4

Market Forces

Have you ever bought an item that was marked down more than 50 percent? Why did you get such a good deal? Was it worth it—even at 50 percent off?

Marketing Terms

- scarcity
- traditional economy
- command economy
- market economy
- mixed economy
- demand
- supply
- market demand
- market supply
- law of demand
- law of supply
- profit motive
- productivity
- competition

Learning Goals

- describe the three types of economic systems
- describe the three main features of a market economy
- identify the three main market forces
- explain the effect that price has on supply and demand, and that supply and demand have on price
- identify three factors that cause changes in demand
- describe three ways a business can increase profits
- explain the role of the consumer in determining which products get produced

In Chapter 2, you learned about economic needs and wants. These are needs and wants that can be satisfied by buying something.

But can you afford everything you need and want? No. Why not? You do not have enough resources to meet all your needs and wants. Your resources include time, money, and your ability to earn money. You do not have enough resources because of a problem called scarcity. **Scarcity** is a condition in which there are not enough resources to meet needs, 4-1.

Like people, countries also have a problem with scarcity. Scarce resources limit the quantity of products (goods, services, and ideas) a nation can produce. The problem of scarcity leads to three questions:

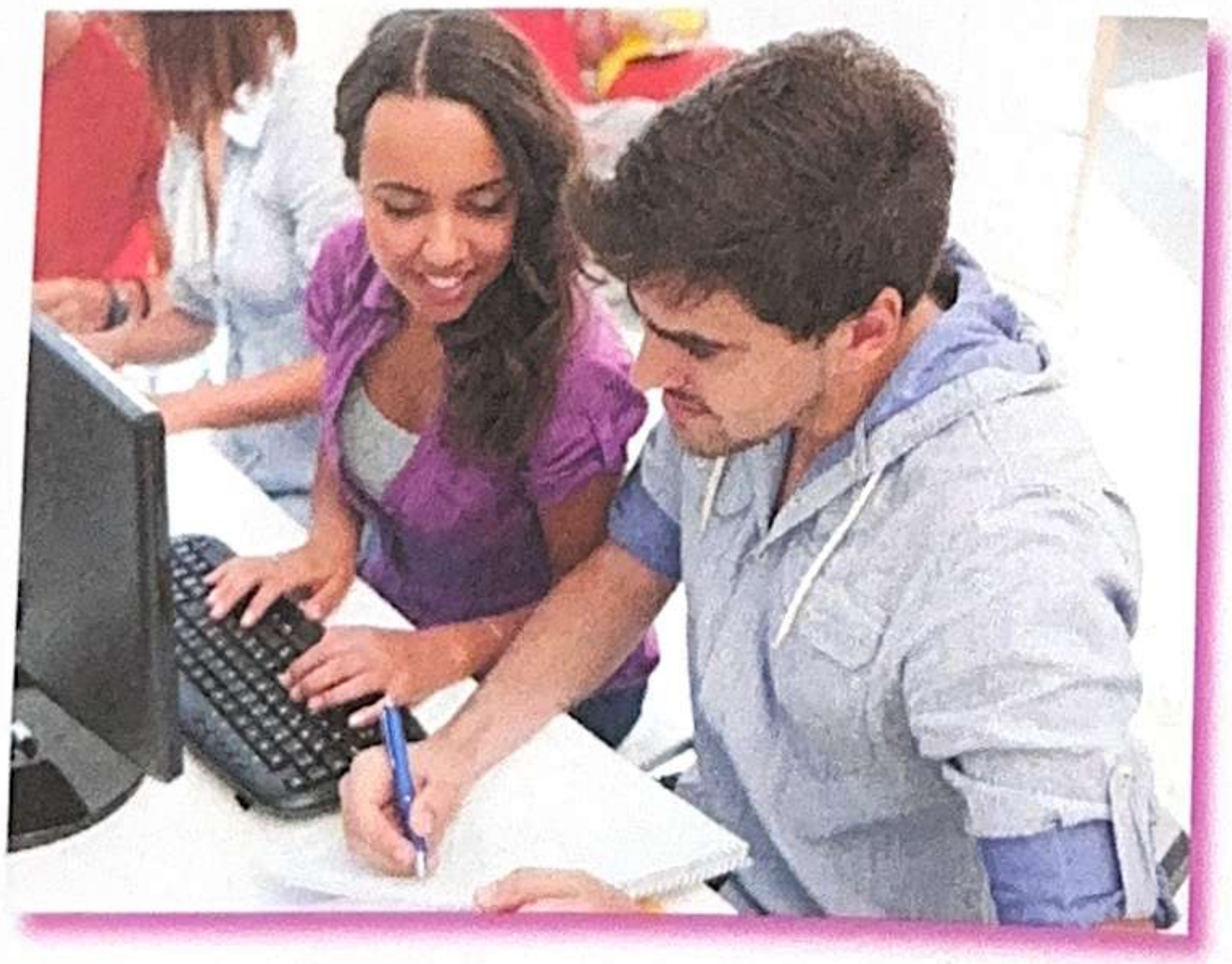
- What should we produce?
- How should we produce it?
- Who should get the products?

