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Reading in Economics

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Concept of Economic:

The ancient Greeks knew the word "economy" that good governance organization of house and family, or that's rules and laws which through by head of household to management his affairs of home and family. Greeks uses the word economy not to manage the affairs of house only , but has expanded it to concept of state affairs by establish rules that regulations and management state governing .

Many people hear the word "Economics" and thing it is all about money , Economics it is not about money , it is about weighing different choices or alternatives .Some of those important choices involve money, but most do not , Most of your daily –monthly or life choices have nothing to do with money , yet they are still the subject of Economics .

Definitions of Economic:

1.Adam Smith in his book "The Wealth of Nations" saying ; economy the science that seeks to achieve the wealth for people and state.

2. John Stuart Mill : kind of collective laws, which arises from the work of human beings in order to produce wealth.

3. Marshall : science that looks at how individual getting income and how it is used .

4.Begout : Science that study the economic welfare .

5.Vixl: Science that studies every effort human organized to satisfy his material needs to achieve social and economic welfare.

6.Robi: Science that studies scarcity of goods and services relative to demand it , the reason for scarcity of production back to the scarcity of the factors of production (Labor - capital – land - Management) and choices mean the selection of factors of production that satisfy as much as possible of human needs.

Economics : that branch of social science , looks at how to use limited resources to satisfy multiple and unlimited human needs as possible **.**

<u>Microeconomics and Macroeconomics</u>:

The field of economics is typically divided into two broad realms: microeconomics and macroeconomics. It is important to see the distinctions between these broad areas of study.

Microeconomics is the branch of economics that focuses on the choices made by individual decision-making units in the economy—typically consumers and firms—and the impacts those choices have on individual markets.

Macroeconomics is the branch of economics that focuses on the impact of choices on the total, or aggregate, level of economic activity.

Is the total level of economic activity rising or falling? Is the rate of inflation increasing or decreasing? What is happening to the unemployment rate? These are questions that deal with aggregates, or totals, in the economy; they are problems of macroeconomics. The question about the level of economic activity, for example, refers to the total value of all goods and services produced in the economy. Inflation is a measure of the rate of change in the average price level for the entire economy; it is a macroeconomic problem. The total levels of employment and unemployment in the economy represent the aggregate of all labor markets; unemployment is also a topic of macroeconomics.

Both microeconomics and macroeconomics give attention to individual markets. But in microeconomics that attention is an end in itself; in macroeconomics it is aimed at explaining the movement of major economic aggregates—the level of total output, the level of employment, and the price level.

We have now examined the characteristics that define the economic way of thinking and the two branches of this way of thinking: microeconomics and macroeconomics. In the next section, we will have a look at what one can do with training in economics.

Microeconomics :

Deals with individual units in the economy as a individual or family and Firm , where Focusing on consumer behaviour and how family income expenditure is distributed in to various goods and services . microeconomic interested about determine level production and making pricing decisions that enable firm to Maximize the profits .

Macroeconomics :

its dealing with the total national economy ignoring Individual units. Focusing on the national economy as a whole , like :

1.Study and analysis of macroeconomic variables , such as Gross Domestic Product (GDP) , national income, employment , General level of wages.

2. Total expenditure , economic growth and balance of payments .

3. Analysis and study problems of inflation , unemployment .

4. Study monetary and fiscal policies .

Economic theory :

Economic theory Explain the behaviour of various economic phenomena , and known as set of rules and principles that serve as a guide to decision-making under Set of circumstances . theory is composed of :

1. collection of Definitions that clarify the meaning of economic concepts .

2.aset of Assumptions .

3. one or more of Hypotheses .

Positive economics :

We are used forms for the purpose of deriving theory and laws that depict the relationship between Economic factors , Often these relationships using mathematical and graphical methods . the relationship between economic factors positive if events change in the same . it is not included in the analysis any personal values which explain the phenomenon , Describes theories and laws for interpretation Remarkable economic phenomenon .

Economic laws :

Economic laws came to reflect the economic phenomena , its processes taking place in the circle of production relations . The function of economic researcher is discover laws that lead to Increasing wealth creation in the community. Economic laws are aimed to achieving a set of goals , like classification and organization of economic phenomena , they have Granting researchers ability of predictability .

Applied economics :

Its application of economic theory on real economic , we cannot considered it a separate science , nor a branch of economics we can looking for it as a linked between economic facts and various problems . as economic growth , economics of labor and economic development ... Etc. and study analysis practical solutions , like econometric and input-output analysis .

Introduction To
Economizing Problem

Economic problem appears in any society when trying to use the available resources to satisfy multiple needs. then the economic problem existence of limited resources with unlimited and growing needs .

The Economic Way of Thinking:

Economists study choices that scarcity requires us to make. This fact is not what distinguishes economics from other social sciences; all social scientists are interested in choices. An anthropologist might study the choices of ancient peoples; a political scientist might study the choices of legislatures; a psychologist might study how people choose a mate; a sociologist might study the factors that have led to a rise in single-parent households. Economists study such questions as well. What is it about the study of choices by economists that makes economics different from these other social sciences?

Three features distinguish the economic approach to choice from the approaches taken in other social sciences:

- Economists give special emphasis to the role of opportunity costs in their analysis of choices.

1. Economists assume that individuals make choices that seek to maximize the value of some objective, and that they define their objectives in terms of their own self-interest.
2. Individuals maximize by deciding whether to do a little more or a little less of something. Economists argue that individuals pay attention to the consequences of small changes in the levels of the activities they pursue.

The emphasis economists place on opportunity cost, the idea that people make choices that maximize the value of objectives that serve their self-interest, and a focus on the effects of small changes are ideas of great power. They constitute the core of economic thinking. The next three sections examine these ideas in greater detail.

Opportunity Costs Are Important :

If doing one thing requires giving up another, then the expected benefits of the alternatives we face will affect the ones we choose. Economists argue that an understanding of opportunity cost is crucial to the examination of choices.

As the set of available alternatives changes, we expect that the choices individuals make will change. A rainy day could change the opportunity cost of reading a good book; we might expect more reading to get done in bad than in good weather. A high income can make it very costly to take a day off; we might expect highly paid individuals to work more hours than those who are not paid as well. If individuals are maximizing their level of satisfaction and firms

are maximizing profits, then a change in the set of alternatives they face may affect their choices in a predictable way.

The emphasis on opportunity costs is an emphasis on the examination of alternatives. One benefit of the economic way of thinking is that it pushes us to think about the value of alternatives in each problem involving choice.

Scarcity:

Our resources are limited. At any one time, we have only so much land, so many factories, so much oil, so many people. But our wants, our desires for the things that we can produce with those resources, are unlimited. We would always like more and better housing, more and better education—more and better of practically everything.

If our resources were also unlimited, we could say yes to each of our wants—and there would be no economics. Because our resources are limited, we cannot say yes to everything. To say yes to one thing requires that we say no to another. Whether we like it or not, we must make choices.

Our unlimited wants are continually colliding with the limits of our resources, forcing us to pick some activities and to reject others. Scarcity is the

condition of having to choose among alternatives. A scarce good is one for which the choice of one alternative requires that another be given up.

Consider a parcel of land. The parcel presents us with several alternative uses. We could build a house on it. We could put a gas station on it. We could create a small park on it. We could leave the land undeveloped in order to be able to make a decision later as to how it should be used.

Suppose we have decided the land should be used for housing. Should it be a large and expensive house or several modest ones? Suppose it is to be a large and expensive house. Who should live in the house?. There are alternative uses of the land both in the sense of the type of use and also in the sense of who gets to use it. The fact that land is scarce means that society must make choices concerning its use.

