BASIC ECONOMIC CONCEPTS

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OBJECTIVES

1. TO EXPLAIN THE BASIC ECONOMIC CONCEPTS

2. TO EXPLAIN THE CONCEPT OF PRODUCTION POSSIBILITY CURVE (PPC)

3. TO EXPLAIN THE CIRCULAR FLOW IN CLOSED ECONOMIC
Basic ECONOMIC concepts

(SCARCITY)
Eg. Land, labor, capital...)

(CHOICE)

(OPPORTUNITY COST)
ECONOMICS - "science of scarcity"

Scarcity

Choices

Opportunity Cost
What is given up
In other words
"THIS is not the case”.

"No horn of plenty”

Choices

Unlimited Needs and Wants Demand

Limited Resources Supply

In other words
"THIS is not the case”.

"No horn of plenty”
Human wants

- Unlimited wants
Resources

• used to produce goods / services to satisfy human wants

• limited in supply

• scarce: i.e. their quantities are insufficient to satisfy all human wants
Types of resources

• Natural resources: e.g. sunshine, rain, crude oil

• Human resources: labour service

• Man made resources: e.g. machines, equipments
Resources – Factors of Production

- **Natural resources** (Land) – “free gifts of nature”
  - Land, minerals, oil, forests, air, and timber

- **Capital Resources** – “manufactured aids to production”
  - Tools, machines, equipment, factories
  - Things used in producing goods and services and getting them to consumers.

- **Human Resources** (Labor) – “mankind’s physical and mental talent”
  - These are the skills people have that are used to produce goods and services.

- **Entrepreneur** – the individual who combines the factors of production in order to produce a good or service.
  - Risk taker, policy maker, and innovator
The Factors of Production

**Land** includes the “gifts of nature,” or natural resources not created by human effort.

**Capital** includes the tools, equipment, and factories used in production.

**Labor** includes people with all their efforts and abilities.

**Entrepreneurs** are individuals who start a new business or bring a product to market.
Scarcity

- Meaning: Resources are insufficient (limited) to satisfy ALL human wants (unlimited)
- A relative concept: we want more than we have
- Basic economic problem in human societies
- What we should do?
  - Make an efficient choice
- Method to overcome
  - Less our wants or needs
  - Use the products efficiently
  - Get more resources
  - Improve the use of resources
Choice

• Caused by
  – Scarcity problem

• What we should do?
  – Make the best choice among others.
Making choices

• Which restaurant will you go for lunch?

• What would you like to study at university?

• What will you buy with $100? CD or dress?

• Which girl (boy) will you marry?
**Concept Map**

- Unlimited human wants
- Relative limited resources
- Scarcity
- Choice
- Concept of opportunity cost in terms of the highest-valued option forgone
Opportunity Cost

• Definition –
  – Opportunity cost is the highest-valued option forgone
  – the cost expressed in terms of the next best alternative sacrificed

• Helps us view the true cost of decision making

• Implies valuing different choices

• Decisions require comparing costs and benefits of alternatives.
  – ±Whether to go to college or to work?
  – ±Whether to study or go out on a date?
  – ±Whether to go to class or sleep in?
“The Economic Problem”

- **Scarcity… What is it?**
  - Limited resources but unlimited wants

- **Unlimited wants VS Limited Resources**
  - You can’t buy 10 candy bars if the store only has 5 candy bars to sell.
  - Can’t buy 3 burgers if you only have enough money for 1.

- What are some things that you “want” to have? Do you have the resources to purchase them?

- **Needs VS Wants**
  - What are some of your needs...wants.
**PRODUCTION POSSIBILITY CURVE (PPC)**

**DEFINITION**
- How much the production can be produced by economic if all of resources efficiently used.
- Known as transformation function.

**ASSUMPTIONS**
- Produce 2 type of products
- Limited in FOP
- Technology level is fixed
- Short term period
- Economics achieve maximum efficiency level

**TYPE OF CURVES**
- Straight line (opportunity cost constant)
- Convex (opportunity cost increase)
- Concave (opportunity cost decrease)
This PPC Line means we are operating at full capacity with best available resources/technology & producing at its full potential.

Inefficient

Unattainable
[More/better Resources, Technology]

*Shows opportunity cost more than anything
1. **Resources are fixed**. There is no way to increase the availability of land, labor, capital or entrepreneurship. However, reallocation of these resources is possible.

