

Exercise walk-through

2.3

Supply

IGCSE Economics

The price mechanism

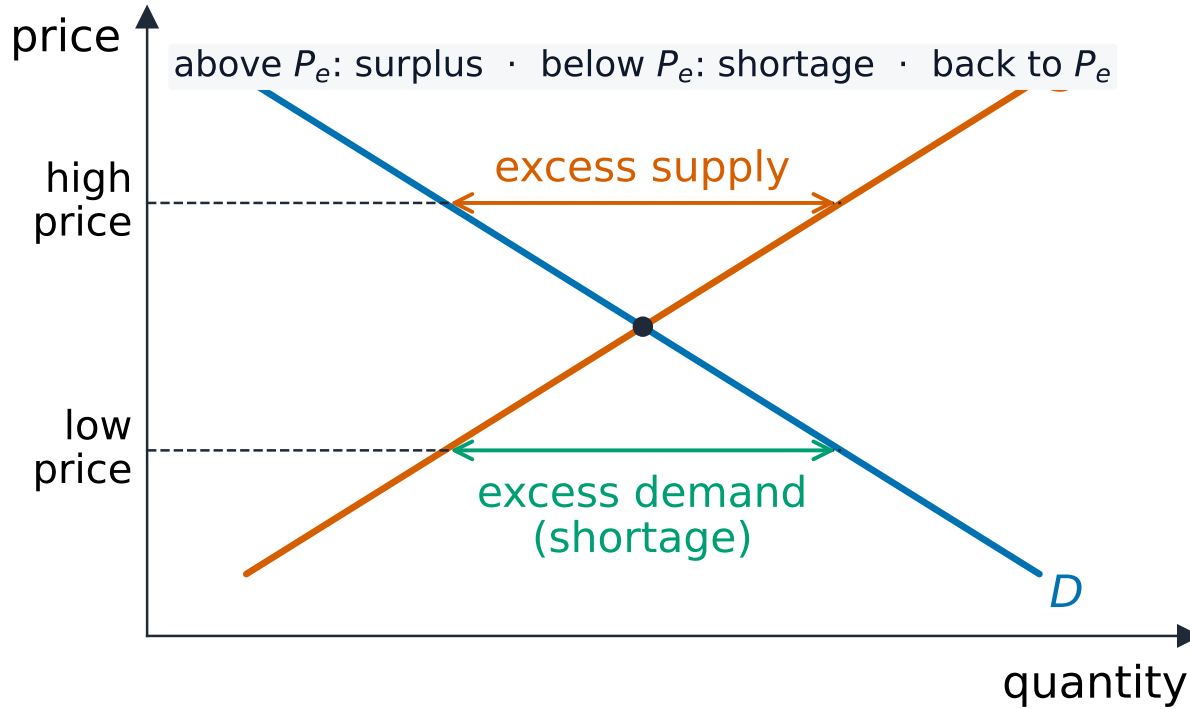
In a free **market** , the **price mechanism** **allocates** resources – deciding what is made, how, & for whom.

- **signalling** – tells what to make
- **incentive** – a reason to supply
- **rationing** – shares out scarce goods



Prices guide who buys and what is made

Equilibrium – two



Equilibrium

Public goods

Private good

rival + excludable
firms supply it for profit
(e.g. an apple, a phone)

Public good

non-rival + non-excludable
free-rider problem, so the
government must supply
(e.g. street lighting)

Exam: public goods fail the free-rider test — non-rival and non-excludable → government supply

A **public good** (street lights) is **non-rival** and **non-excludable**, so the market supplies none of it.

Exercises 2.1-2.3

2.1 State the *law of supply*.

[2]

2.2 State two conditions that shift the supply curve.

[2]

2.3 State the effect on supply of a rise in the costs of production.

[1]

Exercises 2.1-2.3

2.1 State the *law of supply*. [2]

2.1

- the **law of supply**: when price **rises**, quantity supplied **rises** (and vice versa) (K)
-

2.2 State two conditions that shift the supply curve. [2]

2.2

- any **two** of: **costs of production** / **technology** / **taxes or subsidies** / **weather** / **number of firms** (K, K)
-

2.3 State the effect on supply of a rise in the costs of production. [1]

2.3

- higher costs mean firms supply less at every price
- supply **falls** (the curve shifts **left**) (K)

Exercises 3.1-3.2

3.1 A government **subsidy** to producers will shift the supply curve:

[1]

☐

- A left, because costs rise
- B right, because costs fall
- C left, because demand falls
- D there is no effect on supply

3.2 Using a supply diagram, explain how a rise in the cost of raw materials affects supply.

[4]

Exercises 3.1·3.2

3.1 A government **subsidy** to producers will shift the supply curve:

[1]

☐

- A left, because costs rise
- B right, because costs fall
- C left, because demand falls
- D there is no effect on supply

3.1 B

- a **subsidy** lowers costs, so supply shifts **right** (K)
- A is a tax; C confuses demand with supply; D is false

3.2 Using a supply diagram, explain how a rise in the cost of raw materials affects supply.

[4]

3.2

- draw a labelled supply diagram: supply shifts **left** $S \rightarrow S_1$ (K)
- dearer raw materials **raise costs** (An)
- firms supply less at every price $\rightarrow$ the supply curve shifts **left** (An)

Exercise 3.3

3.3 Analyse how an improvement in technology would affect the supply of a good. [6]

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3.3

- technology is a **condition of supply** (K)
- better technology **lowers costs**, so firms can make more for the same cost (An)
- the supply curve **shifts right** → supply rises (and, with demand unchanged, price falls and quantity rises) (An)