

SUPPLY AND DEMAND

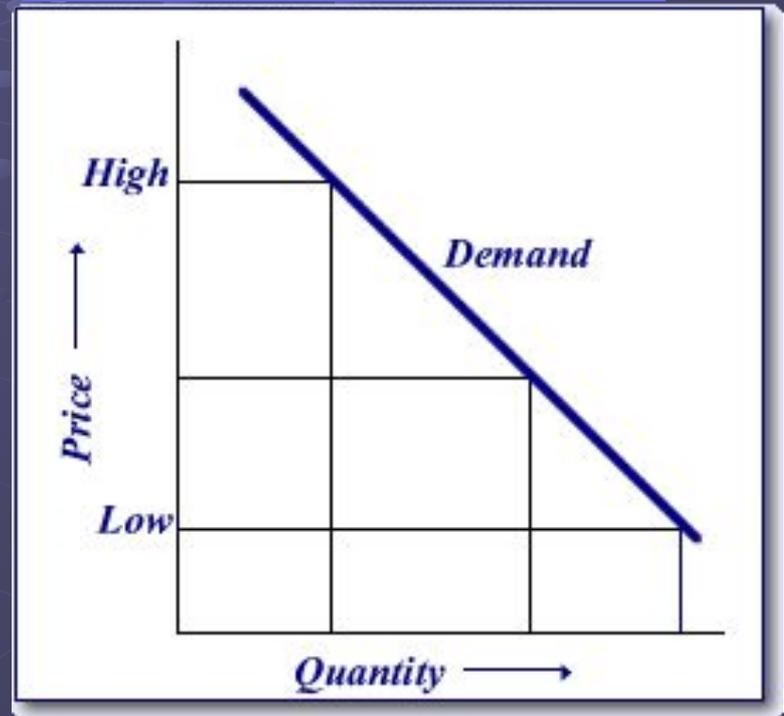
Alex Volkov “ИЭУИС” 1-11

Demand And Supply

Demand

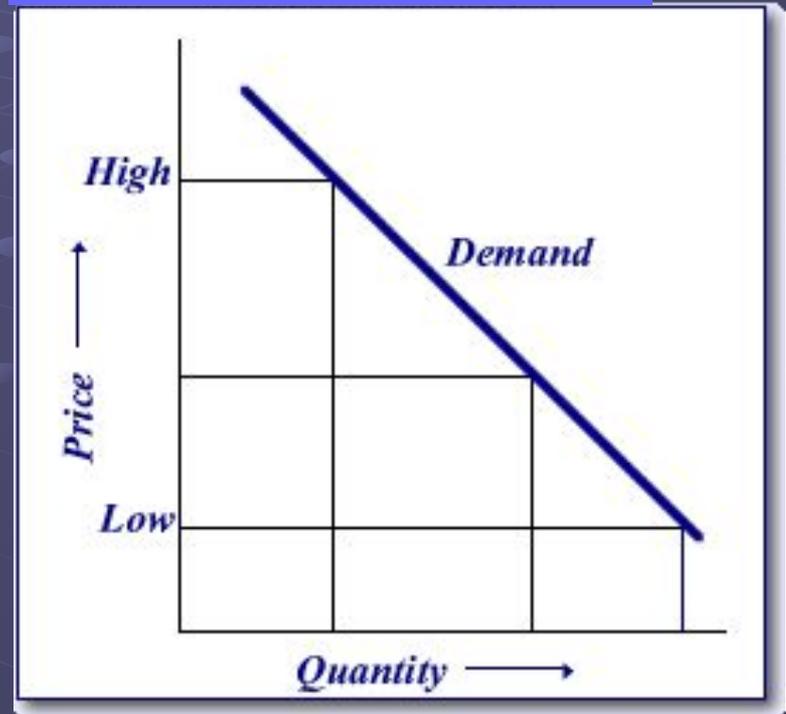
The demand for a product or service is how much of a product or service people are willing and able to purchase at various prices. Demand is represented graphically as a downward sloping curve with price on the vertical axis and quantity on the horizontal axis

Market demand curve



Generally the relationship between price and quantity is negative. This means that the higher the price level the lower will be the quantity demanded and, the lower the price the higher will be the quantity demanded.

