

Chapter

Introduction

ECONOMICS:

The word Economics is derived from the Greek word 'Oikonomia' which means 'household management'. In early days Economics was known as political economy. Adam Smith is considered the father of Economics. Alfred Marshall for the first time used the term Economics instead of 'political economy'. The following table shows the important definitions in Economics.

Definition	Name of Economists	Books	Year of publication
Wealth	Adam Smith	An Enquiry into the Nature and Causes of Wealth of Nations	1776
Welfare	Alfred Marshall	Principles of Economics	1890
Scarcity	Lionel Robbins	An Essay to Nature and significance of Economics	1932
Growth	Paul.A.Samuelson	Economics	1964

BRANCHES OF ECONOMICS. Economics is broadly divided into two branches. They are the following.

MICROECONOMICS: It is the branch of economics which deals with individual units. It is also called price theory, demand theory, cost theory etc. **MACROECONOMICS:** It is another branch of Economics which deals with aggregates. John Maynard Keynes is considered as the father of Macro Economics. It is otherwise called income theory. The main difference between MICRO and MARCO Economics are the following.

POINTS OF DIFFERENCE	MICRO ECONOMICS	MACRO ECONOMICS
Unit of study	Individual	Aggregate
Method	Partial Equilibrium	General Equilibrium
View point	Worm's eye view	Birds eye view
Example	Demand for a pen, salary of a person, utility, cost etc.	National income, aggregate demand, inflation, money supply

PREPARE A SEMINAR PAPER ON CENTRAL PROBLEMS OF AN ECONOMY:

Respected teachers and my dear friends,

The topic of my seminar paper is “central problems of an economy”. As we know the Central problems of an economy arises due to the following reasons. 1 Human wants are unlimited. 2. Resources are limited 3. Resources have alternative uses. In my seminar paper, I would like to present the Central problems of an economy.

INTRODUCTION: The resources available to the human are limited, but their wants are unlimited. Due to the scarcity of resources, the economy faces the problem of choice. This mismatch between unlimited wants and limited resources that gives rise to three Central problems faced by every economy.

Contents:

1. WHAT TO PRODUCE AND IN WHAT QUANTITIES?

Every society wants thousands of goods and services. Since resources are scarce, all these goods and services cannot be produced. So it has decided to what type of goods are produced.

2. HOW TO PRODUCE:

It is a problem related to the technique of production. There are two techniques of production --- Labour intensive and Capital intensive. Labour intensive is a production technique, which uses more amount of labour and less amount of capital. The capital intensive is a production technique, which uses more amount of capital and less amount of labour.

3. FOR WHOM TO PRODUCE:

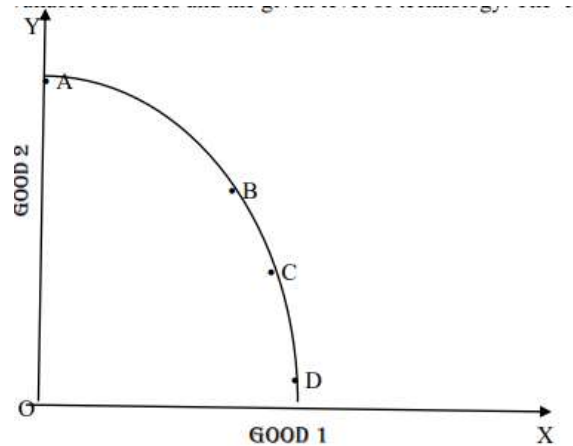
It is a problem related to distribution. It means the distribution of output among the factors of production. This is called functional distribution.

CONCLUSION:

Thus it can be concluded that every economic system faces three basic economic problems. The solution to these economic problems depends upon the nature of the economic system.

PRODUCTION POSSIBILITY CURVE OR PRODUCTION POSSIBILITY FRONTIER

It is defined as the locus of points of two goods which an economy can produce with the available resources and the given level of technology. The following is a PPC.



In the above PPC, the OX axis OY axis represents quantities of GOOD 1 and GOOD 2. A, B, C and D are the different production possibilities.

