market is shrinking, the item is out dated, competitor prices are dropping or there is a

predicted price reduction the demand will fall which will move the entire curve to the left.

Q 2: Suppose that when everyone wakes up tomorrow, they discover that the government has given them an additional amount of money equal to the amount they already had. Explain what effect this doubling of the money supply will likely have on the following

Changes in living standard over time are also large in the united state, income have historically growth about 2 percent per year(after adjusting for changes in the cost of living). At this rate, average income double every 35 years. Over the past century average income risen about eightfold, al variation in living standard attributable to difference in countries' productivity is the amount of goods and services where workers can produce a large amount of goods and services per unit of time. key to affect ability of goods and services and the worker should be educated.

Q.2.a: The total amount spent on goods and services?

Ans: Expenditures made by the household sector on final goods and services, or gross

domestic product. Consumption expenditures play a central role in macroeconomic activity

affecting both short-run business cycles and long-run economic growth. The motivation

behind consumption expenditures is the general process of consumption, which is the use of

goods and services to satisfy wants and needs, and are officially measured by personal

consumption expenditures. These are one of four expenditures on gross domestic product.

The other three are investment expenditures, government purchases, and net exports.

b.The quantity of goods and services purchased if prices are sticky?

How does the introduction of sticky prices affect, qualitatively and quantitatively, the

response of unemployment and other variables to aggregate shocks? To address this question

I analyse the response to monetary and technology shocks of two versions of the model

economy developed earlier, with the presence or not of staggered price setting in the final

goods sector as the only different among them. In both cases I maintain the assumption of full

wage flexibility.

c.The price of goods and services prices can adjust?

The law of supply and demand is an economic theory that explains how supply and demand

are related to each other and how that relationship affects the price of goods and services. It's

a fundamental economic principle that when supply exceeds demand for a good or service,

prices fall. When demand exceeds supply, prices tend to rise.

There is an inverse relationship between the supply and prices of goods and services when

demand is unchanged. If there is an increase in supply for goods and services while demand

remains the same, prices tend to fall to a lower equilibrium price and a higher equilibrium

quantity of goods and services. If there is a decrease in supply of goods and services while

demand remains the same, prices tend to rise to a higher equilibrium price and a lower

quantity of goods and services.

Q3.Explain any of the five principals of economics in your own words?

Ans: 1. People make rational choices:

If you drove to work/school today, I bet you would disagree with this one (because of all of

the irrational drivers out there). However, it is an assumption that economists make to let the

models work. Remember that to economists, rationality means that people act in their own

best interest with the information that they have available to them. It doesn't mean they make

the best long term decisions, it just means they make the best decisions according to their

own desire for happiness (with the information that they have).

2. Costs and opportunity costs:

The most common use of the word cost is a monetary cost. Generally we are concerned with

the trade-offs that are associated with decisions we make. We have to pay for food, movies,

or classes. But there are other types of costs; in economics we call these opportunity costs.

For more info on opportunity costs, look here. To summarize, opportunity costs are the value

of the highest foregone activity

3. Benefits:

The reason we incur costs is because we also derive benefits from them. Benefits can take

many forms, but the most common are monetary or happiness related. In economics we try

to measure happiness using the word “utility”, which is basically a numerical measure of how

satisfied someone is consuming or using a good or service. We are interested in benefits

because they are typically the thing that individuals and firms are trying to maximize with

their behavior (utility and profit respectively).

4. Incentives:

Incentives are the rewards and punishments we experience every day. This is sometimes

called the carrot and the stick. The carrot is a benefit trying to make someone do something

(positive reinforcement) while the stick is a cost trying to scare someone into doing

something (negative reinforcement.

We like to get rewards, so we will generally make a decision so that we will get rewarded.

At the same time we don’t like punishment so we will avoid decisions that will result in us

getting punished. Economists are interested in how people respond differently to rewards and

punishments for similar scenarios.

5. Marginal Analysis:

Almost everything analyzed in economics is done so on the margin. This means that

economists are interested in the NEXT decision being made. Focusing on the margin means

only considering the NEXT piece of pizza eaten, or the NEXT video game being made. If

you are familiar with calculus then this concept makes sense. If not, think about drinking

beer with your friends. Whenever you order your NEXT beer you consider how much you

want that NEXT beer, and how much money that NEXT beer will cost you. While decisions

made in the past will affect your happiness from that NEXT beer, and the amount of money

you have, the decision to buy that NEXT beer is made then