



ECONOMICS

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These activities will look at different approaches to solving the basic economic problem facing all societies – How do we decide the best way to use the limited resources we have available?

We will start with an overview of the role of economics in society and the useful contribution an understanding of economic concepts can make to improving how society functions.

Economics is all about the allocation of our precious and scarce resources. During these four weeks you will look at different ideas and approaches to this issue.

Throughout industrial history different thinkers, politicians, sociologists and philosophers have given consideration to the questions what do we make? how do we make it? and who do we make it for?

You will look at three different approaches to these three fundamental questions.

Week 1

What is economics? What are the key economic problems faced by society, and how can economics contribute to solving them. You will look at the role of economists and different views of the good and sometimes bad they can do in terms of decision making. You will explore some basic economic ideas and thinkers how they differ in their approach.

Economics is about choices. It is the study of how there are limited resources but people have unlimited wants, so individuals have to make choices about what to use those resources for. This means they have to decide what to give up; in economics we call this the opportunity cost of the decision made.

- **The opportunity cost = the next best alternative forgone (which means opportunity cost = the value of your second choice)**

Task

1. Imagine that you are on a desert island. You are alone. The island is empty apart from one palm tree. The sea is salt water.
2. You can choose five of the items below for survival... Which five will you choose?
3. Knife; Spade; Seeds; Tent; First Aid Kit; Sleeping Bag; Plastic Sheet; Fishing Net; Matches; Bug Spray; Sunblock.
4. Now rank the five you chose from most essential to least essential.
5. What is your most essential item?
6. What is the second item on your list?
7. What is there were several people all stranded together? If you could only have five between you, how would you choose as a group which five to keep? Describe different systems you could use to make this decision.

There are different ways we choose to ‘solve the economic problem’. The following weeks’ activities are designed to help you explore the different approaches to allocating resources.

Find out more about what we mean by the following terms:

1. The Free Market
2. A Planned or Command Economy
3. A Mixed Economy

Week 2

Read the following article then answer the questions underneath:

Adam Smith (1723–1790)

Adam Smith is viewed to be the founder of **classical economics** and was a key advocate of the market economy. *The Wealth of Nations*, which Smith wrote in 1776, remains a classic book in economics. His key conclusion is that, by pursuing their own **self-interest**, individuals would be led '**as by an invisible hand**', with resources allocated in such a way that is in the best interests of society.

He was writing at a time when most firms were owned and run by single individual **capitalists** who had an active, hands-on approach to running their businesses. Like today, most capitalists ran their businesses with the self-interested aim of **maximising profit**.

Consumers also had their own self-interest at heart when making decisions about what to buy. Smith argued that these self-interest objectives, via the operation of **the price mechanism**, leads to the **optimum resource allocation** and therefore the best outcome for society.

The 'invisible hand' enables consumers and producers to interact in the market so that both can achieve their objectives. For example, if consumers suddenly want more robot vacuum cleaners, then this will push up the price in the market: consumers are **competing** with each other for the existing number of robot vacuum cleaners.

Firms currently in the market will react by wanting to supply more of the product since there is greater scope to make higher profits, while new suppliers will be enticed into the market to take advantage of the profit opportunity. (Smith said low **barriers to entry** were essential to make this happen.) More resources are then being allocated to the production of robot vacuum cleaners, which is precisely what consumers wanted. Therefore everyone is happy.

Smith believed that competition in markets ensures that firms, whose main objective is to maximise profits, produce their goods at the lowest possible **cost**. This benefits society and ensures markets will use resources efficiently.

Smith recognised the dangers of **monopoly power** but at the time of his writing this was not viewed as being too significant. He also believed prices would end up being 'fair' but that competition was essential in achieving this (low barriers to entry are necessary to prevent firms from gaining monopoly power).

Smith also wrote about the process of specialisation and the division of labour, and how this production method could increase production and create wealth. By breaking down the production process into smaller, specialised parts, productivity rises. This is because this process helps incorporate some automation into the production process, which speeds up production. Workers also spend less time switching between tasks and the repetition of tasks makes their efficiency increase..

1. Find out the meaning of the following key terms:
 - Capitalist
 - Barriers to entry
 - Cost
 - Monopoly
2. Can you explain in your own words how '**the price mechanism**' works?
3. Why might low barriers to entry mean it is hard for firms to gain monopoly power?
4. What do you think are the main criticisms of a free market system?
5. What do you think it might be like as a worker in a factory in the kind of system proposed by Adam Smith?

Research ideas

Explain how a fall in demand for CD music systems would lead to fewer resources being allocated to the production of this good in a market economy

Week 3

Read the following article then answer the questions underneath:

Karl Marx (1818–1883)

Karl Marx was an extremely influential thinker whose ideas ignited the movement by a third of the world's countries towards **communism** in the 20th century. Marx provided a criticism of capitalism.

Capitalism is a system where the small minority – the '**bourgeoisie**' (the owners of capital such as machines and factories) – are the ruling class, and the masses – the '**proletariat**' (the labourers) – provide the labour to produce goods and services.

