

Course– PRINCIPLES OF ECONOMICS

Lecture 9 LAW OF DEMAND

July, 2015



TOPICS TO BE DISCUSSED

1. Law of Demand:

- Statement
- Assumptions
- Explanation through Demand Schedule and Curve

2. Factors Affecting Demand

- Income of households
- Taste and Preferences
- Other Factors

LAW OF DEMAND

Other things remaining constant, as price rises, the quantity demanded decreases, and as price falls, the quantity demanded increases.

There is an inverse relationship between price and the quantity demanded, *Ceteris Paribas*.

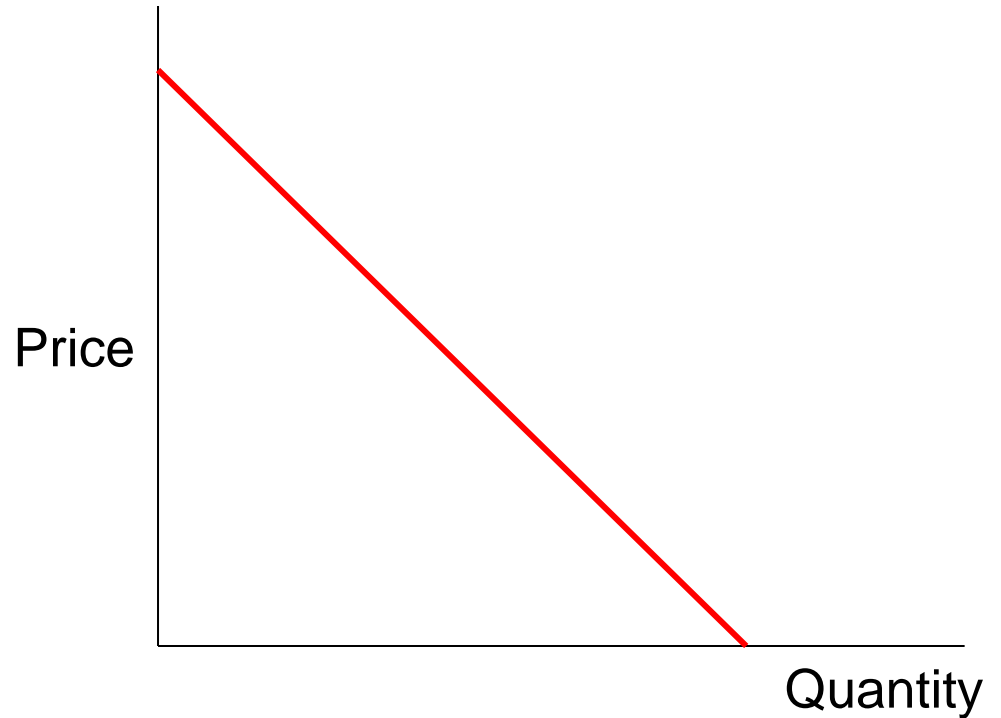
- $Q_d = f(P_x)$

LAW OF DEMAND: ASSUMPTIONS

- No change in taste and preferences.
- Income of the consumer is constant.
- No change in customs, habit, quality of goods.
- No change in substitute products, related products and the price of the product.
- No change in government policies
- No change in advertising expenditure

LAW OF DEMAND: DEMAND SCHEDULE & CURVE

Demand for Milk	
Price (Rs./Kg)	Quantity (Kg.)
1	40
2	30
3	20
4	10



Demand Curve Slopes Downwards

Why Does Demand Curve Slope Downwards? Or Reasons Behind Law of Demand

- Principle/law of diminishing marginal utility
- Income Effect- Fall in Price leads to increase in real income
- substitution effect- Consumers prefer to substitute cheaper goods for dearer ones.
- Different Uses

DEMAND FUNCTION

Demand Function- describes the functional relationship between quantity demanded and the factors which affect it.

$$Q_d = f(P, P_r, I, T, A, G_p, N)$$

P = Price of the commodity

P_r = Price of related goods

I = Income of the Consumers

A = Advertising Expenditure

G_p = Govt. Policies

N = Population (No. of Consumers)

