The Demand Curve

Kumar Nitin

Demand or Desire

Suppose you wish to purchase a brand new laptop with only Rs. 1000 in your pocket, do you think you are creating demand for laptops in the market, and will any seller be ready to sell a laptop at your desired price?

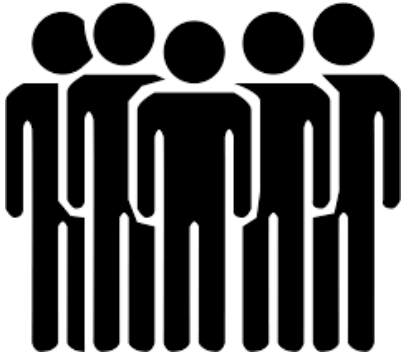
Demand

Demand refers to that quantity of a commodity that a consumer is **willing** and **able** to purchase at various **prices** and particular period of **time**.

Types

Individual Demand

Market Demand



Market Demand

Individual demand refers to that quantity of a commodity that a consumer is **willing** and **able** to purchase at various **prices** and particular period of **time**.

Market demand refers to that quantity of a commodity that all the consumers are **willing** and **able** to purchase at various **prices** and particular period of **time**.

What factors can lead to a change in demand for tea?

Factors determining individual demand for a product

Factors determining Individual demand for a product

Price of the commodity

Factors determining Individual demand for a product

Price of the commodity

Price of related or other goods

Factors determining Individual demand for a product

Price of the commodity

Income of the consumer

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Factors determining Individual demand for a product

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Taste and Preferences

Factors determining Individual demand for a product

Price of the commodity

Income of the consumer

Consumer expectation

Price of related or other goods

Taste and Preferences

Price of the commodity

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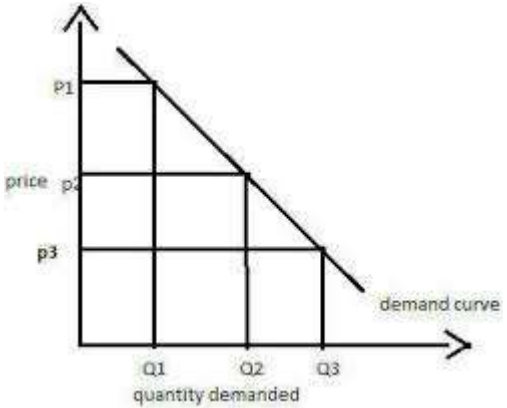
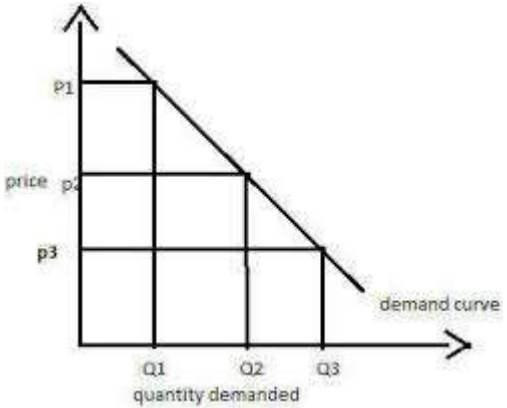
What happens to the demand of tea as its price changes?

Price of the commodity



As P increases, Q decreases

Price of the commodity



Inverse relation between price and demand of the commodity

Price of related goods

Price of related goods

Complementary Goods

Price of related goods

Complementary Goods

Goods which are used together

Price of related goods

Complementary Goods

Goods which are used together

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Goods which are used together

Substitute Goods

Price of related goods

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Goods which are used in place of one another.

Price of related goods

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Goods which are used in place of one another.

Complementary Goods

What happens to the demand for tea as the price the sugar changes?

Relation

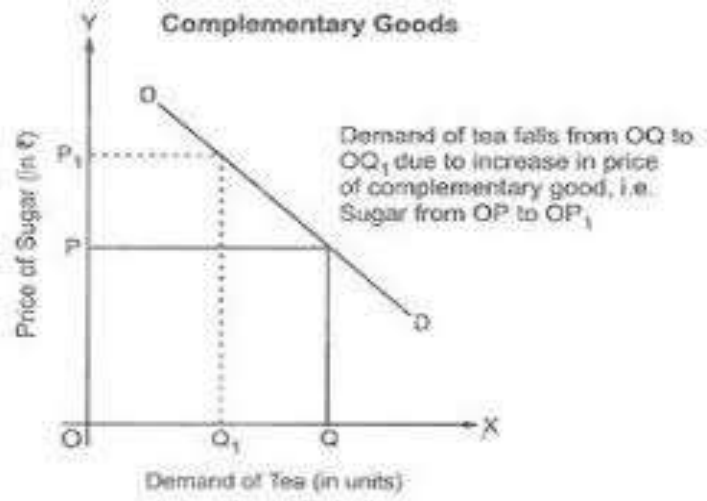


Fig. 3.11

Relation

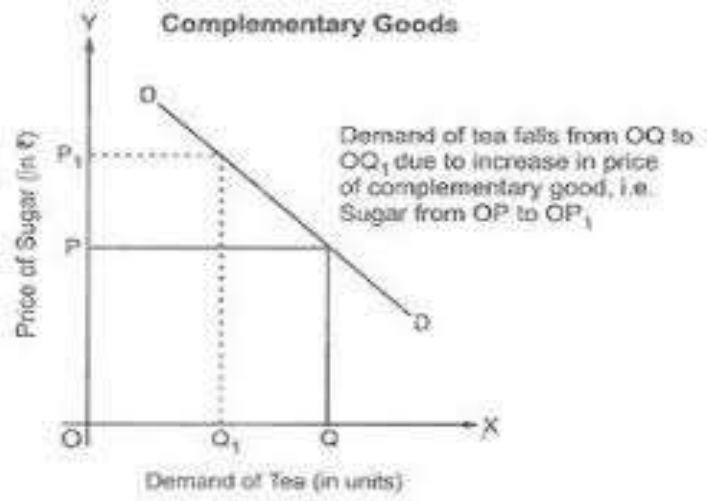
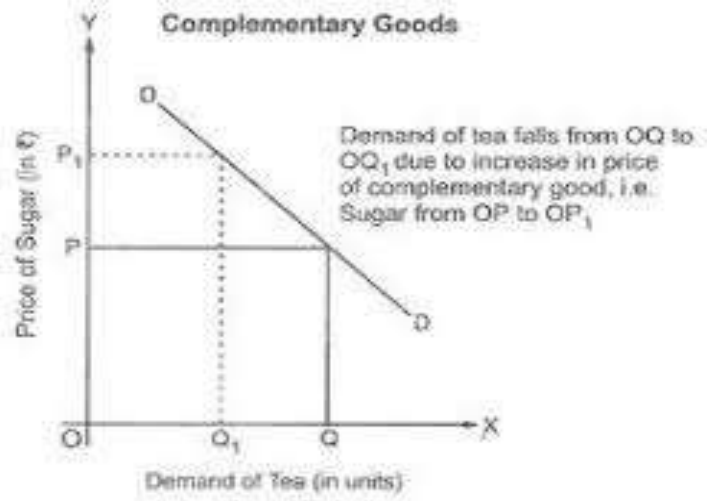


Fig. 3.11

Price of sugar increases

Relation



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Price of sugar increases

It would be relatively costly to use both the goods together

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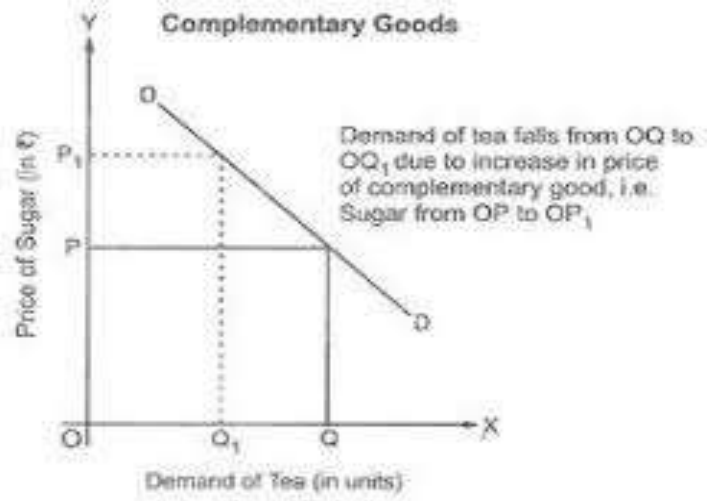

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It would be relatively costly to use both the goods together

Demand for tea would decrease

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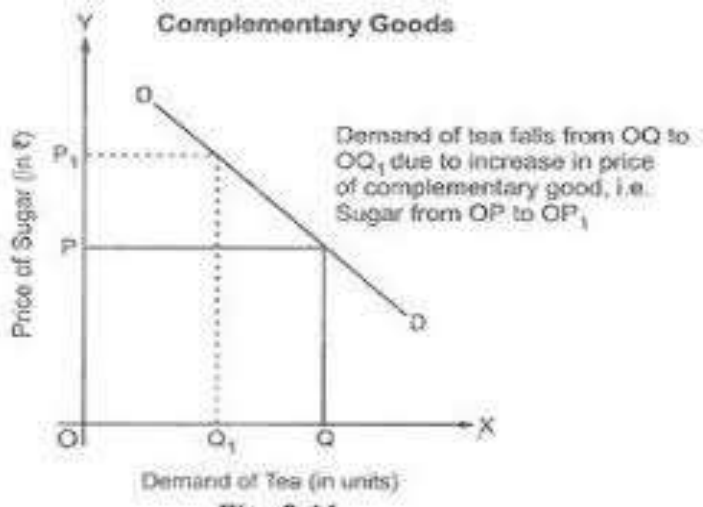

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Price of sugar increases

It would be relatively costly to use both the goods together

Demand for tea would decrease

Inverse relation between price of the commodity and demand of its complementary good

Substitute Goods

What happens to the demand for tea as the price the coffee changes?

Relation

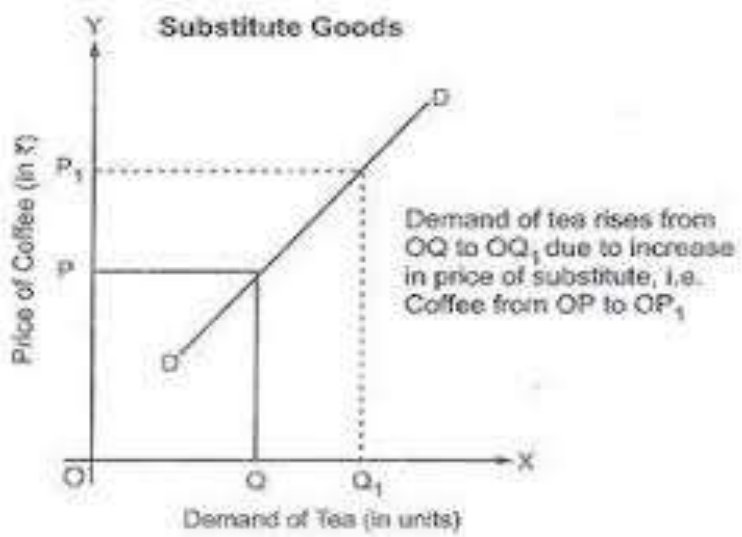


Fig. 3.10

Relation

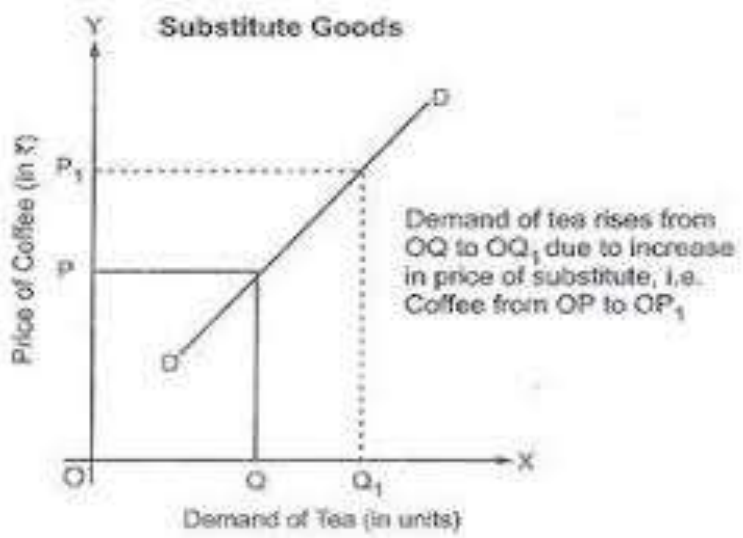
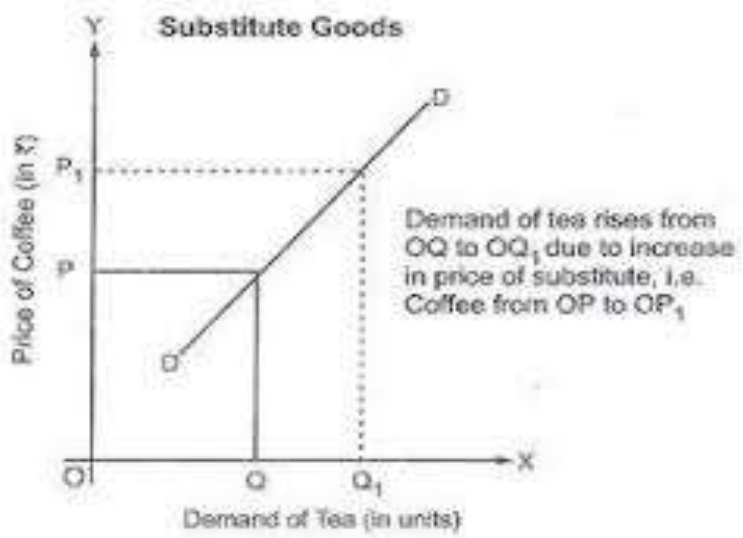


Fig. 3.10

Price of Coffee increases

Relation



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Price of Coffee increases

Tea becomes relatively cheaper

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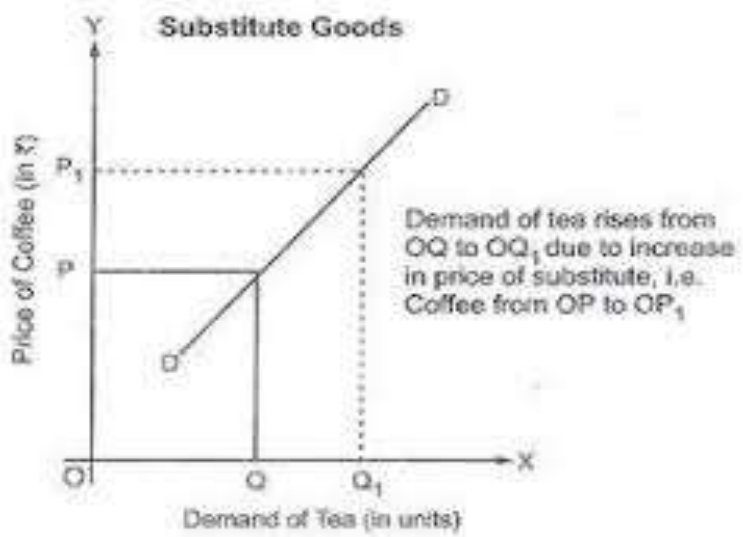

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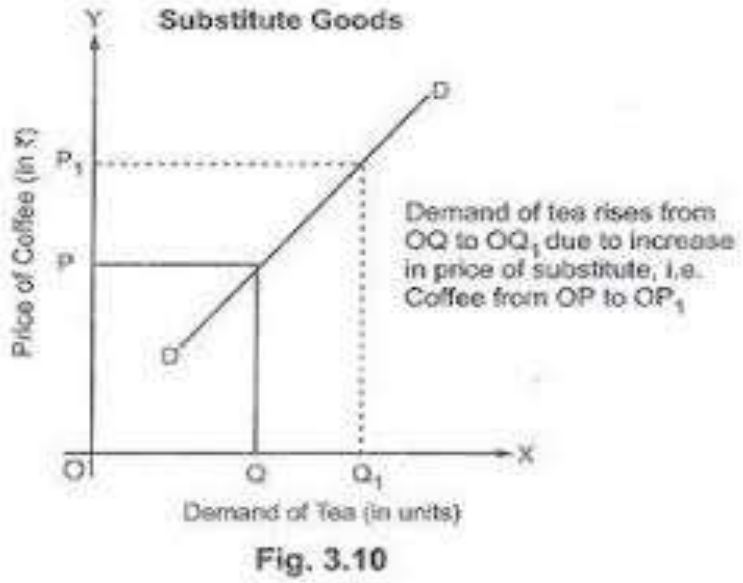


Fig. 3.10

Price of Coffee increases

Tea becomes relatively cheaper

Demand for tea increases

Direct relation between the Price of the commodity and demand of its substitute good.

