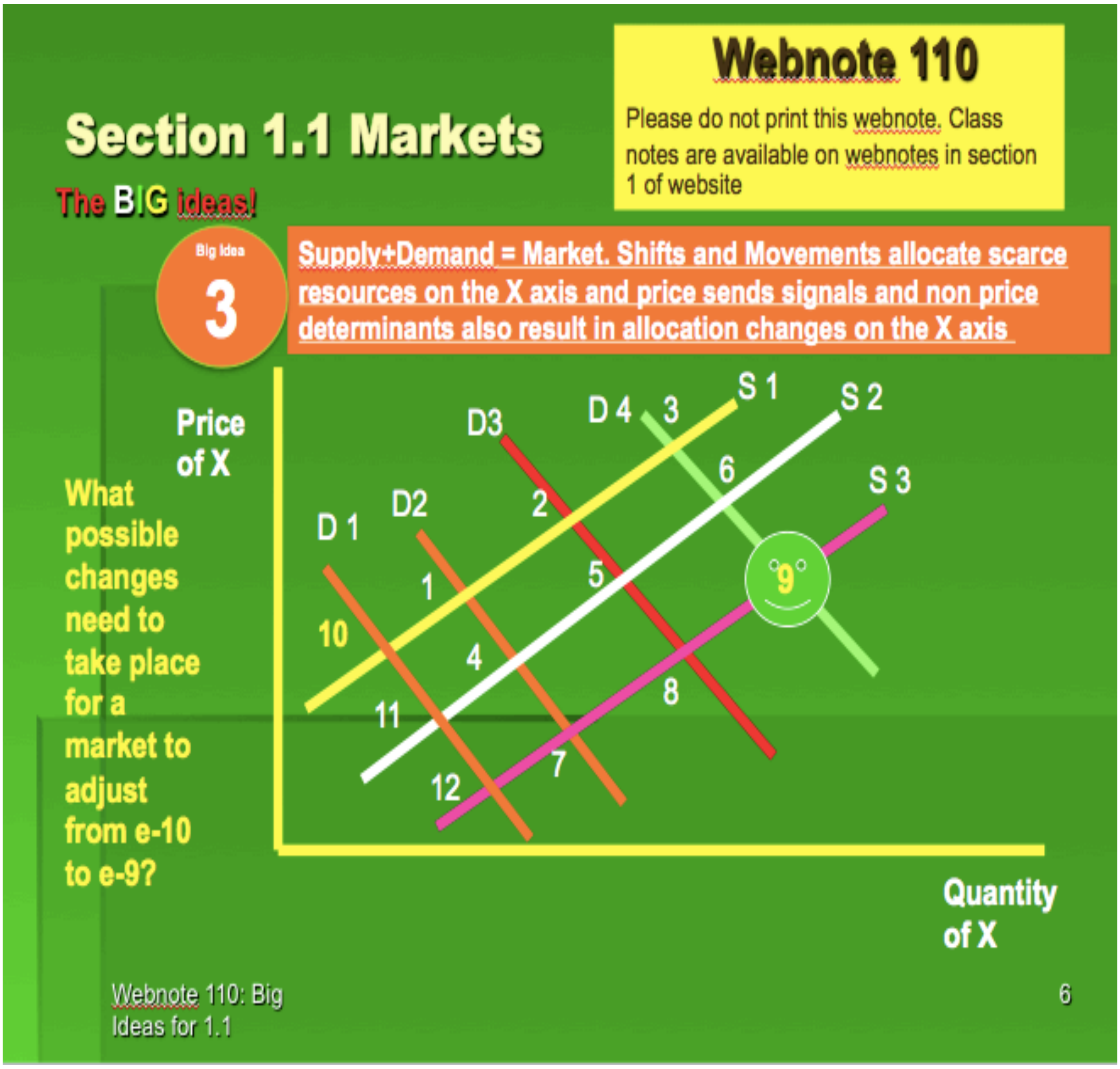
SYLLABUS REFERENCE 1.1 SUPPLY FUNCTION

Big Question: What causes changes to the Supply in the market?

Webnote 202

Syllabus: 7-11
(HL only item 11)