Virtually everything is scarce. Consider the air we breathe, which is available in huge quantity at no charge to us. Could it possibly be scarce?

The test of whether air is scarce is whether it has alternative uses. What uses can we make of the air? We breathe it. We pollute it when we drive our cars, heat our houses, or operate our factories. In effect, one use of the air is as a garbage dump. We certainly need the air to breathe. But just as certainly, we choose to dump garbage in it. Those two uses are clearly alternatives to each other. The more garbage we dump in the air, the less desirable—and healthy—it

will be to breathe. If we decide we want to breathe cleaner air, we must limit the activities that generate pollution. Air is a scarce good because it has alternative uses.

Not all goods, however, confront us with such choices. A free good is one for which the choice of one use does not require that we give up another. One example of a free good is gravity. The fact that gravity is holding you to the earth does not mean that your neighbor is forced to drift up into space! One person's use of gravity is not an alternative to another person's use.

There are not many free goods. Outer space, for example, was a free good when the only use we made of it was to gaze at it. But now, our use of space has reached the point where one use can be an alternative to another. Conflicts have already arisen over the allocation of orbital slots for communications satellites. Thus, even parts of outer space are scarce. Space will surely become more scarce as we find new ways to use it. Scarcity characterizes virtually everything. Consequently, the scope of economics is wide indeed.

Scarcity and the Fundamental Economic Questions :

The choices we confront as a result of scarcity raise three sets of issues. Every economy must answer the following questions:

1. **What should be produced?** Using the economy's scarce resources to produce one thing requires giving up another. Producing better education,

for example, may require cutting back on other services, such as health care. A decision to preserve a wilderness area requires giving up other uses of the land. Every society must decide what it will produce with its scarce resources.

2. **How should goods and services be produced?** There are all sorts of choices to be made in determining how goods and services should be produced. Should a firm employ a few skilled or a lot of unskilled workers? Should it produce in its own country or should it use foreign plants? Should manufacturing firms use new or recycled raw materials to make their products?
3. **For whom should goods and services be produced?** If a good or service is produced, a decision must be made about who will get it. A decision to have one person or group receive a good or service usually means it will not be available to someone else. For example, representatives of the poorest nations on earth often complain that energy consumption per person in the United States is 17 *times* greater than energy consumption per person in the world's 62 poorest countries. Critics argue that the world's energy should be more evenly allocated. Should it? That is a "for whom" question.

Every economy must determine what should be produced, how it should be produced, and for whom it should be produced. We shall return to these questions again and again.

Opportunity Cost :

It is within the context of scarcity that economists define what is perhaps the most important concept in all of economics, the concept of opportunity cost. Opportunity cost is the value of the best alternative forgone in making any choice.

The opportunity cost to you of reading the remainder of this chapter will be the value of the best other use to which you could have put your time. If you choose to spend $20 on a potted plant, you have simultaneously chosen to give up the benefits of spending the $20 on pizzas or a paperback book or a night at the movies. If the book is the most valuable of those alternatives, then the opportunity cost of the plant is the value of the enjoyment you otherwise expected to receive from the book.

The concept of opportunity cost must not be confused with the purchase price of an item. Consider the cost of a college or university education. That includes the value of the best alternative use of money spent for tuition, fees, and books. But the most important cost of a college education is the value of the forgone alternative uses of time spent studying and attending class instead of using the time in some other endeavor. Students sacrifice that time in hopes of even

greater earnings in the future or because they place a value on the opportunity to learn. Or consider the cost of going to the doctor. Part of that cost is the value of the best alternative use of the money required to see the doctor. But, the cost also includes the value of the best alternative use of the time required to see the doctor. The essential thing to see in the concept of opportunity cost is found in the name of the concept. Opportunity cost is the value of the best opportunity forgone in a particular choice. It is not simply the amount spent on that choice.

The concepts of scarcity, choice, and opportunity cost are at the heart of economics. A good is scarce if the choice of one alternative requires that another be given up. The existence of alternative uses forces us to make choices. The opportunity cost of any choice is the value of the best alternative forgone in making it.

First fundamental fact : Unlimited Wants

1.Economic wants are desires of people to use goods and services that provide utility, which means satisfaction.

2.Products are sometimes classified as luxuries or necessities.

3.Businesses and Government also have wants.

4.Over time wants change and multiply.

Second fundamental fact: Scarce Resources

1.Economic resources are limited relative to wants.

2. Economic resources are sometimes called factors of production and include four categories :

- Land or natural resources.

- Capital or investment goods which are all manufactured aids to production like tools, equipment, transportation ….etc., .

- Labour or human resources, which include physical and mental abilities used in production.

- Entrepreneurial ability , a special kind of human resources that provides important functions :

1.Employment and Efficiency: Efficiency requires full employment of available resources and full production.

- Full Employment: means all available resources should be employed.

- Full Production: means that employed resources are providing maximum satisfaction of our economic wants .and full production implies two kinds of efficiency:

1.Allocative efficiency: means that resources are used for producing the combination of goods and services most wanted by society , for example producing compact discs instead of long –playing records with productive resources or computers with word processors rather than manual typewriters.

2.Productive efficiency: means that least costly production techniques are used to produce wants goods and services.

2.Unemployment and Growth: Unemployment and productive efficiency occur when the economy is producing less than full production , in a growing economy the production possibilities was increasing .

Types of Unemployment :

1.Frictional Unemployment : The easiest type of unemployment to explain is known as frictional unemployment .its unemployment that occurs because it takes workers some time to move from one job to another .While it may be the

case that some workers find new jobs before they leave their old ones , a lot of workers leave or lose their jobs before they have other work lined up.in these cases a worker must look around for a job that it a good fit for them and this process takes some time.

2.Cyclical Unemployment: it's probably not surprising that unemployment is higher during recessions and depressions and lower during periods of high economic growth .because of this economists have coined the term cyclical unemployment to describe the unemployment associated with business cycles occurring in the economy. cyclical unemployment occurs during recessions because when demand and services for goods and services in an economy falls , some companies respond by cutting production and laying off workers rather than by reducing wages and prices.

3.Structural unemployment: There are two ways to think about Structural unemployment , one is that Structural unemployment occurs because some labour markets have more workers than their jobs available , and for some reasons wages don't decrease to bring the markets equilibrium. Another way to think about structural unemployment is that a results when workers possess

skills that aren't in high demand in the marketplace and lack skills that are in high demand . in other words Structural unemployment results when there is a mismatch with workers skills and employer's needs.

4. Technological Unemployment : this is term used to describe the loss of jobs due technological changes or innovation. This type of unemployment typically comes from workers either being replaced by machines or having their jobs made easier and require fewer workers to accomplish the same task .though Technological Unemployment has been a general concern since the industrial revolution , it has become an increasingly prominent concern with real consequences in the western world .

5.Seasonal Unemployment: its type of working arrangement in which a person is employed routinely for part of year , but spend the remaining months or weeks without a job.

Factors of Production :

Choices concerning what goods and services to produce are choices about an economy's use of its factors of production, the resources available to it for the production of goods and services. The value, or satisfaction, that people derive

from the goods and services they consume and the activities they pursue is called utility. Ultimately, then, an economy's factors of production create utility; they serve the interests of people.

The factors of production in an economy are its labor, capital, and natural resources. Labor is the human effort that can be applied to the production of goods and services. People who are employed or would like to be are considered part of the labor available to the economy. Capital is a factor of production that has been produced for use in the production of other goods and services. Office buildings, machinery, and tools are examples of capital. Natural resources are the resources of nature that can be used for the production of goods and services.