Income of the consumer

Income of the consumer

Inferior Goods

Income of the consumer

Inferior Goods

Normal Goods

Inferior Goods

As income increases the demand decreases. eg.

Inferior Goods

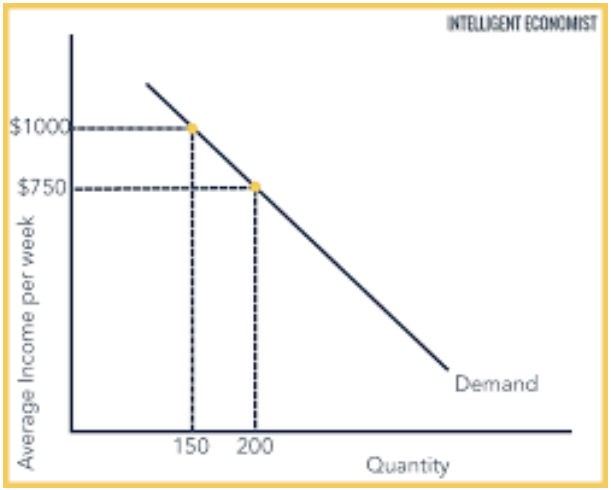
Inferior Goods

Income increases

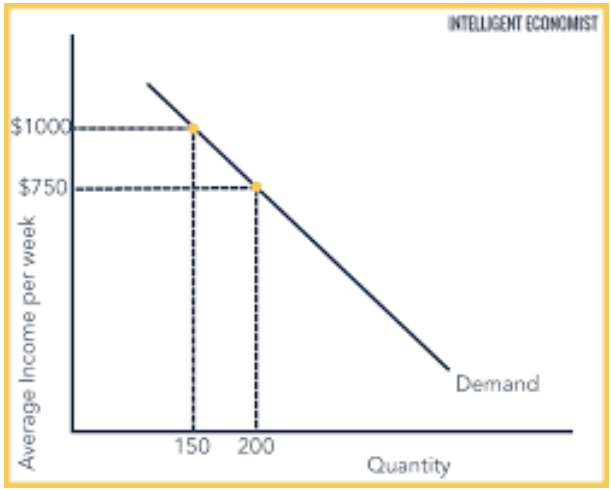
Demand decreases

Income decreases

Demand increases

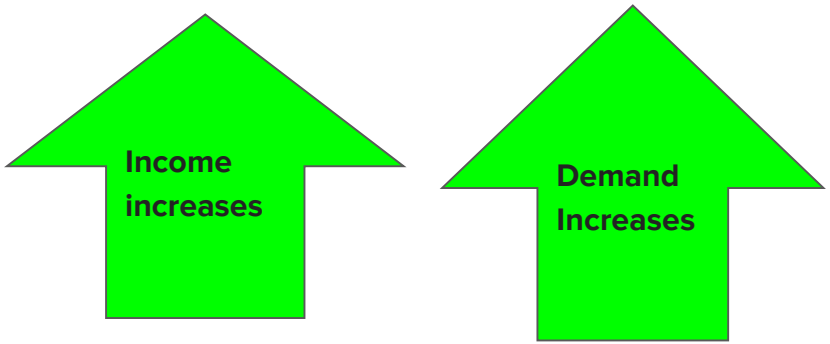


Inferior Goods

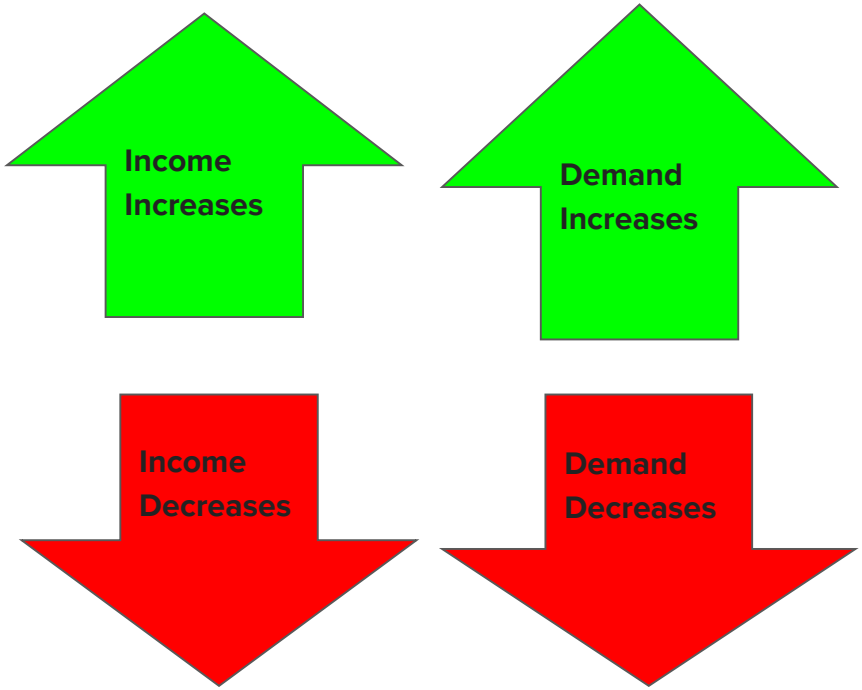


Inverse relation between income of the consumer and demand for inferior goods

Normal Goods



Normal Goods



Normal Goods

Income Increases

Demand Increases

Income Decreases

Demand Decreases

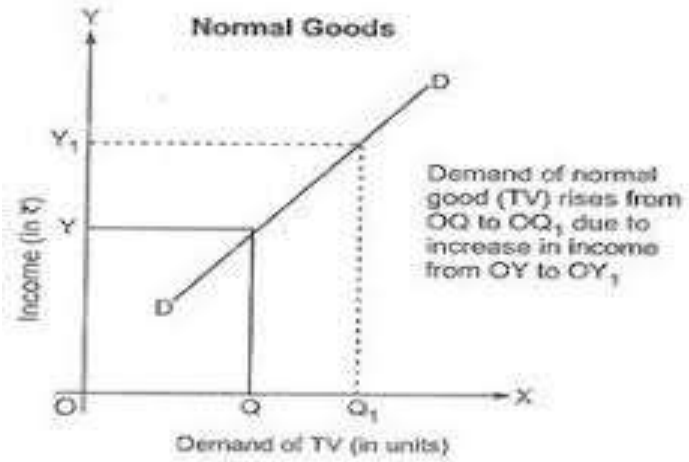


Fig. 3.16

Normal Goods

Income Increases

Demand Increases

Income Decreases

Demand Decreases

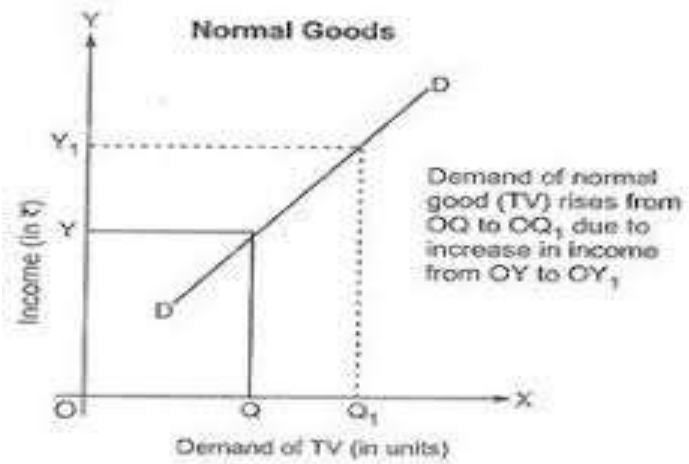


Fig. 3.16

Direct relation between the income of the consumer and the demand for normal goods

Taste and Preferences

Taste and Preferences

Organic in demand

Taste and Preferences

Organic in demand

Fashion

Taste and Preferences

If there is a favourable change in the taste and preferences then the demand for those products would increase

Taste and Preferences

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If there is a unfavourable change in the taste and preferences then the demand for those products would decrease

Future Expectation of Price

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How would a customer react if the government announces that the price of petrol is to rise tomorrow?

Future Expectation of Price

A long queue at the petrol pump

Future Expectation of Price

A long queue at the petrol pump

If it is expected that the price of the product is about to rise in future then the demand for the product would rise today.

Future Expectation of Price

A long queue at the petrol pump

On the contrary, if the price of the product is to fall in future then we would demand less of it today.

Does market demand also depend on the same factors as individual demand?

Determinants of Market Demand

In addition to the determinants that we have studied
Price of the product
Price of related goods - substitute and complementary
Income of the consumer - inferior and normal
Taste and preferences of the consumer
Future expectation of the price

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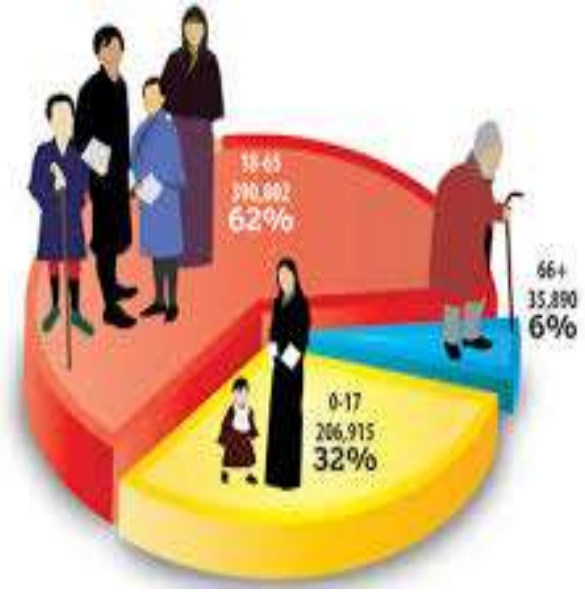
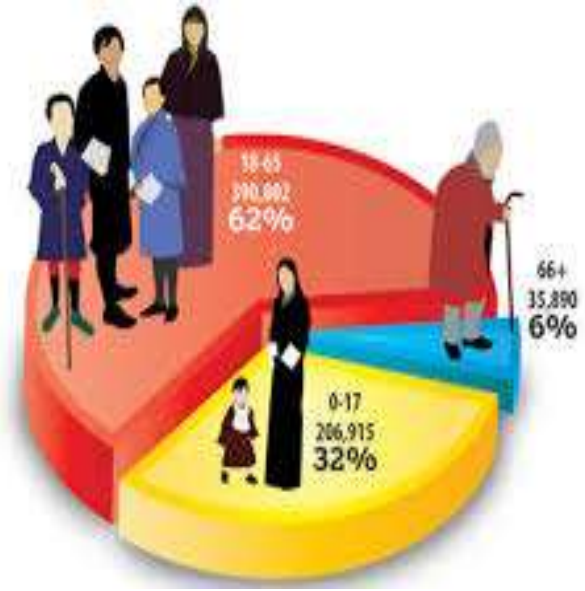
Size and composition of the population
Season and weather
Distribution of income

Size and Composition of the Population

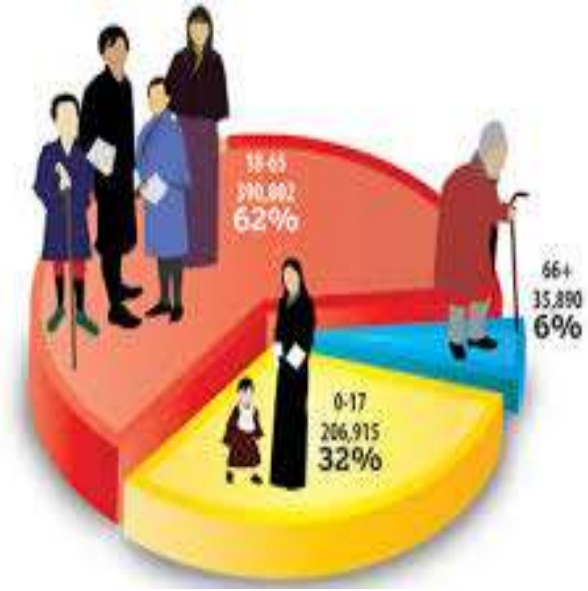


Size and Composition of the Population



If there are more health freaks in the society then the demand for gym and sports club would be high.

Size and Composition of the Population



If there are more health freaks in the society then the demand for gym and sports club would be high.

Similarly if the number of old age people is high in the society the demand for medicine, club houses, and hospitals might increase.

Season and Weather

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As and when the season and weather changes, it affects the demand for the product.

Rainy season - Demand for raincoats and umbrella increases

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Rainy season - Demand for raincoats and umbrella increases

Winter season - Demand for woollen clothes increases

I want to open a showroom of some branded garment, what do you think would be right selection. Will it be Dharavi or Nariman Point?

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Dharavi is the largest slum in Asia

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Dharavi is the largest slum in Asia

Nariman point is one of the posh locality in Mumbai

Distribution of Income

Distribution of Income

Since the income level of people in that slum is low then the market demand for branded clothes would also remain low. **Distribution of income** also plays an important role in determining market demand.

Let us combine the determinants together and establish a relation between demand and its factors.

Demand Function

The functional relation between the demand and the factors influencing it is known as the demand function.

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$$f(x)$$

Demand Function

Individual Demand Function

$$Di = f\{P, Pr, Y, T, O\}$$

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Market Demand Function

$$Dm = f\{P, Pr, Y, T, O, S, N, Po\}$$

Question

State true or false

1. If a fall in the price of good A leads to a rise in demand of good B, then the two goods are substitute goods - True/False

1. Demand for a commodity can change even when its price remains constant. - True/False

1. If a consumer buys more of a commodity as his income increases, then the given commodity is inferior good - True/False

1. Size and composition of the population affects the demand for an individual - True/False

Question

State true or false

1. If a fall in the price of good A leads to a rise in demand of good B, then the two goods are substitute goods - False

1. Demand for a commodity can change even when its price remains constant. - True

1. If a consumer buys more of a commodity as his income increases, then the given commodity is inferior good - False

1. Size and composition of the population affects the demand for an individual - False

Summary

Desire Vs Demand

Individual demand

Market demand

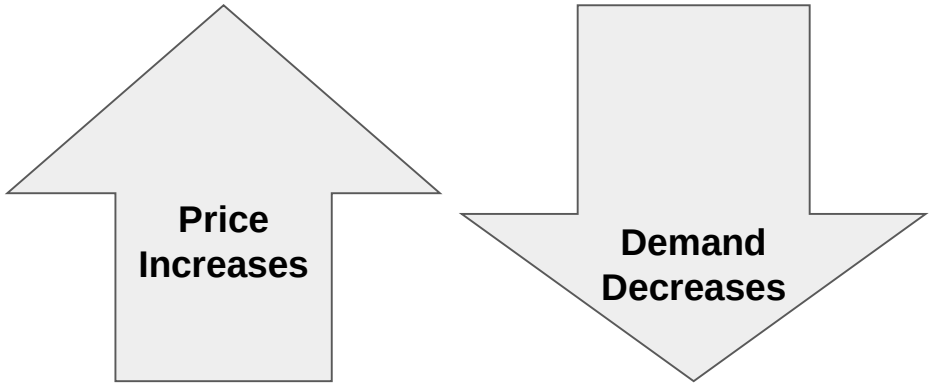
Determinants of individual demand

Determinants of market demand

Demand function

Let us recall

There is an inverse relation between the price of the product and its demand.


