PURPLEGROWTH

TRAINING & EXECUTIVE COACHING

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MODULE 1

LEARNING UNIT 1

MARKET MECHANISMS

DEMONSTRATE AN UNDERSTANDING OF THE FUNCTION OF THE MARKET MECHANISM IN A NEW VENTURE- 263514

LEARNING OUTCOMES

Be	By the end of this unit, you will be able to:
Explain	Explain the free market system in terms of perfect and imperfect competitive markets
Discuss and illustrate	Discuss and illustrate the interaction of demand and supply in price determination
Identify and discuss	Identify and discuss the factors that drive economic activity
Describe	Describe the development and significance of markets with particular reference to South Africa.

INTRODUCTION TO THE **ECONOMY**

As an entrepreneur, you'll always have to make decisions about your business to meet your needs and wants. Most of the time, these decisions are made based on the limited resources of your business and other things, like how customers feel about it. You need to know the basics of economics, the business market, and the things that drive economic activity so that you can make decisions that will help your business succeed in the long run

A business’s success depends in part on the economic systems of the countries where it is located and where its sells its products.

Economics is the study of how a society uses scarce resources to produce and distribute goods and services.

The resources of a person, a firm, or a nation are limited. Hence, economics is the study of choices—what people, firms, or nations choose from among the available resources.

Every economy is concerned with what types and amounts of goods and services should be produced, how they should be produced, and for whom. These decisions are made by the marketplace, the government, or both.

You probably know more about economics than you realise. Every day, many news stories deal with economic matters: a union wins wage increases at Eskom, the Reserve Bank lowers interest rates, price of petrol goes up, the shortage of cooking oil.

ECONOMICS CAN BE DIVIDED INTO **TWO SEPARATE FIELDS OF STUDY**

MICRO ECONOMICS

Microeconomics is the study of individuals, households and firms' behaviour in decision making and allocation of resources.

It generally applies to markets of goods and services and deals with individual and economic issues

MACRO ECONOMICS

It is concerned with understanding economy-wide events such as the total amount of goods and services produced, the level of unemployment, and the general behaviour of prices.

DIFFERENT **MARKETS**

Businesses and other organizations operate according to the *economic systems* of their home countries.

Today the world's major economic systems fall into two broad categories: free market, or capitalism; and planned economies, which include communism and socialism.

However, in reality many countries use a mixed market system that incorporates elements from more than one economic system.

