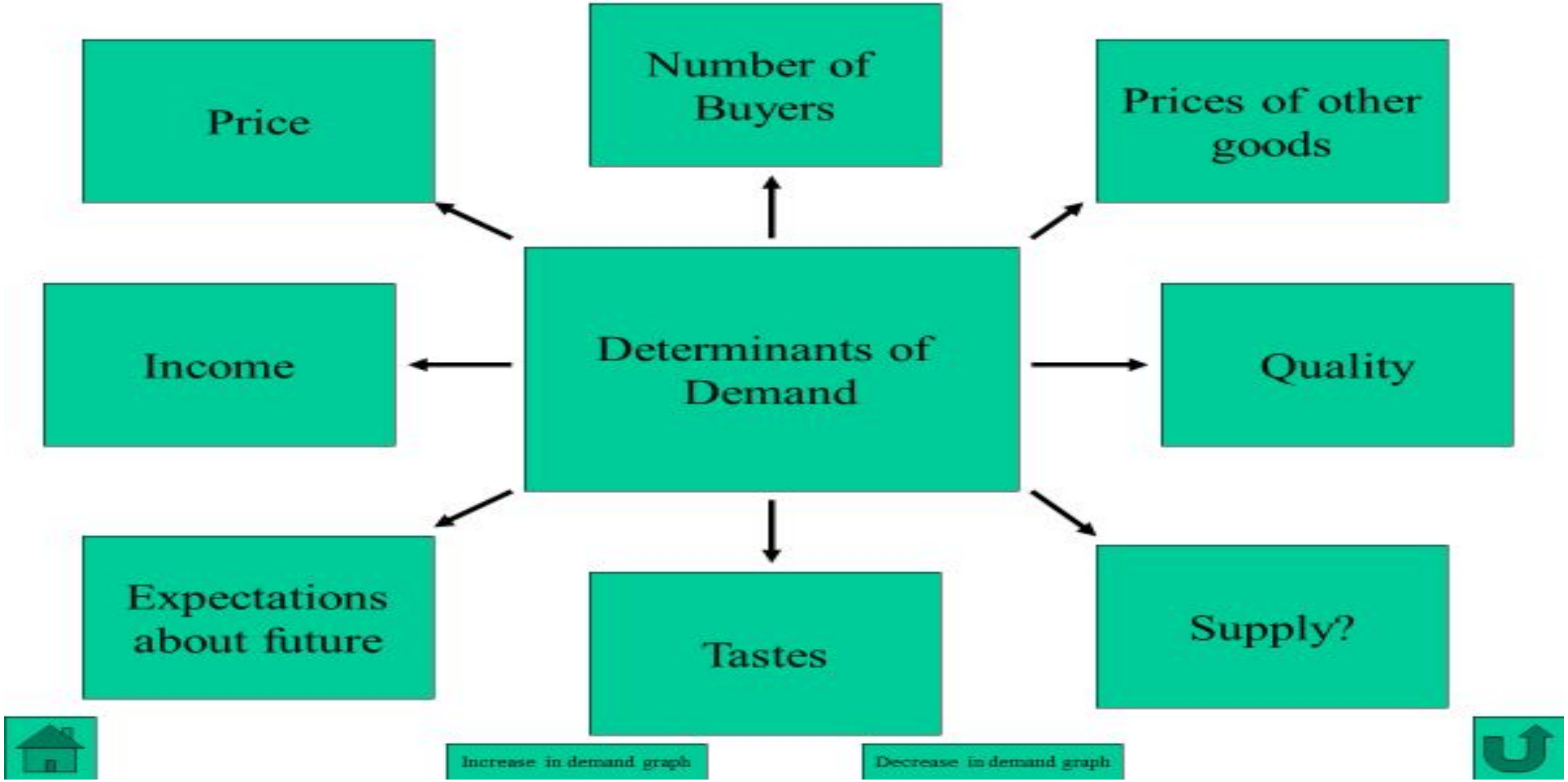
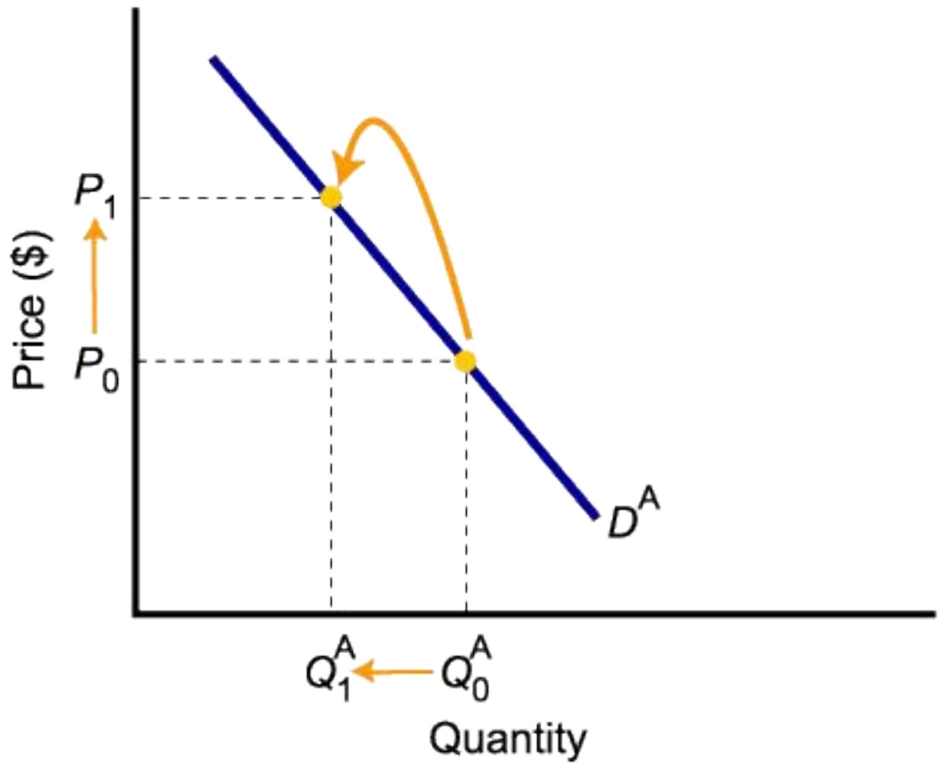
LECTURE 6: DETERMINANTS AND FACTORS AFFECTING DEMAND

