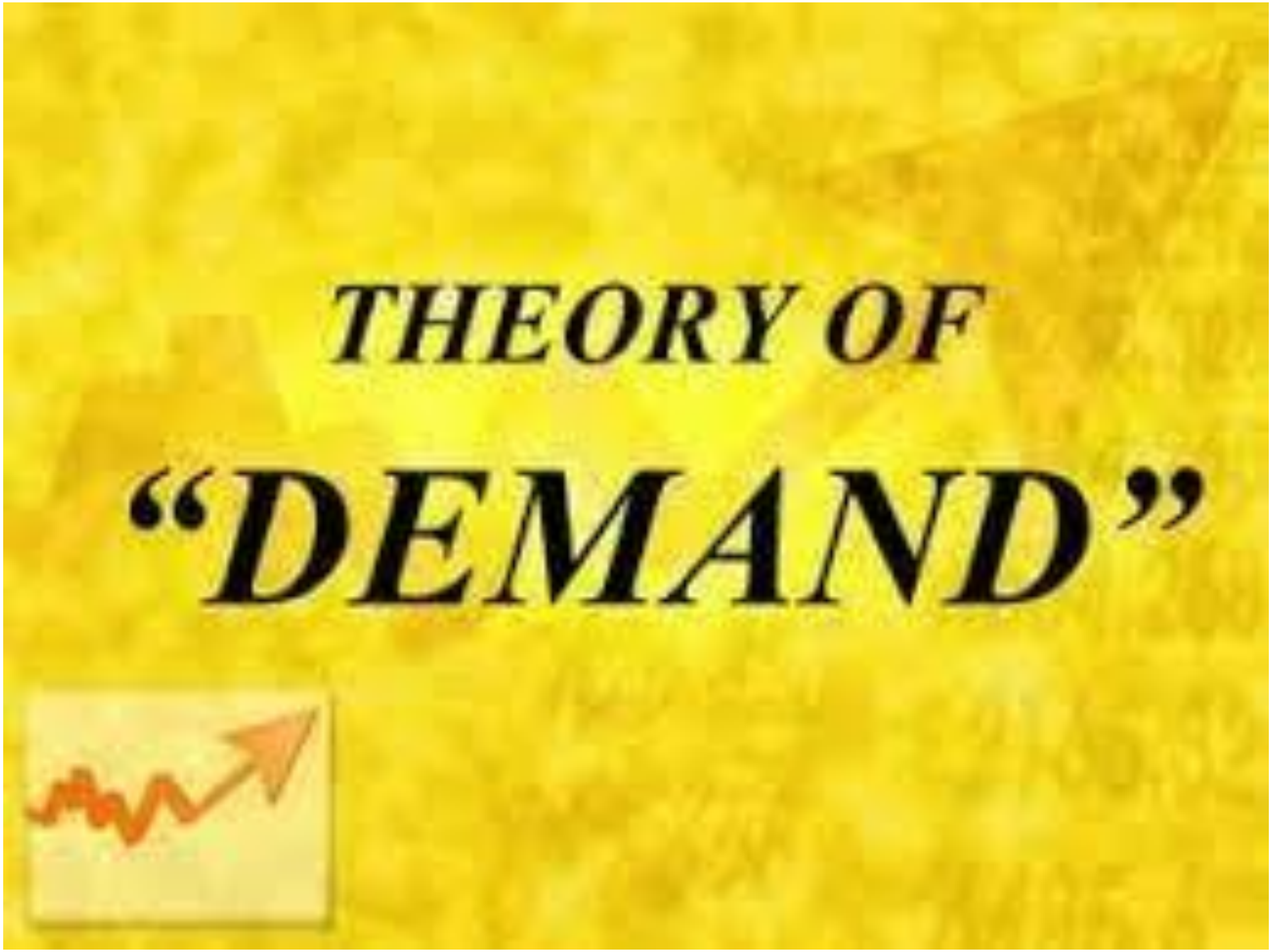
MGT 104

Micro Economics


THEORY OF
“DEMAND”

