An Introduction to Microeconomics
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Lecture – 07
Introduction to Demand and Supply

Welcome again to NPTEL lectures on microeconomics. Today we are going to discuss demand, supply and market equilibrium.

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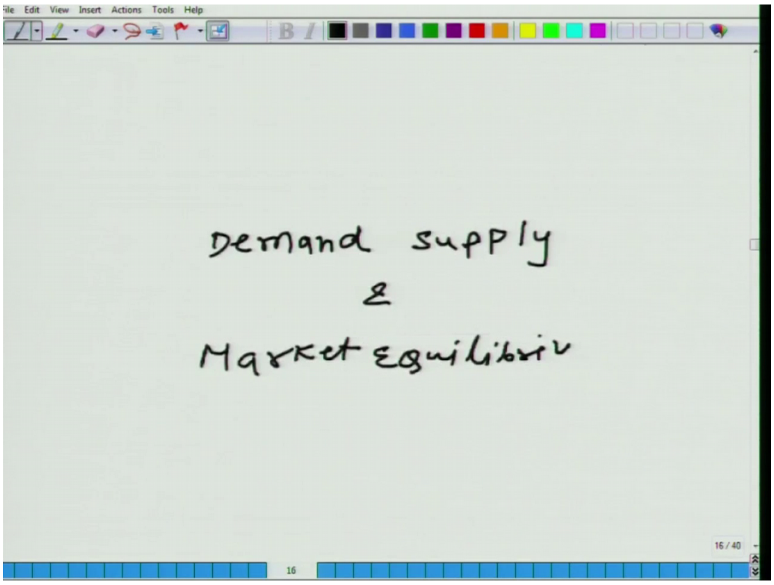

I will begin with a simple story. A very simple story, a short story. And then I will talk about some facts. And we will discuss why do we observe such kind of things in our society in our economy. So, the title of the story is let there be cheapness. The story is from roman empire. Approximately around 302 A.D there was an emperor named diocletian. And what he observed that wherever his army massed, the price of food items all the consumables increased tremendously.

So, he was very worried. He was very disturbed. He thought that sellers are trying to make easy money. So, he was very unhappy. So, he said let there be cheapness. In fact, he issued an edict, which reads that unprincipled greed appears wherever our armies following the command of public wheel march.

Not only in villages and cities, but also upon all highways. With the result that prices of foodstuffs mount not only 4fold and 8fold, but transcend all measures. Our law shall fix a measure and limit to this greed. So, idea of the simple story is; that he tried he tried to fix the prices in the market through his edit. Just imagine can you think of what happened after he issued this edit, will we will come back to this question.

But I want you to ponder that what happened once he issued this edict. Another thing another let us focus some at some other facts. Have you ever seen long line waiting to get gas cylinder outside a shop?

Student: Yes sir, yeah.

Have you ever seen long line of cars waiting to get their tank filled?

Student: Yes sir.

That is fine, also think about think about just another scenario. Whenever let us say mangoes are in the season, what happens to the mango prices?

Student: Go down.

The prices.

Student: Go.

Go down. Of all the items are all the different kind of mangoes, but think about when there is a season for hotels; like, some are in similar, what happens to the prices of.

Student: They rise.

Room?

Student: (Refer Time: 03:08).

It rises, why? If mangoes are in the season, the price of a mango goes down. But when rooms are in the season a price of a room or here rent of that room goes up. What is happening? So, all these sort of things and also some other, let me also add one more that these days it is in the news; that the food grains are rotting. Why do you think it is happening? Why do you think government procures so much of food grain that it cannot save it that much it cannot safely keep, what is happening there?

So, to understand all these phenomena, we are going to concentrate on the basic workhorse of microeconomics. Demand, supply and market equilibrium. And this is the title of this chapter. Demand, supply and market equilibrium.

