SUPPLY AND DEMAND PART II

Supply always comes on the heels of demand.
-Robert Collier

TABLE AND CHART: DEMAND (D) VS. QUANTITY DEMANDED (Q_d)

P	Q_d
$1.00	1
0.75	3
0.50	5
0.25	7

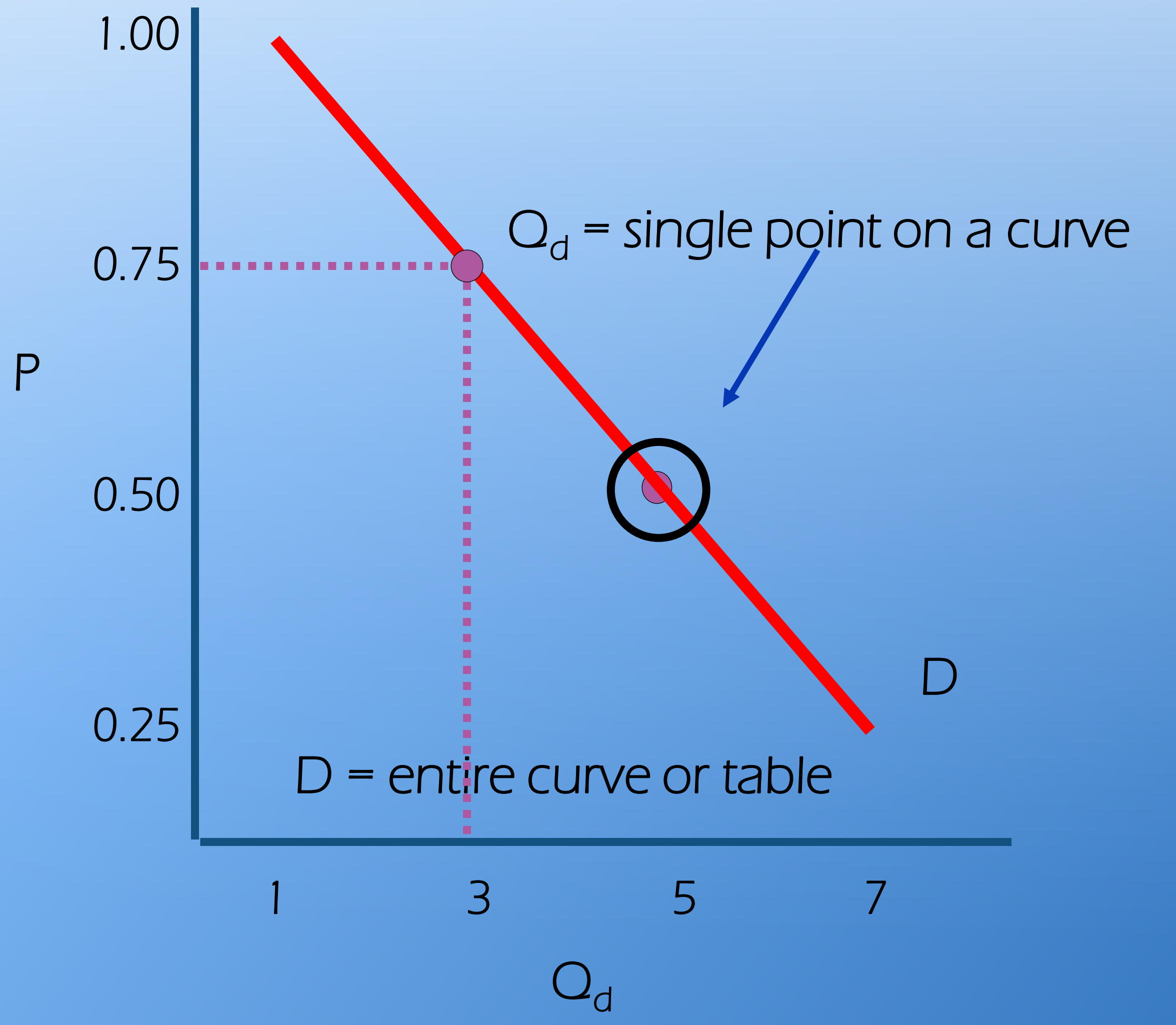

TABLE AND CHART: QUANTITY DEMANDED (Q_d)

P	Q_d
$1.00	1
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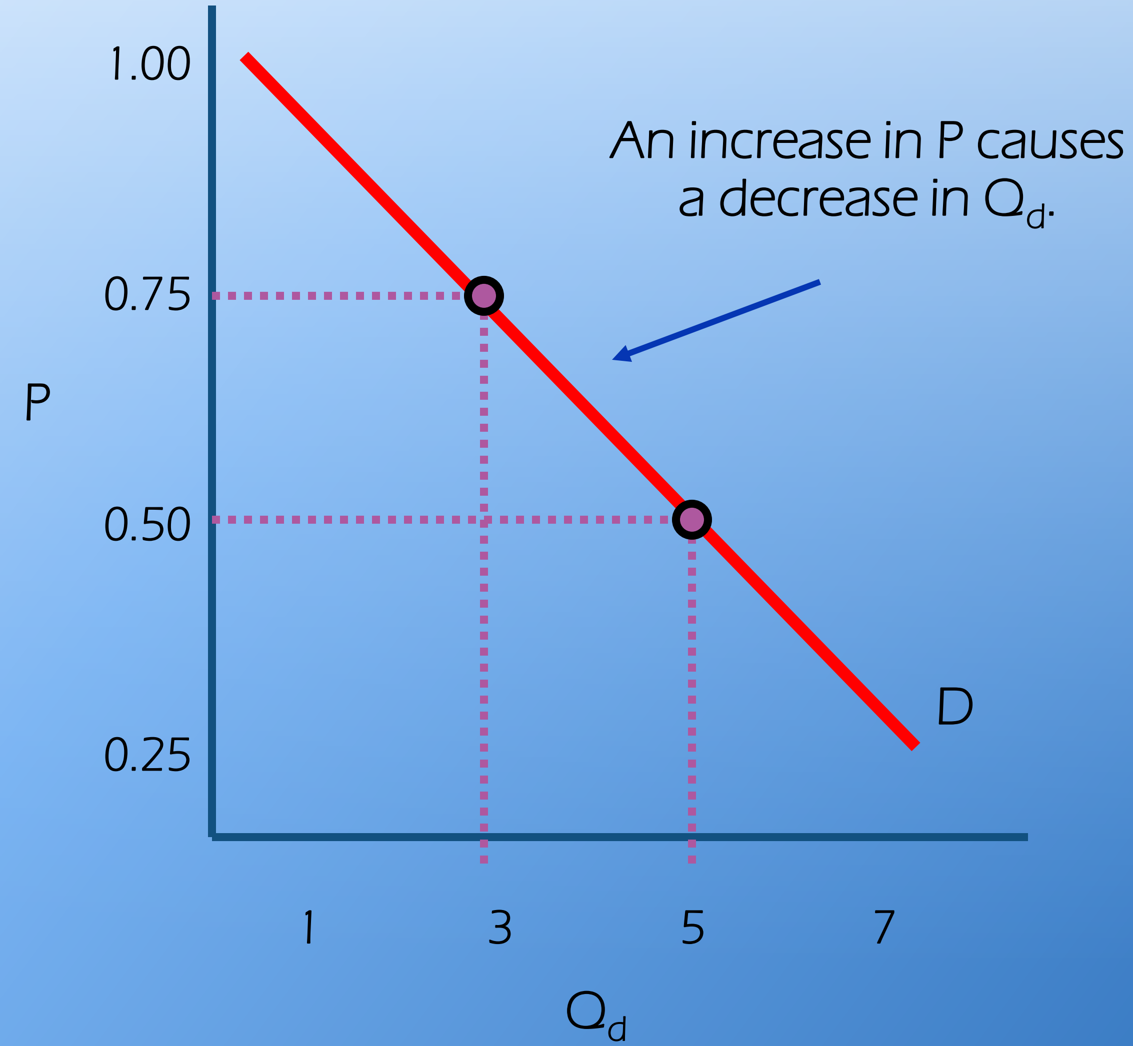


