

**BEC1116**

**Principles of Economics**

Demand and Supply Changes  
and Market Intervention

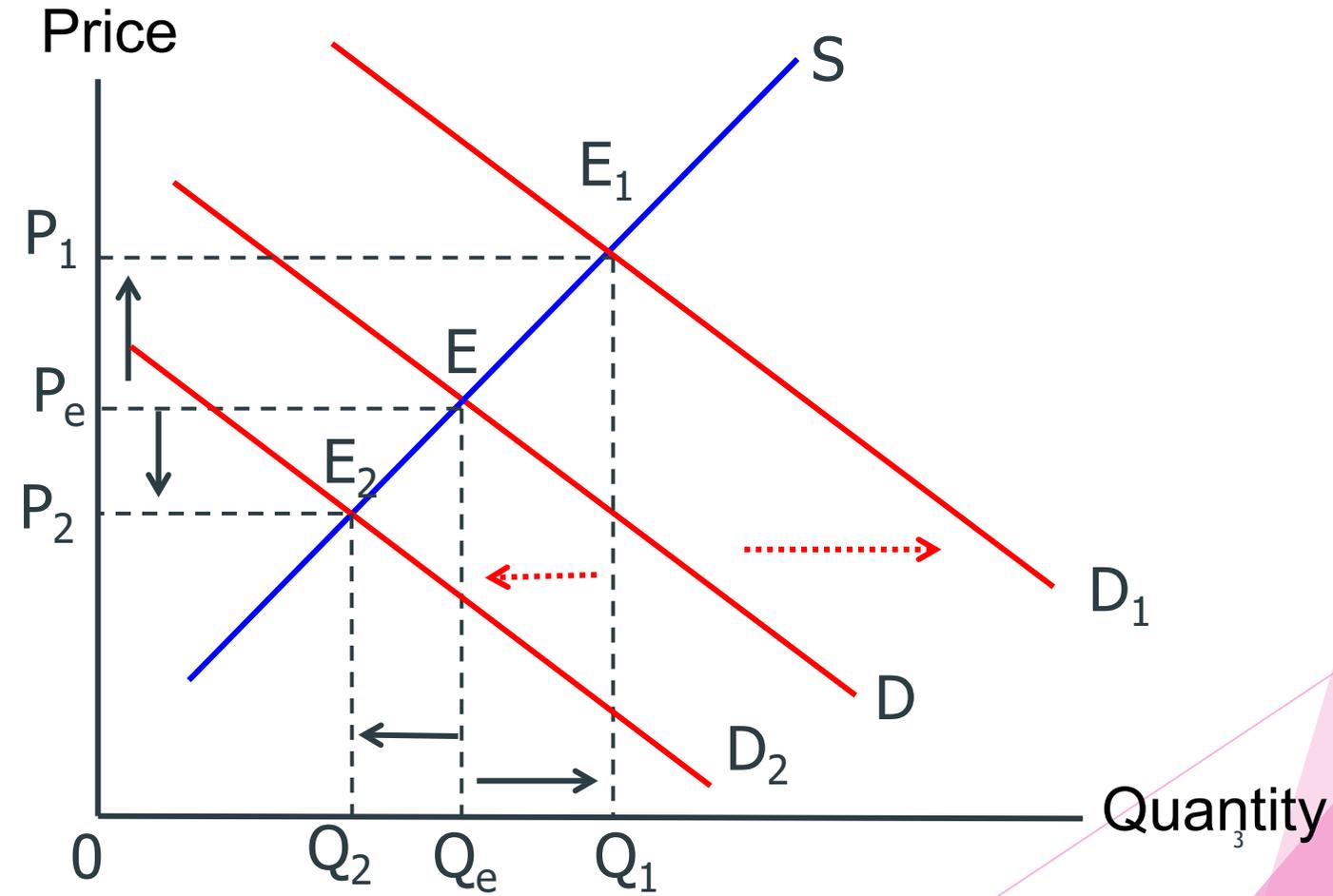
# Effects on Price and Quantity of Goods Resulting from Changes in the Level of Demand or Supply

Changes in market equilibrium may arise from the following factors

- ▶ Changes resulting from a shift in the demand curve, while supply remains constant
- ▶ Changes resulting from a shift in the supply curve, while demand remains constant
- ▶ Changes resulting from simultaneous shifts in both the demand and supply curves

