

Principles of Economics

Twelfth Edition



GLOBAL
EDITION



Chapter 2

The Economic Problem: Scarcity and Choice

Principles of Economics

TWELFTH EDITION

Karl E. Case • Ray C. Fair • Sharon E. Oster

PEARSON

Copyright © 2017 Pearson Education, Inc.

2-1

This chapter is largely unrelated to other chapters.
Key aspects covered in this chapter:

- Division of work based on specialization
- Benefits of specialization and trade
- Two-person economy and production possibility frontier (PPF)
- Introduction to a few technical terms related to economics
- Learn to quantify opportunity cost
- PPF of a country
- Different types of economic systems

Recall the simple economy example with two individuals: Collaborate, coordinate, and cooperate

- Human needs are better met when we are allowed to exchange our produce or our skills for G&S
- Of course it is not possible for a single individual to produce what all she/he wants to consume
- Time is a scarce resource and our skills are different; at the same time needs are unlimited!

The Economic Problem: Scarcity and Choice (1 of 2)

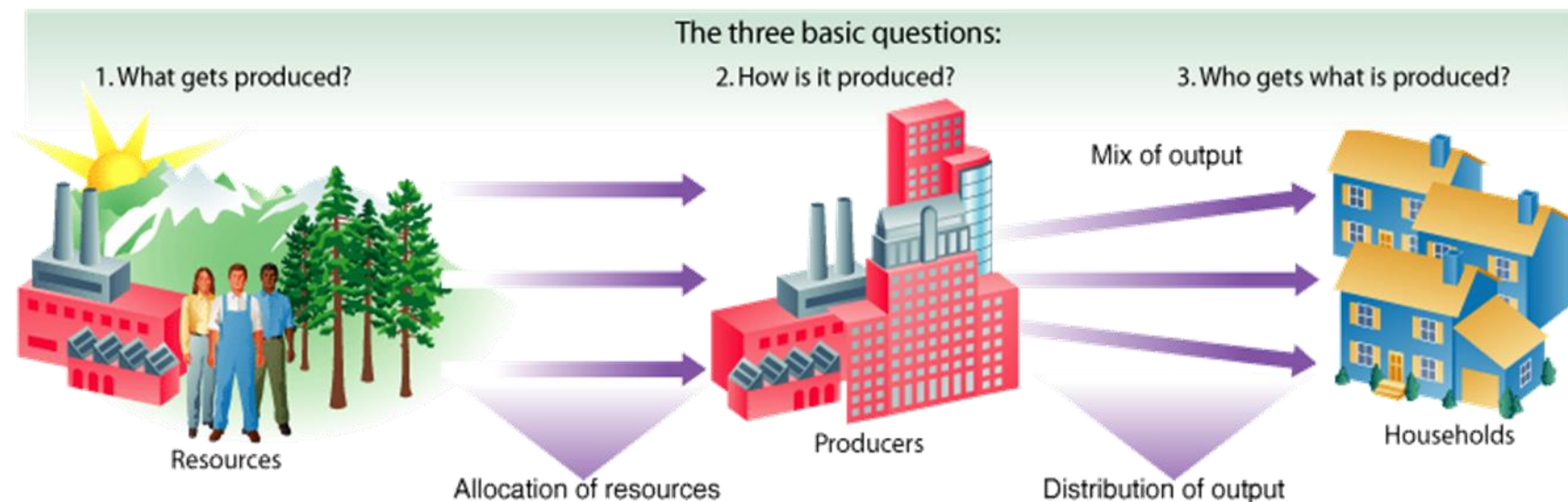
- As discussed in the introductory session, on the surface, economic issues seem quite different from one another.
- But the fundamental concern is *choice* in a world of scarcity.
- Individuals' choices determine three key features of society:
 - What gets produced?
 - How is it produced?
 - Who gets what is produced?

Discussion in section 2 is covered till this point.

The Economic Problem: Scarcity and Choice *(2 of 2)*

- **capital** Things that are produced and then used in the production of other goods and services.
- **factors of production** (or **factors**) The inputs into the process of production. Another term for resources.
- **production** The process that transforms scarce resources into useful goods and services.
- **inputs** or **resources** Anything provided by nature or previous generations that can be used directly or indirectly to satisfy human wants.
- **outputs** Goods and services of value to households.

FIGURE 2.1 The Three Basic Questions



Every society has some system or process that transforms its scarce resources into useful goods and services.

In doing so, it must decide what gets produced, how it is produced, and to whom it is distributed.

The primary resources that must be allocated are land, labor, and capital.

Scarcity, Choice, and Opportunity Cost

Scarcity and Choice in a One-Person Economy

- Nearly all the same basic decisions that characterize complex economies must also be made in a simple economy.
- A person must decide what to produce and how and when to produce it.

Scarcity and Choice in a One-Person Economy

Opportunity Cost

- The concepts of constrained choice and scarcity are central to the discipline of economics.
- **opportunity cost** The best alternative that we give up, or forgo, when we make a choice or decision.

Scarcity and Choice in an Economy of Two or More *(1 of 3)*

Suppose you have the following information about two individuals' daily production when they put all their resources into production of each output individually (interpret it as: its either poems or TV commercials in a day):

| | Krystal | Mark |
|------------------------|---------|------|
| Writing Poems | 8 | 12 |
| Writing TV Commercials | 2 | 4 |