Foreword

The International General Certificate of Secondary Education (IGCSE) is an internationally recognized qualification that aims to help students prepare for further education, including progression to A or AS Level studies.

In architecture, laying the foundation is the most important step. In education it is the same – students must build a strong foundation in their secondary education before they can have the freedom and knowledge to explore more diverse disciplines later in their studies. The right mix of proper attitude, guidance, and hard work is the formula for success.

Designed for a two-year course, the IGCSE Economics syllabus enables students to develop an understanding of economic principles and concepts. As students learn to interpret and examine economic sources, they are challenged to apply the concepts to real-life situations, identify issues and problems, present reasoned arguments and provide possible solutions. They will also gain a wider perspective of the roles that consumers, producers and citizens play in the local and global economy.

Economics is a dynamic discipline that has a strong impact on our everyday lives. In order to achieve a good result in the IGCSE exam, it is essential for students to have a solid understanding of the mechanisms involved before they can confidently establish exam strategies. We believe that this study guide will help students do just that.

NTK's study guides, courses and educational consulting services are designed to help prepare students for exam success as they continue to pursue secondary and college education. As a leading educational service provider in Southeast Asia for more than 15 years, NTK has helped thousands of students reach their academic goals. Whether they are in primary, secondary, or postgraduate studies, our students have benefited greatly from our specialized academic programs and expertise in all major international curricula and exams.

As you continue on your studies, I wish you every success; and most importantly, I hope you enjoy the learning process as well.

T.K. Ng

Founder and Managing Director
NTK Academic Group

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Demand and Supply

Introduction

The word ‘economics’ comes from *oikonomikos*, which means ‘skilled in household management.’ Although the word is very old, the discipline of economics as we understand it today is a relatively recent development. Throughout the years, the economic problems with which society struggles remain the same:

- How do we decide what to produce with our limited resources?
- How do we ensure stable prices and full employment of our resources?
- How do we provide a rising standard of living both for ourselves and for future generations?

There have been several main schools of economics proposing different answers to these questions.

1.1 Demand and supply curves

Demand

Demand can be defined as the quantity of goods or services that a consumer is willing and able to purchase at different prices in a given time period. It can be represented by a downward sloping line called the demand curve.

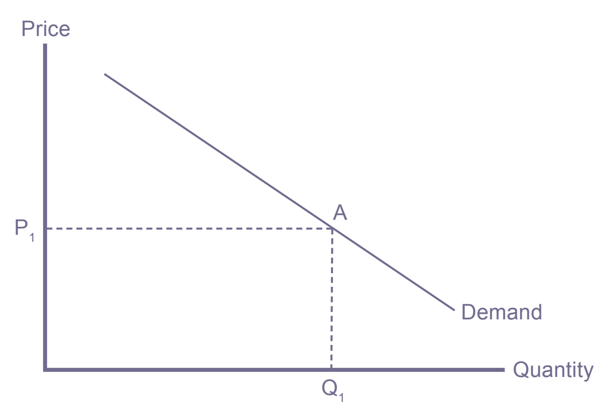

Figure 1.1 Demand curve

Quotation

“Teach a parrot the terms ‘supply and demand’ and you’ve got an economist.”
Thomas Carlyle

The demand curve shows an inverse relationship between price and quantity demanded. Quantity demanded refers to the quantity of goods or services that a consumer is willing and able to purchase at a given price in a given time period. For example, at the price P_1, the level of quantity demanded is Q_1.

Price and quantity demanded are inversely related because when the price of a good is higher, it becomes less affordable to consumers for the same amount of the good. As a result, the quantity demanded of that particular good will decrease.

Movements along the demand curve

Any changes in the price will trigger a movement along the demand curve, which can be shown in the diagram below.

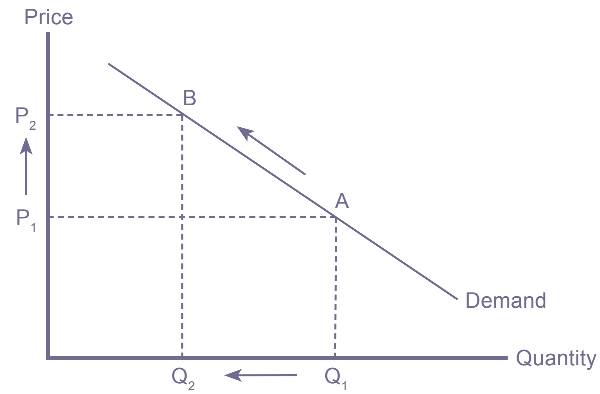

Figure 1.2 Decrease in the quantity demanded when price increases

It can be seen that when the price increases from P_1 to P_2, there will be a movement along the demand curve from point A to point B. The quantity demanded will decrease from Q_1 to Q_2.

Shifts in the demand curve

Unlike the movement along the demand curve, a shift in the demand curve is triggered by changes in any factor other than the price. This shift represents a change in demand. If the demand curve is shifted to the right, it means there is an increase in demand at any given price and vice versa.