Price
Increases
Demand
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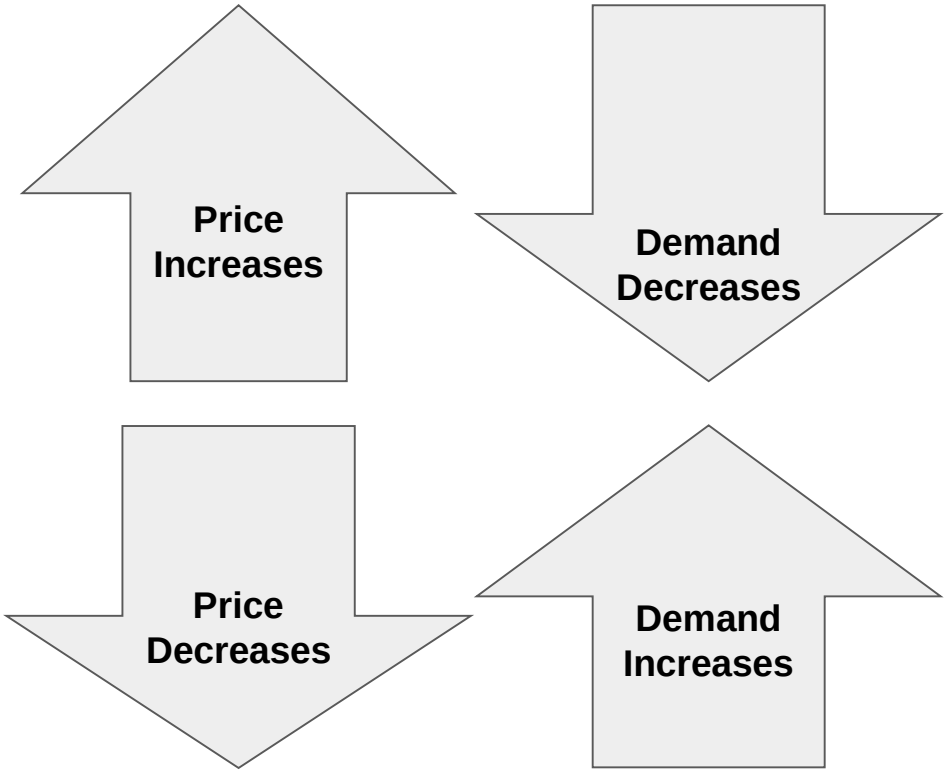
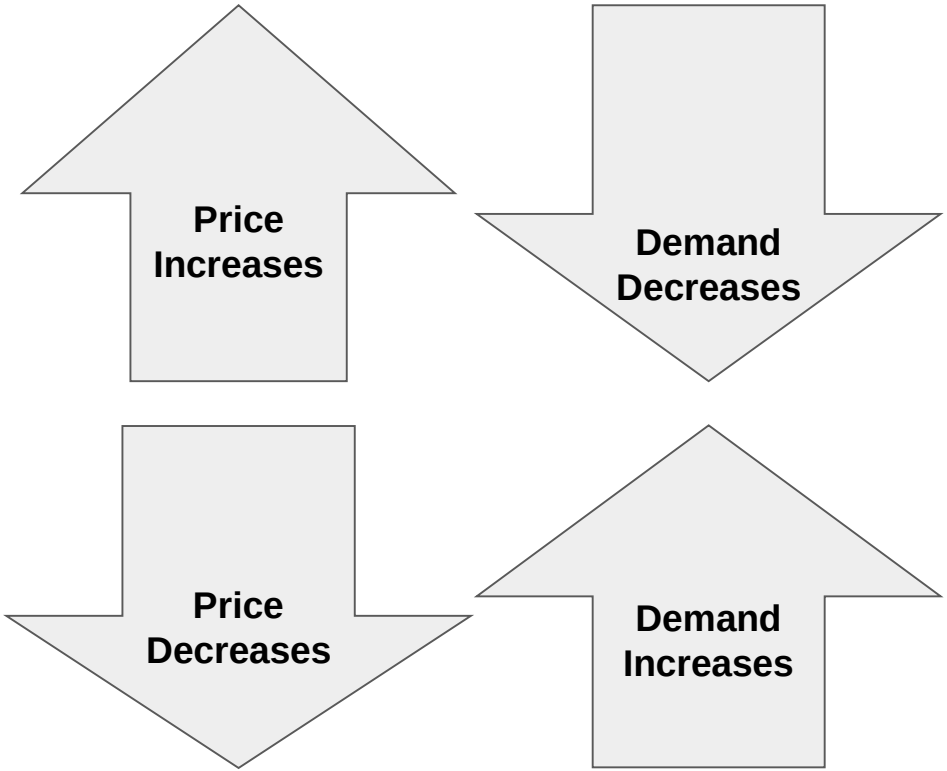

Price Increases
Demand Decreases
Price Decreases
Demand Increases



Such a behaviour of the consumers is formulated as the

Law of Demand

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Ceteris paribus - keeping other factors constant.

What are the Other Factors in the Law of Demand?

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Factors affecting the Individual demand (other than the own price of the commodity):

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Factors affecting the Individual demand (other than the own price of the commodity):

Income of the consumer

Future Expectation of price

Price of related goods

Taste and preferences

Why do we need Ceteris Paribus?

Why do we need Ceteris Paribus?

Have you ever played Tug of War.

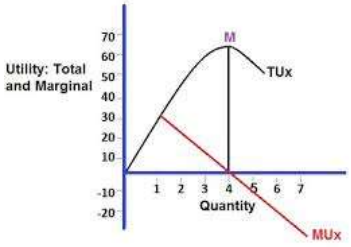
Why do we need Ceteris Paribus?

Why do we need Ceteris Paribus?

To understand the separate influence of one factor, it is necessary, that all the factors are held constant.

So all the other factors influencing demand are held constant while studying the changes in demand due to a change in price.

What are the factors which lead us to this law?



The law of diminishing marginal utility

Substitution effect

Income Effect

Alternative uses

Number of users

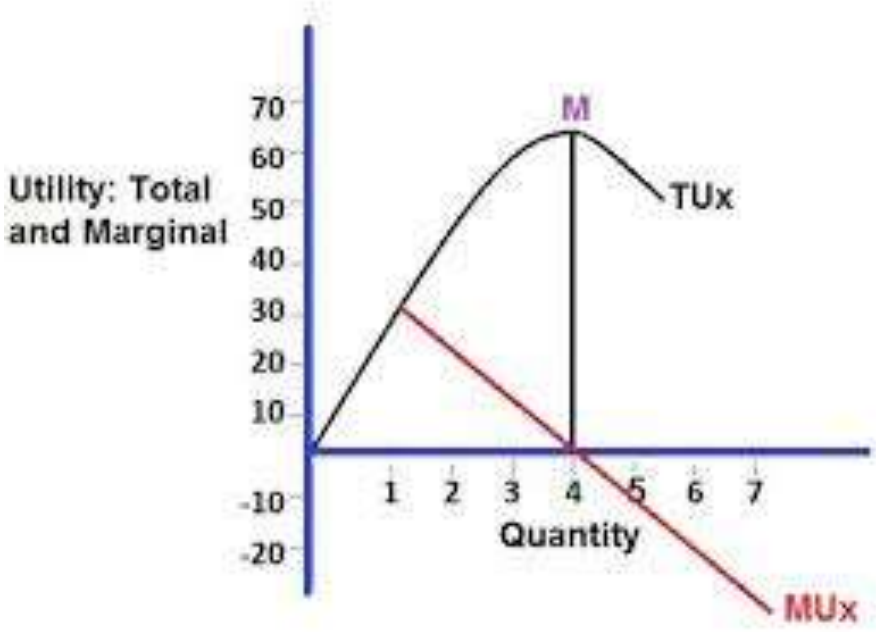
The law of diminishing marginal utility

Let’s Recall

Conditions for the Consumer Equilibrium.

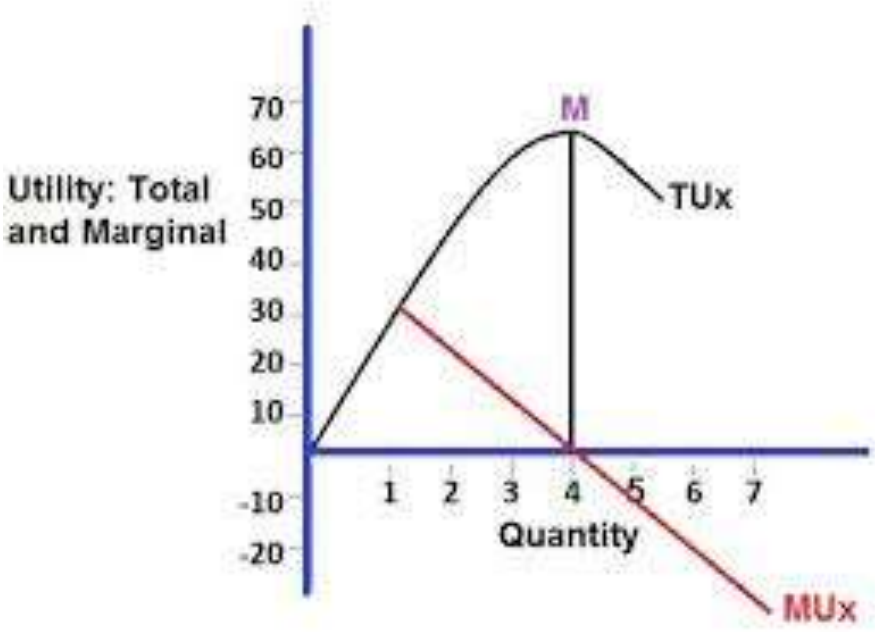
MUx = Px

MUx/Px = MUy/Py



The law of diminishing marginal utility

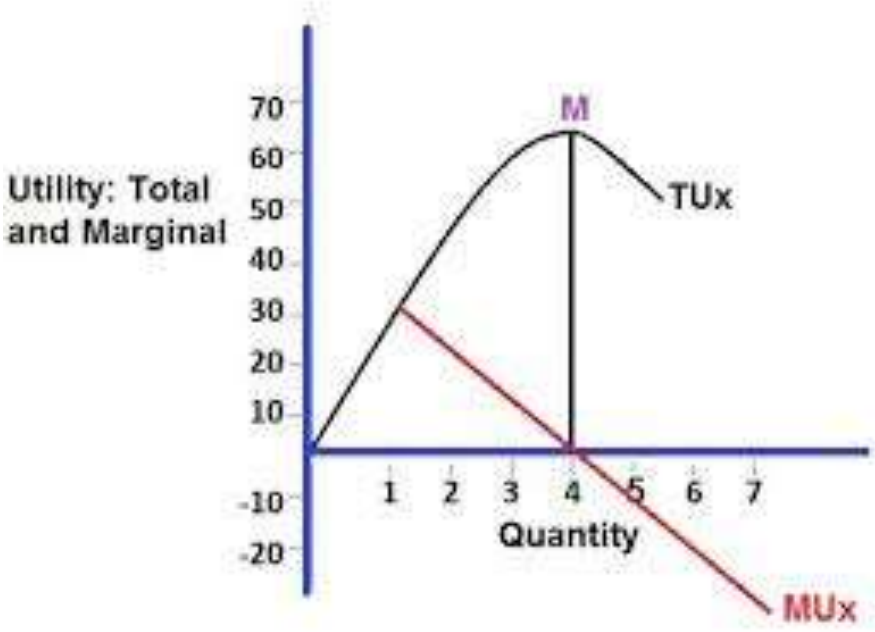
As the price of the commodity falls



The law of diminishing marginal utility

As the price of the commodity falls

Mux > Px



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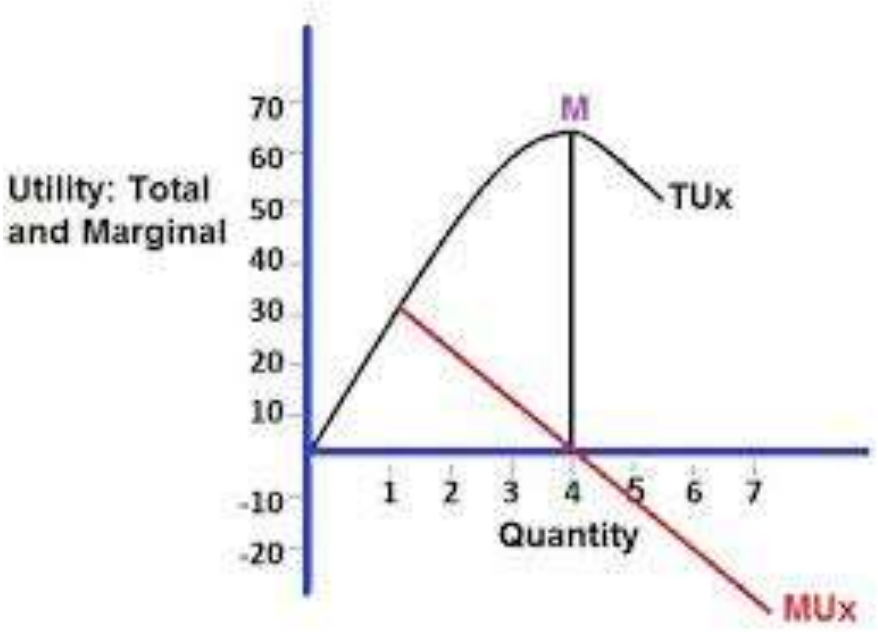
Mux > Px

The customer buys more units of the commodity to attain equilibrium.



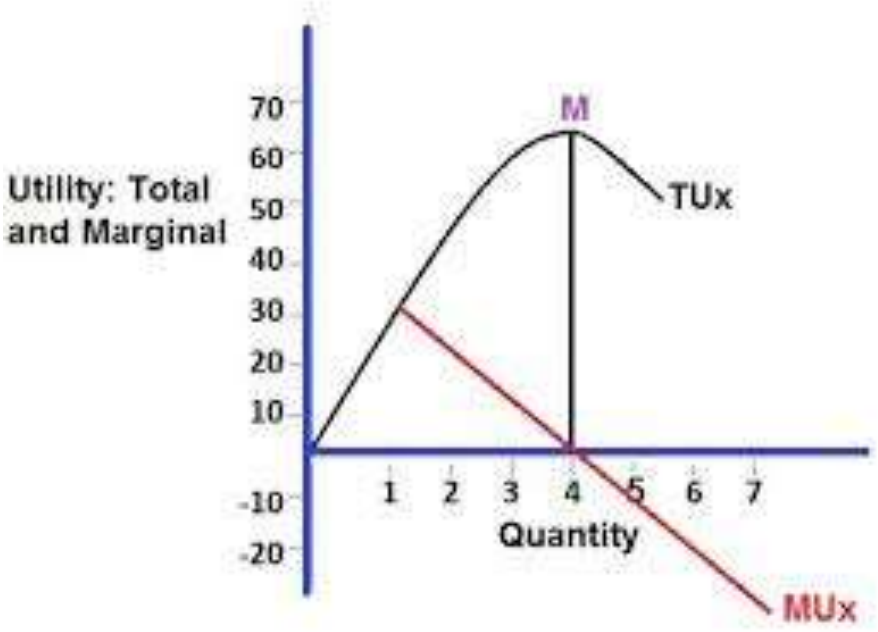
The law of diminishing marginal utility

As the price of the commodity falls

Mux > Px

The customer buys more units of the commodity to attain equilibrium.

Thus demand increases when the price falls.



Substitution effect

If the price of tea falls, with no change in the price of coffee, tea becomes relatively cheaper and will be substituted for coffee.

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Substitution effect refers to substituting one commodity in place of other when it becomes relatively cheaper.

Income Effect

If you buy 4 cups of tea at Rs 20 each with your pocket money spending total Rs 80. The price of tea reduces to Rs 16 per cups, now with Rs 80 you can purchase 5 cups of tea.

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This is because your **real income** has increased or say your **purchasing power** has increased.

Income Effect

Income effect refers to effect on demand when the real income of the buyer changes due to change in the price of the given commodity.

Alternative uses

Commodities like milk or electricity have several uses. When the price of such goods increases its use gets restricted to the most important uses.

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If milk becomes expensive then its use gets restricted to drinking and demand for other milk product like paneer and cheese decreases.

