GCSE Economics: Theme 1.1 Economic Groups and Factors of Production

Exam Criteria

- **Explain** the role of the main economic groups: consumers, producers and the government, including their interdependence
- **Explain** the factors of production: land, labour, capital and enterprise, including how they might be combined

How can the government protect those with less influence in the economy? Why do the economic groups need one another?

What role do Consumers have in the economy?

Buys goods and services for personal use. They are the end user of a good; the decision to buy is at the very end of the production process.

Consumers make choices about their spending by weighing up the satisfaction (benefit) from using the good against the price they would be paying.

Consumers generally act on an individual basis and have little power in the market. They may need protecting by the government through legislation.

What role do the Government have in the economy?

They make and enforce rules within the country they run. Some of these rules will directly affect consumers or producers.

Governments spend money in the economy. Government also transfers money to individual consumers, enabling them to spend. Governments act as buyer of goods and services and as producers.

Governments can affect the economy through their chosen policies (taxation, interest rates). These actions can influence the price, quantity and quality of a product.

What role do Producers have in the economy?

Supply goods and services. They make choices about what and how they produce. They have influence over the quantity, price and quality.

You will look in more detail at producers in Topic 2.6

What does interdependence in economics?

Each economic group responds to the actions off another group.

The decisions that each individual consumer, producer or government take all contribute to the final decisions on the use of the economy's resources.

Why are factors of production offered for use in the economy? How can factors of production be combined for the good of society?

What are Factors of Production? What does CELL stand for?

The resources in an economy that can be used to make goods and services.

They are categorised into: **C**apital **E**nterprise **L**and **L**abour

What is Land as a factor of production?

All natural resources in the economy are classed as land. The reward for offering land for use is rent.

What is Capital as a factor of production?

All human-made aids to production.

All artificial resources that are inputs into production and all infrastructure:

Technology, **I**nfrastructure, **M**achines

TIM

The reward for offering capital for use is interest.

What is Labour as a factor of production?

All human resources that are available in the economy.

Will depend on **s**ize and **a**ge of the population, the **w**orking age in a country and the impact of **m**igration, quality of workforce (level of **e**ducation and **t**raining) and the **h**ealth of the population.

SAWMETH

The reward for offering labour for use is wages.

What is Enterprise as a factor of production?

The organisation of the other factors of production to make goods and services.

Requires an individual (entrepreneur) to:

- Organise production
- Bear the risks of the project

The reward for offering enterprise for use is profit.

How might factors of production be combined?

The world only has limited resources and increasing requirements for them from a growing population. If these resources are used to produce one thing, they can't be combined in another way to produce something else. Advances in technology play a part in how factors of production are combined – use of capital overtakes the use of labour.

You will look in more detail at the combination of factors of production when we look at Specialisation in Topic 2.1

Key Vocab

Word Wall

Consumer – A person or organisation that directly uses a good or service

Interdependence – The state of being dependent upon others

Production – The total output of goods and services produced by a firm or industry in a time period

Government – A political authority that decides how a country in run and manages its operations

Producer – A person, company or country that makes, grows or supplies goods and/or services

Enterprise – The factor of production that takes a risk in organising the other factors of production

Additional Key Terms

Good – A tangible product; one that can been seen or touched

Service – An intangible product; one that cannot be seen or touched

GCSE Economics: Theme 1.2

The Basic Economic Problem

How can we approach the basic economic problem?

What are scarce resources?

When there are fewer resources to make goods and services than are desired. Other useful words to describe scarce resources are finite, limited and insufficient

What are unlimited wants?

The desire for everything a consumer would like whether they have the resources to purchase it or not. There are too many uses for the resources.

What is the basic economic problem?

How to best use the limited resources to satisfy the unlimited wants of consumers.

1. What should be produced?
2. How should it be produced?
3. Whom should it be produced for?

How does the UK approach the basic economic problem?

1. **What goods and services should be produced with available resources?** Most decisions are made based on what consumers are willing and able to buy. The government intervenes in some markets by providing goods directly to consumers (NHS).

2. **How should resources be used most efficiently to produce these goods?** Producers will mostly determine how goods are to be produced as they look for lowest costs. *You will look in more detail at producers in Topic 2.6.* The government sometimes intervenes with legislation on production

3. **How should the goods be allocated among the population?** In most instances goods and services are allocated to consumers who can afford to buy them. The government sometimes intervenes where goods and services are deemed particularly important to the economy e.g. free education to all under 19. *You will look in more detail at limitations of markets in Topic 3.8*

What is the difference between needs and wants?

Wants are unlimited and include anything a consumer would like whether they can purchase it or not.

What is meant by opportunity cost?

Something that is given up when making a decision on the use of scarce resources.

The value of the next best alternative when making a decision.

Exam Criteria

- **Explain** what is meant by scarce resources and unlimited wants
- **Explain** the economic problem,
- **Explain** what is meant by 'what goods and services should be allocated'
- **Explain** what is meant by 'for whom goods and services should be allocated'
- **Explain** what is meant by 'how goods and services should be produced"
- **Explain** what is meant by opportunity cost
- **Explain** the impact of economic choice on economic sustainability
- **Explain** the impact of economic choices on social sustainability
- **Explain** the impact of economic activity on environmental sustainability
- **Evaluate** the costs and benefits of economic choices

How do economic choices affect us all?

What is economic sustainability?

Ensures the most responsible use of scare resources so that a firm or economy can continue to *develop and grow*.

Consideration will be given to economic factors such as **c**osts involved in production, **p**rice consumer pays, impact on **u**nemployment and impact on government **s**pending and **t**ax revenue.

CPUST

You will look in more detail at Unemployment in Topic 3.2 and at Government Spending and Tax Revenue in Topic 3.5

What is social sustainability?

Considers how economic activity (*development or growth*) affects quality of life and well-being.

It requires that any growth or development meet the basic needs of all, now and into the future, encourages fairness and a better society. It may also consider who benefits within society and who pays.

What is environmental sustainability?

Considers how economic activity (*development or growth*) impacts the environment now and in to the future.

Focuses on the impact on renewable and non-renewable resources, pollution creation and climate change, and the availability of future resources.

It is important for all countries and their governments to consider the impact on the environment

Key Vocab

Word Wall

Sustainability – The ability to be maintained at a given rate

Economic – The best use of resources

Environmental – Relating to impact of human activity on the natural world

Social – Relating to society and the people within it

Scarce – In short supply

Desired – Wished for or intended

Additional Key Terms

Scarce resources – When there is an insufficient amount of something to satisfy all wants.

Economic problem – How to best use the limited resources to satisfy the unlimited wants of people.

Economic choice – An option for the use of selected scarce resources.

GCSE Economics: Theme 2.1 The Role of Markets

How has the UK economy changed in the last 15 years?

What is a Market?

Where buyers and sellers come together to buy and sell goods and services. It can be a physical or virtual environment.

A market economy relies on the forces of supply and demand to determine the allocation of scarce resources *(see topic 1.2)* as well as government intervention.