Also known as Determinants of Demand

INDIVIDUAL Vs MARKET DEMAND FUNCTION

Individual Demand Function- describes the relationship between quantity demanded of a commodity by an individual and the factors which affect it.

$$Q_d = f(P, P_r, I, T, A)$$

$$Q_d = a - bP_x$$

$$Q_d = 10 - 2P$$

a= Intercept, Initial demand irrespective of price

b=coefficient showing slope of the function

Negative sign with b shows the inverse relationship between price and quantity demanded

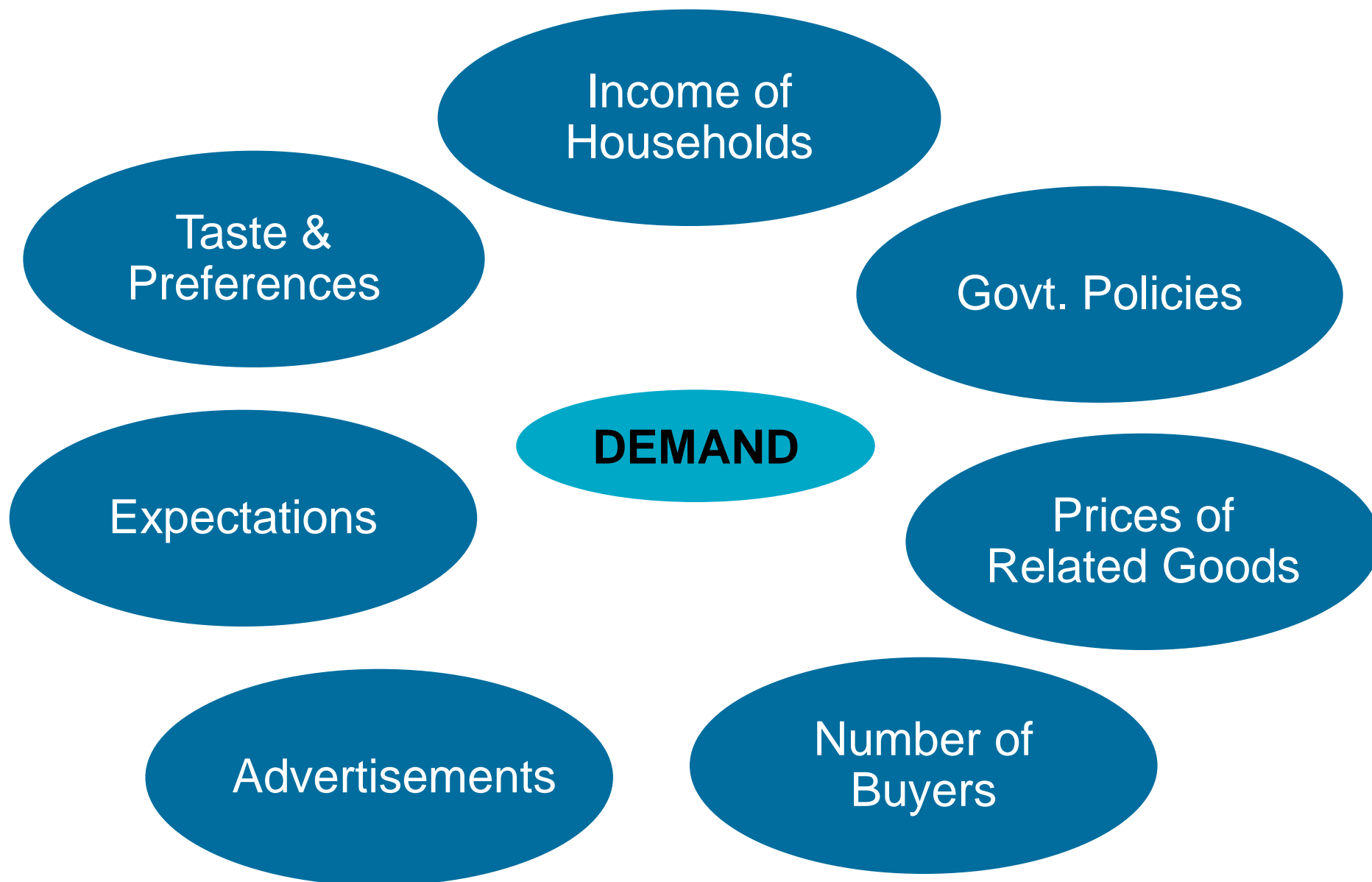
Market Demand Function- describes the relationship between quantity demanded of a commodity by all the individuals together in the market and the factors which affect it.

