PART 1

Ten Principles of Economics

PRINCIPLES OF

Microeconomics

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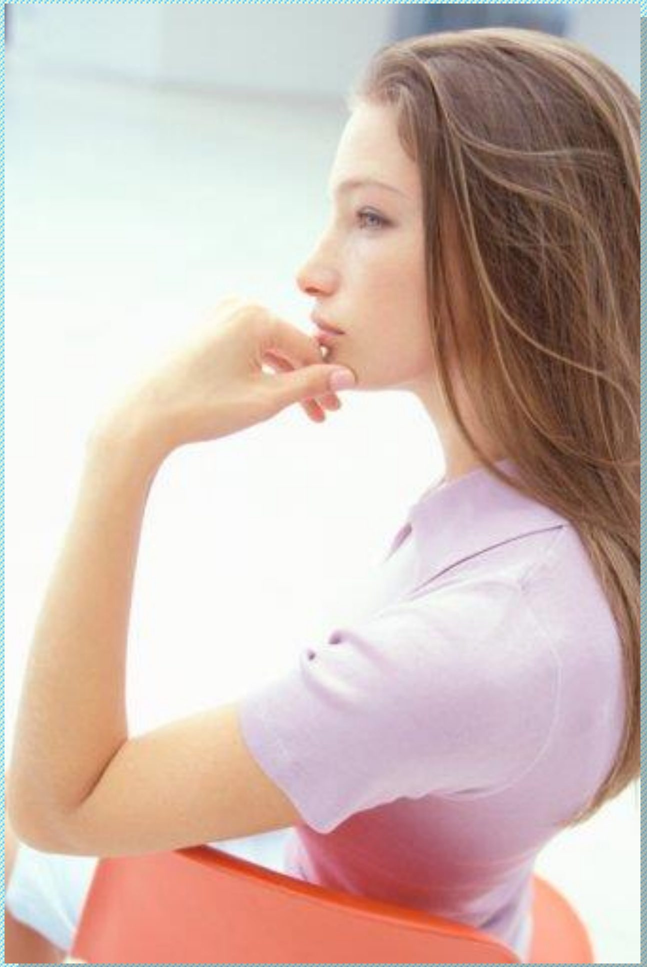
Chapter 2: How do people influence each other



Chapter 2: How do people influence each other

- The four principles we studied in Chapter 1 are about how people make decisions.
- The decisions you make in daily life not only affect yourself but also impact others.
- The three principles in Chapter 2 are about how people interact.

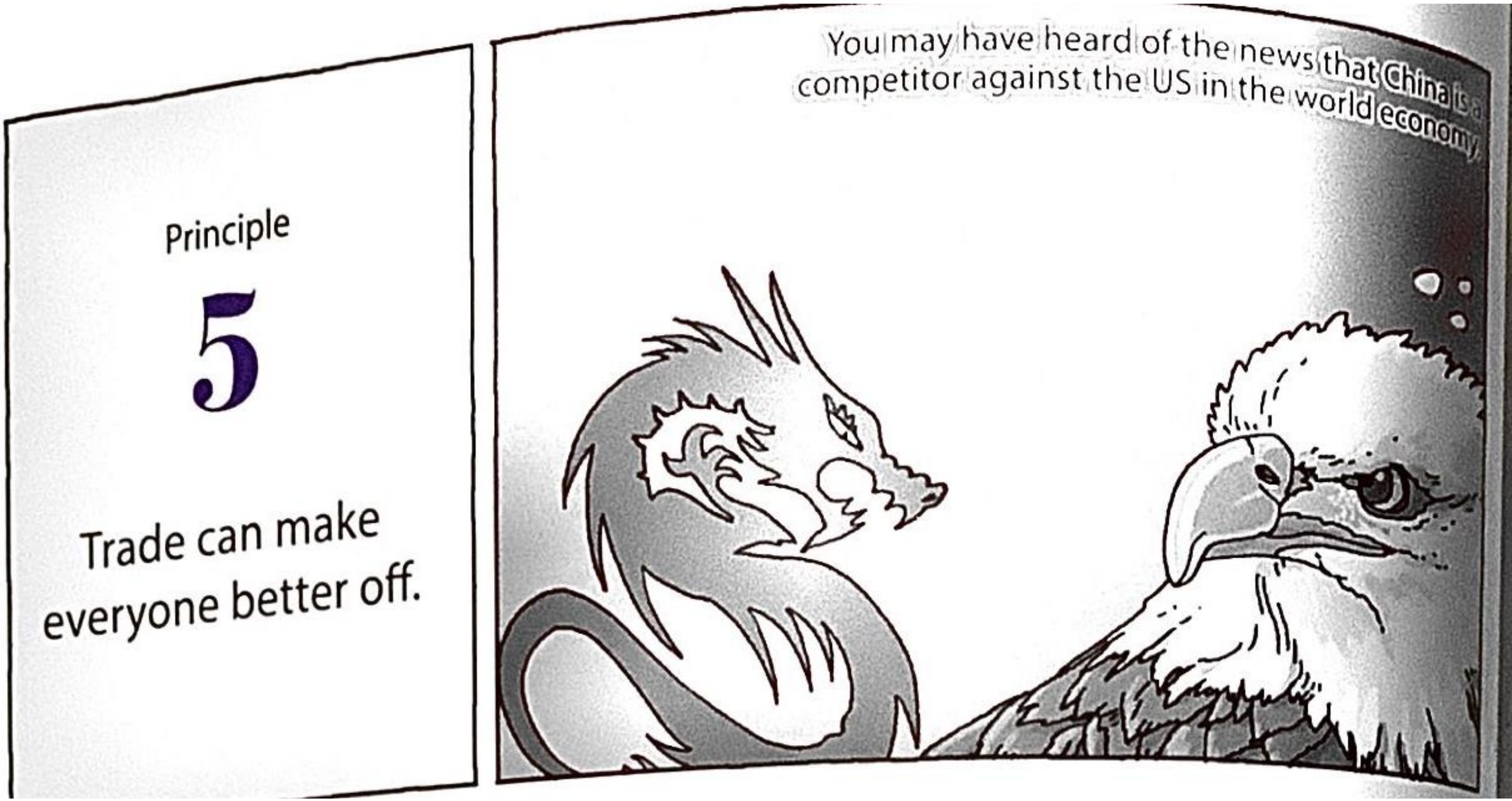
Chapter 2: How do people influence each other

- Principle 5: Trade can make everyone better off.

- Principle 6: Markets are usually a good way to organize economic activity.

- Principle 7: Governments can sometimes improve market outcomes.

Principle 5: Trade can make everyone better off



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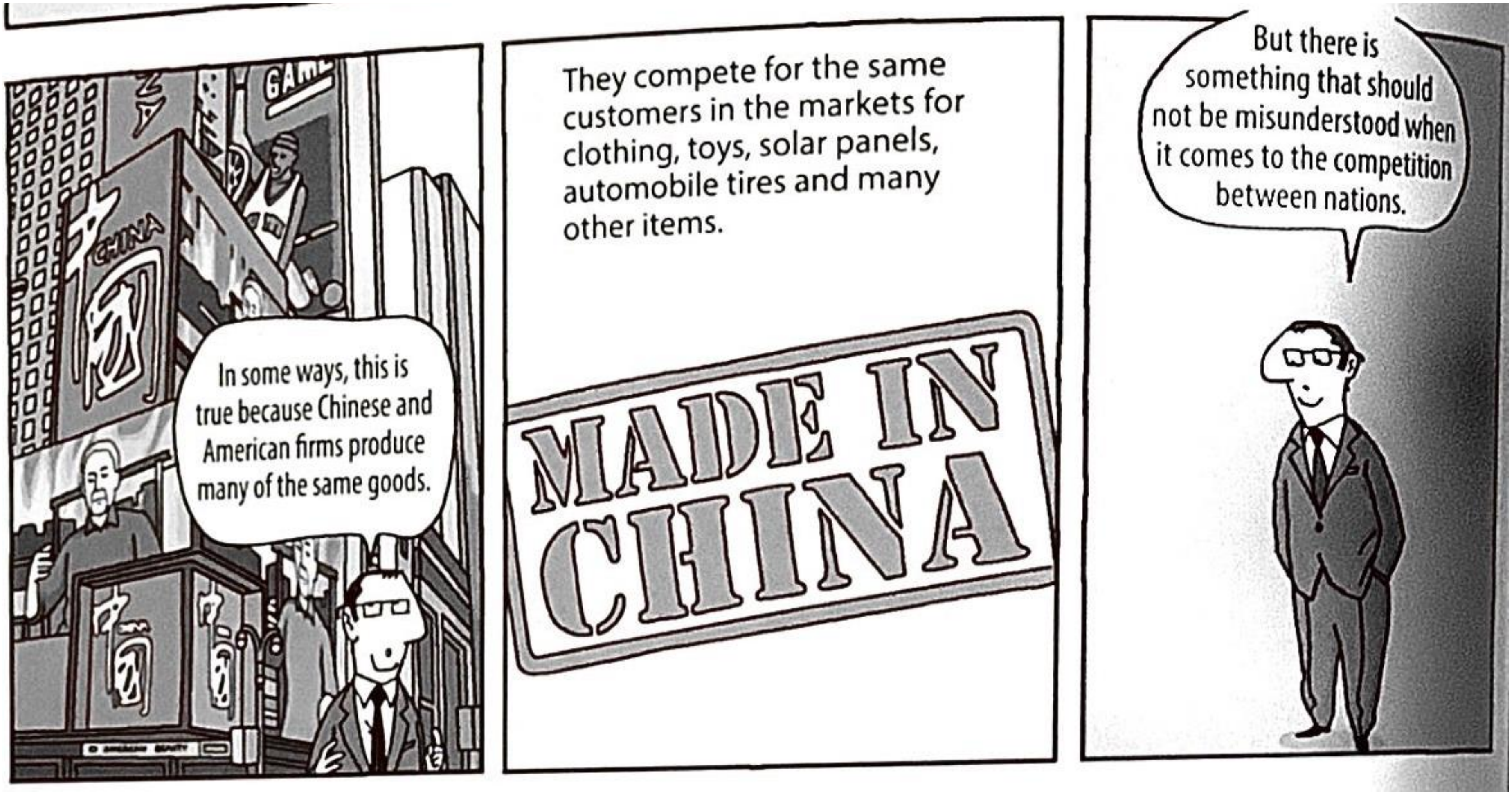

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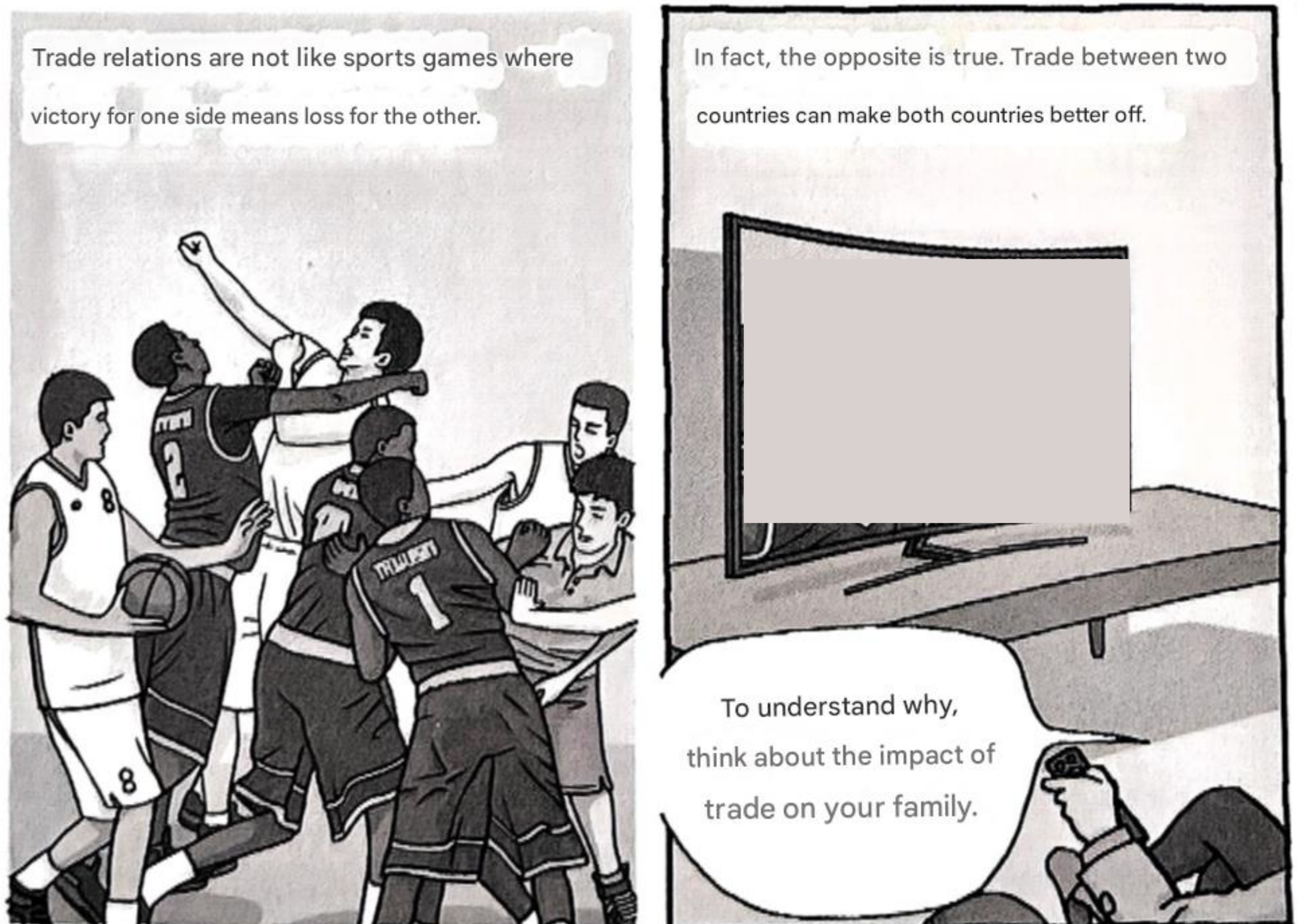

International relations involve not only competition but also cooperation.

Principle 5: Trade can make everyone better off

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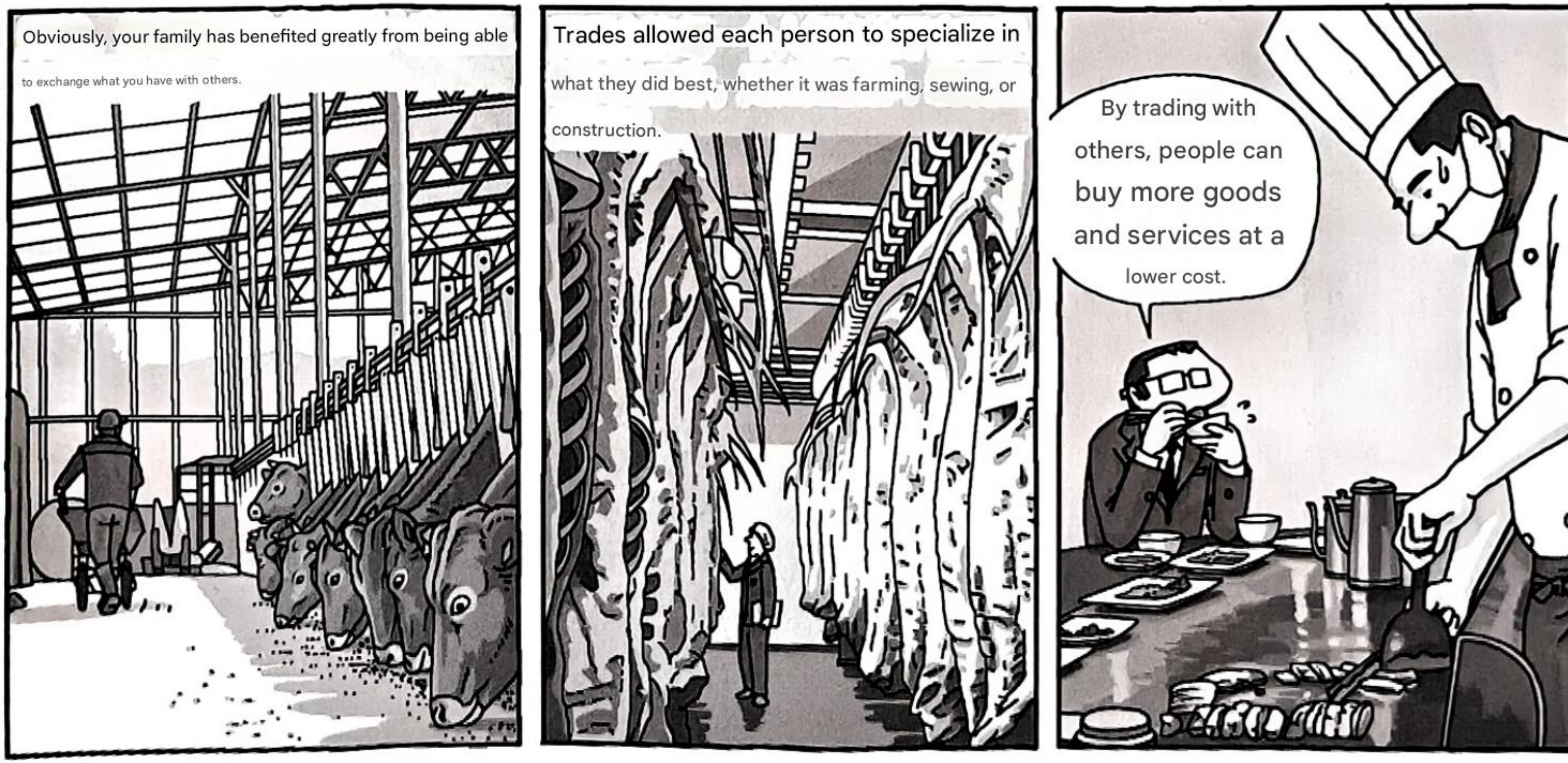

