Complete Economics for Cambridge IGCSE® & O Level Workbook

Third Edition

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Oxford excellence for Cambridge IGCSE® & O Level
What’s in your workbook?

Your workbook is divided into six main parts matching those of the Cambridge IGCSE and O Level syllabus in Economics. These are further sub-divided into a number of sections covering all the topics and aims of the Cambridge Economics course.

In each section you will find:

<table>
<thead>
<tr>
<th>Content</th>
<th>Key Words</th>
<th>Revision Summary</th>
</tr>
</thead>
<tbody>
<tr>
<td>These pages cover all the topics and aims of your economics course. On each page there is: a series of questions to help you develop your knowledge and understanding of at least one key topic and aim space under each question for you to write your answer an extension exercise to extend your key skills in economics.</td>
<td>An exercise to help you learn, revise and use economic vocabulary and terminology covered in the section. The exercise involves matching key terms to the definitions and explanations provided. Together, the key word sections in your workbook will build a complete dictionary of all the key economic terms you will need to know and understand by the end of your course.</td>
<td>A full summary of all the key economic facts, definitions, concepts, principles and theories covered in the section. You will need to complete the summary with missing economic terms and definitions. Spaces are provided for you to write in your answers. Taken together, all the summaries in your workbook will provide a useful revision guide to help refresh and strengthen your knowledge of economics as you prepare for your final exams.</td>
</tr>
</tbody>
</table>

At the end of each unit you will find:

<table>
<thead>
<tr>
<th>Working with data and diagrams</th>
<th>Multiple choice questions</th>
<th>Structured questions</th>
</tr>
</thead>
<tbody>
<tr>
<td>The ability to use data and diagrams to demonstrate economic concepts and changes in economic conditions is an important skill. This section provides practical help and exercises to build your skills of analysis including making calculations with economic data and presenting data in diagrams and charts.</td>
<td>Eight or more multiple choice questions to test your understanding of all the topics covered in the unit and to provide exam practice.</td>
<td>A series of structured questions that require longer written answers. Completing them will test your knowledge and help you to build your skills in presenting economics facts, theories and arguments.</td>
</tr>
</tbody>
</table>

At the end of your workbook there are:

<table>
<thead>
<tr>
<th>Answers</th>
</tr>
</thead>
<tbody>
<tr>
<td>Model answers for every question in your workbook, including key word and revision exercises, for you to learn and revise from. Compare them with your own answers to check your understanding and to make sure that you have covered the key points.</td>
</tr>
</tbody>
</table>
How you will be assessed

This workbook is designed to help you develop and practise the three key skills you will need to demonstrate in your answers to examination questions in order to achieve a good grade.

**KNOWLEDGE AND UNDERSTANDING**

You will be assessed on how well you:

✓ show knowledge and understanding of definitions, formulas, concepts, principles and theories
✓ use economic vocabulary and terminology.

**ANALYSIS**

The exams will test your ability to:

✓ select, organize and interpret data
✓ use economic information and statistics to recognize patterns in data and to deduce economic relationships
✓ apply economic knowledge and understanding to written, numerical, diagrammatic and graphical data
✓ analyse economic issues and situations, identifying causes and links.

**EVALUATION**

You will also be assessed on your ability to:

✓ evaluate economic information and data
✓ distinguish between economic analysis and reasoned statements
✓ recognize uncertainties of the outcomes of economic decisions and events
✓ communicate your economic thinking in a logical and clear manner.

Your skills will be assessed in two examination papers. The key skills assessed in each paper are listed below in order of the importance placed on them.

<table>
<thead>
<tr>
<th>Paper</th>
<th>Duration</th>
<th>Types of questions</th>
<th>Key skills assessed</th>
<th>Contribution of paper to final grade</th>
</tr>
</thead>
<tbody>
<tr>
<td>1 Multiple choice</td>
<td>45 minutes</td>
<td>30 questions – all must be answered</td>
<td>An, KU</td>
<td>30%</td>
</tr>
<tr>
<td>2 Structured questions</td>
<td>2 hours  15 minutes</td>
<td>1 compulsory question from Section A plus a choice of 3 questions from Section B</td>
<td>Ev, An, KU</td>
<td>70%</td>
</tr>
</tbody>
</table>

Your answers to all examination questions will be marked and your overall performance graded A to G. The grade you achieve will depend on how well you demonstrate the required skills in each paper.
Grade A students must show excellence in all key skills. Answers to more difficult questions should be outstanding and show good use of real world examples.

Grade C students must demonstrate they have a good understanding of the course content and some ability to answer the more difficult questions.

Grade F students must show some familiarity with the key economic concepts and issues covered in the course. They should be able to answer basic questions correctly and attempt some of the more difficult questions.

To prepare for your final exams it is important that you practise providing answers to many different examination questions throughout your course.

**Answering multiple choice questions**

A multiple choice question requires you to choose an answer from four possible options. When you have decided on the correct response, you must indicate your choice on the answer sheet. Each right answer to a question is awarded one mark. No marks are deducted for wrong answers.

You have just 45 minutes to answer 30 multiple choice questions in Paper 1. This means you have 1.5 minutes on average to read and answer each question. However, some questions may take more time to read and answer than others.

