

# ECO 2013 – Principles of Economics (Macro)

PREFACE X

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# X. What is Economics: Unraveling the Science of Choice

Have you ever wondered why some products are more expensive than others, or how governments decide on policies that affect millions of people?

Welcome to the fascinating world of economics! This field of study is far more than just money and business-it's about understanding how people, businesses, and societies make decisions in a world of limited resources.

As we explore the basics of economics, you'll discover how it shapes nearly every aspect of our daily lives and influences the future of our global community.

The infographic features a central balance scale. The left pan is lower and holds a red box with the text 'We have unlimited wants'. The right pan is higher and holds a blue box with the text 'Resources to satisfy these wants are limited'. Above the scale, the word 'Scarcity' is written in large red letters, followed by 'DESIRE' in a black box. Below the scale, a cartoon man with his hands outstretched looks up at the imbalance. To the left of the scale is a cartoon emoji with a wide, happy mouth, and to the right is a cartoon emoji with a thoughtful expression, hand on chin, with palm trees in the background.

## Unlimited Wants

*People never get enough. We always want or need more.*

# Scarcity

**DESIRE**

*The basic economic problem we all face is scarcity.*

**We have unlimited wants**

**Resources to satisfy these wants are limited**

## The Essence of Economics

At its core, economics is the study of scarcity and choice. But what does that really mean? Imagine you have \$20 to spend on a Friday night. You could go to the movies, treat yourself to a nice dinner, or save it for something more special. The fact that you can't do all three with your limited budget is an example of scarcity.



Economics helps us understand how individuals, businesses, and entire nations make decisions when faced with limited resources and unlimited wants. This concept of scarcity is fundamental to economics because it forces us to make choices. If we had unlimited resources, we could have everything we wanted, and there would be no need for economics.

**How does the federal government spend our money? Before we begin, what presuppositions do we bring to this conversation?**

- **How does the federal government raise revenue?**
- **Where do you think the federal government spends most of this revenue?**
- **Where do you think the federal government SHOULD spend this revenue?**

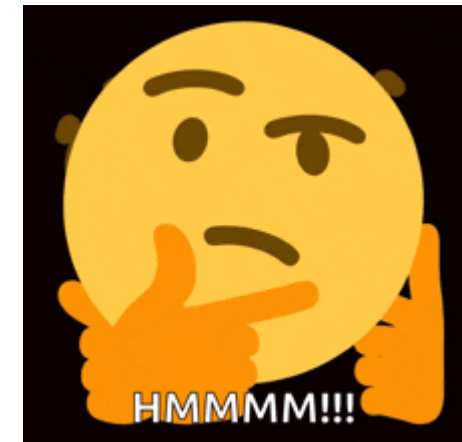
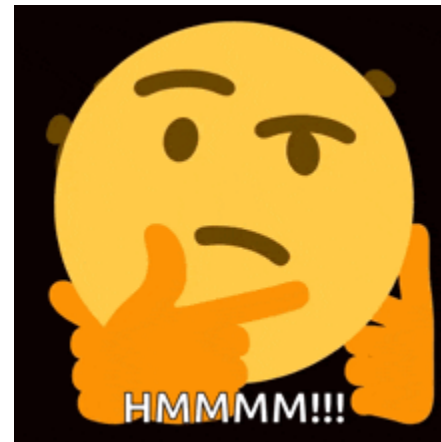
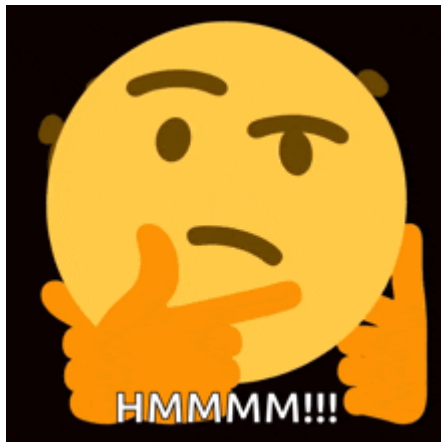
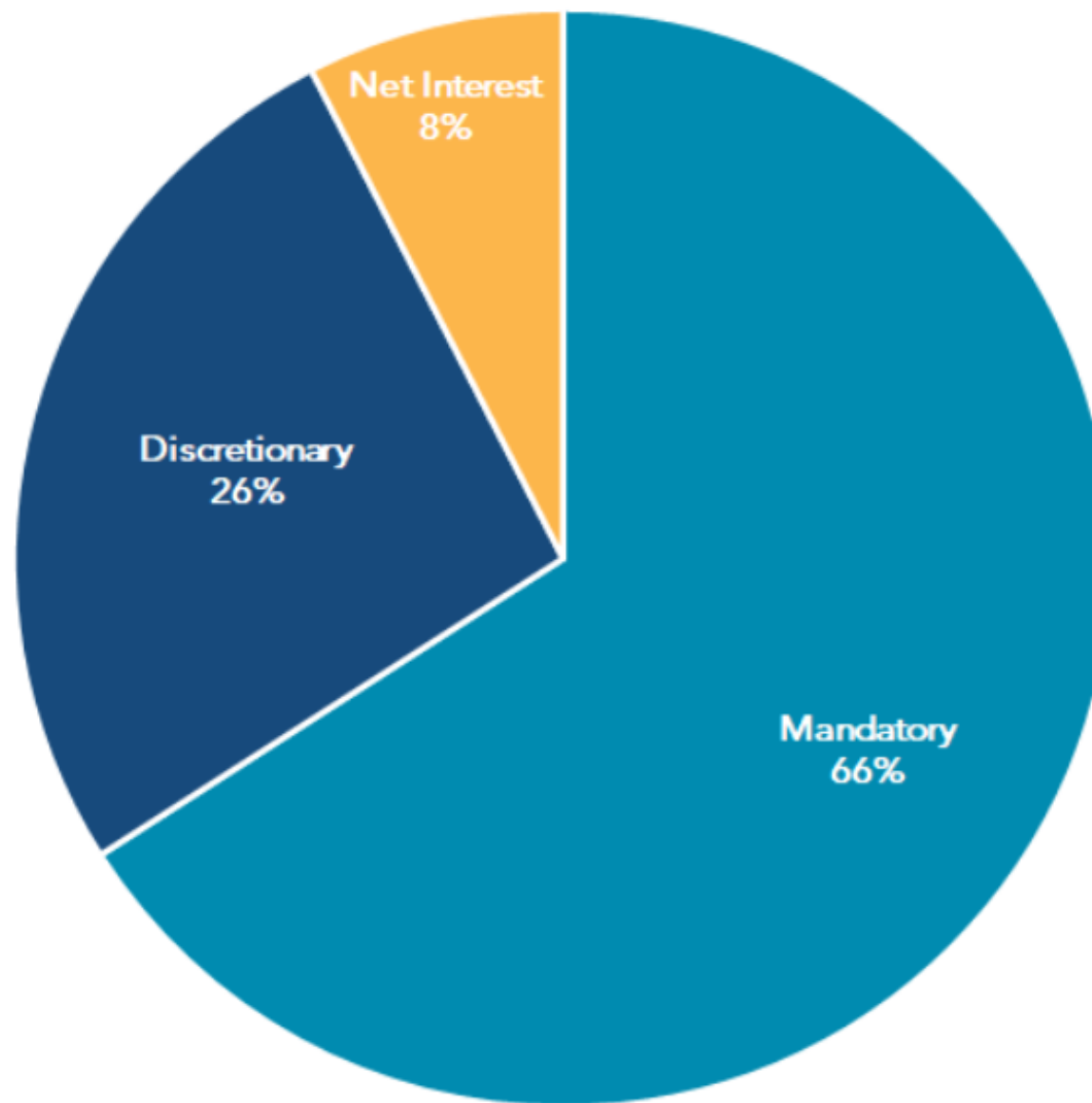


FIGURE 1

# Composition of Federal Spending

Fiscal year 2022

Share of total



Source: Congressional Budget Office. *The Budget and Economic Outlook: 2023 to 2033*, Historical Budget Data, Table 3: Outlays, by Major Category, Since 1962. February 2023.