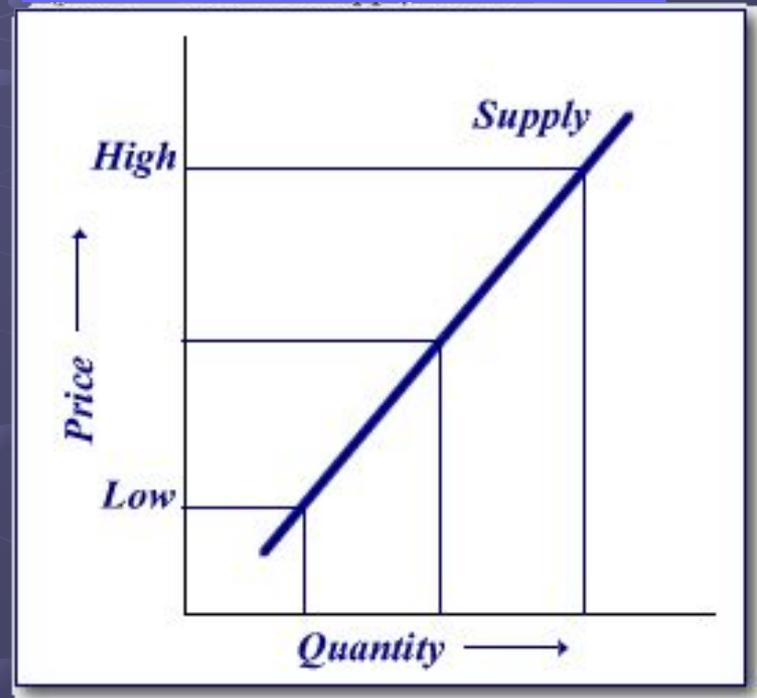
Market demand curve



Supply

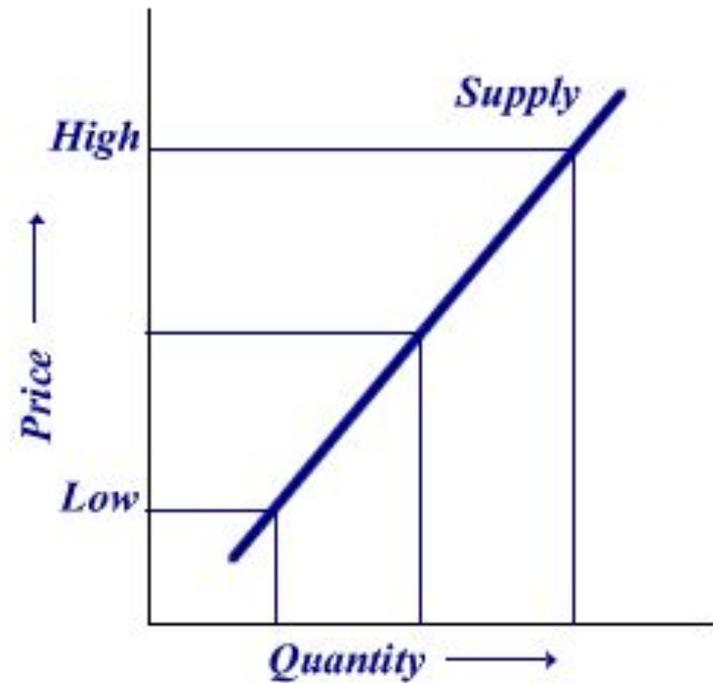
The market or total supply is the quantity producers are willing to supply to the market (sell) over a range of prices for any given time period. The total supply is the sum of the individual amounts of product that each individual producer supplies to the market

Market supply curve



An increase in price in will result in producers wanting to increase the quantity of a product they will sell on the market (chasing profits). Therefore the relationship between the price and supply is positive - the higher the price the higher the quantity supplied.

