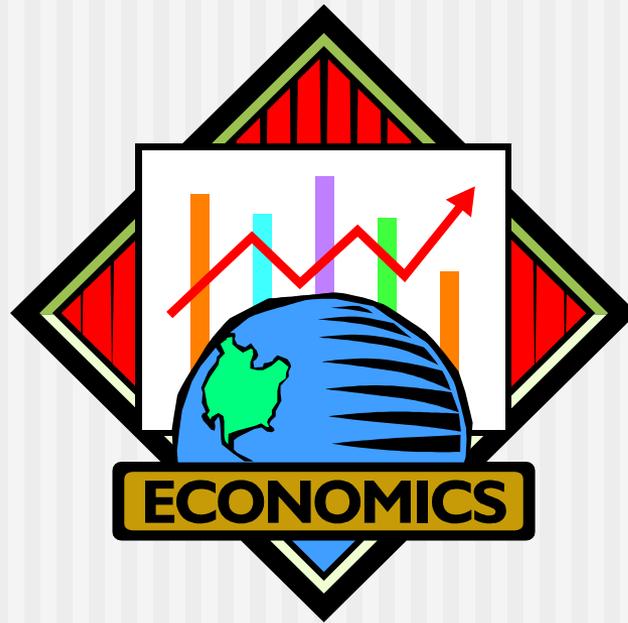


Chapter 1

What is Economics?



Section 1

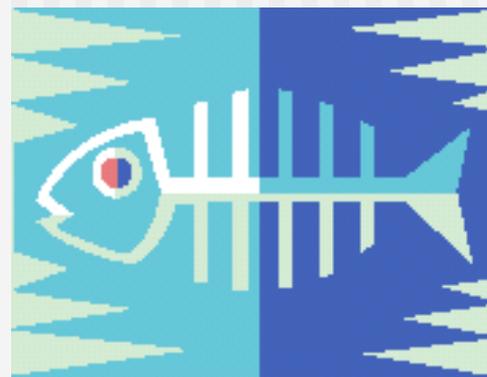
What is Economics?

- **Economics** is the study of how people try to satisfy what appears to be seemingly unlimited and competing wants through the careful use of relatively scarce resources
 - Enables us to become better decision makers
 - Making wise choices for political candidates
 - Understanding the free-enterprise system



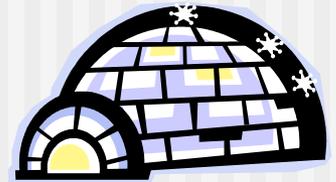
The Main Problem

- The fundamental economic problem facing all societies is
 - **Scarcity** is the condition where unlimited human wants face limited resources.
 - Economics is the study of how people satisfy wants with scarce resources.



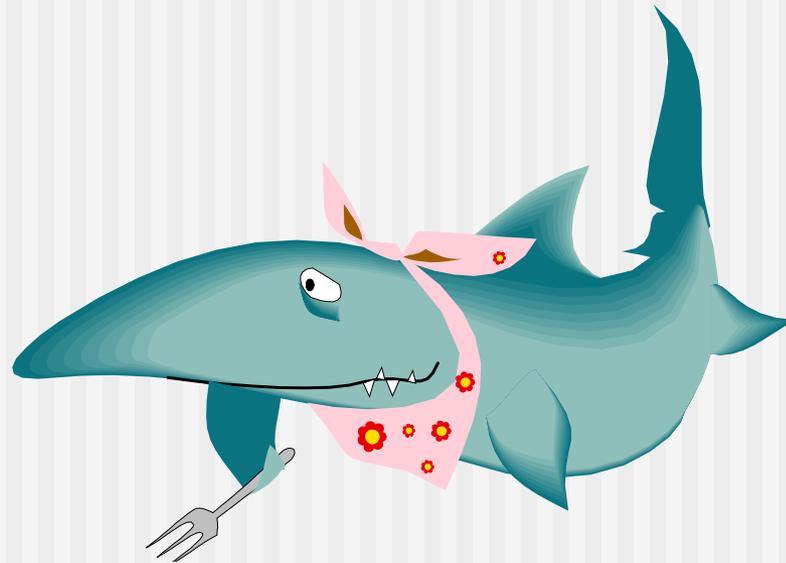
The Main Problem

- **need** is something basic that people need in order to survive.
 - Example: Food, clothing, and shelter.
- **want** is a way of deciding how you would like to get something you need.
 - Example, when you are hungry, your need is food. Your want may be pizza, or a taco, or a pear.



