LAW OF SUPPLY

- P.Bharathi

SUPPLY

- *Quantity supplied* is the amount of a good that sellers are willing and able to sell at each possible price
- *Supply* is a full description of how the quantity supplied of a commodity responds to changes in its price

LAW OF SUPPLY

A direct relationship that exists between price and quantity supplied

- As Price Rises…

  …Quantity Supplied Rises

- As Price Falls…

  …Quantity Supplied Falls

SUPPLY SCHEDULE

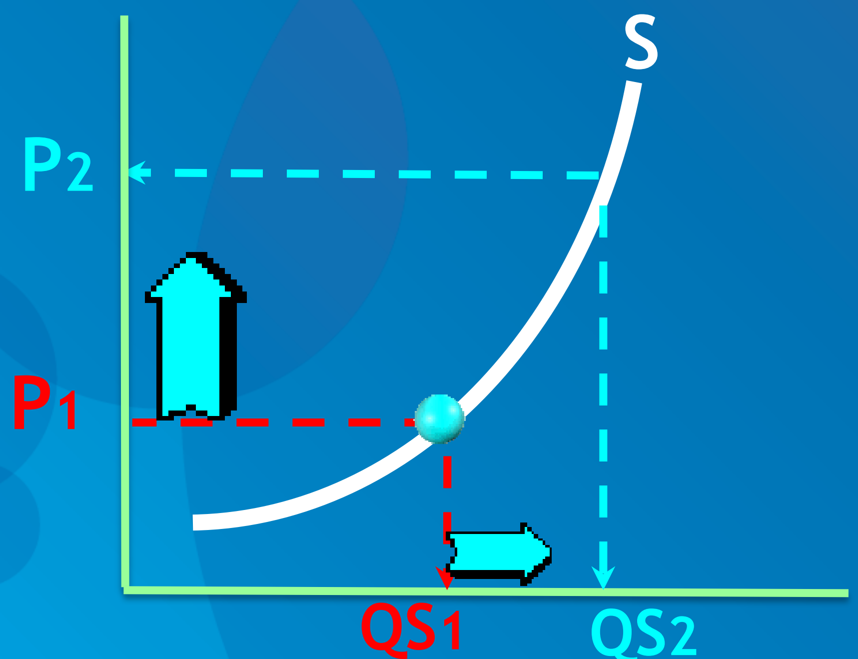
Supply schedule is a table showing the amounts of a product that producers are willing and able to make available for sale at each of a series of possible prices.

Supply Schedule

P	Q_S
Rs 1	5
2	20
3	35
4	50
5	60

LAW OF SUPPLY

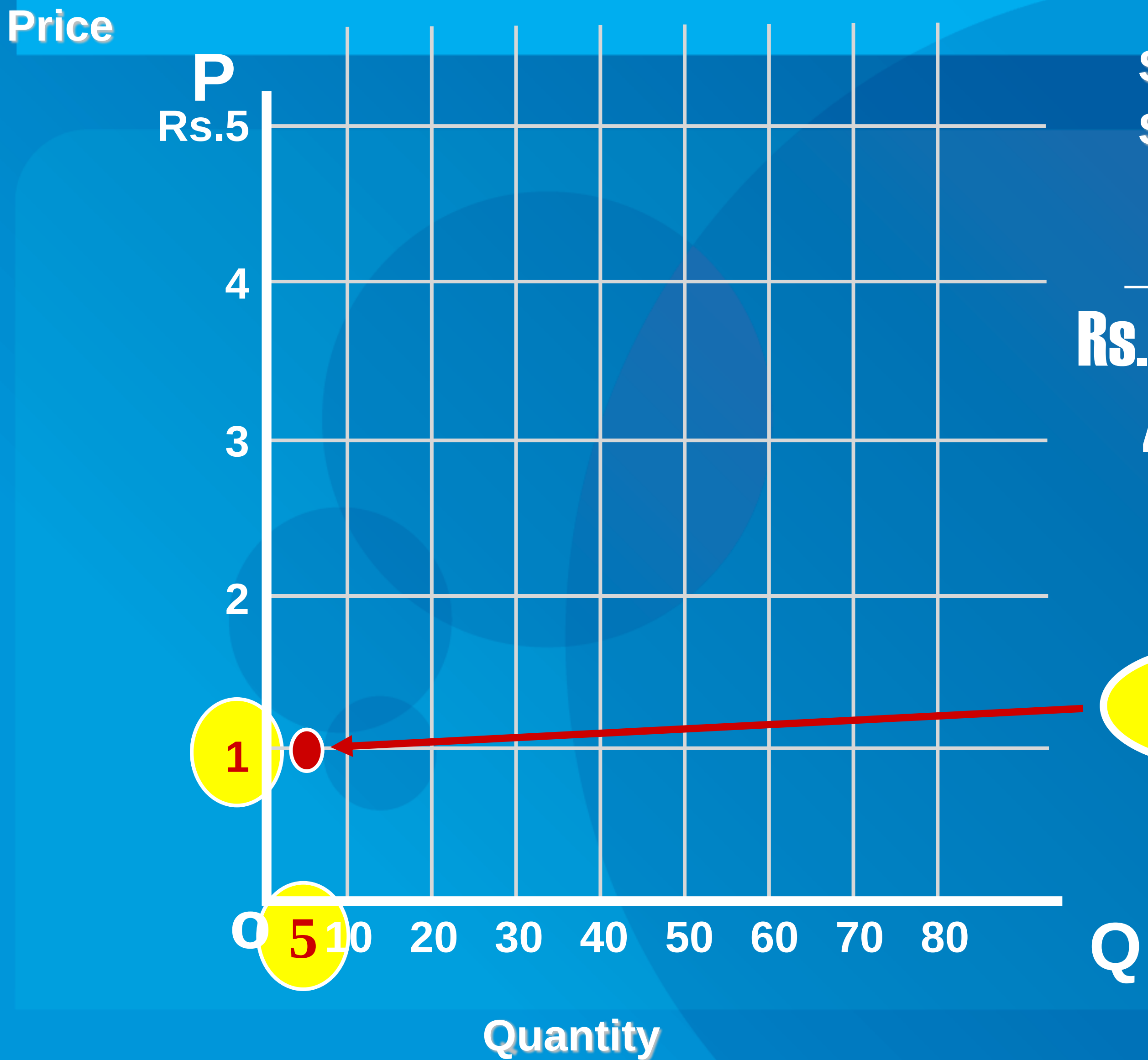
There is direct relation between Price and Supply.
When Price increases Quantity supplied increases;
When Price decreases Quantity supplied decreases