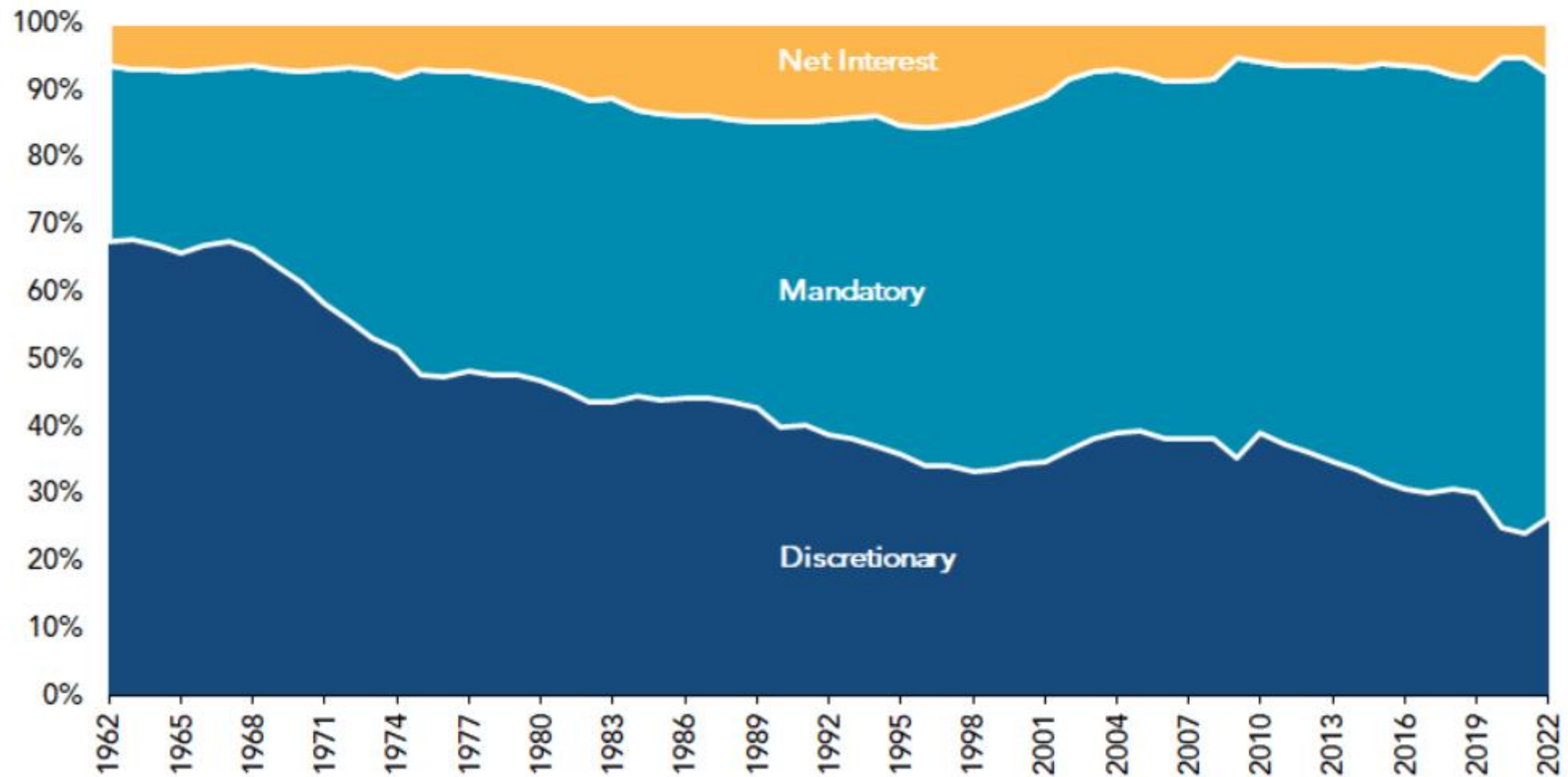
FIGURE 2

# Composition of Federal Spending

Fiscal years 1962 – 2022



Share of total



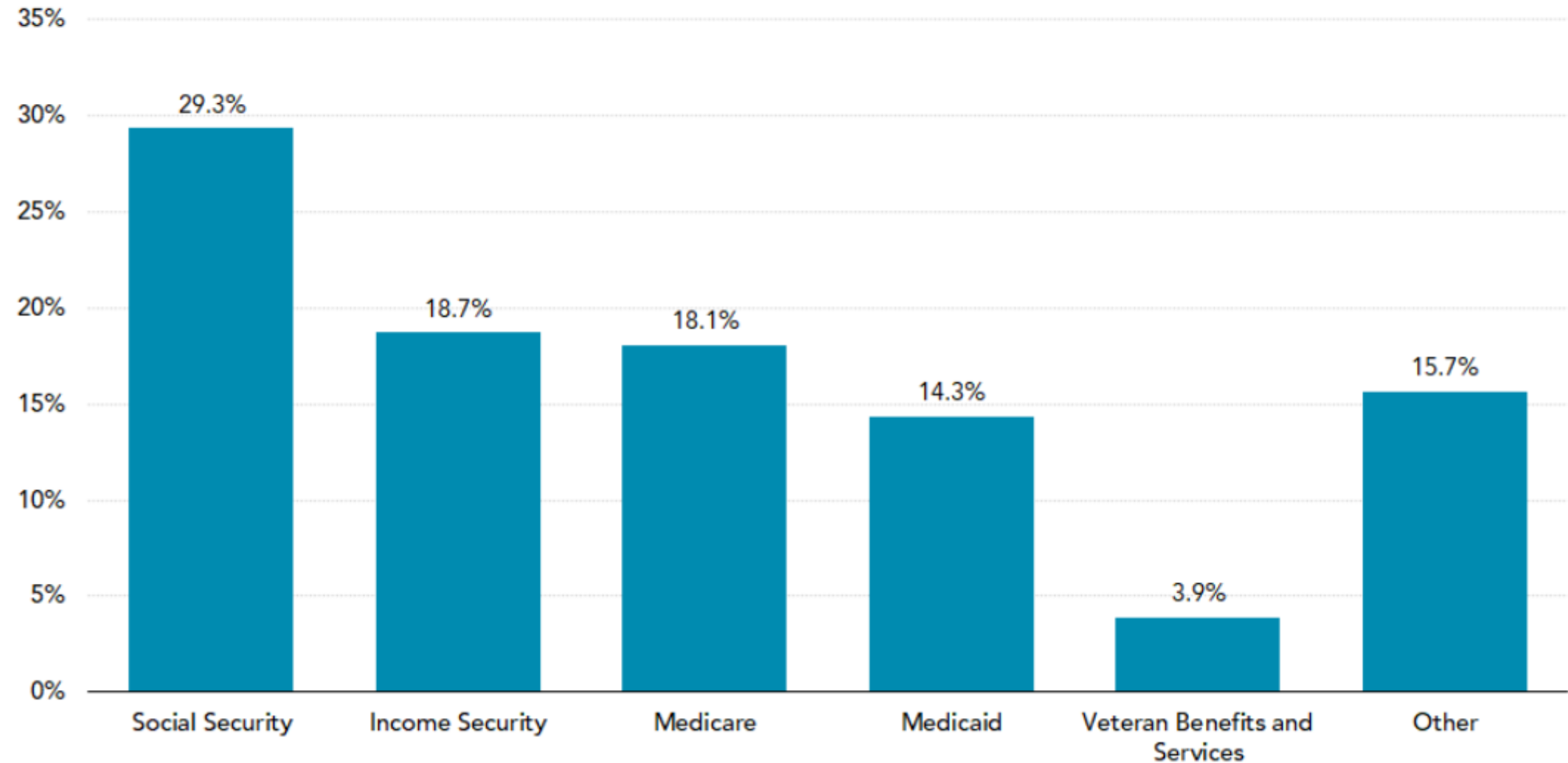
Source: Congressional Budget Office. *The Budget and Economic Outlook: 2023 to 2033*, Historical Budget Data, Table 3: Outlays, by Major Category, Since 1962. February 2023.

FIGURE 3

## Composition of Federal Mandatory Spending Fiscal year 2022



Share of total



Source: Office of Management and Budget. Historical Tables. Table 8.5, "Outlays for Mandatory and Related Programs: 1962–2028," March 2023.