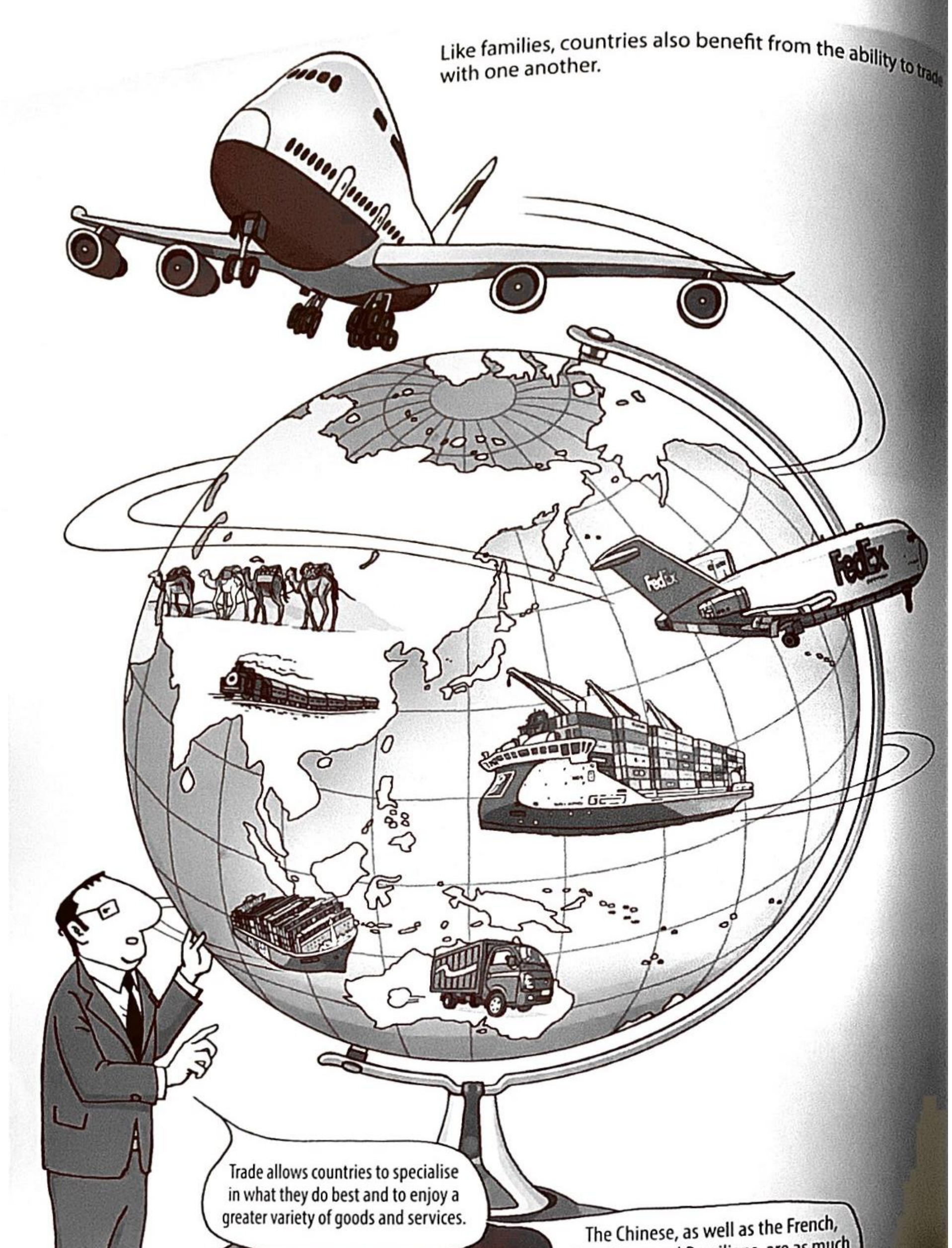
Like families, countries also benefit from the ability to trade with one another.
Trade allows countries to specialise in what they do best and to enjoy a greater variety of goods and services.
The Chinese, as well as the French, Egyptians, and Brazilians, are as much partners in the world economy as they are competitors.

Free trade ushered in the British Golden Age

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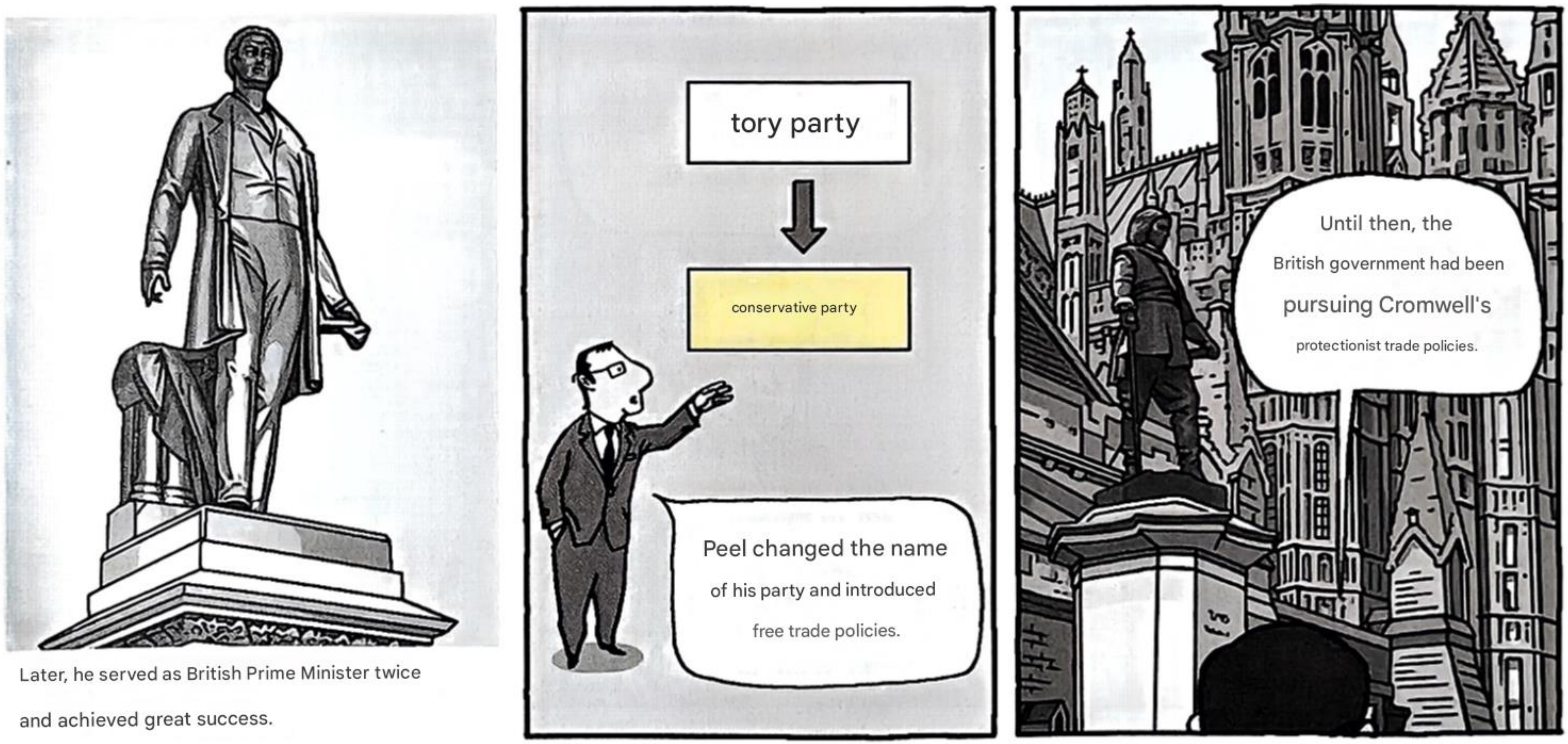
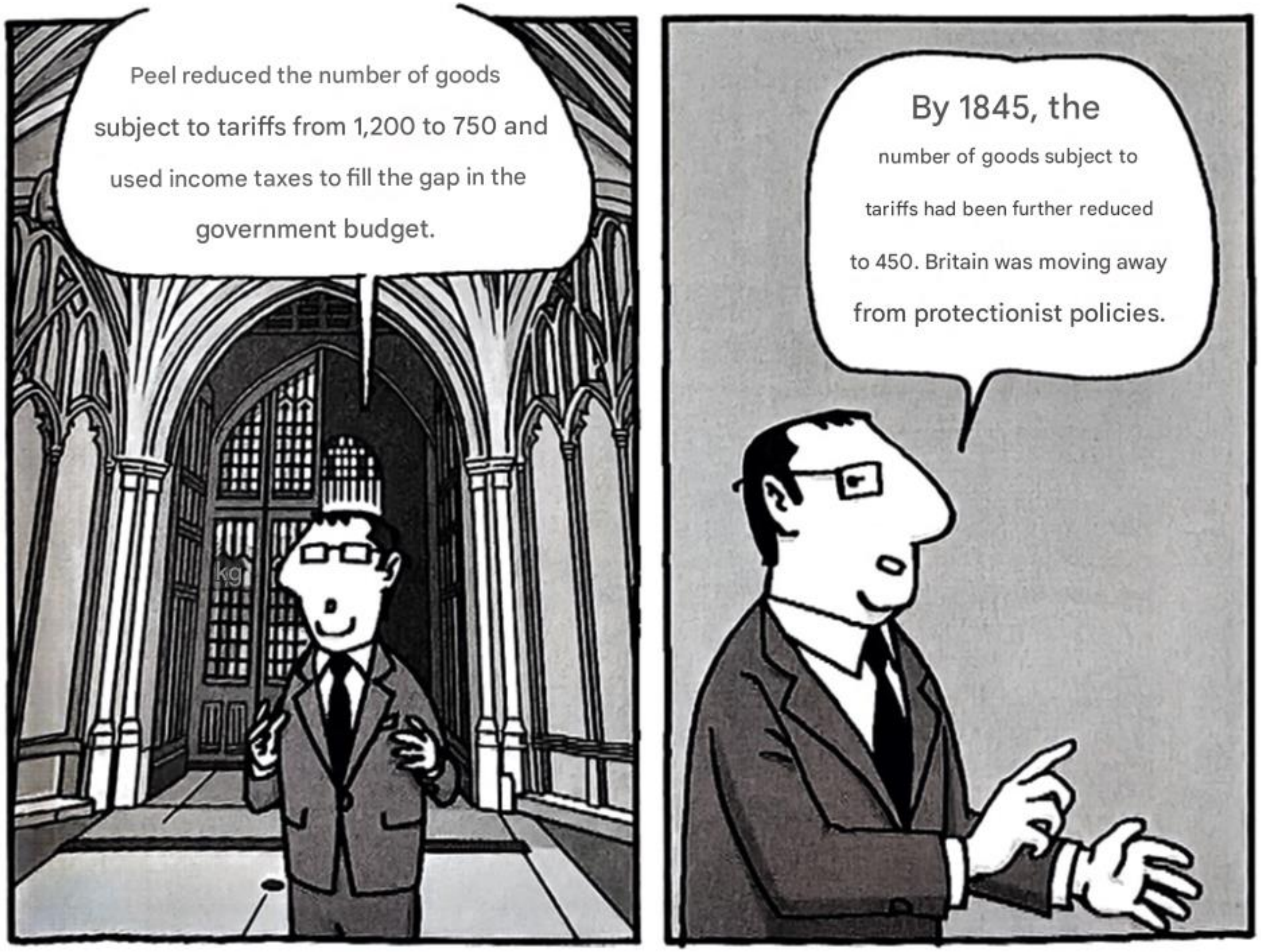


