Study Guide

Chapter 3  Supply and Demand

1. Competitive market

2. Demand
   a) Relationship between quantity demanded and price
   b) Factors that influence demand: income; tastes; price of complements; price of substitutes; expectation of future price; etc.
   c) Substitute goods (such as Coke and Pepsi, hamburgers and sandwiches); complementary goods (such as toothpaste and toothbrush; Oreo and milk).
   d) Demand schedule – is a **table** showing the relationship between price and quantity demanded.
   e) Demand curve – is a downward slopping **line** showing the relationship between price and quantity demanded.
   f) Law of demand
   g) Changes in quantity demanded (if quantity demanded increase, a point on the curve moves to the right and down along the same curve; it moves to the left and up otherwise.)
   h) Changes in demand (if demand increases, the demand curve shifts to the right; it shifts to the left otherwise)
   i) Market demand

3. Supply
   a) Relationship between quantity supplied and price
   b) Factor that influence supply: technology; prices of resources (i.e. cost of production); price of other related goods; expectation of future prices; number of seller in the market, etc.
   c) Supply schedule and curve
   d) Law of supply
   e) Changes in quantity supplied (if quantity supplied increase, a point on the curve moves to the right and up along the same curve; it moves to the left and down otherwise.)
   f) Changes in supply (if supply increases, the supply curve shifts to the right; it shifts to the left otherwise)
   g) Market supply

4. Market equilibrium
   a) When quantity supplied equals quantity demanded, the market is in equilibrium (i.e. when the amount of a product firms want to sell exactly matches with the amount of product consumers want to buy **at a particular price**, the market is in equilibrium). This particular price is called equilibrium price, and that equal amount of product being bought and sold is equilibrium quantity.
   b) Excess demand – shortage
   c) Excess supply – surplus
### d) If there is shortage, the excess demand will push the price up until it equals equilibrium price; if there is surplus, the excess supply will push the price down until it equals equilibrium.

### e) A change in demand (or supply) will lead to a change in equilibrium.

#### Figure 3-1

![Graph showing supply (S) and demand (D) curves]

#### Example. Refer to Figure 3-1,

1. The equilibrium price is $10, equilibrium quantity is 50.

2. If the price is $14, the amount people want to buy (quantity demanded) is 30; the amount firms want to offer for sale (quantity supplied) is 70; there is a surplus because quantity supplied is greater than quantity demanded.
   The amount of surplus = $70 - 30 = 40.$
   The surplus will push the price down until it reaches $10.

3. If the price is at $8, quantity demanded is 60 (you can find the quantity demanded on the demand curve), quantity supplied is 40 (you can find the quantity supplied on the supply curve). Since quantity demanded is greater than the quantity supplied, there is a shortage.
   The amount of the shortage = 60 - 40 = 20.
   The shortage will push the price up until $10.

*Now test your understanding!* If the price is at $12, what is the quantity demanded? Quantity supplied? Is there a shortage or surplus? In what amount?

Answer: 40; 60; surplus; 20.