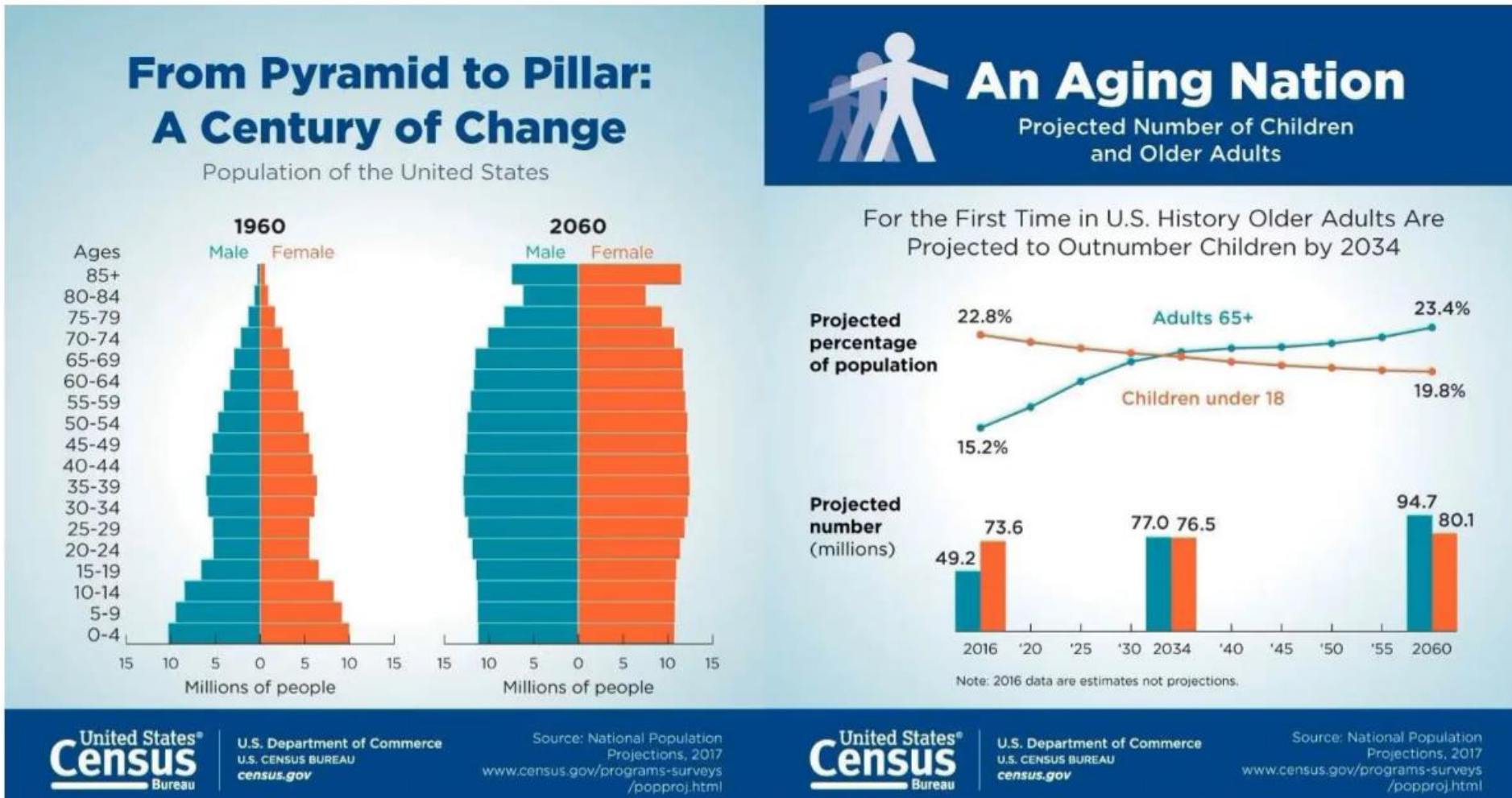
## Mandatory Spending

Mandatory spending covers outlays controlled by laws other than appropriations acts. Almost all such spending is for “entitlements,” for which expenditures depend on individual eligibility and participation; they are funded at whatever level needed to cover the resulting costs.

Mandatory spending has grown from about 26 percent of the budget in 1962 to 66 percent in 2022 (figure 2).

This growth is largely because of new entitlements, including Medicare and Medicaid (both of which started in 1965), the earned income tax credit (1975), and the child tax credit (1997).

In addition, increases in both Social Security benefits during the 1960s and early 1970s and rapid growth of both the elderly and the disabled populations have contributed to increased Social Security and Medicare spending.



Nearly half of mandatory spending in 2022 was for Social Security and other income support programs such as the Child Tax Credit, food and nutrition assistance, and federal employee benefits (figure 3). Most of the remainder paid for the two major government health programs, Medicare and Medicaid.

**Medicaid**

MEDICAID

For individuals, families, and children with limited income & resources

**VS**

**Medicare**

MEDICARE

Generally for people who are 65 & older, or who have a qualifying disability

**Child Tax Credit**

*[chī(-ə)ld 'taks 'kre-dit]*

A tax benefit granted to American taxpayers for each qualifying dependent child.

Investopedia

**USDA**

**Supplemental Nutrition Assistance Program**

Putting Healthy Food Within Reach

# Discretionary Spending

Discretionary spending covers programs that require appropriations by Congress. Unlike mandatory spending, both the programs and the authorized levels of spending require regular renewal by Congress. The share of the budget going for discretionary spending has fallen from two-thirds in 1962 to 26 percent now.

About 45 percent of FY 2022 discretionary spending went towards national defense, and most of the rest went for domestic programs, including transportation, education and training, veterans' benefits, income security, and health care (figure 4). About 4 percent of discretionary spending funded international activities, such as foreign aid.



## U.S. Department of Health and Human Services Centers for Disease Control and Prevention

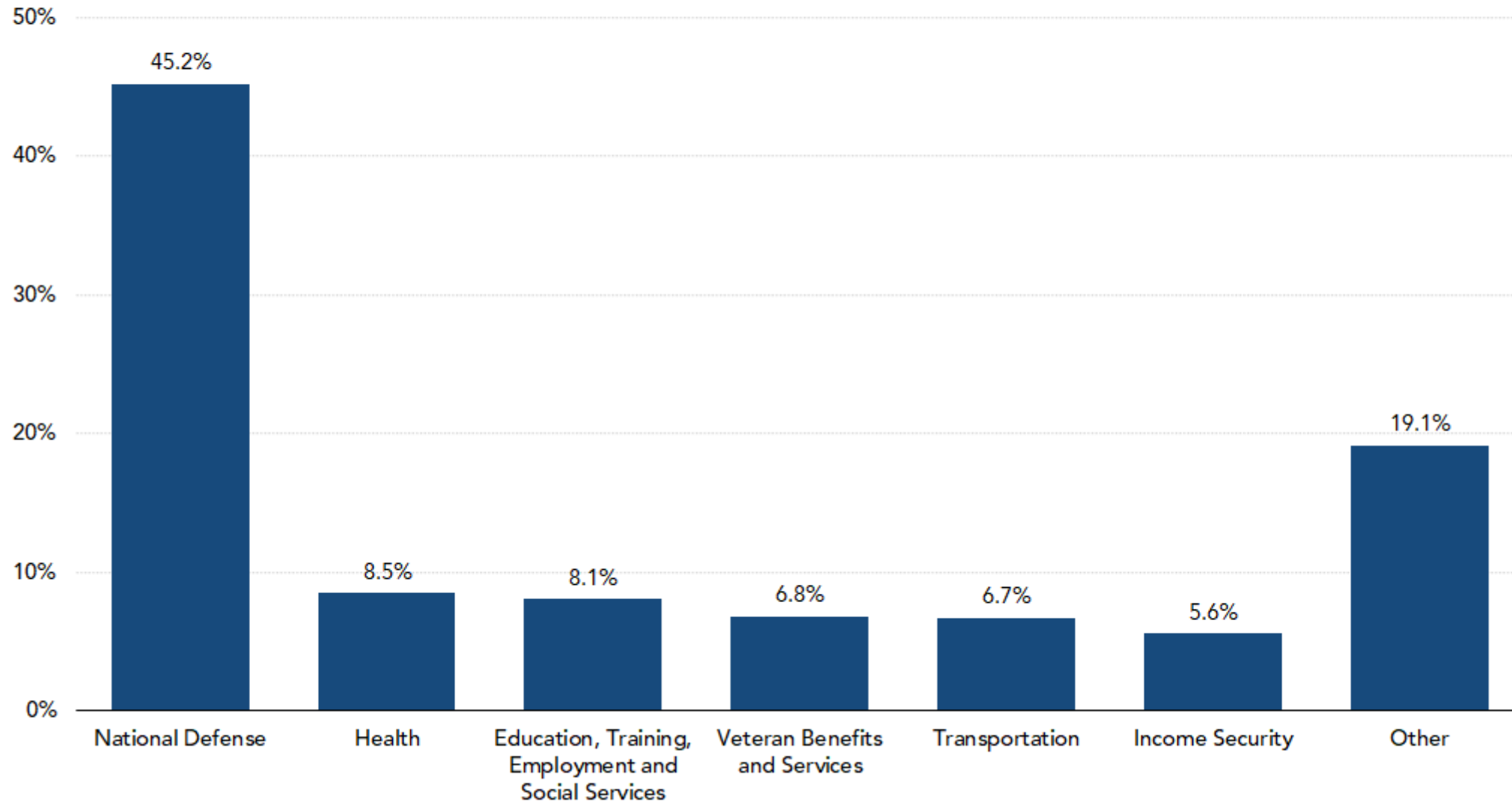


FIGURE 4

## Composition of Federal Discretionary Spending Fiscal year 2022



Share of total



Source: Office of Management and Budget. Historical Tables. Table 8.7, "Outlays for Discretionary Programs: 1962–2028," March 2023.