TINSTAAFL

- Someone has to pay for production costs
 - **There Is No Such Thing As A Free Lunch**



Unlimited Wants

Limited Resources

Scarcity

Choices

What to Produce

How to Produce

For Whom to
Produce

Three Basic Questions

- **What must we produce?**
 - Society must choose based on its needs.
- **How should we produce it?**
 - Society must choose based on its resources.
- **For whom should we produce?**
 - Society must choose based on its population and other available markets.

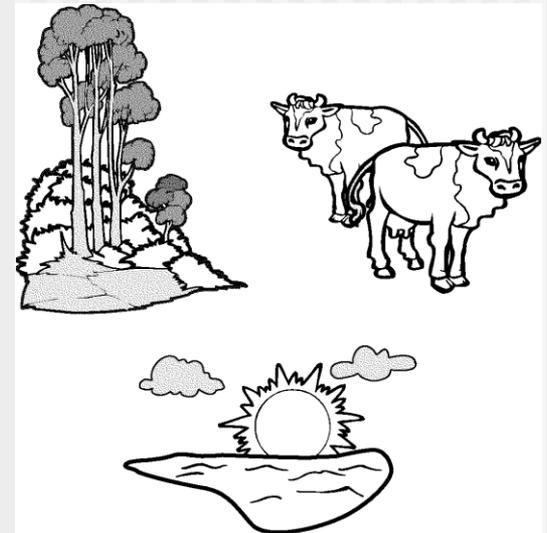
The Factors of Production

- Factors of production are resources necessary to produce what people want or need.



Land

- **Land** is the society's limited natural resources—landforms, minerals, vegetation, animal life, and climate.



Capital



➤ **Capital** is the means by which something is produced such as money, tools, equipment, machinery, and factories.

➤ **Financial capital** is the money used to buy the tools and equipment needed for production



Labor

- **Labor** is the workers who apply their efforts, abilities, and skills to production.



Entrepreneurs

- **Entrepreneurs** are risk-takers who combine the land, labor, and capital into new products.
 - Either start new business or bring new products to the market



Production

- **Production** is the process of creating goods and service
 - This is result of land, capital, labor, and entrepreneurs.
 - **Note!!** Everything we produce require these factors.



The Factors of Production

- Example of each factor of production
 - Wheat is needed to make flour for the cookies.
 - An oven is needed to bake the cookies.
 - Bakers are needed to make the cookies.
 - An entrepreneur is needed to pull these factors together.



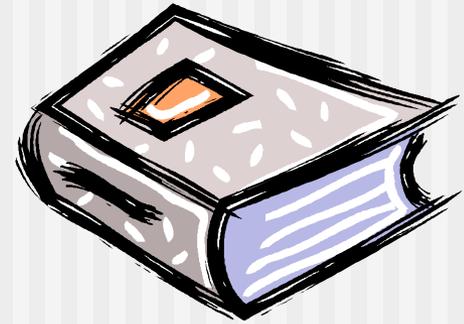
The Scope of Economics

- Study of Economics includes:
- Deals with the **description** of economic activity
 - Uses terms such as **Gross Domestic Product (GDP)**, which is the dollar value of all final goods, services, and structures produced within country's borders in a 12-month period.
- **Analysis** looks at the “why” and “how” of economic activity
 - why prices go up and down, for example, or how taxes affect savings.
- **Explanation** refers to how economists communicate knowledge of the economy and its activities to the society's population.
- **Prediction** refers to how yesterday's and today's economic activities advise us of potential future activity.

Section 2

Basic Economic Concepts

- **Economic products** are useful, at least a little bit scarce, and can be passed from one person to another.



Goods, Services and Consumer (continued)

- **Goods** are items that are economically useful or satisfy an economic want.
 - They are tangible and can be classified as consumer/capital and durable/nondurable.