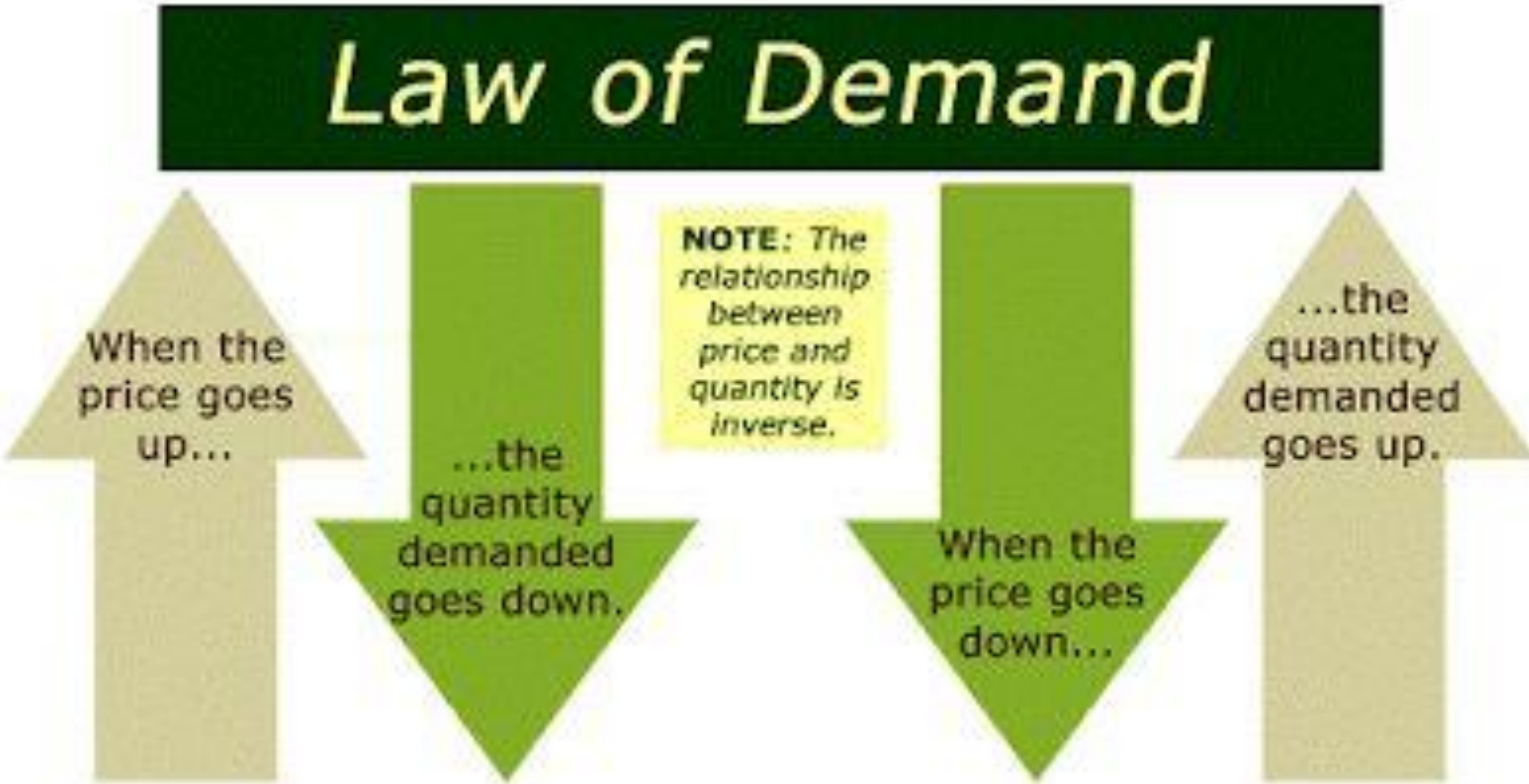
Demand

[di-ˈmand]

An economic principle referring to a consumer's desire to purchase goods and services and willingness to pay a price for a specific good or service.

Investopedia


LAW OF DEMAND
DISTINCTION
INCOME
INCREASE
RELATED
DEPENDENT
STATES
OPPOSITE
EXPECT
DETERMINANTS
GOOD
RELEVANT
RIDERS
STATUS
PARENTHESIS
CURVE
SUBSTITUTION
HOUSEHOLD
QUANTITY
REMAIN
INVERSE
EXPANSION
LOWER
VARIABLE
DAILY
POSTULATES
BUY
DEMAND
SYMBOL
UNCHANGED
HIGHER
EXCEPTIONS
SHOWN
CAUSATIVE
FUNCTION
CONSUMER
CONTRACTION
CHANGE
PRICE
VIOLATES
POTATOES
RELATION
CAUSAL
EXPENSIVE
EXPRESSION
FALLS
AMOUNT
INDEPENDENT
COMMODITY



Law of Demand
When the price goes up...
...the quantity demanded goes down.
NOTE: The relationship between price and quantity is inverse.
When the price goes down...
...the quantity demanded goes up.

