IB Economics Year 1 Check List

Here is the list of things the IB wants you to know. Use this checklist to follow along with the course and make sure you are keeping up with the material.

Syllabus
❏ Explain that economics is a social science.
❏ Outline the social scientific method.
❏ Explain the process of model building in economics.
❏ Explain that economists must use the ceteris paribus assumption when developing economic models
❏ Distinguish between positive and normative economics.
❏ Examine the assumption of rational economic decision-making.
❏ Explain that scarcity exists because factors of production are finite and wants are infinite.
❏ Explain that economics studies the ways in which resources are allocated to meet needs and wants.
❏ Explain that the three basic economic questions that must be answered by any economic system are: “What to produce?”, “How to produce?” and “For whom to produce?”
❏ Explain that as a result of scarcity, choices have to be made.
❏ Explain that when an economic choice is made, an alternative is always foregone.
❏ Explain that a production possibilities curve (production possibilities frontier) model may be used to show the concepts of scarcity, choice, opportunity cost and a situation of unemployed resources and inefficiency.
❏ Outline the meaning of the term market
❏ Explain the concept of utility, marginal utility and the phenomenon of diminishing marginal utility

DEMAND

Syllabus

❑ Negative relationship between price and quantity demanded
❑ rare exceptions to the law of demand (Giffen and Veblen goods)
❑ Individual demand vs. Market demand
❑ What is the demand curve
❑ Draw a demand curve
❑ Determinants of demand (INSECT) - exogenous factors that change quantity demanded at every price
❑ Movement of the demand curve
❑ Movement along the demand curve
❑ Draw diagrams that show these differences
HL only ❑ Explain a demand function (equation) of the form Qd = a – bP. ❑ Plot a demand curve from a linear function (eg. Qd = 60 – 5P). ❑ Identify the slope of the demand curve as the slope of the demand function Qd = a – bP, that is –b (the coefficient of P). ❑ Outline why, if the "a" term changes, there will be a shift of the demand curve. ❑ Outline how a change in "b" affects the steepness of the demand curve.

SUPPLY

Syllabus
❑ Positive relationship between price and quantity supplied
❑ Producer's supply vs. Market supply
❑ What is the supply curve
❑ Draw a supply curve
❑ Determinants of supply (COGENT) – exogenous factors that change quantity supplied at every price
❑ Movements of the supply curve
❑ Movements along the supply curve

❏ Draw diagrams that show these differences
HL only ❏ Explain a supply function (equation) of the form Qs = c + dP. ❏ Plot a supply curve from a linear function (eg, Qs = –30 + 20 P). ❏ Identify the slope of the supply curve as the slope of the supply function Qs = c + dP, that is d (the coefficient of P). ❏ Outline why, if the "c" term changes, there will be a shift of the supply curve. ❏ Outline how a change in "d" affects the steepness of the supply curve.

EQUILIBRIUM

Syllabus
❏ How equilibrium is produced
❏ Use diagrams to show how changes in the determinants of supply and demand result in a new market equilibrium.
HL only ❏ Calculate the equilibrium price and equilibrium quantity from linear demand and supply functions. ❏ Plot demand and supply curves from linear functions, and identify the equilibrium price and equilibrium quantity. ❏ State the quantity of excess demand or excess supply in the above diagrams.

ROLE OF THE PRICE MECHANISM

Syllabus
❏ Explain why scarcity necessitates choices that answer the "What to produce?" question.
❏ Explain why choice results in an opportunity cost.
❏ Explain, using diagrams, that price has a signalling function and an incentive function, which result in a reallocation of resources when prices change as a result of a change in demand or supply conditions.

MARKET EFFICIENCY

Syllabus
❏ Explain the concept of consumer surplus.
❏ Identify consumer surplus on a demand and supply diagram.
❏ Explain the concept of producer surplus.
❏ Identify producer surplus on a demand and supply diagram.
❏ Explain that the best allocation of resources from society's point of view is at competitive market equilibrium, where social (community) surplus (consumer surplus and producer surplus) is maximized (marginal benefit = marginal cost).

