Macroeconomics©

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Chapter 1 - Limits, Alternatives and Choices

The Economic Perspective

- **Wants** - nice house, car, vacation ....
- **Needs** - food, shelter, water, air, clothing .... versus
- In order to satisfy the above, the economy uses **resources** - land, labor, tools, mineral deposits .... to produce goods and services.
- **Economic system or economy** - The organizational mechanism by which we accomplish the satisfying of needs and wants is called the economic system.
- **There is no free lunch** - Because there is scarcity, there is always an opportunity cost - someone always has to pay.
- **Opportunity cost** - to get more of a product you have to give up some of the other.
- **Utility** - the pleasure, happiness, or satisfaction obtained from consuming a good or service.
- **Marginal analysis** - Marginal benefit vs. marginal cost (Marginal = Extra)

Theories, Principles, and Models

- The methodology of economics is the **scientific method**.
- Data hypothesis ➠ testing of the hypothesis ➠ acceptance/rejection of the hypothesis ➠ continued testing of the hypothesis ➠ continued favorable results ➠ **theory**
- A widely accepted theory is a **law/principle**
- Combinations of laws/principles are **models**. Economic laws and principles are usually less certain than the laws of physics!
- The process of deriving theories and principles is called **theoretical economics**.
- In constructing theories, economists use the *Ceteris Paribus* or **other things equal** assumption. All variables held constant except those under consideration.

Microeconomics vs Macroeconomics

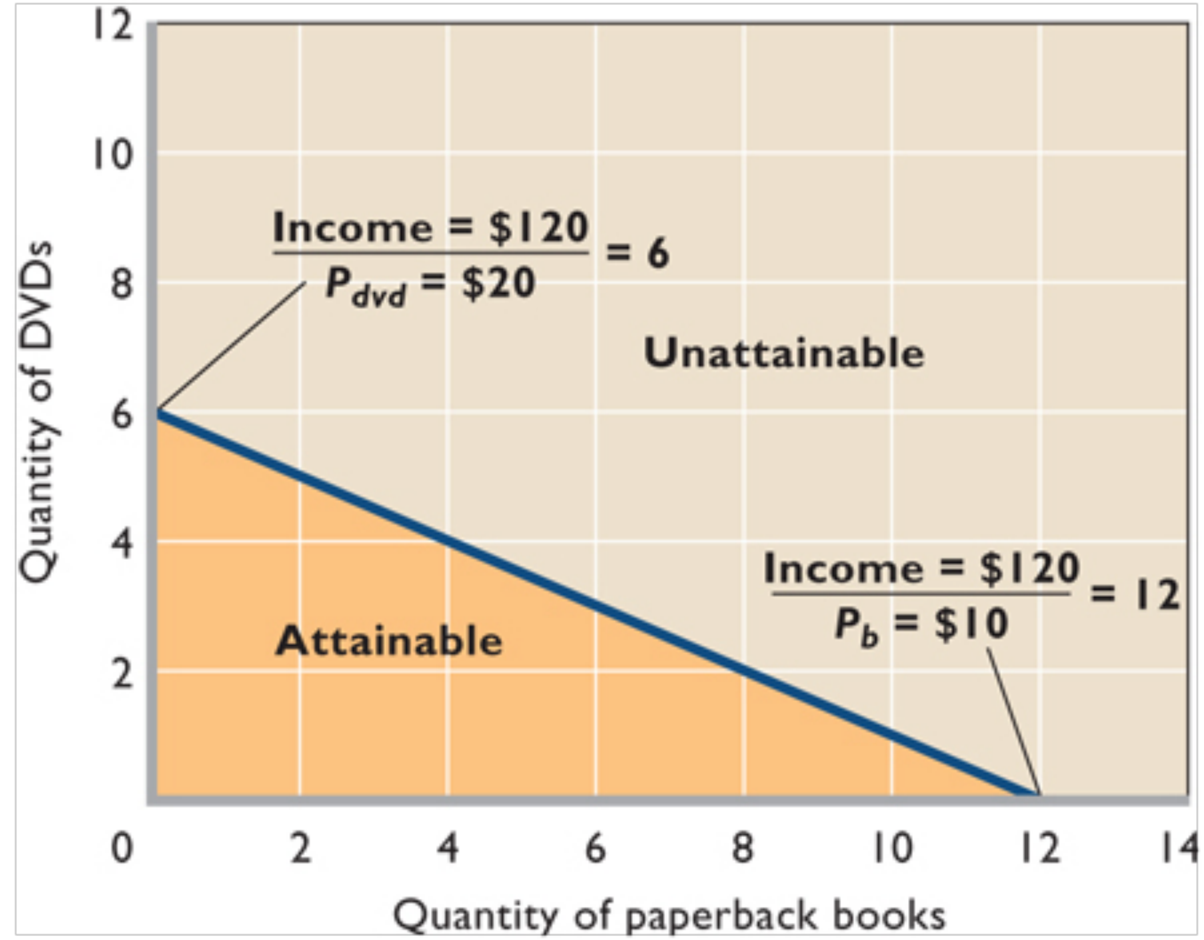
- **Microeconomics** - details of an economic unit
- **Macroeconomics** - examines the economy as a whole or its basic aggregates such as the government, household or business unit
- **Positive economics** - focuses on facts and cause and effect
- **Normative economics** - incorporates value judgements, what the economy should be