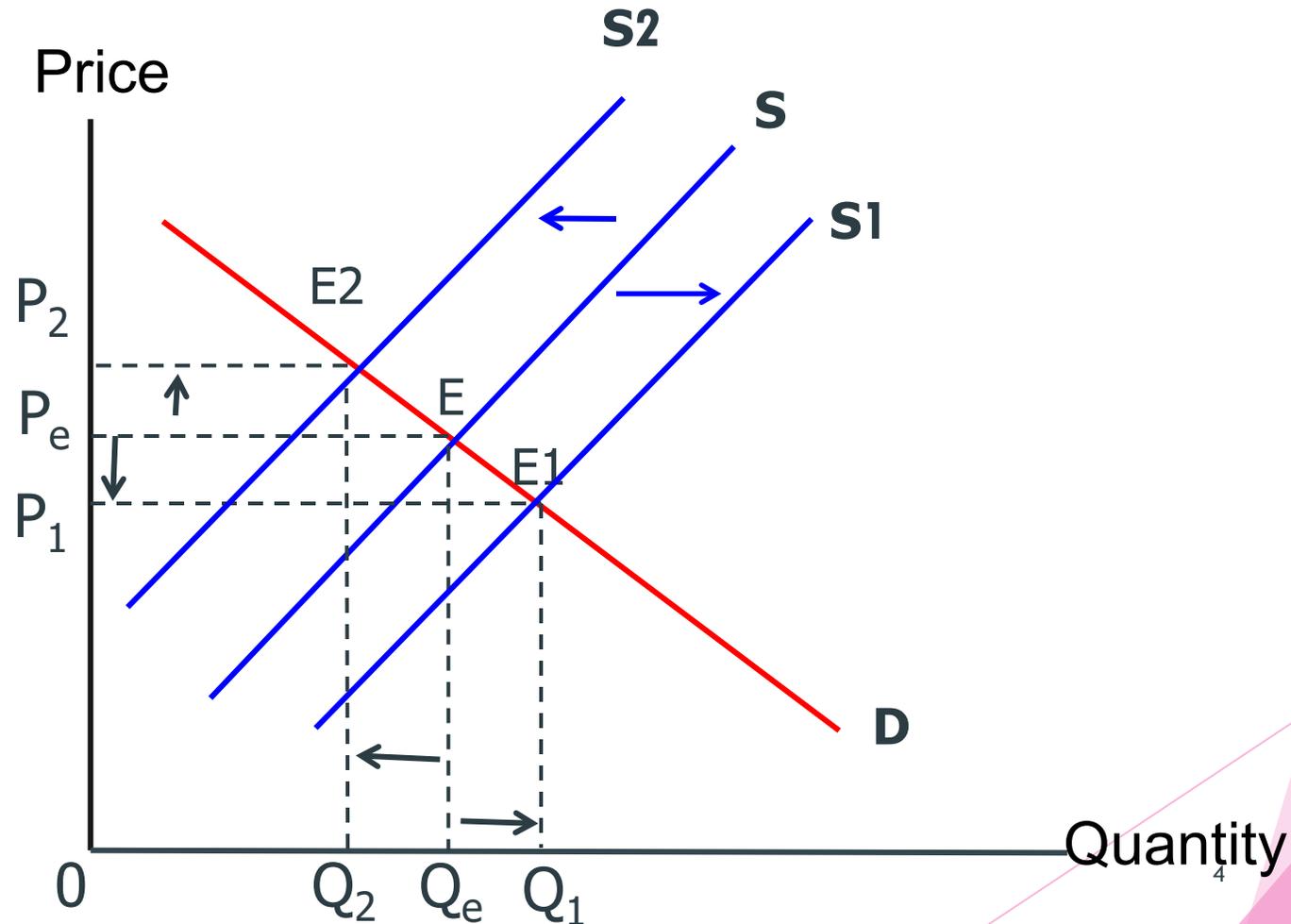
# A Shift in the Demand Curve

For example, an increase or decrease in income



# A Shift in the Supply Curve

For example, improvements or deteriorations in production technology



