Maggie 24/25

1. (a) Explain why governments impose price floors (minimum prices). [10 marks]

Answers should include:

- ☑ a definition of price floor
- ☑ a diagram of the application of a price floor
- ☑ and explanation of possible reasons for a price floor, for example regarding
  - ☑ equity (minimum wage),
  - ☑ to support the income of producers (agricultural price supports)
  - ☑ or to discourage the consumption of [demerit] goods (we haven't covered demerit goods, so mention of goods that the government doesn't want us to consume is sufficient)
- ☑ examples of where a price floor has been applied.

Level		Marks
0	☐ The work does not reach a standard described by the descriptors below.	☐ 0
1	☐ There is little understanding of the specific demands of the question. ☐ Relevant economic terms are not defined. ☐ There is very little knowledge of relevant economic theory. ☐ There are significant errors.	☐ 1 ☐ 2 ☐ 3
2	☐ There is some understanding of the specific demands of the question. ☐ Some relevant economic terms are defined. ☐ There is some knowledge of relevant economic theory. ☐ There are some errors.	☐ 4 ☐ 5 ☐ 6
3	☐ There is understanding of the specific demands of the question. ☐ Relevant economic terms are defined. ☐ Relevant economic theory is explained and applied. ☐ Where appropriate, diagrams are included and applied. ☐ Where appropriate, examples are used. ☐ There are few errors.	☐ 7 ☐ 8
4	☐ There is clear understanding of the specific demands of the question. ☐ Relevant economic terms are clearly defined. ☐ Relevant economic theory is clearly explained and applied. ☐ Where appropriate, diagrams are included and applied effectively. ☐ Where appropriate, examples are used effectively. ☐ There are no significant errors.	☑ 9 ☐ 10

(b) Discuss the consequences for producers, consumers and the government of imposing a price floor (minimum price) on a good. [15 marks]

Answers may include:

☐ definition of price floor
☐ diagram to illustrate possible impacts (eg to show a change in business revenues)
☐ explanation of the consequences for producers (change in revenues), ☐ consumers (higher prices) and ☐ government (cost of implementation)
☐ examples of consequences when a price floor has been introduced
☐ Discussion may include: the consequences of introducing a price floor on the different stakeholders.

Award a maximum of level 2 if only minimum wage is discussed. Award a maximum of level 2 if only one stakeholder is discussed. Award a maximum of level 3 if only two stakeholders are discussed. Level 4 can be awarded if three stakeholders have been discussed.

Examiners should be aware that candidates may take a different approach which, if appropriate, should be rewarded.

Opinions or conclusions should be presented clearly and should be supported by appropriate examples.

Effective evaluation may be to: ☐consider short-term versus long-term consequences ☐ examine the impact on different stakeholders ☐discuss advantages and disadvantages ☐prioritize the arguments.

Level		Marks
0	☐The work does not reach a standard described by the descriptors below.	☐0
1	☐There is little understanding of the specific demands of the question. ☐Relevant economic terms are not defined. ☐There is very little knowledge of relevant economic theory. ☐There are significant errors.	☐1 ☐2 ☐3 ☐4 ☐5
2	☐There is some understanding of the specific demands of the question. ☐Some relevant economic terms are defined. ☐There is some knowledge of relevant economic theory. ☐There are some errors.	☐6 ☐7 ☐8 ☐9
3	☐There is understanding of the specific demands of the question. ☐Relevant economic terms are defined. ☐Relevant economic theory is explained and applied. ☐Where appropriate, diagrams are included and applied. ☐Where appropriate, examples are used. ☐There is an attempt at synthesis or evaluation. ☐There are few errors.	☐10 ☐11 ☐12
4	☐There is clear understanding of the specific demands of the question. ☐Relevant economic terms are clearly defined. ☐Relevant economic theory is clearly explained and applied. ☐Where appropriate, diagrams are included and applied effectively. ☐Where appropriate, examples are used effectively. ☐There is evidence of appropriate synthesis or evaluation. ☐There are no significant errors.	☐13 ☐14 ☑15

fantastic!

Maggie Question 1. #1

PART A

Price floor is a ~~legally set~~ ~~mini~~ legal minimum price set by the government on a good or service or factor of production.

~~Equilibrium qua~~ Market equilibrium is a state of balance in a free market achieved when quantity demanded is equal to quantity supplied; so that there is neither surplus nor shortage.

Surplus occurs when the quantity ~~s~~ supplied is greater than the quantity demanded.

Market for ~~a appl~~ apples.

