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Demand

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MODEL OF DEMAND

The model of demand is an attempt to explain the amount demanded of any good or service.

DEMAND DEFINED

The amount of a good or service a consumer wants to buy, and is able to buy per unit time.

THE "STANDARD" MODEL OF DEMAND

The DEPENDENT variable is the amount demanded.

The INDEPENDENT variables are:

- the good's own price
- the consumer's money income
- the prices of other goods
- preferences (tastes)

YOU COULD WRITE THE MODEL THIS WAY:

The demand for tacos

$$Q_D(\text{tacos}) = D(P_{\text{tacos}}, \text{Income}, P_{\text{spaghetti}}, P_{\text{beer}}, \text{tastes})$$

ECONOMISTS HAVE HYPOTHESES ABOUT HOW CHANGES IN EACH INDEPENDENT VARIABLE AFFECT THE AMOUNT DEMANDED

THE DEMAND CURVE

The demand curve for any good shows the quantity demanded at each price, holding constant all other determinants of demand.

The DEPENDENT variable is the quantity demanded.

The INDEPENDENT variable is the good's own price.

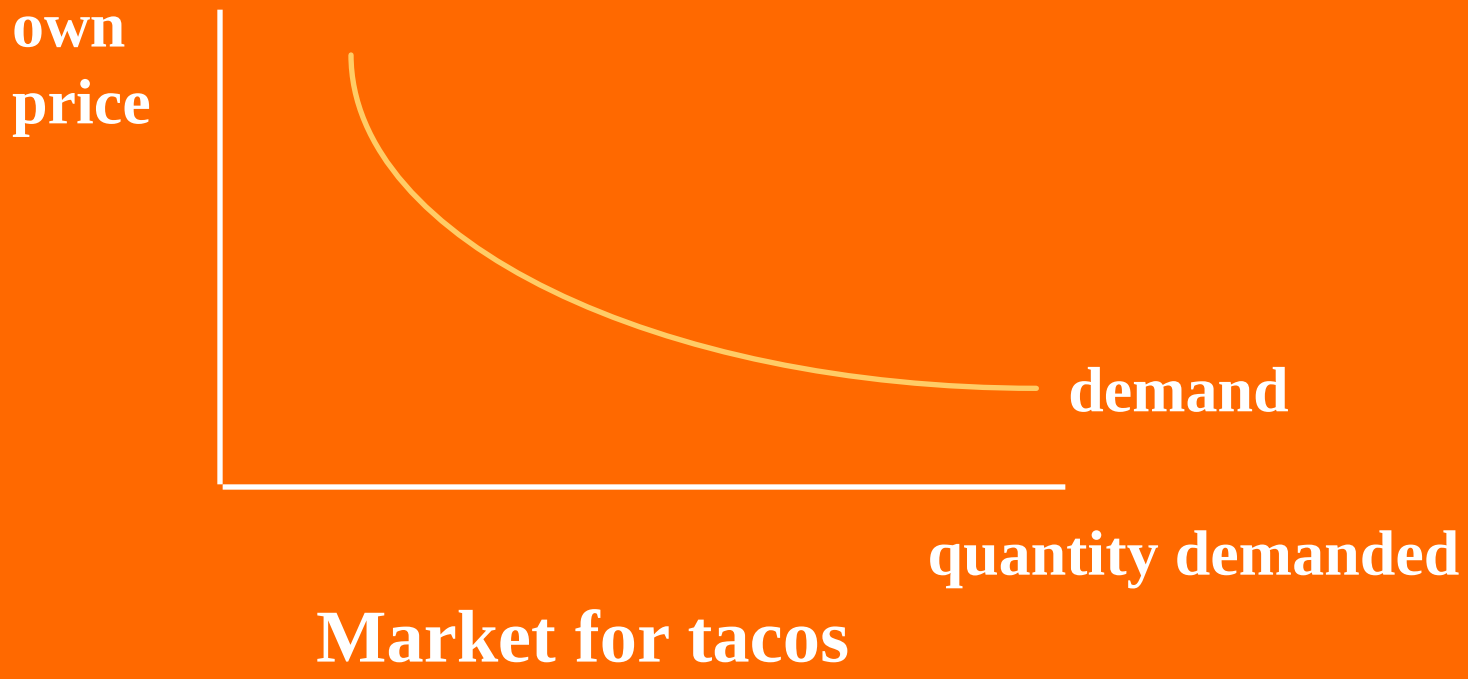
THE LAW OF DEMAND

The Law of Demand says that a decrease in a good's own price will result in an increase in the amount demanded, holding constant all the other determinants of demand.