TABLE AND CHART: DEMAND (D)

P	Q_{d1}	Q_{d2}
$1.00	1	2
0.75	3	6
0.50	5	10
0.25	7	14

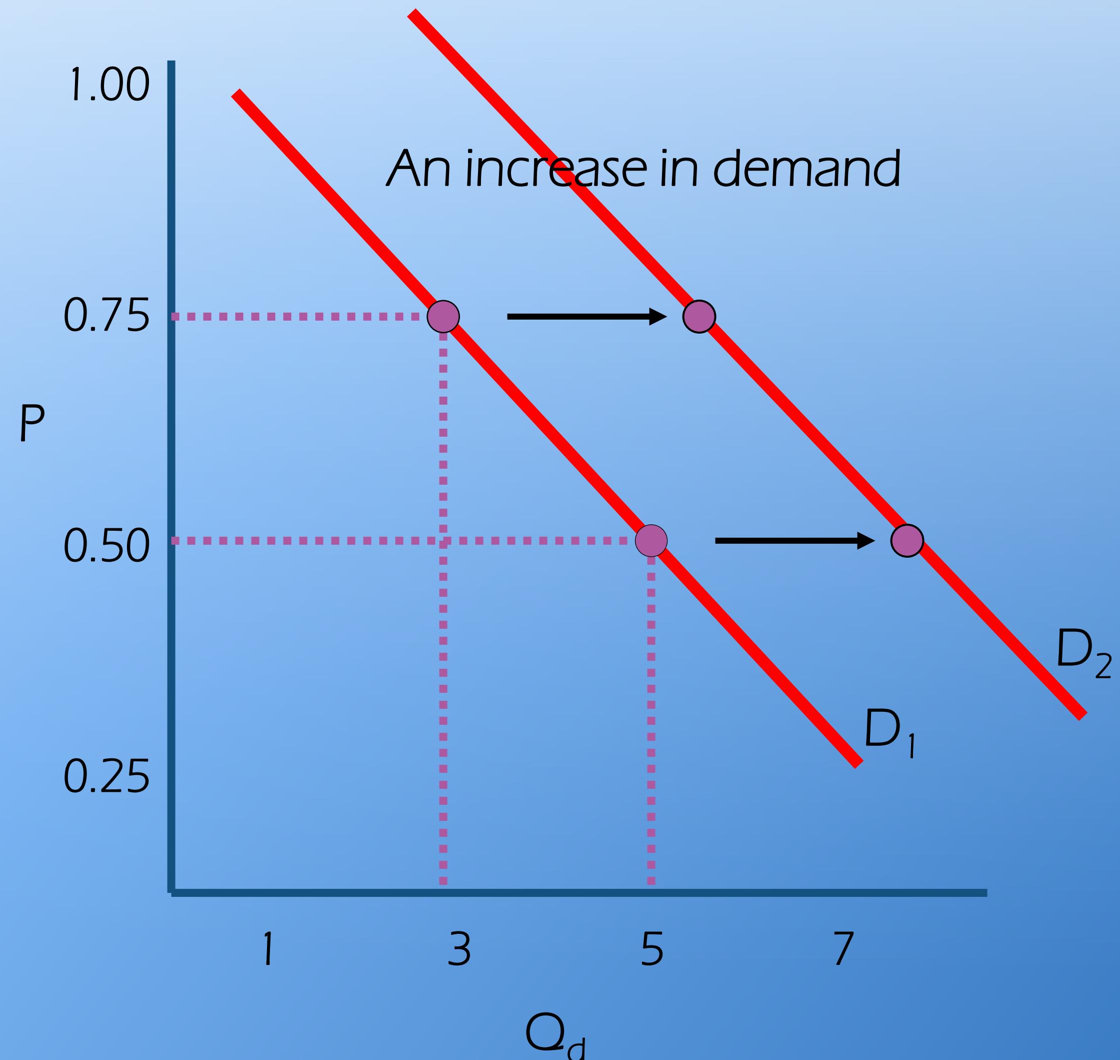
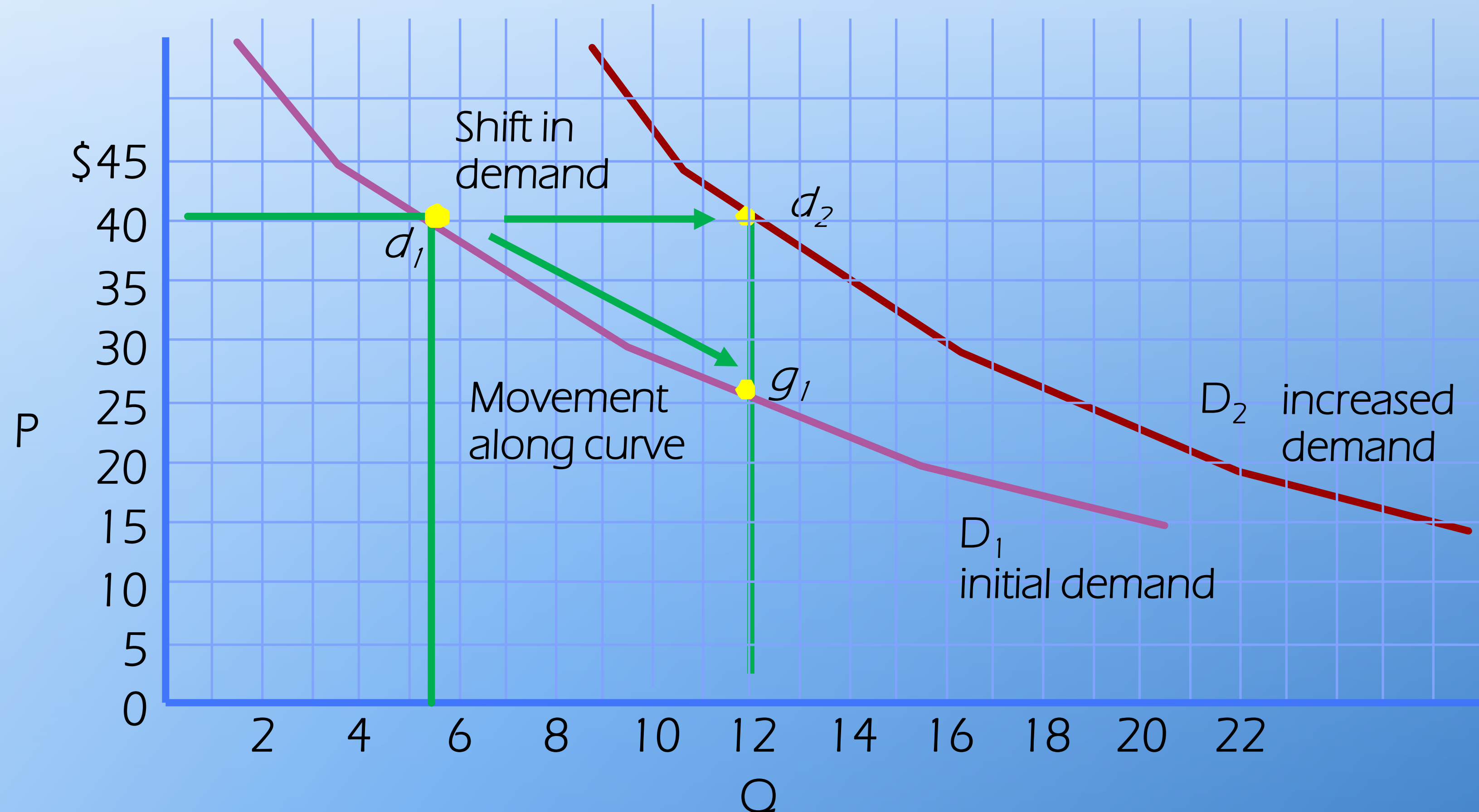


