



Prifysgol Cymru
Y Drindod Dewi Sant
University of Wales
Trinity Saint David

Bachelor of Arts Business Management

Management Economics (LCBB5003)

Supply and Demand and the consumer-
Individual and Market Demand

Monday & Thursday-14:00-16:00

Trawsnewid Addysg; Trawsnewid Bywydau
Transforming Education; Transforming Lives



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Learning Outcomes

- ❑ Define supply, demand, and equilibrium price
- ❑ Demonstrate how the supply and demand concepts can be used by managers to make decisions about prices and resources
- ❑ Explore supply and demand diagrams to determine the market price in the short run and in the long run.

Demand definition

The **demand** for a good or service could be defined as:

Quantities of a good or service that people are ready to buy at various prices within some given time period, other factors besides price held constant.

Keat, P., Young, P., Erfle, S., (2014) Managerial Economics- Economic Tools for Today's Decision Makers, 7th Edition

Demand Example

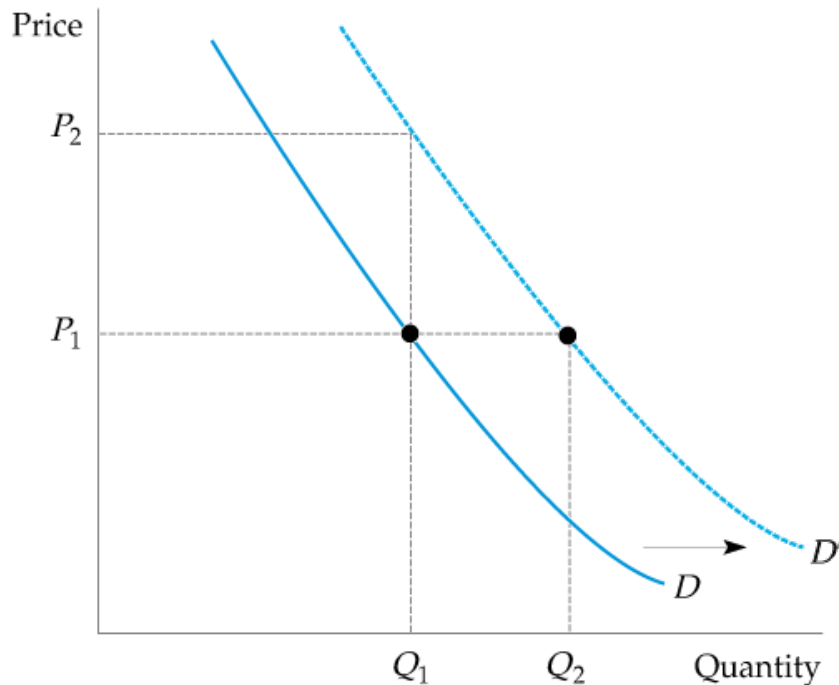
- Imagine we ask customers how many coffees and at what price they would be prepared to buy in one week. The price would start at £4.50, £3.50, £2 and £1.
- For this example, we will take the answers from 4 fellow students as customers buying coffee from the coffee machine and each customer would have their own pattern or response. (QDC-Quantity-Demand-Customer/ QDM-Quantity-Demand-Market)

Price of Coffee	Q _{DC1}	Q _{DC2}	Q _{DC3}	Q _{DC4}	Q _{DM}
£4.50					
£3.50					
£2					
£1					

Keat, P., Young, P., Erfle, S., (2014) Managerial Economics- Economic Tools for Today's Decision Makers, 7th Edition

The Demand Curve

Demand curve: Relationship between the quantity of a good that consumers are willing to buy and the price of the good.



The Demand Curve

The demand curve is downward sloping: consumers will want to purchase more of a good as its price goes down.

Variables that affect demand-
Use our example

A higher income level shifts the demand curve to the right (from D to D').

