Ib ap economics unit 1 introduction to economics

Literature, Russian Literature

IB/AP Economics Unit 1 Introduction to Economics Introduction to Economics AP and IB Economics Unit 1 Definitions of social science and economics Definitions of microeconomics and macroeconomics Definitions of growth, development and sustainable development Positive and normative concepts Ceteris paribus Scarcity - factors of production: land, labor, capital and management/entrepreneurship - payments to factors of production: rent, wages, interest, profit Choice Utility: basic definition Opportunity cost - Free and economic goods - Production possibility curves: definition >> diagrams showing opportunity cost, actual and potential output >> diagrams showing economic growth and economic development Rationing systems - basic economic questions >> what to produce? >> how to produce? >> for whom to produce? - mixed economies >> public >> private >> central planning vs. free market >> economies in transition Welker's Wikinomics www. welkerswikinomics. com 1 IB/AP Economics Unit 1 Introduction to Economics Introduction to Economics What is Economics? Question: What " law of nature" does the science of aerospace engineering attempt to overcome? Answer: gravity Question: What " law of nature" does the science of economics attempt to overcome? Answer: scarcity The Basic Economic Problem: Humans' wants and needs are infinite, while the resources needed to satisfy those wants and needs are limited and scarce.

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IB/AP Economics Unit 1 Introduction to Economics Introduction to Economics What is Economics? Scarcity - definition: something is scarce when it is both desirable and limited. Not all goods are scarce. Some goods that humans consume are infinite... Place the following words under the correct category, Scarce or Not Scarce Scarce or Murderers Computers Swiss francs factory workers Water HIV Oxygen Mosquitos British Pounds Doctors Creativity Nitrogen Sewing machines Diamonds Worms Happiness Apartments in Zurich Love Clouds Teachers Dirt Football players Air not scarce?

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IB/AP Economics Unit 1 Introduction to Economics Introduction to Economics What is Economics? Your first economics riddle: The Diamond/Water Paradox Something to think about: - Nobody needs diamonds, yet they are EXTREMELY EXPENSIVE - Everybody needs water, yet it is EXTREMELY CHEAP Why are diamonds so expensive? Why is water so cheap?

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IB/AP Economics Unit 1 Introduction to Economics Introduction to Economics What is Economics? Free goods and economics goods What is meant by " goods" in economics? - Goods are... - Haircuts, cars, toothbrushes, TVs, movies, happiness, shoes, vacations, friendship, hamburgers, love, jewelry, education, air (to breathe, duh!), fresh water, public transportation, sunshine, etc... Some goods are ECONOMIC goods: Scarce resources are used in the production of economic goods. Some goods are FREE goods: The resources used in the production of free goods are NOT scarce. Usually, free goods are those things you enjoy that you don't have to pay for! the stuff people WANT because it make us feel GOOD! From the list above, identify which are FREE and which are ECONOMICS goods Free goods or Economic goods Welker's Wikinomics www. welkerswikinomics. com 5

IB/AP Economics Unit 1 Introduction to Economics Introduction to Economics Do you think like an Economist? Answer the questions to the best of your ability. Discuss with a classmate if you become stumped. T T T T T T T T T T F F F F F F F F F F Because it is desirable, sunshine is scarce. Because it is limited, polio is scarce. Because water covers three-fourths of the earth's surface and is renewable, it cannot be considered scarce. The main cost of going to college is tuition, room and board. If mass transportation fares are raised, almost everyone will take the trains anyway. You get what you pay for. If someone makes an economic gain, someone else loses. If one nation produces everything better than another nation, there is no economic reason for these two nations to trade. A non-regulated monopoly tends to charge the highest possible price. A business owner's decision to show more care for consumers is a decision to accept lower levels of profits. Source: NCEE's " AP Microeconomics" by John Morton Welker's Wikinomics www. welkerswikinomics. com 6 IB/AP Economics Unit 1 Introduction to Economics Introduction to Economics What is Economics? Discussion Quesiton: What does Economics mean to YOU? Economics is the study of... - - - - - scarcity resources trade-offs opportunity cost marginal analysis - - - - - producers/consumers supply/demand trade markets prices Microeconomics vs. Macroeconomics Welker's Wikinomics www. welkerswikinomics. com 7 IB/AP Economics Unit 1 Introduction to Economics Introduction to Economics What is Economics? Two fields of Economic study: Micro and Macro Economics is divided into two main fields of study Microeconomics: Studies the behaviors of INDIVIDUALS within an economy: Consumers and producers in particular markets. Examples: The Automobile market in Switzerland, the market for movie tickets in Zurich, the market for airline tickets between the US and Europe, the market for vacations to Spain, the market for international school teachers. Macroeconomics: Studies the total effect on a nation's people of all the microeconomic activity within that nation. The four main concerns of macroeconomics are: 1) total output of a nation, 2) the average price level of a nation, 3) the level of employment (or unemployment) in the nation and 4) distribution of income in the nation Examples: Unemployment in Canada, inflation in Zimbabwe, economic growth in China, the gap between the rich and the poor in America Welker's Wikinomics www. welkerswikinomics. com 8