2. **All resources are fully employed**. No unused land, labor, capital, or entrepreneurship exists. The economy is running at full production and producing goods and services at the least cost (productive efficiency).

3. **Technology is fixed**. No new technological breakthroughs. PPC represents one specific time period.

4. **Only two things can be produced**[2-good model] “There is no free pizza.”
   
   [We are freezing the economy in time to focus on the economy’s productive alternatives based on research and technology of today.]
1. **Scarcity** is represented by the frontier line.

2. **Choices** represented by pts A, B, or C.

3. **Opportunity Cost** is illustrated in terms of moving from one point to another when resources are utilized to their full potential. [must make choices]

4. **Efficiency** - producing maximum output with available resources and technology. We can't increase production of one good without decreasing that of another.

5. **Economic growth** occurs for one of two reasons.
   - A. **More resources** [land, labor, or capital] become available.
   - B. **Technology** improves. [more outputs from same inputs]
TYPES OF CURVE

Increasing Cost

Constant Cost

Decreasing Cost
## A Production Possibilities Table and Curve

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<th>Number of butter</th>
<th>% of resources devoted to production of butter</th>
<th>Pounds of guns</th>
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</table>
A PRODUCTION POSSIBILITIES TABLE AND CURVE

Guns

1 pound of butter
2 pounds of butter
5 pounds of butter

Butter

4 guns
3 guns
12
11
10
9
8
7
6
5
4
3
2
1
0

A
B
C
D
E
F

1 gun
3 guns
4 guns
5 pounds of butter
2 pounds of butter
1 pound of butter
The WHOLE PPC represents “FULL PRODUCTION”

- Productive Efficiency
- Full-Employment of Resources
A, B, C, D, E, F

- Combination of efficient production
- Resources/FOP used efficiently

P

- Inefficient in production
- A lot of resources can be used
- Resources wastage

Q

- Inefficient in production
- Scarce in resources
In production, we’d like to have *productive efficiency* - achieving as much output as possible from a given amount of inputs or resources.

Any point within the production possibility curve represents inefficiency.

**Inefficiency** – getting less output from inputs which, if devoted to some other activity, would produce more output.
EFFICIENCY AND INEFFICIENCY

Unattainable point, given available technology, resources and labor force.
Can we produce outside the production possibility curve?
- Can we have more?
Society can produce more output if:

- Technology is improved.
- More resources are discovered.
- Economic institutions get better at fulfilling our wants.
CHANGE IN PPC CURVE

1. INCREASE IN PRODUCTION FACTORS
   - LABOR
   - CAPITAL

2. TECHNOLOGY INCREASE
“OUR ECONOMY IS DRIVEN BY TECHNOLOGICAL ADVANCEMENT”
The Circular Flow is an abstract, oversimplified model, showing how economic transactions [resources, products (g/s), and money] take place.

1. a. Goods and services
2. b. Consumer expenditures
3. c. Land, labor, cap., entrepreneur
4. d. Rent, wages, interest, & profits
GOVERNMENT’S ROLE in a Mixed Economy

NET TAXES FLOW TO GOVERNMENT FROM BUSINESSES

BUSINESSES

GOODS & SERVICES

BUSINESSES

GOVERNMENT

GOODS & SERVICES

GOVERNMENT

GOODS & SERVICES

REVENUE

CONSUMPTION

PRODUCT MARKET

GOVERNMENT GOODS & SERVICES FLOW TO BUSINESSES

HOUSEHOLDS

NET TAXES FLOW TO GOVERNMENT FROM BUSINESSES

RESOURCES

INPUTS

$ COSTS

$ INCOMES

GOODS & SERVICES

$ CONSUMPTION

$ INCOMES

GOODS & SERVICES

RESOURCES

INPUTS

BUSINESSES
CONCLUSION

- Limited resources in family
  - Income
  - Time
- This limited resources:
  - Family cannot satisfy all the needs & wants at one time.
  - So, All resources must be fully utilized.

- A PPC shows all combinations of goods & services that can be produced given available resources & technology.
- A PPC is used to illustrate concepts such as scarcity and opportunity cost.
- Circular flow in closed economic.
THANK YOU FOR YOUR ATTENTION