Individuals' Economizing Problem

Limited income vs unlimited wants

A Budget Constraint

It is a schedule or a curve that shows various combinations of two products a consumer can purchase with a specific money income.



The Budget Line: Whole-Unit Combinations of DVDs and Paperback Books Attainable with an Income of $120		
Units of DVDs (Price = $20)	Units of Books (Price = $10)	Total Expenditure
6	0	($120 = $120 + $0)
5	2	($120 = $100 + $20)
4	4	($120 = $80 + $40)
3	6	($120 = $60 + $60)
2	8	($120 = $40 + $80)
1	10	($120 = $20 + $100)
0	12	($120 = $0 + $120)

Society's Economizing Problem

Society has limited or scarce **economic resources - land, labor, capital and entrepreneurial ability**

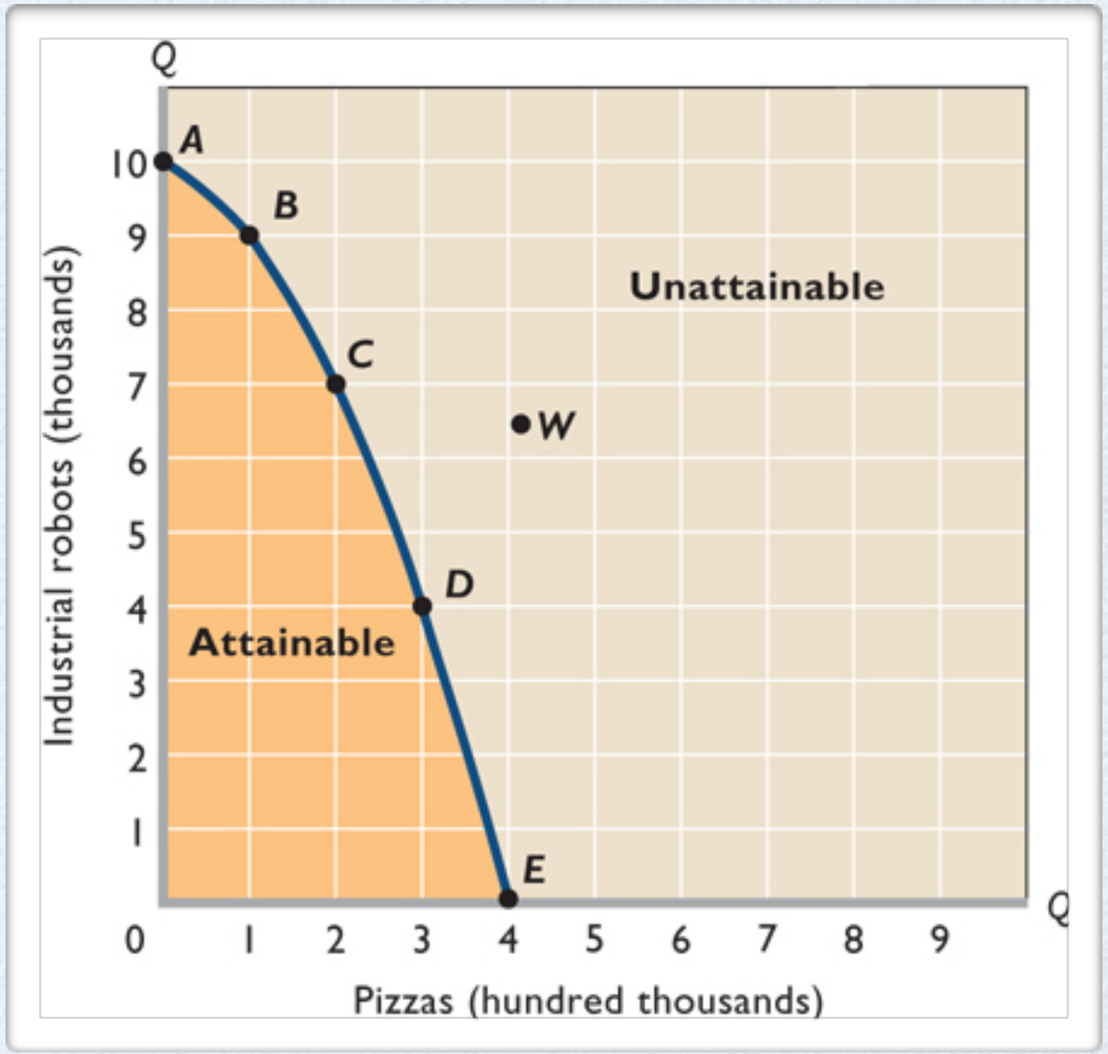
Production Possibilities Model

Assumptions:

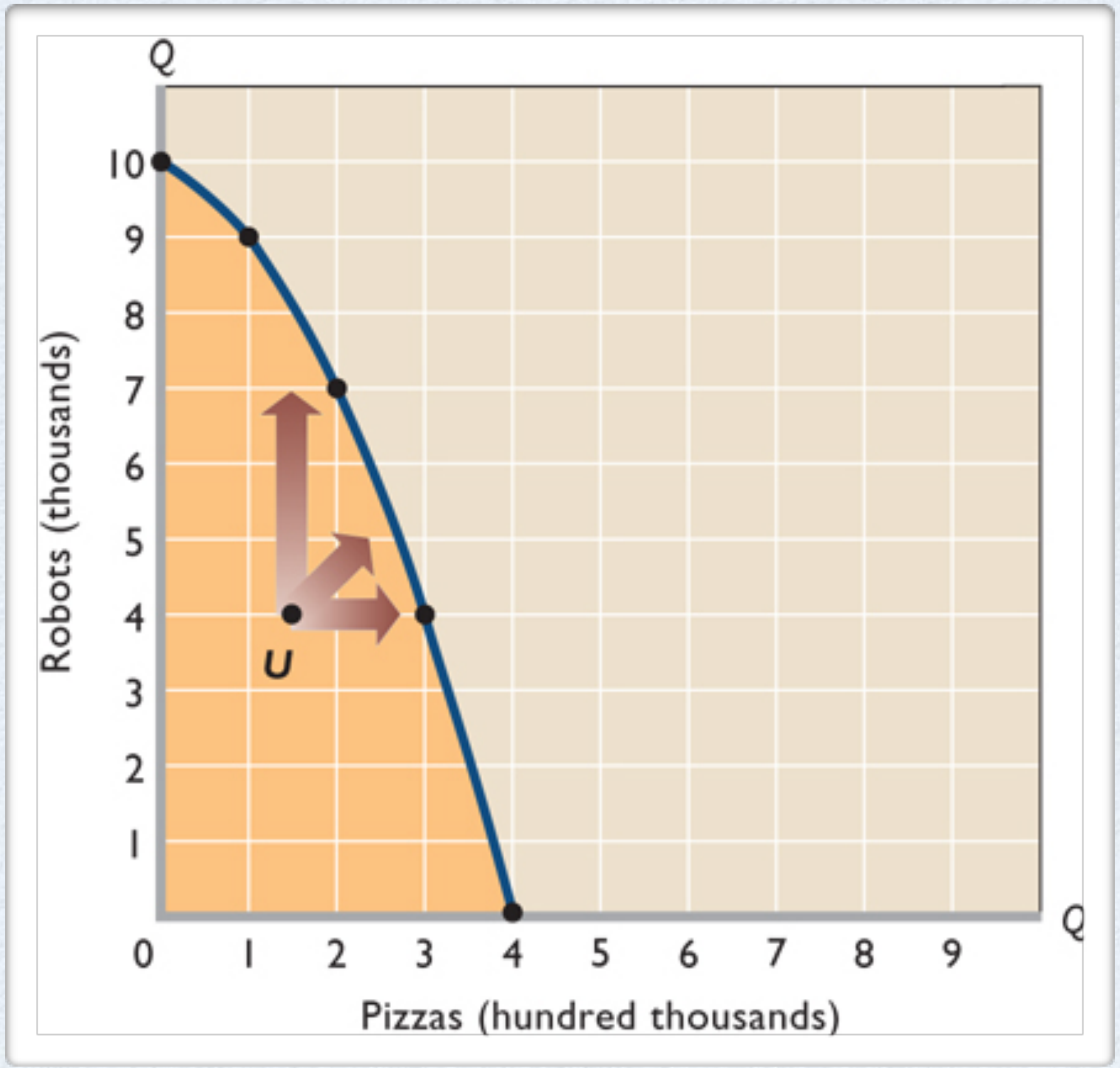
Full employment, fixed resources, fixed technology, two goods - consumer and capital goods

