THE ECONOMIC SIDE

1. **What is economics?**

The study of how individuals and societies choose to allocate and use scarce resources to satisfy unlimited wants.

Economics is about economizing; that is, about choice among alternative uses of scarce resources. Choices are made by millions of individuals, businesses, and government units. Economics examines how these choices add up to an economic system, and how this system operates. (L.G. Reynolds).

2. **Concept of scarcity**

- Scarcity means the goods available are too few to satisfy individuals' desires.
- The degree of scarcity is constantly changing
- The quantity of goods, services and usable resources depends on technology and human action

Why scarcity does exist?

- Scarcity exists because individuals want more than can be produced.
- **Economics is the study of how society manages its scarce resource.**

Microeconomics vs. Macroeconomics

- Microeconomics focuses on the individual parts of the economy: How households and firms make decisions and how they interact in specific markets
- Macroeconomics looks at the economy as a whole. Economy-wide phenomena, including inflation, unemployment, and economic growth.

Let's Check Your Understanding!

Which of the following questions involve microeconomics, and which involve macroeconomics? In each case, explain your answer.

Why did consumers switch to smaller cars in 2019? This is a microeconomic question because it addresses decisions made by consumers about a particular product

Why did overall consumer spending slow down in 2019? This is a macroeconomic question because it addresses consumer spending in the overall economy

Why did the standard of living rise more rapidly in the current administration compared to previous administration? This is a macroeconomic question because it addresses changes in the overall economy

Why have starting salaries for students with geology degrees risen sharply of late? ……………………...

What determines the choice between rail and road transportation? …………………………………………..

Why has banana got cheaper over the past 20 years? …………………………………………..

10 PRINCIPLES OF ECONOMICS

The word economy comes from a Greek word for "One who manages a household."

Economists study:

- How people make decisions...
- How people interact with each other….
- The forces and trends that affect the economy as a whole.

How People Make Decisions: The four 4 principles of individual decision-making

1. **People face tradeoffs**

To get one thing; we usually have to give up another thing.

- Guns vs. Butter
- Food vs. Clothing
- Leisure Time vs. Work
- Efficiency vs. Equity

Efficiency	Equity
means getting the most you can from scarce resources	**Equity means benefits of resources are distributed fairly among society.**

2. **The Cost of Something Is What You Give Up to Get It**

Decisions require comparing costs and benefits of alternatives

- Going to university vs. going to work

Opportunity Cost: is what you give up from one alternative (choice) to get what you want (from another choice)

3. **Rational People Think at the Margin**

Marginal changes are small, incremental adjustments to an existing plan of action. Comparing extra benefits and costs of a critical choice
Marginal Benefits => MB
Marginal Costs => MC

4. **People Respond to Incentives**

Marginal changes in costs or benefits from decisions motivate people to respond. Decision to choose one good over another occurs when MB > MC.

How People Interact: (3 principles):

5. **Trade Can Make Everyone Better Off**

- Individuals gain from their ability to trade with others
- Competition results in gains from trading.

- Trade allows one to specialize in what they do best.

6. **Markets Are Usually a Good Way to Organize Economic Activity**

   - In a Market Economy, households and business firms determine what to buy, who to work for, who to hire and what to produce.
   - Interaction between household and business is as if by an "invisible hand."

7. **Governments Can Sometimes Improve Market Outcomes**

   Market failure results in inefficiency - failure of the "invisible hand."
   Market failure may be the result of of **an externality**, which is the impact of one person's actions on the well-being of a bystander. (Example: pollution)
   Market power is the ability of a single person or small group to unduly influence market prices.

When the market fails (breaks down) the government intervenes to: • promote Efficiency • promote Equity

How the Economy as a Whole Works: (3 principles) :

- ✓ A country's standard of living depends on its ability to produce goods and services.
- ✓ Prices rise when the government prints too much money.
- ✓ Society faces a short-run tradeoff between inflation and unemployment.

8. **Standard of living depends on a country's production.**

   Standard of Living may be measured in different ways (e.g. personal income or total market value of a nation's production.) Differences in standard of living between countries or even provinces is attributable to the **productivity** of the country or province.

   Productivity is the amount of goods and services produced from each hour of a worker's time.
   Productivity => Standard of Living

9. **Prices Rise When The Government Prints Too Much Money**

Inflation is an increase in the overall level of prices in the economy. One cause of inflation is the growth in the quantity of money.

10. **Society Faces a Short-Run Tradeoff Between Inflation and Unemployment**

    This tradeoff is called the Phillips Curve.