DETERMINANTS OF DEMAND



PRICE

- Price is the most important determinant of demand.
- A "demand curve" plots combinations of prices and quantity demanded.
- A change in price causes a movement along the demand curve



FACTORS AFFECTING DEMAND (OR, SHIFT FACTORS OF DEMAND)

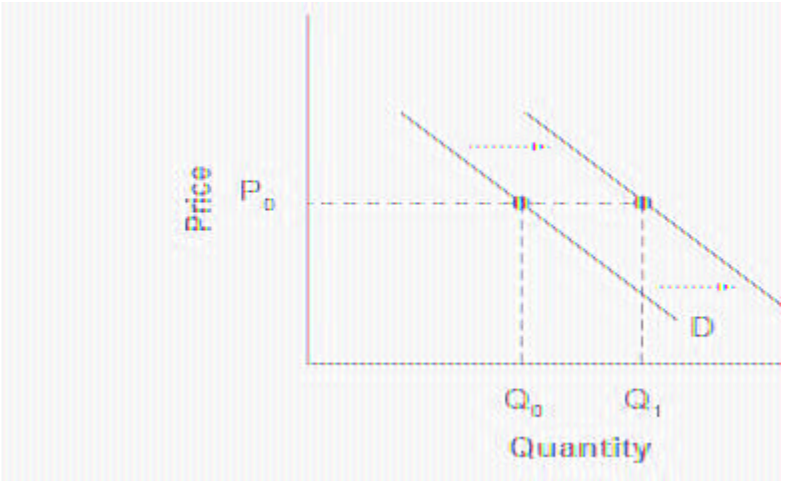
- **1. Income**
- **2. The Prices of Related Goods**
- **3. Tastes and Preferences**
- **4. Expectations about Future Prices and Market Conditions**
- **5. Population/ No of Consumers**