Production possibilities curve

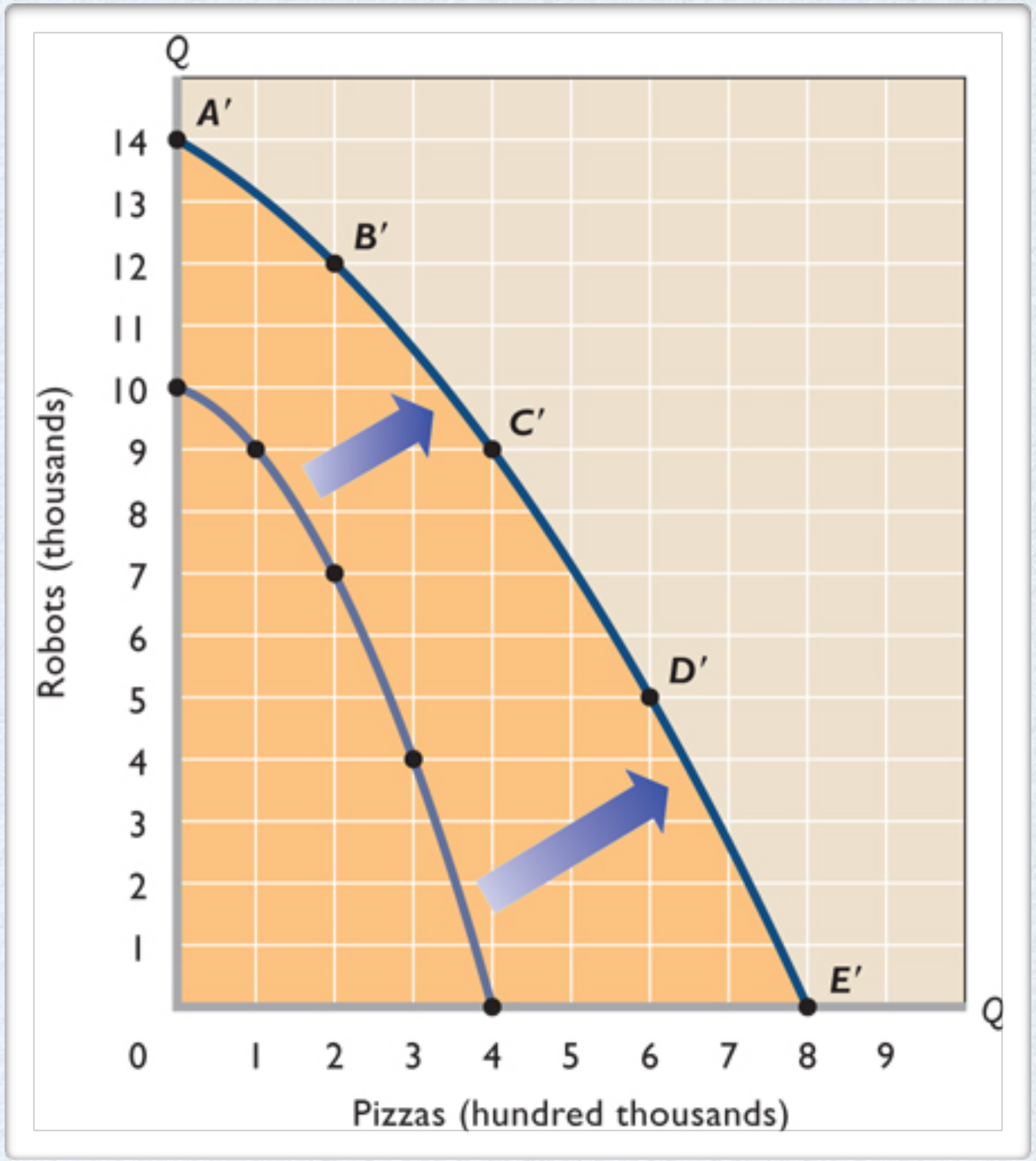
Law of increasing opportunity cost - as the production of a particular good increases, the opportunity cost of producing an additional unit rises.



