Personal Budgeting & Opportunity cost

Aishwarya. B. G. [2.54]
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Individuals face constraints when deciding how to spend limited income. In the ex; a student receives \$100 per month to spend on gas (\$2 per gallon) & 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 & 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 income → shifts outward (more goods affordable)

Lower income or higher prices → shifts inward (fewer good affor).

Lower prices (with same income) → shifts outward (more goods affor)

Opportunity cost is the value of alternative you give up.

At current prices, each DVD (\$10) costs the opportunity of 5 gallons of gas (\$2 each).

Conversely, each gallon of gas costs one-fifth of a DVD.

Opportunity cost depends on relative prices, not just money prices. Even if prices rise equally (eg. DVDs, \$20 & gas \$4). the trade-off remains the same (1 DVD = 5 gallons of gas).