INDIRECT TAXES

Syllabus
❏ Explain why governments impose indirect (excise) taxes.
❏ Distinguish between specific and ad valorem taxes.
❏ Draw diagrams to show specific and ad valorem taxes, and analyse their impacts on market outcomes.
❏ Discuss the consequences of imposing an indirect tax on the stakeholders in a market, including consumers, producers and the government.

SUBSIDIES

Syllabus
❏ Explain why governments provide subsidies, and describe examples of subsidies.
❏ Draw a diagram to show a subsidy, and analyse the impacts of a subsidy on market outcomes.
❏ Discuss the consequences of providing a subsidy on the stakeholders in a market, including consumers, producers and the government.

PRICE CONTROLS

Syllabus
❏ Explain why governments impose price ceilings, and describe examples of price ceilings, including food price controls and rent controls.
❏ Draw a diagram to show a price ceiling, and analyse the impacts of a price ceiling on market outcomes.
❏ Examine the possible consequences of a price ceiling, including shortages, inefficient resource allocation, welfare impacts, underground parallel markets and non-price rationing mechanisms.
❏ Discuss the consequences of imposing a price ceiling on the stakeholders in a market, including consumers, producers and the government.
❏ Explain why governments impose price floors, and describe examples of price floors, including price support for agricultural products and minimum wages.
❏ Draw a diagram of a price floor, and analyse the impacts of a price floor on market outcomes.
❏ Examine the possible consequences of a price floor, including surpluses and government measures to dispose of the surpluses, inefficient resource allocation and welfare impacts.
❏ Discuss the consequences of imposing a price floor on the stakeholders in a market, including consumers, producers and the government.

PRICE ELASTICITY OF DEMAND (PED)

Syllabus
❏ Explain the concept of price elasticity of demand, understanding that it involves responsiveness of quantity demanded to a change in price, along a given demand curve.
❏ Calculate PED using the following equation. PED = percentage change in quantity demanded percentage change in price
❏ State that the PED value is treated as if it were positive although its mathematical value is usually negative

❏ Explain, using diagrams and PED values, the concepts of price elastic demand, price inelastic demand, unit elastic demand, perfectly elastic demand and perfectly inelastic demand.
❏ Explain the determinants of PED, including the number and closeness of substitutes, the degree of necessity, time and the proportion of income spent on the good.
❏ Calculate PED between two designated points on a demand curve using the PED equation above.
❏ Explain why PED varies along a straight line demand curve and is not represented by the slope of the demand curve.
❏ Examine the role of PED for firms in making decisions regarding price changes and their effect on total revenue.
❏ Explain why the PED for many primary commodities is relatively low and the PED for manufactured products is relatively high.
❏ Examine the significance of PED for government in relation to indirect taxes.

Cross price elasticity of demand (XED)

Syllabus
❏ Outline the concept of cross price elasticity of demand, understanding that it involves responsiveness of demand for one good (and hence a shifting demand curve) to a change in the price of another good.
❏ Calculate XED using the following equation. XED = percentage change in quantity demanded of good x percentage change in price of good y
❏ Show that substitute goods have a positive value of XED and complementary goods have a negative value of XED.
❏ Explain that the (absolute) value of XED depends on the closeness of the relationship between two goods.
❏ Examine the implications of XED for businesses if prices of substitutes or complements change.

Income elasticity of demand (YED)

Syllabus
❏ Outline the concept of income elasticity of demand, understanding that it involves responsiveness of demand (and hence a shifting demand curve) to a change in income.
❏ Calculate YED using the following equation. YED = percentage change in quantity demanded percentage change in income
❏ Show that normal goods have a positive value of YED and inferior goods have a negative value of YED.
❏ Distinguish, with reference to YED, between necessity (income inelastic) goods and luxury (income elastic) goods.
❏ Examine the implications for producers and for the economy of a relatively low YED for primary products, a relatively higher YED for manufactured products and an even higher YED for services.

Price elasticity of supply (PES)

Syllabus
❏ Explain the concept of price elasticity of supply, understanding that it involves responsiveness of quantity supplied to a change in price along a given supply curve.
❏ Calculate PES using the following equation. PES = percentage change in quantity supplied percentage change in price
❏ Explain, using diagrams and PES values, the concepts of elastic supply, inelastic supply, unit elastic supply, perfectly elastic supply and perfectly inelastic supply.
❏ Explain the determinants of PES, including time, mobility of factors of production, unused capacity and ability to store stocks.
❏ Explain why the PES for primary commodities is relatively low and the PES for manufactured products is relatively high.