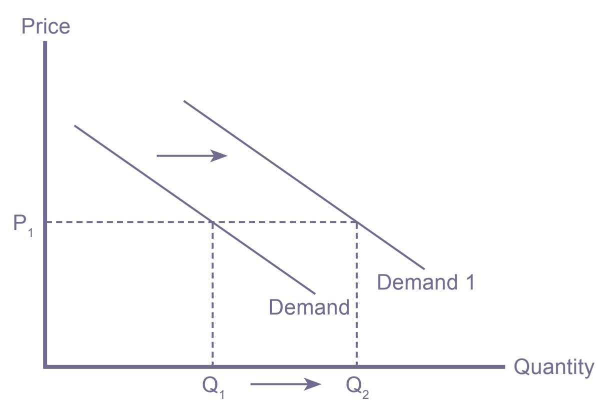

Figure 1.3 Rightward shift of the demand curve

In Figure 1.3, there is a rightward shift in the whole demand curve due to a change in any factor other than price. At the same price P_1, the quantity demanded increases from Q_1 to Q_2, indicating an increase in demand. On the other hand, a leftward shift in the demand curve shows a decrease in demand.

Factors affecting demand

Factors which may cause a shift in the demand curve are called determinants of demand. They include:

Income

The level of income reflects a consumer's ability to purchase goods and services. When there is a change in income, the demand for goods will change too. The actual impact depends on the nature of the goods, which can be divided into the following two categories.

- Normal goods

  Normal goods are goods that consumers will demand more when there is a rise in the income level. For example, when the income in the economy increases, people tend to eat out more often. Dining in restaurants is a normal good in this case. The demand for it is higher (the demand curve shifts to the right) when income increases.

- Inferior goods

  Inferior goods are goods that consumers will demand less when there is a rise in the income level. For example, people will consume less canned foods or instant noodles when there is a rise in their income as proper meals are more affordable to them now. In this case, canned foods and instant noodles are inferior goods. The demand for them drops (the demand curve shifts to the left) when income rises.

Changing tastes and preferences

As demand is the willingness of consumers to purchase goods and services, the demand pattern changes when there is a change in consumers' tastes and preferences, which can be affected by the following factors.

- Advertising and promotions

  These are the means used by sellers to influence the tastes and preferences of consumers. The sellers usually put a lot of money on advertising new products to attract consumers' attention and thus increase their demand.

- Fashion

  When a change in fashion is in favour of a good, the demand for it will increase and vice versa. For example, 2G mobile phones are considered old-fashioned nowadays because of the development of 3G and even 4G technology. So the demand for 2G mobile phones has decreased greatly in recent years.

Fun Fact

Advertisement control over tobacco

Many products cannot be advertised, such as tobacco products. On 27 February 2005, the WHO (World Health Organization) Framework Convention on Tobacco Control came into effect. 168 States agreed to the treaty banning tobacco advertising.

http://www.who.int/fctc/signatories_parties/en/index.html

- Medical reports

  They can have great impacts on people's preferences too. For example, in 2006, there were reported outbreaks of bird flu around the world, which dramatically reduced the world demand for poultry.

Population

The following are the determinants of the population distribution that will affect the market demand.

- Size

  Since market demand is the sum of all individuals' demand, a bigger population means that there will be more consumers in the market and the demand will increase.

- Age

  If a country's population has a longer life expectancy, ageing will become an issue. There will be an increase in the demand for elderly homes and healthcare services.

- Dependency ratio

  This ratio compares the size of the dependent population with the size of the working population. The dependent population includes children, students, housewives, the unemployed and pensioners. The higher the dependency ratio, the more the dependent population is supported by the working people, and therefore the less spare money that working people can spend. For example, countries with a higher dependency ratio will have a lower demand for overseas holidays as they need to spend a higher proportion of their income to support the people not working.

Changing prices of substitutes

Substitutes are goods which are in competitive demand and act as replacements for another product. Examples include butter and margarine, buses and trains, ball pens and fountain pens. An increase in the price of a substitute for good X will cause a rise in the demand for good X. For example, an increase in the price of traditional cameras encourages consumers to shift their demand from traditional cameras to digital cameras, leading to a rise in the demand for digital cameras.

Changing prices of complements

Complements are goods related to each other because they are usually consumed together. Two complements are said to be in a joint demand. Examples include gasoline and cars, DVD players and DVDs, films and cameras. A rise in the price of a complement to good Y will cause a decrease in the demand for good Y and vice versa. For example, a reduction in the market price of computers would lead to an increase in the demand for printers, scanners and software applications.

DVD players and DVDs together make an example of complements.

Supply

Supply can be defined as the quantity of goods or services that a producer is willing and able to sell at different prices in a given time period. It can be represented by an upward sloping line called the supply curve.

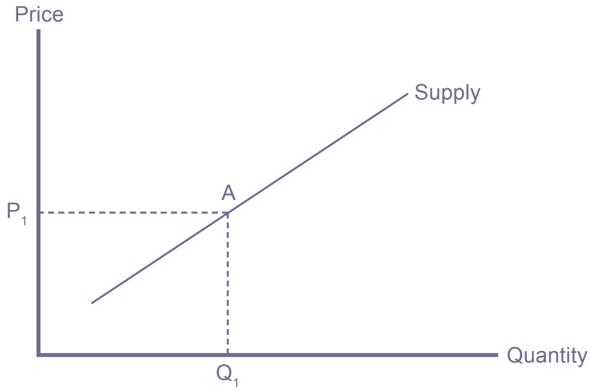

Figure 1.4 Supply curve

The supply curve shows a positive relationship between price and quantity supplied. Quantity supplied refers to the quantity of goods or services that a producer is willing and able to sell at a given price in a given time period. For example, at the price P_1, the level of quantity supplied is Q_1.

Price and quantity supplied are positively related because when the price of a good is higher, it is more profitable for the producers to sell this good as they can earn more for each unit of good sold. So the quantity supplied of that particular good will increase.

Movement along the supply curve

Any changes in the price will trigger a movement along the supply curve, which can be shown in the diagram on the next page.