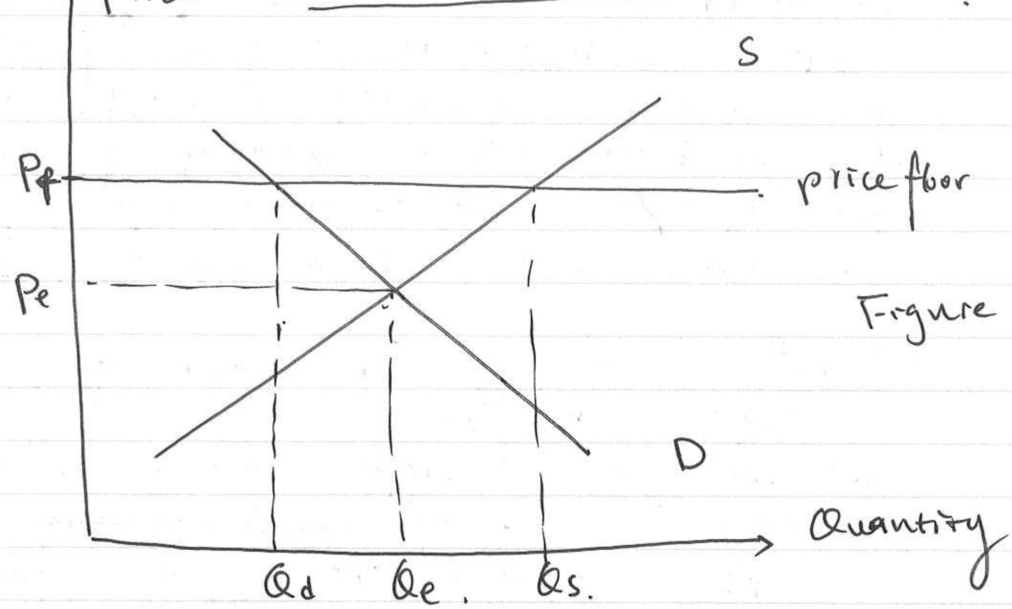

Figure 1.

~~when~~ Figure 1 shows the effect of price floor on the market for apples. Initially, the market is at equilibrium at Pe, with ~~Qe~~ quantity supplied and demanded both at Qe; However, when a price floor is imposed, the price of apple can not go lower than the legal minimum ~~Pe~~ price Pf, as a result, quantity demanded is forced to decrease from Qe to Qd, as a result of the law of demand, and quantity supplied is forced to increase from Qe to Qs, because of the law of supply, resulting in a ~~sto~~ surplus for apple. Yes!

~~The reas~~ Price mechanism is the reason behind the change in quantity. When the price increases from Pe to Pf, ~~price is signalling~~ the suppliers have ~~less~~ more incentive ~~to~~ produce because an ~~p decrease~~ increase in price leads to a ~~decrease~~ increase in their revenue, and thus ~~less~~ more profits. As a result, quantity supplied ~~decreases~~ increases; on the other hand, the ~~price~~ increase in price from Pe to Pf ~~signals the p consumers~~ creates less incentive ~~and~~ in consumer and signals them to purchase less apples as they're becoming less affordable, leading to a decrease in quantity demanded. As quantity demanded decreases and quantity supplied increases, quantity supplied ~~to~~ is more than quantity demanded, leading to a shortage. Yes!

There are mainly three reasons for governments to impose price floors.

First reason is to support farmers on agricultural production. Because of ~~inelastic demand~~ low PED and PES of agricultral goods, farmers always have very unstable income! As figure 2 shows, a slight chang in ~~quantity~~ supplyed can result in a huge variation in price, and thus a large change in income. To protect these farmers, governments choose to impose price floors.

A second ~~sea~~ reason is to protect low-income group. The price floor in a labour market is also known as minimum wages. In this way, the goverment ensures the basic

#3.