INCOME

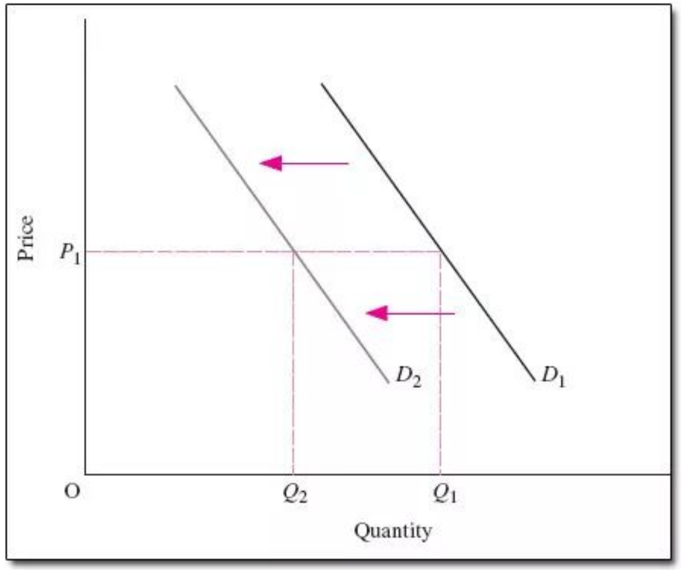
- Ceteris paribus, when people's income changes, demand change (shifts in demand)
- Normal Goods – A good whose demand increases with an increase in income is called a "normal good."
- Inferior Goods –A good whose demand decreases with an increase in income is called an "inferior good."

INCOME

- Normal Goods – For normal goods demand increases with an increase in income or vice-versa.



