CATCHING-UP ALONG THE GLOBAL VALUE CHAIN: MODELS, DETERMINANTS AND POLICY IMPLICATIONS

CATCHAIN

Marie Sklodowska Curie PCN - Horizon 2020

The Laws of Supply and Demand

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Supply and Demand

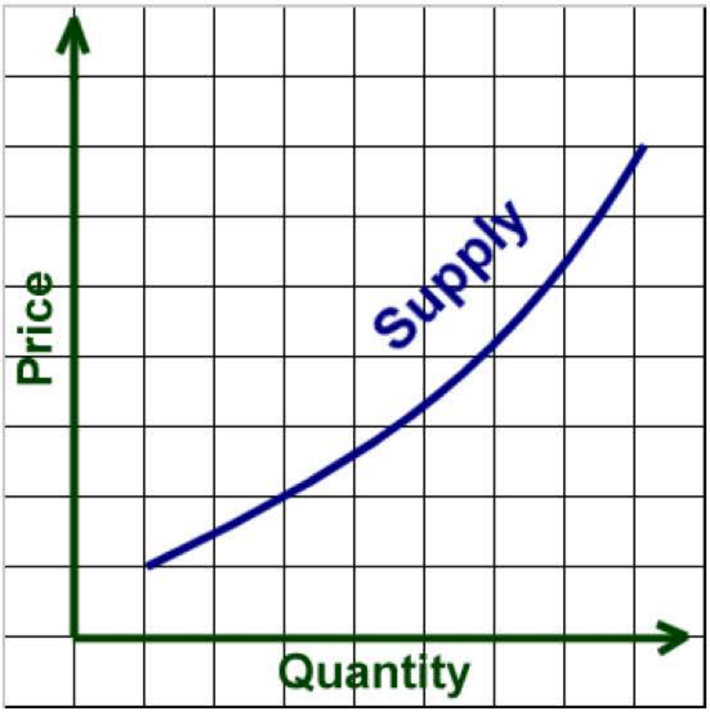
A Basic Law of Economics

Supply and demand is one of the basic ideas of economics. In a free market, the price of a product is determined by the amount of supply of the product and the demand for the product.

What is supply?

The supply of a product is how much of the product is available for purchase at a given price. The law of supply says that as the price of a product increases, companies will build more of the product.

When graphing the supply vs. the price of a product, the slope rises as shown in this graph.



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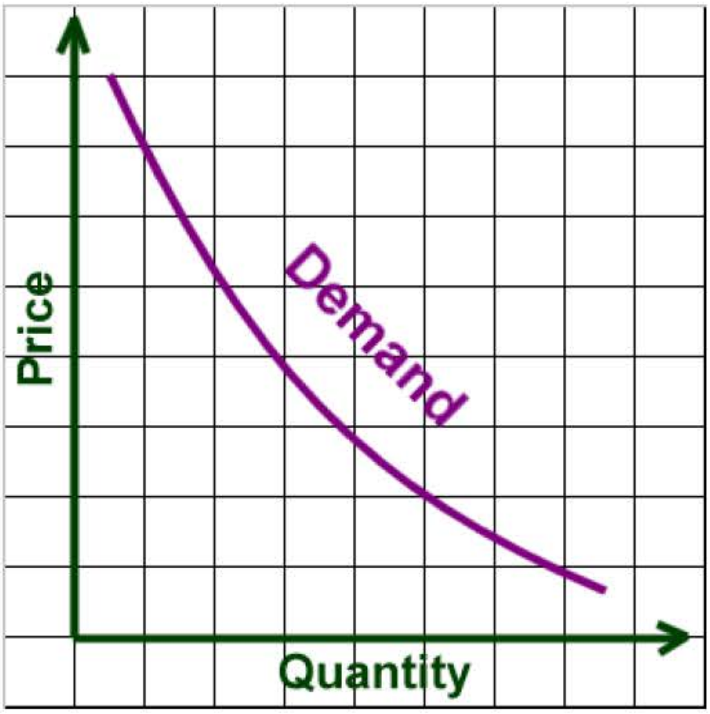
What is demand?

Demand of a product is the amount of product that people want to buy at a given price. The law of demand says that as the price of a product increases, the less of that product people will want to buy.

When graphing the demand vs. the price of a product, the slope falls as shown in this graph.



How Supply and Demand Determine Price

There are four basic laws that describe how supply and demand influence the price of a product:

1) If the supply increases and demand stays the same, the price will go down.

