Chapter 2

Demand and Supply: The Basics of the Market Economy

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| Chapter Outline | Alternate Lecture Outline |
| * Prices, Buyers, and Sellers   + Local, National, and Global Markets   + The Market Price * How Price Affects the Quantity Demanded   + The Law of Demand   + The Special Case of Zero Price   + Graphing the Demand Curve * How Price Affects the Quantity Supplied   + The Law of Supply   + Graphing the Supply Schedule * New Markets | * Prices, Buyers, and Sellers   + The Market Price * How Price Affects the Quantity Demanded   + The Law of Demand   + The Special Case of Zero Price * How Price Affects the Quantity Supplied   + The Law of Supply * How Price Affects the Quantity Demanded   + Graphing the Demand Curve * How Price Affects the Quantity Supplied   + Graphing the Supply Schedule * Prices, Buyers, and Sellers   + Local, National, and Global Markets * New Markets |

Potential Stumbling Blocks

Students might have difficulty correctly using the words “demand” and “supply.” Remind them that these words refer to the *relationships* between price and quantity. This will become more important in the next chapter when they put supply and demand together.

Make sure students know that any time you construct a demand or supply schedule or curve, it relates to a specific good, a specific group of buyers, and a specific time frame. Each can be defined as narrowly or broadly as needed. For example, you could speak of the demand for apples in Cook County, Illinois during 2007 or the demand for Fuji apples in Hyde Park in June 2007, and so on.

Finally, as you know, many students are uncomfortable with graphing. Beginning with a demand or supply schedule (as a table) is a helpful way to ease students into the demand and supply curves because information on a table is often easier to understand. If you did not take the time to cover the material in the appendix to Chapter 1, you may find now that it is helpful.

Additional Resources

The *New York Times* ran an opinion piece on the proposed “summer gasoline tax holiday” that was much discussed by U.S. presidential candidates in the spring of 2008. In it, the author clearly confused the terms “demand” and “quantity demanded.” This kind of confusion leads to an awful (and unrealistic) price cycle: prices go down, which increases *demand*, which causes prices to go up. A *Washington Post* story on the same issue makes the same error.

[New York Times article](http://www.nytimes.com/2008/05/04/us/politics/04economy.html)

[Washington Post article](http://www.washingtonpost.com/wp-dyn/content/article/2008/04/30/AR2008043003575.html)

Changes to the Third Edition

The Economic Milestone box discussing the first prepaid tuition plan in 1986 has been relocated to under the *Prices, Buyers, and Sellers* heading. The Spotlight discussing the Great Ethanol Boom now introduces the regulatory cause of the increase in ethanol demand and discusses what would happen if the ethanol mandate was reduced. New examples and updated statistics have been added throughout.

Spotlight Questions

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| Spotlight: The Milk Market | |
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| 1. The market for fluid milk in the United States is mainly a    1. national market.    2. global market.    3. local market.    4. public market. | 1. A complicated set of government regulations \_\_\_\_\_\_\_\_\_\_ long-distance shipments of fluid milk.    1. encourages    2. discourages    3. prohibits    4. requires |

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| Spotlight: The Great Ethanol Boom | |
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| 1. Rising prices of corn between 2005 and 2007 resulted in    1. a decrease in demand.    2. a decrease in quantity demanded.    3. an increase in supply.    4. an increase in quantity supplied. | 1. The corn ethanol boom was NOT good for    1. consumers who eat pork and beef.    2. farmers who grow corn.    3. consumers who use corn ethanol.    4. government regulators. |

Spotlight Questions Answer Key

1: C, 2: B, 3: D, 4: A

Chapter Quiz Answer Key

1: C, 2: C, 3: A, 4: D, 5: B, 6: D, 7: B, 8: B, 9: A, 10: D

Chapter 2 Quiz Name: \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_ Date: \_\_\_\_\_\_\_\_\_\_\_\_\_

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| 1. Which of the following goods or services is most likely to be bought and sold in a local market?    1. Textbooks    2. Magazine subscriptions    3. Dog grooming    4. Precious metals 2. Suppose that a house is listed for sale at $250,000. What can be said about the price that a home buyer eventually pays for the house?    1. The homebuyer will pay $250,000 because this is the market price for the house.    2. If the homebuyer waits for a sale, he or she may be able to buy the house for less.    3. Through negotiation, the home buyer may pay less for the house or have additional items added to the purchase.    4. If the home buyer buys enough homes, he or she may qualify for a volume discount and pay less for the house. 3. What are the two variables shown in a demand schedule?    1. Price and quantity demanded    2. Market price and sales price    3. Individual quantity demanded and market quantity demanded    4. Demand and supply 4. What does the Latin phrase ceteris paribus mean?    1. "Buyer beware"    2. "And so on"    3. "Led by an invisible hand"    4. "All other things equal" 5. The law of demand    1. is always and everywhere true.    2. describes a general tendency that is true in most normal situations.    3. applies only to the goods and services that buyers want most.    4. has been repeatedly discredited. | 1. Suppose a local bowling alley offers a membership program in which games are free to those who pay a monthly membership fee. Which of the following statements is true regarding how many games members will bowl per month?    1. Members will bowl as many games as they have time for.    2. Members will bowl as many games as they can until they are physically unable to bowl anymore.    3. Members will bowl as many games as they would have in the absence of a membership program.    4. Members will bowl as many games as it takes so that additional games no longer make them happier than other things they could spend their time doing. 2. What is the best way to investigate a consumer’s demand behavior?    1. Mail her a survey.    2. Observe her buying behavior.    3. Subject her to psychological evaluations.    4. Interview her in person. 3. A supply curve is    1. downward-sloping.    2. a graphical representation of the information in a supply schedule.    3. always a straight line.    4. All of the above are true of supply curves. 4. The market supply schedule    1. combines the quantity supplied by all of the businesses in a market.    2. has as many columns as the market does businesses.    3. relates quantity demanded and supplied.    4. does not initially exist in new markets. 5. Why do new markets arise?    1. New technologies    2. Changing needs of consumers    3. Increased incomes of developing nations    4. All of the above can give rise to new markets. |