Demand Theory

Demand theory is a principle that emphasizes the relationship between consumer demand and the price for goods and services within a market.

The price of the good decreases as quantity increases. Vice-versa, where the price of the good increases as the quantity decreases.

Demand Theory

The demand for a good or service is generally driven by two factors:

-utility and ability to pay for the good or service.

The two aspects coincide with one another. Demand happens when a good or service yields some level of utility while being backed by the ability, which ultimately provides satisfaction to the consumer.

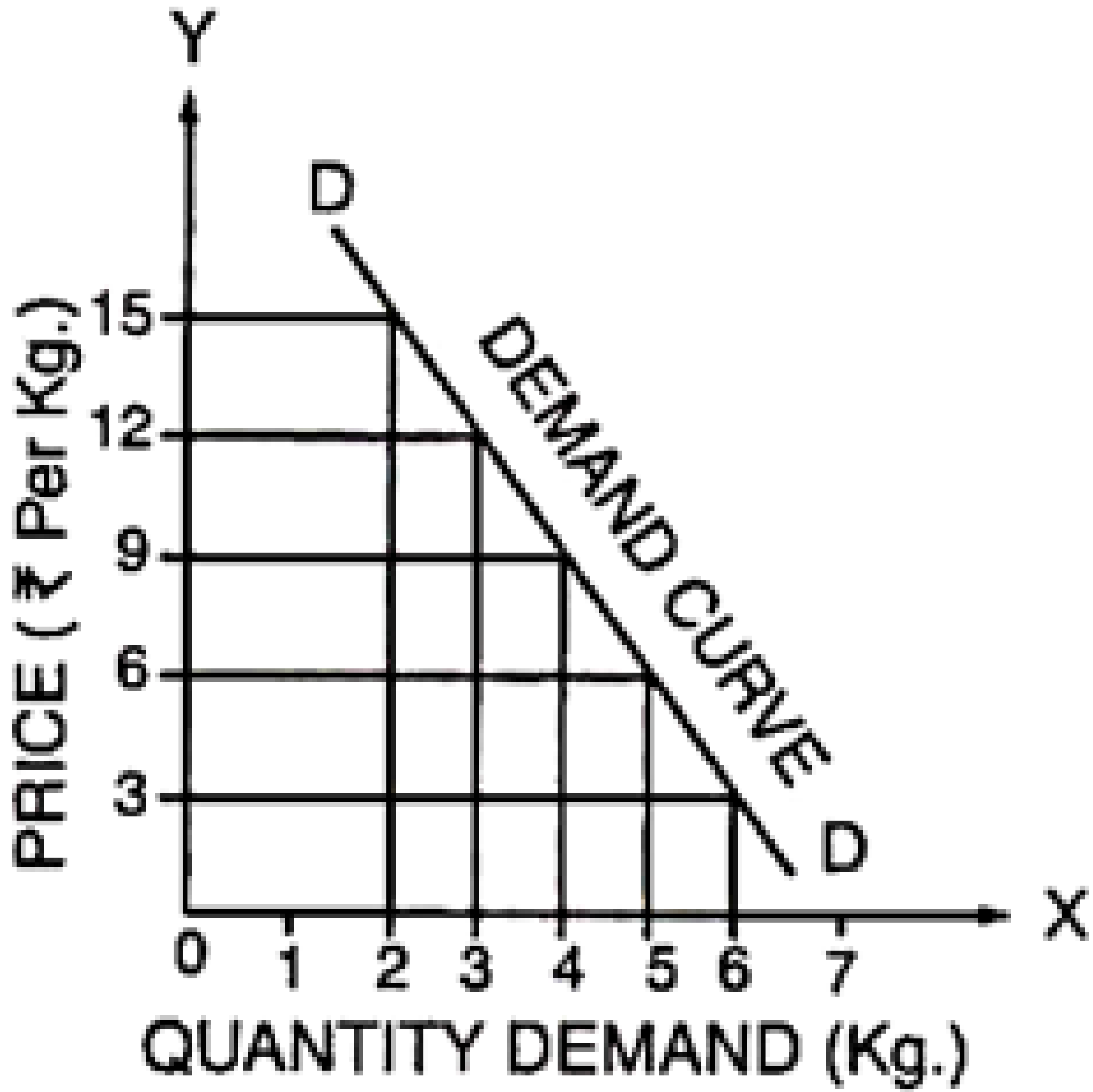

Y
D
DEMAND CURVE
D
X
PRICE (₹ Per Kg.)
15
12
9
6
3
0
1
2
3
4
5
6
7
QUANTITY DEMAND (Kg.)