Connect...

Your family is like a small country. How do the three economic questions get answered in your family?

Types of Economic Systems

Economists classify types of national economic systems based on who answers those three basic economic questions. There are three basic types of economies: traditional, command, and market.



4-1

Countries, groups, and individuals struggle with scarcity of time and resources. For example, if your school does not have enough computers for everyone, you may have to share or wait your turn.

People in traditional economies perform economic and social activities the way they have always been done. They may use simple or animal-powered machines. Often, the elders of the society preserve the traditions and answer questions for the society. Following tradition is seen as a way of keeping the society safe and healthy. In a **traditional economy**, the economic questions are answered by the elders based on the society's traditions, 4-2. Some Inuit who live in the remote regions of Canada's North, for example, still maintain a traditional economy.

In a **command economy**, the national government answers the economic questions. The government decides what, how, and for whom. For example, the government decides how much land will be used to produce wheat. It decides how many resources will go to the military and how many will go to produce consumer goods. It decides who will be farmers and who will be engineers. It decides who gets the products.

One of the goals of a command economy is to make sure that everyone in the country shares the limited resources. In a command economy, the government makes sure that everyone who wants to work gets a job. The government also makes sure that everyone gets an education, medical care, and a place to live. Cuba, North Korea, and the former Soviet Union are examples of command economies.

Connect...

Do you know anyone (or do you know about anyone) who has lived in a command economy? What was life like for that person?

In a pure **market economy**, individuals answer the economic questions. Individuals decide what to produce, how to produce it, and who gets the products. Individuals control distribution because each individual is free to buy whatever he or she wants, based on price and ability to pay, 4-3. Canada, Australia, New Zealand, the United States,

4-2

Traditional economies are based on the society's traditions. Such economies developed early in human history and are based on early technology.

and many countries of South America and Europe are examples of market economies.

Mixed Economies

However, there are no pure command or pure market economies. Most modern economies are mixed economies. In a **mixed economy**, both the government and individuals are involved in making economic decisions. It would be fair to say that Canada and the United States have mixed economies. Canadian citizens want the government to take an active role in keeping the government stable and helping people in need. This means that the government regulates business to some degree. Government ensures that businesses produce quality products and pay workers a minimum wage. Businesses must meet environmental standards and protect the health and safety of workers. The government also protects Canadians through employment insurance, old age benefits, maternity leave, and universal health care.

4-3

A market economy is often called a consumer economy. Consumers influence the economy through what they buy and how much they buy.

Market Economy Features

Three of the main features of a market economy are (1) private property, (2) economic freedom, and (3) market forces.

Private Property

A market economy is based on the right of individuals to own land and make their own products. Ownership means that each person has the right to do whatever he or she wants with his or her property (as long as the action is legal). For example, a person can use his or her land to build a house, run a farm, graze cattle, build a basketball factory, or sell it to someone else. By contrast, in a command economy, the national government owns all the land and decides how it is to be used. In a traditional economy, land and its resources may be shared by the whole community. Indigenous peoples usually do not say that they "own" the land, but that it was "entrusted" to them.

Economic Freedom

In a market economy, individuals make their own economic decisions. In other words, individuals decide what to buy, how to use it, and what to sell. In a command economy, the central government owns and runs all businesses; individuals are not permitted to start businesses.

In a market economy, individuals control their own labour. Each person is free to decide what work he or she will do, 4-4. Individuals may choose which companies they will work for. In a command economy, the government controls the labour of the

4-4

In a market economy, each individual decides what type of work he or she will do. This woman is a laboratory technician.

individual. The government decides which citizens will do which jobs. People in a command economy are not free to choose their work or quit their jobs. However, the government does make sure that everyone who wants to work has a job.

Connect...

From your experience, describe an example of one of the features of a market economy. If Canada were a command economy, how would that example be different?

Market Forces

Market economies, even mixed ones, are affected by market forces. Even though individuals are free to make economic decisions, market forces influence their decisions. The three major market forces are supply and demand, profit, and competition. A market economy is often called a free market economy because market forces are free to influence economic decisions. You will explore these forces in the next section.

