

1 Demand

Tuesday, October 19, 2021 1:33 AM

Demand

All of the quantities of a good or service that buyers would be willing and able to buy at all possible prices; demand is represented graphically as the entire demand curve.

Quantity Demanded

The specific amount that buyers are willing to purchase at a given price; each point on a demand curve is associated with a specific quantity demanded.

Change in quantity demanded

A movement along a demand curve caused by a change in price; a change in quantity demanded is a movement along the *same* curve

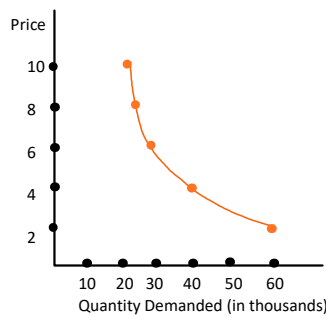
Change in demand

When buyers are willing to buy a different quantity at all possible prices, which is represented graphically by a shift of the entire demand curve; this occurs due to a change in one of the determinants of demand.

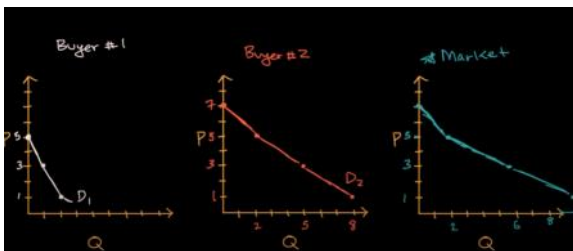
Law of demand

All other factors being equal, there is an inverse relationship between a good's price and the quantity consumers demand; in other words, when price goes down, people respond by buying a larger quantity.

Demand Schedule		
Scenario	Price	Quantity Demanded
A	2	60,000
B	4	40,000
C	6	30,000
D	8	25,000
E	10	23,000



Market Demand as a sum of Individual demand



Normal good

A good for which demand will increase when buyers' incomes increase (e.g. - movie tickets)

Inferior good

A good for which demand will decrease when buyers' incomes increase (e.g. - cheap car)

Substitute goods

Goods that can replace each other; when the price of a good increases, the demand for its substitute will increase.

Complement goods

Goods that tend to be consumed together; when the price of a good increases the demand for its complement will decrease.

From where do we get the demand curve?

1 Substitution Effect

The substitution effect is the decrease in sales for a product that can be attributed to consumers switching to cheaper alternatives when its price rises.

2 Income Effect

The income effect is the change in demand for a good or service caused by a change in a consumer's purchasing power resulting from a change in **real income**. This change can be the result of a rise in wages etc., or because existing income is freed up by a decrease or increase in the price of a good that money is being spent on.

For normal goods: E.g. - movie tickets

Income falls Makes you poorer Consumption falls

For inferior goods: E.g. - noodles

Income falls Makes you poorer Consumption rises

3 Diminishing Marginal Utility

Each extra unit of good increases the utility by less than the previous unit of the good

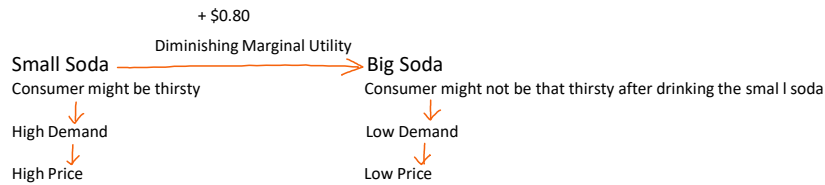
E.g. - The difference in soda prices in McD for small soda and larger soda is less

Small soda = \$1.25 + \$0.80

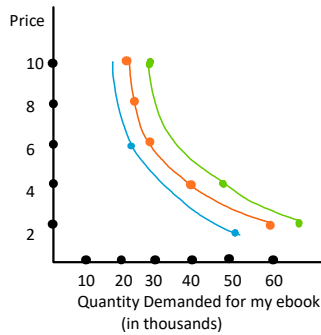
Each extra unit of good increases the utility by less than the previous unit of the good

E.g. - The difference in soda prices in McD for small soda and larger soda is less

