

Edexcel (A) Economics A Level

Theme 1: An introduction to markets and
market failure

Flashcards



Ad valorem tax



Ad valorem tax

An indirect tax imposed on a good where the value of the tax is dependent on the value of the good



Asymmetric information



Asymmetric information

Where one party has more information than the other, leading to market failure



Capital



Capital

One of the four factors of production;
goods which can be used in the
production process



Capital goods



Capital goods

Goods produced in order to aid production of consumer goods in the future



Ceteris paribus



Ceteris paribus

All other things remaining the same



Command economy



Command economy

All factors of production are allocated by the state, so they decide what, how and for whom to produce goods



Complementary goods



Complementary goods

Negative XED; if good B becomes more expensive, demand for good A falls



Consumer goods



Consumer goods

Goods bought and demanded by households and individuals



Consumer surplus



Consumer surplus

The difference between the price the consumer is willing to pay and the price they actually pay



Cross elasticity of demand (XED)



Cross elasticity of demand (XED)

The responsiveness of demand for one good to a change in the price of another good



Demand



Demand

The quantity of a good/service that consumers are able and willing to buy at a given price at a given moment in time



Diminishing marginal utility



Diminishing marginal utility

The extra benefit gained from consumption of a good generally declines as extra units are consumed; explains why the demand curve is downward sloping



Division of labour



Division of labour

When labour becomes specialised during the production process so do a specific task in cooperation with other workers



Economic problem



Economic problem

The problem of scarcity; wants are unlimited by resources are finite so choices have to be made



Efficiency



Efficiency

When resources are allocated optimally, so every consumer benefits and waste is minimised



Enterprise



Enterprise

One of the four factors of production; the willingness and ability to take risks and combine the three other factors of production



Equilibrium price/quantity



Equilibrium price/quantity

Where demand equals supply so there are no more market forces bringing about change to price or quantity sold



Excess demand



Excess demand

When price is set too low so demand is greater than supply



Excess supply



Excess supply

When price is set too high so supply is greater than demand



Externalities



Externalities

The cost or benefit a third party receives from an economic transaction outside of the market mechanism.



External cost/benefit



External cost/benefit

The cost/benefit to a third party not involved in the economic activity; the difference between social cost/benefit and private cost/benefit



Free market



Free market

An economy where the market mechanism allocates resources so consumers and producers make decision about what is produced, how to produce it and for whom



Free rider principle



Free rider principle

People who do not pay for a public good still receive benefits from it so the private sector will under-provide the good as they cannot make a profit



Government failure



Government failure

When government intervention leads to a net welfare loss in society



Habitual behaviour



Habitual behaviour

A cause of irrational behaviour; when consumers are in the habit of making certain decisions



Incidence of tax



Incidence of tax

The tax burden on the taxpayer



Income elasticity of demand (YED)



Income elasticity of demand (YED)

The responsiveness of demand to a change in income



Indirect tax



Indirect tax

Taxes on expenditure which increase production costs and lead to a fall in supply



Inferior goods



Inferior goods

$YED < 0$; goods which see a fall in demand as income increases



Information gaps



Information gaps

When an economic agent lacks the information needs to make a rational, informed decision



Labour



Labour

One of the four factors of production;
human capital



Land



Land

One of the four factors of production;
natural resources such as oil, coal,
wheat, physical space



Luxury goods



Luxury goods

$YED > 1$; an increase in incomes causes an even bigger increase in demand



Market failure



Market failure

When the free market fails to allocate resources to the best interest of society, so there is an inefficient allocation of scarce resources



Market forces



Market forces

Forces in free markets which act to reduce prices when there is excess supply and increase them when there is excess demand



Minimum price



Minimum price

A floor price which a firm cannot charge below



Mixed economy



Mixed economy

Both the free market mechanism and the government allocate resources



Model



Model

A hypothesis which can be proven or tested by evidence; it tends to be mathematical whilst a theory is in words



Negative externalities of production



Negative externalities of production

Where the social costs of producing a good are greater than the private costs of producing the good



Non-excludability



Non-excludability

A characteristic of public goods;
someone cannot be prevented from using
the good



