

Webnote 120

Please do not print this webnote. Class notes are available on webnotes in section 1.2 of website

1.1 **6** Big Ideas

Big Idea

1

Big Idea

2

Big Idea

3

Big Idea

4

Big Idea

5

Big Idea

6

4 elasticities-Big Ideas

Section 1.1 Markets

The BIG ideas!

Webnote 110

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Syllabus Items 1-17

HL only: 6,11+13

Search

1.1 Syllabus Items

116 IB Questions for 99

Syllabus 1.1 Markets

102 Supply Function

103 Demand Function

104 Consumer Producer Surplus

105 Consumer + Producer Surplus

108 Allocation (Fish in Duesseldorf)

109 Market (price mechanism) Advantages

111 Market (price mechanism) Disadvantages I

112 Market (price mechanism) Disadvantages II



STRESS MANAGEMENT TECHNIQUES
1.
2.
3.
4.

"Howl at an ambulance or fire siren every chance you get. Run around the room in circles with a sock in your mouth. Eat a messy meal without using your hands or utensils. Ask a friend to scratch your belly..."

Adam Smith- 'Invisible hand'.



Adam Smith: The In..
Liberty Learn



Episode 14: Market ..

The Price Mechanism



AS-Level Economic...

110 - Big Ideas 1.1

You Tube for 1.1

113 - S + D worksheet

114 - Data Response

106 Supply Worksheet

107 Demand Worksheet

115 Supply + Demand Worksheet

117 Crossword Microeconomics

118 Signal + Incentive

Webnote 110: Big Ideas for 1.1

Section 1.1 Markets

The **BIG** ideas!

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Key concepts in section 1.1:

1. Demand
2. Supply
3. Evaluate market system
4. Exam question
5. Linear function (**hl only**)

Section 1.1 Markets

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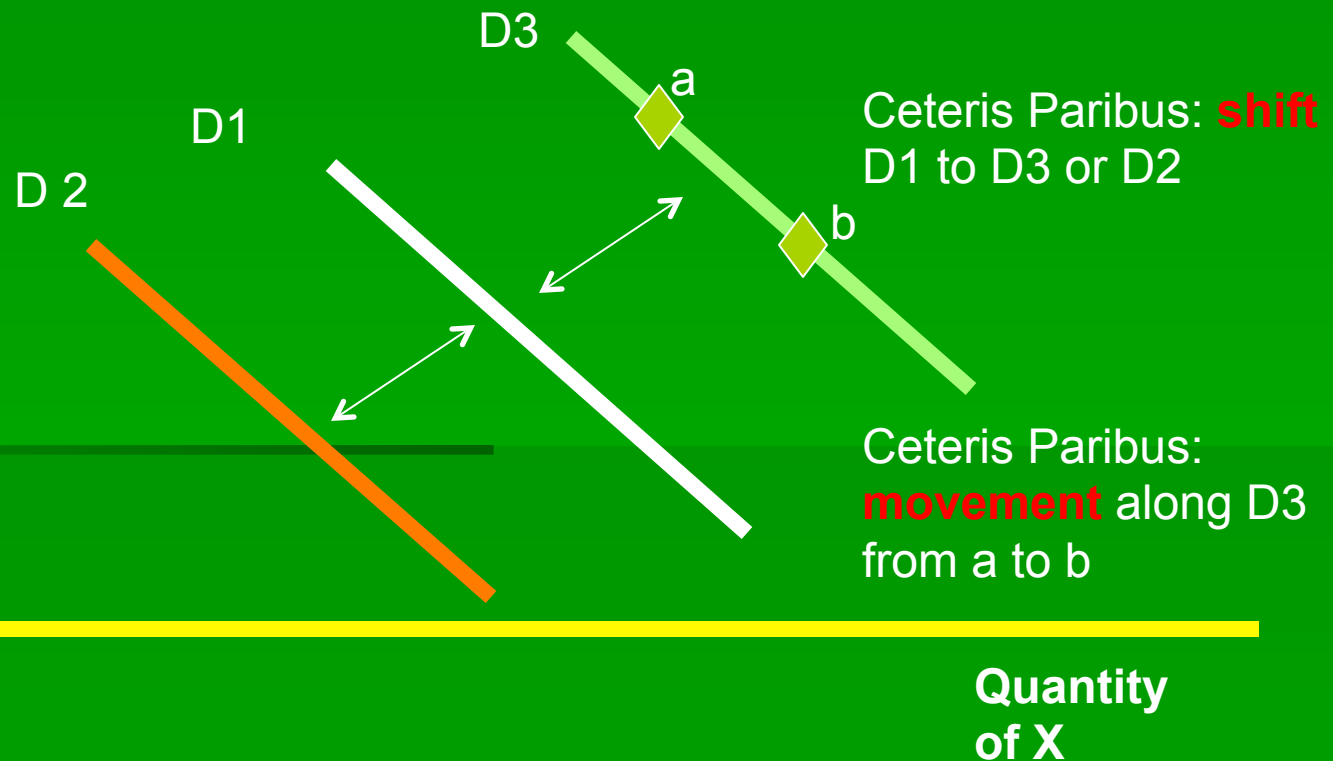
The BIG ideas! Demand