Free trade ushered in the British Golden Age



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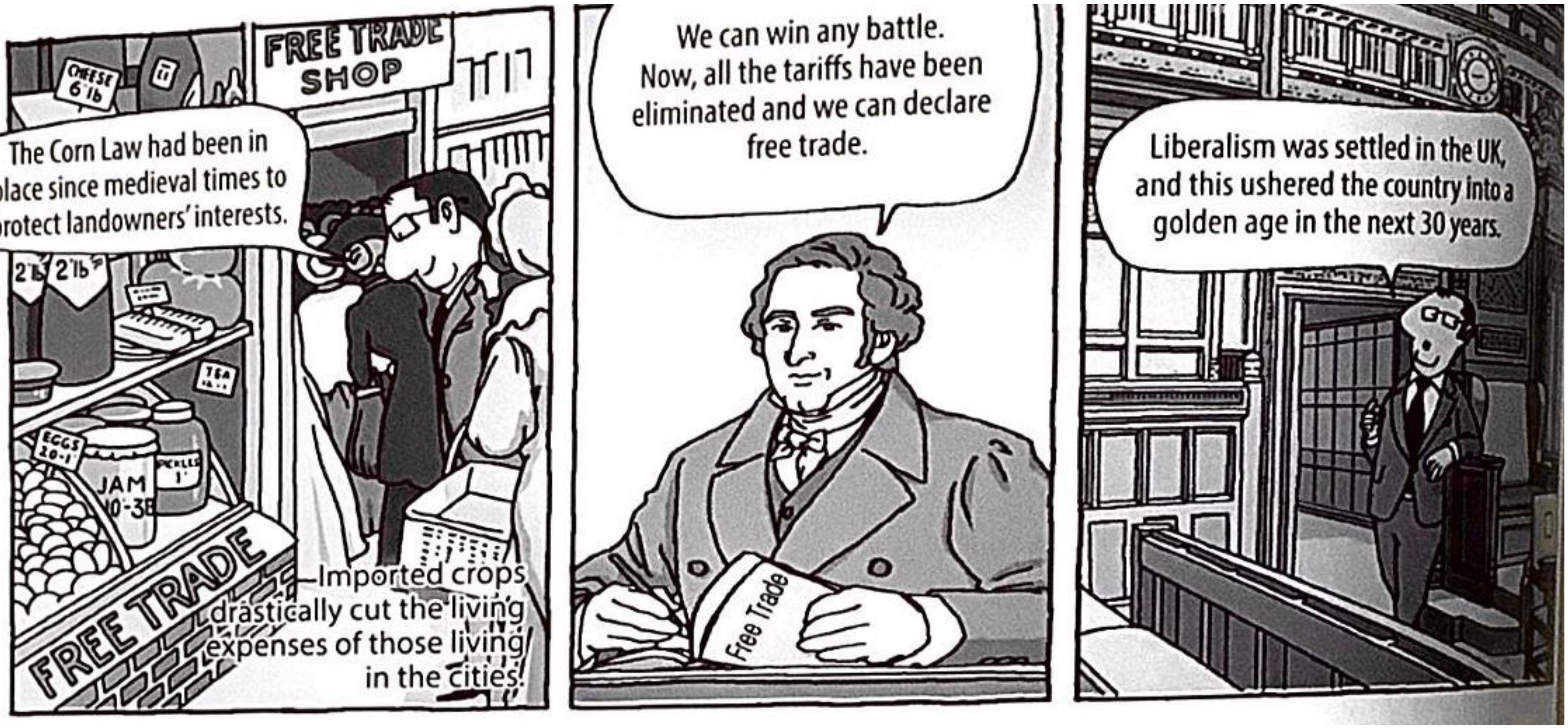
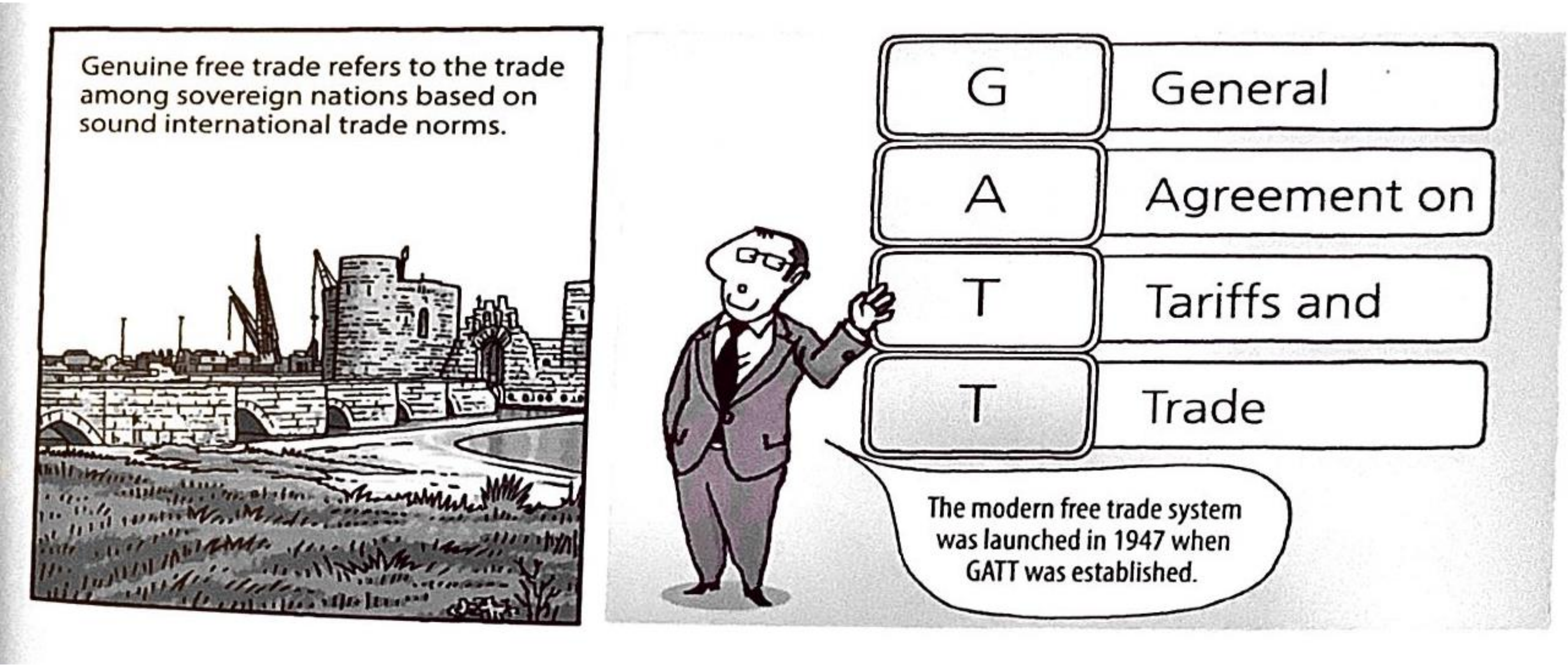
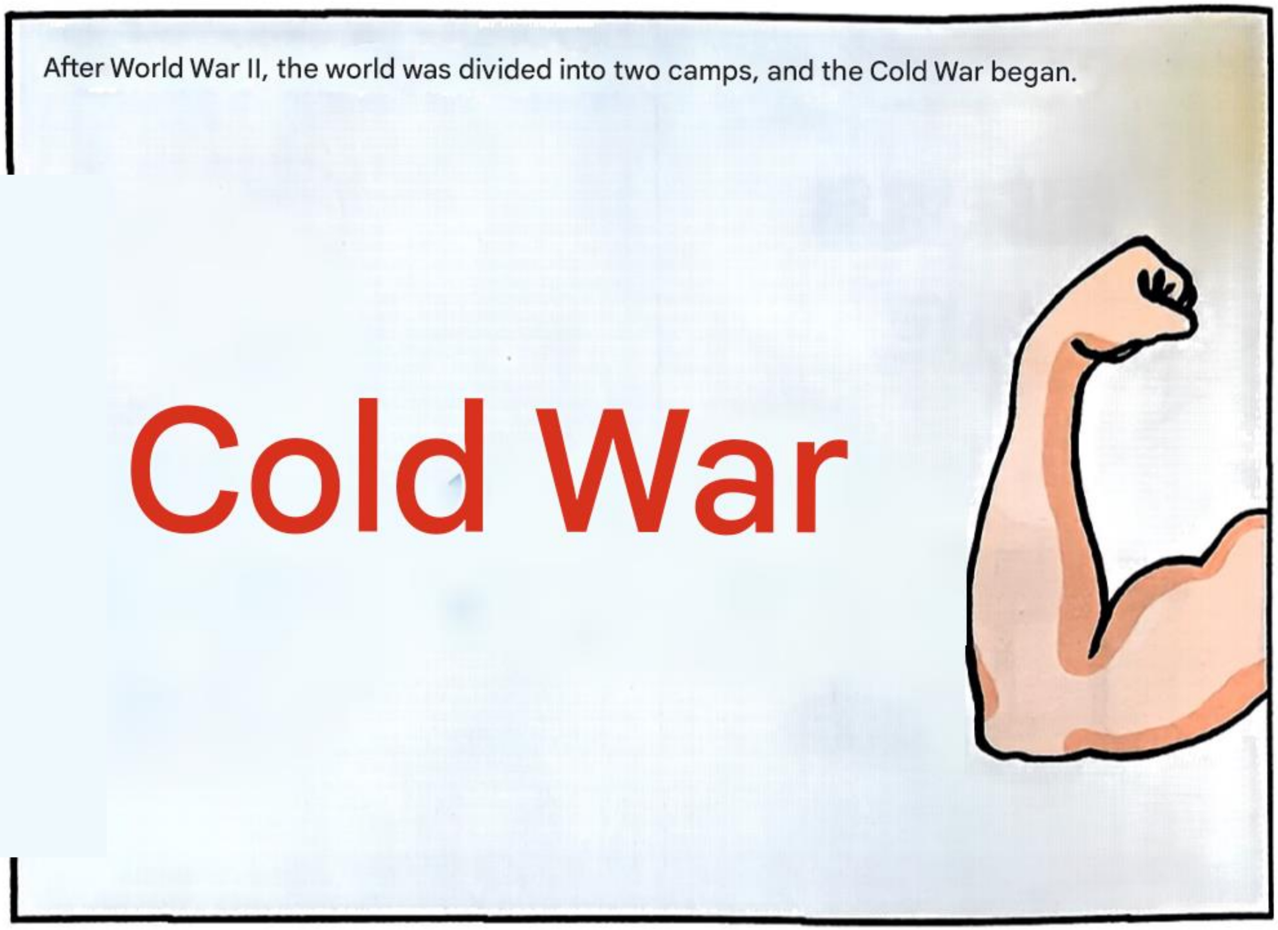


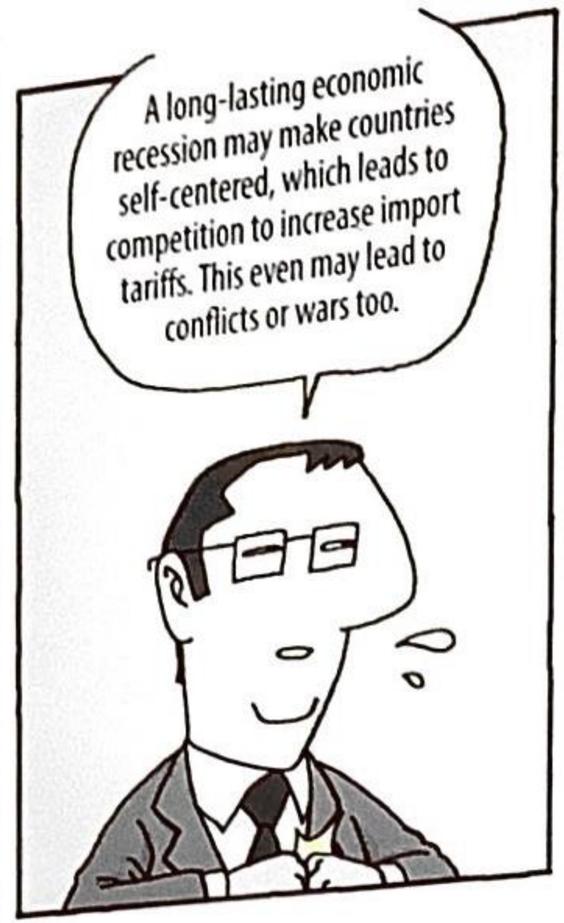
The Corn Laws **restricted grain imports.**

International Trade Agreements



International Trade Agreements





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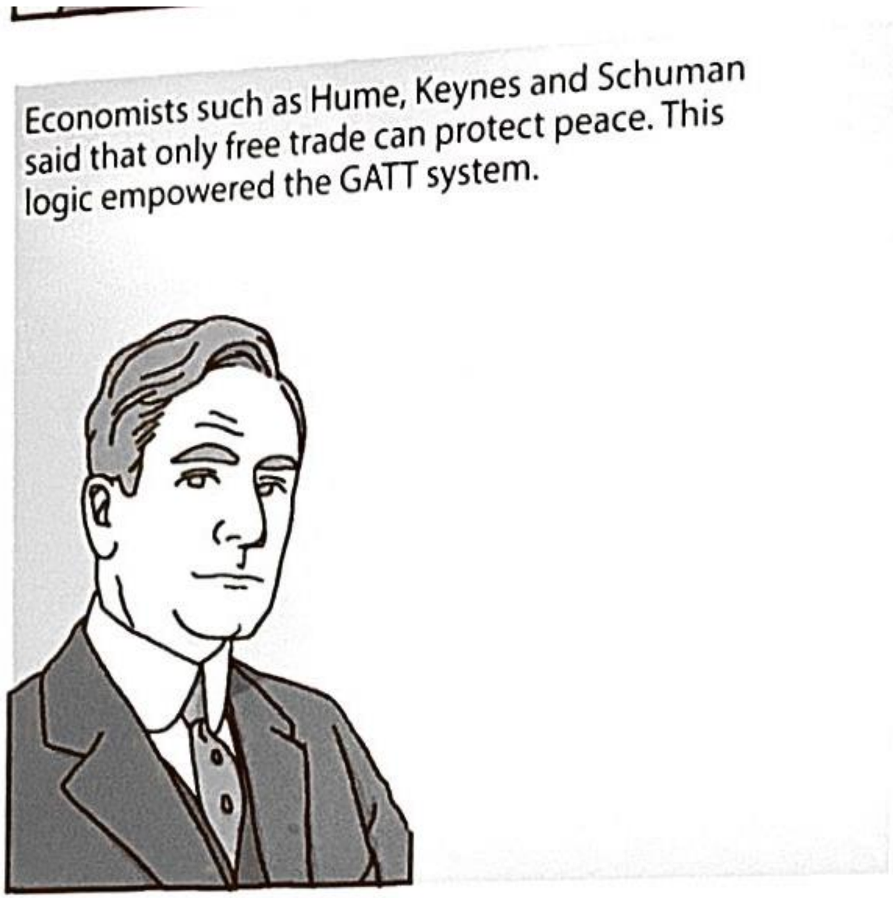
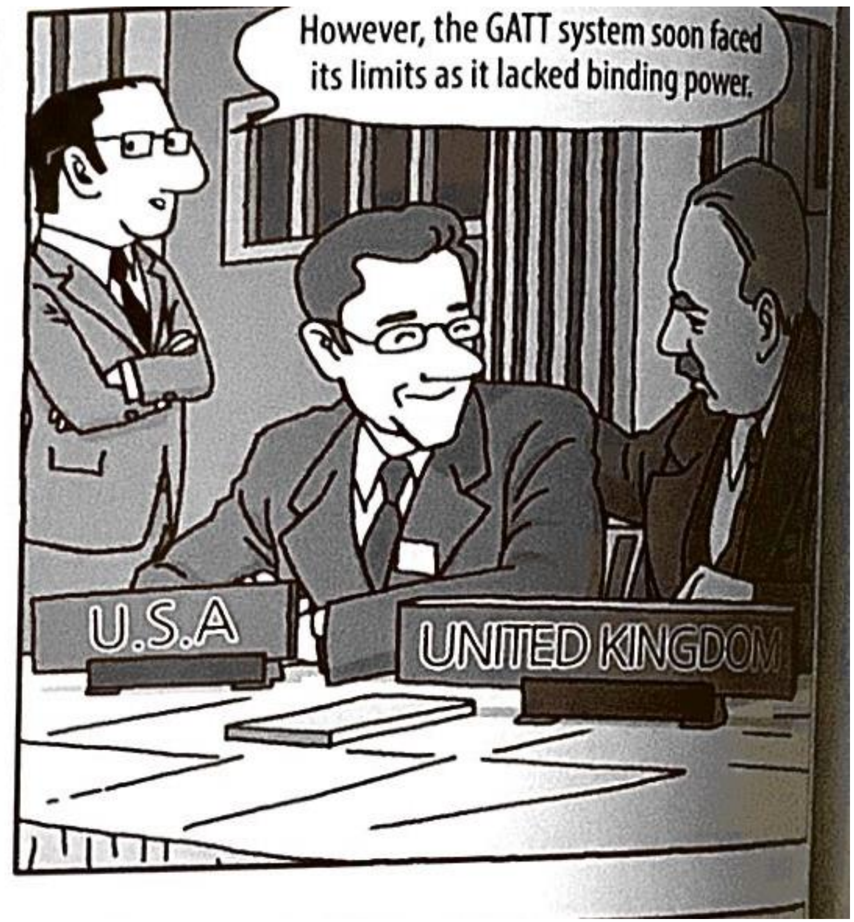




International Trade Agreements

Dumping refers to a company selling its products in an overseas market at a price that is below its fair value in the domestic market.

SUMMARY

- Trade relations are not like a sports competition where one side wins and the other is inevitably defeated.
- Trade between two countries can make each nation better off.
  - Trade enables individuals to focus on their most proficient work, gaining access to a wider variety of goods and services at lower costs.
  - Similarly, countries also benefit from trade. It allows nations to specialize in areas where they possess a **comparative advantage** and enjoy a broader range of goods and services.

SUMMARY

- Here are explanations of some fundamental terms in international trade
  - Free trade refers to a trade policy that does not restrict imports and exports, allowing individuals and companies to conduct transactions autonomously.
  - Trade protection refers to a trade policy in which the government intervenes to restrict imports, representing the opposite of free trade. To protect domestic industries, governments impose or increase tariffs, implement import quotas, or restrict the import of specific goods and services.
  - The General Agreement on Tariffs and Trade (GATT) refers to an international free trade policy signed by 23 countries in Geneva in 1947, aimed at promoting international trade by reducing or eliminating trade barriers such as tariffs.

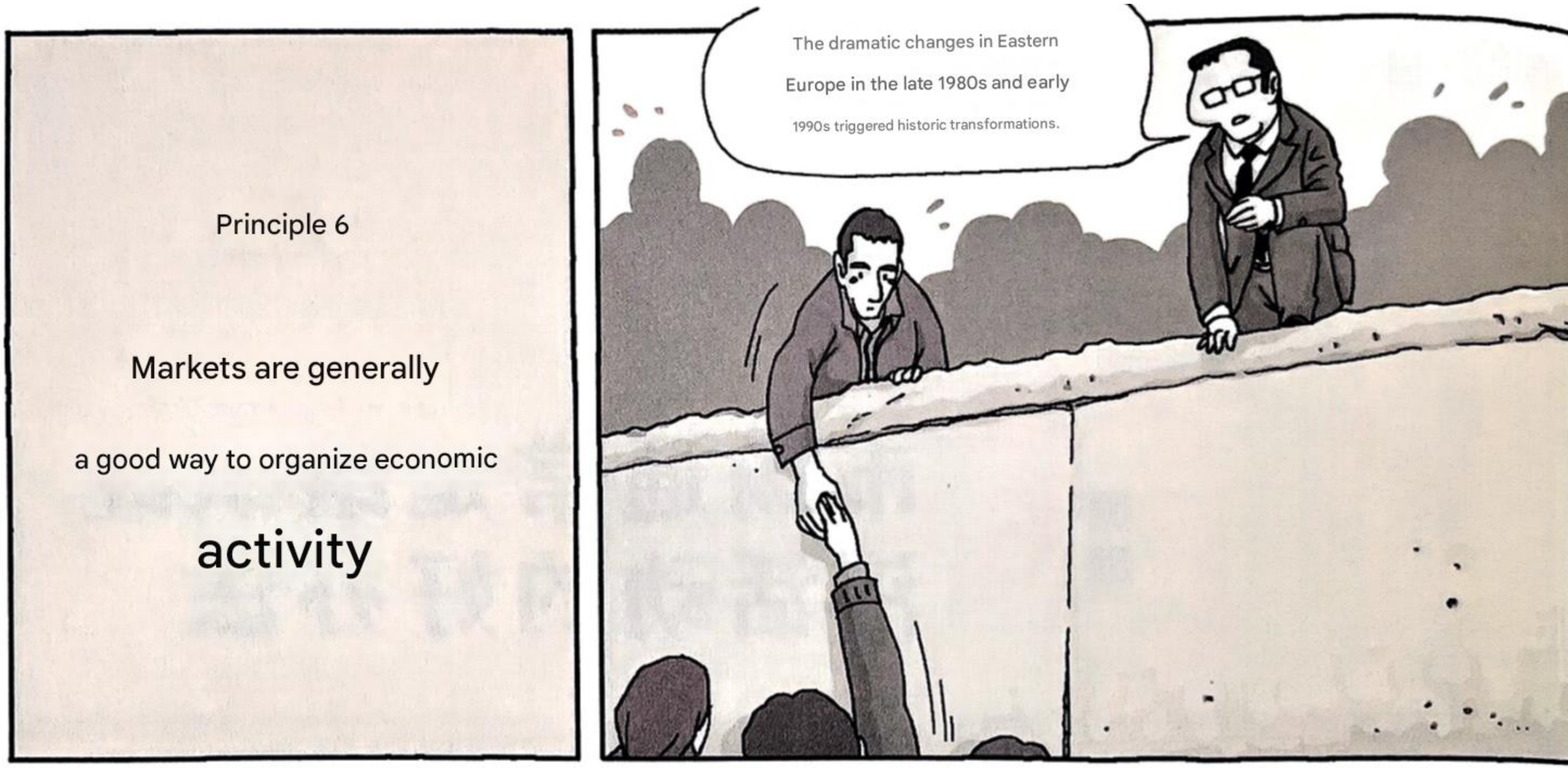
SUMMARY

- Here are explanations of some fundamental terms in international trade
  - The WTO is an intergovernmental organization created to promote global trade. It regulates international trade and oversees the implementation of the agreement on behalf of the GATT.
  - A Free Trade Agreement (FTA) is a preferential trade agreement under which the signatory countries provide each other with exclusive trade benefits through the abolishment of tariffs and other barriers so as to trade goods and services between the countries.