<u>Reasons For Upward sloping "Supply" Curve</u>

1. Current producers produce more
2. New producers are attracted to the market.

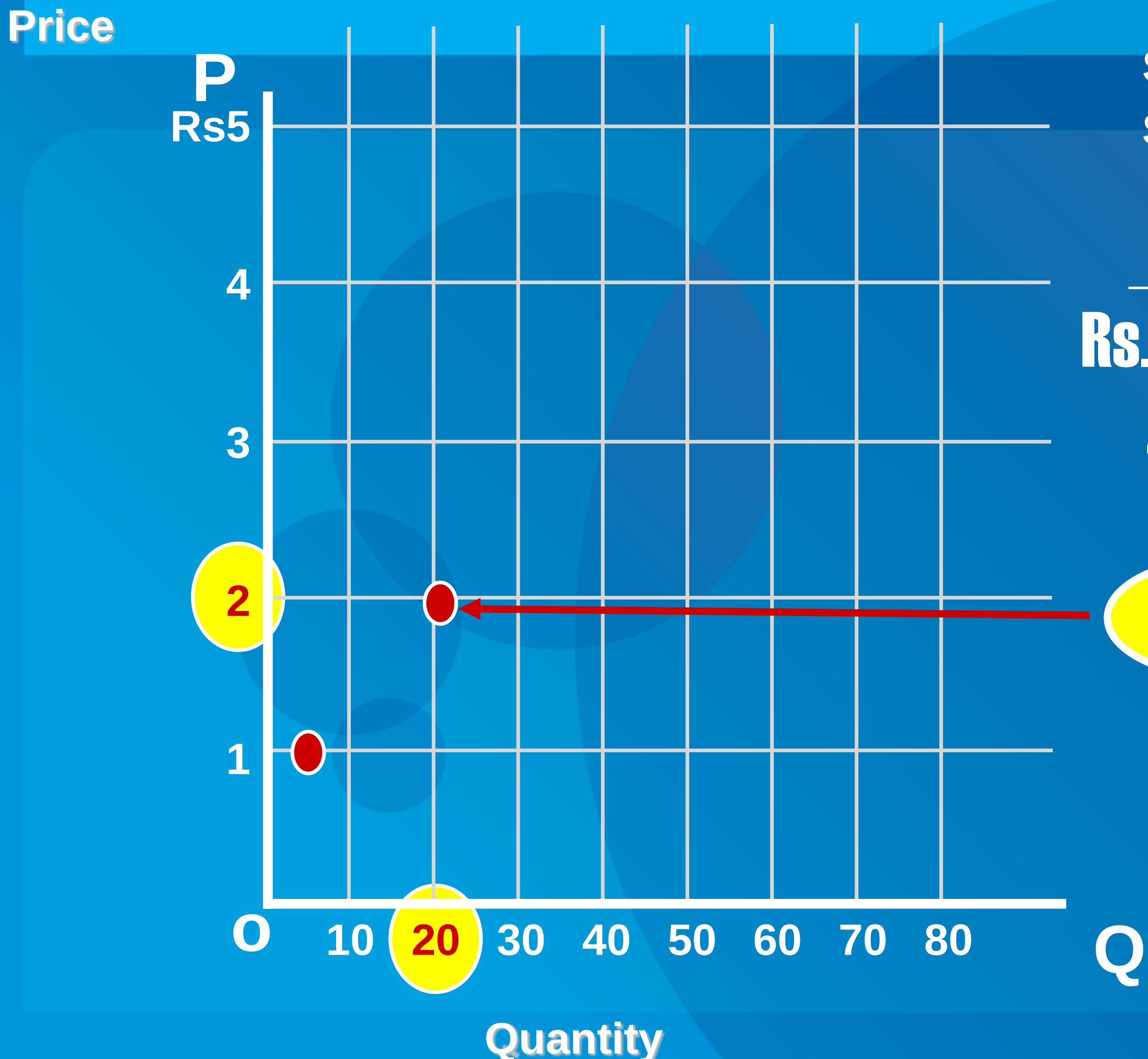
SUPPLY CURVE



Supply Schedule

P	Q_s
Rs.5	60
4	50
3	35
2	20
1	5

SUPPLY CURVE



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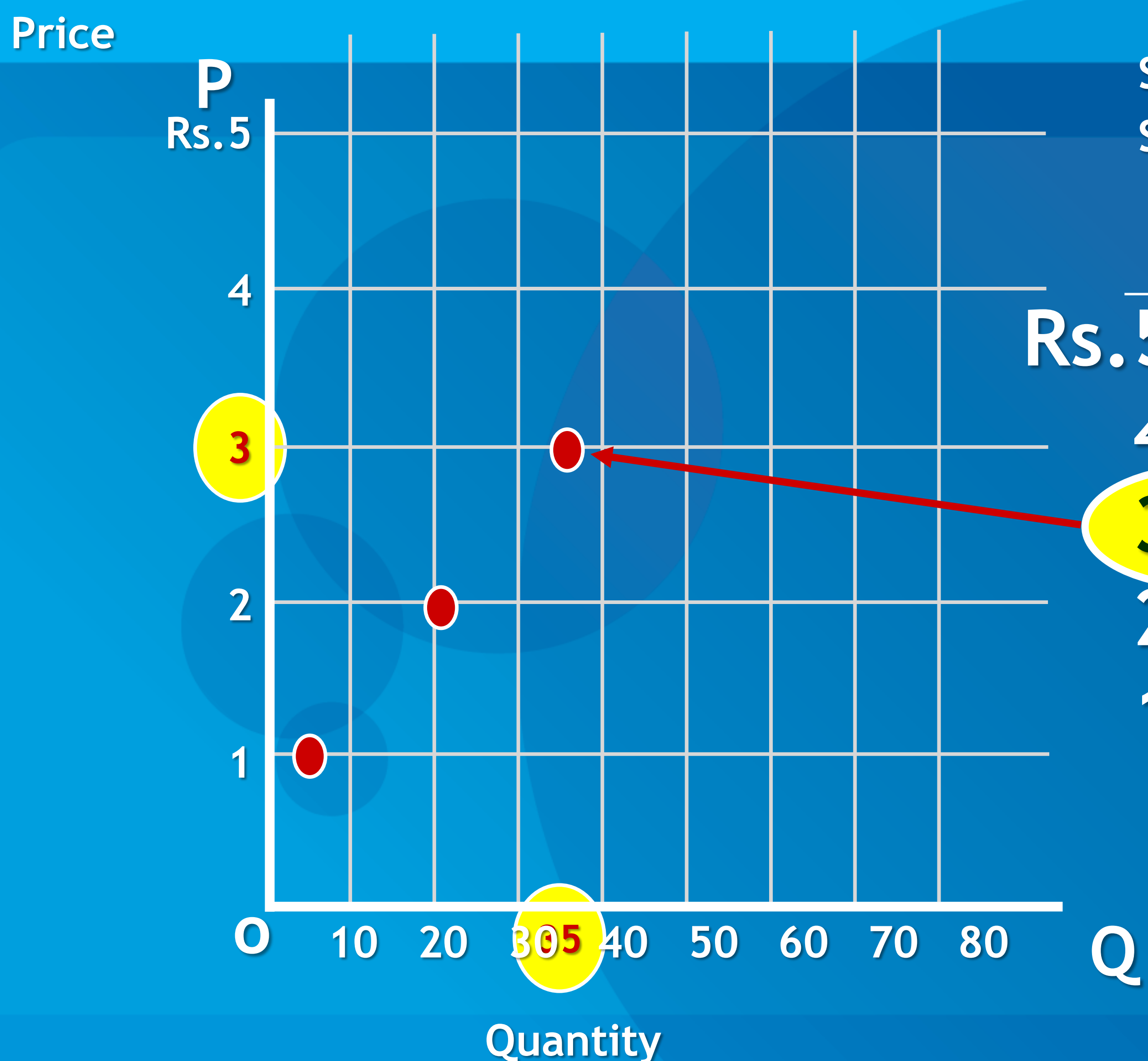

