

# Economics Part 1

Economic Foundations, An Introduction To Economics

# What Is Economics?

- Economics is the study of the allocation of scarce resources.
- A starting point to understand this subject is to consider the “Economic Problem” ...

# What is the Economic Problem?

- The **economic problem** is that people have an **unlimited amount of wants and needs, but we only have a finite amount of resources.** These resources are called **factors of production.**
- The purpose of economic activity is the production of goods and services to support the ever developing needs of society.

# The difference between wants & needs.

- **Need** – A need is something that is required for survival, such as food, water, or shelter.
- **Want** – A want is something we desire, but that is not necessarily needed for survival. For example, certain gadgets or pieces of technology, or certain fashionable items.

# Independent Task – 5 Minutes

Separate the following goods into wants and needs:

- Smartphone
- Bread
- Shoes
- Vacuum cleaner
- Vaccinations
- Gas/Electricity

# Independent Task – 5 Minutes

Separate the following goods into wants and needs:

- Smartphone – Want
- Bread – Need
- Shoes – Need (although some more expensive designer shoes may be considered a want)
- Vacuum cleaner – Want
- Vaccinations – Need
- Gas/Electricity – Need

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- **How to produce?** What methods are we going to use to produce these items? For example if you are a car manufacturer, should you use more machinery and robotics to build your cars, or should you use more labour?

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- **How to produce?** What methods are we going to use to produce these items? For example if you are a car manufacturer, should you use more machinery and robotics to build your cars, or should you use more labour?
- **Who are we producing for?** Who should benefit from the things that we produce and how should we distribute our goods and services to ensure that the people we wish to benefit actually benefit? For example, how does a government ensure that the poorest members of it's nation still get access to the most basic needs (food, water, shelter & healthcare)?

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- **Consumers** – Consumers are those who demand the goods and services, most people are consumers. Being a consumer doesn't always mean you have to pay. For example you may visit the doctor for a medical condition, you probably won't be charged by your doctor but you have still “consumed” the medical service.

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- **Government** – The Government are the people who decide how to distribute goods and services and who should benefit from this. The Government is controlled up of **elected representatives**, however, most of the work done by the Government is done by employed individuals.

# Discussion – 5 minutes

- A limited amount of space has become available for development in your local area. The local council are trying to decide whether to build a new hospital or a new factory on the site. Discuss with your partner what you would choose to do and why.

# Economics Part 1

Factors of Production



# Retrieval

1. What is the economic problem?
2. Give 3 economic groups...
3. Give 3 examples of a need and 3 examples of a want...
4. What 3 questions do economists consider when making decisions?

# Factors of Production

- All the resources we have talked about so far can be organised into 4 categories, Land, Labour, Capital & Enterprise. These are known as the four **Factors of Production**. Possession of any one of these factors of production grants the owner certain “rewards” or “benefits”.

# Factors of Production

- **Land** – Land includes all natural physical resources – e.g. fertile farmland, the benefits from a temperate climate or the harnessing of wind power and solar power and other forms of renewable energy. The reward for land is called **rent**.

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- **Capital** - Capital goods are used to produce other consumer goods and services in the future. The reward for capital is called **interest**.
- **Enterprise** - Regarded by some as a specialised form of labour input, enterprise (or an entrepreneur) is an individual who supplies products or services. Their main reward is the **profit** made from running the business.

# Independent Task 5 minutes

- Match the Factor of Production to the example:

Factor of Production	Example
Land	Accountant
Labour	JCB Digger
Capital	Gold Ore/Nugget
Enterprise	Market stall owner

# Independent Task Answers

Factor of Production	Example
Land	Gold Ore/Nugget
Labour	Accountant
Capital	Digger
Enterprise	Market stall owner



# Economics Part 1

Making Choices

# Retrieval

1. What are the four factors of production?
2. What are the rewards for each factor of production?
3. Give one example of each of the four factors of production.

# Making Choices

- As we have seen, one of the issues with having a finite number of resources is that sometimes we must make choices about what gets produced.
- Sometimes these choices are made by the **government**, however, sometimes these choices are made by **consumers**.
- For example, if a product does not generate sufficient demand to reward the entrepreneur with enough profit, it will not be produced.

# Making Choices

- How we as consumers make choices, is often influenced by **price**.
- The price of an item acts as a signal to the consumer to indicate the value of the product. The price of goods/services can be compared with one another to enable the consumer to make a choice.