**Multiple choice ‘do’s and don’ts’**

- Do read through each question carefully. Some questions may appear to have more than one right answer, but only one will be correct. Eliminate all the wrong answers before selecting the best one.
- Don’t spend too long on a question. If a question is difficult then move on to the next question and return to the difficult ones later.
- Do try to leave yourself at least 5 minutes before the end of the exam to check your answers and to complete any you may have missed.
- Don’t worry if you are unsure about the answer to a question. You have a 25% chance of choosing the right answer to a multiple choice question. So ...
- Do make sure you provide answers to all 30 questions.

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1. An entrepreneur is someone who:
   - A produces goods and services (X)
   - B owns and runs a factory (X)
   - C organizes resources in a firm (✓)
   - D supervises other workers (X)

   A is wrong because workers are also producers of goods and services.
   B is partially true but not all firms have factories.
   C is the best answer.
   D refers to labour. A supervisor is a senior worker or manager in a firm organized by an entrepreneur.
Answering structured questions

A **structured question** is a series of related questions based on some information describing a real economic situation. Some questions may require short, one word answers or a single sentence. Others will require more detailed explanations.

Exam Paper 2 requires you to complete four structured questions.

<table>
<thead>
<tr>
<th>Section A</th>
<th>Section B</th>
</tr>
</thead>
<tbody>
<tr>
<td>Contains up to a page of information including text, statistical tables and charts on a real economic situation. You must complete the structured question in this section. It will contain a mixture of up to eight short answer questions and more difficult questions about the information presented. A maximum 30 marks are available in this section.</td>
<td>Contains six structured questions. You must complete three of these. Each structured question contains: • a sentence or short paragraph introducing a real economic situation • four individual questions based on the introduction. A maximum 60 marks are available in this section, i.e. 20 marks per structured question.</td>
</tr>
</tbody>
</table>

Here is an example of the type of structured question you may find in Section B.

Developing countries have characteristics that are different from those of more developed countries. One of these is the amount of poverty in such countries.

(a) Define **absolute poverty**. [2]

(b) Explain **two** features of a developing country. [4]

(c) Analyse what is likely to happen to the occupational structure and geographical distribution of the population in a country as it becomes more developed. [6]

(d) Discuss whether government policies will always be successful at reducing poverty in a developing country. [8]

How much should I write to answer each question?

You will be provided with an answer booklet in the exam in which to write your answers. Enough space for you to write a good answer to each question is provided in the booklet. The more space given, the longer and more detailed your answer must be to earn full marks.

This is a short answer question. It only requires a short definition or explanation to be given. Two line spaces will normally be enough.

This question requires you to present arguments for and against the statement to demonstrate critical evaluation skills. Eight or more line spaces will be provided for your answer.
### How do I know what the questions want me to do?

A command word or phrase, such as ‘define’, ‘explain’, ‘analyse’ or ‘discuss’ is used at the start of each question to tell you what you need to do. Each command word tells you to answer a question in a particular way in order to assess different key skills.

<table>
<thead>
<tr>
<th>Common commands</th>
<th>What you need to do</th>
<th>Key skills assessed</th>
</tr>
</thead>
<tbody>
<tr>
<td>Analyse</td>
<td>Examine the information provided to identify and describe economic reasons why an outcome may or may not occur.</td>
<td></td>
</tr>
<tr>
<td></td>
<td>‘Analyse the motives that might cause a person to save’</td>
<td>An</td>
</tr>
<tr>
<td></td>
<td>‘Analyse three reasons why a market economic system may fail’</td>
<td>Ev</td>
</tr>
<tr>
<td></td>
<td>‘Analyse the motives that might cause a person to save’</td>
<td>KU</td>
</tr>
<tr>
<td>Calculate</td>
<td>Work out a number(s) or percentage(s) from the information provided.</td>
<td>An</td>
</tr>
<tr>
<td></td>
<td>‘Calculate the reduction in profit between 2007 and 2008’</td>
<td></td>
</tr>
<tr>
<td></td>
<td>‘Calculate the change in total employment. Show your workings’</td>
<td></td>
</tr>
<tr>
<td>Define</td>
<td>Give a precise meaning for a key economic term.</td>
<td>KU</td>
</tr>
<tr>
<td></td>
<td>‘Define deflation’</td>
<td></td>
</tr>
<tr>
<td></td>
<td>‘Define economic growth’</td>
<td></td>
</tr>
<tr>
<td>Describe</td>
<td>State key points about a topic or give characteristics or main features.</td>
<td>KU</td>
</tr>
<tr>
<td></td>
<td>‘Describe two reasons why car production is usually undertaken by large multinationals’</td>
<td></td>
</tr>
<tr>
<td></td>
<td>‘Describe what can influence the demand for smart phones’</td>
<td></td>
</tr>
<tr>
<td>Discuss</td>
<td>Explain and contrast, in a structured way, economic reasons or arguments for and against a particular statement or proposal. Where possible, say what arguments or reasons you support and why to gain full marks. These type of questions usually award 8 or more marks.</td>
<td></td>
</tr>
<tr>
<td></td>
<td>‘Discuss why a small food shop might survive when there are very large supermarkets’</td>
<td>KU</td>
</tr>
<tr>
<td></td>
<td>‘Discuss how firms might achieve a rise in profits’</td>
<td>Ev</td>
</tr>
<tr>
<td>Explain</td>
<td>Set out why and/or how an economic situation or outcome can occur. Make relationships between different economic variables clear and support your answers with relevant evidence.</td>
<td></td>
</tr>
<tr>
<td></td>
<td>‘Explain why the social costs of car use are greater than the private costs’</td>
<td>KU</td>
</tr>
<tr>
<td></td>
<td>‘Explain why a reduction in unemployment might increase inflation’</td>
<td>An</td>
</tr>
<tr>
<td></td>
<td>‘Explain why the social costs of car use are greater than the private costs’</td>
<td>Ev</td>
</tr>
<tr>
<td>Give</td>
<td>Provide an answer from recall or memory.</td>
<td>KU</td>
</tr>
<tr>
<td></td>
<td>‘Give an example of an indirect tax’</td>
<td></td>
</tr>
<tr>
<td></td>
<td>‘Give three ways of measuring the size of a firm’</td>
<td></td>
</tr>
<tr>
<td>Identify</td>
<td>Name or select, from information provided, relevant economic facts, characteristics, relationships, measures or factors that may have caused changes in economic conditions to occur.</td>
<td></td>
</tr>
<tr>
<td></td>
<td>‘Identify two functions of money’</td>
<td>KU</td>
</tr>
<tr>
<td></td>
<td>‘Using information from the extract, identify two characteristics of monopoly’</td>
<td></td>
</tr>
<tr>
<td></td>
<td>‘Using information from the extract, identify two indicators of improved living standards in Mozambique’</td>
<td></td>
</tr>
<tr>
<td>State</td>
<td>Express economic factors, relationships or facts in clear terms.</td>
<td>KU</td>
</tr>
<tr>
<td></td>
<td>‘State four ways in which multinational companies can help a developing country such as Bangladesh’</td>
<td></td>
</tr>
<tr>
<td></td>
<td>‘State two types of tax’</td>
<td></td>
</tr>
</tbody>
</table>
Structured question ‘do’s and don’ts’