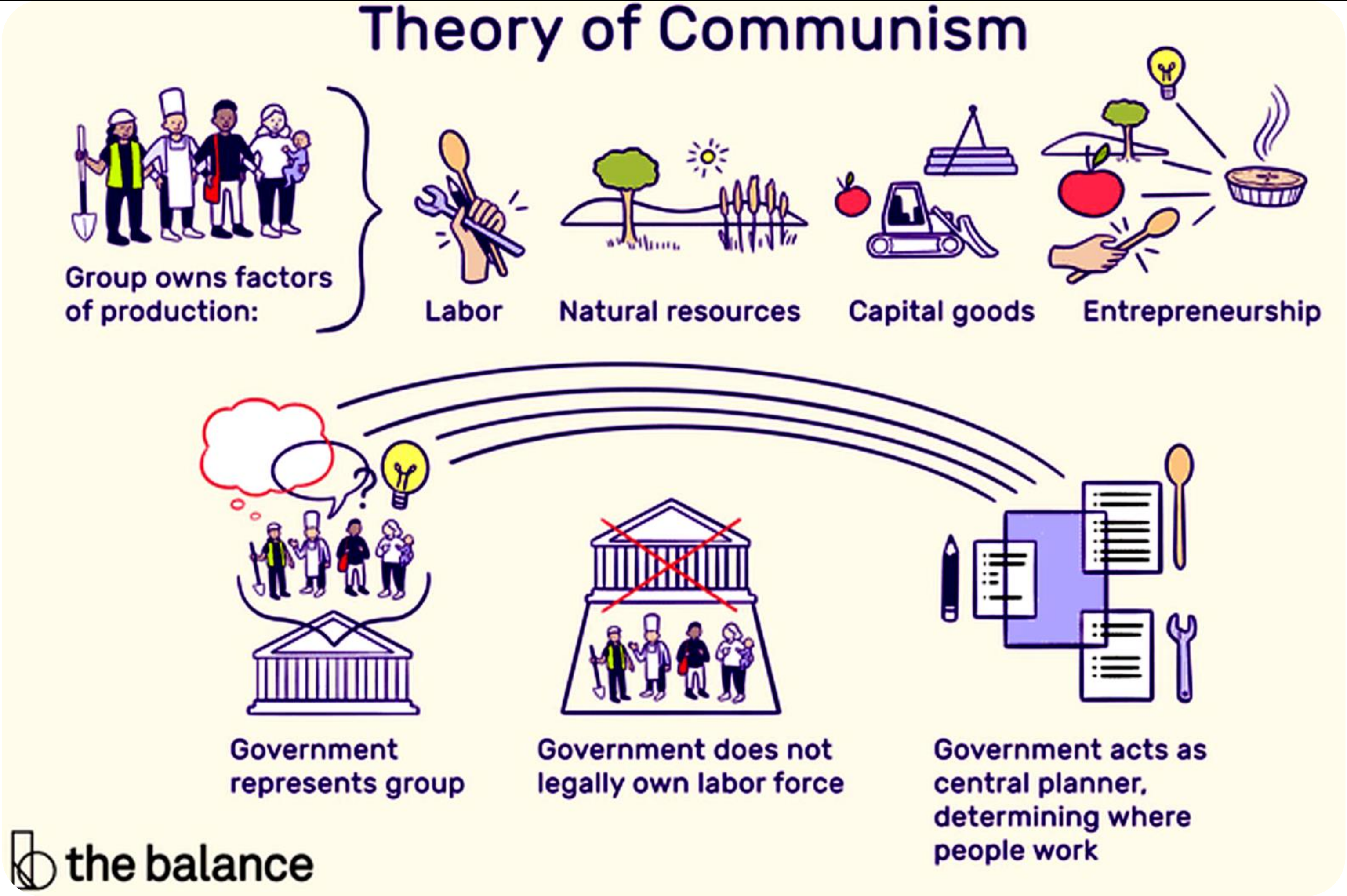
COMMUNIST ECONOMY

Communism is an economic system where the government owns the factors of production.

The factors of production are labour, entrepreneurship, capital, and land.

Although the government doesn't legally own the labour force, the central planners tell the people where they should work.

COMMUNIST ECONOMY



COMMUNIST ECONOMY

The communist ideology was developed by Karl Marx and Friedrich Engels and is the opposite of a capitalist one, which relies on democracy and production of capital to form a society.

Prominent examples of communism were the Soviet Union and China. While the former collapsed in 1991, the latter has drastically revised its economic system to include elements of capitalism.

Communism is an economic ideology that advocates for a classless society in which all property and wealth are communally-owned, instead of by individuals.

FORMATIVE

ACTIVITY **A1**

CAPITALIST
ECONOMY/FREE MARKET

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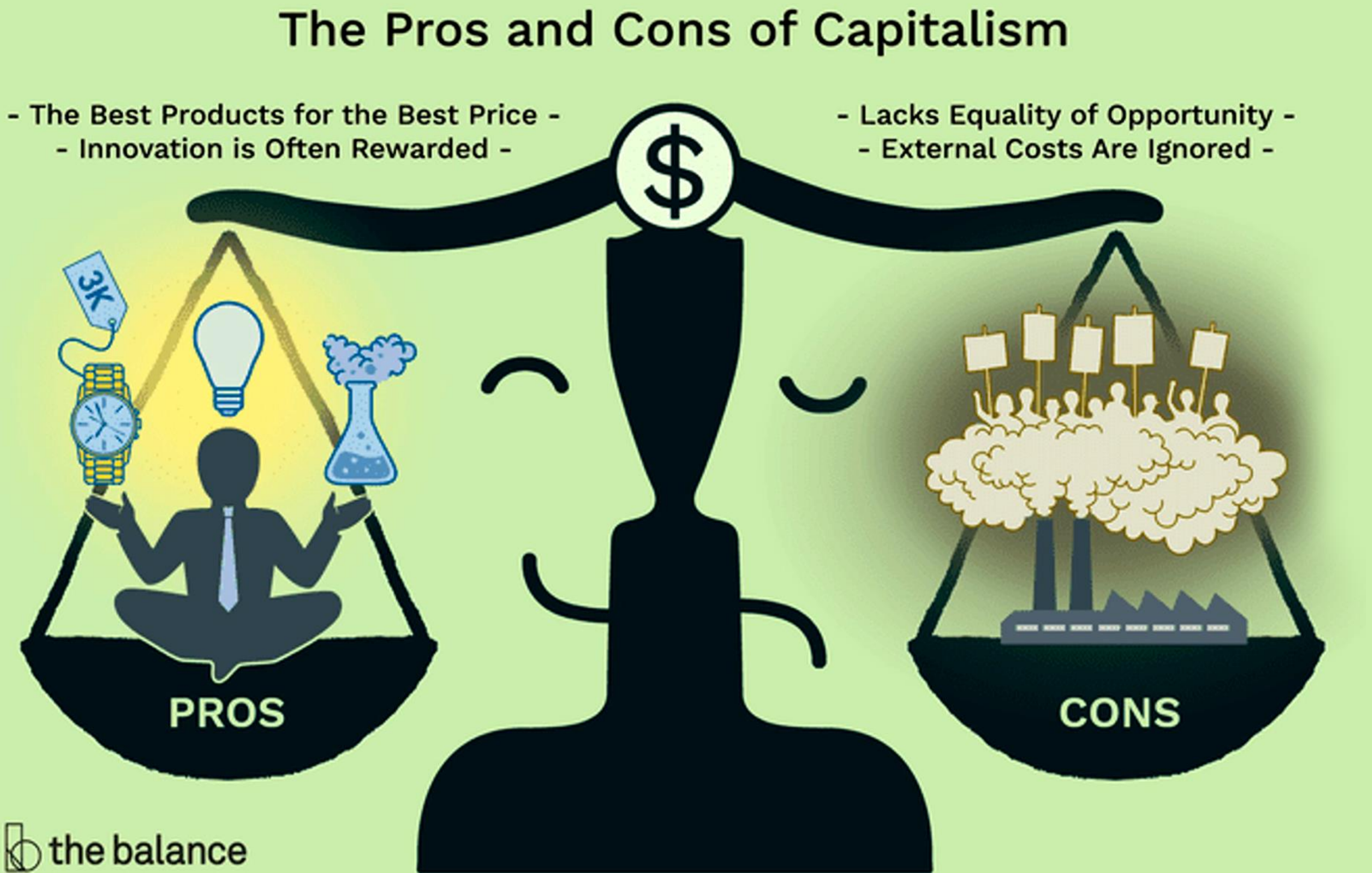
Capitalism is an economic system that focuses on a free market to determine the most efficient allocation of resources and sets prices based on supply and demand.

