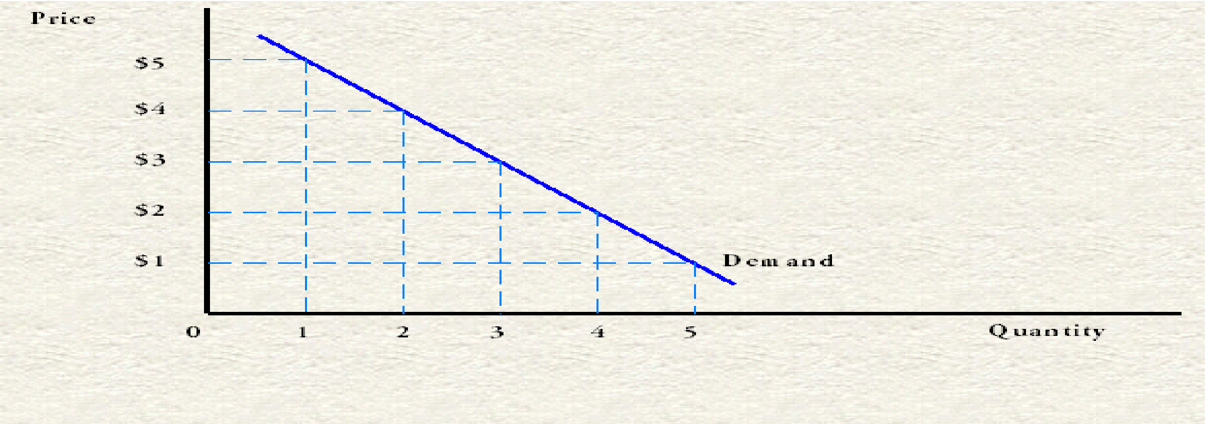
Principles of Economics lecture 2:

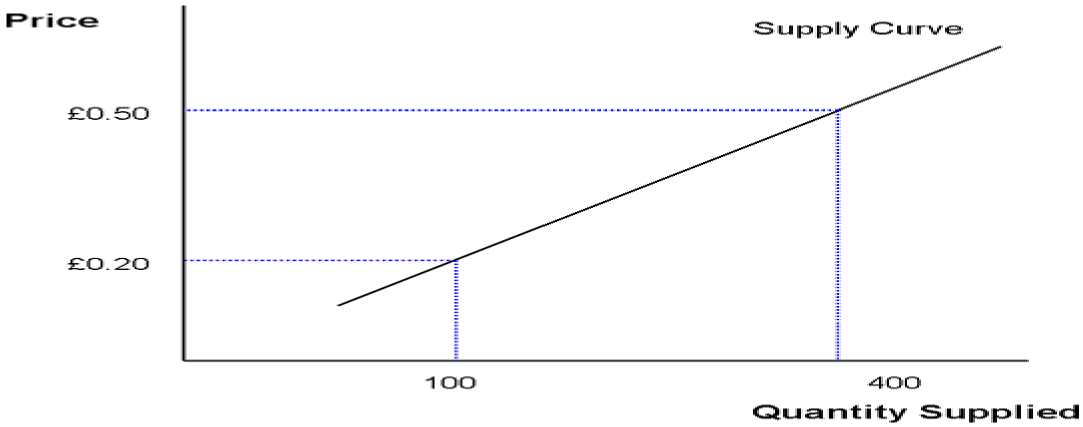
In economics -> market = relationship between a buyer and a seller -> involving voluntary exchange of ownership. Supply and demand -> determines market price that the voluntary exchange occurs at.

Demand: A set of quantities a buyer is willing and able to purchase at different prices (Graphical representation of demand)

