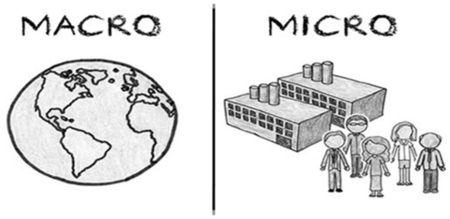
UNIT 2



MICROECONOMICS

Standard SSEMI2

Explain how the law of demand, the law of supply, and prices work to determine production and distribution in a market economy.

a. Define the law of supply and the law of demand.

b. Distinguish between supply and quantity supplied, and demand and quantity demanded.

c. Describe the role of buyers and sellers in determining market clearing price (i.e. equilibrium).

d. Illustrate on a graph how supply and demand determine equilibrium price and quantity.

Demand

Demand: is the desire and ability of consumers to buy a good or service.

Desire without ability does not constitute demand.

Demand

Astin Martin AM-RB 001 –
I have the desire but not the ability to buy one.

McDonalds Happy Meal –
I have the ability but not the desire.

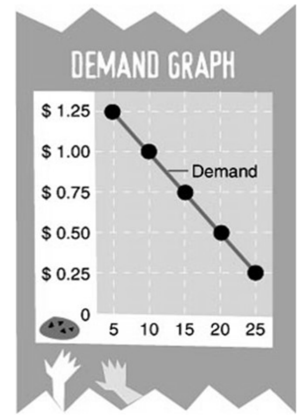
Demand

<u>Demand Schedule</u>: is a table or schedule that shows the various quantities demanded by consumers of a good at all prices that might prevail in the market at a given time

Demand

<u>Demand Curve</u>: is the graphical picture of the demand schedule.

It contains the same information, but in a different format.



Demand

<u>Law of Demand</u>: states that the quantity demanded of a good or service varies <u>inversely</u> with its price.

Inversely means opposite.

When price goes up, the quantity demanded decreases.

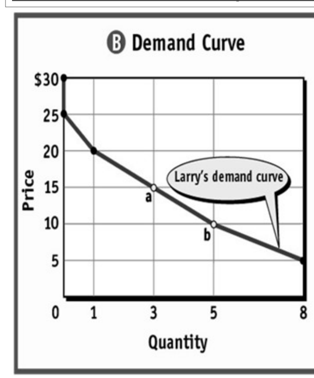
When price goes down, the quantity demanded increases.

<u>The Demand for Compact Discs</u>

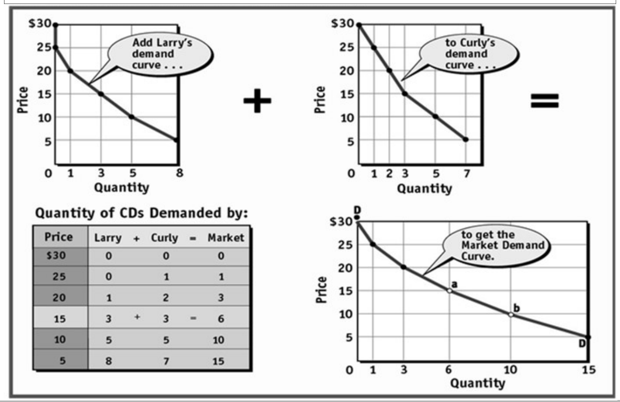
A Demand Schedule

Price	Quantity Demanded
$30	0
25	0
20	1
15	3
10	5
5	8

<u>The Demand for Compact Discs</u>



Individual and Market Demand Curves

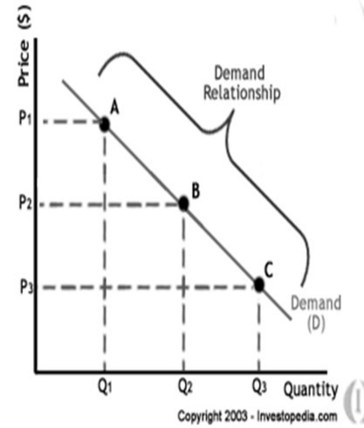


Quantity of CDs Demanded by:

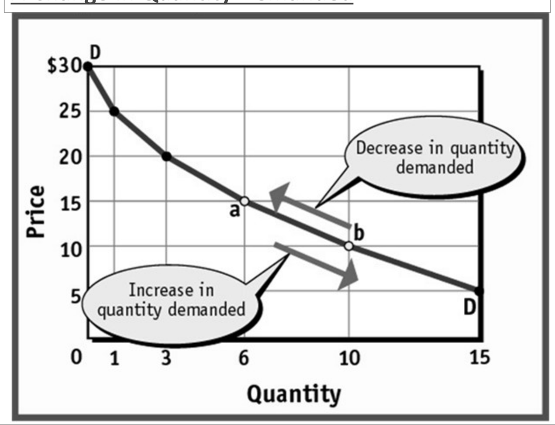
Price	Larry	+	Curly	=	Market
$30	0		0		0
25	0		1		1
20	1		2		3
15	3	+	3	=	6
10	5		5		10
5	8		7		15

<u>Change in Quantity Demanded</u>: this is a movement along the demand curve and shows a change in the quantity purchased in response to a change in price.

