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Lecture 1
Basics & Prerequisites

Economics
& Society

SMU

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Basics & Prerequisites

★★★★★

WHAT IS ECONOMICS?

★★★★★

OPORTUNITY COST

★★★★★

BASIC NOTIONS

★★★★★

GRAPHS & EQUATIONS

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★★★★★

WHAT IS ECONOMICS?

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Economics

> Introduction to Economics

- ★ **Where** does the word economics come from?

<i>home</i>		<i>laws</i>
<i>οικονομικά</i>	= οίκος + νόμοι	
<i>(ikos)</i>		<i>(nomi)</i>
- ★ **Economics** is the study of how humans **choose** to use the **scarce** resources, which **nature** and **previous generations** have provided
- ★ Contrary to what most people believe, Economics is:
 - ▶ **Less about** money, finances and business
 - ▶ **More about**
- ★ Why?

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The 2 branches of Economics

> Introduction to Economics

★ **Microeconomics**

- ▶ Examines the behavior of individual decision-making **units** or **groups**
- ▶ Deals with the decisions of the **firms, industries, households, market regulators**.

★ **Macroeconomics**

- ▶ Examines the behavior of the economy as a **whole**
- ▶ Deals with **income, production, employment, productivity** in a national scale.

★ **Micro** or **macro**?:

Macro: the examined variable refers to the **entire economy**

Micro: the examined variable pertains to some **individual decision maker**.

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Micro vs. Macro

> Introduction to Economics

★ **Why** economic units and the economy as a whole are analyzed with different branches of economics?

★ The reason is the **fallacy of composition**

the **erroneous belief** that what is true for a part must also be true for the whole

★ **Question**:

★ **Other examples**:

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Economic actors

> Introduction to Economics

★ For Economics, society is built by 3 different **basic blocks**:

- ▶ The households: sometimes referred to as “consumers” or “individuals” is the **consuming unit** of the economy
- ▶ The firms: sometimes referred to as “sellers” or “producers” is the **producing unit** of the economy
- ▶ The government: the economic unit that **sets the rules** for the economic activity.

★ The same individual could be a household when we consider her choices as a **consumer** and a firm when she is **producing** or **selling** something

★ Sony and Tesla are **firms**, the owners of which are **households**

★ MRT or SMU are **firms**, the owner of which is the **government**.

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Opportunity Cost

> Basic notions

- ★ Making a choice automatically entails that we **give up** the rest of the alternatives
if I **go for a run** on Sunday morning, I **forgo** the pleasure from reading a book
 - ★ **Opportunity Cost**: the benefit lost from a choice over its **next best** alternative
 - ★ Opportunity costs are **not paid** to anyone but are **still incurred**:
-
- ★ Accountants **do not count** opportunity cost
because it is **not actually paid to anyone** and there are **no receipts or invoices** for it
 - ★ Economists always **take it into account**
because decisions **must always involve ALL** benefits and ALL costs

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Sophia's real cost

> Basic notions

- ★ Sophia works at a store for **\$150 per day**
- ★ Alternatively, she could make and sell **bracelets**:
 - ▶ Sophia can make 20 bracelets per day
 - ▶ **Raw materials** for each bracelet cost \$8.
- ★ According to an accountant, the **cost per bracelet** would be \$8
- ★ According to an economist, the **cost per bracelet** should also include her **labor**
 $\$8 + \$150/20 = \$15.5$ per bracelet
- ★ This difference in the definition of cost leads to 2 definitions of **profit**:
 - ▶ **Accounting profit** = Revenues – explicit costs
 - ▶ **Economic profit** = Revenues – ALL costs



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External video

From a lecture given by Nobel laureate in Economics, Milton Friedman, in Pennsylvania in 1978. A member of the audience tries to lure Friedman into a logical fallacy. See how he shoots down the argument by making the fallacy visible to the audience. Try to figure out which kind of fallacy it is.

YouTube



The Most Persistent Economic Fallacy of All Time!

brittle13 · 378K views · 10 years ago

From a lecture given by Dr. Milton Friedman in Erie, Pennsylvania (1978). This is essentially a restatement of the 'parable of the ...

2:52

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Internal video

This video will take you through graphs and equations at the level we will need them in this course. If you already have some technical background, you will find this video really easy. If not, it will not be hard to follow till the end.

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Thank you!
(you are welcomed to stay for consultation or discussion)

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⚠ WARNING! ⚠

The slides in this handout are created with the intention to serve as visual aid for the audience during the live presentation of the material in the lecture. As such, **they are not designed to be standalone reading material** and should be used strictly as **reference**, side by side with notes taken in the lecture. Studying solely from the slides **is not recommended** and might in some cases **mislead** those who have not attended the relevant lecture. **Little or none tasks in test and exam can be answered solely from the slides.**

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