ECONOMICS ASSIGNMENT

NAME OF THE STUDENT

NAME OF THE UNIVERSITY

STUDENT'S ID

Contents

Introduction

The concerned questions of the assignment suggests an overview of the macroeconomics which a branch of economics that critically inspects the behaviour of an economy in an aggregative basis which mainly examines price levels, national income, inflation, growth rate, GDP (Gross Domestic Product) and unemployment changes.

The questions to be discussed in the later section of the essay are mostly related to interventions of OPEC in pricing system of oils when oil is considered to be an inelastic good. Following this discussions are to be made on price floors and ceilings of binding nature, then cost measurements are to be done following a table. The following questions are related to inflationary situations and the impacts of monetary policies associated, changes in interest rates during inflationary and recession periods as assessed by RBA and finally a case study considering effectiveness of fiscal policy.

Question 1

Oil is considered as an inelastic product. An inelastic product is one whose quantity remains same even when its price changes. Yet OPEC fails to keep the price of oil high because in the short run, supply is inelastic as the quantity of oil reserves and the capacity to extract oil cannot be changed easily. Demand is also inelastic as the buying habits do not respond directly to the price change (Sims, 2018). Henceforth, in the short run both supply and demand curve is steep and when the supply shifts from S1 to S2 price change is large from P1 to P2.

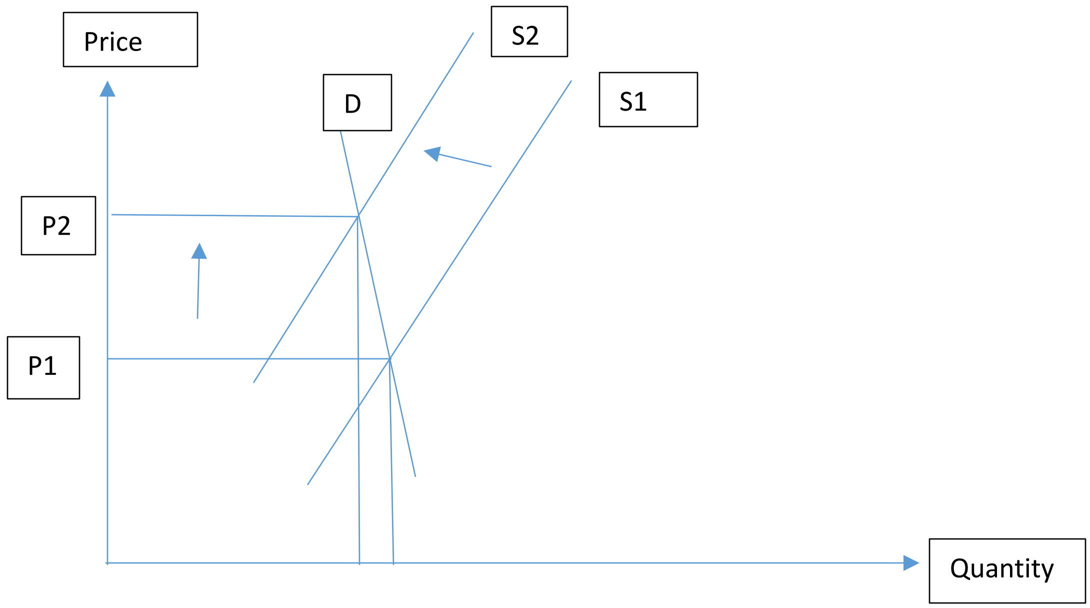

Figure 1: change in price in short run

(Source: As created by the author)

In the long run however, the situation is different. Over time, the oil producers respond to the changes in price by increasing exploration of oil and obtaining new extraction capacity. Consumer also start responding to the price. In long run both the supply and demand curve are elastic (Obstfeld and Rogoff, 2018). Thus shift in the supply curve from S1 to S2 causes a smaller increase in price.

