

What is Supply & Demand all about?



Okay well let's begin by taking a look at the Mars Bar. How much would you pay for a single bar?

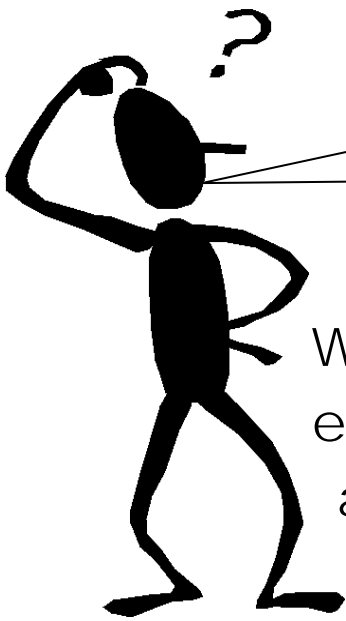
Well that will be £5 please and can I interest you in our range of suet puddings?



That will be 5p please.

Which shop keeper would you buy from and why?

Can you spot the problems for both shops?



What's wrong with me buying the cheapest deal? Surely this is a bargain!

Well maybe yes, but a business needs to learn exactly what price they should sell their goods at.

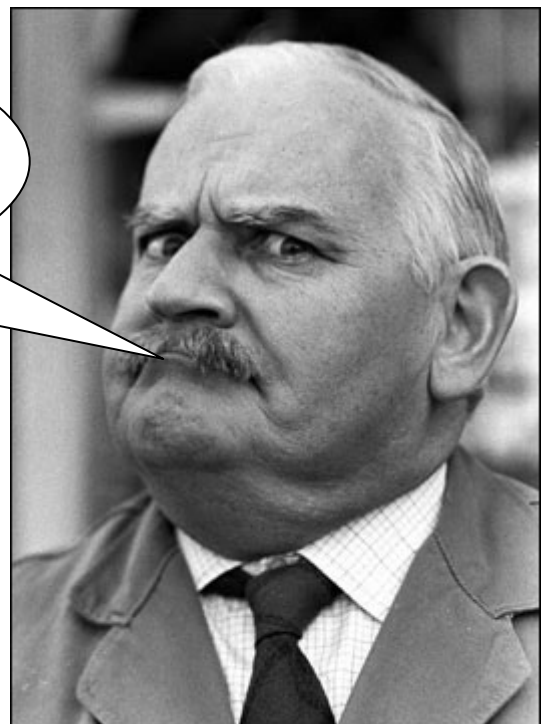
If they sell them **TOO CHEAP** then they won't make any **PROFIT** and the customer might think that there is something wrong with the product e.g. maybe it's out of date.

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Sell your product at **TOO EXPENSIVE** a price and the customer will simply go elsewhere to buy it and again your profits will be low.

Okay so what price should I sell my Mars Bars at then? And can I interest you in a suet pudding?

A good business will try to find what is called the **MARKET CLEARING PRICE**. This is the price at which everything that you offer is sold!

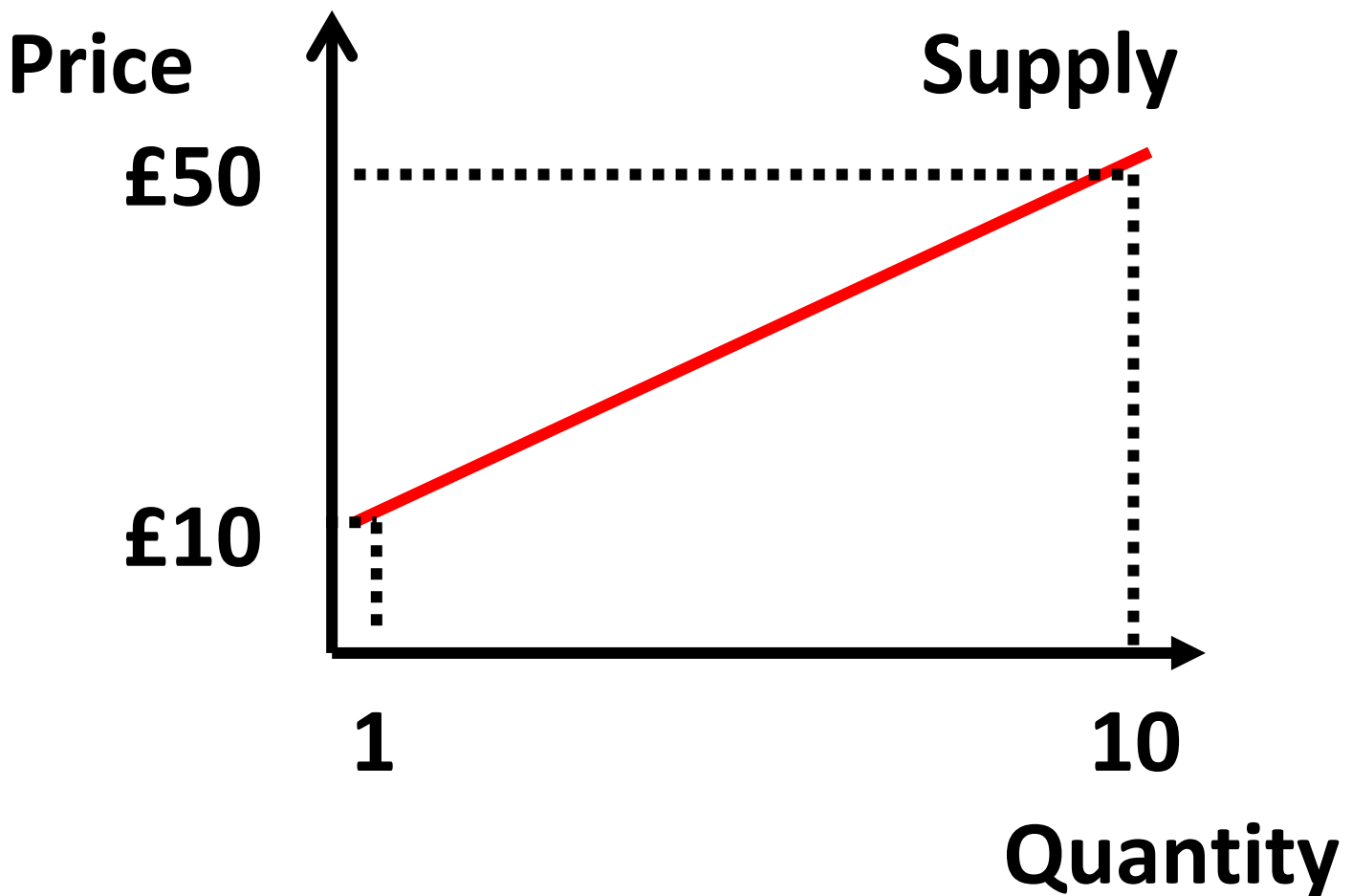




Tell me more about this Market Clearing Price.

