CONCEPT OF DEMAND

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Demand refers to the willingness or ability of a buyer to pay for a particular product.

Desire for a commodity and consumer has ability and willingness to pay for that.

Ex- Bagger's desire for a car not demand

Demand Function is relation between demand of a commodity and its various determinants.

D_X = Function of (P_X,Y,P_r,T,E…)

Factors affecting Demand

Dx = Function of (Px,Y,Pr,T,E…)

Px = Price of the product

Generally, there exists an inverse relationship between price and quantity demanded. It means, as price increases, quantity demanded falls due to decrease in the satisfaction level of consumers.

Y = Income of the consumer

Demand for a commodity is also affected by income of the consumer. However, the effect of change in income on demand depends on the nature of the commodity.

i. If the given commodity is a normal good, then an increase in income leads to rise in its demand and vise versa.

ii. If the given commodity is an inferior good, then an increase in income reduces the demand, while a decrease in income leads to rise in demand.

Pr = Price of related goods(Substitute and Complementary goods):

i) **Substitute Goods:**Substitute goods are those goods which can be used in place of one another for satisfaction of a particular want, like tea and coffee. An increase in the price of substitute leads to an increase in the demand for given commodity and vice-versa.

ii) **Complementary goods:**are those goods which are used together to satisfy a particular want, like tea and sugar,Car and petrol. An increase in the price of complementary good leads to a decrease in the demand for given commodity and vice-versa

T = Taste or preference of consumer:

Taste and preference include changes in **fashion, customs, habits,** etc. If a commodity is in fashion or is preferred by the consumers, then demand for such a commodity rises. On the other hand, demand for a commodity falls, if the consumers have no taste for that commodity.

E = Future expected price:

If the price of a certain commodity is expected to increase/decrease in near future, then people will buy more or less of that commodity than what they normally buy at present.

Factors are also known as Determinants of demand.

Law of Demand

The law states that other things remain constant there exist an inverse relation between price and quantity demand of a commodity.

It may be defined in Marshall's words as **"the amount demanded increases with a fall in price, and diminishes with a rise in price".** The law refers to the direction in which quantity demanded changes with a change in price.

Assumptions of the Law of Demand:

(i) There is no change in the tastes and preferences of the consumer

(ii) The income of the consumer remains constant

(iii) There should not be any substitutes of the commodity

(iv) There should not be any change in the prices of related products

(v) There should not be any possibility of change in the price of the product in near future.

(vi) The habits and customs remain unchanged. Given these conditions, the law of demand operates. If there is change even in one of these conditions, it will stop operating

Individual &Market Demand

IndividualDemand:

Quentities of a commodity which an individual consumer will buy at all possible prices at a given time.

