Understanding Basic Economics

BA291 Week 3

THAMMASAT
people & sustainability

Agenda

1. What Is This Thing Called the Economy?
2. Economic Systems
3. The Forces of Demand and Supply
4. The Macro View: Understanding How an Economy Operates
5. Government's Role in a Free-Market System

Learning Objectives

1. Define economics and explain why scarcity is central to economic decision making
2. Differentiate among the major types of economic systems
3. Explain the interaction between demand and supply

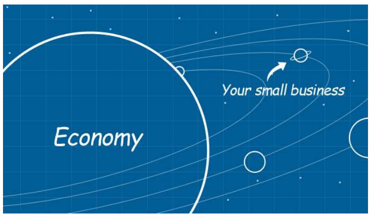
Learning Objectives (cont.)

4. Identify four macro-economic issues that are essential to understanding the behavior of the economy
5. Outline the debate over de-regulation and identify four key roles that governments play in the economy
6. Identify the major ways of measuring economic activity

1. What Is This Thing Called the Economy?

Economy

–The sum total of all the economic activity within a given region



Economics

– The study of how a society uses its scarce resources to produce and distribute goods and services

What Is This Thing Called the Economy?

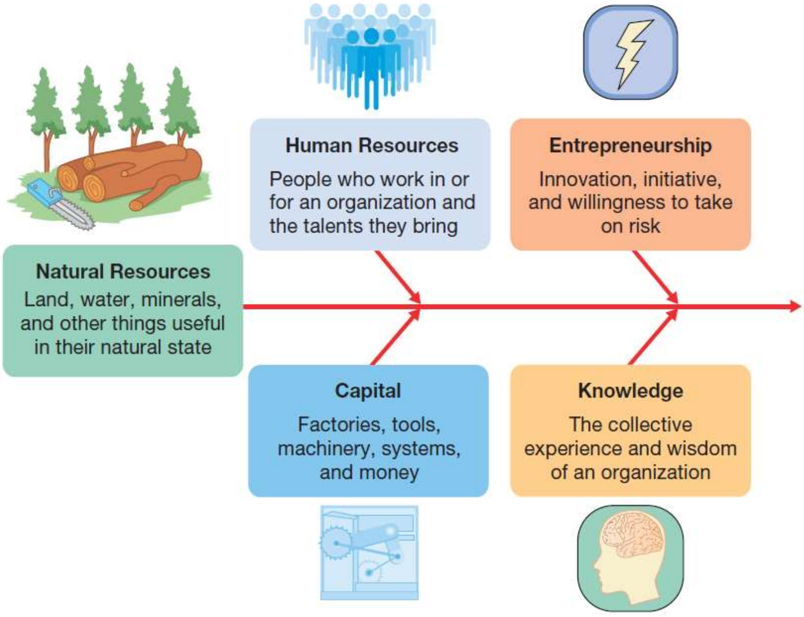
Macroeconomics

The study of "big picture" issues in an economy, including competitive behavior among firms, the effect of government policies, and overall resource allocation issues

Microeconomics

The study of how consumers, businesses, and industries collectively determine the quantity of goods and services demanded and supplied at different prices

Factors of Production



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Factors of Production

- **Natural resources**
  - Land, forests, minerals, water, and other tangible assets usable in their natural state.
- **Human resources**
  - All the people who work in an organization or on its behalf.
- **Capital**
  - The funds that finance the operations of a business as well as the physical, human-made elements used to produce goods and services, such as factories and computers.
- **Entrepreneurship**
  - The combination of innovation, initiative, and willingness to take the risks required to create and operate new businesses.
- **Knowledge**
  - Expertise gained through experience or association.

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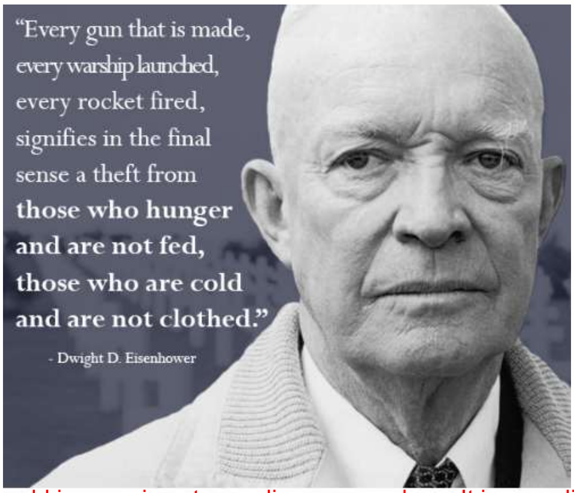
The Economic Impact of Scarcity

- **Scarcity**
  - A condition of any productive resource that has finite supply.
- **Opportunity cost**
  - The value of the most appealing alternative not chosen

Engagement Question

Share your recent trade-off by explaining the choices you have, the choice you made, and its opportunity cost.

