FUNDAMENTALS OF SUPPLY AND DEMAND

Introducing Microeconomics

Microeconomics: The study of how individuals, households, and firms make decisions about using limited resources.

Economic resources include:

Human resources: Workers and managers.

Nonhuman resources: Land, technology, minerals, oil, etc.

Microeconomists assume that people and firms are rational and seek to **maximize** benefits.

Trade-offs: Choosing one thing requires giving up another.

Scarcity: The existence of limited resources.

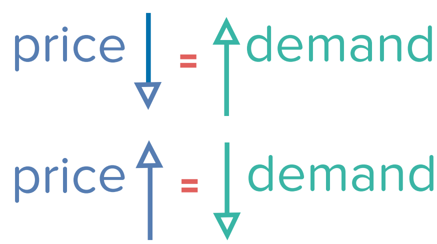
When an individual or group makes a decision, their **opportunity cost** is equal to the value of the foregone option(s)**.**

Economic units: People, households, and firms.

Marginal benefits: Small, incremental benefits.

Supply and Demand

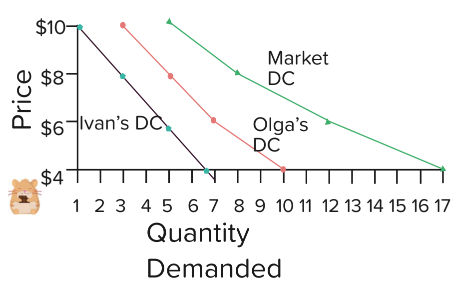
Law of demand: When the price of a good increases, demand for it decreases, and vice versa.



Demand schedule: Lists the quantity demanded of a product or service at various prices.

Market demand schedule: A demand schedule that encompasses the entire market's demand for a good or service at various price points.

Demand curve (DC): Plots the quantity of a good or service demanded at different prices.



Market demand curve: Shows the market demand schedule.

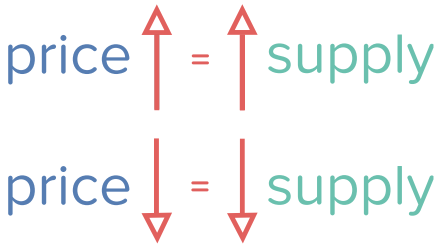
When **demand curves shift:**

to the *left*—market demand has decreased.

to the *right*—market demand has increased.

Market price: The price at which a good or service is offered in the marketplace.

Law of supply: When the market price for a good increases, the quantity that suppliers produce and sell increases, and vice versa.

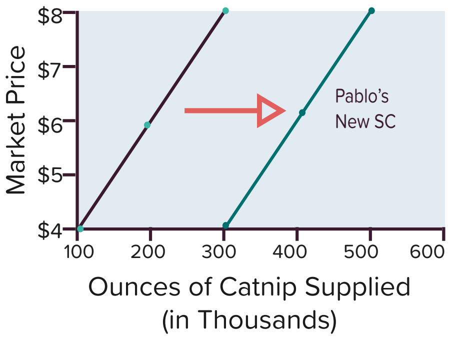


Supply schedule: Lists the quantity of a product supplied at various price points.

Supply curve (SC): Plots the supply schedule.

Market supply: The summation of all of the individual supplies of a good or service.

Market supply curve: Shows how the total quantity supplied of a good changes as its price changes.



When **supply curves shift:**

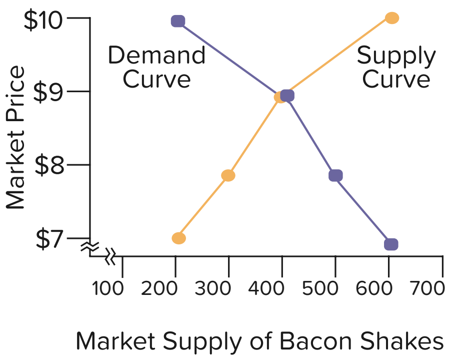
to the *left*—market supply has decreased.

to the *right*—market supply has increased.

Factors Contributing to Equilibrium

Equilibrium: When the amount of goods supplied is equal to the quantity demanded.

Equilibrium price: The price where equilibrium occurs ($9 on the chart).



Equilibrium quantity: The quantity where equilibrium occurs (400 on the chart).

Equilibrium point (EP): The point at which the price and quantity demanded is equal to the price and quantity supplied.

Price acts as a motivator:

When there is a *low* price for goods or services, consumers buy more and sellers supply less.

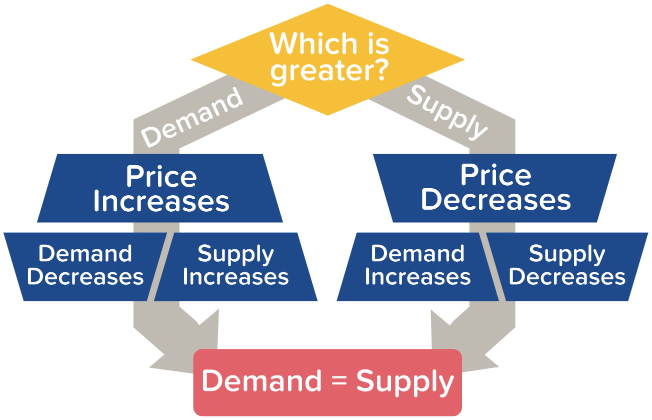
When there is a *high* price for goods or services, consumers buy less and sellers supply more.

Law of supply and demand: The price of any good will naturally adjust until market equilibrium is reached.

Supply > **demand:** There is a **surplus**. Prices will drop until equilibrium is met.

Demand > **supply:** There is a **shortage**. Prices will rise until equilibrium is met**.**

Supply = **demand:** The market has reached equilibrium.



To recognize events that alter equilibrium:

1. Identify a shift in the DC and/or the SC.
2. Determine if the curve(s) shift left or right.
3. Use a graph to see how the shifts change the EP.