Small soda = \$1.25
Big Soda = \$2.05



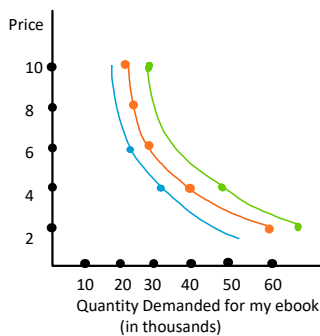
Price of related products and demand



Price of other ebooks rises - at any point of price, my ebook will be a good **substitute**. Hence, demand will rise at every price

Price of Kindle rises - at any given price, quantity demanded will lower since Kindle is a **complementary** product

Change in expected Future Prices, Income, Population or Preferences and Demand



Future Prices

Expect the Future prices might go up - demand increases
Expect the future prices to go down - demand decreases

Income Changes (only for normal goods)

Income increases - demand increases
Income decreases - demand decreases

Population changes

Population increases - demand increases
Population decreases - demand decreases

Determinants of change in Demand

TONIE -

Taste, Other goods (complementary and substitute goods), Number of buyers, Income, Expectations (future price)

Change in demand vs. change in quantity demanded

- A change in demand and a change in quantity demanded are not the same thing. **Demand changes only when one of the determinants of demand change (TONIE)**. For instance, rising consumer incomes (one of the determinants) will increase demand for new cars, a normal good, which would shift the entire demand curve to the right. More cars will be demanded at every price when demand increases.
- Price is not a determinant of demand, thus a change in **price does not cause demand to increase or decrease**. If the price of new cars changes, ceteris paribus, there will be a change in the quantity demanded and a movement along the demand curve

2 Supply

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The law of supply

The law of supply states that there is a positive relationship between price and quantity supplied, leading to an upward-sloping supply curve. Sellers like to make money, and higher prices mean more money!

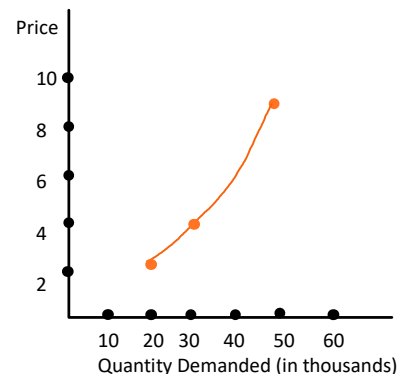
Common Misperceptions

You may often hear people say, incorrectly, that higher prices lead to “more supply” and that lower prices lead to “less supply.” However, this is an incorrect use of the terms. Higher prices will result in an increased quantity supplied and lower price will result in a decrease in quantity supplied. **Only a change in a non-price determinant of supply causes a good's supply to increase or decrease.**

Determinants of supply

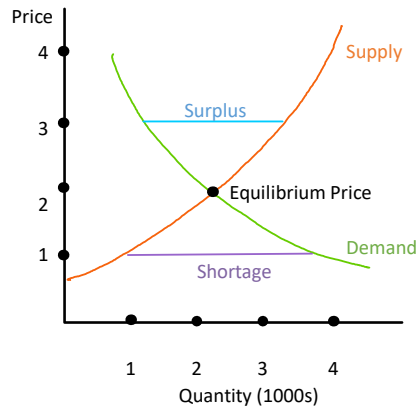
changes in non-price factors that will cause an entire supply curve to shift (increasing or decreasing market supply); these include

- 1) the number of sellers in a market (no. of sellers goes up, supply goes up)
- 2) the level of technology used in a good's production (technology improves, supply goes up)
- 3) the prices of inputs used to produce a good (price of input goes up, supply goes down)
- 4) the amount of government regulation, subsidies or taxes in a market (regulations increases, supply goes down)
- 5) the price of other goods sellers could produce (price of other goods goes up, supply goes down)
- 6) the expectations among producers of future prices (expected prices to go up, supply goes down)