Price	D(A)
60	2
40	3
30	5
24	7

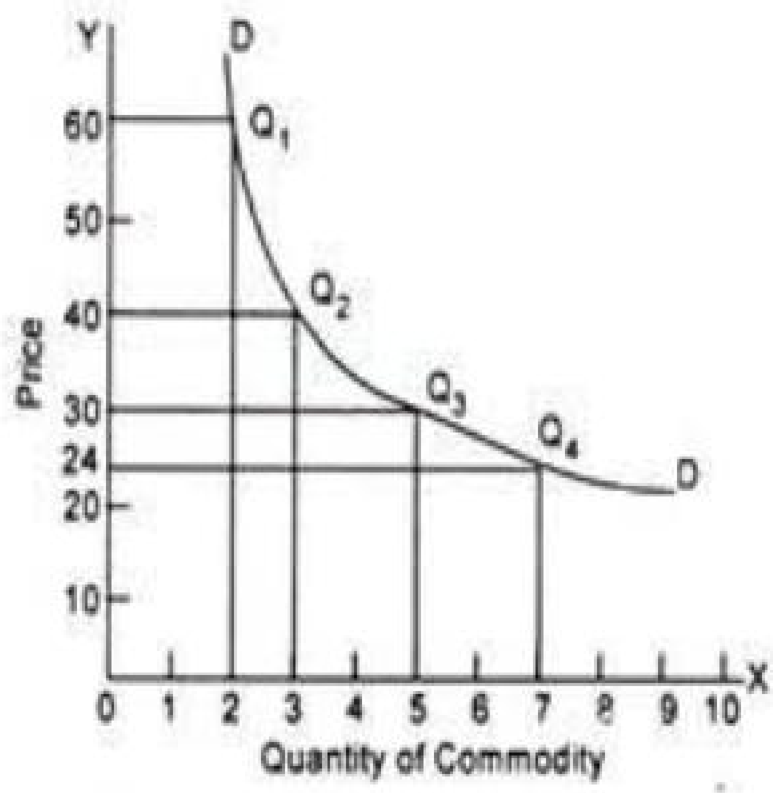


Fig. 3.17. Demand curve

Market Demand:

Quantities of a given commodity which all consumers will buy at all possible prices at a given time period.