Goods, Services and Consumer (continued)

- **Consumer good**, such as a sports car, is intended for use by individuals.
- **Capital good**, such as an oven, is made to produce other goods and services.
 - To arrive at an economic decision, a grid may be used to evaluate
- **Durable good** is any good that lasts 3 or more years when used on a regular basis
- **Nondurable good** is an item that lasts for less than 3 years when used on a regular basis.

Goods, Services and Consumer (continued)

- **Services** are work performed for someone and are intangible.
- **Consumers** use goods and services to satisfy wants and needs.



Value, Utility and Wealth

(continued)

- **Value** is how much something is worth in dollars and cents.



Value, Utility and Wealth

(continued)

- Puzzling is the **paradox of value**—a situation in which some things that people really do not need
 - Diamonds, are worth more than some things that people cannot live without, such as water.
 - Something must be scarce to be valuable.



Value, Utility and Wealth

(continued)

- Scarcity is not enough
- Must have **utility**, or the ability to be useful and satisfy people.



Value, Utility and Wealth

(continued)

➤ **Wealth** is the accumulation of goods that are tangible, scarce, useful, and transferable to another person.

- Does not include services.
- Nations, as well as individual people, own wealth.

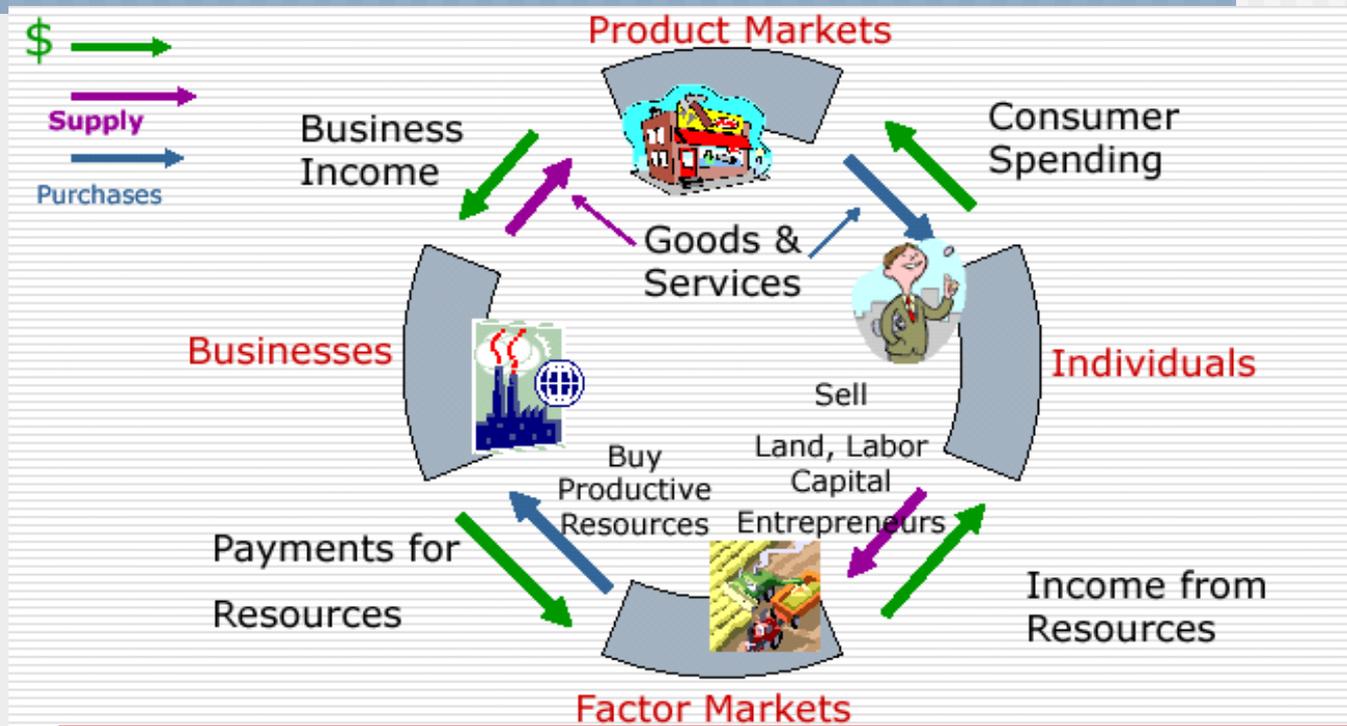


The Circular Flow of Economic Activity

- **Markets** are locations/ mechanisms for buyers and sellers to trade.
 - Classified as local, regional, national, global, and cyberspace (Internet).
- A **factor market** is where people earn their incomes.
 - Center on the four factors of production: land, capital, labor, and entrepreneurs.
- A **product market** is where people use their income to buy from producers.
 - Center on goods and services.



