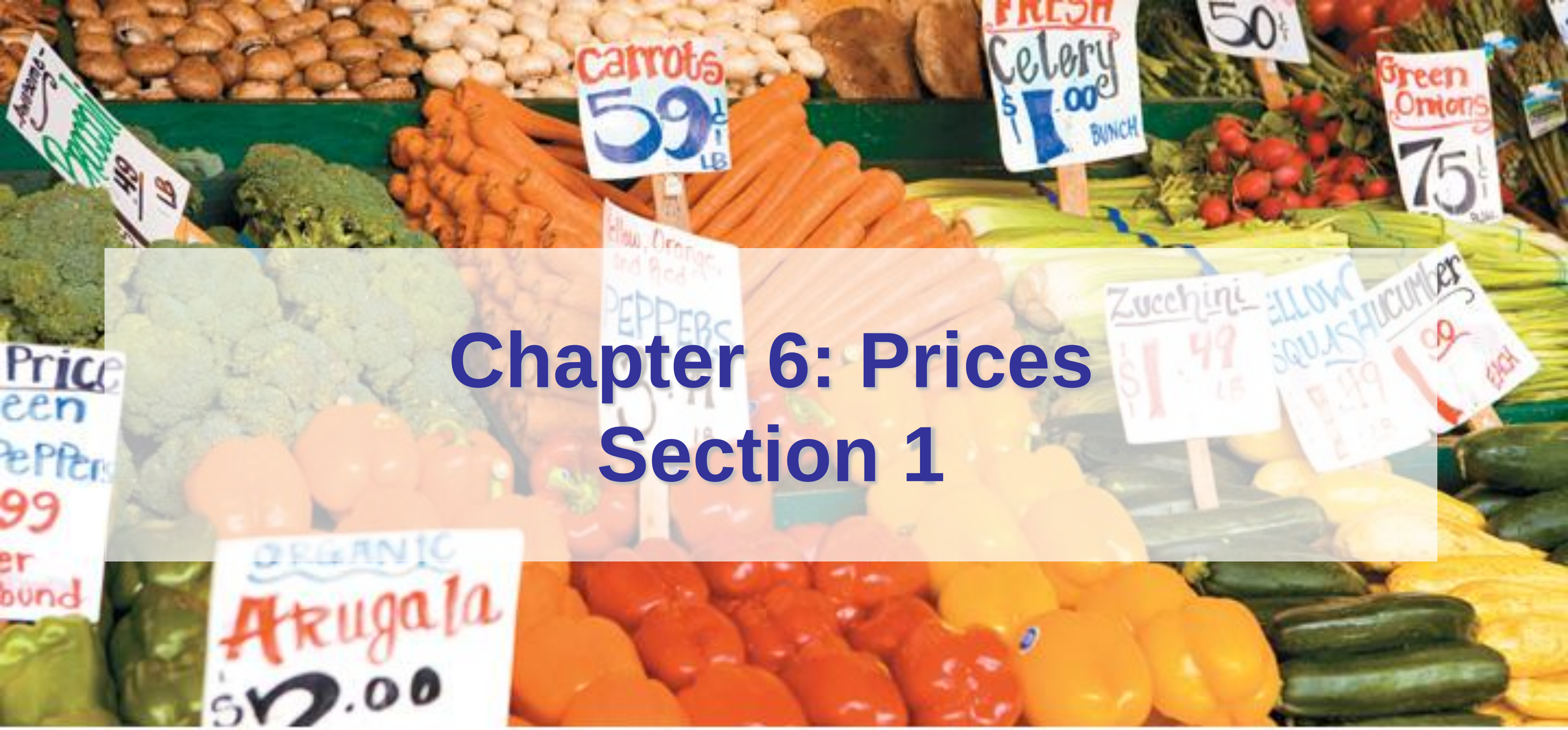

Chapter 6: Prices
Section 1

Prentice Hall

ECONOMICS

PEARSON

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Objectives

1. **Explain** how supply and demand create equilibrium in the marketplace.
2. **Describe** what happens to prices when equilibrium is disturbed.
3. **Identify** two ways that the government intervenes in markets to control prices.
4. **Analyze** the impact of price ceilings and price floors on a free market.