Demand

The relationship between the price and the quantity demanded of coffee is called Law of demand

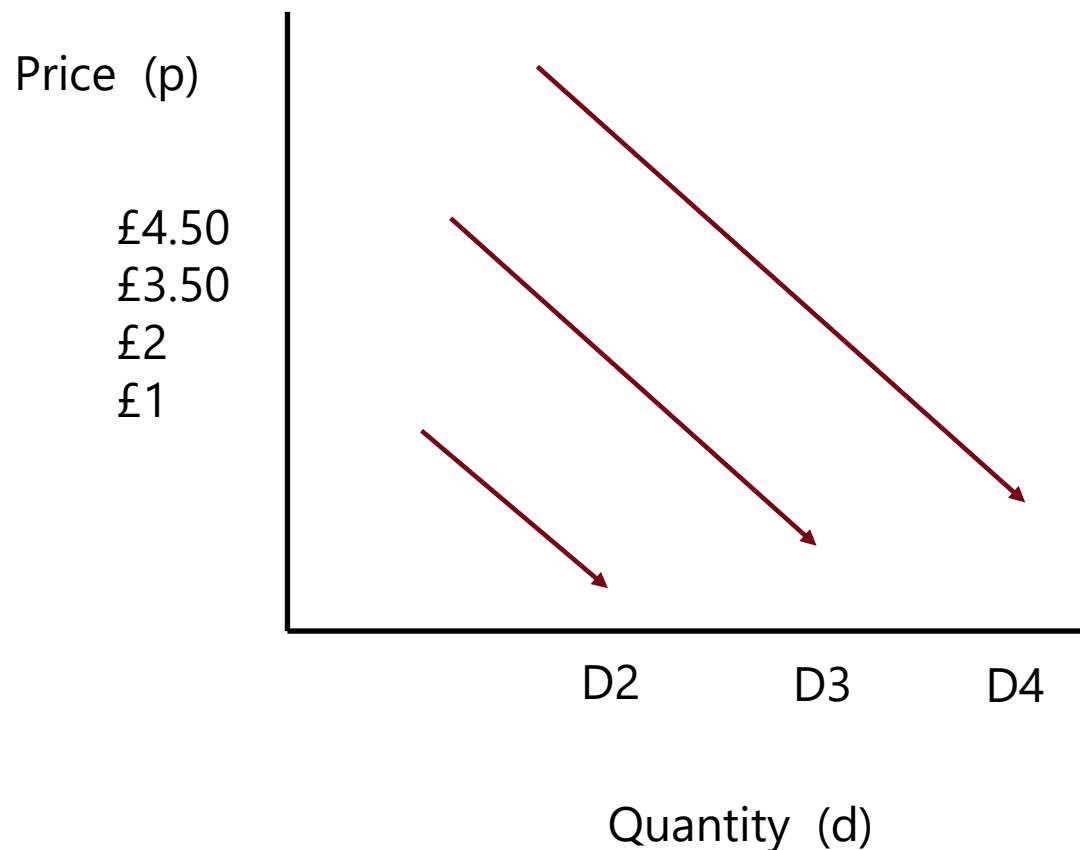
Keat, P., Young, P., Erfle, S., (2014) Managerial Economics- Economic Tools for Today's Decision Makers, 7th Edition

Demand

- ❑ However they will be instances that consumer behave irrational by buying more as price is rising and less when price falls as they associate price with quality
 - ❑ In these instances these factors are called nonprice determinants of demand
1. Tastes and preferences- Why do people buy things
 2. Income- As people's incomes rise, it is reasonable to expect their demand for a product to increase
 3. Prices of related products-A good or service can be related to another by being a substitute- Pepsi vs Coca cola, Margarine vs Butter or by being a complement- Software-PC, Petrol and Cars, PlayStation and Games
 4. Future expectations-Buyers waiting for prices to come down in the future- electric cars- DVDs etc
 5. Number of buyers-more Buyers- demographics- tastes/ preferences etc

