Econ 101

Economic Theory

- Mercantilism
  - Mercantilists believed that a nation's wealth came primarily from the accumulation of gold and silver
    - Nations without mines could obtain gold and silver only by selling more goods than they bought from abroad
      - *Think of the British and their opium solution to reverse the flow of bullion into China …*
    - leaders of those nations intervened extensively in the market
      - imposing tariffs on foreign goods to restrict import trade
      - granting subsidies to improve export prospects for domestic goods
    - Mercantilism represented the elevation of commercial interests to the level of national policy

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Economic Theory

- Classical School
  - 1776: Adam Smith's, *The Wealth of Nations*.
    - land, labor, and capital
      - three factors of production and the major contributors to a nation's wealth
    - In Smith's view
      - ideal economy a self-regulating market system
      - automatically satisfies the economic needs of the populace
      - laissez-faire economics
        - » belief that markets and the private sector operate well on their own, without state intervention

Econ 101

Economic Theory

- Marxism
  - Karl Marx saw capitalism as an evolutionary phase in economic development
    - believed capitalism would ultimately destroy itself
      - be succeeded by a world without private property
    - believed that all production belongs to labor
      - because workers produce all value within society.
    - believed that market system allows capitalists (*bourgeoisie*), the owners of machinery and factories, to exploit workers *(proletariat)* by denying them a fair share of what they produce.
    - predicted that capitalism would produce growing misery for workers as competition for profit led capitalists to adopt labor-saving machinery
    - creating a "reserve army of the unemployed" who would eventually rise up and seize the means of production
      - **“dictatorship of the proletariat”**

Econ 101

Economic Theory

- Keynesian economics
  - promotes a mixed economy,
    - both the state and the private sector play an important role
    - modern rationale for the use of government spending and taxing to stabilize the economy.

Econ 101

- The law of demand
  - states that, if all other factors remain equal, the higher the price of a good, the less people will demand that good.
  - In other words, the higher the price, the lower the quantity demanded.
- The law of supply
  - demonstrates the quantities that will be sold at a certain price.
- Imagine that a special edition CD of your favorite band is released for $20.
  - Because the record company's previous analysis showed that consumers will not demand CDs at a price higher than $20, only ten CDs were released because the opportunity cost is too high for suppliers to produce more.
  - If, however, the ten CDs are demanded by 20 people, the price will subsequently rise because, according to the demand relationship, as demand increases, so does the price.
  - Consequently, the rise in price should prompt more CDs to be supplied as the supply relationship shows that the higher the price, the higher the quantity supplied.

