Unit III

Demand – determinants of demand – law of demand- exceptions to law of demand-elasticity of demand- types of elasticity –measurement –factors influencing elasticity of demand uses –consumer surplus

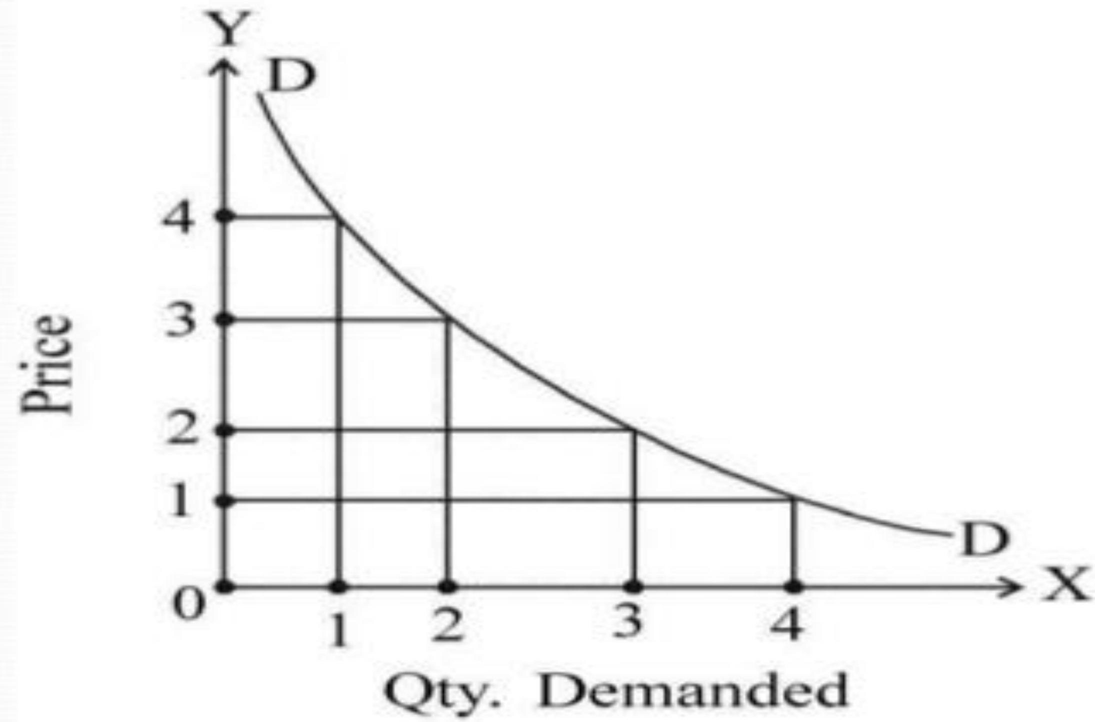
- "It is the amount of goods and services consumers are willing and able to buy at a given period of time".

- Thus desire for a good accompanied by enough purchasing power and willingness to pay determine the demand for that particular commodity.

The Law of Demand…

- The law of demand presents the functional relationship between price and quantity demanded.
- The statement of the law is as follows:
- “Other things remaining constant, the quantity demanded increases when price falls and quantity demanded decreases when price rises”.
- Thus price and quantity demanded are inversely related keeping other affecting variables constant.

Demand Curve



Determinants of Demand

- The following determinants cause shifts in the entire demand curve:

1. Change in consumer tastes
2. Change in the number of buyers
3. Change in consumer incomes
4. Change in the prices of complementary and substitute goods
5. Change in consumer expectations

Exceptions of law of demand

- The following points highlight the six important exceptions to the law of demand. The exceptions are:
- 1. Speculative Demand
- 2. Snob Appeal or Veblen Good
- 3. Using Price as an Index of Quality
- 4. Giffen Good
- 5. Possibility of Future Rise in Prices
- 6. Highly Essential Good.

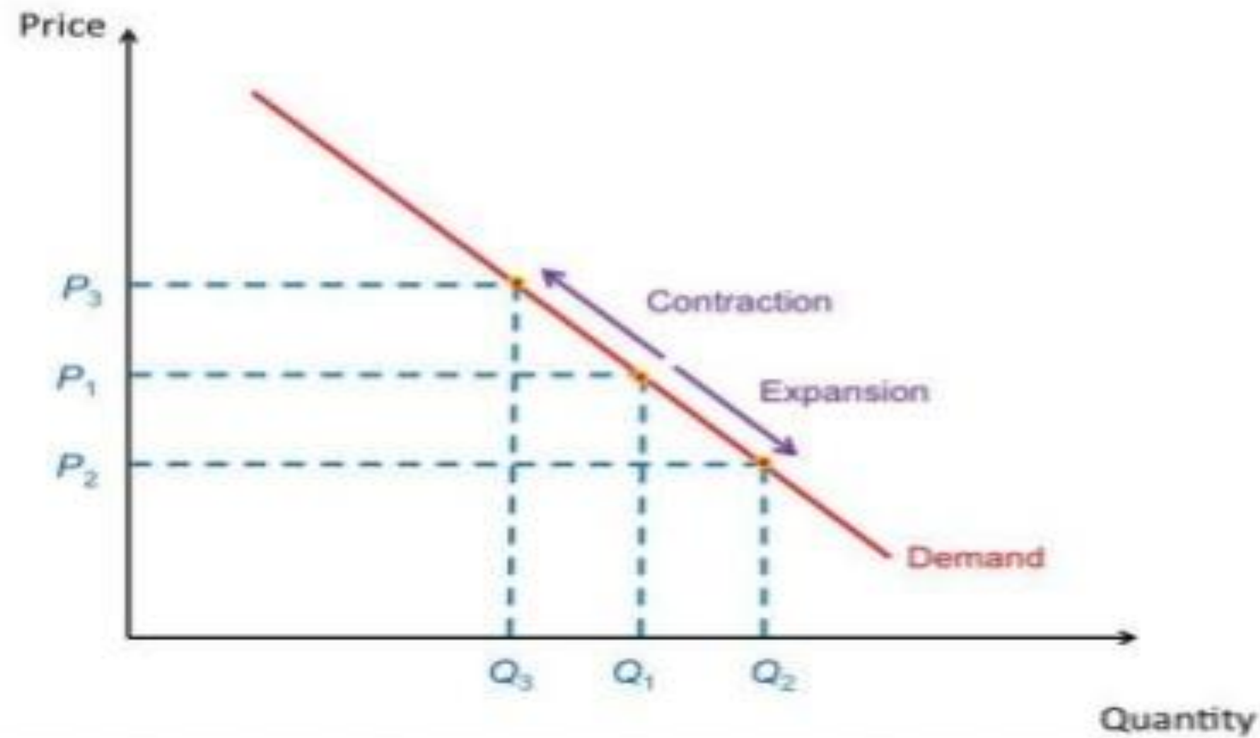
Extension and Contraction of Demand...