This is simply a restatement of the law of demand.

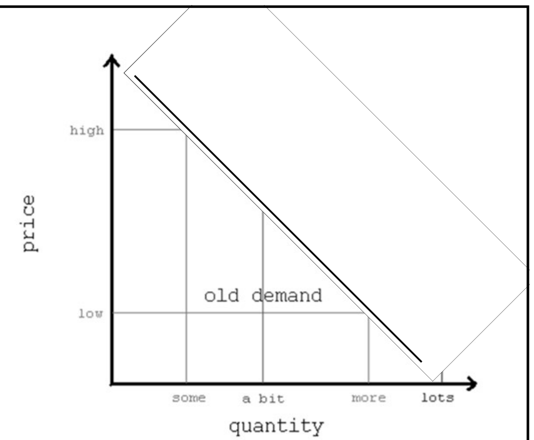


A Change in Quantity Demanded



<u>Change in Demand</u>: occurs when people are now willing to buy different amounts of the product at the same prices as before.

This is shown as a shift in the curve, not a movement along the curve.

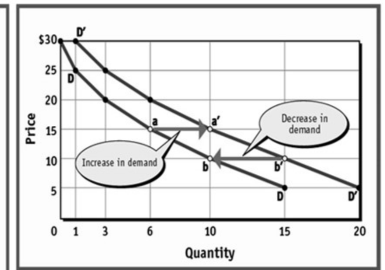


IRDL THE TURTLE

Figure 4.4
A Change in Demand

Quantity Demanded

Price	Old (DD)	New (D'D')
$30	0	1
25	1	3
20	3	6
15	6	10
10	10	15
5	15	20



Standard SSEMI2

Explain how the law of demand, the law of supply, and prices work to determine production and distribution in a market economy.

e. Identify the determinants (shifters) of supply (e.g., changes in costs of productive resources, government regulations, number of sellers, producer expectations, technology, and education) and illustrate the effects on a supply and demand graph.

f. Identify the determinants (shifters) of demand (e.g., changes in related goods, income, consumer expectations, preferences/tastes, and number of consumers) and illustrate the effects on a supply and demand graph.

Demand Shifters

There are 5 factors that <u>can shift the demand curve to the right or left</u>. These factors have nothing to do with the price of the product.

1. Tastes and Preferences **T**
2. Income of Consumers **I**
3. Related Goods **R**
4. Expectation of Change **E**
5. Size & Demographic of Population **S**

T

Tastes & Preferences: this reflects our likes and dislikes.

What affects our tastes:
- Advertising
- news report
- fashion trends
- seasonal changes

I

Income of Consumers:
An increase in income allows consumers to buy more of most goods and services, so the curve shifts right.

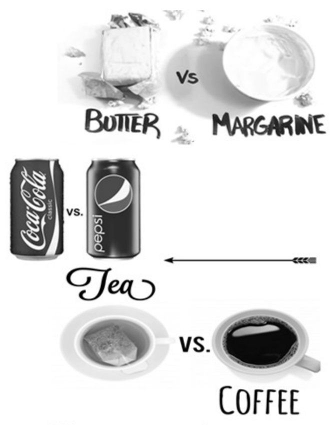
A decrease in income would cause a decrease in demand and therefore a leftward shift of the curve.

R

Related Goods
A change in the price of a related good changes demand for the original good.

Substitutes:
products that can be used in place of other products.

When the price of 1 good goes up, the demand for the substitute will increase, and vice versa.

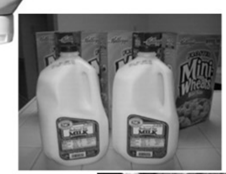


R

Related Goods

Complements:
products that are used together.

When the price of 1 good goes up, the demand for the complement will decrease, and vice versa.



E

Expectation of Change:
demand may change because of the expectation of some future event.

If I expect prices to rise in a few weeks, I might buy more now. If I think I might lose my job soon, I'll begin to spend less now.

S

Size or Demographic of Population:
more buyers in the market will lead to an increase in demand. Fewer buyers will lead to a decrease in demand.

Some things that might affect number of buyers are:

- Population changes
- Immigration trends
- Medical advancements
- Trade Agreements like NAFTA