Capitalism has many unique features, some of which include a two-class system, private ownership, a profit motive, minimal government intervention, and competition.

In capitalist economies, there exists a private sector that owns, property, plants, and equipment.

The owners of production decide how to run their businesses, how much to produce, and how many people to hire.

CAPITALISM


The Pros and Cons of Capitalism
- The Best Products for the Best Price -
- Innovation is Often Rewarded -
- Lacks Equality of Opportunity -
- External Costs Are Ignored -
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FORMATIVE

ACTIVITY **A2**

MARKET STRUCTURE

The competitive environment, in which these buyers and sellers operate, is known as the market structure. There are four types of market structure.

PERFECT COMPETITION has a large number of buyers and sellers that make decisions and do not take the effect of their actions into account. This is due to the fact that individual economic units in perfect competition are small and are unrelated to other economic units. Their actions have no impact on other buyers and sellers.

MONOPOLY is where a single organisation sells a product or service but has no close substitutes. There is virtually no competition; however, entry into this market is very difficult, almost impossible.

OLIGOPOLY has a few sellers of a differentiated product or service, or a homogenous good. Entry into this market is not very easy but is possible.

IMPERFECT COMPETITION

Monopoly, monopolistic competition and oligopoly are forms of **imperfect competition,** which exists because entry into these markets is not necessarily easy.

Few firms and businesses operate in these markets in order to gain maximum control over the price of their goods and services.

Consumers have little influence on the price of goods and services.

Examples include diamond sales by De Beers's Central Selling Organisation (CSO) and SA Breweries' (SAB) production of beer.

PERFECT COMPETITION

Perfect competition is an ideal type of market structure where all producers and consumers have full and symmetric information and no transaction costs.

There are many producers and consumers competing with one another in this environment.

Perfect competition means that businesses and consumers will only exchange products and services if they both benefit from the trade.

In perfect competition, production occurs at a minimum cost but this does not mean that it is more efficient than other market systems.

Examples include

WHY IS COMPETITION IMPORTANT IN FREE MARKETS

The labour government of South Africa deems competition as being beneficial for the economy as it is the main force behind productivity growth in the economy.

It encourages businesses to reduce slack and costs while providing incentives for more efficient production.

Competition also helps consumers to get lower prices as well as a greater variety of products and services.

Improvements to quality and customer service are also gains from market competition, as well as allowing consumers to make better informed choices.

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SOCIALIST ECONOMY

Socialism is an economic and political system based on collective ownership of the means of production.

All legal production and distribution decisions are made by the government in a socialist system. The government also determines all output and pricing levels and supplies its citizens with everything from food to healthcare.

Supporters of socialism believe that it leads to a more equal distribution of goods and services and a more equitable society.

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ACTIVITY **A3, A4, A5, A6**

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MARKET

Without a market, you have no supply or demand, and, therefore, no business at all, because there's no one to sell anything to.

Thus, the first factor a business should consider in the supply and demand arena is whether there is indeed a market of buyers who want a particular item and sellers who want to sell it to them.