CHART: MOVEMENTS VS. SHIFTS



Important: An increase in demand is always shown as a shift to the right, while a decrease is shown as a shift to the left.

MARKET DEMAND

- *Market demand* is the total quantities of a good or service people are willing and able to buy at alternative prices in a given time period.
- It is the sum of individual demands.

MARKET DEMAND

Market demand is determined by the number of potential buyers and their respective preferences, incomes, other goods and expectations.

THE MARKET DEMAND CURVE

- **Market demand** represents the combined demands of all market participants.
- The separate demands of individual consumers are added up to determine the total quantity demanded at any given price.

CHARTS: CONSTRUCTION OF THE MARKET DEMAND CURVE

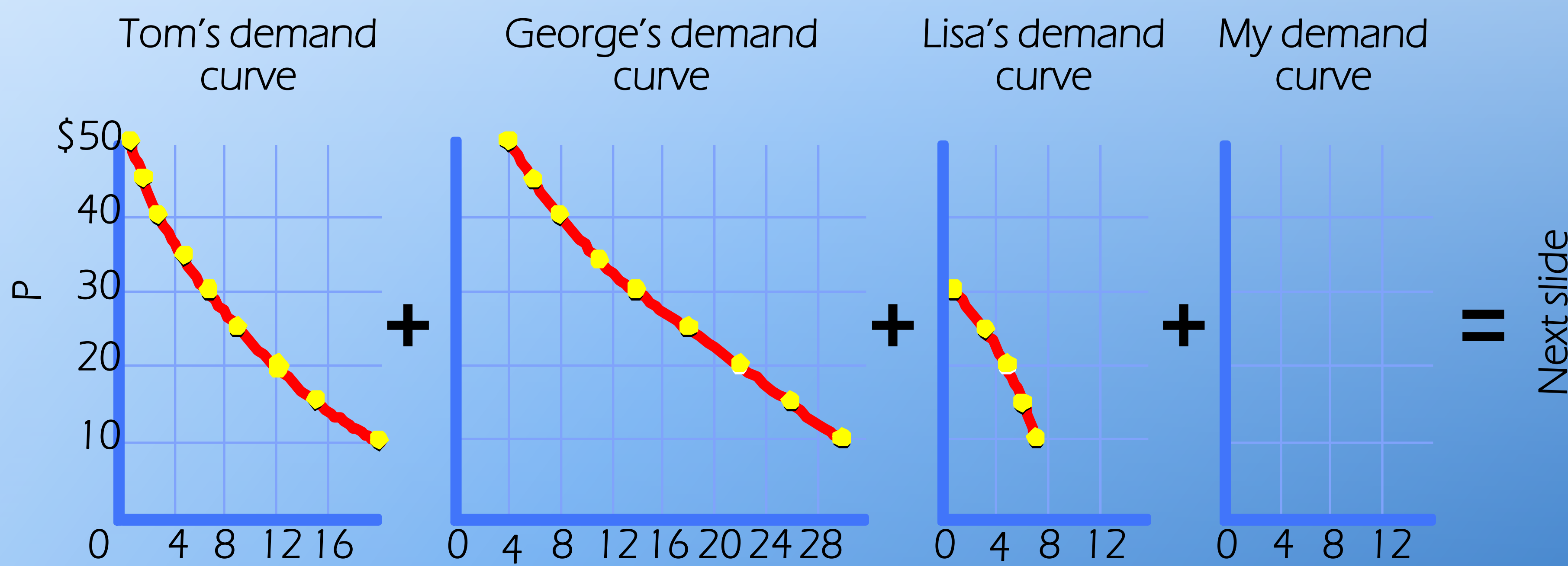
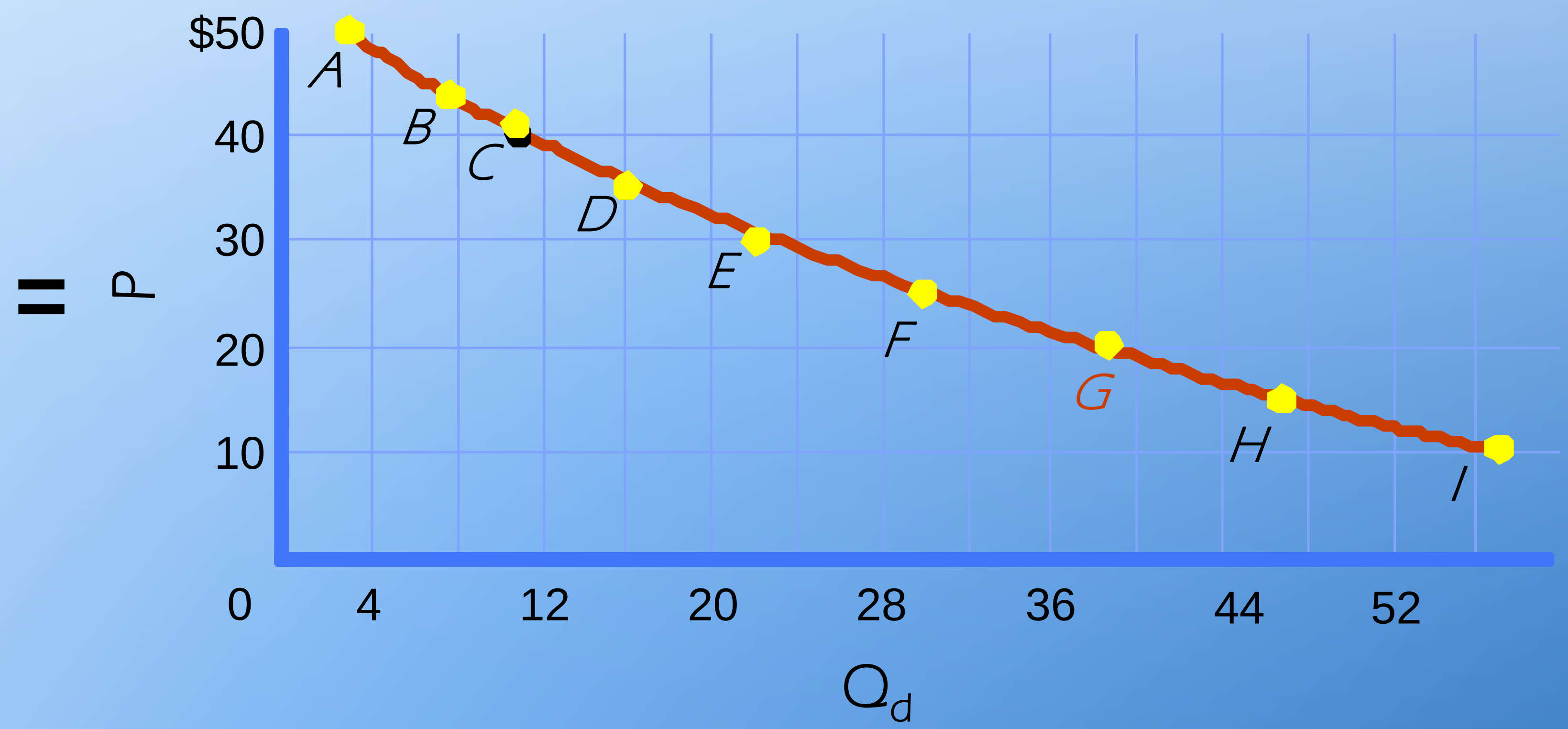