D(A)= Demand of consumer A

D(B)= Demand of consumer B

Price	D(A)	D(B)	Market D
10	5	7	12
20	3	5	08
30	2	4	06
40	1	2	03

Market Demand Curve

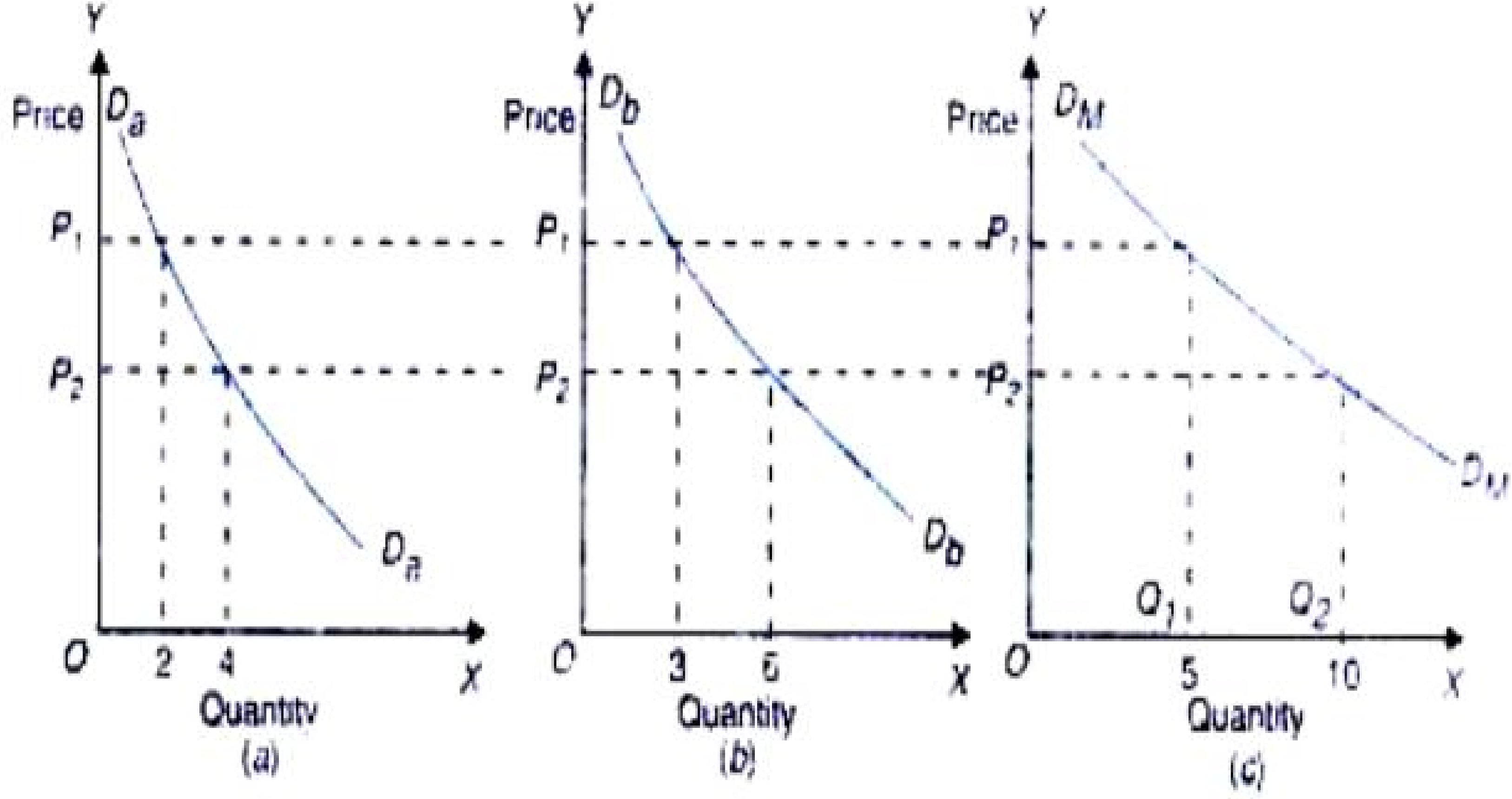


Fig. 6.2. Horizontal Addition of Individual Demand Curves to get Market Demand

Why Demand curve is downward slope?

1. The law of demand is based on the law of Diminishing Marginal Utility. According to this law, when a consumer buys more units of a commodity, the marginal utility of that commodity continues to decline. Therefore, the consumer will buy more units of that commodity only when its price falls.

2. Income Effect: When the price of a commodity falls, the real income of the consumer increases because he has to spend less in order to buy the same quantity. On the contrary, with the rise in the price of the commodity, the real income of the consumer falls.

3. Substitution Effect: The other effect of change of the price of the commodity is the substitution effect. With the fall in the price of a commodity, the prices of its substitutes remaining the same, consumers will buy more of this commodity rather than the substitutes.

4.Different use of product: There are different uses of certain commodities and services that are responsible for the negative slope of the demand curve. With the increase in the price of such products, they will be used only for more important uses and their demand will fall.

5.Size of population: when price diminishes., number of consumer increases. They demand more goods and vice versa.

Limitations/Exceptions of law of demand:

1. Giffen goods:

   Giffen goods are those inferior good fro which,when price decreases demand diminishes. Cheaper varieties of goods like low priced rice, low priced bread, etc. are some examples of Giffen goods.

2. Goods having prestige value(Veblen Goods)

   Few goods like diamond can be purchased only by rich people. The prices of these goods are so high that they are beyond the capacity of common people. The higher the price of the diamond the higher the prestige value of it.

3. Price expectation in near future:

   When the consumer expects that the price of the commodity is going to fall in the near future, they do not buy more even if the price is lower.

4. Fear of shortage:

When people feel that a commodity is going to be scarce in the near future, they buy more of it even if there is a current rise in price.

5. Change in income:

The demand for goods and services is also affected by change in income of the consumers.

If the consumer's income increases, they will demand more goods or services even at a higher price.

6. Change in fashion,Habit,custom:

The law of demand is not applicable when the goods are considered to be out of fashion.

7. Basic necessities of life:

In case of basic necessities of life such as salt, rice, medicine, etc. the law of demand is not applicable as the demand for such necessary goods does not change with the rise or fall in price.