Market Forces at Work

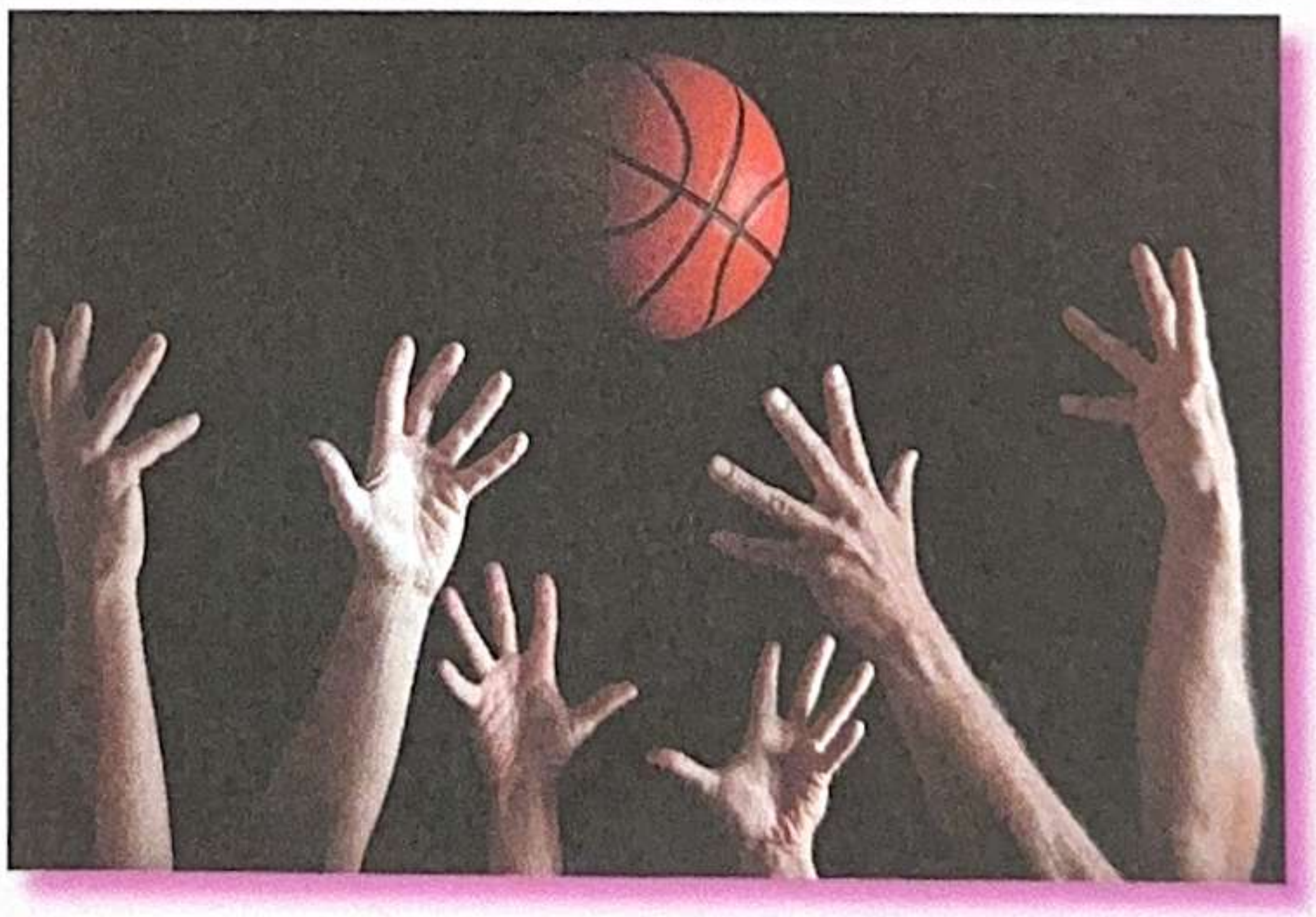
Here is a simplified example of how market forces work. Imagine the market for basketballs and soccer balls. For this example, all the balls are of the same good quality. In this market, the supply of basketballs equals the supply of soccer balls. In this market, the price of the balls starts out the same.

Suppose basketball becomes more popular than soccer. The demand for basketballs rises, 4-5. Customers buy the basketballs, and the supply of basketballs goes down. Customers compete for the remaining basketballs. As the demand rises and the supply falls, the price of the basketballs goes up. The customers who can afford the higher prices get the basketballs. The basketball sellers are making lots of money.

