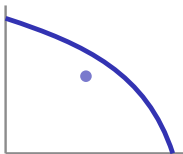


Basic Economic Ideas

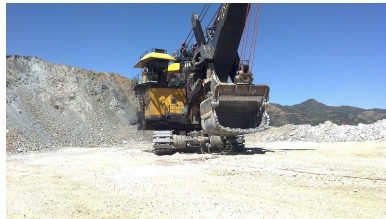
A-Level Economics ■ Topic 1

A-Level Economics



What we will cover

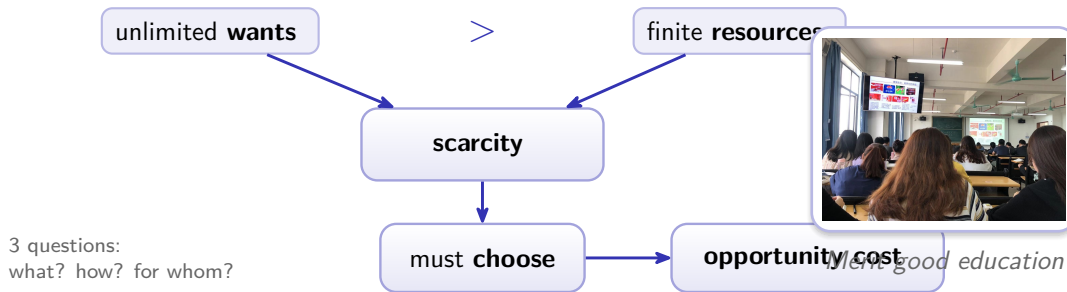
- 1 Scarcity & opportunity cost
- 2 Thinking like an economist
- 3 Factors of production
- 4 Economic systems & prices
- 5 Production possibility curve
- 6 Types of goods



scarce natural resources



The economic problem



Scarcity forces a choice on all three agents

scarcity

we never have enough to give everyone everything they want
– the one idea the whole subject starts from

consumers

buy a phone and you give up the holiday that money could have paid for

producers and firms

use a factory to make cars and you give up the trucks it could have made

governments

spend tax money on hospitals and you give up the schools that money could have built

the common answer

opportunity cost – the **next best alternative given up**, not the money spent

Every economic question is one of three: **what** to produce, **how** to produce it, and **for whom**. Scarcity is why all three must be answered.

Thinking like an economist

positive

a **fact** – can be
tested true or false

normative

an **opinion** – rests
on a value judgement

Ceteris paribus : change one thing, hold the rest fixed. **Microeconomics** studies one market;
macroeconomics the whole economy.

Economics as a social science

It studies how people behave when they make choices.

Like other sciences, it builds **models** (simple pictures of the real world) and tests them with data.

How economists actually reason

ceteris paribus

change one thing and hold everything else fixed – because the real world is too complex to reason about all at once

models

deliberately simplified, and judged by whether they **predict**, not by whether they are realistic

positive statements

claims about what **is** – testable against evidence

normative statements

claims about what **ought** to be – value judgements, which evidence cannot settle

why the split matters

economists disagree far more on normative questions than on positive ones

“A tax on sugar reduces consumption” is positive. “The government should tax sugar” is normative. The exam asks you to label them.



Factors of production



Each **factor of production** earns a reward; **enterprise** bears the risk of bringing the other three together.

The four factors, and what each is paid

land

all natural resources – including **non-renewable** ones like oil and coal, which can run out. Paid **rent**

labour

human work, both physical and mental. Paid **wages**

capital

man-made things used to produce – machines, tools, factories. Paid **interest**

enterprise

supplied by the **entrepreneur**, who organises the other three and **takes the risk**. Paid **profit**

Each factor earns a **different** kind of income, and that is how national income is divided. Naming the payment is half of many mark schemes.

Specialisation and the division of labour



Specialisation : make only what you are best at, then trade.

- + faster, better, lower cost per unit
- – boring; one absence can stop the line; narrow skills

Mobility : how easily a factor moves job (**occupational**) or place (**geographical**).

