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David Colander

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CONTENT ARTICLE IN ECONOMICS

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Introduction to symposium on opportunity cost

David Colander

Department of Economics, Middlebury College, Middlebury, VT, USA

Opportunity cost is a basic, but illusive, concept in economics. The general idea is easily understood: one must take all relevant costs into account when making a decision. The precise meaning of "all relevant costs" and how those relevant costs should be measured, however, is not simple. The ambiguity of the precise measure of the opportunity cost concept was shown when Ferraro and Taylor (2005) asked a number of economists to answer an opportunity cost question at the American Economic Association meetings. There was no agreement; the answers of how precisely to measure opportunity costs ranged the gamut.

While this lack of agreement might seem problematic, for most economists it was not. On the one hand, those focused on teaching economics generally use the opportunity cost concept in a way that does not require a precise measure. (For example, they use it to remind students to take into account implicit costs, such as the owner's time, that are not included in accounting costs when thinking about "all relevant costs.") They seldom asked for explicit measurement of opportunity costs. On the other hand, practicing economists who needed specific measures to arrive at a specific conclusion did not even use the opportunity cost concept. They did not have to because it was built into the structure of their models. Since the relevant costs become clear in the context of the model, for practicing economists the opportunity cost concept was a superfluous concept that needed no precise measure. The bottom line was that no one was especially concerned about precise measurement of opportunity costs.

Despite the fact that no one was especially concerned with precise measurements of opportunity costs, it still was a bit of an embarrassment for the profession when the ambiguity of precise opportunity cost measures became clear. The result was an ongoing discussion of opportunity costs, of which this symposium is a part.

The symposium consists of five articles. It begins with one by Michael Parkin who looks at the historical use of opportunity costs and distinguishes between a value specification and a quantity specification. In his article, he traces the history of both specifications and argues in favor of using a quantity specification. That article is followed by three others by economists who have been active in the opportunity cost debate. These three articles consider Parkin's preferred usage and suggest problems with it. The last article is Parkin's response. He agrees with many of the points his critics made. He argues, however, that the problem is not with his preferred quantity specification, but rather with his lack of clarity about valuation criteria he meant to be used in the quantity specification. Not only are there two specifications of opportunity costs, there are also two specifications of value. He argues that when the quantity specification is "properly stated and understood," he believes that all four economists are in general agreement. Whether that is the case, we leave for the readers to decide.

Reference

Ferraro, P. J., and L. O. Taylor. 2005. Do economists recognize an opportunity cost when they see one? A dismal performance from the dismal science. *Contributions to Economic Analysis and Policy* 4 (1): Article 7, December.

CONTACT David Colander colander@middlebury.edu Department of Economics, Middlebury College, Munrow Hall 215, Middlebury, VT 05753, USA.