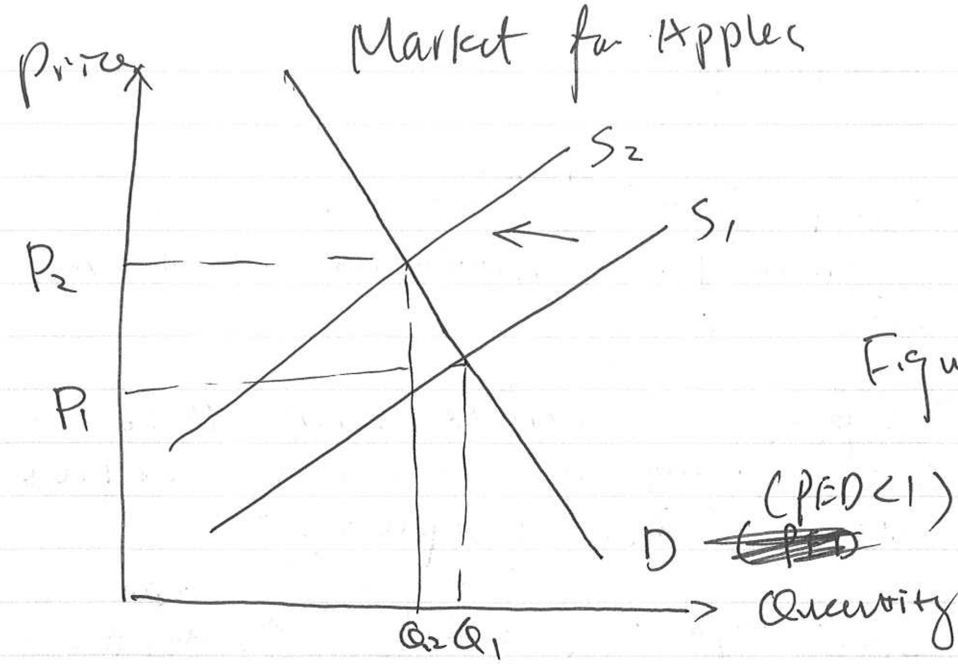

Figure 2.

need of these low-incom group will be satisfied. An example will be the minimum wage for workers in China is set at ¥1000 a month. The third reason is to disencourage consumption of harmful goods, as higher price gives less incentive to consumers. For example, there is a price floor for ~~alco~~ alcohol in Canada by the government to prevent abusive ~~use of~~ consumption.

$\boxed{\text{PART B}}$

~~Unemployment of labour occurs when not all labors are working; i.e. human resources are not optimally used~~.

Welfare loss occurs when there is a decrease in the sum of consumer surplus and ~~sur~~ producer surplus.

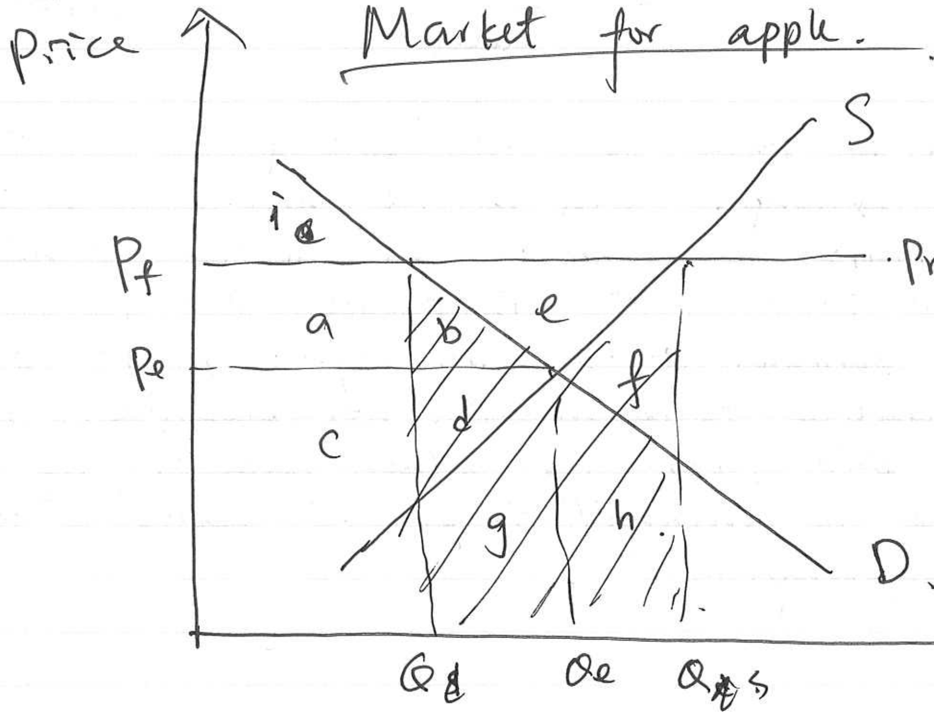

Figure 3

As figure 3 shows, initially at Pe, Qe, consumers has surplus a+b+i, which is the benefit they get when they purchase a good lower than their maixmum acceptable price; and supplier ~~to~~ surplus is the area c+d. When a price floor is imposed, the quantity supplied decreases to Qs, and thus ~~the~~ consumer surplus decrease's to i~~a~~. ~~and~~. However, ~~Sur~~ producer surplus increases to

#5

a + c + e + b + d.
~~The area Pf * Qs, which is a+b+e+c+d+g+h+f~~, So the total welfare becomes i + a+b+c+d+e ~~+f+g+h~~. However, as there is excess ~~supp~~ supply, and government is going to help suppliers and thus buy thos apples, there is a revenue spent on that, and the quantity is $(Qs - Qd) * Pf$, Therefore, there is a welfare loss of a total of $(b + d + g + h + f)$, Wow! We haven't covered this yet!

An example of such is a price floor on ~~the~~ apples in China to ensure the stability of income for ~~fa~~ local farmars.

