Pricing

Pricing is nothing more than the combination of the demand curve and supply curve. The point where demand and supply intersect is the *Equilibrium*. At equilibrium supply equals demand (\(S=D\)) and the market will clear. The number of goods produced will be the same as the number purchased. Both the consumers and the producers are constantly trying to get to the equilibrium price.

Anytime supply and demand are not equal the market is said to be in *Disequilibrium*. Either supply is greater than demand, which cause there to be a surplus. The other case is when demand is greater than supply this will cause a shortage in the market. In both cases the market forces will move price to create equilibrium.

When price is high (above equilibrium) supply > demand goods will be put on sale or a rebate maybe given both of which reduce price so that the market will clear. (First graph above) In the second graph price is a low price (below equilibrium) it will increase until some consumers leave the market and/or producers will increase production levels to clear the market.

The government intervenes in some markets and establishes price controls. The government may impose a *price ceiling*: maximum price allowed by law. OR *price floor*: minimum price allowed by law.

Price ceilings are set below equilibrium, therefore they cause shortages. Rent control is an excellent example. By setting prices artificially low rent becomes affordable for lower income families; however, it will force some landlords out of the market taking properties away or lowering the quality of the properties available. Landlords will not invest capital if there is no return on investment. In other words they cannot recover their cost.

Price floor are set above equilibrium; therefore, they cause a surplus. Examples of price floors are things like milk, cigarettes, and minimum wage. By providing a minimum price for milk it helps some farmers stay in business. Cigarettes are highly addictive, as well as, heavily taxed. People who smoke will buy them even at prices that are artificially high; this will also guarantee tax revenues.