IB/AP Economics Unit 1 Introduction to Economics Introduction to Economics What is Economics? Micro Examines: - Individual markets - the behavior of firms (companies) and consumers - the allocation of land, labor and capital resources - Supply and demand - The efficiency of markets - Product markets - Supply and Demand - Profit maximization - Utility maximization - Competition - Resource markets - Market failure Macro Examines: - National markets - Total output and income of nations -

Total supply and demand of the nation - Taxes and government spending - Interest rates and central banks - Unemployment and inflation -

Income distribution - Economics growth and development -

International trade Welker's Wikinomics www. welkerswikinomics. com 9

IB/AP Economics Unit 1 Introduction to Economics Introduction to Economics What is Economics? Economics is about... Scarcity: Economics is about the allocation of scarce resources among society’s various needs and wants. Resources: Economics is about the allocation of resources among society’s various needs and wants. Tradeoffs: individuals and society as whole are constantly making choices involving tradeoff between alternatives. Whether it’s what goods to consume, what goods to produce, how to produce them, and so on. Opportunity Cost: “ the opportunity cost is the opportunity lost". In other words, every economic decision involves giving up something. NOTHING IS FREE!! The Basic Economic Problem: Humans' wants are unlimited, while the resources needed to meet those wants are limited and scarce Welker's Wikinomics www. welkerswikinomics. com 10

IB/AP Economics Unit 1 Introduction to Economics Introduction to Economics What is Economics? Economics is about... Producers (firms) and consumers (households): The economy is made up of these two major groups (there’s also government, but that comes later). Most interactions in the marketplace are between households (that’s us) and firms (that’s the companies who make the stuff we demand) Supply and Demand: Economics is about supply and demand. We (households) are the demanders and they (firms) are the suppliers. The price we pay is determined by the level of demand and the level of supply of any particular good. Trade and exchange: Without trade, none of us would be here right now. Economics will help you understand how trade makes everyone better off Markets: Markets are where all economic transactions take place. There are many different kinds of markets, some more competitive than others Your first lesson in Economics - SCARCITY EXISTS All resources are limited, yet human wants are unlimited. Economics is the science devoted to dealing with the problem of scarcity.

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The Economic Revolution: from " The Worldly Philosophers"

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The Economic Revolution: from " The Worldly Philosophers"

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The Economic Revolution: from " The Worldly Philosophers" Reading discussion questions: - How is the struggle against scarcity a struggle for survival of man? - Is man by nature a social creature? How does man's nature pose a challenge to his survival? Discuss... - Discuss the benefits and dangers of the two ways societies organized economic activities throughout most of human history -tradition -command - Why was there no need for " economists" throughout most of human history? - " It was not at all obvious that with each man out only for his own gain, society could in fact endure. It was by no means clear that all jobs of society - the dirty ones as well as the plush ones - would be done if custom and command no longer ran the world. When society no longer obeyed one man's dictates, who was to say where it would end?" - Evaluate the author's claim that the economic revolution was " fundamentally more disturbing by far than the French, the American, or even the Russian Revolution." Welker's Wikinomics www. welkerswikinomics. com 14 IB/AP Economics Unit 1 Introduction to Economics Introduction to Economics Opportunity Cost Opportunity Cost (is the opportunity lost) The MOST important concept in all of economics is that of Opportunity Cost Because resources are scarce, every decision humans make involves tradeoffs. You must give something up in order to have something you want

Opportunity Cost: The opportunity cost of anything is what is given up in order to have it. The opportunity cost is the opportunity lost! - The opportunity cost of watching TV on a weeknight is the benefit you could have gotten from studying. - The opportunity cost of going to college is the income you could have earned by getting a job out of high school - The opportunity cost of starting your own business in the wages you give up by working for another company - The opportunity cost of using forest resources to build houses is the enjoyment people get from having pristine forests. Examples: Opportunity Cost - Solman video Welker's Wikinomics www. welkerswikinomics. com 15

