Chapter 1: The Scope and Method of Economics

Week 2

Presenter:Zheng Zhang

Jan 25, 2012

Table of Contents

Questions

- what is economics?(twice *2011 Midterm I M1*;2011Fin M1)
- What is opportunity cost?(4 times)
  (*PEQ1 Part 1*; *2012 Mid I M2*; *2011 Mid I M4*; 2010Mid1 M40; *2011Fin M2*)
- What is sunk cost ?(*PEQ1 part2*; 2011 Mid1 M2)
- What is marginal cost?(*2011 Mid I M5*)
- What is efficient market?(*2012 Mid I M4*)
- Why do you think opportunity cost is important in the economic way of thinking?

Economics:Definition

2011 Midterm I M1 Page 203;2011Fin M1Page 289
Economics is best defined as the study of:

A financial design-making

B how consumers make purchasing decision

C inflation,unemployment, and economic growth

D choices made by people faced with scarcity

Back

Economics:Definition

2011 Midterm I M1 Page 203

Economics is best defined as the study of:

A A topic in Micro

B A topic in Micro

C Concerns of Macro

D Right Answer!

Back

Trade-off

Figure 1: Choice between A and B

Opportunity Cost

Figure 2: What is the opportunity cost of studying hard (playing Video Games)?

Opportunity Cost

2012 Midterm I M2 Page 191; 2011 Mid I M4 Page 203

Opportunity cost can be best defined as:

A the value of the best alternative given up when making a choice.

B the cost of making one additional unit.

C the cost of finding profitable opportunities.

D sunk costs

E the explicit cost of an action.

Back

Opportunity Cost

2012 Midterm I M2 Page 191; 2011 Mid I M4 Page 203

Opportunity cost can be best defined as:

A the value of the best alternative given up when making a choice.

B the cost of making one additional unit.

C the cost of finding profitable opportunities.

D sunk costs

E the explicit cost of an action.

Back

Opportunity Cost: Application

PEQ 1 part 1Page 159

- Q:Why would an economist argue that tuition is not the largest cost of attending a state university?
-

Back

Opportunity Cost: Application

PEQ 1 part 1Page 159

- Q:Why would an economist argue that tuition is not the largest cost of attending a state university?
- A:The largest cost of attending a university is the **opportunity cost** of the student's time. This could be measured by the forgone income that could have been earned if the student worked instead of attending classes.

Back

Opportunity Cost: Application

2011 Mid I M4 Page 203

Which of the following is an opportunity cost of attending college?

A the income you could have earned if you didn't attend college

B the cost of your apartment or dorm

C the cost of the food that you consume while you are attending college

D all of the above

Back

Opportunity Cost: Application

2011 Mid I M4 Page 203

Which of the following is an opportunity cost of attending college?

A the income you could have earned if you didn't attend college

B the cost of your apartment or dorm

C the cost of the food that you consume while you are attending college

D all of the above

Back

Opportunity Cost: Application

2011Fin M2 Page 289
You own Kil Bill on DVD. The opportunity cost of watching this DVD for the third time

A is the value of the alternative use of the time you spend watching the DVD

B must be the same as the opportunity cost of watching it the first time.

C is one-third the cost of the DVD, as this is the third time you have watched it.

D is zero,since you own it.

Back

Opportunity Cost: Application

2011Fin M2 Page 289
You own Kil Bill on DVD. The opportunity cost of watching this DVD for the third time

A is the value of the alternative use of the time you spend watching the DVD

B must be the same as the opportunity cost of watching it the first time.

C is one-third the cost of the DVD, as this is the third time you have watched it.

D is zero,since you own it.

Back

Sunk Cost

PEQ 1 part 2 Page 159

- Q: Suppose that you have purchased a round trip ticket to the Bahamas for spring break. The ticket is non refundable and cannot be changed. Your best friend tells you that she is getting married during the same week in Chicago (where you live) and has asked you to be in the wedding party. Does the price you paid for your Bahamas trip matter in your decision of whether to go to the Bahamas or Chicago? Why or why not?
-

Back

Sunk Cost

PEQ 1 part 2 Page 159

- Q: Suppose that you have purchased a round trip ticket to the Bahamas for spring break. The ticket is non refundable and cannot be changed. Your best friend tells you that she is getting married during the same week in Chicago (where you live) and has asked you to be in the wedding party. Does the price you paid for your Bahamas trip matter in your decision of whether to go to the Bahamas or Chicago? Why or why not?
- A: It should not matter because the plane ticket is a **sunk cost**. No matter what decision you make, you will have to pay for the ticket to the Bahamas. Thus, the only thing that should factor into your decision is how much enjoyment you would gain out of the two alternatives.