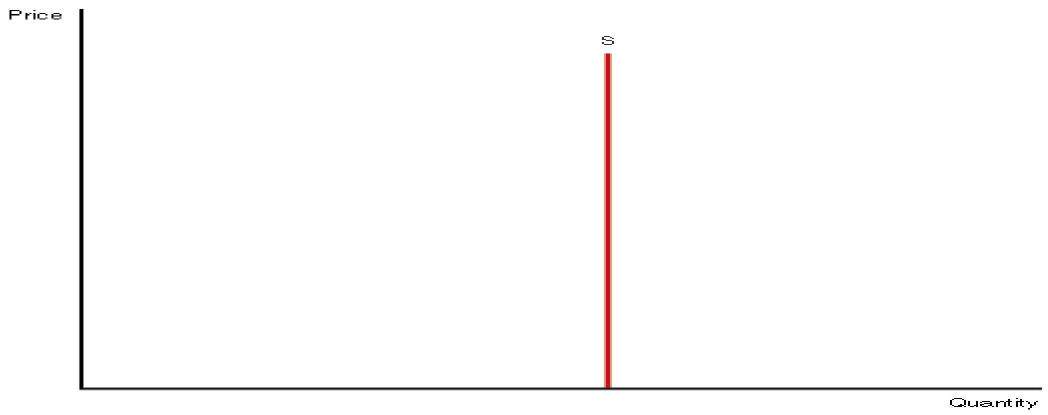


Supply curve: The quantity a seller will offer at a certain price (increases as the price rises)

If the company supplies more = Not make enough profit.



Vertical supply curve = Fixed quantity (can be used to show deflation or inflation of dollar, there will still be the same amount of money it will just be worth less)

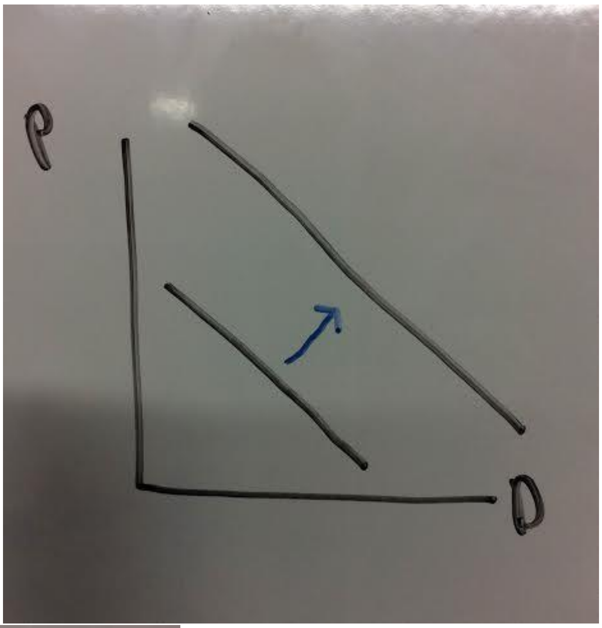


Demand + Supply graph:

-Price increase so does supply (sellers)
-Price increases demand decreases (buyers)

Equilibrium = price matches quantity sellers will supply with the quantities buyers will buy.

Therefore price goes up & supply goes up causing demand to go down until equilibrium is reached.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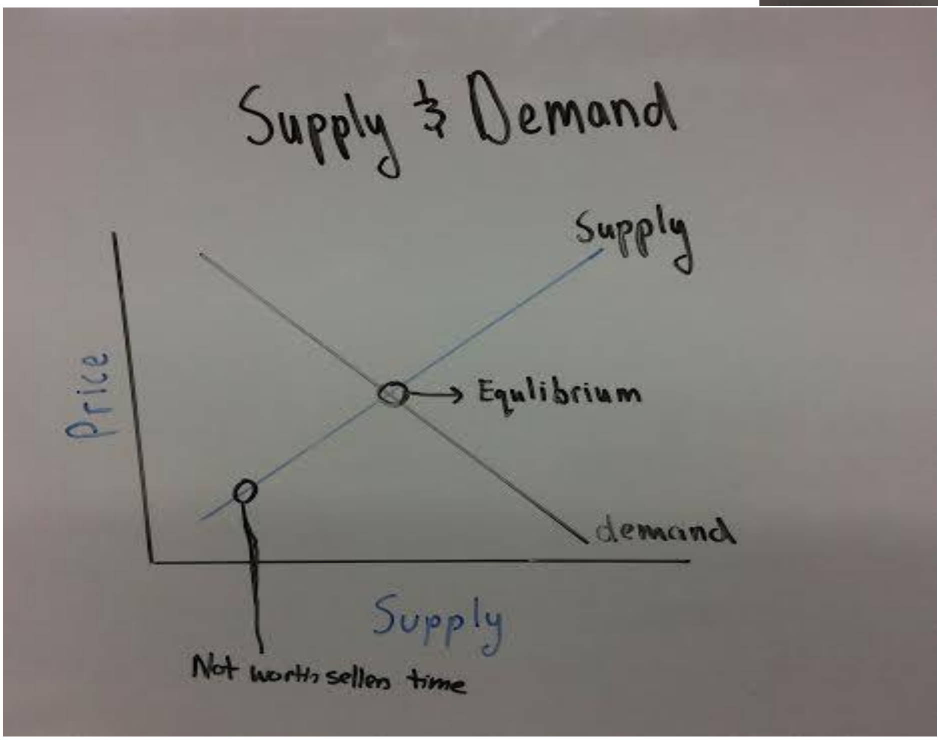