Meanwhile, no one is buying soccer balls. The demand for soccer balls is low, but the supply is high. In order to try to get the soccer balls to sell, the soccer ball sellers lower the price. Because of the lower prices, more soccer balls sell. However, the long-term demand for soccer balls does not increase because the people who bought the soccer balls would really rather be playing basketball. The soccer ball sellers are losing money because they had to lower prices to sell the soccer balls.

Meanwhile, more and more people are buying basketballs. The profit in the basketball business goes up. The basketball sellers hire more people to make basketballs. New companies enter the basketball market. Now there are more companies making basketballs. These companies compete with each other for customers. They look for ways to better meet customers' needs. They also start researching faster and better ways to make the basketballs. The quality of basketballs improves.

Meanwhile, as the price of soccer balls falls, the profit in the soccer ball business falls. Fewer and fewer soccer balls are sold. Soccer ball businesses let workers go and close



4-5

As the demand for basketballs rises, more customers buy basketballs; and the supply falls.

factories. Fewer soccer balls are produced. The people who produced soccer balls start working in the basketball business.

The net result is what the customers wanted: more basketballs and fewer soccer balls. In turn, if the customers change their minds, and soccer becomes more popular than basketball, the same process will work again. The result will be more soccer balls.

There are many economic processes going on in the preceding example. The following sections will examine the three main market forces in more detail: (1) supply and demand, (2) profit, and (3) competition.

Connect...

Identify places in the example where the forces of supply and demand, profit, and competition are at work.

Supply and Demand

Demand is the quantity of a specific product that a buyer is able and willing to buy at a certain price, usually at a particular time and place. (Remember that *price* is the amount of money exchanged for a product.) **Supply** is the quantity of a specific product that the supplier is willing to supply at a certain price.

There are two ways to think about supply and demand: individual and market. Individual demand is the quantity of a product demanded by an individual consumer. Individual supply is the quantity of a product supplied by an individual supplier. However, when we talk about supply and demand as forces in the economy, we are referring to market supply and market demand. **Market demand** is the sum of all the individual demands for a specific product, for a specific time period. **Market supply** is the sum of all the individual suppliers' supply of a specific product, for a specific time period, 4-6. From this point on, when we refer to supply and demand, we are referring to market supply and market demand.

4-6

Market supply is the sum of all individual suppliers' supply of a specific product, not the supply provided by just one supplier.

Effect of Price on Supply and Demand

The laws of supply and demand tell us what happens to supply and to demand as prices change. These laws apply to situations where other factors do not change. Other factors include marketing campaigns, the economic situation, and social trends. When

Effect of Price on Supply and Demand

Price Level	Effect on Demand	Effect on Supply
High	Falls	Rises
Low	Rises	Falls

4-7

The price level of a product will affect the demand and supply.

these other factors do not change, we call it a constant environment.