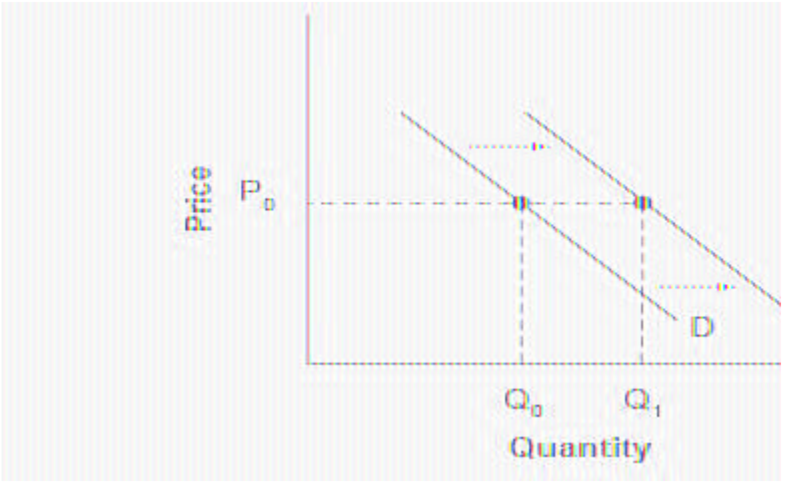
Higher income => higher demand



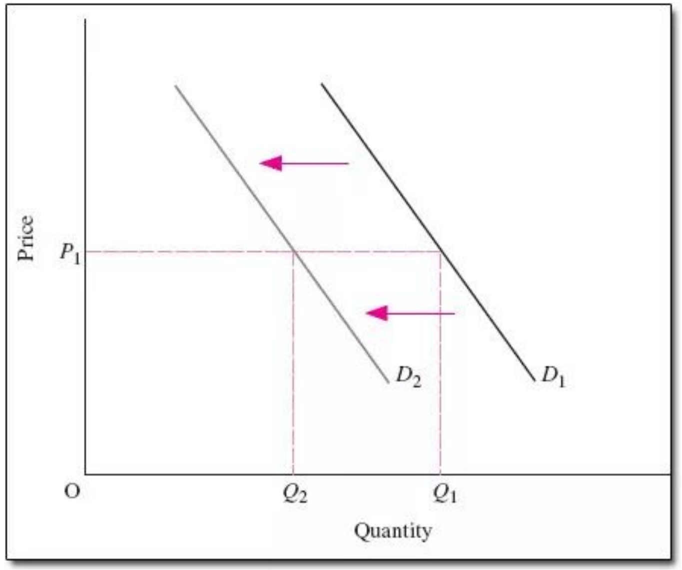
Lower income => lower demand

INCOME

- Inferior Goods –For inferior goods demand decreases with an increase in income or vice-versa.



Lower income => higher demand



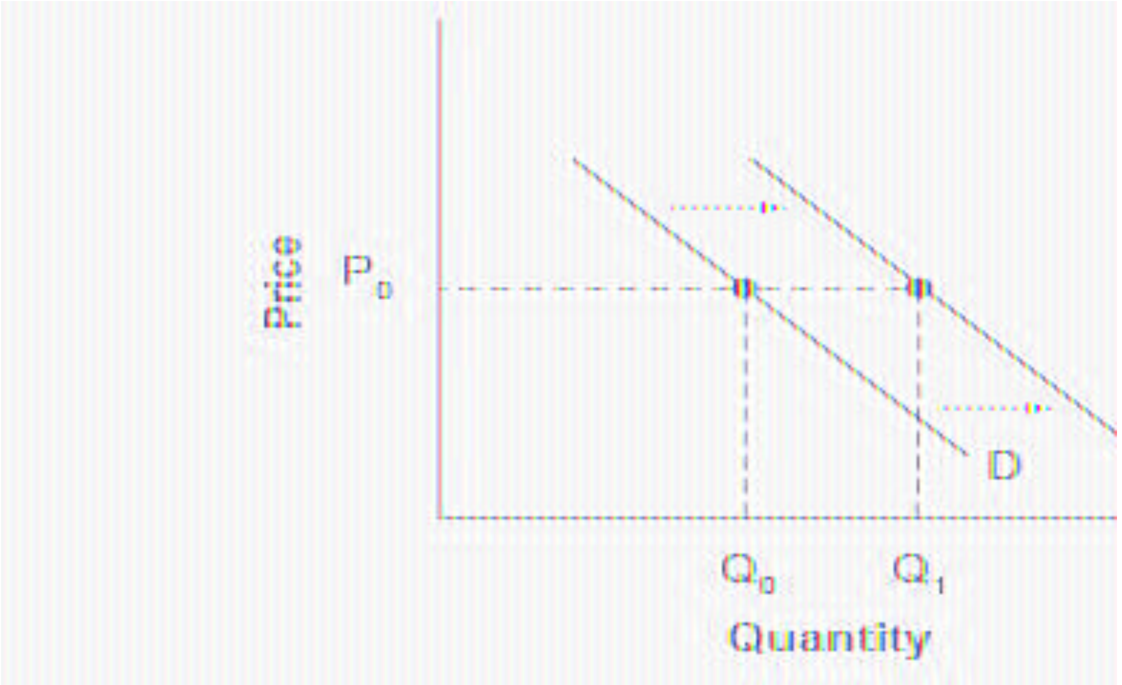
Higher income => lower demand

PRICES OF RELATED GOODS

- Changes in the prices of related goods can increase or decrease demand.
- Substitute Goods: Two goods are substitute goods if an increase in price of one good causes an increase in the demand for another good.
- Complementary Goods: Two goods are complementary goods if an increase in price of one good causes a decrease in the demand for another good.

