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Personal Budgeting and the Opportunity Cost of Choices

The section discusses personal budgeting constraints and opportunity cost of choices individuals face due to limited income and resources. In the example a student receives $100 per month to spend on gas ($2 per gallon) and DVDs ($10 each). The combinations of these two goods that can be purchased are shown on a budget line, which represents all possible ways of spending the full income.

- On the budget line: you spend all $100 on gas and DVDs.

- Below the budget line: you spend less than $100, leaving money for savings or other items.

- Above the budget line: combinations are unattainable with the current income.

Changes in income or prices shift the budget line:
Higher the income → shifts outward means (more goods affordable).

Lower income or higher prices → Shifts inward (fewer goods affordable).

Lower prices (with same income) → Shifts outward (more goods affordable).

Opportunity cost is the value of the alternative you give up.

At current prices, each DVD ($10) costs the opportunity of 5 gallons of gas ($2 each). Coversely, each gallon of gas costs one-fifth of a DVD. Opportunity cost depends on relatives prices, not just money prices. Even if prices rise equally (e.g., gas $4, DVDs $20) the trade-off remains the same (1 DVD = 5 gallons of gas).

The budget line shows all affordable choices with limited income, and opportunity cost explains what you sacrifice when choosing one good over another.