Chapter 2: How do people influence each other

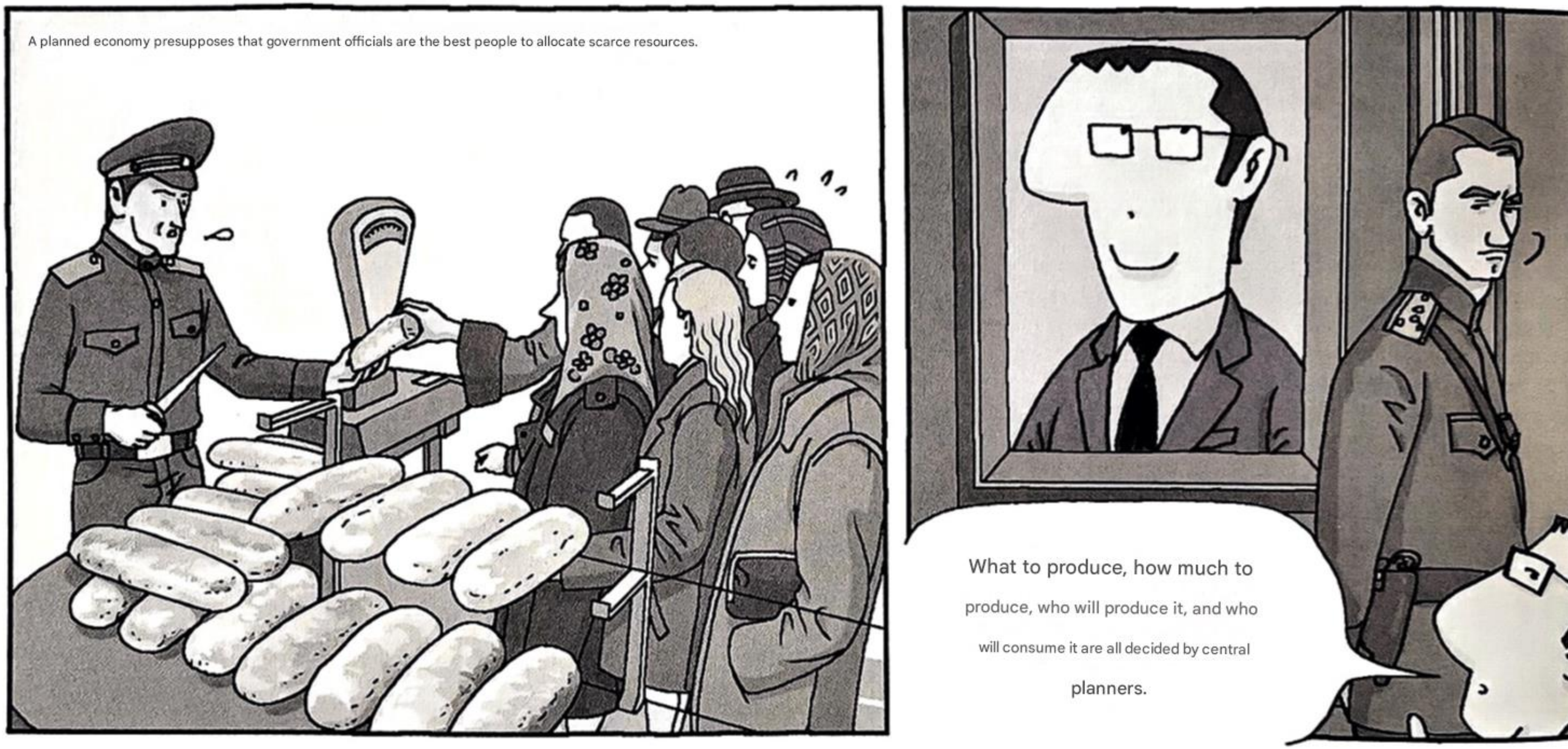
- Principle 5: Trade can make everyone better off.
- Principle 6: Markets are usually a good way to organize economic activity.
- Principle 7: Governments can sometimes improve market outcomes.

Principle 6: Markets are usually a good way to organize economic activity



Eastern European Turmoil refers to the major historical event in the late 1980s and early 1990s, during which a series of socialist countries in Eastern Europe underwent rapid successive political transitions. The socialist systems were overthrown and replaced by Western-style multi-party systems and market economies.

Principle 6: Markets are usually a good way to organize economic activity



Principle 6: Markets are usually a good way to organize economic activity

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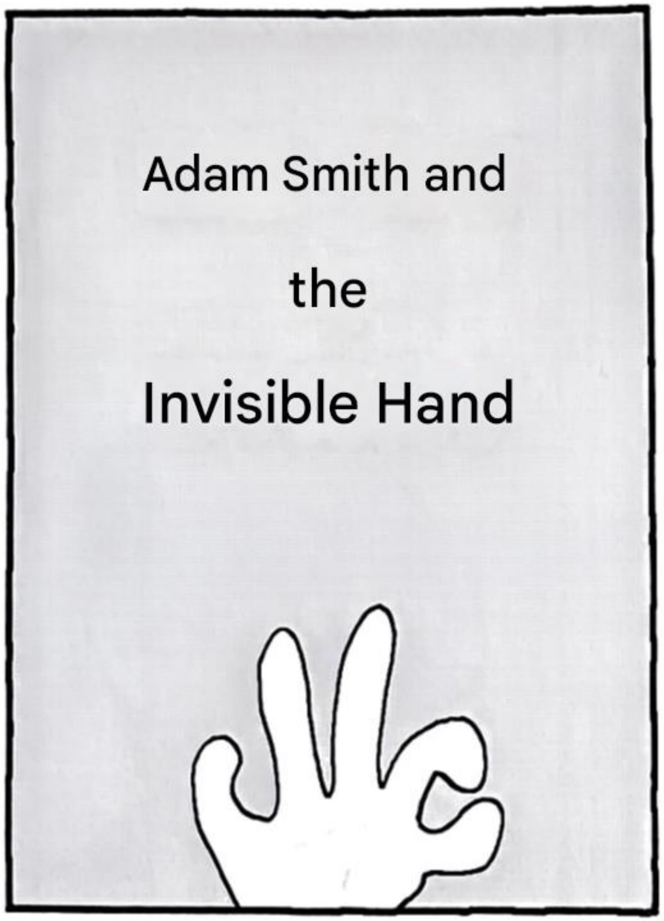
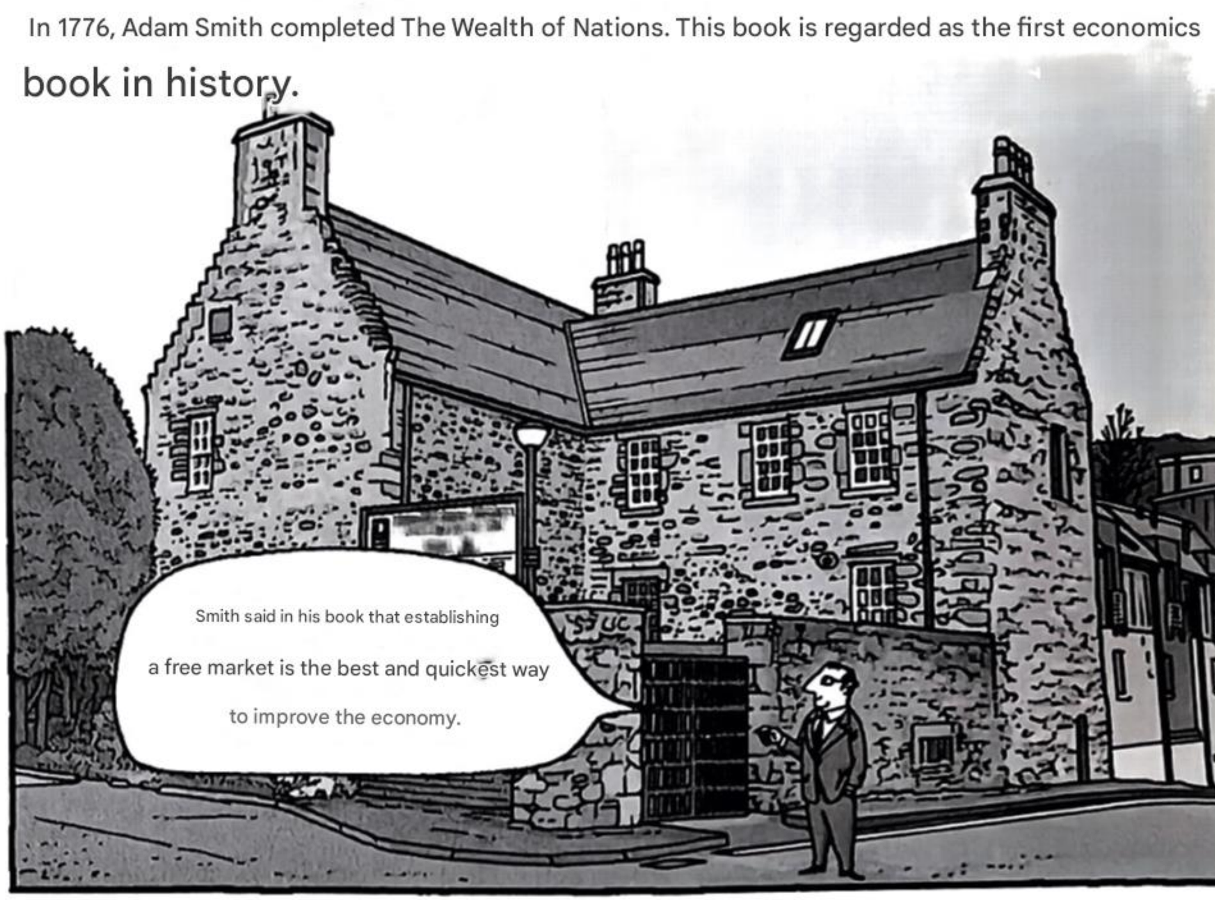
"The invisible hand" refers to prices.

Principle 6: Markets are usually a good way to organize economic activity

Adam Smith and the Invisible Hand





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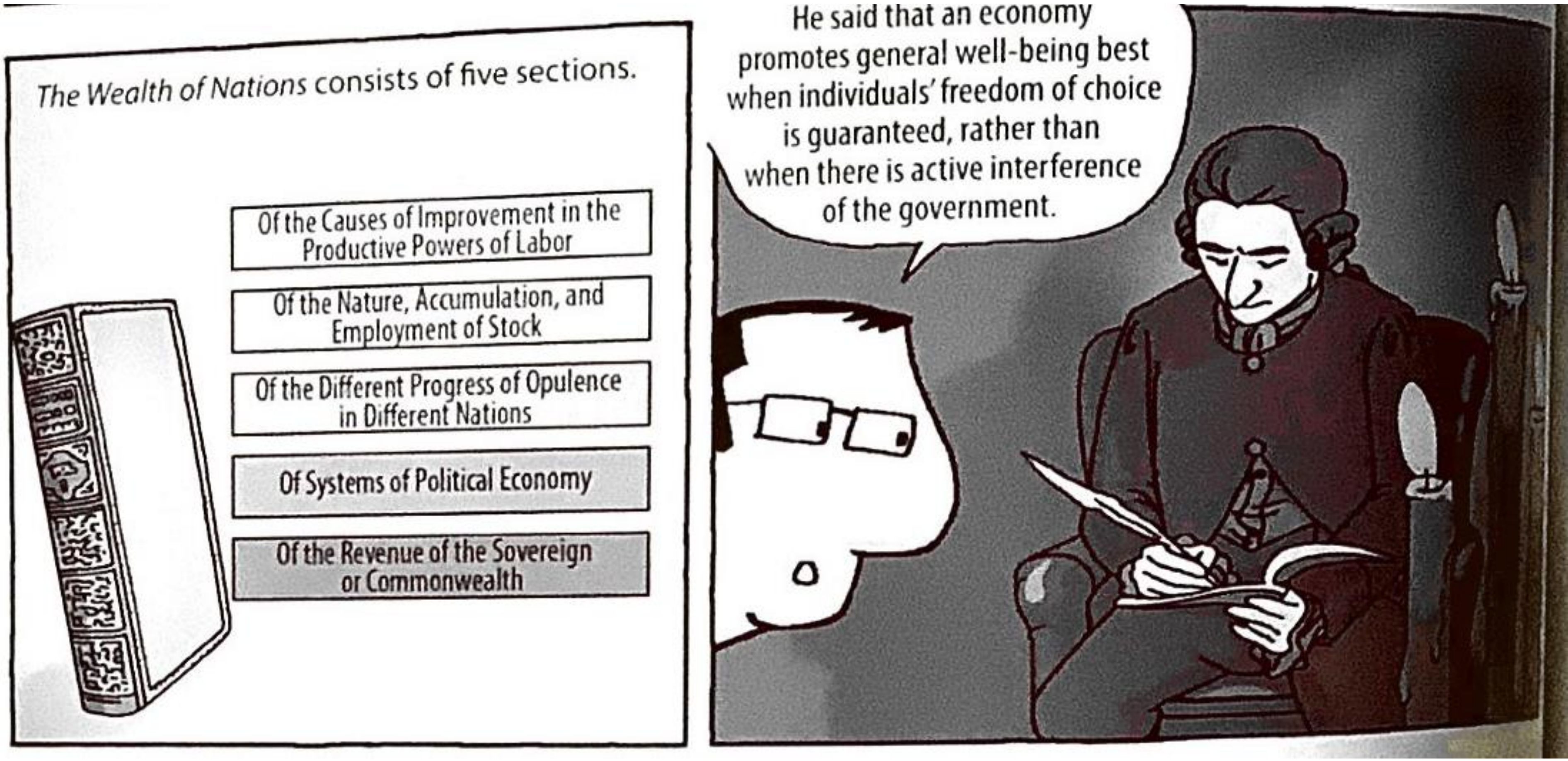

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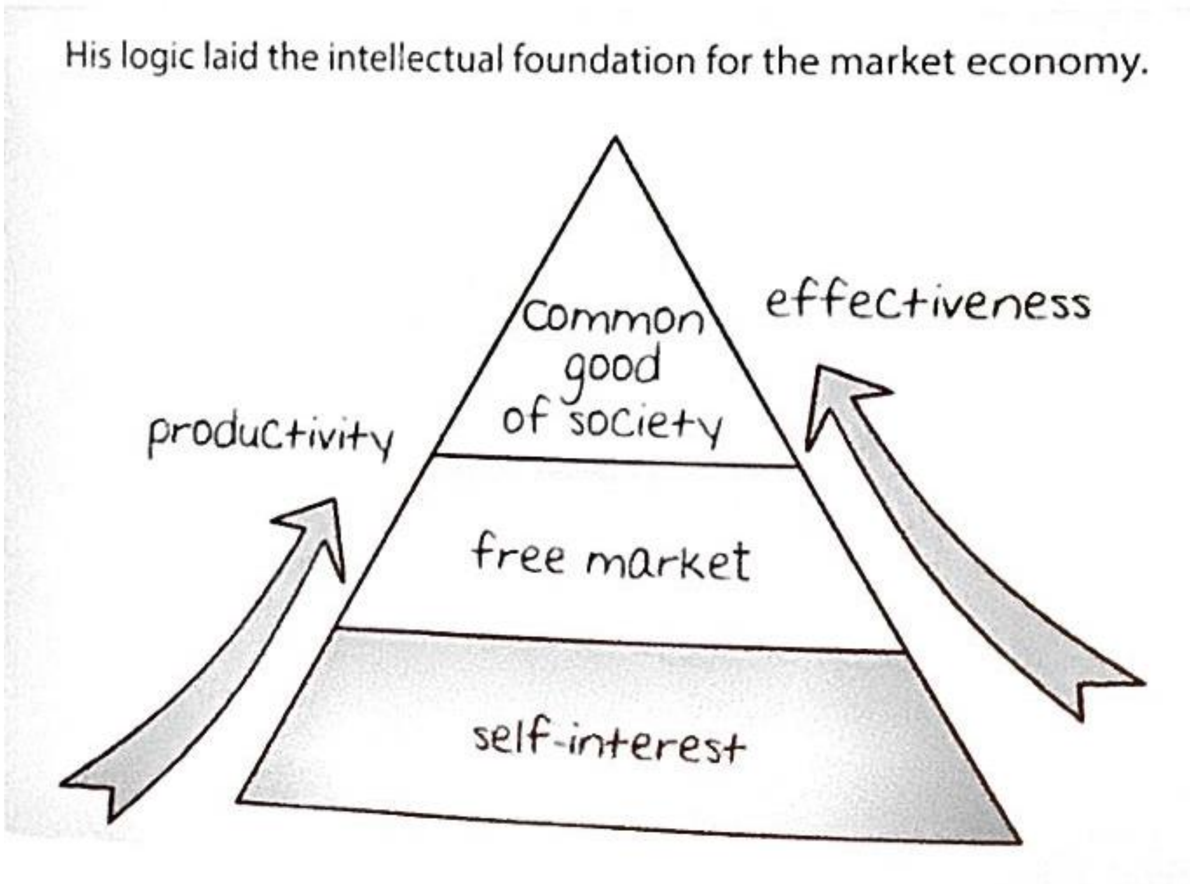