Non-renewable resources



Non-renewable resources

Resources which cannot be readily replenished or replaced at a level equal to consumption; the stock level decreases over time as they are consumed



Non-rivalry



Non-rivalry

A characteristic of public goods; one person's use of the good does not prevent someone else from using it



Normal goods



Normal goods

$YED > 0$; demand increases as income increases



Normative statements



Normative statements

Subjective statements based on value judgements and opinions; cannot be proven or disproven



Opportunity cost



Opportunity cost

The value of the next best alternative
forgone



Perfectly price elastic good



Perfectly price elastic good

PED/PES=Infinity; quantity demanded/supplied falls to 0 when price changes



Perfectly price inelastic good



Perfectly price inelastic good

$PED/PES=0$; quantity
demanded/supplied does not change
when price changes



Positive externalities of consumption



Positive externalities of consumption

Where the social benefits of consuming a good are larger than the private benefits of consuming that good



Positive statements



Positive statements

Objective statements which can be tested with factual evidence to be proven or disproven



Possibility production frontier (PPF)



Possibility production frontier (PPF)

Depicts the maximum productive potential of an economy, using a combination of two goods or services



Price elasticity of demand



Price elasticity of demand

The responsiveness of demand to a change in price



Price elasticity of supply



Price elasticity of supply

The responsive of supply to a change in price



Price mechanism



Price mechanism

The system of resource allocation based on the free market movement of prices, determined by the demand and supply curves



Private cost/benefit



Private cost/benefit

The cost/benefit to the individual participating in the economic activity



Private goods



Private goods

Goods that are rivalry and excludable



Producer surplus



Producer surplus

The difference between the price the producer is willing to charge and the price they actually charge



Public good



Public good

Goods that are non-excludable,
non-rivalry, non-rejectable and have zero
marginal cost



Rationality



Rationality

Decision-making that leads to economic agents maximising their utility



Regulation



Regulation

Laws to address market failure and promote competition between firms



Relatively price elastic good



Relatively price elastic good

When $PED/PES > 1$; demand/ supply is relatively responsive to a change in price so a small change in price leads to a large change in quantity demanded/supplied



Relatively price inelastic good



Relatively price inelastic good

When $PED/PES < 1$; demand/supply is relatively unresponsive to a change in price so a large change in price leads to a large change in quantity demanded/supplied



Renewable resources



Renewable resources

Resources which can be replenished, so the stock of resources can be maintained over a period of time



Scarcity



Scarcity

The shortage of resources in relation to the quantity of human wants



Social cost/benefit



Social cost/benefit

The cost/benefit to society as a whole due to the economic activity



Social optimum position



Social optimum position

Where social costs equal social benefits;
the amount which should be
produced/consumed in order to
maximise social welfare



Social science



Social science

The study of societies and human
behaviour



Specialisation



Specialisation

The production of a limited range of goods by a company/country/individual so they aren't self-sufficient and have to trade with others



Specific tax



Specific tax

A tax imposed on a good where the value of the tax is dependent on the quantity that is bought



State provision



State provision

When the government provides public goods or merit goods which are underprovided in the free market



Subsidy



Subsidy

Government payments to a producer to lower their costs of production and encourage them to produce more



Substitutes



Substitutes

Positive XED; if good B becomes more expensive, demand for good A rises



Supply



Supply

The ability and willingness to provide a particular good/service at a given price at a given moment in time



Symmetric information



Symmetric information

Where buyers and sellers both have access to the same information



Trade pollution permits



Trade pollution permits

Licenses which allow businesses to pollute up to a certain amount. The government controls the number of licenses and so can control the amount of pollution. Businesses are allowed to sell and buy the permits which means there may be incentive to reduce the amount they pollute



Unitary price elastic good



Unitary price elastic good

When $PED/PES=1$; a change in price leads to a change in output by the same proportion



Utility



Utility

The satisfaction derived from consuming a good



Weakness at computation



Weakness at computation

A cause of irrational behaviour; when consumers are bad at making calculations, estimating probabilities and working out future benefits/costs