Change in quantity demand

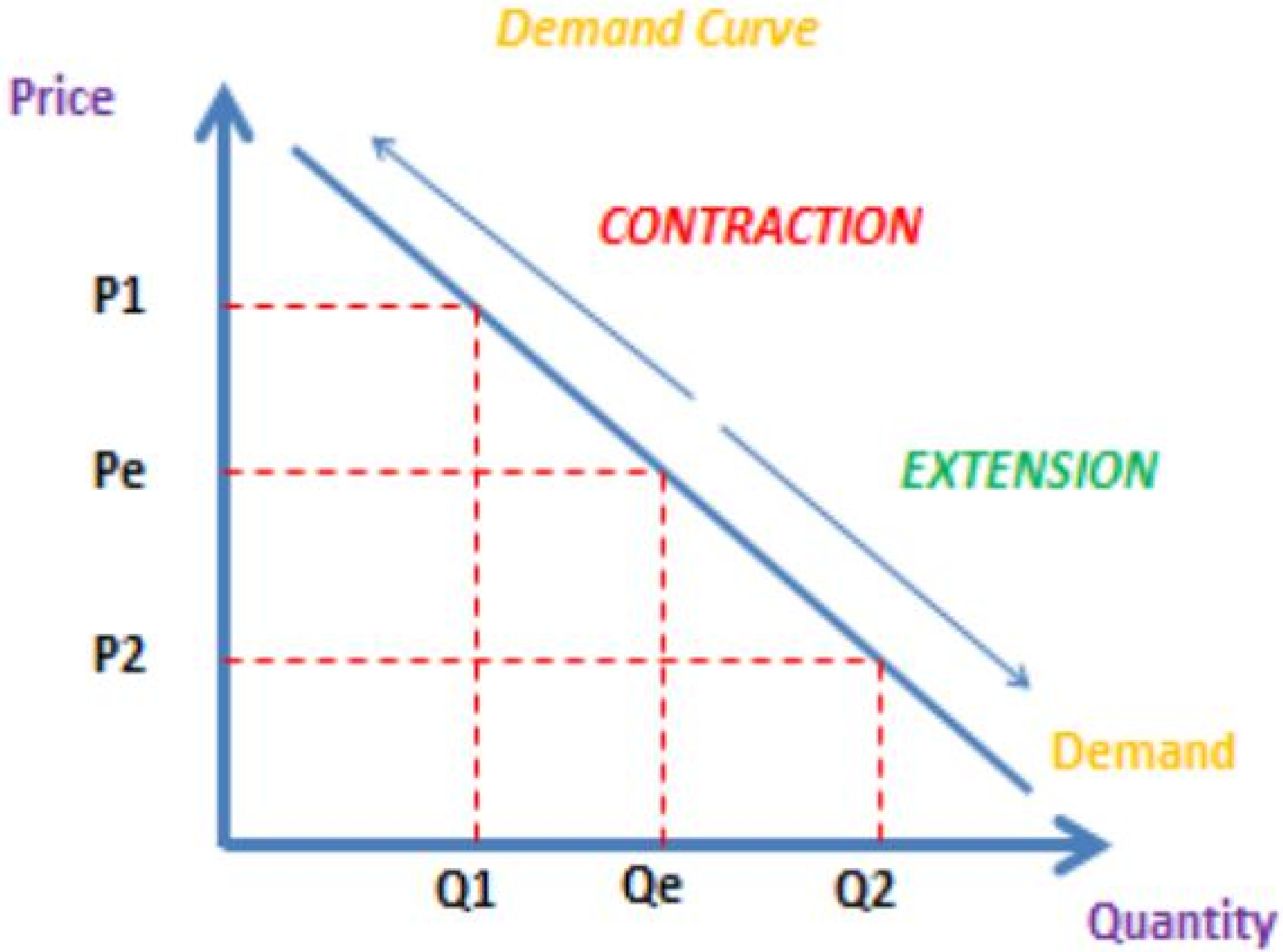
Change in quantity demanded refers to change in the quantity purchased due to increase or decrease in the price of a product.

1. Extension of Demand:

   Expansion of demand refers to the period when quantity demanded is more because of the fall in prices of a product.

2. **Contraction of Demand:**

   Contraction of demand takes place when the quantity demanded is less due to rise in the price of a product.



