Exercise walk-through

Mixed economic system ▪ 2.10

eXercise

You must be able to

- explain what a mixed economy is
- describe the methods of government intervention
- analyse and evaluate government intervention to correct market failure

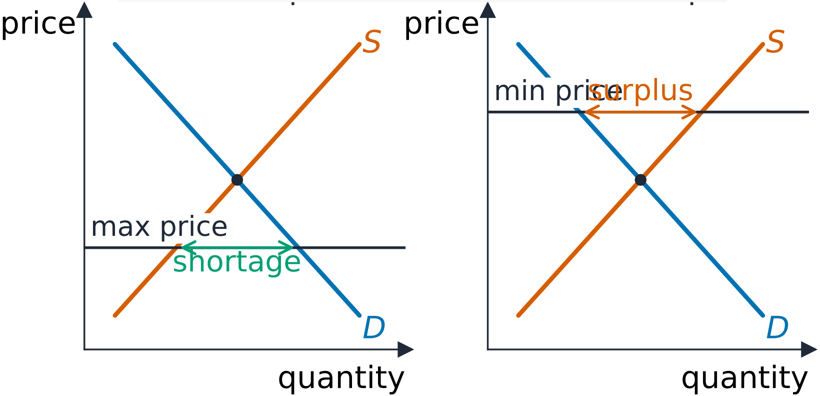
Method — Government intervention

- **Mixed economy 混合经济**: a **private sector 私营部门** (price mechanism) + a **public sector 公共部门** (government).
- **Maximum price 最高价格** (below equilibrium) → a shortage. **Minimum price 最低价格** (above equilibrium) → a surplus.
- **Indirect tax 间接税** (cuts demerit goods), **subsidy 补贴** (raises merit goods), **regulation 监管**, **direct provision 直接提供**.

Answer shapes: an **Analyse [up to 6]** answer may use a price-control diagram; **Discuss [8]** adds a judgement (Ev).

Method — Government intervention

max price → shortage · min price → surplus



A maximum price causes a shortage; a minimum price causes a surplus

Method — Government intervention

Merit good	**Demerit good**
better for you than you realise → under-consumed (e.g. education, healthcare)	worse for you than you realise → over-consumed (e.g. cigarettes, alcohol)

Merit goods are under-consumed and demerit goods over-consumed when left to the market

Practice 2.1 ▪ 2 marks

Define the term *mixed economy*.

Solution 2.1

Method: Government intervention

Worked steps

an economy with both a private sector (guided by the price mechanism) and a public sector (run by the government) (2 for a clear definition; 1 for a partial idea).

Practice 2.2 ▪ 1 mark

State the effect of a **maximum price** set below the equilibrium price.

Solution 2.2

Method: Government intervention

Worked steps

a shortage (excess demand), because quantity demanded exceeds quantity supplied (1).

Practice 2.3 ▪ 2 marks

Identify two methods of government intervention.

Solution 2.3

Method: Government intervention

Worked steps

any two of: maximum/minimum price; indirect tax; subsidy; regulation; direct provision $(1 + 1)$.

Exam-style 3.1 ▪ 1 mark

A government sets a **minimum price** above the equilibrium. This will cause:

- **A** a shortage
- **B** a surplus
- **C** the market to clear
- **D** demand to rise

Solution 3.1

Method: Government intervention

A a shortage

B a surplus ✓

C the market to clear

D demand to rise

Worked steps

B. A minimum price above equilibrium causes a surplus.

Exam-style 3.2 ▪ 4 marks

Using a diagram, explain the effect of a maximum price set below the equilibrium price.

Solution 3.2

Method: Government intervention

Worked steps

[4] K 1 + **diagram up to 2** (demand and supply, a maximum price line below P_e, excess demand) + An 1 — a maximum price held below equilibrium means quantity demanded exceeds quantity supplied $\rightarrow$ a shortage forms, because the price is not allowed to rise to clear the market.

Exam-style 3.3 ▪ 8 marks

Discuss whether a government should use an indirect tax to reduce consumption of a demerit good.

Solution 3.3

Method: Government intervention

Worked steps

[8] K/App/An up to 5 + Ev up to 3. **For a tax:** it raises the price → cuts consumption of the harmful good, raises government revenue, and makes consumers pay for the external cost. **Against:** if demand is inelastic (addiction), consumption falls little; the tax is regressive (hits the poor more); a black market may form. **Judgement (Ev):** a tax helps, but works best combined with education and regulation — its success depends on the price elasticity of demand for the good.