Well, it is also known as the **PRICE EQUILIBRIUM** and it is the point in a supply & demand diagram where the supply and demand lines cross. Let's take a look!

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What is that diagram all about? I can't understand that!



It's really easy....honest!
First, remember that supply is the amount of a good that someone or some business is willing to make available at a given price.

If we look at the diagram, we can see that at a price of £10, the supplier was only willing to give us 1 item. When the price went up to £50 then they were happy to supply 10 items!

WHY? Well the simple reason is that they stand to make more money at the higher price and so will provide more.

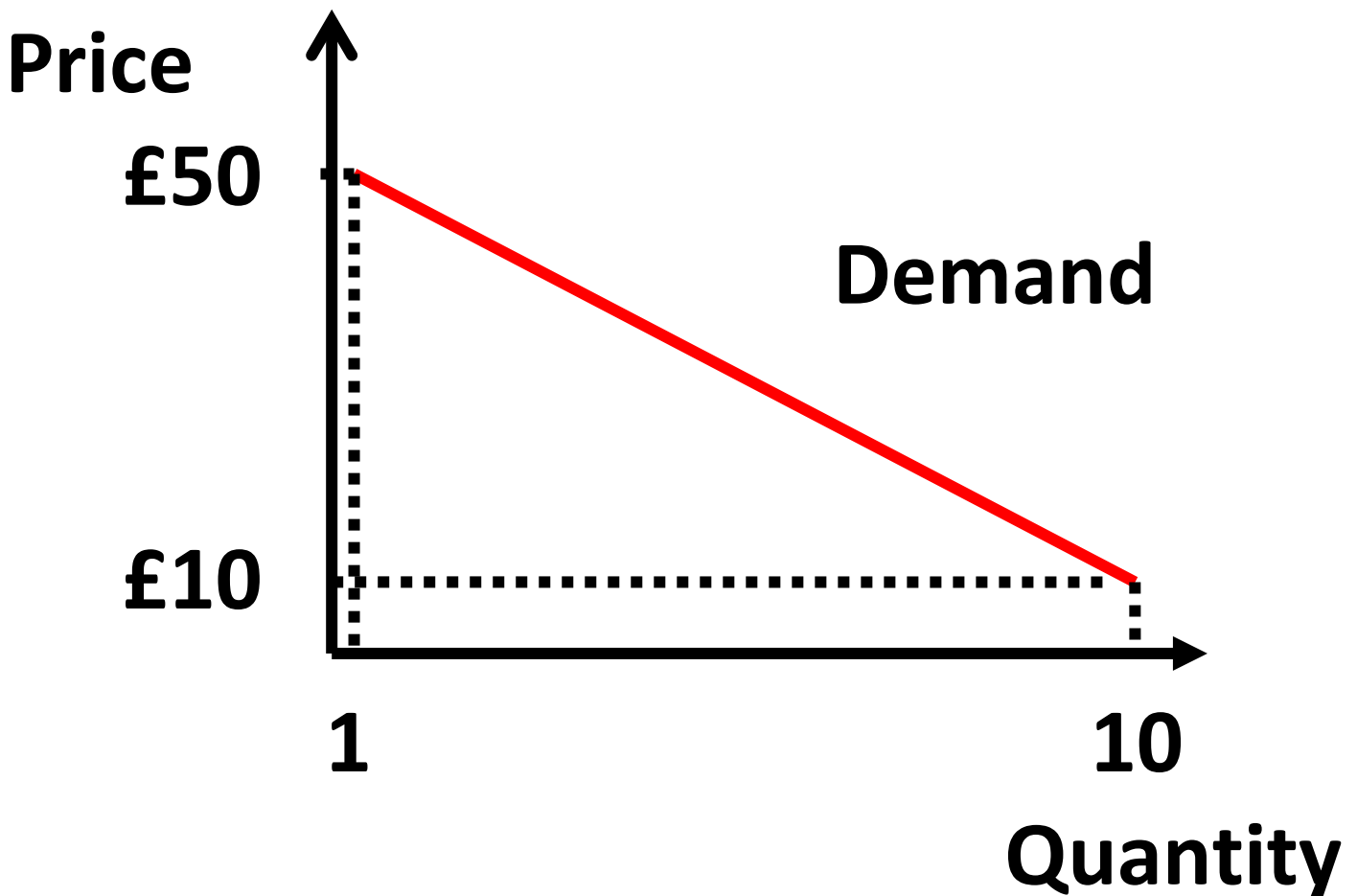
EXAM TIP. A Supply line ALWAYS goes in an UPWARDS direction. Can't remember that...well Supply also has the word **SUPPLY** in it to help you!

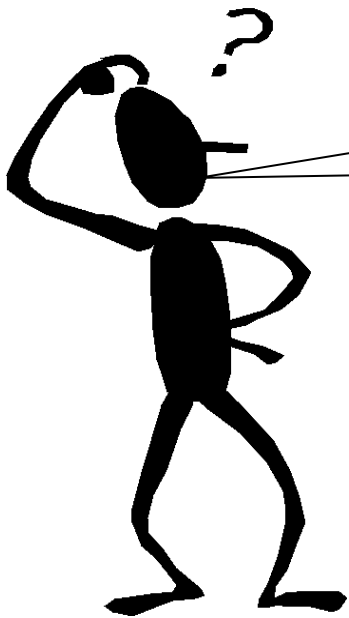


Okay so what about the Demand Curve?

Well the Supply Curve showed us how many items a supplier was prepared to offer us at a given price. The Demand Curve shows how many items customers are able and willing to buy at a given price.

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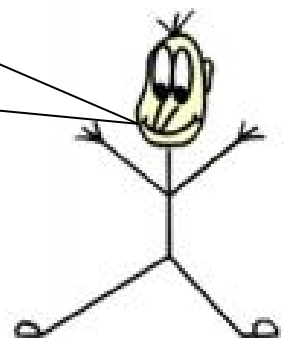
So what does this demand chart show me?

If we look at the diagram, we can see that at a price of £10, the customer was happy to buy 10 items but when the selling price went up to £50, then customers were only wanting to buy one item!

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WHY? Well the simple reason is customers are getting a much better deal at the cheaper price and they are not prepared to pay the higher price.

EXAM TIP. A Demand line ALWAYS goes in an DOWNWARDS direction.
Can't remember that...well **D**emand starts with the letter 'D' for Down!