The Law of Demand says that demand curves are negatively sloped.

A DEMAND CURVE

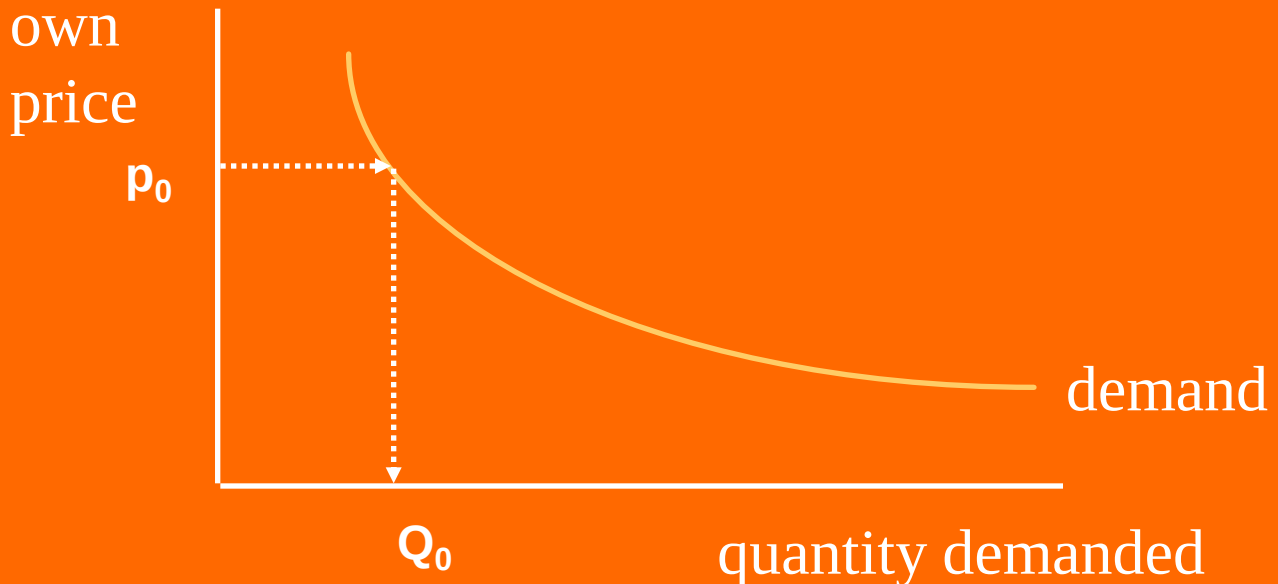
A demand curve must look like this, i.e., be negatively sloped.



Market for tacos

The demand curve means:

You pick a price, such a p_0, and the demand curve shows how much is demanded.



Market for tacos

What if the price of tacos were less than p_0?

How do you show the effect on demand?

