Module 1 — Key Concepts (Ch. 1)

Big Picture: What is Economics?

- **Economics** studies how individuals and societies **choose** to allocate **scarce** resources, **why** they make those choices, and the **consequences** of those choices.
- **Microeconomics** focuses on individual decision-making and small units (people, firms, markets).

Ch. 1 - Core Principles of Decision Making

1. Cost–Benefit Principle

- **Do something if** the **benefit > cost**.
- Always compare marginal benefit to marginal cost for decisions.

2. Opportunity Cost Principle

- **Opportunity cost:** The value of the **next best alternative** you give up when making a choice.
    - Important: *only* the next best option counts, not every possible forgone alternative.

3. Marginal Principle (Marginal Analysis)

- Decisions are made **at the margin**: ask whether the **additional** unit's benefit exceeds its cost.

4. Interdependence Principle

- Choices depend on other changing conditions (prices, weather, incomes, tastes).
- We often hold other things constant (*ceteris paribus*) but remember they can change.

Common Mistakes (Decision Errors)

1. Ignoring **unintended consequences**.
2. Confusing **correlation** with **causation**.
3. **Fallacy of composition**: assuming what’s best for one is best for all.
4. **Sample-selection/self-selection bias** in inference.