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The Big Question

What happens if the mangoes your parents bought last week are now half the price? Why are vegetables expensive in the morning but cheaper in the evening? Why does the price of onions change every few months? Why does the same flight seat cost differently on different days? Why do shops announce discounts at certain times? These questions arise from the interaction of demand and supply in markets. This chapter explores how demand, supply, and price determination work together in real-world markets.

Demand

Demand is the quantity of a product that people are willing and able to buy at a particular price, influenced by their needs, preferences, income, and other factors. It is not just desire but includes purchasing power.

Law of Demand

The Law of Demand states that when the price of a product rises, the quantity demanded decreases, and when the price falls, the quantity demanded increases. This inverse relationship is shown by a downward sloping demand curve.

Individual and Market Demand

Individual demand is the quantity a single consumer wants to buy at different prices. Market demand is the total quantity demanded by all consumers at different prices, obtained by summing individual demands.

Other Determinants of Demand

- **Price of related goods:** Substitute goods (e.g., tea and coffee) and complementary goods (e.g., smartphones and earphones) affect demand.

- **Income of the consumer:** Higher income generally increases demand.
- **Taste and preference:** Personal likes affect demand.
- **Seasonality:** Demand changes with seasons and festivals.
- **Future price expectations:** Expectations about future prices influence current demand.
- **Population size and composition:** Different groups demand different products.

Exam Question

Q: What is the Law of Demand? Explain with an example.
A: The Law of Demand states that as the price of a product falls, the quantity demanded rises, and vice versa. For example, when mango prices fall from ₹150 to ₹50 per kg, consumers buy more mangoes.

Supply

Supply is the quantity of a product that sellers are willing and able to offer at different prices. The Law of Supply states that as price rises, quantity supplied increases, and as price falls, quantity supplied decreases.

Individual and Market Supply

Individual supply is the quantity a single seller offers at different prices. Market supply is the total quantity supplied by all sellers at different prices.

Other Determinants of Supply

- **Price of related goods:** Profitability of alternative goods affects supply.
- **Number of sellers:** More sellers increase market supply.
- **Technology:** Improved technology can increase supply by reducing production costs.
- **Future expectations:** Expectations about future demand and prices influence current supply.

Exam Question

Q: What is the Law of Supply? Illustrate with an example.
A: The Law of Supply states that as the price of a product rises, the quantity supplied increases. For example, as mango prices rise from ₹50 to ₹150 per kg, sellers supply more mangoes.

Market Equilibrium

Market equilibrium is the point where quantity demanded equals quantity supplied, resulting in stable prices without shortage or surplus.

Real World Dynamics

In reality, markets are dynamic and constantly adjust due to changes in technology, income, weather, and other factors. Equilibrium shifts over time rather than remaining fixed.

Exam Question

Q: What is market equilibrium? Does it exist in the real world?
A: Market equilibrium is when quantity demanded equals quantity supplied, stabilizing prices. In the real world, equilibrium is dynamic and changes due to various factors.

Role of Government in the Economy

The government intervenes in markets to ensure fairness, protect vulnerable groups, regulate unfair practices, provide public goods, and prevent monopolies.

Regulation of Unfair Practices

The government sets price ceilings (maximum prices) and price floors (minimum prices) to protect consumers and workers. It also regulates monopolies to prevent exploitation.

Provision of Public Goods

Public goods like roads, parks, national defence, and sanitation are provided by the government because private companies may not supply them due to lack of profit.

Limitations of Government Intervention

- Price distortions can reduce producer incentives.
- Compliance burdens can hinder small businesses.
- Excessive regulation may discourage innovation and entrepreneurship.

Exam Question

Q: Why does the government intervene in markets? Mention any two reasons.
A: The government intervenes to protect consumers from unfair practices and to provide public goods that private firms may not supply.

Solved Examples

1. **Example 1:** If the price of mangoes falls from ₹150 to ₹50, how does the quantity demanded change?
   Answer: According to the Law of Demand, quantity demanded increases as price falls. So, consumers buy more mangoes at ₹50 than at ₹150.
2. **Example 2:** A seller supplies 1 kg of mangoes at ₹50 and 3 kg at ₹150. What does this illustrate?
   Answer: This illustrates the Law of Supply, where quantity supplied increases with price.

Practice Set

Easy

- Define demand and supply.
- What happens to demand when price falls?

Moderate

- Explain the difference between individual demand and market demand.
- List any three determinants of demand other than price.

Challenging

- Discuss the role of government in regulating markets and providing public goods.
- Explain why market equilibrium is dynamic in the real world.

Answer Key

- Demand is the quantity consumers are willing and able to buy at different prices. Supply is the quantity sellers are willing and able to offer at different prices.
- When price falls, demand increases.
- Individual demand is the quantity demanded by one consumer; market demand is the total demand by all consumers.
- Determinants include income, taste and preference, price of related goods, seasonality, future expectations, and population.
- The government regulates markets to protect consumers and provide public goods.
- Market equilibrium changes due to shifts in demand and supply caused by external factors.

Quick Reference

- **Demand:** Quantity consumers want and can buy at different prices.
- **Supply:** Quantity sellers offer at different prices.
- **Law of Demand:** Price and quantity demanded have an inverse relationship.
- **Law of Supply:** Price and quantity supplied have a direct relationship.
- **Market Equilibrium:** Point where demand equals supply.
- **Price Ceiling:** Maximum price set by government.
- **Price Floor:** Minimum price set by government.
- **Monopoly:** Single seller controls market.
- **Public Goods:** Goods provided by government for all.

Glossary

- **Demand:** Willingness and ability to buy a product at a given price.
- **Supply:** Willingness and ability to sell a product at a given price.
- **Purchasing Power:** The ability to buy goods and services with a unit of currency.
- **Price Ceiling:** Maximum price allowed by law.
- **Price Floor:** Minimum price allowed by law.
- **Monopoly:** Market with a single seller.
- **Hoarding:** Accumulating goods beyond immediate need.
- **Black Marketing:** Illegal trade of banned or regulated goods.
- **Market Equilibrium:** Situation where quantity demanded equals quantity supplied.