Go to hidden slide

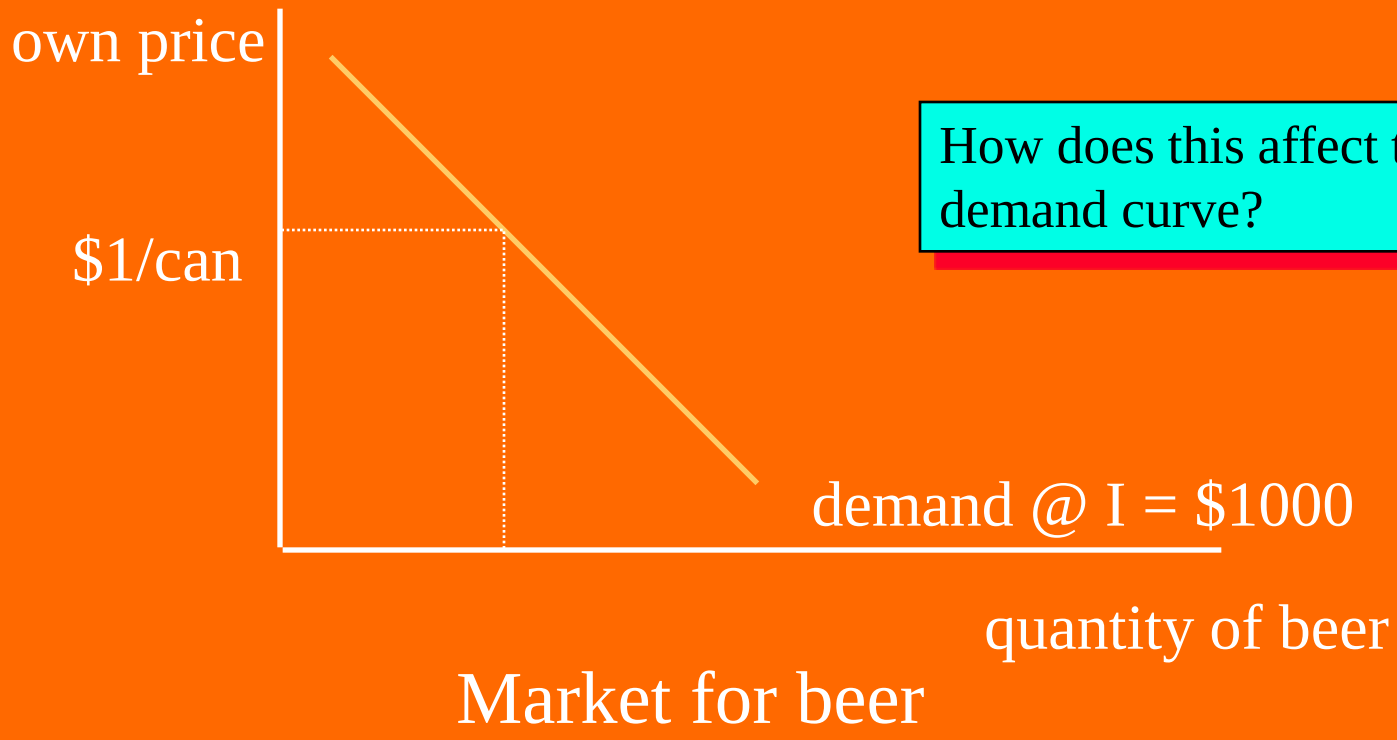
AN IMPORTANT POINT

When drawing a demand curve notice that the axes are reversed from the usual convention of putting the dependent (y) variable on the vertical axis, and the independent (x) variable on the horizontal axis.

Other factors affecting demand

The question here is how to show the effects of changes in income, other goods' prices, and tastes on demand.

Suppose people want to buy more of a good when incomes rise, holding constant all other factors affecting demand, including the good's own price.



How does this affect the demand curve?