In the next three sections, we will take a closer look at the factors of production we use to produce the goods and services we consume. The three basic building blocks of labor, capital, and natural resources may be used in different ways to produce different goods and services, but they still lie at the core of production. We will then look at the roles played by technology and entrepreneurs in putting these factors of production to work. As economists began to grapple with the problems of scarcity, choice, and opportunity cost two centuries ago, they focused on these concepts, just as they are likely to do two centuries hence.

1.Labour: Labour is human effort that can be applied to production. People who work to repair tires, pilot airplanes, teach children, or enforce laws are all part of the economy's labour. People who would like to work but have not found employment—who are unemployed—are also considered part of the labour available to the economy.

In some contexts, it is useful to distinguish two forms of labor. The first is the human equivalent of a natural resource. It is the natural ability an untrained, uneducated person brings to a particular production process. But most workers bring far more. The skills a worker has as a result of education, training, or experience that can be used in production are called human capital. Students who are attending a college or university are acquiring human capital. Workers who are gaining skills through experience or through training are acquiring human capital. Children who are learning to read are acquiring human capital.

The amount of labor available to an economy can be increased in two ways. One is to increase the total quantity of labor, either by increasing the number of people available to work or by increasing the average number of hours of work per week. The other is to increase the amount of human capital possessed by workers.

2.Capital: Long ago, when the first human beings walked the earth, they produced food by picking leaves or fruit off a plant or by catching an animal and eating it. We know that very early on, however, they began shaping stones

into tools, apparently for use in butchering animals. Those tools were the first capital because they were produced for use in producing other goods—food and clothing.

Modern versions of the first stone tools include saws, meat cleavers, hooks, and grinders; all are used in butchering animals. Tools such as hammers, screwdrivers, and wrenches are also capital. Transportation equipment, such as cars and trucks, is capital. Facilities such as roads, bridges, ports, and airports are capital. Buildings, too, are capital; they help us to produce goods and services.

Capital does not consist solely of physical objects. The score for a new symphony is capital because it will be used to produce concerts. Computer software used by business firms or government agencies to produce goods and services is capital. Capital may thus include physical goods and intellectual discoveries. Any resource is capital if it satisfies two criteria:

4. The resource must have been produced.
5. The resource can be used to produce other goods and services.

One thing that is not considered capital is money. A firm cannot use money directly to produce other goods, so money does not satisfy the second criterion for capital. Firms can, however, use money to acquire capital. Money is a form of financial capital. Financial capital includes money and other “paper” assets (such as stocks and bonds) that represent claims on future payments. These

financial assets are not capital, but they can be used directly or indirectly to purchase factors of production or goods and services.

3.Natural Resources : There are two essential characteristics of natural resources. The first is that they are found in nature—that no human effort has been used to make or alter them. The second is that they can be used for the production of goods and services. That requires knowledge; we must know how to use the things we find in nature before they become resources.

Consider oil. Oil in the ground is a natural resource because it is found (not manufactured) and can be used to produce goods and services. However, 250 years ago oil was a nuisance, not a natural resource. Pennsylvania farmers in the eighteenth century who found oil oozing up through their soil were dismayed, not delighted. No one knew what could be done with the oil. It was not until the mid-nineteenth century that a method was found for refining oil into kerosene that could be used to generate energy, transforming oil into a natural resource. Oil is now used to make all sorts of things, including clothing, drugs, gasoline, and plastic. It became a natural resource because people discovered and implemented a way to use it.

Defining something as a natural resource only if it can be used to produce goods and services does not mean that a tree has value only for its wood or that a mountain has value only for its minerals. If people gain utility from the

existence of a beautiful wilderness area, then that wilderness provides a service. The wilderness is thus a natural resource.

The natural resources available to us can be expanded in three ways. One is the discovery of new natural resources, such as the discovery of a deposit of ore containing titanium. The second is the discovery of new uses for resources, as happened when new techniques allowed oil to be put to productive use or sand to be used in manufacturing computer chips. The third is the discovery of new ways to extract natural resources in order to use them. New methods of discovering and mapping oil deposits have increased the world's supply of this important natural resource.

4.**Technology and the Entrepreneur:** Goods and services are produced using the factors of production available to the economy. Two things play a crucial role in putting these factors of production to work. The first is technology, the knowledge that can be applied to the production of goods and services. The second is an individual who plays a key role in a market economy: the entrepreneur. An entrepreneur is a person who, operating within the context of a market economy, seeks to earn profits by finding new ways to organize factors of production. In non-market economies the role of the entrepreneur is played by bureaucrats and other decision makers who respond to incentives other than profit to guide their choices about resource allocation decisions.

The interplay of entrepreneurs and technology affects all our lives. Entrepreneurs put new technologies to work every day, changing the way factors of production are used. Farmers and factory workers, engineers and electricians, technicians and teachers all work differently than they did just a few years ago, using new technologies introduced by entrepreneurs. The music you enjoy, the books you read, the athletic equipment with which you play are produced differently than they were five years ago. The book you are reading was written and manufactured using technologies that did not exist ten years ago. We can dispute whether all the changes have made our lives better. What we cannot dispute is that they have made our lives different.

The Sources of Economic Growth:

Economic growth implies an outward shift in an economy's production possibilities curve. Recall that when we draw such a curve, we assume that the quantity and quality of the economy's factors of production and its technology are unchanged. Changing these will shift the curve. Anything that increases the quantity or quality of the factors of production available to the economy or that improves the technology available to the economy contributes to economic growth.

Consider, for example, the dramatic gains in human capital that have occurred in the United States since the beginning of the past century. In 1900, about 3.5% of U.S. workers had completed a high school education. By 2006,

that percentage rose almost to 92. Fewer than 1% of the workers in 1900 had graduated from college; as late as 1940 only 3.5% had graduated from college. By 2006, nearly 32% had graduated from college. In addition to being better educated, today's workers have received more and better training on the job. They bring far more economically useful knowledge and skills to their work than did workers a century ago.

Moreover, the technological changes that have occurred within the past 100 years have greatly reduced the time and effort required to produce most goods and services. Automated production has become commonplace. Innovations in transportation (automobiles, trucks, and airplanes) have made the movement of goods and people cheaper and faster. A dizzying array of new materials is available for manufacturing. And the development of modern information technology—including computers, software, and communications equipment—that seemed to proceed at breathtaking pace especially during the final years of the last century and continuing to the present has transformed the way we live and work.

Look again at the technological changes of the last few years described in the Case in Point on advances in technology. Those examples of technological progress through applications of computer technology—from new ways of mapping oil deposits to new methods of milking cows—helped propel the United States and other economies to dramatic gains in the ability to produce

goods and services. They have helped shift the countries' production possibilities curve outward. They have helped fuel economic growth.

Table 2.1 "Sources of U.S. Economic Growth, 1948–2002" summarizes the factors that have contributed to U.S. economic growth in the past half century. When looking at the period of 1948–2002 as a whole we see that about 60% of economic growth stems from increases in the quantities of capital and labor and 40% from increases in the qualities of the factors of production and improvements in technology. In the most recent period, 1995–2002, however, these percentages are essentially reversed, with a little less than 30% explained by increases in quantities of the factors of production and a whopping 70% explained by improvements in factor quality and technology.

Classifying Economic Systems:

Each of the world's economies can be viewed as operating somewhere on a spectrum between market capitalism and command socialism. In a market capitalist economy, resources are generally owned by private individuals who have the power to make decisions about their use. A market capitalist system is often referred to as a free enterprise economic system. In a command socialist economy, the government is the primary owner of capital and natural resources and has broad power to allocate the use of factors of production. Between these two categories lie mixed economies that combine elements of market capitalist and of command socialist economic systems.

