Unit 1: Basic Economic Concepts

I WON THE LOTTERY!
I’ll give you anything you want other than money.
What do you want?
Would your list ever end?
Why not?
Scarcity!!!
What is Economics?

• **Economics** is the science of scarcity.

• **Scarcity** - we have unlimited wants but limited resources.

• Since we are unable to have everything we desire, we must make **choices** on how we will use our resources.

Economics is the study of **choices**.

In economics we will study the choices of individuals, firms, and governments.
Examples:
You must choose between buying jeans or buying shoes. Businesses must choose how many people to hire. Governments must choose how much to spend on welfare.

Textbook Definition

Economics- Social science concerned with the efficient use of scarce resources to achieve maximum satisfaction of economic wants.

(Study of how individuals and societies deal with scarcity)
Micro vs. Macro

MICROeconomics-
Study of small economic units such as individuals, firms, and industries (ex: supply and demand in specific markets, production costs, labor markets, etc.)

MACROeconomics-
Study of the large economy as a whole or economic aggregates (ex: economic growth, government spending, inflation, unemployment, international trade etc.)
How is Economics used?

• Economists use the scientific method to make generalizations and abstractions to develop theories. This is called theoretical economics.
• These theories are then applied to fix problems or meet economic goals. This is called policy economics.

Positive vs. Normative

Positive Statements - Based on facts. Avoids value judgements (what is).
Normative Statements - Includes value judgements (what ought to be).
5 Key Economic Assumptions

1. Society has unlimited wants and limited resources (scarcity).

2. Due to scarcity, choices must be made. Every choice has a cost (a trade-off).

3. Everyone’s goal is to make choices that maximize their satisfaction. Everyone acts in their own “self-interest.”

4. Everyone makes decisions by comparing the marginal costs and marginal benefits of every choice.

5. Real-life situations can be explained and analyzed through simplified models and graphs.
Cuteness vs. Number of Legs

- Awww... Adorable!
- Cute
- Pretty Normal
- Unfortunate
- Creepy
- Gaaaah! Kill it! Kill it!!!

Number of Legs
How much we enjoy childhood things

OMG THIS IS THE COOLEST THING EVER!!!

This is relative to my interests.

Kinda cool...

Meh. Whatever.

"That's for babies."

Ew.

Young Child  Grade School  Middle School  High School  College
Usefulness of Shotgun in Video Games

Y-Axis:
- OMG best weapon ever!
- Pretty cool
- Decent.
- I'd like that rifle better...
- Who the hell uses a shotgun?
- WTF?!

Video Game:
- Halo
- Tactical Shooter
- Zombie Game
- Call of Duty
- Covert Ops
Probability of Being Right

Relationship Status

Single  Dating  Relationship  Engaged  Married

Probability

100%  90%  80%  70%  60%  50%  40%  30%  20%  10%  0%
Thinking at the Margin

<table>
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<tr>
<th># Times Watching Movie</th>
<th>Benefit</th>
<th>Cost</th>
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<tr>
<td>1st</td>
<td>$30</td>
<td>$10</td>
</tr>
<tr>
<td>2nd</td>
<td>$15</td>
<td>$10</td>
</tr>
<tr>
<td>3rd</td>
<td>$5</td>
<td>$10</td>
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<tr>
<td><strong>Total</strong></td>
<td><strong>$50</strong></td>
<td><strong>$30</strong></td>
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Would you see the movie three times? Notice that the total benefit is more than the total cost but you would NOT watch the movie the 3rd time.
Marginal Analysis

In economics the term marginal = additional
Marginal analysis (aka: thinking on the margin)
making decisions based on increments

Example:
• When you decide to go to the mall you consider the additional benefit and the additional cost (your opportunity cost).
• Once you get to the mall, you continue to use marginal analysis when you shop, buy food, and talk to friends.
• Since your marginal benefits and costs can quickly change your analyzing them every second.
• What if your ex-girlfriend shows up?

The Point: You will continue to do something as long as the marginal benefit is greater than the marginal cost
All Resources are Scarce!