You will look in more detail at the forces of demand and supply in chapters 2.2, 2.3 and 2.4

What is a product market?

A market where finished goods or services are offered to consumers, businesses and the public sector. They are not concerned with the buying and selling of raw materials.

Effective product markets ensure consumers benefit from lower prices and increased choice by increasing competition. They also encourage firms to innovate. Price is determined by the interaction of supply and demand.

You will look in more detail at Demand and Supply in Topics 2.2 and 2.3 and at Competition in Topic 2.5.

What is a factor market?

The market where the services of the factors of production (CELL) are bought and sold. Price for each factor is based on supply and demand and is a derived demand.

You will look in more detail at Demand and Supply in Topics 2.2 and 2.3 and at Derived Demand in Topic 2.7.

What is the primary sector?

The direct use of natural resources. The extraction of basic goods from the land and sea.

Products will either be consumed directly or used as raw materials in the production process.

What is the secondary sector?

All economic activity concerned with either manufacturing or construction.

Manufacturing includes both *direct* use (using raw materials to make a finished product) and indirect use (using raw materials to make a component of something else).

Construction is the process of constructing a building or infrastructure.

What is the tertiary sector?

All economic activity where a service is provided.

Services can be provided firm to firm, individuals or the government.

The only sector concerned with dealing with people directly.

Most economies have seen a shift to the tertiary sector over the past 100 years or so.

Exam Criteria

- **Explain** what is meant by a market
- **Explain** the difference between primary, secondary and tertiary markets
- **Explain** the difference between factor and product markets
- **Understand** the interdependence between factor and product markets
- **Evaluate** the costs and benefits of specialisation and exchange for producers
- **Evaluate** the costs and benefits of specialisation and exchange for workers
- **Evaluate** the costs and benefits of specialisation and exchange for regions
- **Evaluate** the costs and benefits of specialisation and exchange for countries

Does specialisation and exchange create winners and losers? (a)

What is specialisation?

When individuals, firms, regions or counties concentrate on producing the goods and services they have an advantage in making it more efficient and often increasing output. This can apply to all factors of production *(see 1.1).*

This often means they have to give up producing other goods and services.

What is exchange?

Giving up something an individual has in return for something the need but do not possess. All economic behaviour involves the exchange of one scarce resource for another; today this is usually money.

Key Vocab

Word Wall

Market – A way of bringing together buyers and sellers to buy and sell goods and services

Specialisation – The process of concentrating on producing those things you are best at producing

Exchange – The giving up of something that you have in return for something that you desire but do not have

Sector – An area of the economy in which businesses share the same of related activities

Innovate – To introduce something new or make changes to something established

Key Terms

Division of Labour – Where workers specialise in, or concentrate on, one area of the production process.

Secondary Sector – All activities concerned with manufacturing or construction

Tertiary Sector – All activities in the economy that involve the idea of a service

Factor Market – Markets where the services of factors of production are bought and sold

Product Market – Markets where goods and services are offered to consumers, businesses and the public sector

Does specialisation and Exchange create winners and losers? (b)

How does specialisation impact Producers?

World output has increased through firms specialising.

Producers exchange income from selling products for the components they need to produce them.

Benefits	Costs
Higher output	Diseconomies of scale (eventually)
Higher productivity	Dependency
Higher quality	Failure of exchange
Bigger market	Movement of workers
Economies of Scale	
Time saving	

You will look in more detail at Productivity, Economies of Scale and Diseconomies of Scale in Topic 2.6.

How does specialisation impact Regions?

Originally, specialisation by region would depend on local natural resources.

Today, regional specialities are often based on services.

Regions will produce things in addition to their known speciality but the speciality will make an important contribution to the local economy.

Benefits	Costs
Efficient use of resources	Risk of fall in demand
Creates jobs for residents	Resource exhaustion
Infrastructure development	Loss of adventure

You will look in more detail at Demand in Topic 2.2, and the impact of Infrastructure on Economies of Scale in Topic 2.6.

Study Tip - Evaluation

Evaluation is based on analysis.

Make sure you have used economic ideas, concepts, diagrams etc. in the body of your answer **before** evaluating.

For evidence evaluating is taking place, examiners will look for words such as:

- Because
- However
- More important
- To a greater extent

Must take place in context of the question.

Study Tip – Use of Date

Examiners like to see up to date figures and information in answers.

How does specialisation impact Workers?

Unless totally self-sufficient all workers specialise. They exchange their labour for money in order to be able to buy goods and services.

Benefits	Costs
Increased skill	Boredom
Natural strength	Deskilling
Increased job satisfaction	Unemployment
Increased standard of living	

You will look in more detail at how increased skills can lead to higher wages in Topic 2.7, Increased Standard of Living in Topic 3.1 and Unemployment in Topic 3.2

How does specialisation impact Countries?

Originally, countries would specialise in producing what they get the greatest advantage from.

Today, many countries now specialise in particular skills and knowledge. Countries specialising leads to international trade.

Benefits	Costs
Economies of scale	Unemployment
More jobs	Over-dependence
International trade	Over-exploitation
Improved standard of living	Negative externalities
Government revenue	

You will look in more detail at Economies of Scale in Topic 2.6, Increased Standard of Living in Topic 3.1, Unemployment in Topic 3.2, Negative Externalities in Topic 3.8, International Trade in Topic 4.1 and the impact of over-exploitation of natural resources on Sustainable Development in Chapter 4.4.

GCSE Economics: Theme 2.2 Demand

What do economists mean by demand?

What is Demand?

The quantity of a good or service that consumers are willing and able to buy at a given price in a given time period.

What is Derived Demand?

Demand that comes about because of the demand for another product.

What is a normal good?

A good where demand increases as income increases.

What is the law of demand?

For most goods and services the quantity demanded varies ***inversely*** with price.

What is the relationship between price and demand?

As prices increase, demand falls. As prices fall, demand increases.

What is individual demand?

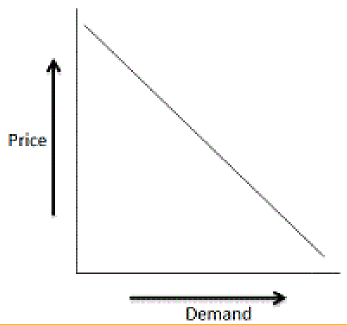
The demand for goods and services by an individual consumer. This shows they amount they would be prepared to buy at difference prices. It ***does not*** tell us how many she will buy.

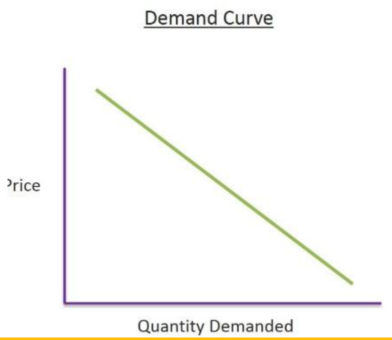
What is a market demand?

The total demand for a good or service. It can be found by adding the individual demands together.

How do you draw demand?