With many buyers and sellers in a competitive market, each has little effect on the price, allowing it to be driven by overall sentiment.

DEMAND & SUPPLY

IN THE MARKET

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A business owner must always be thinking in terms of supply and demand.

Demand is the amount of product or service demanded by consumers at the different prices.

Supply shows how much the market can offer or the amount of a product or service sellers are willing to offer for sale.

Demand and supply relationships illustrate the forces and factors that affect the allocation of resources.

THE LAW OF DEMAND

The law of demand states that as the price of an item increases, buyers are less willing and able to buy it and vice versa

It's up to the business owner to find the right price that brings in as much money as possible without making people stop buying.

When the main goal is to make money, it is important to keep a close eye on the supply and demand of each product line and to do this on a regular basis.

LAW OF DEMAND VIDEO

https://youtu.be/QvGLcCTXk9o

THE LAW OF SUPPLY

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It states that as the price of an item increases, producers want to supply more of it (to increase their revenue and profits) and *vice versa*.

The law of supply explains how producers usually respond to price changes.

Remember – quantity responds to price, not the other way around!

This concept helps explain why when prices of goods and services increase, more goods and services are likely to appear in the market.

LAW OF DEMAND

AND SUPPLY RELATIONSHIP

https://youtu.be/TvCYq3RGsNo

THE EQUILIBRIUM PRICE

AND QUANTITY

https://youtu.be/7eZcPs9z9OA

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ACTIVITY **A7, A8**

THE EQUILIBRIUM PRICE

AND QUANTITY

Equilibrium price is determined when the demand and supply curves are joined and intersect at a specific point. It is at this point that the allocation of goods and services are at its most efficient.

Here, the amounts of goods or services that are being demanded are the same as the amount of goods or services that are being supplied.

This means that suppliers are selling all the goods or services being produced and consumers are obtaining all the products and services they are demanding.

DISEQUILIBRIUM

This is a state where there is excess demand or excess supply.

EXCESS SUPPLY occurs when the price is too high and not enough demand has occurred.

Suppliers produce more in order to sell and increase profits; however, those that consume the products or services end up consuming less due to the price increase making the product or service less attractive.

EXCESS DEMAND occurs when the price is set below the equilibrium price. This means that too many consumers demand the product or service while suppliers are not providing enough. This ends up stabilising in the long run as the price will eventually increase due to the competition between consumers. This brings the price closer to the equilibrium.

FACTORS AFFECTING

DEMAND

A change in demand describes **a shift in consumer desire to purchase a particular good or service, irrespective of a variation in its price**. The change could be triggered by a shift in income levels, consumer tastes, or a different price being charged for a related product.

https://youtu.be/Enz6z9jGmsk

FACTORS AFFECTING

SUPPLY

Change in supply refers to **a shift, either to the left or right, in the entire price-quantity relationship that defines a supply curve**. Essentially, a change in supply is an increase or decrease in the quantity supplied that is paired with a higher or lower supply price.

://youtu.be/t5YyLWYYdes

MONEY DEFINED

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Money is **a commodity accepted by general consent as a medium of economic exchange**.

It is the medium in which prices and values are expressed.

It circulates from person to person and country to country, facilitating trade, and it is the principal measure of wealth.

INFLATION DEFINED

Inflation is the rate of increase in prices over a given period.

Inflation is typically a broad measure, such as the overall increase in prices or the increase in the cost of living in a country.

Inflation is usually measured with the annual percentage increase of a CPI, otherwise known as a consumer price index. There are other methods that can be used, but this method is generally preferable.

FACTORS CAUSING
INFLATION

The main contributing factors include :

- increase in the money supply,
- worker shortages and rising wages,
- supply chain disruption eg Covid lockdown impact
- fuel price increases.
- increases in production costs, such as raw materials and wages.
- Increased demand (surplus demand) pushing prices up

FOREIGN CURRENCY

- Foreign exchange is the swapping of one currency for another. It is needed to settle transactions between people or entities located in countries that use different currencies. This exchange is needed to complete international transactions.

Examples of foreign exchange are:

- A business in South Africa pays a supplier in the United States, which requires the business to convert South African Rands (ZAR) into U.S. Dollars (USD).
- A person travels to Canada from the United States, exchanging U.S. Dollars (USD) at the Canadian border for Canadian Dollars (CAD).

WHY FOREIGN CURRENCY

This is important for entrepreneurs who are competing internationally, or who want to set a comparative price for their products or services.

The foreign exchange market is the market in which foreign currencies are exchanged.

A strong domestic currency means improved Gross Domestic Product (GDP) and strong economy.

FORMATIVE

ACTIVITY **A9-A12**