This video was made in 2008.
Did it come true?
Review with your neighbor…

1. Define scarcity
2. Define Economics
3. Identify the relationship between scarcity and choices
4. Explain how Macroeconomics is different than Micro
5. Explain the difference between positive and normative economics
6. Identify the 5 main assumptions of Economics
7. Give an example of marginal analysis
8. Name 10 Disney movies
Analyzing Choices
Given the following assumptions, make a rational choice in your own self-interest (hold everything else constant)…

1. You want to visit your friend for a week. You will return Sunday night.
2. You work every weekday earning $100 per day
3. You have three flights to choose from: Thursday Night Flight = $275 Friday Early Morning Flight = $300 Friday Night Flight = $325

Which flight should you choose? Why?
Trade-offs vs. Opportunity Cost

ALL decisions involve trade-offs.

**Trade-offs** - ALL the alternatives that we give up when we make a choice

(Examples: going to the movies)

**Opportunity cost** - most desirable alternative given up when you make a choice.

What are trade-offs of deciding to go to college?

What is the opportunity cost of going to college?

GEICO assumes you understand opportunity cost. Why?
Econ of College

GOOD GRADES

CHOOSE TWO

SOCIAL LIFE

ENOUGH SLEEP
"Every gun that is made, every warship launched, every rocket fired signifies, in the final sense, a theft from those who hunger and are not fed, those who are cold and are not clothed. This world in arms is not spending money alone. It is spending the sweat of its laborers, the genius of its scientists, the hopes of its children."

“The cost of one modern heavy bomber is this: a modern brick school in more than 30 cities. It is two electric power plants, each serving a town of 60,000 population. It is two fine, fully equipped hospitals. It is some fifty miles of concrete pavement."

“We pay for a single fighter plane with a half million bushels of wheat. We pay for a single destroyer with new homes that could have housed more than 8,000 people.”

-Dwight Eisenhower

Speaking against the military build up of the cold war
The USS Dwight Eisenhower
Launched in 1975 and cost $679 million ($4.5 billion in 2007 dollars)
46. Karen works part-time at a local convenience store and earns $10 per hour. She wants to spend next Saturday afternoon attending a music concert. The full price of a concert ticket is $75, but Karen was able to get a discounted price of $50 from a friend who purchased the ticket but has become unable to attend. If Karen took 4 hours off from her job to attend the concert, what was her opportunity cost of attending the concert?

(A) $40
(B) $50
(C) $75
(D) $90
(E) $115
Economic Terminology

Utility = Satisfaction!
Marginal = Additional!
Allocate = Distribute!
Price vs. Cost
What’s the price? vs. How much does that cost?
Price = Amount buyer (or consumer) pays
Cost = Amount seller pays to produce a good

Investment
Investment = the money spent by BUSINESSES to improve their production
Ex: $1 Million new factory

• Consumer Goods - created for direct consumption (example: pizza)
• Capital Goods - created for indirect consumption (oven, blenders, knives, etc.)
• Goods used to make consumer goods
The 4 Factors of Production
The Four Factors of Production

ALL resources can be classified as one of the following four factors of production:

1. **Land** - All natural resources that are used to produce goods and services. (*Ex: water, sun, plants, animals*)

2. **Labor** - Any effort a person devotes to a task for which that person is paid. (*Ex: manual laborers, lawyers, doctors, teachers, waiters, etc.*)

3. **Capital** -
   - **Physical Capital** - Any human-made resource that is used to create other goods and services (*Ex: tools, tractors, machinery, buildings, factories, etc.*)
   - **Human Capital** - Any skills or knowledge gained by a worker through education and experience
Program for International Student Assessment (PISA) is a worldwide evaluation of 15-year-old school children's scholastic performance.

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<td>20.</td>
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<td>487</td>
<td>20. Luxembourg</td>
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The Four Factors of Production

4. **Entrepreneurship** - ambitious leaders that combine the other factors of production to create goods and services.

- **Examples** - Henry Ford, Bill Gates, Inventors, Store Owners, etc.

Entrepreneurs:

1. Take The Initiative
2. Innovate
3. Act as the Risk Bearers

So they can obtain **PROFIT**.

Profit = Revenue - Costs