- Don’t rush. Plan your exam time carefully and make sure you understand what each question is about before you start writing your answers. This means reading each question slowly and in full and re-reading them if necessary.
- Do look out for the command words and economic terms in each question to identify what the question is about and what is expected from your answer.
- Don’t try to write down everything you know about the economic concepts, theories or facts in each question. Only write down what the question requires as a response. Writing more than necessary wastes valuable time and is unlikely to gain you any extra marks.
- Do look at the marks for each question to consider how long or detailed your answer should be. The more marks there are, the more is expected.
- Don’t forget to correctly label any diagrams you draw.

Now let’s see how well the student below applied these ‘do’s and don’ts’ to the structured question example on page vi.

(a) Define absolute poverty. [2]

<table>
<thead>
<tr>
<th>Student answer</th>
</tr>
</thead>
<tbody>
<tr>
<td>Absolute poverty occurs when people cannot meet their basic human needs including food, safe drinking water, sanitation, health, shelter and education. The extent of absolute poverty in a country is usually measured by the number of people living on the equivalent of less than around $2 to $3 per day. Absolute poverty is widespread in a number of countries in Africa but also remains significant in many rapidly developing countries including India and China.</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Examiner’s comments</th>
</tr>
</thead>
<tbody>
<tr>
<td>The student has correctly explained what absolute poverty is in the first sentence and this will gain full marks. However, the answer provided is far too long for 2 marks. It provides examples of countries where many people live on less than around $2 or $3 each day. This is not required and will not earn any extra marks.</td>
</tr>
</tbody>
</table>
(b) **Explain two features of a developing country.** [4]

<table>
<thead>
<tr>
<th><strong>Student answer</strong></th>
<th><strong>Examiner’s comments</strong></th>
</tr>
</thead>
<tbody>
<tr>
<td>A developing country has a relatively low level of economic development and low average income per head. Many people live in poor housing conditions with poor sanitation and have relatively low life expectancy. Birth and death rates are high resulting in rapid population growth. Road, rail and communication networks also tend to be underdeveloped.</td>
<td>The student describes a number of features of a developing economy correctly but only two are required for full marks. Writing more than necessary will have wasted valuable examination time.</td>
</tr>
</tbody>
</table>

(c) **Analyse what is likely to happen to the occupational structure and geographical distribution of the population in a country as it becomes more developed.** [6]

<table>
<thead>
<tr>
<th><strong>Student answer</strong></th>
<th><strong>Examiner’s comments</strong></th>
</tr>
</thead>
<tbody>
<tr>
<td>As a country develops it experiences growth in its manufacturing, construction and service industries. Employment and incomes generated by these industries increase. Over time they will account for a larger and larger proportion of jobs and incomes in the country. The share of total employment accounted for by farming and other primary industries falls. As incomes and education improve, people also tend to marry later and have less children. As a result the average age of the population tends to increase. This is shown in the diagram.</td>
<td>The student has clearly understood the term occupational distribution for 1 mark and has correctly identified that increased economic development is usually associated with growth in manufacturing, construction and service industries and employment. This will gain a further 2 marks. However, the student has failed to describe the movement of people from rural areas to growing urban areas that also tends to occur with increased development. Instead the student wrongly describes what may happen to the age distribution and draws an age–sex population pyramid in an attempt to demonstrate this. The diagram is not required but it is also missing labels that will explain what the diagram shows.</td>
</tr>
</tbody>
</table>

(d) **Discuss whether government policies will always be successful at reducing poverty in a developing country.** [8]

