**Scarcity**

**LVL I Answer the following questions as you read**:

1. What is scarcity?
2. What are the scarce productive resources named?
3. What is the difference between scarcity and a shortage of a good/service?
4. What risks do entrepreneurs take when starting a business?
5. What is the primary factor that influences entrepreneurs to take risks?
6. What other factors influence entrepreneurs to take risks?
7. What does opportunity cost mean?

**a. Define scarcity as a basic condition that exists when unlimited wants exceed limited productive resources.**

**Scarcity** should be defined as a basic condition that exists when unlimited wants exceed limited productive resources. The scarce productive resources (factors of production) are land, labor, capital, and entrepreneurship. Things that are scarce are both limited AND desirable. For example, crude oil is a land resource that is limited because there is only so much of it that can produced and made available to society at any given time. It is also desirable because it is used to produce goods and services. In market economies, things that are scarce are usually allocated by price. Items that are more relatively scarce (more limited and/or more desirable) will usually carry a relatively high price. In some cases, something that was once considered not scarce can become so. For example, there was a time when restaurants had to pay companies to haul away used cooking oil (undesirable). Now used cooking oil is often purchased by biofuel companies because it can be used in production. The cooking oil has become both limited AND desirable. There are also a small number of “free” goods that are desirable but not limited. For example, we can enjoy the sunshine outside or breathe the oxygen around us without paying for it.

Not everything that is scare is tangible. A good example of this phenomenon is time. At some point, all of us wished that we had more time for something like studying, working, spending time with friends/family, etc.

However, you must recognize the difference between scarcity and a shortage. Scarcity always exists while a shortage is temporary. **Shortages** occur when a resource, good, or service becomes unavailable for a period of time due to circumstances affecting the market. For instance, if a gasoline pipeline is damaged and has to be shut down for repair, geographic areas that get fuel from that pipeline may find their gas stations temporarily out of fuel. Gasoline is always scarce (limited and desirable). However, in this example, the market for gasoline is experiencing a temporary shortage until the pipeline is repaired.

**Is it scarce?**

|  |  |  |  |
| --- | --- | --- | --- |
| **Example** | **Is it limited?** | **Is it desirable?** | **Is it scarce?** |
| Time |  |  |  |
| Water |  |  |  |
| Garbage |  |  |  |
| Air We Breathe |  |  |  |

**b. Define and give examples of productive resources (i.e. factors of production): natural resources (i.e. land), human resources (i.e. labor and human capital), physical capital and entrepreneurship.**

**Productive resources**, also known as **factors of production**, are scarce items used in the production of goods and services in an economy. The four factors of production are land, labor, capitol and entrepreneurship. **Natural resources**, also known as **land** resources, are the gifts of nature we use to produce goods and services. For example, a tree is a natural resource used in the production of goods like lumber or paper. **Human resources** are the people involved in the production of goods and services. People offer their time to production as well as their physical abilities, knowledge, and skills. The abilities each person brings to the production process is known as their **human capital**. Producers of goods and services need physical capital too. **Physical capital** refers to tools, machines, and structures used over and over again in the production of goods and services. While natural, human, and capital resources are essential to production, we rely on the fourth productive resource, **entrepreneurship**, to bring the resources together in innovative ways to produce a product. An entrepreneur is a person who takes risks such as using one’s own financial resources to make a prototype of a product or buy the capital resources required to start the business.

**c. Explain the motivations that influence entrepreneurs to take risks (e.g., profit, job creation, innovation, and improving society).**

Becoming an **entrepreneur** usually involves taking risks such as using one’s own financial resources to make a prototype of a product or buy the capital resources required to start the business. Some entrepreneurs may have to quit jobs from which they receive a relatively secure, predictable income in order to have enough time to invest in their new enterprise. In most cases, entrepreneurs begin new businesses because they believe the potential rewards of success outweigh the potential costs associated with the risks. The motivations of entrepreneurs include profit, job creation, innovation, and improving society. Traditionally, the field of economics sees the **profit motive** as the primary driver of entrepreneurship. Those who start private firms believe they can operate the business in a way that the revenues (price times the quantity of goods/services sold) they receive will be greater than the costs (costs of production plus the income they gave up to start the business). In very basic terms, profit is equal to a firm’s revenue minus its costs. Entrepreneurs may also be motivated by the opportunity to create a successful business that can **provide jobs** for people in the industry. According to [a](http://www.kauffman.org/what-we-do/resources/entrepreneurship-policy-digest/the-importance-of-young-firms-for-economic-growth) 2015 reportby the Kauffman Foundation, new businesses accounted for ALL net new job creation and 20 percent of gross job creation. **Innovation** is another key motivation. Many successful entrepreneurs work as employee experts in their industry before venturing out on their own. During their time as employees, they often see ways companies could improve efficiency or production. They may apply their expertise to new products during their non-working hours. At some point, the desire to put their ideas to the test may become greater than their need for the security of a regular salary. Finally, some entrepreneurs start for-profit companies or non-profit organizations because they believe their product or service will **improve society**. For example, there are microfinance companies linking individual lenders to individual borrowers. This service provides financial resources to people who would be unlikely to qualify for traditional bank loans and a return to lenders who would like to see their money help grow the businesses of others.

**d. Define opportunity cost as the next best alternative given up when individuals, businesses, and governments confront scarcity by making choices.**

The study of economics is all about the choices made by individuals, businesses, and governments. From an economist’s view, all choices involve both benefits and cost. The value of one’s next best alternative given up when a choice is made is called **opportunity cost**. For example, if you have the choice of going to the movies with your friends or studying for your economics quiz tomorrow. Since you choose to study because you care about your grade very much and wouldn’t want to disappoint me, the opportunity cost of your decision is going to the movie. However, do note, that opportunity cost is only between two items. If you have more than two options the opportunity cost is ONLY between the two most desirable options, not any of the other ones. Opportunity cost can also be in monetary form. For example, if your choice is between mowing your neighbor’s lawn for $25 and going fishing, and you choose fishing, then the opportunity cost of that decision is $25. Additionally, the cost could include the cost of what option you choose. For instance, if the choice is between mowing your neighbor’s yard, again for $25, or going to buy a new fishing pole for $50. If you chose to buy the pole, your opportunity cost is $75 because you must add the cost of the pole to what you would have gained by mowing the lawn.

**LVL II Consider the following questions**

1. What two characteristics make something scarce?
2. What is an example of a scarce land resource?
3. How are scarce items allocated in a market economy?
4. What is the typical relationship between scarcity and price?
5. What is an example of each of the four productive resources (factors of production)?

**LVL III Do the following**

1. List 5 decisions you’ve had to make today. Discuss the trade-offs associated with each decision and specify what the opportunity cost of your decision was.