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Demand diagram



Assumptions

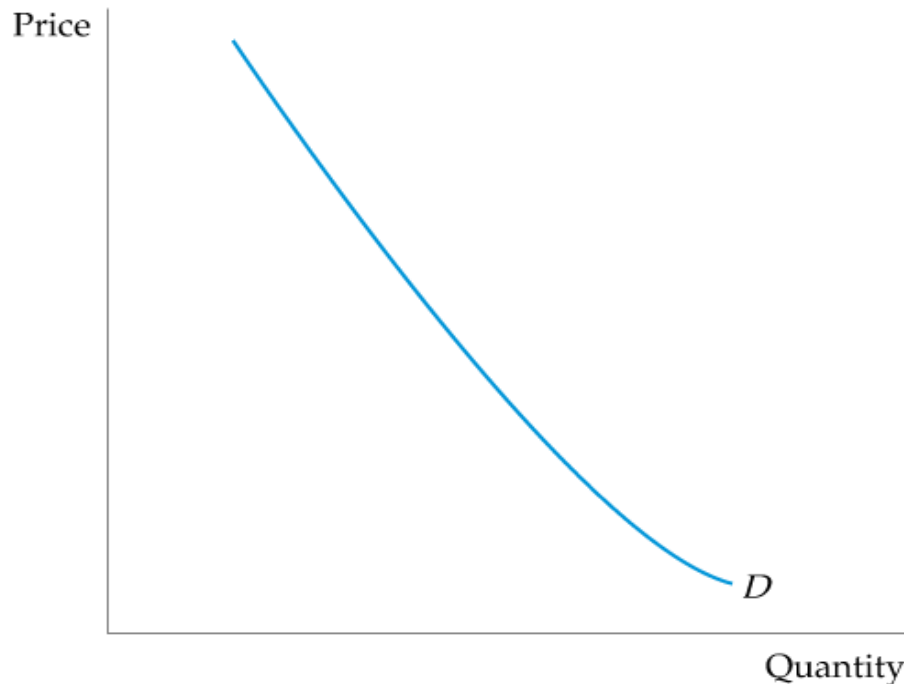
- Changes in demand
- Nonprice determinants of demand
- Changes in disposable income
- Change in the price of substitute goods
- Change in the price of complementary goods
- Change in fashion and tastes
- Changes in population

The Demand Curve

Demand curve: Relationship between the quantity of a good that consumers are willing to buy and the price of the good.

The Demand Curve

- ☐ Coffee suppliers reduce prices by 10%
- ☐ The price of coffee beans increases
- ☐ Price of tea decrease
- ☐ Government increase/decrease tax on coffee beans imports
- ☐ Change in income of people
- ☐ Consumers expect coffee to decrease next year



Supply definition

The **supply** of a good or service is defined as

Quantities of a good or service that people are ready to sell at various prices within some given time period, other factors besides price held constant.

Keat, P., Young, P., Erfle, S., (2014) Managerial Economics- Economic Tools for Today's Decision Makers, 7th Edition

Supply definition

The **supply** of a good or service is defined as

Quantities of a good or service that people are ready to sell at various prices within some given time period, other factors besides price held constant.

The only difference between this definition and that of demand is that in this case the word *sell* is used instead of *buy*.

Just as in the case of demand, supply is based on an assumed length of time within which price and the other factors can affect the **quantity supplied**.

Keat, P., Young, P., Erfle, S., (2014) Managerial Economics- Economic Tools for Today's Decision Makers, 7th Edition

Supply definition

- ❑ Just as there are nonprice determinants of demand, there are **nonprice determinants of supply**
- 1. Costs and technology-costs of production, such as labor costs, costs of materials, rent, interest payments- technology- improvements introduced to reduce the unit cost of production or new products
- 2. Prices of other goods or services offered by the seller- substitutes or complements- sellers choosing to change what they produce
- 3. Future expectations-sellers anticipate a rise in price, they may choose to hold back the current supply to take advantage of the higher future price
- 4. Number of sellers-number of sellers has a direct impact on supply
- 5. Weather conditions-Bad weather (e.g., floods, droughts, unusual seasonal temperatures) will reduce the supply of an agricultural commodity

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The Supply Curve

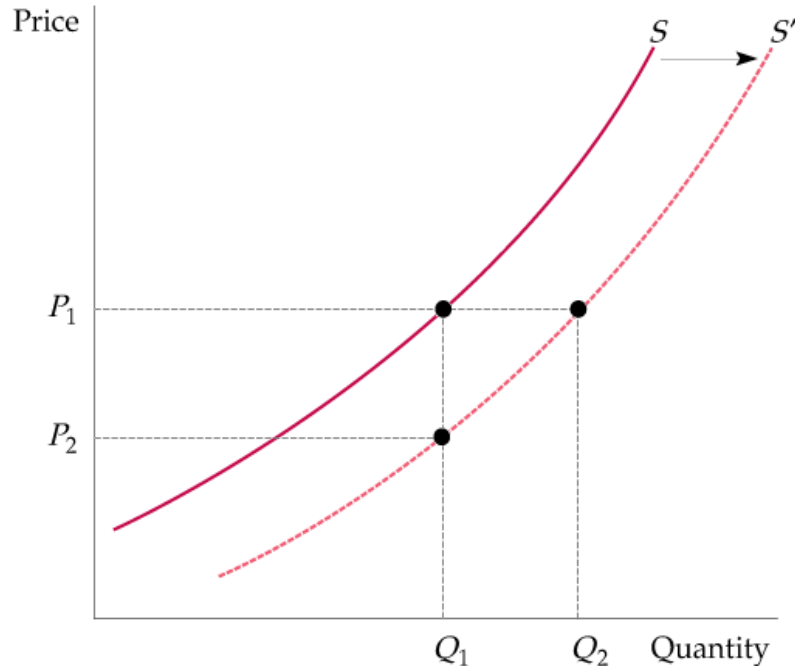
Supply curve: Relationship between the quantity of a good that producers are willing to sell and the price of the good.