# Demand and Supply Curves Shift Simultaneously

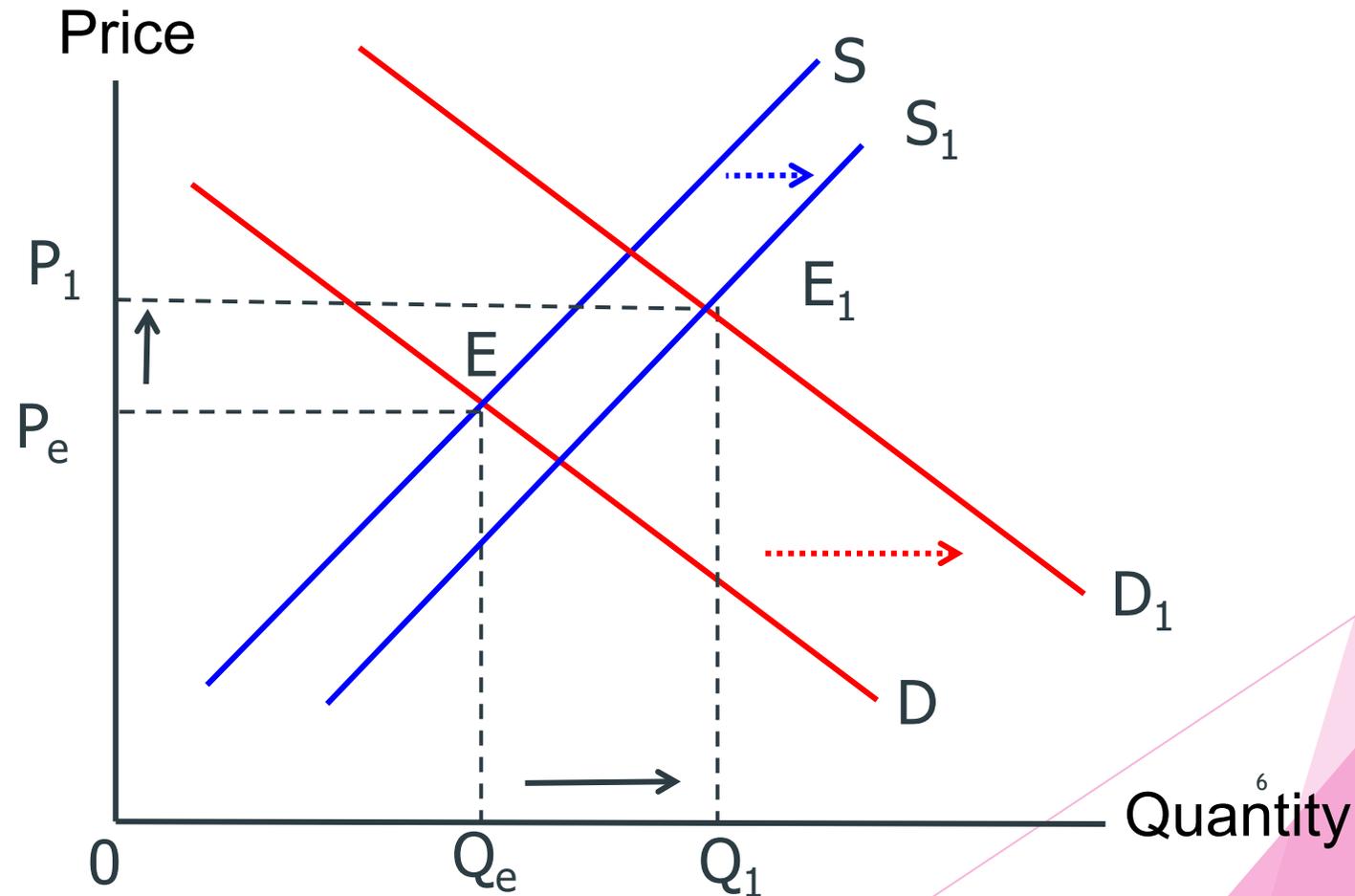
In cases where both demand and supply change simultaneously, the new market equilibrium will be determined at the intersection of the new demand curve and the new supply curve.