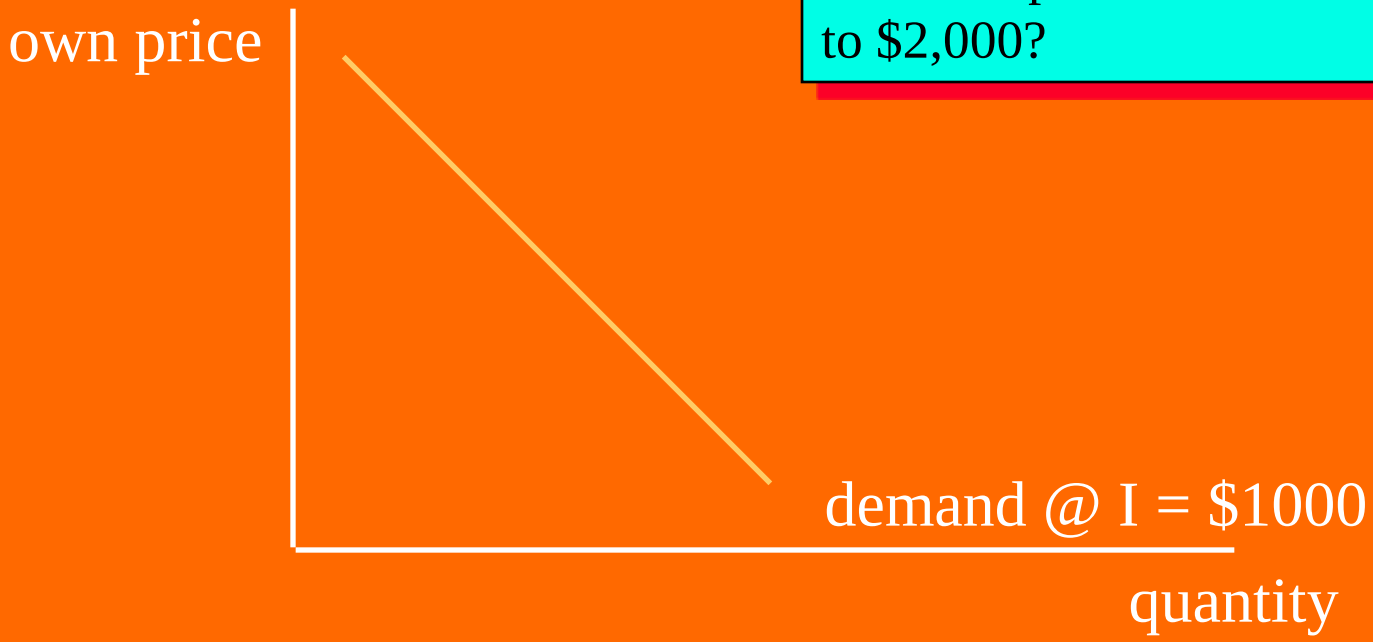
Normal and inferior goods defined

Normal good: When an increase in income causes an increase in demand.

Inferior good: When an increase in income causes a decrease in demand.

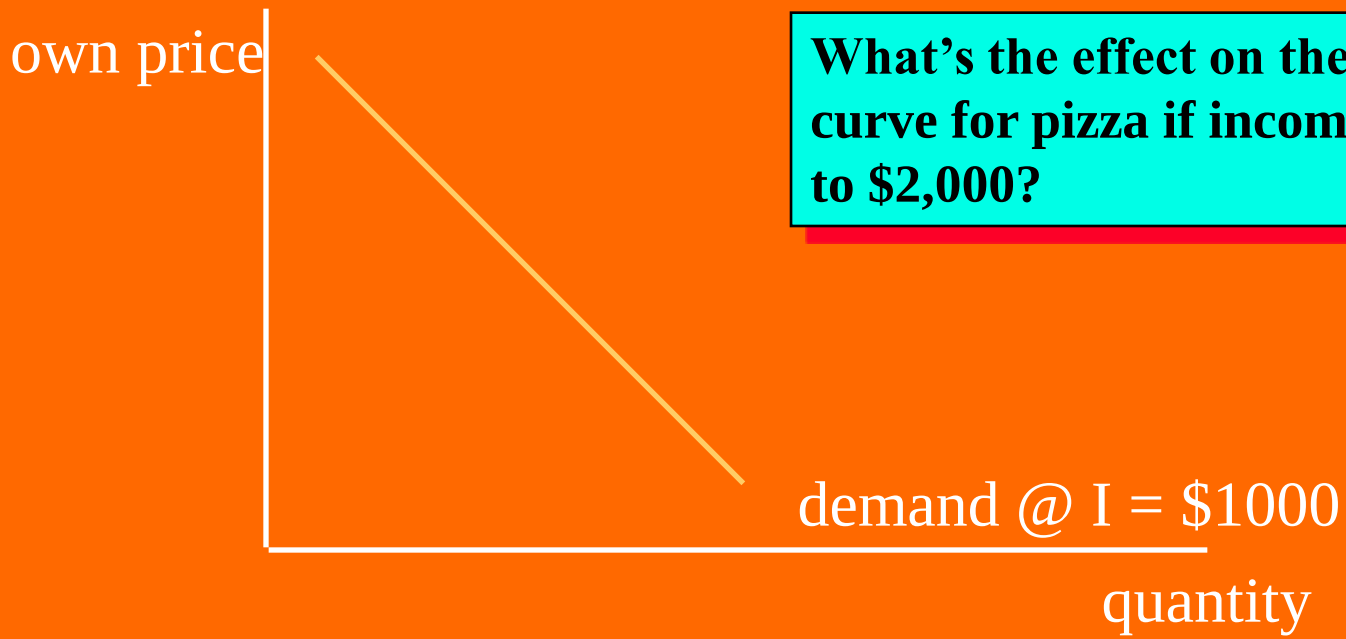
Pizza is a normal good.