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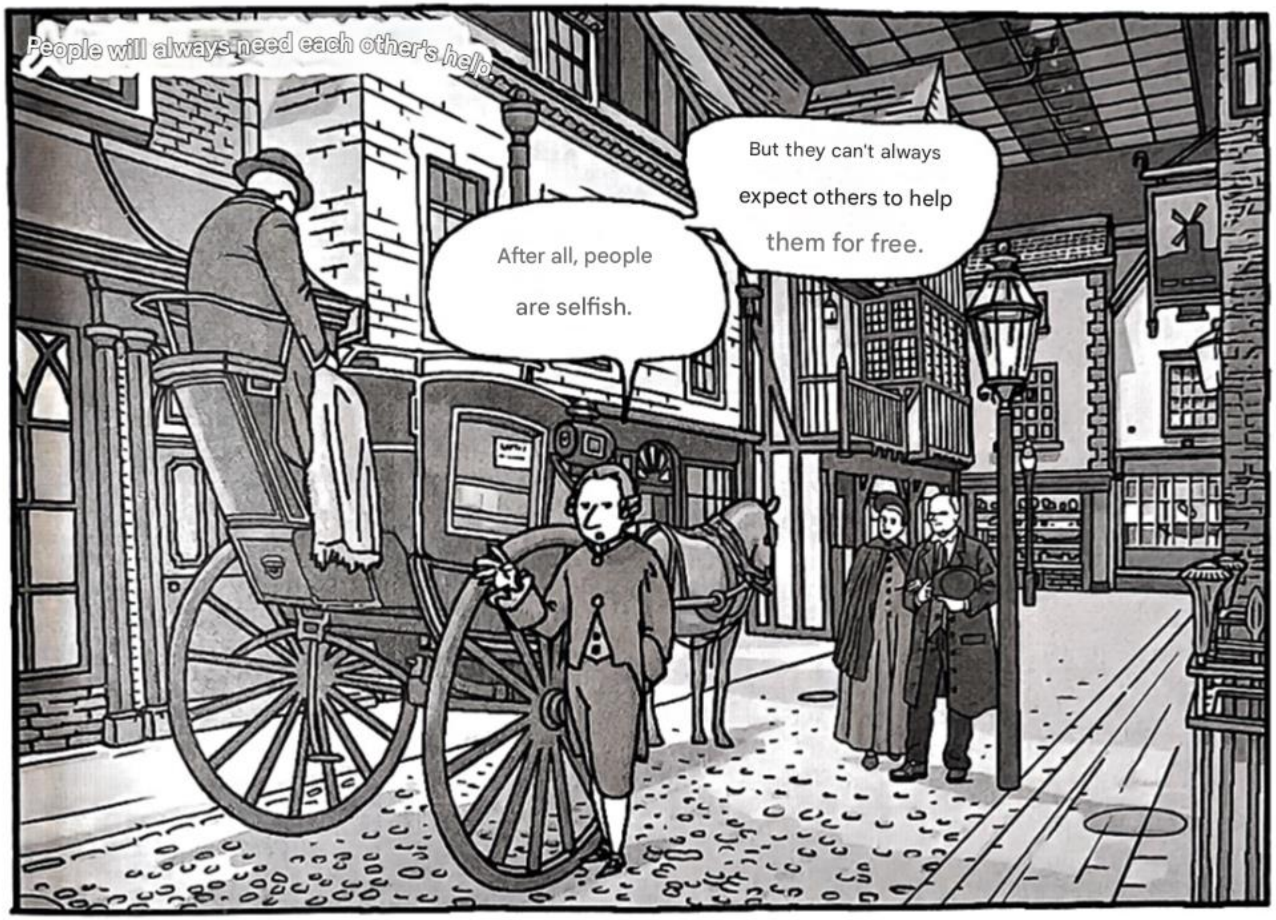

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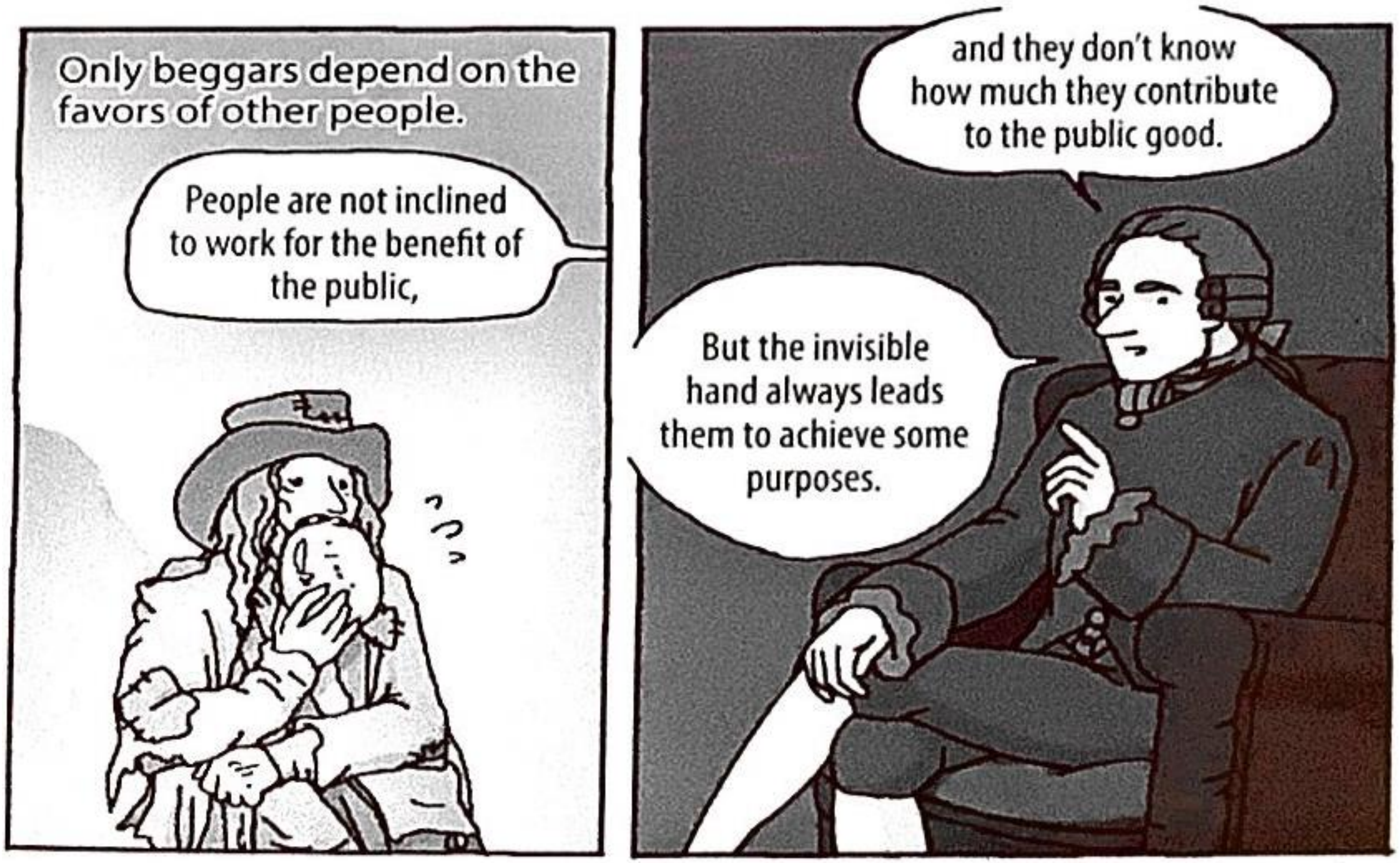

SUMMARY

- In a planned economy, central planners determine the production, distribution, and consumption of all goods and services.

- In a market economy, however, the power of decision-making lies in the hands of numerous businesses and households.

SUMMARY

- Adam Smith, in his work "The Wealth of Nations," used the metaphor of an "invisible hand" that benefits participants in a free market.
    - This "invisible hand" uses prices to guide businesses and households, coordinating their decisions precisely with the goal of maximizing the welfare of society as a whole.
    - Government control over prices restricts the ability of the "invisible hand" to adjust prices according to supply and demand.

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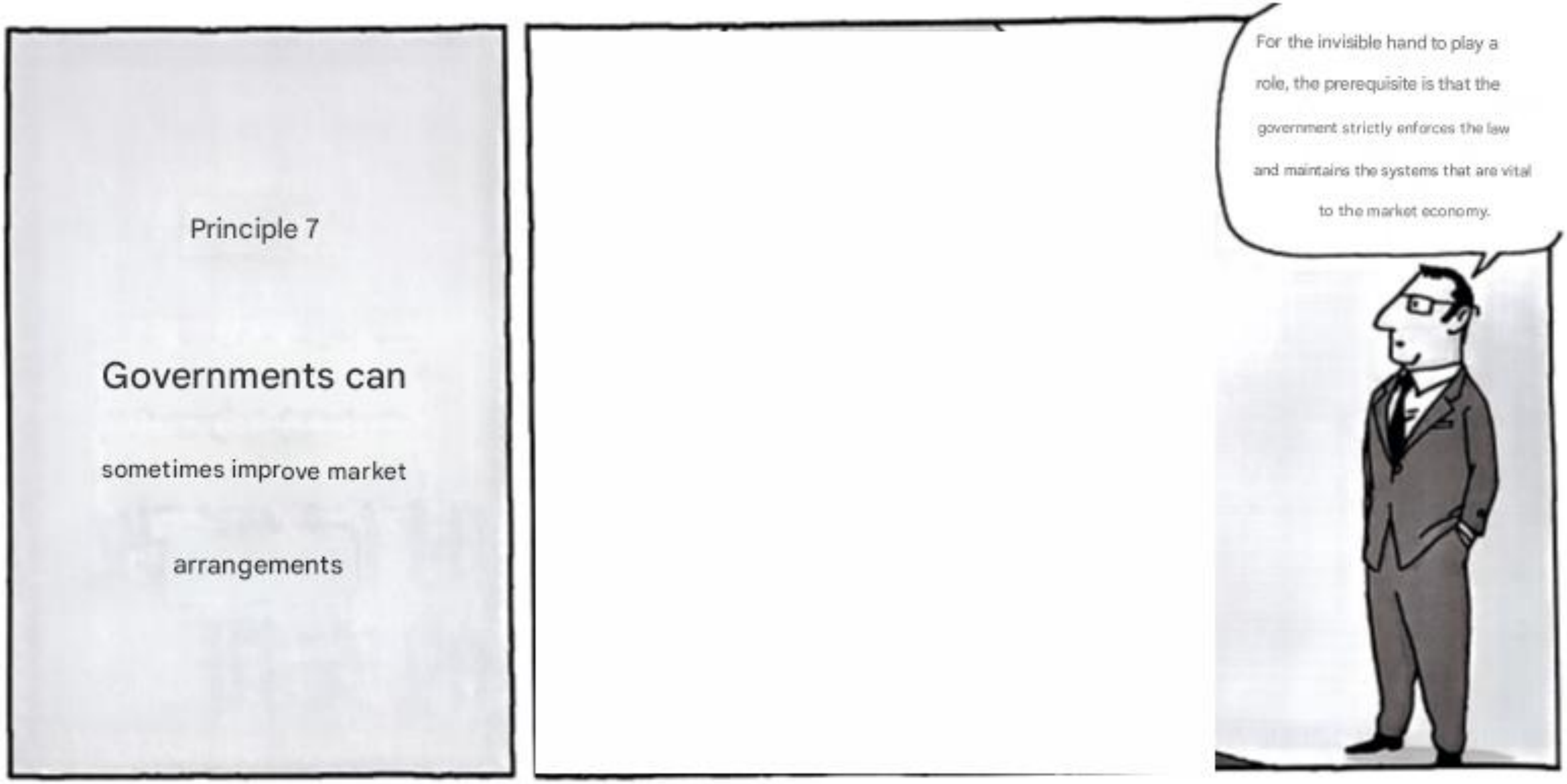

Principle 7: Governments can sometimes improve market outcomes.

Property rights define a set of rules regarding what owners can and cannot do with their property, as well as what others must do and cannot do with respect to that property.

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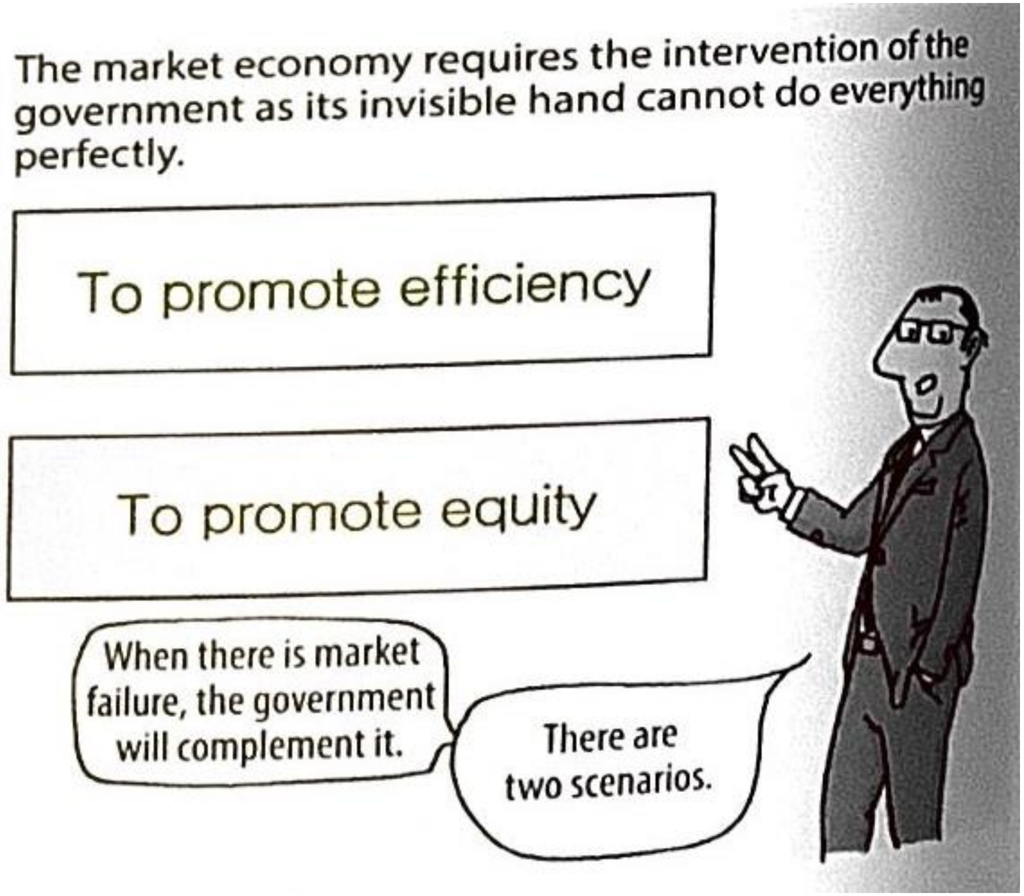

