Year 11 Economics Revision Questions

1. What is the economic problem?

The economic problem is trying to allocate our limited resources for the satisfaction of our limited and competing wants. It involves a choice which in turn is the opportunity cost.

2. What are wants? What are needs? What are resources?

Wants can be defined as the material desires of individuals or the community. Needs are the basic items needed for human survival. Resources are the items used to produce goods and services.

3. What is opportunity cost?

Opportunity cost represents the alternative use of resources. Often referred to as the ‘real’ cost of satisfying one want over an alternative want. This is also known as the economic cost.

4. What is a production possibility curve? What does the production possibility curve assume?

The production possibility curve is a graphical representation of all the possible combinations of the production of two goods or services (or two types of goods or services) that the economy can produce at any given time. It assumes that the economy only produces two goods, the state of technology is constant, the quantity of resources available remains unchanged, and all resources are fully employed.

5. What are some current choices, implications and future implications of individuals?

An individual may choose to forego an overseas holiday or extravagant lifestyle and instead take out a mortgage and purchase a house.

6. What are some current choices of businesses and what would be some implications of those?

A business may choose to focus on one area of business activity over another. Businesses have a limited amount of labour, capital, entrepreneurial skill and other resources and must, therefore, focus on the products in which they are likely to have the greatest success.

7. What are some current choices of governments and what would be some of the implications of those?

The decisions of governments have very important long term implications, both for governments themselves and the entire economy. A government may choose to give highest priority in its spending to satisfying immediate needs, such as increased welfare benefits and health care.

8. Why do individuals save?

Individuals save depending on their income levels, some reasons for saving include: plans for future purchases, investments, budgeting and money for rainy days (emergencies).

9. Why do individuals work?

Individuals work to raise their standard of living and to earn an income. An individual may also work to provide for their families.

10. Why do individuals study?

Study is the accumulation of skill and can be counted as intellectual capital (skills) which can then be used in work. Education is important as it provides the necessary knowledge for most occupations.

11. Why do individuals retire?

Individuals retire once they believe they have accumulated enough wealth and income to sustain their lifestyles.

12. Why do individuals influence government?

Individuals influence governments to in turn (vote) choose for a political party's economic polices for the country. Individuals also influence government as they provide goods and services directly.

13. What are some economic factors underlying decision making by governments?

Governments make their economic decisions based on factors such as economic growth and domestic, world markets. Equally, governments may wish to encourage certain economic activities and may provide incentives for them.

14. What is land? What is labour? What is capital? What is enterprise? What is the return?

Land is all the resources provided by nature that is used in the process of production. Labour is human effort, both physical and mental, used to produce goods and services. Capital is the 'produced' means of production, goods not for immediate consumption but to be used in the production of other goods and services. Enterprise involves organizing the other factors of production (natural resources, labour and capital) for the purpose of producing goods and services. Return is the reward achieved from the 4 factors of production.

15. Discuss the questions to solve the economic problem

Working out how to distribute what an economy produces is difficult. We have to strike a balance that provides rewards for investment, entrepreneurs and innovation, as well as ensuring that everyone has an acceptable quality of life.

16. Discuss the provision of income through land, labour and capital.

Market economies provide people with income as reward for their contribution to the production process. Workers are paid according to the value of their labour. The price that is paid for inputs determines the individual’s share of total output and will generally depend on how scare or high demanded resources are.

17. What is the Primary industry? The Secondary industry and Tertiary industry?

The primary sector of the economy extracts or harvests products from the earth. The primary sector includes the production of raw material and basic foods. The secondary sector of the economy manufactures finished goods. All of manufacturing, processing, and construction lies within the secondary sector. The tertiary sector of the economy is the service industry. This sector provides services to the general population and to businesses.

18. What does the quality of life depend on?

Quality of life is affected by economic factors as dips or recessions in the economy lead to unemployment which then has flow on effects to standards of living and can affect quality of life.

19. What are upswing, boom, recession and downswing?

Upswing is when the economy is growing after a period of slow or downswing. A boom in economic growth is associated with increased investment and production. Recession is the stage in the business cycle where the economy has 2 quarters of negative growth (a fall in GDP). Downswings are where the economy has taken a slight dip in its performance.

20. What does the circular flow of income show?

The circular flow of income shows the operation of the economy and the linkages between the main sectors in the economy.

