SUPPLY AND DEMAND

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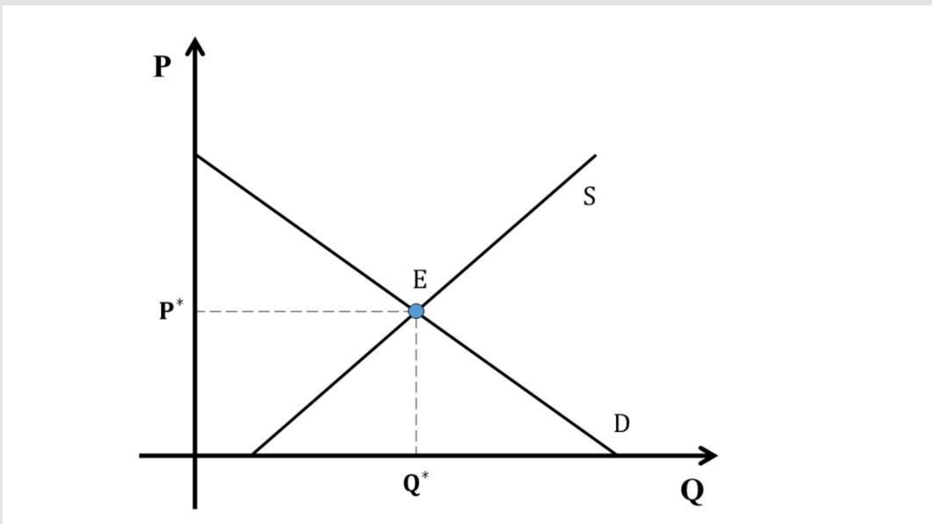
What is the market?

A market is a place where sellers (producers) sell or rent out products, commodities, assets, services or anything else what is tradeable to buyers (consumers). Some markets are organized as auctions (of paintings for example) or like stock exchanges, while other markets can be dispersed over large territories or extended over long times like cereals markets, Bazos or eBay marketplace. Vegetable market in centres of towns in Slovakia is an example of a typical market.

Supply on the market is provided by sellers (often producers) while demand is formed by buyers (often consumers). Sellers prefer higher price to lower price. When price goes up sellers are ready to sell more. This is the law of supply: sellers sell more at higher price. On the other hand, buyers prefer lower prices. When price is lower buyers are willing to buy more, which is the formulation of the law of demand.

Equilibrium price is the price at which quantity supplied by sellers is equal to quantity demanded by buyers. At this price there is neither surplus nor shortage at the market. Equilibrium price changes. It is not the same for a long time. Sometimes it changes from minute to minute (stock exchange) and sometimes it changes over longer period of time (prices of flats or houses).



Changing prices and quantities

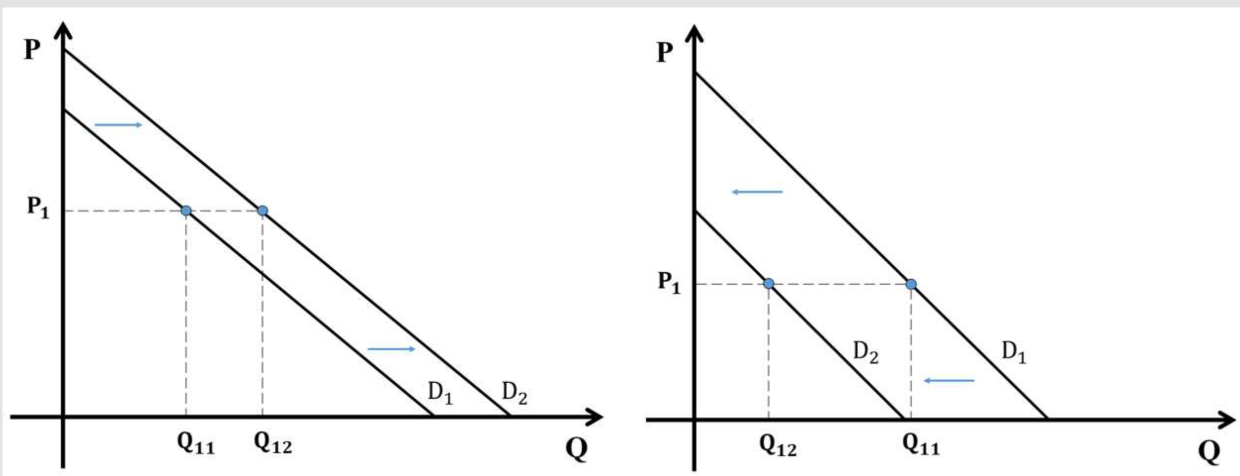
Why are market prices and quantities changing? And is it important to us? Imagine the situation that you own a restaurant in the centre of Topoľčany. When can you expect a price change and how will it affect your business?