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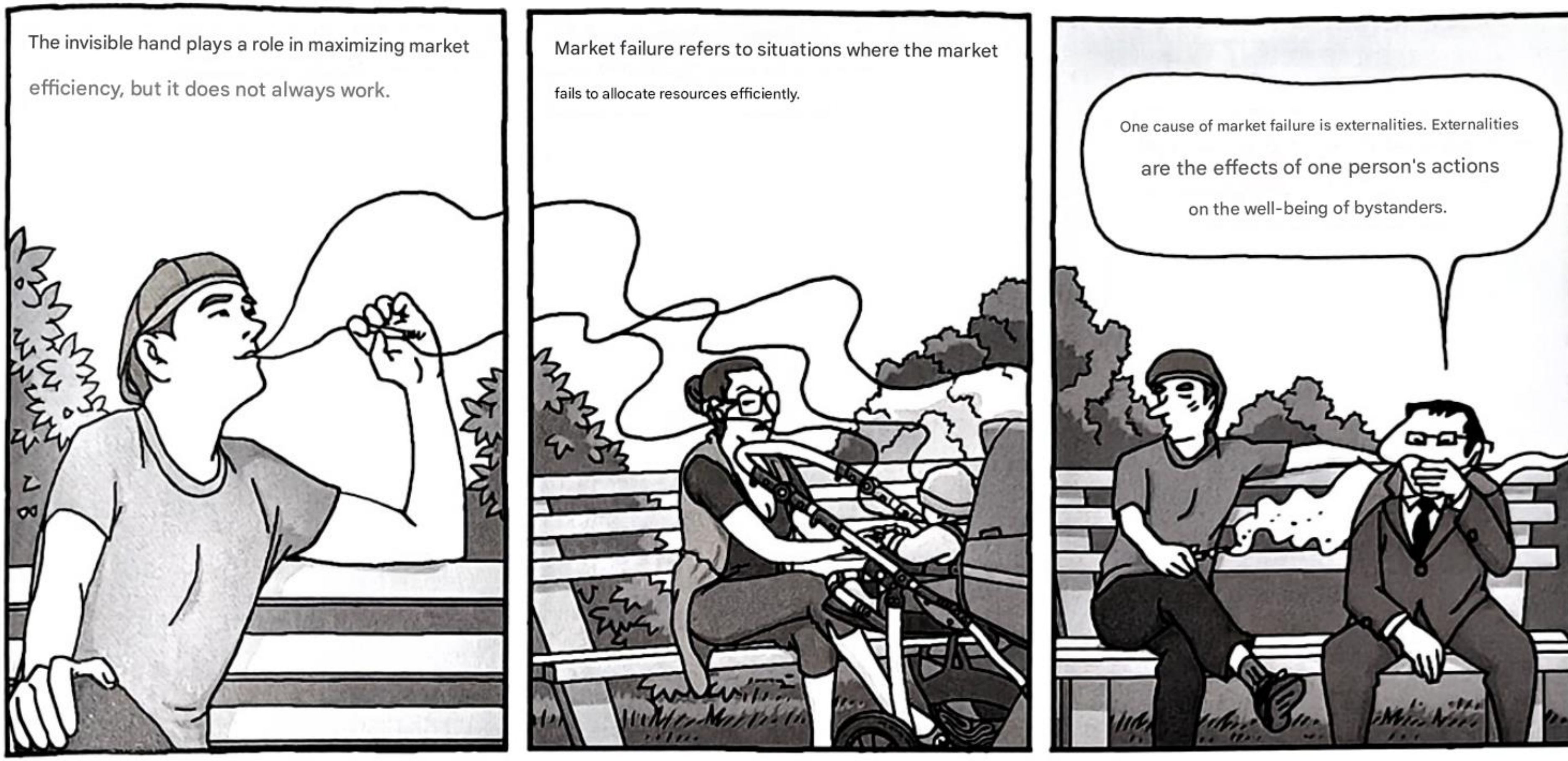

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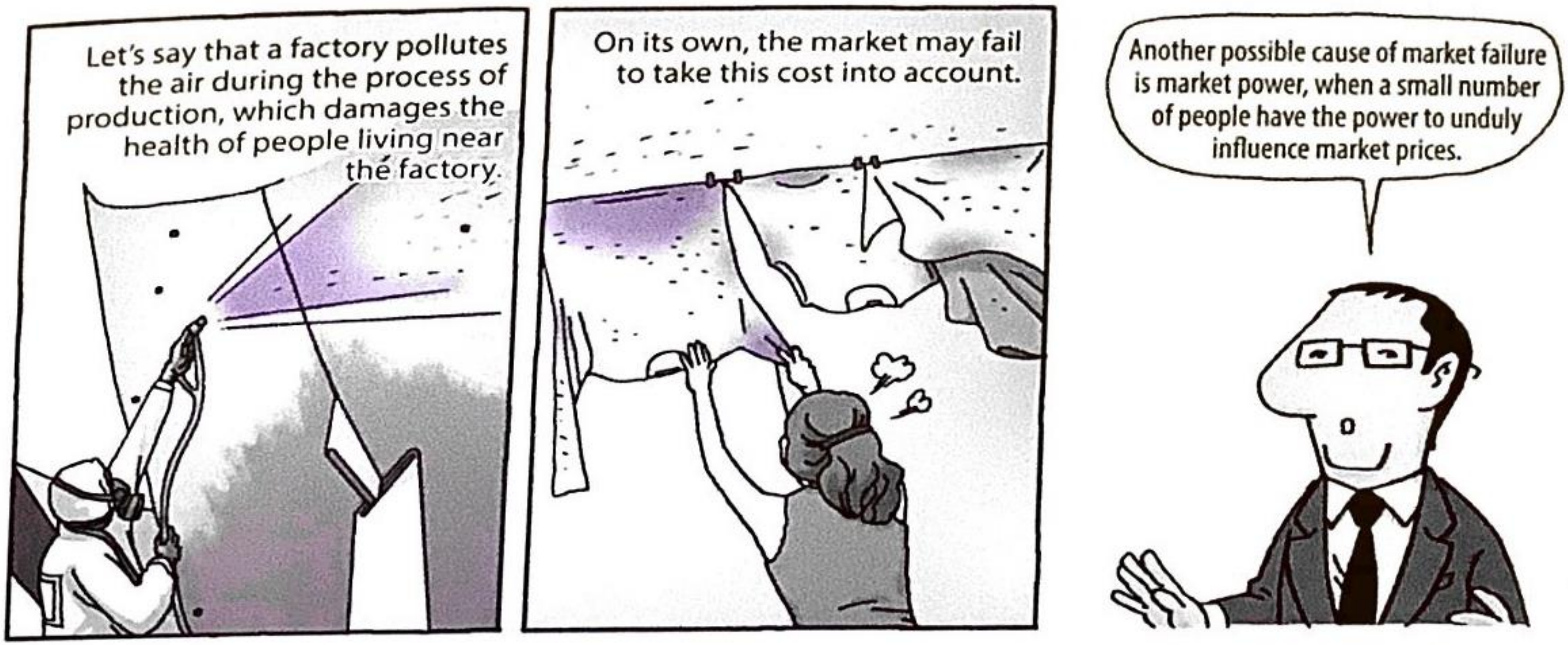

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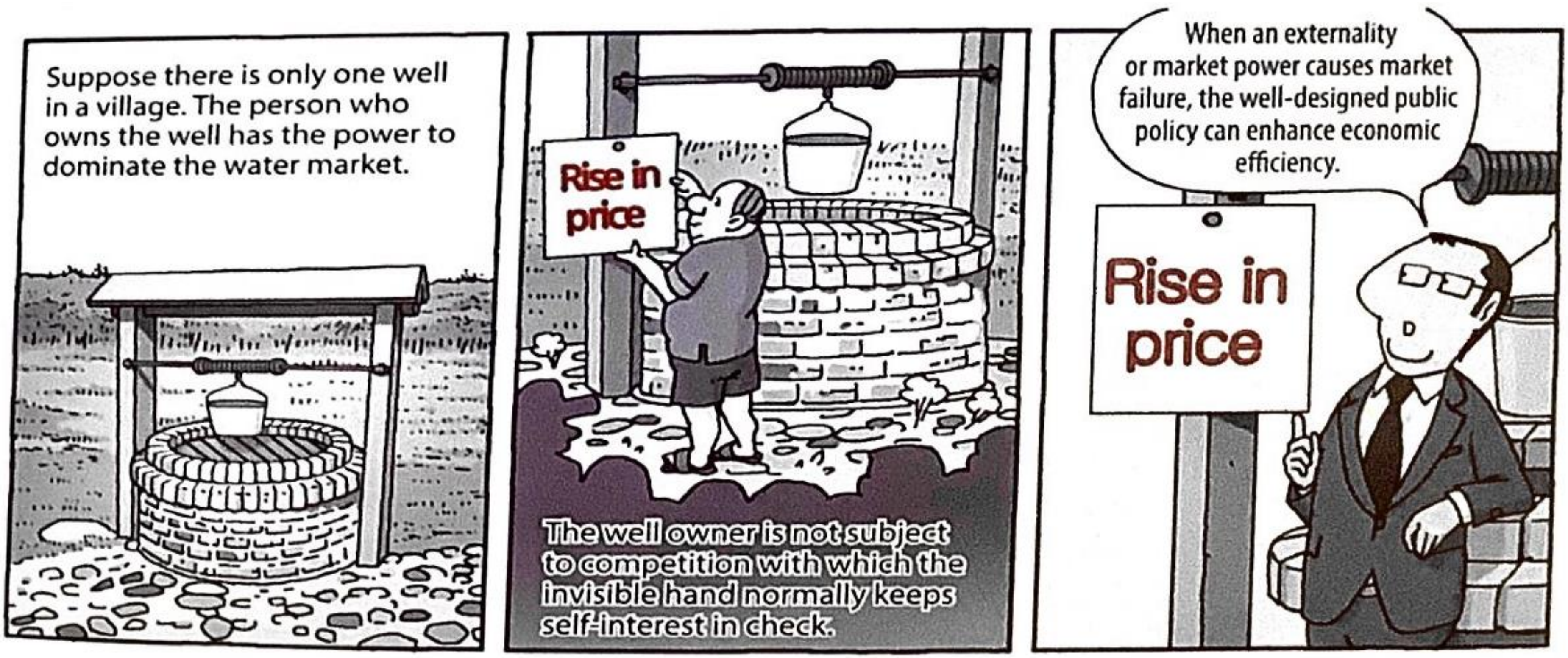

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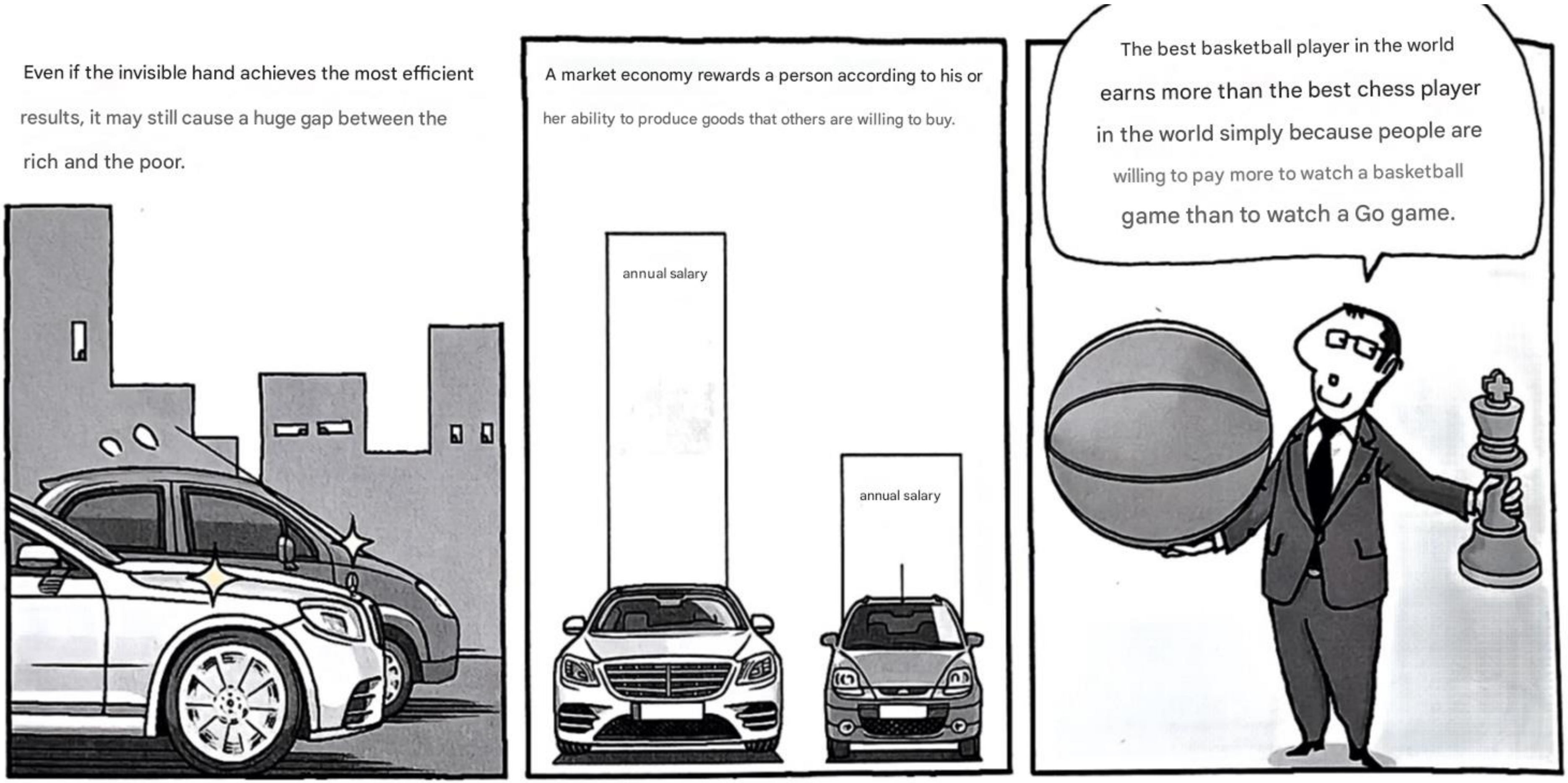
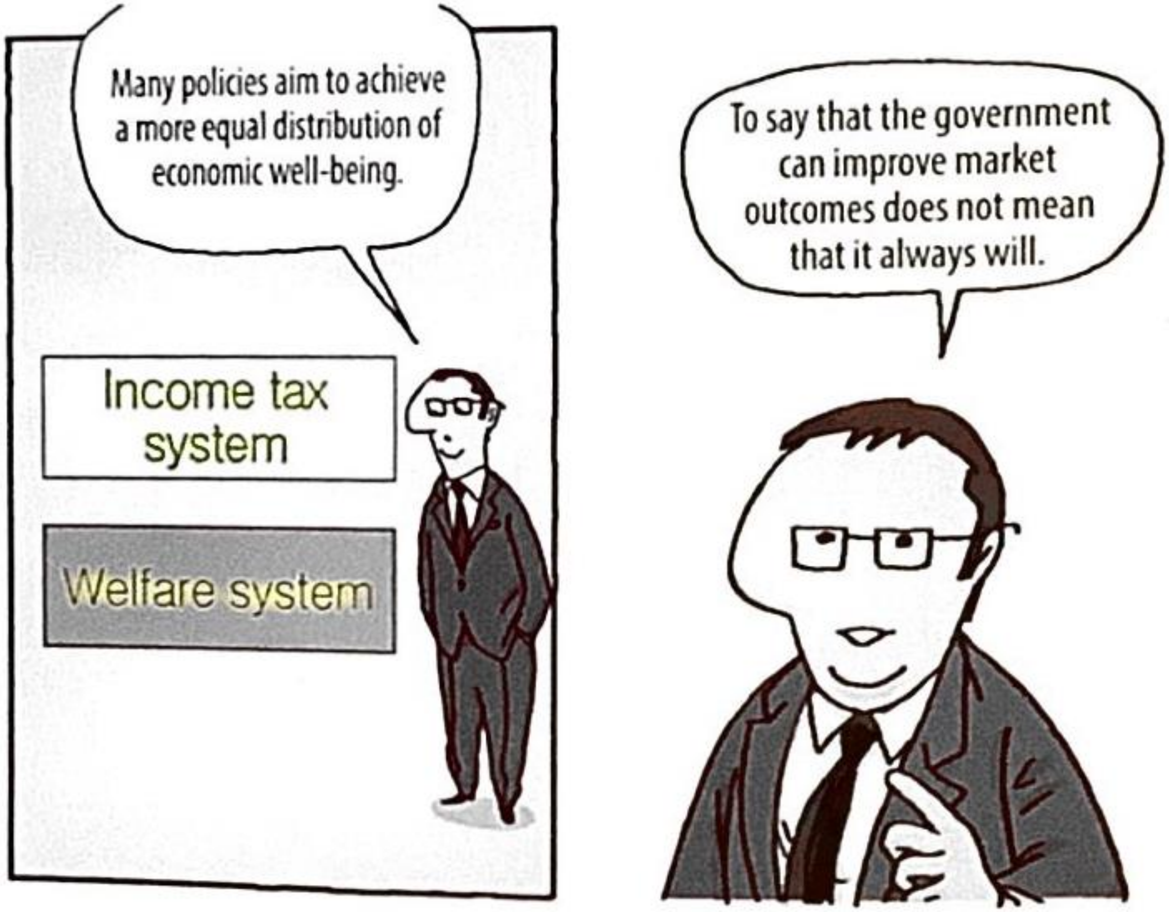