The Supply Curve

The supply curve is upward sloping: the higher the price, the more firms are able and willing to produce and sell.

If production costs fall, firms can produce the same quantity at a lower price or a larger quantity at the same price.

The supply curve then shifts to the right (from S to S').



Supply and demand

Lets watch a video

<https://www.youtube.com/watch?v=kIFBaaPJUO0>

Market Equilibrium

Equilibrium price: The price that equates the quantity demanded with the quantity supplied

Equilibrium quantity: The amount that people are willing to buy and sellers are willing to offer at the equilibrium price level

Market Equilibrium

Shortage: A market situation in which the quantity demanded exceeds the quantity supplied.

- ❑ A shortage occurs at a price below the equilibrium level.

Surplus: A market situation in which the quantity supplied exceeds the quantity demanded.

- ❑ A surplus occurs at a price above the equilibrium level.

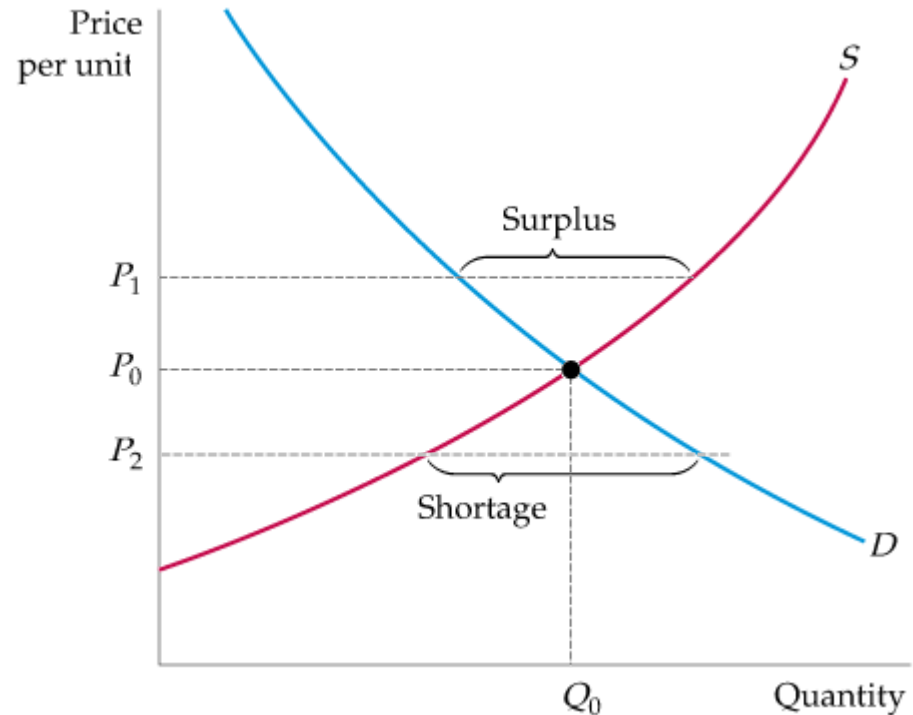
Market Equilibrium

Supply and Demand

The market clears at price P_0 and quantity Q_0 .

At the higher price P_1 , a surplus develops, so price falls.