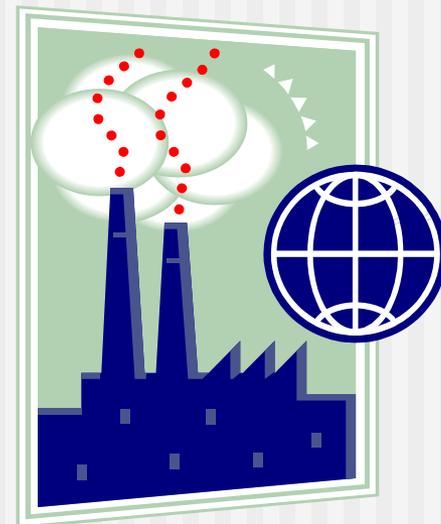
Circular Flow



The circular flow diagram shows the high degree of economic interdependence in our economy. The factors of production & the products made from them flow in one direction. The payment for the factors, which consumers spend on goods & services, flow in the opposite direction.

Growth & Productivity

- **Economic growth** occurs when a nation's total output of goods and services increases over time.
- **Productivity** is a measure of the amount of output produced by a given amount of inputs during a specific period of time.



Division of Labor & Specialization

- **Division of labor** is work that is divided up so that each worker does just a few jobs rather than a lot of different jobs.
 - A characteristic maybe an assembly line production
- **Specialization** takes place when factors of production perform tasks that they can do relatively more efficiently than others.



Division of Labor & Specialization (continued)

- **Human Capital** is the sum of the skills, abilities health, and motivation of people.
 - Government & Businesses can invest in human capital (labor) by providing education (training) and health care to improve the skill and motivation of its workers.



Depending On Each Other

- Productivity is also helped by **economic interdependence**—the fact that we depend on one another for goods and services
 - Actions in one part of the country or world that have an economic impact on what happens elsewhere



Section 3

Economic Choices & Decision Making

- **Trade-offs** are the alternative choices people face in making an economic decision.
 - A decision-making grid lists the advantages and disadvantages of each choice.



Costs and Benefits

- **Opportunity cost** is the cost of the next best alternative among a person's choices.
 - It's the money, time, or resources a person gives up, or sacrifices, to make his final choice.
 - Opportunity costs are incurred when trade-offs are made



Production Possibilities Curve

- The **production possibilities frontier** is a diagram that shows how goods and/or services can be combined in different ways in an economy that is using all its resources
- Economy at PPF is operating at full potential
 - **Shows the concept of opportunity cost**

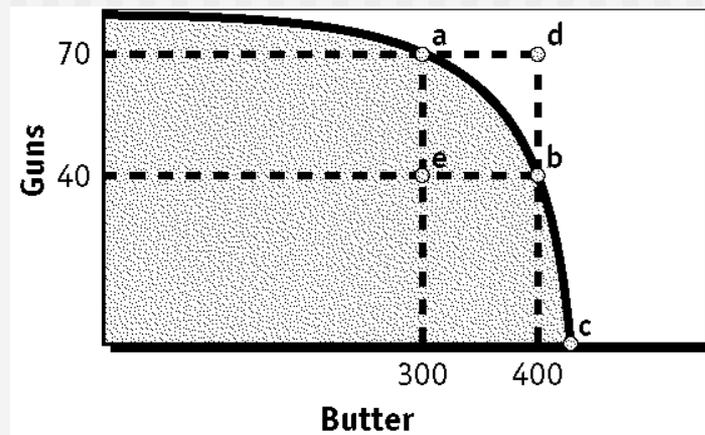


Diagram shows a country can produce 70 guns and 300 units of butter using all its resources.