CHART: CONSTRUCTION OF THE MARKET DEMAND CURVE

The market demand curve



SUPPLY

Now, let's turn our attention to the concept of Supply.

Market supply is the total quantities of a good that sellers are willing and able to sell at alternative prices in a given time period, *ceteris paribus*.

DETERMINANTS OF SUPPLY

The determinants of market supply include:

- Resource (factor) prices
- Technology
- Prices of other goods the firm could produce
- Taxes and subsidies
- Producers' expectations
- Number of sellers in the market

RESOURCE PRICE

- factors of production - land, labor, capital, entrepreneurship
- price falls, producer willing to make more
- price goes up, producer not willing to make more

TECHNOLOGY

- Improvement can produce more.
- advancement in technology
- lower per-unit cost

PRICE OF OTHER GOODS

- substitute production for other goods
- getting a lower per-unit cost

VS.

TAXES AND SUBSIDIES

- Increase – per-unit cost goes up, not willing to produce more
- Decrease – per-unit cost goes down willing to produce more

PRICE EXPECTATIONS

Know consumers are willing to pay a higher price for good, more willing to supply the good.

NUMBER OF SELLERS

Competition – More sellers in market the higher the supply. Less sellers in the market the lower the supply.

LAW OF SUPPLY

- There is a direct relationship between the price of a good and the quantity sellers are willing to offer for sale in a defined time period, *ceteris paribus*
- In other words, the higher the price of a product the higher quantities sellers will sell.

LAW OF SUPPLY

According to the *law of supply*, the quantity of a good supplied in a given time period increases as its price increases, *ceteris paribus*.

Supply curves are upward-sloping to the right because only at a higher price will it be profitable for sellers to incur the higher opportunity cost associated with supplying a larger quantity.

MARKET SUPPLY

- The market supply curve is just a summary of the supply intentions of all producers.
- Market supply is an expression of sellers' intentions – an offer to sell – not a statement of actual sales.

TABLE: MARKET SUPPLY

		Quantity Supplied By:			
	Price (per hour)	Ann +	Bob +	Cory =	Market
j	$50	94	35	19	148
i	45	93	33	14	140
h	40	90	30	10	130
g	35	86	28	0	114
f	30	78	12	0	90
e	25	53	9	0	62
d	20	32	7	0	39
c	15	20	0	0	20
b	10	10	0	0	10