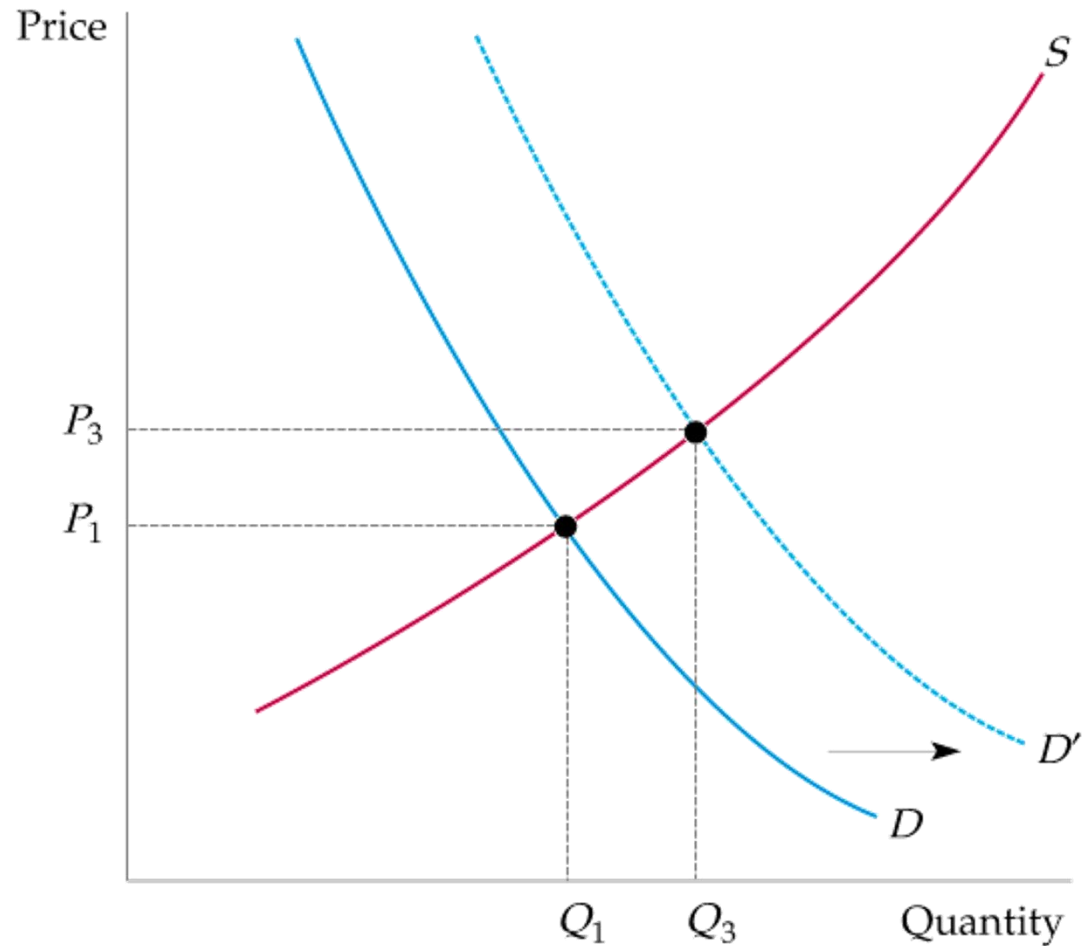
At the lower price P_2 , there is a shortage, so price is bid up.