IB/AP Economics Unit 1 Introduction to Economics Introduction to Economics The productive Resources What are the SCARCE RESOURCES? Examples of resources: Land Labor Capital " Natural capital": Land resources include all the " gifts of nature". Forests, fisheries, minerals, oil, gas, soil, commercial and residential real estate, etc... " Human capital": Labor resources are those provided by the body and minds of man and woman. Includes menial physical labor or high skilled technical labor. Doctors, teachers, construction workers, etc... " Physical capital": Capital is the machinery or tools that workers use to transform natural resources into finished products. Includes robots, simple and complex machines, computers, etc...

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IB/AP Economics Unit 1 Introduction to Economics Introduction to Economics The productive Resources In order to produce anything, three types of productive resources must be employed (used): Land: the " gifts of nature". Includes forests (timber), minerals, fisheries, agricultural land, real estate, cotton, silk, corn, soy beans, etc... ANYTHING THAT ORIGINATED FROM LAND OR SEA. Also called " NATURAL RESOURCES" Labor: includes physical, mental and intellectual labor, services and manufacturing. Any activity that puts the skills of man or woman to work. Also called " HUMAN RESOURCES" or " HUMAN CAPITAL" Capital: the " machinery" of an economy. Can be as simple as a pair of scissors and tape or as complicated as an industrial robot. Also called " PHYSICAL CAPITAL" and the fourth productive resource is??? Hint: what do you call someone who uses his or her skills to put all the other productive resources together in innovative ways? Welker's Wikinomics - www. welkerswikinomics. com 17

IB/AP Economics Unit 1 Introduction to Economics Introduction to Economics The productive Resources Entrepreneurship: The fourth productive resource. Includes the innovation and creativity innate in humans. Entrepreneurship is the only resource that is not considered " scarce" since there is no limit to the creativity of humans. Entrepreneurs are the " risk takers" who put their skills and innovations to the test by employing other resources to produce a good or service that they are willing to bet will succeed in the marketplace. Discussion questions: - How did scarcity give rise to the field of economics? - Modern economics arose only 232 years ago. Why do you think economics is such a young science? Welker's Wikinomics www. welkerswikinomics. com 18 IB/AP Economics Unit 1 Introduction to Economics Introduction to Economics The productive Resources Payments for resources: Since resources are scarce, there is a cost associated with their use. Firms (resource demanders) must provide households (resource suppliers) with a payment for their resources. For LAND: Firms pay households RENT.

Landowners have the option to use their land for their own use or to rent it to firms for their use. If the landowner uses his land for his own use, the opportunity cost of doing so is the rent she could have earned by providing it to a firm. For LABOR: Firms pay households WAGES. To employ workers, firms must pay workers money wages. If a worker is self employed, the opportunity cost of self-employment is the wages he could have earned working for another firm. For CAPITAL: Firms pay households INTEREST. Most firms will take out loans to acquire capital equipment. The money they borrow comes mostly from households' savings. Households put their money in banks because they earn interest on it. Banks pay interest on loans, which becomes the payment to households. If a household chooses to spend its extra income rather than save it, the opportunity cost of doing so is the interest it could earn in a bank. For ENTREPRENEURSHIP: Households earn PROFIT for their entrepreneurial skills. An entrepreneur who takes a risk by putting his creative skills to the test in the market expects to earn a normal profit for his efforts. Welker's Wikinomics www. welkerswikinomics. com 19 IB/AP Economics Unit 1 Introduction to Economics Introduction to Economics TNSTAAFL Announcement: All economics students will receive a FREE LUNCH of pizza and soda compliments of your Economics teacher this Friday! Welker's Wikinomics www. welkerswikinomics. com 20

IB/AP Economics Unit 1 Introduction to Economics Introduction to Economics TNSTAAFL " THERE'S NO SUCH THING AS A FREE LUNCH! " True or False Why? Arguments FOR TNSTAAFL: Arguments AGAINST TNSTAAFL: What is the OPPORTUNITY COST of having lunch a " free lunch" with your Economics teacher on Friday? Welker's Wikinomics www. welkerswikinomics. com 21