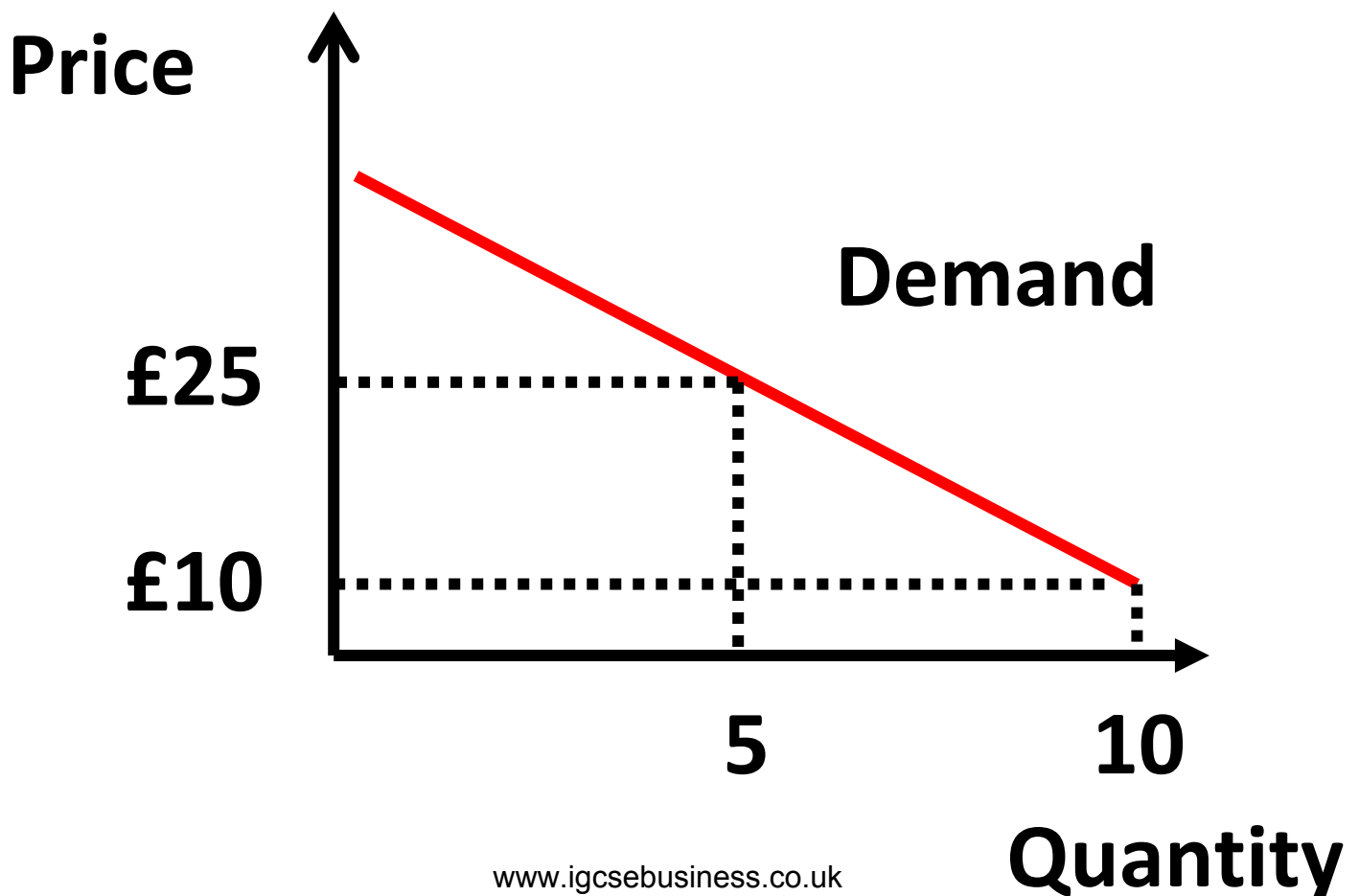




So is that all I need to know about Supply and Demand?

Erm well actually there's more to it than this! We need to be able to explain what happens when prices change or the lines themselves actually SHIFT!

Let's start by looking at Demand. What do you think will happen to the level of demand if the price rises from £10 to £25?