No economy represents a pure case of either market capitalism or command socialism. To determine where an economy lies between these two types of systems, we evaluate the extent of government ownership of capital and natural resources and the degree to which government is involved in decisions about the use of factors of production.

"Economic Systems" suggests the spectrum of economic systems. Market capitalist economies lie toward the left end of this spectrum; command socialist economies appear toward the right. Mixed economies lie in between. The market capitalist end of the spectrum includes countries such as the United States, the United Kingdom, and Chile. Hong Kong, though now part of China, has a long history as a market capitalist economy and is generally regarded as operating at the market capitalist end of the spectrum. Countries at the command socialist end of the spectrum include North Korea and Cuba.

Economic Freedom and Income

The horizontal axis shows the degree of economic freedom —"free," "mostly free," "mostly unfree," and "repressed"—according to the measures used by the Heritage Foundation and *The Wall Street Journal*. The graph shows the relationship between economic freedom and per capita income. Countries with higher degrees of economic freedom tended to have higher per capita incomes.

Market capitalist economies rely on economic freedom. Indeed, one way we can assess the degree to which a country can be considered market capitalist is by the degree of economic freedom it permits. Several organizations have attempted to compare economic freedom in various countries. One of the most extensive comparisons is a joint annual effort by the Heritage Foundation and *The Wall Street Journal*. The 2008 rating was based on policies in effect in 162 nations early that year. The report ranks these nations on the basis of such things as the degree of regulation of firms, tax levels, and restrictions on international trade. Hong Kong ranked as the freest economy in the world. North Korea received the dubious distinction of being the least free.

It seems reasonable to expect that the greater the degree of economic freedom a country permits, the greater the amount of income per person it will generate. This proposition is illustrated in Figure 2.15 “Economic Freedom and Income”. The group of countries categorized as “free” generated the highest incomes in the Heritage Foundation/*Wall Street Journal* study; those rated as “repressed” had the lowest. The study also found that countries that over the last decade have done the most to improve their positions in the economic freedom rankings have also had the highest rates of growth. We must be wary of slipping into the fallacy of false cause by concluding from this evidence that economic freedom

generates higher incomes. It could be that higher incomes lead nations to opt for greater economic freedom. But in this case, it seems reasonable to conclude that, in general, economic freedom does lead to higher incomes.

Government in a Market Economy

The production possibilities model provides a menu of choices among alternative combinations of goods and services. Given those choices, which combinations will be produced?

In a market economy, this question is answered in large part through the interaction of individual buyers and sellers. As we have already seen, government plays a role as well. It may seek to encourage greater consumption of some goods and discourage consumption of others. In the United States, for example, taxes imposed on cigarettes discourage smoking, while special treatment of property taxes and mortgage interest in the federal income tax encourages home ownership. Government may try to stop the production and consumption of some goods altogether, as many governments do with drugs such as heroin and cocaine. Government may supplement the private consumption of some goods by producing more of them itself, as many U.S. cities do with golf courses and tennis courts. In other cases, there may be no private market for a good or service at all. In the choice between security and defense versus all other goods and services outlined at the beginning of this chapter,

government agencies are virtually the sole providers of security and national defense.

All nations also rely on government to provide defense, enforce laws, and redistribute income. Even market economies rely on government to regulate the activities of private firms, to protect the environment, to provide education, and to produce a wide range of other goods and services. Government's role may be limited in a market economy, but it remains fundamentally important.

Key Takeaways

The ideas of comparative advantage and specialization suggest that restrictions on international trade are likely to reduce production of goods and services. Economic growth is the result of increasing the quantity or quality of an economy's factors of production and of advances in technology. Policies to encourage growth generally involve postponing consumption to increase capital and human capital. Market capitalist economies have generally proved more productive than mixed or command socialist economies. Government plays a crucial role in any market economy.

Some European economies, such as France, Germany, and Sweden, have a sufficiently high degree of regulation that we consider them as operating more toward the center of the spectrum. Russia and China,

which long operated at the command socialist end of the spectrum, can now be considered mixed economies. Most economies in Latin America once operated toward the right end of the spectrum. While their governments did not exercise the extensive ownership of capital and natural resources that are one characteristic of command socialist systems, their governments did impose extensive regulations. Many of these nations are in the process of carrying out economic reforms that will move them further in the direction of market capitalism.

The global shift toward market capitalist economic systems that occurred in the 1980s and 1990s was in large part the result of three important features of such economies. First, the emphasis on individual ownership and decision-making power has generally yielded greater individual freedom than has been available under command socialist or some more heavily regulated mixed economic systems that lie toward the command socialist end of the spectrum. People seeking political, religious, and economic freedom have thus gravitated toward market capitalism. Second, market economies are more likely than other systems to allocate resources on the basis of comparative advantage. They thus tend to generate higher levels of production and income than do other economic systems. Third, market capitalist-type systems appear to be the most conducive to entrepreneurial activity.

Suppose Christie Ryder had the same three plants we considered earlier in this chapter but was operating in a mixed economic system with extensive government regulation. In such a system, she might be prohibited from transferring resources from one use to another to achieve the gains possible from comparative advantage. If she were operating under a command socialist system, she would not be the owner of the plants and thus would be unlikely to profit from their efficient use. If that were the case, there is no reason to believe she would make any effort to assure the efficient use of the three plants. Generally speaking, it is economies toward the market capitalist end of the spectrum that offer the greatest inducement to allocate resources on the basis of comparative advantage. They tend to be more productive and to deliver higher material standards of living than do economies that operate at or near the command socialist end of the spectrum.

National Income Accounting

A term used in economics refer to the bookkeeping system that national government uses to measures' the level of the country economic activity in a given time period. National Income Accounting records of activity in accounts such as total revenue earned by domestic corporations , wages paid to foreign and domestic workers . and amount spent on sales and income taxes by corporations and individuals residing in the country .

National Income accounting provides economists and statisticians with detailed information that can be used to track the health of an economy and to forecast future growth and development . Although National Income accounting is not an exact science , its provides useful insight into how well an economy is function , and where monies are being generated and spent .

The most common measures of the aggregate production in an economy is Gross domestic Product (GDP) . It is the market value of all final goods and services produced in an economy within a given period of time (Typically Year) , whether or not those goods are sold to the final consumer . It does not matter who owns the resources as long as it is contained within the geographical border

of a country . What is happening to the GDP of a country over time is an important indicator of how well the economy is performing .

Calculating GDP involves adding together trillions of different goods and services produced by the economy .Computation of the GDP focuses on transactions involving final output of goods and services produced in the current year .

To Calculate GDP for a number of different goods national income accounting uses market prices . For example , if the economy were to produce **8 tons** of wheat and **4 pears** , each ton of wheat sold for **1 thousand dollar** who they sold **1.5 thousand** for each ton , GDP would equal the total of the quantity of wheat times its price and quantity of pears times its price . this would like look :

GDP = price of wheat . quantity of wheat + price of pears .

quantity of pears

GDP = 1000 $. 8 tons + 1.500 $. 4

= 14000 $

There are two principal ways of calculating GDP :

1.Expenditure Approach :

GDP = C + I + G + (X-M)

The first way focuses on total expenditures on goods and services produced in the period .

2.Income Approach :

NI = W + R + i + PR

The second Approach concentrates on the payments to the factors of production involved in those production activities within the period .

In principle the two approaches should result in the same GDP value since expenditure by one party is always an income for some other party , however some discrepancies arise due to measurement errors .