Simultaneous changes may take the following forms

- Demand increases and supply increases
- Demand increases and supply decreases
- Demand decreases and supply increases
- Demand decreases and supply decreases

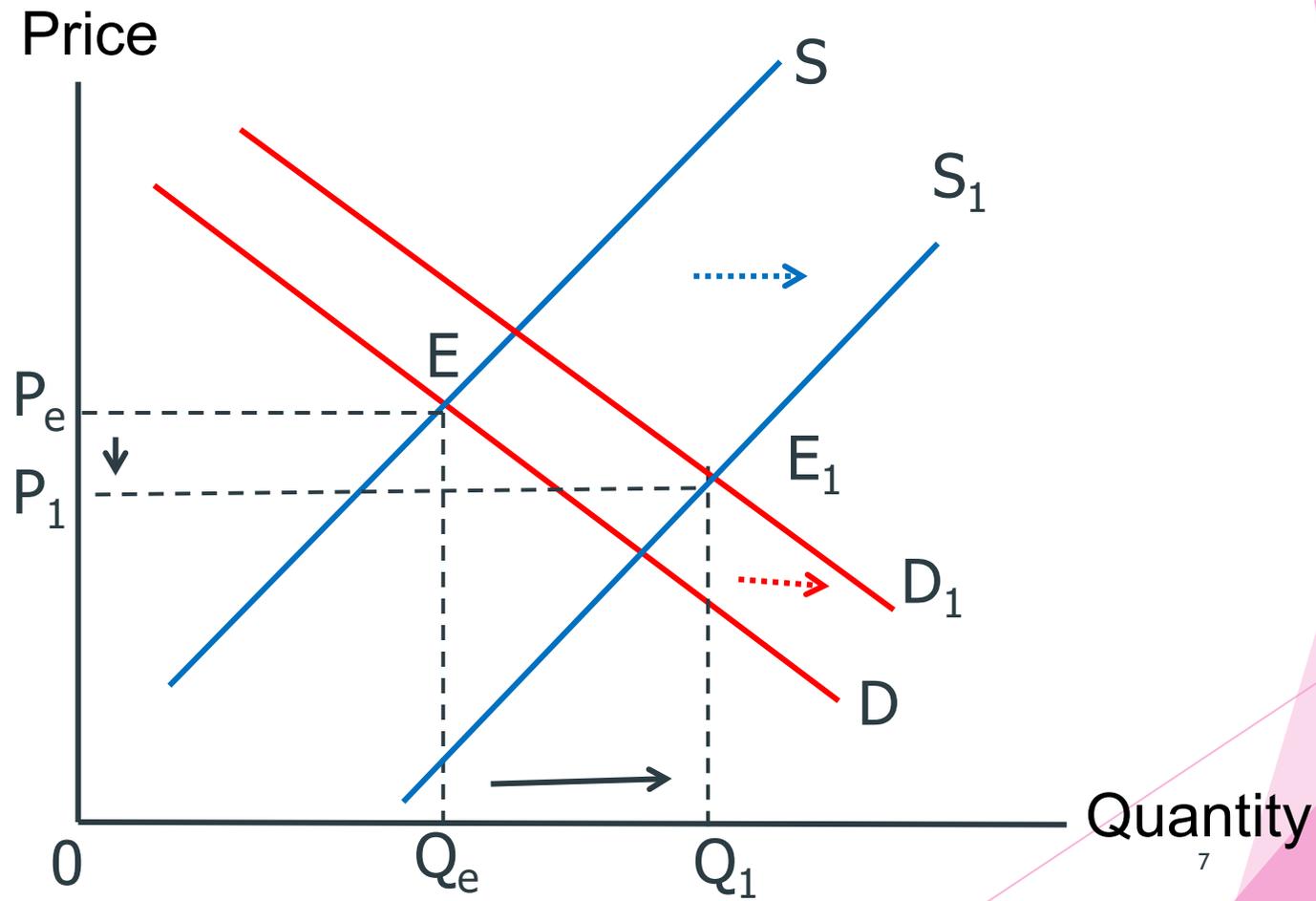
# Demand Increases More Than Supply

$$D \uparrow > S \uparrow$$

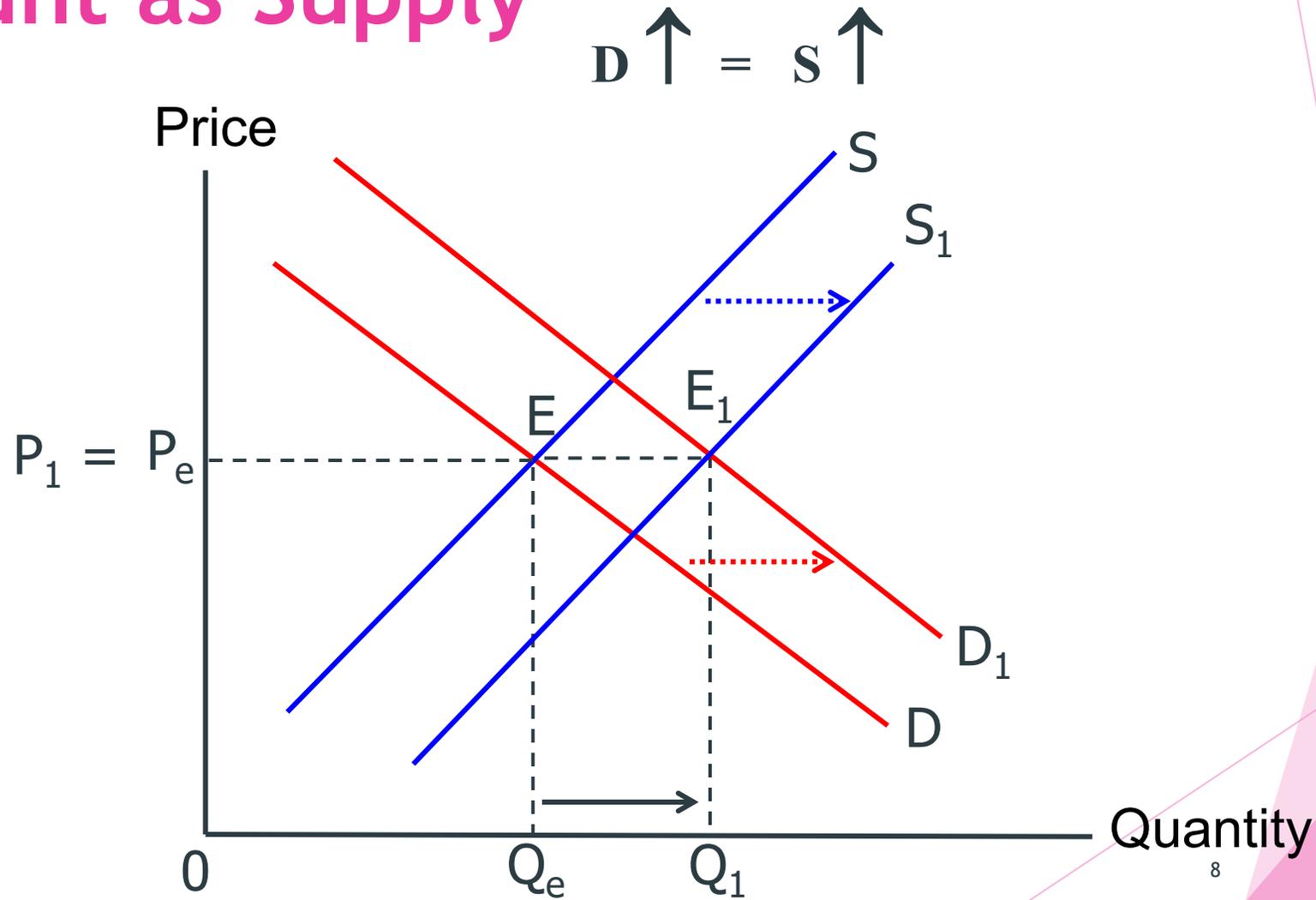


# Supply Increases More Than Demand

$$s \uparrow > D \uparrow$$



# Demand Increases by the Same Amount as Supply



# Intervention in the Operation of the Price Mechanism

---

- The free operation of the price mechanism effectively reflects the needs of society.
- However, in some cases, intervention in the operation of the price mechanism is unavoidable.
- The government needs to intervene in the price mechanism primarily to help alleviate economic inequality among individuals in society.
- This is done by implementing policies according to different objectives in each case.
- Setting a minimum price level (Minimum Price Level)
  - Price guarantee policy or price support policy (Price Support Policy)
  - Minimum wage policy (Minimum Wage Policy)
- Setting a maximum price level (Maximum Price Level)
- Imposition of commodity taxes