21. What is the formula for GDP and what is it?

Y = C + I + (X - M) + G

Income = Consumers + Income + (Exports – Imports) + Government Spending

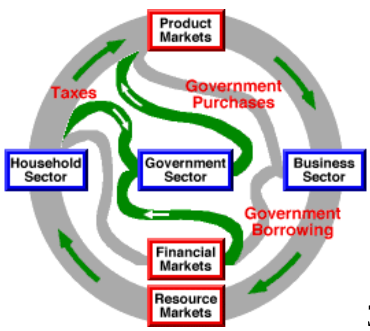
22. What are three ways used to calculate GDP?

The Output method - where you calculate the total value of all the final goods and services produced. The Income method - finding the total income of the nation. The main types of income are rent, wages, interest and profit. The Expenditure method - finding the total amount of money spent in the economy. This is done by summing consumption, investment, government spending and exports then subtracting imports.

23. What is the two sector model? What does it assume? What are the injections and leakages?

In the simple two sector circular flow of income model the state of equilibrium is defined as a situation in which there is no tendency for the levels of income (Y), expenditure (E) and output (O) to change, that is: Y = E = O This means that the expenditure of buyers (households) becomes income for sellers (firms). The firms then spend this income on factors of production such as labour, capital and raw materials, "transferring" their income to the factor owners. The factor owners spend this income on goods which leads to a circular flow of income.

24. What is the three sector model? What does it assume? What are the injections and leakages?
25. What is the four sector model? What does it assume? What are the injections and leakages?



3 Sector Model

4 Sector Model

26. What is the five sector model? What does it assume? What are the injections and leakages?

LEAKAGES	INJECTION
Saving (S)	Investment (I)
Taxes (T)	Government Spending (G)
Imports (M)	Exports (X)

27. How is equilibrium gained in the five sector model? What are the injections and leakages?

Equilibrium is gained from the 5 sector model when all leakages are equal to injections.

Savings + Taxes + Imports = Investment + Government Spending + Exports

S + T + M = I + G + X.

28. What is the price mechanism?

Price mechanism is the process by which the forces of supply and demand interact to determine the market price at which goods and services are sold, and the quantity produced.

29. What are two main markets?

Product market is the interaction of demand for and supply of the outputs of production, i.e. goods and services. Factor market is a market for any input process, including land, labour capital and enterprise.

30. What is a market economy? How is the economic problem solved?

In a pure market economy all major economic decisions are made by individuals and private firms, who are both motivated by self-interest. Under this system, most economic resources are owned by the private sector and people are able to seek wealth without the government intervening or affecting their business activities.

31. What is a mixed market economy? How is the economic problem solved?

A mixed economy is an economic system where the decisions concerning production and distribution are made by a combination of market forces and government decisions.

32. What is a planned economy? How is the economic problem solved?

Under a planned economy, government planners make economic decisions, and there is little scope for individual choice to influence the economy.

33. What is a welfare state?

A welfare state is where a comprehensive system of welfare benefits such as the aged pension and unemployment benefits, free access to health care, and subsidized access to other government services such as transport and housing. The welfare state was intended to create a more equal society.

34. Why does the government intervene?

Resource allocation: provide important things that would not otherwise be provided, restrict production of harmful things
Income distribution: create a fairer society and look after people
Economic stability: smooth out sharp fluctuations in the economic cycle

35. What is consumer sovereignty? Why is it important?

Consumer sovereignty refers to the manner in which consumers, collectively through market demand determine what is produced and the quantity of production. Businesses will produce whatever goods and services are in demand.

36. What are some patterns of consumer spending and saving?

The theory of consumption behavior is often referred to as the life-cycle theory of consumption. Individuals and households tend to smooth their consumption. Over the course of our lifetime, consumption and spending patterns change. School = Dissavings, Work, Retirement = Dissavings

37. What is disposable income?

The amount of money that households have available for spending and saving after income taxes have been accounted for.

38. What is real income?

The income of an individual or group after taking into consideration the effects of inflation on purchasing power.

39. What are prices, prices of substitutes, price of complements, preferences/tastes, and advertising? How do they affect consumer spending?

A substitute is a good that consumers may choose to buy in place of another good, such as butter and margarine or tea and coffee. A complement is a good that is used in conjunction with another good. E.g. DVDs would be a complement of DVD players. As consumer tastes and preference change over time, so too will the demand for particular goods. Technological progress lead to consumers demanding new and better products at the expense of superseded ones. Advertising can have a major impact on individual consumer choice, sometimes even creating demand for a particular good or service where none existed before.