IB/AP Economics Unit 1 Introduction to Economics Introduction to Economics The Production Possibilities Curve What is the PPC? The PPC illustrates the possible combinations of goods or services 10 that can be produced by a single nation, firm, or individual. What does it show? That nothing is free and that everything has an opportunity cost. If society wants more pizzas, it must give up robots. What basic economic concepts can it be used to model? - Scarcity, tradeoffs, opportunity cost, economic growth, efficiency, unemployment. Italy's PPC B D Robots A C Pizzas 200 Understanding the PPC: The graph above shows that Italy can produce EITHER 10 robots OR 200 pizzas, or some combination of the two products, as long as it remains on or within its PPC. A point inside the PPC is attainable but not desirable. A point outside the PPC is desirable but unattainable. Welker's Wikinomics www. welkerswikinomics. com 22

IB/AP Economics Unit 1 Introduction to Economics Introduction to Economics The Production Possibilities Curve Italy's PPC Assumptions about the PPC: - The PPC is attainable only if a nation achieves full-employment of its productive resources - The nation's resources are fixed in quantity - Assumes the nation must chose between only two goods - The economy is closed, i. e. does not trade with other countries - Represents only one country's economy 9 A E B Robots 7 D 2 C 65 130 195 Questions to consider about the PPC: Pizzas 1) Which point(s) are attainable and desirable? WHY?

2) Which point(s) are attainable but not desirable? WHY?

3) Which point(s) are unattainable? Is this point desirable? Explain.

4) Which point will mean more consumption in the future? Explain.

5) Which point means more consumption now? Explain.

6) Why is the PPC bowed outwards?

7) How does the PPC illustrate opportunity cost? Tradeoff? Scarcity?

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The Production Possibilities Curve

1) Which point(s) are attainable and desirable? - Points on the PPC (A,

B and C) are attainable through full employment,

and thus desirable because they represent efficient use of Italy's resources.

2) Which point(s) are attainable but not desirable? -

Point D is inside the PPC, thus represents inefficient use of resources,

and most likely high unemployment, and is thus undesirable.

3) Which point(s) are unattainable? Is this point desirable? -

Point E is beyond Italy's production possibilities and is thus unattainable.

It is desirable because it represents greater

consumption of both pizzas and robots. Italy's PPC 9 A E Robots 7 D B 2 C 65

130 195 Pizzas 4) Which point will mean more consumption in the future? -

Point A represents more consumption in the future,

because Robots are a capital good,

used to make other products for consumption.

If Italy produces more robots now, it may

mean more consumer goos in the future.

5) Which point means more consumption now? -

Point C because pizza is a consumer good.

Households don't buy and use robots, but they do like to eat pizzas.

6) Why is the PPC bowed outwards? - The Law of Increasing Opportunity Cost

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IB/AP Economics Unit 1 Introduction to Economics Introduction to Economics The Production Possibilities Curve Robots Law of increasing opportunity cost: As the production of a particular good increases, the opportunity cost of producing an additional unit rises. Rationale: Economic resources are not completely adaptable to alternative uses. Many resources are better at producing one type of good than at producing others. Pizzas and Robots: Assume Italy was producing 10 robots and 0 pizzas. Surely, many of the resources (land, labor and capital) being used to make robots would be better suited to making pizzas. As Italy starts making its first few pizzas (0-100) it has to give up very few robots, since only those resources that are suited for pizza production will be used. But as the country makes more and more pizzas, the opportunity cost increases, because at some point robotics engineers will have to flip pizzas. As Italy approaches 200 pizzas, the opportunity cost in terms of robots given up grows, as resources better suited for robot production are employed in pizzerias 10 9 8 7 6 5 4 3 2 1 0 Italy's PPC constant opportunity cost A B C D 20 40 60 80 100 120 140 160 180 200 Pizzas Italy's PPC increasing opportunity cost A B C 10 9 8 7 6 5 4 3 2 1 0 Robots D 20 40 60 80 100 120 140 160 180 200 Pizzas

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IB/AP Economics Unit 1 Introduction to Economics Introduction to Economics The Production Possibilities Curve Italy's PPC 9 How does the PPC illustrate: E A B Robots 7 D - - - - - - - C Scarcity? Tradeoffs? Decisions? Resources? Opportunity costs? Actual output? Potential output? 2 And some more challenging ones: - Unemployment? - Economic growth? - Economic development? part 2 65 130 195 Pizzas Video: The Production Possibilities Curve - Solman, part 1 Activity: From " Favorite Ways to Teach Economics" by David Anderson: Problem sets 1. 1-1. 5. Opportunity Cost and PPCs Welker's Wikinomics www. welkerswikinomics. com 26