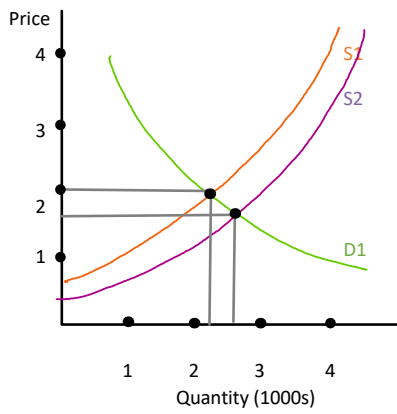
3 Market equilibrium and changes in equilibrium

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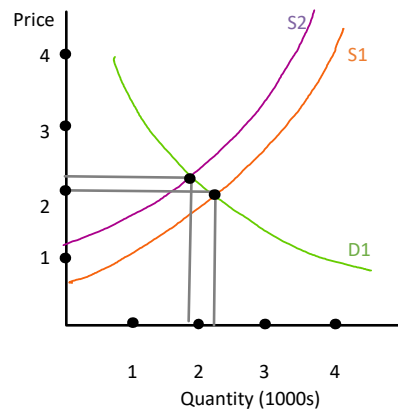
Changes in market equilibrium

1) Supply Increases



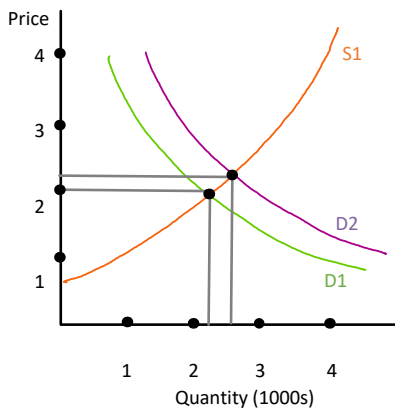
Price decreases
Quantity Increases

2) Supply Decreases



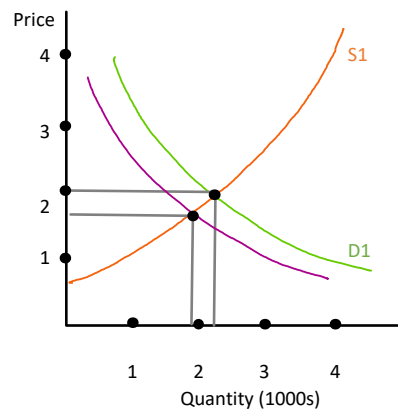
Price Increases
Quantity Decreases

3) Demand Increases



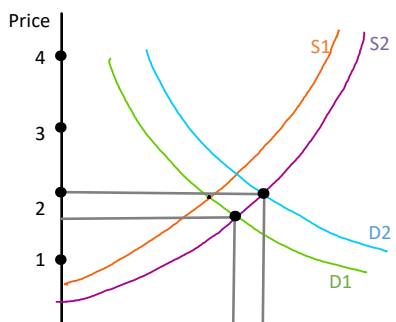
Price Increases
Quantity Increases

4) Demand Decreases



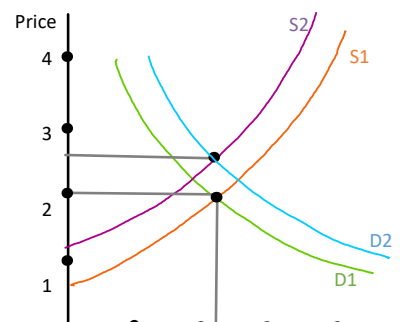
Price Decreases
Quantity Decreases

5) Supply Increases and Demand Increases

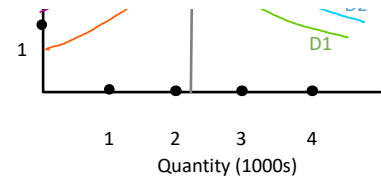
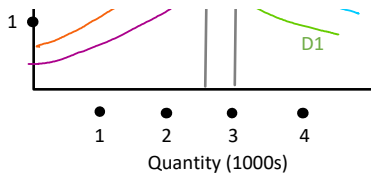


Price indeterminate
Quantity Increases

6) Supply Decreases and Demand Increases



Price Increases
Quantity indeterminate



7) Demand Decreases and Supply Increases



Price Decreases
Quantity indeterminate

8) Demand Decreases and Supply Decreases



Price indeterminate
Quantity Decreases