Week 3 Overview

Supply and Demand

Overview

Welcome to Week 3! Last module we introduced the supply and demand model to explain how free markets work. One of the main concepts we learned about free markets was that they tend to gravitate toward an "equilibrium" price and quantity. This module we will use the same conceptual model to answer one important question: **Are free markets the best way to distribute society's resources?**

In order to answer this question we are going to have to answer these other questions first:

- How do economists measure social welfare?
- How much social welfare is generated by free markets?
- Is it possible to generate more social welfare by distributing society's resources in a different way, namely through government intervention?

Goals and Objectives

After you actively engage in the learning experiences in this module, you should be able to:

- Apply the concept of "surplus" to measure social welfare in an economy.
- Use the model of supply and demand to illustrate the social welfare generated by a market situation.
- Use the model of supply and demand to see the effects government intervention (such as price controls) has on social welfare.

Key Phrases/Concepts

Keep your eyes open for the following key terms or phrases as you complete the readings and interact with the lectures. These topics will help you better understand the content in this module.

- Equilibrium
- Consumer surplus
- Producer surplus
- Total surplus
- Price ceilings
- Price floors

Guiding Questions

Develop your answers to the following guiding questions while completing the readings and working on assignments throughout the week.

- What measures consumer welfare in an economy?
- What measures producer welfare in an economy?
- What happens to total surplus when the government imposes either a price ceiling or a price floor in the market?

Optional Readings and Resources

- Chapters 4 and 5, *Microeconomics,* Krugman and Wells, 3rd Ed.
- Econ Tutorial: Government Policies