Scarcity means we must make a choice.



"This world in arms is not spending money alone. It is spending the sweat of its laborers, the genius of its scientists, the hopes of its children."

2. Economic Systems

Public/government ownership of productive resources; centralized economic planning and control

Communism
- State ownership of all major productive resources
- Absence of economic classes
- Few opportunities for entrepreneurship

Socialism
- State ownership of certain productive resources
- Managed efforts to minimize dramatic differences between economic classes
- Opportunities for entrepreneurship, with varying degrees of restrictions

Capitalism
- Private ownership of most productive resources
- Few efforts to minimize differences between economic classes
- Government policies actively support entrepreneurship

Private ownership of productive resources; free-market economic principles

Economic system

The policies that define a society's particular economic structure; the rules by which a society allocates economic resources

✓What will we produce?
✓How will we produce it?
✓Who gets it?

Free-Market Systems

An economic system in which, decisions about what to produce and in what quantities, are decided by the market's buyers and sellers

Capitalism

Economic system based on economic freedom and competition.

Private ownership of resources becomes the bases for the production and distribution of good and services

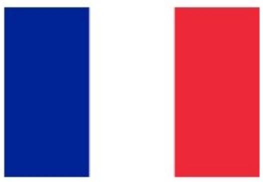
Capitalist are people who personally own or control the physical capital of industrial production such as machinery, factories and distribution networks, raw materials and technology

Planned Systems

- **Planned system**
  - Economic system in which the government controls most of the factors of production and regulates their allocation.

Socialism

- **Socialism**
  - Economic system characterized by public ownership and operation of key industries combined with private ownership and operation of less-vital industries



Nationalization and Privatization

- **Nationalization**
  - A government's takeover of selected companies
  - or industries
- **Privatization**
  - Turning over services once performed by the government and allowing private businesses to perform them instead

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Engagement Question

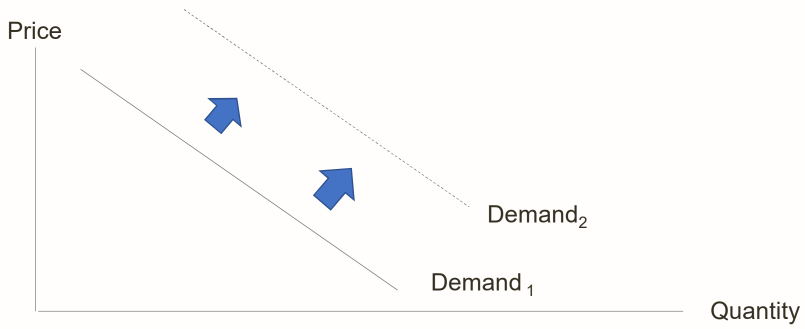
Would you rather pay lower taxes and accept the fact that you need to pay for many services such as health care and education or pay higher taxes with the assurance that the government will provide many basic services for you? Why?

3. The Forces of Demand and Supply

- **Demand**
  - Buyers' willingness and ability to purchase products at various price points
- **Supply**
  - A specific quantity of a product that the seller is able and willing to provide at various prices

Understanding Demand

- **Demand curve**
  - A graph of the quantities of a product that buyers will purchase at various prices.