## Debt Service

Interest on the national debt has fluctuated over the past half century along with the size of the debt and interest rates. It climbed from 6.4 percent of total outlays in 1962 to over 15 percent in the mid-1990s, fell to 6 percent in 2015, but climbed back to 7.6 percent by 2022 (figure 2). Since 2016, historically low interest rates have held down interest payments despite the national debt reaching a peacetime high of 97 percent of GDP in 2022, in part due to the federal stimulus to tackle the COVID-19 pandemic. Overall, interest payments as a share of outlays are projected to rise because of projected increases in both the national debt and interest rates.

Updated January 2024

Federal spending

The previous slides are taken from the Tax Policy Center and the U.S. Office of Management and Budget.

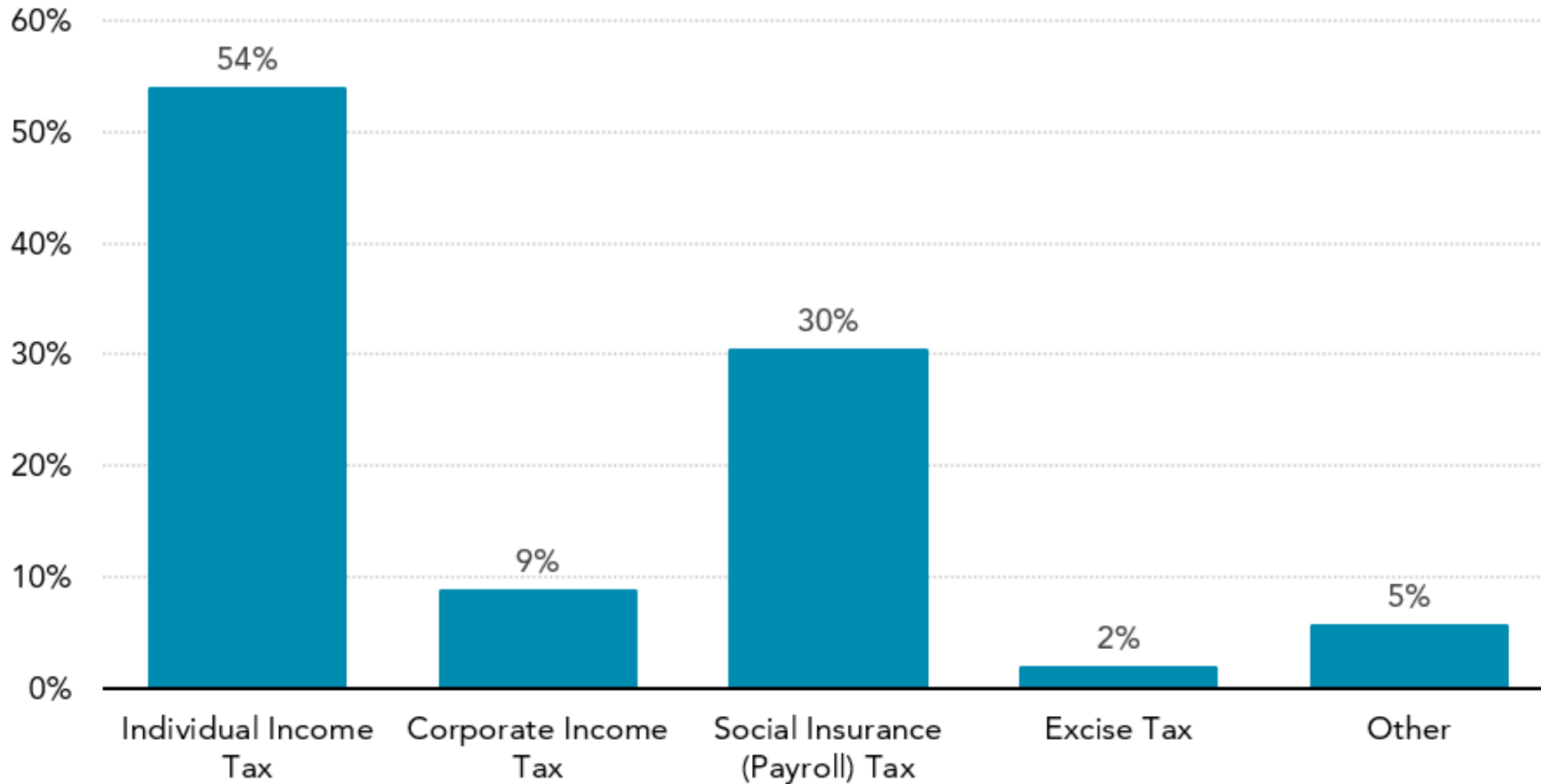
FIGURE 1

# Sources of Federal Revenue

Fiscal year 2022



Share of total



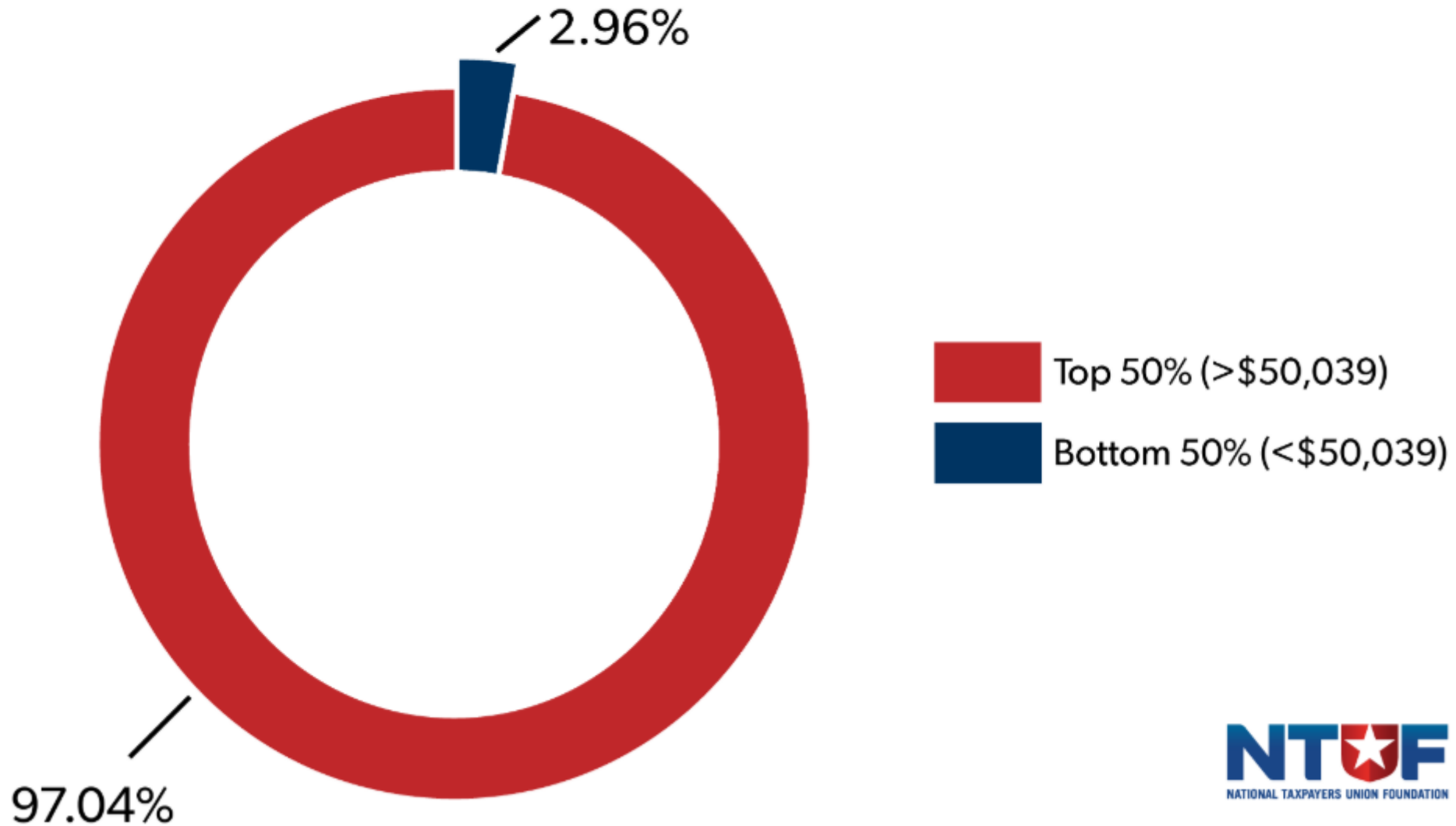
Source: Office of Management and Budget. Historical Tables. Table 2.1, "Receipts by Source: 1934–2028," March 2023.