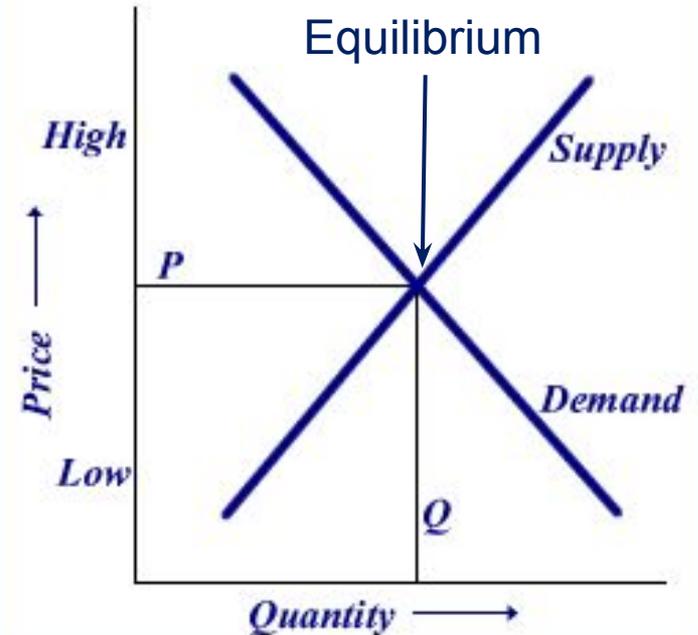
Market supply curve



Equilibrium Price

If we plot both demand and supply curves, where they intersect we have the market equilibrium. This equilibrium gives us the market price (P) and the quantity sold (Q).

Market equilibrium

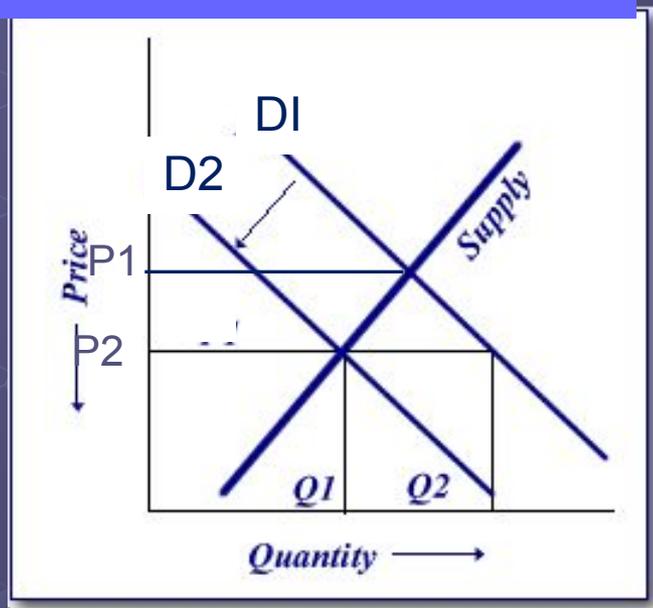


Shifts in Demand and Supply Curves

Both demand and supply curves can shift, that is move inwards or outwards.

When a demand or supply curve shifts this means that at all price levels there will be a change in the quantity demanded or supplied

Market demand curve shifts



Here we see a shift to the left of the demand curve, D1 to D2.

The effect is to reduce quantity demanded from Q2 to Q1, and the price from P1 to P2

Factors that Shift the Demand Curve

1. Change in consumer real incomes.

Because a consumer's demand for goods and services is limited by income, higher income levels allow the consumer to purchase more products, when this happens the demand curve shifts to the right.

