LGA Economics

**What is Economics? – January 15, 2015**

*Vocabulary and Notes*

Economics – A study of how individuals and societies make decisions in a world where the resources are limited

\*Also called the science of decision making – economics helps us think about the process of making decisions in a world where resources are limited

Needs – Things that are required for survival – food, clothing, and shelter

Wants – Things we would like to have – entertainment, vacations, or things that make life more comfortable and enjoyable

Scarcity – when we do not have enough resources to produce all the things we would like to have

\*Scarcity is the condition in which our wants are greater than the resources available to satisfy those wants

\*Even the United States doesn’t have enough productive resources to provide everything we would like to have (public transportation, education, national defense, entertainment, etc).

\*Choices have to be made. For example, a rational consumer compares prices and makes choices based on their limited resources when making purchases

\*The game of musical chairs is a visual example of the concept of scarcity because there aren’t enough chairs to go around

Economic Choices - There are three basic economic questions since resources are limited –

1. What to Produce?

2. How to Produce?

3. For Whom to Produce?

Economic Models – simplified representations of the real world that are used to explain how the economy works or predict what would happen if something in the economy should change

\*These models help in answering economic questions. However, these models are based on assumptions or things we take for granted as true. The models can be revised if proved to be wrong or used again if it turns out right.

Trade-Offs – the alternative you face if you decide to do one thing rather than another

1. Opportunity Cost – cost of the next best use of your time or money when you choose to do one thing rather than another \*More than money, includes discomforts and inconveniences linked to choice made (example - time lost)
2. Fixed Costs – Costs or expenses that are the same no matter what (example - mortgage payment)
3. Variable Costs – Costs that change with the number of products produced (in business raw materials can increase or decrease)
4. Total Costs – Variable plus fixed cost
5. Marginal Cost – Additional cost of producing one additional unit of output
6. Marginal Revenue – Additional cost of selling one additional unit
7. Marginal Benefit – the additional benefit associated with an action

Cost-Benefit Analysis – an economic model that compares the marginal costs and marginal benefits of a decision - Benefits should outweigh the costs

Market Economy – an economic system in which supply, demand, and prices help people make decisions and allocate resources

Capitalism – a system in which private citizens own most if not all, of the means of production

Free Enterprise – basis of a market economy because businesses are allowed to compete for profit with a minimum of government interference

Incentives – rewards that are offered to try to persuade people to take certain economic actions

\*How do economic incentives influence behavior?

\*Examples of Incentives include price, bonuses to salespeople, and low interest rates

Rational Choice – choosing the alternative that has the greatest value from among comparable-quality products \*Not always the same for everyone – based on the perceived value for an expense