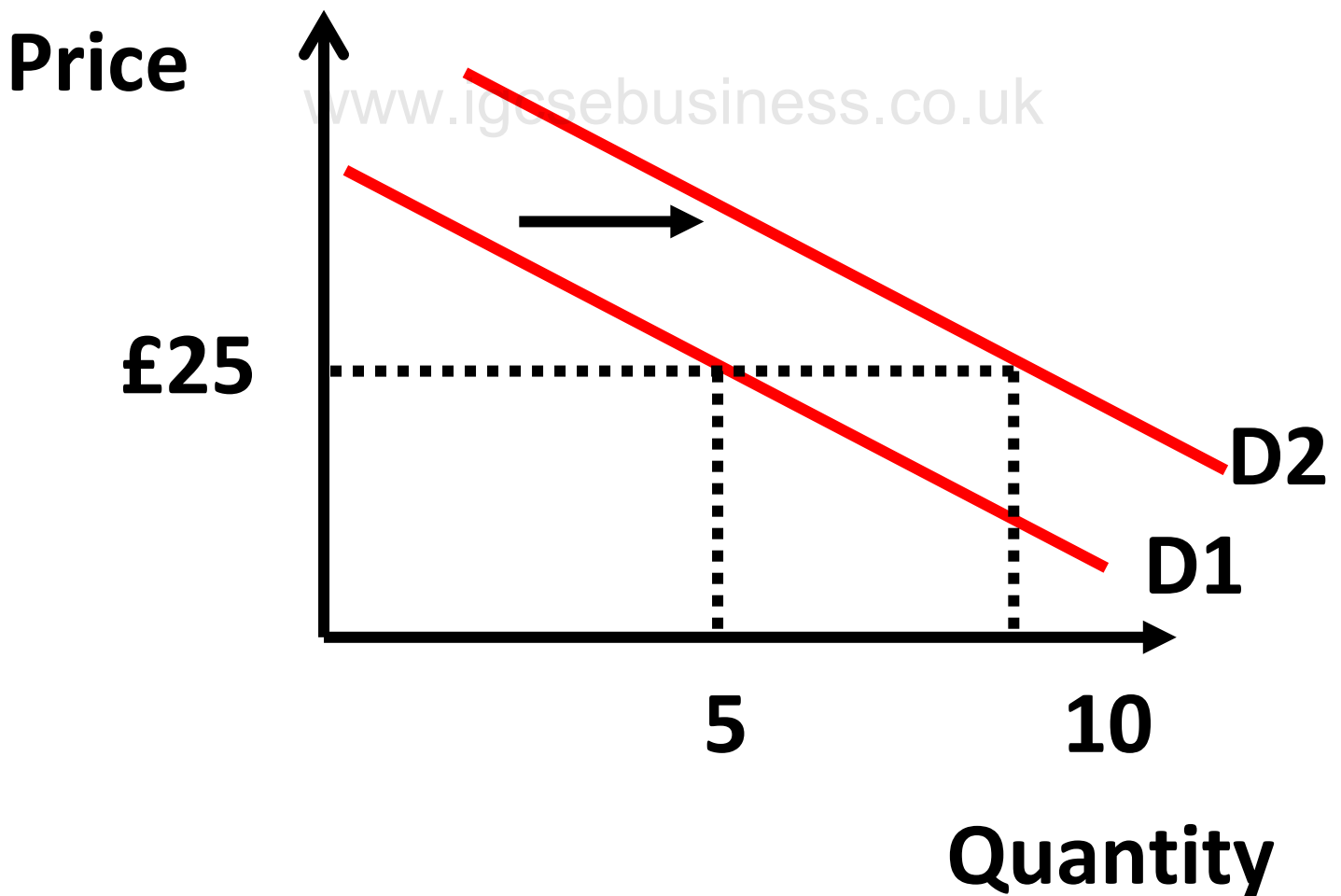


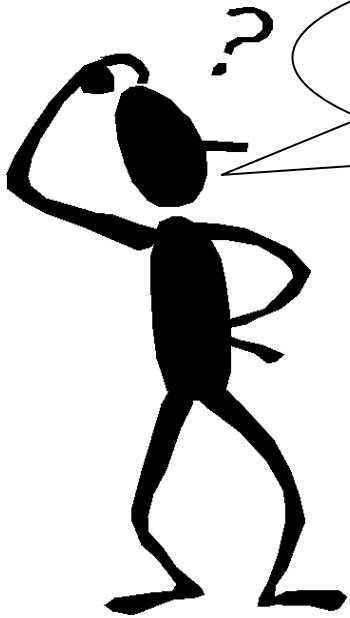


Right so if I put my prices up then I can expect fewer customers! Suet pudding anyone?

Yes! And also if you lower your prices then you can normally expect demand to rise.

Sometimes though, demand for an item might go up or down at every price level. This means that the entire demand line will SHIFT. Let's take a look...

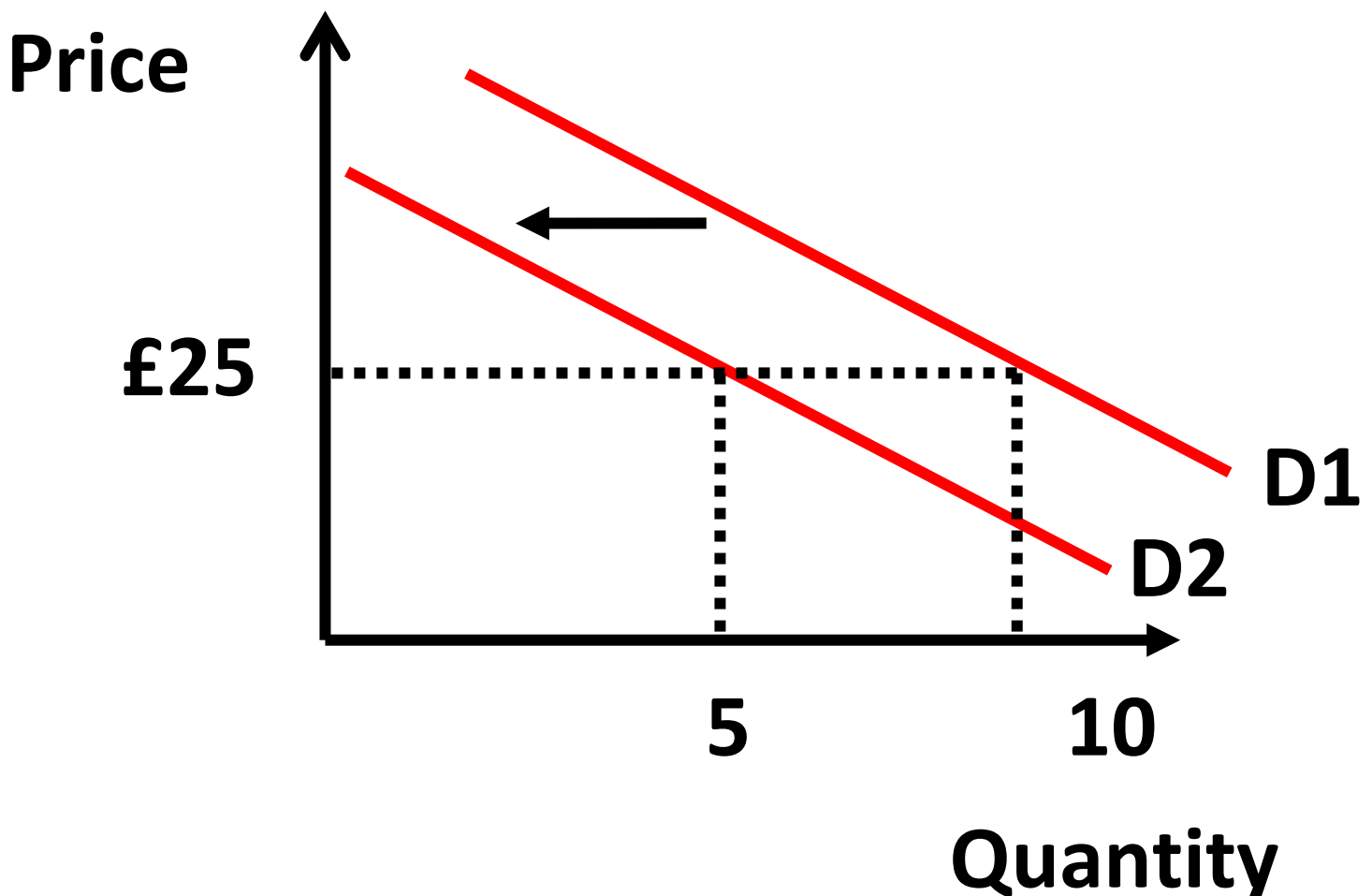




Why does the line shift though?

Well it might be that the product has become really popular and that has meant that demand has increased. When demand increases the Demand Curve shifts to the **RIGHT**.

If the product became really unpopular, then we might find that the Demand Curve shifts to the **LEFT** as we can see below.