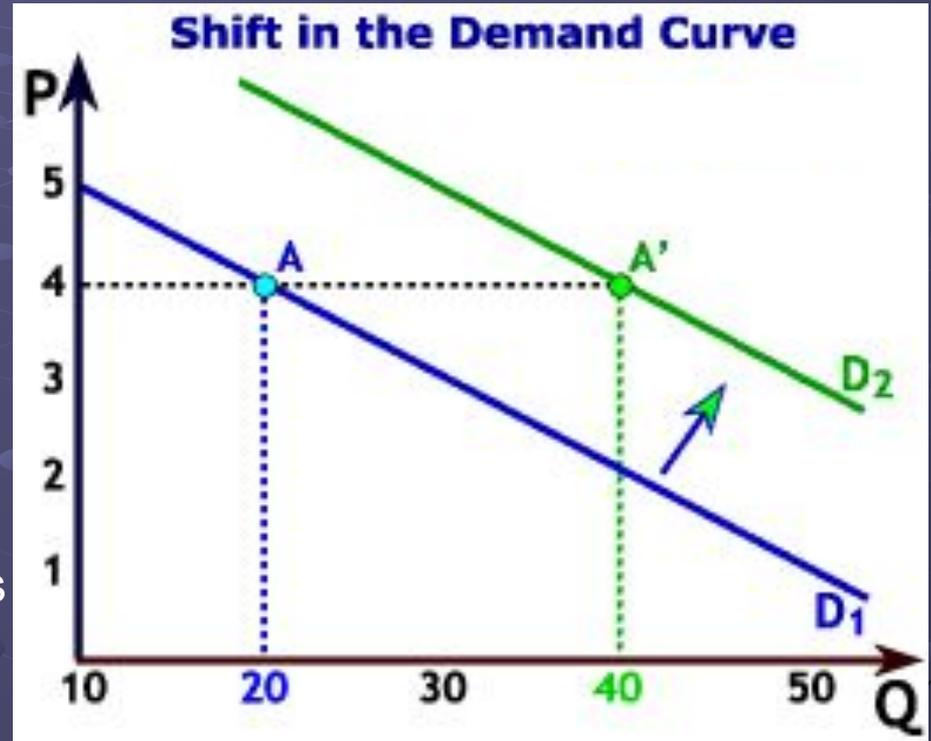
When the opposite occurs, a decrease in real income, this shifts the demand curve to the left. When the economy enters a recession and more people become unemployed and so incomes fall, the demand for many goods and services shifts to the left.

2. Population change:

An increase in population shifts the demand curve to the right D_1 to D_2 .

3. Consumer preferences - fashion:

If a good becomes fashionable the demand curve for that good shifts to the right



4. Prices of related goods: If prices of related goods change, the demand curve for the original good can change as well. Related goods can either be substitutes or complements.

Substitutes are goods that can be consumed in place of one another. If the price of a substitute increases, the demand curve for the original good shifts to the right. People buy less of the substitute, and more of the alternative.

Complements are goods that are normally consumed together. If the price of a complement increases, the demand curve for the original good shifts to the left. If the price of a complement decreases, the demand curve for the original good shifts to the right. If, for example, the price of cars falls, then the demand curve for petrol shifts to the right.

Factors that Shift the Supply Curve

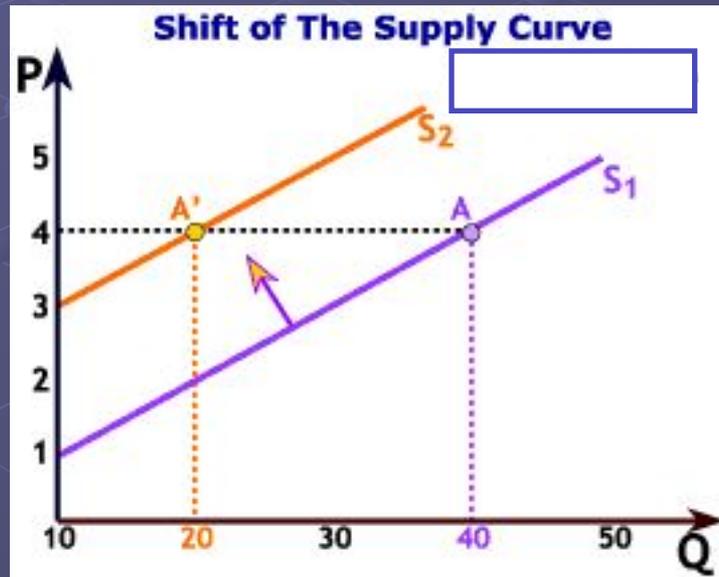
1. Change in input costs:

An increase in input costs shifts the supply curve to the left.

If input costs decline, output increases and the supply curve shifts to the right

2. Change in size of the industry.

If new firms enter an industry, the supply curve shifts to the right.



The diagram shows a shift to the left of the supply curve, (S_1 to S_2). This could have been caused by an increase in costs of supplying companies

3. Improvements in technology:

An improvement in technology shifts the supply curve to the right. Technological progress allows firms to produce a given item at a lower cost. With the advancement of technology, the supply curve for goods and services shifts to the right.

