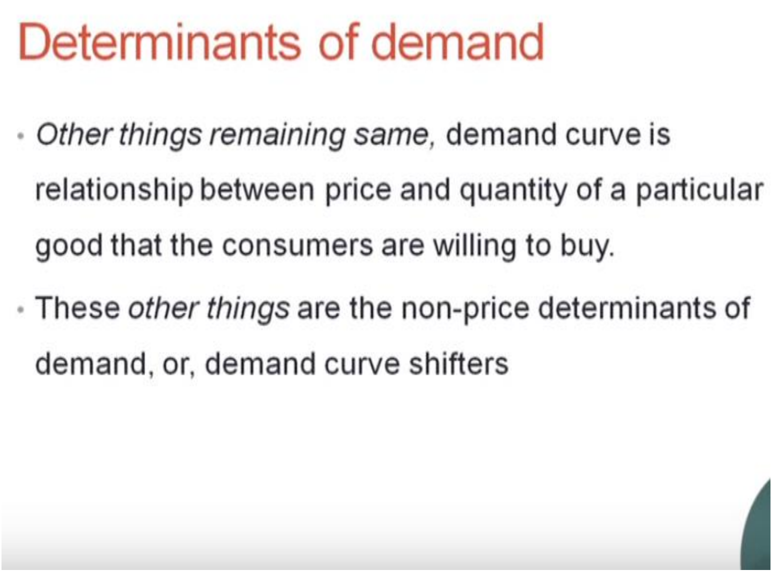
Foundation Course in Managerial Economics
Prof. Barnali Nag
Vinod Gupta School of Management
Indian Institute of Technology-Kharagpur

Lecture - 03
Determinants of Demand

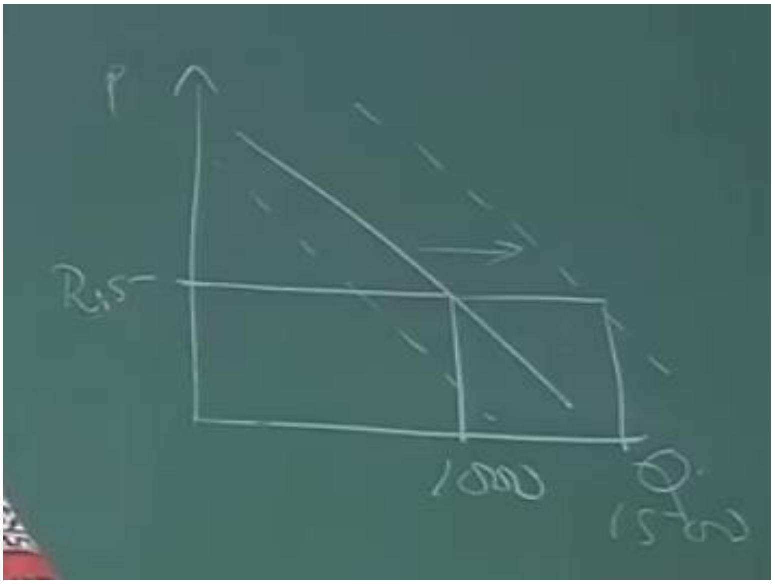
Welcome to the third module of the of this week's lecture on Demand and Supply. We started with the demand supply framework and we discussed how demand is determined in the market and we have not yet talked about the supply side. In this module I am going to discuss about the price and non-price determinants of demand. So I showed in the previous module that demand is a function of the price of a good and also a lot of factors which could influence demand.

(Refer Slide Time: 01:02)



So what are the determinants of demand? Now other things remaining same demand curve is relationship between price and quantity of a particular good that the consumers are willing to buy. Now other things remaining same, this is italicized, because as I had mentioned earlier that there are lot of factors which influence demand and the demand curve that I drew for say for Tom, the relationship between price and quantity, price and quantity of ice-creams.

(Refer Slide Time: 01:35)



So this, this was the demand curve for either the individual Tom or we can imagine this to be the demand curve for the market of ice-creams. Other things remaining same means that the price of other products say for example frozen desserts or cold drinks or other alternatives of ice-cream that the consumer might consider, those prices are same; people's tastes are same, the weather is same outside.

So given all the variables that can influence demand being same how changes in price is going to change my demand for a certain good say in this example the demand for ice-creams. So if the price of ice-cream falls, I am going to demand more of it. If the price of ice-cream increases I am going to demand less of it. So that is the demand of ice-creams.

Now, focusing on the other things. These other things are the non-price determinants of demand or demand curve shifters. So say for example if any of the variables that I talked about in the which determine demand, any of the variables they change, then the demand curve is going to basically change right or left. That is for the same price now the consumer is going to demand either more of that good or less of that good depending on which variable has changed. So let us see some examples.

