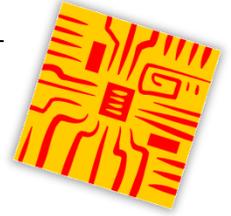


NICE PRICE



Why did exchange prices of computer chips concentrate around \$28 per chip? The answer is that this price was the only one that balanced the market. Here's why.

A market exists whenever buyers and sellers exchange with one another. But the amount sellers want to sell can be very different from the amount buyers want to buy. In the game you played, only a price of \$28 per chip balanced these two amounts.

The table below shows what was happening in the market for computer chips. The table shows what all the buyers' cards were telling them to do. And it shows what all the sellers' cards were telling them to do.

Figure 1: Demand and Supply Schedules for Computer Chips

Demand Schedule (D1)

Price Per Chip	Number of Chips Buyers Want to Buy
\$20	32
\$22	30
\$24	28
\$26	26
\$28	24
\$30	20
\$32	16
\$34	10
\$36	4

Supply Schedule (S1)

Price Per Chip	Number of Chips Sellers Want to Sell
\$20	4
\$22	10
\$24	16
\$26	20
\$28	24
\$30	26
\$32	28
\$34	30
\$36	32

Note that the equilibrium price is the only one at which buyers want to buy the same number of chips that sellers want to sell. Here, a price of \$28 is the equilibrium price because it balances these two quantities at 24 chips.

HOW TO BALANCE A MARKET

The numbers in Table 1 illustrate the laws of demand and supply. Sellers offer more chips for sale at higher prices than at lower prices. In contrast, buyers want to buy fewer chips at higher prices than at lower prices.

For example, look at table 1 to see what happens when the price is \$36. At this price, sellers want to sell 32 chips. But buyers only want to buy 4 chips at that price. So the market is unbalanced. A surplus of 28 chips exists. This means sellers want to sell 28 more chips than buyers want to buy at that price. Because of the surplus, sellers reduce their prices. Only by decreasing their prices to \$28 can they sell all the chips they want to sell.

On the other hand, the price can also be too low. Look what happens when the price is \$20. Here, too, the market is unbalanced. A shortage of 28 chips exists. This means that buyers want to buy 28 more chips than sellers want to sell at that price. Because of the shortage, buyers increase their prices. Only by increasing their prices to \$28 per chip can they buy all the chips they want.

A price of \$28 per chip turns out to be a special price. It is special because of what it does: It balances the number of chips that buyers and sellers want to trade. Because of its special role in balancing the share demanded and supplied, this price is called the equilibrium price. It is the only price at which the chips demanded and supplied are in equilibrium.

The game you played shows how buyers and sellers adjust their prices to reach a balance, or equilibrium. But these balances seldom stay the same. Demand and supply are continually changing, and buyers might want to buy more at each possible price. If so, they bid the price up to a new equilibrium level. Or sellers might want to sell more at each possible price. If so, they push the price down to a new equilibrium level.

So there is no mystery behind the ups and downs of prices for computer chips - or for other goods and services. Prices change because buyers and sellers become more or less willing to buy or sell something. Then they work our new equilibrium prices to balance the market - just as your class did for computer chips.

A graph can be used to illustrate visually what happens in a market. This may not seem important now, but it is useful when the supply and demand curves change. Draw a graph in Figure 2 to illustrate the information contained in Figure 1.

Figure 2: Supply and Demand Curves for Computer Chips

