Review Session.

Exam: Pauley Ballroom (2nd floor ASUC)  
Friday 5/14/99 5-7pm.  
Please be on time.  
Please bring photo ID.  
Exam lasts 2 hours.  
Required to answer 10/14 questions  
from 2 sections in the paper.  
Micro Section: 6/9 questions  
Macro Section: 4/5 questions

Exam advice: DON’T PANIC  
Read through whole paper-Make notes  
Time your answers: after you have read  
through the paper, 10 questions in X minutes  
= X/10 minutes per questions.  
Remember the marginal returns to starting a  
new question outweigh the returns to trying  
to finish an existing one.

Economics is a ‘doing’ subject!
Microeconomics.

Economics concerned with scarce resources.

Given shape in the *production possibility frontier* and the concept of *opportunity cost*.

Remember to think about: shifts in the curve, its concave shape, efficiency.

Chief tool for analyzing micro markets was *demand and supply curves*.

\[ Q_d = f(p, y, t, p_b, m) \]
\[ Q_s = f(p, c, t, p_{ro}, s) \]

Remember to think about: the movement along a curve and a shift in the curve.

Models of *price ceilings* or *price floors*. 
Price elasticity of demand:
\[% \Delta Q/\% \Delta P \text{ or } (\Delta Q/\Delta P) \times (P/Q)\]

Remember to think about: how to calculate the change in expenditure from price changes.

What lies behind the demand and supply curves: the behavior of economic agents.

Consumers: utility and the diminishing willingness to pay for a good.

Remember to think about: equating marginal utility and price, and consumer surplus.

Producers: diminishing marginal product and marginal cost = marginal revenue.

Remember to think about: marginal physical product, MPP\times P=MRP, fixed and variable costs, marginal cost, average cost,
profit maximizing rules: \( P = MC, \ MC = MR \); economies of scale.

Industry or market structure was bound into ‘Theories of the Firm’:

Perfect competition: many producers and consumers, price takers, homogenous goods, free entry and exit, zero economic profit.

Remember to think about: profit max condition in the short and long run, new firms entering the industry, taxes on the product or the costs, difference between fixed and variable costs.

Monopoly: one producer, price giver, barriers to entry, persistent profits.

Remember to think about: Profit max: \( MC = MR \). Profits = \( Q \times (AR - AC) \).
Differences in price and output between monopoly and perfect competition.

*Oligopoly*: few firms, some barriers, profits to be made.

Remember to think about: kinked demand curves and price stability, game theory and strategy: dominant strategies, maximin strategies, prisoners dilemma and escaping using ‘tit for tat’.

What happens if the market equilibrium price and quantity does not reflect the efficient allocation of goods and services in the economy? *Market Failure*.

*Externalities*: detrimental and beneficial.

Remember to think about: marginal private cost and marginal social cost.
Public Goods: available to all and not provided by the market at the right cost.

Remember to think about: depletability and excludability, free-riding.

Differing prices: bad products driving out good and certain forms of price discrimination.

Remember to think about: how producers gain consumer surplus, the implications of imperfect information.

Labor as a factor of production: demand, supply, and the distribution of factor income.

Remember to think about: how the derived demand curve results from the MRP schedule; labor supply and income and substitution effects; minimum wages; what
factors contribute to observed increase in dispersion of income.

**Macroeconomics**

What determines the income/product flows in the economy.

Chief tool for this: Aggregate demand (AD) and Aggregate supply (AS) curves.

*Determination of the AD curve:*

*Aggregate expenditure model:*

\[ AE = Y = C + I + G + X - M. \]

Remember to think about: consumption function, marginal propensity to consume (MPC) and save (MPS), investment, government expenditure and marginal propensity to import; the multiplier.
Increases in autonomous expenditure and the effects on national income: *Multiplier*.

**Remember to think about:** Government spending multiplier, tax multiplier, and the balanced budget multiplier; how to derive them from the model.

Implications for policy from the shape of the AD and AS curves.

*Money markets and the effects on the aggregate demand curve.*

**Remember to think about:** money supply definitions, creation of money through the banking system, reserve requirements, money balances and the transactions/speculative motives, what shifts the money demand curve and the money supply curve; open market operations.
Links between the real and money sector and aggregate demand.

Remember to think about: Fishers equation of exchange; planned investment and the interest rate; fiscal expansions and money constraints; money expansions and real sector constraints.

Shape of the AS curve: provides the responsiveness of AD policies. Shape determined by excess capacity, expectations and the ability to trade-off unemployment and inflation.

Remember to think about: Phillips curve, expectations, unemployment and inflation, differences over the long and short run.
Why nations trade? Move beyond their own production possibility frontier.

Remember to think about: difference of absolute and comparative advantage, terms of trade.