PRODUCTION POSSIBILITY SET:

Production possibility set of two goods are produced, with the given technology and resources. The following table shows different production possibilities of two goods --- Rice and Wheat

PRODUCTION POSSIBILITIES	RICE	WHEAT
A	20	0
B	13	5
C	10	7
D	4	10
E	0	15

The graphical representation of the above table is called a production possibility curve.

OPPORTUNITY COST:

Opportunity cost is the next best alternative product or service that has been sacrificed or forgone.

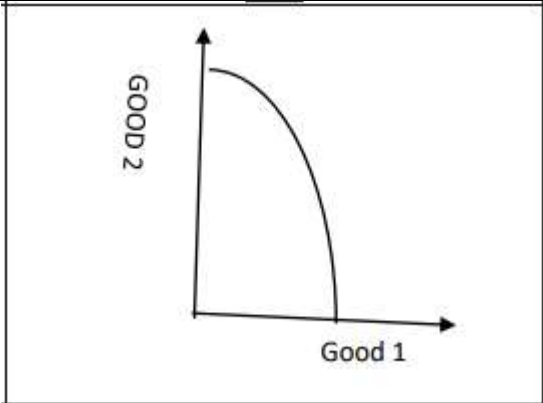
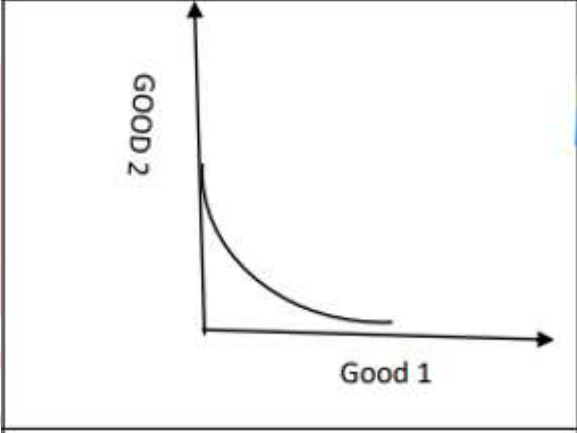
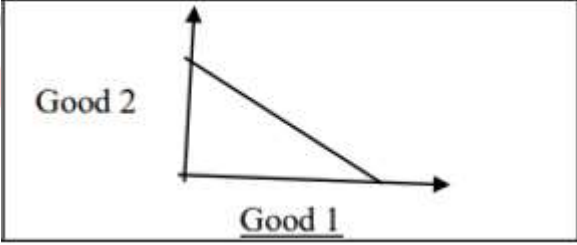
MARGINAL OPPORTUNITY COST:

It means the additional cost in terms of several units of good sacrificed to produce an extra unit of other good. In other words, it is the ratio between ΔX and ΔY .

$$MOC = \frac{\Delta Y}{\Delta X} = \text{change in the quantity of good Y}$$

$$\Delta X \Delta Y = \text{change in the quantity of good X}$$

There is an important relationship between MOC and PPC. If the MOC increases, PPC becomes Concave in shape. If the MOC decreases, PPC becomes Convex in shape. If the MOC, constant PPC become a straight line in shape. This can be illustrated with the following table

MOC	PPC	SHAPE
Increasing		concave
Decreasing		Convex
Constant		Linear

ORGANISATION OF ECONOMIC ACTIVITIES:

Every economy tries to solve Central problems differently. According to the way to solve Central problems economies broadly divided into three.

1. Centrally Planned Economy OR Socialist Economy.

It is an economic system where all the means of production are under the ownership and control of the government. Centralized planning, public welfare, public sector etc. are the important features of the centrally planned economy.

2. Market Economy OR Capitalist Economy:

It is an economic system where all the means of production are under the ownership of private individuals. Price mechanism, Private sector, Profit motive etc. are the features of the market economy.

3. Mixed Economy:

It is an economic system where all the means of production are under the ownership and control of both private individuals and the government.

POSITIVE AND NORMATIVE ECONOMICS:

Positive economics evaluate how different mechanism works. It deals with 'what is'.

normative economics evaluate mechanisms desirable or not. It deals with 'what ought to be'.