Key Terms

- **equilibrium**: the point at which the demand for a product or service is equal to the supply of that product or service
- **disequilibrium**: any price or quantity not at equilibrium
- **shortage**: when quantity demanded is more than quantity supplied
- **surplus**: when quantity supplied is more than quantity demanded

Key Terms, cont.

- **price ceiling**: a maximum price that can legally be charged for a good or service
- **rent control**: a price ceiling placed on apartment rent
- **price floor**: a minimum price for a good or service
- **minimum wage**: a minimum price that an employer can pay a worker for one hour of labor

Introduction

- What factors affect price?
  - Prices are affected by the laws of supply and demand.
  - They are also affected by actions of the government.
    - Often times the government will intervene to set a minimum or maximum price for a good or service.

What is Equilibrium?

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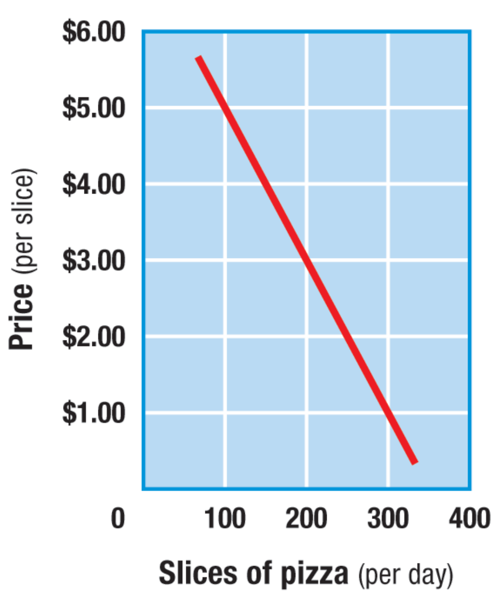
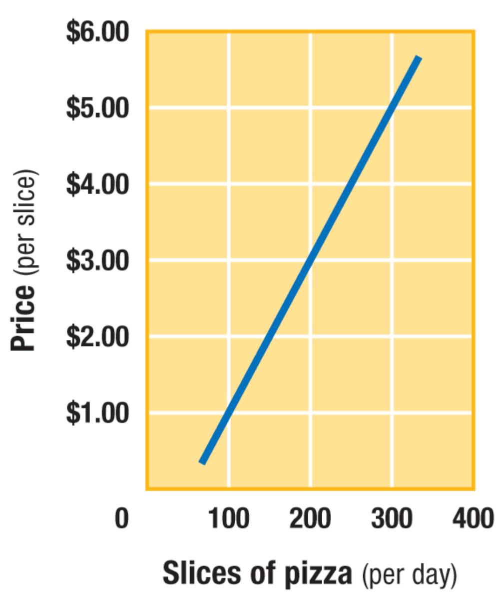
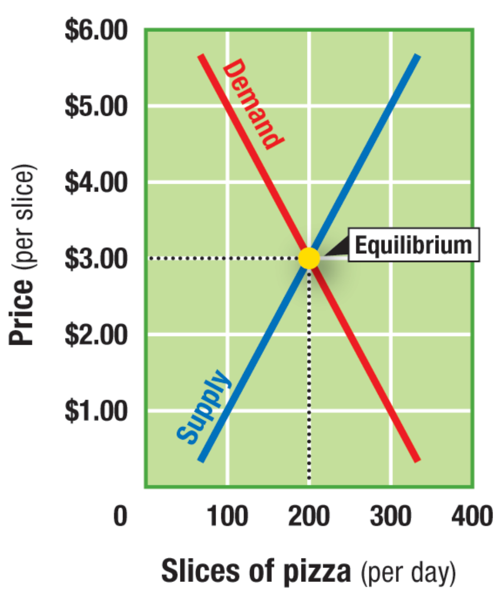
DEMAND CURVE



SUPPLY CURVE



FINDING EQUILIBRIUM



Equilibrium

- In order to find the equilibrium price and quantity, you can use supply and demand schedules.
- When a market is at equilibrium, both buyers and sellers benefit.
  - How many slices are sold at equilibrium?