Number of buyers: The rise of number of buyers (population growth or immigration) shifts the demand curve to the right. Outmigration or reduction of population growth shifts demand curve to the left. Change of the distribution of buyers by age or education or income shifts the demand curve too; negative changes decrease the demand and positive changes increasing it.

Preferences: Preferences of buyers need not stay fixed. They can be affected by marketing, new scientific evidence, changes in lifestyles or other factors. Change of preferences of consumers' leads to the shift of the demand curve to the right or to the left.

Expectations: Buyers form expectations about future, which affects current decisions. If buyers expect that the price will decrease in the future, they are less willing to buy the good at the current price. They will postpone purchase decision and current demand curve shifts to the left.

Income: The rise of income shifts demand curve to the right for normal goods, while it shifts demand curve to the left for inferior goods.



Increasing demand Decreasing demand

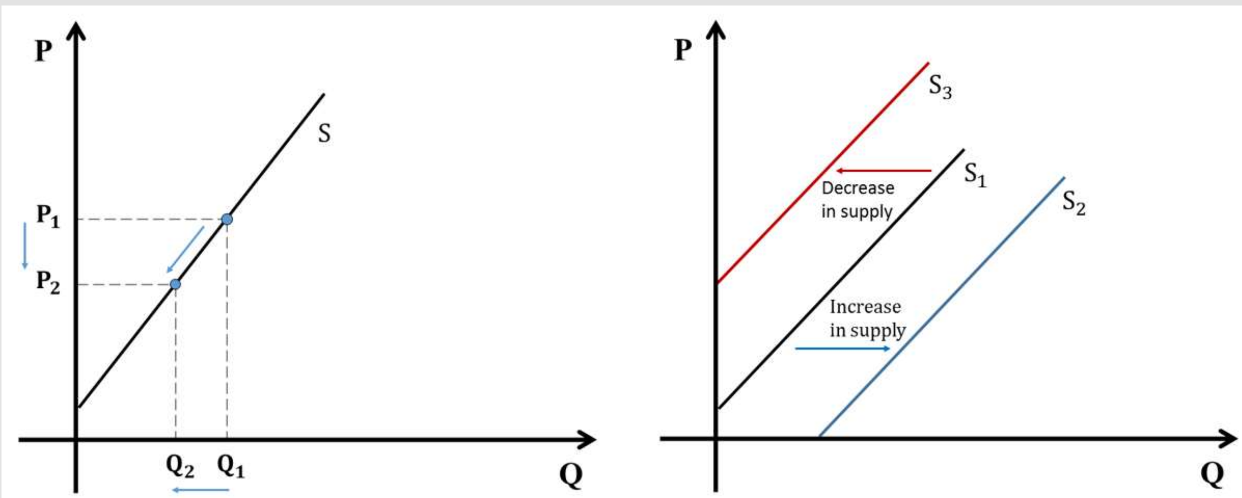
Input price: If the price of one or more inputs rises, the production costs increase and at given price firms produce less. Some firms leave the market as they are not competitive at higher input costs. For example, the rise of rental price of land causes the decline of agricultural production.

Technology affects production function. Better technology means that more output (or better) is produced from the same amount of inputs. Unit costs therefore decline, and supply curve shifts to the right. At given price firms produce more.

Prices of other goods: Usually, producers produce more than just one output. Vegetable growers produce for example carrots, tomatoes, potatoes, cabbage, etc. If market price of carrots increases, producers devote more land to production of carrots and less land is available for other commodities, which means that supply curve for other goods shifts to the left.

Expectation of future affect current decisions. If producers expect that price will increase in the future, they will increase production immediately and store products for future sale at higher price. Current supply curve will shift to the left.

Number of sellers is closely related to market supply. If number of vendors of hot-dogs increases, supply of hot-dogs in the city goes up too. In the end, supply curve for hot-dogs shifts to the right.



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