

# AGEC 410 – Agricultural and Food Policy

## 5 – Analytical Frameworks

Review and develop frameworks used in agricultural policy analysis

Theory of firm

Economic model of a sector

Simple general equilibrium model of an economy

Why use these frameworks?

clarity,

organized thinking

responses consistent with economic theory

Theory of the Firm

Assumptions:

profit maximizing producers

producers are price takers

certainty

homogenous good

free mobility of resources

free entry/exit

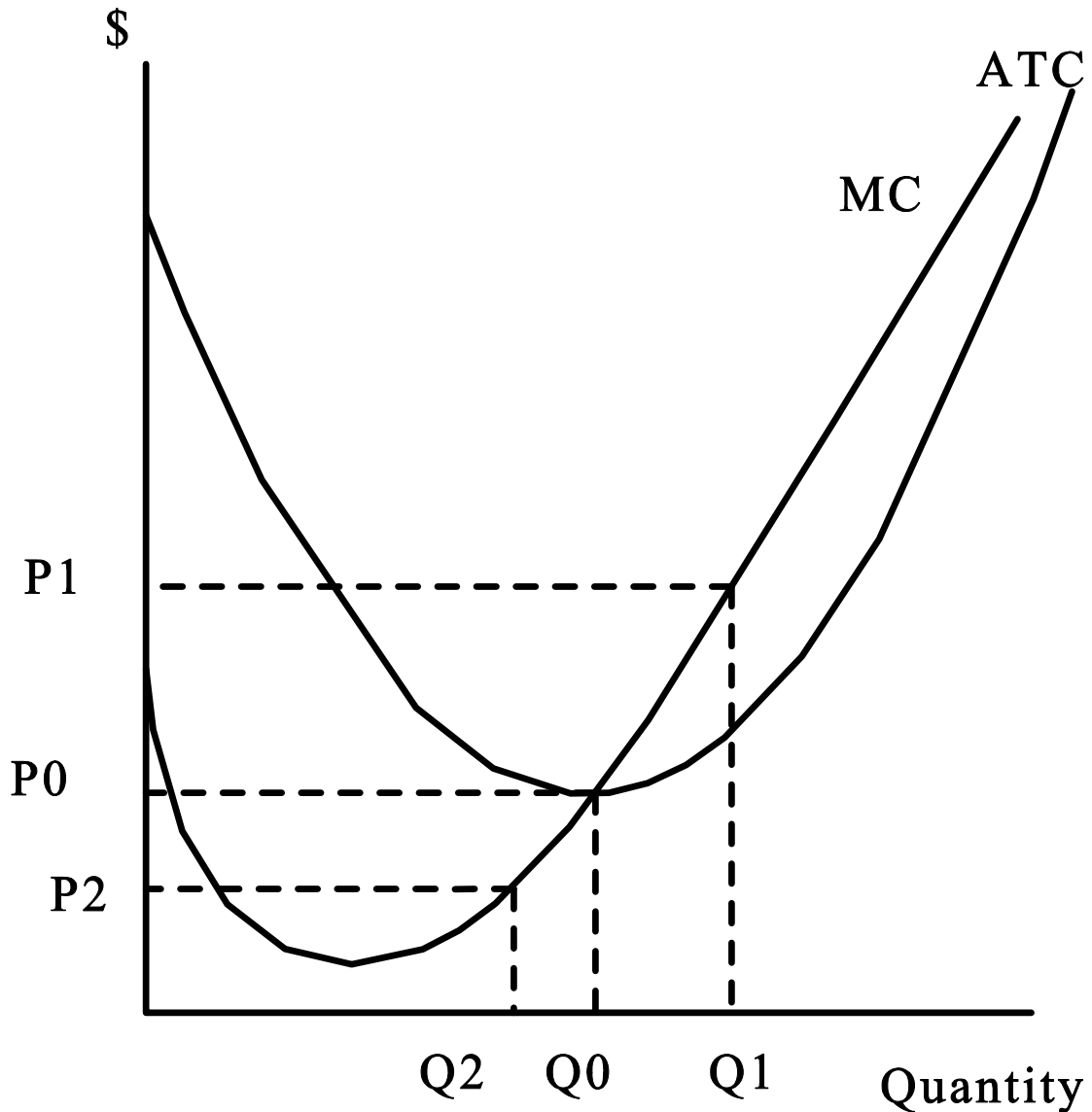
Shape of average cost reflects returns to scale

Equilibrium at minimum average cost, where MC cuts ATC, and  $P = MR + mc$

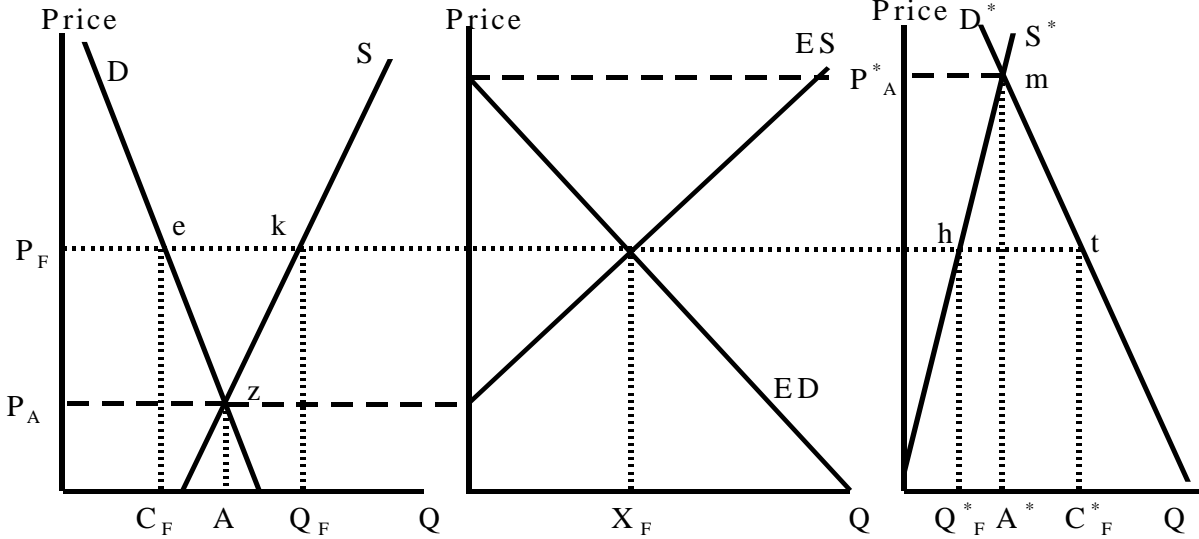
why?

As  $Q$  increases, if  $MR > MC$ , unit profit increases

As  $Q$  increases in  $MR < MC$ , unit profit decreases



# Sector Equilibrium, Free Trade



# Full Economy Equilibrium, Free Trade