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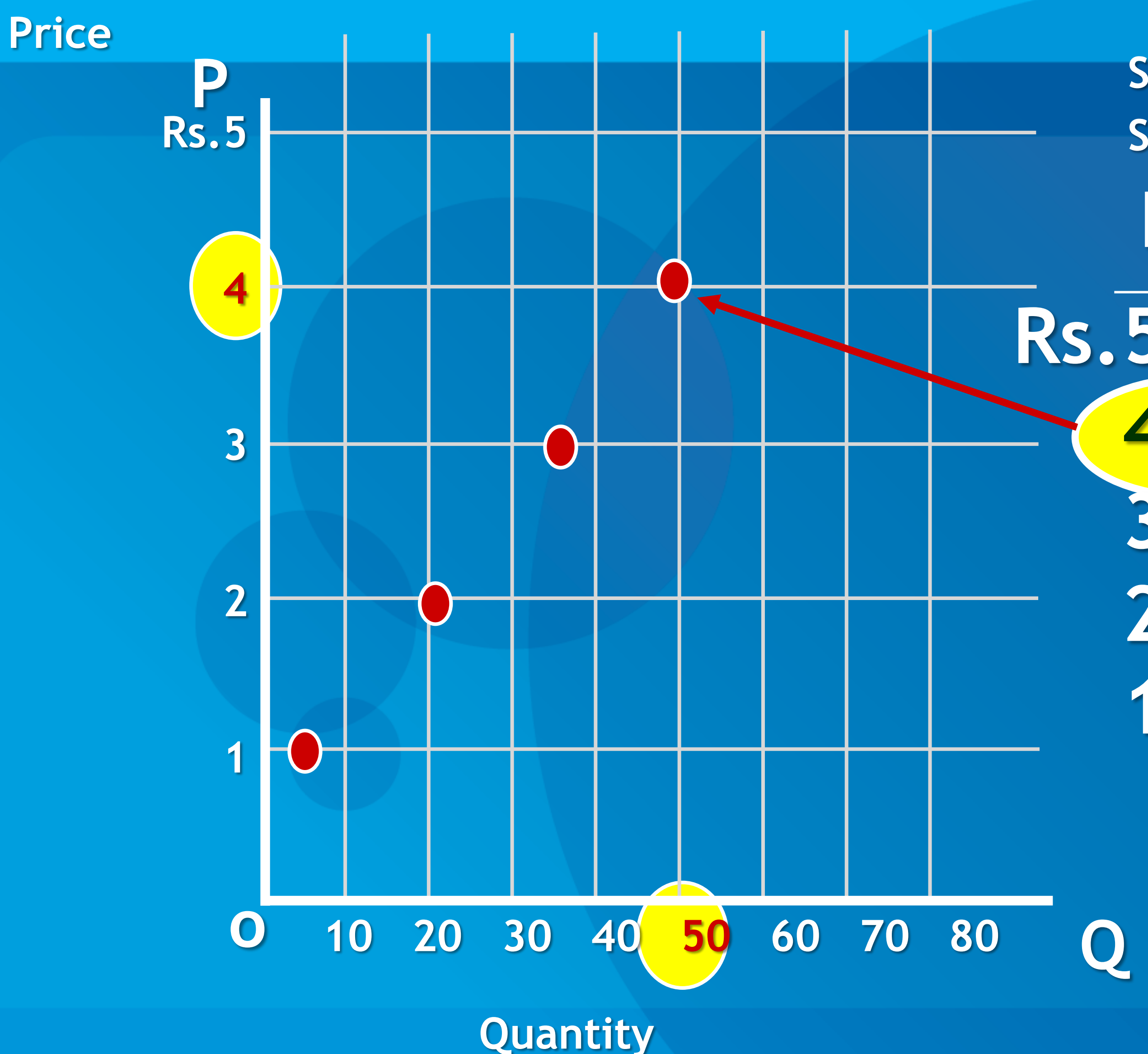

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Rs.5	60
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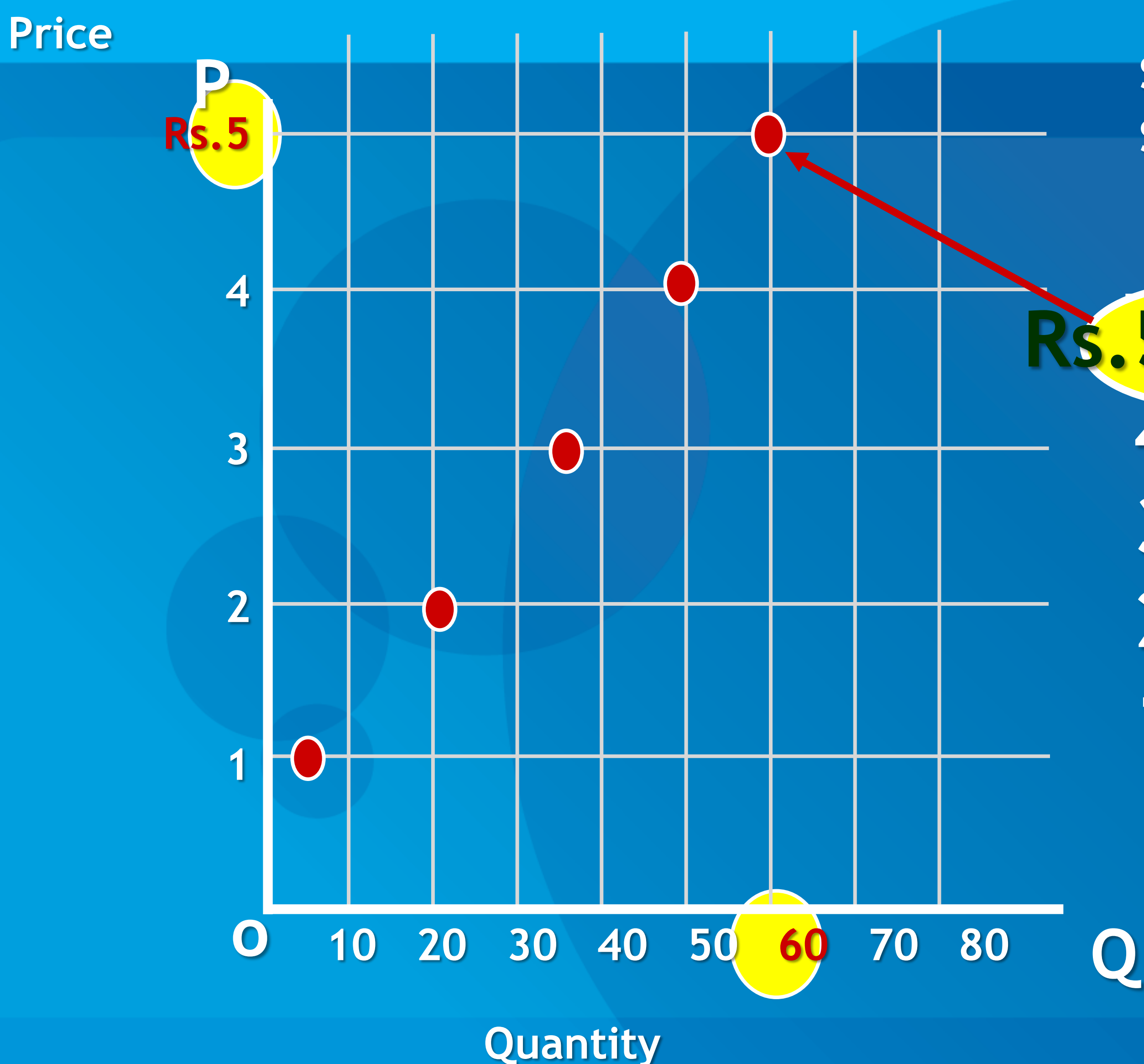