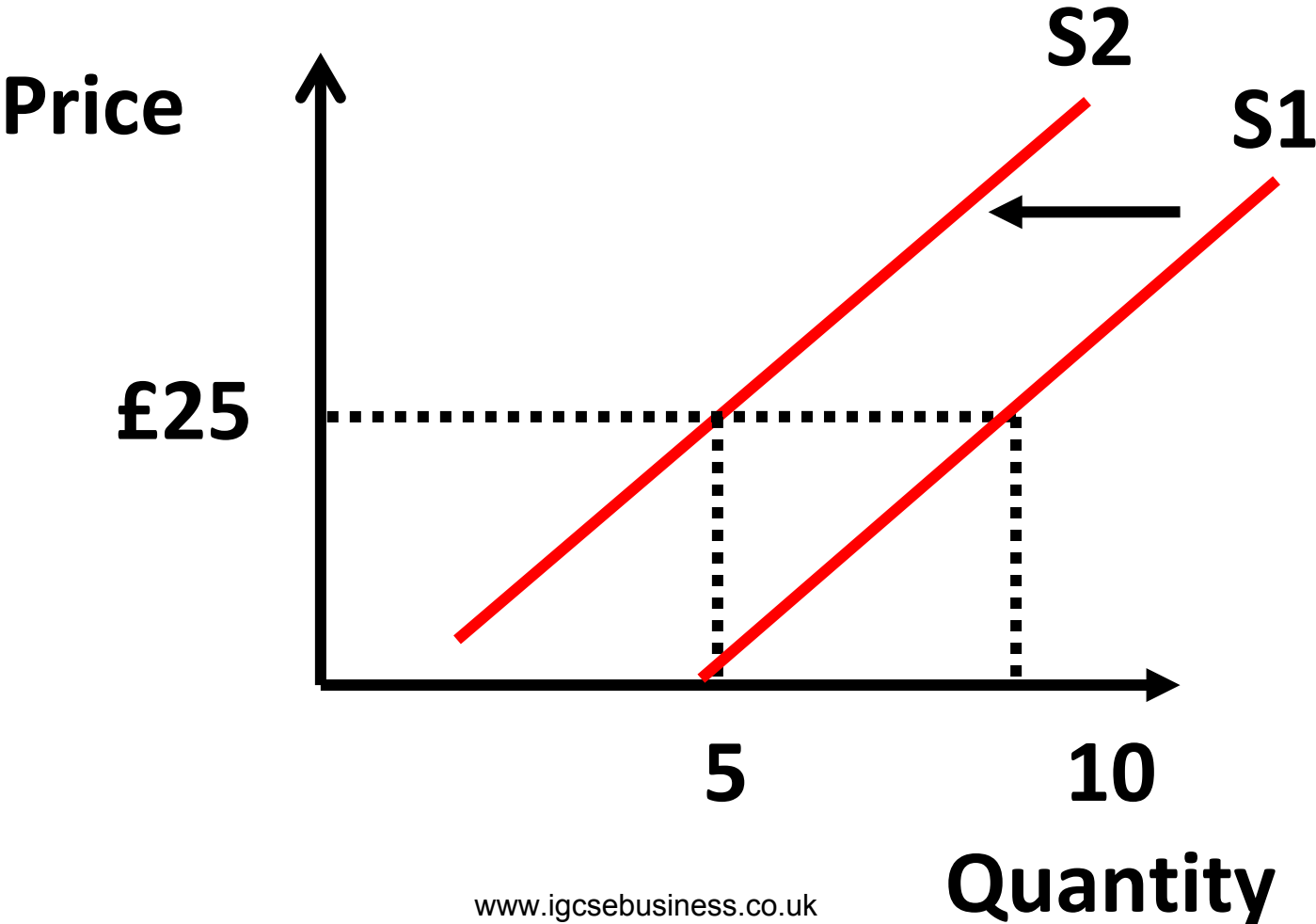




Does the Supply Curve work in the same way?

Basically yes! In the case of supply though, we need to think about how much of a good is available e.g. has there been a good or bad harvest of a crop etc?

In this example, you can see that if the harvest is poor and prices remain at £25 then the supplier will supply **LESS** i.e. 5 items and not 10!





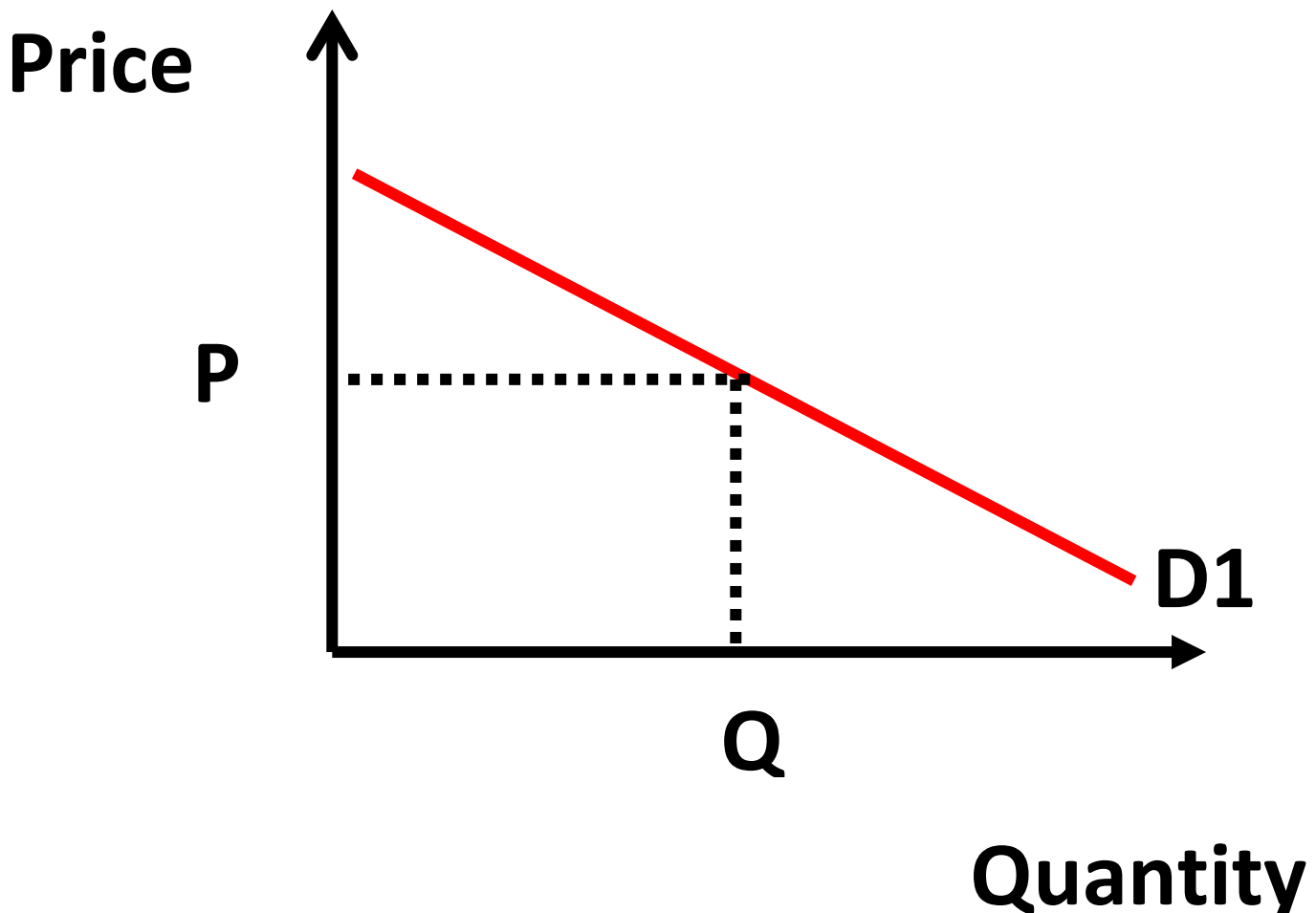
Bob the Blob's Question Time

Can you answer these questions?