IB/AP Economics Unit 1 Introduction to Economics Introduction to Economics The Basic Economic Questions Remember the " Basic Economic Problem"? Limited resources in a world of unlimited wants and needs i. e. Scarcity exists! Because of this problem, choices must be made. These choices can be represented by three basic economic questions: 1. What should be produced? 2. How should things be produced? 3. Who should things be produced for? Welker's Wikinomics www. welkerswikinomics. com 27

IB/AP Economics Unit 1 Introduction to Economics Introduction to Economics the Basic Economic Questions The basic economic questions can be answered in various ways. Command economy Mixed economy Free market economy State-owned enterprises limited government role markets entrepreneurship Price mechanism Property rights Government Smith capitalism Economic priorities ownership of determined centrally property freedom of choice North Korea incentives laissez-faire Marx Sweden Private ownership " iron rice bowl" USA of resources Communist France Central planning profit motive Competition What to produce determined Switzerland by government priorities self-interest China USSR utility maximization " Invisible hand" Rationing system cost minimization Socialist Communism vs. Capitalism - Solman Video Welker's Wikinomics www. welkerswikinomics. com 28 IB/AP Economics Unit 1 Introduction to Economics Introduction to Economics Transition Economies Transition Economy: An economy undergoing the transition from one economic system to another. Most commonly from a centrally planned, command economy to a free market or mixed economy. Research Assignment: With a partner, research and prepare a brief report on a transition economy of your choice. Gather figures from the internet, identify the main problem areas that the countyr has faced in its transition, and explain the extent to which it is solving such problems. Factors to include in your presentation: - economic trends: GDP per capita, inflation, unemployment, types of goods and services produced, tax structure, debt levels, levels of foreign investment. - health and education factors - political structure - infrastructure - population issues: birth and death rates, migration rates - environmental issues Prepare a PowerPoint of 3-5 slides with an overview of the transition economy of your choice, outlining the challenges, obstacles, successes and failures of the transition from a command to market system. Welker's Wikinomics www. welkerswikinomics. com 29

IB/AP Economics Unit 1 Introduction to Economics Introduction to Economics Transition Economies Choose a transition economy to research: Asia * Cambodia * China * Laos * Mongolia * Thailand * Vietnam Commonwealth of Independent States * Armenia * Azerbaijan * Belarus * Georgia * Kazakhstan * Kyrgyz Republic * Moldova Central/Eastern Europe * Russia * Albania * Tajikistan * Bosnia & Herzegovina * Turkmenistan* * Croatia * Ukraine * Republic of Macedonia * Uzbekistan * Montenegro * Serbia

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IB/AP Economics Unit 1 Introduction to Economics Introduction to Economics Transition Economies The International Monetary Fund lists the following four ingredients, necessary for a successful transition from a command to a market economy: Liberalization: the process of allowing most prices to be determined in free markets and lowering trade barriers that had shut off contact with the price structure of the world's market economies. Macroeconomic stabilization: primarily the process through which inflation is brought under control and lowered over time Restructuring and privatization: the processes of creating a viable financial sector and reforming the enterprises in these economies to render them capable of producing goods that could be sold in free markets and of transferring their ownership into private hands. Legal and institutional reforms: These are needed to redefine the role of the state in these economies, establish the rule of law, and introduce appropriate competition policies. Source: IMF. org

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IB/AP Economics Unit 1 Introduction to Economics Introduction to Economics Quick Quiz 1. What is the Basic Economic Problem? 2. What are the four productive resources? 3. List the three basic economic questions. 4. Using a Production Possibilities Curve, explain the basic economic concepts of tradeoffs, scarcity, and opportunity cost. 5. Briefly contrast how scarce resources are allocated in a command vs. a free market economy.