Division of labour: both sides of it

what it is a big job split into small tasks, each **worker** doing one of them repeatedly

gain workers get **faster and better** at one task

gain output per worker rises, so **costs fall**

cost doing one task is **boring**, so workers may quit

cost workers learn only one **narrow skill**, which makes them hard to re-employ

the dependency if one stage stops, the whole chain stops

Specialisation raises output and lowers **occupational mobility** at the same time. That tension runs through the whole labour-market topic.



Economic systems

How a country allocates scarce resources:

- **market economy** – prices decide; little government
- **planned economy** – the state decides all
- **mixed economy** – both; almost every real country

Economic systems, in detail



Exam: real economies are mixed — the question is how far market vs government decides

Economic systems form a spectrum: a pure market at one end, full government planning at the other, mixed economies in between.

Who decides, in each system

Market economy

Prices decide. The **private sector** – firms and households – owns the resources and follows the profit signal.

Planned economy

A **planned economy**, also called a **command economy**: the government owns resources and decides what is made, how, and for whom.

Mixed economy

Both. The private sector and the **public sector** each make decisions, and the argument is about where the line sits.

What is being allocated

Resources are what we use to make goods and **services** – and land includes **non-renewable resources** such as oil and coal, which can run out.

Every system answers the same three questions – what, how, and for whom. They differ only in who answers them.

The three systems, compared

market

strengths: choice, low prices, strong incentive to work and invent

weaknesses: a large gap between rich and poor, and some goods – **national defence** – simply not supplied

planned (command)

strengths: a smaller gap between rich and poor, and key goods provided for all

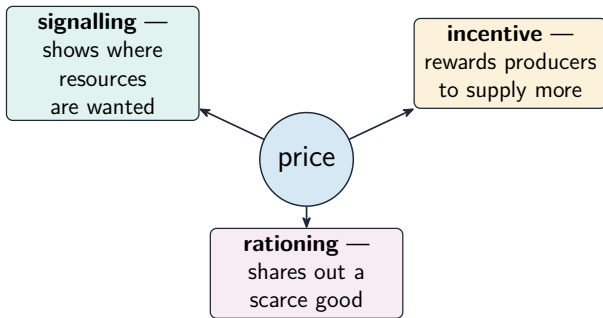
weaknesses: weak incentive, shortages and surpluses, and slow to change

mixed

tries to keep the good points of both – but **the right balance is hard to find**

No country sits at a pure extreme. China is officially a *socialist market economy*: markets set most prices while the state directs strategic sectors.

The price mechanism



In a market, the price does three jobs at once:

- **signalling** — shows where resources are wanted
- **incentive** — rewards producers to supply more
- **rationing** — shares a scarce good to those who pay



Production possibility curve

The **PPC** shows the most of two goods an economy can make.

- **on** – fully **efficient**
- **inside** – waste (e.g. **unemployment**)
- **outside** – impossible today (scarcity)

Moving along it shows the **trade-off** .

Reading a production possibility curve

On the curve

All resources used with full **efficiency** – and any more of one good now costs some of the other.

Inside it

Unemployment or waste: more of both goods is available at no cost.

Outward shift

Growth. It happens with more resources, or better ones – new **technology**, a bigger or more skilled workforce.

Inward shift

War or disaster can move the curve inward – **economic decline**.

The curve is a picture of opportunity cost: its slope *is* what one more unit of this good costs in units of that one.

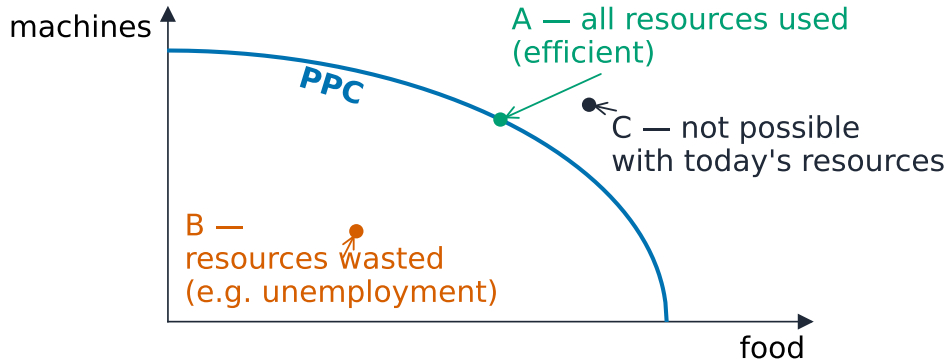
Worked example – why the PPC is bowed outwards

Why is a production possibility curve usually drawn rather than as a straight line?