Number of Users

As the price of the commodity falls, many new consumers (who were not consuming the commodity) start buying it. And the old consumers demand more due to reduced price. Thus the demand increases at the reduced price.

Does this law hold good for all the goods and in every condition?

No, there are a few situations and conditions in which the Law of demand does not hold good.

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Exceptions to the Law of Demand

Story Time

Sir Robert Giffen

Scottish economist

Price of bread increased

Low wage British workers bought more bread

Main diet was bread and meat

Price of bread and meat both increased

Meat became relatively expensive

To maintain their intake of food, meat consumption was reduced and bread was purchased more even when its price had increased.

Giffen Goods

Veblen good

Diamond

Prestige goods or goods used as status symbol are known as goods of ostentation or **Veblen goods**

Vintage Cars

When the price of such goods increases then they are wanted more by the rich for prestige and distinction disobeying the law of demand

Ignorance

Consumer buys more units of the commodity at a higher price as they are ignorant of the price rise.

Disobeying the law of demand

Necessities of Life

Goods like food grains, milk, life saving drugs are purchased even when their price has increased. It is because of their necessity for the survival of human.

Future Expectation of Price

Suppose that the price of the product went up from Rs. 10 to Rs. 15 per unit and it is expected that the price would rise further.

Then will the demand for the product rise at the increased price of Rs. 15?

It is expected that the demand would rise further even the increased price of Rs 15 will induce customers to buy more at the increased price of Rs 15.

Fashion Related Goods and Services

Fashion items are the one which are least affected by the price rise. People tend to buy the fashion related goods even when the price rises.

Fear of shortage of goods

Suppose the plantation of tomato failed in India this year and there is a shortage of tomatoes.

Still at the increased price people will demand more tomatoes as they expect that the product might not be available for purchase in future.

This law does not explain...

This law does not explain...

By how much does the demand change with increase in price? (Only Qualitative Relation, no Quantitative Relation)

This law does not explain...

By how much does the demand change with increase in price? (Only Qualitative Relation, no Quantitative Relation)

What if the demand of the commodity increases, what would happen to the price? (One sided Relation)

What do you what would happen if the inverse relation between the price and demand is put in the form of a schedule?

What do you what would happen if the inverse relation between the price and demand is put in the form of a schedule?

The tabular representation of the inverse relation between price and quantity demanded is known as **demand schedule**.

Individual Demand Schedule

The demand schedule of chocolates for Jigyasa	
Price (Rupees)	**Demand**
2	200
4	150
8	75
14	25
20	10

What would be the market demand schedule?

Market Demand Schedule

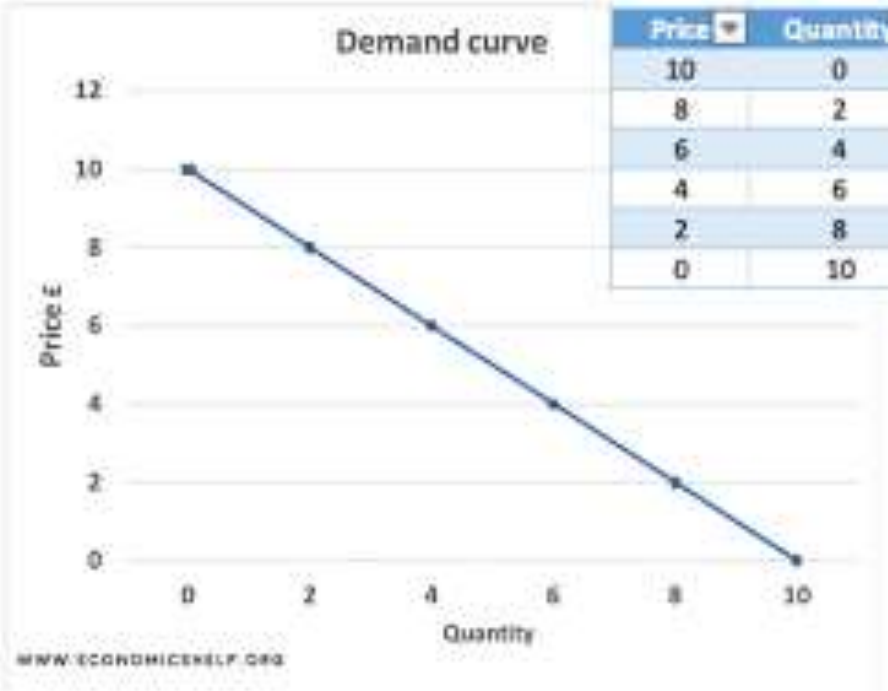
The market demand for chocolates by Jigyasa, Ritika, and Manisha				
Price(Rupees)	**Demand by Jigyasa**	**Demand by Ritika**	**Demand by Manisha**	**Market Demand**
2	200	150	210	
4	150	100	180	
8	75	40	120	
14	25	20	30	
20	10	10	6	

What do you think would be the shape of a demand curve if we plot the schedule we just made?

Demand Curve

The graphical representation of the inverse relation between price and quantity demanded is known as the **demand curve.**

Individual Demand



Price	Quantity
10	0
8	2
6	4
4	6
2	8
0	10

Market Demand Curve

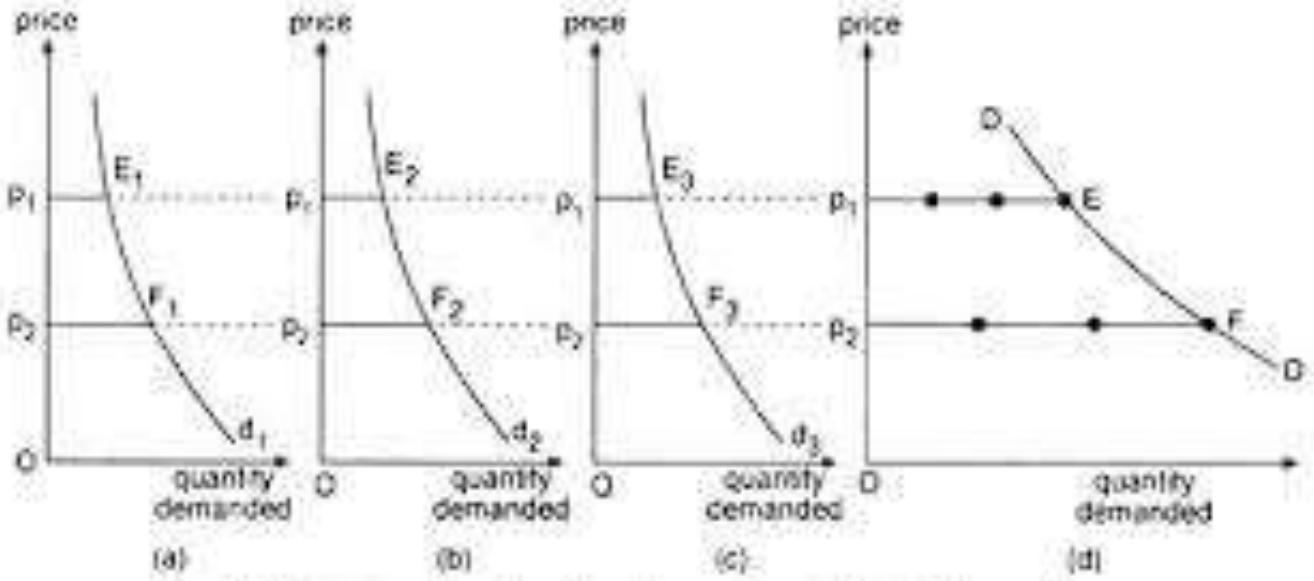
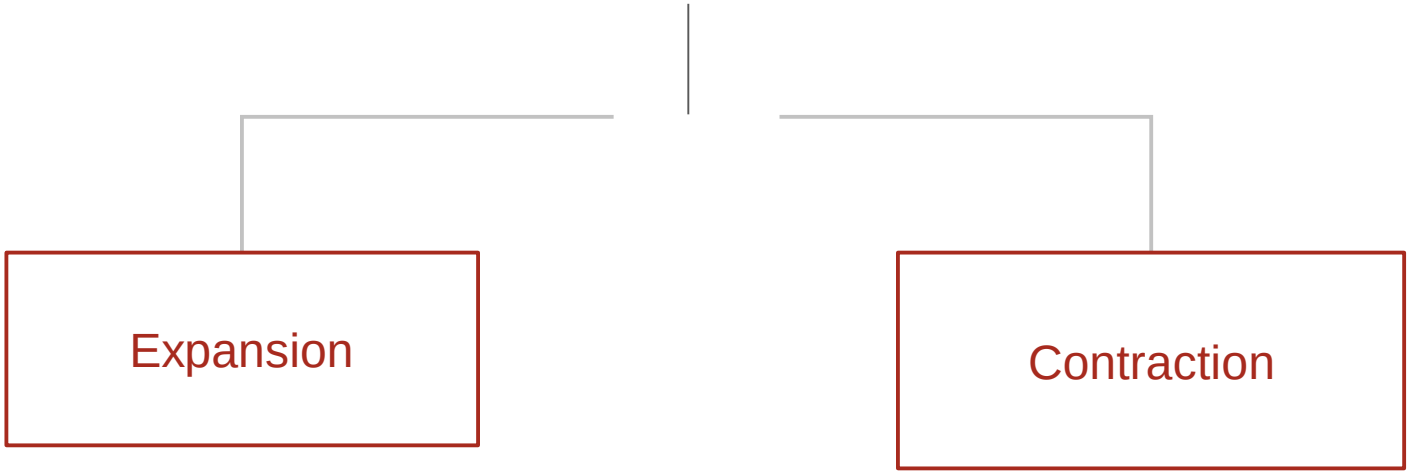


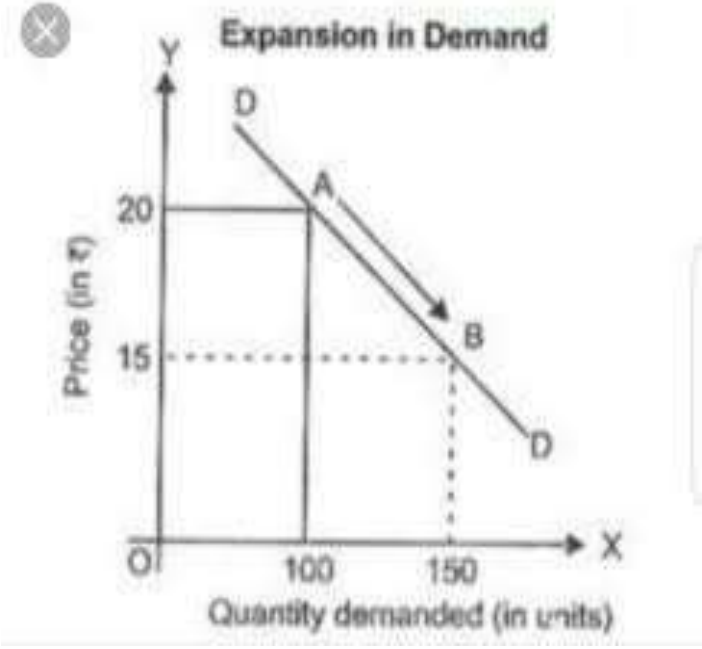
Fig. 1.4 Derivation of market demand curve from individual demand curves

What do you call it when the consumer moves up and down on the same demand curve due to change in the price of the product?

Change in Quantity Demanded
OR
Movement Along the Demand Curve



Expansion



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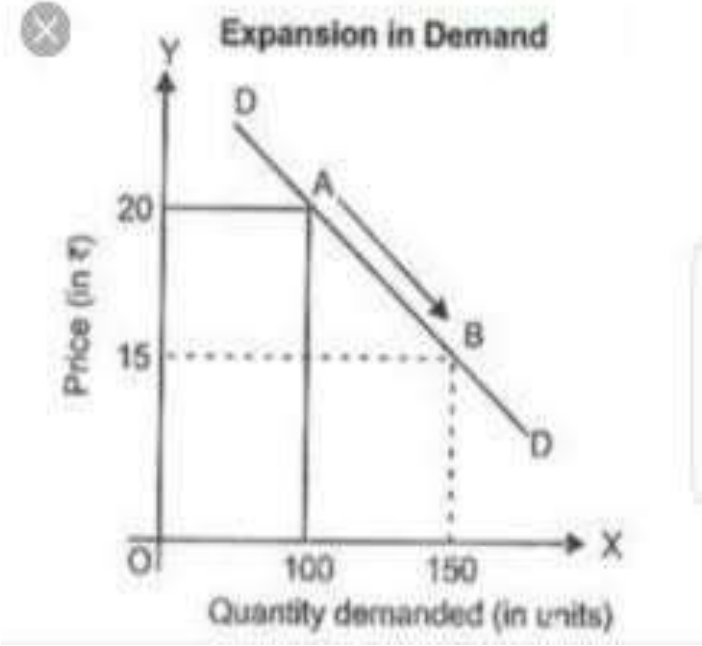
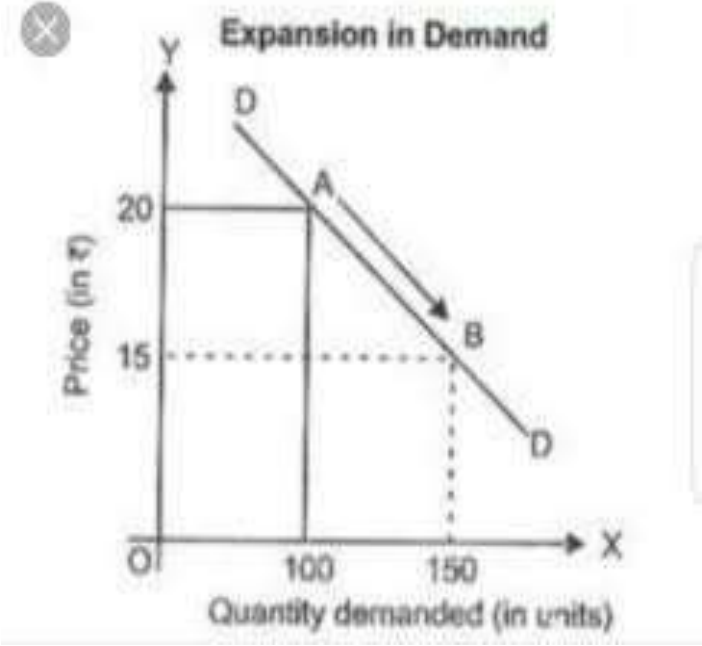


Cause - **Decrease in price**

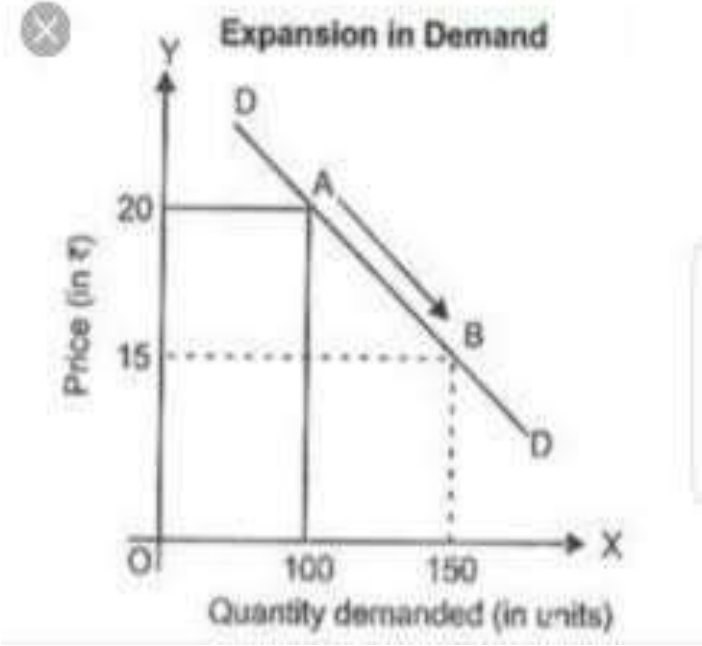
Expansion



Cause - **Decrease in price**

Effect on the Demand Curve - **Move down on the same demand curve**

Expansion



Cause - **Decrease in price**

Effect on the Demand Curve - **Move down on the same demand curve**

Alternative Name - **Downward movement along the demand curve**

Contraction

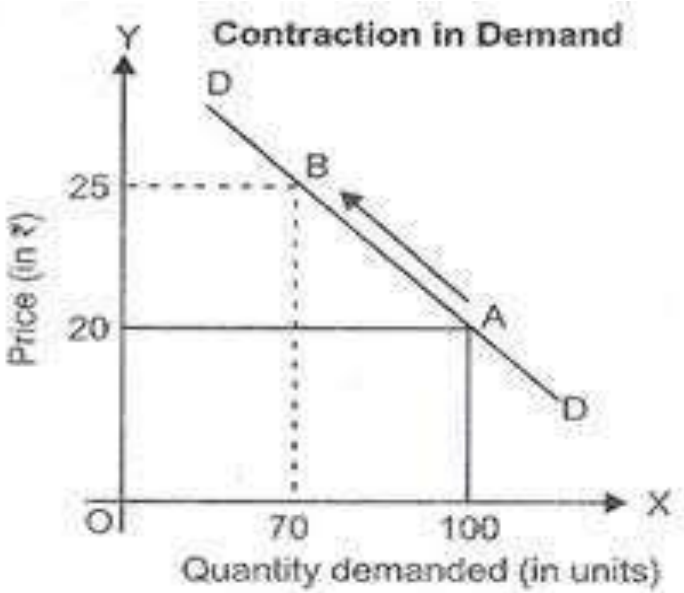


Fig. 3.6

The demand schedule of chocolates for Jigyasa	
Price (Rupees)	**Demand**
2	200
4	150
8	75
14	25
20	10