Big Idea

1

Demand Function: $q_D^X = f(P_X, P_C, P_S, Y, \text{Taste/fashion, advertising, population etc})$

Price of X



See webnote 102

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The **BIG** ideas! Supply

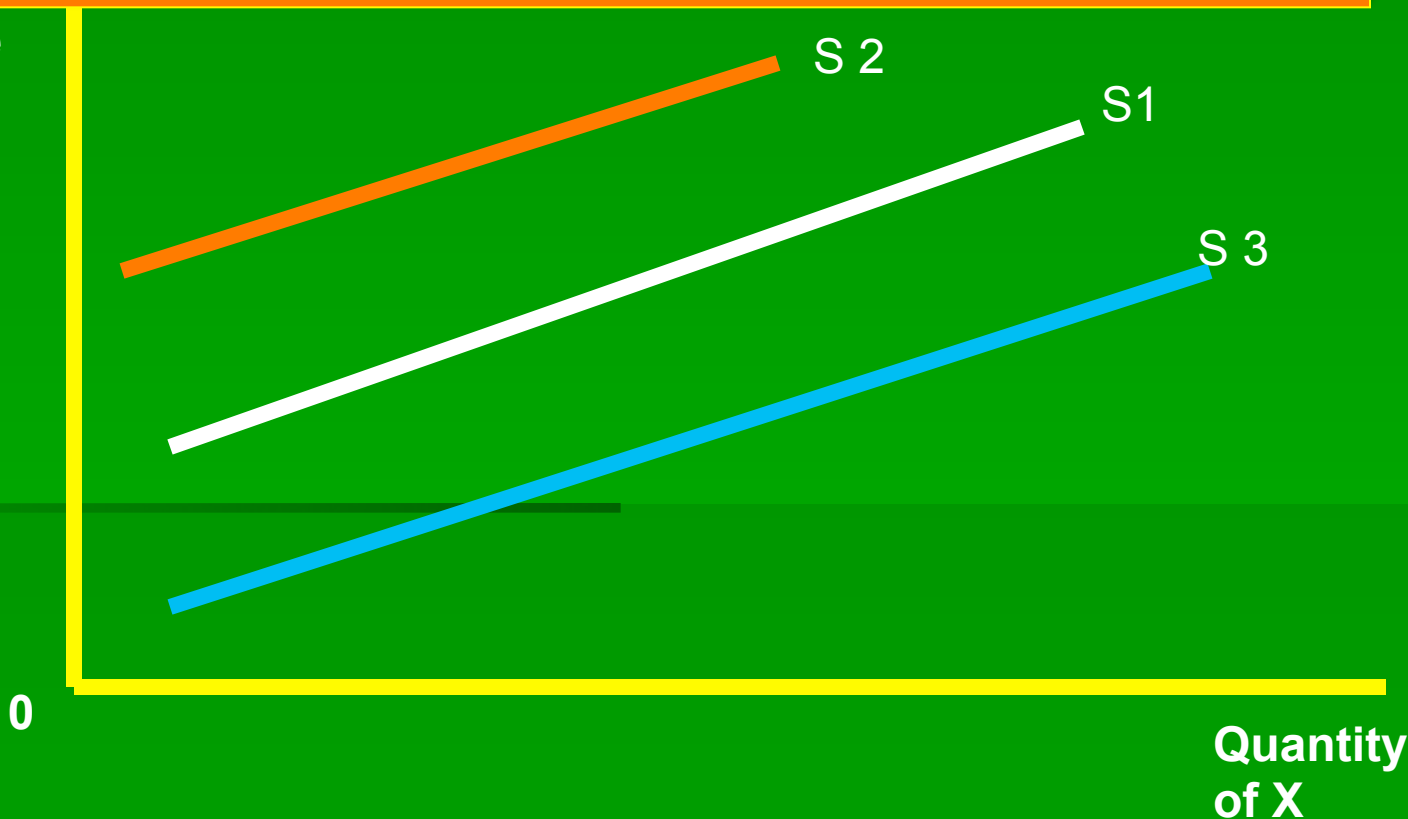
Big Idea

2

Supply Function: $q_S^X f: (P_X, P_f, P_s, G, \text{technology, weather etc})$

