

1.1 Choice, models and market adjustment

Name: _____ Class: _____ Date: _____ **Total: 6 marks**

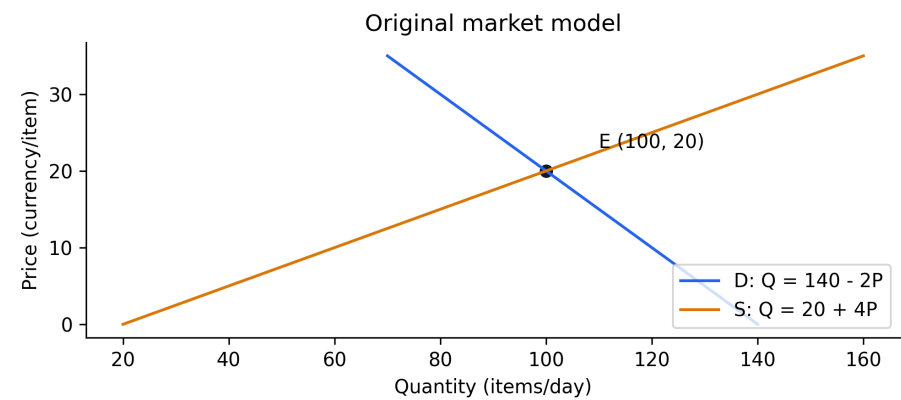
KEY WORDS scarcity • opportunity cost • equilibrium
• excess demand

Objective

Apply the supported native methods to original data and justify a qualified transfer conclusion.

1 Key knowledge and worked examples

A model specifies variables and holds other relevant influences constant. Scarcity requires choice; opportunity cost is the benefit of the next-best alternative. Marginal choice compares additional benefit and cost. A positive statement can in principle be tested; a normative statement adds a value judgement. Consumer and firm objectives are model assumptions, not a claim that everyone calculates perfectly.



In an original market model, $Q_d=140-2P$ and $Q_s=20+4P$, where P is currency units per item and Q is items per day. Explain equilibrium and a price of 15.

Equilibrium requires $Q_d=Q_s$. Thus $140-2P=20+4P$; $120=6P$; $P=20$ currency units/item. $Q_d=140-2(20)=100$ items/day and $Q_s=20+4(20)=100$ items/day. At $P=15$, $Q_d=110$ and $Q_s=80$ items/day, giving excess demand $=110-80=30$ items/day.

In the simple adjustment story, buyers bid up price or suppliers change prices; quantities then move along unchanged curves. A demand shift requires a different determinant, such as income or preferences. Shortages do not prove instantaneous adjustment or unrestricted competition.

2 Practice

2.1 For the worked case, state the method, show its application and give a limitation.[3]

3 Exam-style questions

3.1 A publicity campaign raises demand while a supplier's input costs increase. Explain why equilibrium quantity cannot be predicted from these directions alone and describe the diagram. [3]