The demand curve is plotted sloping downwards between ***Price*** on the vertical axis and ***Quantity Demanded*** on the horizontal axis.

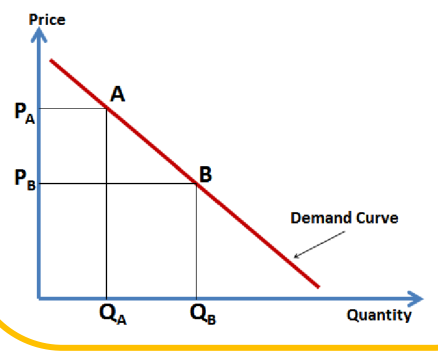




What is the difference between a movement along and a shift in Demand? (a)

What causes a movement along the curve/How do you draw a movement?

A change in price is the only thing that will cause a movement along the curve.



What are the consequences of movements along the curve?

A movement along the demand curve will lead to price and quantity moving in the opposite direction.

Movement	Effect
Increase in quantity demanded due to a fall in price causing a movement down the curve	The price falls but the quantity increases ***(an expansion in demand)***
Decrease in quantity demanded due to an increase in price causing a movement up the curve	The price increases but the quantity falls ***(a contraction of demand)***

Exam Criteria

- **Explain** what is meant by demand
- **Draw and Explain** individual demand curves
- **Draw and Explain** market demand curves
- **Analyse** the causes and consequences of shifts in the demand curve for consumers and producers
- **Analyse** the causes and consequences of movements along the demand curve for consumers and producers
- **Draw** shifts in the demand curve
- **Draw** movements along the demand curve
- **Explain** price elasticity of demand
- **Draw** demand curves of different elasticities
- **Evaluate** the importance of price elasticity of demand for consumer

Key Vocab

Word Wall

Substitute – A good or service that can be used in place of another

Compliment – A good or service that can be used in place of another

Subsidy – An amount of money the government gives directly to firms to encourage production and consumption

Derive – To obtain something from

Elasticity – the degree to which a demand or supply is sensitive to changes in price or income.

Elastic – When the percentage change in quantity demanded is greater than the percentage change in price

Inelastic – When the percentage change in quantity demanded is less than the percentage change in price

Inverse - something that is the opposite or reverse of something else

Key Terms

Demand – The willingness and ability to purchase a good or service at the given price in a given time period

Tax – A compulsory payment to the government

Law of Demand – For most products the quantity demanded varies inversely with its price

Individual Demand – The demand for a good or service by an individual consumer

Market Demand – The total demand for a good or service

Movement along the curve – When the price changes, leading to a movement up or down the existing curve

Shift of the curve – A complete movement of the existing demand curve either outward or inward

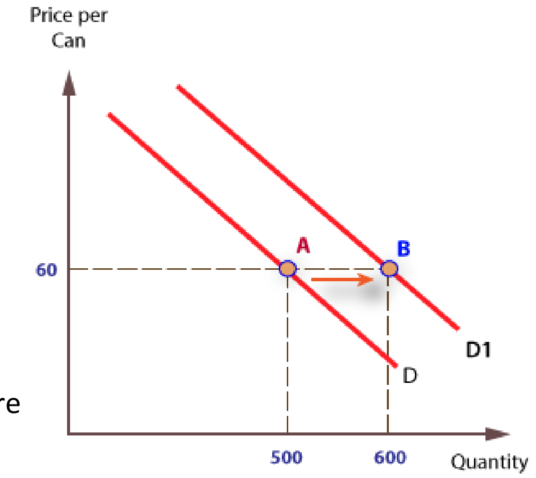
What is the difference between a movement and a shift in Demand? (b)

What causes a shift in demand /How do you draw a shift?

This is when the whole demand curve moves to the right or left. This occurs when the quantity of a good demanded changes even when price stays the same.

Factors affecting demand:

- Income
- Population
- Marketing
- Tastes/Fashion
- Substitutes/Compliments
- Government policies
- Price expectations for future



What are the consequences of shifts in demand?

In nearly all cases a shift of the demand curve will lead to price and quantity moving in the same direction.

Movement	Effect
Increase in demand due to a rightward shift of the demand curve	Both the price and quantity demanded of the product increases
Decrease in demand due to a leftward shift of the demand curve	Both the price and quantity demanded of the product decreases

Study Tips

Remember to label a diagram fully. If you leave off price and quantity then the person marking the paper has no idea wha is being measured.

Make sure you are absolutely clear as to the difference between a movement of a demand curve, a shift in demand and a change in quantity demanded.

Always remember to include the minus sign for PED values; a prices increase, QD will decrease.

Study Tip – Analysis

Analyse means the ability to present logical chains of reasoning based on knowledge and application. Appropriate use of economic terms and explanation of diagrams are likely to indicate that analysis is taking place. Analysis means using economic ideas, terms, concepts and diagrams to help explain your answer.

Why is Price Elasticity of Demand important?

What is elasticity of demand?

A measure of the responsiveness of quantity demanded to a change in the price of the product.

What does inelastic demand mean?

The price change will lead to a smaller change in demand.

The PED value will be between 0 and -1.

What does elastic demand mean?

The price change will lead to a larger change in demand.

The PED value will be between -1 and infinity.

How does PED affect consumers?

Governments could impose taxes on goods with inelastic demand.

Some customers have forced inelastic demand have to pay higher prices.

How does PED affect producers?

Knowledge of PED can be used to impact revenue by changing pricing strategies.

How do you calculate PED?

$$\frac{\text{\% Change in Quantity Demanded}}{\text{\% Change in Price}}$$

What do the PED values mean?

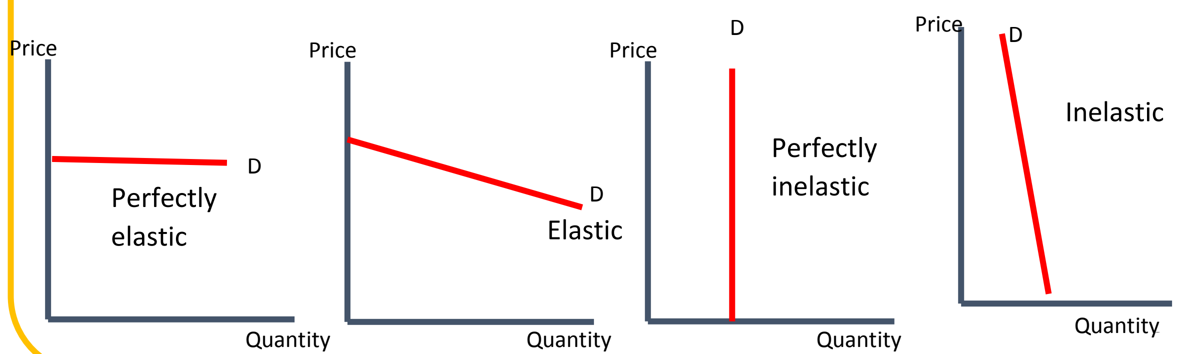
Value	Name	How responsive?	Impact on revenue	Slope of curve
0	Perfectly inelastic	No change in demand	Higher prices - higher revenue Lower prices – lower revenue	
0-1	Inelastic	Change in demand less than change in price	Increase prices - increase revenue	
1	Unitary	Equal changes	No change	
1-∞	Elastic	Change in demand higher than change in price	Increase prices – decrease revenue. Lower prices – increase revenue	
∞	Perfectly elastic	Any change in price kills demand	Any change in price, revenue zero	

What does unitary demand mean?

