

Foundations of Economics

Notes

SCARCITY

- All economic questions arise because we are unable to satisfy all our wants – we face...

• **Human wants and needs are more than available resources**

NEEDS VERSUS WANTS

- Wants: **desires for goods and services** would like to have but not need.
- Needs are a special kind of want, and refer to....
things required for Survival.
Such as food, water, and money/currency

FOUR FACTORS OF PRODUCTION

1. Land

- "gifts of nature"
- Includes all natural resources not modified by humans:
 - agricultural and non-agricultural land
 - Everything under and above the land

2. Labour

- Physical and mental effort that contributes to the production of goods.
- Examples: Efforts of a teacher, construction worker, an economist, doctor, taxi driver, plumber.

3. Capital (physical capital)

- Human-made factor of production used to produce goods.
- Examples: machinery, tools, factories, buildings, road systems... airports, harbours, electricity generated

4. Entrepreneurship

- Special human skills possessed by some people.
- Involves the ability to:
 - Innovate by developing new ways of doing things.
 - seek new opportunities for opening and running a business
 - organize the other factors of production, and
 - Takes risk of success or failure of a business

OTHER MEANINGS OF CAPITAL

Human capital

- Refers to the **skills, abilities, and knowledge** acquired by people, and... good level of health, all of which make them more productive.
- When you go to school or... get a vaccine.

Natural capital (environmental capital)

- Expanded definition of land, necessary for humans to live
- Also includes: air, soil, global climate, atmosphere
- Necessary for humankind's ability to live, survive and produce in the future.

Financial capital

- Financial instruments like stocks or bonds
- Money used to buy financial instruments

THE THREE BASIC ECONOMIC QUESTIONS

1. What to produce?
2. How to produce
3. For whom to produce

DOES EVERYTHING IN ECONOMICS HAVE A COST? Yes.

- **Opportunity cost:** Cost of not pursuing the next-best opportunity. Required to be a free-will choice.
- Opportunity cost is the value of the alternative
-

FREE GOODS VERSUS ECONOMIC GOODS

- **Free goods:** a good that is so abundant we say there is practically no... Scarcity.

Example: air, sunlight, water

- **Economics Goods:** a good that is considered scarce and involves an opportunity cost.

Example: clean air, clean water

WHAT IS ECONOMICS?

Economics is the social science that studies the choices individuals, businesses, governments and societies make as they cope with scarcity.

There are two "branches" to the study of economics:

1. **Microeconomics**
2. **macroeconomics**

MICRO AND MACRO ECONOMICS

- Microeconomics is the study of individuals, households, and firms' behaviour in decision-making and allocation of resources
 - o patterns of supply and demand
 - o determination of price and output, and
 - o individual markets (e.g. coffee industry)
- Microeconomics focuses on:
 - o unemployment
 - o national income
 - o GDP
 - o inflation, deflation
- Macroeconomics is the study of the behaviour and performance of an economy as a whole
- Macroeconomics focuses on:
 - o unemployment
 - o national income
 - o GDP
 - o inflation, deflation

POSITIVE AND NORMATIVE ECONOMICS

Positive (or analytical economics)

- Deals with:
 - facts
 - observation of world around Govt.
- Concerned with two types of statements:
 1. Descriptive
 - How things are / were
 - Example:
"Unemployment went to 7%"
 2. Conditional
 - If x, then y
 - Example: If cost groceries ↑
quantity sold will ↓
- Normative (policy) economics:
 - Deals with statements that contain:
value judgements
 - Cannot be confirmed or refuted solely by reference to facts.
 - Open to debate
 - Goals and policy statements of governments, firms, institutions and interest groups are usually normative statements.
 - Example: Municipal governments should provide more housing to homeless people

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Foundations of Economics Problem Sets

- Identify two or three of your most important needs and wants. Then explain whether these needs are satisfied by goods and services.

Food
Shelter
Internet) All are goods and services

- Why is economics a study of choices?

Choices of individuals, firms, and households that create an economy.

- Explain the relationship between scarcity and the need to avoid waste in the use of resources.

There are unlimited needs and wants but limited supply of resources. Wasting resources means a need / want not being fulfilled, where it could be.