So... who pays????

The newest data reveals that the top 1% of earners, defined as those with incomes over \$680,164, paid nearly 45% of all income taxes



# Figure 3. AGI Bracket vs. Percentage of Federal Personal Income Tax Paid (2022)



In the real world, however, we must constantly decide how to allocate our limited resources—whether that's money, time, or natural resources—to satisfy our diverse needs and wants.

We've been discussing the federal budget, But let's look at our more personal needs.

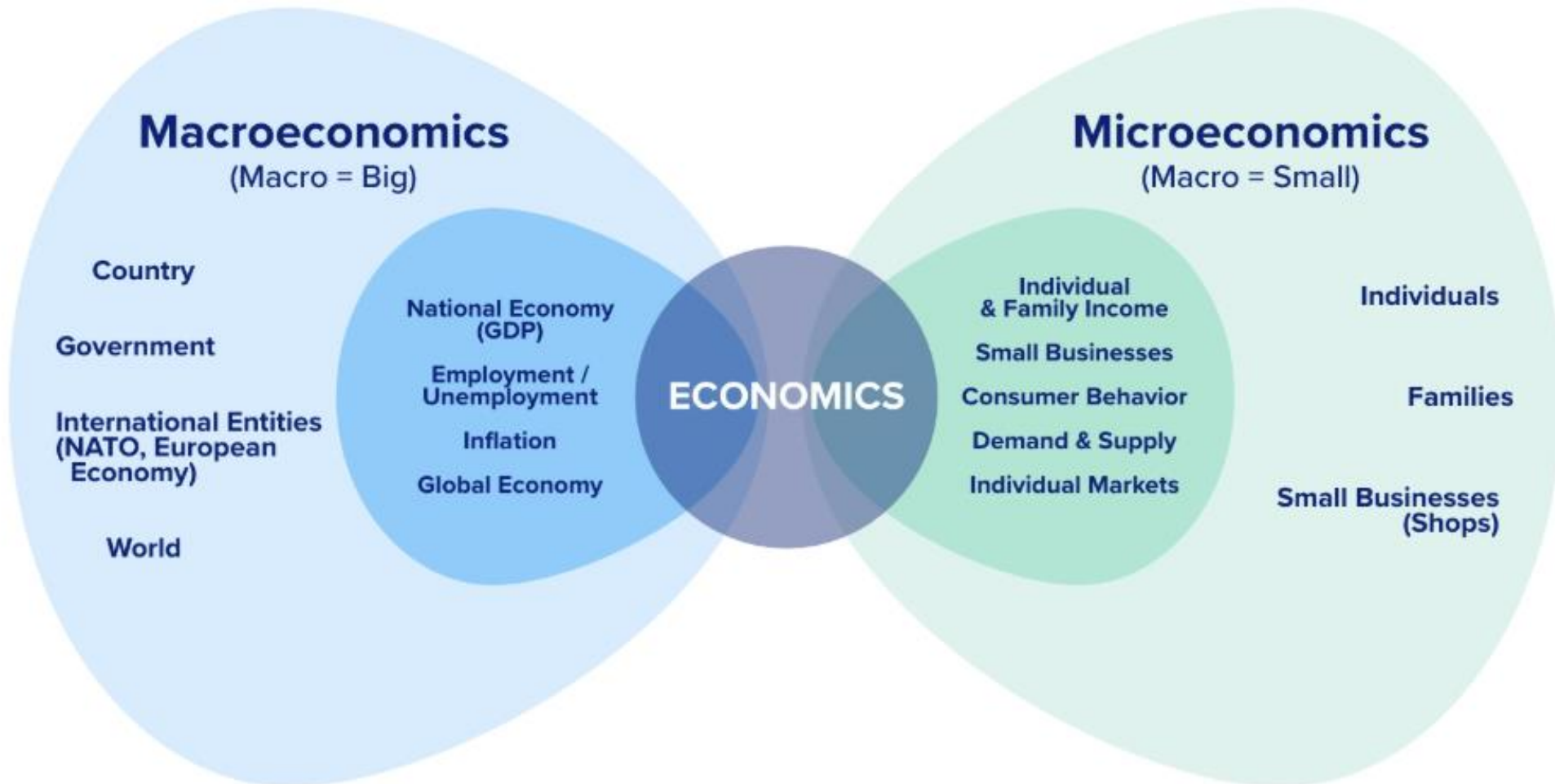
<https://www.sofi.com/learn/content/50-30-20-budget/>



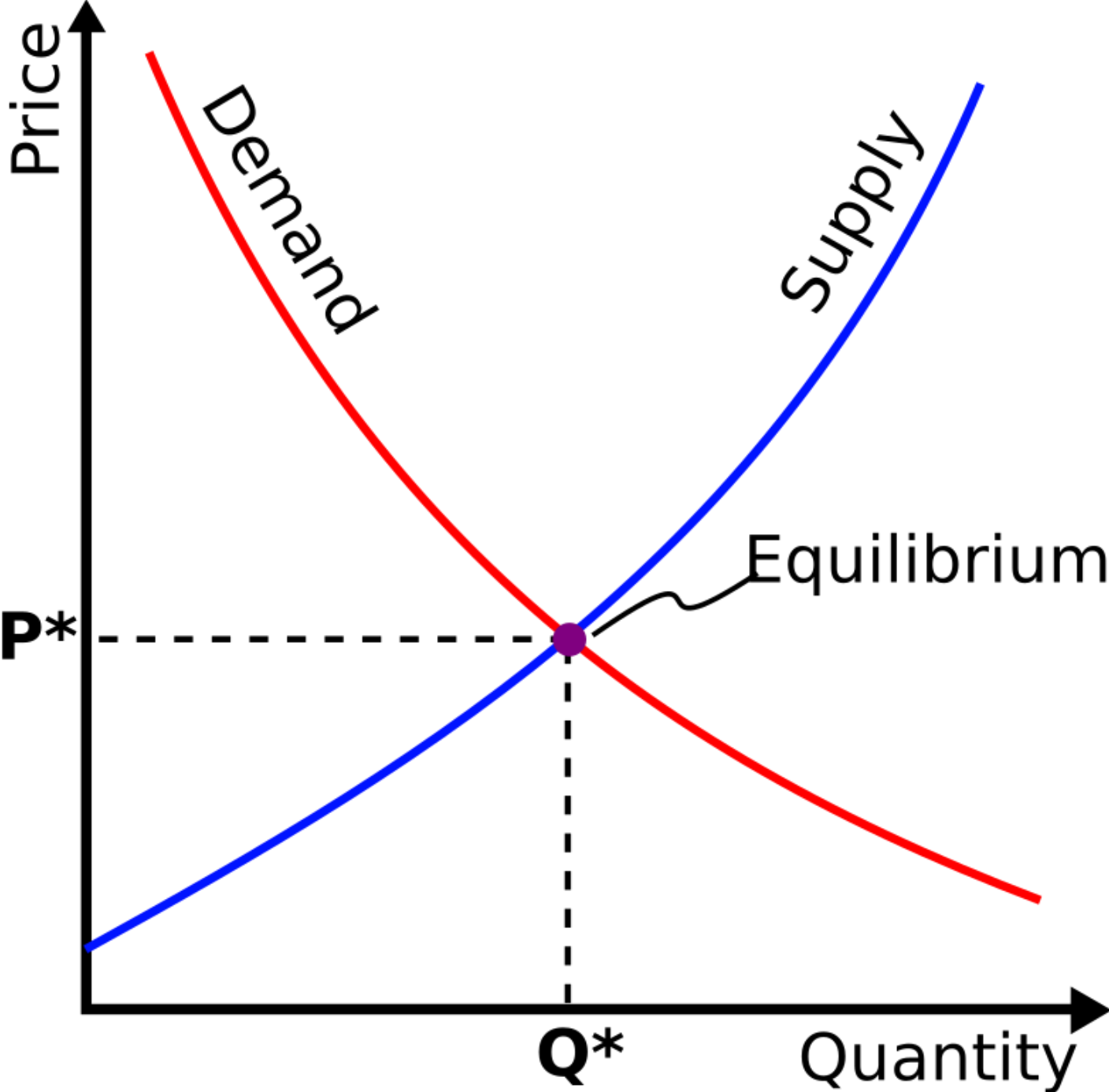
# Key Components of Economic Study

## 1. Microeconomics vs. Macroeconomics

Microeconomics focuses on individual decisions of consumers and firms, while macroeconomics looks at the economy as a whole, including topics like inflation, unemployment, and economic growth. For example, when you study how a single company sets its prices, that's microeconomics. But when you examine how a country's total production affects its unemployment rate, that's macroeconomics.