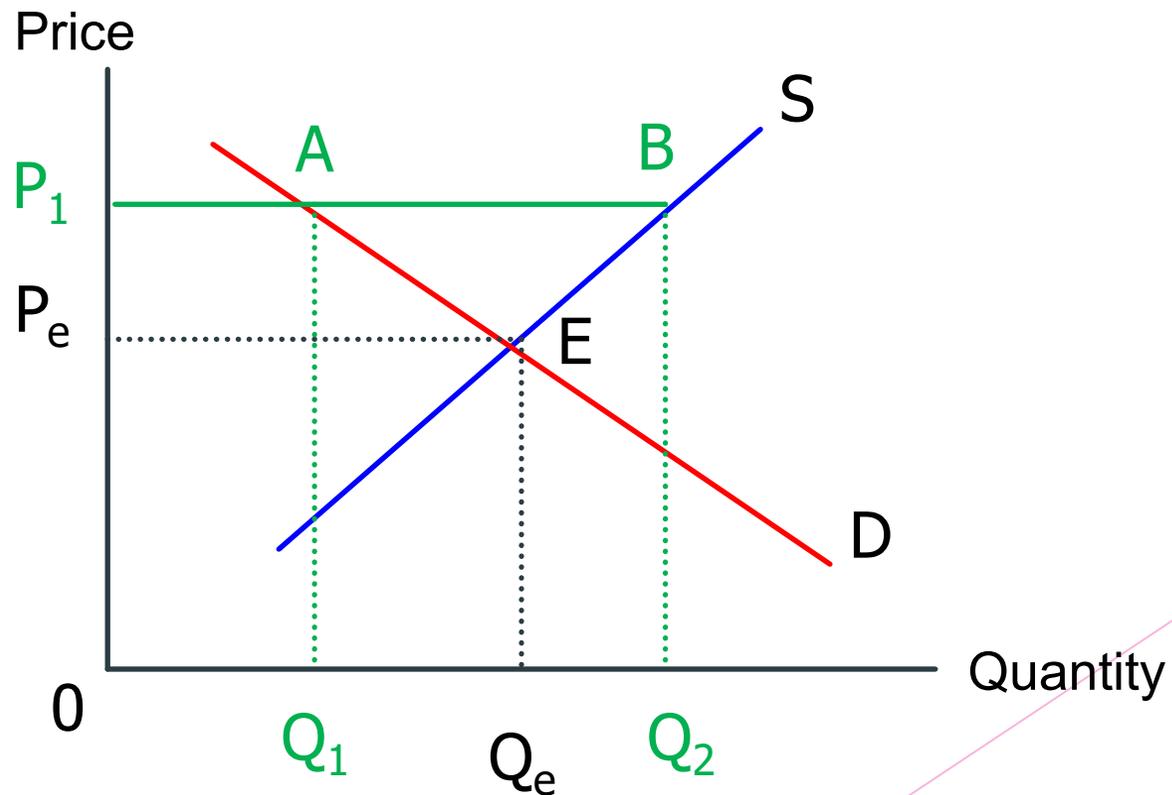
# Setting a Minimum Price Level



- The price level of goods that is lower than the market price (equilibrium price) due to excess supply.
- Examples of agricultural products such as paddy rice, sugarcane, and natural rubber, where farmers suffer hardship.
- The government sets the minimum selling price at a level higher than the market price.

# Setting a Minimum Price Level (Price Support Policy)

- The government sets a minimum price at  $P_1$ . As a result, consumer demand decreases to  $Q_1$ , while producers increase output to  $Q_2$ .
- Excess supply of  $Q_2 - Q_1$  units occurs → surplus goods in the market.
- The government purchases  $Q_2 - Q_1$  units at price  $P_1$  and utilizes them for public purposes, such as exporting or distributing aid to the population during times of disaster.



# Setting a Maximum Price Level

It is a policy used by the government when market prices, as determined by supply and demand, are excessively high and cause hardship for consumers.