(Refer Slide Time: 03:14)

So these are the non-price determinants of demand. Number one is the number of buyers. Say let us take an example of a college campus where there is a book shop. Now if the college campus the college has increased the number of seats for students this year and more number of students have joined the college the demand for books is going to go up. So basically the demand curve shifts to the right if the number of students has gone up in the college campus this year. So the number of buyers increasing increases the market demand curve.

Second is income. As I already said that if someone has more of income he is he or she is probably going to demand more of a good. If I am rich, probably I can afford more ice-creams, more pizzas, more of the good stuff and if I am not so rich I am going to demand less. So if my income goes up, I have a big promotion, I am going to probably demand more of some goods.

Now there is a difference. There is something called normal good and there is something called inferior good. Now, what is normal good? Normal good is, the demand for normal good increases with income. So this is what I said the good stuff about. It is the all those things that I would ideally like to consume more but I could not because I had less income.

So when my income goes up I am going to start consuming more of these goods. So in case of normal goods again my demand curve is going to shift to the right if my income goes up but there are certain goods which are called inferior goods. These are goods where if my income goes up I would like to probably like to consume less of these goods or maybe I am probably shifting to other kind of goods.

A good example could be the quality of rice that I consume. So if my income goes up, I am going to consume probably better quality rice and the existing quality of rice that I am currently consuming, probably I will stop consuming those rice. So in that case if my income goes up my demand curve is going to shift to the left. So for the same price I am going to consume less of that product. So these are called inferior goods.

Third is the prices of related goods. Related goods means one could be it could be a substitute. As I said in case of ice-creams the price of frozen dessert, kulfi, cool drinks. So these are probably substitute goods and the demand increases with increase in price of substitute. Lot of substitute products one can imagine say for example say tea and coffee beverages.

So imagine in the railway platform there is a person who is selling tea and the price, going price is 5 Rs and that 5 Rs he is probably selling 1000 cups of tea, 1000 cups of tea. Now say there is a coffee outlet somewhere and suddenly that person decides I am going to charge a, he was earlier charging a certain price and he decides I am going to charge much more okay. People are really fond of coffee and I am going to charge a much higher price for coffee.

So in that case, lot of people who were earlier buying coffee they are going to now shift to the tea seller and at the same price that the tea seller was selling his tea at Rs 5 now he is going to sell instead of 1000 units he is going to sell more of those units say 1500 okay. So at the same price his demand increases. So his demand shifts to the right.

On the other hand there are certain kinds of products which have compliments. They are these are called compliments. Say for example say a person who is selling coffee or say in the say for example compliments is say a printer and the ribbon that you use in the printer. They are complimentary goods. So if the price of ribbon goes up, the demand for printer probably is going to go down.

So or if the more importantly say if the price of printer goes up the demand for ribbons is probably going to go down. So these are in case of complimentary goods your the price the way you respond to a price is the same that you respond to the same good and in case of substitute goods your response is going to be in the opposite direction.

Say for example if the price of the substitute good goes up your demand for the good goes up. If the price of the complimentary good goes up your demand for this good goes down. So this was about price of related goods. Another is taste and preference. Taste and preference. Say people have become very environment conscious and they decide we are no longer going to drive petrol driven or diesel driven cars. So what is going to happen?

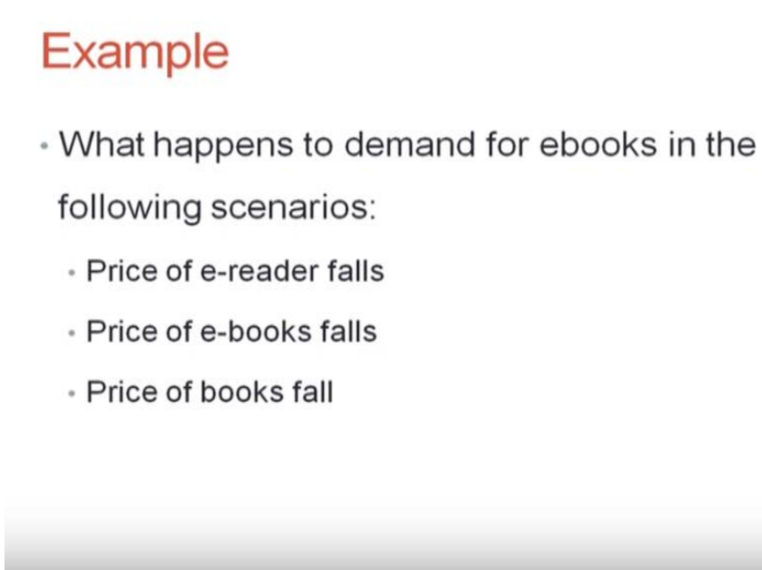
The demand for these petrol driven or diesel driven cars is going to go down and maybe the demand for say battery operated cars are going to go up or say for example people are turning into vegetarians. So the demand for non-veg goods or non-veg items are going to go down and when demand goes down for the same price the demand curve is going to shift to the left and in case of the battery operated car for the same price people are going to demand more of the good. So the demand curve shifts to the right.