Back

Marginal Cost

2011 Mid I M5 Page 203

If you eat at a pizza parlor that charges $5 for its all-you-can-eat buffet, then the marginal cost of your 5th slice of pizza is

A $25

B zero

C $1

D $5

Back

Marginal Cost

2011 Mid I M5 Page 203

If you eat at a pizza parlor that charges $5 for its all-you-can-eat buffet, then the marginal cost of your 5th slice of pizza is

A $25

B zero

C $1

D $5

Back

Opportunity Cost vs Marginal Cost vs Sunk Cost

- Opportunity cost: the cost you think about when comparing choices
- Sunk cost: could not be avoided because it has been incurred
- Marginal Cost: additional cost of consuming or producing one more unit of goods or services

Efficient Market

2012 Midterm I M4 Page 191

Efficient markets are those in which

A buyers and sellers do not face opportunity costs.

B many people search for profit opportunities such that these opportunities are almost instantaneously eliminated.

C consumers and firms consider sunk costs in their decisions to buy and produce, respectively.

D buyers and sellers face difficulties in finding each other.

E profit opportunities never exist.

Efficient Market

2012 Midterm I M4 Page 191

Efficient markets are those in which

A buyers and sellers do not face opportunity costs.

B many people search for profit opportunities such that these opportunities are almost instantaneously eliminated.

C consumers and firms consider sunk costs in their decisions to buy and produce, respectively.

D buyers and sellers face difficulties in finding each other.

E profit opportunities never exist.

Table of Contents

Questions

- What's the difference between Positive and Normative Economics?
  (5 times) (*2012Mid1 M1 Page 191*;2011 Mid1 M3 Page 203;2010Mid1 M3 Page213;2011Fin M3 Page 289;2010Fin M36)
- What does Positive economics include?
- What is a model?*2012 Midterm I M5*
- What is post hoc Fallacy? (*PEQ1 part 3 2012 Midterm I M3*; 2010Mid1 M4)
- What is fallacy of composition?

Method of Economics

2012 Midterm I M5 Page 191

Which statement is not true regarding the method of economics?

A Positive economics includes descriptive economics and economic theory.

B A model is a formal statement of a theory.

C Models should contain details that are irrelevant to understand certain behavior.

D An economic theory should avoid the fallacy of composition.

E Empirical economics can be used to test economic theories.

Back

Method of Economics

2012 Midterm I M5 Page 191

Which statement is not true regarding the method of economics?

A Positive economics includes descriptive economics and economic theory.

B A model is a formal statement of a theory.

C Models should contain details that are irrelevant to understand certain behavior.

D An economic theory should avoid the fallacy of composition.

E Empirical economics can be used to test economic theories.

Back

Normative vs Positive Economics

2012 Midterm I M1 Page 191
Which of the following is a normative statement?

A companies earn profits from the sale of prescription drugs.

B Hospital bills are greater in Canada than in the United States.

C Health care costs too much.

D Hospitals are under increasing pressure to cut costs.

E All of these.

Back

Normative vs Positive Economics

2012 Midterm I M1 Page 191
Which of the following is a normative statement?

A companies earn profits from the sale of prescription drugs.

B Hospital bills are greater in Canada than in the United States.

C Health care costs too much.

D Hospitals are under increasing pressure to cut costs.

E All of these.

Back

Post hoc Fallacy

PEQ 1 part 3 Page 159

- Q:A policymaker in a less developed nation sees that citizens of wealthy nations spend a lot of time on the Internet. He, therefore, proposes to have every household in his nation wired to the Internet to make them wealthier. How do you react to this proposal?
-

Back

Post hoc Fallacy

PEQ 1 part 3 Page 159

- Q:A policymaker in a less developed nation sees that citizens of wealthy nations spend a lot of time on the Internet. He, therefore, proposes to have every household in his nation wired to the Internet to make them wealthier. How do you react to this proposal?
- A: This proposal suffers from the **post hoc fallacy**. Our nation's output did increase after and during the growth of Internet usage. Both phenomena, however, were caused by other factors such as an increase in technology.

Back

Post hoc Fallacy

2012 Midterm I M3 Page 191
The Post Hoc Fallacy is defined as:

A the error of mistakenly assuming that an event caused the other because it happened after.

B the error of mistakenly assuming that an event caused the other because it happened before.

C the error of assuming that two variables are correlated when they are not.

D the error of assuming that correlation implies causation.

E None of the above.

Back

Post hoc Fallacy

2012 Midterm I M3 Page 191
The Post Hoc Fallacy is defined as:

A the error of mistakenly assuming that an event caused the other because it happened after.

B the error of mistakenly assuming that an event caused the other because it happened before.

C the error of assuming that two variables are correlated when they are not.

D the error of assuming that correlation implies causation.

E None of the above.

Back