Kazakh University of International Relations and World Languages named after Abylai khan.

Demand

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Plan

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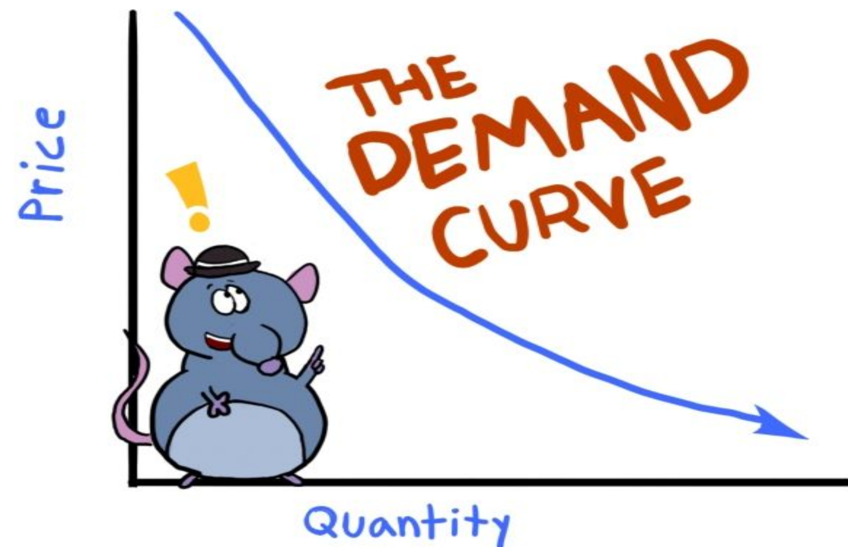
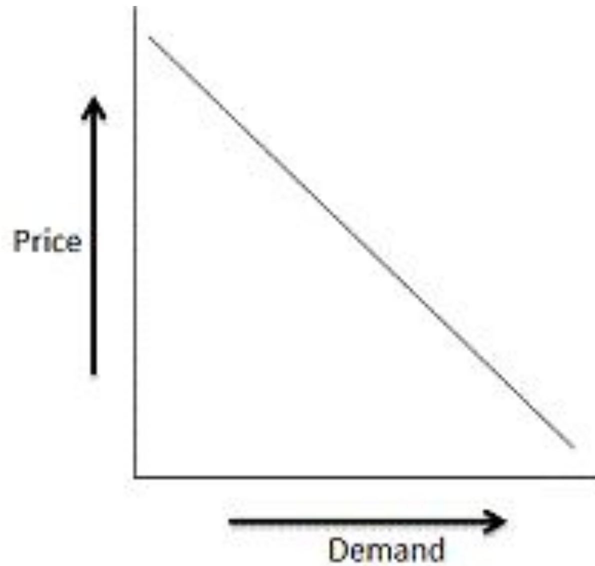
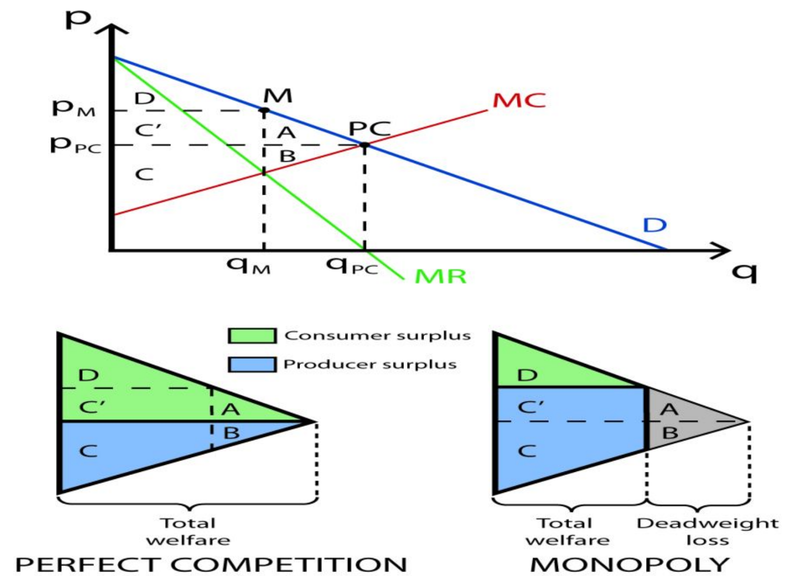
What`s the demand?

Demand is the economic term for the cumulative wants and desires of consumers as they relate to a particular good or service. Generally speaking, if all other factors remain constant, as demand increases for a good, so does the price of that good. Think of demand in the context of an auction. If only one person bids on the item being auctioned, the price does not move. But if a lot of people start bidding, the price goes up. The more people who bid, the higher the price continues to go.