CHARTS: MARKET SUPPLY

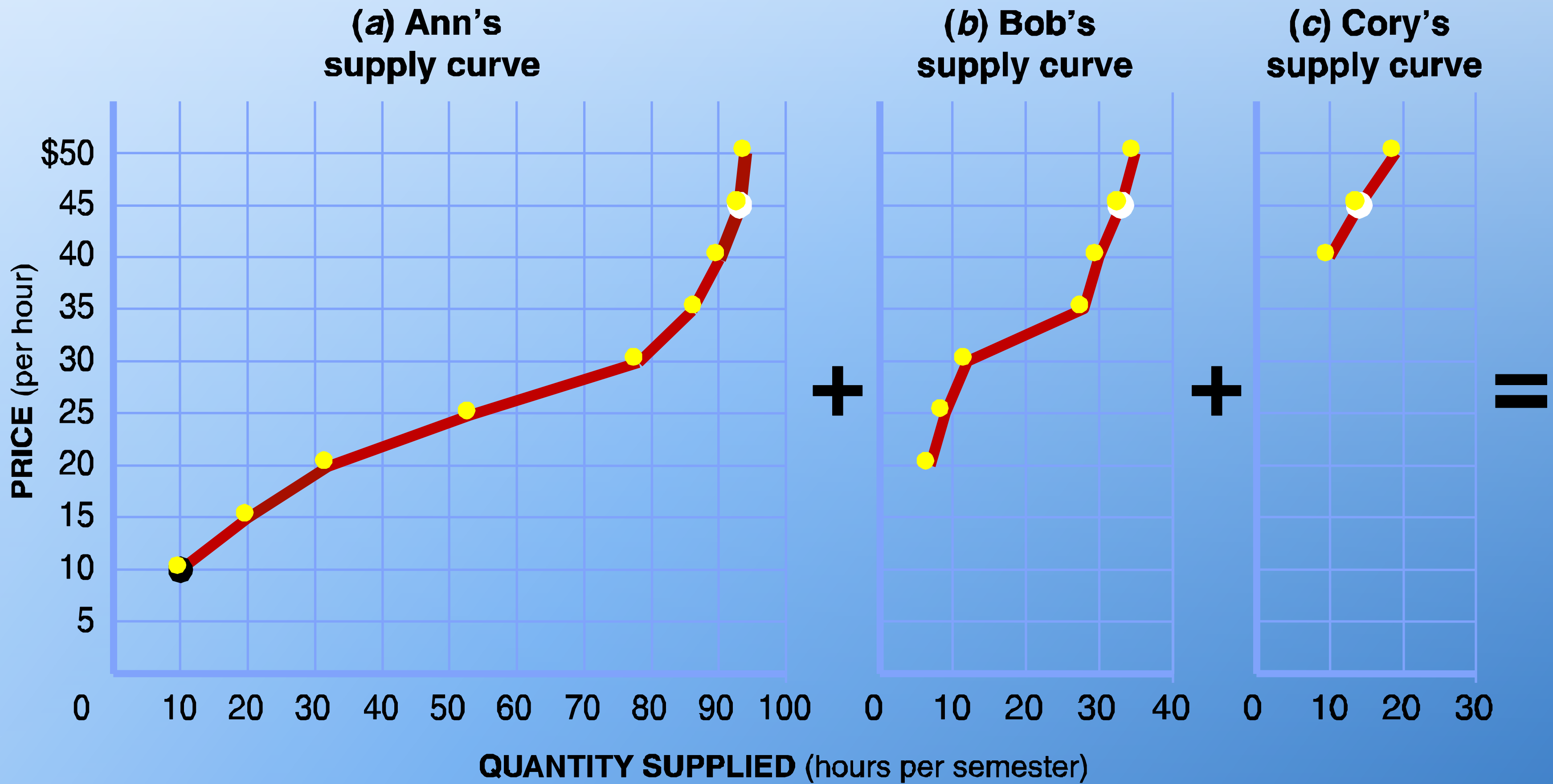
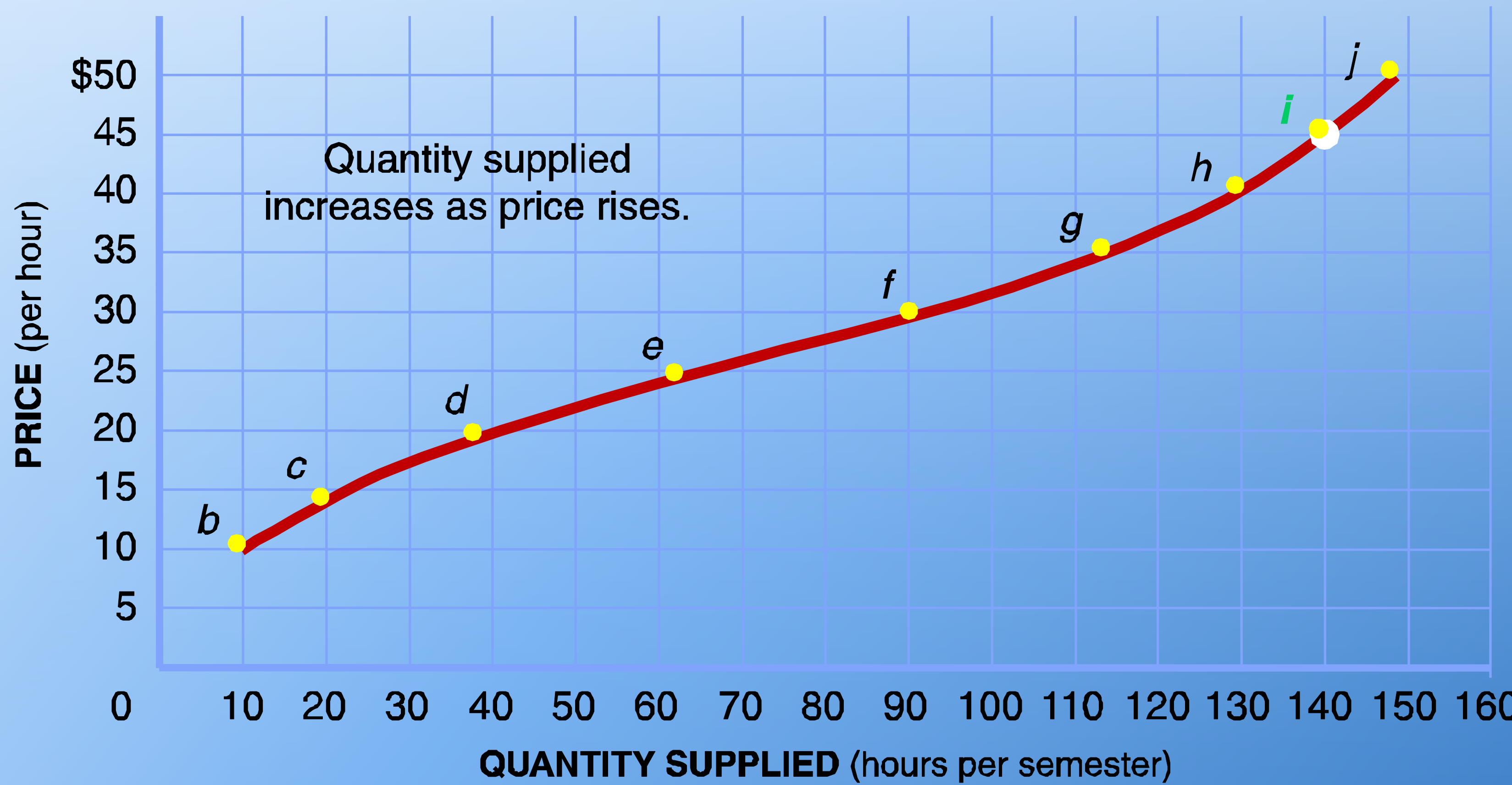


CHART: MARKET SUPPLY



SHIFTS IN SUPPLY

- *Changes in the quantity supplied* — movements along the supply curve.
- *Changes in supply* — shifts in the supply curve.