- Using the concept of scarcity, explain why diamonds are far more expensive than water, even though diamonds are a want and water is a need.

Diamonds is much more scarce while water is more abundant.

- Read the scenarios below, then write whether the situation represents a want or a need.

a) You have been wearing the same pair of shoes for the past three years. You go to the store and buy a new pair of shoes.	Want
b) Your parents go to the store and buy bread, milk, and chicken for your family.	Need
c) You have a two-year old TV that works just fine. You purchase a new TV that has the newest technology.	Want

d) For the holidays you receive 15 gifts, such as the Nintendo Switch, a hover board, and an itunes gift card.	Want
e) On the way to school today, your parents get a flat tire. They immediately drive to the local tire business and have the tire replaced.	Need
f) Every morning you take a shower and brush your teeth. You find out that your family pays to have water in your house.	Need
g) A member of your family is sick and goes to the doctor who prescribes them medicine.	Need
h) This weekend, your grandparents bring you to the ice cream shop and buy you two ice cream cones.	Want
i) For your birthday, your parents rent out a bounce house and purchase cake, cookies, and a variety of party gifts.	Want
j) Your family buys a brand new car even though they already have two cars.	Want

6. Read the example below, then provide an example of a choice you recently had to make and the benefit and costs of the decisions.

Option	Choice	Benefit	Opportunity Cost
a) Go to school or stay home and play video games.	Stay home and play video games.	Enjoyment received from playing the games.	Going to school and learning.
b) Spend your time watching a movie or play a game of flag football outside.	watch a movie	Enjoyment from movie	not going outside to be active

c) Spend time with your family, or hang out with your friends.	Time w Farm	See family and enjoyment	Miss out on friends
d) Your parents give you the option of a jolly rancher or a Snickers bar.	Jolly Rancher	Jolly rancher enjoyment	Miss out on enjoyment of snickers
e) Stay home and sleep or go to school.	School	not have to deal w/ repercussions	Happy in moment

7. You were planning to spend Saturday working at your part-time job, but a friend asks you to go to the beach. Another friend asks you to hang out at the bowling alley. As another option, you considered taking the same time to study for your economics exam. Ultimately, you decide to go to the beach. You determine that if you had not gone to the beach you would have spent your time working.

- a) What is the opportunity cost of going to the beach?

Studying

- b) Why is there always a cost to every decision we make?

Every choice eliminates potential benefit of another choice

- c) Why is opportunity cost not the cost of every possible choice that we can make in our lives?

Opportunity cost is not present when there is no choice.

8. Which of the following is NOT part of the opportunity cost of attending university? Why?

Cost of tuition,
Cost of textbooks
Costs of meals

Income that could have been earned by working

Tuition, texts, meals is not opportunity while income is,

9. Would water count as a “free good?” Why or why not?

Yes - abundant. Clean is different

10. Read the scenarios below. Then write which factor of production is underlined and being described.

Scenario	Factor of Production
a) A baker uses <u>apples</u> to make his apple pies.	<u>Land</u>
b) A carpenter uses a <u>hammer</u> , <u>drill</u> , and <u>saw</u> to construct wood furniture.	<u>Physical Capital</u>
c) A <u>teacher</u> performs a writing lesson to her 5 th grade class.	<u>Labour</u>
d) The local McDonalds company uses a <u>computer</u> to record customers' orders	<u>Physical Capital</u>
e) The Holiday Inn employs <u>cleaning ladies/men</u> to prepare the rooms.	<u>Labour</u>
f) <u>Your parents</u> decide to open up a bagel shop in town and are excited to own their own company.	<u>Entrepreneurship</u>
g) The Globe and Mail newspaper uses <u>cameras</u> to take pictures for their newspaper and website.	<u>Physical Capital</u>
h) A taxicab driver uses their <u>taxi cab</u> as a way to provide transportation in the city.	<u>Physical Capital</u>
i) <u>Trees</u> from the forest are cut down and used to build homes in your neighborhood.	<u>Land</u>
j) In Ontario, <u>water</u> is used to create electricity.	<u>Land</u>

11. Read and identify the factors of production included in the following scenario. You and your family are really hungry and decide to order a pizza. You call the company and order a pizza. The information shows up on the company's computer, and the pizza-maker begins making the pizza. He mixes together the salt, flour, eggs, and milk, and then forms the pizza. The pizza-maker puts the pizza in the brick oven and waits 10 minutes for it to cook. The delivery person takes the pizza in the company car and delivers it to your door. You call up the owner and tell her how delicious the pizza was and how you can't wait to order again!