<table>
<thead>
<tr>
<th><strong>Student answer</strong></th>
<th><strong>Examiner’s comments</strong></th>
</tr>
</thead>
<tbody>
<tr>
<td>Yes. I believe that government policies designed to reduce poverty will always do so otherwise there would be no point introducing them. For example, lowering taxes and increasing welfare payments will boost the incomes of the poorest people in society. Increasing the minimum wage will also help to increase incomes. The government can also spend more on education to help people get better paid jobs in the future. Policies designed to boost economic growth will help to increase employment and incomes.</td>
<td>The student has only presented economic arguments that support a view that government policies successfully reduce poverty. Reasons why some government policies designed to reduce poverty may fail to do so are not presented. For example, lowering taxes and/or increasing welfare benefits may still leave a lot of people on very low incomes; raising the minimum wage will only benefit those people able to work; not everyone benefits equally from economic growth. Only up to 4 marks can be awarded for a one-sided presentation. Many students find questions that require them to present and discuss reasoned arguments difficult. Many will often express their opinions rather than presenting and contrasting different economic theories and evidence.</td>
</tr>
</tbody>
</table>
What should I do if I am running out of time in my exam?
It is always a good idea to prepare your answer to a difficult question, especially one requiring a longer answer, by writing down all the key points you want to make in a series of short notes before you write your answer in full. This will help you think through what the most important points are and to make any corrections before you finalize your answer.

Making notes in your answer booklet will be an especially sensible thing to do if you are running out of time in your final exam and will not be able to answer every question you need to in full. This is because examiners will award marks for your notes if they show you have understood the question and they demonstrate a good knowledge and understanding of the relevant economic ideas, facts and theories.

Example
Discuss whether a reduction in agricultural subsidies will be beneficial to employment and the standard of living in a country.

<table>
<thead>
<tr>
<th>How to structure your answer</th>
<th>The notes you might make in the exam</th>
</tr>
</thead>
</table>
| Give reasons why the action may be beneficial | • Other jobs may be created if the government gives subsidies to other industries instead, invests in new infrastructure projects or cuts taxes  
• Importing more food may be cheaper than subsidizing domestic farms |
| Suggest reasons why the action may not be beneficial | • Reducing subsidies will increase farm production costs, reduce profits and reduce the supply of food products  
• Prices of domestic agricultural products are likely to rise – consumers will be worse off, especially those on low incomes  
• Employment and income may fall significantly if the agricultural sector is a major employer |
| Suggest and justify any alternative actions you can think of | Government could instead:  
• invest in re-training farm workers to take other jobs  
• help to train farmers in new farming methods so they become more productive, reduce costs and increase the supply of food |
| Summarize and conclude your arguments | Cutting agricultural subsidies may be beneficial if:  
• other industries can expand to provide more jobs  
• farms become more efficient as a result  
• imported food is cheaper  
• taxes can be lowered |
### 1.1 The nature of the economic problem

#### 1.1.1 Finite resources and unlimited wants

1. What problem in economics do the two newspaper headlines below illustrate? [2]

   - **Extreme weather will triple food shortages**
   - **Engineering jobs hardest to fill as skills shortage continues**

2. All countries face economic problems, so choices have to be made. Define *economic problem*. [2]

3. A factory producing motor vehicles runs out of important component parts and has to stop production. Explain how this illustrates the basic economic problem. [2]

4. Using examples, explain *two* ways in which human *wants* differ from human *needs*. [4]

   - [Continue explanation]

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**E**

Explain why it is impossible to solve the basic economic problem.
1.1.2 Economic and free goods

1. Explain why air is an example of a free good in economics. [2]

2. Explain why cars are economic goods. [4]

3. Identify one way in which free goods and economic goods are similar and one way they differ. [4]

4. Explain how a new idea posted on the internet may be considered a free good. [4]

Which of the following are examples of free goods and which are economic goods?

<table>
<thead>
<tr>
<th></th>
<th>Free good?</th>
<th>Economic good?</th>
</tr>
</thead>
<tbody>
<tr>
<td>Pebbles on the beach</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Computers</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Air</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Factories</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
1.2 The factors of production

1.2.1 Definitions of the factors of production and their rewards

1. Explain the difference between ‘labour’ and ‘enterprise’ and how they are rewarded. [4]

2. Explain two ways in which labour is different from land. [4]


Factors of production are scarce productive resources. They are organized into firms by entrepreneurs to produce goods and services. We consume or ‘use up’ goods and services to satisfy our different needs and wants.

Identify two examples of labour, land and capital resources that are likely to be used in the production of the following products: (a) clothing (a durable consumer good), (b) milk (a non-durable consumer good), (c) the teaching of educational courses (a service), and (d) a newly constructed office block (a capital good).
1.2.2 The mobility of the factors of production

1. Define *factor mobility*. [2]

2. Explain how a lorry is an example of a mobile factor of production. [4]

3. Explain how (a) geographical immobility and (b) occupational immobility may affect the allocation of labour in an economy. [4]

4. Explain the concepts of factor mobility and factor immobility using an area of farmland as an example. [4]

Describe how a firm may increase the mobility of the labour and capital it uses. What are the potential benefits to the firm of increasing the mobility of the resources it employs?
1.2.3 Quantity and quality of the factors of production

1. Using examples, explain the difference between renewable and non-renewable resources. [4]

2. Explain two ways farmers could improve the quality of their farmland. [4]

3. Explain what schools and colleges can do to increase the quality of labour. [4]

4. Explain two ways the factor of production of land could be increased in an economy. [4]

Using examples, explain how advances in technology have improved both the quantity and quality of different factors of production.
### Key words