Contraction

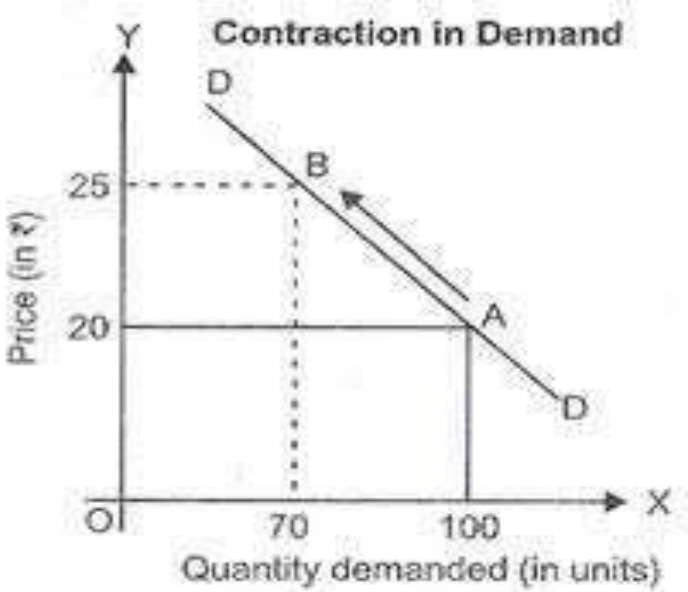


Fig. 3.6

Cause - **Increase in Price**

Contraction

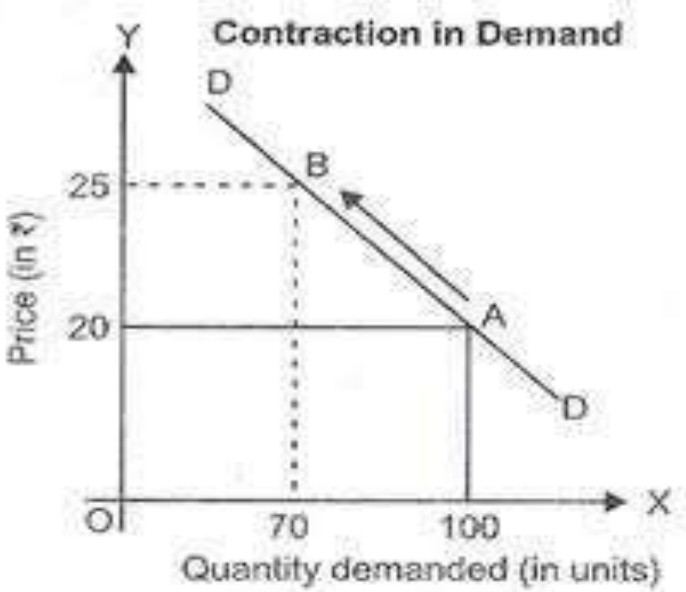


Fig. 3.6

Cause - **Increase in Price**

Effect on the Demand Curve - **Move up on the demand curve**

Contraction

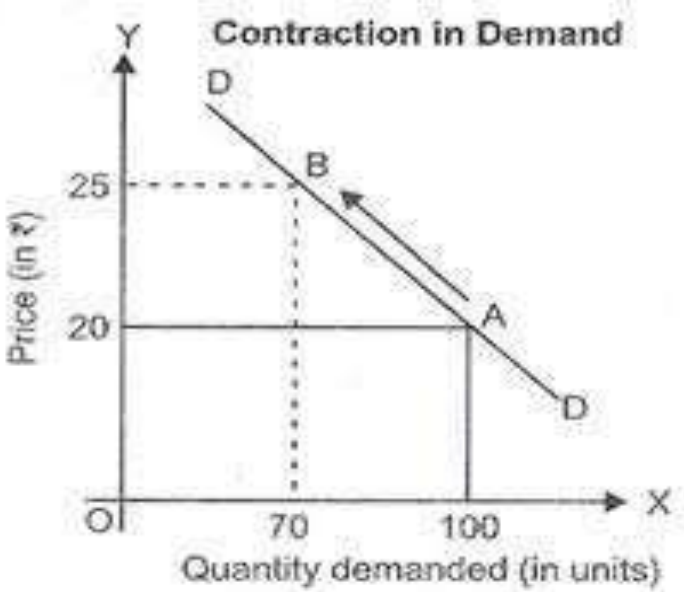


Fig. 3.6

Cause - **Increase in Price**

Effect on the Demand Curve - **Move up on the demand curve**

Alternative Name - **Upward movement along the demand curve**

The factors other the price also lead to a change in demand. How would the demand curve change when the other factors change?

Price for tea is constant

↓

Price of sugar or coffee changes

↓

What will be the impact on the demand curve of tea?

↘

It would result in the shift in the demand curve.

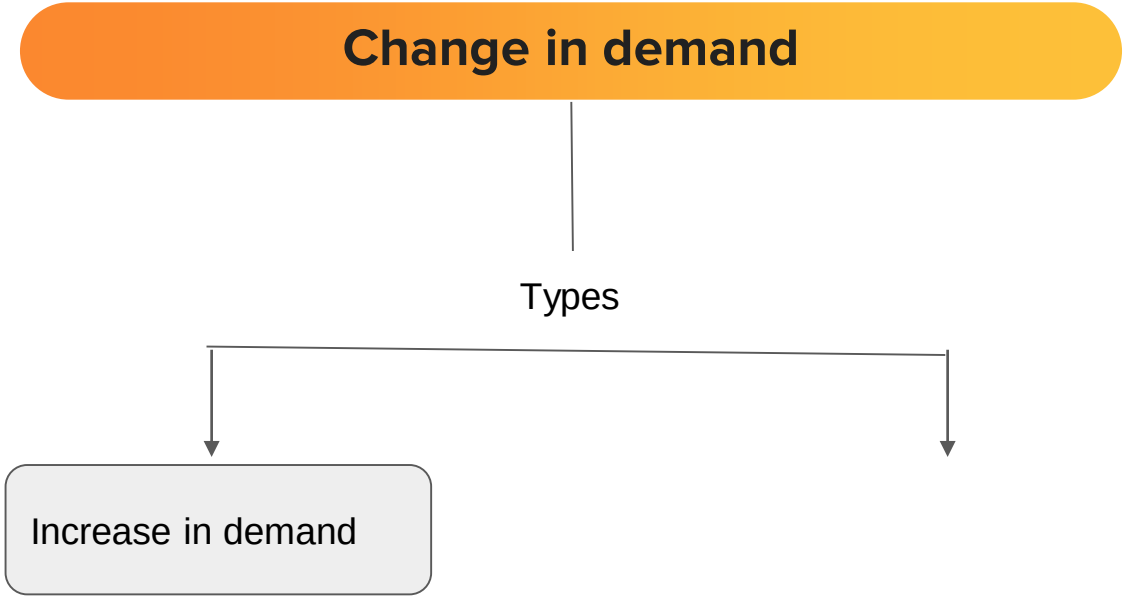
The factors other the price also lead to a change in demand. How would the demand curve change when the other factors change?

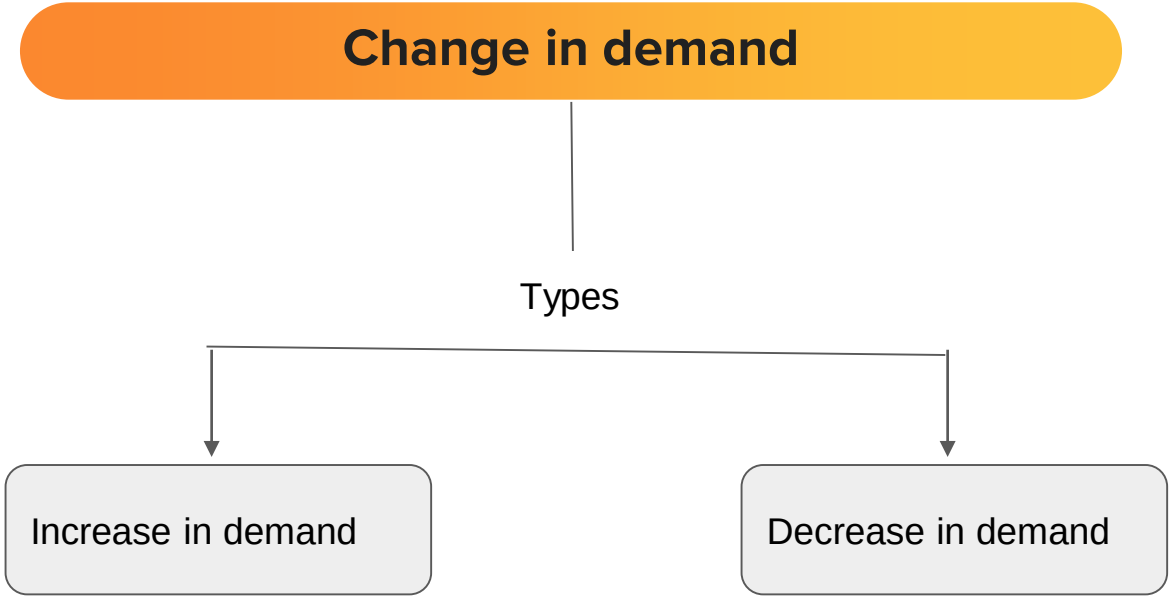
When the demand changes due to factors other than the price of the commodity, it is known as

Change in demand

or

Shift in the demand curve


Change in demand
Types
Increase in demand


Change in demand
Types
Increase in demand
Decrease in demand

Increase in demand

Price remains constant and at the same price more units of the commodity are demanded due to change in factors other than the price.

Increase in demand

Price remains constant and at the same price more units of the commodity are demanded due to change in factors other than the price.

Increase in price of substitute goods
Decrease in the price of the complementary goods
Increase in income in case of normal goods
Decrease in income in case of inferior goods
Increase in population
Favourable change in taste
Future expectation of increase in price

Decrease in demand

Price remains constant and at the same price less units of the commodity are demanded due to change in factors other than the price.

Decrease in demand

Price remains constant and at the same price less units of the commodity are demanded due to change in factors other than the price.

Decrease in price of substitute goods
Increase in the price of the complementary goods
Decrease in income in case of normal goods
Increase in income in case of inferior goods
Decrease in population
Unfavourable change in taste
Future expectation of decrease in price

Question

Q. There are train and plain service between Bangalore and Chennai, the train fares between the to cities come down. How will that affect the demand curve of the plain service between the two cities?

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Q. Ceteris paribus in the law of demand states that the price of the commodity remains constant. (true/false)

Answer. False

Summary Slide

Law of demand -

Reasons for the law of demand

Exceptions to the law of demand -

Demand schedule -

Demand Curve-

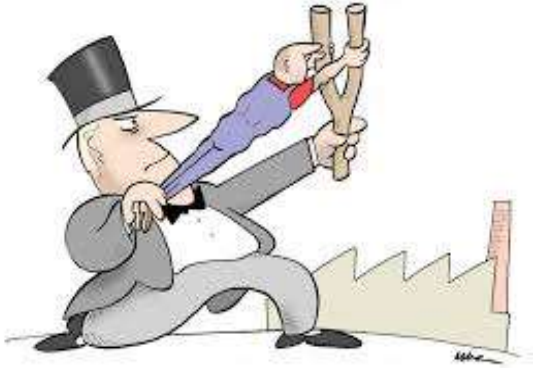
Change in demand - increase or decrease in demand

Change in quantity demanded - expansion or contraction

The law of demand shows the inverse relation between price and quantity demanded keeping other factors constant. But it does tell the magnitude of the change in quantity demanded.

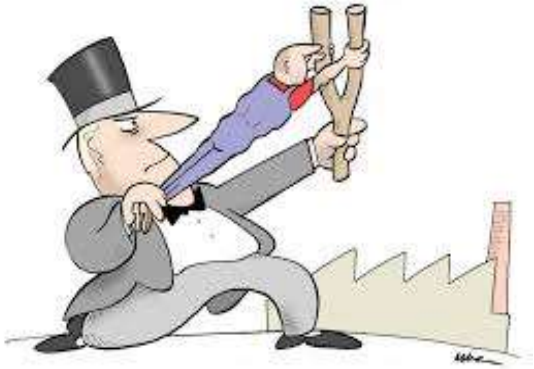
How do we find that an increase in price leads to what change in its demand?

Elasticity of Demand



Elasticity of Demand

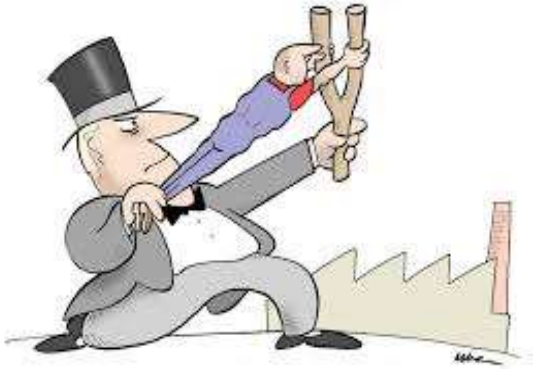
Price Elasticity of Demand



Elasticity of Demand

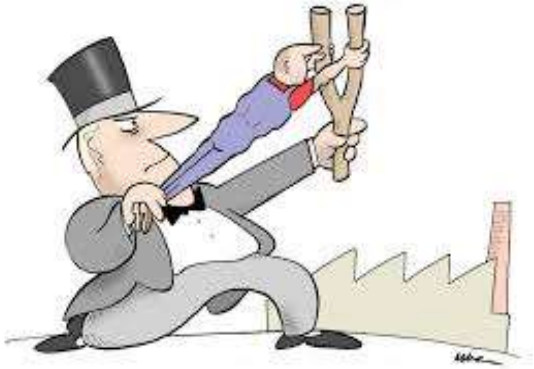
Price Elasticity of Demand

Income Elasticity of Demand



Elasticity of Demand

- Price Elasticity of Demand
- Income Elasticity of Demand
- Cross Elasticity of Demand



Price Elasticity of Demand

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The Degree of responsiveness of percentage change in quantity demanded due to percentage change in its price.

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$$Ed = \frac{\%\ \text{Change in Quantity Demanded}}{\%\ \text{Change in Price}}$$

Price Elasticity of Demand

The Degree of responsiveness of percentage change in quantity demanded due to percentage change in its price.

$$Ed = \frac{\%\ \text{Change in Quantity Demanded}}{\%\ \text{Change in Price}}$$

How is the percentage change for a component calculated?