The meaning of market failure

Syllabus

❏ Analyse the concept of market failure as a failure of the market to achieve allocative efficiency, resulting in an over- allocation of resources (over- provision of a good) or an under-allocation of resources (under-provision of a good)

Types of market failure

Syllabus
❏ Describe the concepts of marginal private benefits (MPB), marginal social benefits (MSB), marginal private costs (MPC) and marginal social costs (MSC).
❏ Describe the meaning of externalities as the failure of the market to achieve a social optimum where MSB = MSC.
❏ Explain, using diagrams and examples, the concepts of negative externalities of production and consumption, and the welfare loss associated with the production or consumption of a good or service.
❏ Explain that demerit goods are goods whose consumption creates external costs.
❏ Evaluate, using diagrams, the use of policy responses, including market-based policies (taxation and tradable permits), and government regulations, to the problem of negative externalities of production and consumption
❏ Explain, using diagrams and examples, the concepts of positive externalities of production and consumption, and the welfare loss associated with the production or consumption of a good or service.
❏ Explain that merit goods are goods whose consumption creates external benefits.
❏ Evaluate, using diagrams, the use of government responses, including subsidies, legislation, advertising to influence behaviour, and direct provision of goods and services.
❏ Using the concepts of rivalry and excludability,and providing examples, distinguish between public goods (non-rivalrous and non- excludable) and private goods (rivalrous and excludable).
❏ Explain, with reference to the free rider problem, how the lack of public goods indicates market failure.
❏ Discuss the implications of the direct provision of public goods by government.
❏ Describe, using examples, common access resources.

❏ Describe sustainability.
❏ Explain that the lack of a pricing mechanism for common access resources means that these goods may be overused/depleted/ degraded as a result of activities of producers and consumers who do not pay for the resources that they use, and that this poses a threat to sustainability.
❏ Explain, using negative externalities diagrams, that economic activity requiring the use of fossil fuels to satisfy demand poses a threat to sustainability.
❏ Explain that the existence of poverty in economically less developed countries creates negative externalities through over-exploitation of land for agriculture, and that this poses a threat to sustainability.
❏ Evaluate, using diagrams, possible government responses to threats to sustainability, including legislation, carbon taxes, cap and trade schemes, and funding for clean technologies.
❏ Explain, using examples, that government responses to threats to sustainability are limited by the global nature of the problems and the lack of ownership of common access resources, and that effective responses require international cooperation.

The circular flow of income model

Syllabus
❏ Describe, using a diagram, the circular flow of income between households and firms in a closed economy with no government.
❏ Identify the four factors of production and their respective payments (rent, wages, interest and profit) and explain that these constitute the income flow in the model.
❏ Outline that the income flow is numerically equivalent to the expenditure flow and the value of output flow.
❏ Describe, using a diagram, the circular flow of income in an open economy with government and financial markets, referring to leakages/ withdrawals (savings, taxes and import expenditure) and injections (investment, government expenditure and export revenue).
❏ Explain how the size of the circular flow will change depending on the relative size of injections and leakages.

Macroeconomic goals:

Define:

Variable	Macroeconomic Objective	Measurement
Economic growth	A steady rate of increase of national output	GDP
Employment	A low level of unemployment	Employment rate
Price stability	A low and stable rate of inflation	Inflation rate
External stability	A favorable balance of payments position	Balance of payments data
Income distribution	An equitable distribution of income	Lorenz curve/ Gini-coefficient

Measures of economic activity: gross domestic product (GDP), and gross national product (GNP) or gross national income (GNI)

Syllabus
❏ Distinguish between GDP and GNP/GNI as measures of economic activity.
❏ Distinguish between the nominal value of GDP and GNP/GNI and the real value of GDP and GNP/GNI.
❏ Distinguish between total GDP and GNP/GNI and per capita GDP and GNP/GNI.
❏ Examine the output approach, the income approach and the expenditure approach when measuring national income.
❏ Evaluate the use of national income statistics, including their use for making comparisons over time, their use for making comparisons between countries and their use for making conclusions about standards of living.
❏ Explain the meaning and significance of “green GDP”, a measure of GDP that accounts for environmental destruction.