Over a one-year period much like GDP , this means that the economic activity of U.S.A citizen who is working abroad is counted in the U.S.A GNP and not in GDP . But when a Japanese's workers in the U.S.A geographical boundary of U.S.A they will be counted in Japanese's GNP and U.S.A GDP not GNP .

GNP : is called the net foreign factor income , where foreign income that is earned domestically subtracted from income

received from foreign domestic sources .In other words it is a country's Gross Domestic Product subtracted from its Gross National Product . In many countries there are significant differences between their GDP and GNP .This is not as much of an issue for the U.S.A as it for developing countries because of their revenue comes from foreign direct investment .This means that foreign companies are locating within another country's borders and doing business . The revenue from the foreign company will count in the home country's GDP but not in their GNP . If a country has a lot of foreign investment then it will have not a higher GNP than GDP .

Net National Product (NNP) is the Gross National Product Minus capital depreciation

NNP = GNP - Depreciation

Depreciation: Is usually about ten percent of GNP and subtracting it from GNP displays the net result of all economic activity .

Demand

The first side in the market, where the consumer demand and purchase goods and services, the consumer but the own table that quantities will purchase each possible price for this commodity.

Understanding Demand Schedule

A demand schedule most commonly consists of two columns. The first column lists a price for a product in ascending or descending order. The second column lists the quantity of the product desired or demanded at that price. When the data in the demand schedule is graphed to create the demand curve, it supplies a visual demonstration of the relationship between price and demand, allowing easy estimation of the demand for a product or service at any point along the curve.

The demand schedule shows exactly how many units of a good or service will be bought at each price. Using this data, economists and industry analysts can create a demand curve. Both the curve and the schedule describe the relationship between a good's price and the quantity demanded of that good.

the consumer capacity to purchase the commodity with no desire to obtain will not have an (effective demand). The law of demand guides

this relationship, It states that the quantity demanded will drop as the price rises, or "all other things being equal." Those other things that must remain equal are the determinants of demand: the price of related goods, income, tastes, and expectations. There's an additional determinant for aggregate demand: the number of potential buyers in the market. We'll review how to describe demand schedules in terms of price elasticity along with an example of how you can use a demand schedule to project how much beef a family would buy over the course of a year. Finally, the time period in which the consumer request must be determined on the commodity, where the consumer can change its request for the commodity over time. Table (1) illustrates the request table for a particular consumer on a commodity over a specific period of time.

(1)

Demand Schedule

month	Prices Dollar/lbs	Quantity in lbs.
Jan	3.4	10
Feb	3.5	9.8
Mar	3.6	9.5
Apr	3.8	9.3
May	3.9	9.2
Jun	4	9.1
Jul	4.1	8.8
Aug	4.2	8.7
Sep	4.3	8.5
Oct	4.5	8.3

What Is Quantity Demanded

Quantity demanded is a term used in economics to describe the total amount of a good or service that consumers demand over a given interval of time. It depends on the price of a good or service in a marketplace, regardless of whether that market is in equilibrium .The relationship between the quantity demanded and the price is known as the demand curve, or simply the demand. The degree to which the quantity demanded changes with respect to price is called the elasticity of demand.

Inverse Relationship of Price and Demand

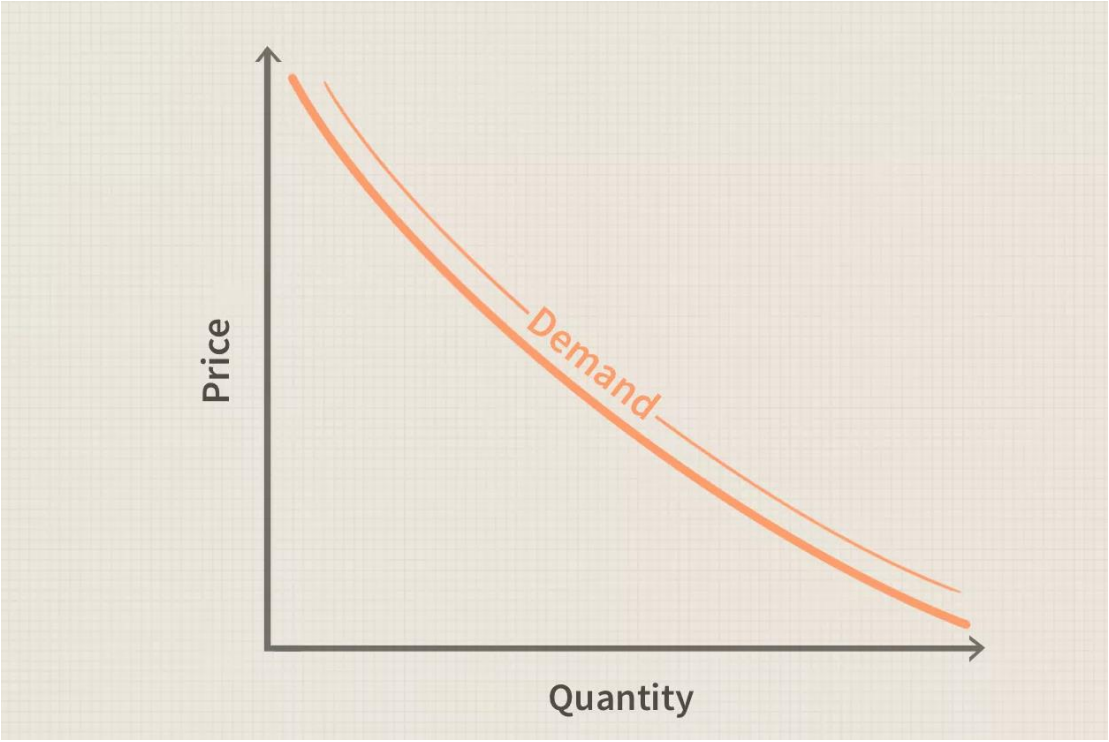
The price of a good or service in a marketplace determines the quantity that consumers demand. Assuming that non-price factors are removed from the equation, a higher price results in a lower quantity demanded and a lower price results in higher quantity demanded. Thus, the price of a product and the quantity demanded for that product have an inverse relationship, as stated in the law of demand.

Change in Quantity Demanded

A change in quantity demanded refers to a change in the specific quantity of a product that buyers are willing and able to buy. This change in quantity demanded is caused by a change in the price.

Increase in Quantity Demanded

An increase in quantity demanded is caused by a decrease in the price of the product (and vice versa). A demand curve illustrates the quantity demanded and any price offered on the market. A change in quantity demanded is represented as a movement along a demand curve. The proportion that quantity demanded changes relative to a change in price is known as the elasticity of demand and is related to the slope of the demand curve.



Price Elasticity of Demand

The proportion to which the quantity demanded changes with respect to price is called elasticity of demand. A good or service that is highly elastic means the quantity demanded varies widely at different price points. Conversely, a good or service that is inelastic is one with a quantity demanded that remains relatively static at varying price points. An example of an inelastic good is insulin. Regardless of price point, those who need insulin demand it at the same amount.

Determinants of Demand:

The goods prices are not only the factor that determines the quantity demand of goods, there are many factors affecting in the quantity demand:

1.Income: When income rises, so will the quantity demanded. When income falls, so will demand. But if your income doubles, you won't always buy twice as much of a particular good or service. There's only so many pints of ice cream you'd want to eat, no matter how wealthy you are , and this is an example of "marginal utility." Marginal utility is the concept that each unit of a good or service is a little less useful to you than the first. At some point, you won’t want it anymore, and the marginal utility drops to zero. The first pint of ice cream tastes delicious.