Formula

$$Ed = \frac{\frac{\text{Change in Q}}{Q}}{\frac{\text{Change in P}}{P}}$$

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$$Ed = \frac{\frac{\text{Change in Q}}{Q}}{\frac{\text{Change in P}}{P}}$$

$$Ed = \frac{\text{Change in Q}}{\text{Change in P}} \times \frac{P}{Q}$$

Let us Solve a question on the basis of the formula learned.

Q. Calculate the price elasticity of demand for the given data.

Price(Rs)	Total Expenditure(Rs)
5	500
6	420

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Let us Solve a question on the basis of the formula learned.

Q. Calculate the elasticity of demand for the given data.

Price(Rs)	Total Expenditure(Rs)	Quantity (TE/P)
5	500	500/5 = 100
6	420	420/6 = 70

$$Ed = \frac{\text{Change in Q}}{\text{Change in P}} \times \frac{P}{Q}$$

Price(Rs)	Total Expenditure(Rs)	Quantity (TE/P)
5	500	500/5 = 100
6	420	420/6 = 70

Change in Q = 100 - 70 = 30

Change in P = 5 - 6 = -1

Price(Rs)	Total Expenditure(Rs)	Quantity (TE/P)
5	500	500/5 = 100
6	420	420/6 = 70

Change in Q = 100 - 70 = 30

Change in P = 5 - 6 = -1

Ed = 30/(-1) X 5/100

Ed = -30/20

Ed = (-) 1.5

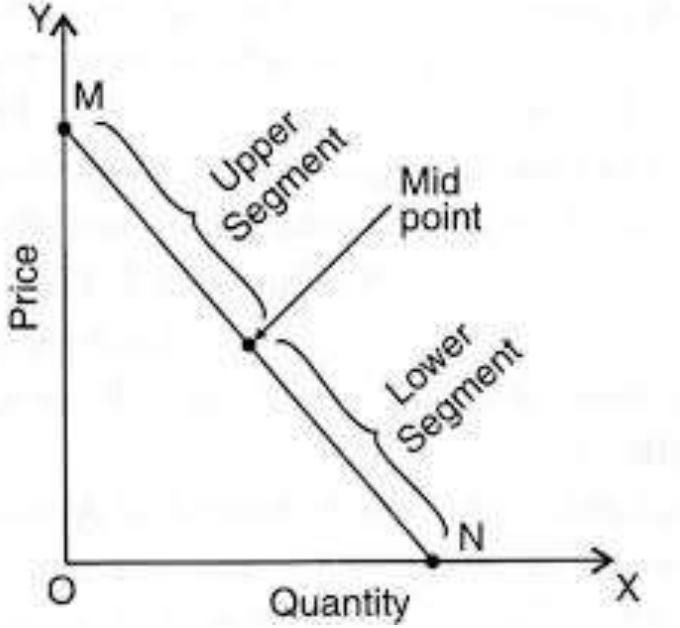
One more method

One more method

Geometric Method

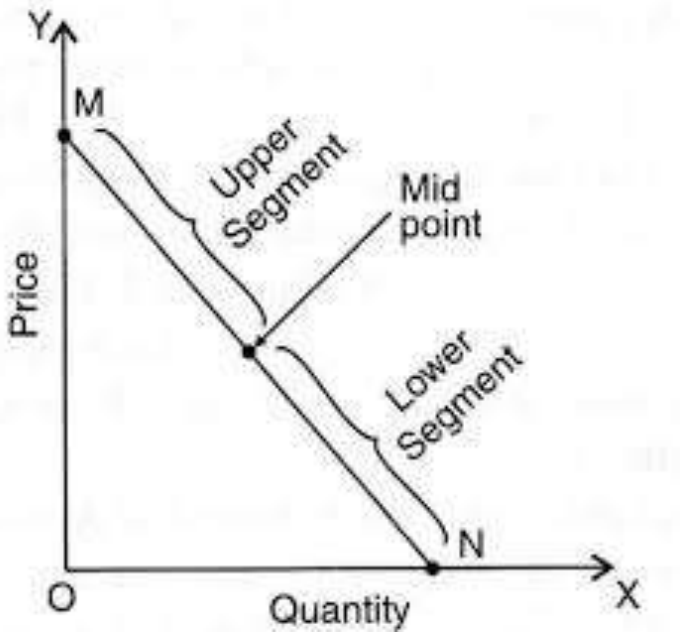
One more method

Geometric Method



One more method

Geometric Method



By this method the elasticity is calculated at the particular point on the demand curve.

The formula is

$$Ed = \frac{\text{Lower segment}}{\text{Upper segment}}$$

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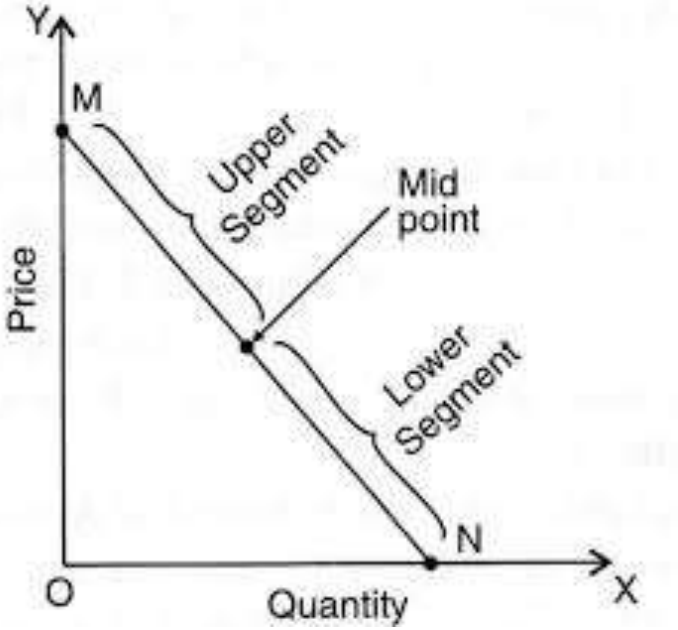
Geometric Method



By this method the elasticity is calculated at the particular point on the demand curve.

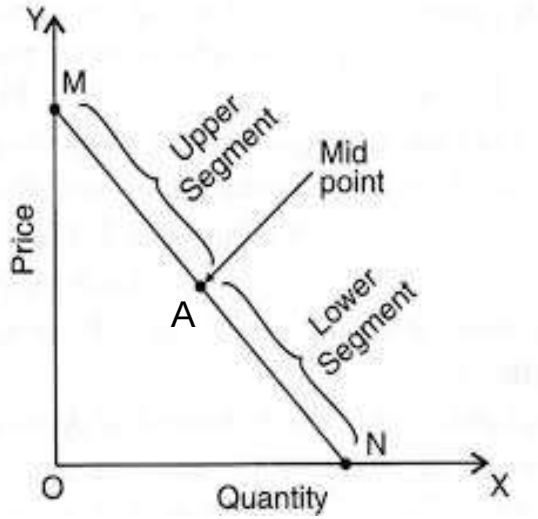
The formula is

$$Ed = \frac{\text{Lower segment}}{\text{Upper segment}}$$

Also known as the
Point method of calculation of price elasticity of demand

Let us Solve a question on the basis of the formula learned.

The diagram shown here shows MN is the demand curve of a commodity. A is the midpoint of line MN. Find elasticity at different points on the curve.



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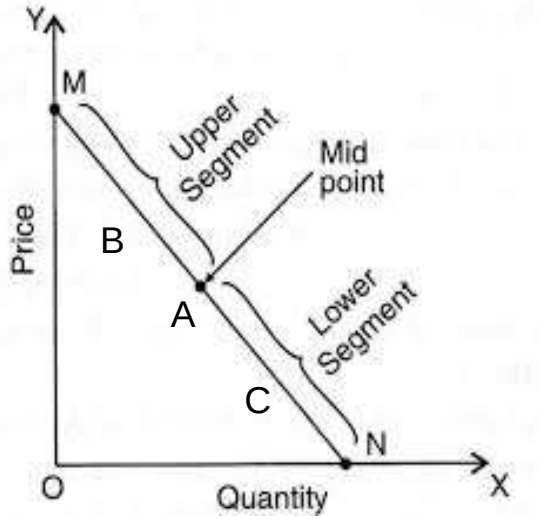

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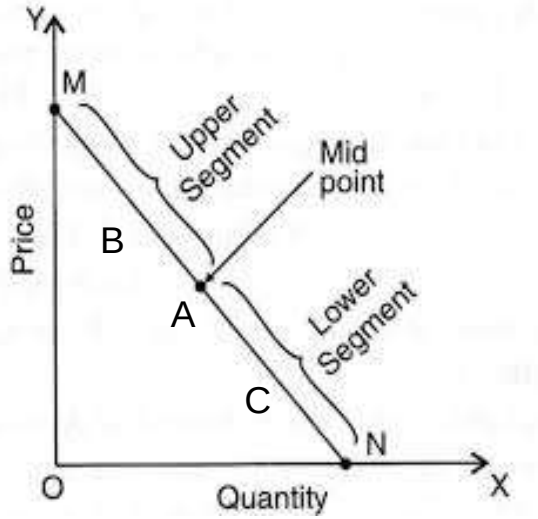

Ed = lower segment / upper segment

Ed at M = MN/0 = infinite

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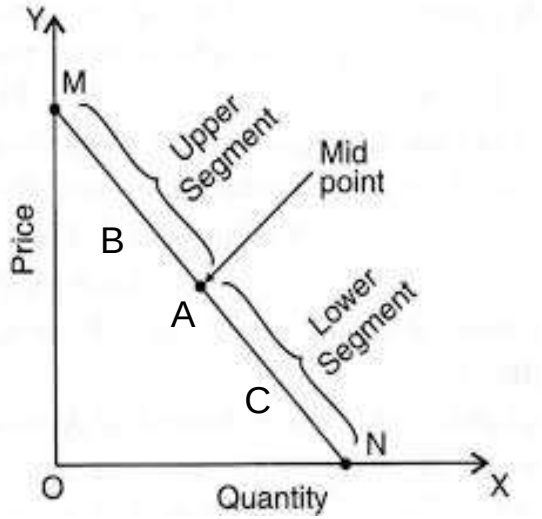

Ed = lower segment / upper segment

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Ed at B = BN/MB, thus Ed>1

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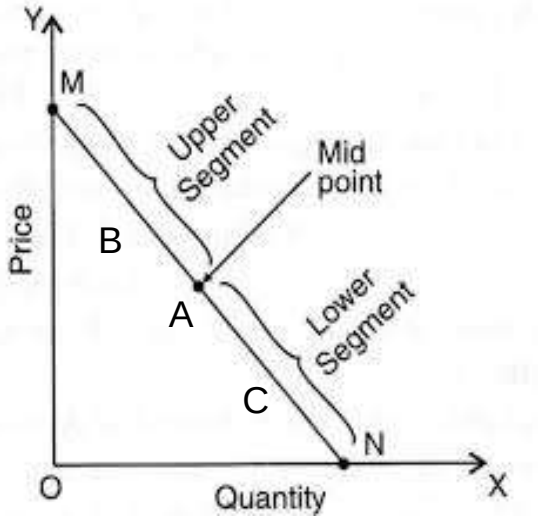

Ed = lower segment / upper segment

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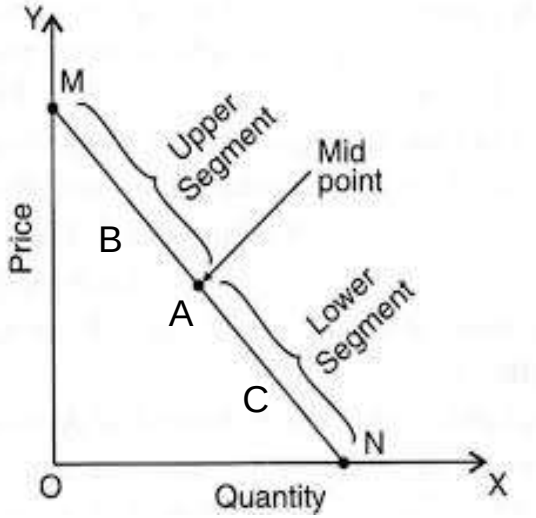

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Ed at C = CN/MC, thus Ed <1

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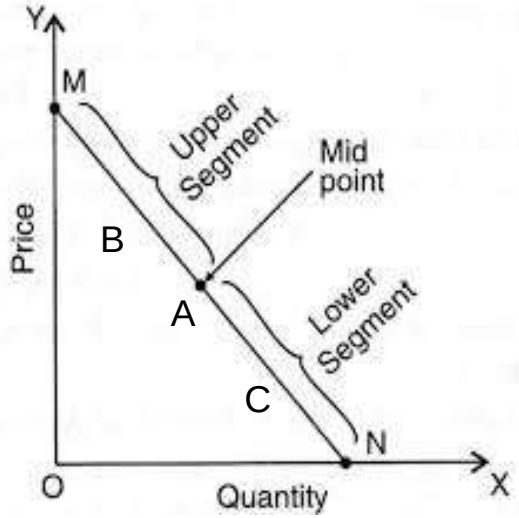