**Match economic terms with their definitions**

<table>
<thead>
<tr>
<th></th>
<th>Human needs</th>
<th>Human-made resources including machinery, tools and factory buildings, used in the production of other goods and services</th>
</tr>
</thead>
<tbody>
<tr>
<td>2</td>
<td>Human wants</td>
<td>Skills possessed by successful entrepreneurs: business know-how and the ability to organize productive activities</td>
</tr>
<tr>
<td>3</td>
<td>Production</td>
<td>The using up of goods and services by consumers to satisfy their human needs and wants</td>
</tr>
<tr>
<td>4</td>
<td>Free goods</td>
<td>The ability to move or reallocate factors of production from one productive task to others</td>
</tr>
<tr>
<td>5</td>
<td>Economic goods</td>
<td>All scarce resources used to produce other goods and services. They are the inputs to productive activities</td>
</tr>
<tr>
<td>6</td>
<td>Consumption</td>
<td>These are limited in supply. People are therefore willing to pay to obtain them</td>
</tr>
<tr>
<td>7</td>
<td>Goods and services</td>
<td>The ability or extent to which factors of production can be moved or reallocated between different productive uses without incurring significant costs or a loss of output</td>
</tr>
<tr>
<td>8</td>
<td>Capital goods</td>
<td>Human desires for different goods and services to give them satisfaction. These desires are without limit and increasing</td>
</tr>
<tr>
<td>9</td>
<td>Consumer goods</td>
<td>The ability to move or reallocate factors of production from one location to another</td>
</tr>
<tr>
<td>10</td>
<td>Factors of production</td>
<td>Human effort used up in productive activities</td>
</tr>
<tr>
<td>11</td>
<td>Land</td>
<td>Basic human requirements for life and survival</td>
</tr>
<tr>
<td>12</td>
<td>Labour</td>
<td>Goods produced to satisfy consumer needs or wants</td>
</tr>
<tr>
<td>13</td>
<td>Capital</td>
<td>Organizations in which entrepreneurs combine and organise factors of production to produce goods and services</td>
</tr>
<tr>
<td>14</td>
<td>Enterprise</td>
<td>The outputs (or ‘products’) of productive activities using scarce resources</td>
</tr>
<tr>
<td>15</td>
<td>Firms</td>
<td>Goods produced specifically to make other goods and services and not intended for immediate consumption</td>
</tr>
<tr>
<td>16</td>
<td>Entrepreneur</td>
<td>These are goods we may need or want that are without limit</td>
</tr>
<tr>
<td>17</td>
<td>Factor mobility</td>
<td>Using resources to make and deliver goods and services to satisfy the needs and wants of consumers</td>
</tr>
<tr>
<td>18</td>
<td>Occupational mobility</td>
<td>All natural resources used to produce other goods and services</td>
</tr>
<tr>
<td>19</td>
<td>Geographic mobility</td>
<td>A person with enterprise who is willing to take the risks and decisions necessary to organize scarce resources into firms to produce goods and services</td>
</tr>
</tbody>
</table>
1. ____________ of resources is the central problem in economics. Human wants are ____________ and there are just not enough resources in the world to produce all the goods and services required to satisfy all our needs and wants.

2. Resources are the inputs to productive activities and economic goods are the outputs of productive activities. Economic goods are therefore ____________ in supply because the resources used up to produce them are finite.

3. Resources are also known as ____________ because they are used to produce goods and services.

4. Economists recognize four broad types of factors of production: labour, enterprise, land and capital. Entrepreneurs organize and combine these factors of production into ____________ in order to produce goods and services that will satisfy some of our needs and wants. If they are successful and able to sell the goods or services they produce at a price that exceeds their cost of production, they will be rewarded with ____________.

5. Entrepreneurs possess a factor of production called ____________. It refers to their willingness and ability to organize production into firms.

6. ____________ consists of all natural resources, including water, minerals, oils, plants and animals, that are used up in the production of other goods and services.

7. ____________ is the mental and physical effort supplied by people to firms to make goods and services, usually in return for ____________ or salaries.

8. ____________ refers to human-made resources, including machinery, equipment and factory buildings. These ____________ goods are not intended for immediate consumption but are instead used to produce and supply other goods and services.

9. Increasing both the quantity and ____________ of factor resources available can help to increase the amount of economic goods and services they are able to produce. As a result, more human needs can be met and more human wants can be ____________.

10. For example, increasing the number of skilled workers will increase labour productivity and ____________. This will make it easier to move labour between different productive uses either within a firm or between different firms in different industries.

11. The more mobile factors of production are the easier it is for them to be allocated to their best possible uses so that they are able to produce as many goods and services as they possibly can. However, some factors of production are ____________. This will make it difficult to move them from one productive use to another as consumer demand for different product changes or technology changes.

12. For example, a factory building cannot be moved. That is, it is ____________ immobile but it could be used to produce computers or car parts. In contrast, while it is possible to move a floating oil platform, it can only be used to drill for oil and gas at sea. Similarly, a bricklayer could not quickly or easily change occupation to become a surgeon. Many workers with limited or very specialist skills are ____________ immobile.
1.3.1 Definition of opportunity cost

1.3.2 The influence of opportunity cost on decision making

1. What, according to the definition of ‘opportunity cost’, is sacrificed when a decision on how to use scarce resources is taken? [2]

2. Explain why the scarcity of resources creates an opportunity cost. [4]

3. Explain why all organizations should consider opportunity cost when deciding how to use their factors of production. [4]

Explain how the two newspaper headlines below illustrate the economic concepts of scarcity and opportunity cost.

