Economics 2010-100 University of Colorado
Soojae Moon Fall 2011

Chapter 6: Supply, Demand & Government Policies

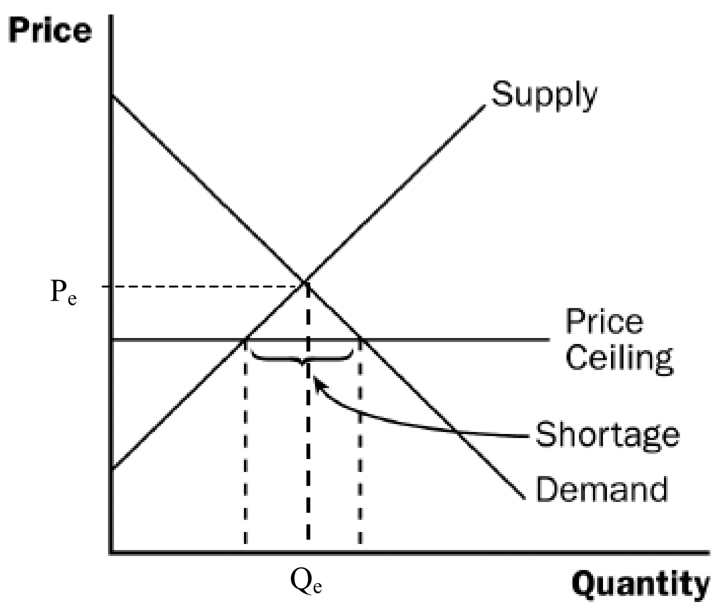
- What are price ceilings and price floors? What are some examples of each?
- How do price ceilings and price floors affect market outcomes?
- How do taxes affect market outcomes? How do the effects depend on whether the tax is imposed on buyers or sellers?
- What is the incidence of a tax? What determines the incidence?

<u>Price Controls</u>

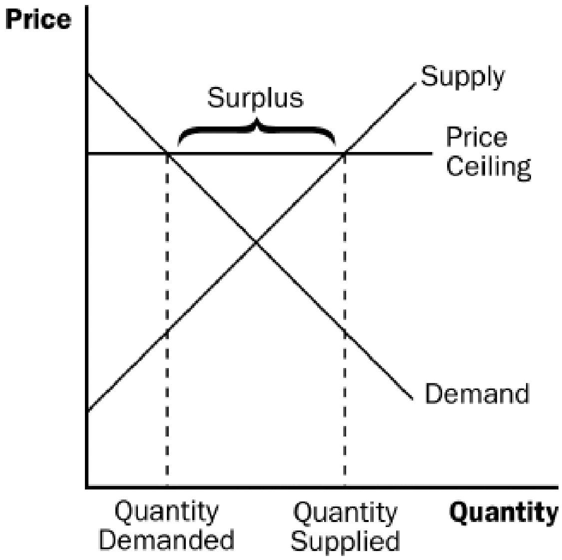
<u>price ceiling:</u>

<u>price floor:</u>

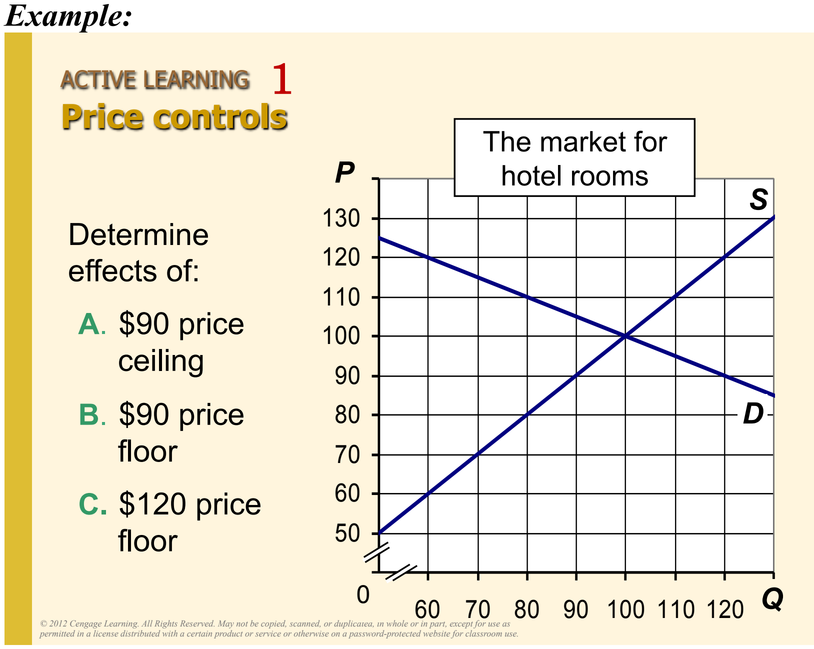
- **Price ceiling**
  - Binding price ceiling always less than equilibrium price
  - If it is above equilibrium price, not binding and no effect on p or q