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Ed at M = MN/0 = infinite

Ed at B = BN/MB, thus Ed>1

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Ed at N = 0/MN = 0

Types of Elasticity

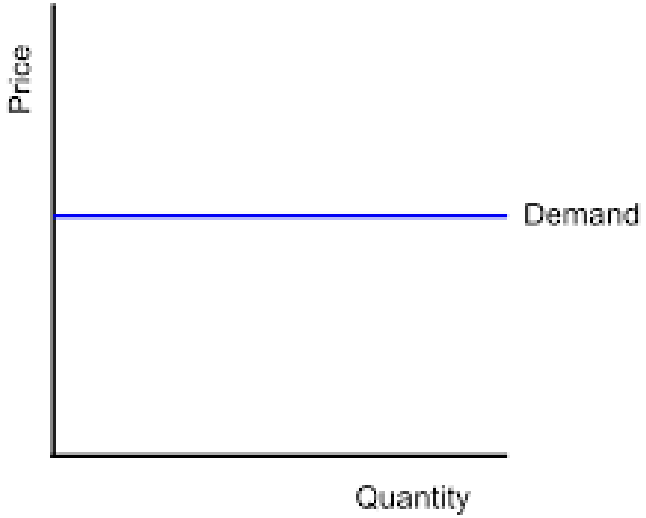
Types of Elasticity

Types of Elasticity

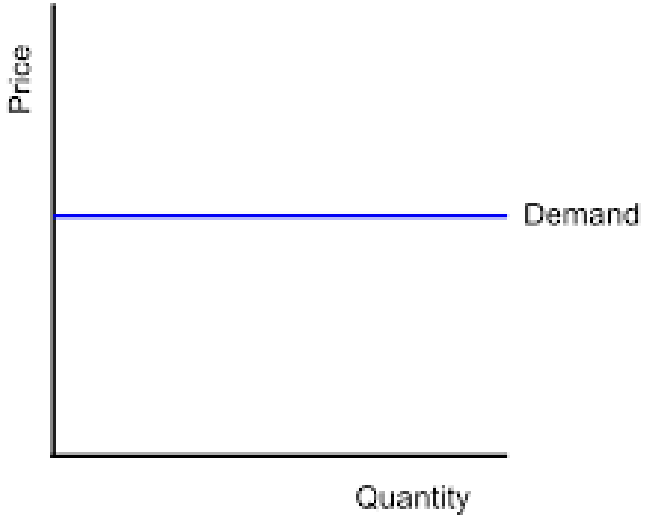
Elastic Demand

Inelastic Demand

Perfectly Elastic Demand

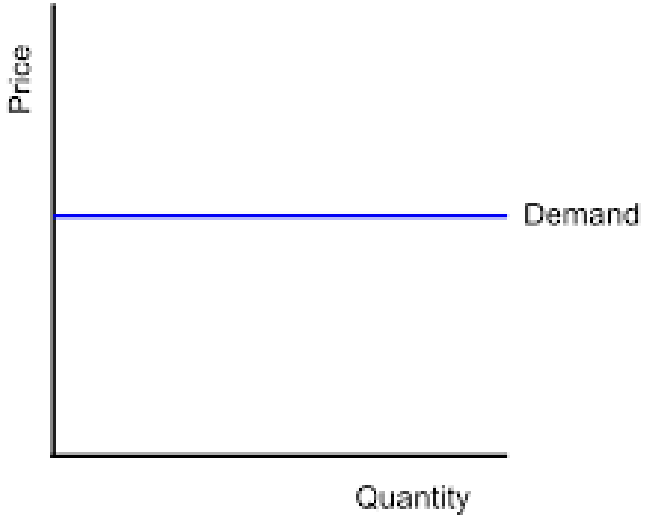


Perfectly Elastic Demand



The change in price is zero

Perfectly Elastic Demand



The change in price is zero

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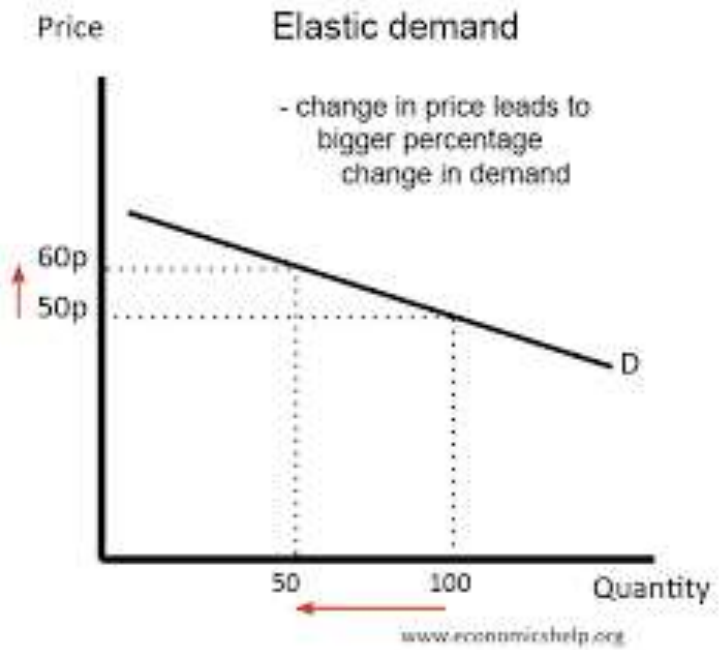
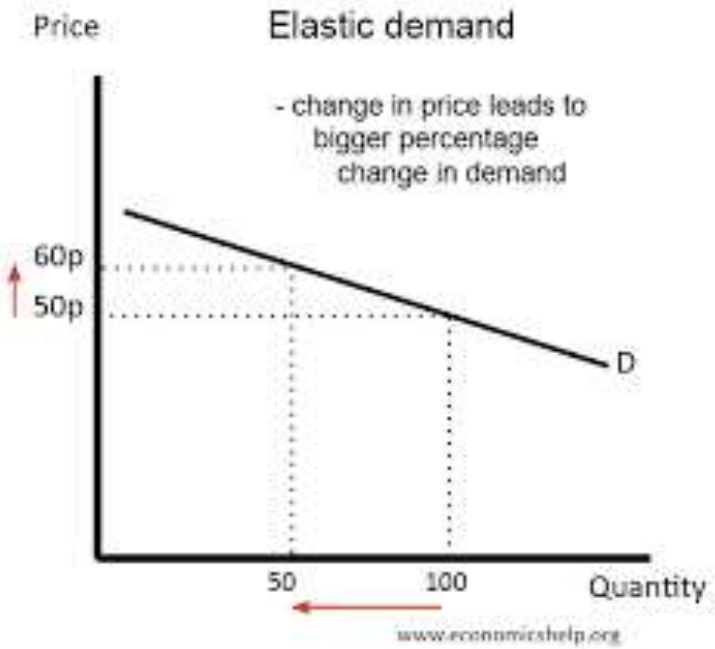
Elastic Demand

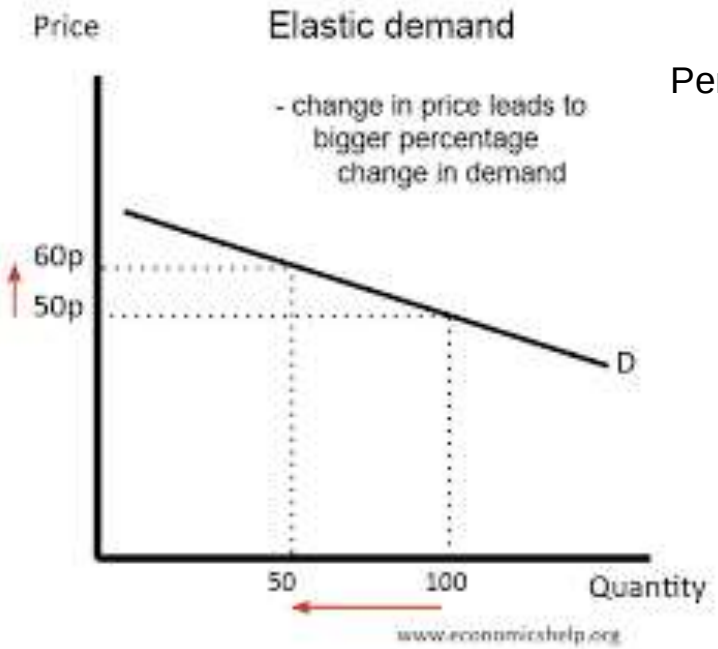


Elastic Demand



Percentage change in price is less than the percentage change in quantity.

Elastic Demand



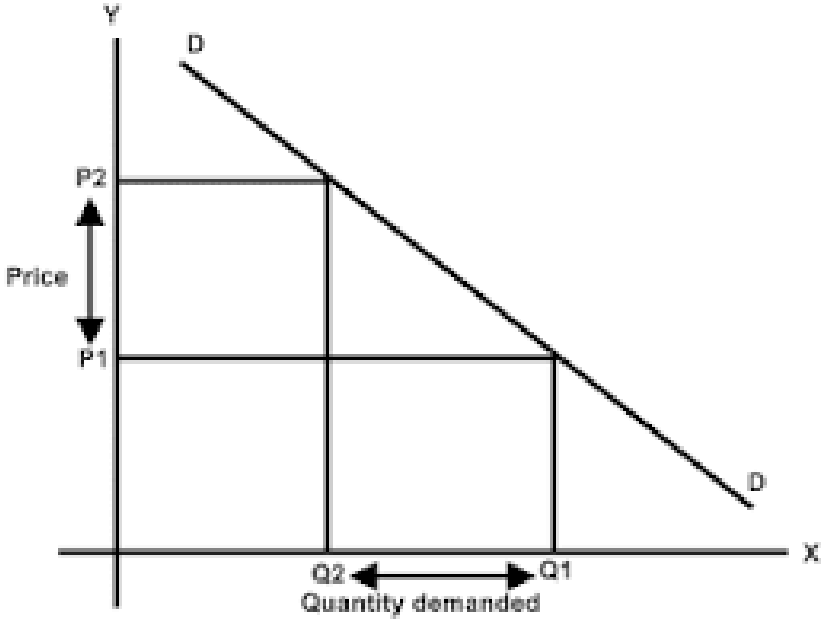
Percentage change in price > Percentage change in quantity.