40. What are some sources of income?

Consumers gain their income from a variety of sources. Consumer income mainly comes as a return for resources such as labour, land, capital and entrepreneurial initiative. These resources are also known as the factors of production can also come from the government in the form of social welfare. Returns to factors of production: wages from labour, rent from land, income from capital and profit from entrepreneurial skills

41. What is a firm? What is an industry?

A business firm is an organization involved in using entrepreneurial skills to combine factors of production to produce a good or service for sale. An industry consists of those firms involved in making a similar range of items that usually compete with each other.

42. What is a quaternary industry? What is a quinary industry?

The quaternary sector of the economy consists of intellectual activities. Activities associated with this sector include government, culture, libraries, scientific research, education, and information technology. The quinary sector would include the top executives or officials in such fields as government, science, universities, non-profit, healthcare, culture, and the media.

43. What is a sole trader? What is a partnership? What are incorporated firms? What are public and private companies?

Sole Trader: This is the most straightforward structure for a business. Basically it means the business decisions are being made by one person. A partnership is the relationship existing between two or more persons who join to carry on a trade or business. Each person contributes money, property, labour or skill, and expects to share in the profits and losses of the business. A corporation is a legal entity that is created under the laws of a state designed to establish the entity as a separate legal entity having its own privileges and liabilities distinct from those of its members. There are many different forms of corporations, most of which are used to conduct business. A public company or publicly traded company is a company that offers its securities (stock/shares, bonds/loans, etc.) for sale to the general public, typically through a stock exchange, or through market makers operating in over the counter markets. A privately held company or close corporation is a business company owned either by non-governmental organizations or by a relatively small number of shareholders or company members which does not offer or trade its company stock (shares) to the general public on the stock market exchanges, but rather the company's stock is offered, owned and traded or exchanged privately.

44. Describe the firm’s production decisions.

Production decisions are based on the skills and experience of the business operator. Industries with strong consumer demand. Specific business opportunities and the amount of capital available and required to start the business. The firm must then decide on how much to produce and how to produce.

45. Describe profit maximization

Profit motive refers to the process by which a business seeks to maximize profits by using the lowest cost combination of resources and charging the highest possible price.

46. Describe maximizing growth. How is it achieved?

Another motive of management may be to maximize the rate of growth of the firm’s assets. In the long run, a larger asset base should allow a business to achieve profits.

47. Describe increasing market share
48. Describe shareholder expectations

Because the entrepreneurial function of larger businesses today is generally split between the owners (shareholders) and paid managers, the goal of profit maximization may not always be the highest priority. The shareholders take on the function of risk. They risk their capital and seek maximum profit as the reward for this risk. On the other hand, the paid managers take on the organizational function and may seek increased salaries, power and prestige as their rewards. Their perceived managerial ability, and thus their rewards, may be more dependent upon increasing sales rather than maximizing profits. As a result, there may have to be a compromise between the objectives of profit maximization and increasing market share.

49. Describe satisficing

Satisficing behavior is the idea that firms will attempt to pursue a satisfactory level in all goals (profit maximization, sales maximization etc.) rater than maximizing any single goal.

50. What is productivity? What are the benefits of it?

Productivity refers to the quantity of goods and services the economy can produce with a given amount of inputs such as capital and labour. Benefits include: less wastage of scare resources, lower production costs and high profits for the business firm. A lower inflation rate, higher incomes and improved international competitiveness of our industries.

51. How can a firm grow?

A firm can grow by increasing productivity and this increasing the quantity produced per unit of time.

52. What are internal economies of scale? Give some examples.

Internal economies of scale are the cost saving advantages that result from a firm expanding its scale of operations. They occur when a firm's output level is below the technical optimum.

53. What are external economies of scale? Give some examples.

External diseconomies of scale are the disadvantages faced by a firm because of the growth of the industry in which the firm is operating, and are not the result of a firm changing its scale of operations.

54. What are internal diseconomies of scale? Give some examples.

Internal diseconomies of scale are the cost disadvantages (specifically, the costs per unit) faced by a firm as a result of the firm expanding its scale of operations beyond a certain point. The firm's output level is above the technical optimum.

55. Describe production methods, prices, employment, output, businesses, types of products and globalization.

Production methods: the impact of technological change on production methods has varied from firm to firm. However in many cases it has led to lower costs, increased efficiency, a reduction in the workforce size and the possibility of larger production runs.