SHIFTS IN SUPPLY

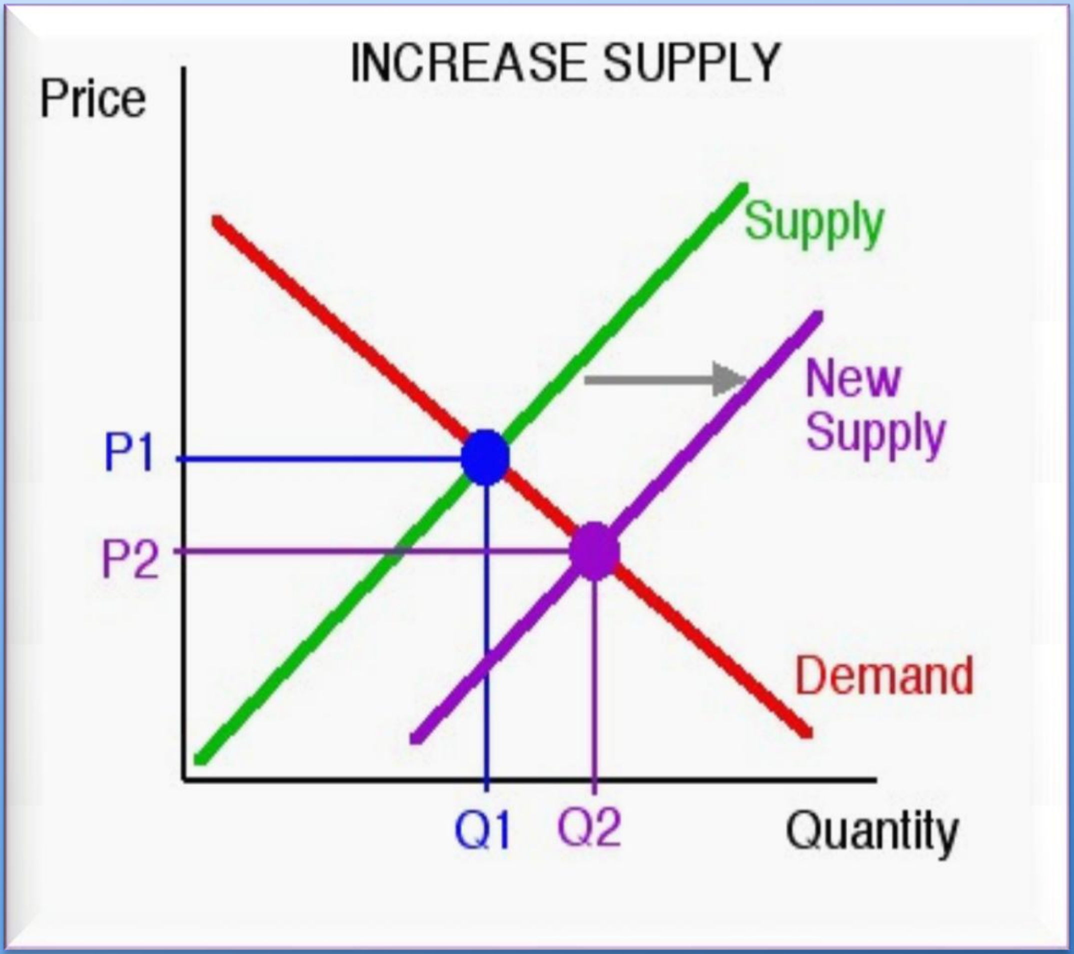
- Since markets tend toward equilibrium, a change in supply will set market forces in motion that lead the market to a new equilibrium price and quantity supplied.
- Excess Supply
  - A *surplus* is a situation in which quantity supplied is greater than quantity demanded. If a surplus occurs, producers reduce prices to sell their products. This creates a new market equilibrium.
- A Fall in Supply
  - The exact opposite will occur when supply is decreased. As supply decreases, producers will raise prices and demand will decrease.

SHIFT DUE TO INCREASE IN SUPPLY

- Supply increases (moving the curve to the right) if
  - COSTS ARE LOWER due to
    - lower resource prices
    - new production technology
  - larger number of sellers
  - favorable environment for producing or selling
  - lower taxes
- When supply increases for one of these reasons, it will move the equilibrium, thus decrease the price and increase the quantity supplied.

CHART: SHIFT DUE TO INCREASE IN SUPPLY

The original equilibrium (the green supply and red demand) occurs at price P1 and quantity Q1.
As the supply curve moves (to the purple curve), the equilibrium price decreases to P2 and the quantity to Q2. Sellers sell more of the good, but are paid a lower price to sell it.



SHIFT DUE TO DECREASE IN SUPPLY

- Supply can decrease (moving the supply curve to the left) if
  - COSTS ARE HIGHER due to
    - higher resource prices
    - smaller number of sellers
  - unfavorable environment for producing or selling
  - higher taxes
- When supply decreases for one of these reasons, it will move the equilibrium, increase the price and decrease the quantity supplied:

CHART: SHIFT DUE TO DECREASE IN SUPPLY

The original equilibrium (the green supply and red demand) occurs at price P1 and quantity Q1.
As the supply curve moves (to the purple curve), the equilibrium price increases to P2 and the quantity decreases to Q2. Sellers sell less of the good, but get paid a higher price to sell it.