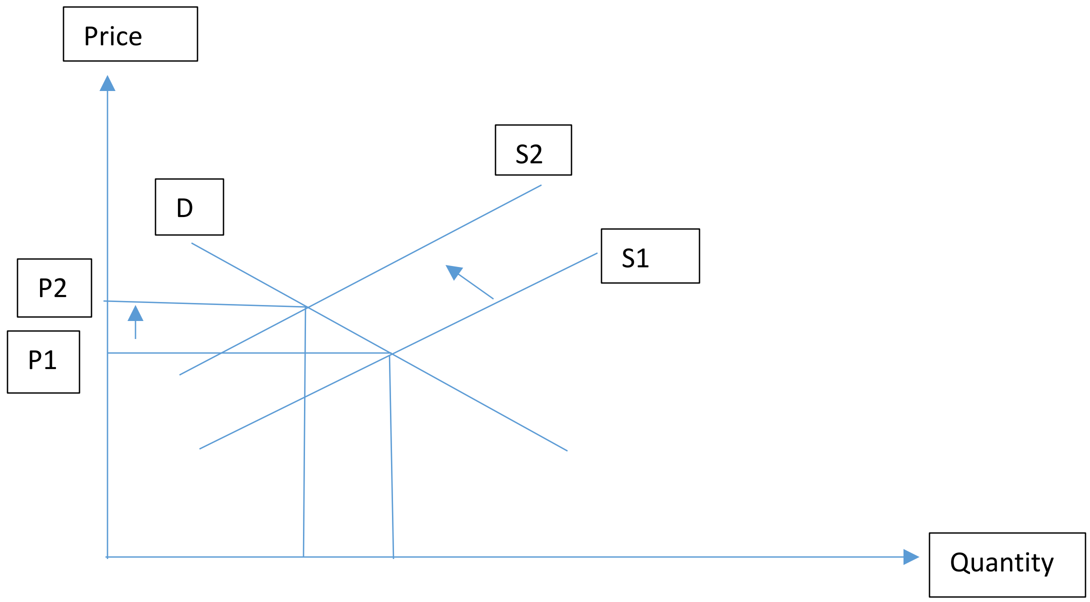

Figure 2: change in price in long run

(Source: As created by the author)

Question 2

Price ceilings can be considered as tools utilized by the government for regulatory purposes. A price ceiling is the price of a product or service that can never go up than the ceiling being imposed. For instance, considering a floating balloon inside a house, it can never go beyond the ceiling. The price ceiling is a similar concept concerning price ceiling and prices that are not allowed to go beyond the regulatory ceiling. This concept may get a bit tricky while considering price ceiling of binding nature that occurs to be lower than the price equilibrium. It may confuse individuals that how can a ceiling be lower than something, but this makes true sense on analysing (Mankiw, 2014). Again, considering the same example of a balloon, it may want to float up to 50meters, but for complete effectiveness the ceiling can be lower than 50meters. Now if in this context the ceiling is found to be at 100 meters, it is easier for the balloon (economically, prices) may rise up to 50meters without any issues.

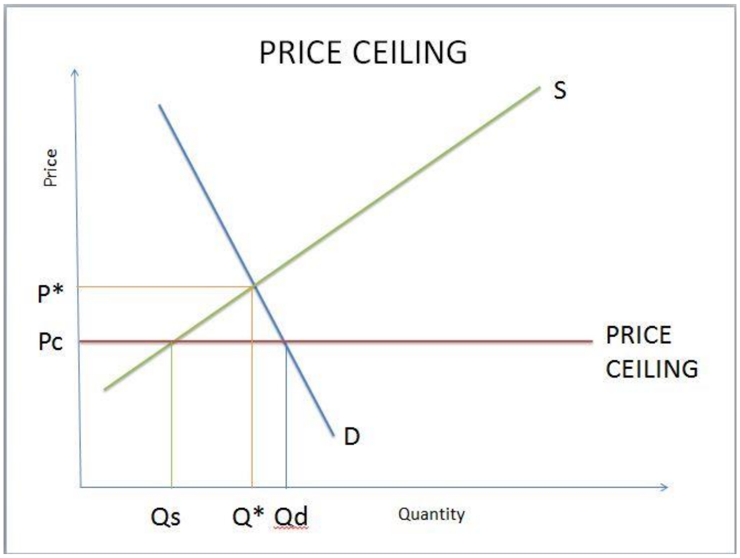

Figure 3: Price ceiling

(Source: As created by the author)

On the other hand, the price floors are meant by the prices of a product or service that can never go down than the floor imposed on prices. The most recognisable and commonly used example of price floors can be the law of a minimum wage which is the minimum payments made to labour. Price floors are also considered to be tools utilized by the government for regulatory purposes. It is the lowest price at which a commodity may be sold legally. These are implemented by the government for prevention of prices being too low (Baumol, 2018). The price floors also gets implemented in the agricultural sector for protecting the farmers from getting exploited due to presence of asymmetry in the market. For the binding nature of the price floors i.e. for these being effective, floors must be imposed higher than the equilibrium level of prices or else the entire process may become irrelevant.

