

Economics – Chapter 1 – What Economics is About

Economics is based mainly on logic. You should know from common sense that businesses want to make money, while consumers want to save money. You should know, at least vaguely, the law of supply and demand. Watch the news, read the papers, **use your head**, memorize these terms, and you'll be fine.

1. **Scarcity** – The condition in which our wants are greater than the limited resources available to satisfy those wants
 - a. Competition exists because of scarcity
 - b. Choice exists because of scarcity. If you had everything you want, you don't have to choose
2. **Economics** – The science of scarcity: The science of how individuals and societies deal with the fact that wants are greater than the limited resources available to satisfy those wants
3. **Economic Analysis** – The process of applying economic tools and the economic way of thinking to real world problems
4. **Utility** – the satisfaction one receives from a good
5. **Good** – anything from which individuals receive utility or satisfaction. Examples: Cars, computers, TV's
6. **Bad** – anything from which individuals receive disutility or dissatisfaction
7. **Disutility** – the dissatisfaction one receives from a bad
8. **Land** – natural resources, minerals, forests, water, unimproved land, oil, wood, animals, etc
9. **Labor** – the physical and mental talents people contribute to the production process. In other words, work
10. **Capital** – produced goods that can be used as inputs for further production. Examples: Factories, machinery, tools, computers, buildings, etc
11. **Entrepreneurship** – the particular talent that some people have for organizing the resources of land, labor, and capital to produce goods, seek new business opportunities, and develop new ways of doing things
12. **Rationing device** – a means for deciding who gets what of available resources and goods. Example: Money
 - a. Whatever the rationing device, people will compete for it
13. **Opportunity Cost** – the most highly valued opportunity or alternative forfeited when a choice is made
 - a. We make choices because there are opportunity costs
14. **Decisions at the Margin** – decisions making characterized by weighting additional benefits of a change against the additional costs of a change with respect to current conditions
 - a. Example: Should I stay open for 2 more hours? It's not open or close for the whole day, but what are the costs and benefits of staying open two MORE hours?
15. **Theory** – an abstract representation of the real world designed with the intent to better understand the world
 - a. Theories are judged by how well they predict, not the accuracy of its assumptions
16. **Abstract** – the process of focusing on a limited number of variables to explain or predict an event
17. **Fallacy of Composition** – the erroneous view that what is good or true for the individual is necessarily good or true for the group. Example: 1 man runs to exit, he leaves faster. Everyone runs to the exit, everyone is slowed
18. **Ceteris Parabus** – A Latin term meaning "all other things held constant"
19. **Positive Economics** – the study of "what is" in economic matters
20. **Normative Economics** – The study of "what should be" in economic matters
21. **Microeconomics** – the branch of economics that deals with human behavior and choices as they relate to relatively small units – an individual, a firm, an industry, or a single market
22. **Macroeconomics** – the branch of economics that deals with human behavior and choices as they relate to highly aggregate markets (such as the goods and services market), or the entire economy

Added 1/28/03

1. Land earns rent, labor earns wages, capital earns interest, entrepreneurship earns profit
2. **Big Microeconomic questions** – what, how, and for whom are goods and services produced?
3. **Big Macroeconomic Questions** – What determines standard and cost of living? Why does the economy fluctuate?
4. **Cost of living** – amount of money it takes to buy the goods and services a typical family consumes
5. **What Tradeoffs** – go to the movies or buy coffee? Guns Vs Butter
6. **How tradeoffs** – trade labor for capital (machines replacing workers)
7. **For Whom Tradeoffs** – voluntary payments, theft, benefits by the government – transfer of wealth
8. **Big Tradeoff** – equality and efficiency – efficiency is better overall, but uneven distribution of wealth. Give everyone the same amount, and you lose efficiency since there's no incentive to work harder
9. **Standard of living tradeoffs** – save more now, higher standard of living for the future
10. **Output-inflation tradeoff** – higher output results in higher inflation, so lower it to lower inflation
11. **Marginal Cost** – cost of producing one extra unit, going a little bit further
12. **Marginal benefit** – benefit of producing one extra unit, going a little bit further
13. **incentive** – an inducement to take a particular action
14. **Post Hoc** – cause and effect doesn't always follow time – Christmas causes increased holiday shopping