The price change will lead to the exact change in demand.

The PED value is 1.

What do the PED curves look like?



GCSE Economics: Theme 2.3 Supply

What do economists mean by Supply?

What is Supply?

The quantity of a good or service that producers are willing and able to supply at a given price in a given time period.

What is the relationship between price and supply?

As prices increase, supply increases. As prices fall, supply falls.

What is the law of supply?

For most goods and services the quantity demanded varies ***directly*** with price.

What is individual supply?

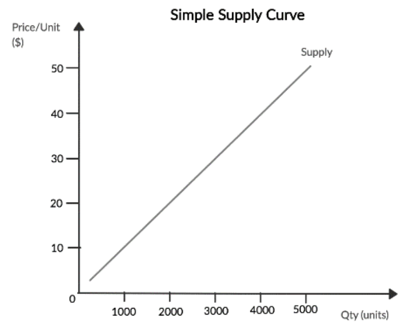
The supply of goods and services by an individual producer. This shows the amount they would be prepared to sell at difference prices. It ***does not*** tell us how many they will sell.

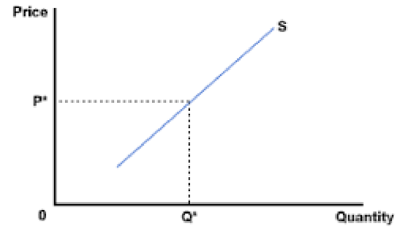
What is a market supply?

The total supply of a good or service. It can be found by adding the individual producers supply together.

How do you draw supply?

The supply curve is plotted sloping upwards between ***Price*** on the vertical axis and ***Quantity*** on the horizontal axis.

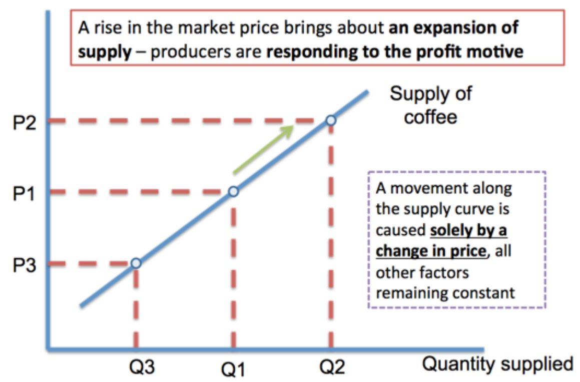




What is the difference between a movement along and a shift in Supply? (a)

What causes a movement along the curve/How do you draw a movement?

A change in price is the only thing that will cause a movement along the curve.



What are the consequences of movements along the curve?

A movement along the demand curve will lead to price and quantity moving in the opposite direction. Price increases may lead to increased profits or new firms entering the market, causing a shift.

Movement	Effect
Increase in quantity supplied due to a rise in price causing a movement up the curve	Both price and quantity supplied rise ***(an expansion of demand)***
Decrease in quantity supplied due to an fall in price causing a movement down the curve	Both price and quantity supplied fall ***(an expansion of demand)***

Exam Criteria

- **Explain** what is meant by supply
- **Draw and Explain** individual supply curves
- **Draw and Explain** market supply curves
- **Analyse** the causes and consequences of shifts in the supply curve for consumers and producers
- **Analyse** the causes and consequences of movements along the supply curve for consumers and producers
- **Draw** shifts in the supply curve
- **Draw** movements along the supply curve
- **Explain** price elasticity of supply
- **Draw** supply curves of different elasticities
- **Evaluate** the importance of price elasticity of supply for consumer

Key Vocab

Word Wall

Regulation – the action of controlling by means of rules. A rule or directive set by authority.

Subsidy – An amount of money the government gives directly to firms to encourage production and consumption

Elasticity – the degree to which a supply or supply is sensitive to changes in price or income.

Elastic – When the percentage change in quantity supplied is greater than the percentage change in price

Inelastic – When the percentage change in quantity supplied is less than the percentage change in price

Key Terms

Supply – The willingness and ability to purchase a good or service at the given price in a given time period

Tax – A compulsory payment to the government

Law of Supply – For most products the quantity supplied varies directly with its price

Individual Supply – The supply for a good or service by an individual producer

Market Supply – The total supply for a good or service

Movement along the curve – When the price changes, leading to a movement up or down the existing curve

Shift of the curve – A complete movement of the existing supply curve either outward or inward

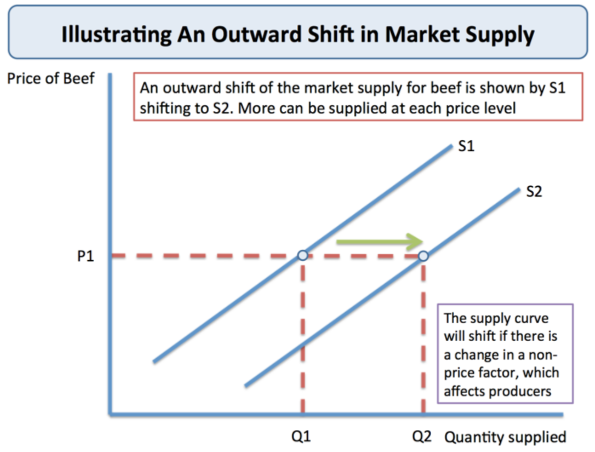
What is the difference between a movement and a shift in Supply? (b)

What causes a shift in supply /How do you draw a shift?

This is when the whole demand curve moves to the right or left. This occurs when the quantity of a good demanded changes even when price stays the same.

Factors affecting demand:

- Income
- Population
- Marketing
- Tastes/Fashion
- Substitutes/Compliments
- Government policies
- Price expectations for future



What are the consequences of shifts in supply?

In nearly all cases a shift of the supply curve will lead to price and quantity moving in opposite directions. Other consequences are:

- Economies of scale (*chapter 2.6*)
- Efficiency (*chapter 2.6*)
- Sales
- Exports (*chapter 4.1*)
- Monopoly (*chapter 2.5*)

Movement	Effect
Increase in supply due to a rightward shift of the supply curve	Price falls and the quantity supplied increased
Decrease in supply due to a leftward shift of the supply curve	Both the price and quantity demanded of the product decreases

Study Tips

Remember to label a diagram fully. If you leave off price and quantity then the person marking the paper has no idea what is being measured.

Make sure you are absolutely clear as to the difference between a movement of a supply curve, a shift in supply and a change in quantity supplied.

Supply can also refer to the supply of labour (*chapter 2.7*) and the supply of money (*chapters 2.8 and 3.6*).