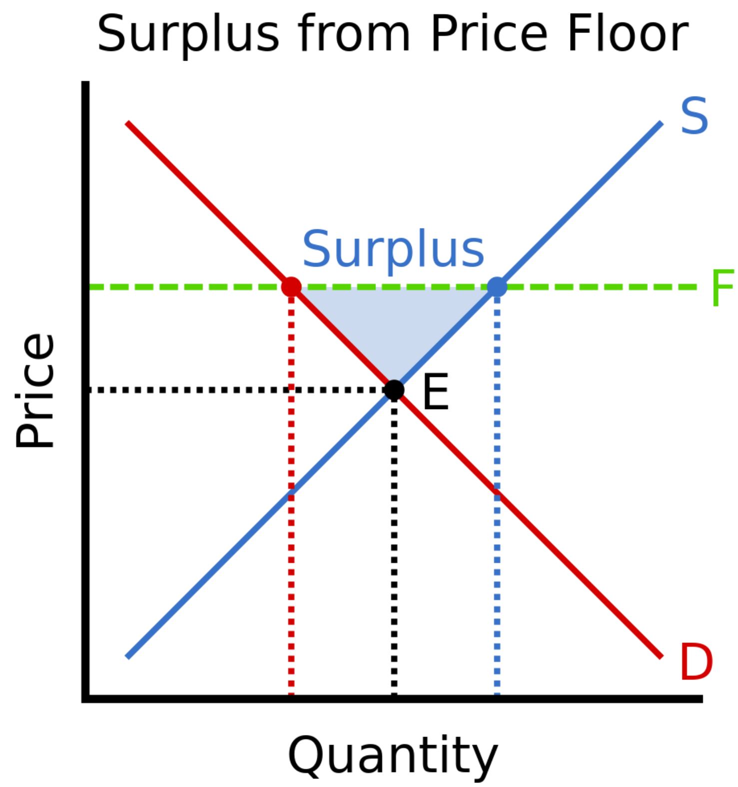

Figure 4: Price flooring

(Source: As created by the author)

Question 3

Quantity of soap sold per hour	**Total cost ($)**	**Fixed cost ($)**	**Variable cost ($)**	**Average fixed cost ($)**	**Average variable cost ($)**	**Average total cost ($)**	**Marginal cost ($)**
0	8.0	8.0	0.0	1	0	0	
1	8.30		0.30		0.3	8.3	0.3
2	8.50		0.50		0.25	4.25	0.2
3	9.80		1.80		0.6	3.26667	1.3
4	10.10		2.10		0.525	2.525	0.3
5	10.20		2.20		0.44	2.04	0.1
6	10.60		2.60		0.4333	1.76667	0.4

7	11.0		3.0		0.42857	1.57143	0.6
8	11.30		3.30		0.4125	1.4125	0.3
9	11.60		3.60		0.4	1.28889	0.3
10	12.0		4.0		0.4	1.2	0.4

The above table shows the measures of cost that include the calculation of average fixed cost, average variable cost, also average total cost and marginal cost.

Question 4

Economically, inflation can be referred to as an increase in levels of price caused by an increase in the monetary quantity in general; the money stock grows at a faster rate than the productivity level in an economy. Exactly this nature as exhibited by increases in prices is much of a debatable context with respect to economics, although the term inflation mostly can be referred to as a monetary circumstance (Dornbusch, 2018).

Impacts of monetary policy on inflation:

Central banks and modern governments rarely prints and distributes material money for influencing supply of money, rather they rely on various other measures of control which includes interest rates imposed on lending among the banks (Dornbusch and Edwards, 2018). Among all other reasons accounted, the two most important and significant are as follows:

1. Historical assessments suggest that printing of a handful of money can lead to disasters resulting in mass recession and hyperinflation.

2. Account electronic balances, new instruments of finance and additional changes observed in the money holding traits of individuals makes the predictability regarding monetary controls questionable.

a) How supply and demand for money determine the equilibrium price level.

