Advantages of the market system

**Webnote 109**

**Syllabus: 2.1 Price system as an allocative system (price based rationing). What are the advantages of price mechanism?**

**Efficiency:**

Draw a PPF to show how an economy using a market system may have a higher level of efficiency than a command economy. (draw the diagram on this webnote).

C

**PPF**

L

1. **Efficiency. On the demand side the price system improves the allocation of scarce resources. As demand for a good increases (See d1 to d)**

* **the market responds by putting more resources- land, labour and capital- into the production of that good.**

1. **On the supply side the Firm must try to seek the low cost production alternative assuming that there are competitors offering substitute goods.**

* **see p2q2 or a similar alternative This may result in lower average unit costs and therefore more efficiency**



**1. Efficiency**



**2. ‘consumer sovereignty’**

1. **Individual Freedom is improved. This is sometimes called ‘consumer sovereignty’+ represents consumer power in the market. In the market the consumer influences ‘what? ’ is produced. The decision to purchase belongs to the consumer. Producers respond to this power. This concept works well in a competitive market.**

**3. economic growth**

1. **The price system leads to economic growth ie an increase in the output of goods and services. If efficiency is improved by means of increases in productivity for each unit of a factor of production then growth occurs. The key factor here is profit and loss. Resources follow profits. Profits attract competition.**
2. **On the supply side the Firm must try to seek the low cost production alternative assuming that there are competitors offering substitute goods q2 or increase the output at current prices q3**
3. **Profit = TR – TC**
4. **See e1 -e2. Draw change in TR. What do you notice? See also webnote 234.**
5. **In essence the price system attempts to answer the 3 key economic questions:**

**what? how? for whom ?**



Task 1

Research Task option

**Webnote 109**

Group based task:

**Study webnotes: 109 + 111 + 112**

**Task: Evaluate the market system.**

**(Provide real world examples to make your argument.)**

1. **Evaluate: advantages vs disadvantages**
2. **Evaluate: prioritize**
3. **Evaluate: long run vs short run**
4. **Evaluate: prioritize**

**Guidelines for research:**

Present to the class one or more of the following ( based on 3 groups having max 15 minutes)

1. animation/ cartoon that passes a critical comment on the market system
2. video clip (blinkx.com or other news source) highlighting a real world story about the market system
3. news article – economist, business week or other suitable source
4. podcast – radio report or other medium to answer the research question.
5. Powerpoint (maybe containing a combination of the above approaches)

7. Guidelines: you must also do….

* + Information must be presented to the class using the whiteboard
  + A handout must be given to each student summarizing your presentation and allowing the reader to have printed real world examples that will assist them in evaluating the market system. I would like this handout to be maximum 2 pages of A4 photocopied back to back

Task 2: Exam Question Theme: Market is best allocative system/ intervention to regulate the market

Exam Question: SL(and HL) 2005 May paper 1 Q 4

**4. (a) Explain the main characteristics of a market economy.**

**(b) Evaluate the proposition that economic development is best achieved**

**through the market system.**

**Note: before answering this question read webnotes 231 and 232.**

Answer

Reduce textbox to see answer to question 4b

Task 2

Exam

Focus

**Bullet Answer to part (b) Points for discussion might include:**

1. **definition of economic development**
2. **advantages of the market system in terms of enhancing**

**development**

**more efficient resource allocation**

**greater productivity**

**greater consumer choice**

**increased business competitiveness**

**export led economic growth**

**problems of state planning/interventionist policies**

1. **disadvantages of the market system in terms of enhancing**

**development**

**under provision of merit goods**

**over provision of demerit goods**

**positive and negative externalities**

**under provision of public goods**

**income inequality**

**benefits of alternative development strategies**

**inward-orientated strategies *e.g.* import substitution**

**state planning/interventionist policies**.

1. **Decide: advantages < or > disadvantages**

Examiners should be aware that candidates may take a different approach, which if appropriate should be rewarded.

***15 marks / up to 35 minutes to answer***