

What is the relationship between trade-offs and opportunity costs?

Trade-off

- A trade-off occurs when we choose one course of action over another.
- In Economics, we can never have everything we want or need.
- We must make choices.
- A woman spends ten dollars buying her lunch at a local restaurant. She cannot use the same ten dollars to buy a book. A trade-off has occurred.

It's All About Scarcity!

- Scarcity exists. Our wants and desires are limitless but our natural resources are limited.
- We can always want more than we have. As such, we are constantly choosing one course of action over another.
- We cannot spend ten dollars on a movie ticket and the same ten dollars on a restaurant meal.

Opportunity Cost

- Whenever we make a decision, we receive one thing but give other things up.
- If I chose to study tonight for the examination, I cannot go to the party or the movies or walk the dog.
- The most desirable alternative given up for the decision is the opportunity cost.
- Think of the opportunity cost as the best course of action of all those things you didn't get.

Guns or Butter

- Government officials also must choose where to spend tax dollars.
- When a government spends more money on the military, it must invariably spend less money on consumer goods like roads and schools.
- Economists refer to government trade-offs as Guns or Butter.

Thinking at the Margin

- Sometimes a decision involves whether to add or subtract one additional unit of a resource.
- After studying many hours, a student might ask herself: “Should I study one more hour?”
- This question is a question at the margin.
- Deciding whether to add or subtract one additional unit occurs at the margin.