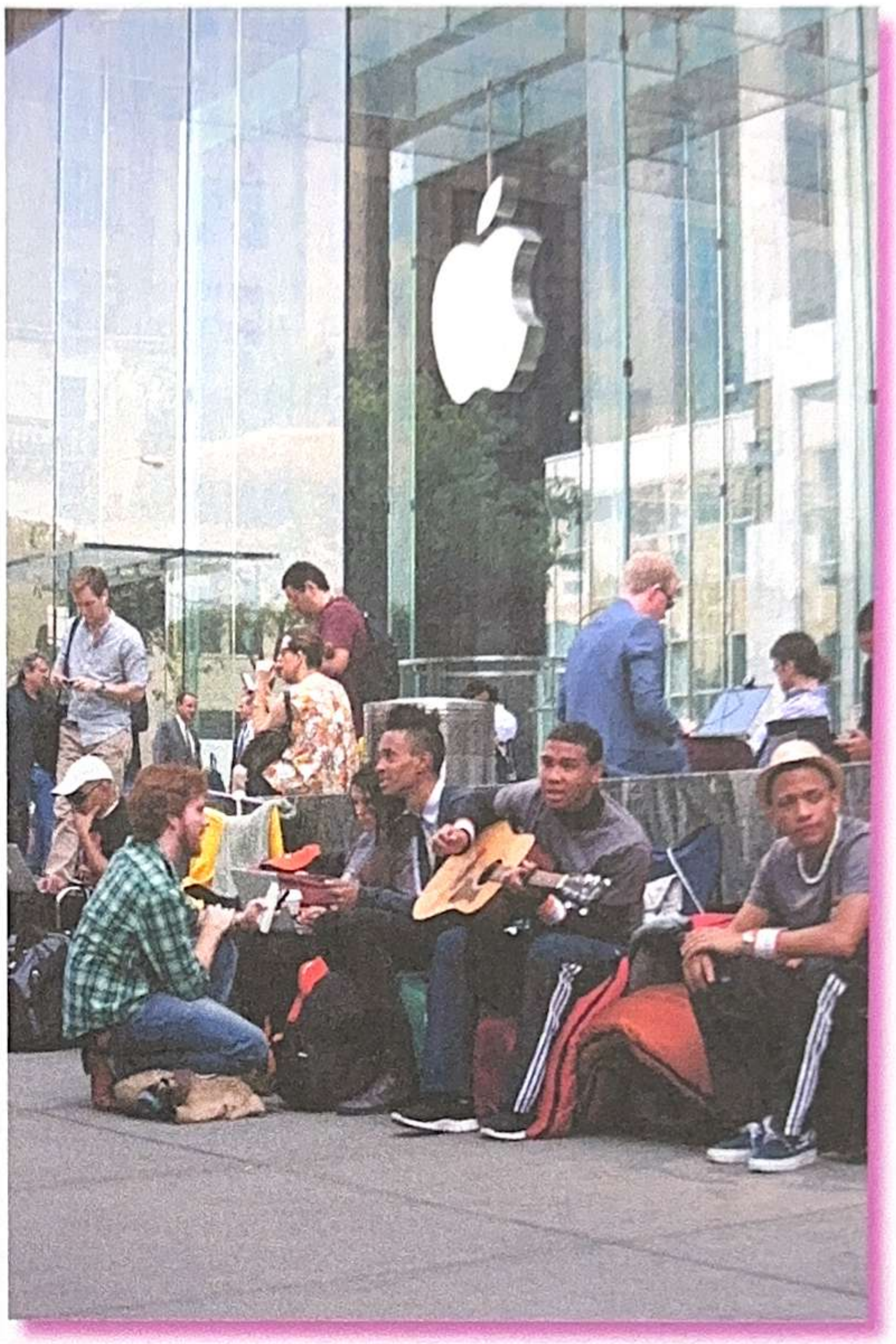
In a constant environment, the **law of demand** says that when prices fall, demand will rise. That is, consumers will buy more when prices are low. Conversely, when prices rise, demand will fall. That is, consumers will buy less when prices are high.

In a constant environment, the **law of supply** says that when prices are high, supply will rise. That is, suppliers are willing to supply more when the price of the product is high. Conversely, when prices fall, supply will fall. That is, suppliers are willing to supply less when prices are low, 4-7.

Here is how the laws of supply and demand worked in our basketball example. The soccer ball suppliers wanted to cause a rise in demand. Therefore, they lowered the price of the soccer balls. When they lowered the price of the soccer balls, more consumers bought them. Also, when the prices of basketballs rose, it encouraged the suppliers to supply more basketballs.

Connect...

Has a drop in price ever changed your individual demand for a product? Give an example.



4-8

Marketing, changes in the economy, and social trends can all change the demand for goods and services. Lining up for the latest Apple product, for example, became a phenomenon in the early twenty-first century.

Changes in Demand

The environment is rarely constant. Changes in marketing campaigns, the economic situation, and social trends cause changes in demand, 4-8. In fact, one of the major roles of marketing is to increase demand. Marketing increases demand through promotion. For example, advertisements for a certain toy during the December gift-giving season can result in increased demand for the toy.

The condition of the economy can also increase or decrease demand. When the economy is doing well, consumers have plenty of money. As a result, the demand for many products increases when the economy is doing well. When the economy is doing poorly, consumers have less money. As a result, the demand for many products decreases when the economy is doing poorly.

Changes in society also affect demand. One of the major changes during the twenty-first century has been an increase in the number of single-person households. By 2011, there were more people living alone in Canada than there were couples with children. This change in society resulted in an increased demand for many items, including pre-packaged, single-portion convenience food.

In our basketball example, a social trend caused the increase in demand for basketballs. For a variety of social reasons, including the phenomenal success of superstars such as Michael Jordan, Kobe Bryant, and Chris Bosh, basketball became as popular as soccer.

The Effect of Supply and Demand on Price

Price is one of the Four Ps. Many factors affect how marketers set price. One of the main factors that affects price is the interaction of supply and demand. When demand is low, but supply is high, marketers lower prices. When marketers lower price, demand usually increases and more of the product is sold.

When demand is high, but supply is low, marketers can raise prices. The buyers will compete for the few products and are willing to pay higher prices, 4-9.

In our basketball example, the basketball sellers raised prices when demand was high, but supply was low. Conversely, when the soccer ball sellers had large supplies of soccer balls and low demand, they lowered the price of the soccer balls.