Why is Price Elasticity of Supply important?

What is elasticity of supply?

A measure of the responsiveness of quantity supplied to a change in the price of the product.

What does inelastic supply mean?

The price change will lead to a smaller change in supply.

The PES value will be between 0 and -1.

What does elastic supply mean?

The price change will lead to a larger change in supply.

The PES value will be between -1 and infinity.

How does PED affect producers?

In most cases an elastic PES is better. Elasticity can be increased by:

- Adopting the latest technology
- Creating spare capacity
- Improving storage methods
- Keeping large amounts of stock
- Training employees in more than one job

How do you calculate PES?

$$\frac{\text{\% Change in Quantity Supplied}}{\text{\% Change in Price}}$$

What do the PED values mean?

Value	Name	How responsive?	Slope of curve
0	Perfectly inelastic	No change in supply	
0-1	Inelastic	Change in supply less than change in price	
1	Unitary	Equal changes	
1-∞	Elastic	Change in supply higher than change in price	
∞	Perfectly elastic	Any change in price kills supply	

How does PES affect consumers?

If supply is inelastic it might make it difficult to buy more of a product without paying more.

If supply is fixed (popular concerts) the ability to pay may not guarantee the product.

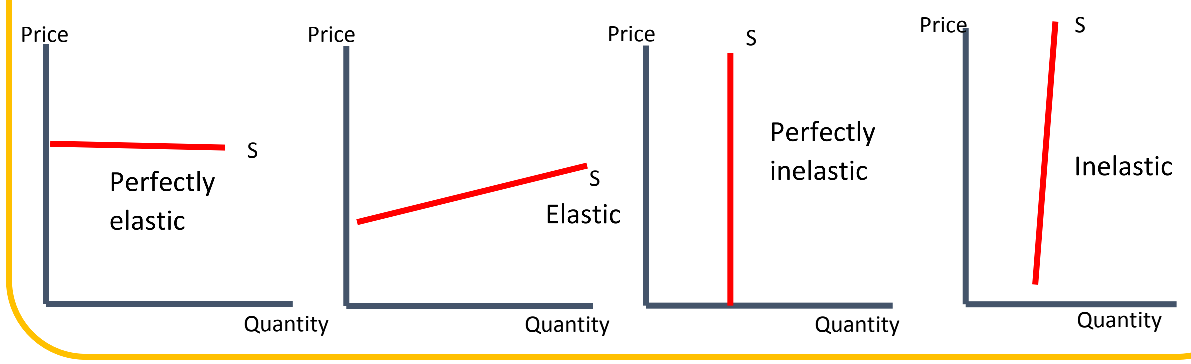
PES is elastic it is easier to obtain the product but less flexibility in negotiating price.

What does unitary supply mean?

The price change will lead to the exact change in supply.

The PES value is 1.

What do the PES curves look like?



GCSE Economics: Theme 2.4 Price

How does price determine an efficient distribution of scarce resources?

What does price mean?

The sum of money you have to pay for a good or service. It is determined by the interaction of supply and demand.

Is price a reflection of worth?

Price is used to indicate worth but is not an accurate measure of worth in all cases. Some people may place more value on something depending on their circumstances.

What three functions does price fulfil?

- Signalling
- Transmission of preferences
- Rationing

What is meant by signalling?

Prices change to signal where resources are needed.

Prices rise and fall to reflect scarcities and surpluses.

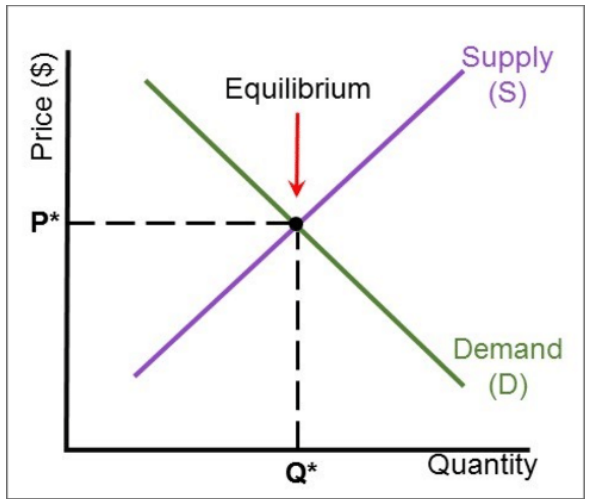
Price rises indicate more resources are needed (producers should enter the market). Price falls indicate less resources are needed.

How do we find equilibrium in markets?

What is meant by equilibrium price and quantity?

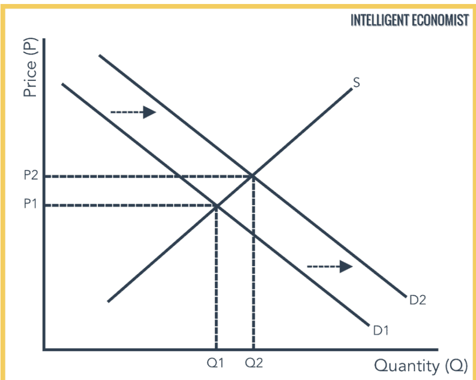
Where the quantity supplied exactly matches the quantity demanded.

We assume markets will always move towards their equilibrium. This is efficient because there is neither an excess of supply nor a shortage.



How do we draw the interaction of supply and demand?

1. Draw axes and label.
2. Draw a demand curve and label D
3. Draw a supply curve and label S
4. Label initial equilibrium (P and Q)
5. Ask whether you would expect price to rise or fall and what would happen to quantity.
6. Decide whether it is a change in demand or supply.
7. Decide whether it is an increase or decrease.
8. Draw and label the new curve.
9. Label the new equilibrium.
10. Check the finished diagram shows what you expect



How do we analyse the interaction of supply and demand?

Make use of phrases such as:

- This means that
- The effect of this is
- This has an effect on
- This can cause
- As a result

If using a diagram, make sure it is clearly referred to in the text by using letters such as P to P1 or D to D1.

Exam Criteria

- **Explain** whether price is a reflection of worth
- **Explain** the role of markets in determining an efficient distribution of resources
- **Explain** what is meant by equilibrium price and quantity
- **Draw** and **analyse** the interaction of demand and supply
- **Explain** the role of markets in the determination of price
- **Explain** the role of markets in the allocation of resources
- **Analyse** how the market forces of demand and supply affect equilibrium price and quantity

What is meant by the transmission of preferences?

Through their choices, consumers send information to producers about the changing nature of needs and wants.

Higher prices act as an incentive to raise output because the supplier stands to make a better profit.

Producers can also send signals to their resource supplier through their choices.

When economy is not doing well, some producers may choose to withdraw.

What is meant by rationing?

When resources are scarce, prices rise so that only those willing and able to pay the higher price are allocated the resource.

Key Vocab

Word Wall

Price – The sum of money you have to pay for a good or service. It is determined by the interaction of supply and demand.

Worth – How much you value something.

Efficiency – The optimal production and distribution of scarce resources.