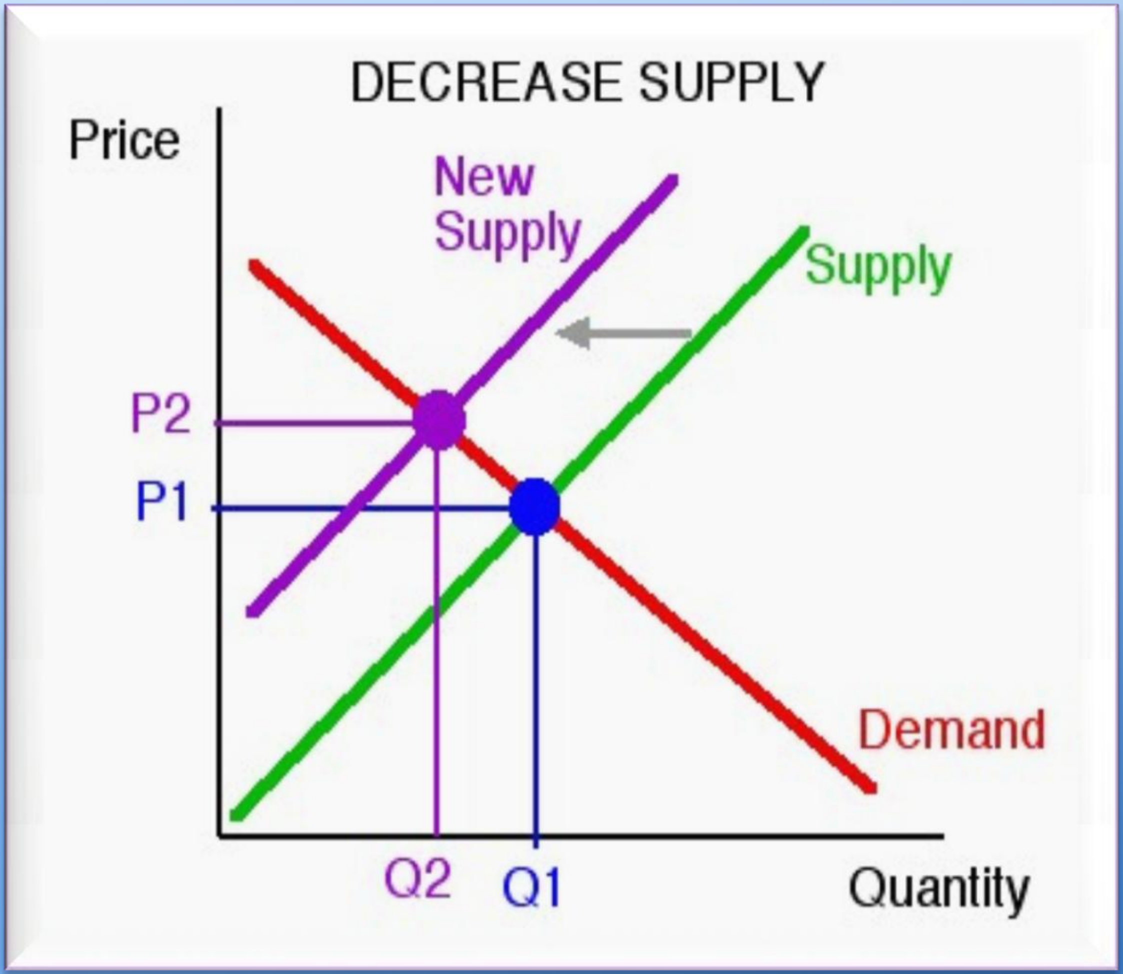


TABLE AND CHART: SUPPLY (S) VS. QUANTITY SUPPLIED (Q_s)

P	Q_s
$150	8
120	6
90	4
60	2

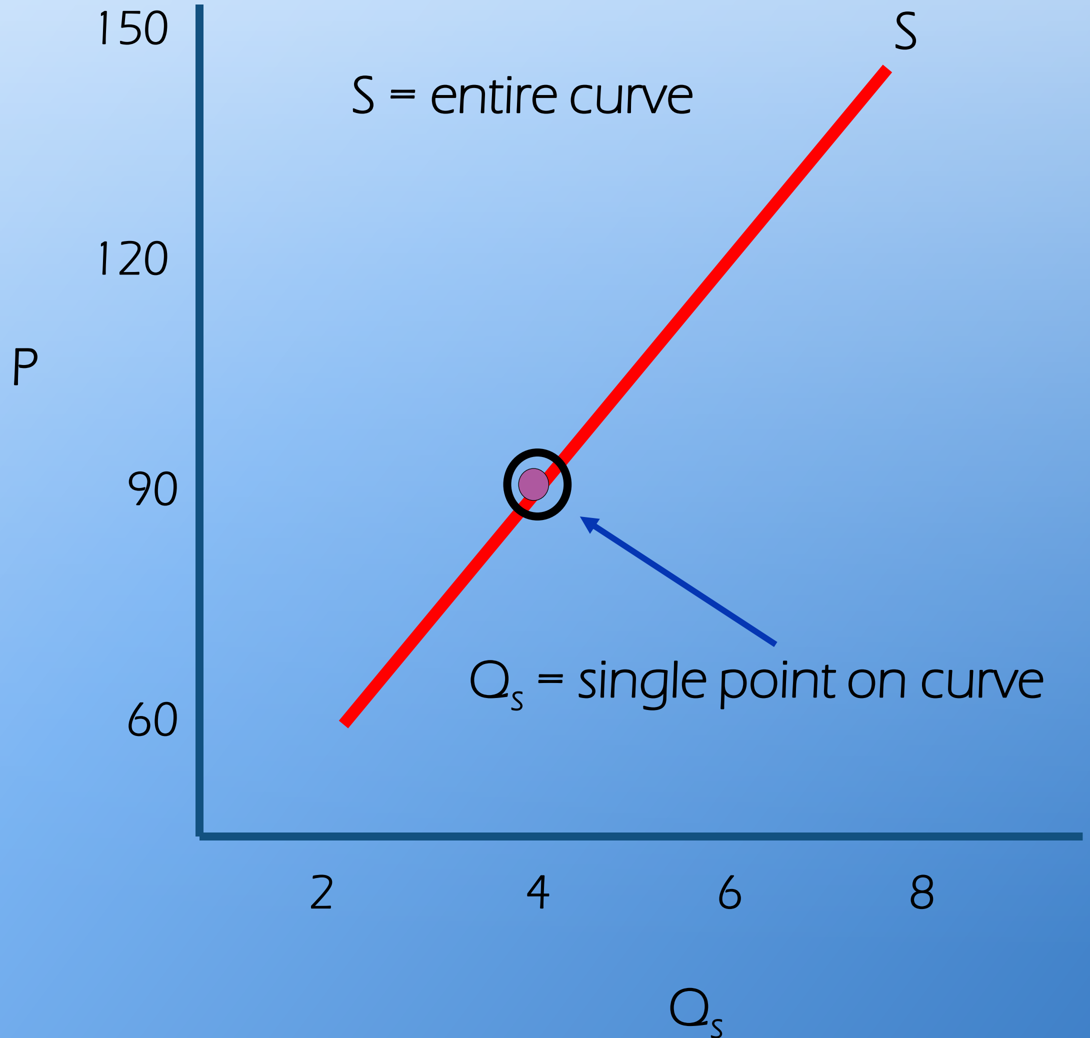


TABLE AND CHART: QUANTITY SUPPLIED (Q_s)