Add a new Demand Curve to the diagram below to show the impact of everybody suddenly wanting to buy a new Xbox 360 for Christmas.

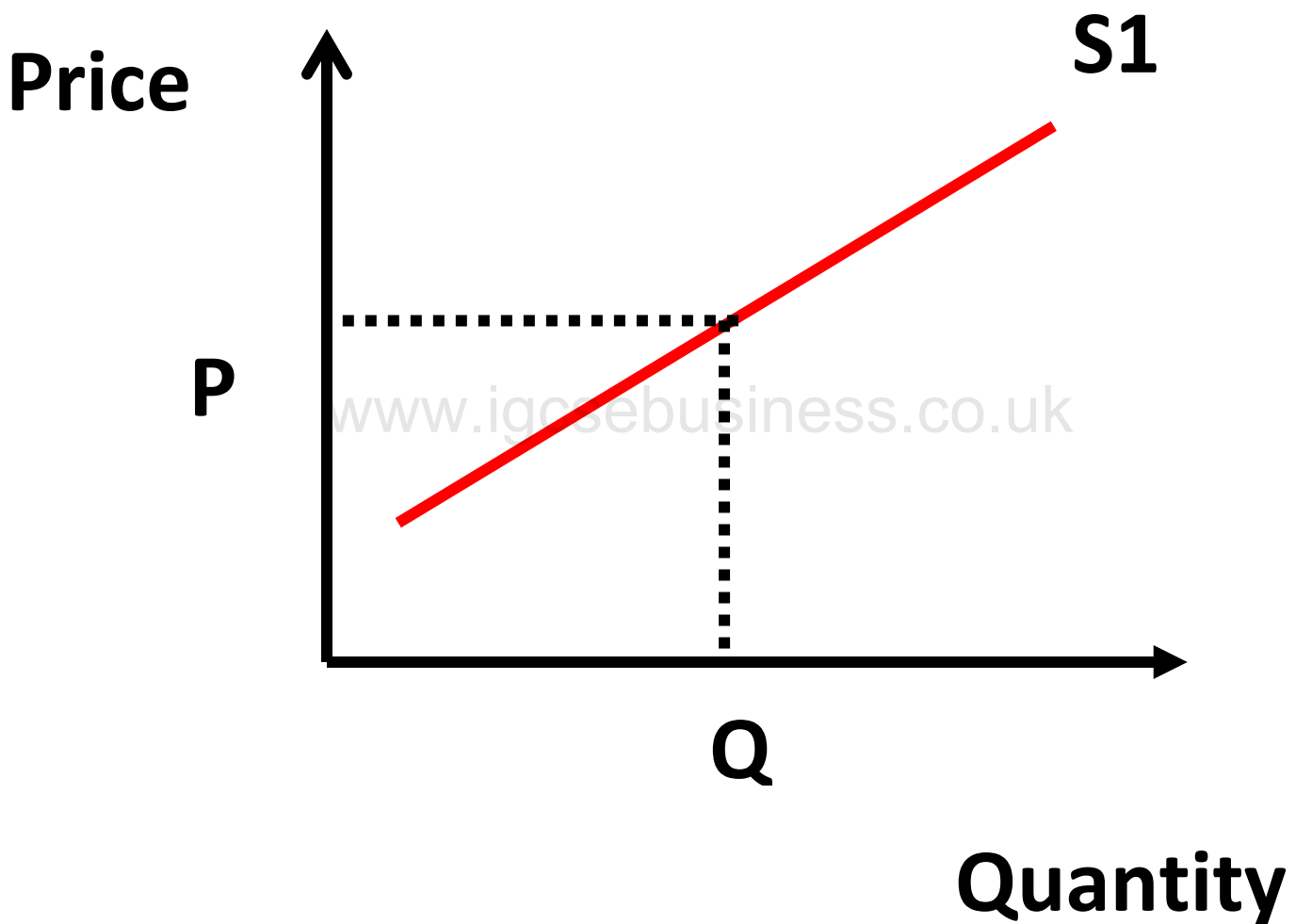


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Add a new Supply Curve to show the impact upon supply that a very successful apple harvest will have upon the cider industry.

