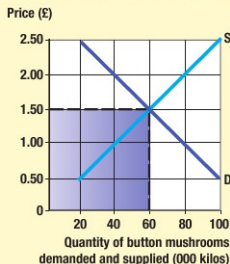

Markets

2017-18

THE INTERACTION OF SUPPLY AND DEMAND

- ▶ We say that *markets clear* when $\text{supply} = \text{demand}$
- ▶ The price level where $\text{supply} = \text{demand}$ is known as *equilibrium price*

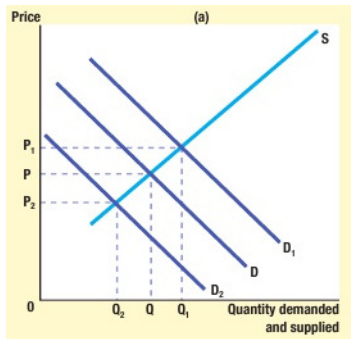
The demand for and supply of button mushrooms



- ▶ Since *equilibrium price* and *equilibrium quantity* is known, we can compute the *total revenue* at equilibrium:
$$TR = P \times Q$$

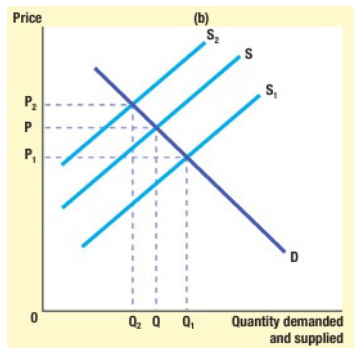
CHANGES IN DEMAND

- ▶ **if the demand for a product increases**
→ prices ↑
- ▶ **if the demand for a product falls**
→ prices ↓



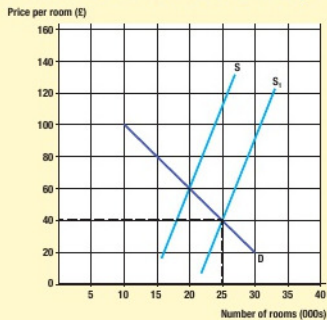
CHANGES IN SUPPLY

- ▶ **if the supply for a product increases**
→ prices ↓
- ▶ **if the supply for a product falls**
→ prices ↑



WORKED EXAMPLE

The market for accommodation in a UK city

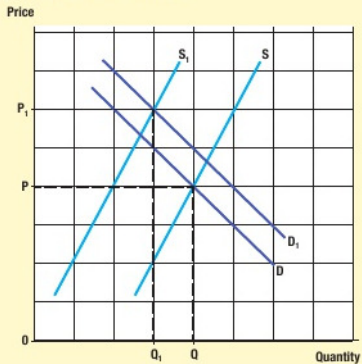


CHANGES IN SUPPLY AND DEMAND TOGETHER

- ▶ if supply and demand change simultaneously

CHANGES IN SUPPLY AND DEMAND TOGETHER

A change in supply and demand



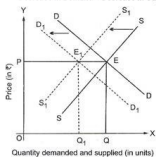
CHANGES IN SUPPLY AND DEMAND TOGETHER

BOTH DEMAND AND SUPPLY DECREASE

The effect on price and quantity depends on

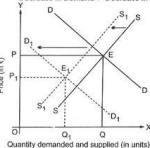
- ▶ steepness of the curves
- ▶ amplitude of the shift

Decrease in Demand = Decrease in Supply



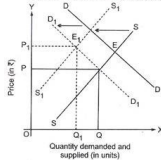
- New Equilibrium is determined at E₁
- Equilibrium Price remains same at OP
- Equilibrium Quantity falls from OQ to OQ₁

Decrease in Demand > Decrease in Supply



- New Equilibrium is determined at E₁
- Equilibrium Price falls from OP to OP₁
- Equilibrium Quantity falls from OQ to OQ₁

Decrease in Demand < Decrease in Supply

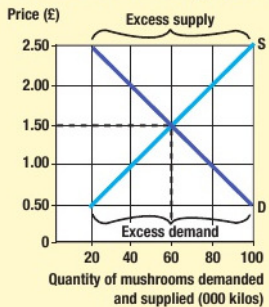


- New Equilibrium is determined at E₁
- Equilibrium Price rises from OP to OP₁
- Equilibrium Quantity falls from OQ to OQ₁

DISEQUILIBRIUM IN THE MARKET

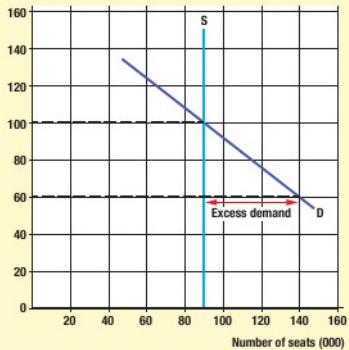
- ▶ *Excess demand*: if the price charged in the market is *below* the equilibrium price
- ▶ *Excess supply*: if the price charged is set *above* the equilibrium price

The excess demand for and excess supply of button mushrooms



The market for FA Cup Final tickets

Price per seat (£)



KEY TERMS

- ▶ **Equilibrium price or market clearing price:** the price where supply and demand are equal
- ▶ **Excess demand:** the position where demand is greater than supply at a given price and there are shortages in the marketing
- ▶ **Excess supply:** the position where supply is greater than demand at a given price and there are unsold goods in the market
- ▶ **Total revenue or total expenditure:** the amount of revenue generated from the sale of goods calculated by multiplying price by quantity in a given period of time