

Best Uses:

- ⊙ (dis)advantages of market (stakeholders)
- ⊙ welfare gain (market increases in size)
- ⊙ welfare loss (market reduces in size)
- ⊙ price power of firm (producer sovereignty)
- ⊙ consumer power (sovereignty)
- ⊙ Perfect Competition (lower prices+higher output)
- ⊙ Imperfect Competition (higher prices + lower output)

ED 1: consumer+producer surplus

Consumer Surplus + Producer Surplus

Alternative uses of Economics Diagrams : Consumer Surplus + Producer Surplus

Syllabus References :

- 1.2: The free market and the price mechanism can bring about equilibrium at e or e_2 where the community surplus is maximized. They represent the price quantity that maximizes community (CS+PS) surplus. This is why the free market is desirable and provides an effective allocation of resources (with the exceptions offered by market failure).
- 2.2: It can be used to show how consumers win under PC and lose under Monopoly. Under Monopoly $P = P_2$ and under PC $P = P_1$. Under Monopoly conditions the consumer loses the consumer surplus of CS 1. Under PC the area of consumer surplus is CS 1 + CS 2. The consumer and society is better off. Why society? $CS + PS = CS$, (community surplus) This is important as at P_1 community surplus is maximized (CS 2 + CS 1). If price is at P_2 then society loses WL (Welfare loss) in so much as this quantity is not produced and price is higher than P_1 .

Note on diagram:

- $CS_1 + CS_2 =$ benefit to consumer, P_1 or $P_2 <$ ability to pay higher prices exists
- $PS =$ benefit to producer, $P_1 >$ willingness to supply at lower prices exists
- This is why the market is desirable and can allocate resources effectively. Both the consumer and the producer can have a surplus. The issue is how the surplus is shared.

