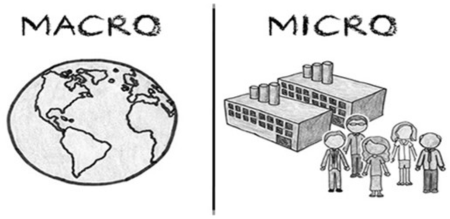
UNIT 2



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.

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.

Price

<u>Price</u>: is the monetary value of a product or service and is established by supply and demand.

Price

Prices act as signals that help us make our economic decisions.

Prices communicate information and provide incentives to buyers and sellers.

Price

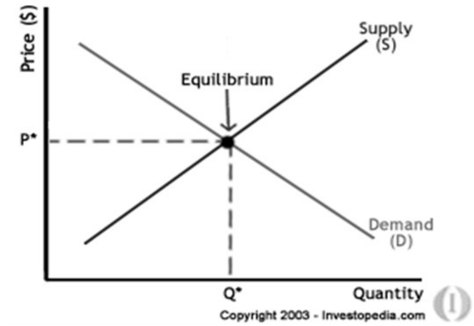
For example:

High Price – firms want to produce more consumer want to buy less

Low Price – firms want to produce less consumers want to buy more

Equilibrium

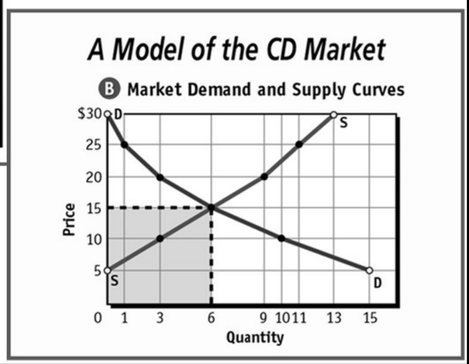
Market Equilibrium: is a situation in which prices are relatively stable and the quantity supplied is equal to the quantity demanded.



A Model of the CD Market

A Market Demand and Supply Schedules

Price	Quantity Demanded	Quantity Supplied	Surplus/ Shortage
$30	0	13	13
25	1	11	10
20	3	9	6
15	6	6	0
10	10	3	−7
5	15	0	−15

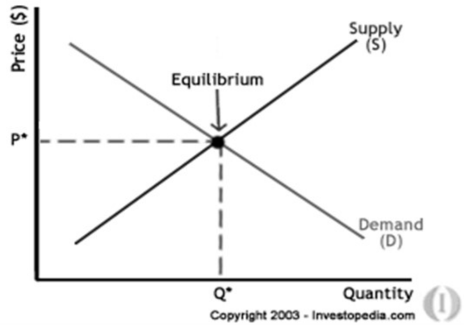


KMHS Market for Muffins

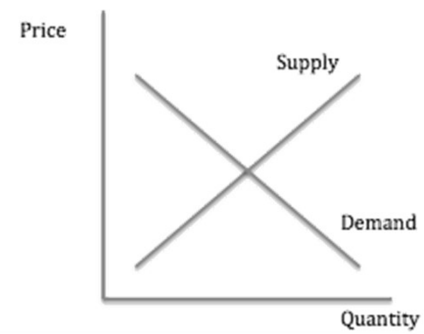
Price	Quantity Supplied	Quantity Demanded
$1.50	200	800
$2.00	300	700
$2.50	400	600
$3.00	500	500
$3.50	600	400
$4.00	700	300

Equilibrium

Equilibrium Price: the price that clears the market by leaving neither a surplus nor a shortage. (Qs = Qd)



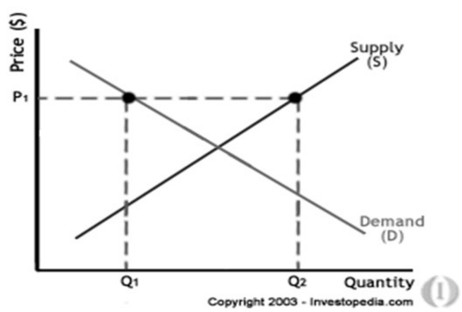
Market for Oranges



1. A late spring freeze ruins half the year's crop of oranges.
2. Scientists announce a new discovery: Orange juice prevents colds.
3. Media reports state Florida oranges are sprayed with an insecticide that allegedly causes cancer.
4. Researchers develop a new fertilizer that increases the yield of orange trees.
5. "An apple a day keeps the doctor away." Everyone is eating more apples.

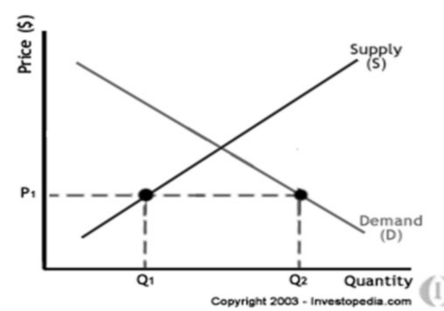
Equilibrium

Surplus: when the quantity supplied is greater than the quantity demanded at a given price. The result of the surplus is that price will fall. (Qs > Qd)



Equilibrium

Shortage: when the quantity demanded is greater than the quantity supplied at a given price. The result of the shortage is that price will rise. (Qd > Qs)



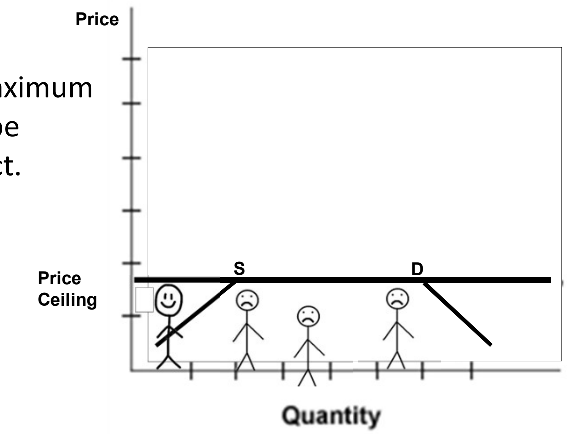
Equilibrium

- Sometimes society may have to sacrifice some efficiency and freedom in order to achieve greater equity and security.
- Think back to the economic and social goals in unit 1.
- One common way to achieve more equity or security for certain groups of people is for the government to set prices at the socially desirable level.
- When this happens, prices are not allowed to adjust to reach equilibrium.

Equilibrium

Price Ceiling: the maximum legal price that can be charged for a product.

Ex. Rent control on apartments



Equilibrium

Price Floor: the lowest legal price that can be charged for a product.

Ex. Minimum wage