Market equilibrium essay sample

Finance, Market

How organizations maintain a balance between supply and demand determines market equilibrium. Market equilibrium is when the quantity demanded equals quantity supplied (McConnell, Brue, Flynn, 2009). Prior to understanding market equilibrium an exploration of supply and demand needs to occur. In addition, surplus and shortage along with market efficiency each have an effect on market equilibrium. Demand

The law of demand refers to the relationship between price and demand. " Other things equal, as price falls, the quantity demanded rises, and as price rises, the quantity demanded falls" (McConnell, Brue, Flynn, 2009, p 47). Price is not the only factor to affect demand. The other factors are referred to as determinants. The five basic determinants of demand are consumers' tastes (preferences), the number of buyers in the market, consumers' incomes, the prices of related goods, and consumer expectations (McConnell, Brue, Flynn, 2009). When there is an increase in demand the demand curve moves to the right and when there is a decrease the demand moves left (McConnell, Brue, Flynn, 2009). Supply

The law of supply refers to the relationship between price and quality supplied. The law of supply indicates that as price rises, the quantity supplied rises; as price falls, the quantity supplied falls (McConnell, Brue, Flynn, 2009). Supply can also be affected by other factors. The six basic determinants of supply are resource prices, technology, taxes and subsidies, prices of other goods, producer expectations, and the number of sellers in the market (McConnell, Brue, Flynn, 2009). When there is a change in one or more of these supply determinants it will cause the supply curve for that product to shift either left or right. When the supply curve shifts to the right

it signifies an increase in supply and when a shift to the left occurs it indicates a decrease in supply (McConnell, Brue, Flynn, 2009). Shortages and Surpluses

Surpluses drive prices down while a shortage will drive the price up because consumers are in need of the product and willing to pay more. Both a surplus and shortage will change the equilibrium price as the consumers’ willingness to pay changes. Understanding both the shortage and surplus is important when trying to establish an equilibrium price. The equilibrium price is when there is no burdensome surplus for sellers and no inconvenient shortage for potential buyers (McConnell, Brue, Flynn, 2009). Market Efficiency

Market efficiency is when the market is able to quickly adapt to the most recent information available. The central idea of the efficient market theory is that any information is available to market participants, so prices always incorporate and reflect all relevant information (Birău, R., 2011). In an efficient market price would become more random and less predictable because of the amount of information available and the speed at which that information can get to the consumer or investor. Equilibrium and Shifts

The graphs below will reflect changes in supply or demand and the effect that change has on the equilibrium price and equilibrium quantity.
This graph represents a decrease in supply with a increases equilibrium price and decreases equilibrium quantity. An increase in supply would have caused a decrease in equilibrium price and increases equilibrium quantity.

This graph represents an increase in demand with an increases equilibrium price and decreases equilibrium quantity. A decrease in demand would decrease both equilibrium price and equilibrium quantity. Conclusion

Market equilibrium is about more than just supply and demand. Supply and demand are affected by additional factors referred to as determinates as well as supply surpluses and shortages. In addition, market efficiency can cause market equilibrium to change often and randomly because of the amount of available information. Changes in either supply or demand can change the equilibrium price as seen in the graphs. So therefore it is important to understand all the factors that affect market equilibrium.