Prices: One of the most significant changes that information and communications technologies are bringing is a far better marketplace. Through the internet, consumers have ready access to multiple businesses locally or abroad and can improve pricing between firms. This is likely to squeeze profit margins more tightly in the future, and force firms to reduce their costs to an absolute minimum in an environment where it will be difficult to raise prices.

Employment: New technologies have a mixed impact on firm's demand for employees. On the other hand, the growth of new technologies provides new job opportunities, with strong demand for employees with specific information technology skills such as computer programming.

Outputs and Profits: by using the latest technology firms are better able to respond to changes in market demand and to compromise their output to specific needs of the marketplace. Businesses must be prepared to make investments in new technology in order to obtain an economic benefit.

Types of Products: Technological change creates completely new products and industries. Improvements in technology are a major reason why some people regularly update products like computers, cars and cameras. If a new production technology is more flexible, it may make it possible to customise output to the specific wants of individuals. Smaller production runs may become more affordable, thus broadening the range of products and making it easier to satisfy consumer demand.

Globalisation: technology is one of the major driving forces behind the globalisation of markets. The development of global money and stock markets, mediated by global computer networks has made it possible for businesses to attract investment funds from across the world, and for

individuals to diversify their investments. Globalisation often leads to the outsourcing of production to countries with lower wages, raising the question of exploitation and ethical production methods.
Environmental Sustainability: a concept that involves minimising pollution and waste, preserving the natural environment and increasing the use of renewable energy. Businesses may change their activities to make them more environmentally sustainable in response to demands by consumers, new regulations or financial incentives or because of business ethics that value the natural environment. Efforts to make business more environmental sustainable are a significant driver of investment in new technologies.

56. What is horizontal integration? What is vertical integration? What is backward integration? What is forward integration?

Horizontal integration: When a company expands its business into different products that are similar to current lines. E.g. A hot dog vendor expanding into selling hamburgers would be an example of horizontal integration. Vertical Integration: When a company expands its business into areas that are at different points of the same production path. E.g. A car company that expands into tire manufacturing would be an example of vertical integration. A company such as this is often referred to as vertically integrated. Backward Integration: A form of vertical integration that involves the purchase of suppliers in order to reduce dependency. E.g. A bakery business bought a wheat farm in order to reduce the risk associated with the dependency on flour. Forward Integration: A business strategy that involves a form of vertical integration whereby activities are expanded to include control of the direct distribution of its products. E.g. a farmer sells his/her crops at the local market rather than to a distribution centre.

57. What are diminishing returns? ~~What is APP? What is MPP? What is TPP?~~

In economics, diminishing returns (also called diminishing marginal returns) is decrease in the marginal (per-unit) output of a production process as the amount of a single factor of production is increased, while the amounts of all other factors of production stay constant. The law of diminishing returns (also law of diminishing marginal returns or law of increasing relative cost) states that in all productive processes, adding more of one factor of production, while holding all others constant, will at some point yield lower per-unit returns. The law of diminishing returns does not imply that adding more of a factor will decrease the total production, a condition known as negative returns, though in fact this is common.

~~58. Draw graphs for external economies and internal economies of scale.~~

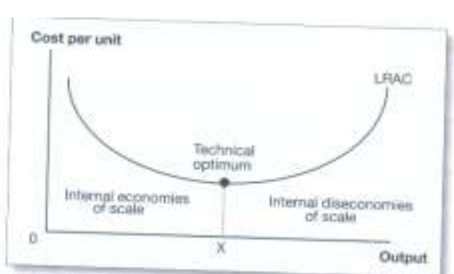


Figure 5.3 – The long-run average cost curve

Learning by doing

A benefit of continuously repeating production processes is that a firm gets more practice – and can become more efficient at completing the same tasks in the production process over time. Learning by doing, as it is known, results in a downward shift of the firm's long-run average cost curve – meaning lower per-unit production costs at each level of output.

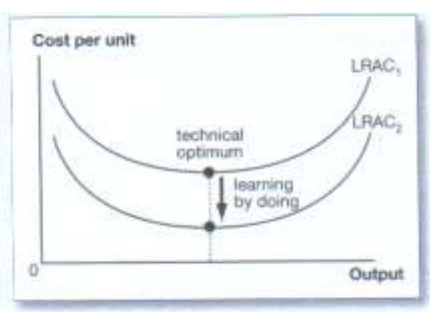


Figure 5.4 – Learning by doing