Fig. 7·1

Factors That Affect Demand

- ❑ Consumer Preferences
- ❑ Taste
- ❑ Choices
- ❑ Income
- ❑ Related Goods or Substitute Goods

Exceptions to Law of Demand

1. Giffen Goods:

Giffen goods are the inferior goods whose demand increases with the increase in their prices. There are several inferior commodities, much cheaper than the superior substitutes often consumed by poor households as an essential commodity.

Whenever the price of the Giffen goods increases its quantity demanded also increases because, with an increase in the price, and the income remains the same, the poor people cut the consumption of superior substitute and buy more quantities of Giffen goods to meet their basic needs.

Exceptions to Law of Demand

2. Veblen Goods:

Another exception to the law of demand is given by the economist Thorstein Veblen, who proposed the concept of "Conspicuous Consumption." According to Veblen, there are a certain group of people who measure the utility of the commodity purely by its price, which means, they think that higher-priced goods and services derive more utility than the lesser-priced commodities.

For example, goods like a diamond, platinum, ruby, etc. are bought by the upper echelons of the society (rich class) for whom the higher the price of these goods, the higher is the prestige value and ultimately the higher is the utility or desirability of them.

Exceptions to Law of Demand

3. The expectation of Price Change in Future:

When the consumer expects that the price of a commodity is likely to further increase in the future, then he will buy more of it despite its increased price in order to escape himself from the pinch of a much higher price in the future.

On the other hand, if the consumer expects the price of the commodity to further fall in the future, then he will likely postpone his purchase despite less price of the commodity in order to avail the benefits of much lower prices in the future.

Exceptions to Law of Demand

4. Ignorance: Often people are misconceived as high-priced commodities are better than the low-priced commodities and rest their purchase decision on such a notion. They buy those commodities whose prices are relatively higher than the substitutes.

5. Emergencies: During emergencies such as war, natural calamity- flood, drought, earthquake, etc., the law of demand becomes ineffective. In such situations, people often fear the shortage of essentials and hence demand more goods and services even at higher prices.

Exceptions to Law of Demand

6. Change in fashion and Tastes & Preferences: The change in fashion trends and tastes and preferences of the consumers negates the effect of the law of demand. The consumer tends to buy those commodities which are very much 'in' in the market even at higher prices.

7. Conspicuous Necessities: There are certain commodities that have become essentials of modern life. These are the goods which consumer buys irrespective of an increase in the price. For example TV, refrigerator, automobiles, washing machines, air conditioners, etc.

Exceptions to Law of Demand

8. Bandwagon Effect: This is the most common type of exception to the law of demand wherein the consumer tries to purchase those commodities which are bought by his friends, relatives or neighbors. Here, the person tries to emulate the buying behavior and patterns of the group to which he belongs irrespective of the price of the commodity.

For example, if the majority of group members have smartphones then the consumer will also demand the smartphone even if the prices are high.

EXCEPTIONS TO THE LAW OF DEMAND
1
GIFFEN GOODS
2
ARTICLES OF DISTINCTION GOODS
3
CONSUMERS IGNORANCE
4
SITUATIONS OF CRISIS
5
FUTURE PRICE EXPECTATIONS
GEEKTONIGHT

Demand Curve

A demand curve is a graph that shows the relationship between the price of a good or service and the quantity demanded within a specified time frame.

Demand curves can be used to understand the price-quantity relationship for consumers in a particular market, such as corn or soybeans.

In addition, demand curves are commonly combined with supply curves to determine the equilibrium price and equilibrium quantity of the market.

Demand Curve

Drawing a Demand Curve

The demand curve is based on the demand schedule. The demand schedule shows exactly how many units of a good or service will be purchased at various price points.