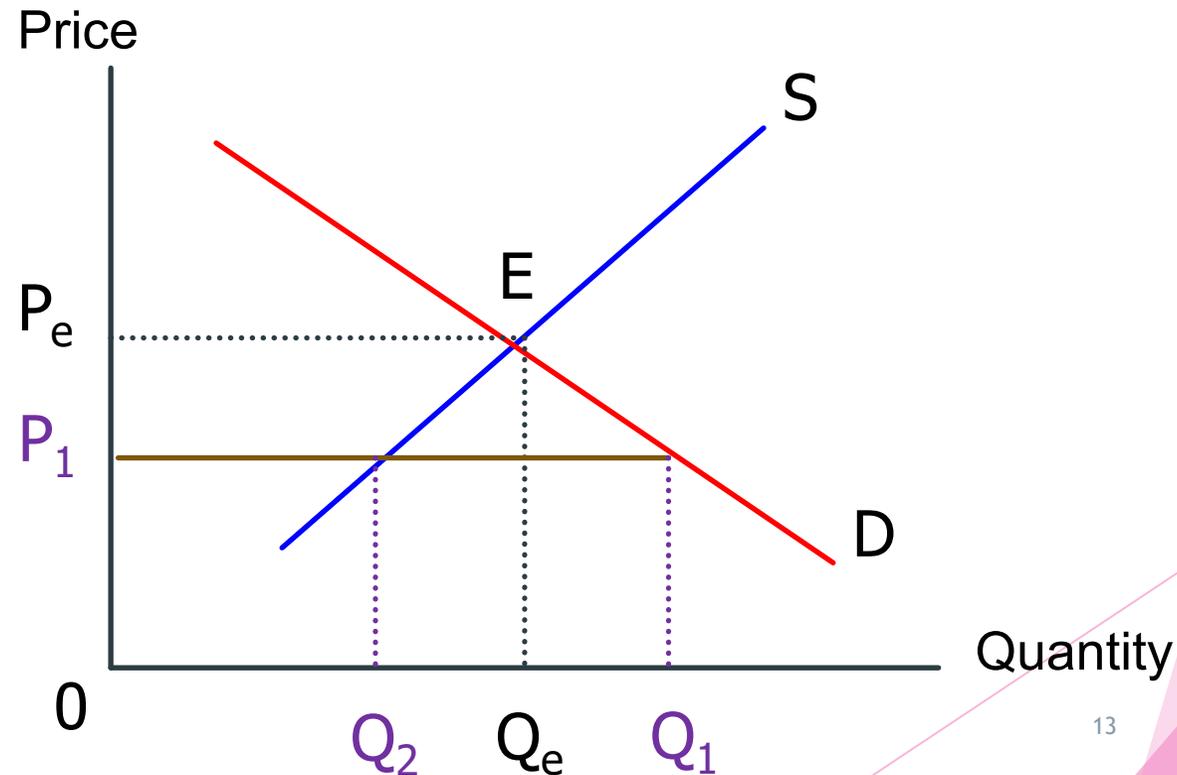
Therefore, the government finds ways to alleviate such hardship by setting commodity prices at a level lower than the original equilibrium price.

This is referred to as a **Price Control Policy**.

It is applied particularly to essential goods for livelihoods, such as public utility charges and diesel fuel.

# Setting a Maximum Price Level (Price Control Policy)

- The government sets the price at  $OP_1$ , which is regarded as the highest price at which buying and selling are legally permitted.
- Consumers increase their purchases to  $OQ_1$  units, while producers are willing to supply only  $OQ_2$  units.
- As a result, excess demand of  $Q_2Q_1$  units occurs → a shortage of goods arises, leading to illegal trading in the black market.