Price of X

See webnote 103



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Section 1.1 Markets

The **BIG** ideas!

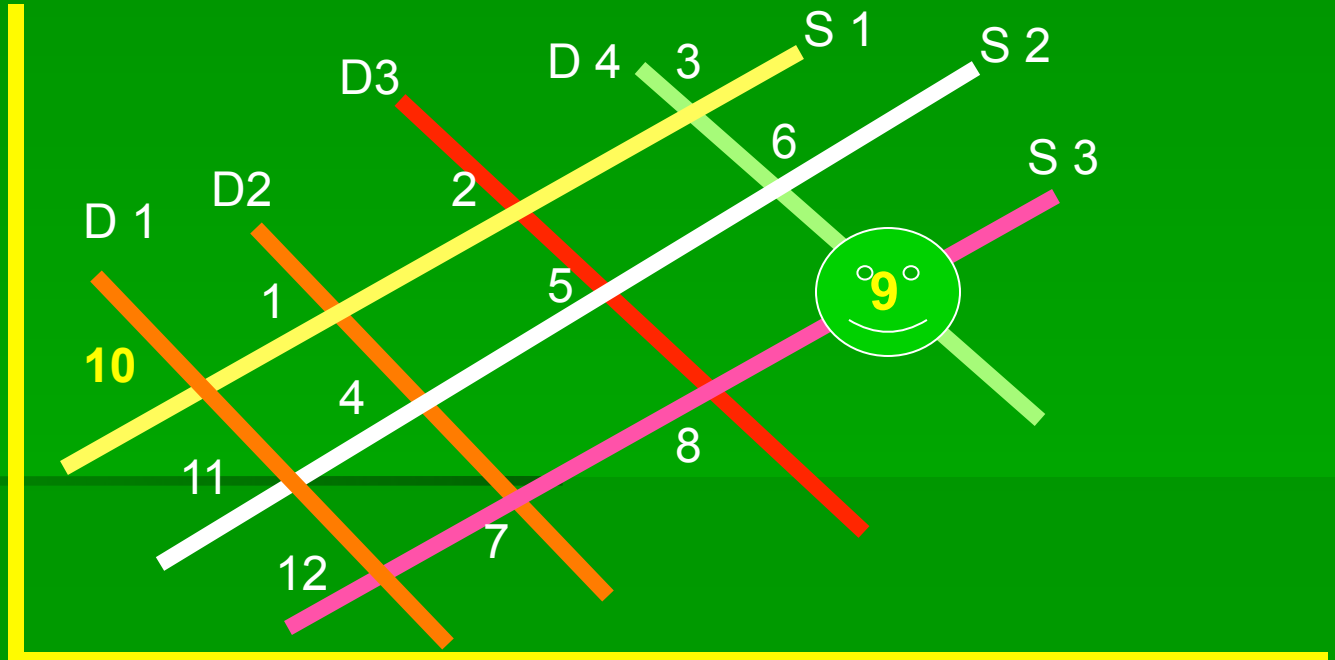
Big Idea

3

Supply+Demand = Market. Shifts and Movements allocate scarce resources on the X axis and price sends signals and non price determinants also result in allocation changes on the X axis.