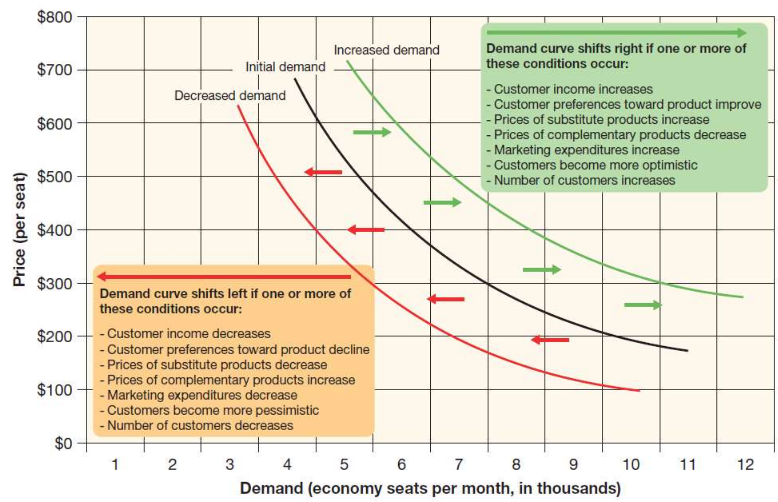


Shift in Demand

Major factors that can cause overall demand to increase or decrease:

- Customer income
- Customer preferences toward the product
- The price of substitute products
- The price of complementary products
- Marketing expenditures
- Customer expectations about future prices and their own financial well-being

Demand Curve

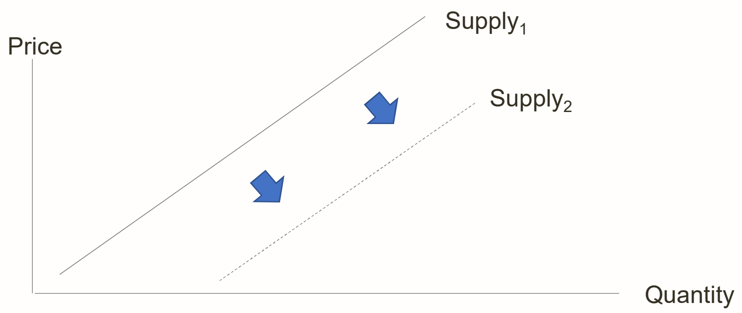


Engagement Question (in Moodle's Forum)

- Give example of a shift in Demand in Thailand
- Explain the situation and its cause
- Did the demand curve go back to its original place?

Understanding Supply

- **Supply curve**
  - A graph of the quantities of a product that sellers will offer for sale, regardless of demand, at various prices.

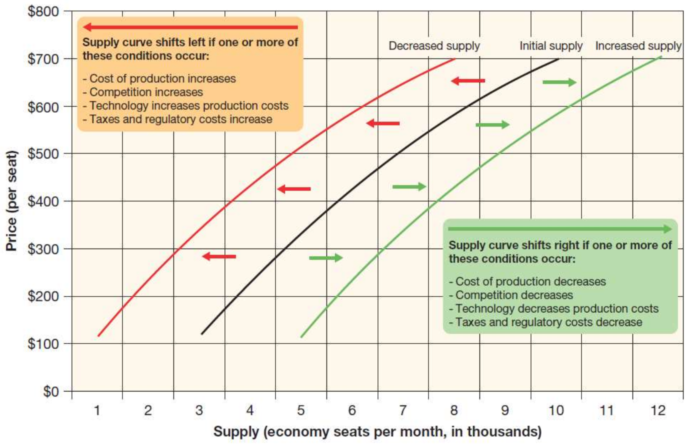


Shift in Supply

Major factors that can cause overall supply to increase or decrease:

- Cost of production increase
- Competition increase
- Technology decreases production costs
- Taxes and regulatory costs increase

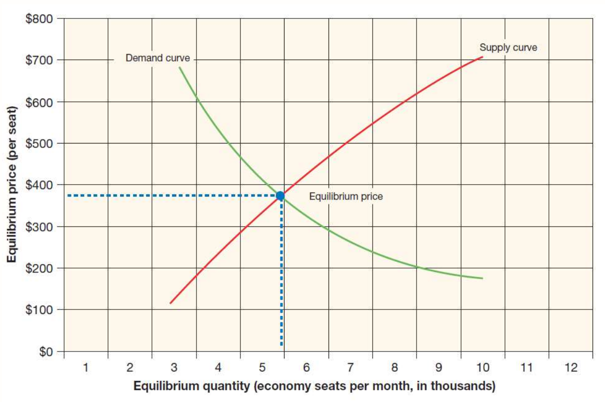
Supply Curve



Engagement Question (in Moodle's Forum)