Demand Curve
Price
CONTRACTION
P1
Pe
EXTENSION
P2
Demand
Q1
Qe
Q2
Quantity

Increase and Decrease in Demand:

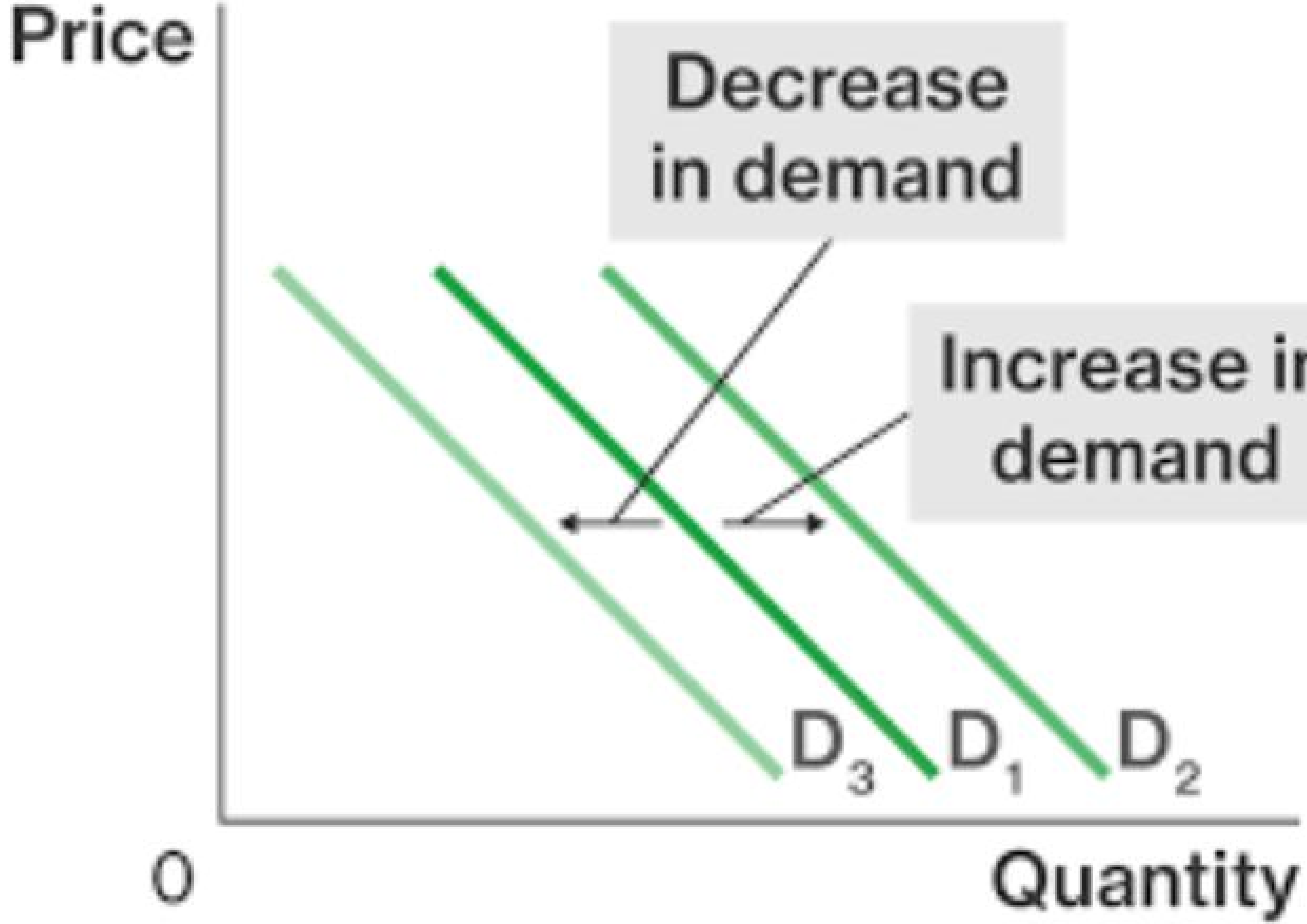
Increase and decrease in demand are referred to change in demand due to changes in various other factors such as change in income, distribution of income, change in consumer's tastes and preferences, change in the price of related goods

Increase in Demand: increase in demand refers to the rise in demand of a product at a given price.