Marx essentially believed that economic systems progress through different stages – capitalism is just one stage in this development process and, due to its weaknesses and flaws, will eventually self-destruct, leading to the final stage of communism.

Marx believed that capitalists (the owners of capital), whose objective is to make a profit, must end up **exploiting** workers to achieve this objective. This means that workers will earn wages lower than their true value.

Capitalists will also have an **incentive** to replace labour with machines, creating both more **monotonous** jobs as well as unemployment. The combined effect will be to create an exploited and alienated workforce, leading to social unrest.

He also believed that competition would cause many firms to go bust, leading to a few firms holding monopoly power which would allow them to further exploit both workers and consumers. This would also lead to owners of the bust firms joining the ever-increasing proletariat majority, causing social tensions to further increase.

The capitalist economic system is also weak, Marx said, since it is an unplanned system which causes one crisis after another. This impacts most negatively on the proletariat. Marx believed that **revolution** among the proletariat was inevitable. Revolution would enable workers to seize the capital (so that ownership would be among the majority).

Economic planning would direct economic activity. As the economic system moves towards communism, there would be abolition of private property replaced by common ownership of resources.

However, although Marx wrote a lot criticising capitalism, he wrote relatively little on how communism would work. Marxism has had a resurgence lately. Many global problems, such as the Global Financial Crisis and growing inequalities observed in many economies, may have their root cause in the free market system.

1. What do you understand by the term 'communism'?
2. What do the following terms mean:
 - Exploiting
 - Incentive
 - Monotonous
3. Who are the winners and losers under a system of communism?
4. Who makes the decisions about the allocation of resources under the kind of system proposed by Marx?
5. What do you think are the main criticisms of a Marxist system/communism?
6. What do you think it would be like for a worker in a factory in this kind of system?

Research ideas

1. Watch the video clip The World According to Marx from the BBC Two Masters of Money series, by Stephanie Flanders (www.bbc.co.uk/programmes/p00z0yb2). It is approximately four minutes long. Stephanie explains why capitalism, according to Marx, is inherently unstable and will lead to crisis after crisis. Watch the video and write a summary of the key points.
2. The end of the 20th century saw the general collapse of communism. Identify the reasons why communism in practice had major weaknesses as an economic system.



Week 4

Read the following article then answer the questions underneath:

John Maynard Keynes (1883 – 1946)

John Maynard Keynes was a British economist, whose ideas fundamentally changed the theory and practice of **macroeconomics** and the economic policies of governments. Originally trained in mathematics, he built on and greatly refined earlier work on the causes of **business cycles**, and was one of the most influential economists of the 20th century. Widely considered the founder of modern macroeconomics, his ideas are the basis for the school of thought known as Keynesian economics.

During the Great Depression of the 1930s, Keynes spearheaded a revolution in economic thinking, challenging the ideas of **neoclassical economics** that held that free markets would, in the short to medium term, automatically provide full employment, as long as workers were flexible in their wage demands.

He argued that aggregate demand (total spending in the economy) determined the overall level of economic activity, and that inadequate aggregate demand could lead to prolonged periods of high unemployment.

Keynes advocated the use of government policies to reduce the adverse effects of economic **recessions and depressions**. He detailed these ideas in his book, *The General Theory of Employment, Interest and Money*, published in 1936. In the mid to late-1930s, leading Western economies adopted Keynes's policy recommendations. Almost all capitalist governments had done so by the end of the two decades following Keynes's death in 1946.

Keynes's influence started to wane in the 1970s, partly as a result of the stagflation that plagued the Anglo-American economies during that decade, and partly because of criticism of Keynesian policies by Milton Friedman and other monetarists

When Time magazine included Keynes among its Most Important People of the Century in 1999, it stated that "his radical idea that governments should spend money they don't have may have saved capitalism." The Economist has described Keynes as "Britain's most famous 20th-century economist."

1. Keynes' ideas promote what we call a 'mixed economy'. Describe what we mean by this phrase.
2. How do Keynes' economic ideas differ from:
 - Adam Smith
 - Karl Marx
3. Explain the following terms (you may need to research them):
 - Macroeconomics
 - Business cycle
 - Neoclassical Economics
 - Recessions and Depressions
4. What is the economic role of the free market/private businesses in a system proposed by Keynes?
5. Find out what we mean by the term 'Market Failure'
6. What role does the government play in a Keynesian system?

Additional Task:

Produce a short presentation/powerpoint slides summarising the three different economic approaches of Smith, Marx and Keynes. You can do further research if you choose, and can be as creative as you wish. I would welcome seeing what you produce!

Further reading

To further your knowledge of literature, you could read some of the texts suggested below.

- Tim Harford – *The Under Cover Economist* – Introduction and Chapter 1
- Crash Course Economics Introduction - https://www.youtube.com/watch?v=3ez10ADR_gM. These are fast moving videos from America, but this series is a very good summary of what Economics is all about!