2. Supply and Demand This fundamental concept explains how prices are determined in a market economy. When demand for a product increases, its price typically rises, and vice versa. Supply and demand interact constantly in markets, influencing everything from the price of your favorite snack to the salary you might earn in your future career.



3. Opportunity Cost Every choice we make has a cost-not in money, but in the next best alternative we give up. If you choose to study for an exam instead of going to a party, the fun you miss out on is your opportunity cost. This concept helps us understand why even "free" things aren't really free-they always cost us something, even if it's just our time.



# Opportunity Cost

*[,ä-pər-'tü-nə-tē 'kɒst]*

The potential benefits that an individual, investor, or business misses out on when choosing one alternative over another.

## Economics in Your Daily Life

You might not realize it, but you're an economist in your everyday life.

When you decide how to spend your time or money, you're engaging in economic decision-making.

Let's look at a real-world example:

Suppose you're deciding whether to buy fun things at Target or save that money for college.

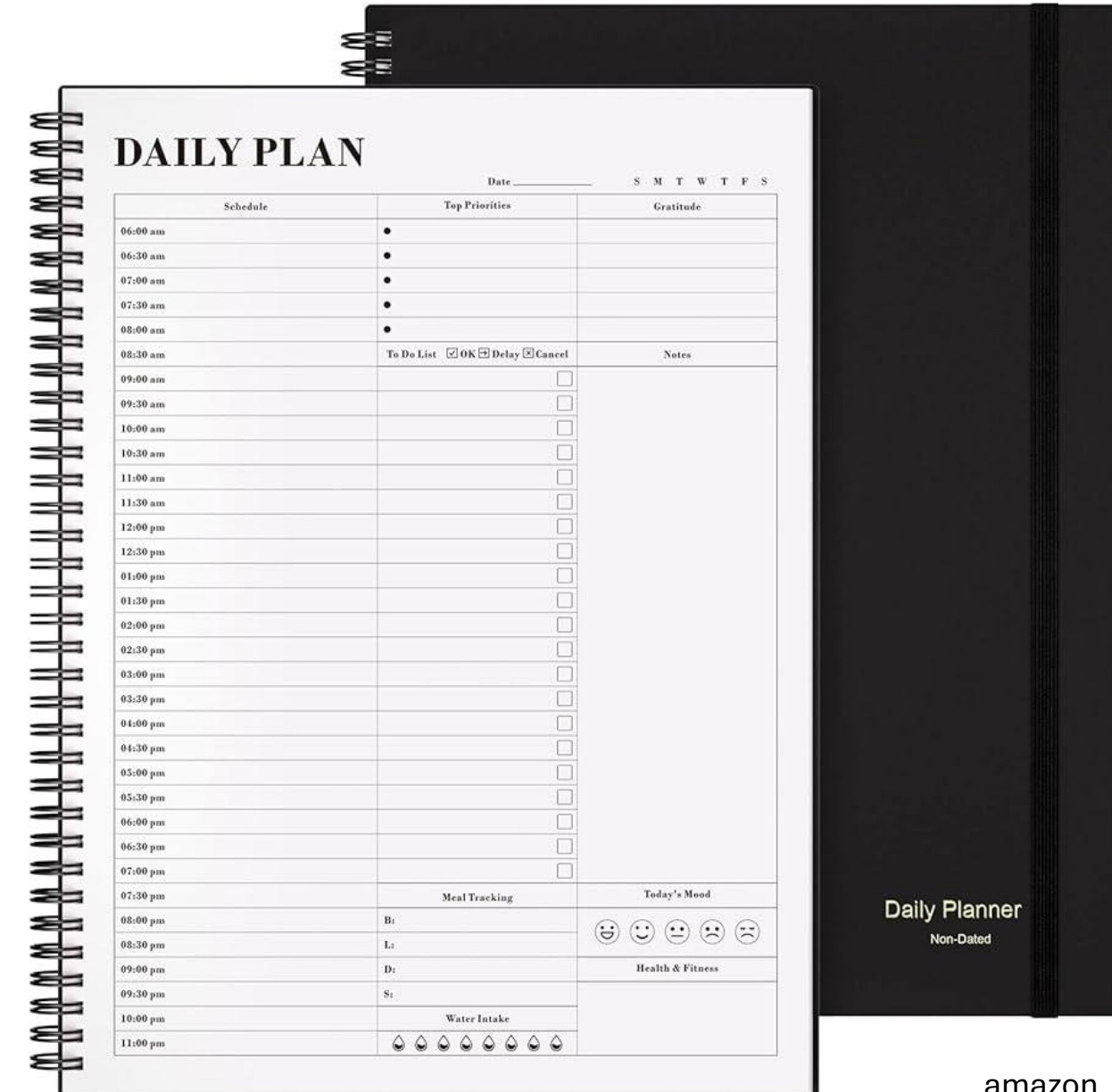
By choosing one option, you're giving up the other—this is opportunity cost in action.

You might consider factors like the usefulness of the fun things at Target, your future education needs, and your current financial situation.

This process of weighing costs and benefits is at the heart of economic thinking.



Even simple decisions, like choosing what to eat for lunch, involve economic principles. You're weighing the costs (money, time, health impacts) against the benefits (taste, nutrition, convenience) to make the best choice for yourself given your constraints. Best bet... keep an agenda for your time, and a budget for your expenses.



# TEEN BUDGET PLAN

MONTH


INCOME / DATE	AMOUNT
.....	.....
.....	.....
.....	.....
.....	.....
.....	.....

TOTAL INCOME:

EXPENSES / DATE	AMOUNT
.....	.....
.....	.....
.....	.....
.....	.....
.....	.....

TOTAL EXPENSES:

TOTAL SAVINGS:

A man in a dark suit, light blue shirt, and striped tie is holding a white rectangular sign. The sign has the text 'TIME FOR REVIEW' written on it. 'TIME FOR' is in blue, and 'REVIEW' is in red. Both are in a bold, serif font with a double underline effect.

**TIME FOR**

**REVIEW**

## The Broader Impact of Economics

Economics isn't just about personal decisions—it plays a crucial role in shaping our society and the world at large. Here are some ways economics impacts the bigger picture:

1. **Government Policies:** Economic theories and data help policymakers decide on everything from tax rates to environmental regulations.

For instance, when a government considers raising the minimum wage, it uses economic analysis to predict how it might affect employment, inflation, and overall economic growth.

### PROS & CONS OF RAISING THE MINIMUM WAGE

#### PROS

1. Higher salaries for the poor
2. Better job satisfaction
3. Improved workforce participation
4. Boosted economic growth
5. Higher consumer spending
6. Social mobility is easier
7. Lessens income inequality

#### CONS

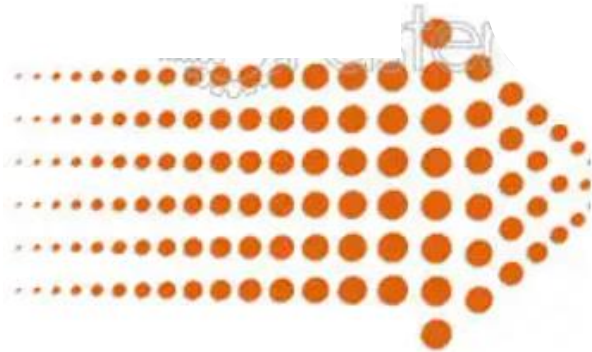
1. Consumer prices increase
2. Unmanageable labor costs
3. Limited Working Hours
4. Fewer job vacancies
5. More outsourcing of jobs
6. Expanded automation
7. Deterioration of benefits

2. Global Trade: Economics explains why countries trade with each other and how this affects jobs, prices, and economic growth. It helps us understand complex issues like trade deficits, currency exchange rates, and international economic cooperation.