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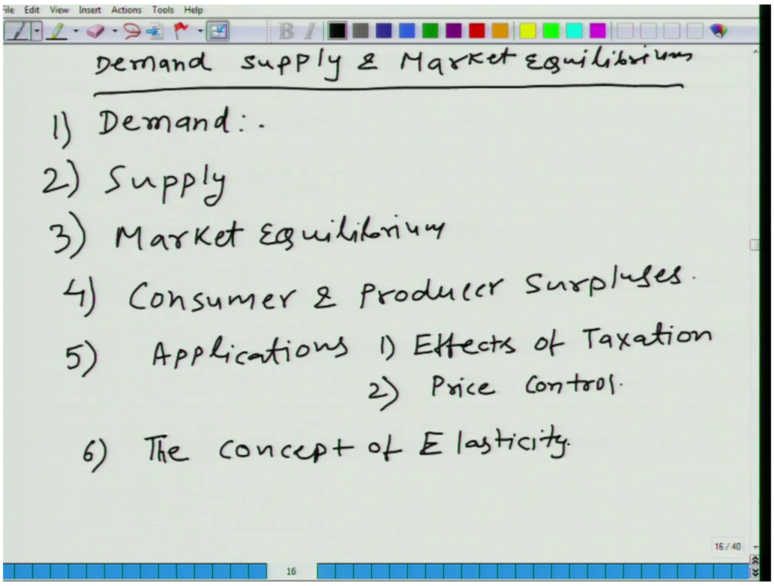

Let me write; in this chapter we are going to study 6 broad topics. The first topic is of course, demand what is demand? What do we mean by demand? That how many units of a good buyers are willing to purchase at a particular price.

So, we are going to learn about it the factors that influences the buying decision and so on. Similarly, we are going to learn about supply. How many units of a good.

Student: Produced in a.

A particular seller is willing to sell at a particular price. And when we take all such price and quantity combination we get supply curve. So, after learning about demand and supply, we are going to learn about market equilibrium. And what is market equilibrium?

Student: A.

A particular price where quantity demanded is equal to.

Student: Quantity.

Quantity supplied. So, we are going to study all these things in more details. The 4th topic that we are going to cover is consumer.

Student: (Refer Time: 05:49).

And producer surpluses. What is consumer surplus? When you buy an item. Let us say when you want to buy an apple. Let us say the price of a that apple at present is 5 rupees in the market. You can buy one unit of apple, one apple by paying 5 rupees. But that is not your maximum willingness to pay. It is possible that the price of this apple was 6 rupees, and you still have bought it. Or maybe 7 rupees you may still have bought it.

So, you have something called maximum willingness to buy. The money that you are willing to pay, maximum amount of money that you are willing to pay to get one unit of apple. That is your maximum willingness to buy. So, you are willing to pay something higher, but the price is if price is lower then only you will buy. So, there is a difference between the maximum willingness to pay, and the price of that apple.

So, when you buy this apple you are gaining the difference. For example, let us say your maximum willingness to pay is 10 rupees. And that apple is available for 5 rupees in the market. So, your value for that apple is 10 rupees. That is why your if your value was 11 rupees you would have even paid 10 rupees 50 paisa to get that apple.

So, maximum willingness to pay indicates your valuation of that good. So, when you buy that apple in 5 rupees, it means you are gaining 5 rupees out of this transaction.

Student: Yes sir.

And that is your surplus from this transaction. So, similarly we are going to study producer surplus also. And then we are going to talk about social surplus also. The fifth topic that we are going to talk about the applications of the concepts of demand and supply. And we will pick 2 particular applications, the first is going to be effect of taxation. Effects of taxation, and second application we are going to study about price control.

I already gave you an example of price control through the story of diocletian. Let there be cheapness. It is the diocletian was trying to control the price. So, we will see the repercussion of an attempt of controlling the price through mechanism other than generated by the market. Fine, and last, we will introduce the concept of elasticity. Because we are not only interested in how much money we pay to buy one unit of apple. We are also interested in how our demand of apple changes with a change in price of that apple. So, we will learn all those things in this particular section.