- Australian government boosts spending on defence and surveillance while continuing to cut funding for health, education and welfare
- Increase in demand for land to grow soybeans threatens further deforestation of the Amazon Rainforest
The basic economic problem

1.4 Production possibility curve (PPC) diagrams

1.4.1 Definition of a PPC
1.4.2 Points under, on and beyond a PPC
1.4.3 Movements along a PPC

1. The cost of a decision in an economy to use more of its resources to increase the production of consumer goods will be fewer capital goods. Draw a production possibility curve diagram in the space provided to show this impact. [4]

2. Using a diagram, analyse how a production possibility curve can be used to illustrate the concept of opportunity cost. [6]

A firm is able to produce handbags and shoes. The most handbags it can produce per week is 1,000. Alternatively, it can produce up to 600 pairs of shoes per week. Draw and label a diagram to show its production possibility curve.

Currently the firm produces 500 handbags and 300 pairs of shoes each week. Mark this point on your diagram and explain why the firm could produce more output without the need for additional resources. Also explain why it is currently unable to produce 900 handbags and 700 pairs of shoes per week.
1.4.4 Shifts in a PPC

1. The diagrams below show what has happened to the production possibility curves for two economies. Which economy has expanded its capacity to produce goods and services and which economy has experienced negative economic growth? [2]

A

![Diagram A]

B

![Diagram B]

2. Explain two factors that would cause the production possibility curve of an economy to shift outwards. [4]

3. Explain two factors that would cause the production possibility curve of an economy to shift inwards. [4]

International migration is reducing the supply of labour and enterprise in some countries and increasing it in others. Draw two production possibility curve diagrams to show the impact these changes could have on two different national economies.
### Key words

**Match economic terms with their definitions**

<table>
<thead>
<tr>
<th></th>
<th>Topic</th>
<th>Definition</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Opportunity cost</td>
<td>This is shown by an outward shift in a PPC resulting from an increase in the quantity and/or quality of the resources available either to an individual firm or an entire economy</td>
</tr>
<tr>
<td>2</td>
<td>Production possibility curve (PPC)</td>
<td>Any area, such as a nation state, in which the economic activities of production, exchange and consumption take place</td>
</tr>
<tr>
<td>3</td>
<td>A decrease in productive capacity</td>
<td>A curved line on a diagram that shows all the possible combinations of two products that a firm or an entire economy is able to produce with its existing resources and know-how if they are fully and efficiently used</td>
</tr>
<tr>
<td>4</td>
<td>An inefficient allocation of resources</td>
<td>The benefit that is foregone from choosing one use of scarce resources over the next best use of those same resources</td>
</tr>
<tr>
<td>5</td>
<td>An increase in productive capacity</td>
<td>This occurs if factor resources are not fully or effectively used either within a firm or an entire economy. Production will be at a point below its PPC. More output could be produced if existing resources were better utilized</td>
</tr>
<tr>
<td>6</td>
<td>An economy</td>
<td>This is shown by an inward shift in a PPC resulting from a decrease in the quantity and/or quality of the resources available either to an individual firm or an entire economy</td>
</tr>
</tbody>
</table>
### Revision summary

1. Because resources are scarce relative to human __________, all societies must choose how to allocate them between different uses: what goods and services to produce, how to produce them and which needs and wants to satisfy.

2. Making a choice between alternative uses of scarce resources therefore always involves a cost in terms of what we have to give up in return. The benefit of the next best alternative foregone is the ___________ of that decision.

3. ___________ is therefore the cost of choice. Choosing one use for scarce resources will always mean giving up the opportunity to use those same resources in another way, and the loss of other goods and services they might otherwise have produced instead.

4. A ___________ curve (PPC) diagram provides a simple way of illustrating opportunity cost and the most efficient allocation of resources between the production of two products. Moving along a PPC indicates more of one product can be produced but only at the expense of reducing production of the other product.

5. An increase in the productive potential of an economy will shift its PPC __________. This may be the result of an increase in the quantity or quality of resources available.

6. However, the PPC will shift __________ towards the origin if there is a reduction in the resources available to the economy; for example, if workers emigrate, if non-renewable resources become depleted or worn-out capital equipment is not replaced.
Production possibility curve (PPC) diagrams are used to illustrate the economic concept of opportunity cost. Like all diagrams, it is important to label and use them correctly.

1. The diagram below shows the production possibility curve for a firm producing bicycles and skateboards. It shows the firm is able to produce a maximum of either 500 skateboards or 400 bicycles each week with its factors resources. However, important labels are missing from the diagram. From the list provided, add the correct labels to the correct places on the diagram.