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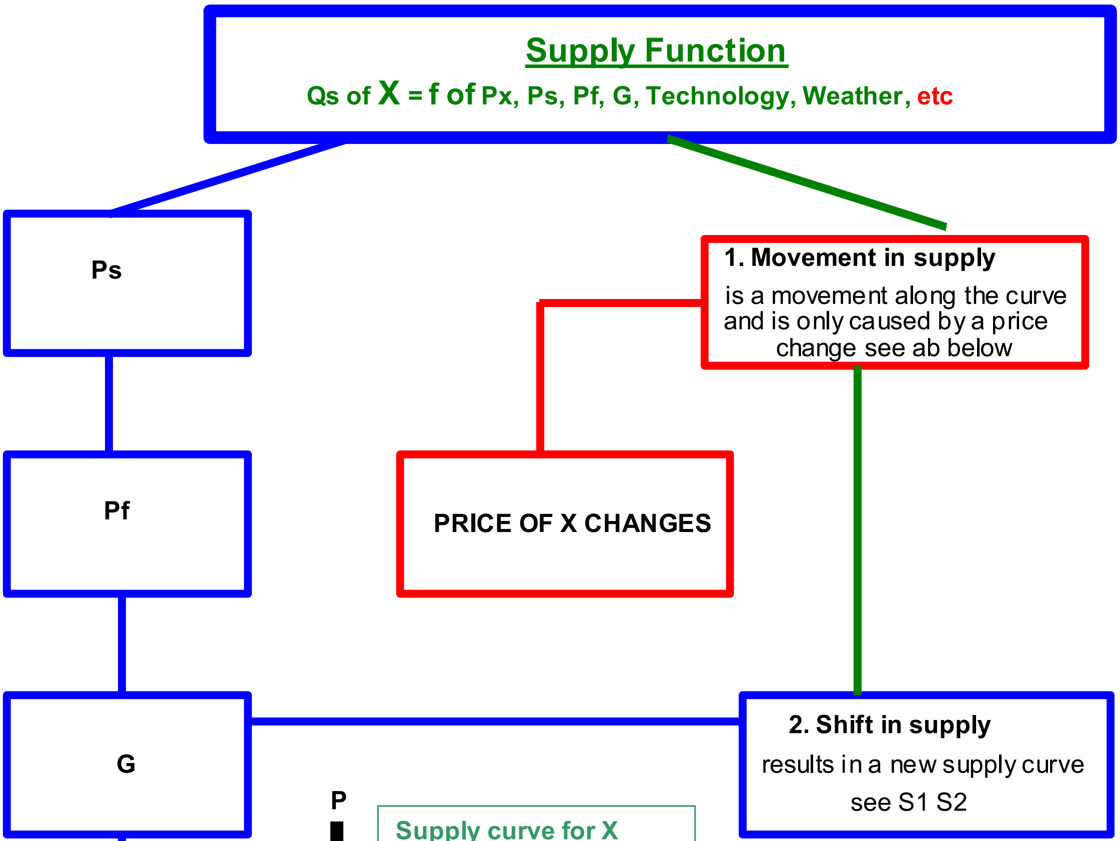

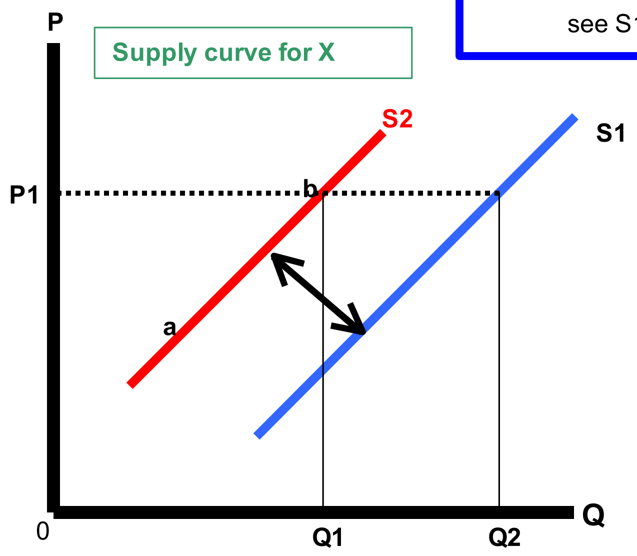

Ps = price of substitute good/service
Pf – price/cost of factors of production
G = role for government i.e. indirect taxation (blue to red) or subsidy (red to blue)
TECH = impact of technology on costs of production
Weather = impact of weather on output

Notes:

1. **supply curve as a resource allocation curve**
2. **role of government: indirect taxation and subsidies**
3. **growth occurs as we move along the X axis from q1 to q2**

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Non Price determinantsSupply Function Changes: explained in the context of 'Ceteris Paribus'.			
Non Price determinants	**What does it mean?**	**Note**	**How does supply shift?**
Price of substitutes	This refers to substitute goods that the firm produces. E.g. a farmer with his factors of production can produce wheat or beef	Note substitutes here are not substitutes in the context of the demand curve. Substitutes refers to the different goods the firm can produce with the factors of production.	Shift If price of Y rises then supply of X results in S1 shifting to S2
Cost of factor of production	Rising costs of land, labour + capital mean less output can be produced at current prices. Market will shrink in this case and total revenue of firm will fall.	If price does not change then the firm will produce less output due to higher costs. Falling costs on the other hand would result in increases in output	Shift If costs of factors of production rise then supply of X results in S1 shifting to S2
Government: indirect taxes and subsidies	Indirect taxes result in markets shrinking as the firm will supply less goods due to higher taxes Taxes (indirect): Market will shrink in this case and total revenue of firm will fall.	Taxes (indirect) reduce the size of the market. Subsidies increase the size of the market.	Shift: If indirect tax rises then supply of X results in S1 shifting to S2. Opposite occurs for a subsidy.
Technology	Better technology results in higher output and visa versa. Best technology: Market will grow in this case and total revenue of firm will rise.		Shift If technology improves then supply of X results in S2 shifting to S1. Opposite occurs for a poor technology.
Weather	Good/bad weather cause supply shocks. Bad weather: Market will shrink in this case and total revenue of firm will fall.	Agriculture suffers regular supply shocks e.g drought	Shift If weather is poor then supply of X results in S1 shifting to S2. Opposite occurs for good weather i.e. bumper crop.
Price Change	**What does it mean?**	**Note**	**How does supply change?**
Price of good X	Firms change the price of the good along the supply curve	Price change is determined by the firm.	Movement along the supply curve following the law of supply.