Price	Quantity Demanded
$ 10.00	1000
$ 9.00	1200
$ 8.00	1400
$ 7.00	1700
$ 6.00	2000
$ 5.00	2400
$ 4.00	3000
$ 3.00	3700
$ 2.00	4500

Drawing a Demand Curve

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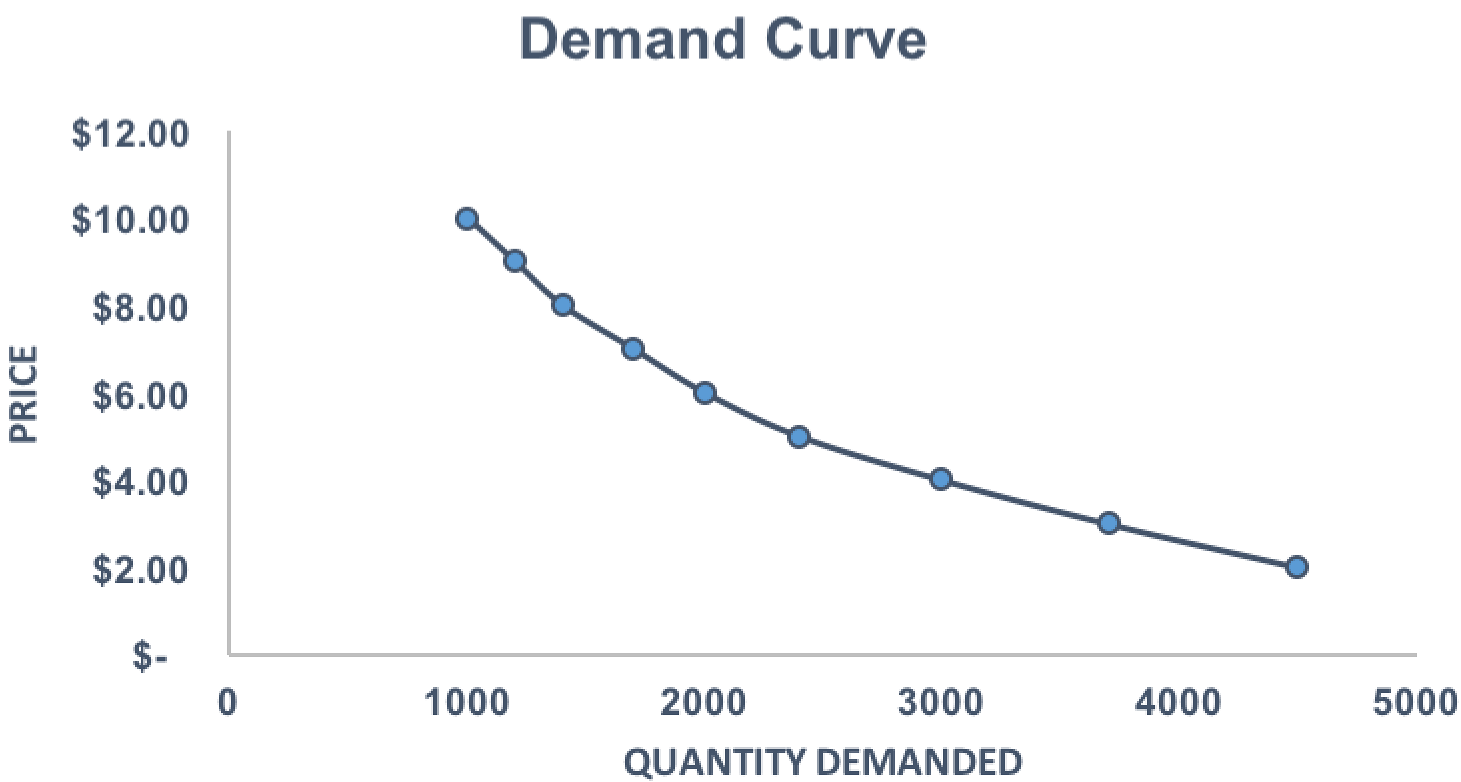