# Opportunity Cost

- When we are making choices, we often consider the **Opportunity Cost** of the choice.
- Opportunity cost is the cost of any possible alternative when making a choice.
- For example, if you choose to buy a new car, this may leave you with no money to spend on a holiday, so the opportunity cost of buying a new car is missing the holiday.
- When we make decisions, we try to consider the costs and benefits of each option.

# Independent task – 5 minutes

- List 3 possible benefits of purchasing a car (e.g. 62 plate Vauxhall Astra J 2.0L SRI) & 3 further benefits of going on a holiday (eg to SkegVegas)

Car	Holiday

# Economics Part 2

The Role of Markets

# Retrieval

1. Name 1 factor of production and give an example of this factor.
2. What is opportunity cost?
3. What type of resource/Factor of production is a cow?
4. How are consumers decisions influenced?



# What is a market?

- At the most basic level, a market is an opportunity for buyers and sellers to meet and determine the price of goods/services.
- A market stall is a good example of this, although prices may have been set prior to the meeting, previous customers may have indicated the price they were willing to pay.

# Markets

- The term market has come to mean all the different ways that buyers and sellers interact.
- We can have internet interactions (Amazon/Uber), markets for complex goods such as currency, and platforms for genuine price discussions (e.g. Ebay).
- Markets can be local, regional, national or even global.

# The role of markets in the economic problem

- Markets are one way of determining how our finite resources get distributed according to our infinite demand.
- Many people want luxury items like sports cars and yachts. However, there isn't enough resources in the world to produce these items for everybody.
- Because of this, only people with enough wealth can purchase these items. In this model the **price** of the items determines who the items are distributed to.

# The role of markets in the economic problem

- The 'markets' for cars and yachts have determined the relative desire for these items and matched this against the cost of producing them.
- If enough people are willing to buy a product, and the amount they are willing to pay is satisfactory to the producer, then an interaction will take place.

# Independent task - 5 minutes

- Rank these items, in order of price, with 1 being the highest price and 5 being the lowest.
  1. Loaf of bread
  2. Pack of AA batteries
  3. Pint of milk
  4. Mars bar
  5. iPad mini

# Independent task - 5 minutes

- Rank these items, in order of price, with 1 being the highest price and 5 being the lowest.
  1. iPad mini
  2. Pack of AA batteries
  3. Loaf of Bread
  4. Mars bar
  5. Pint of milk

# Price

- What do you think determines the price of the iPad mini and why is it more expensive than a loaf of bread?

# Price

- What do you think determines the price of the iPad mini and why is it more expensive than a loaf of bread?
  1. Cost of manufacturing/materials
  2. Brand premium
  3. Government Subsidies reduce cost of bread
  4. Desirability



# What is the function of price?

- **Rationing** - The price of goods/services allows some people to afford these goods and services but prevents others from buying them. One's ability to purchase goods and services will depend on the wealth of the individual relative to the value of the product and the value of other products (i.e., the opportunity cost).

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- **Signaling** – the price signals something about the good/service that is important to potential buyers. A price rise may signal an increase in the cost of production. A price fall (for example, during a sale) may indicate that the seller will no longer continue to provide the good or service. In the UK, the price of healthcare is often 'free' (e.g. prescriptions for medicines for anyone under the age of 16) as the government wants to encourage consumption of health care.

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- **Incentive** – the price of a good or service can act as an incentive for a supplier to provide it. As prices rise, the supplier may make more profits and therefore receive a greater reward for investing in the supply of the product or service.

# Independent task – 10 minutes

- In October 2015, a 5p charge for plastic bags supplied by stores (such as supermarkets) was introduced UK wide for stores with more than 250 employees.
- Previously, many of the stores would have given the bags away for free as a method of attracting people to purchase goods within the stores. However, there was concern that an overuse of the bags was having a negative environmental impact.
- The introduction of the 5p charge (which is not collected by the government as a tax) was made to make people change their use of these bags. It was estimated that by October 2016, 500m less plastic bags were being used in the UK – a reduction of almost 85% compared to before the charge was introduced.
- Do you think the 5p charge on plastic bags was using price as a rationing, signalling or incentive function (explain your answer)?

# Economics Part 2

Factor and Product markets

# Retrieval

1. State 3 functions of price
2. State 3 economic groups
3. State 3 types of economic decision
4. What is the role of markets in the economy?