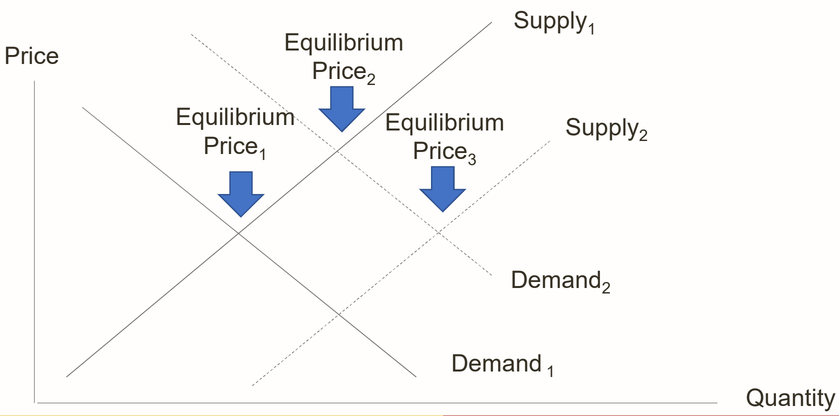
- Give example of a shift in Supply in Thailand
- Explain the situation and its cause
- Did the supply curve go back to its original place?

The Relationship Between Demand and Supply



- **Equilibrium point**
  - The point at which quantity supplied equals quantity demanded. Because the supply and demand curves are dynamic, so is the equilibrium point. As variables affecting supply and demand change, so will the equilibrium price.

Understanding How Demand and Supply Interact



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Engagement Questions

Are there any products or brands you are so loyal to that you will purchase them at almost any price? Will you accept less-expensive substitutes?

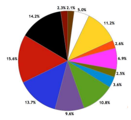
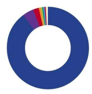
Have you ever purchased something simply because it was on sale? Why or why not?

4. The Macro View: Understanding How an Economy Operates

✓Competition in a free-market system
✓Business cycle
✓Unemployment
✓Inflation

Competition in a Free-Market System

- **Pure competition (Perfect Competition)**
  - A situation in which so many buyers and sellers exist that no single buyer or seller can individually influence market prices
- **Monopolistic competition**
  - A situation in which many sellers differentiate their products from those of competitors, in at least some small way
- **Oligopoly**
  - A market situation in which a very small number of suppliers, sometimes only two, provide a particular good or service
- **Monopoly**
  - A situation in which one company dominates a market to the degree that it can control prices

	Perfect Competition	Monopolistic Competition	Oligopoly	Monopoly
1. # of sellers	Large 	Large	Few 	Only 1 
2. Products	Identical	Differentiated, highly similar	Identical Differentiated	Unique
3. Market Entry & Exit	Easy; Free	Easy	Some	Almost impossible
4. Market Power	None	Small	Large	Complete

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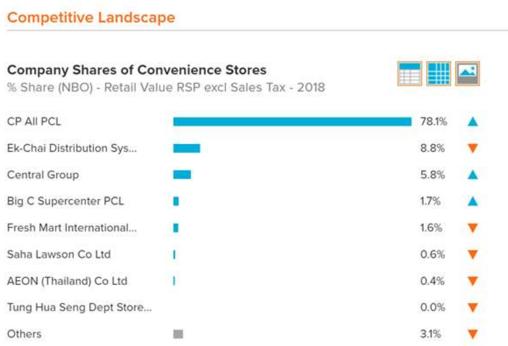
Some key terms: Market Share

- The total percentage of a product a company sells in a particular market

Retail Industry (Convenience Stores) in Thailand



Source: Euromonitor 2019

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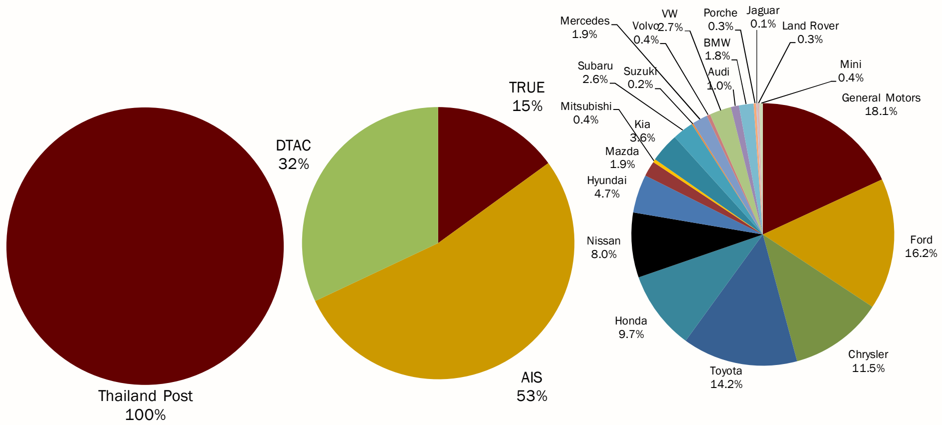
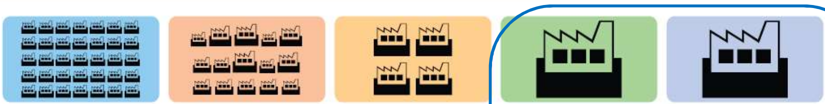
Some key terms: Market Concentration



