



WHAT IS A MARKET?

The fundamental economic problem is that of scarcity, as illustrated by that famous London School of Economics student Mick Jagger, who once sang "you can't always get what you want." Throughout history societies have faced the fundamental economic questions of deciding what to produce and for whom to produce it in a world of scarce resources. Markets enable buyers and sellers to get together. In a market, a buyer agrees to give up money in return for a good, while a seller agrees to give up a good and gets money in return.

Self-Interest & Profits. A market economy is based on self-interested behavior. Adam Smith wrote in *The Wealth of Nations* that although an individual considers only his own advantage, his actions in a market economy are "led by an invisible hand to promote an end that was not part of his intention." Market prices guide this invisible hand. People acting in their own interest respond to relative price changes. This encourages producers to find least-cost methods of production and consumers to use their incomes to maximize their satisfaction. In a market economy, consumers direct the allocation of resources by making choices about how to spend and save their income.

1. What does this mean in your own words?

Free Enterprise. Individuals are free to obtain resources, use them in the production of goods and services, and sell them in markets of their choice. Consumers are free to buy the goods and services that best satisfy their economic wants. Individuals are also free to work where they want and to buy the goods and services they want with their earnings. This freedom allows consumers and producers to focus on what they do best, and to freely trade surplus production or wealth. Because markets encourage trade, they also help create wealth.

2. What does this mean in your own words?

Competition. Buyers and sellers are free to enter or leave any market, and buyers and sellers act independently in the marketplace. Competition pressures firms to satisfy consumer demand or be forced from the market by firms that can. Competition keeps prices in line with the costs of production. If one seller raises prices in an attempt to earn excessive profits, competition from other sellers (who also want to earn profits) will drive the prices down. Pure competition assumes that sellers can easily leave one business and easily enter another one. Competition among buyers prevents anyone buyer from controlling prices by refusing to buy something.

3. What does this mean in your own words?

System of Markets & Prices. Markets bring together buyers and sellers of goods and services. In a market system, the forces of supply and demand, not the government, determine prices. If there is a surplus of goods available at the going price, the price will fall. If there is a shortage of goods available at the going price, the price will rise.

4. What does this mean in your own words?

Private Property. In a market economy, resources used to produce goods and services in the economy are largely owned by private individuals and private institutions rather than government. This private ownership means individuals can negotiate legally binding contracts to obtain and use resources as they choose, including selling the property they own to other individuals. The right to own private property (property rights) provides incentives to owners to take care of the property and to invest in it and therefore encourages the efficient allocation of resources.

5. What does this mean in your own words?

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Limited Government. Government has a different function in a market economy than in a command economy. In a command economy, government produces or directs the production of goods and services. The collapse of communism illustrated that this method does not work very well. In a market economy, government protects the rights of citizens, including private property rights, and enforces contracts, making sure agreements are honored. Because a market economy is self-regulating, the government does not need to set prices or quantities.

6. What does this mean in your own words?

Market ... or Not?

Use the characteristics of a market economy described above to determine whether the following scenarios represent a market or not. If you think that a scenario represents a market, place an M for market in the blank. If you think that this scenario does not represent a market, place a NM for not market in the blank. If you are not sure, place a U for uncertain in the blank. Then explain WHY OR WHY NOT?

1. People are lined up outside a car dealership waiting for it to open. A special deal was advertised in today's paper, and many consumers have come early to try to get the best bargain they can.
 2. People are lined up outside Yellowstone National Park waiting to buy a ticket to enter the park. Visitors must purchase a day pass from park rangers in order to drive into the park.
 3. People are lined up outside the Department of Motor Vehicles office to buy license plates. A vehicle can be driven legally only if it has a license plate and is registered with the state.
 4. People swamp the Web site of a new long-distance phone company offering rates that are 50 percent less than the rates of the large, national long-distance carriers. Many who log on are hoping to switch to the new carrier.
 5. People are lined up outside a national doughnut chain store opening today for the first time; they want to be among the first to buy a dozen doughnuts.
 6. People are lined up outside a government building waiting to receive free cheese provided by a federal government program.
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The Rap Music Market

A very large market in the United States is the one for rap music. If you have purchased a CD, listened to the radio, or downloaded MP3 files from the Internet, then you have participated in this market. Imagine that you have just heard about the latest song released from the amazing rapper, Krispy Rice. You know that his last two CDs have topped the charts, so you know you'll have to rush right down to the CD Emporium if you hope to get a copy. On your way to the CD Emporium, take a moment to think about how your desire to purchase this CD and his record company's desire to sell the CD represent characteristics of a market economy. Use the data chart below to provide examples for each of the features of a market (not all cells will be full for both you and Crackle Snap Pop Music Krispy Rice's record label).

	You	Crackle Snap Pop Music (Krispy Rice's Record Label)
Self-Interest & Profits	Example: You get the benefit of listening to the song and enjoying the music	Example: They make money on the sale of the CD
Free Enterprise		
Competition		
System of Markets & Prices		
Private Property		
Limited Government		