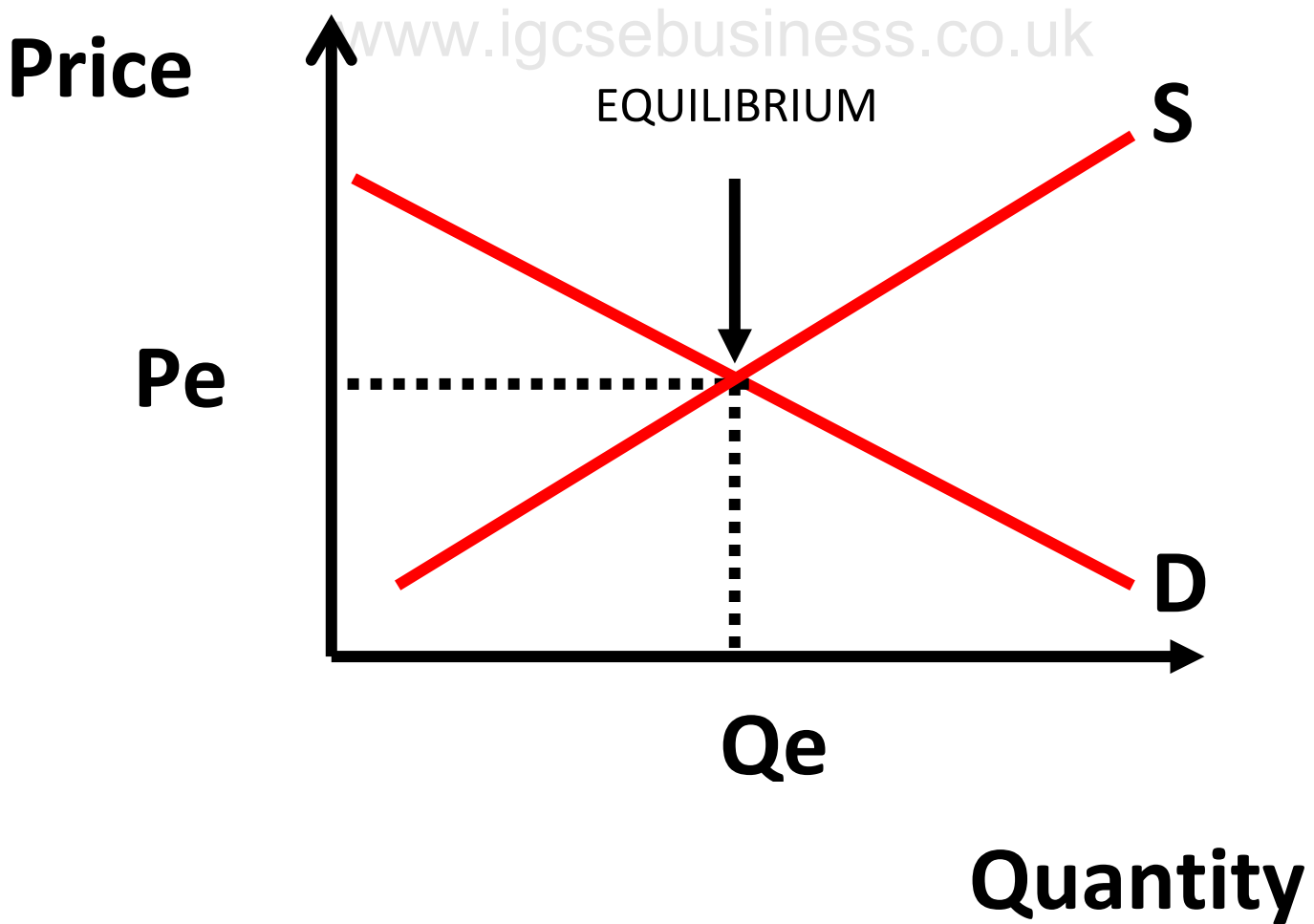


Now add another line to show what would happen to the Supply Curve if the apple harvest had been poor.



What happens when we bring both charts together?

A more detailed diagram will have both the Supply and Demand Curves on the same chart. Where the two lines cross this is the **EQUILIBRIUM POINT**.



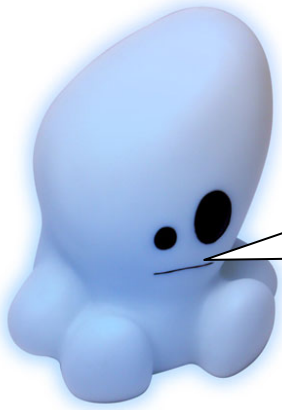
All you need to remember is that at the equilibrium point, then the level of supply is exactly the same as the level of demand. This means that at the equilibrium price, then everything you offer for sale will actually be sold. It is the **MARKET CLEARING PRICE**.

This is all very interesting but what price am I going to charge for my Mars Bars? And no-one has still bought one of my suet puddings!



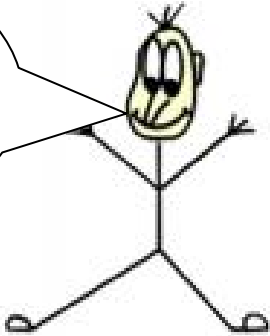
Let's have a look at this data:

PRICE	SUPPLY	DEMAND
10p	0	20
20p	5	15
30p	10	10
40p	15	5
50p	20	0

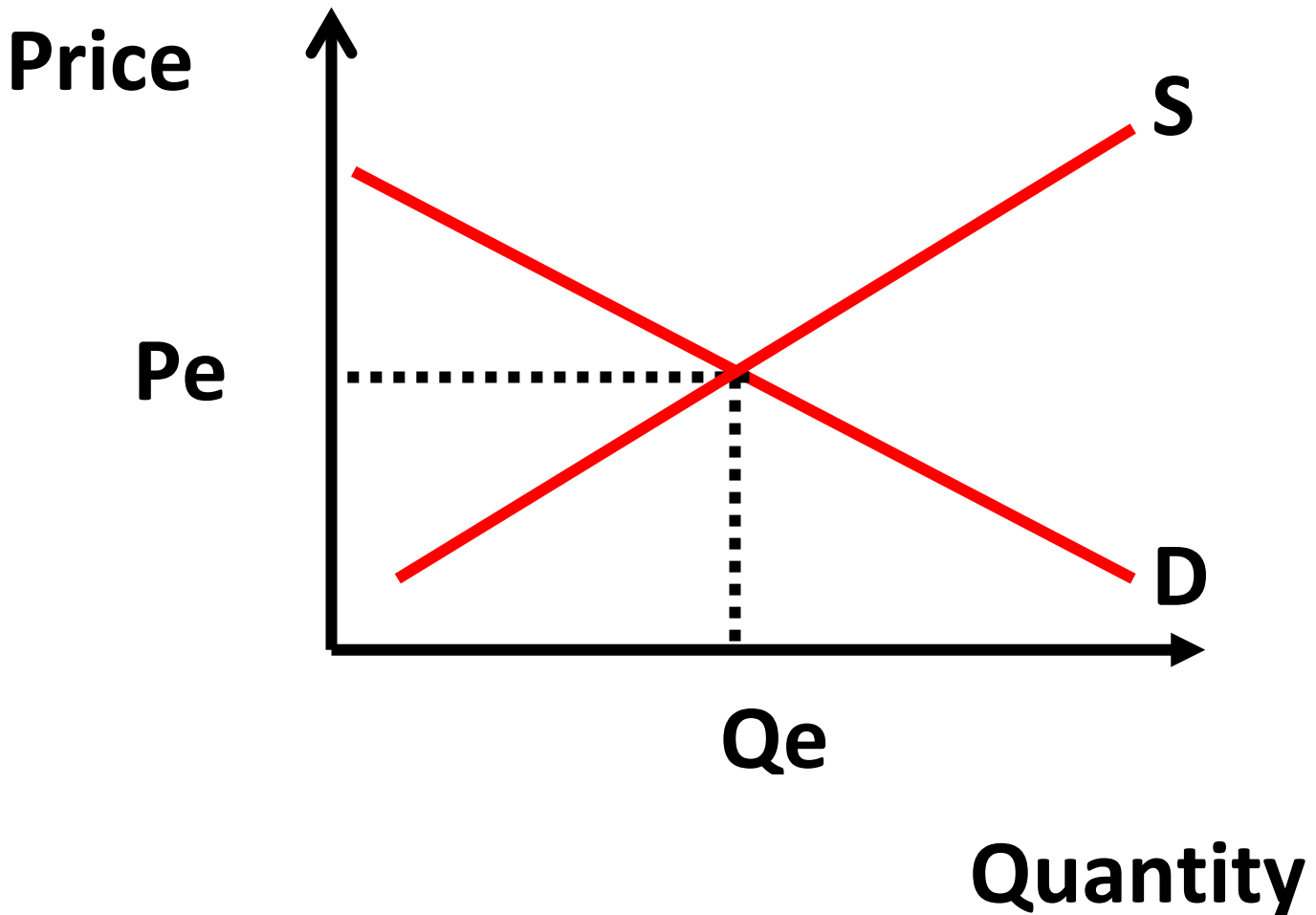


Can you work out what price Arkwright should sell his Mars Bars for using the table?