Supply Schedule

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SUPPLY CURVE

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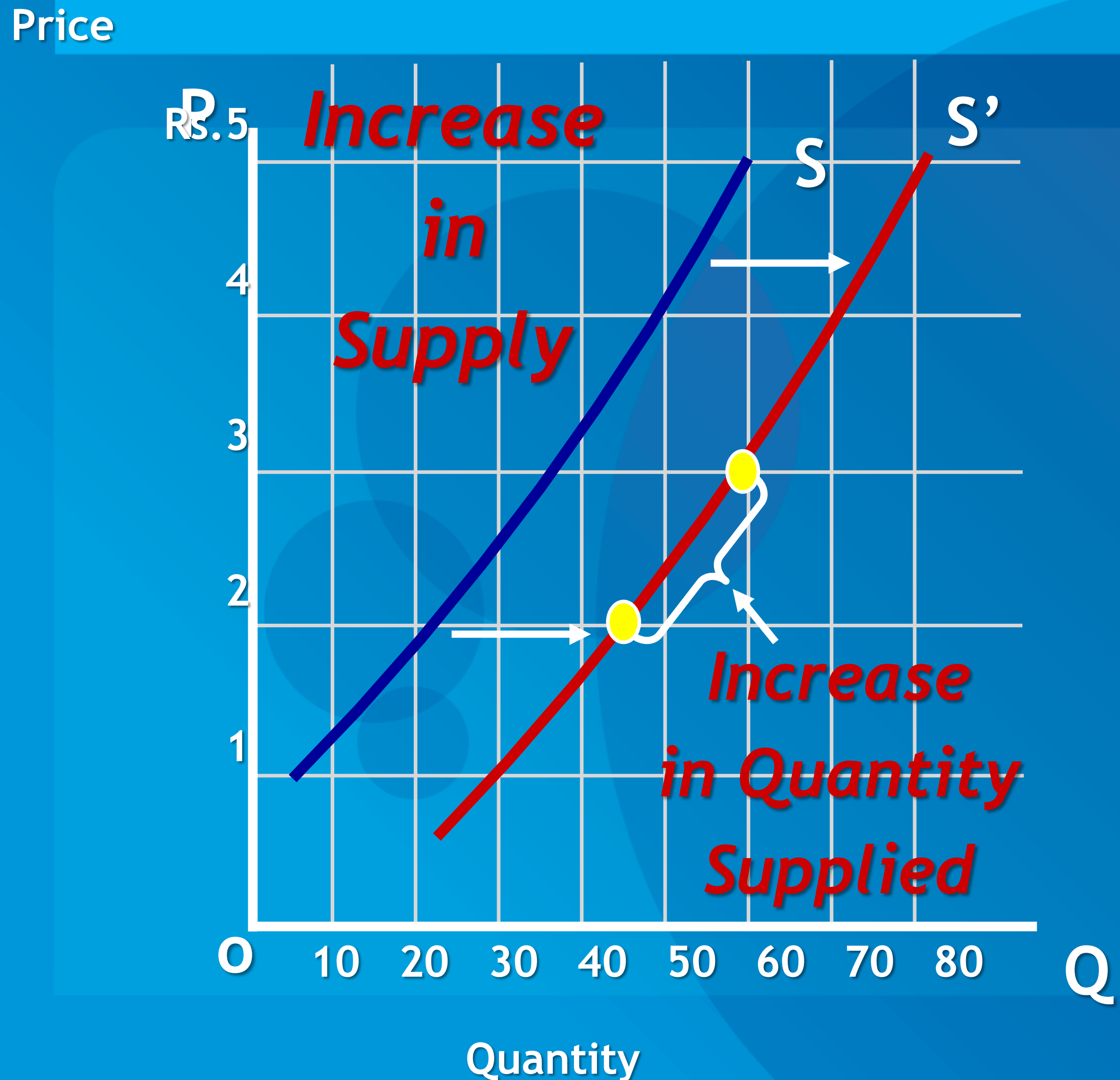
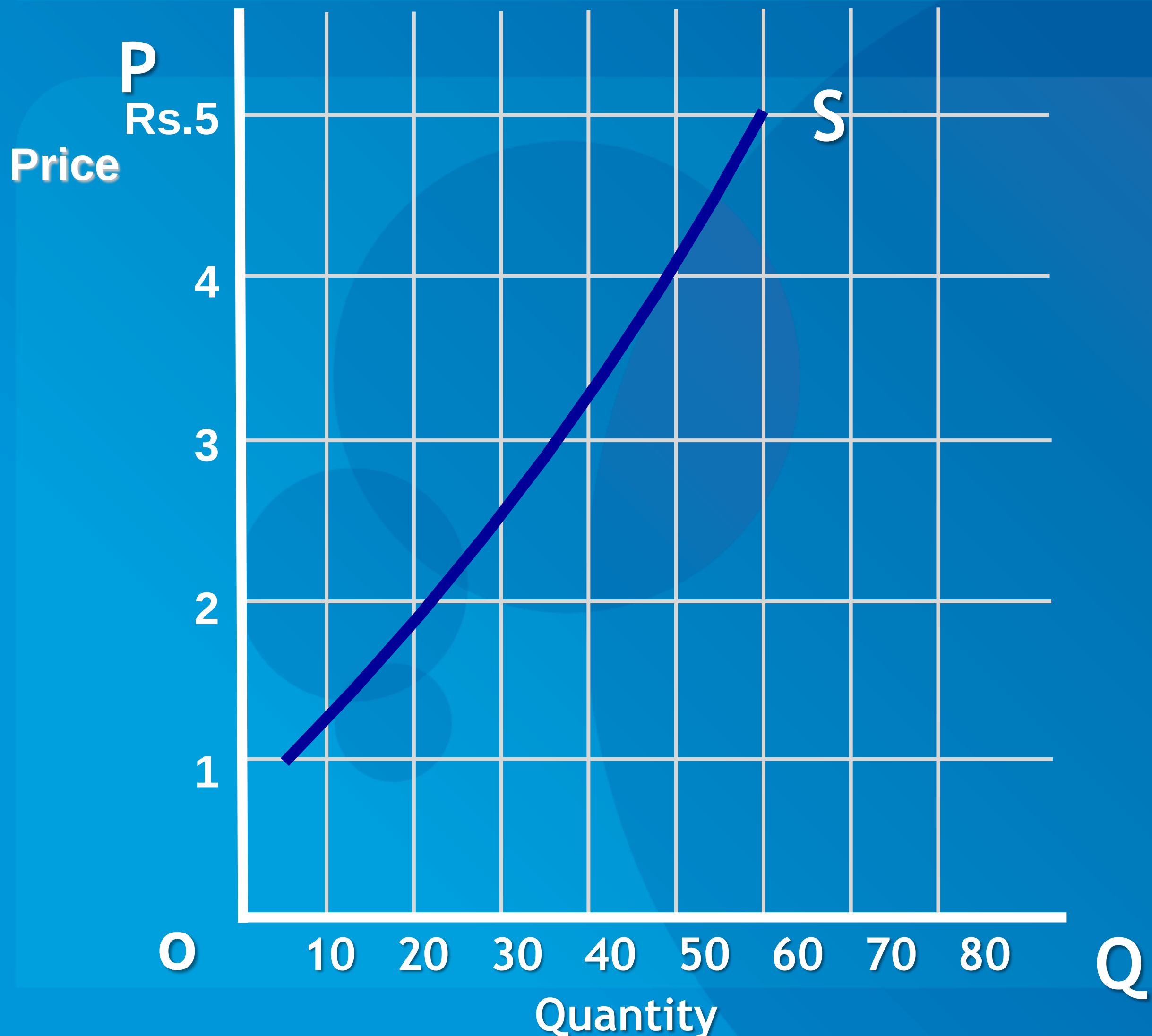