The business cycle

Syllabus
❑ Short-term fluctuations and long-term trend
❑ Explain, using a business cycle diagram, that economies typically tend to go through a cyclical pattern characterized by the phases of the business cycle.
❑ Explain the long-term growth trend in the business cycle diagram as the potential output of the economy.
❑ Distinguish between a decrease in GDP and a decrease in GDP growth.

Aggregate demand (AD)

Syllabus
❑ Distinguish between the microeconomic concept of demand for a product and the macroeconomic concept of aggregate demand.
❑ Construct an aggregate demand curve.
❑ Explain why the AD curve has a negative slope.
❑ The components of AD ❑ Describe consumption, investment, government spending and net exports as the components of aggregate demand.
❑ The determinants of AD or causes of shifts in the AD curve
❑ Explain how the AD curve can be shifted by changes in consumption due to factors including changes in consumer confidence, interest rates, wealth, personal income taxes (and hence disposable income) and level of household indebtedness.
❑ Explain how the AD curve can be shifted by changes in investment due to factors including interest rates, business confidence, technology, business taxes and the level of corporate indebtedness.
❑ Explain how the AD curve can be shifted by changes in government spending due to factors including political and economic priorities.
❑ Explain how the AD curve can be shifted by changes in net exports due to factors including the income of trading partners, exchange rates and changes in the level of protectionism.

Aggregate supply (AS)

Syllabus
❏ Describe the term aggregate supply.
❏ Explain, using a diagram, why the short-run aggregate supply curve (SRAS curve) is upward sloping.
❏ Explain, using a diagram, how the AS curve in the short run (SRAS) can shift due to factors including changes in resource prices, changes in business taxes and subsidies and supply shocks.
❏ Alternative views of aggregate supply ❏ Explain, using a diagram, that the monetarist/new classical model of the long-run aggregate supply curve (LRAS) is vertical at the level of potential output (full employment output) because aggregate supply in the long run is independent of the price level.
❏ Explain, using a diagram, the determination of short-run equilibrium, using the SRAS curve.
❏ Examine, using diagrams, the impacts of changes in short- run equilibrium.

Equilibrium in the monetarist/new classical model

Syllabus
❏ Explain, using a diagram, the determination of long-run equilibrium, indicating that long-run equilibrium occurs at the full employment level of output.
❏ Explain why, in the monetarist/new classical approach, while there may be short-term fluctuations in output, the economy will always return to the full employment level of output in the long run.
❏ Examine, using diagrams, the impacts of changes in the long-run equilibrium.

Equilibrium in the Keynesian model

Syllabus
❏ Explain, using the Keynesian AD/AS diagram, that the economy may be in equilibrium at any level of real output where AD intersects AS.

❏ Explain, using a diagram, that if the economy is in equilibrium at a level of real output below the full employment level of output, then there is a deflationary (recessionary) gap.
❏ Discuss why, in contrast to the monetarist/new classical model, the economy can remain stuck in a deflationary (recessionary) gap in the Keynesian model.
❏ Explain, using a diagram, that if AD increases in the vertical section of the AS curve, then there is an inflationary gap.
❏ Discuss why, in contrast to the monetarist/new classical model, increases in aggregate demand in the Keynesian AD/AS model need not be inflationary, unless the economy is operating close to, or at, the level of full employment.

Economic growth

Syllabus
❏ The meaning of economic growth
❏ Define economic growth as an increase in real GDP.

Causes of economic growth

Syllabus
❏ Describe, using a production possibilities curve (PPC) diagram, economic growth as an increase in actual output caused by factors including a reduction in unemployment and increases in productive efficiency, leading to a movement of a point inside the PPC to a point closer to the PPC.
❏ Describe, using a PPC diagram, economic growth as an increase in production possibilities caused by factors including increases in the quantity and quality of resources, leading to outward PPC shifts.
❏ Describe, using an LRAS diagram, economic growth as an increase in potential output caused by factors including increases in the quantity and quality of resources, leading to a rightward shift of the LRAS curve.