Effect of Supply and Demand on Price

Level of Demand	Level of Supply	Effect on Price
High	Low	Rises
High	High	No effect
Low	High	Falls
Low	Low	No effect

4-9

The level of supply and the level of demand will affect prices.

Connect...

Think of a situation in which high demand and low supply resulted in higher prices. Describe the situation.

Profit

Profit is another powerful force in a market economy. *Profit* is the money left over after all business expenses and costs are paid.

Profit = Sales – Expenses and Costs

Suppose you own a basketball factory. Last year, your sales totaled $380 000. In order to make those sales, you had expenses and costs of $345 000. Your expenses and costs included rent, utilities, raw materials, machinery, machinery maintenance, salaries, and marketing. Your profit is $35 000, 4-10.

In a pure market economy, business owners keep the profits. In a pure command economy, the national government gets the profits. In a mixed economy, business owners keep most of the profits. Business owners pay a portion of their profits to the government in the form of taxes.

Calculating Simple Profit

Formula

Profit = Sales – Expenses and Costs

Data

Sales = $380 000

Expenses and Costs = $345 000

Profit = $380 000 – $345 000

Profit = $35 000

4-10

Profit is the money left over after all business expenses and costs are paid.

The **profit motive** is the drive to earn more profit. In a command economy, the profit motive does not operate because the citizens do not get to keep the profits. In a market or mixed economy, the chance to keep profits motivates people to start new businesses, expand existing businesses, and develop ways to increase profits. In our basketball example, as profits in the basketball business increased, more people entered the basketball business.

Businesses are always looking for ways to increase profits. Three of the main ways to increase profits are to (1) decrease costs or expenses, (2) increase productivity, or (3) increase sales.

Decrease Costs or Expenses

Think about the basketball factory. If costs or expenses could be lowered, profits would increase. On the other hand, if costs or expenses rise, profits decrease. If costs or expenses rise too much, the business might lose money, 4-11.

A business owner looks for ways to decrease costs and expenses by studying what money is spent on in the business. Costs and expenses include rent, raw materials, and machinery maintenance. The business could look for a place where rent is lower, less expensive raw materials, and less expensive ways to maintain machinery.

Increase Productivity

Another way to increase profits is to increase productivity. **Productivity** is the amount of product a worker produces per hour (product/hour). For example, in the basketball factory, a worker might produce ten basketballs per hour. An increase in productivity would occur if a worker could complete twenty basketballs in an hour. Productivity would double. As a result, output doubles. That is, the factory produces twice as many basketballs.

Effect of Costs and Expenses on Profit

Situation	Sales	– Costs and Expenses	= Profits
Original	$380000	– $345000	= $35000
Expenses down	$380000	– $300000	= $80000
Expenses up	$380000	– $375000	= $ 5000
Expenses up a lot	$380000	– $400000	= –$20000 (loss)

4-11

When expenses go down, profit goes up. When expenses go up, profits go down.

Costs would go up because there would be twice as many raw materials in twenty basketballs; but costs would not double. The company now has twice as many basketballs to sell. Sales go up and profits go up. An increase in productivity can greatly increase profits, 4-12. An increase in productivity means that each product costs less to make. The business could easily lower the prices of the basketballs and still make a good profit.

How can a business increase productivity? There are two main ways: increase efficiency and use new technology. One of the ways to increase efficiency is through specialization. Henry Ford used the

Sample Effect of Productivity on Profit

Situation	Sales	– Expenses and Costs	= Profit
Original	$380000	– $345000	= $ 35000
Productivity and sales double	$760000	– $545000	= $215000

4-12

When productivity goes up, sales and profits go up.

assembly line and specialization to increase efficiency in car manufacturing.

The following is a simplified example. Before the assembly line, each worker assembled one car. If there were ten workers, each worker assembled one car in a day. Ten workers produced ten cars. Using the assembly line, each worker would specialize in one-tenth of the car assembly. The ten workers would each assemble their specialty. Specialization speeds up production and makes it more efficient. Now the ten workers could produce thirty cars in a day.