2. The firm in the diagram above is currently producing 400 skateboards and 200 bicycles each week at point A on its production possibility curve. Using the diagram, calculate the opportunity cost of a decision to increase the production of bicycles to 300 each week (point B). [2]

3. What would be the opportunity cost of a decision to only produce bicycles (point C)? [2]

4. Explain why the firm is unable at present to produce the combination of outputs at point D. [2]

5. Imagine that the firm is currently only producing 300 skateboards and 150 bicycles each week (point E). What advice, if any, would you give the owners of the firm? [2]
Multiple choice questions (Paper 1)  

Tick or circle the correct answers

1. The basic economic problem is:  
   (a) Destruction of the natural environment  
   (b) Increasing prices  
   (c) Underemployment of scarce resources  
   (d) Human wants exceed available resources

2. Which of the following is a factor of production?  
   (a) The bread produced in a bakery  
   (b) The oven used in a bakery  
   (c) The wages paid to bakery workers  
   (d) The profit received by the bakery owner

3. Parvin runs a small business. She has just completed a course to learn how to start and run a successful business. Which factor of production is most likely to have increased as a result?  
   (a) Capital  
   (b) Enterprise  
   (c) Labour  
   (d) Land

4. Which of the following resources used in the production of glass would an economist classify as land?  
   (a) A kiln  
   (b) Skilled glass workers  
   (c) Sand  
   (d) Safety goggles

5. What, according to the definition of opportunity cost, is given up when a decision is taken?  
   (a) An identical alternative  
   (b) The next best alternative  
   (c) All possible alternatives  
   (d) The least desirable alternative

6. A firm produces 1,000 units of a good X and 600 units of a good Y each week using its resources. It wants to increase output of X to 1,200 units per week. To do so it must cut production of Y to 500 units per week. What will be the opportunity cost of the decision to increase the output of good X by 200 units each week?  
   (a) 200 units of Y per week  
   (b) 500 units of Y per week  
   (c) 100 units of Y per week  
   (d) 250 units of Y per week

7. A firm making smart phones and tablet computers operates its two factories 24 hours each day in order to maximize production at point X on its production possibility curve. However, a problem at one of its suppliers of component parts causes the firm to close one of its factories temporarily. Which point on the diagram could represent its new position?

8. A farmer uses one of his fields to plant corn. What could be the opportunity cost of this decision?  
   (a) The cost of the seeds  
   (b) Wages paid to his farm workers  
   (c) The water used to irrigate the field  
   (d) Using the field to grow potatoes
Structured questions (Paper 2, part A)

1. Boeing ramps up production of its Dreamliner

US aircraft maker Boeing is ramping up production rates for two of its most popular planes, the 737 and the 787 Dreamliner. The Boeing Vice President of product development said that increasing automation has been key to achieving higher production rates including retraining its workforce to operate more advanced machinery and industrial robots.

During the first three quarters of this year, Boeing delivered 101 Dreamliners, a 29 percent increase over the same period last year. Boeing in the third quarter also delivered 126 model 737s, compared to 120 in the third quarter of last year. In contrast, production of its 767, 747 and 777 plane models has reduced.

The recent announcement by Boeing’s Chief Executive that the company plans to open a 737 completion plant in China could boost production rates for the model further in the future. The planned facility would install seats, in-flight entertainment systems, and some galleys and lavatories, as well as completing the custom paint job for each airline. However, engineers and machinists in Boeing’s US factories fear the move could mean some of their jobs being transferred to Chinese workers.

a) Give an example of opportunity cost from the extract. [2]
b) Using examples from the extract, identify three factors of production used to make and supply aircraft. [6]
c) Using a production possibility curve, analyse how Boeing may allocate its resources between its 787 Dreamliner and other aircraft models. [6]

Structured questions (Paper 2, part B)

2. All economic decisions involve an opportunity cost.
   a) Define opportunity cost. [2]
   b) Explain why economic decisions will involve an opportunity cost. [4]
   c) Using a production possibility curve diagram, analyse how it can demonstrate the concept of opportunity cost. [6]
   d) Discuss the extent to which the concept of opportunity cost is relevant only to government spending decisions. [8]

3. All countries face the economic problem and must choose how to allocate their factors of production.
   a) Define the economic problem. [2]
   b) Using appropriate examples, explain the four factors of production. [4]
   c) Analyse how a production possibility curve can be used to show the consequences of a change in the allocation of resources between the production of two goods. [6]
   d) Discuss whether more factors of production should be used to build roads. [8]
2.1 Microeconomics and macroeconomics

2.1.1 Microeconomics

2.1.2 Macroeconomics

1. Explain the difference between microeconomics and macroeconomics. [4]

2. Identify the three main groups of decision makers involved in the study of microeconomics. [4]

3. Describe three key macroeconomic issues. [6]

Identify the macro or microeconomic issues and decision makers described in each news article.

The Czech central bank has raised interest rates for the fourth time in just under a year, as the country’s economy continues to accelerate and record-low unemployment pushes up wages fuelling fears of rising price inflation.

Car maker Porsche axes all diesel cars from its range due to ‘falling consumer demand’ for the fuel type.

Demand for gold jewellery in India fell by as much as 30% in the run-up to the Diwali festival due to heavy rains in October and an increase in gold bullion prices after the introduction of the new goods and services tax.
2.2 The role of markets in allocation of resources

2.2.1 Key resource allocation decisions
2.2.2 The market system
2.2.3 The price mechanism

1. What three questions can be used to define the problem of resource allocation in an economy? [3]

2. Explain the difference between market equilibrium and market disequilibrium in a market economy. [4]

3. Analyse the role of the price mechanism in a market economy. [6]

How are producers in a market economy likely to respond to the following changes in market conditions?

