Notes on Chapter 1

For definition and examples, you should consult the text book. The purpose of these notes is to provide a general guideline as to what has been covered in class and their relative importance. These notes are never intended to be used as a replacement of the text book.

We started our discussion with the distinction between **Renewable and Nonrenewable** natural resources. We pointed out the fact that natural resources, be it renewable or nonrenewable, are finite in supply (scarce) and care should be taken in using these.

Since human wants are **insatiable** and resources are **scarce**, we need to make choices. Even if we had unlimited supply of natural resources, still the problem of scarcity would have existed. The problem of scarcity remains because we need time to convert resources into goods and services and since our wants are unlimited, we will never have enough time to produce all the goods that would be demanded at a given point of time. So even if the resource supply are unlimited, there would be scarcity of goods and services that is available for final consumption and the problem of choice would continue to be a part of every society. It is this problem of choice where the origin of economics lies. Please study the definition of **Economics** carefully and its **four central issues** (who produces what, how it is produced, who consumes and who decides). In relation to who decides, we discussed the issue of **Consumer Sovereignty** (make sure you know what it is).

**Economic Models:**

Things to remember: Definition of Economic model, what is meant by abstraction from reality. The notion of **Ceteris Paribus**. Make sure you know what is meant by the **Circular Flow Model of Goods and Money**. It is important that you know what is the difference between the **product market** and the **resource market** and what is exchanged in these markets and from whom to whom.

**Micro and Macro Economics:**

Once again the definitions are very important and it is also important for you to identify if a particular issue is a Micro or a Macro issue. In other words it is important for you to look at the examples and think of some Micro and Macro issues by yourselves.

**Positive and Normative Economics:**

You have to be able to identify and distinguish between a normative and a positive statement.

Notes on Chapter 2

**Production Possibilities and Opportunity Costs:**

We started our discussion with the analysis of Factors of Productions. We talked about Labor, Capital, Land and Entrepreneurship. These are broad categories, please make sure which productive resource belong to what category. For example, the resources of the sea
are considered under the land category. A little strange, but that is how the resources are broadly classified.

With the example of Robinson Crusoe, we presented the idea of Production Possibility Frontier (PPF). The book is very good in discussing and presenting this concept, please study it carefully, making sure that you completely understand the idea of Opportunity cost and the Law of Increasing Costs.

What causes the PPF to shift? If there is a natural disaster, what would happen to the PPF of a country? What about scientific innovations which make all resources more productive?

If a country operates somewhere within the PPF (not on the line itself), then this means that there exists underutilized capacity and unemployed/unutilized resources in that country. We consider such a situation to be economically inefficient. On the other hand, if a country operates on any point on the PPF, it signifies efficiency and full utilization of its resources.

**Production Possibilities and Economic Specialization:**

We thoroughly discussed the concept of Absolute Advantage and Comparative Advantage with help of examples. Under a two country setting, I showed you how to determine which country has absolute advantage / comparative advantage in the production of which commodity. We did that in two different ways, in the first set of examples the tables we used had information about the quantity of the two products that each country can produce in a given amount of time (e.g., the tables in pages 37 and 38). We used that information to find out the opportunity cost of each product in each country and then decided which country had absolute and comparative advantage in what commodity.

In the second type of setup, the table provided information about the labor it is needed to produce a unit of each commodity in question (e.g., practice problem 3 on page 41). We then used this input information to compute the opportunity cost of the commodities in question. Once the opportunity costs were computed, the method of determining the absolute and comparative advantage was the same. Please make sure that you understand how to find out absolute and comparative advantage under both these two methods.

**Notes on Chapter 3**

**Demand and Supply:**

We discussed the Law of Demand, which works behind the demand curve. With the help of demand schedules we showed how the demand curves can be downward sloping straight lines or curves.

We demonstrated how the Market Demand curve could be obtained by horizontal summation of all individual demand curves.
We talked about the supply curve and with the help of the fishermen example showed the distinction between Market-Day, Short-run and Long-run Supply.

We also introduced the concept of equilibrium price by combining the demand and supply curves.

**Changes in Demand and Changes in Quantity Demanded:**

When the price of a commodity changes, it leads to a movement along the demand curve. The location of the demand curve, however, does not change, we simply move from one point of the demand curve to another one. However, when some other factors which have influence on demand, changes there would be a shift in the demand curve (this change is known as a change in demand). For example, if income increases, more would be demanded at each price, and showing an outward shift in the demand curve could only accommodate that effect. Make sure that you know which factors can cause shifts in the demand curve. Same thing applies to supply. You should make yourself familiar with factors, which causes shifts in the supply curve. In other words, you should know what causes supply to change and what causes quantity supplied to change.

**Combined Effect of Demand and Supply Change:**

By using graphical analysis, we analyzed what would happen when both demand and supply increase, or when one increase and the other decrease, when both decrease, etc. Make sure that you can determine what would be the effect on equilibrium price and quantity when demand and supply changes.