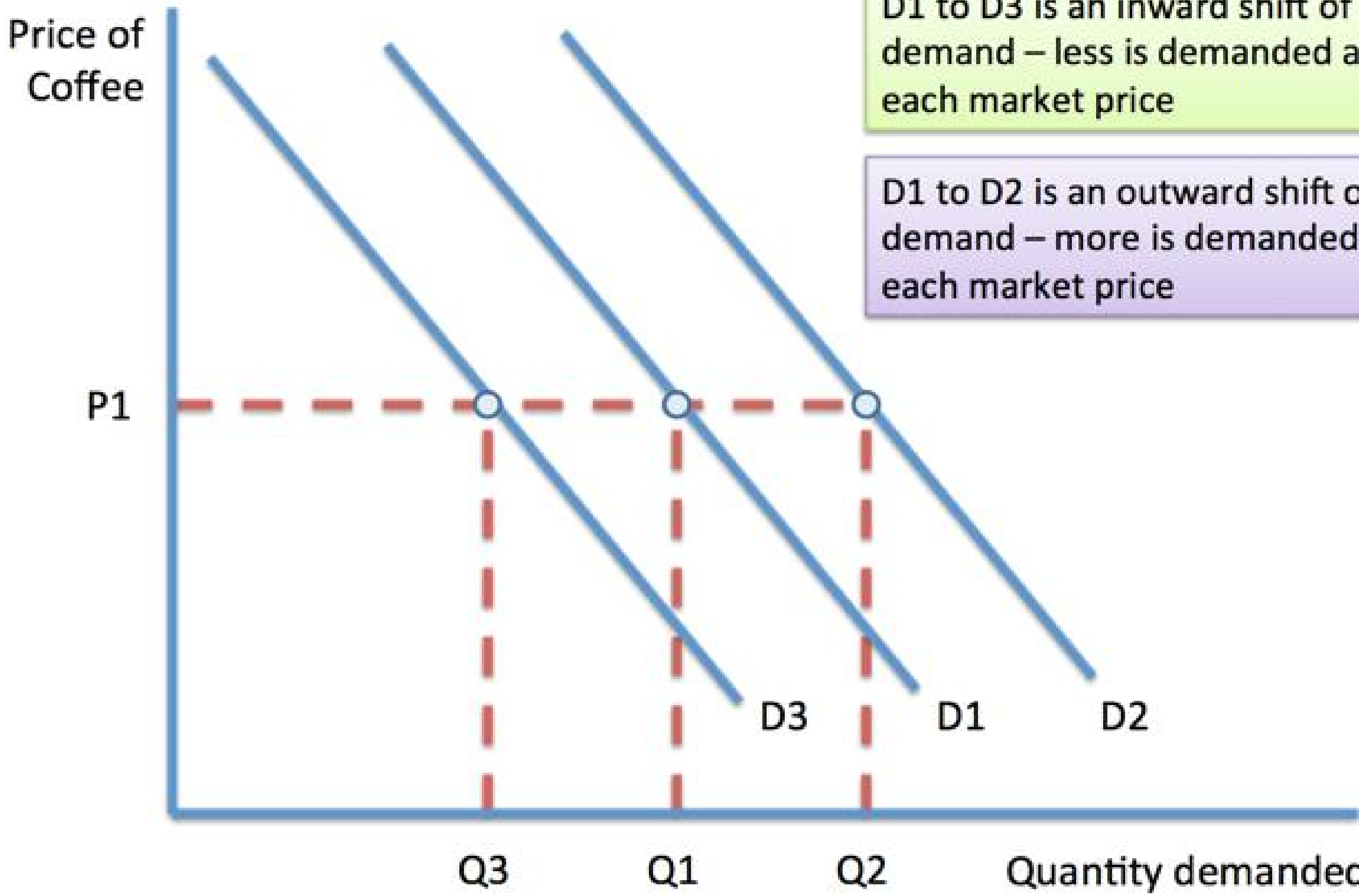
Same price more Demand

Decrease in Demand: Decrease in demand refers to the fall in demand of a product at a given price.

Same price less Demand.


Price
Decrease
in demand
Increase in
demand
D_3
D_1
D_2
0
Quantity

Illustrating Shifts in the Demand Curve



D1 to D3 is an inward shift of demand – less is demanded at each market price

D1 to D2 is an outward shift of demand – more is demanded at each market price