

OUTLINE — September 5, 2018

- Economic Systems
- Model of Supply and Demand
 - Demand
 - Supply
 - Equilibrium

Fill in the empty seats

Laptops closed; Cell phones silenced & put away

Announcements sent by e-mail

Extra handouts: in racks outside 532 Evans

Who decides: What, How, For Whom?

- Depends upon the “Economic System”
 - Command Economy
 - Laissez-Faire Economy
 - Commonly called free or open market system
 - “Consumer Sovereignty”
 - Mixed Economy

Economic Systems Demand Supply Equilibrium

Model of Demand & Supply

- Question
- Simplifications
- Assumptions

Economic Systems **Demand** Supply Equilibrium

Demand

- For a particular product, what quantity will buyers be willing and able to buy at each of many prices?

Economic Systems **Demand** Supply Equilibrium

What about time frame?

of pairs of jeans you would buy . . .

- . . . per week?
- . . . per year?
- . . . per decade?

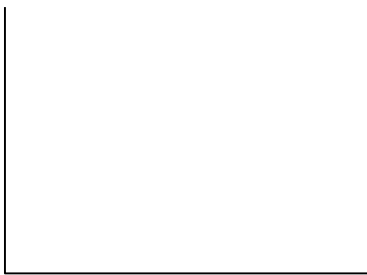
Economic Systems **Demand** Supply Equilibrium

Need more information

- Define market precisely
- Make assumptions explicit
 - When I ask about response to change in price, assume only price is changing
- "*Ceteris Paribus*" = "holding all else constant"

Economic Systems **Demand** Supply Equilibrium

Demand for new jeans



Economic Systems **Demand** Supply Equilibrium

p and q_D are Inversely Related

- Terminology
 - Individual Demand
 - Market Demand
- "Law of Demand"
- More Terminology – *very important!*
 - Demand
 - Quantity Demanded

Economic Systems **Demand** Supply Equilibrium

Change in Income: Normal Good

- ↑ Buyer Income



Economic Systems **Demand** Supply Equilibrium

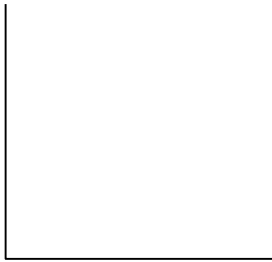
What shifts Demand?

- Δ price \Rightarrow *MOVE ALONG* curve
- Δ anything else \Rightarrow *SHIFT OF* curve
- What shifts demand? Recall our assumptions!
 - If any of these 5 things change, demand shifts
 - 1.
 - 2.
 - 3.
 - 4.
 - 5.

Economic Systems **Demand** Supply Equilibrium

Change in Income: Inferior Good

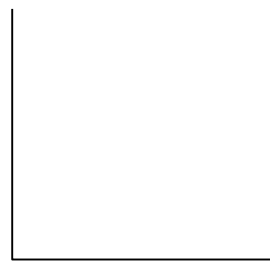
- ↑ Buyer Income



Economic Systems **Demand** Supply Equilibrium

Change in Wealth: Normal Good

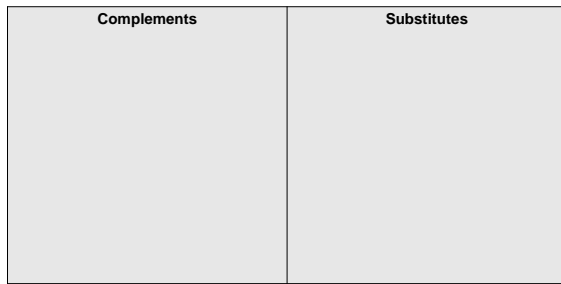
- ↑ Buyer Wealth



Economic Systems **Demand** Supply Equilibrium

A Different Example

- Instead, think about demand for a 50-yardline alumni-section ticket to the Cal-Stanford football game.



Economic Systems Demand Supply Equilibrium

Change in "Other Prices"

- Complements in Demand:
 ↓ P of complement



Economic Systems **Demand** Supply Equilibrium

Change in "Other Prices"

- Substitutes in Demand:
 ↑ P of substitute



Economic Systems **Demand** Supply Equilibrium

Change in Preferences

- Preference shifts away from good:



Economic Systems **Demand** Supply Equilibrium

Supply

- For a particular product, what quantity will be offered for sale at each of many prices?
 - Individual firm supply
 - Market supply

Economic Systems Demand **Supply** Equilibrium

Again, need more information

- Define market precisely
 - product characteristics
 - time period
- Make assumptions explicit
 - When I ask about response to change in price, assume
- "*Ceteris Paribus*" = "holding all else constant"

Economic Systems Demand **Supply** Equilibrium

Supply Curve



Economic Systems Demand **Supply** Equilibrium

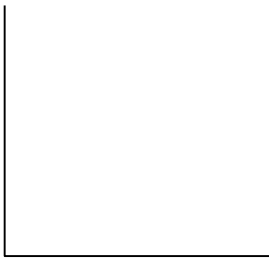
p and q_s are Directly Related

- Terminology important!
 - ✓ Supply
 - ✓ Quantity Supplied

Economic Systems Demand **Supply** Equilibrium

Change in Input Costs

- ↑ cost of input



Economic Systems Demand **Supply** Equilibrium

What Shifts Supply?

- $\Delta p \Rightarrow$ MOVE ALONG curve
- Δ anything else \Rightarrow SHIFT OF curve
- What shifts Supply? Recall our assumptions!
- If any of these things change, supply shifts
 - input costs
 - technology
 - prices of related products
 - # of sellers

Economic Systems Demand **Supply** Equilibrium

Change in Technology

- better technology



Economic Systems Demand **Supply** Equilibrium

Change in price of “related products”

- Substitutes in production (either – or)



- ↑ price of substitute output

Economic Systems Demand **Supply** Equilibrium

Change in price of “related products”

- Complements in production (by-products)

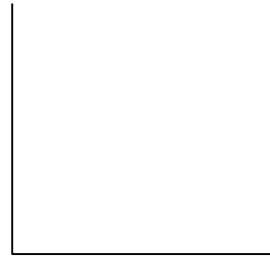


- ↑ price of complement output

Economic Systems Demand **Supply** Equilibrium

Change in # of Sellers

- ↑ # of sellers



Economic Systems Demand **Supply** Equilibrium

Market Equilibrium

- When price is at its equilibrium, quantity demanded equals quantity supplied
 - When $p = p^*$, $q_D = q_S$ (p^* stands for “equilibrium price”)



Economic Systems Demand Supply **Equilibrium**

Adjustment Process

- If $p < p^*$
- If $p > p^*$

Economic Systems Demand Supply **Equilibrium**