

Chapter 1

- **Economics:** study of the choices people make to attain their goals given scarce resources
- **Scarcity:** unlimited wants exceed the limited resources available to fulfill those wants
- **Rationality assumption:** economists generally assume that people are rational - people use available info as they act to achieve goals - weigh costs and benefits
- **Fundamental questions:**
 - What goods and services will be produced?
 - How will the goods/services be produced?
 - Who will receive the goods/services produced?
- **Three key economic ideas**
 - People are rational
 - People respond to economic incentives
 - Optimal decisions are made at the margin
- **Marginal Analysis:** analysis that involves comparing marginal benefits and marginal costs
 - Economists use "marginal" to mean extra or additional
 - **Opportunity cost:** highest valued alternative that must be given up to engage in activity
- **Centrally planned economy:** gov't decides how economic resources will be allocated
- **Market economy:** decisions of households and firms interacting in markets allocate economic resources
- **Mixed Economy:** most economic decisions result from interaction of buyers and sellers in markets but gov't plays significant role in the allocation of resources
- **Efficiency and Equity:** there is often a tradeoff between efficiency and equity
 - **Productive efficiency:** good/service is produced at lowest possible cost

- o **Allocative efficiency:** production is in accordance with consumer preferences – in particular, every good/service is produced up to the point where the last unit provides a marginal benefit to society equal to the marginal cost of producing it
 - o **Equity:** the fair distribution of economic benefits
- **Scientific method & economic model**
 - o Method:
 - Decide on assumptions to use in developing model
 - Formulate a testable hypothesis
 - Use economic data to test the hypothesis
 - Revise the model if it fails to explain the economic data well
 - Retain the revised model to help answer similar economic questions in the future
 - o **Economic variable:** something measurable that can have different values, such as the incomes of doctors
- **Positive analysis:** concerned with what is
- **Normative analysis:** concerned with what ought to be
- **Microeconomics:** study of how households and firms make choices, how they interact in markets, and how the gov't attempts to influence their choices
- **Macroeconomics:** the study of the economy as a whole, including topics such as inflation, unemployment, and economic growth

Chapter 2

- **Production possibilities frontier:** curve showing max attainable combinations of two products that may be produced with available resources and current technology
- **Opportunity cost:** highest valued alternative that must be given up to engage in activity
- **Increasing marginal opportunity costs:** bowed outward PPF; occurs because some workers, machines and other resources are better suited to one use than another

- **Economic growth:** the amount of physical capital available in the country increases
- **Specialization and gains from trade (see trade example on ipad)**
 - **Absolute advantage:** ability of an individual, firm or country to produce more of a good or service than competitors using the same amount of resources
 - **Comparative advantage:** ability to produce good/service at a lower opportunity cost than competitors
 - Basis for trade
 - Specialize in something when you have the comparative advantage and then trade
- **Market:** group of buyers/sellers of a good/service and the institution or arrangement by which they come together to trade
 - **Product market:** market for goods and services
 - Households are demanders, firms are suppliers
 - **Factor market:** market for the factors of production (labor, capital, natural resources, and entrepreneurial activity)
- **Circular flow diagram** (see ipad)
- **Legal basis of market system**
 - **Property rights:** rights that individuals/firms have to the exclusive use of their property, including the right to buy or sell it
 - **Intellectual property rights**

CHAPTER 3

- **Law of demand:** ceteris parabis, when the price of a product falls, the qty demanded of the product will increase and vice versa
- **Quantity demanded:** amount of a good/service a consumer is willing & able to purchase at a given price
- **Market demand:** demand by all the consumers of a given good or service
- **Variables that shift demand**
 - Income