

# MICROECONOMICS

SECOND EDITION



ROGER A. ARNOLD

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ROGER A. ARNOLD

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TO  
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# MICROECONOMICS



# PREFACE

In the second edition of *Microeconomics*, I have tried to retain the strengths of the first edition, eliminate any weaknesses, and continue in my endeavor to write a text that is both exciting and pedagogically sound. It is a cliché, perhaps, but nevertheless true: one of the major motivating factors for my writing a principles text is to convey to students the excitement, richness, and power of economic analysis that I, and thousands of economics professors across the country, experience daily.

The second edition of *Microeconomics* is a cleaner, better organized, more innovative text than the first edition. I have listened to the constructive comments of numerous reviewers and colleagues, hundreds of students, the editorial staff of West Publishing Company, and the little voice inside of me, to write a book that I trust you will find worth your time.

## ORGANIZATION OF THE SECOND EDITION

**Section I. Economics: The Science of Scarcity.** This book is organized into three sections. Section I discusses the key concepts and tools in economics. Two of the four chapters are devoted to supply-and-demand analysis. Upon completion of this section, the student should have a solid understanding of the economic way of thinking.

**Section II. Microeconomics.** Readers of the second edition will find the chapter organization of microeconomics the same as in the first edition—with one important change. Chapter 5, the first microeconomics chapter in the text, briefly discusses the players in microeconomics—consumers, firms, factor owners, and government—so that students know right away who and what is involved. Then it develops a “microeconomics mindset” the student can use to organize, categorize, and understand the myriad topics in microeconomics as he proceeds to read on. The “mindset” came by asking this question: What is microeconomics about? Here is my three-part answer.

First, the student learns that microeconomics is about consumers, firms, and factor owners sharing a reality: each has an objective, each faces constraints, and each has to make choices. Objectives-Constraints-Choices. For example, consumers’ objective is to maximize utility, and they are constrained by their limited incomes and by the positive prices for each good. Given limited purchasing ability, the consumer will attempt to gain as much utility as possible from each dollar spent. In practice, this is done by *choosing* marginal analysis in making consumption decisions—by comparing additional (marginal) benefits and additional (marginal) costs of each purchase. In short, the trilogy of objectives-constraints-choices gives our microeconomic discussion of consumers focus. The student quickly sees the key elements around which the whole discussion takes place.

Second, students learn that microeconomics is about the interaction between consumers and firms, and between firms and factor owners, in market settings. In

short, microeconomics is about markets. Once the student understands this, and realizes that much of what she learns has to do with the interactions of economic agents, we can go on to specify different types of market settings—e.g., perfectly competitive, monopolistic, and so on.

Third, microeconomics is about the workings of markets with and without government intervention. The student is instructed to examine both the *purpose* and the *effects* of government's involvement in markets. The *effects*, in particular, can be related to the objectives, constraints, and choices of consumers, firms, and factor owners. To illustrate, suppose government decides to tax firms. We would want to know how the tax affects the objectives, constraints, and choices of the firm, and then how the (perhaps) changed behavior on one side of the market (supply side) affects overall market outcomes.

In conclusion, the microeconomics mindset the student carries through his learning microeconomics includes the following points:

- Microeconomics is about consumers, firms, and factor owners.
- Consumers, firms and factor owners each have objectives.
- They try to achieve their objectives in the face of certain constraints.
- Because they try to achieve objectives in a world of constraints, they are forced to make choices.
- They make their choices in a certain way: by weighing additional benefits and additional costs.
- Consumers and firms, and firms and factor owners, interact in market settings. In any market, there is always something being bought and something being sold.
- There exist different types of market settings.
- Government can affect the behavior of consumers, firms, and factor owners, and thus affect overall market outcomes.