- a straight line means a **constant** opportunity cost
- but factors are **not equally suited** to both uses
- move the best-suited first, so later units cost **more**
- so the curve steepens: **increasing opportunity cost**

The shape *is* the economics: a straight PPC would say a farmer and a machinist are interchangeable.

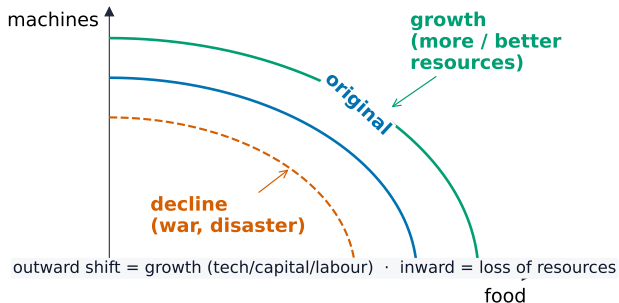
Production possibility curve, in detail



on = efficient · inside = inefficient · outside = unattainable

The **PPC** shows the most of two goods an economy can make.

Growth: shifting the curve



More or better resources shift the PPC **outward** – **economic growth** ; war or disaster shifts it inward. Making more **capital goods** now means fewer **consumer goods** today, but faster future growth.



Types of goods

Split by **rivalry** & **excludability** :

- **private good** – rival & excludable
- **public good** – **non-rivalry** and **non-excludability** : since non-payers cannot be shut out, nobody pays, and the **free-rider problem** means the market supplies none of it
- **merit good** / **demerit good** – misjudged via **information failure**

Types of goods, in detail

	Excludable	Non-excludable
Rival	Private good food, clothes	Common resource ocean fish, air
Non-rival	Club good cinema, toll road	Public good street light, defence

Exam: classify by rivalry × excludability — free-rider problem only for non-excludable goods

Split by **rivalry** and **excludability** : a **private good** is both; a **public good** is neither $\Rightarrow$ the **free-rider problem** ; a **merit good** or **demerit good** is mis-judged, through **information failure** .

Merit, demerit, public and free goods

merit good

better for you than you realise, so people buy **too little** – education, vaccination

demerit good

worse for you than you realise, so people buy **too much** – cigarettes, alcohol

public good

non-rival and **non-excludable**, so the market supplies none of it – street lighting, national defence

free good

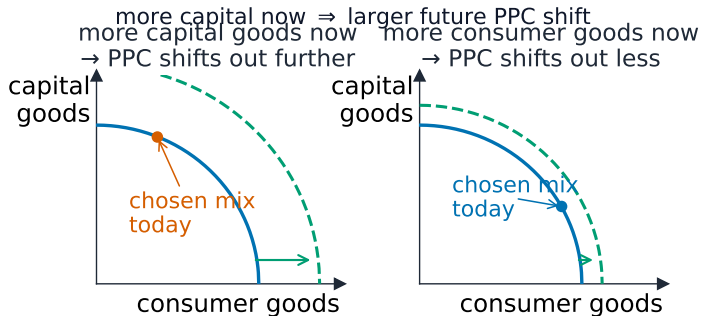
no scarcity at all, so no opportunity cost – and therefore no price

the link

the first three are all **information or excludability** failures, which is why each has a different remedy

Merit and demerit goods turn on what the *consumer* misjudges; a public good turns on what the *market* cannot charge for. Do not mix the two arguments.

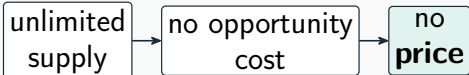
Shifts and growth



Choosing more capital goods today means fewer consumer goods now, but the future PPC shifts out further.

