

# Microeconomics

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# Supply and Demand

# Demand Curve I

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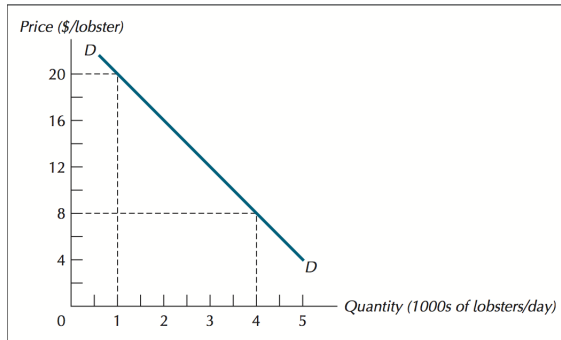
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## Definition: Demand Curve

Description of the relationship between a price of a good or service and a number of units a buyer wants to buy for a given price

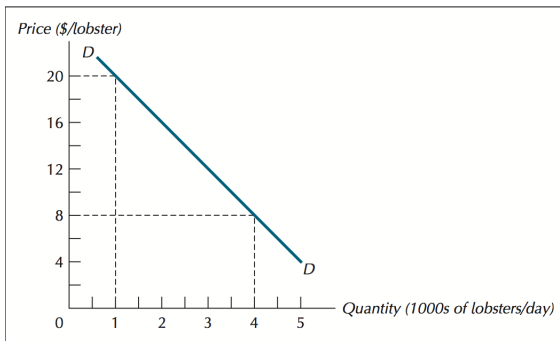
# Demand Curve II

## ■ Demand Curve:



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### ■ Horizontal vs. vertical interpretation of the demand curve



## Demand Curve III

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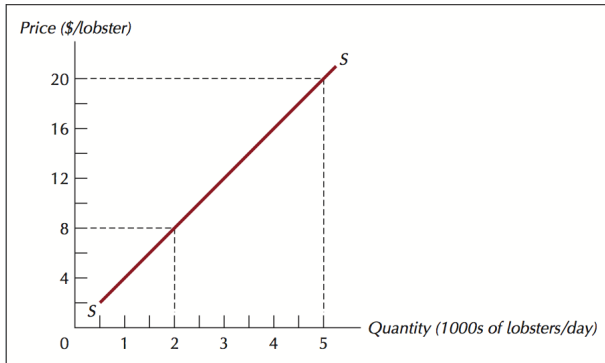
### The Law of Demand

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- When price rises people switch to substitute goods i.e. buy rice instead of pasta. – **substitution effect**
- When price rises people cannot afford to buy as much as before. – **income effect**

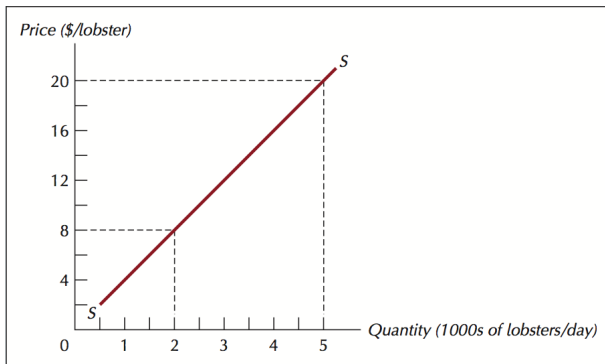
# Supply Curve I

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- Again: Horizontal vs. vertical interpretation of the supply curve

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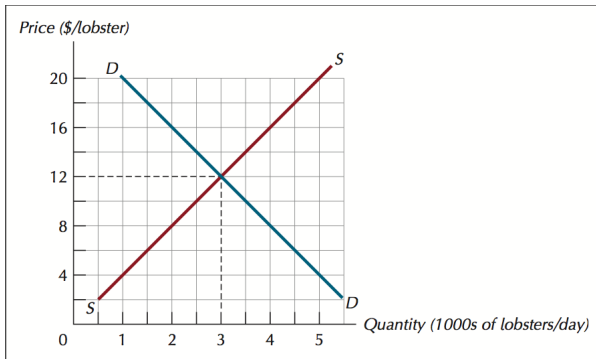
The empirical observation that when the price of a product rises, firms offer more of it for sale.

- Price must cover the marginal cost of producing a good.
- This cost tends to rise with the number of units produced.