- A new consumer report confirms that demand for plant-based food is on the rise. The report states that the sales growth of vegan food and produce is outpacing total food and beverage sales in supermarkets.

- The sales and profitability of hard disk computer drives has been on the decline this year because of slow demand for personal computers and tough competition from solid-state drives.

- UK manufacturers feel the pinch as raw material costs rise.
### Key words

| 1  | Microeconomics | E  | A | This occurs in a market when consumer demand for the product is exactly equal to the amount producers are willing and able to supply each period. As a result, the market price and quantity traded will be stable from period to period. |
| 2  | Macroeconomics | B  | The means by which decisions are made about what goods and services are produced, how they are produced and who they are produced for in a free market economy. |
| 3  | Macroeconomy | C  | The distribution of scarce productive resources among different uses. |
| 4  | Resource allocation | D  | Any set of arrangements that brings together all the producers and consumers of a good or service so they may engage in trade or exchange. |
| 5  | Market economic system | E  | The study of the economic decisions and actions of individual consumers, producers and households and how they interact to determine different market outcomes. |
| 6  | Mixed economic system | F  | The state of a market when the quantity producers are willing and able to supply each period differs from the quantity consumers are willing and able to buy. |
| 7  | Market | G  | The study of major economics issues and conditions that affect a national economy. |
| 8  | Market equilibrium | H  | An economic system that combines free markets with government planning to allocate its scarce resources and distribute goods and services. |
| 9  | Market disequilibrium | I  | The means by which the decisions of many different consumers and producers interact and cause changes in market prices which in turn help to determine how scarce resources should be allocated within a market economy. |
| 10 | Price mechanism | J  | A national economy. |
The allocation of resources

2.1 Microeconomics and macroeconomics

2.2 The role of markets in allocation of resources

Revision summary

Fill in the missing words and economic terms

1. The problem of \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_ involves finding solutions to three key questions: what goods and services to produce; how to produce them; and who to produce them for. Who decides and how they decide the 'answers' to these questions in an economy is referred to as its \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_.

2. The decisions of many individual consumers, producers and households will determine what goods and services are produced and who they are produced for in a \_\_\_\_\_\_ economic system.

3. The \_\_\_\_\_\_ mechanism in a market economy ensures that scarce resources are allocated to their most profitable uses. Changes in \_\_\_\_\_\_ prices provide signals to producers about what goods and services consumers want and will earn the most \_\_\_\_\_\_.

4. \_\_\_\_\_\_economics involves studying what influences the economic decisions of consumers, producers and households, how their decisions interact and the impact they can have on different market outcomes (market prices and quantities exchanged).

5. In contrast, \_\_\_\_\_\_economics involves the study of major economic issues and actions, including those taken by a government in a \_\_\_\_\_\_ economic system, that affect the national economy.
2.3 Demand

2.3.1 Definition of demand
2.3.2 Price and demand
2.3.3 Individual and market demand

1. Define demand. [2]

2. Explain the difference between a ‘human want’ for a product and an ‘effective demand’ for a product. [3]

3. If you plot the market demand curve for a product on a graph, what units would you measure (a) on the vertical axis, and (b) on the horizontal axis? [4]

4. Explain why market demand curves for most products are ‘downward sloping’. [4]

5. Explain the difference between a ‘movement along a demand curve’ and a ‘shift in a demand curve’. [4]
2.3.4 Conditions of demand

1. What is the difference between complementary products and products that are substitutes in demand? [4]

2. Using examples, explain what is likely to happen to the demand for (a) a normal good, and (b) an inferior good following an increase in the disposable incomes of consumers. [4]

3. State three factors that may have caused the shift in the market demand curve from D1 to D2 in diagram (a) and three different factors that may have caused the shift in the market demand curve from D1 to D2 shown in diagram (b). [6]

A rise in the price of product A results in a fall in demand for product B and a rise in demand for product C. Which two of these products are in joint demand and which two are products that can satisfy the same consumer demand?
2.4 Supply

2.4.1 Definition of supply
2.4.2 Price and supply
2.4.3 Individual and market supply

1. Define supply. [2]

2. Explain how the supply curve of a product of an individual firm and the market supply curve for the same product are related. [4]

3. If you plot the market supply curve for a product on a graph, what units would you measure (a) on the vertical axis, and (b) on the horizontal axis? [4]

4. Explain why the market supply curves for most products are ‘upward sloping’. [4]

5. Explain the difference between a ‘movement along a supply curve’ and a ‘shift in a supply curve’. [4]
2.4.4 Conditions of supply

1. The profitability of producing a product A has increased due to technical advance, reducing its cost of production. In contrast, new regulations have increased the cost of producing a product B. Explain the impact these changes are likely to have on the allocation of resources between product A and B and the amount of each product producers are willing to supply to consumers. [4]

2. State three factors that may have caused the shift in the market supply curve from S1 to S2 in diagram (a) and three different factors that may have caused the shift in the market supply curve from S1 to S2 shown in diagram (b). [6]

(a) (b)

---

From each article below, identify how market supply conditions have changed.

- Government announces deep cuts in subsidies for solar panels
- Japanese car makers struggle to continue production as earthquake hits parts suppliers
- Warm spring weather is welcome news for strawberry growers
- Falling oil price reduces manufacturing costs
- Minimum wage rise in Shenzhen where some of China's largest electronics manufacturers are located, could impact tech product costs worldwide
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