Another determinant of demand is expectations. If people are expecting say prices to rise, people are expecting say some festival is coming up and you expect the price of sugar to go up or price of some other fruits and vegetables generally to go up. So you might like to buy more of it and hoard it in your fridge. So your expectation about the price in the future makes you demand more right now.

Say there is some disturbance in the middle-east and you speculate that the price of oil is going to go up. So you might like to fill up your tank right now because you know that probably in the next 15 days, 1 month prices are going to really shoot up. So this is how expectation influences your demand.

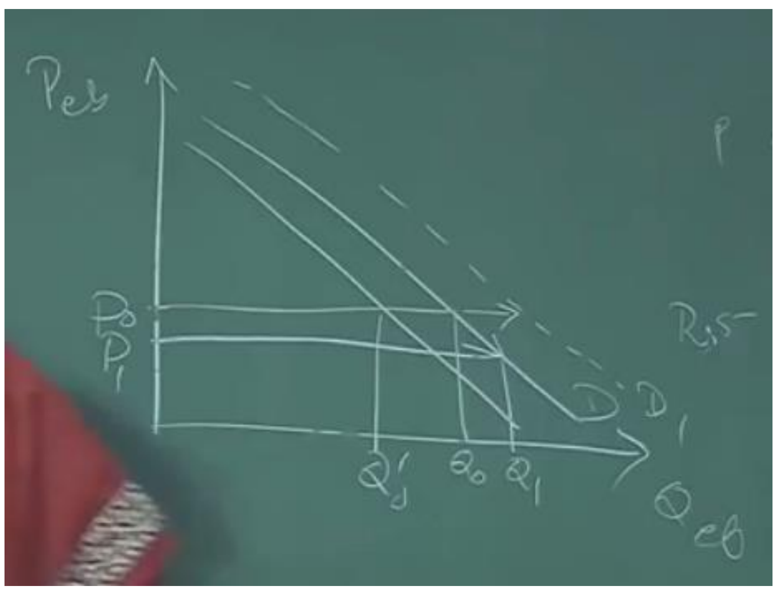
So these are the non-price determinants of demand and the what is price determinant of demand is the price itself. So if the price changes your demand, your movement is going to be along the demand curve and if the non-price determinants they change in the economy the demand curve is basically going to shift to the right, right or the left.

(Refer Slide Time: 11:33)



So let us take an example. What happens to demand for e-books in the following scenarios? So there is a demand for e-books. So let us say this is the demand for e-books and these are the prices of e-books and this is the demand curve.

(Refer Slide Time: 11:47)



So what happens to demand for e-books in the following scenarios? Say price of e-reader falls. So what happens when the price of e-reader falls? What is e-reader basically? E-reader is what you use the e-reader to read the e-books. So if the price of e-reader falls, lot of people are going to start buying the e-readers.

Say for example the demand for kindle goes up in the and you start purchasing kindle online on Amazon and when the price of e-reader falls you buy more of e-readers, the people have started buying more of e-readers and so when they buy e-readers they have to buy e-books also to read on those e-readers. So the demand for e-books also go up.

So for the same price of e-books, if this is the average price of e-books, for the same price of e-books demand goes up. So demand curve shifts to the right. So demand curve shifts to the right. So at every price, at every price, now the number of e-books that is demanded is more than what was there earlier.

Second, say price of e-books fall. So what happens in that case? Do the does the demand curve shift? Does the demand curve shift to the right or left, no. The demand curve does not shift because the price has changed. So when price of e-books fall, so if this was the existing price and price has now fallen, movement is basically along the demand curve and when movement is along the demand curve and this is the new price P1 and this is the new quantity Q1 which is more than the earlier quantity.

So when the price of e-books e-book falls movement is along the demand curve and the total quantity demanded goes up. Price of books fall, say price of paperbacks. The price of paperbacks fall. Then what happens? What are books? Books are basically substitute of e-books. Books are substitute of e-books.

So when price of books fall the demand for e-books is going to go down. People would like to maybe continue to buy more of paperbacks or books. So the demand goes down. So for the same price of e-books now people are demanding less of the e-books. People are demanding less of the e-books. So this is what happens in case of when price of books fall.

So this summarizes how the what are the price and non-price determinants of demand are and we have seen that if the price changes the output changes along the demand curve and all other determinants of demand when they change the demand curve basically shifts to the right or the left. So the quantity demanded can change in response to both price and non-price determinants of demand.

So price is also a determinant of demand and other factors are also determinants of demand but only the non-price determinants shift the demand curve and the price determinant basically leads to movement along the demand curve. In the next module we are going to talk about, we are going to develop the supply curve, we are going to see what are the determinants of supply curve and we are going to see what are the shifters of supply curve. Thank you.