What possible changes need to take place for a market to adjust from e-10 to e-9?

Price of X



Quantity of X

Quick Task!

Where to....the market allocates?



- On a supply and demand diagram start at E 9+ show how the following statements will affect the market for mobile phones:

Note the market is currently at **E9**

1. Government increases indirect taxation on mobile phones from 19 to 23%
2. incomes fall due to an economic slowdown
3. Consumer legislation forces firms to offer a 2 year guarantee of their products
4. Government introduces laws to limit the use of mobile phones in public places
5. Micro chip design allow mobile phone operators to reduce their input costs
6. Studies show that use of mobile phones can damage hearing and increase levels of concentration

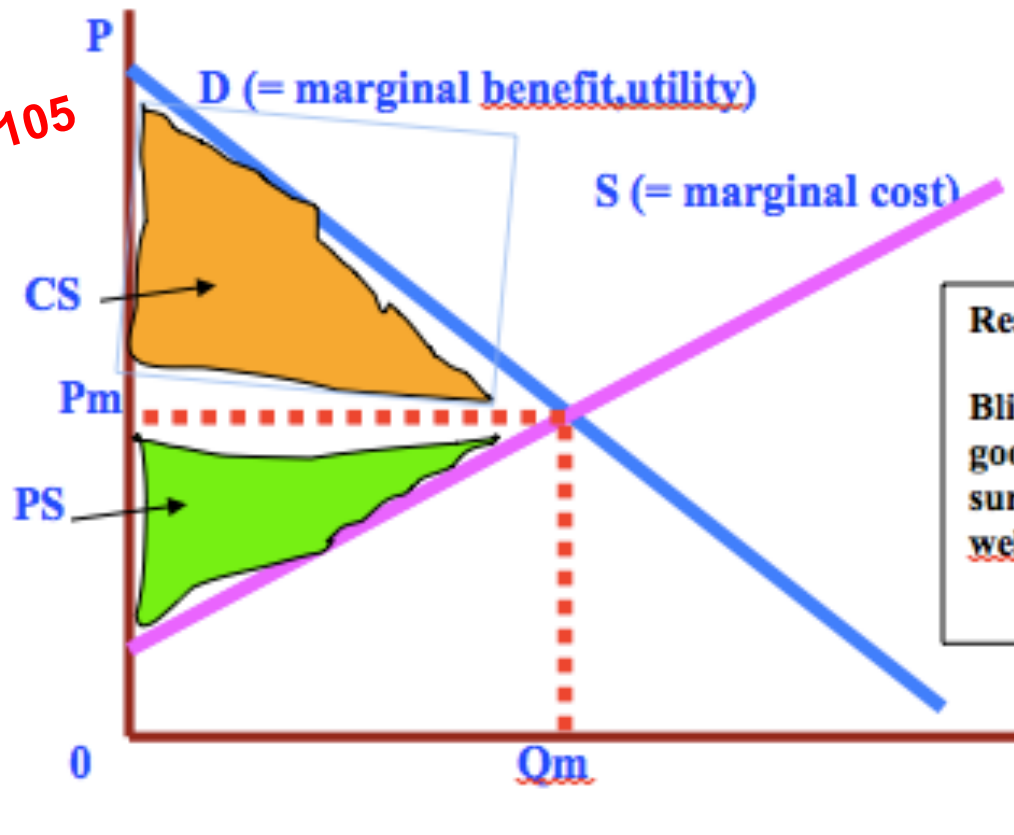
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Big Idea