4. Effects of weather, this is especially important for agricultural products

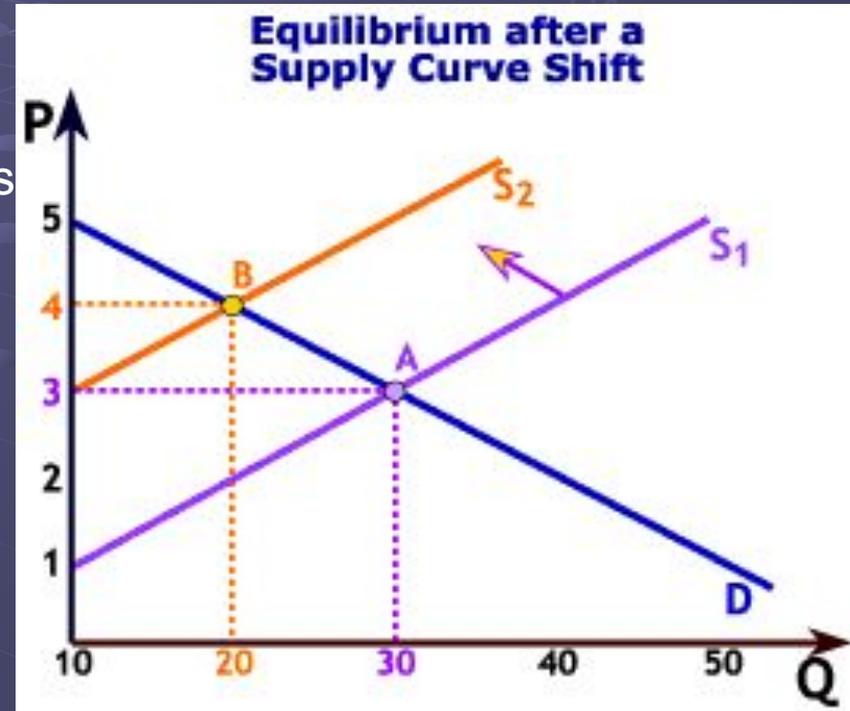
Good weather followed by a good harvest, shifts supply to the right, poor weather leading to a poor harvest shifts supply to the left

Shift in the supply curve

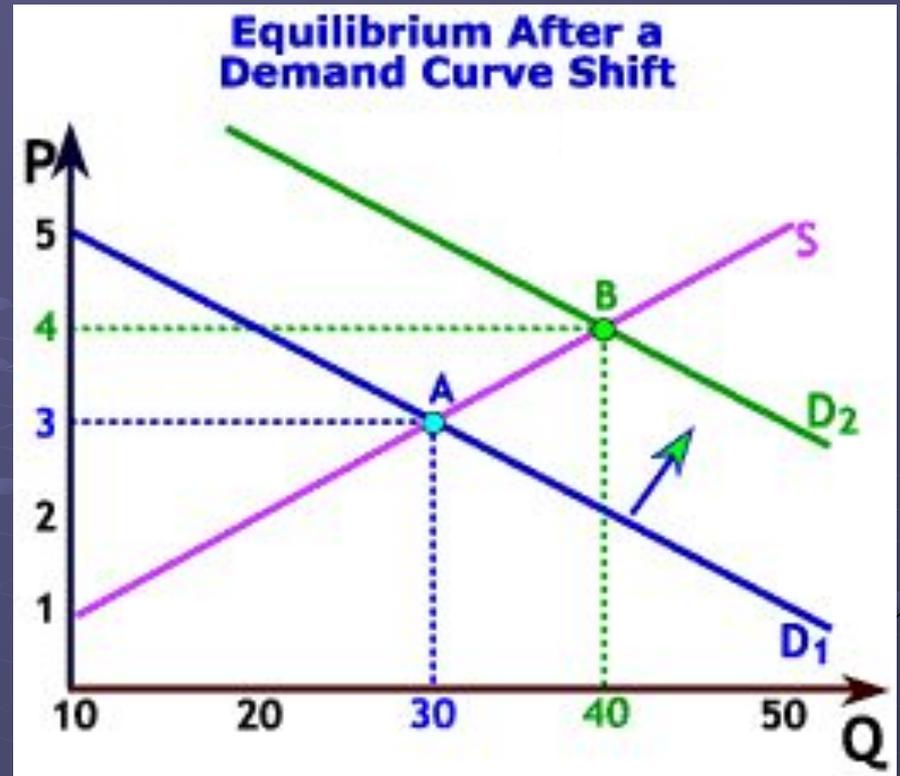
When either demand or supply shifts, the equilibrium price will change.