P	Q_s
$150	8
120	6
90	4
60	2

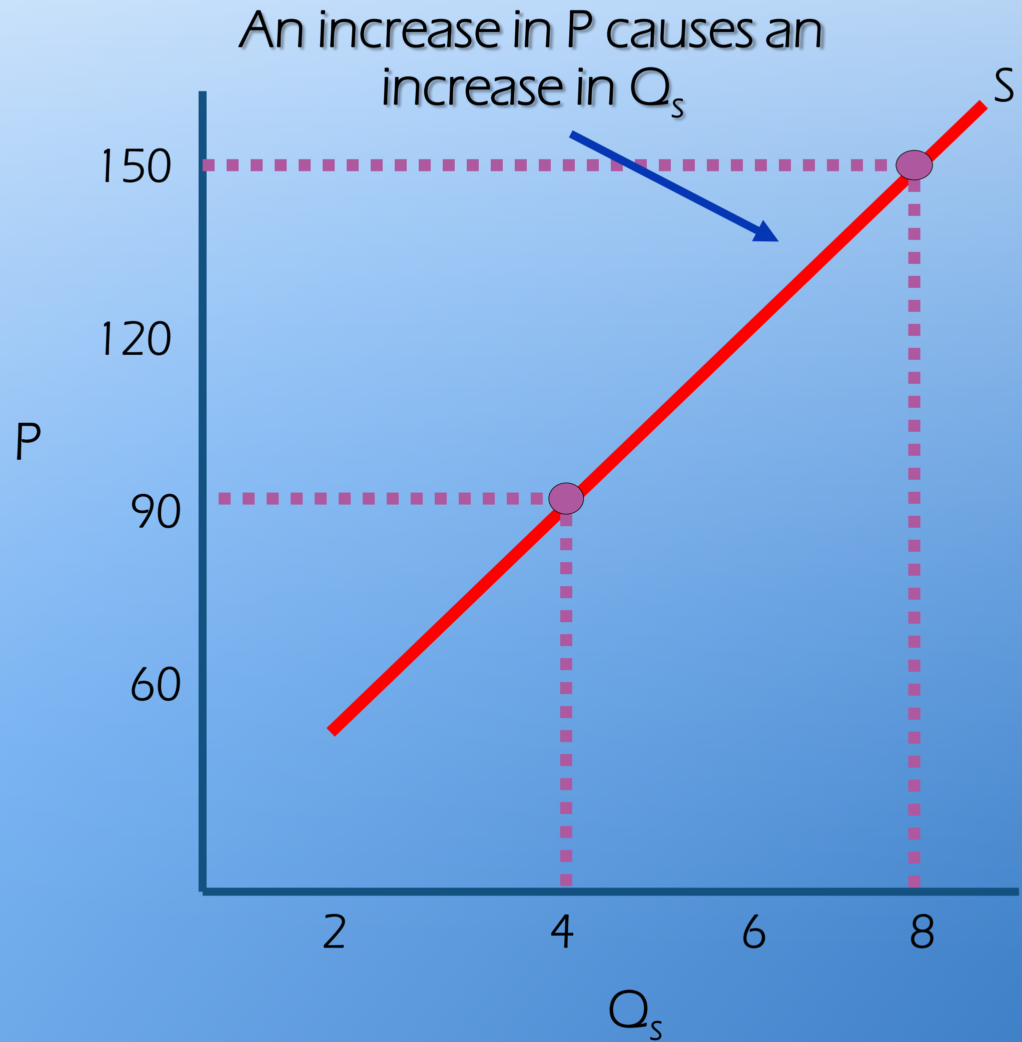
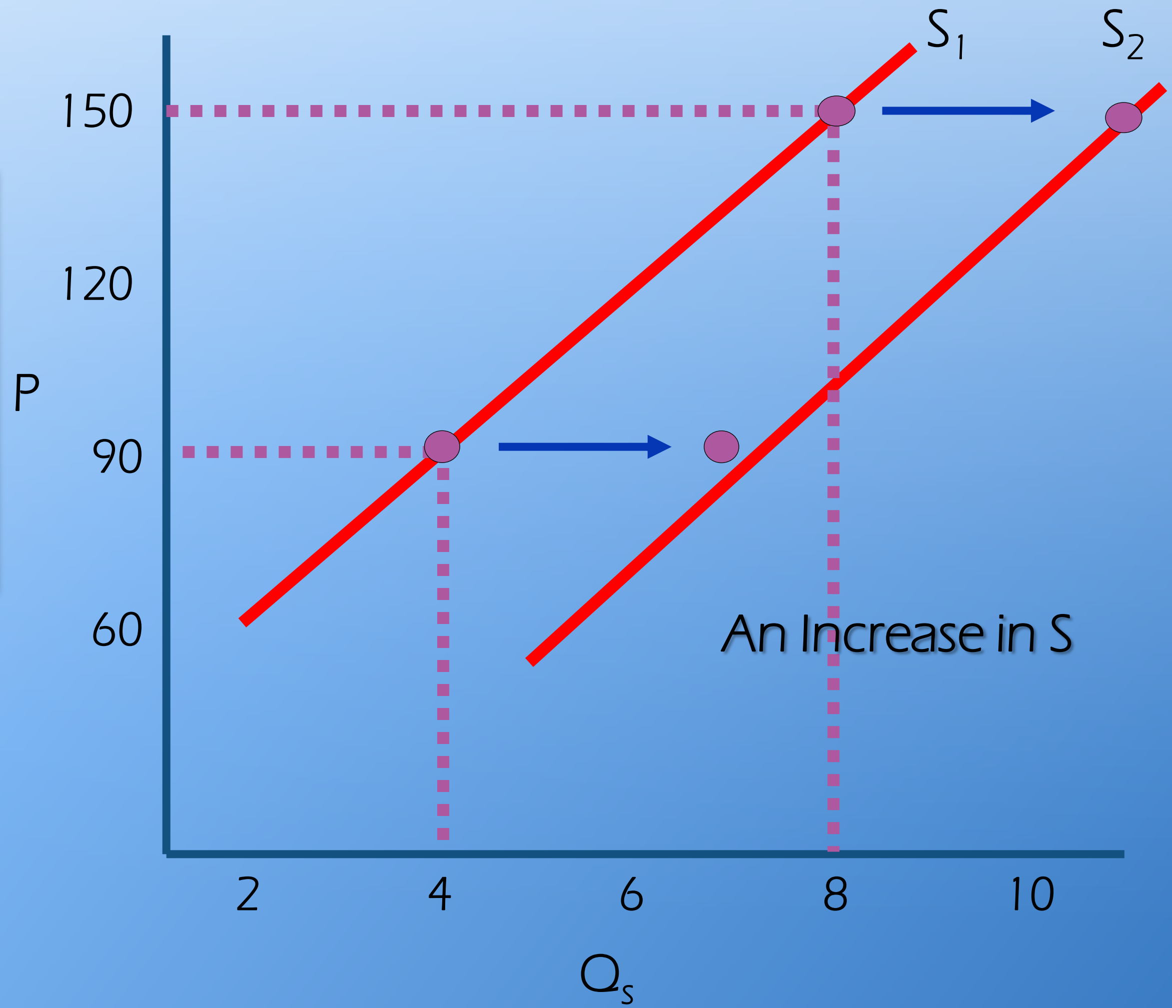


TABLE AND CHART: SUPPLY (S)

P	Q_{s1}	Q_{s2}
$150	8	11
120	6	9
90	4	7
60	2	5



EQUILIBRIUM

The *equilibrium price* is the price at which the quantity of a good demanded in a given time period equals the quantity supplied.

CONTINUED IN *SUPPLY & DEMAND PART III*