Supply Schedule

P	Q_S	
Rs.5	~~60~~	80
4	~~50~~	70
3	~~35~~	60
2	~~20~~	45
1	~~5~~	30

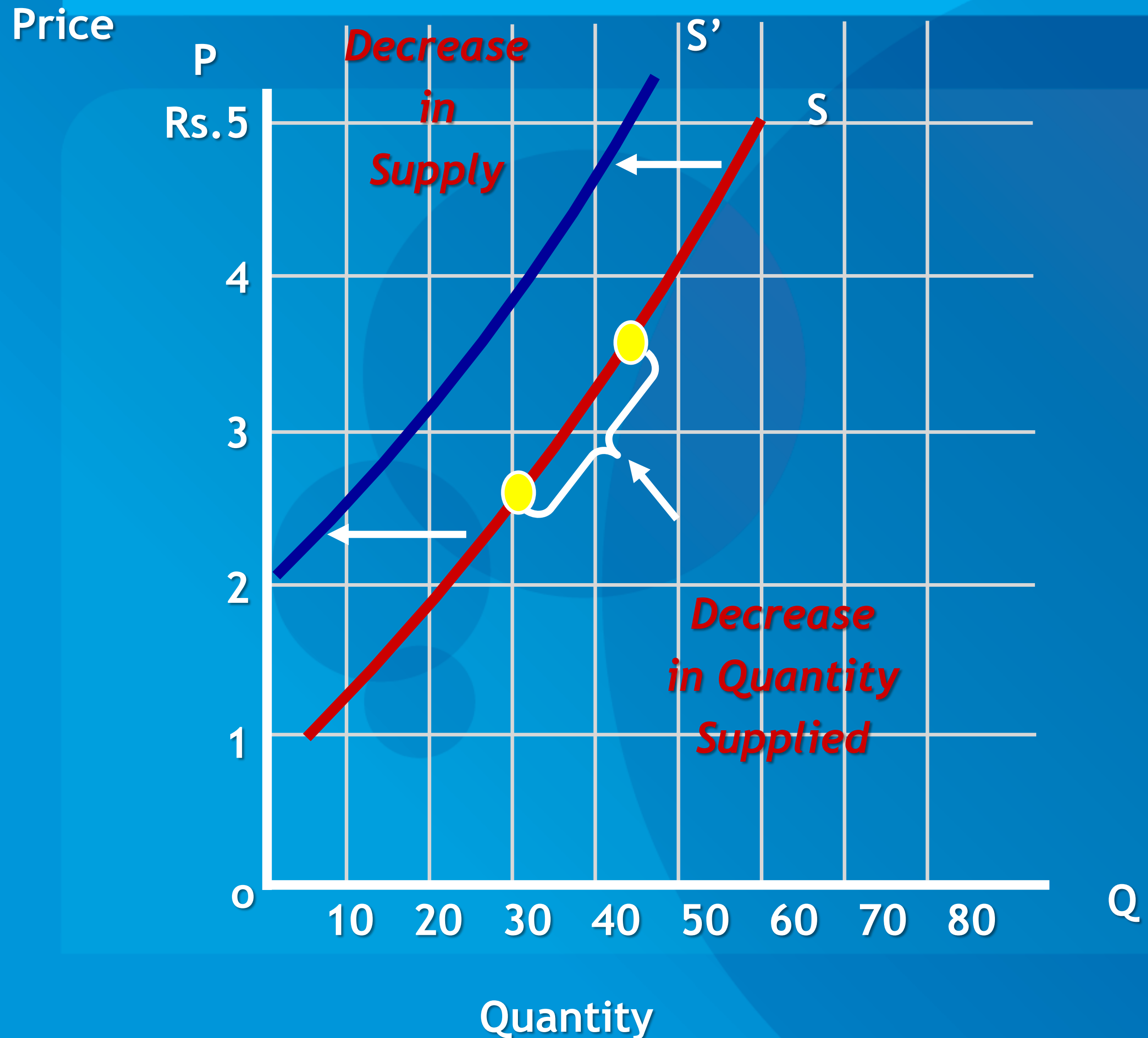
SUPPLY CURVE



Supply Schedule

P	Q_S
Rs.5	60
4	50
3	35
2	20
1	5

SUPPLY CURVE



Supply
Schedule

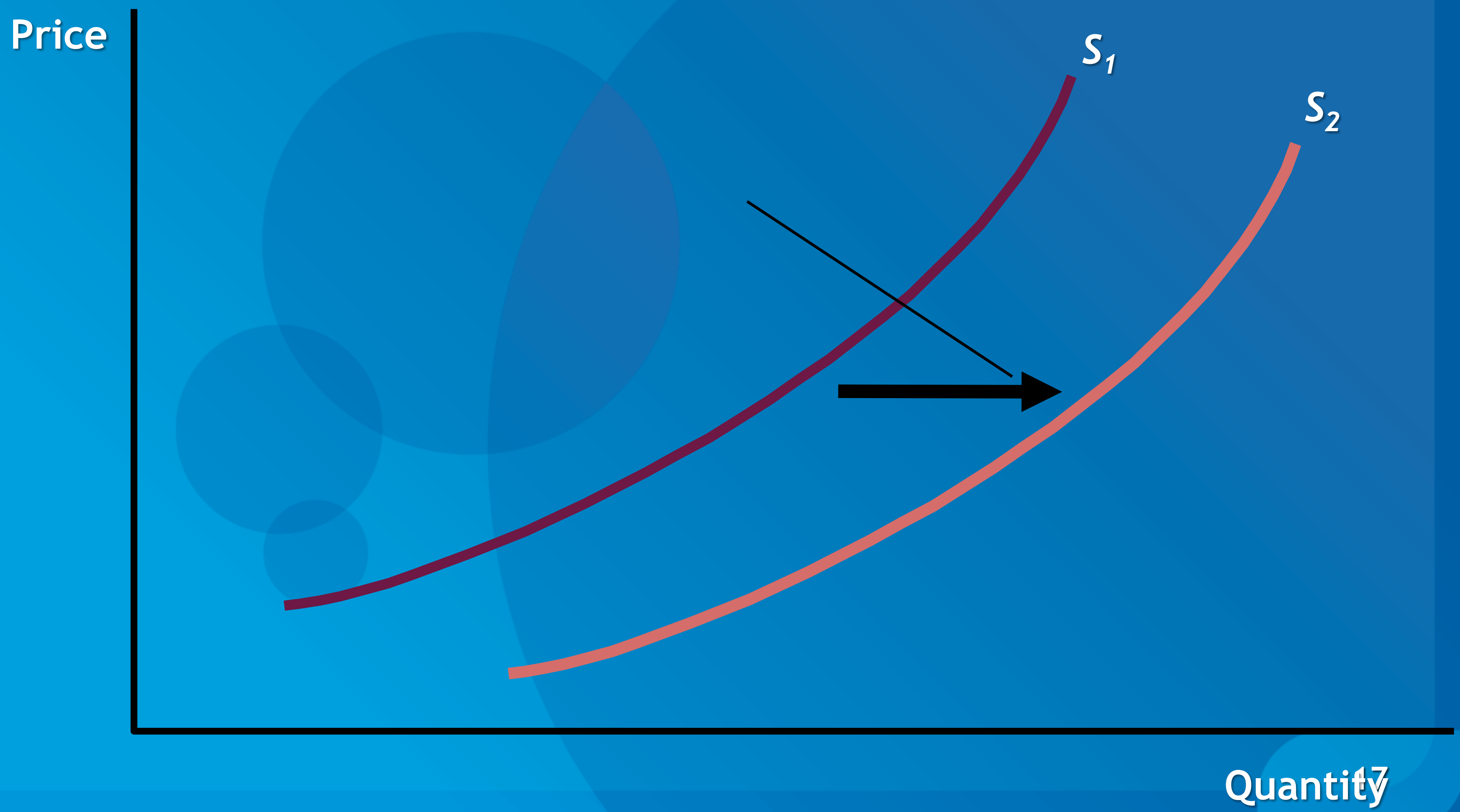
P	Q_S	
Rs.5	~~60~~	45
4	~~50~~	30
3	~~35~~	20
2	~~20~~	0
1	~~5~~	--

Changes in Quantity Supplied

Entire supply curve shifts rightward when:

- price of input ↓
- price of complement good ↓
- number of firms ↑
- expected price ↑
- technology advances
- favorable weather