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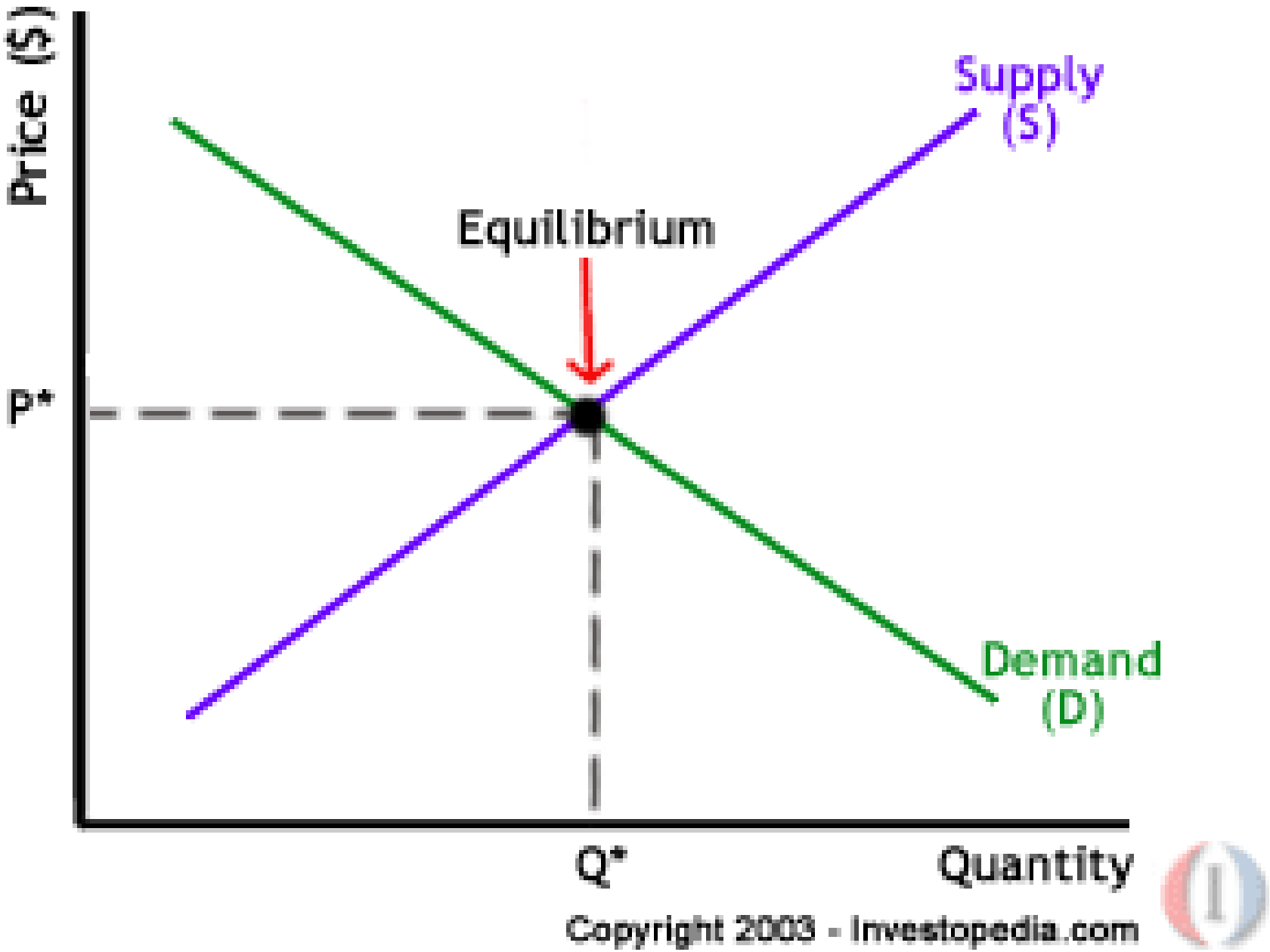
- If, however, there are 30 CDs produced and demand is still at 20, the price will not be pushed up because the supply more than accommodates demand.
- In fact after the 20 consumers have been satisfied with their CD purchases, the price of the leftover CDs may drop as CD producers attempt to sell the remaining ten CDs.
- The lower price will then make the CD more available to people who had previously decided that the opportunity cost of buying the CD at $20 was too high.

- When supply and demand are equal the economy is said to be at equilibrium.
  - At this point, the allocation of goods is at its most efficient
    - the amount of goods being supplied is exactly the same as the amount of goods being demanded.