Unemployment, Growth and the Future



A growing economy



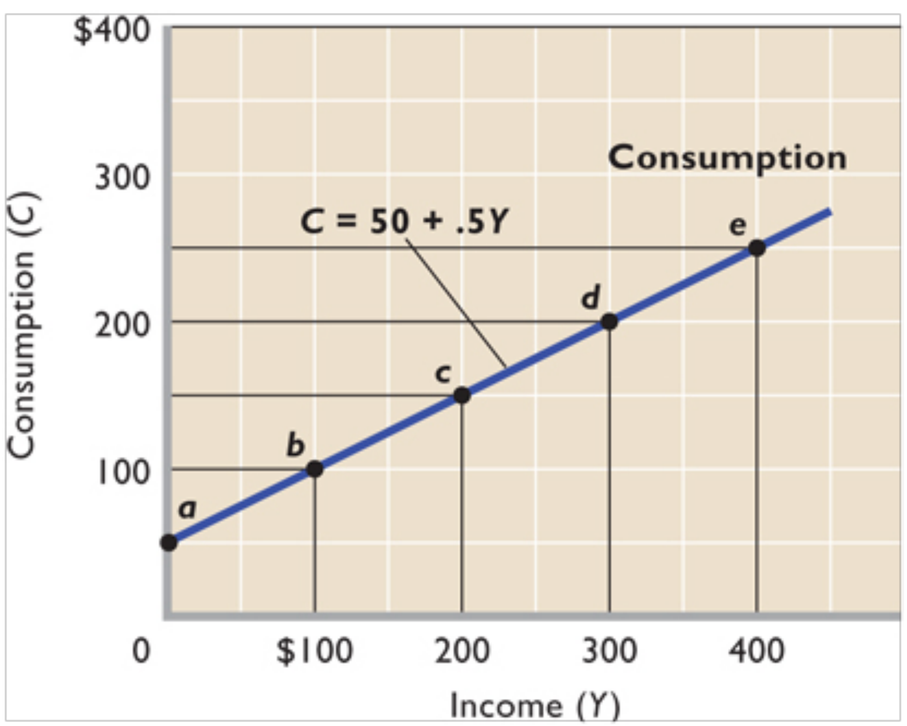
Appendix 1 -Graphs and their meaning

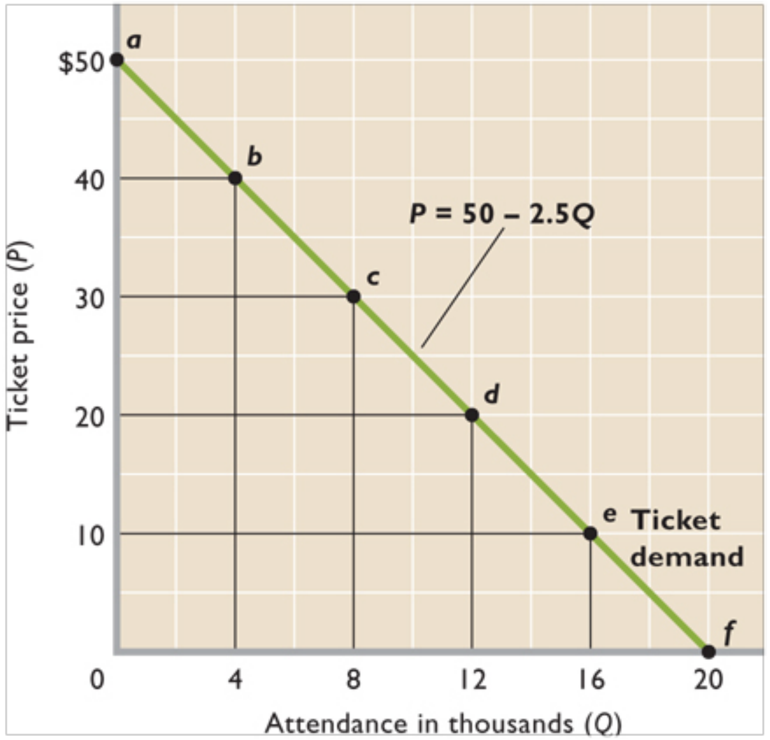
Construction of a graph

Direct vs indirect relationship - Dependent vs independent variables

Income per Week	Consumption per Week	Point
$ 0	$ 50	*a*
100	100	*b*
200	150	*c*
300	200	*d*
400	250	*e*

Ticket Price	Attendance, Thousands	Point
$50	0	*a*
40	4	*b*
30	8	*c*
20	12	*d*
10	16	*e*
0	20	*f*

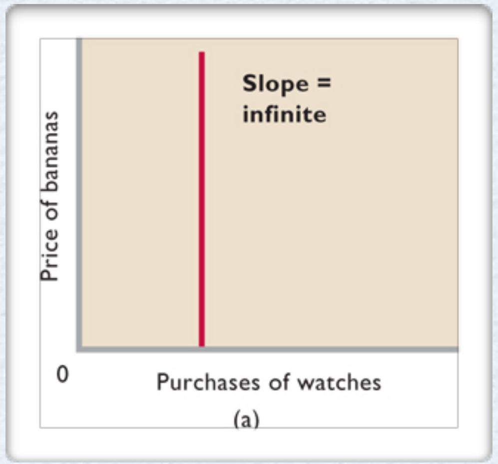


