

Exercise walk-through

2.8

Market economic system

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

Micro and macro, and what a market is

microeconomics

single parts of the economy – one industry, one product, one household

macroeconomics

the economy as a whole – growth, inflation, unemployment, trade

a market

any place *or system* where buyers and sellers meet to trade

no building needed

it can be online, or over the phone – what makes it a market is the trading, not the location

**ceteris
paribus**

“other things equal” – change one thing at a time and hold the rest fixed

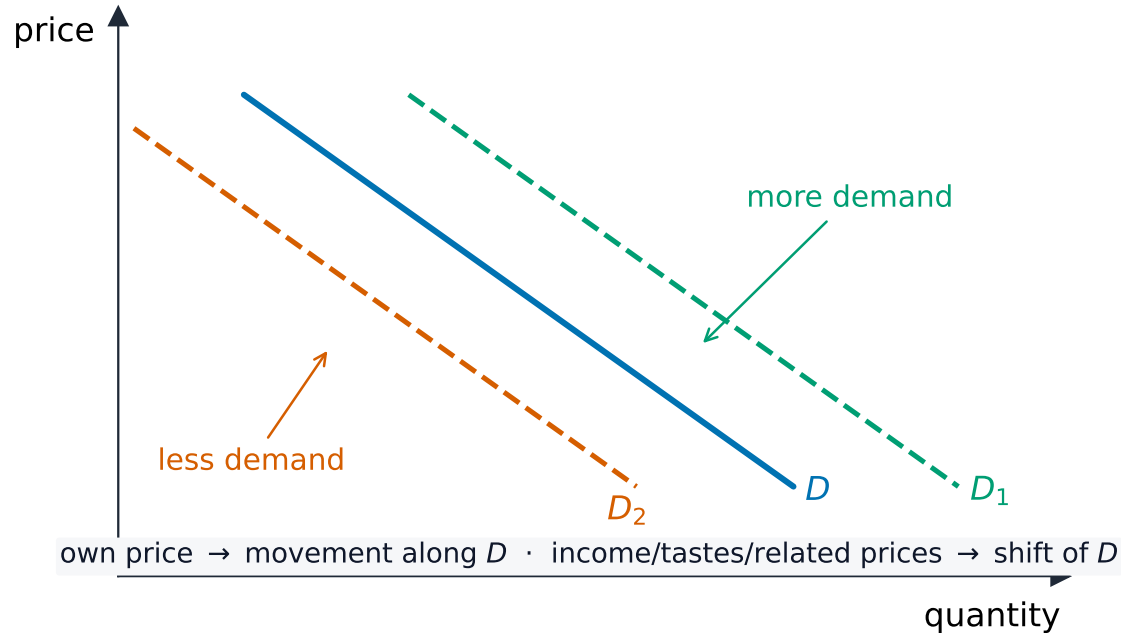
Every demand or supply diagram carries *ceteris paribus* silently. It is the reason a curve can shift at all.

Demand

Demand slopes **down**: a higher price, less bought (**law of demand**).

Own price → a **movement along**; income, tastes & related prices **shift** the curve.

Demand, in detail



The demand curve slopes down. A change in income, tastes, population or related prices shifts the whole curve; a change in the good's own price is a movement along it.

Movements along, and shifts of, the curve

Two different ideas, and the exam separates them:

- **quantity demanded** – the amount bought *at one price*;
- **demand** – the whole pattern of buying at *every price*.

- A change in the good's **own price** $\Rightarrow$ a **movement along** the curve. You slide to a new point on the same line.
- A change in **anything else** $\Rightarrow$ a **shift** of the whole curve.
Rightward: more at every price.

Own price moves you **along**; everything else **shifts** the line.

Exercises 2.1-2.3

2.1 Define the term *market economy*.

[2]

2.2 State two advantages of the market economic system.

[2]

2.3 State one disadvantage of the market economic system.

[1]

Exercises 2.1-2.3

2.1 Define the term *market economy*. [2]

2.1

- a **market economy** lets the **price mechanism** (demand and supply) make all resource-allocation decisions, with no government planning (K)

2.2 State two advantages of the market economic system. [2]

2.2

- any **two** of: prices guide resources without planning / **competition** lowers costs and creates new goods / wide **consumer choice** (K, K)

2.3 State one disadvantage of the market economic system. [1]

2.3

- any **one** of: useful but unprofitable goods are not made / the **poor** may get little / markets can **fail** (K)

Exercises 3.1·3.2

3.1 In a market economy, decisions about what to produce are made by: [1]

☐

A the government

B the price mechanism (demand and supply)

C a central planner

D trade unions

3.2 Explain one disadvantage of relying only on the market system to allocate resources. [4]

Exercises 3.1·3.2

3.1 In a market economy, decisions about what to produce are made by: [1]

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- A the government
- B the price mechanism (demand and supply)
- C a central planner
- D trade unions

3.1 B

- in a market economy the **price mechanism** decides what to produce (K)
- A and C are a planned economy; D is not an allocator

3.2 Explain one disadvantage of relying only on the market system to allocate resources. [4]

3.2

- the market only makes goods that earn a **profit** (K)
- **public goods** (street lighting) and **merit goods** may be under-provided (An)
- the poor, who cannot pay, may go without essentials (An)

Exercise 3.3

3.3 Discuss whether a market economy is the best way to allocate a country's resources.[8]

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3.3

- **for:** prices allocate efficiently; competition drives lower costs and innovation; consumers have choice (K + An)
- **against:** it under-provides public and merit goods, ignores external costs, and can leave the poor with too little (An)
- **judgement (Ev):** the market works well for most goods, but a **mixed** economy usually allocates resources better