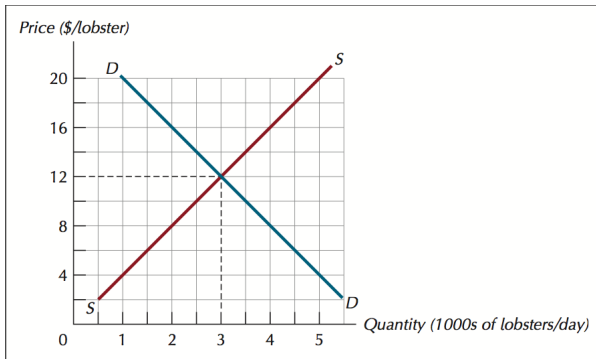
# The Market I

## ■ Market in Equilibrium:



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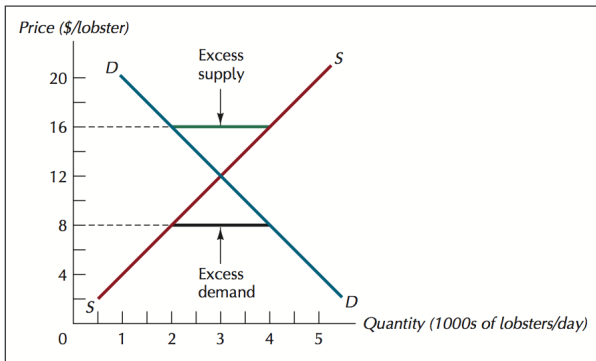
## ■ Market in Equilibrium:



- **Pareto efficiency:** No reallocation can improve some people's position without harming the position of at least some others.

# The Market II

## ■ Market in Disequilibrium:



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- Market in disequilibrium is **NOT** Pareto efficient!
- Possibility of transactions in which at least one party is better off.
- **"The Invisible Hand"** (Adam Smith): Market will adjust to equilibrium on its own!

# Price Regulation

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A **minimum price** for a good, established by law

- Examples: agricultural products in the EU, minimum wages etc.



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- Effect on the market? Pareto efficiency?

# Determinants of Demand I

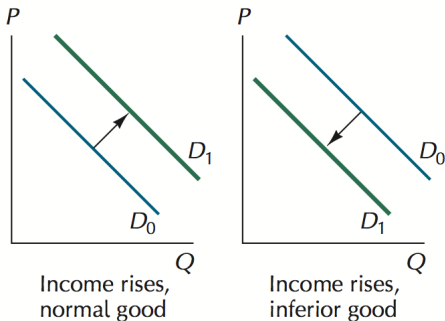
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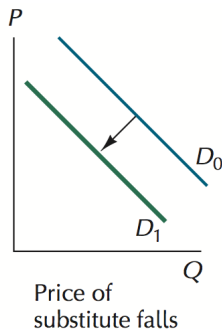
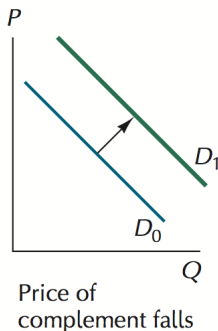
## 2. Prices of Substitutes and Complements

- **Substitutes:** goods that serve a similar purpose.
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## 5. Population

- The number of people who buy a product grows as the number of potential buyers grows.

# Determinants of Supply I

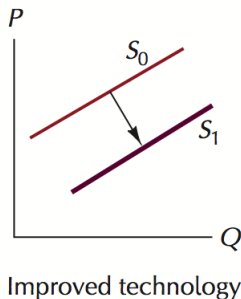
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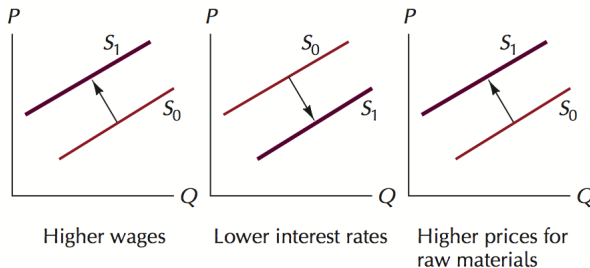
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- Costs depend on the payments to factors of production: labor, capital etc.

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## 5. Random Events

- Example: Weather in agricultural production



# The Effect of Taxes and Subsidies