Supply ⅋ Demand
Supply
Price
Equlibrium
demand
Supply
Not worth sellers time

Factors that affect demand: (NIPET)

-Number of potential buyers

-Income (goes up -> demand increases)

One of the rare cases when price goes up so does demand →

-Price of substitute good (complimentary good): Price of motorbikes drops significantly demand for cars decreases.

-Expectations about future prices. Eg: belief that house prices will rise causing a demand for houses)

-Tastes change. Eg: cigarette demand drops because of de-marketing campaigns.

Factors affecting supply: (AU-CNET)

-Alternative products that are profitable

-Unpredictable events

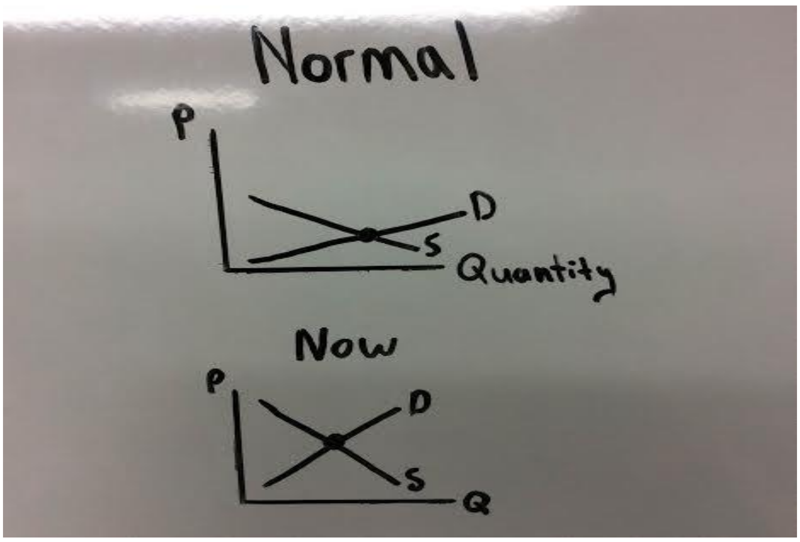
-Cost of supply

-Number of suppliers

-Expectations of future price change

-Technological innovations that increase supply

Eg: War in the Middle East & how it will affect petrol



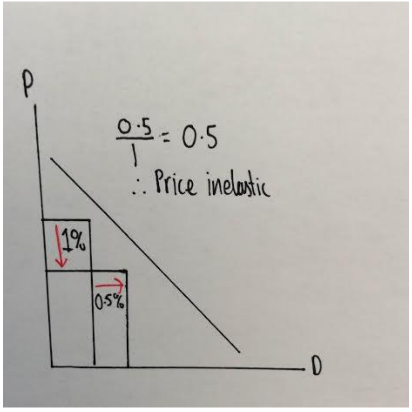
Price Elasticity of demand:

Price goes up → Demand changes = price is elastic

Measuring: If the effect is bigger than the cause price is elastic

Formula: Effect (change in %) / Cause (change in %)

Eg: 0.5/1 = 0.5 therefore inelastic



Ans> 1 (price elastics)

Ans<1 (Price inelastic)

Ans=infinity (perfectly price elastic)

Ans=0 (Perfectly inelastic)

Ans=1 unit price elastic

<u>What effects price elasticity?</u>

-The more expensive an item is the more responsive you will be to a price change.

-Lots of substitutes = more price elastic. Eg: electricity is price inelastic because there are few alternatives.

-Affected by time, eg: the amount of time a consumer has to purchase an item

-Innovation and imitation of original invention can cause price elasticity.

-Biology, you have to have food because there is no substitute.

-Culture. In some cultures something is considered a substitute eg: south East Asia noodles are a substitute for rice.