2.4 Price determination

Name: _____ Class: _____ Date: _____ **Total: 15 marks**

KEY WORDS equilibrium • price determination • demand • supply • market

Objective

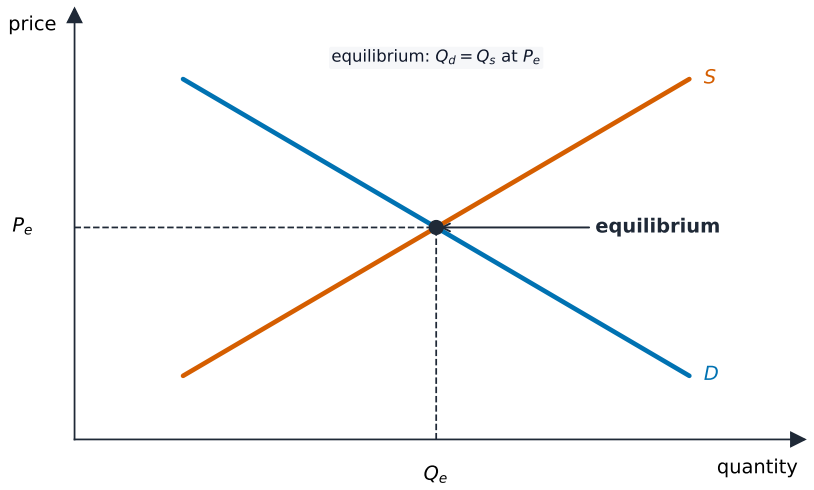
Build the skills to answer exam questions on **price determination** – market **equilibrium**, the equilibrium price and quantity, and reading a demand-and-supply diagram.

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

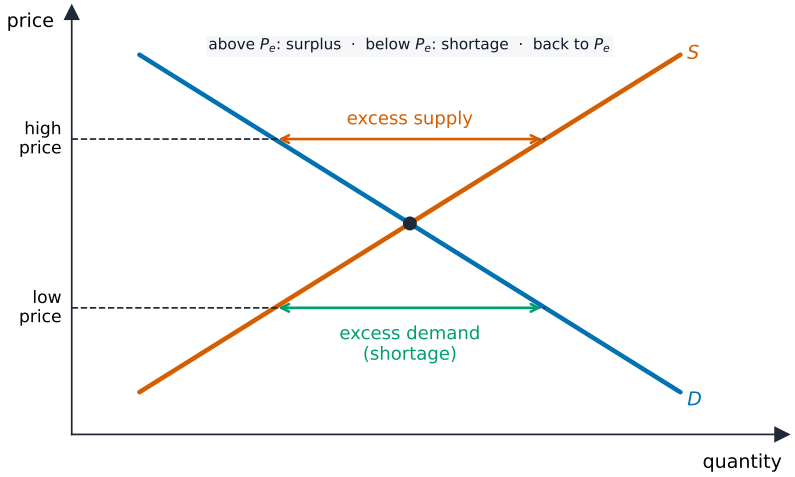
1 Key knowledge and worked examples

Market equilibrium



At equilibrium P_e, Q_e: quantity demanded = quantity supplied

- **Equilibrium** : 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.



Away from equilibrium a shortage or surplus forces the price back to P_e

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

2 Practice

2.1 Define the term *equilibrium price*. [2]

2.2 State what is true about quantity demanded and quantity supplied at equilibrium. [1]

2.3 State what determines the price of a good in a free market. [1]

3 Exam-style questions

3.1 At the equilibrium price: [1]

- **A** there is excess demand
- **B** there is excess supply
- **C** quantity demanded equals quantity supplied
- **D** the price is rising

3.2 Using a demand and supply diagram, show and explain the equilibrium price and quantity. [4]

3.3 Analyse how the equilibrium price and quantity change when demand for a good increases. [6]

Solutions

IGCSE Economics answers are marked by **level of response**: award **K** knowledge, **App** application, **An** analysis and **Ev** a justified judgement.

Each answer shows the steps, then the **result**.

2.1

- **equilibrium price** is the price at which quantity demanded **equals** quantity supplied, so there is no pressure for it to change (K)

2.2

- at equilibrium they are **equal** (K)

2.3

- the **interaction of demand and supply** (where they cross) (K)

3.1 C

- at equilibrium, quantity demanded **equals** quantity supplied (K)
- A is a shortage; B is a surplus; D is a market still adjusting

3.2

- draw labelled demand and supply curves that **cross** (K)
- they cross at one point → equilibrium price P_e and quantity Q_e (An)
- here the amount buyers want **exactly equals** the amount firms supply (An)

3.3

- an increase in demand **shifts demand right** (K)
- at the old price there is **excess demand** (a shortage) (An)
- buyers bid the price up; quantity supplied rises along the supply curve → **higher price and higher quantity** (An)