$$Q_d = f(P, P_r, I, T, A, G_p, N)$$

Example: $Q_A = 10 - 2P, Q_B = 20 - 4P, Q_C = 30 - 6P$

$$\begin{aligned} Q_M &= Q_A + Q_B + Q_C = (10 - 2P) + (20 - 4P) + (30 - 6P) \\ &= 60 - 12P \end{aligned}$$

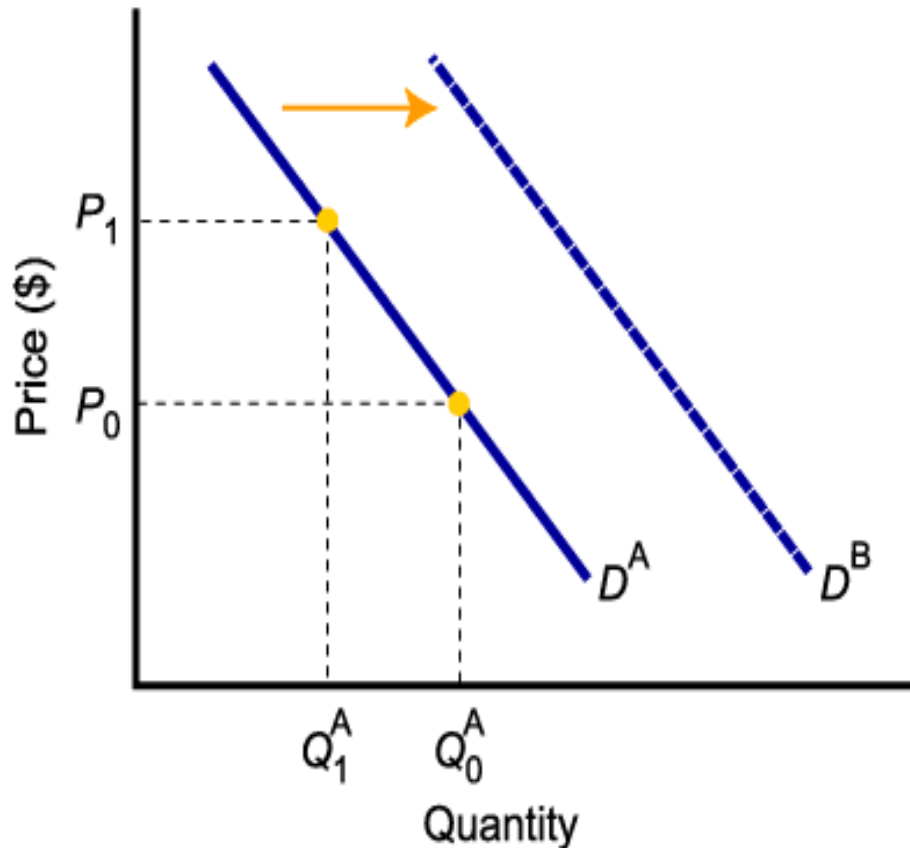
NON-PRICE DETERMINANTS OF DEMAND



RELATED GOODS

- ***Substitutes*** are goods that can serve as replacements for one another; when the price of one increases, demand for the other goes up. *Example: Tea and Coffee*
- ***Complements*** are goods that “go together”; a decrease in the price of one results in an increase in demand for the other, and vice versa. *Example: Car and Petrol*

SHIFT OF DEMAND VS MOVEMENT ALONG A DEMAND CURVE



- A change in **demand** is not the same as a change in **quantity demanded**.
- In this diagram, a higher price causes lower **quantity demanded**.
- Changes in determinants of demand, other than price, cause a change in **demand**, or a **shift** of the entire demand curve, from D_A to D_B .

THANK YOU 😊