WJEC (Eduqas) Economics A-level

Microeconomics

Topic 1: Scarcity and Choice

1.1 Scarcity, choice and opportunity cost

Notes

The basic economic problem

- The basic economic problem is scarcity. Wants are unlimited and resources are finite, so choices have to be made. Resources have to be used and distributed optimally.
- For example, if you only have £1 and you go to a shop, you can buy either the chocolate bar or the packet of crisps. The scarcity of the resource (the money) means a choice has to be made between the chocolate and the crisps.
- This gives rise to **opportunity cost**. The opportunity cost of a choice is the value of the next best alternative forgone. In the above example, the opportunity cost of choosing the crisps is the chocolate bar.
- If a car was bought for £15,000 and after 5 years the value depreciates by £5,000, the opportunity cost of keeping the car is £5,000 (which could have been gained by selling the car), regardless of the starting price.
- Opportunity cost is important to economic agents, such as consumers, producers and governments. For example, producers might have to choose between hiring extra staff and investing in a new machine. The government might have to choose between spending more on the NHS and spending more on education. They cannot do both because of finite resources, so a choice has to be made for where resources are best spent.
- When producing goods, the economy has to consider the following questions:
    - **What to produce:** determined by what the consumer prefers. Consumers tell producers what they prefer by demanding goods and using their 'spending votes'.
    - **How to produce it:** producers seek profits and aim to minimise production costs
    - **For whom to produce it:** whoever has the greatest purchasing power in the economy, and is therefore able to buy the good

Economic and free goods

- **Economic goods** benefit society, have the problem of scarcity and have an opportunity cost. Since they are scarce, they have some value, so consumers will pay for them, and they can be traded.

- **Free goods** have no opportunity cost, because there is no scarcity of the good. For example, air and water are free goods. These goods are not traded because they are freely available.