



Basic Terminology in Economics

TUI University

What is economics?

It's the study of the choices people and institutions make about scarce resources

Society's wants exceed the resources available to satisfy them

Everybody faces scarcity to some degree

Thus, we're all interested in the choices we make

Five big economic questions

What?

How?

When?

Where?

Who?

What?

What goods and services are produced, and in what quantities?

Guns or butter?

How?

How are goods and services produced?

Humans or machines?

When?

When are goods and services produced and consumed?

Increase or decrease production?

Speed up or slow down consumption?

Where?

Where are goods and services produced?

US or abroad?

Large or small facilities?

Who?

Who consumes goods and services?

Rich or poor?

Big Ideas of Economics

Idea 1:

Choices involve tradeoffs – we always give something up to get something else

Big Ideas of Economics

Idea 2:

We make choices in small steps, and choices involve incentives

Big Ideas of Economics

Idea 3:

Voluntary exchange makes both sellers and buyers better off, and markets are an efficient way to organize that exchange

Big Ideas of Economics

Idea 4:

The market doesn't always work efficiently; then,
government action may be needed

Big Ideas of Economics

Idea 5:

For the economy as a whole, expenditure equals
income equals the value of production

Big Ideas of Economics

The overall burden:

How people approach the choices they make about resources matters A LOT to our lives – and we'd better understand what's going on

Macro vs. Micro

MICROeconomics is about individual people and companies and how their choices and decisions interact

MACROeconomics is about how choices affect societies and the world generally

Positive vs. Normative Economics

Positive statements are about what *is*

- Can be proven right or wrong

- Can be tested with facts

Normative statements are about what *ought to be*

- Depends on personal values

- Cannot be tested as such

Economics is about words

The body of experience is yours

The question is how you describe it to understand it

Importance of vocabulary

Words are used in specialized senses

It's important to understand precise definitions

That's what distinguishes economics from muddling through

Now let's define some terms...

What follows is some of the terminology near and dear to the hearts of economists

We'll be using these terms a lot in this course, so you need to understand them well

Remember, they're not always used in quite the way we'd ordinarily use them

Resources

Things you need to survive and thrive

There aren't enough of them to go around – hence,
scarcity is a fact of life

Categories of resources

Land (natural resources)

Labor (human resources)

Capital

Produced goods that can be used as inputs to further production

Entrepreneurship

Sometimes called “human capital”

Choice and tradeoff

There are different things you can do

Whatever you do means that you can't do something else

Utility / Value

A measure of the satisfaction, happiness, or benefit resulting from the use of a resource

Implies substitutability – the idea that one thing might be taken rather than another if it produces the same value

Cost

What you give up in order to acquire a resource

May be either material or nonmaterial

Opportunity cost

What you give up to acquire a *particular* resource

That is, what's the value of what you can't buy
because you bought something else

Indifference

The point at which your cost and your opportunity cost are equal

That is, both choices give you equal utility

Marginality

The idea that what matters is less the value of the absolute amount of something than the value of the *next amount* of it

Marginal cost

The cost of acquiring the *next* unit of something I have or want

Marginal utility

The value to me of acquiring the next unit of something I have or want

Production

The creation of useful goods and/or services by the application of human ingenuity to nature's stuff

(not quite a technical definition, but you get the idea...)

Technology

The body of skills and knowledge concerning the use of resources in production

May be physical or conceptual

Efficiency

The condition in which maximum output is produced with given resources and technology

Implies the possibility of gains in one area without losses in another

Optimality

Doing the best we can within our constraints

Usually something less than the maximum
theoretically possible

Supply

The willingness and ability of sellers to produce and offer to sell different quantities of a resource at different prices during a given period

Demand

The willingness and ability of buyers to purchase different quantities of a resource at different prices during a given period

Price

What buyers and sellers are willing to exchange in order to compensate each other for a transfer of resources from one to another

Implies that there is a unit of measurement comparable across transactions

Equilibrium

The point at which supply and demand are equal

Neither buyers nor sellers have any reason to change their positions

Money

A unit of measurement comparable across transactions

(surprise!)

Market

A place where buyers and sellers come together to carry out exchanges

May be physical or conceptual

Even virtual (I.e., E-Bay)

Elasticity

The degree to which either supply or demand can vary across time or space

Assumptions

Things we agree on as a basis for discussion

Often we don't even talk about them

Sometimes a problem...

Model

A simplified expression of the relationships among phenomena

Usually based on a number of assumptions

But the map is not the territory...

Ceteris Paribus: Other things being equal

An important assumption in most economic models

Never literally true

But functionally, maybe...

Consequences

What happens as a result of something we do

May be short or long term

Visible or invisible

Unintended consequences

The things that happen that we didn't plan on

(i.e., most of life...)

So – where does this leave us?

More or less ready to try thinking like economists

With a lot left to learn and think about

And a lot more language to acquire and learn to use...