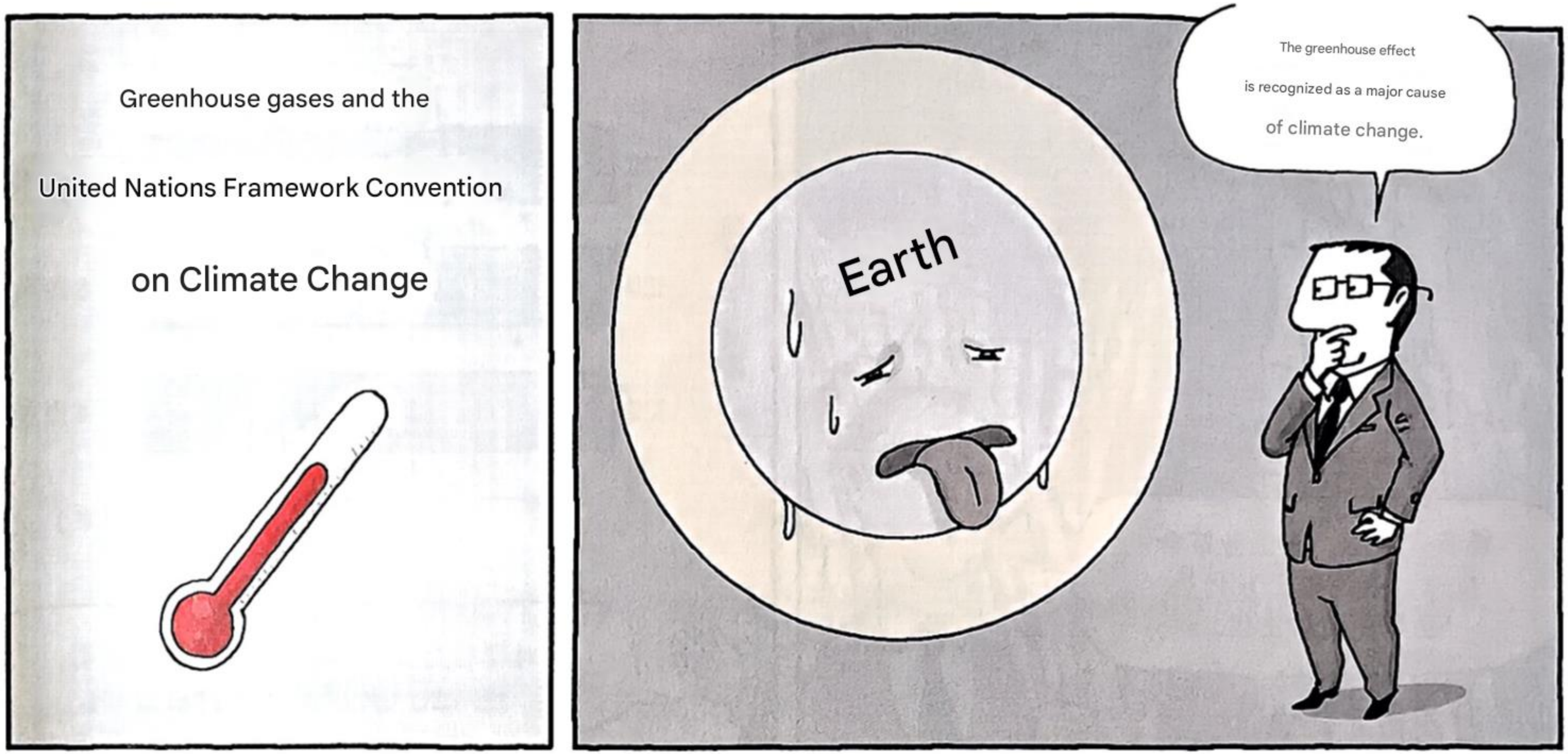
Principle 7: Governments can sometimes improve market outcomes.

The top 20% of the population holds 80% of the society's wealth.

Principle 7: Governments can sometimes improve market outcomes.



Greenhouse Gases and the United Nations Framework Convention on Climate Change



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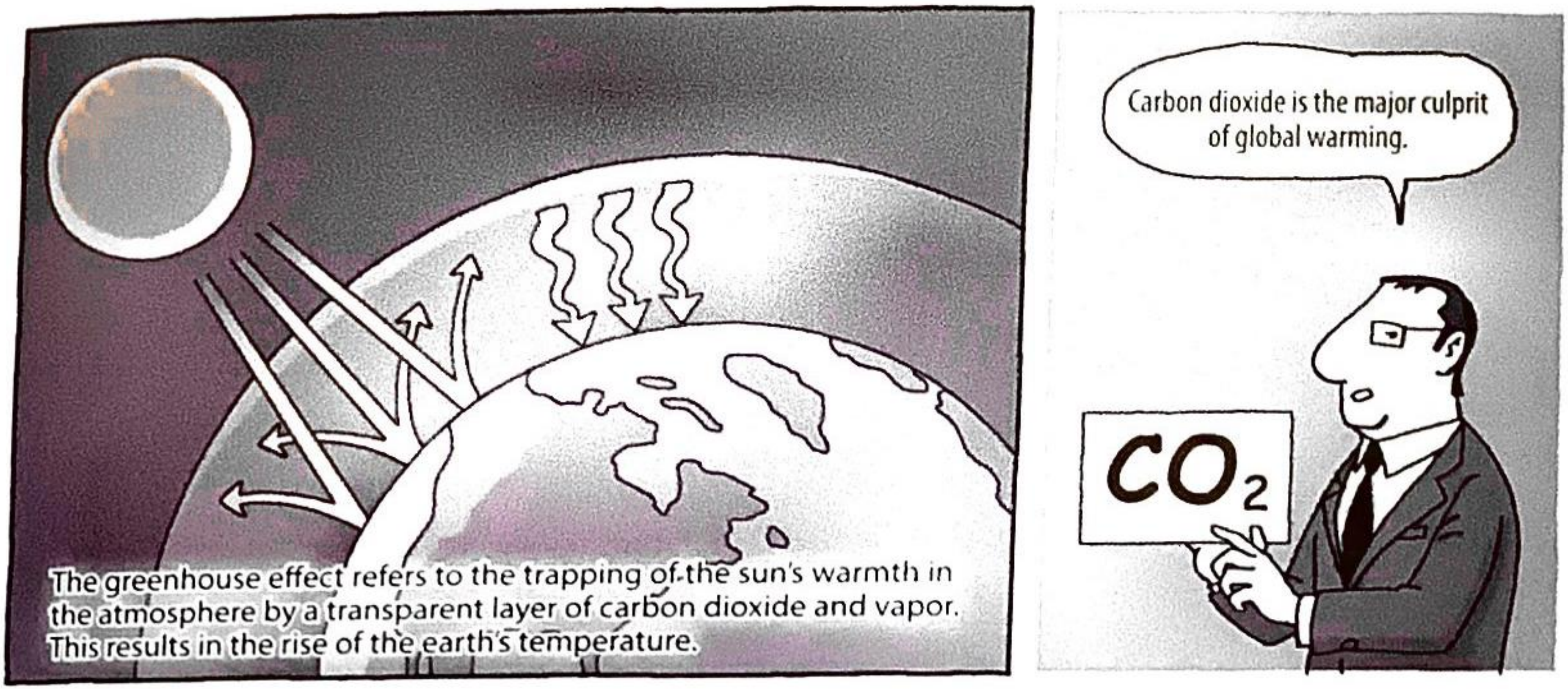

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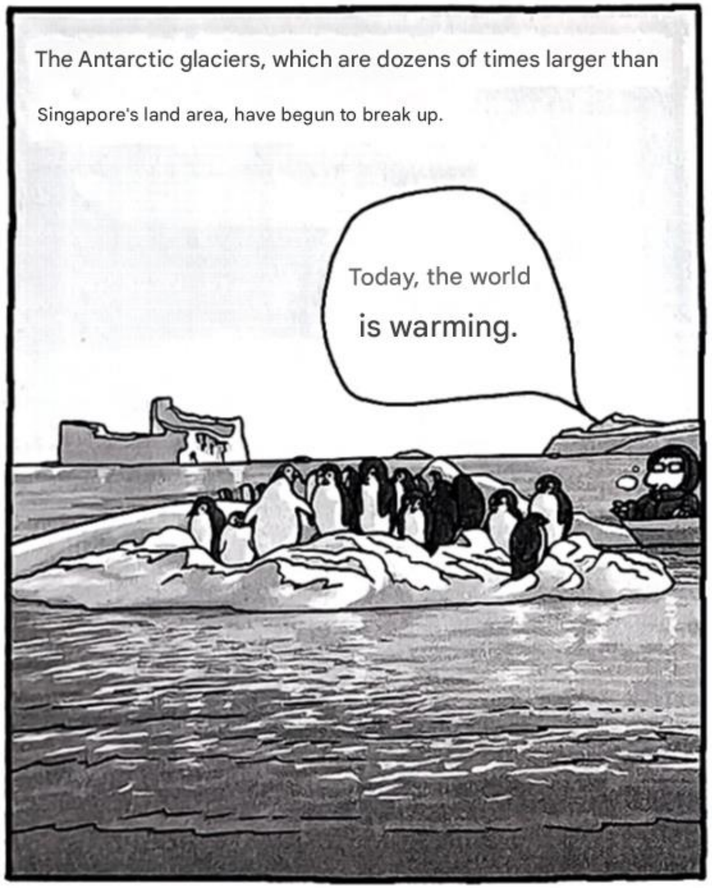

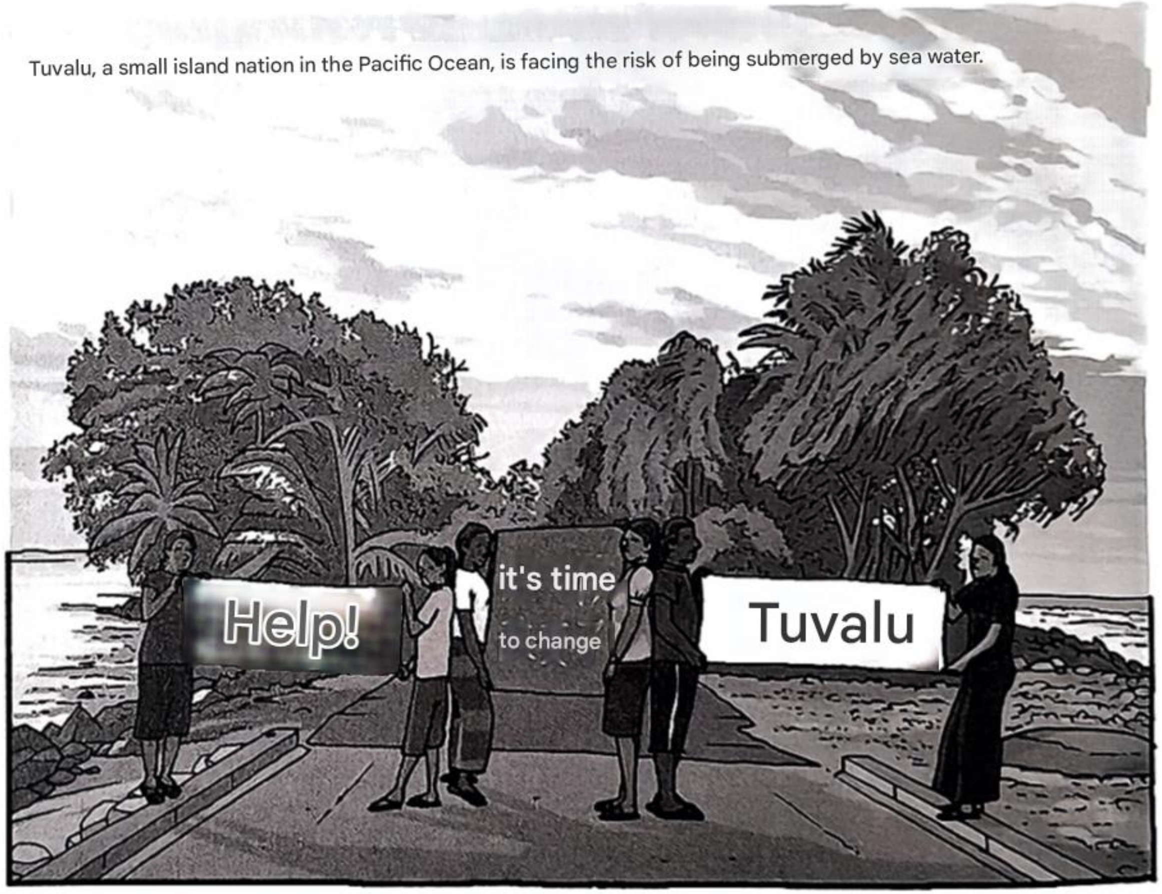

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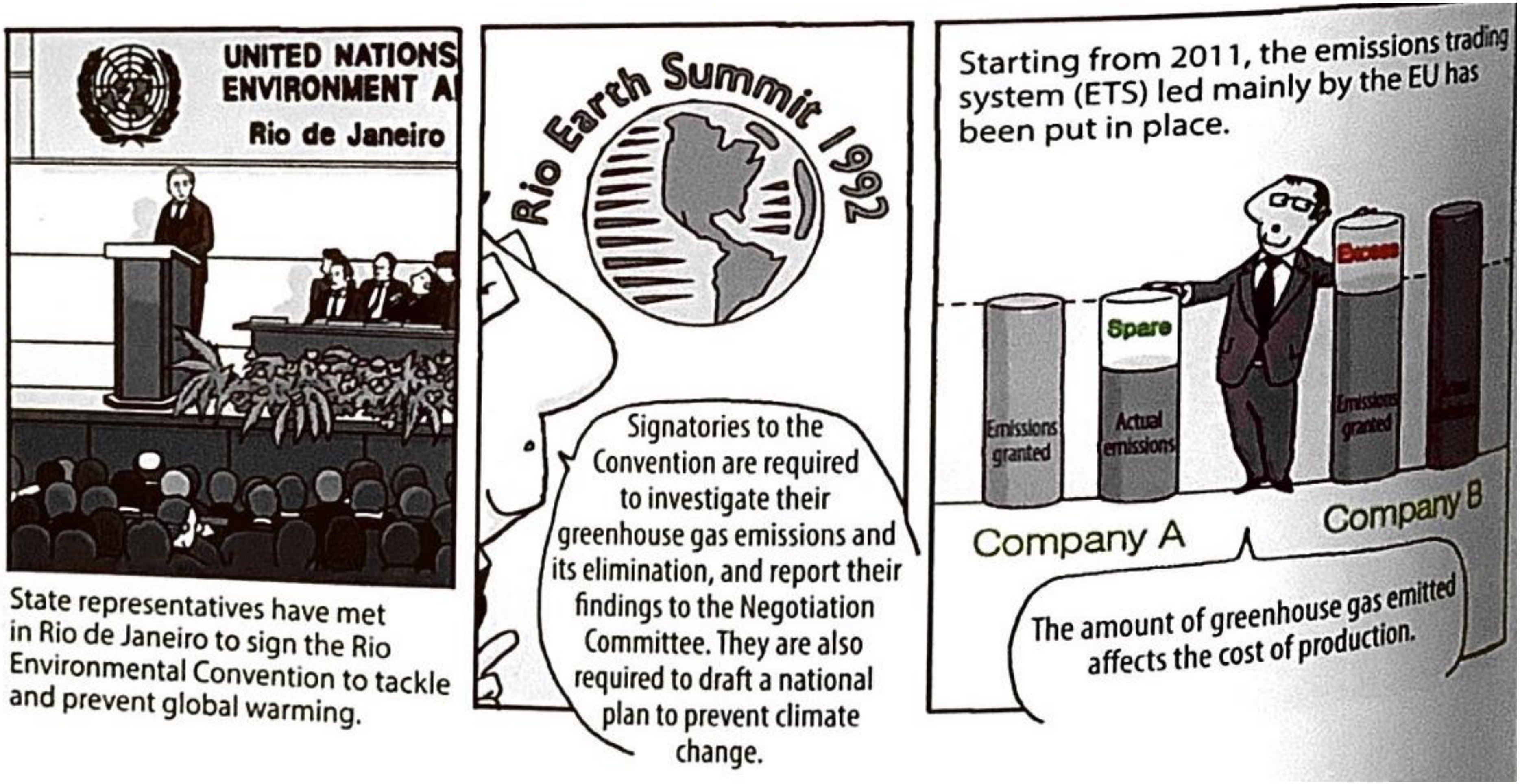