4

Consumer+producer surplus shows how stakeholders win + lose



Read:

Blink pp 38-39 for a good summary of surplus. See also [webnote 105](#)

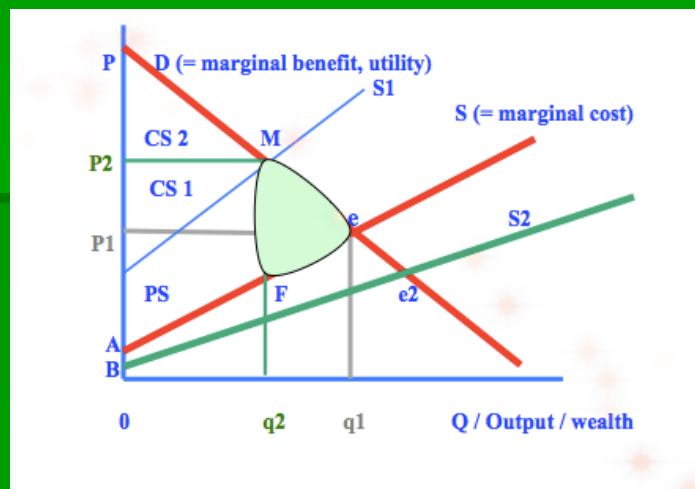
See webnote 104+105

Consumer+producer surplus:

1. Markets bring growth + benefits. **Incentives** for firms and households are increased as surplus increases as markets increase in size
2. Markets through the price mechanism send **signals**. Firms and households interact to agree prices and determine what, how and for whom? Resource allocation is carried out as a result and is seen on the X axis of the diagram.

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See webnote 105 for details.

Section 1.1 Markets

The BIG ideas!

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Big Idea

5

Evaluate market system: be aware that the market system for allocating scarce resources has significant advantages + disadvantages

FOR:

- Efficiency
- 'consumer sovereignty / consumer surplus
- Economic growth

See webnote 108, 109 + 111

(disadvantages see Blink/Oxford book pages 139-146)

Against:

1. 'externalities' (1.4)
2. Public + merit goods (1.4)
3. Monopoly (1.5)
4. Income / wealth distribution
5. Factor immobility (= regional unemployment)₁₀

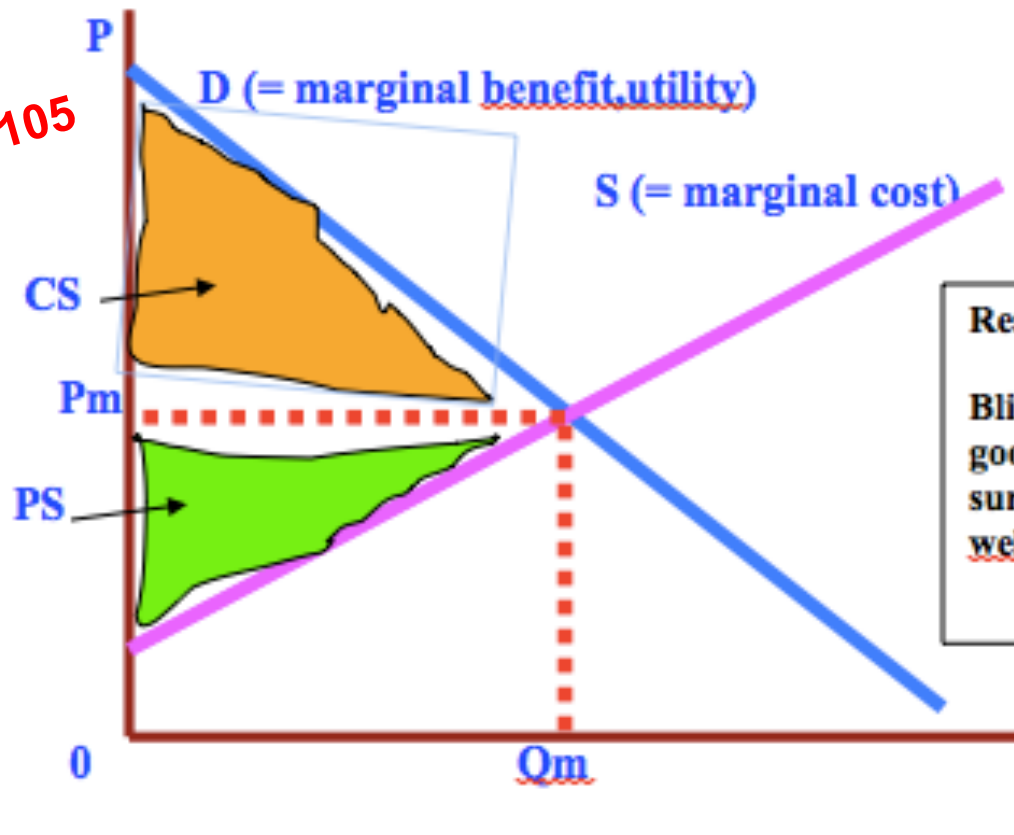
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Big Idea

