Topic 1.2 The Market

Demand
A measure of the quantity of a product that consumers want and buy at a given price, at a particular time.

Factors Affecting Demand
- **Substitutes** – the demand for a particular brand or product type can be affected by a price change of a substitute (a product that replaces another).
- **Complementary products** – products which are used together, e.g. printers and ink cartridges. if the price of the printers were to increase, the demand for printers might fall, and so the demand for ink cartridges could fall too.
- **Consumer income** - a higher income can lead to an increase in demand for more expensive products, whereas a fall in income can increase the demand for cheaper goods and services.
- **Fashion, consumer tastes and consumer preferences** – demand for a product relies on what consumers want. E.g. warnings about the dangers of eating too much sugar could lead to a change in consumer diets - this could lead to a fall in demand for sugary drinks and an increase in demand for healthier drinks.
- **Advertising and branding** - increase demand for a product or encourage existing consumers to be loyal to the product or brand and repeatedly buy the product to stop demand falling.
- **Demographics** – changes in population can lead to changes in demand. E.g. advances in healthcare mean that people are living longer. This has led to an increase in demand for goods and services for the older generation.
- **Seasonal changes** – demand for goods and services can changes throughout the year. E.g. summer leads to an increase in demand for fans.
- **External shocks** - this include the threat of war, diseases, and extreme weather. E.g. a risk of flooding may lead to an increase in demand for sandbags.

Supply
The quantity of a product that suppliers are willing and able to supply to a market at a given price, at a particular time.

Factors Affecting Supply
- **Cost of production** - if the cost of production increases then the profit made from selling the product at a given price decreases, so there will be a fall in supply.
- **Indirect taxes** - The government can influence supply by changing taxation where if the tax on a good or service increases, then this effectively increases the costs for the producer and they are likely to reduce their supply
- **Subsidies** - a subsidy is money given to a business by the government to help it with its costs and encourage it to produce more of a particular product.
- **New technology** - this can lead to more efficient production techniques and therefore cost savings. Lower costs would mean that a firm would be willing and able to increase the supply of its good or service.
- **Weather conditions** - a severe change in weather can affect the supply of goods and services, especially in agriculture where the weather affects harvests.
- **External shocks** - this includes shocks such as war, which can affect supply.

Key Words

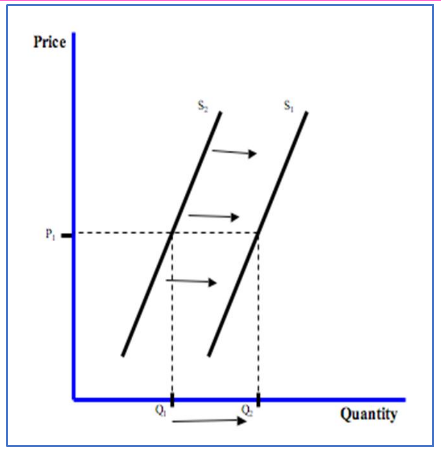
Supply Curve	Demand Curve	Subsidy
Complementary Goods	Normal Goods	Inferior Goods
Elastic	Inelastic	Unitary

Price Elasticity of Demand
The relationship between a change in the price of a product and the change in demand for the product.

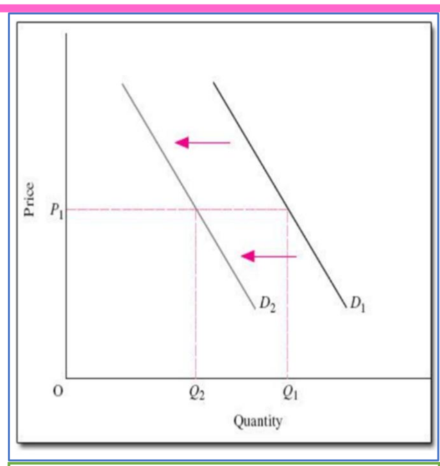
PRICE ELASTICITY OF DEMAND = % CHANGE IN QUANTITY DEMANDED/ % CHANGE IN PRICE

	PRICE ELASTIC	PRICE INELASTIC
PRICE INCREASE	Leads to a big % decrease in quantity demanded. Revenue falls	Leads to a small % decrease in quantity demanded. Revenue still rises
PRICE DECREASE	Leads to a big % increase in quantity demanded. Revenue rises	Leads to a small % increase in quantity demanded, but revenue fall due to lower prices

Factors Affecting PED
- Number of substitutes/competitors.
- Relative effort/costs of switching to another product.
- Extent to which the product is considered a necessity.
- Perceived value of the brand.
- Time – the PED for a product will tend to fall over time as consumers find substitutes.
- Percentage of income spent on the product.



Shift in Supply Curve



Shift in Demand Curve

PED

>1 (Highly Price Elastic) 1 (Price Elastic) 0 (Price Inelastic)

YED

>1 (Highly Elastic) 1 (Income Elastic) 0 (Inelastic)

Income Elasticity of Demand
The relationship between a change in income and the change in demand for a product.

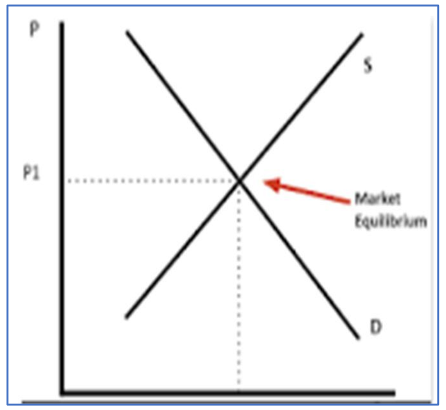
INCOME ELASTICITY OF DEMAND = % CHANGE IN QUANTITY DEMANDED/% CHANGE IN INCOME

Factors Affecting YED
- Whether the product is considered a necessity.
- Whether the product is considered a luxury.
- The price relative to people's incomes (%). For example, the YED of a chocolate bar is relatively inelastic as it costs a small percentage of most people's income.

Elastic and Inelastic Demand
- **INCOME ELASTIC DEMAND** – this means that a percentage change in incomes would lead to a proportionate or greater percentage change in quantity demanded. Goods that have income elastic demand include cars, TVs, and clothing.
- **INCOME INELASTIC DEMAND** – this is where a percentage change in incomes will lead to a proportionately lower change in the quantity demanded. These products might be considered necessities, such as some food types.
- **NORMAL GOODS** – this is where an increase in incomes leads to an increase in the quantity demanded. Normal goods have a positive income elasticity of demand.
- **INFERIOR GOODS** – an increase in incomes will lead to a fall in demand. A decrease in incomes will lead to an increase in demand. Inferior goods have a negative income elasticity of demand.

Remember
PED:
- A rise in demand = Shift to the right.
- A fall in demand= Shift to the left.

YED:
- A rise in income= Shift to the right.
- A fall in income= Shift to the left.



Market Equilibrium