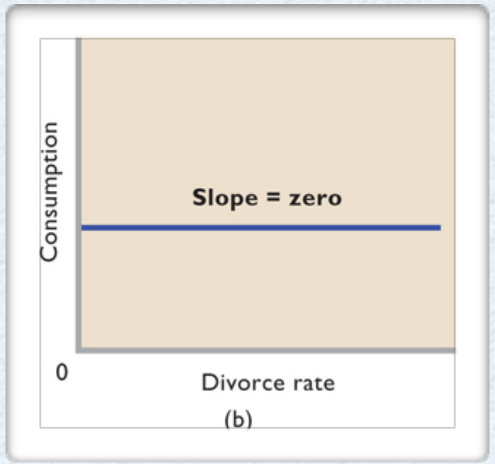


Construction of a graph

Positive Slope - Slope = vertical change/horizontal change = 50/100 = 1/2 = 0.5

Negative Slope - Slope = vertical change/horizontal change = -10/4 = -2.5





Slopes and marginal analysis

$y = mx + b$ ➟ equation of a line

y = dependent variable, m = slope of the line, x = independent variable, b = vertical intercept

$$C = 50 + 0.5Y$$

Slope = 0.5 ➟ \$0.50 of extra or marginal consumption is associated with each \$1 change in income.

$$P = 50 - 2.5Q$$

Slope of a Nonlinear Curve