Shifts in the Curve

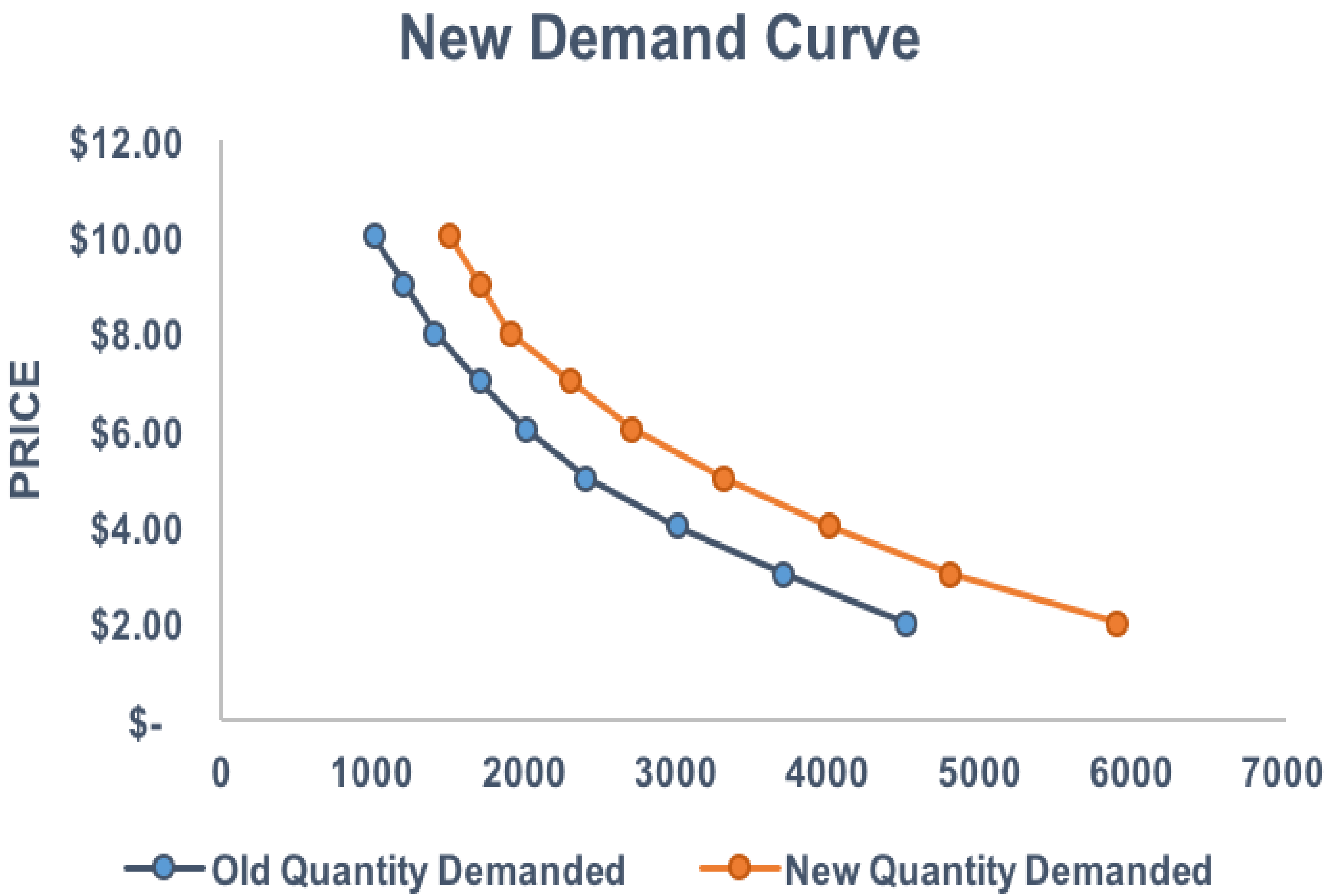
Shifts in the demand curve are strictly affected by consumer interest. Several factors can lead to a shift in the curve, for example:

1. Changes in income levels
2. Changes in the market's size
3. Changes in the price of related goods and services

Shifts in the Curve

Price	Quantity Demanded	New Quantity Demanded
$ 10.00	1000	1500
$ 9.00	1200	1700
$ 8.00	1400	1900
$ 7.00	1700	2300
$ 6.00	2000	2700
$ 5.00	2400	3300
$ 4.00	3000	4000
$ 3.00	3700	4800
$ 2.00	4500	5900