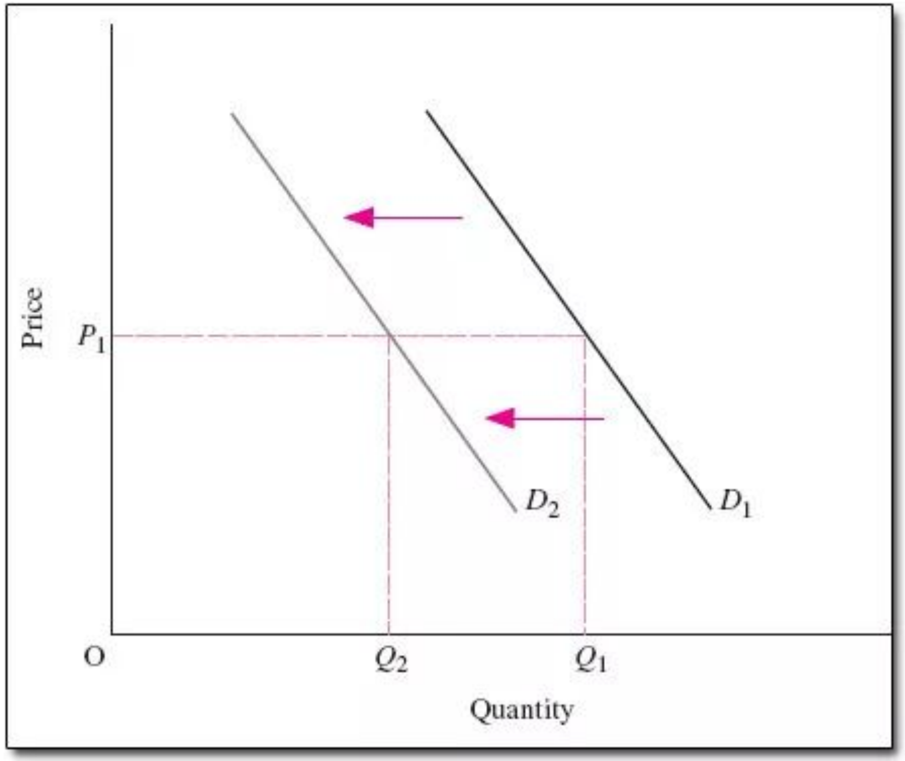
PRICES OF RELATED GOODS

- Substitute Goods: $P_1 \uparrow Q_1^d \downarrow D_2 \uparrow$



- Two goods: good 1 and good 2.
- P_1 : Price of good 1
- Q_1^d: Quantity demanded of good1.
- D_2: Demand for good 2