A rule of thumb is that an oligopoly exists when the top five firms in the market account for more than _____% of total market sales.

Categories of Competition



Pure Competition

Characteristics:
- Many small suppliers
- Virtually identical products
- Low barriers to entry

Price competition:
- No single firm can grow large enough to influence prices across the market

Buyers' choices:
- Extensive

Monopolistic Competition

Characteristics:
- Can have few or many suppliers, of varying size
- Products can be distinguished but are similar enough to be replacements
- Variable barriers to entry but market open to all

Price competition:
- Firms that excel in one or more aspects can gain some control over pricing

Buyers' choices:
- Extensive

Oligopoly

Characteristics:
- Small number of suppliers, even as few as just two (a *duopoly*)
- Products can be distinguished in important ways, but replacements are still available
- Barriers to entry tend to be high, making entering the market difficult

Price competition:
- Individual firms can have considerable control over pricing

Buyers' choices:
- Limited

Pure Monopoly

Characteristics:
- Only one supplier in a given market
- Monopoly achieved without government intervention, by innovation, specialization, exclusive contracts, or a simple lack of competitors
- Products are unique, with no direct replacements available
- Barriers to entry are extremely high, making entering the market difficult or impossible

Price competition:
- Suppliers can charge as much as they want, at least until people stop buying

Buyers' choices:
- None

Regulated Monopoly

Characteristics:
- Only one supplier in a given market
- Monopoly granted by government mandate, such as a license to provide cable TV and Internet service
- No product competition is allowed
- Barriers to entry are infinitely high; new competitors are not allowed

Price competition:
- Prices are set by government mandate

Buyers' choices:
- None

Competition in a Free-Market System (cont.)

Market Structure	Seller Entry Barriers	Seller Number
Perfect Competition	No	Unlimited
Monopolistic competition	No	Many
Oligopoly	Yes	Few
Monopoly	Yes	One

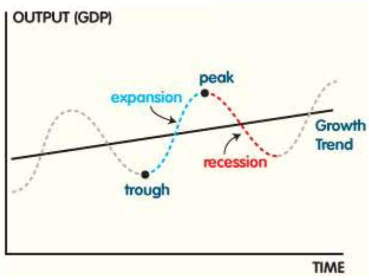
Homework for next week's topic

- Select one market/industry in Thailand
- Research key information about this industry below
  - Specify its category of competition (perfect competition, monopolistic competition, oligopoly, or monopoly) Explain why it falls under that category
  - Who are the major buyers of the industry's products?
  - Who are the major suppliers to the industry's operation?
  - What products can customers purchase instead of using the industry's products?
  - Name 3-5 major brands/players in this industry? Do you think they compete forcefully or not?

Tips: It is recommended that you read various sources and databases to get all the information such as Passport, Industry outlook by BOA, Kasikorn Research Center etc.

Business Cycles

- **Business cycles**
  - Pattern of expansion (recovery) and contraction (recession) in economic activity around the path of trend growth
  - Fluctuations in the rate of growth that an economy experiences over a period of several years
  - Inflation, growth, and unemployment are related through the business cycle



- **Recession**
  - A period during which national income, employment, and production all fall; defined as at least six months of decline in the GDP

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Unemployment

- **Unemployment rate**
  - The portion of the labor force (everyone over 16 who has or is looking for a job) currently without a job