Optimal – Best or most favourable.

Equilibrium – A state in which opposing forces (supply and demand) are balanced.

Key Terms

Market Forces – Factors that determine price levels and the availability of goods and services in an economy without government intervention

Allocation of Resources – How scarce resources are distributed among producers and how scarce goods and services are allocated among consumers.

Determination of Price – The interaction of free market forces supply and demand to establish the general level of price for a good or service.

Consumer Sovereignty – The power of consumers to influence what is produced.

How do market forces affect equilibrium?

What do we mean by market forces?

Forces that determine price level and availability of resources without government intervention. Supply and Demand.

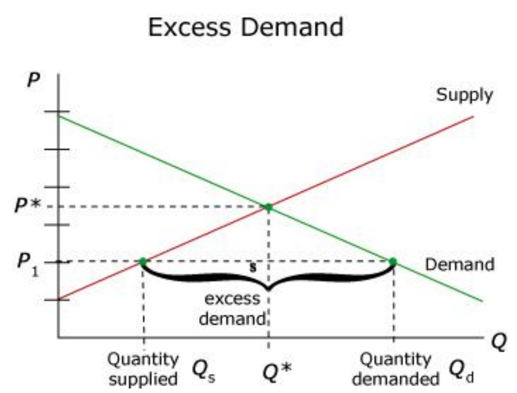
How do markets determine price?

Markets bring buyers and sellers together.

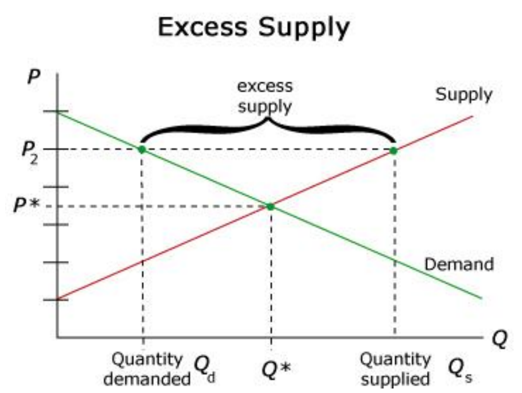
Supply and demand will interact to set the general price level for a good or service.

Market forces push prices up if there is an increase in demand or a fall in supply (excess demand) and pushes them down if demand falls or supply increases (excess supply).

Remember markets will move towards their equilibrium.



P* is equilibrium, if the low price of P1 is set by producers, more consumers will be willing and able to purchase the product (demand more) than suppliers are willing to supply at that level. The increased demand will force prices back up to the market clearing equilibrium price P*.



P* is equilibrium, if the high price of P2 is set by producers, consumers will not be willing and able to purchase the product (demand less) than suppliers are willing to supply at that level. The surplus supply will force prices down to the market equilibrium P*

What role do markets have in allocating resources?

Prices distribute scarce resources among producers and determine how the resulting good and services are allocated to consumers.

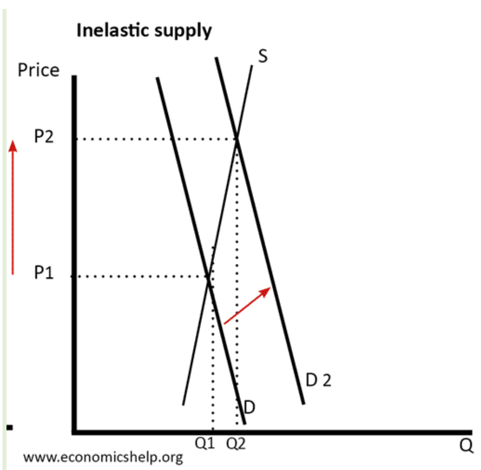
- Scarce resources are rationed
- Incentives (increased profit) are offered to producers to produce more
- Signals are given to both producers and consumers and to the owners of factors of production (signals can be seen working in case of excel supply/demand)
- Consumers can influence resource allocation through their economic choices.
- If consumers are prepared to pay more, producers will move scarce resources to the production of that good.
- This is known as consumer sovereignty

How do market forces (supply and demand) affect equilibrium price and quantity?

Market forces push prices up if there either demand rises or supply falls. Equally they will force prices down if demand falls or supply increases.

Adam Smith (founding father of modern economics) calls this ***the invisible hand***. This is where supply and/or demand change to achieve equilibrium.

An example, increased demand for land for business use:



Consumer demand has resulted in an increased demand for land from D to D2 to build factories, offices, retail outlets etc.

The supply of land is relatively inelastic.

This results in large price increases from P1 to P2 while there is only a small increase in quantity of land supplied from Q1 to Q2.

This results in a new equilibrium of P2Q2 where D2=S

Study Tips

Do not confuse price and cost. Price is the amount it takes to buy a good or service. Cost is how much money it takes to provide the product.

Having drawn a supply and demand diagram, perform a final check: have I labelled the axes and all the lines? Does demand slope downwards and supply upwards? Is the result what I expected? If not then recheck before writing your answer.

Remember to think about elasticity of the product you are discussing; use the correct shaped curve in your diagrams.

If you are answering a question about supply and demand, always try to draw an appropriate diagram and then explain it. The explanation is vital, as a diagram on its own is not analysis. The two combine to provide analysis.

Remember that price and quantity move in the same direction when there is a change in demand but in opposite directions when there is a change in supply.

GCSE Economics: Theme 2.5 Competition

How does competition affect economic activity?

What is meant by competition?

A large number of producers are trying to sell similar goods/services to a consumer.

A large number of producers compete with one another to satisfy the needs of consumers.

No single producer or groups of producers can decide how the market operates.

Consumers cannot influence the price or quality in the market.

What is price competition?

Most obvious form of competition – firms lowers their prices to try and gain customers and market share. Any firm that cannot compete will lose customers and potentially going out of business.

Firms cannot sell at less than cost price for any length of time as this would also cause them to go out of business.

Most likely where there are a number of larger firms.

Exam Criteria

- **Explain** competition between producers in a market economy
- **Explain** the reasons why producers compete
- **Analyse** how competition affects price
- **Evaluate** the economic impact of competition on producers
- **Evaluate** the economic impact of competition on consumers
- **Explain** what is meant by monopoly
- **Explain** what is meant by oligopoly
- **Explain** how monopoly and oligopoly differ from competitive markets

What is non-price competition?

- Offering a specialised product or service
- Better/more personalised customer service
- Convenience
- Quality of the product
- Marketing

Serve to create brand loyalty.

How does competition impact producers?

Forces an improvement in efficiency, including looking for ways to reduce costs. This has been the driving force behind technical innovation and the application of computerisation to technology.

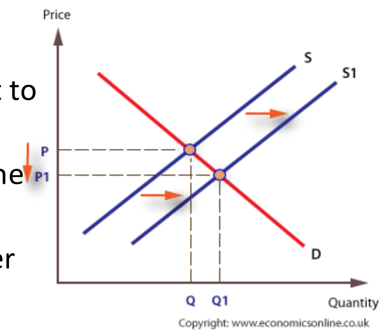
Increased innovation and computerisation will lead to increased productivity in all factors of production *(topic 1.1 and 1.6)* a growth in the economy *(topic 3.1)* and an increase in demand and supply. This leads to greater profits for more efficient producers.