**01**

Imports can cause a decline in domestic production, leading to job losses and economic instability



**02**

Imports can lead to lower prices for consumers, increasing their purchasing power



**03**

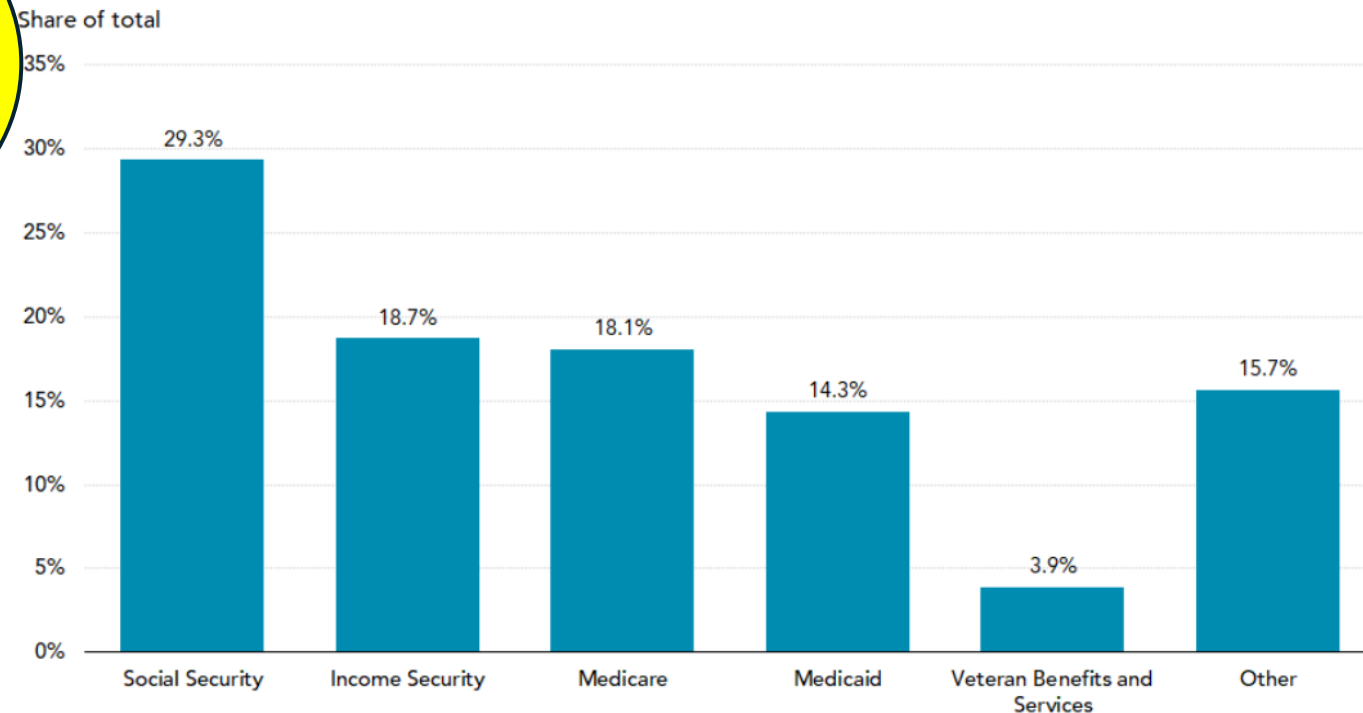
Imports can lead to an increase in competition, driving innovation and productivity

3. Social Issues: Economic analysis can provide insights into complex social problems like inequality, education, and healthcare access. By understanding the economic factors at play, we can develop more effective solutions to these challenges.

As we saw on Slide 7 (below), this is why we have decided, as a country, to assist those who are unable to provide for themselves through mandatory spending to help these individuals.

**From the  
previous  
section**

**FIGURE 3**  
Composition of Federal Mandatory Spending  
Fiscal year 2022



Source: Office of Management and Budget. Historical Tables. Table 8.5, "Outlays for Mandatory and Related Programs: 1962–2028," March 2023.

# Thinking Like an Economist

To understand economics, it's helpful to adopt a way of thinking that involves:

1. Recognizing that every decision involves trade-offs

**TRADE-OFFS**

**DEFINITION**

A trade-off refers to a situation in which gaining one benefit requires sacrificing another. It highlights the balancing act of choices and compromises made when multiple factors are at play. Trade-offs often arise in decision-making when resources such as time, money, or effort are limited and must be allocated sparingly.

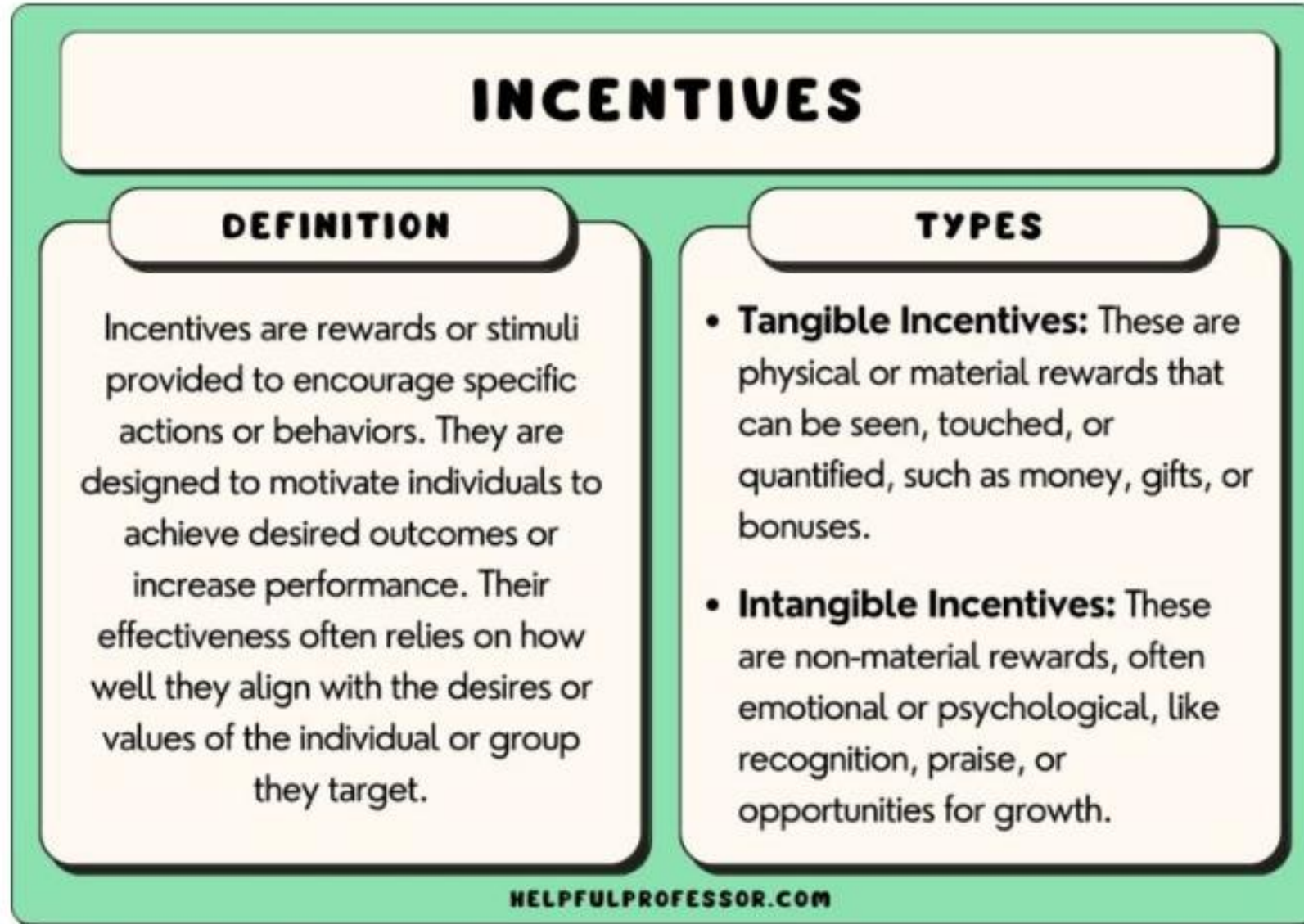
**EXAMPLE**

**Quantity versus Quality**

The quantity vs. quality trade-off refers to the balance between producing more of something (quantity) and ensuring that what is produced meets high standards (quality). Often, increasing the quantity of production can compromise the quality, and vice versa.