Changes in Quantity Supplied

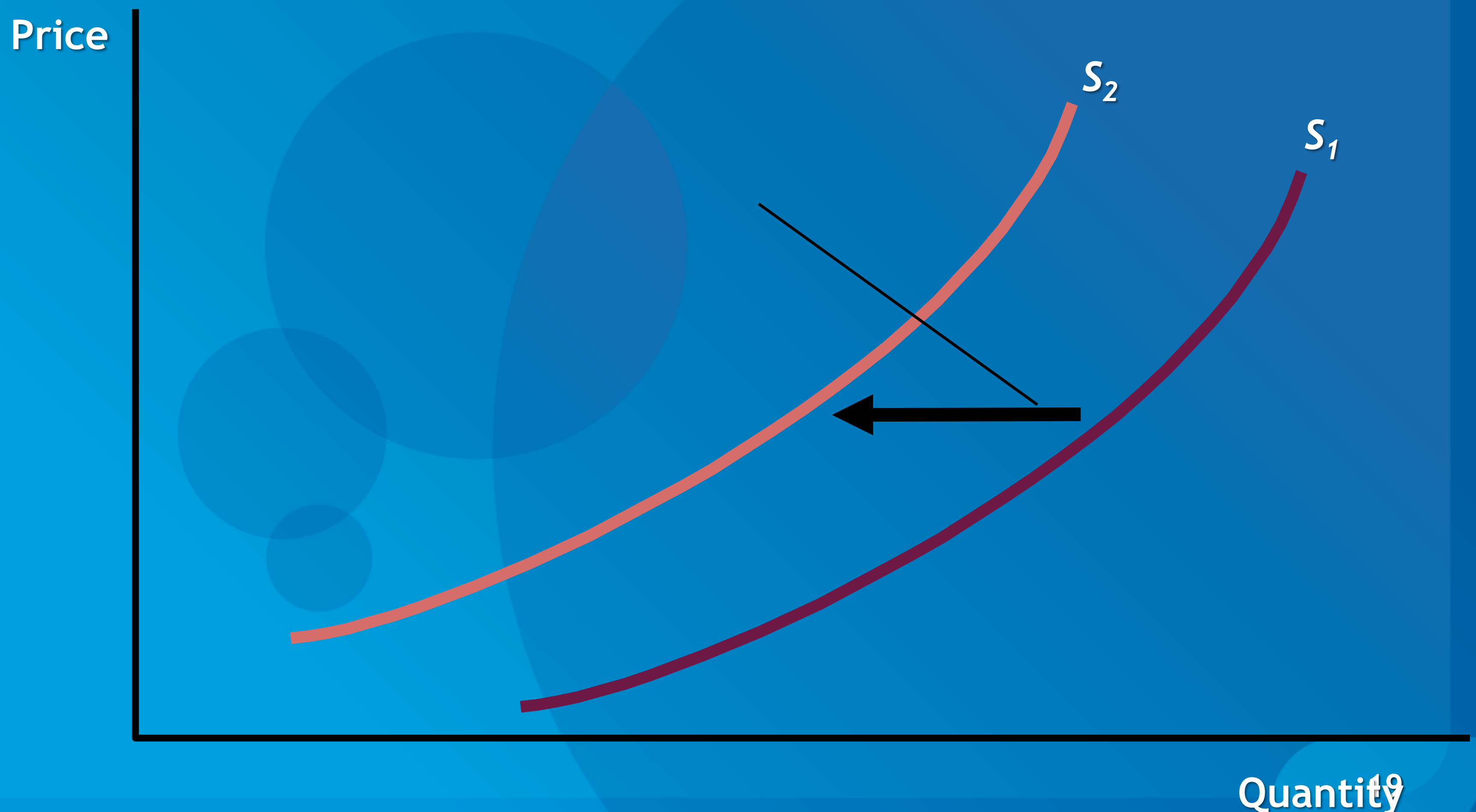


Changes in Quantity Supplied

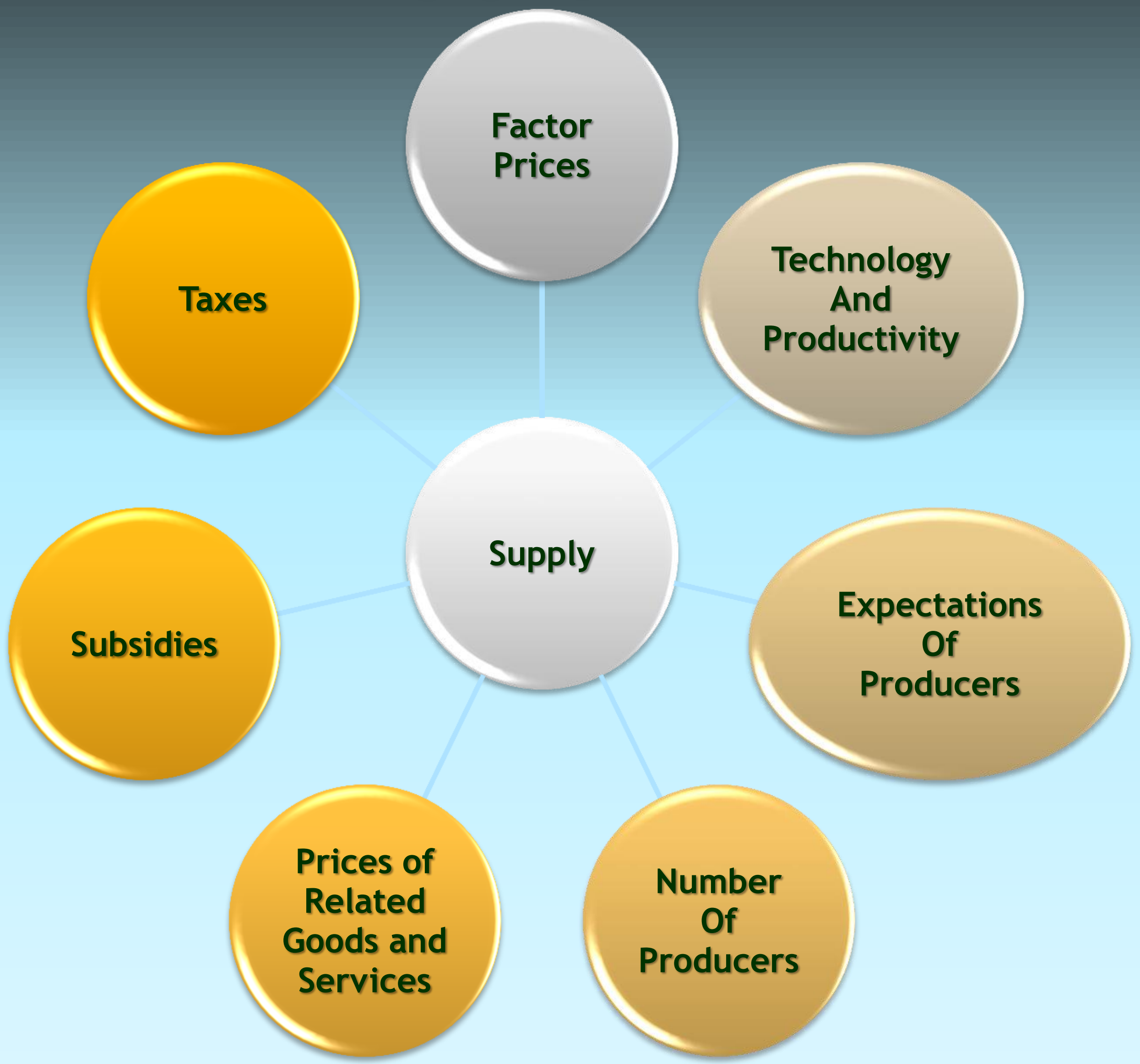
Entire supply curve shifts leftward when:

- price of input ↑
- price of complement good ↑
- number of firms ↓
- expected price ↓
- unfavorable weather