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IB/AP Economics Unit 1 Introduction to Economics Introduction to Economics Product and Resource Markets What is a Market? A place where buyers and sellers come together In economics, we will study two types of market Product Markets Households buy goods and services produced by firms Resource Markets Firms buy productive resources from households

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IB/AP Economics Unit 1 Introduction to Economics Introduction to Economics Product and Resource Markets Product Markets Who are the buyers? Households Resource Markets Who are the buyers? firms Who are the sellers? households Who are the sellers? firms What is bought and sold? What is bought and sold? goods and services Which way does money flow? from households to firms What are the goals of firms and households? Maximize profit (firms) and utility (households) Capital, land, labor Which way does money flow? From firms to households What are the goals of firms and households? Maximize income (households), minimize costs (firms) Why does everyone benefit? Because exchanges are mutual and voluntary Why does everyone benefit? Because exchanges are mutual and voluntary

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IB/AP Economics Unit 1 Introduction to Economics Introduction to Economics Product and Resource Markets Resource Market: - Households supply productive resources (land, labor, capital) - Firms buy productive resources from households. In exchange for their productive resource, firms pay households: -Wages: payment for labor -Rent: payment for land -Interest: payment for capital -Profit: payment for entrepreneurship - Firms seek to minimize their costs in the resource market - Firms employ productive resources to make products, which they sell back to households in the product market Product Market: - Consumers buy goods and services from firms - Households use their money incomes earned in the resource market to buy goods and services - Expenditures by households become revenues for firms - Firms seek to maximize their profits - Households seek to maximize their utility (happiness) Notice the CIRCULAR FLOW of resources and money between these two markets! Welker's Wikinomics www. welkerswikinomics. com 35

IB/AP Economics Unit 1 Introduction to Economics Introduction to Economics The Circular Flow of Resources Expenditures / revenue Product market Goods/Services Households Firms Factors of production Resource market Income: W I R P Questions: - - - - - - - -

Give three examples of resource owners.

Give three examples of transactions you made this week in the product mark et.

Give an example of a transaction you or your family made this month in a fac tor market. What resources or " input factors" do households provide in the resource market? What determines the prices of land, labor,

capital and entrepreneurship in a factor market?

Where do households get the money to buy goods and services in the produc t market?

Where do business firms get the money to pay households for their resource s?

How does the circular flow diagram illustrate interdependence in a market ec onomy? Welker's Wikinomics www. welkerswikinomics. com 36

IB/AP Economics Unit 1 Introduction to Economics Introduction to Economics The Circular Flow of Resources Resource Market Product Market Firms employ productive resources to Productive resources: Households make finished goods and services. provide firms with the productive They sell their products to households resources they need to produce in exchange for money. goods and services -Land Mutual benefits and Households spend their -Labor voluntary exchange income from the sale of -Capital their resources. -Entrepreneurship Resource payments: Firms pay households for their resources, using revenue from the sale of their goods and services, which creates income for households -Rent -Wages -Interest -Profit -Households make expenditures on goods and services - Firms earn revenue, which is needed to cover their costs. Any revenue earned beyond all costs is considered economic profit. - The goal of households is to maximize happiness (utility) - The goal of firms is to maximize profits (TR-TC) NCEE Workbook Activity 5: The Circular Flow Welker's Wikinomics www. welkerswikinomics. com 37

IB/AP Economics Unit 1 Introduction to Economics Introduction to Economics Introduction to Trade What is trade? Trade is one of the concepts fundamental to the field of economics. Voluntary exchanges between individuals and firms in resource and product markets involving the exchange of goods, services, land, labor and capital is a type of trade. International trade involves the exchange of resources, goods, services, assets (both real and financial) across national boundaries. Trade makes everyone better off, and leads to a more efficient allocation of society's scarce resources. " It is not from the benevolence of the butcher, the brewer, or the baker, that we expect our dinner, but from their regard to their own interest. We address ourselves, not to their humanity but to their self-love, and never talk to them of our necessities but of their advantages" - Adam Smith " The Wealth of Nations" Discuss... Welker's Wikinomics www. welkerswikinomics. com 38

IB/AP Economics Unit 1 Introduction to Economics Introduction to Economics Introduction to Trade Food for thought on the philosophical foundations of Market Economics: Video: What do free market economics and evolutionary biology have in common? Without a master plan, an all-knowing designer, what assures that the economy will function? What is the mechanism by which economic decisions are made? Wouldn't society be better off with a planner making all the important decision about what should be produced, who should do what and how scarce resources should be allocated? Discuss... Welker's Wikinomics www. welkerswikinomics. com 39