**The Power of Microeconomics.** I believe that microeconomic tools are the most powerful tools of analysis in the social sciences. From my reading and study, I do not believe that the fields of sociology, political science, or psychology have tools of analysis that come even close to the power of the *economist's microeconomic* tools. However, I also believe that college students are usually unaware of this—sometimes even after having taken an economics course or two. With this in mind, I have tried to sharpen the presentation of microeconomics in this edition, and mainly to apply microeconomic tools in a way that will catch the student's attention. I believe that microeconomic tools not only are powerful enough to tell students about costs, production, firms, market structures and so on, but are also powerful enough to help students gain insights into why they have the number of friends they have (why not more?), why they sometimes get bored, why they chose the major that they did, and why they are sometimes late for class, among other things. My deepest feeling is that unless we use the microeconomics tools we have at our disposal to excite students, they will continue to think that microeconomics is simply about the supply and demand for cars, or about the costs of a firm, and so on. Nobel Laureate James Buchanan once wrote that what a science [such as economics] does, or should do, is simply to allow the average man . . . to command the heights of genius. I rewrote the microeconomics section of the first edition of *Economics* with this statement in mind. I want students to come into the microeconomics principles class with nothing but their notebooks, pens, and an open mind, and I want them to leave feeling like they have found gold.

## THINKING LIKE AN ECONOMIST: A NEW FEATURE



The authors of principles books are quick to point out that their books teach students how to think like an economist—but they never tell us how they accomplish this feat. Supposedly, students will read the book and simply figure out how economists think. It is true that some students do pick up how economists think by using this method, but too many do not. I believe that it is the author's responsibility to explicitly point out, where possible, how economists think. I have done this throughout this book, at appropriate places. These places are easily identifiable throughout the text.

## ECONOMICS IN OUR TIMES: APPLICATIONS



Gary Becker, in his interview in this book, said that the way to give students a good feel for economics is to show them “how to use it to understand the world about them.” I believe Becker is exactly right. In the classroom, I have found that students get unusually excited over economics when I use it to provide them with insights into their world. After all, the student is rational; raise the benefits of learning economics relative to the costs, and he will want to learn more economics. I have tried to make the applications in this book as exciting and relevant to the student as I could. Some people may feel that a few of the applications are a little offbeat, and are not ordinary. Well, I hope so. I don't think that we have to continually use the same old applications to illustrate economic analysis to our students. We can break out of the mold sometimes, get a little daring, and just have some fun.

## INTERSPERSED QUESTIONS: ANTICIPATING WHAT THE READER WANTS TO ASK



Often when I read books I wish the author were around so that now and then I could ask a question. I think students feel the same way when they are reading an economics textbook such as this one. That is why I have interspersed throughout the text questions that the reader might have come up with as he or she is reading along. Then, I have answered these questions.

## INTERVIEWS: SOME NEW, MANY UPDATED



It is one thing to have the author of a text discuss the economic way of thinking, and it is quite another to read what Gary Becker has to say about it. It is one thing to have the author of a text discuss supply and demand analysis, and it is quite another to have Vernon Smith discuss it. There are 13 interviews with well-known economists in this text. The economists interviewed include Gary Becker, George Stigler, Gordon Tullock, William Baumol, John Kenneth Galbraith, Walter Williams, Murray Weidenbaum, Harold Demsetz, James Buchanan, Lester Thurow, Irma Adelman, Allen Kneese, and Vernon Smith. Many of the interviews are new and many are updated from the first edition.



## INTERNATIONAL COVERAGE

With international economic news making front-page headlines, it is imperative to present students with a book that clearly identifies how international economic events affect the U.S. economy and how U.S. economic events affect the world economy. This edition of *Microeconomics* has international economics thoroughly integrated throughout.

## A MODERN BOOK

The second edition of *Microeconomics* continues in the tradition of the first edition: to present the reader with a truly modern book. Topics added to the second edition include experimental economics, environmental economics, economic changes in Eastern Europe and the Soviet Union, and the Japanese economy, among others.

