

# 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

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# Capital

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# 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

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# Enterprise

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# 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 of 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

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# Labour

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# Labour

One of the four factors of production;  
human capital

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# Land

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# 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

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# Model

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# 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 prevent 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

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# Supply

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# 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

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# Utility

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# 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