# The difference between factor and product markets

- **Factor market** – this is a market for factors of production (land, labour, capital and enterprise). For example, a livestock market may trade in sheep or cows. Markets exist for the trade in metals (e.g. aluminium). A fish market may trade in fish caught daily and may be attended by fish mongers (to sell the purchased fish at retail) or by restaurants using the fish to make meals.

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- **Product market** – this is a market concentrating on the sale of the final product or service. For example, if you wished to purchase a burger you may go to McDonald's or Burger King. If you wished to purchase a fence panel you may go to a DIY store or a timber merchant. If you wished to purchase a smartphone you may go to a network provider (e.g. Vodafone), a retailer (e.g. Argos) or the phone manufacturer themselves (e.g. Samsung).



# Independent task – 5 minutes

- Separate the following into factor and product markets:
  1. Bricks
  2. Coal
  3. Coffee beans
  4. Laptops
  5. Cappuccino
  6. Leather
  7. Light bulbs
  8. Trees

# Independent task answers

Factor Market	Product Market
Coal	Cappuccinos
Coffee Beans	Laptop
Trees	Leather
	Bricks
	Light Bulb

# Difference between a product and a service

- Products are physical objects or products that have been farmed, mined or created by a production process.
- Products can be transferred and delivered from buyer to seller.
- A service cannot be weighed or measured. A service is an activity of performing work for customers. At the end of the interaction, the service should provide satisfaction of the wants of the customer.
- At the end of a transaction the ownership of the product passes from the seller to the buyer.
- At the end of the process, the ownership of the service remains with its provider.
- After transaction, a product can be returned or exchanged. Services, however, cannot be returned.

# Economics Part 2

Economic Sectors

# Retrieval

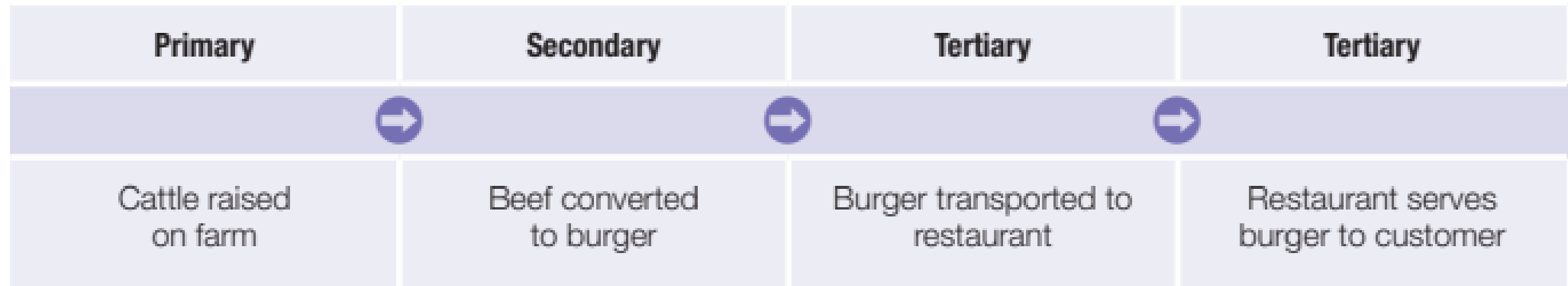
1. Give one difference between a product and a service.
2. Give the three functions of price and a brief description of each function.
3. Name the four factors of production.
4. What is the "reward" for each factor of production.
5. What is the difference between a factor and a product market?

# Economic Sectors

- The economy can be divided into three sectors.
  1. **Primary** – this is any part of the economy that is involved with acquiring the land economic resources (agriculture or mining). For example, coal must be mined, oil must be extracted, wheat must be farmed.
  2. **Secondary** – this is any part of the economy that is involved with the manufacturing or assembly of products. The UK manufactures cars, aeroplanes and pharmaceuticals.
  3. **Tertiary** – this is any part of the economy that is involved in the provision of services that support the primary and secondary sectors. In the UK, we are successful at financial services such as banking and insurance. Many people work in the retailing sector (the selling of produce).

# Economic Sectors

- A chain exists between the three sectors showing an interdependence – i.e. that each sector has a dependence on the other.



# Economic Sectors

- Primary, Secondary and Tertiary Sectors in the UK For many decades now, the tertiary sector has been the largest as a proportion of the total economy of the UK. Compare this to other countries in Europe...