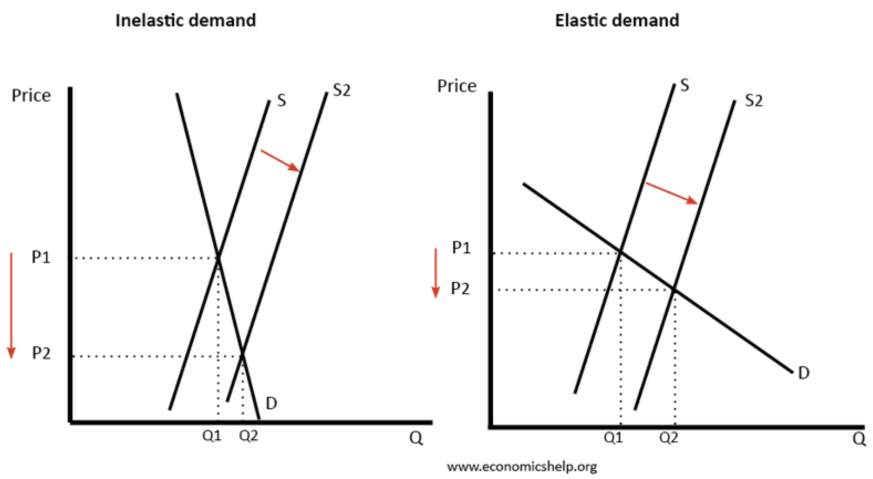
Producers who innovate will stay ahead of competition and attract more consumer demand which will attract more investors (topic 2.8)

Those slow to respond to innovation may go out of business or be forced out of markets. There could be an impact on demand for labour *(topic 2.7)* as machines take over jobs.

How does competition affect price/How is the effect on price shown on a diagram?

It has the potential to drive prices down so that firms produce at the point where total revenue = total costs. Increased competition has caused the supply curve to shift to the right to S1. Prices will fall to P1 and quantity sold will increase to Q1. How much prices will fall will depend on the PED; inelastic PED will result in larger price falls for small quantity increased whereas elastic PED will result in smaller price drops and large increases in quantity.





It has the potential to drive costs (and prices) up. Marketing costs are increased and producers will try to pass these on to their customers. Inventions and innovations cost producers in time and research and development in order to be in front of their competitors. If they are the first to have a product they can charge higher prices.

Why do producers compete?

- To enter a market
- To survive in a market
- To make a profit

You will look at profit more in Topic 2.6

How does competition impact consumers?

Positive - Lower prices, higher quality, increased innovation will lead to more choice. Goods highly priced or poor quality will be forced out of market.

Negative – Producers may introduce harmful goods into production process, consumption may cause negative effects. Consumers may be persuaded to buy goods they do not need.

You will look at negative externalities in more detail in Topic 3.8

Key Vocab

Word Wall

Competition – Where different firms are trying to sell a similar product to a consumer.

Monopoly – A solo producer or seller of a good or service.

Oligopoly – Where a small number of firms control the large majority of the market share.

Homogenous – All the same; alike.

Collusion – an agreement among firms or individuals to divide a market, set prices, limit production or limit opportunities.

Key Terms

Market Share – the portion of a market controlled by a particular company or product.

How do different market structures do things differently?

What is meant by monopoly?

A solo producer or seller of a good or service. This could be in a country or a region.

Characterised by lack of competition.

Legally a producer has to have 25% market share.

They exist because there are no barriers to entry:

- Legal barriers
- Greater efficiency/economies of scale
- Location
- Copyright and patents

What is meant by oligopoly?

A small number of firms control a large majority of the market share. Oligopoly exists if the 5 largest firms control 50% of the market share.

No limit on number of firms but must be low enough to ensure that the actions of one have a significant effect and influence over others.

There will be barriers to entry but not significant enough to stop firms entering the market and increasing competition.

Often try to control the market through collusion. This is illegal in the UK and fines can be issued/the action stopped.

How do oligopoly and monopoly differ from competitive markets?

Firms involved in monopoly and oligopoly are usually much larger. If firms do grow in competitive markets they are moving towards oligopoly.

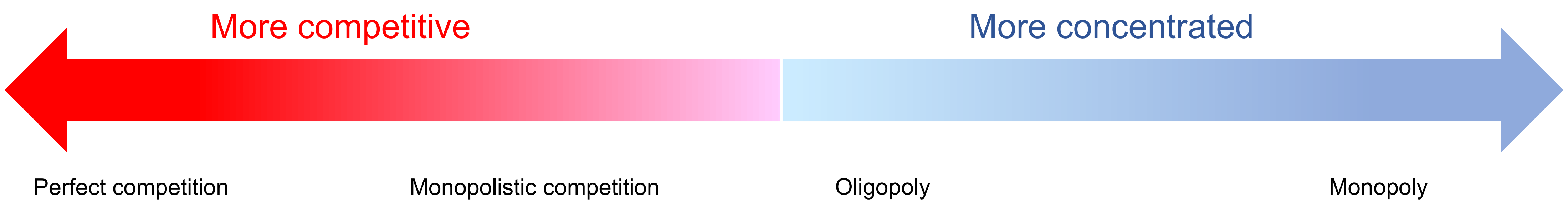
Higher prices are often assumed as there is no need for a monopoly to be efficient. But, firms tend to be much larger and are able to take advantage of economies of scale to lower costs and are able to charge lower prices.

Study Tips

Make sure that you remember that competition takes many forms, it is not just about price.

Remember that when writing about the economic impact of competition on producers and consumers there will be both positive and negative points.

In addition, the emphasis must be on economic impact. For example, high fat cheap food may lead to poor health. But what is the economic impact of this?



Difference	Competitive markets	Oligopoly	Monopoly
Size	Normally relatively small	Can be very large but may also have smaller firms	Usually very large
Number of firms	Many	A few	1
Control of prices	The price is set by the market forces of supply and demand	Can influence the price but is restrained by the reactions of rivals. May try to collude	Is able to set the price but cannot then control the quantity
Level of price and output	Price and quantity are both set by market forces. In theory the prices will be low and quantity greater	Both price and quantity will depend on how strong the competition is and the ability to collude	In theory can charge a higher price and produce a smaller quantity
Efficiency	Competitive markets normally lead to economic efficiency	Usually seen as not being economically efficient	In theory, monopolies are seen as not being efficient, but by achieving larger economies of scale they can be efficient

GCSE Economics: Theme 2.6 Production

Who are the producers in the economy?

What is the role of the producer?

A producer makes and supplies goods and services by combining factors of production. They can be any size from individuals to large multinational corporations.

Producers are responsible for the supply element of supply and demand and help to influence price. They often aim to make a profit.

They are important because the employ people and pay wages. Employment means goods and services are being produced and paying workers enables them to buy the goods and services.