Shifts in the Curve

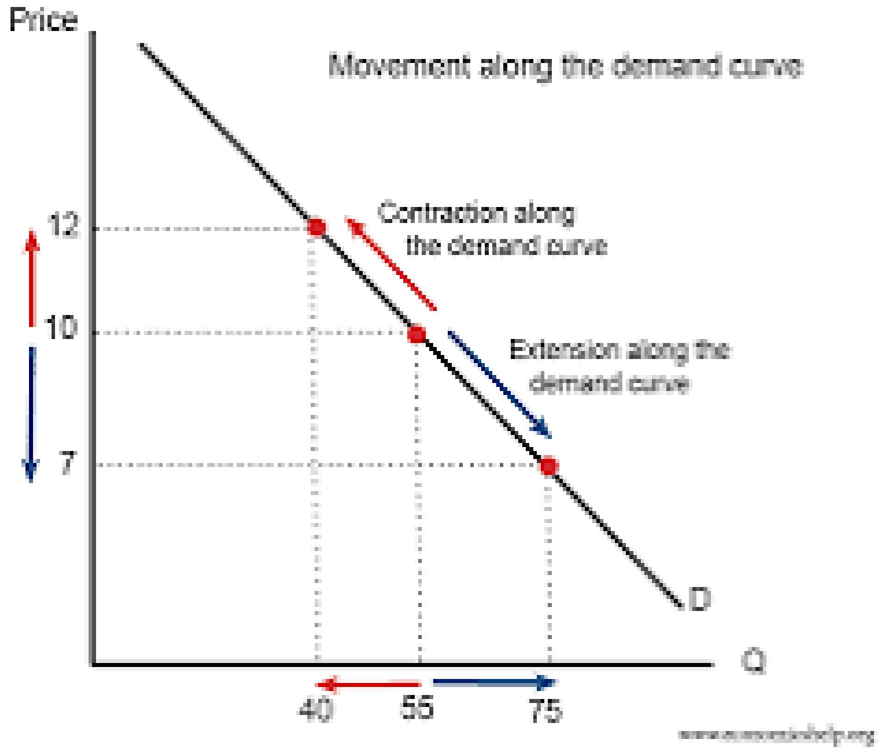


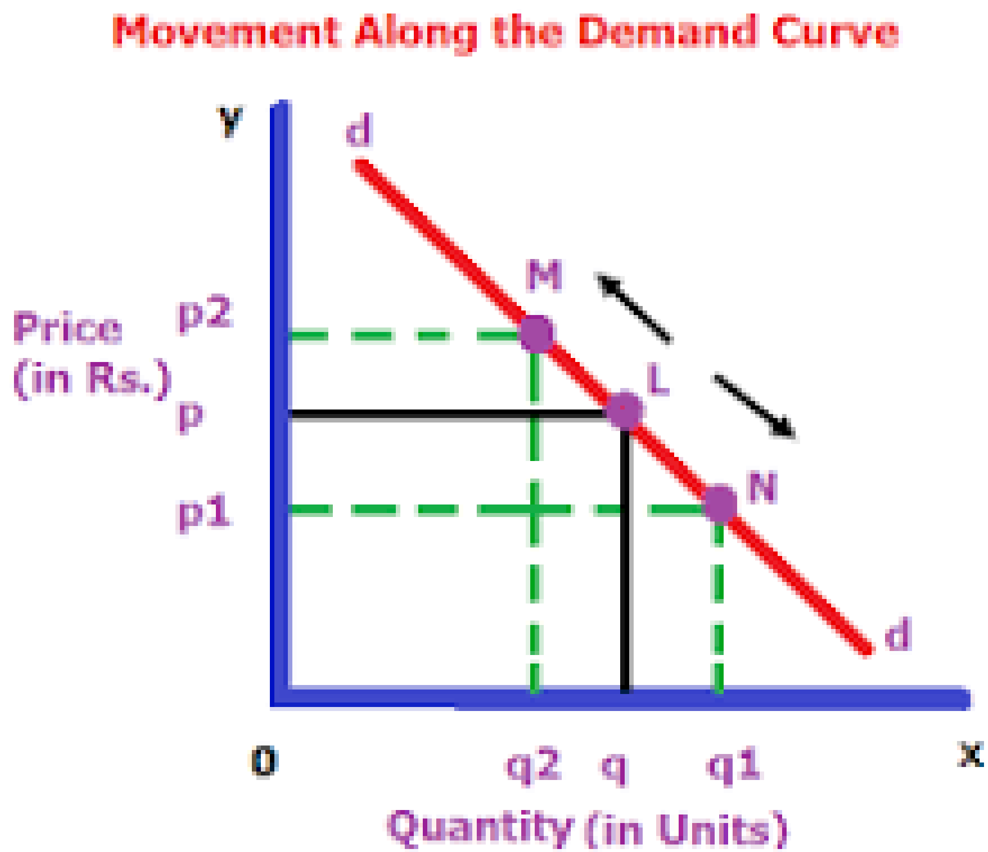
Movement along the Demand Curve

There are two forms of movement in a demand curve: **extension and contraction.**