Price ($)
Supply
(S)
Equilibrium
P*
Demand
(D)
Q*
Quantity
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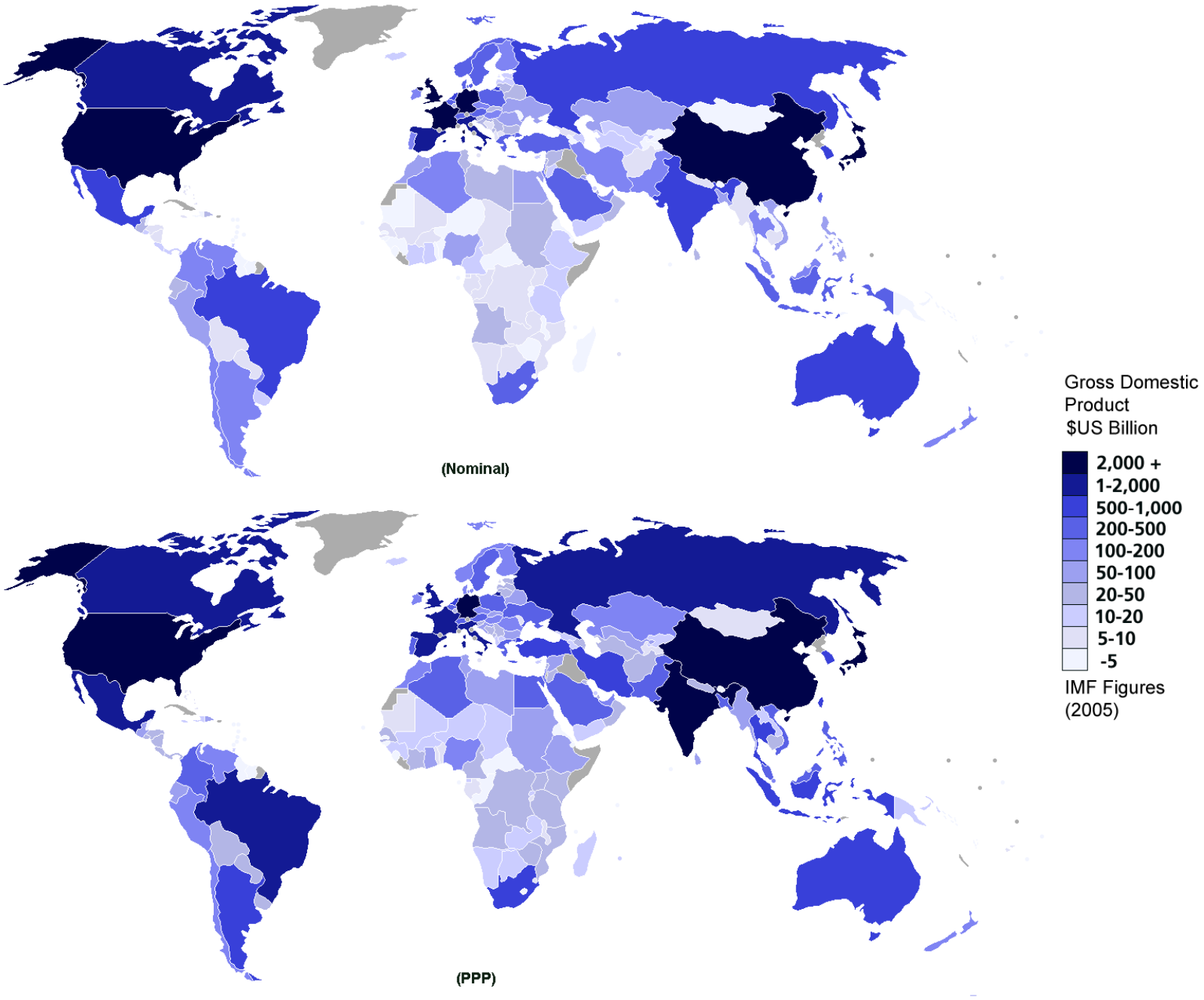
Econ 101

- GLOSSARY OF ECONOMIC TERMS
  - a market in which there are no regulations as to what can be bought, sold, or traded therefore nothing to ensure the well-being of all peoples and the environment
    - FREE TRADE SYSTEM
  - a general increase in prices usually attributed to a situation in which there is too much money chasing too few goods thus driving up the price of all goods by driving down the value of money
    - INFLATION
  - the percentage of a country's labor force (those people who are working or looking for work) that does not have work
    - UNEMPLOYMENT

Econ 101

- GLOSSARY OF ECONOMIC TERMS
  - the total value of the goods and services produced in a country in a given year
    - GROSS DOMESTIC PRODUCT
  - the amount remaining if the amount of money spent is greater than the amount received
    - DEFICIT
  - a condition of limited resources, where society does not have sufficient resources to produce enough to fulfill subjective wants.
    - SCARCITY
  - more than enough resources for everyone (i.e.: an abundance)
    - POST SCARCITY / ABUNDANCE


(Nominal)
(PPP)
Gross Domestic Product
$US Billion
2,000 +
1-2,000
500-1,000
200-500
100-200
50-100
20-50
10-20
5-10
-5
IMF Figures (2005)

World GDP/capita 1-2003 A.D.