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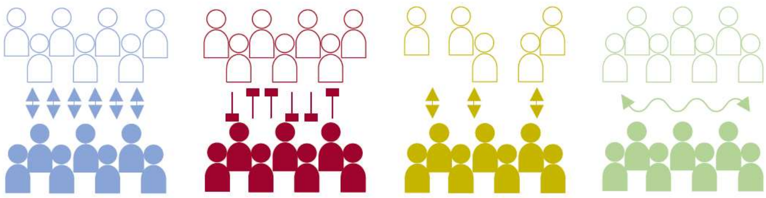
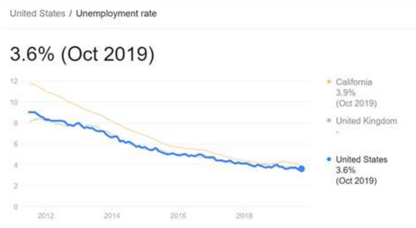
Types of Unemployment





Frictional Unemployment
- The "natural" flow of workers into and out of jobs, such as when a person leaves one job without first lining up a new job
- Always some level of frictional unemployment in the economy

Structural Unemployment
- A mismatch between workers' skills and current employer needs
- Workers can't find jobs that match their qualifications, and employers can't find employees with the skills their job openings require
- A never-ending concern as changes in the external environments of business make some skills obsolete and create demand for new skills

Cyclical Unemployment
- Caused by economic fluctuations
- When demand for goods and services drops, businesses reduce production, thereby requiring fewer workers
- An increasing number of people who want to work can't find jobs
- During catastrophic depressions, can run as high as 20 or 25 percent

Seasonal Unemployment
- Predictable increases and decreases in the need for workers in industries with seasonal fluctuations in customer demand
- Common in agriculture, leisure and entertainment, retailing, and accounting services

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Inflation and Deflation

- **Inflation**
  - An economic condition in which prices rise steadily throughout the economy and consequently, the purchasing power of currency is falling.

Deflation

An economic condition in which prices fall steadily throughout the economy

Deflation is not necessarily bad, but often periods of deflation can lead to economic stagnation and periods of high unemployment. This is because deflation can discourage spending because things will be cheaper in the future. Deflation can also increase debt burdens – reducing the spending power of firms and consumers.

- It is bad for the economy
- It is bad for debtors
- It is bad for companies
- It stops people spending
- It makes it difficult for central bankers to control the economy.

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Engagement Questions

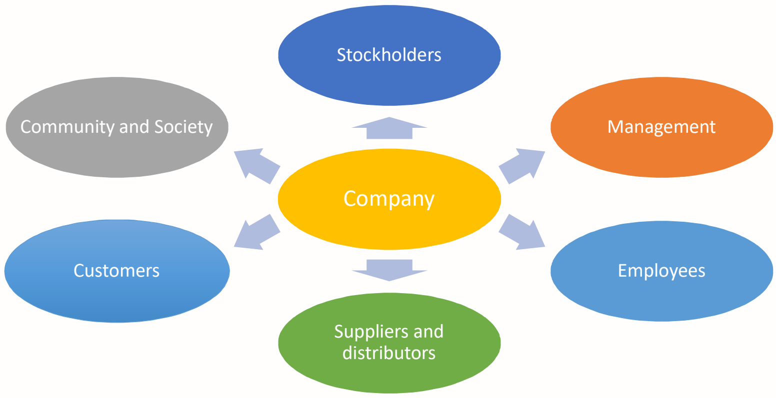
Are colleges and universities an example of pure competition or monopolistic competition? Why?

5. Government's Role in a Free-Market System

✓Protecting stakeholders
✓Fostering competition
✓Encouraging innovation and economic development
✓Stabilizing and stimulating the economy

Stakeholders

People or groups of people who supply a company with productive resources and thereby have an interest or effected by the company behaviors



Government's Role in a Free-Market System (cont.)

- **Regulation**
  - Relying more on laws and policies than on market forces to govern economic activity
- **De-regulation**
  - Removing regulations to allow the market to prevent excesses and correct itself over time

Stabilizing and Stimulating the Economy

- **Monetary policy**
  - Government policy and actions taken by the Federal Reserve Board to regulate the nation's **money supply**

Interest rate

Interest rate

- **Fiscal policy**
  - Strategy for the use of **government revenue** collection and **spending**, to influence the business cycle

Government Spending

Tax

Government Spending

Tax

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Engagement Questions

Would it be wise for the government to put price controls on college tuition? Why or why not?