Ed > 1

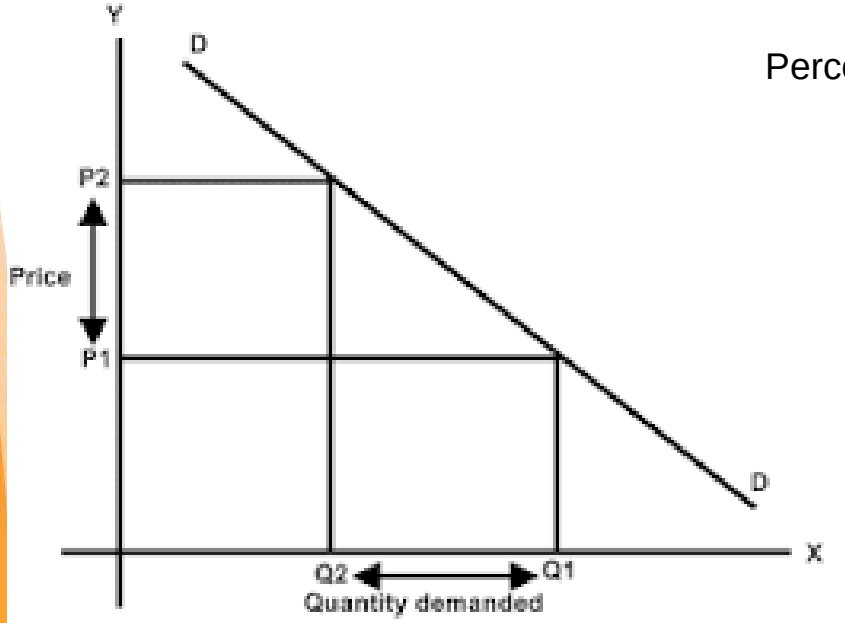
Elastic Demand

Ed > 1

Unit Elastic Demand

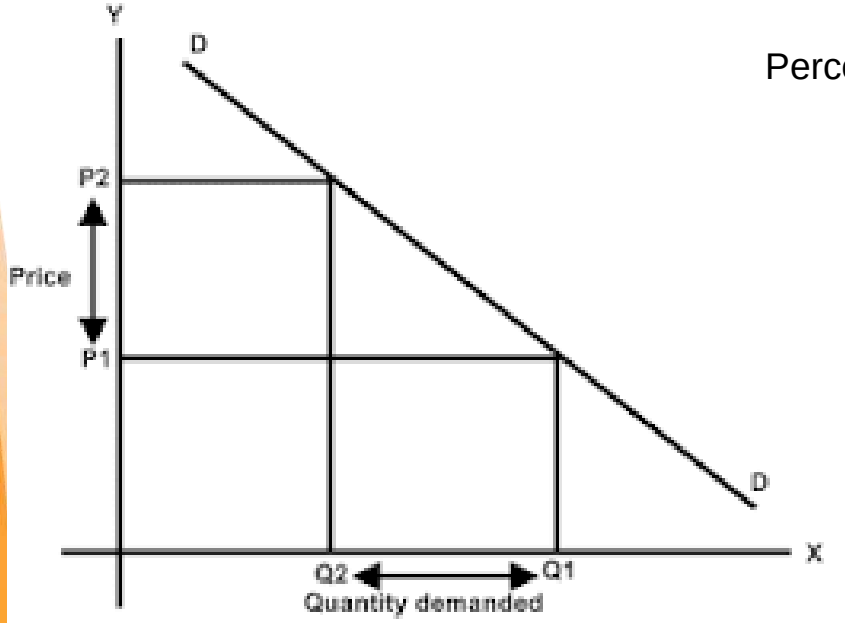


Unit Elastic Demand



Percentage change in price = Percentage change in quantity

Unit Elastic Demand



Percentage change in price = Percentage change in quantity

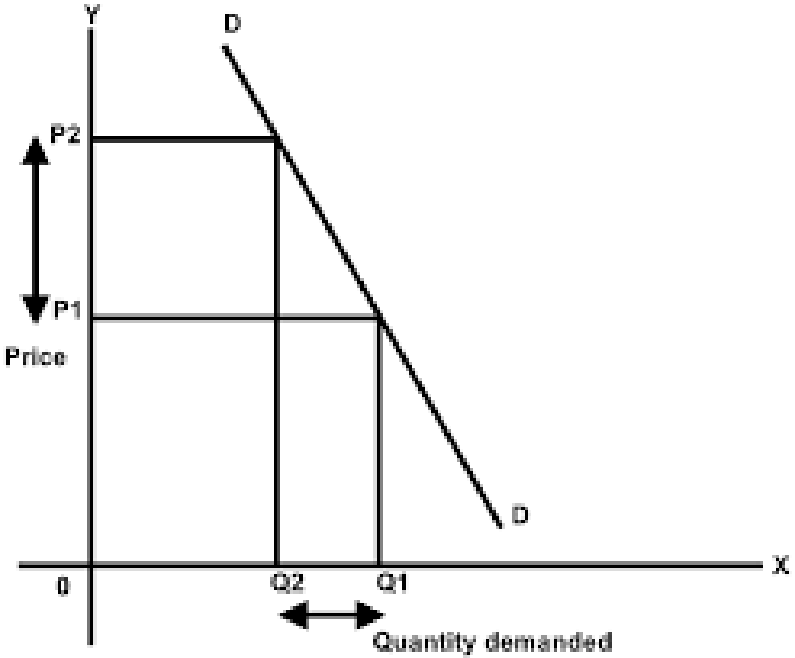
Ed = 1

Unit Elastic Demand

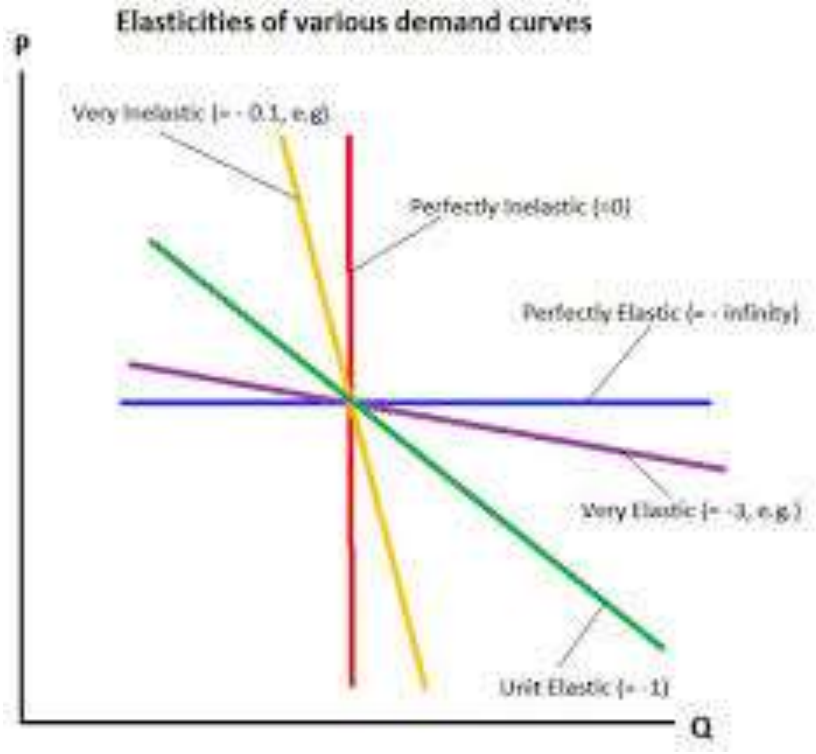
Ed = 1

Scooter

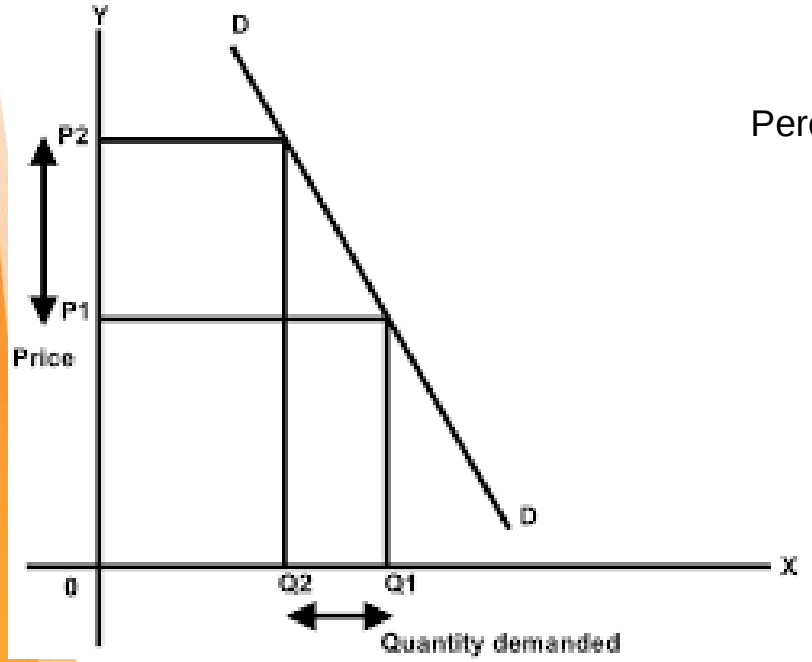
Inelastic Demand



Consolidated Effect

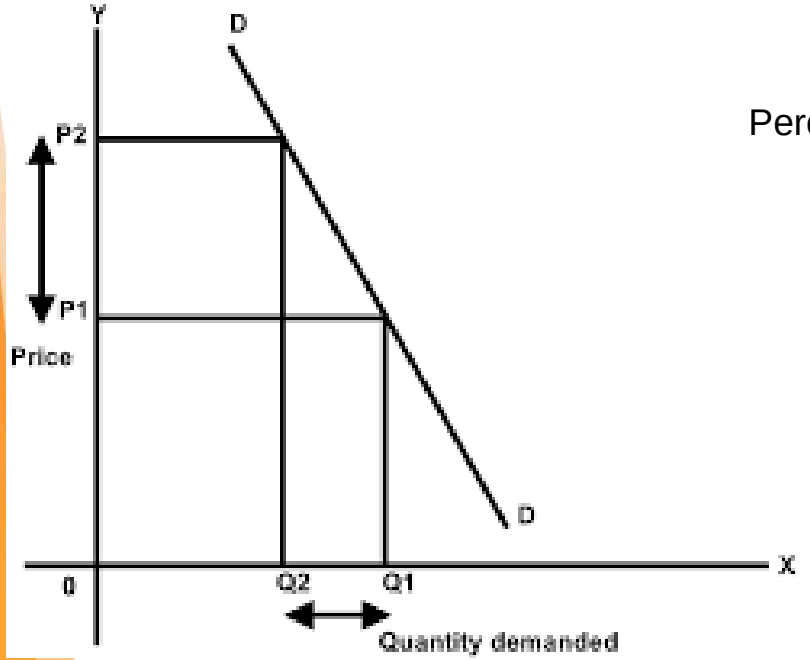


Inelastic Demand



Percentage change in price < Percentage change in quantity

Inelastic Demand



Percentage change in price < Percentage change in quantity

Ed < 1

Inelastic Demand

Ed < 1

Necessities of life

Inelastic Demand

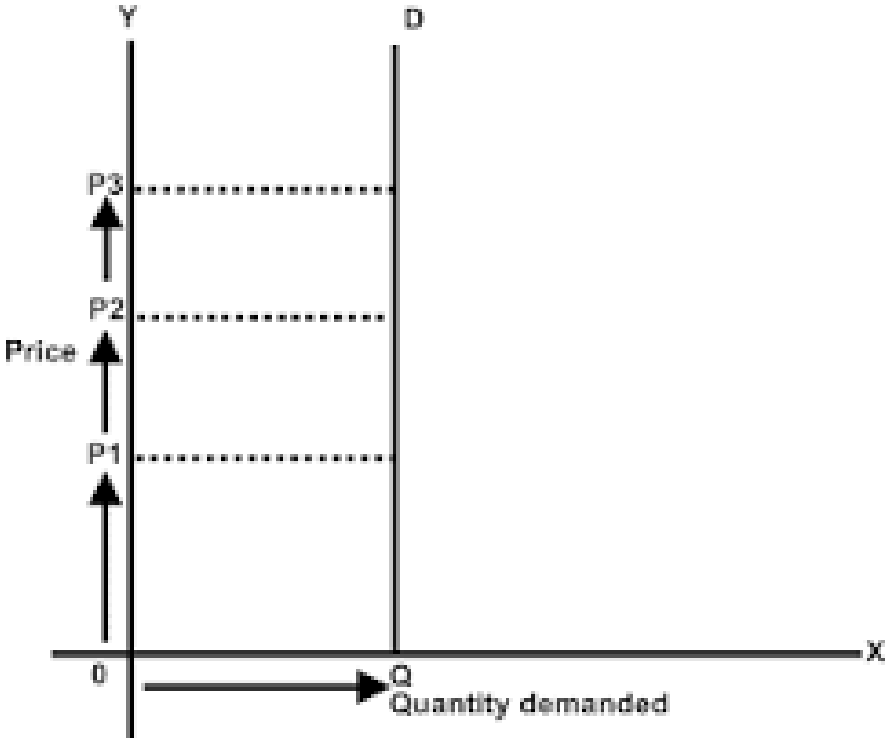
Ed < 1

Salt

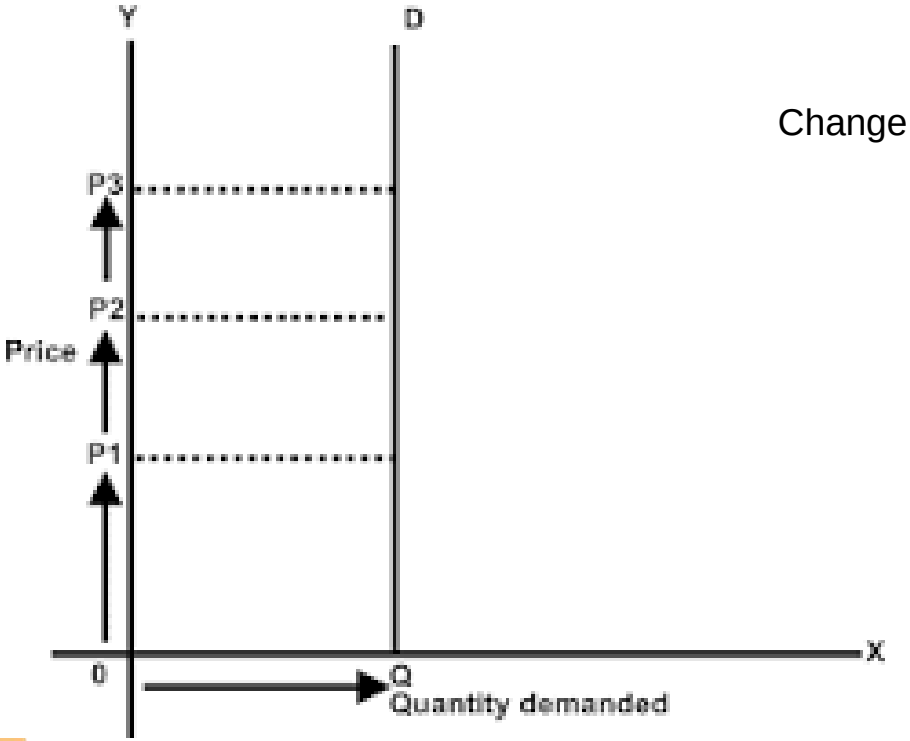
Necessities of life

Life saving drugs

Perfectly Inelastic Demand

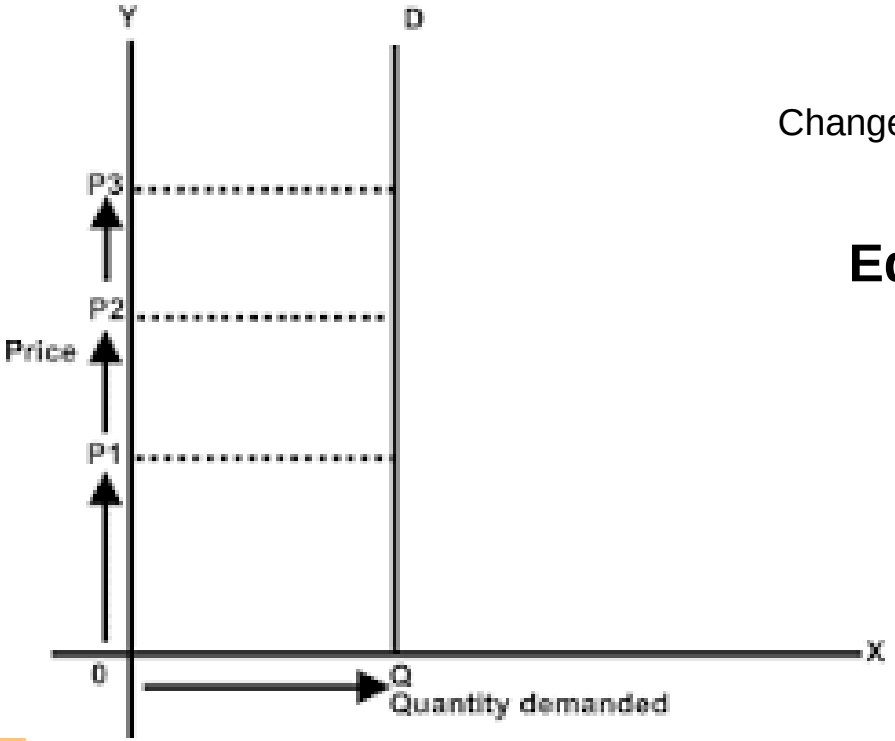


Perfectly Inelastic Demand



Change in quantity is zero

Perfectly Inelastic Demand



Change in quantity is zero

Ed = 0

What affects the price elasticity of demand for a product?

Nature of the Product

Nature of the Product

Necessity

Nature of the Product

Necessity

Inelastic demand

Nature of the Product

Necessity

Inelastic demand

Comfort

Nature of the Product

Necessity

Inelastic demand

Comfort

Less elastic demand

Nature of the Product

Necessity

Inelastic demand

Comfort

Less elastic demand

Luxury

Nature of the Product

Necessity

Inelastic demand

Comfort

Less elastic demand

Luxury

Highly Elastic demand

Habit

Habit

Habit

Even a significant change in price does not lead to a change in the demand of the product as people are habituated.

Habit

Even a significant change in price does not lead to a change in the demand of the product as people are habituated.

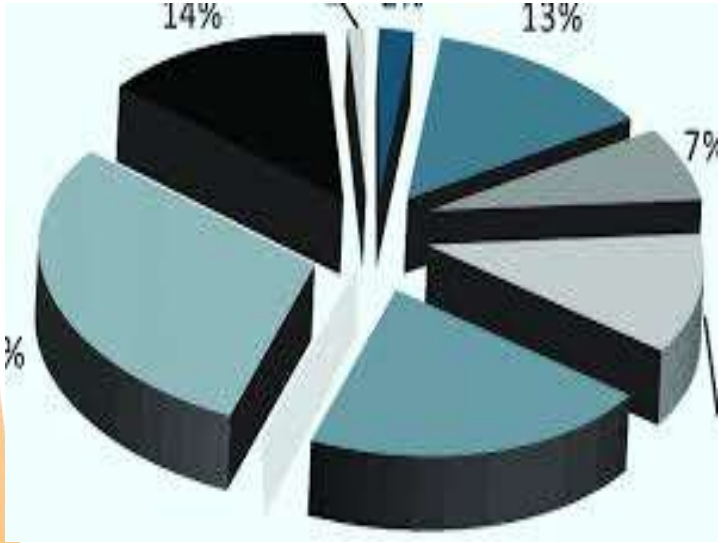
Inelastic

Number of Uses

Number of Uses

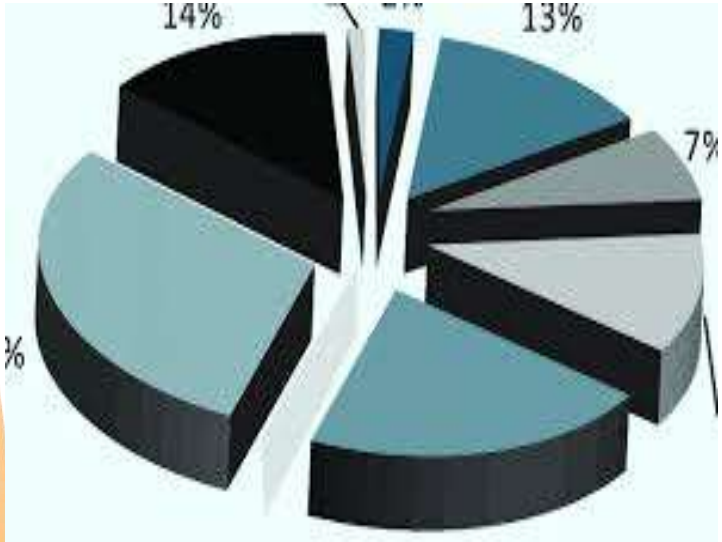
Elastic

Share in total Expenditure



Proportion of consumer’s income spent on a particular commodity influences the elasticity of demand.

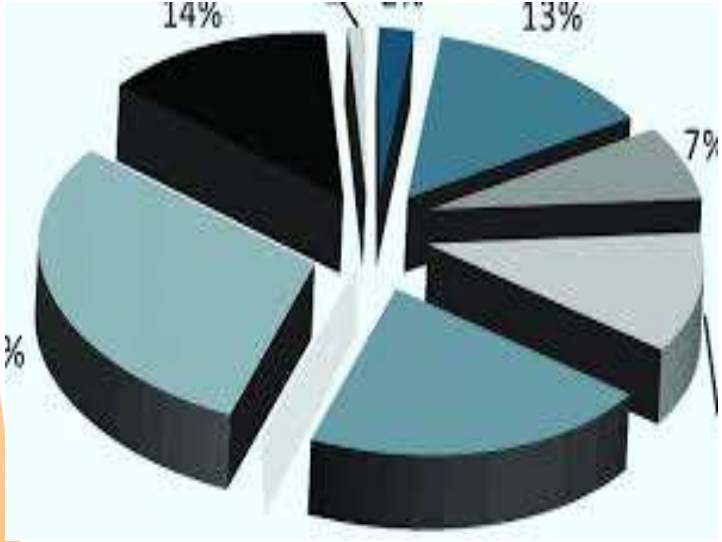
Share in total Expenditure



Proportion of consumer's income spent on a particular commodity influences the elasticity of demand.

Commodity like matchbox, salt, needle, etc have **inelastic** demand as consumer spends a small proportion of the total expenditure.

Share in total Expenditure



Proportion of consumer's income spent on a particular commodity influences the elasticity of demand.

Commodity like matchbox, salt, needle, etc have **inelastic** demand as consumer spends a small proportion of the total expenditure.

If the proportion of income spent on the commodity is large then demand for such commodity will be **elastic**.

Time Period

Elasticity directly varies with the time period.

Time Period

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Consumer find it difficult to change their habit in the short period but with time the demand changes in the long run.

Time Period

Elasticity directly varies with the time period.

Consumer find it difficult to change their habit in the short period but with time the demand changes in the long run.

Inelastic in short period

Time Period

Elasticity directly varies with the time period.

Consumer find it difficult to change their habit in the short period but with time the demand changes in the long run.

Inelastic in short period

Elastic in long period

Price level

Costly goods like laptop - highly elastic

Price level

Costly goods like laptop - highly elastic

Inexpensive items match box, needle - inelastic

Income Level

High income group - less elastic demand

Income Level

High income group - less elastic demand

Low income group - more elastic demand

Substitutes Availability

Large number of substitutes available - Elastic demand

Urgency

Urgent need - inelastic demand

Urgency

Urgent need - inelastic demand

Not so urgent - elastic demand

Substitutes Availability

Large number of substitutes available - Elastic demand

No substitutes available - Inelastic demand

Question

How does the availability of substitutes affect the elasticity of demand?

Question

How does the availability of substitutes affect the elasticity of demand?

Answer. A commodity with large number of substitutes is more elastic as compared to commodity with no substitutes.

Question

What is meant by the unitary elastic demand? Also draw the demand curve.

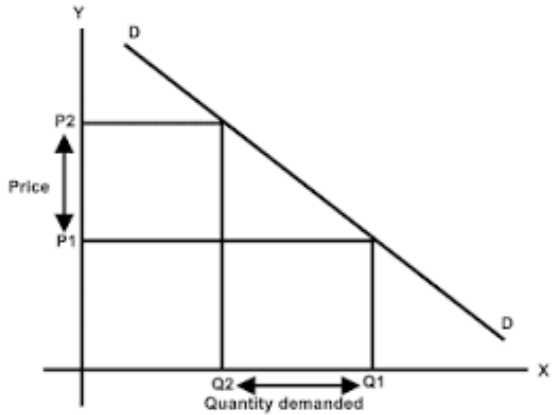
Question

What is meant by the unitary elastic demand? Also draw the demand curve.

Unitary elastic demand

percentage change in price = percentage change in quantity

Ed = 1



Summary

Elasticity of demand

Price elasticity of demand

Formula for Ed

Types of elasticity

Factors affecting price elasticity of demand