You might have another. But after that, the marginal utility starts to decrease to the point where you don't want any more.

2.Prices of related goods or services: The price of complementary goods or services raises the cost of using the product you demand, so you'll want less. For example, when gas prices rose to $4 a gallon in 2008, the demand for gas-guzzling trucks and SUVs fell. Gas is a complementary good to these vehicles. The cost of driving a truck rose along with gas prices. The opposite reaction occurs when the price of a substitute rises. When that happens, people will want more of the good or service and less of its substitute. That's why Apple continually innovates with its iPhones and iPods. As soon as a substitute, such as a new Android phone, appears at a lower price, Apple comes out with a better product. Then the Android is no longer a substitute.

3.Tastes: When the public's desires, emotions, or preferences change in favour of a product, so does the quantity demanded. Likewise, when tastes go against it, that depresses the amount demanded. Brand advertising tries to increase the desire for consumer goods.

4.Expectations: When people expect that the value of something will rise, they demand more of it. That helps explains the housing asset bubble of 2005. Housing prices rose, but people kept buying houses because they expected the price to continue to increase. Prices continued

increasing until the bubble burst in 2007. New home prices fell 22% from their peak of $262,200 in March 2007 to $204,200 in October 2010. However, the quantity demanded didn't increase—even as the price decreased—and sales fell from a peak of 1.2 million in 2005 to a low of 306,000 in 2011.So why didn't the quantity demanded increase as the price fell? It's in part because the broader economy was experiencing a recession. People expected prices to continue falling, so they didn't feel an urgency to buy a home. Record levels of foreclosures entered the market due to the subprime mortgage crisis. Demand for homes didn't increase until people expected future home prices would, too.

5.Number of buyers in the market: The number of consumers affects overall, or "aggregate," demand. As more buyers enter the market, demand rises. That's true even if prices don't change, and the U.S. saw this during the housing bubble of 2005. Low-cost and sub-prime mortgages increased the number of people who could afford a house. The total number of buyers in the market expanded. This increased demand for housing. When housing prices started to fall, many realized they couldn't afford their mortgages. At that point, they foreclosed. That reduced the number of buyers and drove down demand.

6.Other goods prices: The changes of other goods prices may have an impact on demand for a goods. This depends of course on the type of other goods; the three types of goods can be distinguished as follows:

- **Substitutes goods:** Goods that can be replaced by each other in consumption, such as tea and coffee. A high coffee price will increase demand for tea (where tea can replace coffee in consumption). The low coffee price will decline on the demand for tea, Fake goods that can replace each other; when the price of a good increases.

- **complement goods:** goods that tend to be consumed together; when the price of a good increases the demand for its complement will decrease. such as tea, sugar, camera and film. The high price of tea, for example, leads to the low demand for sugar, the low price of tea will rise to high demand for sugar.
- **Independent Goods:** It is not related to the consumption of one of them, such as apple and tea, for example.

5.**Consumer income:** Consumer income is one of the main factors specified for the consumer demand for the goods by type of goods. of goods can be distinguished.

- **normal good** a good for which demand will increase when buyers' incomes increase like luxurious clothing.

- **inferior good** a good for which demand will decrease when buyers' incomes increase for example Fake goods.

Supply

Supply is the other side of the market, where the producing selling various goods and services. At each possible price of the product that intends product, we find a certain amount of product will supply and sell it and this is called the supply.

What is a Supply Schedule?

Supply schedule is a chart that shows how much product a supplier will have to produce to meet consumer demand at a specified price based on the supply curve. In other words, it's basically a supply graph in spreadsheet form listing the quantity that needs to be produced at each product price level.

This concept is particularly important for businesses because they have to understand what happens to their inventory and units sold as the sales price changes. For example, the supply curve shows us that an increase in the selling price of a good will increase the business.

Thus, management can look at the schedule and plan what price they will market the product in the market and how many units they will need to produce at that price point.

This sound simply, but it's fair from that. The quantity supplied can be affected by a number of factors including political conditions of the country where the supplier operates, production costs, climatic conditions affecting the supply of product, prices of substitute and complementary products.

(2)
Supply Schedule

PRICE OF THE PRODUCT ($ PER KG)	QUANTITY SUPPLIED OF COMMODITY A (KG PER WEEK)
5	3.000
10	8.000
15	12.000
20	15.000

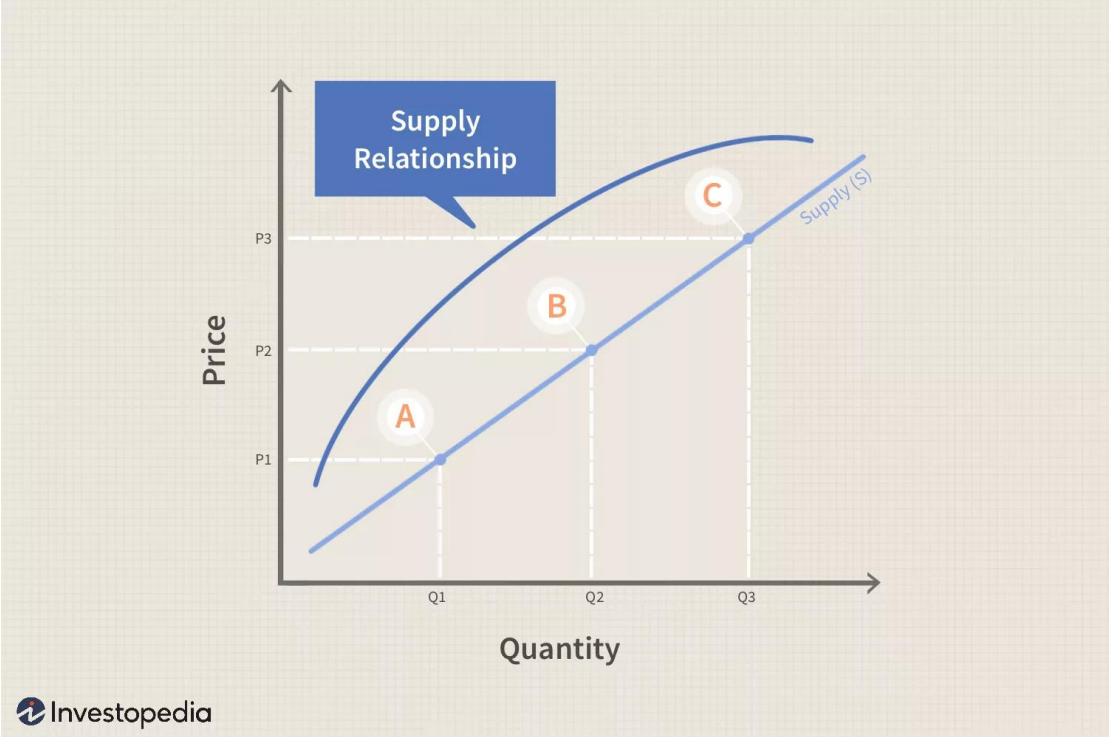
From Table, it is clear that the firm is supplying 3.000 kg per week of commodity A at a price of 5$ per kg. As the price rises from 5 to 10 per kg , the firm also increased the supply to 8.000 per kg. Therefore, the

individual supply schedule shown in Table indicates that the quantity supplied increases with a rise in price.

What is the Law of Supply?

The law of supply is the microeconomic law that states that, all other factors being equal, as the price of a good or service increases, the quantity of goods or services that suppliers offer will increase, and vice versa. The law of supply says that as the price of an item goes up, suppliers will attempt to maximize their profits by increasing the quantity offered for sale.