## SUPPLEMENTS: PRINTED, COMPUTERIZED, AND LASER TECHNOLOGY

The supplements that go along with this book include:

- Study Guides
- MicroGuide Computerized Study Guide
- Instructor's Manual
- Enrichment Lectures
- Test Bank (over 6,000 questions)
- WestTest Microcomputer Testing
- Study Wizard Software Package (Computer Software for Microeconomics and Macroeconomics)
- Transparencies
- Video disc/Videotape

**Study Guide.** The Study Guide was principally written by Thomas Wyrick of Southwest Missouri State University. Each chapter explains, reviews, and tests the student on important facts, concepts, and diagrams found in corresponding chapters in this book. Chapter parts include an introduction to and purpose of each chapter, a review of concepts from earlier chapters, a fill-in-the-blank review of concepts to be learned, and problems and exercises. I wrote the self-test that ends each chapter.

**MicroGuide Computerized Study Guide.** The computerized study guide allows students to sit at the computer and quiz themselves on text material chapter by chapter. The questions are taken from the printed study guide. Students can choose any chapter or combination of chapters and the program will provide multiple-choice, true/false, matching, and fill-in-the-blank questions. Special features include: feedback on the correct answer and page-referencing to the main text, grading at the end of each session, the option to print quiz questions and results. MicroGuide is available for IBM PCs/compatibles with 512K or Macintoshes with Hypercard.

**Instructor's Manual.** The Instructor's Manual was written by Keith A. Rowley, formerly of Baylor University. It offers detailed lecture assistance for this book. Chapter parts include an overview of each text chapter, a list of chapter objectives, a list of key terms, a detailed chapter outline with lecture notes, and answers to end-of-chapter questions.

**Enrichment Lectures.** Twenty-five lectures with accompanying transparencies are included in the supplement package. The lectures are on current topics of high interest to instructors and students alike. The lectures were prepared by Keith Rowley and Thomas Wyrick.

**Test Bank.** The double-size test bank contains more than 6,000 test questions. Approximately 1,000 questions are new, with special emphasis on graphing-related problems. The test bank was prepared by Patricia Freeman of University of Southern Louisiana and Dusan Stojanovic of Washington University.

**WestTest Microcomputer Testing.** The new WestTest 2.0 testing system for either IBM PCs and compatibles or Macintoshes allows you to choose, create, edit, store, and print exams and answer keys. The system is menu-driven with a new desktop format and the options of using keystrokes or a mouse, accelerators, and function keys.

**The New Economics Study Wizard 2.0 Software Package.** There is a microeconomics software package that comes with this book. The software package was developed by Dennis Muraoka of California State University at Long Beach. The software package has the following components: a graphics tutorial that is animated and annotated and contains a quiz on the graphs; terms and definitions in the form of a game; and a quiz that provides a review for the exam. Hardware requirements: IBM PC/compatibles, DOS 2.0 or higher with minimum 256K available in RAM. Graphics tutorials require CGA, EGA, or VGA with color monitor. At the end of each chapter in the text, students will find questions and problems. A few of the questions and problems have a logo next to them, indicating that the material in these questions and problems can be used in conjunction with the software package.

**Transparencies.** 150 transparencies (many in color) of key exhibits in the text are available for classroom use.

**Video Disc/Videotape.** I am excited about the fact that the second edition of *Economics* comes with a supplement like this one. Laser technology now makes it possible, with a touch of a button, to access key diagrams from the text. Not only that but the illustrations are presented in such a way that students can clearly and in proper time sequence see how the diagrams are built. Suppose the instructor wants to show students the intricacies of supply-and-demand analysis. He or she pushes the button, and there is a demand curve. Push the button again, and a supply curve appears. Push again, and the equilibrium point is identified. Push again, there is equilibrium price. And so on. For students this is a way to understand diagrams by seeing how they are built. For instructors, this is a way to offer step-by-step explanations and diagrammatics with simply a push of a button.

The new video disc also makes it possible to access footage from the popular

Economics USA\* series which was funded by the Annenberg/CPB project. This is a way to bring real-world economic events (sights, sounds, and analysis) into the classroom. Economics has never been more real and relevant to students. (All the video segments which appear on the disc are also available on videotape presented as clips in the same order in which they appear on the disc.)

## IN APPRECIATION

This book could not have been written and published without the generous and expert assistance of many people. A deep debt of gratitude is owed to the reviewers of the first edition, the reviewers of the second edition, and the numerous persons who have offered constructive comments and suggestions on one or both of the editions.

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