IB/AP Economics Unit 1 Introduction to Economics Introduction to Economics Introduction to Trade - Lived 1723-1790 - Leading thinker of the Scottish Enlightenment - Two great works: The Theory of Moral Sentiments (1759) and The Wealth of Nations (1776) - Believed that humans acting in their own self-interest would lead to benefits for society as a whole, since the pursuit of self-interest naturally leads individuals to meet the wants and needs of those around them. On mutual benefits of trade: " Whoever offers to another a bargain of any kind, proposes to do this. Give me that which I want, and you shall have this which you want, is the meaning of every such offer; and it is in this manner that we obtain from one another the far greater part of those good offices which we stand in need of." Adam Smith, the father of modern Economics. On self-interest: " Every man…is first and principally recommended to his own care; and every man is certainly, in every respect, fitter and abler to take care of himself than of any other person." Discussion Question: What IS the " invisible hand" that makes all this work?

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IB/AP Economics Unit 1 Introduction to Economics Introduction to Economics Introduction to Trade Abraham Lincoln was once advised to buy cheap iron rails from Britain to finish the transcontinental railroad. He replied, " It seems to me that if we buy the rails from England, then we've got the rails and they've got the money. But if we build the rails here, we've got our rails and we've got our money." To paraphrase: " If I buy meat from the butcher, then I get the meat and he gets my money. But if I raise a cow in my backyard for three years and slaughter it myself, then I've got the meat and I've got my money." Why don't we keep cows in our backyard? Source: " Naked Economics" by Charles Wheelan Discussion Questions: 1. Why do nations trade? 2. What is specialization? 3. How does a nation determine what it should specialize in? 4. How do nations benefit from trade?

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IB/AP Economics Unit 1 Introduction to Economics Introduction to Economics Introduction to Trade Three facts help answer this question: - Uneven distribution of land, labor and capital resources - Efficient production requires different combinations of resources - People may simply prefer products made in other countries due to non-price attributes Labor-intensive goods -Examples: -Where? Land-intensive goods -Examples: -Where? Capital-intensive goods -Examples -Where? What does Switzerland specialize in? Why? China? US? India? UK? Welker's Wikinomics www. welkerswikinomics. com 42 IB/AP Economics Unit 1 Introduction to Economics Introduction to Economics Comparative advantage and the PPC Comparative Advantage: A country has a comparative advantage in production of a certain product when it can produce that product at a lower relative opportunity cost than another country. Production Possibilities Analysis: Specialization is economically desirable because it results in more efficient production. PPC - USA 39 PPC - Korea How much do apples " cost"? - in the US? -> 1a = 1/3c apples apples 24 - in Korea? -> 1a = 1/2c How much do cell phones " cost" - in the US? -> 1c = 3a 13 cell phones 12 cell phones - in Korea? -> 1c = 2a Should the countries trade? Why or why not? Welker's Wikinomics www. welkerswikinomics. com 43

IB/AP Economics Unit 1 Introduction to Economics Introduction to Economics Comparative advantage and the PPC United States: Specialize in apples -> trade apples for cell phones with Korea. Korea should be willing to trade 1 apple for anything up to, but not beyond, 1/2 cell phone. Before trade, 1 apple could only be get America 1/3 cell phone. The US has gained from trade. Korea: Specialize in cell phones -> trade cell phones for apples with the US. The US should be willing to exchange up to three apples for one cell phone. Before trade, Korea could only get two apples for each cell phone it gave up. Korea has gained from trade. Terms of trade: The " real exchange rate" between apples and cell phones will depend on the relative success of the US and Korea at the negotiating table. The red dashed lines represent the best possible outcome for both countries. 39 Trading possibilities line USA 36 Trading possibilities line Korea apples apples 24 13 cell phones 19. 5 12 cell phones Welker's Wikinomics www. welkerswikinomics. com 44

IB/AP Economics Unit 1 Introduction to Economics Introduction to Economics Comparative advantage and the PPC Specialization: " The use of the resources of an individual, a firm, a region, or a nation to concentrate production on one or a small number of goods and services." - What a person, company or country should specialize in depends on the task for which it has the lowest opportunity costs. - Countries should specialize based on the products for which they have a comparative advantage - Terms of trade: terms that are mutually beneficial to the two countries in trade. Where the trade leaves both countries better off than they were originally - Gains from Specialization and Trade: Specialization based on comparative advantage improves global resource allocation. Each country would result in a larger global output with the same total inputs or world resources and technology. Conclusion: " Specialization and trade based on comparative advantage increases the productivity of a nation's resources and allows for greater total output than would otherwise be possible."