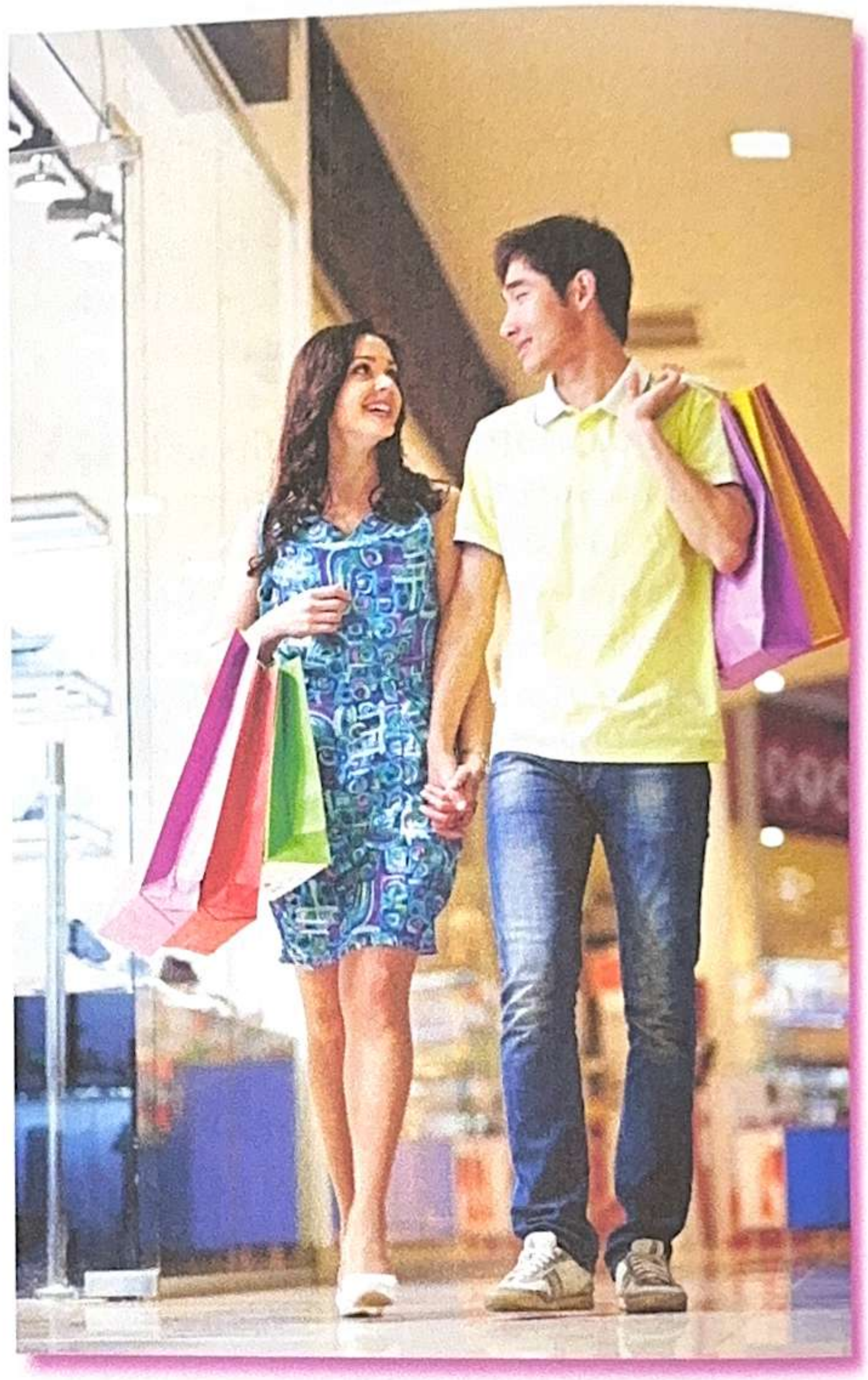
New technology is another way to increase productivity. Toward the end of the twentieth century, productivity in North America took a leap forward. The reason was the widespread use of computers and digital technology. This technology enabled workers to perform various jobs much faster than ever before.

Increase Sales

In our basketball example, forces outside the basketball business led to an increase in demand for basketballs. Often, however, the business itself can do a great deal to increase sales. One of the major roles of marketing is to increase sales. Marketing can develop programs to encourage current customers to buy more, 4-13. For example, rewards for frequent purchases encourage more purchases. Marketing can also develop plans to attract new customers. Advertising campaigns are a common way for marketers to attract new customers. Marketing, along with the other business functions, can also decide to find new markets. For example, a business can decide to open stores in another country.

Connect...

Name a business with which you are familiar. Suggest ways that the business could increase profits.



4-13

One of the major roles of marketing is to increase sales.

Competition

Competition is the contest between two or more businesses to get customers. Businesses also compete with each other for the best workers, materials, processes, location, image, and products. In order for businesses to compete successfully, they work hard to meet customers' needs. They also work hard to improve productivity. The result is better products, better quality, more services, and lower prices. You will learn more about competition in Chapter 6.

In our basketball example, the many basketball suppliers competed with each other for basketball customers. The basketball suppliers worked to improve the quality of the basketballs and to find better ways to make them so that they could lower prices.

