

# Thinking Like a Microeconomist

Some examples and a definition.

# Should You Go to Class?

- Factors to consider:
  - What would you be doing if you weren't in class? (opportunity cost)
  - What is the impact of missing class?
- Marginal Analysis
  - Decision is not whether to go to any classes. Decision is about whether to attend the next class.

# Empirical Study

## Cohabitation or Not?

- Alone, Pat produces 50 units of market goods in one day or 25 units of home goods.
- Alone, Alex produces 75 units of market goods in one day or 50 units of home goods
- Should they cohabit? (Cohabitation as a free trade agreement.)

# Production Possibilities

	Amount of Stuff Produced in One Day	Amount of Cookies Produced in One Day
Pat	50	25
Alex	75	50

# Opportunity Cost

	Market Goods	Home cooked meals (in terms of market goods)
Pat	$1/2$	2
Alex	$2/3$	$3/2$

# Gains from Trade

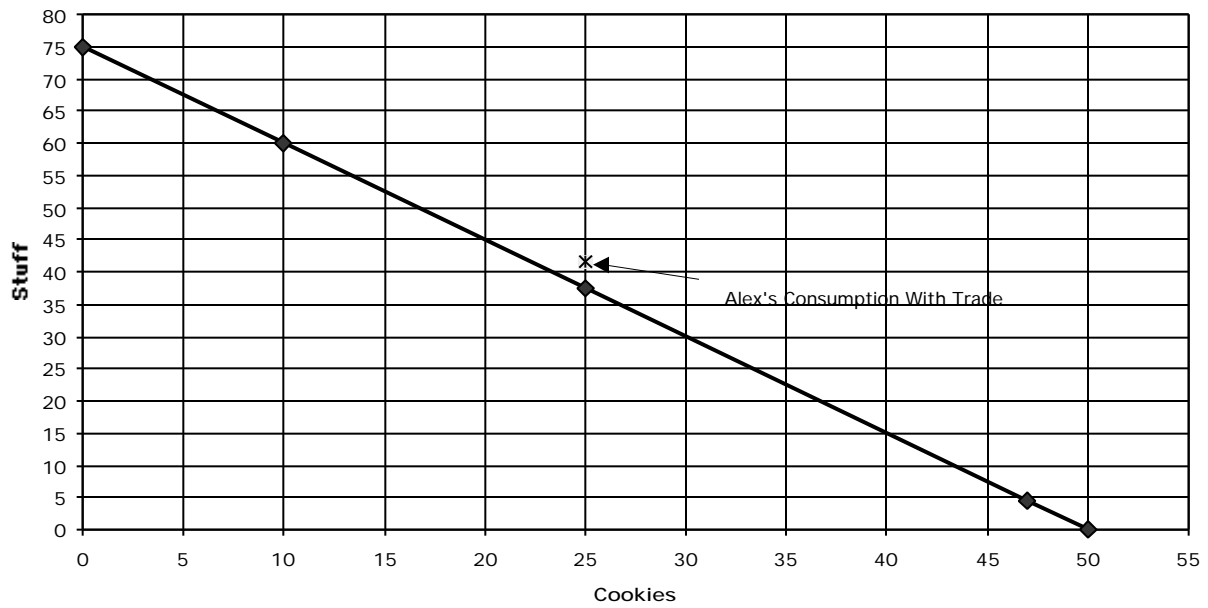
- Pat has comparative advantage in production of stuff; Alex has comparative advantage in production of cookies.
- Trade agreement could make everyone better off.

# Example

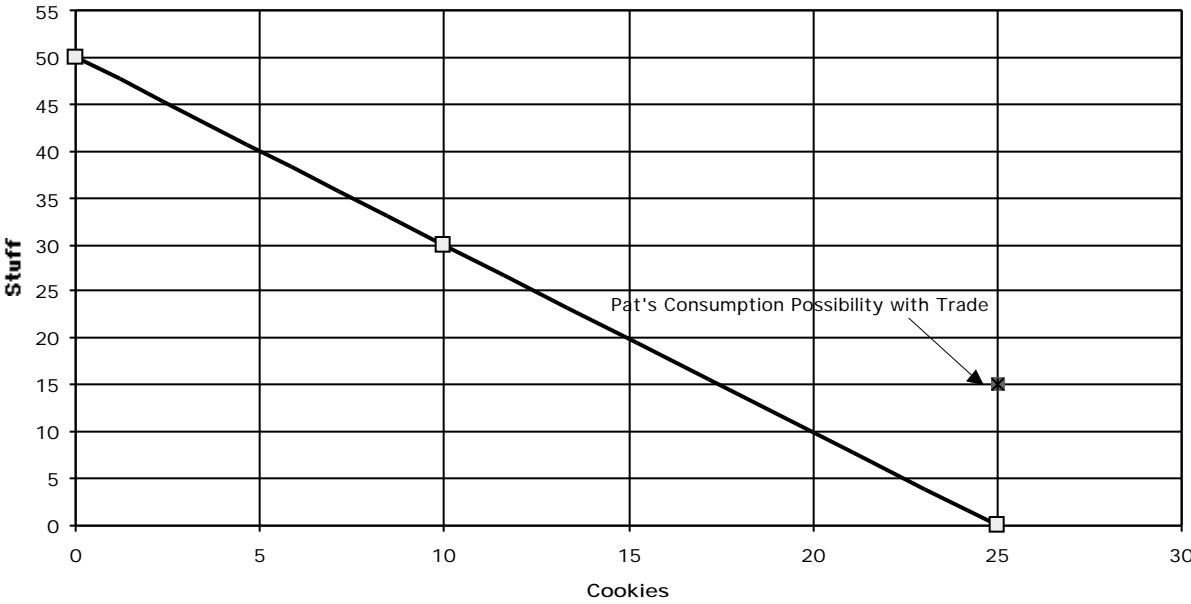
- Pat specializes in stuff and makes 50 units ; Alex in cookies and makes 50 units.
- Alex trades 3 cookies for 5 units of stuff . So with trade Alex could have 25 cookies and  $41 \frac{2}{3}$  units of stuff. Without trade, Alex could consume only  $37 \frac{1}{2}$  units of stuff if he/she produced 25 cookies.
- Pat will have 15 units of stuff and 25 cookies. Without trade, Pat would have 0 units of stuff if he/she consumed 25 cookies.



# Gains from Trade -- Alex



# Gains from Trade -- Pat



# Allocating Parking Spaces at USC

- Number of parking spaces is less than the number of cars that would like to park on campus during class hours
- What are some methods for allocating spaces?
  - Lottery -- no secondary trades allowed
  - First come first serve
  - Auction
  - Lottery - with secondary trades allowed

## Who Gets Spaces?

- Lottery -- random assignment of spaces
- First come -- those with low opportunity cost of waiting in line will get spaces
- Auction -- highest bidders get spaces
- Lottery -- with secondary trades, those with the greatest willingness to pay will have the spaces.

# What Is Microeconomics?

Microeconomics is the study of how individuals (households, firms) allocate scarce resources among competing alternatives. Microeconomics is the study of how prices and outputs of specific goods and services get determined.

# Important Concepts

- Opportunity Cost
- Comparative advantage and gains from voluntary trade
- Decision making at the margin
- Economic efficiency
- The invisible hand
- Divergence between private and social costs and benefits