# Setting a Maximum Price Level Price Control Policy

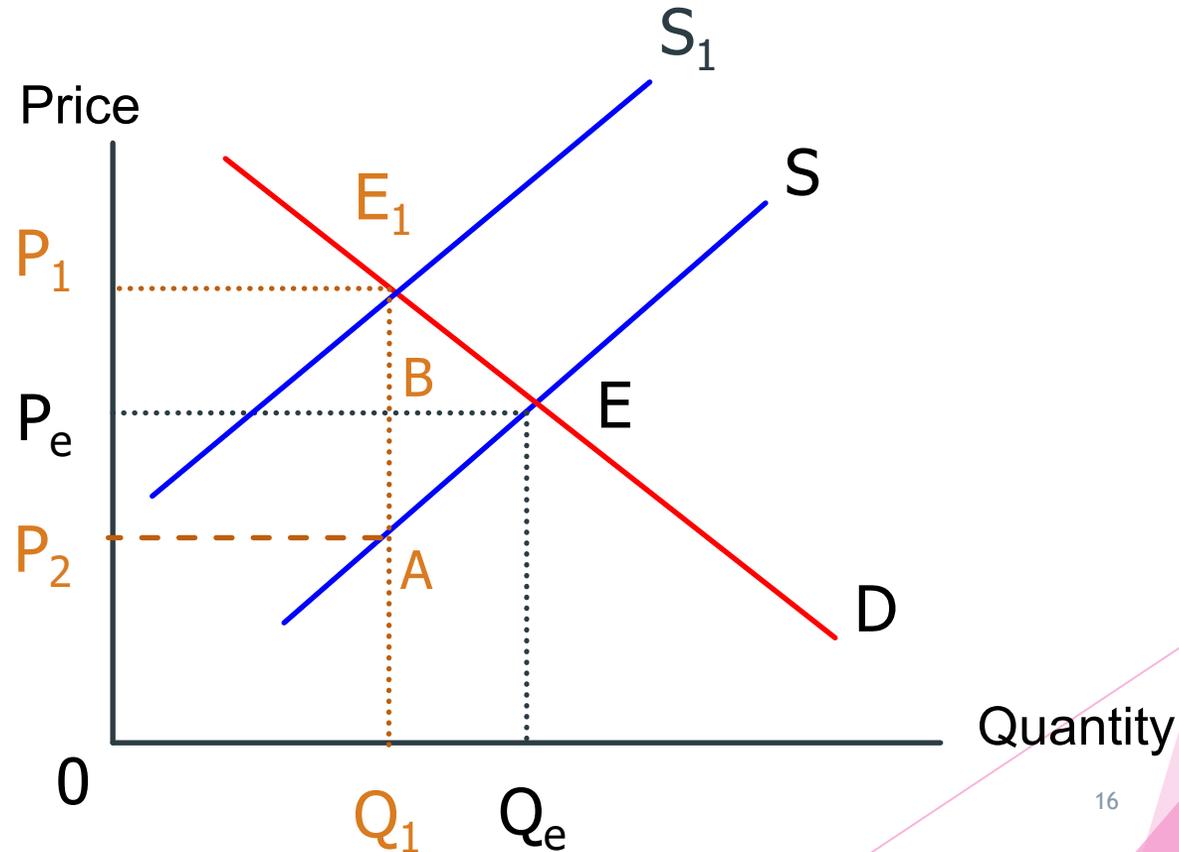
- The emergence of black markets constitutes a loss to consumers, as sellers are willing to sell goods at prices higher than the controlled price.
- Consequently, only consumers with higher incomes are able to obtain the goods.
- Governments often implement control measures, such as a rationing policy, to help distribute scarce goods more equitably among consumers.
- Rationing may be carried out through the distribution of coupons that grant the right to purchase goods.
- The quantity of goods allocated is specified on the coupons according to the necessity of each individual or household.
- For example, allocations may be based on the number of household members or household income.
- The use of price guarantees or price control policies as described is considered a short-term solution to immediate problems.
- A more appropriate approach is to adjust supply and demand so that their quantities are equal, such as:
- If a product is overproduced, the quantity supplied should be reduced.
- This can be achieved by providing producers with information about market demand in order to encourage them to shift production to other goods.
- Alternatively, demand can be increased by expanding the market, and so forth.

# Commodity Taxation

- The government uses taxation policy as a tool to conduct economic activities, such as:
- Promoting domestic production and reducing economic inequality in society.
- Taxation results in changes in market prices of goods.
- Taxation is not a direct determination of higher or lower prices through direct intervention in the price mechanism.
- Rather, it is an indirect intervention, such as imposing a per-unit tax on sellers to reduce excess profits and using tax revenue for the benefit of society as a whole.

# Per-Unit Commodity Tax Imposed on Sellers

- When the government imposes a per-unit tax, the supply curve shifts to  $S_1$ ; the price increases to  $OP_1$ , the quantity decreases to  $OQ_1$ , and the equilibrium shifts from point  $E$  to point  $E_1$ .
- Government tax revenue =  $AE_1$ .



- ▶ It can be observed that, in all cases of government intervention in the price mechanism,
- ▶ such intervention inevitably leads to a loss of social welfare, and this clearly demonstrates that
- ▶ the government should not rely on price intervention policies as a primary instrument for solving problems.
- ▶ Such measures should be employed only as temporary solutions to address short-term issues.
- ▶ In the long run, emphasis should be placed on policies that help increase or decrease demand or supply in accordance with the nature of the underlying problem,
- ▶ while allowing the price mechanism to function as the main driver of economic activity.