Supply and Demand

"The body is a unit, though it is made up of many parts; and though all its parts are many, they form one body."

Understanding the patterns of demand and how to supply this in a reliable, cost effective manner is crucial to managing a business and managing cash flow. The price that you can sell a product is like will normally reflect the relationship between the demand for products or services and the availability of supply.

Example 1: *Electricity*

- Electricity has become an essential requirement and a critical enabler of how we live, work and communicate.
- If there is an abundance of electricity – in other words unlimited supply and a large and steady demand, the price that we pay for the electricity should remain low.
- However, as the economy grows, demand grows. So if additional power plants are not built and so the supply becomes limiting or constrained, the power companies will begin increasing the price of electricity to try to reduce demand. The assumption here is that as the price goes up, people will look for alternates (like solar power, energy saving light bulbs) or switch off lights & appliances when not in use, which reduces consumption.

- There comes a point when raising prices doesn't reduce demand. As in the case with power because this is such an essential component of modern economies.
- But as prices rise, this enables Power generation companies to invest in power generation facilities which will boost supply again to balance the demand.

Example 2: *Strawberries*

- In summer when strawberries are in season the price is low.
- This is because is they are not sold, they will go rotten and need to be thrown away.
- So suppliers and retailers will drop their prices in order to boost or "stimulate" demand.
- In winter when strawberries are not easy to get hold of, prices rise. Most people would decide they don't need strawberries at high prices and just go without. Some, who really want strawberries will be happy to pay the higher price.

- In this way, the suppliers & retailer balance the demand with the available supply by raising or lowering the price.
- Sometimes, if you are selling fresh items like food and demand is lower than you thought, discounting the price right down to the breakeven point is a better option than not selling the item and having to throw it away.

Demand Forecasting:

There are many complex and sophisticated methods and models for forecasting demand. The most simple way is to keep good records of which products you sell at what price and when. By analysing these patterns, you will get a feel times for which days or times of the week/month/year there is more or less demand for your products. This will also help you to track the variations in a product line like which colours and sizes people prefer. This is critical as it helps you to manage **when** to order new stock and **how much** of each stock item to order. This again emphasises the importance of good and regular record keeping.

Supply Chain & Inventory management

A Supply Chain is the sequence of steps that occur in the re-ordering of products.

Inventory is also sometimes called stock and is the physical quantity of each product that you sell in your business. More complex businesses, such as clothing companies will keep very detailed records of their stocks – like red men's XL round neck T-shirts, blue men's round neck XL T-shirts etc. These are known as **stock keeping units (SKU's)**

This sequence usually starts with (1) a forecast of expected demand and (2) a count of how much of each SKU you still have. The forecast and the stock count tell you how fast you are likely to sell the stock that you still have and give an idea of when your new stock needs to arrive to prevent selling out of your stock. This is known as a **stock-out** and we know how frustrating it is to arrive at the shop to find they are out of stock! If you don't stock out often your customers will probably come back, however if they regularly can't get what they want, they will probably shop elsewhere so stock-outs can be very costly and so a reliable supply chain is an essential for success.

In setting up orders, it is important to consider the prices of various suppliers or the cost of your raw materials from a variety of suppliers. Their **availability** of these items as well as **when** you can collect is also important when considering who to buy from, especially if there is a lot of competition and running out of your products will cause your customers to go elsewhere.

One way to prevent a stock out is to carry lots of inventory but this can be very expensive and uses up your cash as it is tied up in the stock that is sitting in your warehouse or on your shelves when it could rather be used for marketing to boost demand or may be needed to pay salaries and other overhead costs. It is therefore advisable to manage stock levels at a level that ensure availability for customers without carrying excess stock.

Boosting Demand

The way that companies boost demand is usually through ***marketing***. We will cover the detailed attributes of marketing later in session 5, but as you promote and advertise your products, choose where to sell from, how to package the products, what after sales service you provide, how customers enjoy coming to your shop and so forth, the demand for your products should grow. Critical to this is also what other competitors are doing and so you should regularly review your product & price offering in order to attract new customers, retain existing customers and remain competitive.

Identifying and keeping track of the things that customers enjoy and that make you different, will assist you to understand what makes you successful and enable you to boost your demand if you continue to do those things excellently.