Economic Measures and Monitors

✓Economic indicator
✓Price indexes
✓National economic output

Economic Measures and Monitors

- **Economic indicators**
  - Statistics that measure the performance of the economy

Consumer Confidence Index (CCI); Purchasing Managers Index (PMI); Housing starts; Durable-goods orders; Price indexes

Leading indicators suggest changes that may happen to the economy in the future and are therefore valuable for planning. In contrast, *lagging indicators* provide confirmation that something has occurred in the past.

employment rate, corporate profits

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Price Indexes

- **Consumer Price Index (CPI)**
  - A monthly statistic that measures changes in the prices of a representative collection of consumer goods and services
- **Producer Price Index (PPI)**
  - A statistical measure of price trends at the producer and wholesaler levels

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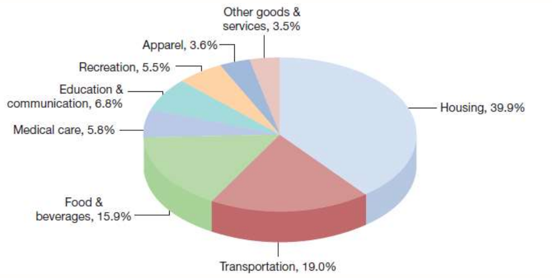
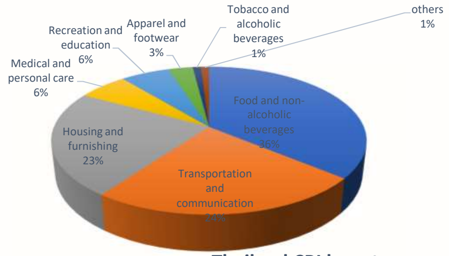
Composition of the Consumer Price Index





Thailand CPI by category

Source: U.S. Bureau of Labor Statistics, "Relative Importance of Items in the Consumer Price Index," December 2012, www.bls.gov.

Source: https://tradingeconomics.com/

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Gross Domestic Product

- Value of all final goods and services produced in a country within a given period
- Y = C + I + G + X – M
  - C = consumption
  - I = investment
  - G = government spending
  - X = export
  - M = import

Rank ▲	Name	GDP (IMF '19)	GDP (UN '16)	GDP Per Capita	2019 Population
1	United States	22.20 trillion	18.62 trillion	$67,063	331,002,651
2	China	15.47 trillion	11.22 trillion	$10,747	1,439,323,776
3	Japan	5.50 trillion	4.94 trillion	$43,450	126,476,461
4	Germany	4.16 trillion	3.48 trillion	$49,617	83,783,942
5	India	3.26 trillion	2.26 trillion	$2,361	1,380,004,385
6	United Kingdom	2.93 trillion	2.65 trillion	$43,118	67,886,011
7	France	2.88 trillion	2.47 trillion	$44,062	65,273,511
8	Italy	2.09 trillion	1.86 trillion	$34,575	60,461,826
9	Brazil	2.06 trillion	1.80 trillion	$9,703	212,559,417
10	Canada	1.83 trillion	1.53 trillion	$48,553	37,742,154
11	South Korea	1.74 trillion	1.41 trillion	$34,024	51,269,185
12	Russia	1.67 trillion	1.25 trillion	$11,426	145,934,462
13	Spain	1.50 trillion	1.24 trillion	$32,020	46,754,778
14	Australia	1.48 trillion	1.30 trillion	$58,097	25,499,884
15	Mexico	1.30 trillion	1.08 trillion	$10,065	128,932,753
16	Indonesia	1.21 trillion	932.26 billion	$4,420	273,523,615
20	Switzerland	740.70 billion	668.85 billion	$85,585	8,654,622
21	Poland	643.27 billion	471.40 billion	$16,997	37,846,611
22	Taiwan	633.70 billion		$26,607	23,816,775
23	Sweden	576.72 billion	514.48 billion	$57,105	10,099,265
24	Belgium	553.78 billion	467.96 billion	$47,782	11,589,623
25	Thailand	547.43 billion	407.03 billion	$7,843	69,799,978
26	Argentina	515.35 billion	545.87 billion	$11,403	45,195,774

Source: Worldpopulationreview.com

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Engagement Questions

Would it be wise for the government to put price controls on college tuition? Why or why not?

Summing Up Things to Do this week

- Moodle’s Forum about supply and demand (individual work)
- Gather basic data about one industry in Thailand (group work)
- Review Quiz2