The figure above depicts the most basic relationship between the price of a good and its demand from the standpoint of the consumer. This is actually one of the most important differences between the supply curve and the demand curve. Whereas supply graphs are drawn from the perspective of the producer, demand is portrayed from the perspective of the consumer.

As the price of a good increases the demand for the product will, except for a few obscure situations, tend to decrease.

For purposes of our discussion, let's assume that the product in question is television sets. If TVs are sold for the cheap price of $5 each, then a large number of consumers will purchase the sets at a high frequency. Most people would even buy more TVs than they need - putting a television in every room and perhaps even some in storage. Essentially, because everyone can easily afford a TV, the demand for these products will remain high. On the other hand, if the price of television sets is $50,000, this gadget will be a rare consumer product as only the wealthy would be able to afford the purchase. While most people would still like to purchase TVs, at that price, demand for them would be extremely low.

The law of demand

The law of demand is one of the most fundamental principles in microeconomics. It's all about how price affects demand. According to the law of demand, for all other things remaining constant, the lower the price of a good or service, the higher the demand will be. Conversely, the higher the price, the lower the demand.
If you were to graph this relationship with the quantity demanded on the x axis and the price on the y axis, the relationship between price and demand would be a downward sloping curve from left to right. This line is referred to as a demand curve. Movement along the demand curve shows demand expanding or demand contracting. The people of Loneland are willing to pay $1000 for a computer when there are 2000 computers in the market. However, if the price falls to $500, Loneland people will demand 3000 computers.

Law of Demand

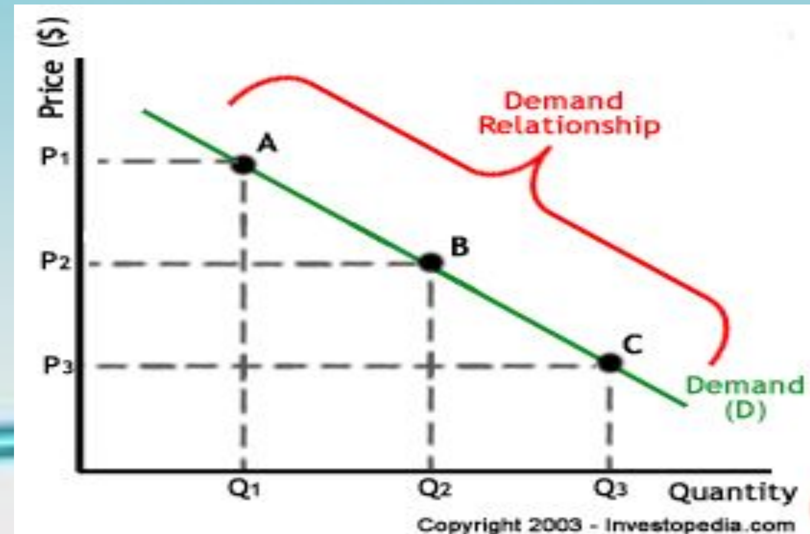
When the price goes up...

...the quantity demanded goes down.

NOTE: *The relationship between price and quantity is inverse.*

When the price goes down...

...the quantity demanded goes up.



This is an example of a change in the demand curve where price is the only variable affecting quantity demanded (or viceversa). In real life, things other than price can affect demand, including income in the economy, price changes in competitive goods, and swings in consumer preferences. This type of change in demand is called a shift of the demand curve.

Imagine the island of Loneland just discovered a huge reserve of oil underground, and now all of its citizens are considerably richer. In this case, the demand curve for computers would actually shift upwards, since their incomes increased. Demand curves shift based on external factors, rather than the quantity demanded or the price.

Determinants of (Factors affecting) demand

Price of related goods:

Personal Disposable Income

Tastes or preferences

Consumer expectations

Population

Good's own price:

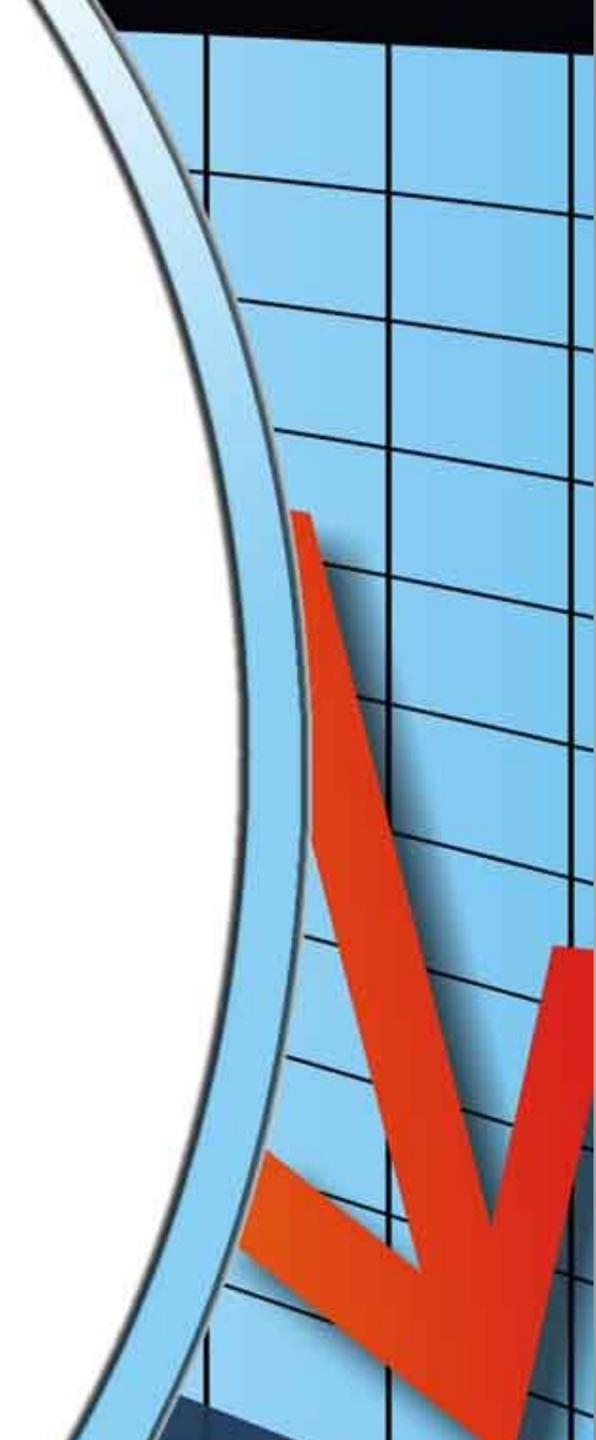
Cross elasticity of demand measures the quantity demanded of one good in response to a change in price of another.

If two goods can be substituted for one another, consumers will usually buy one when the price of another increases.

For example, if the price of butter increases and everything else stays the same, the demand for margarine is likely to grow as consumers try a substitute.

Calculate the cross elasticity of demand by taking the percentage of change in the quantity demanded of one good and dividing it by the percentage of change in price of a substitute.

$$\text{cross-price elasticity of demand} = \frac{\text{percentage change in quantity demanded of good } X}{\text{percentage change in price of some other good } Y}$$



Income elasticity of demand is a measure of how consumer demand changes when income changes. The formula for income elasticity of demand is: Income Elasticity of Demand = % Change in Quantity Demanded/% Change in Income.

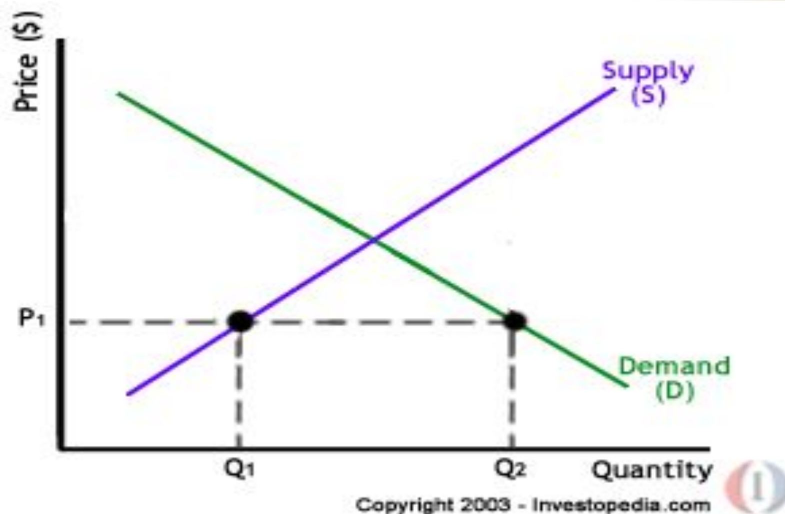
Plotting income elasticity of demand on a graph, where income is on the X-axis and quantity is on the Y-axis will render a line that has a unique slope according to the type of good.

For instance, luxury items have a positive income elasticity of demand. On the graph, a luxury good's curve will slope upward from left to right, meaning as income increases, demand for those types of good increases. The steeper the slope, the more income elastic the good is said to be.

Excess Demand

Excess demand is created when price is set below the equilibrium price. Because the price is so low, too many consumers want the good while producers are not making enough of it.

In this situation, at price P1, the quantity of goods demanded by consumers at this price is Q2. Conversely, the quantity of goods that producers are willing to produce at this price is Q1. Thus, there are too few goods being produced to satisfy the wants (demand) of the consumers. However, as consumers have to compete with one other to buy the good at this price, the demand will push the price up, making suppliers want to supply more and bringing the price closer to its equilibrium.



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