Chapter 4

What does demand indicate?

**how much of a product consumers are both willing and able to buy at each possible price during a given period.**

What does the law of demand state?

**says that quantity demanded varies inversely with price, other things constant.**

When are consumers more willing to purchase a product?

**when its relative price falls.**

**People tend to substitute one product for other goods.**

**This is called the substitution effect of a price change.**

If you were hunger, and ate one piece of pizza, then a second, what economic principle is this demonstrating?

**The satisfaction you derive from an additional unit of a product is called your marginal utility.**

**Example: The additional satisfaction you get from a second slice of pizza is your marginal utility of that slice.**

What does the law of diminishing marginal utility state?

**– the more of a good a person consumes per period, the smaller the increase in total utility from consuming one more unit, other things constant.**

What does an individual point on the demand curve show?

**the quantity demanded at a particular price.**

What does the demand elasticity measure?

**consumer responsiveness to the price change.**

**Elasticity is another word for responsiveness.**

**Specifically, the elasticity of demand measures the percentage change in quantity demanded divided by the percentage change in price.**

Elasticity of demand =

**Percentage change in quantity demanded**

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**Percentage change in price**

What does elastic, unit elastic, and inelastic equal?

-**1. elastic- a percentage change in price will result in a larger percentage change in the quantity demanded.**

**Thus, quantity demanded is considered relatively responsive to a change in price.**

**2. If the percentage change in quantity demanded just equals the percentage change in price, the resulting elasticity is 1.0, and this demand is called unit-elastic.**

**3. If the percentage change in quantity demanded is less than the percentage change in price, the resulting elasticity lies between 0 and 1.0, and this demand is said to be inelastic.**

What are the determinants of demand?

**Consumer income**

**The prices of related goods**

**The number and composition of consumers**

**Consumer expectations**

**Consumer tastes**

When will the demand for an inferior good decrease?

**The demand for an inferior good actually decreases as money income increases.**

**Examples of inferior goods include bologna sandwiches, used furniture, used clothing, trips to the Laundromat, and bus rides.**

The cost of consumption has two components, which are…

**the money price of the good and the time price of the good.**

**Good are demanded because of the benefits they provide.**

Just inside the gates at Disneyland, Disney World, and Universal Studios, visitors see signs posting the waiting times of each attraction and ride.

The waiting times offer a menu of the marginal time cost of each ride or attraction.

What is the opportunity cost of waiting in line?

**is not enjoying other rides or attractions.**

Chapter 5

What motivates the behavior of suppliers?

**Profit is the goal that motivates the behavior of suppliers.**

Profit =

**Profit = Total revenue – Total cost**

What does supply indicate?

**how much of a good producers are willing and able to offer for sale per period at each possible price, other things constant.**

When do producers offer more for sale?

**when the price rises for two reasons.**

**as the price increases, other things constant, a producer becomes more willing to supply the good.**

**Prices act as signals to existing and potential suppliers about the rewards for producing various goods.**

Explain the difference between supply and quantity supplied.

**Supply is the entire relation between the price and quantity supplied, as reflected by the supply schedule or supply curve.**

**Quantity supplied refers to a particular amount offered for sale at a particular price, as reflected by a point on a given supply curve.**

Elasticity of supply=

**Percentage change in quantity supplied**

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**Percentage change in price**

What are the five determinants of market supply?

**Following are the five determinants of market supply other than the price of the good:**

**The cost of resources used to make the good.**

**The price of other goods these resources could make.**

**The technology used to make the good.**

**Producer expectations.**

**The number of sellers in the market.**

What does the state of technology represent in the economy?

**stock of knowledge about how to combine resources efficiently.**

Explain the difference between fixed and variable resources.

**Resources that cannot be altered easily- the size of the building- are called fixed resources.**

**Resources that can be varied quickly to change output are called variable resources.**

Why would hiring a fourth worker in a small company with little production room be a bad idea?

**Beginning with the fourth worker, the law of diminishing returns takes hold.**

**This law states that as more units of one resource are added to all other resources, marginal product eventually declines.**

Three ranges of marginal product are increasing marginal returns, diminishing but positive marginal returns, and negative marginal returns. Which example do firms normally produce?

**Firms normally produce in the range of diminishing but positive marginal returns.**

Why would a summer resort close down in the winter?

**A firm’s minimum acceptable price is a price high enough to ensure that total revenue at least covers variable cost.**

**If the market price is below that minimum, the firm will shut down.**

**A firm that shuts down keeps it productive capacity intact- paying the rent, fire insurance, and property taxes, keeping water pipes from freezing in the winter, and so on.**

**(Businesses in summer resorts often close for the winter).**

Why should firms focus on the average cost?

**Because all resources can vary in the long run, the focus is on the average cost of production, not the marginal cost.**

**Average cost equals total cost divided by output.**

How does Walmart use economies of scale?

**If the firms long-rung average cost declines as the firm size increases, this reflects economies of scale. Walmart**

If the firm’s long run average cost increases as production increases, this reflects diseconomies of scale. What plan did IBM develop to avoid diseconomies of scale?

**divided into six smaller decision-making groups.**