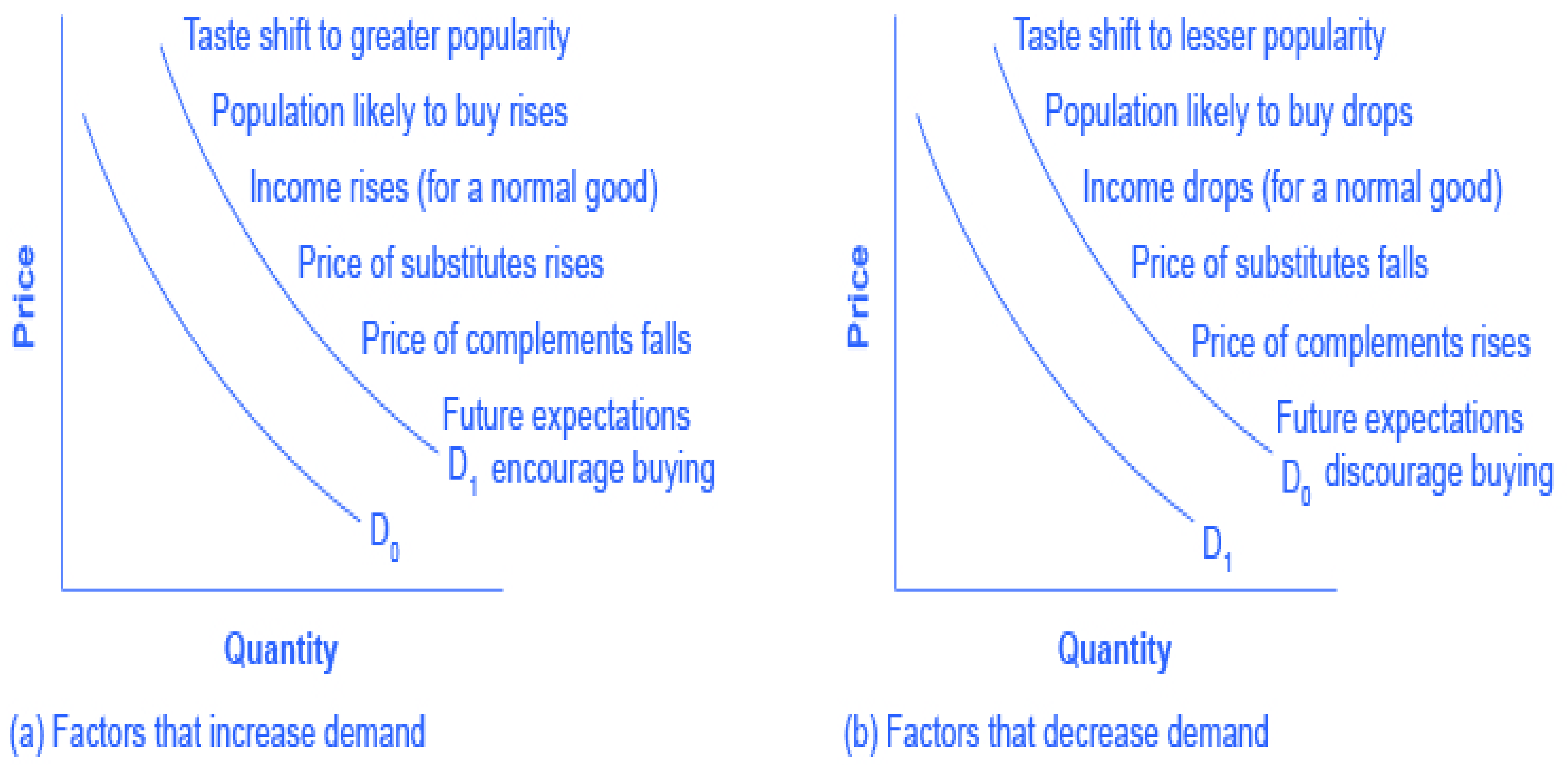
- ✓When the demand for a commodity rises due to a decrease in price, the demand curve extends.
- ✓A contraction in the demand curve occurs when the demand for a commodity diminishes due to a price increase.

Movement along the Demand Curve





Movement along the Demand Curve



Movement along the Demand Curve