The chart below depicts the law of supply using a supply curve, which is upward sloping. A, B, and C are points on the supply curve. Each point on the curve reflects a direct correlation between quantity supplied (Q) and price (P). So, at point A, the quantity supplied will be Q1 and the price will be P1, and so on.



The supply curve is upward sloping because, over time, suppliers can choose how much of their goods to produce and later bring to market. At any given point in time however, the supply that sellers bring to market is fixed, and sellers simply face a decision to either sell or withhold their stock from a sale; consumer demand sets the price and sellers can only charge what the market will bear.

If consumer demand rises over time, the price will rise, and suppliers can choose devoted new resources to production (or new suppliers can enter the market) which increases the quantity supplied. Demand ultimately sets the price in a competitive market, supplier response to the price they can expect to receive sets the quantity supplied.

The law of supply is one of the most fundamental concepts in economics. It works with the law of demand to explain how market economies allocate resources and determine the prices of goods and services.

Determinants of Supply:

The supply law provides for a positive relationship between the goods and quantity price supplied, by assuming other things in their event. It is worth mentioning that there is a difference between the quantity supplied and the supply, as this difference is due to the specific factors. The goods price is the only factor that determines the quantity supplied from the goods. Thus, the change of price will change the quantity supplied positively. Other factors, which are mentioned in the supply law, are the factors that locate the supply curve, and then change these factors will change the entire supply curve to another location, these factors are:

1.Production factors prices: The high prices of production factors used in the goods or service products, will increase the cost of producing this goods or service, so the products will produce fewer amounts, which pays the supply to decline, which means that the quantities shown are less than former at each level. On the other hand, the low prices of production factors mean low cost of producing this good. This helps the product to produce larger quantities.

2.The number of producers: When number of goods producers increases whenever the supply is increasing from goods, so when the number of producer goods was decline whenever the supply from it was decline.

3.The technical used: The development of the technical level used in the goods production process is reduced to reduce the cost of production, and then high supply. The low-level technology or decreases led to increases the cost of production.

4.Tax and Assistance: when the Government has imposed a tax on production, this means the high cost of production of this goods. When the Government gives Assistance to the product, this means low production cost, which helps the products produce greater quantities of the goods.

Markets

Market Importance: Determines the form of the demand curve of the facility and therefore has a direct impact on the expected sales of the facility.

Market Structure Standards:

1. The number of traders in the market (large or few).

2. specifications Goods or service (homogeneous or mixed).

3. Free access to the market or get out of it (available or unavailable).

1.perfect competition

The concept of perfect competition applies when there are many producers and consumers in the market and no single company can influence the pricing. A perfectly competitive market has the following characteristics:

- There are many buyers and sellers in the market.
- Each company makes a similar product.
- Buyers and sellers have access to perfect information about price.
- There are no transaction costs.
- There are no barriers to entry into or exit from the market.

All goods in a perfectly competitive market are considered perfect substitutes, and the demand curve is perfectly elastic for each of the small, individual firms that participate in the market. These firms are price takers–if one firm tries to raise its price, there would be no demand for that firm's product. Consumers would buy from another firm at a lower price instead.

Firm Revenues

A firm in a competitive market wants to maximize profits just like any other firm. The profit is the difference between a firm's total revenue and its total cost. For a firm operating in a perfectly competitive market, the revenue is calculated as follows:

- Total Revenue = Price * Quantity
- AR (Average Revenue) = Total Revenue / Quantity
- MR (Marginal Revenue) = Change in Total Revenue / Change in Quantity

The average revenue (AR) is the amount of revenue a firm receives for each unit of output. The marginal revenue (MR) is the change in total revenue from an additional unit of output sold. For all firms in a competitive market, both AR and MR will be equal to the price.

Comparative Advantage and International Trade

One of the most important implications of the concepts of comparative advantage and the production possibilities curve relates to international trade. We can think of different nations as being equivalent to Christie Ryder's plants. Each will have a comparative advantage in certain activities, and efficient world production requires that each nation

specialize in those activities in which it has a comparative advantage. A failure to allocate resources in this way means that world production falls inside the production possibilities curve; more of each good could be produced by relying on comparative advantage.

If nations specialize, then they must rely on each other. They will sell the goods in which they specialize and purchase other goods from other nations. Suppose, for example, that the world consists of two continents that can each produce two goods: South America and Europe can produce food and computers. Suppose they can produce the two goods according to the tables in Panels (a) and (b) of Figure 2.12 "Production Possibilities Curves and Trade". We have simplified this example by assuming that each continent has a linear production possibilities curve; the curves are plotted below the tables in Panels (a) and (b). Each continent has a separate production possibilities curve; the two have been combined to illustrate a world production possibilities curve in Panel (c) of the exhibit.

2.Monopoly market

A monopoly is an economic market structure where a specific person or enterprise is the only supplier of a particular good.

A monopoly can be recognized by certain characteristics that set it aside from the other market structures:

- **Profit maximize:** a monopoly maximizes profits. Due to the lack of competition a firm can charge a set price above what would be charged in a competitive market, thereby maximizing its revenue.
- **Price maker:** the monopoly decides the price of the good or product being sold. The price is set by determining the quantity in order to demand the price desired by the firm (maximizes revenue).

- **High barriers to entry:** other sellers are unable to enter the market of the monopoly.
- **Single seller:** in a monopoly one seller produces all of the output for a good or service. The entire market is served by a single firm. For practical purposes the firm is the same as the industry.
- **Price discrimination:** in a monopoly the firm can change the price and quantity of the good or service. In an elastic market the firm will sell a high quantity of the good if the price is less. If the price is high, the firm will sell a reduced quantity in an elastic market.

Sources of Monopoly Power

In a monopoly, specific sources generate the individual control of the market. Sources of power include:

- Economies of scale
- Capital requirements
- Technological superiority
- No substitute goods
- Control of natural resources
- Network externalities
- Legal barriers
- Deliberate actions

Monopoly vs. Competitive Market

Monopolies and competitive markets mark the extremes in regards to market structure. There are a few similarities between the two including: the cost functions are the same, both minimize cost and maximize profit,

the shutdown decisions are the same, and both are assumed to have perfectly competitive market factors.

However, there are noticeable differences between the two market structures including: marginal revenue and price, product differentiation, number of competitors, barriers to entry, elasticity of demand, excess profits, profit maximization, and the supply curve. The most significant distinction is that a monopoly has a downward sloping demand instead of the "perceived" perfectly elastic curve of the perfectly competitive market.

conditions of the full monopoly market

- The presence of one product goods.
- There are no presence other facilities produce alternative goods for the monopolist.
- strong contraindications to prevent new competitors to the market.

Causes of monopoly:

- Patent possession
- possession of a trademark
- Get a concession from the government
- Natural monopoly (small market, high costs, one facility - meets the full market need).
-

3.Monopolistic Competition

Monopolistic competition is a type of imperfect competition such that many producers sell products that are differentiated from one another.

Monopolistic competition is a type of imperfect competition such that many producers sell products that are differentiated from one another as goods but not perfect substitutes (such as from branding, quality, or location). In monopolistic competition, a firm takes the prices charged by its rivals as given and ignores the impact of its own prices on the prices of other firms.

Unlike in perfect competition, firms that are monopolistically competitive maintain spare capacity. Models of monopolistic competition are often used to model industries. Textbook examples of industries with market structures similar to monopolistic competition include restaurants, cereal, clothing, shoes, and service industries in large cities.

Monopolistic competition is different from a monopoly. A monopoly exists when a person or entity is the exclusive supplier of a good or service in a market. The demand is inelastic and the market is inefficient.