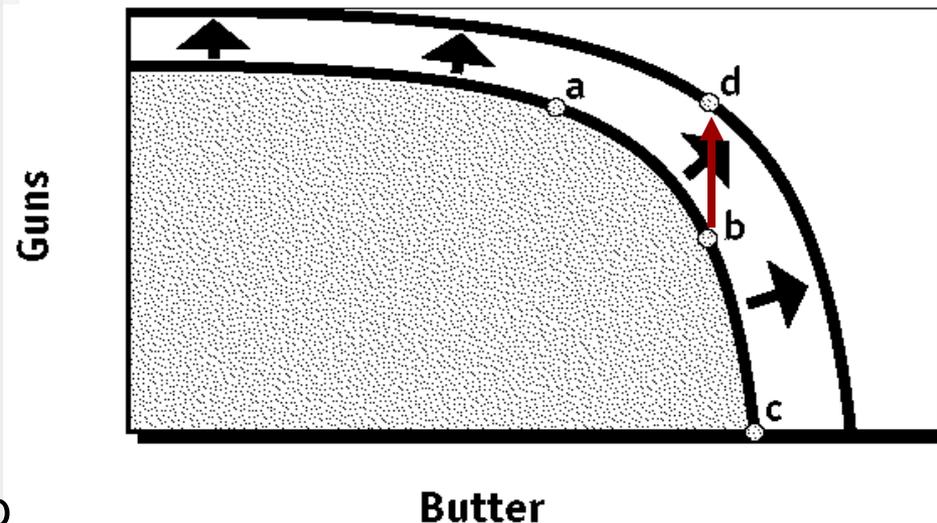
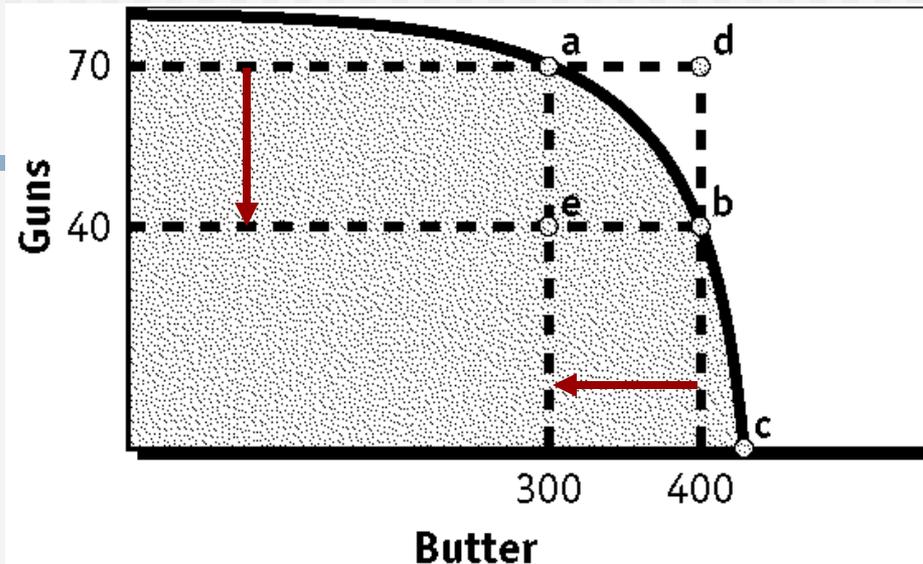
Production Possibilities Frontier

- Characteristic of a production possibilities frontier
- Illustrates the concept of opportunity costs
- Based on full employment of all resources
- Used by economists as a tool for description and analysis



Production Possibilities Curve

- **Alternative Possibilities**
Production can take place anywhere on or inside the frontier
- **Opportunity Cost** of producing 100 units of butter is the 30 guns given up
- **This graph is depicting** ▶
- **Economic Growth** Increased productivity and additional factors of production expand production possibilities
- Increasing productivity causes production to move from point b to point d



Thinking Like an Economist

- To help people make economic choices, economists use simple models
 - circular flow diagram of economic activity and the production possibilities frontier.
- **cost-benefit analysis** is a way of thinking about a problem that compares the costs of an action to the benefits received

The Road Ahead

- **Free enterprise economy** is a system in which consumers and privately owned businesses, rather than the government, make the majority of the **WHAT**, **HOW**, and **FOR WHOM** decisions
- **Standard of living** is the quality of life based on possessions that make life easier