For example, bad weather normally decreases the supply of fruit. This causes a shift in the supply curve to the left, inwards, from S_1 to S_2 . There is a movement along the demand curve to a new equilibrium Price (£3 to £4)

Consumers will buy less because of the higher price (30 to 20)



If the demand curve were to shift out because of increased real incomes, then the new market equilibrium would be at a higher price and higher level of output, than the previous equilibrium.



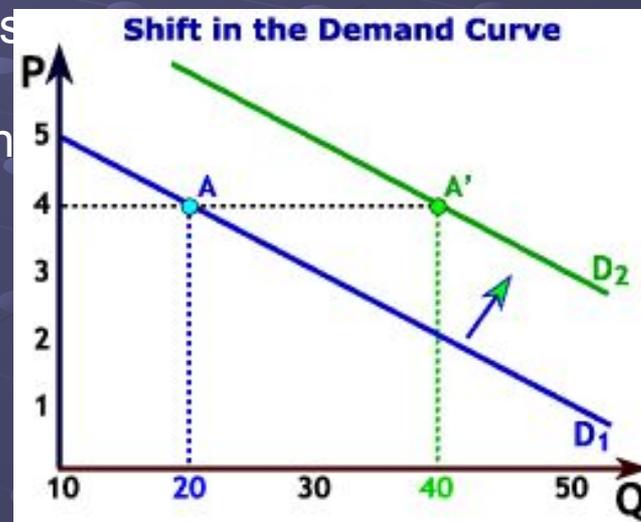
Here the curve shifts from D1 to D2, demand increases from 30 to 40, and price has increased from £3 to £4.

A movement along a Demand Curve

It is essential to distinguish between a *movement along* a demand curve and a *shift* in the demand curve. A change in price results in a movement along a fixed demand curve.

This is also referred to as a *change in quantity demanded*. For example, an increase in coffee prices from £2 to £4 may reduce the quantity demanded from 40 units to 20 units. This price change results in a movement along a given demand curve.

A change in any other variable that influences quantity demanded (for example an increase in incomes) produces a shift in the demand curve. A shift in the demand curve changes the equilibrium position. So this increase in incomes has increased demand for coffee from 20 to 40 at a price of £4

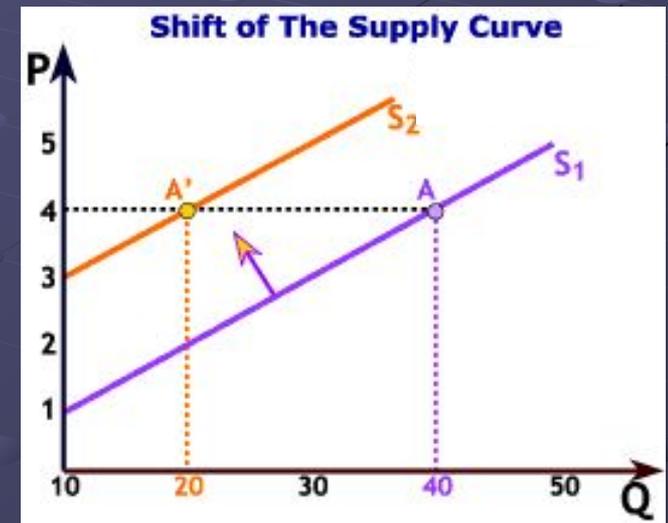


A movement along a Supply Curve

As with demand curves, it is essential to distinguish between a *movement along* a given supply curve and a *shift* in a supply curve.

A change in price results in a movement along a fixed supply curve. This is also referred to as a *change in quantity supplied*. For example, if the selling price of coffee rises from £3 to £4, quantity supplied increases from 30 to 40 units (A)

A change in any other variable that influences quantity supplied (e.g. costs of production) produces a shift in the supply curve. This shift to the left could be caused by increased rent for coffee shops.



Increased rental charges, shifts the supply curve to the left – less coffee shops, less coffee supplied. Now at price of £4 only 20 units supplied (A1).