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IB/AP Economics Unit 1 Introduction to Economics Introduction to Economics Comparative advantage and the PPC Production possibilities tables: Countries' production possibilities can be displayed using tables. These tables come in two types, Output and Input tables. Output Problem Reading the table: Given a fixed amount of resources, Mexico and the USA can choose between the following alternatives. Input Problem Reading the table: In order to produce one ton of output, Mexico and the USA must use the following amount of resources. (in acres of land) Soybeans Mexico 15 Avocados Soybeans Mexico 16 Avocados 60 8 USA 30 90 USA 8 6 How to decide who should specialize in what: - Identify the opportunity costs of soybeans and avocados in Mexico and the USA - The countries should specialize in the one for which they have the lower opportunity cost. - Cross multiplication trick. (maximize output and minimize inputs)

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IB/AP Economics Unit 1 Introduction to Economics Introduction to Economics Comparative advantage and the PPC Another way to determine who should specialize in what using production possibilities tables: CROSS MULTIPLY! Output Problem Input Problem Soybeans Mexico 15 Avocados Soybeans Mexico 16 Avocados 60 = 1800 = 1350 8 = 64 = 96 X USA 30 90 X USA 8 6 For an output problem, simply cross multiply and then choose the highest level of output. Output is maximized when the US specializes in soybeans and Mexico in avocados. For an input problem, cross-multiply and then choose the combination that uses the least amount of inputs. Inputs are minimized when the US specializes in soybeans and Mexico in avocados. Welker's Wikinomics www. welkerswikinomics. com 47

IB/AP Economics Unit 1 Introduction to Economics Introduction to Economics Comparative advantage and the PPC Soybeans 30 Mexico 15 Avocados Soybeans USA 60 Mexico 15 USA 30 90 PPC shows the the two countries potential output. 60 Avocados 90 - Who should specialize in what? - Illustrate the possible gains from trade on the two PPCs Welker's Wikinomics www. welkerswikinomics. com 48

IB/AP Economics Unit 1 Introduction to Economics Introduction to Economics Unit 1 Definitions Economic growth: An increase in total output (and income) or per capita output (and income) of a nation over a period of time. Can be illustrated by an outward shift of the PPC Economic development: a sustained increase in the standard of living of the people of a nation. Characterized by improvements in health, education, life expectancy, and per capita income. Positive and normative concepts: - Positive concepts are those rooted in fact. They are observable and definitive. Example: The average income of Americans HAS increased by 2. 5% per year since 1970. - Normative concepts are those rooted in opinion. They are statements of what should be rather than what is. Example: American incomes should be higher given the increases in productivity since the 1970s.

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IB/AP Economics Unit 1 Introduction to Economics Introduction to Economics Unit 1 Definitions Ceteris Paribus: Translates to " all else equal". Economists assume " ceteris paribus" in all of their models. The purpose is to simplify an economic event down to one or two observable variables, understanding that other factors could change that affect the model. Example: " ceteris paribus", an increase in price of a good will lead to a decrease in the quantity demanded by consumers. The ceteris paribus means that other factors besides price are NOT changing, (i. e. the price of other goods or the incomes of consumers). Utility: The economists word for happiness. Economists assume that rational consumers always behave in a way that maximizes their utility. Free vs. Economic goods: - Free goods are those that are desired but not limited. A free good is available in as great a quantity as desired with zero opportunity cost to society. Air is a free good. Sunlight is a free good - Economic goods are those that are desired and limited. This is most resources and goods in society. They are economic because the supply is limited, therefore there is a price attached to them, or an opportunity cost associated with their use. Welker's Wikinomics www. welkerswikinomics. com 50 IB/AP Economics Unit 1 Introduction to Economics Introduction to Economics Big Ideas Unit 1: Introduction to Economics - BIG IDEAS to understand 1. Scarcity, choice, and opportunity cost 2. Basic Economic Problem and Questions 3. Economic systems 4. Property rights and the role of incentives 5. Circular flow 6. Production possibilities curve 7. Comparative advantage, absolute advantage, specialization, and trade 8. Marginal analysis - NCEE Workbook Unit 1: Activity 8 (p. 26) - Favorite Ways to Learn Economics Problem set 1. 6 (p. 12) Review Activities: Welker's Wikinomics - www. welkerswikinomics. com 51 Attachments Favorite ways ch. 17. pdf APMicroUnit1. pdf APMicroUnit1. jnt