Exercise walk-through

Market economic system ▪ 2.8

eXercise

You must be able to

- explain how a market economy answers what, how and for whom to produce
- state the advantages and disadvantages of the market system
- analyse and evaluate the market system

Method — The market system

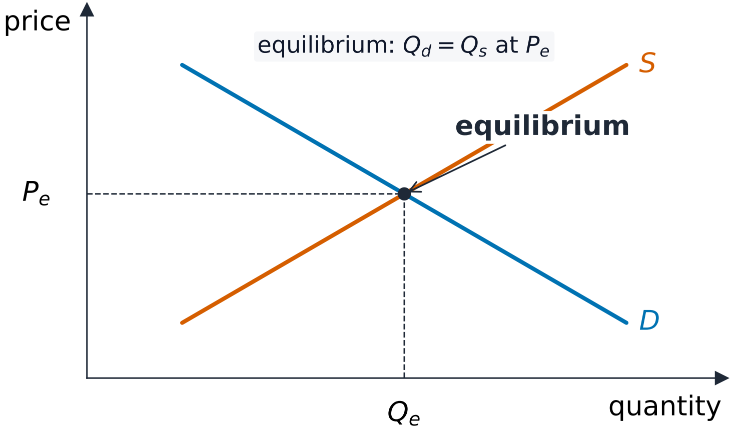
- **Market economy 市场经济**: the price mechanism makes all the choices (no government planning). The opposite is a **planned economy 计划经济**.
- **Advantages:** prices guide resources without planning; firms compete (lower costs, new goods); wide consumer choice.
- **Disadvantages:** some useful goods are not made (no profit); the rich do well, the poor may get little; markets can **fail 失灵**.

Answer shapes: K + App + An + Ev (a justified judgement, for discuss questions).

Method — The market system

A stock exchange is one kind of market

Method — The market system



The price settles where demand and supply cross

Practice 2.1 ▪ 2 marks

Define the term *market economy*.

Solution 2.1

Method: The market system

Worked steps

an economy in which the price mechanism (demand and supply) makes all the resource-allocation decisions, with no government planning (2 for a clear definition; 1 for a partial idea).

Practice 2.2 ▪ 2 marks

State two advantages of the market economic system.

Solution 2.2

Method: The market system

Worked steps

any two of: prices guide resources without planning; competition lowers costs and creates new goods; wide consumer choice $(1 + 1)$.

Practice 2.3 ▪ 1 mark

State one disadvantage of the market economic system.

Solution 2.3

Method: The market system

Worked steps

any one of: useful but unprofitable goods are not made; the poor may get little; markets can fail (1).

Exam-style 3.1 ▪ 1 mark

In a market economy, decisions about what to produce are made by:

A the government

B the price mechanism (demand and supply)

C a central planner

D trade unions

Solution 3.1

Method: The market system

A the government

B the price mechanism (demand and supply) ✓

C a central planner

D trade unions

Worked steps

B. In a market economy the price mechanism decides what to produce.

Exam-style 3.2 ▪ 4 marks

Explain one disadvantage of relying only on the market system to allocate resources.

Solution 3.2

Method: The market system

Worked steps

[4] K 1 + An up to 3 — the market only makes goods that earn a profit → so public goods (like street lighting) and merit goods may be under-provided → and the poor, who cannot pay, may go without essentials → this is an inefficient or unfair outcome.

Exam-style 3.3 ▪ 8 marks

Discuss whether a market economy is the best way to allocate a country's resources.

Solution 3.3

Method: The market system

Worked steps

[8] K/App/An up to 5 + Ev up to 3. **For:** prices allocate resources efficiently without planning, competition drives lower costs and innovation, and consumers have choice. **Against:** it under-provides public and merit goods, ignores external costs (pollution), and can leave the poor with too little. **Judgement (Ev):** the market works well for most goods, but it fails for some, so a *mixed* economy — market plus government correction — usually allocates resources better; it depends on the type of good.