❑ Explain the importance of investment for economic growth, referring to investment in physical capital, human capital and natural capital.
❑ Explain the importance of improved productivity for economic growth.
❑ Discuss the possible consequences of economic growth, including the possible impacts on living standards, unemployment, inflation, the distribution of income, the current account of the balance of payments, and sustainability.

Equity and the distribution of income

Syllabus
❑ Explain the difference between equity in the distribution of income and equality in the distribution of income.
❑ Explain that due to unequal ownership of factors of production, the market system may not result in an equitable distribution of income.
❑ Analyse data on relative income shares of given percentages of the population, including deciles and quintiles.
❑ Draw a Lorenz curve and explain its significance.
❑ Explain how the Gini coefficient is derived and interpreted.
❑ Distinguish between absolute poverty and relative poverty.
❑ Explain possible causes of poverty, including low incomes, unemployment and lack of human capital.
❑ Explain possible consequences of poverty, including low living standards, and lack of access to health care and education.
❑ Distinguish between direct and indirect taxes, providing examples of each, and explain that direct taxes may be used as a mechanism to redistribute income.
❑ Distinguish between progressive, regressive and proportional taxation, providing examples of each.
❑ Explain that governments undertake expenditures to provide directly, or to subsidize, a variety of socially desirable goods and services (including health care services, education, and infrastructure that includes sanitation and clean water supplies), thereby making them available to those on low incomes.

❏ Explain the term transfer payments, and provide examples, including old age pensions, unemployment benefits and child allowances.
❏ Evaluate government policies to promote equity (taxation, government expenditure and transfer payments) in terms of their potential positive or negative effects on efficiency in the allocation of resources.

Low Unemployment

Syllabus
❏ Define the term unemployment.
❏ Explain how the unemployment rate is calculated.
❏ Explain the difficulties in measuring unemployment, including the existence of hidden unemployment, the existence of underemployment, and the fact that it is an average and therefore ignores regional, ethnic, age and gender disparities.
❏ Discuss possible economic consequences of unemployment, including ❏ a loss of GDP, loss of tax revenue, increased cost of unemployment benefits, loss of income for individuals, and greater disparities in the distribution of income.
❏ Discuss possible personal and social consequences of unemployment, including increased crime rates, increased stress levels, increased indebtedness, homelessness and family breakdown.
❏ Describe, using examples, the meaning of frictional, structural, seasonal and cyclical (demand-deficient) unemployment.
❏ Distinguish between ❏ the causes of frictional, structural, seasonal and cyclical (demand-deficient) unemployment.
❏ Explain, using a diagram, that cyclical unemployment is caused by a fall in aggregate demand.
❏ Explain, using a diagram, that structural unemployment is caused by changes in the demand for particular labour skills, changes in the geographical location of industries, and labour market rigidities.
❏ Evaluate government policies to deal with the different types of unemployment.

Inflation

Syllabus
❏ Distinguish between inflation, disinflation and deflation.
❏ Explain that inflation and deflation are typically measured by calculating a consumer price index (CPI), which measures the change in prices of a basket of goods and services consumed by the average household.
❏ Explain that different income earners may experience a different rate of inflation when their pattern of consumption is not accurately reflected by the CPI.
❏ Explain that inflation figures may not accurately reflect changes in consumption patterns and the quality of the products purchased.
❏ Explain that economists measure a core/underlying rate of inflation to eliminate the effect of sudden swings in the prices of food and oil, for example.
❏ Explain that a producer price index measuring changes in the prices of factors of production may be useful in predicting future inflation.
❏ Discuss the possible consequences of a high inflation rate, including greater uncertainty, redistributive effects, less saving, and the damage to export competitiveness.
❏ Discuss the possible consequences of deflation, including high levels of cyclical unemployment and bankruptcies.
❏ Explain, using a diagram, that demand-pull inflation is caused by changes in the determinants of AD, resulting in an increase in AD.
❏ Explain, using a diagram, that cost-push inflation is caused by an increase in the costs of factors of production, resulting in a decrease in SRAS.
❏ Evaluate government policies to deal with the different types of inflation.
❏ Discuss, using a short-run Phillips curve diagram, the view that there is a possible trade-off between the unemployment rate and the inflation rate in the short run.
❏ Explain, using a diagram, that the short-run Phillips curve may shift outwards, resulting in stagflation (caused by a decrease in SRAS due to factors including supply shocks).
❏ Discuss, using a diagram, the view that there is a long- run Phillips curve that is vertical at the natural rate of unemployment and therefore there is no trade-off between the unemployment rate and the inflation rate in the long run.