Changes in Quantity Supplied



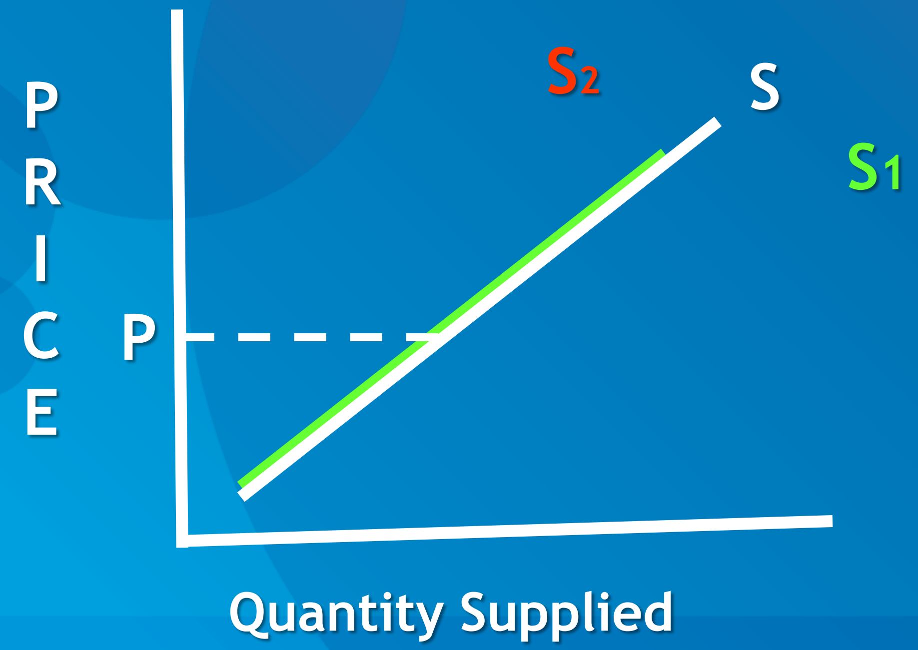
The Supply Shifters



1. Cost of Factors of Production

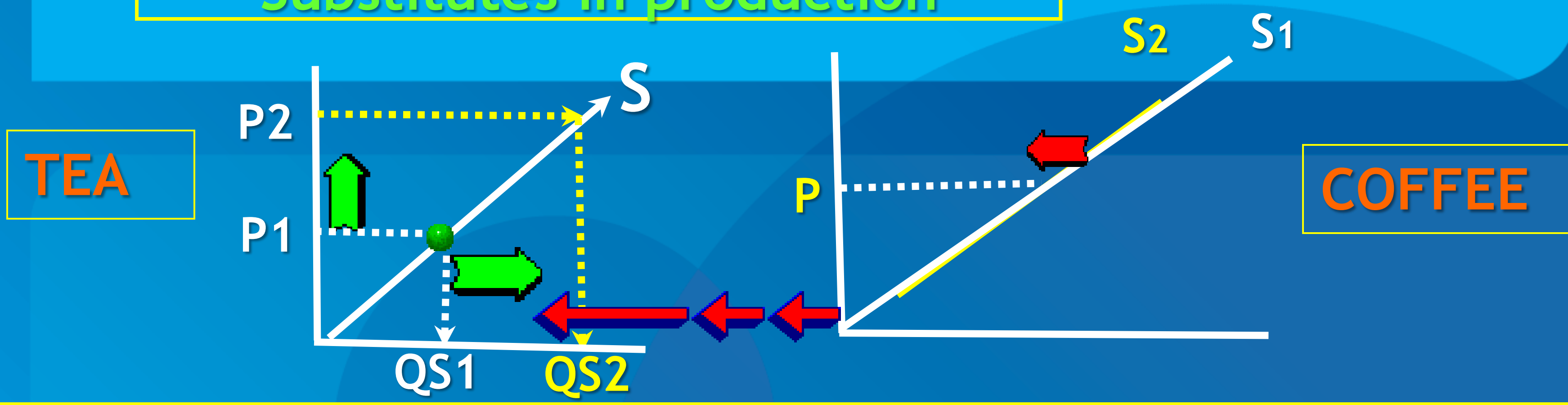
If cost of Factors **Decreases, supply Increases**

If cost of Factors **increases supply Decreases**

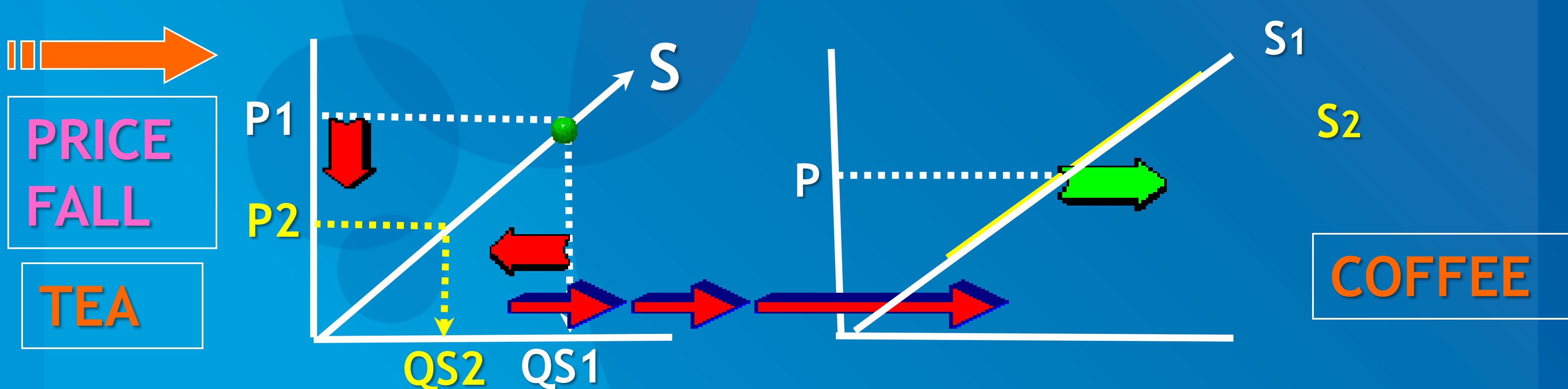


2. Prices of alternative goods

"Substitutes in production"



Producers want to produce more of the good where price is increasing



or at least, where the price is not going down.

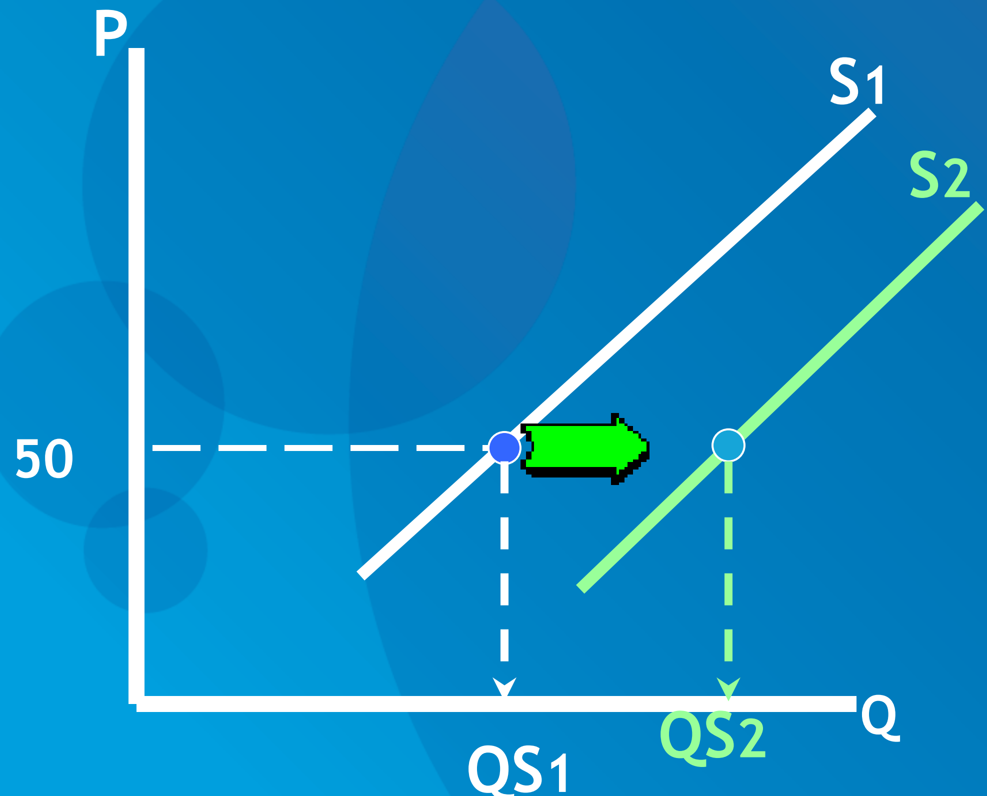
3. Technological Improvement

Technical improvement helps to produce more

Supply curve
moves
to the right.