6

**Equilibrium in a market = allocative efficiency with stakeholders benefitting
($Con S + PS = Com S$)**



Read:
Blink pp 38-39 for a good summary of surplus. See also [webnote 105](#)

See webnote 104+105

Section 1.1 Markets

The **BIG** ideas!

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Exam question 1.1:

Syllabus item 14:

Explain, using diagrams, that price has a signaling function and an incentive function, which result in a reallocation of resources when prices change as a result of a change in demand or supply conditions.



1. (a) Explain the signalling and incentive functions of price in a market economy.

[10 marks].

May 2007 SL paper 1.

See IB answer on Slide 12.

Exam question 1.1:

- 1. (a) Explain the signalling and incentive functions of price in a market economy. [10 marks]
- **Answers may include:**
 - • definition of market economy
 - • description of market forces and how resources are allocated
 - • explanation of the signalling function in relation to producers and consumers, e.g. as consumers increase their demand for a good (shift of demand to the right) the price of the good and profits rise, acting as a “green light” signal to producers to increase their output (movement along the supply curve); as the supply of a commodity becomes more scarce, supply shifts to the left and the rise in price signals to consumers to reduce their demand (movement along the demand curve); these changes in demand and supply bring about changes in resource allocation
 - • explanation of the incentive function in relation to producers: e.g. an increase in demand for a product will raise its price and profitability and provide the incentive for producers to supply more/new firms to enter the market; the higher demand for the product will also lead to an increase in demand for labour to produce the product, causing wages to rise, which will in turn provide an incentive for workers to seek employment in that industry;
 - these changes in demand and supply bring about changes in resource allocation
 - • use of appropriate diagrams e.g. demand and supply
- Candidates may not use the specific terms: signalling and incentive but may explain the functions of price using different terminology and they should be fully rewarded for this.

The **BIG** ideas!

- Big Questions for webnote 99:

Big Questions for 99:

1. Why is the market system the best allocative system?
2. What are the key factors that influence households and firms allocative decisions?
3. Evaluate the market?

The **BIG** ideas!

- HL ONLY: Linear Functions

Section 1.1 Markets

The **BIG** ideas!

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Linear functions

- <http://moodle.isdedu.de/file.php/483/Microeconomics/index.htm>
- http://moodle.isdedu.de/file.php/483/Microeconomics/page_24.htm
- http://moodle.isdedu.de/file.php/483/Microeconomics/page_32.htm

Section 1.1 Markets

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Linear functions

$$Q_s = -20 + 20P$$

$$Q_d = 80 - 5p$$

Where Q_s and Q_d are quantities in thousands of kilos and P is the price per kilo in US\$ answer the following questions:

1. calculate Q_s and Q_d at a price of 3 \$ per kilo

Section 1.1 Markets

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Linear functions

2. Assuming the demand curve is defined as follows: $Q_d = 200 - 2P$

Find the P intercept.

Find the Qd intercept