Monopolistic competitive markets:

- have products that are highly differentiated, meaning that there is a perception that the goods are different for reasons other than price;
- have many firms providing the good or service;
- firms can freely enter and exits in the long-run;
- firms can make decisions independently;

- there is some degree of market power, meaning producers have some control over price; and
- buyers and sellers have imperfect information.

Sources of Market Inefficiency

Markets that have monopolistic competition are inefficient for two reasons. The first source of inefficiency is due to the fact that at its optimum output, the firm charges a price that exceeds marginal costs. The monopolistic competitive firm maximizes profits where marginal revenue equals marginal cost. A monopolistic competitive firm's demand curve is downward sloping, which means it will charge a price that exceeds marginal costs. The market power possessed by a monopolistic competitive firm means that at its profit maximizing level of production there will be a net loss of consumer and producer surplus.

The second source of inefficiency is the fact that these firms operate with excess capacity. The firm's profit maximizing output is less than the output associated with minimum average cost. All firms, regardless of the type of market it operates in, will produce to a point where demand or price equals average cost. In a perfectly competitive market, this occurs where the perfectly elastic demand curve equals minimum average cost. In a monopolistic competitive market, the demand curve is downward sloping. In the long run, this leads to excess capacity.

One of the defining traits of a monopolistically competitive market is that there is a significant amount of non- price competition. This means that product differentiation is key for any monopolistically competitive firm. Product differentiation is the process of distinguishing a product or service from others to make it more attractive to a target market.

Although research in a niche market may result in changing a product in order to improve differentiation, the changes themselves are not differentiation. Marketing or product differentiation is the process of describing the differences between products or services, or the resulting list of differences; differentiation is not the process of creating the differences between the products. Product differentiation is done in order to demonstrate the unique aspects of a firm's product and to create a sense of value.

In economics, successful product differentiation is inconsistent with the conditions of perfect competition, which require products of competing firms to be perfect substitutes.

Consumers do not need to know everything about the product for differentiation to work. So long as the consumers perceive that there is a difference in the products, they do not need to know how or why one product might be of higher quality than another. For example, a generic brand of cereal might be exactly the same as a brand name in terms of quality. However, consumers might be willing to pay more for the brand name despite the fact that they cannot identify why the more expensive cereal is of higher "quality."

There are three types of product differentiation:

- Simple: the products are differentiated based on a variety of characteristics;
- Horizontal: the products are differentiated based on a single characteristic, but consumers are not clear on which product is of higher quality; and

- Vertical: the products are differentiated based on a single characteristic and consumers are clear on which product is of higher quality.

Differentiation occurs because buyers perceive a difference. Drivers of differentiation include functional aspects of the product or service, how it is distributed and marketed, and who buys it. The major sources of product differentiation are as follows:

- Differences in quality, which are usually accompanied by differences in price;
- Differences in functional features or design;
- Ignorance of buyers regarding the essential characteristics and qualities of goods they are purchasing;
- Sales promotion activities of sellers, particularly advertising; and
- Differences in availability (e.g. timing and location).

The objective of differentiation is to develop a position that potential customers see as unique. Differentiation affects performance primarily by reducing direct competition. As the product becomes more different, categorization becomes more difficult, and the product draws fewer comparisons with its competition. A successful product differentiation strategy will move the product from competing on price to competing on non-price factors.

Conditions of the monopolistic competition market

- A large number of sellers in the market
- Freedom of access to the market and get out of it
- Goods or service sold is similar but not homogeneous
- Ability to promote products

Factors of excellence in the market:

- The variation of the goods in terms of shape

- Difference of service in terms of quality

- Difference of advertising methods

- Differences of places

-Different number of working hours

-Additional services associated with the goods

4.An oligopolistic market

Oligopoly is a market structure in which there are a few firms producing a product. When there are few firms in the market, they may collude to set a price or output level for the market in order to maximize industry profits. As a result, price will be higher than the market-clearing price, and output is likely to be lower. At the extreme, the colluding firms may act as a monopoly, reducing their individual output so that their collective

output would equal that of a monopolist, allowing them to earn higher profits.

If oligopolists individually pursued their own self-interest, then they would produce a total quantity greater than the monopoly quantity, and charge a lower price than the monopoly price, thus earning a smaller profit. The promise of bigger profits gives oligopolists an incentive to cooperate. However, collusive oligopoly is inherently unstable, because the most efficient firms will be tempted to break ranks by cutting prices in order to increase market share.

Several factors deter collusion. First, price-fixing is illegal in the United States, and antitrust laws exist to prevent collusion between firms. Second, coordination among firms is difficult, and becomes more so the greater the number of firms involved. Third, there is a threat of defection. A firm may agree to collude and then break the agreement, undercutting the profits of the firms still holding to the agreement. Finally, a firm may be discouraged from collusion if it does not perceive itself to be able to effectively punish firms that may break the agreement.

In contrast to price-fixing, price leadership is a type of informal collusion which is generally legal. Price leadership, which is also sometimes called parallel pricing, occurs when the dominant competitor publishes its price ahead of other firms in the market, and the other firms then match the announced price. The leader will typically set the price to maximize its profits, which may not be the price that maximized other firms' profits.

In an oligopoly, firms are interdependent; they are affected not only by their own decisions regarding how much to produce, but by the decisions of other firms in the market as well. Game theory offers a useful

framework for thinking about how firms may act in the context of this interdependence. More specifically, game theory can be used to model situations in which each actor, when deciding on a course of action, must also consider how others might respond to that action.

For example, game theory can explain why oligopolies have trouble maintaining collusive arrangements to generate monopoly profits. While firms would be better off collectively if they cooperate, each individual firm has a strong incentive to cheat and undercut their competitors in order to increase market share. Because the incentive to defect is strong, firms may not even enter into a collusive agreement if they don't perceive there to be a way to effectively punish defectors.

The prisoner's dilemma is a specific type of game in game theory that illustrates why cooperation may be difficult to maintain for oligopolists even when it is mutually beneficial. In the game, two members of a criminal gang are arrested and imprisoned. The prisoners are separated and left to contemplate their options. If both prisoners confess, each will serve a two-year prison term. If one confesses, but the other denies the crime, the one that confessed will walk free, while the one that denied the crime would get a three-year sentence. If both deny the crime, they will both serve only a one year sentence. Betraying the partner by confessing is the dominant strategy; it is the better strategy for each player regardless of how the other plays. This is known as a Nash equilibrium. The result of the game is that both prisoners pursue individual logic and betray, when they would have collectively gotten a better outcome if they had both cooperated.

A few producers (two more) making any product that directly affects the profits of others and their share in the market.

- Species of competitive market
- oligopolistic competition with homogeneous products
- oligopolistic competition with similar products

The restrictions on entering new producers

- Size economies make unprecedented to many companies work in the same activity.

- Current Producers (Federal Union) cut prices to a limit prevents the new product from entering the market.

Comparison of markets

Market shape	Number of producers	Product Item Type	selling price	Product capacity to control the price	Market entry terms
perfect competition المنافسة الكاملة	very big	Completely homogeneous	Always constant	He has no ability	Easy
Monopoly market سوق الاحتكار التام	One	Different and has no nearby alternatives	Reverse changes to quantity sold	Available very large	Closed
Monopolistic Competition سوق المنافسة الاحتكارية	Big	similar	Reverse changes to quantity sold	Available in a few	Easy
An oligopolistic market سوق منافسة القلة	few	Different and have nearby alternatives	Reverse changes to quantity sold	Available very much	Difficult