Economically, equilibrium is considered to be a state at which the forces including demand and supply balances and it stays the same without being influenced by any external factors. Market equilibrium is referred to as a situation in which market prices are established by competition between the quantity of buyer's demand for a product or service and the quantity of seller's supply of a product or service, which is ought to be equal (Sargent, 2018). But considering the situation of supply of money, equilibrium in market only exists if the money supply and the rate of interest balances, that must not be influenced by any external factors.

b) Consequences of increase in money supply

Monetary policy of expansionary kind can be referred to as an initiative taken in terms of policy implementation through the nation's central bank for expansion or raising the country's supply of money. In most of the economies that are growing, expansions in money supply is implemented for keeping up with the expansionary nature exhibited by the GDP (gross domestic product) of the country (Galor and Zeira, 2018). A consequent decrease is observed in the average rates of interest of an economy is caused by expansionary monetary policy.

Question 5

If the rate of inflation of Australia accounts to be lower than as targeted then a cut un the rates of cash results in reduction of long term rates of interest that may encourage individuals for buying products and services which leads to a fall in rates of deposits in long term and bonds offered by the government reduces the saving incentives and investment rises as mortgages and commercial loans are available at cheaper interest rates. But prices rise up with a rise in demand that brings back the targeted inflation rate (Obstfeld et al., 2018). And for meeting the prices of the market for earing effective revenues organizations end up cutting costs by terminating or cutting down the number of employees. Thus, this is the rationale as suggested and assessed by the RBA (Reserve Bank of Australia) regarding its decisions related to policies.

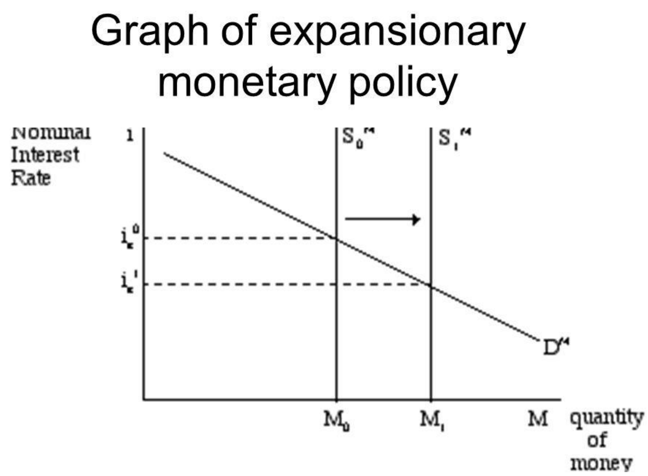

Figure 5: Expansionary monetary policy

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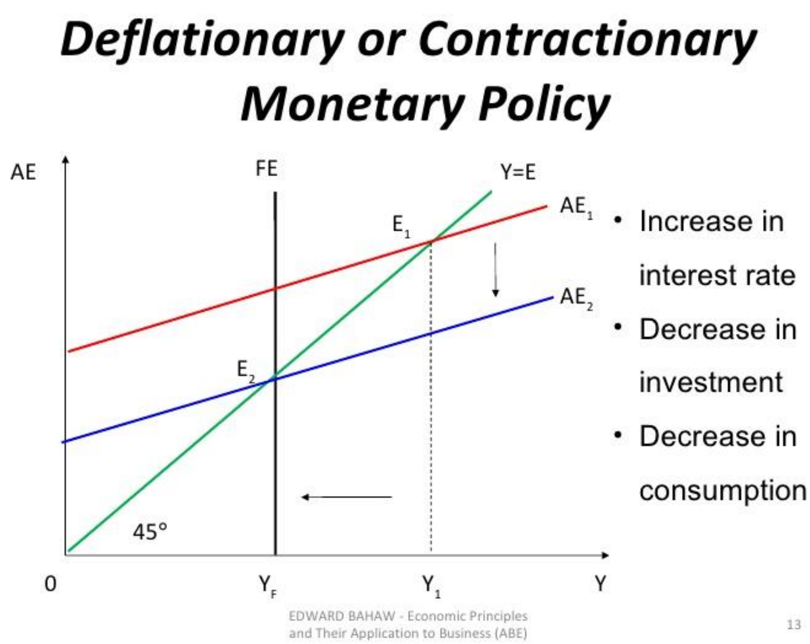

Figure 6: Contractionary monetary policy

(Source: As created by the author)

Question 6

The aggregate demand oriented expansionary fiscal policy by the government affects the aggregate demand through the changes in taxation and government spending. The household income and employment is influenced by these changes that affects the consumer spending and investment. The aggregate demand measures the demand for the GDP of the economy (Blanchard et al., 2018).