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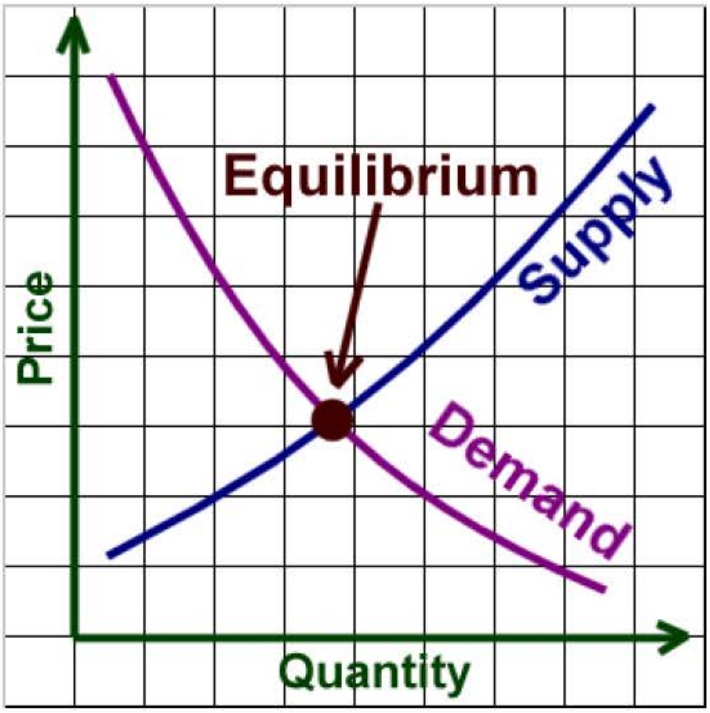
2) If the supply decreases and demand stays the same, the price will go up.
3) If the supply stays the same and demand increases, the price will go up.
4) If the supply stays the same and demand decreases, the price will go down.

Market Equilibrium

Market equilibrium is when the supply of the product equals the demand of the product. The market for a product will move towards equilibrium over time. Equilibrium can be shown on a graph. It is where the supply and the demand curves intersect.



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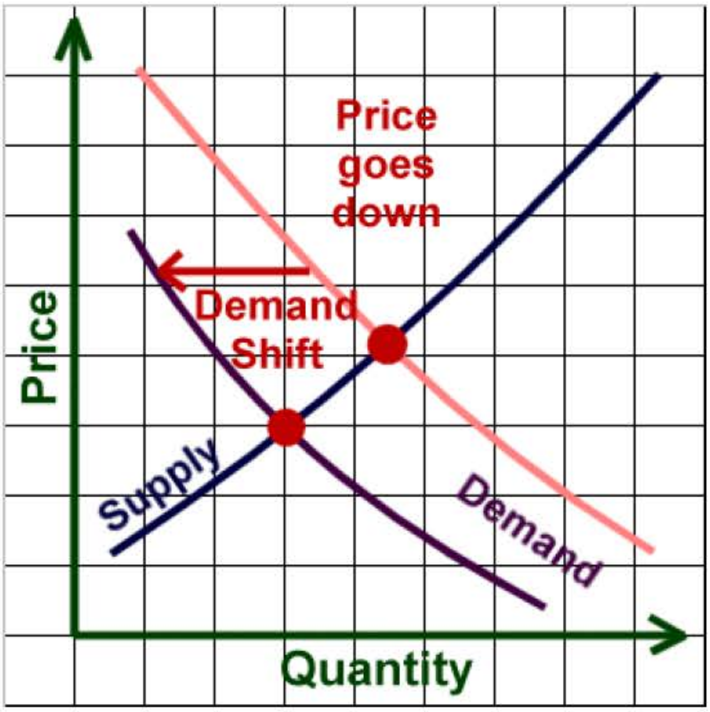
Changes in Supply and Demand

Supply and demand can suddenly change. This can cause a "shift" in the demand or supply curves. Any number of factors can change the supply or demand. For example, the demand for a football team's jerseys would go up if they won the Super Bowl. Also, the supply for those same jerseys may go down if the factory that made them burnt down.

See the graph for an example of a demand curve shift.



Here are some things that can change demand:

- Income - If people have more money, the demand for products can increase.
- Population - As the population increases, there are more buyers. This will increase demand.
- Customer preference - Customers may no longer want a product, reducing the demand.

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- Changes in competition - If the competitors of a product increase their price, then the demand for your product may increase.

Here are some things that can change supply:

- Number of sellers - If the number of sellers increases, then the supply will increase.
- Technology - Improvements in manufacturing can increase supply.
- Resources - If resources needed to build a product are moved to another product, then supply will decrease.
- Costs of manufacturing - If the costs for making a product increase, the supply will decrease.

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