Exercise walk-through

Price determination ▪ 2.4

eXercise

You must be able to

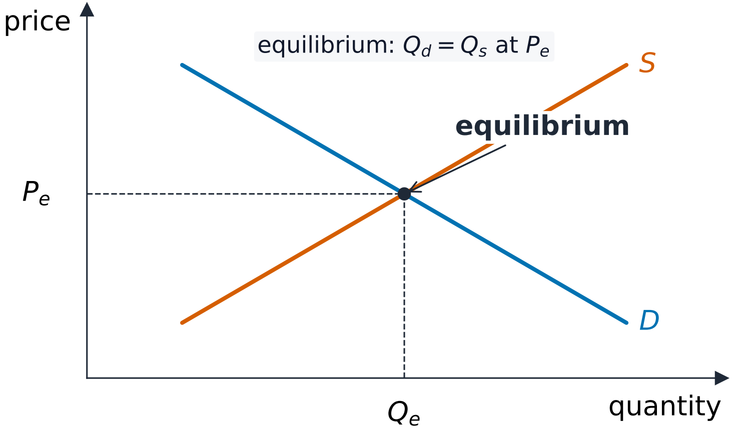
- draw demand and supply and find the equilibrium
- explain why equilibrium is where quantity demanded equals quantity supplied
- read changes in equilibrium from a diagram

Method — Market equilibrium

- **Equilibrium 均衡**: the price where the amount buyers want to buy exactly equals the amount firms want to sell.
- At equilibrium there is no shortage and no surplus — no pressure for the price to change.
- The crossing point of the two curves gives the equilibrium price **and** quantity.

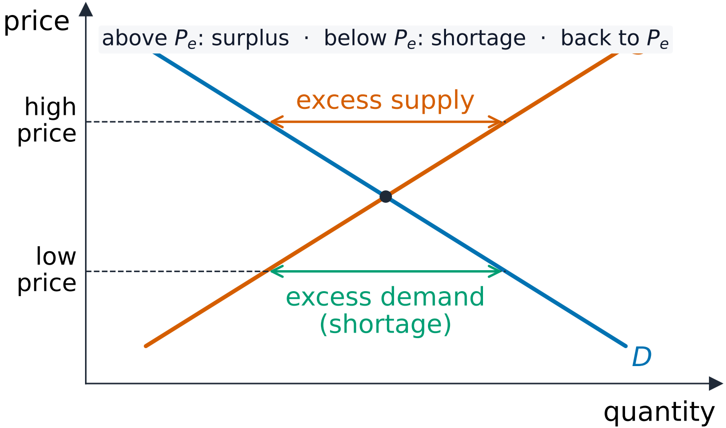
Answer shapes: an **Analyse [up to 6]** answer should use a labelled diagram; **Discuss [8]** adds a judgement (Ev).

Method — Market equilibrium



The price settles where demand and supply cross

Method — Market equilibrium



Above equilibrium there is excess supply; below it there is excess demand

Practice 2.1 ▪ 2 marks

Define the term *equilibrium price*.

Solution 2.1

Method: Market equilibrium

Worked steps

the price at which the quantity demanded equals the quantity supplied, so there is no pressure for it to change (2 for a clear definition; 1 for a partial idea).

Practice 2.2 ▪ 1 mark

State what is true about quantity demanded and quantity supplied at equilibrium.

Solution 2.2

Method: Market equilibrium

Worked steps

they are equal (1).

Practice 2.3 ▪ 1 mark

State what determines the price of a good in a free market.

Solution 2.3

Method: Market equilibrium

Worked steps

the interaction of demand and supply (where they cross) (1).

Exam-style 3.1 ▪ 1 mark

At the equilibrium price:

A there is excess demand

B there is excess supply

C quantity demanded equals quantity supplied

D the price is rising

Solution 3.1

Method: Market equilibrium

A there is excess demand

B there is excess supply

C quantity demanded equals quantity supplied ✓

D the price is rising

Worked steps

C. At equilibrium, quantity demanded equals quantity supplied.

Exam-style 3.2 ▪ 4 marks

Using a demand and supply diagram, show and explain the equilibrium price and quantity.

Solution 3.2

Method: Market equilibrium

Worked steps

[4] K 1 + **diagram up to 2** (labelled demand and supply curves crossing) + An 1 — the two curves cross at one point → this gives the equilibrium price P_e and quantity Q_e → here the amount buyers want exactly equals the amount firms supply.

Exam-style 3.3 ▪ 6 marks

Analyse how the equilibrium price and quantity change when demand for a good increases.

Solution 3.3

Method: Market equilibrium

Worked steps

[6] K/App/An (diagram: demand shifts right) — an increase in demand shifts the demand curve right → at the old price there is excess demand (a shortage) → buyers compete and bid the price up → as price rises, quantity supplied rises along the supply curve → a new equilibrium at a higher price and higher quantity.