Country (2016 stats)	Primary	Secondary	Tertiary
UK	1%	19%	80%
Nepal	32%	14%	54%
Poland	3%	38%	59%



# Independent Task – 10 minutes

1. Suggest a disadvantage of the UK having such a reliance on the tertiary sector.
2. Suggest a disadvantage of Nepal having large primary and tertiary sectors but low secondary sectors.
3. Suggest an advantage of Poland having a large secondary sector.

# Economics Part 2

Specialisation, Division of Labour and Exchange

# Retrieval

- Separate the following into products and services
  1. Packet of crisps
  2. Insurance
  3. Car maintenance
  4. Cinema ticket
  5. Photograph/Painting purchased from a shop
  6. Train Journey
  7. Take away coffee

# Specialisation

- For an economy to be effective at meeting the needs of its inhabitants it must become organised in such a way as to maximise efficiency.

# Specialisation

- Specialisation is the concept of how an economy will start to concentrate on the production of goods or provide services at which it is the most efficient. It will start to reduce the production of goods or provision of services where it is less efficient.
- For example, because of its climate, it would be very inefficient for the UK to mass produce bananas (it would require a great deal of cost in the provision of greenhouses). However, the climate in the UK allows the country to produce certain types of apple very efficiently – at relatively low cost and of good quality.

# Specialisation

- During the industrial revolution, Great Britain increased its production of products as it had large reserves of coal to fuel furnaces. However, now that many of those coal reserves have gone (or have become too expensive to mine) the UK is less efficient at producing energy to run large factories.
- Likewise, regions can specialise. For example, for many years the West Midlands region of England specialised in the production of cars allowing each car manufacturer to benefit from the skills of the local labour force and for the government to invest in infrastructure (e.g. motorways) to allow greater transport of finished goods.

# Advantages of Specialisation

- Higher output - Total production of goods and services is raised and quality can be improved.
- Variety - Consumers have access to a greater variety of higher quality products.
- Lower Prices - Increased competition acts as an incentive to minimise costs and keep prices down.

# Division of Labour

- Just as an economy can benefit from specialisation, a firm can benefit from allowing its workers to specialise in one or just a few parts of the business process. As such, a firm may separate its workforce so that many separate tasks are undertaken by specific individuals – this is called division of labour.



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- For example, in a restaurant, the owner may ask some employees to concentrate on cooking the food and others to serve the food to customers. In this way, it may be more effective to employ a trained chef who concentrates on a high-quality output of food and allow others to concentrate on customer service.

# Advantages of Division of Labour

- An individual worker becomes more competent at a task that they repeat many times. Their output should therefore increase.
- This increase in **productivity** per worker reduces the overall production cost per unit.
- The employer is more able to afford specific training for individuals as their output will increase and justify that investment.
- Workers can repeatedly use a single tool, making it more cost effective for a firm to purchase that tool. This may reduce the cost of production or increase productivity for that worker.

# Disadvantages of Division of Labour

- When an individual repeats tasks many times, they may start to become bored with the job they are doing. This may lead to lower levels of morale which, in turn can lead to lower levels of output and quality of production.
- If a job becomes more boring, an individual is more likely to look for another job. This can lead to high levels of **staff turnover** (the rate at which employees leave a workplace).
- An increase in mass-produced standardised goods may reduce choice for consumers

# Exchange

- For specialisation and division of labour to be a valuable method for improving efficiency in an economy, there must be a method of 'exchange'. For example, if the UK does specialise in the production of apples, it would benefit from a system where it can exchange some of these apples for bananas or other foodstuffs it has not produced.
- Likewise, if an individual specialises in one part of a production process that individual needs to be able to buy other goods and services that they are not able to provide for themselves.

# Exchange

- Economies have developed methods of exchange so that they can benefit fully from the advantages of specialisation and division of labour.
- The primary method of exchange, of course, is 'money'. The UK can directly swap apples for bananas from another country but it is more likely to sell the apples first. Individuals are now more likely to be paid in wages which they use to purchase products and services from other firms.

# Independent task



Consider this image of a pit stop at a Formula One race. Individual drivers need to replace the tyres on their cars at least once (often twice or three times) per race. Each wheel has three people allocated to it. There is one person at the back of the car and one person at the front using 'jacks' to temporarily lift the car to enable the tyres to be replaced and another person holding a board to indicate to the driver when it is safe for them to continue with the race.

Why do you think the Formula One driving teams use so many people to change the tyres in the middle of a race?