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## 2. Analyzing the incentives that drive people's choices

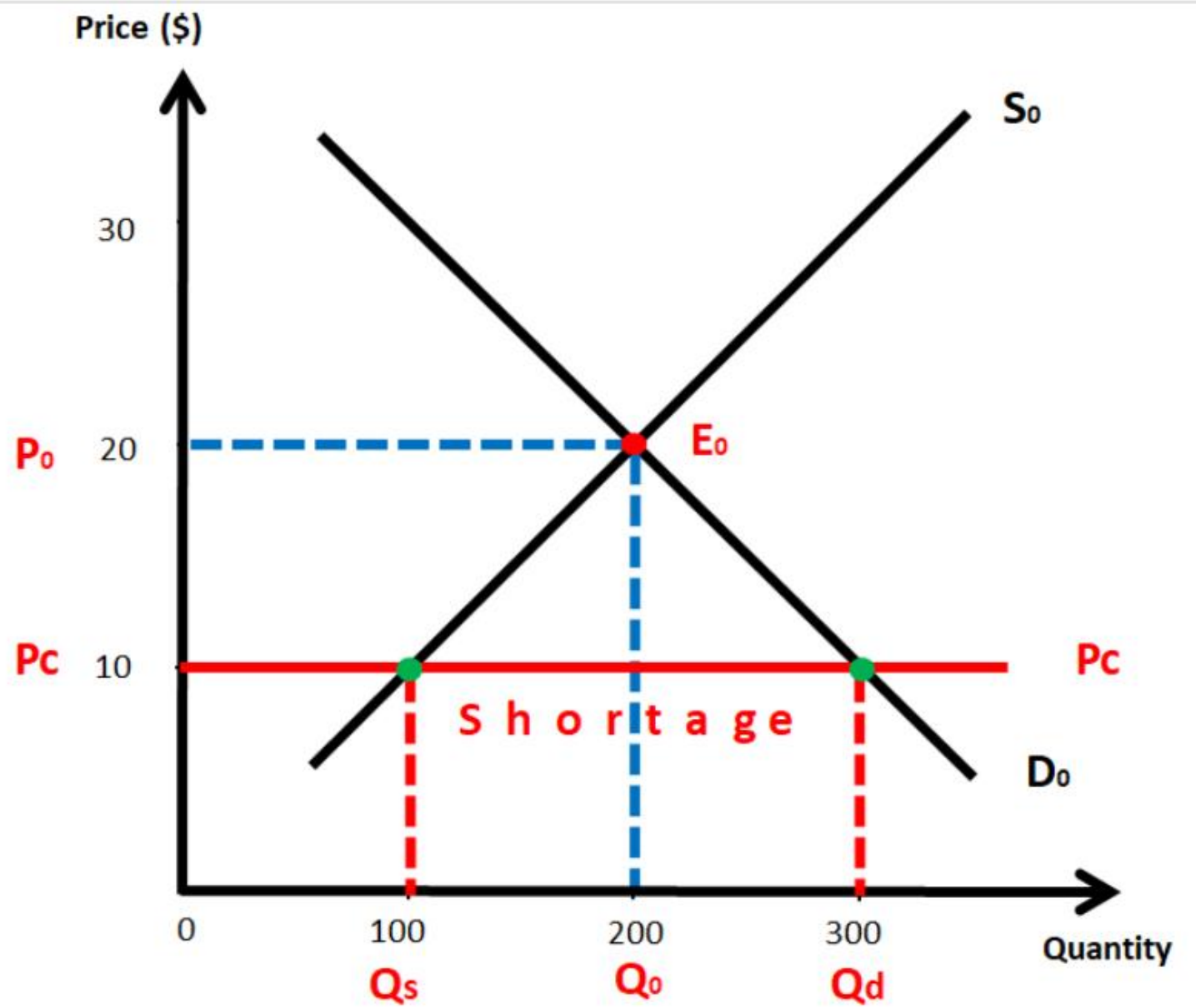


### 3. Considering both the seen and unseen consequences of actions

#### NOT AS COMPLICATED AS IT LOOKS!

This is a simple SD (Supply and Demand curve, to which a government policy of PC (Price Ceilings) was added.

The political intention was to lower prices, though the unforeseen consequence was the shortage caused by this policy.



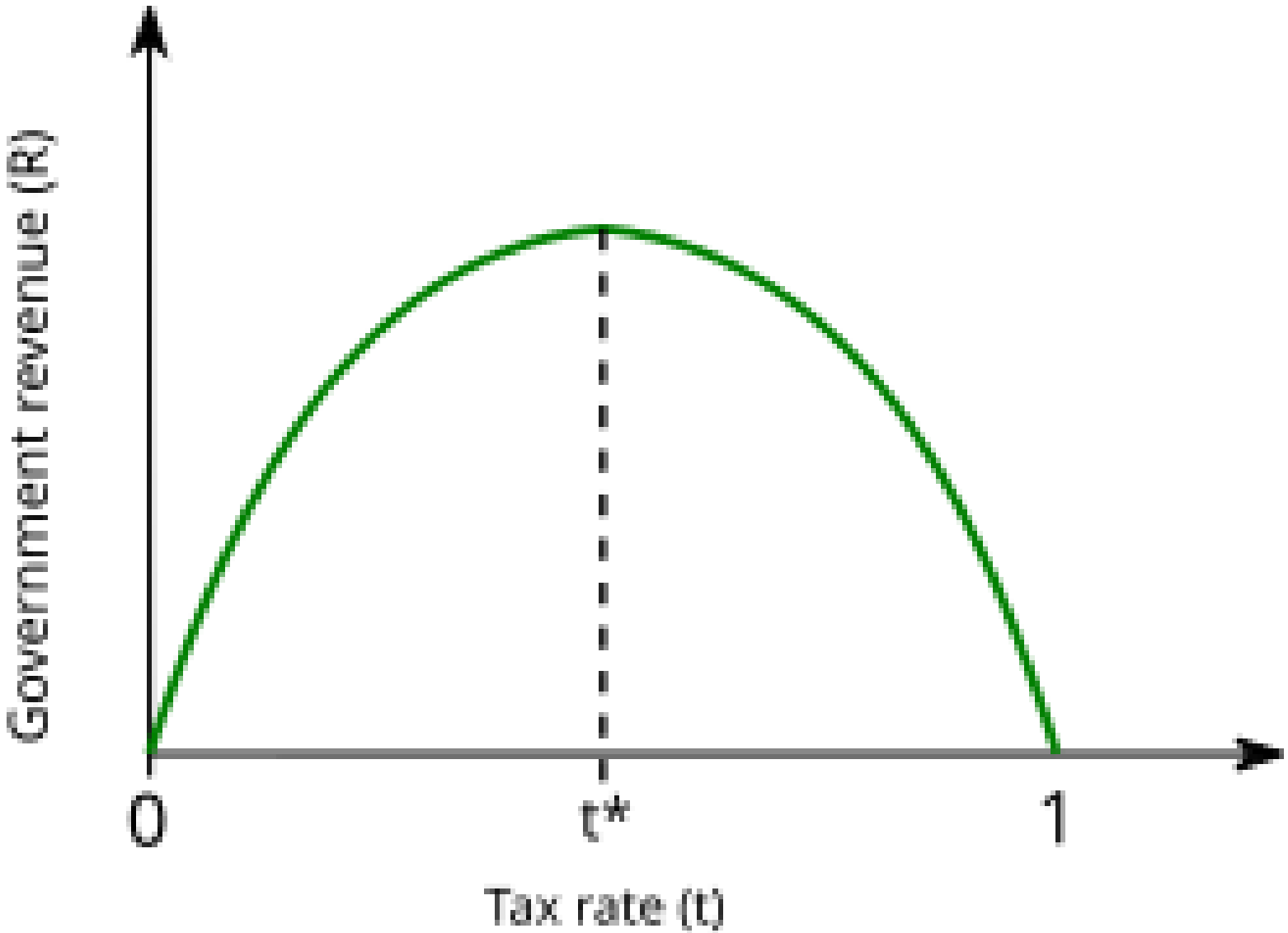
#### 4. Using data and models to understand complex systems

Personally, I love the Laffer Curve, because it expresses its argument with such simplicity.

This curve shows the relationship between the tax rate and government revenue collected.

In all simplicity, Laffer demonstrates that, the higher the tax rate, the more revenue (tax dollars) collected... but only to a point.

Beyond a 50% tax rate, individuals hide their economic activity from the formal economy.



By applying these principles, you can gain valuable insights into the world around you and make more informed decisions in your own life.

Economics is much more than graphs and statistics-it's a powerful tool for understanding human behavior and societal dynamics. As you continue to learn about economics, you'll develop a deeper appreciation for how it shapes our world and influences our daily choices. Whether you're deciding on a career path, understanding global events, or simply managing your personal finances, the principles of economics will serve as invaluable guides throughout your life.

