<table>
<thead>
<tr>
<th>Principle #1: People Face Tradeoffs</th>
<th>Principle #2: The Cost of Something Is What You Give Up to Get It</th>
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<tbody>
<tr>
<td><strong>We have to give up one thing to get another</strong></td>
<td><strong>Decisions require comparing costs and benefits of alternatives</strong></td>
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<td>Task: As a group, make a list of the tradeoffs you’ve made recently. Discuss how tradeoffs affect your everyday life. Determine why it is important to acknowledge life’s tradeoffs.</td>
<td>Task: As a group, list the costs and benefits of three potential decisions you will face. Then figure out the opportunity costs. Discuss. Determine why it is important to look at opportunity costs?</td>
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<tr>
<th>Principle #3: Rational People Think at the Margin.</th>
<th>Principle #4: People Respond to Incentives</th>
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<tbody>
<tr>
<td><strong>People make decisions by comparing costs and benefits at the margin</strong></td>
<td><strong>Because rational people make decisions by comparing costs and benefits, they respond to incentives.</strong></td>
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<tr>
<td>Task: As a group make a list of “black and white” decisions. Ex. Eat or Starve. Then find the margin or “grey area” for each one. Ex. Eat a small lunch and bigger dinner. Discuss. Determine what makes people choose one thing over another.</td>
<td>Task: As a group, write down three situations where incentives affect a market. Ex. Price of apples goes up so people buy pears etc. Then think of a situation where policy affects incentives. Ex. Seatbelt law. Discuss. Determine why incentives are such an important part of Economics.</td>
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**People gain from their ability to trade with one another.**

Task: As a group, make a list of some of the clothes that you are wearing or items in your possession. Look at the tag to figure out where they were made. Try to figure out what country they come from. How does trade affect our everyday life? Discuss. Determine what the benefit is from trading.

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### Principle #6: Markets Are Usually a Good Way to Organize Economic Activity

**A market economy is an economy that allocates resources through the decentralized decisions of many firms and households as they interact in markets for goods and services.**

- **Households decide what to buy and who to work for**
- **Firms decide who to hire and what to produce**

Task: As a group, use the definition of market economy to create an example. Think of a specific item or company and show how the firm and the household interact. You can write it out or create a chart or graphic organizer. Discuss. Determine what role prices have in a market economy.

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### Principle #7: Governments Can Sometimes Improve Market Outcomes.

**Government policies usually aim to either enlarge the economic pie (efficiency) or to change how the pie is divided (equity).**

Task: As a group think of a way the government might intervene in the market to help it become more efficient. Then try to come up with ways the government might help make the market more equitable. Discuss. Determine why the government may make policy that does not help the market.

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### Principle #8: The Standard of Living depends on a Country’s Production of Goods and Services

**Standard of living may be measured in different ways:**

- **By comparing personal incomes**
- **By comparing the total market value of a nation’s production.**

Task: As a group, come up with a list of the benefits of a better standard of living. Considering the definition, decide what kind of polices would help raise the standard of living in a country? Discuss. Why is it important to look at a countries production?
THE ECONOMIC WAY OF THINKING
Chapter 1, Section 2

KEY TERMS

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<thead>
<tr>
<th>Marginal</th>
<th>Incentive</th>
<th>Microeconomics</th>
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<tr>
<th>Macroeconomics</th>
<th>Theory</th>
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FOCUS QUESTIONS

*How do costs and benefits affect decisions?*

*Why are incentives important?*

*Explain the difference between micro- and macroeconomics.*

*Why do economists develop theories?*

Make a T-Chart reflecting the costs and benefits of continuing your education after high school.
The Story of a Broken Window

Use the story to explain why it’s important for economics to look at “what would have been.”

Applying the Principles

Incentives - CHAPTER 1, SECTION 2

Most of economics can be summarized in four words: People respond to incentives.

- Steven Landsburg, economist

Governments use economic incentives to influence the behavior of citizens in a way that benefits society. They create incentives through laws and through taxes.

For example, a government could pass a law prohibiting children from purchasing a product meant for use by adults. Such a law would make it difficult for children to obtain the product.

A government could also place a tax on a certain good to discourage its use. Such a tax would increase the cost of the good. For some people, the cost would then be greater than the benefit, and these people would decrease their consumption of the good.

A government could give tax benefits to encourage an activity. For example, it might provide a credit by giving taxpayers back a portion of a tax, or it might provide a deduction by allowing taxpayers to subtract a certain amount from their income before calculating their taxes. Such a credit or deduction would reduce the cost of the activity. For some people, the benefit will then be greater than the cost, and these people would increase their participation in the activity.

For each of the goals in questions 1-6, think of a government incentive that accomplishes the goal.

EXAMPLE

**Goal:** Decrease the consumption of alcohol.

**Incentive:**

The government taxes the manufacture and sale of alcohol. Such taxation increases the cost of alcohol. For some people, the cost is now greater than the benefit, and these people have decreased their consumption of alcohol.

1. **Goal:** Decrease smoking.

   **Incentive:**

2. **Goal:** Increase the level of education.

   **Incentive:**
3. **Goal:** Increase the rate of private home ownership.
   **Incentive:**

4. **Goal:** Decrease the consumption of fuel oil.
   **Incentive:**

5. **Goal:** Increase the rate of personal savings.
   **Incentive:**

6. **Goal:** Increase donations to charities.
   **Incentive:**

Refer to the goals and incentives in questions 1-6 as you answer questions 7 and 8.

7. What is the trade-off of using tax benefits as incentives?

8. Could any of these incentives have unintended effects? Give a specific example.