Combined Supply and Demand Schedule

Price of a Slice of Pizza	Quantity Demanded	Quantity Supplied	Result
$1.00	300	100	Shortage from excess demand
$2.00	250	150	
$3.00	200	200	Equilibrium
$4.00	150	250	Surplus from excess supply
$5.00	100	300	
$6.00	50	350	

Disequilibrium

- Checkpoint: What market condition might cause a pizzeria owner to throw out many slices of pizza at the end of the day?
  - If the market price or quantity supplied is anywhere but at equilibrium, the market is said to be at disequilibrium.
  - Disequilibrium can produce two possible outcomes:
    - Shortage—A shortage causes prices to rise as the demand for a good is greater than the supply of that good.
    - Surplus—A surplus causes a drop in prices as the supply for a good is greater than the demand for that good.

Shortage and Surplus

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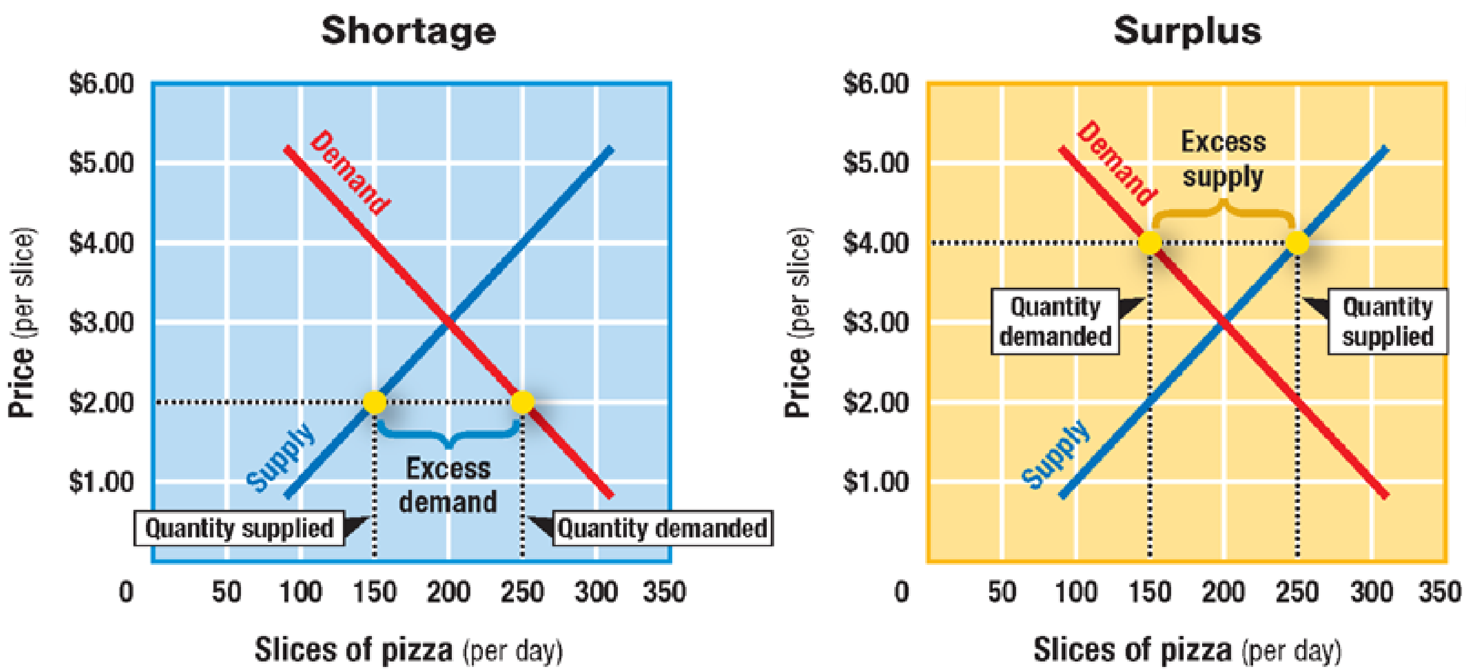
- Shortage and surplus both lead to a market with fewer sales than at equilibrium.
  – How mush is the shortage when pizza is sold at $2.00 per slice?