PRICES OF RELATED GOODS

- Complementary Goods: $P_1 \Uparrow Q_1^d \Downarrow D_2 \Downarrow$
- 

- Two goods: good 1 and good 2.
- P_1 : Price of good 1
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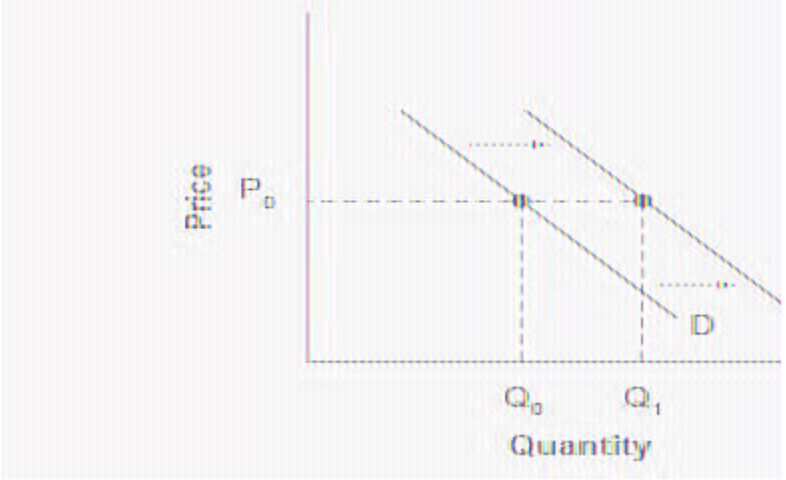
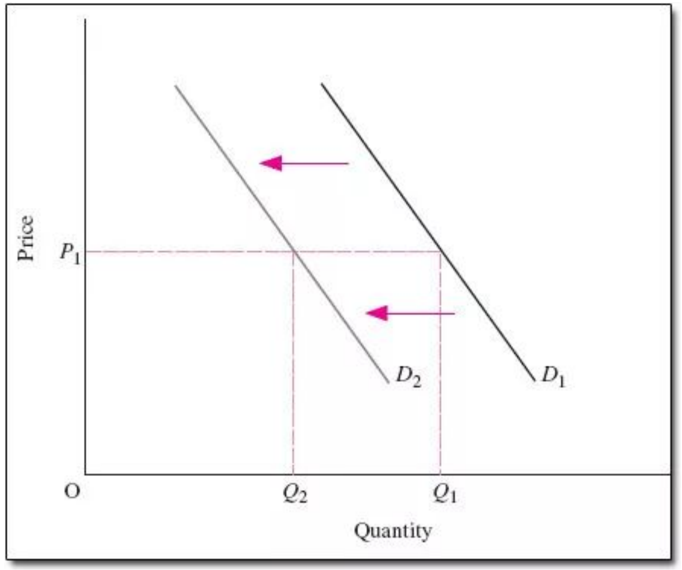
TASTES AND PREFERENCES

- Demand curve can shifts due to changes in tastes over time.



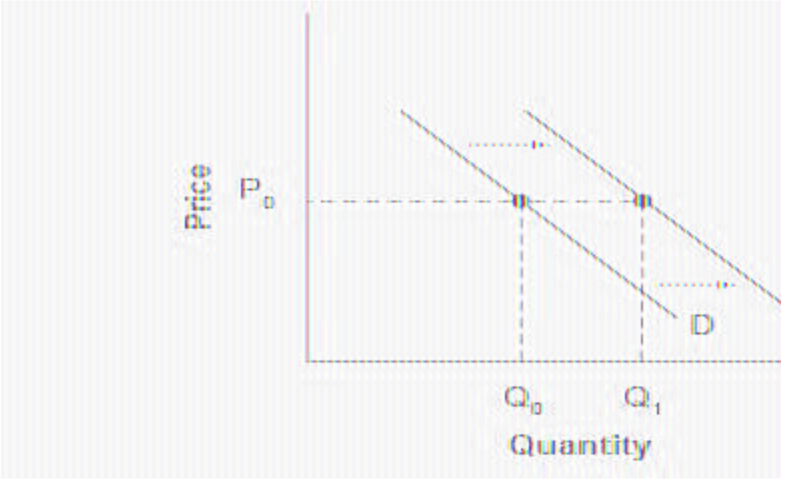
Favorable change in taste => higher demand