What three groups can be producers?

- Individuals
- Firms
- Governments

How can individuals be producers?

Producers of non-market goods such as cooking, cleaning and child-minding.

Self-employed people work for themselves to provide goods and services to the market.

How can firms be producers?

Can be small local firms or can sell nationwide and/or abroad.

Smaller firms are usually involved in competition where larger firms may be oligopolies or monopolies. Larger firms have power over markets by limiting the amount they supply or by lowering prices to drive out competition (*see topic 2.5*).

How can governments be producers?

Governments produce a range of services that the private sector wouldn't produce themselves because the public wouldn't pay for them directly (police/defence). Sometimes the private sector can provide some of these services; private options are often too expensive for some people.

The government can also produce goods although many of these industries have now been privatised.

Why is productivity important?

What is production?

The total amount of goods and services produced by a firm or industry in a given amount of time. It requires combining factors of production (*see topic 1.1*).

What is an increase in production likely to bring about?

- An increase in employment (unless greater productivity reduces it *(Topics 3.1 and 3.2)*
- An increase in profits for firms and the industry
- Larger economies of scale
- An increase in market share if the production of one firm increases against the other firms
- Economic growth for the economy *(Topic 3.1)*
- A rise in the standard of living *(Topic 2.1)*

What is productivity?

A measure of efficiency measured in terms of output per unit of input.

$$\frac{\textbf{Total Output}}{\textbf{Total Input}}$$

What is a diseconomy of scale?

Costs of production increasing as the firm grows in size due to disadvantages of growing.

What does productivity depend on?

Improving inputs to the production process:

- Investment in the production process
- Workforce education and training
- Better quality raw materials

How can producers increase productivity?

- Workers specialising in part of the production process *(see topic 2.5)*
- Investment in new technology and more capital equipment
- Improving the skills of the workforce

Exam Criteria

- **Explain** the role of producers
- **Know** the difference between production and productivity
- **Evaluate** the importance of production for the economy
- **Evaluate** the importance of productivity for the economy
- **Calculate** and **explain** total cost
- **Calculate** and **explain** average cost
- **Calculate** and **explain** total revenue cost
- **Calculate** and **explain** average revenue
- **Calculate** and **explain** profit and loss
- **Evaluate** the importance of cost for producers
- **Evaluate** the importance of revenue for producers
- **Evaluate** the importance of profit and loss for producers
- **Understand** how costs and revenues affect profit and supply
- **Explain** economies of scale

Key Vocab

Word Wall

Profit - The amount of money a producer has left after all the costs have been paid i.e. when total revenue is greater than total cost.

Production - The total output of goods and services produced by a firm or industry in a given period of time.

Productivity - One measure of the degree of efficiency in the use of factors of production. It is measured in terms of output per unit of input.

Loss - When a firms revenue is less than its costs. I.e. total cost is greater than total revenue

Revenue - Income from the sale of goods and services.

Key Terms

Market Share – the portion of a market controlled by a particular company or product.

Average Cost – The cost of producing a unit (unit cost of production)

Total Cost - All of the costs of the firm added together

Average Revenue – The revenue per unit

Total Revenue - The total revenue from a firm from the sale of goods and services

Why is high productivity important?

Individuals are likely to see higher wages and higher standards of living.

Firms will see:

- Lower average costs and increasing economies of scale. More competitive on a global scale, increasing GDP and improving balance of payments.
- Greater profits – can be reinvested (higher wages or new equipment) to improve productivity further

Governments will see:

- Increased total output (greater employment, increased government revenue)
- Greater exports and thus economic growth

You will learn more about wages in topic 2.7, GDP and economic growth in topic 4.1, Balance of payments in topic 4.2, Exports and economic growth in 3.1, 4.1, 4.2 and 4.4 and Economic growth and taxation in topic 3.1 and 3.5.

What are the costs of productivity?

An increase in use of capital equipment could lead to unemployment. This leads to the government having to support the workers in the short term as well as longer term impacts on the family.

Greater international competitiveness could lead to countries retaliating causing a fall in GDP.

You will learn more about GDP and the Balance of Payments in topic 4.2

Study Tips

Be careful that you do not confuse production and productivity. They are quite different even if there are links between the two.

Be very careful that you do not confuse revenue and profit. They are very different concepts and in an exam it must be clear that you realise they are not the same.

Do not state that only large firms gain economies of scale. All firms can gain some economies by growing.

Is it important to know your costs and revenue as a producer?

What is total cost?

The costs of actually producing an item. It will include raw materials and the costs the firm has for simply existing.

Total cost = total fixed costs + total variable costs

$$TC = TFC + TVC$$

What is profit and loss?

Profit - Firms gain more revenue than it pays in costs. Profit maximisation is an aim of most firms.

Loss - Firms lose money because their revenue is less than costs.

How important is revenue?

Without an inflow of money from sales producers cannot make a profit.

Growth in revenue attracts investors.

Steady levels of revenue allow producers to secure loans/overdrafts. Overdrafts mean less short-term worries about paying suppliers/workers etc.

Creates confidence in the firm.

What are external economies of scale?

Firms benefit from these due to industry or location. They are out of the control of the firm:

- Improvement in transport links
- Education and training facilities
- Concentration of firms (suppliers etc)
- Reputable locations

What is average cost?

The cost of producing a single unit. A fall in AC shows that the firm is becoming more efficient and gaining economies of scale.

$$\textbf{Average cost} = \frac{\textbf{total fixed costs}}{\textbf{quantity}}$$

$$AC = \frac{TFC}{Q}$$

What is average revenue?

Revenue per unit sold.

$$\textbf{Average revenue} = \frac{\textbf{total revenue}}{\textbf{quantity}}$$

$$AR = \frac{TR}{Q}$$

How important is Profit?

- It generates finance for investment
- It acts as a signal and tells other producers that they too might be able to make a profit in that market
- It allows a producer to attract more resources to the firm/industry

How important is Loss?

- Short-term may not result in business closing (use reserves or borrow)
- Long term reverses will run out or will have to pay back loans
- It acts as a signal, telling factors of production to leave it to find a market making a profit

What are internal economies of scale?

Result from the growth of the business itself. They lead to cost savings and lower average cost:

- Technical economies
- Economies of increased dimensions
- Purchasing or bulk-buying economies
- Division of labour
- Financial economies
- Managerial economies
- Marketing economies
- Risk-bearing economies
- Research and development economies

What is total revenue?

Total income from the sale of goods and services. Also known as *sales revenue* or *turnover*.

Total revenue = Price x Quantity

$$TR = P \times Q$$

How important are costs?

If costs of production fall, firms can supply more at each price causing the supply curve to shift to the right. If costs of production rise the supply curve shifts to the left; less is supplied at every price.

Firms try to keep their costs low to make or increase profits.

Costs are only one factor in determining price. In some specialised markets, prices are based on cost.

Production costs generally rise as output increased, as costs rise with increasing output so does price, causing the supply curve to slope upwards *(Topic 2.5)*