Action Graph online

Price Ceiling

- While markets tend toward equilibrium on their own, sometimes the government intervenes and sets market prices. Price ceilings are one way the government controls prices.

  - Rent Control
    - Sets a price ceiling on apartment rent
    - Prevents inflation during housing crises
    - Helps the poor cut their housing costs
    - Can lead to poorly managed buildings because landlords cannot afford the upkeep.

The Effects of Rent Control

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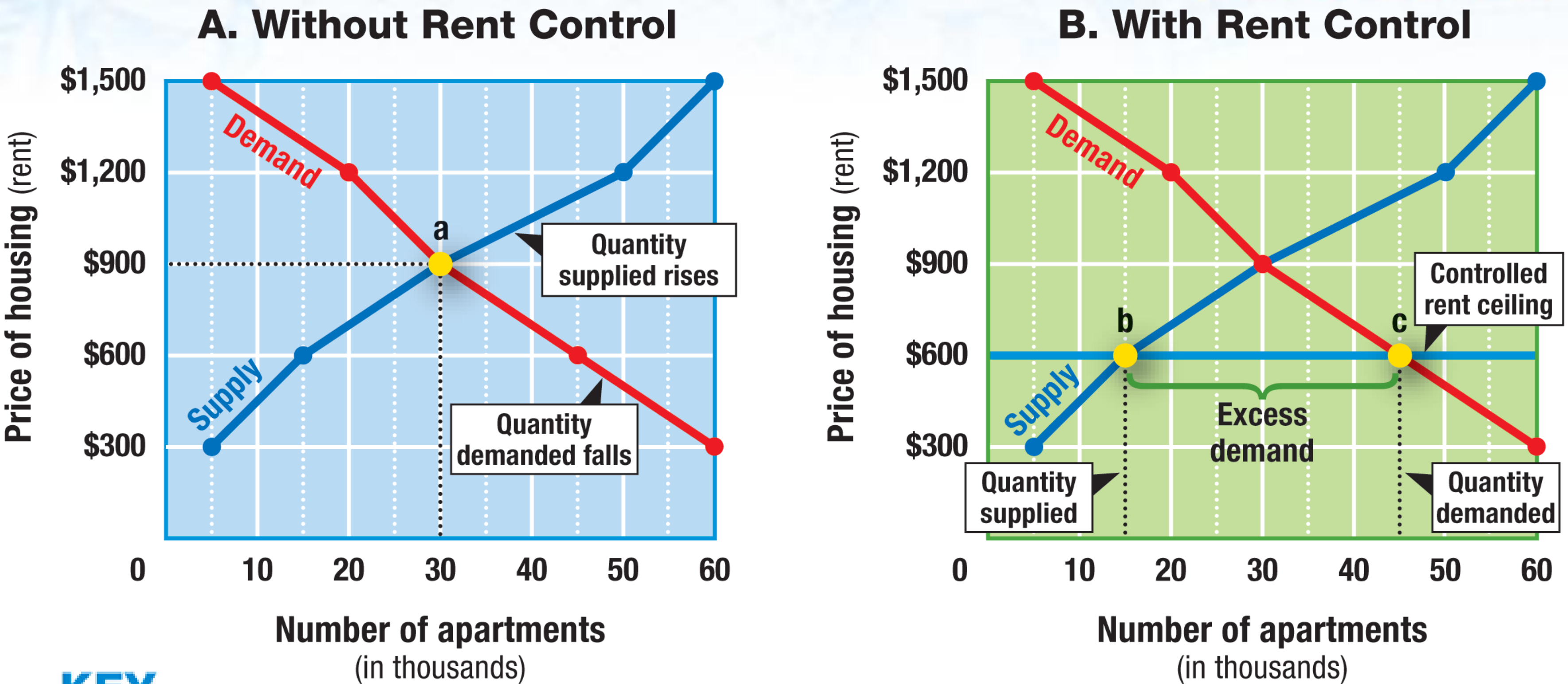


KEY

a. The supply and demand curves for two-bedroom apartments meet at the equilibrium rent of $900 per month.

b. With rent control keeping rents at $600 per month, landlords are willing to supply 15,000 two-bedroom apartments.

