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# Consumers in the Market Economy

## Multiple Choice Answers

1	B	6	B	11	B
2	D	7	C	12	C
3	A	8	B	13	A
4	D	9	B	14	C
5	B	10	A	15	C

## Short Answer Questions

### Question 1

- (a) According to the life cycle theory of consumption, individuals tend to smooth out their consumption and change their level of savings with age. In a person's youth they borrow to finance consumption. In the working years, a person conducts most of their savings, before consuming out of savings for retirement.
- (b) Consumer sovereignty influences production in the economy through consumer demand. Consumers will demand products which they desire, sending a signal to firms that if they produce this product it will be sold. Consumers decide what to produce. In addition, consumers will determine how much is produced through the level of demand for a particular product. The more consumers there are demanding a product, the more that will be produced.
- (c) A correct answer may include any two of the following:
- Marketing can create its own trends through a powerful media presence, or through intrusive techniques to create a stronger demand. Whilst marketing can raise awareness of goods and services, it can also prevent consumers making an informed decision.
  - Misleading or deceptive conduct by firms can result in consumers purchasing goods and services based on false manufacturer claims about the product. This entices consumers to purchase goods or services which would never be sold otherwise.
  - Planned obsolescence may result in consumers purchasing goods and services which may force consumers to make more purchases in the future as the product goes out of date. In this way consumers may be forced to purchase many more products than they originally intended.
  - Monopoly behaviour removes the market power from consumers, since firms will control all supply of the product, and will be able to set prices. With no competitors, consumers will respond to firms, rather than the firms responding to consumers.

**Question 2**

- (a) Income is the flow of money and other benefits that individuals and households receive for their contribution to the production process, or a direct payment from the government.
- (b) Labour
- (c) If the unemployment rate were to fall, there would be a greater proportion of household income coming from wages and possibly a decrease in the proportion of income received as welfare payments, as fewer people would be in receipt of unemployment benefits.
- (d) Social welfare payments aim to provide a minimum income safety net to ensure the most disadvantaged citizens are able to maintain a minimum standard of living. During times of economic downturn, the government can also use welfare payments to increase income in the economy and stimulate economic growth.
- (e) An individual is able to either spend or save their income. An increase in wages will increase income, and increase in the level of savings and spending in the economy. The additional increase in consumption will be determined by the marginal propensity to consume, and the additional increase in savings will be determined by the marginal propensity to save.
- (f) The average propensity to consume is the proportion of an individual's total income that is spent on consumption, whereas the marginal propensity to consume is the proportion of each additional dollar of income that goes to consumption.

**Question 3**

- (a) Consumers communicate their preference for digital cameras over traditional cameras by increasing their demand and number of purchases of digital cameras and reducing the number of traditional cameras they purchase.
- (b) In response to a decrease in demand for rolls of film, the firm may attempt to attract the remaining consumers away from other firms by reducing their price, maintaining a presence in the market. Alternatively, the firm can adapt to the changed business environment and develop a new product (such as memory cards) to cater for the growing consumer demand.
- (c) An individual's level of income will influence their decision to buy a given good or service. Those with higher incomes are better able afford more products, or products which are of higher quality. Another factor is the price of other goods, particularly substitute and complement goods. If the price of a complement for cars (e.g. petrol) was to increase it may deter a consumer from purchasing cars themselves. Finally, consumer tastes and preferences will play a part in an individual's decision of whether to buy a given good or service, as consumers will purchase goods and services that give them the highest level of personal utility.