

## 

## **Basic Economic Concepts Supply and Demand** Production, Cost, and Perfect Competition Unit 1 ↓ Unit 2 ↓ Unit 3 ↓ • Law of Demand—price up, Qd down (downward sloping) • Total cost for a firm is made up of fixed cost and variable cost • Law of Supply—price up, Qs up (upward sloping) (TC = FC + VC)• Scarcity is created by unlimited wants and limited • When Qd = Qs, the market is in equilibrium • Per-unit costs - average costs: AFC, AVC, ATC (ATC = AFC + AVC) and marginal cost • Consumer surplus—difference between price willing to pay (above • Economics is the study of scarcity and opportunity • Per unit and total costs are represented with **cost curves** eq.) and what you actually pay cost—the price of the next best thing when trade-offs are • **Producer surplus**—difference between price willing to sell for • Shut-down rule—if price falls below AVC, a firm should shut made down in the short run (below eq.) and what they actually sell for • Economic systems such as market economies or command • Long run average total cost (LRATC) can be used to identify • Supply and demand can shift based on market changes, changing economies dictate how scarce resources are allocated economies of scale, constant returns to scale, or diseconomies price and/or quantity • We model opportunity cost and productive efficiency on the production possibilities curve (PPC) • Economic profit takes into account opportunity - $\%\Delta Qd/\%\Delta P$ , same applies to supply • The law of **comparative advantage** tells us how countries cost-maximized where MR = MC • Cross price and income elasticity identify substitutes/complements can increase productivity by specializing and trading • Perfectly competitive firms are price takers that follow the and normal/inferior goods respectively • Marginal analysis is used to calculate optimal consumption market equilibrium price with low barriers to entry • Price controls like floors and ceilings lead to disequilibrium with limited income • Perfect competition is allocatively and productively efficient at (shortage / surplus) and deadweight loss • Choices are driven by the law of diminishing marginal utility long run equilibrium • Tariffs and quotas similarly create deadweight loss • Allocative efficiency: P=MC, productive efficiency: P=minimum • When trade occurs, consumer surplus is greater than producer **Imperfect Competition Factor Markets Tips & Tricks Market Failure and Role of Government** Unit 6 ↓ Unit 4 ↓ Unit 5 ↓ FRQ ↓ Imperfect competition is a type of • Even if a question does not ask you to market structure in which price is Social efficiency point is at MSB (Marginal graph, you can still graph to show your Factors of production—land, labor, not determined strictly by supply Social Benefit) = MSC (Marginal Social Cost) work and solve the problem capital—Unit 5 focuses mostly on labor Over/underproduce ⇒ inefficiency and • Pay attention to action words, like identify. and a little bit capital Monopolies are firms that control

- In a monopoly, MR < D since a monopoly cannot price discriminate
- Monopolies create deadweight loss
- When a monopoly price
- discriminates, CS=0, MR=D, and it is allocatively efficient
- In monopolistic competition, firms enter, leading to a leftward shift in MR and D where D=ATC ⇒ normal
- An **oligopoly** is a market structure with few firms that are interdependent
- Game Theory: A dominant strategy exists when the payoff to a particular action is always higher regardless of the other's choice
- Nash Equilibrium—condition describing the set of actions in which no player can increase his or

- Because there is demand for products, there is a derived demand for factors such as labor
- Similarly to product markets, factor markets are governed by supply and demand finding an equilibrium wage
- In factor markets, businesses are the consumers and workers are sellers
- Perfectly competitive labor markets have a market defined wage
- As more workers are hired, marginal product produced goes down
- Marginal product \* price = marginal revenue product (MRP) and, in perfect competition, wage = marginal resource cost (MRC)
- Profit is maximized where MRP = MRC
- **Monopsonies** exist when a firm is the only buyer of labor in an area - MRC > Supply because a monopsony cannot wage discriminate
- Monopsonies pay a lower wage than MRC

- **Positive externality** (spillover benefits) when MSB > MPB  $\Rightarrow$  Gov. correction: per-unit subsidy shifts MPB right
- Negative externality (spillover costs) when MSC > MPC ⇒ Gov. correction: per-unit tax shifts MPC left
- **Public goods**: type of **market failure** that gov. must provide because free market failed to
- Public goods must have **shared consumption** and (non-rivalry) non-exclusion
- **Free riders** benefit from public goods
- ceiling/floor, per-unit tax/subsidy, lump
- **Income inequality** is graphically represented by Lorenz Curve and numerically represented by Gini coefficient
- Types of taxes: progressive, regressive, proportional

- explain, graph, etc.
- Be sure to practice the more mathy aspects of AP Micro—this includes calculations like comparative advantage. cost curves, game theory, and figuring out how many workers to hire
- Know your area formulas! Particularly, for a triangle, A=1/2bh, since you may have to calculate things like consumer and producer surplus, and percent change, final-initial/initial\*100, for elasticity
- Assume your answers are correct if your answer in part (b) is consistent with your answer in part (a), you'll get the point for (b) regardless of (a), given (b) was correct and consistent.
- Don't go down the cause and effect rabbit hole—don't do something like: Supply decreases, meaning price increases, meaning demand does this, meaning the market does this... etc etc - it will not get vou the correct answers!!!