Did you get the right answer? You should have worked out that at 30p levels of supply and demand are equal. This is EQUILIBRIUM!



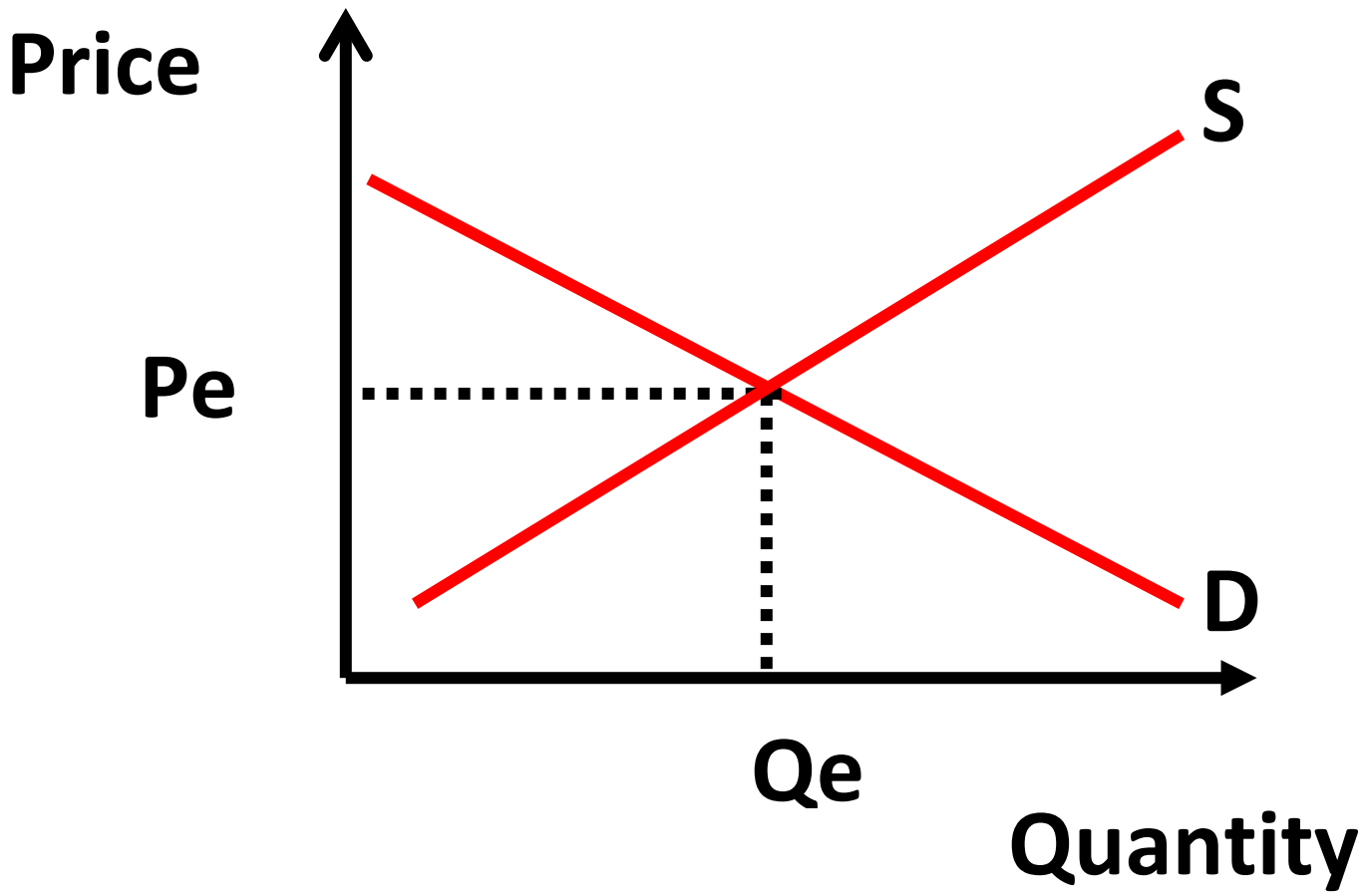
Explain in as much detail as you can, what would happen if Arkwright were to sell his Mars Bars for a higher or lower price than 30p. You **MUST** use the data in the table to help you!



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Draw on the chart above to show what would happen to the Equilibrium point if levels of Demand fell so that the Demand Curve shifted to the left.

Explain why the equilibrium point has changed in this way.



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Draw on the chart above to show what would happen to the Equilibrium point if levels of Supply rose so that the Supply Curve shifted to the right.

Explain why the equilibrium point has changed in this way.

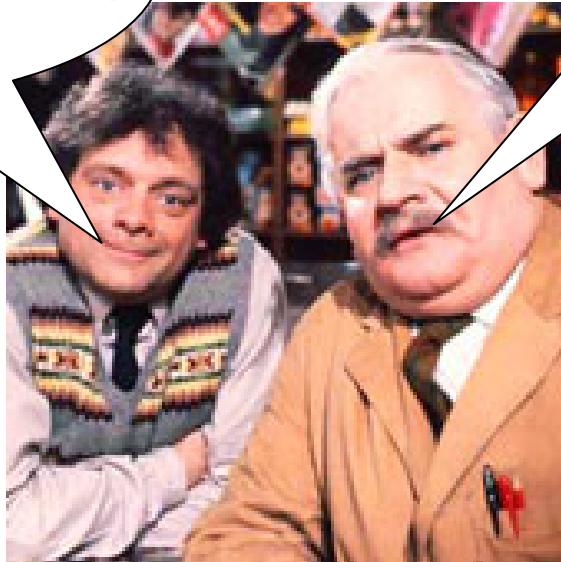


Hey this equilibrium lark is quite useful isn't it!

Now then, what's the equilibrium price for those suet puddings?

I see we still haven't sold those puddings.

Oh go fetch a cloth!



Copy out the paragraph below and use the words in the box to fill in the gaps. You will need to use some words MORE THAN ONCE!

EQUILIBRIUM	DEMAND	SUPPLY	PRICE
QUANTITY	MARKET CLEARING	SHIFT	MOVEMENT

Supply and Demand diagrams are designed to help us to work out the _____ price. This means the price that ensures that _____ and _____ levels are the same and that all items sold at this price are bought by the customer. This is sometimes also called the _____ price. The _____ curve goes in an upwards direction. The _____ curve is drawn in a downwards direction. When we change the price of a good we can normally read along the line to see the change in demand or supply. This is called _____ along the curve. Sometimes though, the entire supply or demand line can _____. The X-Axis of a supply and demand chart is used to measure _____ and the Y-Axis is used to measure _____.

Explain in your own words the meaning of the term equilibrium.