- The change in demand due to change in price only, where other factors remaining constant, it is called extension and contraction of demand.

- When the quantity demanded of a commodity rises due to a fall in price, it is called extension of demand.

- When the quantity of demanded falls due to rise in price, it is called contraction of demand.

…Extension and Contraction of Demand



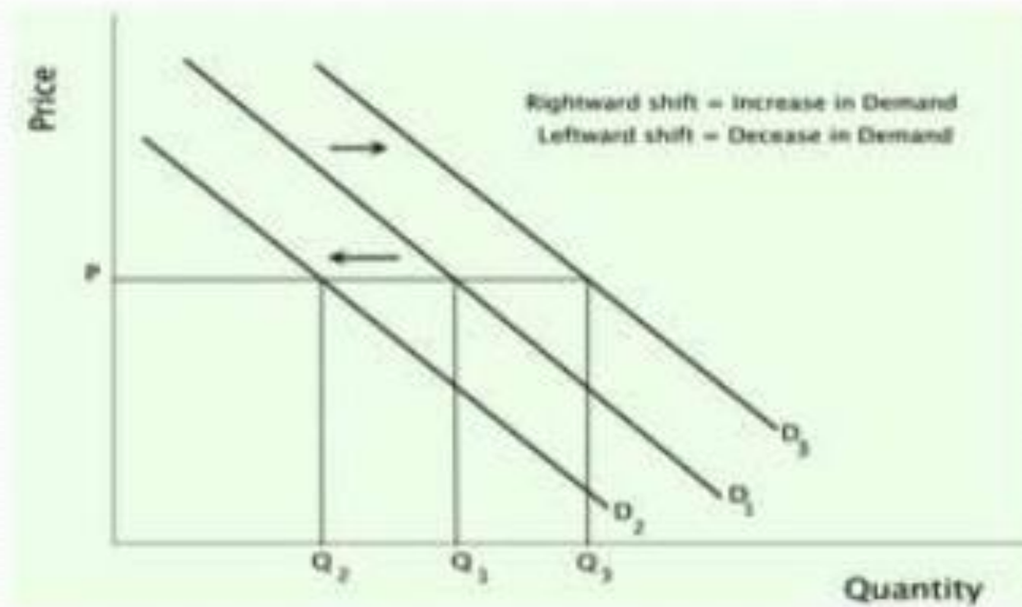
Shift in Demand…

- When the demand changes due to changes in other factors, like taste and preferences, income, price of related goods etc., it is called shift in demand.

- Due to changes in other factors, if the consumer buy more goods, it is called increase in demand or upward shift.

- If the consumer buy fewer goods due to change in other factors, it is called downward shift or decrease in demand.

...Shift in Demand



...Elasticity of Demand

- The degree of responsiveness in quantity demanded to a change in price.
- It represents the rate of change in quantity demanded due to change in price.
- Thus it measures the effect of a change in any factor affecting demand on the total consumption expenditure on a product.

Types of Demand Elasticity

- There are mainly three types of elasticity of demand.

1. Price Elasticity of Demand
2. Income Elasticity of Demand
3. Cross Elasticity of Demand

Types of Price Elasticity

- There are five types of price elasticity of demand.

1. Perfectly elastic demand ($e = \infty$)
2. Perfectly inelastic demand ($e = 0$)
3. Relatively elastic demand ($e > 1$)
4. Relatively inelastic demand ($e < 1$)
5. Unitary elastic demand ($e = 1$)

Determinants of Elasticity

- Nature of commodity
- Availability/range of substitutes
- Extent/variety of uses
- Postponement/urgency of demand
- Income level
- Amount of money spend on the commodity
- Durability of commodity
- Purchase frequency of a product/time
- Range of prices
- Others

METHODS OF MEASUREMENT OF ELASTICITY

1. Percentage method or proportionate method
2. Total outlay method or total revenue method
3. Geometric method or point method
4. Arc elasticity of demand

Importance of elasticity of demand

- Useful for business
- Fixation of prices
- Helpful to finance minister
- Fixation of wages
- In the sphere of international trade
- Paradox of poverty
- Significant for government economic policies
- Determination of price of public utilities

Meaning –CONSUMER SURPLUS

- Alfred Marshall, British Economist defines consumer’s surplus as follows: “Excess of the price that a consumer would be willing to pay rather than go without a commodity over that which he actually pays.”
- Hence, Consumer’s Surplus = The price a consumer is ready to pay – The price he actually pays

REFERENCES

- https://www.slideshare.net/ShompaDhali/elasticity-of-demand-112668060
- https://www.slideshare.net/gannibhai/10-revenue