As shown in this example and the graph, the price floor on agricultural products has a negative impact on society as a whole ~~due to~~ welfare loss. Now we examine the effect on each stakeholders.

For producers, they're better off. They have a larger total revenue as the price increases to Pf, while the quatity supplied remains the same. However, their quality of products may decrease because of the government insurance from price floors.

For consumers, they are worse off. When the price floor is imposed, the price increases from Pe to Pf, and quatity demanded ~~also~~ decreases. As a result, they are receiving less and paying more, and thus worse off.

For governments, it is also worse. In order to ensure that there is no excess supply and all the additional agricultural goods produced are consumed, and thus ~~ensure~~ protecting farmers, ~~they have to find ways to dispose~~ they have to pay ~~to~~ buy these surplus, as shown in Figure 4.

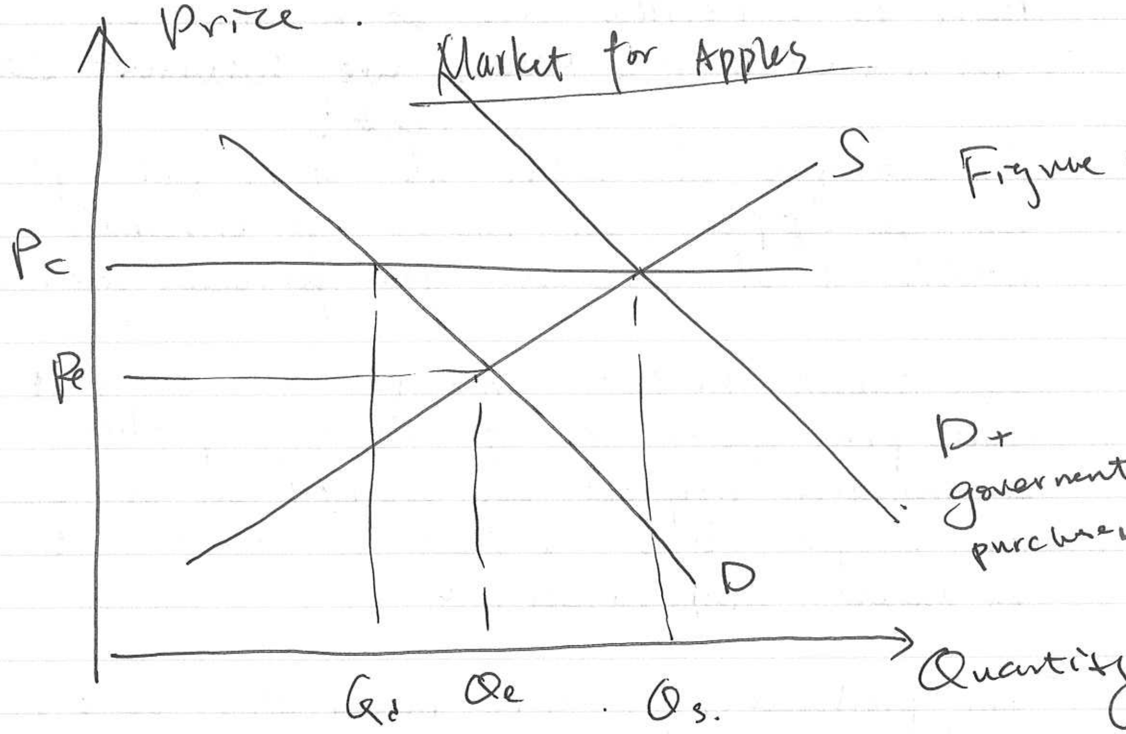

Figure 4.

These ~~price~~ money comes from government revenue. ~~in a~~ therefore, either leading to more tax on other goods, or a deficit. in either case it is bad.

Moreover, in order to dispose these agricultural goods, government have limited choices. If they choose to store these goods, there will be extra money spent on storage, which also leads to further decrease in government revenues. Alternatively, if these goods were sold elsewhere, the price becomes too high to competitive with others. that are sold at equilibrium price. On the other hand, however, by imposing price floors on ~~go~~ agricultural goods, and thus help increase wages for farmers, government can gain popularity among farmers and thus have more political support.

In a nutshell, there are both pros and cons for stakeholders when a price floor is imposed. In reality, we still need to take other factors into consideration to weigh whether or not to impose a ~~f~~ price floor.

Maggie

Section A

Answer **one** question from this section.

agriculture
support (owin--

Microeconomics

1. (a) Explain why governments impose price floors (minimum prices). [10]

   (b) Discuss the consequences for producers, consumers and the government of imposing a price floor (minimum price) on a good. [15]

2. (a) Explain the view that an increase in price will lead to a decrease in the quantity demanded whilst an increase in demand will lead to an increase in price. [10]

   (b) Discuss the significance of price elasticity of demand for government intervention in markets. [15]

PED

tax