

KEY TAKEAWAYS 1

Chapter 1 : The challenge of Economics

A- Importance of Economics

- Economics also allows individual agents to balance expectations.
- Economics provides distilled frameworks to analyze complex societal interactions, as in the case of consumer and firm behavior.
- Being knowledgeable about economics foundations allows an individual to be an active and aware participant rather than a passive economic agent.

- Economics is a social science. This means that economics has two important attributes. Economics studies human activities and constructions in environments with scarce resources, and uses the scientific method and empirical evidence to build its base of knowledge.
- The evaluation of human interactions as it relates to preferences, decision making, and constraints is a significant foundation of economic theory. The complexity of the dynamics of human motivation and systems has led to the establishment of assumptions that form the basis of the theory of consumer and firm behavior, both of which are used to model circular flow interactions within the economy.

- By developing an understanding of the foundations of economics, individuals can become better decision makers with respect to their own lives and maintain a balance with respect to an externality that has the potential to supplement or deter their plans.
- Since economic theories are a basis of decision making and regulatory policy, being knowledgeable about economics

foundations allows an individual to be an active and aware participant rather than a passive economic agent.

I- Is Economics a Science?

Economics is a **social science** that has diverse applications.

Key Points

- Economics incorporates both qualitative and quantitative assessment.
- Economics is divided into two broad areas: microeconomics and macroeconomics.
- Economics can be applied throughout society from business to individual behavior with further application in the study of crime, family and other social institutions and interactions.

II- Scarcity Leads to Tradeoffs and Choice

Key Points

- Scarce resources diminish as they are used and almost all resources are scarce.
- In order to use a scarce resource, you are inherently using the resource for one purpose and not an alternative.
- The cost of using a resource is called the opportunity cost: the value of the next best alternative that you could be using the resource for instead.

III- Ceteris Paribus

Ceteris paribus is defined as “all else being equal,” or “holding all else constant”.

Key Points

- When ceteris paribus is employed in economics, all other variables with the exception of the variables under evaluation are held constant.
- An example of the use of ceteris paribus in macroeconomics is: what would happen to the demand for labor by firms if a minimum wage was imposed at a level above the prevailing wage rate, ceteris paribus.
- An example of the use of ceteris paribus in microeconomics is: what would happen for the demand for a normal good when income increases, ceteris paribus.

IV- Individuals Face Opportunity Costs

- Individuals face opportunity costs when they choose one course of action over another.

Key Points

- The opportunity cost is the value of the next best alternative foregone.
- Every decision necessarily means giving up other options, which all have a value.
- The opportunity cost is the value one could have derived from using the same resources another way, though this is not always easily quantifiable.

Opportunity Cost : By choosing to go to spend time and money things like classes and computers, you are necessarily choosing not to spend it on something else, like going on vacation. This is an opportunity cost.

- Rational individuals will try to minimize their opportunity costs. By doing so, individuals are maximizing the amount that they can get out of their resources (time, money, effort, etc.). This makes sense: individuals should seek to get the most and give up the least.

B- Differences Between Macroeconomics and Microeconomics

I- Macroeconomics

Key Points

- For most macroeconomists, the purpose of this discipline is to maximize national income and provide national economic growth.
- The most common macroeconomic topics of study for national entities are sustainability, full employment, price stability, external balance, equitable distribution of income and wealth, and increasing productivity.

II- Microeconomics

- Microeconomics deals with the economic interactions of a specific person, a single entity or a company; it is the study of markets

Key Points

- One of the major goals of microeconomics is to analyze the market and determine the price for goods and services that best allocates limited resources among the different alternative uses.
- Microeconomics assumes businesses are rational and produce goods that maximize their profit.
- The science of microeconomics covers a variety of specialized areas of study including: industrial organization, labor economics, financial economics, public economics, political economy, health economics, urban economics, law and economics, and economic history.

III- Key Differences between Microeconomics and Macroeconomics

- **Microeconomics** focuses on individual markets, while macroeconomics focuses on whole economies.

Key Points

- Microeconomics and macroeconomics both focus on the allocation of scarce resources. Both disciplines study how the demand for certain resources interacts with the ability to supply that good to determine how to best distribute and allocate that resource among many consumers.
 - Microeconomics studies the behavior of individual households and firms in making decisions on the allocation of limited resources. Another way to phrase this is to say that microeconomics is the study of markets.
 - **Macroeconomics** is generally focused on countrywide or global economics. It studies involves the sum total of economic activity, dealing with the issues such as growth, inflation, and unemployment.
 - There are some economic events that are of great interest to both microeconomists and macroeconomists, but they will differ in how and why they analyze the events.
-
- Stemming from **Adam Smith**'s seminal book, *The Wealth of Nations*, microeconomic and macroeconomics both focus on the allocation of scarce resources.
 - Both disciplines study how the demand for certain resources interacts with the ability to supply that good to determine how to best distribute and allocate that resource among many consumers.
 - Both disciplines are about maximization: microeconomics is about maximizing profit for firms, and surplus for consumers and producers, while macroeconomics is about maximizing national income and growth.

IV- The different Economic actors in an economy

- Economic actors refer to the participants in economic activities in an economy.
- They use productive resources and interact with each other with their respective motives and compensation, involving the flow of goods and income.
- Synonym market participants are economic agents.