4. Number of Suppliers

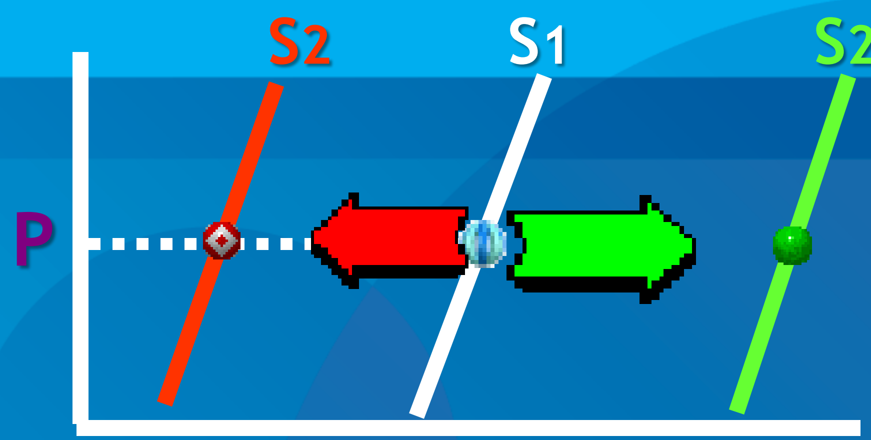
Increase in the number of suppliers would increase the supply



Supply

5. Producer's Expectations about Future Price

If Prices
are expected
to decrease



If Prices
are expected
to increase

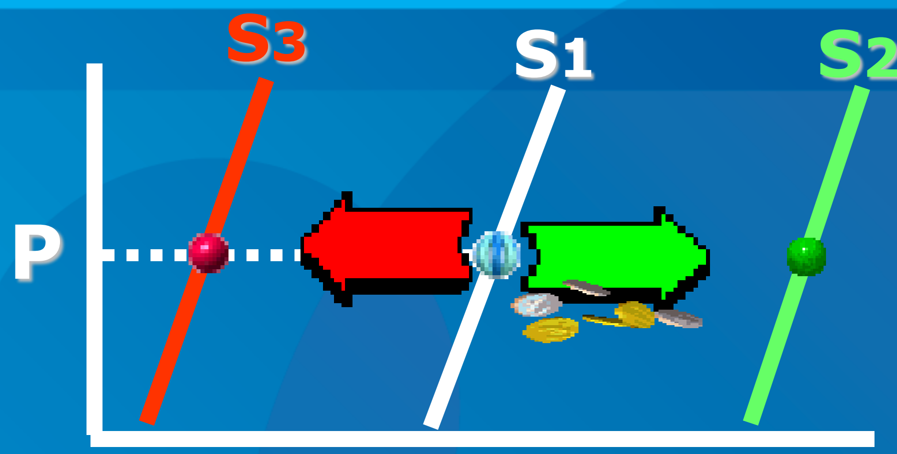
If producers expect future prices to decline, they will (increase / decrease) current production.

____

If producers expect future prices to increase, they will (increase / decrease) current production.

____

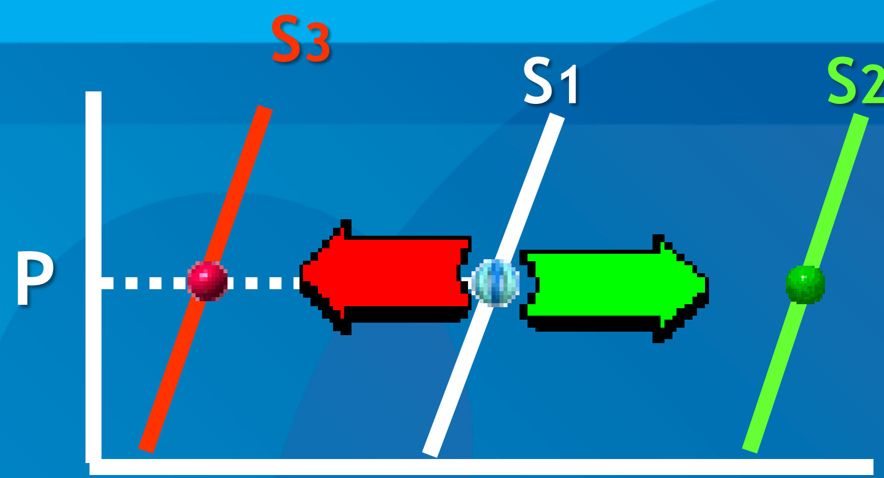
6. Subsidies - free money from Government



Free money from the Government (subsidies) induces suppliers to supply more.

When subsidies are taken away, then suppliers lose money and will decrease supply.

7. Taxes



When taxes are decreased, the supply curve moves to the right.

When taxes are raised,
the supply curve moves to the left.

DETERMINANTS OF SUPPLY

- Prices of Factors of Production
- Availability / Cost of Technology
- Taxes & Subsidies
- Prices of Other Goods
- Expectations about Price
- Number of Sellers in the market

ELASTICITY OF SUPPLY

- Elasticity of supply measures the relationship between change in quantity supplied and a change in price.

- Formula:

$$E_S = \frac{\text{Percentage Change in Quantity Supplied}}{\text{Percentage Change in Price}}$$

ELASTICITY OF SUPPLY

(1) When supply is elastic, producers can increase production without a rise in cost or a time delay

(2) When supply is inelastic, firms find it hard to change their production levels in a given time period.

The determinants of Elasticity of Supply

- Ability of sellers to alter output : The responsiveness depends on how easy it is to alter output when price changes

  - If the cost of supplying additional units rises sharply as output expands, then a higher price will result in a little increase in quantity supplied
  - If the marginal cost rises slowly as output expands, the chance of a higher price will lead to a large increase in output

The determinants of Elasticity of Supply

- Time period

  - Supply is more elastic in the long run.

- Supply becomes more elastic over time as producers adjust to price changes

- The longer the time period, the more able producers are to adjust to changes in relative prices

The determinants of Elasticity of Supply

- Factor substitution possibilities
  - Factor substitutability with a change in demand
  - Factor substitution at low cost
  - When factors are highly specialized, substitution may be harder and thus supply will be inelastic

- Availability of excess production capacity
  - When there is spare capacity, businesses can expand output easily to meet rising demand without upward pressure on costs

The determinants of Elasticity of Supply

- Stocks (inventories) available to meet the demand
  - A low level of stocks makes supply inelastic in the short term
  - When stocks can be released into the market, supply is elastic
- The time frame allowed
  - Brief period (fixed supply)
  - Short run (inelastic supply)
  - Long run (elastic supply)
- Supply limitations
  - E.g. The Regulation on the supply may limit the volume


THANK YOU