Market Equilibrium

New Equilibrium Following Shift in Demand

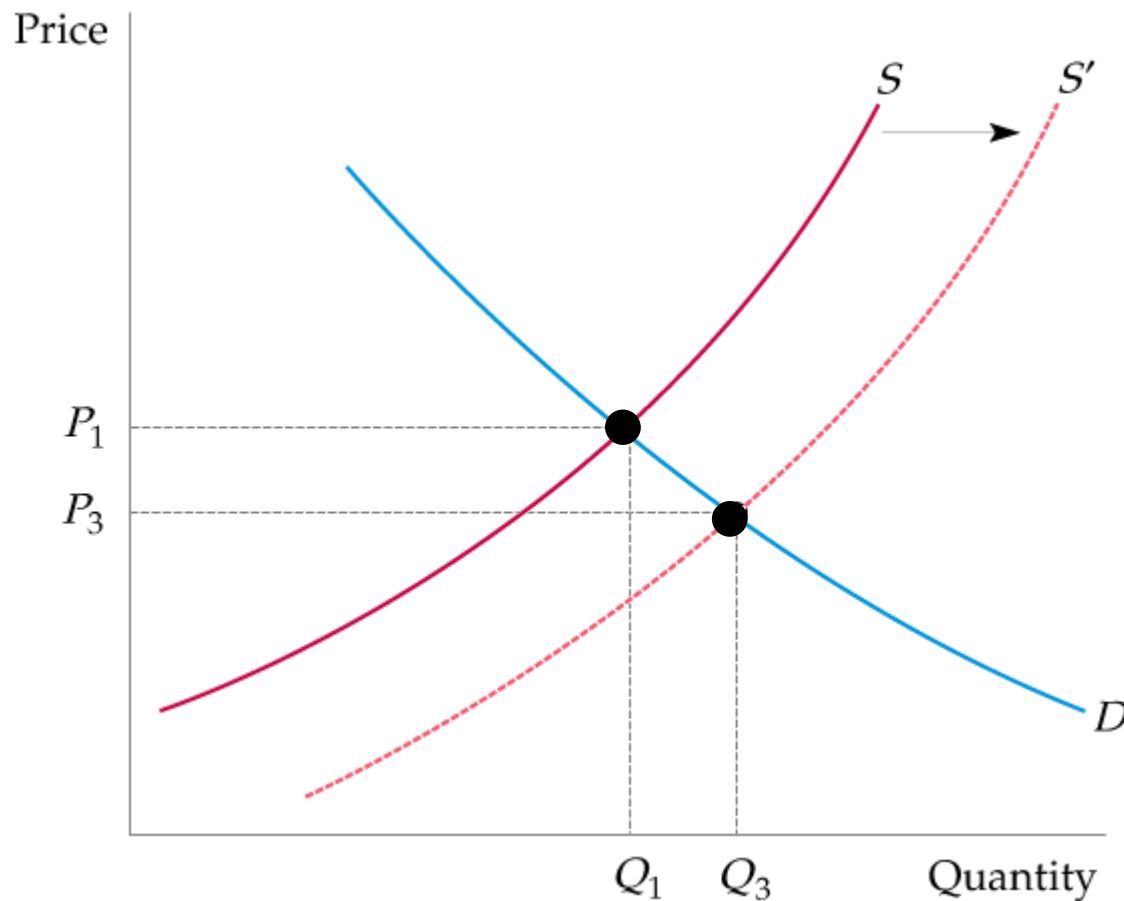
When the demand curve shifts to the right, the market clears at a higher price P_3 and a larger quantity Q_3 .



Market Equilibrium

New Equilibrium Following Shift in Supply

When the supply curve shifts to the right, the market clears at a lower price P_3 and a larger quantity Q_3 .



Classroom Activity

Find supply & demand examples- how managerial decisions are affected?

Elasticity- elastic demand

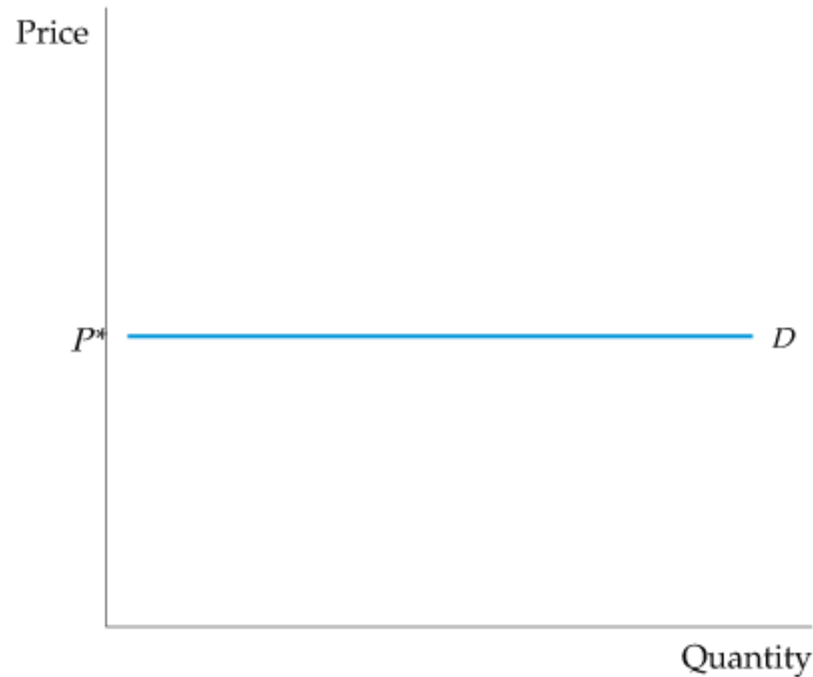
(a) Infinitely Elastic Demand

(a) For a horizontal demand curve, $\Delta Q/\Delta P$ is infinite. Because a tiny change in price leads to an enormous change in demand, the elasticity of demand is infinite.