❏ Explain that the natural rate of unemployment is the rate of unemployment that exists when the economy is producing at the full employment level of output.

Fiscal policy

Syllabus
❏ The government budget - Sources of government revenue
❏ Explain that the government earns revenue primarily from taxes (direct and indirect), as well as from the sale of goods and services and the sale of state-owned (government- owned) enterprises.
❏ Explain that government spending can be classified into current expenditures, capital expenditures and transfer payments, providing examples of each.
❏ Distinguish between a budget deficit, a budget surplus and a balanced budget.
❏ Explain the relationship between budget deficits/ surpluses and the public (government) debt.
❏ Explain how changes in the level of government expenditure and/or taxes can influence the level of aggregate demand in an economy.
❏ Describe the mechanism through which expansionary fiscal policy can help an economy close a deflationary (recessionary) gap.
❏ Construct a diagram to show the potential effects of expansionary fiscal policy, outlining the importance of the shape of the aggregate supply curve.
❏ Describe the mechanism through which contractionary fiscal policy can help an economy close an inflationary gap.
❏ Construct a diagram to show the potential effects of contractionary fiscal policy, outlining the importance of the shape of the aggregate supply curve.
❏ Explain how factors including the progressive tax system and unemployment benefits, which are influenced by the level of economic activity and national income, automatically help stabilize short-term fluctuations.
❏ Explain that fiscal policy can be used to promote long-term economic growth (increases in potential output) indirectly by creating an economic environment that is favourable to private investment, and directly through government spending on

physical capital goods and human capital formation, as well as provision of incentives for firms to invest.
❏ Evaluate the effectiveness of fiscal policy through consideration of factors including the ability to target sectors of the economy, the direct impact on aggregate demand, the effectiveness of promoting economic activity in a recession, time lags, political constraints, crowding out, and the inability to deal with supply-side causes of instability.

Monetary policy

Syllabus
❏ Interest rate determination and the role of a central bank
❏ Describe the role of central banks as regulators of commercial banks and bankers to governments.
❏ Explain that central banks are usually made responsible for interest rates and exchange rates in order to achieve macroeconomic objectives.
❏ Explain, using a demand and supply of money diagram, how equilibrium interest rates are determined, outlining the role of the central bank in influencing the supply of money.

Supply side policies

Syllabus
❏ Explain that supply-side policies aim at positively affecting the production side of an economy by improving the institutional framework and the capacity to produce (that is, by changing the quantity and/or quality of factors of production).
❏ State that supply-side policies may be market-based or interventionist, and that in either case they aim to shift the LRAS curve to the right, achieving growth in potential output.
❏ Explain how investment in education and training will raise the levels of human capital and have a short-term impact on aggregate demand, but more importantly will increase LRAS.

❏ Explain how policies that encourage research and development will have a short-term impact on aggregate demand, but more importantly will result in new technologies and will increase LRAS.
❏ Explain how increased and improved infrastructure will have a short-term impact on aggregate demand, but more importantly will increase LRAS.
❏ Explain that targeting specific industries through policies including tax cuts, tax allowances and subsidized lending promotes growth in key areas of the economy and will have a short-term impact on aggregate demand but, more importantly, will increase LRAS.
❏ Explain how factors including deregulation, privatization, trade liberalization and anti-monopoly regulation are used to encourage competition.
❏ Explain how factors including reducing the power of labour unions, reducing unemployment benefits and abolishing minimum wages are used to make the labour market more flexible (more responsive to supply and demand).
❏ Explain how factors including personal income tax cuts are used to increase the incentive to work, and how cuts in business tax and capital gains tax are used to increase the incentive to invest.
❏ Evaluate the effectiveness of supply-side policies through consideration of factors including time lags, the ability to create employment, the ability to reduce inflationary pressure, the impact on economic growth, the impact on the government budget, the effect on equity, and the effect on the environment.