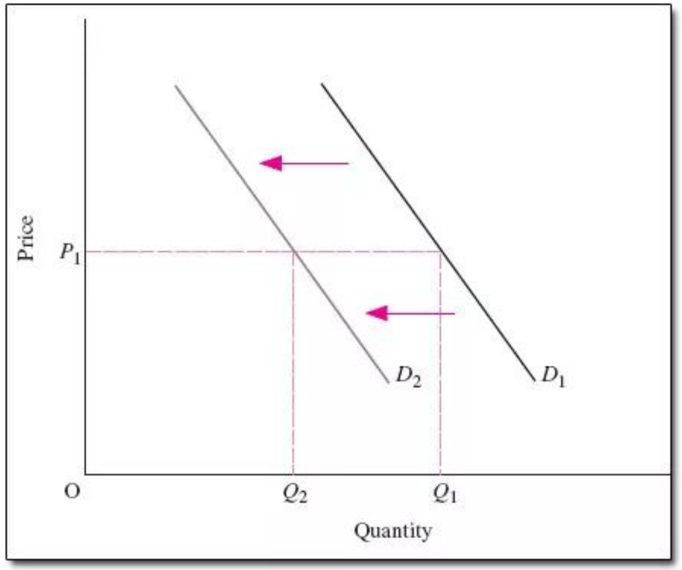
Unfavorable change in taste => lower demand

EXPECTATIONS ABOUT FUTURE PRICES AND MARKET CONDITIONS

- Demand curve can shifts due to changes in expectations.
- For example, if you expect the price of computers to fall soon, you may put off buying one until later.



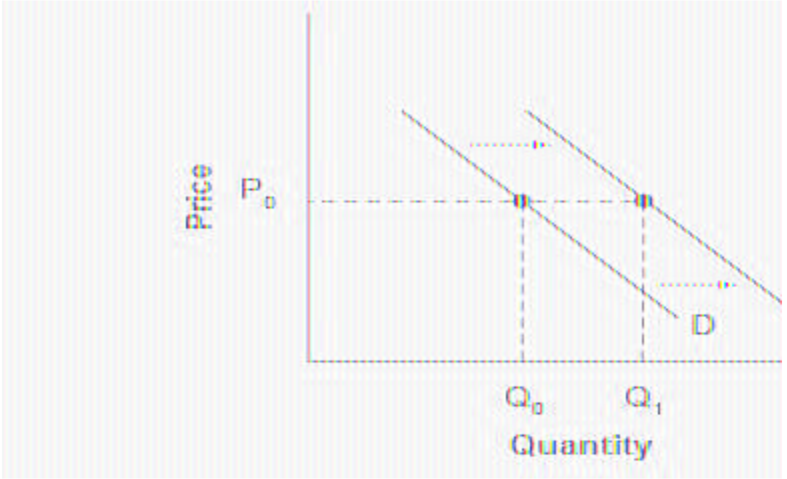
Positive expectation=> higher demand



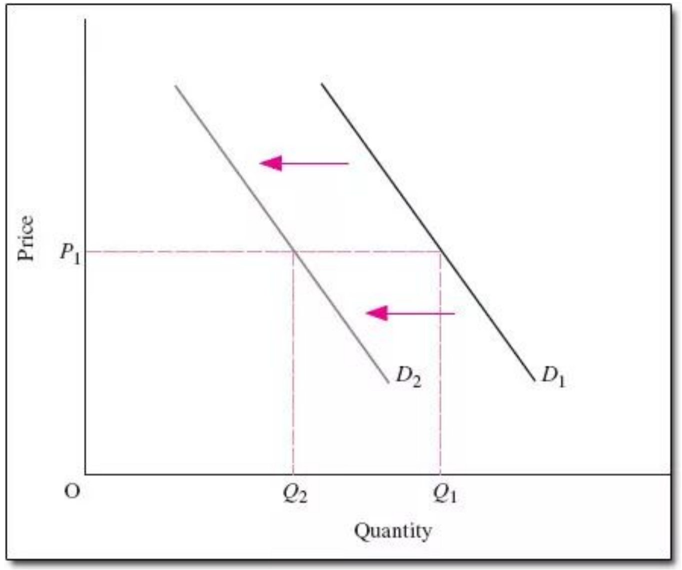
Negative expectation=> lower demand

POPULATION/ NO OF CONSUMERS

- Demand curve can shifts due to changes in population/ no of consumers.



Increase in population/no of consumers => higher demand



decrease in population/no of consumers => lower demand