Infinitely elastic demand

Principle that consumers will buy as much of a good as they can get at a single price, but for any higher price the quantity demanded drops to zero, while for any lower price the quantity demanded increases without limit.

Linear Demand Curve



(a)

Elasticity-inelastic demand

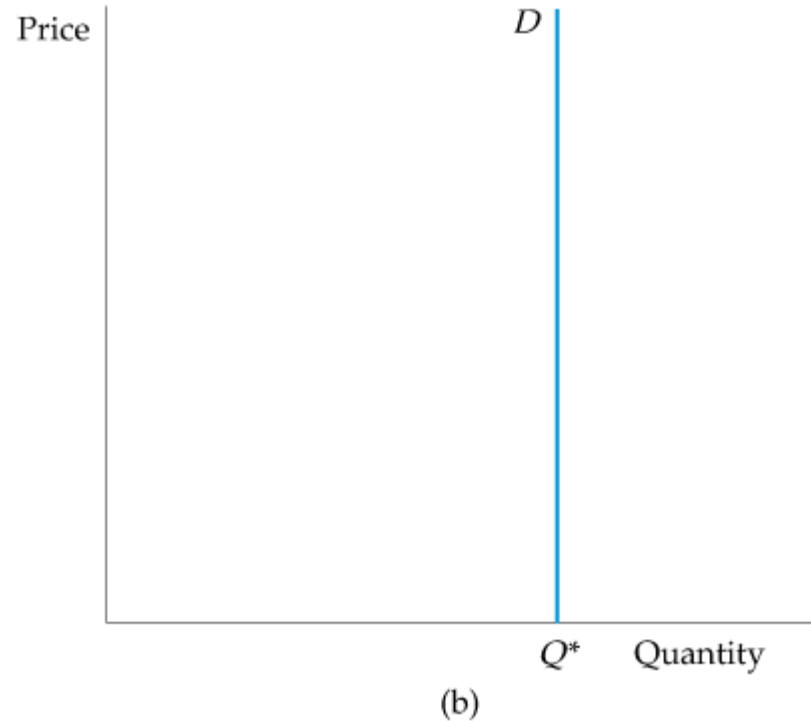
(b) Completely Inelastic Demand

(b) For a vertical demand curve, $\Delta Q/\Delta P$ is zero. Because the quantity demanded is the same no matter what the price, the elasticity of demand is zero.

completely inelastic demand

Principle that consumers will buy a fixed quantity of a good regardless of its price.

Linear Demand Curve



Elasticity- Demand- Factors

- ☐ Ease of substitution
- ☐ Proportion of total expenditures-salt example-demand for salt is small-any price increase (e.g., from 44 cents to 54 cents per gram) would probably would not affect consumption of salt very little
- ☐ Durability of product
- ☐ Possibility of postponing purchase
- ☐ Possibility of repair
- ☐ Used product market
- ☐ Length of time period

Elasticity

Let's watch a video that explains further Elasticity

<https://www.youtube.com/watch?v=HHcblIxiAAk>

Classroom Activity

Find examples Elasticity demands- how managerial decision are effected?

Do you have any questions about the session?



Practical activity

Individually work on our weekly practical activity

Do you have any Questions about our practical activity?



Thank you!

References

Reading for the session (online access through our library)

- ❑ Samuelson, W., Marks, S., (2010) Managerial Economics, Study Guide, London, John Wiley & Sons
- ❑ Keat, P., Young, P., (2014) Managerial Economics- Economic Tools for Today's Decision Makers, 7th Edition
- ❑ Sloman, J., Hinde, K., Garrat (2013) Economics for Business, Harlow, Pearson

A blurred background image showing students in a classroom. In the foreground, a student wearing a blue and red plaid shirt is sitting at a desk, holding a red pen over an open notebook. Other students are visible in the background, also working at their desks.

Next week.....

We will look at;

The Cost of Production and Profit
Maximization (analysis of business
costs and resource allocation-
business decision)