AQA Economics A-level
Microeconomics

Topic 1: Economic Methodology and the Economic Problem

1.4 Scarcity, choice and allocation of resources

Notes

- The basic economic problem is scarcity. Wants are unlimited and resources are finite, so choices have to be made. Resources have to be used and distributed optimally.

- For example, if you only have £1 and you go to a shop, you can buy either the chocolate bar or the packet of crisps. The scarcity of the resource (the money) means a choice has to be made between the chocolate and the crisps.

- This gives rise to **opportunity cost**. The opportunity cost of a choice is the value of the next best alternative forgone. In the above example, the opportunity cost of choosing the crisps is the chocolate bar.

- If a car was bought for £15,000 and after 5 years the value depreciates by £5,000, the opportunity cost of keeping the car is £5,000 (which could have been gained by selling the car), regardless of the starting price.

- Opportunity cost is important to economic agents, such as consumers, producers and governments. For example, producers might have to choose between hiring extra staff and investing in a new machine. The government might have to choose between spending more on the NHS and spending more on education. They cannot do both because of finite resources, so a choice has to be made for where resources are best spent.