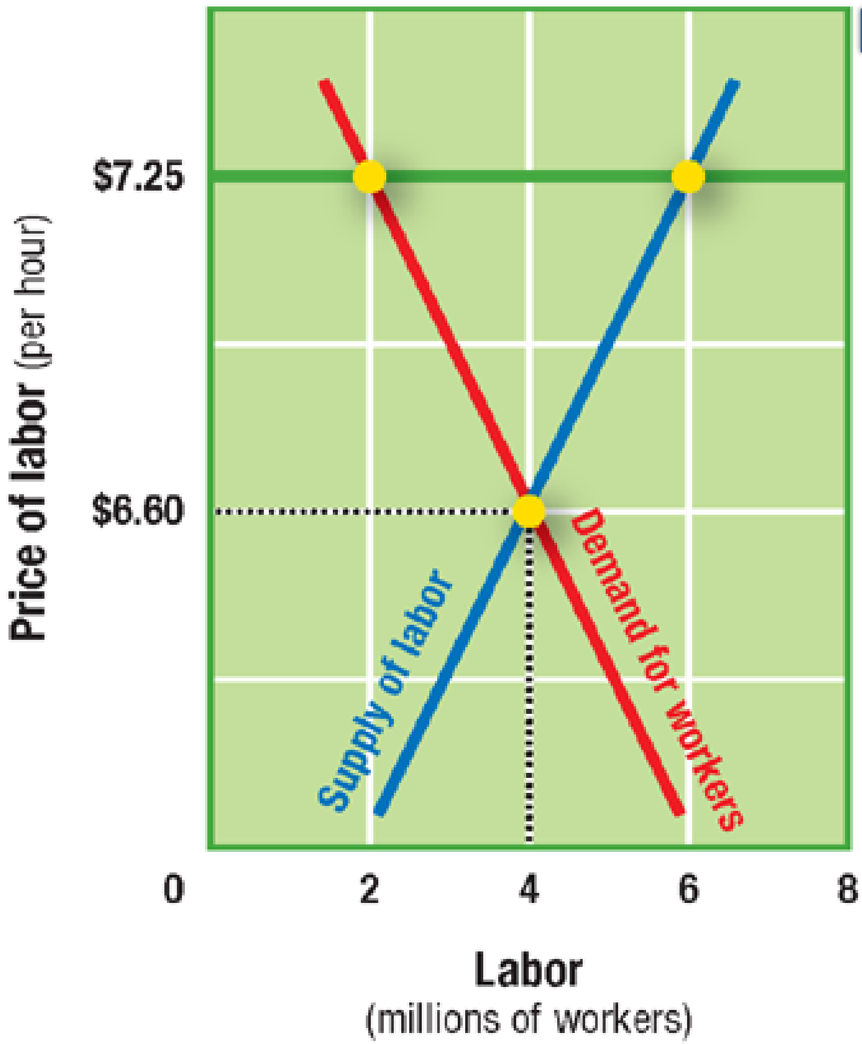
c. With rent control keeping rents at $600 per month, potential tenants are seeking 45,000 two-bedroom apartments.

Action Graph online

Price Floors

- A price floor is a minimum price set by the government. The minimum wage is an example of a price floor.
- Minimum wage affects the demand and the supply of workers.

  – At what wage is the labor market at equilibrium?



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Price Supports in Agriculture

- Price supports in agriculture are another example of a price floor.
- They began during the Great Depression to create demand for crops.
- Opponents of price supports argue that the regulations dictate to farmers what they should produce.
- Supporters say that without government intervention, farmers would overproduce.

Review

- Now that you have learned about the factors that affect price, go back and answer the Chapter Essential Question.
  - What is the right price?