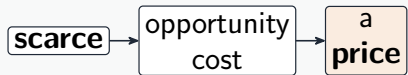
Free goods and economic goods

free good - air, sunlight



nobody gives anything up to use it

economic good - an apple

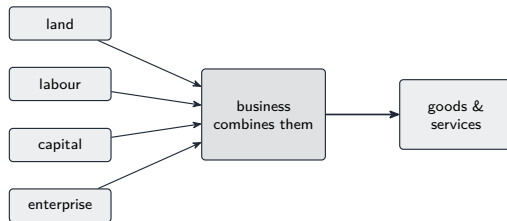


rivalry: if I eat it,
you cannot

excludability: no
payment, no apple

A free good has no opportunity cost and no price; an economic good is scarce, rival and excludable

Factors of production, continued



The four factors of production and the reward each earns

How mobile is a factor?

occupational mobility

how easily a factor moves from one **job or use** to another –
a teacher who retrain as a nurse

geographical mobility

how easily it moves from one **place** to another

labour is often immobile

family ties, the cost of housing, and **missing skills** all make
it hard for workers to move

why it matters

immobile labour is why unemployment can be high in one
region while vacancies go unfilled in another

land

geographically immobile by definition, though its *use* can
often change

Immobility is the reason markets clear slowly. Any policy answer about regional unemployment has to name which kind of mobility is missing.

Positive and normative statements

positive - a statement of **fact**

“a higher price of petrol
reduces the amount people buy”

can be **tested**:
true or false?

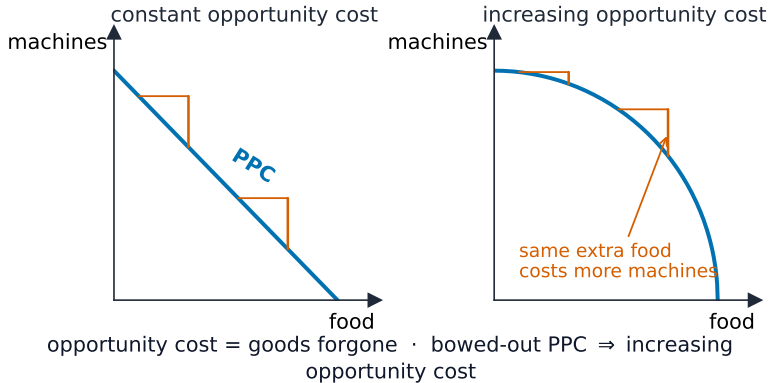
normative - an **opinion**

“the government *should*
make petrol cheaper”

cannot be tested -
a **value judgement** (“should”)

A positive statement can be tested; a normative statement is a value judgement

Production possibility curves



A straight PPC means each extra unit of food costs the same; a bowed PPC means each extra unit costs more and more machines.

Exam tips

- Frame answers around **scarcity and choice**: every choice has an **opportunity cost** – the next best alternative given up.
- Read a **PPC**: a point inside means unused resources, on the curve is efficient, outside is unattainable; the slope shows opportunity cost.
- Distinguish **positive** (a testable fact) from **normative** (“should”, a value judgement) statements.
- Classify goods: free versus economic, and **public / merit / demerit** goods (non-excludable, non-rival, and so on).



Worked example – opportunity cost on a PPC

An economy on its PPC moves from 60 tonnes of food + 30 machines to 50 food + 45 machines. What is the opportunity cost?

- Being **on** the curve means all resources are already fully and efficiently used.
- So gaining machines must mean **giving up** food.
- Machines +15, food -10 $\Rightarrow$ the opportunity cost of **15 machines is 10 tonnes of food**.
- Per machine: $10/15 = 0.67$ tonnes of food each.

Opportunity cost = **the next best alternative given up**. It exists only **on** the curve – inside it there are spare resources, so you can gain both.

Topic 1 – key takeaways

1

Scarcity

wants $>$ resources $\Rightarrow$ choice & opportunity cost

2

Factors

land, labour, capital, enterprise

3

Prices

signal, incentivise, ration in a market

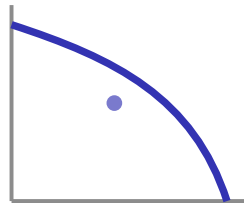
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PPC

on = efficient; outward shift = growth

Check yourself

- 1 What is the reward to capital?
- 2 “Petrol should be cheaper” – positive or normative?
- 3 A point inside the PPC shows what?
- 4 Why won't firms supply a public good?



Answers 1. interest 2. normative 3. wasted resources (e.g. unemployment)
4. free-rider problem (non-excludable)