- **Price floor**
  - Binding price floor always greater than equilibrium price
  - If it is below equilibrium price, not binding and no effect on p or q


Price
Surplus
Supply
Price Ceiling
Demand
Quantity Demanded
Quantity Supplied
Quantity

Example:


ACTIVE LEARNING 1
Price controls
Determine effects of:
A. $90 price ceiling
B. $90 price floor
C. $120 price floor
The market for hotel rooms
P
130
120
110
100
90
80
70
60
50
0
60 70 80 90 100 110 120
Q
S
D
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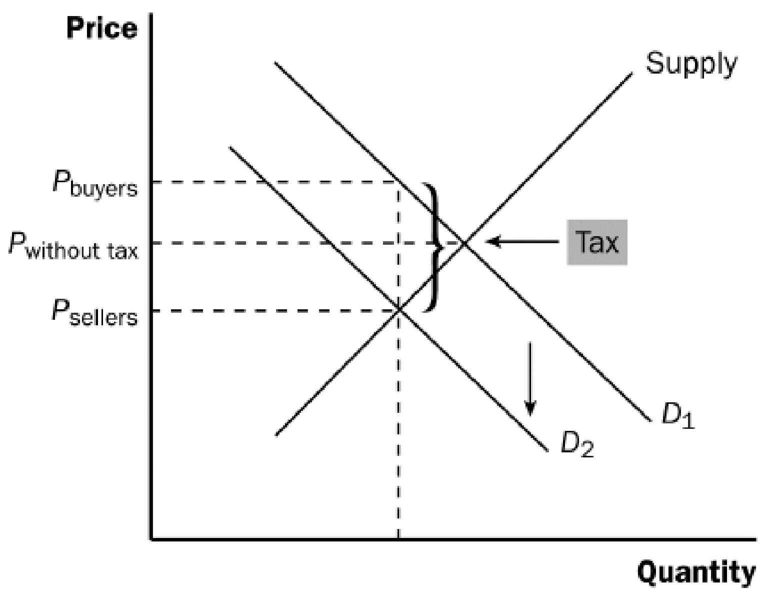
Taxes:

tax incidence: the manner in which the burden of a tax is shared among participants in an economy

- **Taxes on Buyers – How Affect Market Outcomes**
  - Pay certain amount on a good (e.g., $1 per unit bought), causes a decrease in demand Here, let's look at the effects of a $1.50 per unit tax on buyers in the market for pizza.

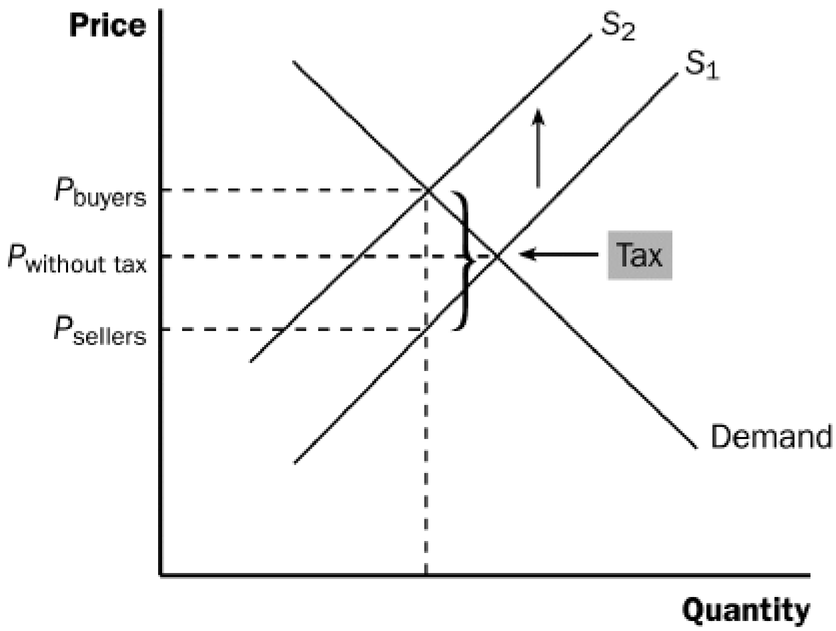


  - Demand curve will shift in by the amt of the tax
  - Quantity of good sold will ______________________
  - What happened?