Rockefeller's Market Power and the Role of Government

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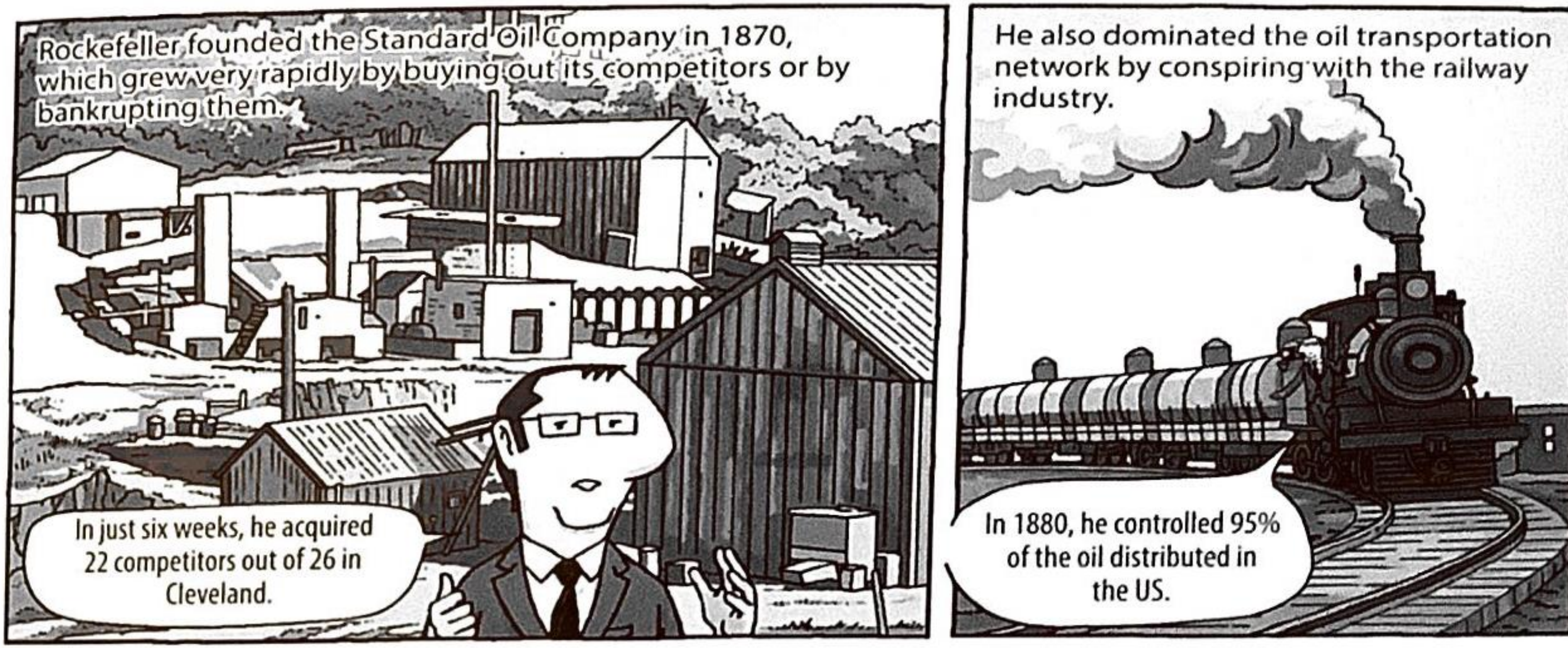

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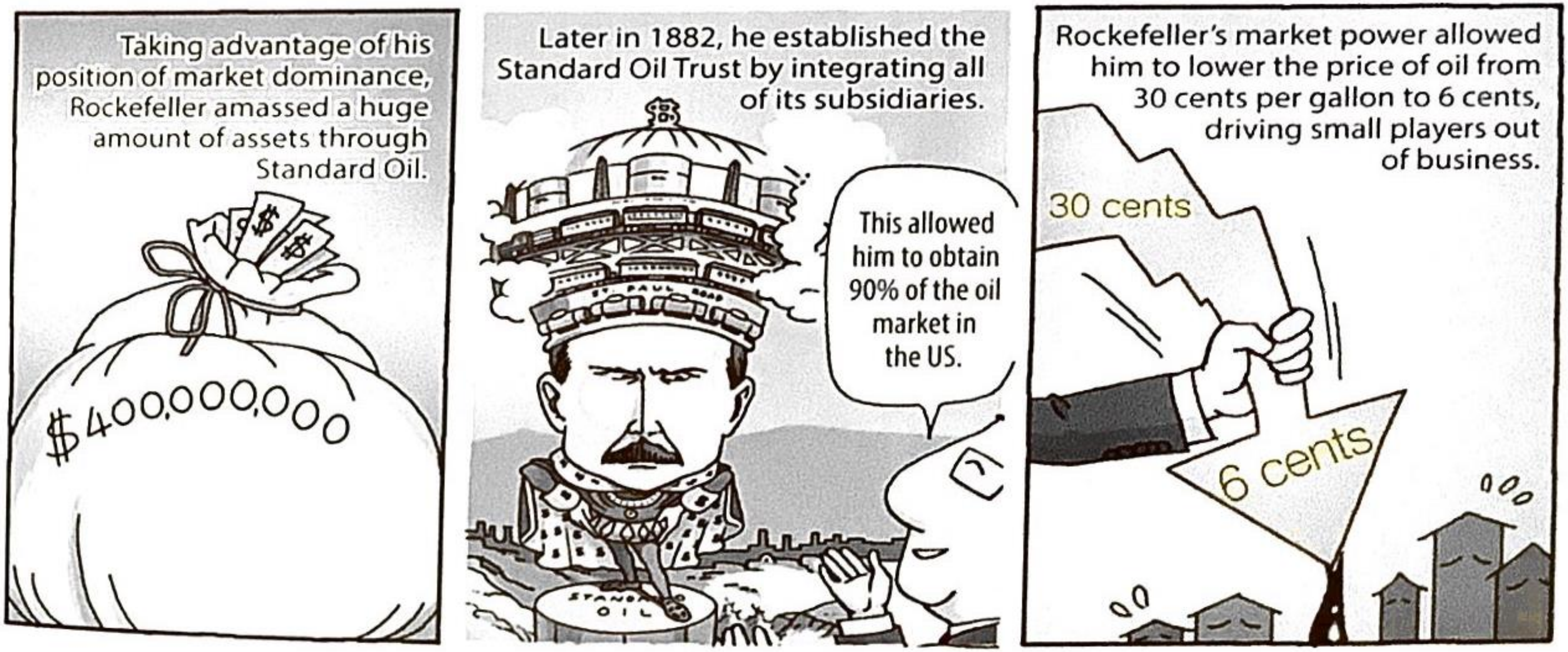

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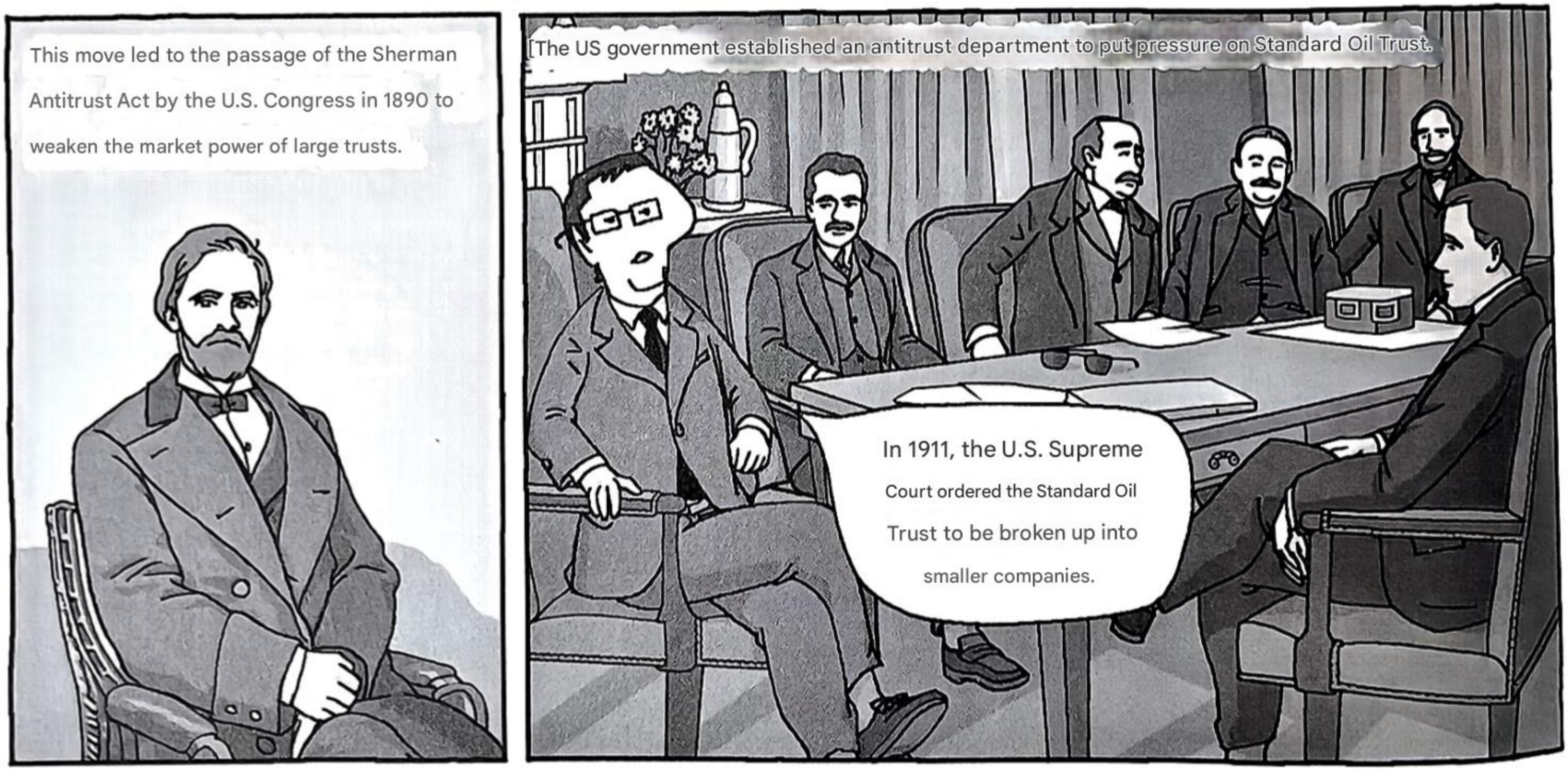

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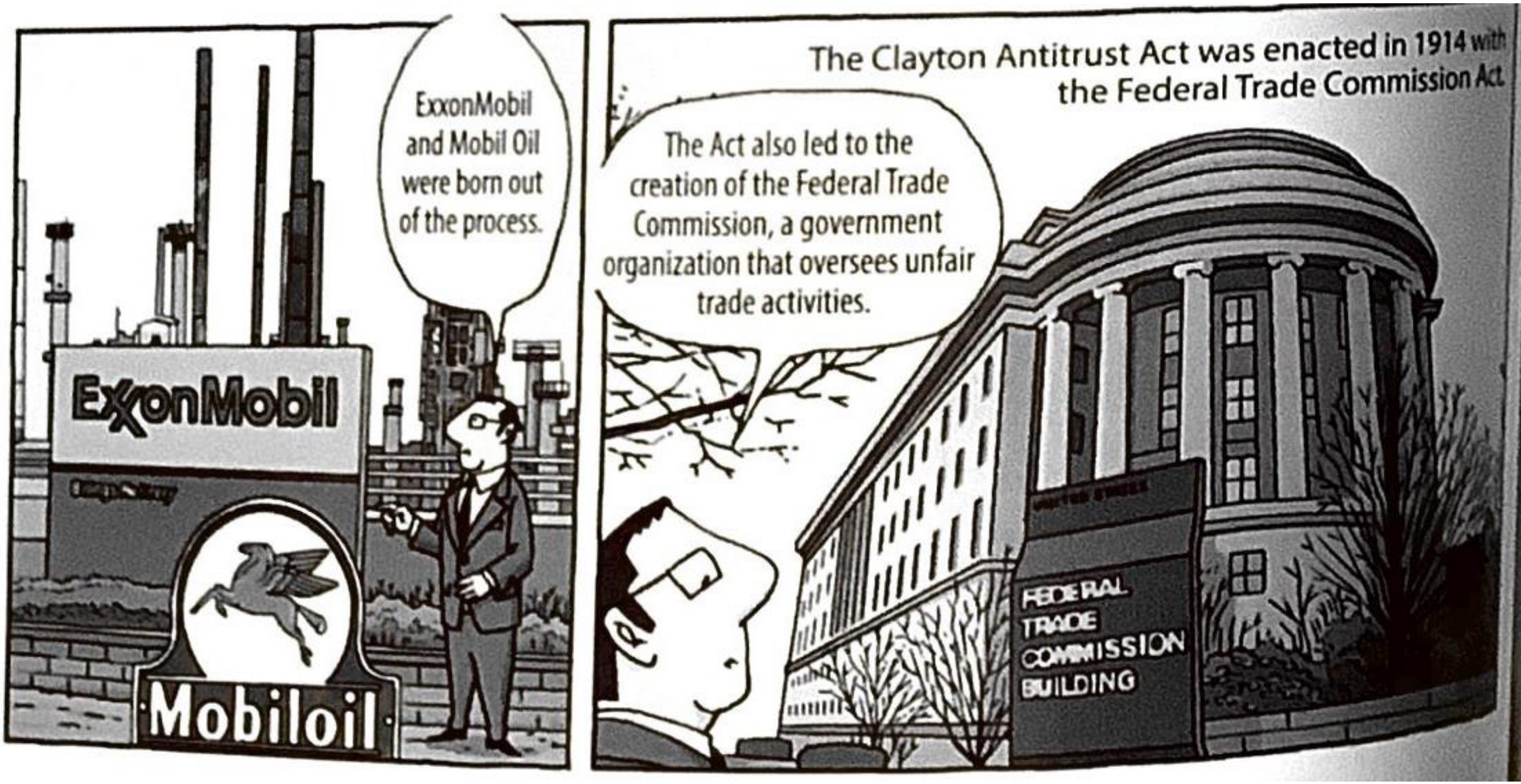

SUMMARY

- The invisible hand can only function effectively when the government strictly enforces laws and maintains institutions crucial to the market economy, such as property rights.

- The fundamental reason for government intervention in the market is to promote efficiency and equity.
  - Policies aimed at improving efficiency seek to enlarge the economic pie, while policies enhancing equity change how the pie is divided.

SUMMARY

- When market failures occur, such as the presence of externalities or market power, the government can implement relevant policies to enhance economic efficiency.
  - Market failure refers to situations where the market fails to achieve efficient resource allocation.
  - Externalities occur when one party's actions affect the economic well-being of a third party, such as environmental pollution.
  - Market power refers to the ability of an individual, a small group, or a single company to significantly influence market prices.

SUMMARY

- World Climate Treaties
  - 1992 Rio Summit: Government and civil society representatives gathered in Rio de Janeiro, Brazil, to discuss global issues such as climate change and industrial waste. The United Nations Framework Convention on Climate Change (UNFCCC) was signed during the summit. This international environmental treaty aims to prevent further global warming by limiting greenhouse gas emissions.
  - 1997 Kyoto Protocol: Following the adoption of the UNFCCC, parties met in Kyoto to discuss how to achieve the treaty's goals and signed the Kyoto Protocol to fulfill their commitments. The protocol required 38 developed countries, which accounted for 55% of global greenhouse gas emissions in 1990, to reduce their emissions by an average of 5.2% below 1990 levels by 2012. In March 2001, the United States withdrew from the Kyoto Protocol, citing incompatibility with its national interests. This led to a reduction in the overall emission cuts from the targeted 5.2% to an actual 1.8%.

SUMMARY

- World Climate Treaties
  - 2012 EU Emissions Trading System: Environment ministers from the 15 European Union member states agreed to establish an emissions trading system, enabling the trading of carbon dioxide emission rights. This means companies that need to exceed their emission quotas can purchase emission rights from those with lower emissions, thereby allowing them to emit more carbon dioxide.
  - 2015 Paris Agreement: This agreement outlined actions for countries to address climate change starting in 2020, replacing the Kyoto Protocol. Unlike the Kyoto Protocol, which only required emission reductions from developed countries, the Paris Agreement imposed binding commitments on all 195 signatory parties, including China. However, the United States withdrew from this agreement in 2017.

Quick Quiz

1. Do the following policies promote efficiency or equity? If they promote efficiency, discuss which type of market failure is involved.

(1) In 2007, Hong Kong announced the creation of the world's first "smoke-free society“. 500,000 venues, including parks, stadiums, and beaches, were designated as non-smoking areas. Anyone caught smoking in these areas would be fined HKD 5,000.

(2) In 1911, under the Sherman Antitrust Act, the Standard Oil Trust, which controlled over 90% of the U.S. refining market, was broken up into 33 companies. Standard Oil was founded by oil tycoon John D. Rockefeller in 1870.

(3) The government implements a "three-strikes" policy for drunk driving, stipulating that individuals caught violating the law three times (such as for drunk driving) will face severe punishment. The term originates from baseball, where a batter is called out after three missed swings in a single at-bat.

Quick Quiz

1. Do the following policies promote efficiency or equity? If they promote efficiency, discuss which type of market failure is involved.

(4) Sweden is one of the most renowned welfare states. It implements a progressive tax system — the higher the income, the higher the tax rate. Sweden is known for having one of the highest tax rates in the world, with the top marginal income tax rate reaching 57%.

(5) The U.S. Food Stamp Program first appeared in 1939 during the Great Depression as a form of support for impoverished populations. The program provides food stamps to low-income individuals, allowing them to purchase food.

思考题

2. Is there a difference between trade between nations and a win-lose contest?

思考题

3. What role does the invisible hand play in the market?

思考题

4. Please name two causes of market failure. For each cause, provide one example.

思考题

5. Adam Smith's "invisible hand" refers to:

a. The means by which companies earn profits from consumers

b. A function of the market economy that enables market participants, while pursuing self-interest, to achieve public benefit

c. The regulatory role played by the government without consumers' awareness

d. The phenomenon where producers and consumers harm third parties through their actions

思考题

6. Government intervention in the market aims to:

a. Protect property rights

b. Correct market failures caused by externalities

c. Ensure equitable income distribution

d. All of the above are correct