AD = C+ I + G+ NX

Where C is consumer spending, I is investment, G is government expenditure and NX is total export – total imports

The demand sided fiscal policy focuses on increasing the aggregate demand (AD) which is done in times of recession.

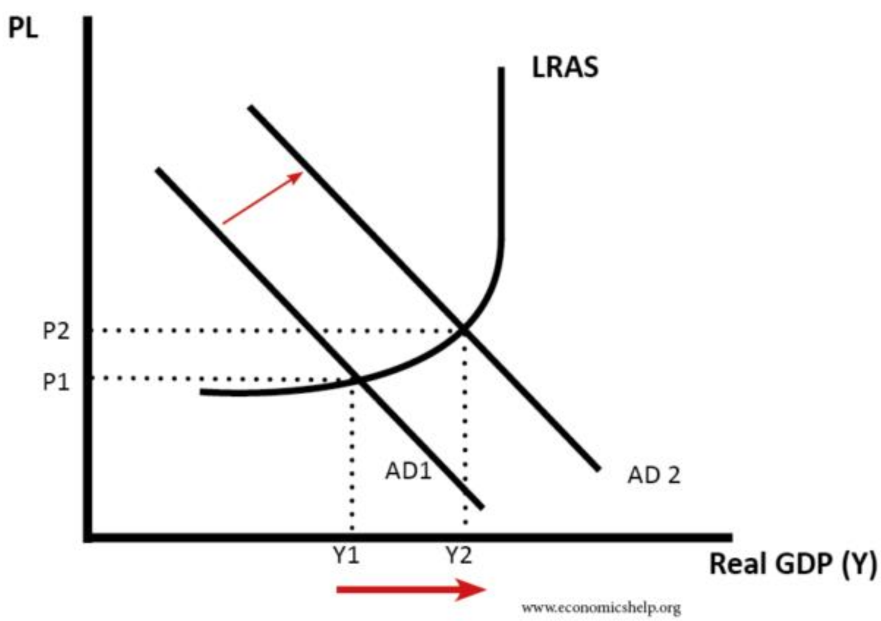

Figure 7: The demand sided fiscal policy

(Source: As created by the author)

In the above case, the economy at Y1 has scarce capacity but with the implementation of demand sided fiscal policy there is an increase in AD that leads to the rise in the GDP.

The supply sided fiscal policy aims in improving economic growth that is done through increasing the productivity and efficiency of the economy.

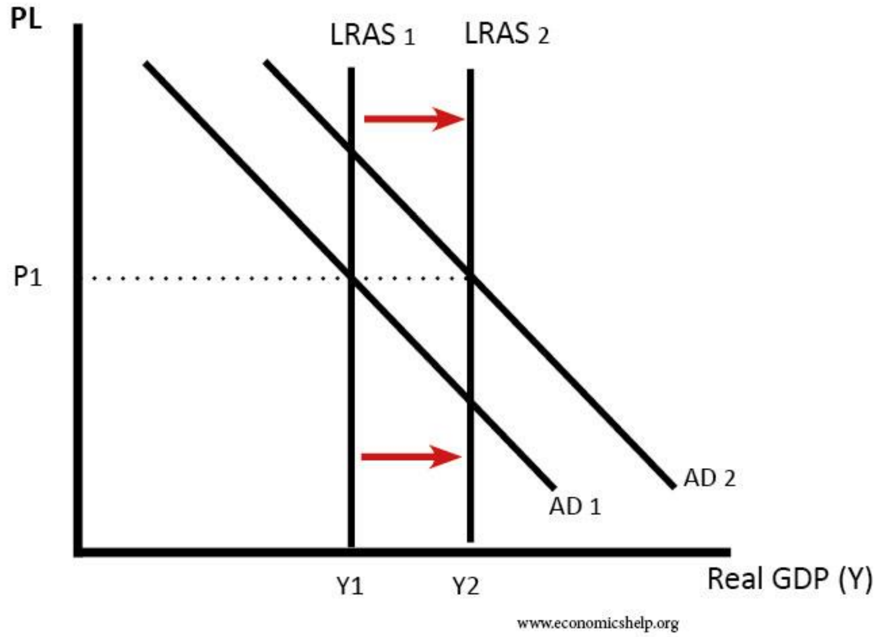

Figure 8: The supply sided fiscal policy

(Source: As created by the author)

Conclusion

From the above questions, clear idea about the different concepts of macroeconomics can be gathered.

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