Figure 21-1: Equilibrium in capital markets

The graph illustrates the equilibrium in capital markets with the following axes:

- The vertical axis represents the interest rate, labeled as $i$, with $i^*$ indicating the equilibrium interest rate.
- The horizontal axis represents capital, labeled as $K$, with $K^*$ indicating the equilibrium level of capital.

The supply curve (S) is upward sloping, indicating that as the interest rate increases, the supply of capital also increases. The demand curve (D) is downward sloping, showing that as the interest rate increases, the demand for capital decreases. The equilibrium point (e) occurs where the supply and demand curves intersect, with the interest rate at $i^*$ and capital at $K^*$.
Figure 21-2: Intertemporal substitution

\[ \text{Slope} = -(1+i) = -1.1 \]
Figure 21-3: Intertemporal substitution with an increase in the interest rate: substitution effect dominates.

Substitution effect

Income effect
Figure 21-3: Intertemporal substitution with an increase in the interest rate: income effect dominates

\[ \text{Income effect dominates} \]

\[ \text{Substitution effect} \]

\[ \text{Income effect} \]
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