- **Taxes on Sellers – How Affect Market Outcomes**

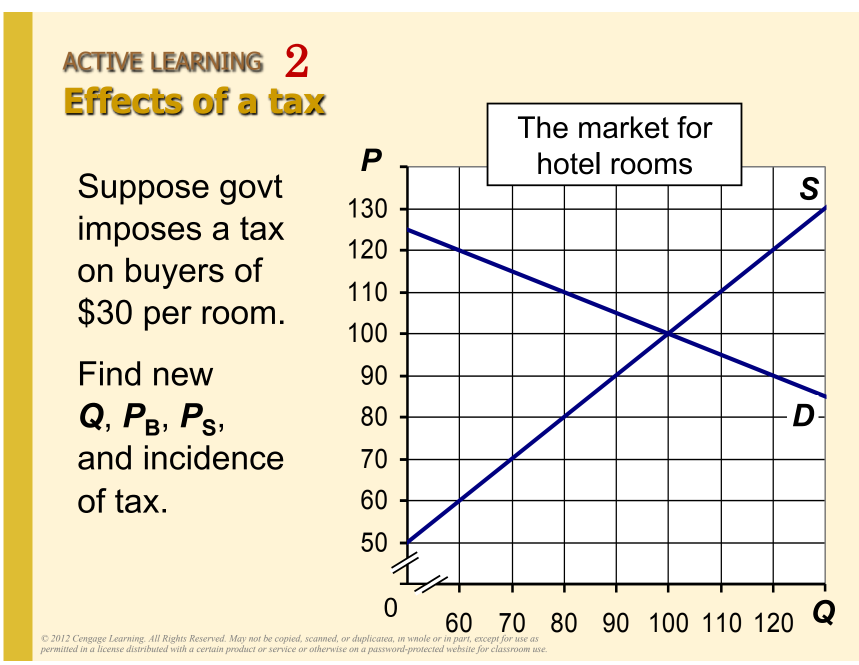
Here, let's look at the effects of a $1.50 per unit tax on sellers in the market for pizza.

- Gov requires sellers to pay certain amount for each unit sold.

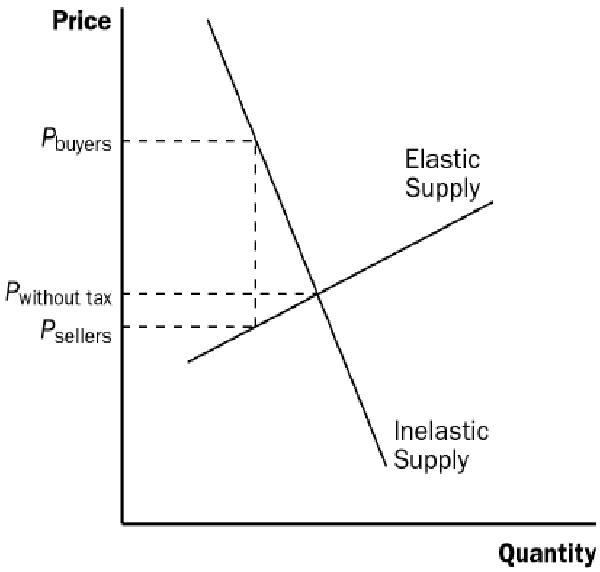


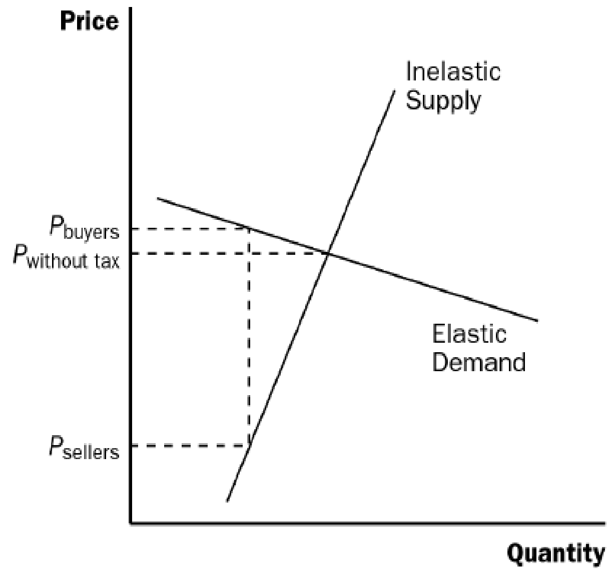
- Shifts supply curve __________.
- Quantity sold will ____________________
- Buyers & sellers share burden

The effects on P and Q, and the tax incidence are the same whether the tax is imposed on buyers or sellers!!



- **Elasticity and incidence of a tax**
  - Largest share of the burden falls on the more inelastic curve.
    - Case 1: Demand inelastic, supply elastic – __________________ pay more
    - Case 2: Demand elastic, supply inelastic – __________________ pay more





Suggested problems: Problems and Applications- 3, 4, 9