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What Economics Is About

Scarcity

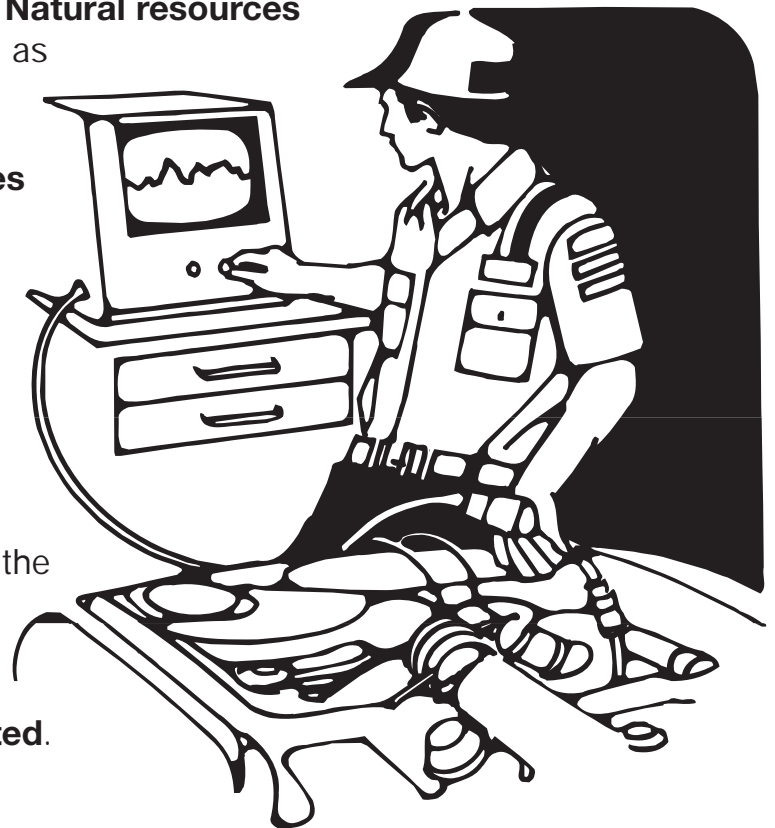
Every society is endowed with **resources** which are used to **produce** the goods and **services** that enable it to survive and prosper. These resources, called **productive resources**, can be classified into three groups: natural resources, human resources, and capital resources. **Natural resources**

(often called **land**) refer to resources such as minerals, water, trees, and land itself.

Raw materials used in production come from natural resources. **Human resources**

(**labor**) describe the human work effort, both physical and mental, expended in production. **Capital resources** are the man-made physical resources (such as buildings, tools, machines, and equipment) used in production.

The study of **economics** explains how productive resources are used to provide the **goods** and **services** that satisfy human wants.¹ Because productive resources are limited, the goods and services that can be produced from them are also **limited**. In contrast, the goods and services wanted by individuals and societies are virtually **unlimited**.



This tension between unlimited wants and the limited productive resources available for satisfying these wants is what economists refer to as **scarcity**. Thus, stereos, hot dogs, education, lawn mowers, T.V. repair services, and bubble gum are all considered **scarce** because many individuals desire these things, but their availability is limited. Scarce goods and services command a price in the marketplace. The price indicates how scarce a good is relative to other goods.

1. In many elementary school textbooks, a distinction is made between wants and needs. However, economists (to the chagrin of many teachers) typically lump the terms together under the general category of "wants."

A good with a high price is relatively more scarce than a good with a lower price. It is quite difficult to think of things that are *not* scarce. Some examples might include sand in a desert, salt water at the beach, or the air you are breathing at this moment. But even air is scarce to the scuba diver or astronaut; and certainly clean air is scarce for the inhabitants of urban areas. It is safe to conclude that in economics, most things in this world are considered scarce. That is, they are not *freely* available to individuals in unlimited quantities.²

Scarcity is sometimes confusing to students because it does not correspond exactly to the common usage of the word. Are hot dogs and candy really *scarce*? They are readily available to most students, who would more likely apply the term to diamonds or gold. A teacher can address this common misunderstanding by offering a free piece of candy to the class. It is a safe bet that more than one student will want it, and the point is proved: in economics, if individuals want more of an item than is freely available, then that item is considered scarce and will command a price in the marketplace.

The Basic Economic Problem

The existence of scarcity creates the **basic economic problem** faced by every society, rich or poor: how to make the best use of limited productive resources to satisfy human wants.

To solve this basic problem, every society must answer these three basic questions:

1. **What** goods and services will be produced?
2. **How** will goods and services be produced?
3. **Who** will consume the goods and services?



2. It should be noted that in certain situations, the desire for particular goods and services by particular individuals can be satisfied. For example, at some point a teacher will not want more (and may even want fewer!) desks in her classroom. However, in an economic sense, desks are a scarce good — they are not freely available in unlimited quantities to anyone who wants them.

Economic Systems

Several fundamental types of **economic systems** exist to answer the three questions of what, how, and for whom to produce: traditional, command, market, and mixed.

- **Traditional Economies:** In a **traditional economy**, economic decisions are based on custom and historical precedent. For example, in tribal cultures or in cultures characterized by a caste system, people in particular social strata or holding certain positions often perform the same type of work as their parents and grandparents, regardless of ability or potential.
- **Command (Centralized) Economies:** In a **command economy**, governmental planning groups make the basic economic decisions. They determine such things as which goods and services to produce, their prices, and wage rates. Cuba and North Korea are examples of command economies.
- **Market (Decentralized) Economies:** In a decentralized **market economy**, economic decisions are guided by the changes in prices that occur as individual buyers and sellers interact in the market place. As such, this type of economy is often referred to as a **price system**. Other names for the market system are **free enterprise, capitalism**, and **laissez-faire**. The economies of the United States, Singapore, and Japan are identified as market economies since prices play a significant role in guiding economic activity.
- **Mixed Economies:** There are no pure command or market economies. To some degree, all modern economies exhibit characteristics of both systems and are, therefore, often referred to as **mixed economies**. For example, in the United States the government makes many important economic decisions, even though the price system is still predominant. Even in strict command economies, private individuals frequently engage in market activities, particularly in small towns and villages.

The key point to remember is that every individual and every society must contend with the problem of scarcity. Every society, regardless of its political structure, must develop an **economic system** to determine how to use its limited productive resources to answer the three basic economic questions of what, how, and for whom to produce.



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