- Computer: Physical capital
- Pizza Maker: Labour
- Salt, flour, eggs, and milk: Land
- Delivery person: Labour

- Company car: Physical capital
- Owner: Entrepreneur or labour

12. Identify whether each of the following statements is positive or normative.

Statements	Positive or normative?
a) It is raining today.	Positive
b) It is too humid today.	Normative
c) The moon is made of blue cheese.	Positive
d) Economics is a study of choices.	Positive
e) Economics should be concerned with how to reduce poverty	Normative
f) If household savings increases, ceteris paribus, there will be a fall in household spending.	Positive
g) Households save too little of their income.	Normative

Great Job, you completed the worksheet!

Please answer the following reflection questions based on what you learned throughout the activity.

1. List 1-3 things that you learned about basic economic concepts.

1. _____

2. _____

3. _____

2. List 1-3 things that you want to know more about basic economic concepts.

1. _____

2. _____

3. _____

Central Concepts in IB Economics

Notes

WHAT IS A CONCEPT?

- Concepts are big ideas or important themes that are present throughout different topics.
- They link different areas of study together and help us see the big picture when thinking about economics.
- The IB has chosen nine central or "key" concepts for this course.

#1. SCARCITY

- **Scarcity:** the limited ability of resources relative to societies'... unlimited demand for resources
- **Economics** is... the study of how humans make decisions in the face of scarcity

#2. CHOICE

- Resources are scarce, so humans must make.... choices
- We cannot satisfy all needs & wants.
- With every choice, there is an opportunity cost
- Economics studies the consequences of our choices, both present and future.

#3. EFFICIENCY

- Efficiency is quantifiable.
- Efficiency = $\frac{\text{useful output}}{\text{total input}}$
- **Allocative efficiency:** making the best possible use of scarce resources to produce the combination of goods that give optimum for society - minimizing opportunity cost

#4. EQUITY

- **Equity:** condition of being fair or just.
- **Equality:** state of being equal
- Equity is a normative concept it is difficult to define and measure.
- For most economists, equity relates to how fairly income, wealth, and opportunity are distributed between different groups in society.

#5. ECONOMIC WELL BEING

- **Economic well being:** multi-dimensional concept relating to the level of prosperity and quality of living standards enjoyed by members of an economy
- Includes:
 - Present and future financial security
 - Ability to meet basic needs
 - Ability to make economic choices permitting achievement of personal satisfaction
 - Ability to maintain adequate income levels over the long term

#6. SUSTAINABILITY

- **Sustainability:**

- Ability of present generations to meet their needs without compromising future-generations from meeting their needs
- Often refers to limiting the degree to which economic activities of current generation are creating harmful environmental outcomes, such as resource depletion or degradation.

#7. CHANGE

- The economy is in a state of continual flux.
- Economists study change in:
 - i) **Economic theory**
 - From one situation to another situation that has been caused by a change in one or more variables
 - ii) **Real-world events**
 - Including change institutional, technological, social, political, and cultural environments in which economic events occur

#8. INTERDEPENDENCE

- Interdependence:** the idea that economic decision-makers interact and depend on each other.
- Consumers, firms, households, workers, and governments interact with each other and across nations to achieve economic goals.
- To an interdependent world, events in one part may give rise to unintended consequences

- Economists must take into consideration both intended and unintended consequences of economic and events when there is a high degree of interdependence.

#9. INTERVENTION

- Intervention** typically refers to... government intervention when govt becomes involved in the inner-workings of markets
- Markets offer many advantages to achieve economic objectives, but on their own do not achieve societal goals such as
 - **equity**
 - **sustainability**
 - **economic well-being**
- When this happens at the micro or macro levels, there may be a need for government intervention.
 - Economists and policymakers often disagree on the need for, degree and method of intervention.
 - Key debate in econ: advantages and disadvantages of free markets versus government intervention.