Role of the Consumer

You may have heard these statements: Consumers decide which products are produced. Consumers set the prices of products. There is truth to these statements, but they are not entirely true. An individual consumer does not have any effect on the economy. Consumers affect the economy as a group. Consumers affect the economy through the forces of supply and demand. When a large number of consumers want and buy a product, the demand for the product goes up. When a large number of consumers decide they do not want a product, the demand for the product goes down. Businesses and the economy respond to these large-scale changes in demand.

More accurate statements are the following: Consumers as a group affect which products are produced through what they buy. Consumers as a group affect the prices of products through the aggregate effect of their demand. Consumers "vote" for products with their dollars.

Here is an example. A new restaurant opens in your neighbourhood. If a large number of people like the food and go to the restaurant many times, the restaurant will succeed. If very few people like the restaurant, the restaurant will go out of business. In our basketball example, people voted for basketballs over soccer balls by buying more basketballs.

Connect...

Describe a product that was successful because many consumers bought it. Describe a product that failed because few people bought it.

CHAPTER 4 REVIEW

Key Learnings

- The three basic economic questions are (1) what should we produce? (2) how should we produce it? and (3) who should get the products?
- Canada is a mixed economy. In a mixed economy, both government and individuals answer the economic questions.
- Market forces control a market economy, not the government or a group of people.
- The three main market forces are (1) supply and demand, (2) profit, and (3) competition.
- Low prices increase demand; high prices reduce demand. Low prices reduce supply; high prices increase supply.
- Marketing campaigns, the economy, and social trends can change demand.
- The interaction of supply and demand affects price. When supply is low, but demand is high, the price rises. When supply is high, but demand is low, the price falls.
- Businesses can increase profits by (1) reducing costs or expenses, (2) increasing productivity, and (3) increasing sales.
- Consumers vote with their dollars to determine which products are produced.

Knowledge & Understanding

1. How is a market economy different from a command economy?
2. Who controls a market economy?
3. What are market forces?
4. Who affects the demand for products?
5. Who affects the supply of a product?
6. What is the difference between supply and market supply?
7. State the law of demand.
8. State the law of supply.
9. List three factors that can change demand.
10. How does the condition of the economy affect demand?
11. True or False. Profit is all the money that a business receives.
12. State the equation for determining profit.
13. True or False. Consumers set the prices of products.

Thinking

1. Describe and analyze how market forces control a market economy.
2. Why do both the law of supply and the law of demand include the words "in a constant environment"?
3. Explain the law of demand by giving an example.
4. When prices are high, demand falls. Why?
5. How can marketing affect demand?
6. Why is competition good for customers?

Application

1. Imagine that you live in a command economy. Predict how this experience would differ from living in a mixed market economy. Provide three examples that relate to your life.
2. Visit a supermarket during a busy time. Observe the cashiers. How would you

measure the productivity of a cashier? How does technology help the cashiers be more productive? Are some cashiers more productive than others? What interferes with a cashier's productivity? What has the store done to help cashiers be more productive?

3. Read about Canada's jobs of the future on the *Marketing Dynamics* website. Many of these jobs are based on products that will continue to be in demand, and on population changes. How is this information also relevant to marketers?
4. Surplus goods are goods that a supplier has too much of. Go to a website that sells overstock or surplus, such as Overstock. Find out how the website gets its goods to sell. How does the website price these goods? What is the advantage to the website of obtaining and reselling overstock? What is the advantage to the customer? What advantage is there to the supplier? Explain your answers.
5. Imagine that you own a factory. Outline three ways you could increase profit.
6. Do you comparison shop on the Internet? Choose a product that you would like to buy. Find two websites that offer that product. Compare and contrast the product on the two websites. Which website would you use to purchase the item? Why?
7. Name an industry with which you are familiar, such as the soft drink industry, the jeans industry, or the computer game industry. Name at least three businesses in this industry that are in competition with each other. How does their competition affect you as a customer?

Communication

1. Create a graphic organizer that compares command economies with market economies on the basis of the following:
   - how economic decisions are made
   - individual freedom
   - ability to share resources equally
2. Visit a department store. Name a good that many people use, such as jeans, shoes, or bedding. Write down the names of the brands. For each brand, list the products offered and the varieties, such as size. Design a form to record this information. How many brands are there? For each brand, how many varieties of products are there? Why are there so many choices? Would there be as many choices in a command economy?
3. Technology has changed a great deal in recent years. Interview a person who has been in the workforce, such as a parent or grandparent, neighbour, or teacher. Ask this person how the technology he or she uses at work has changed since he or she first started working. Present your interview in writing or as a video.