What's the effect on the demand curve for pizza if income rises to $2,000?



Market for pizza

Suppose instead that pizza was an inferior good.



What's the effect on the demand curve for pizza if income rises to $2,000?

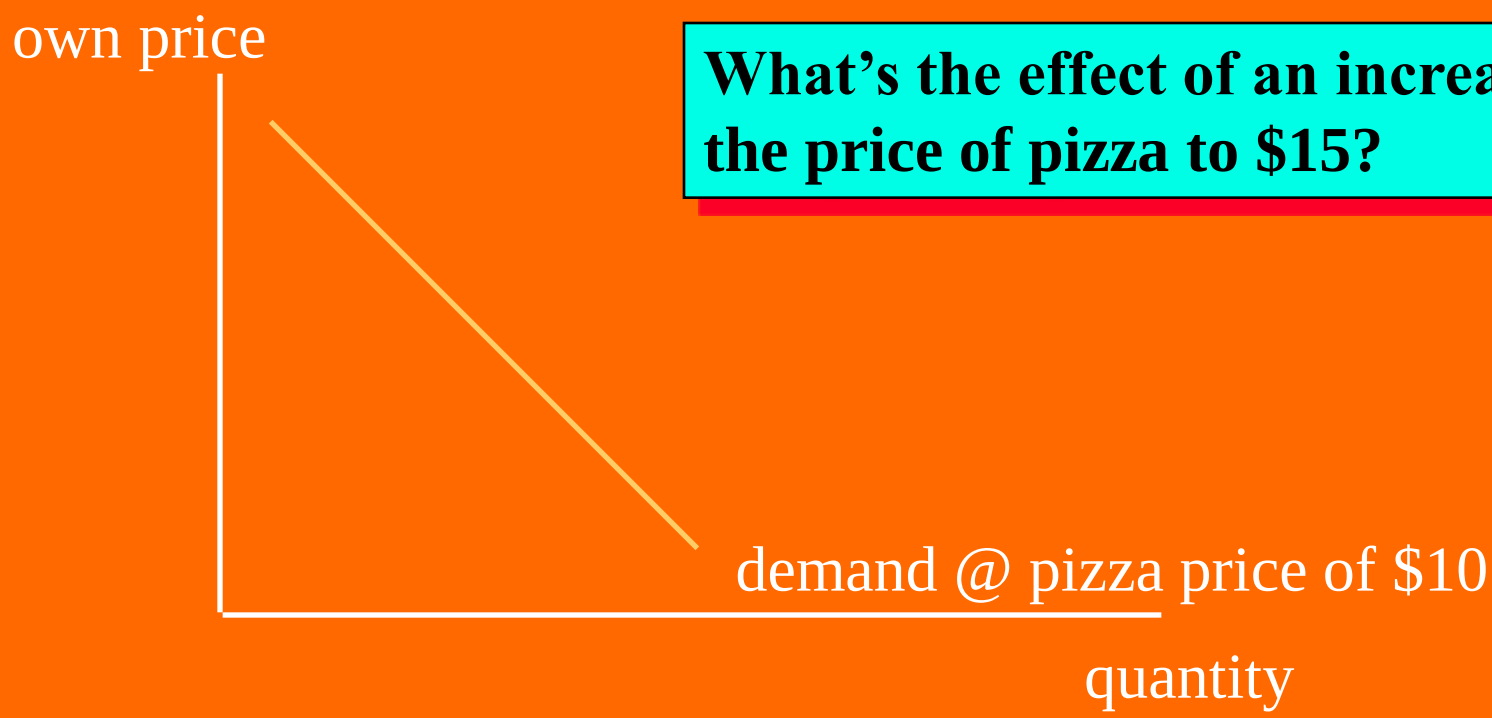
Market for pizza

Substitutes defined

Substitutes: Two goods are substitutes if an increase in the price of one of them causes an increase in the demand for the other.

Thus, an increase in the price of pizza would increase the demand for spaghetti if the goods were substitutes.

The graph shows the demand curve for spaghetti when pizzas cost $10 each.



What's the effect of an increase in the price of pizza to $15?

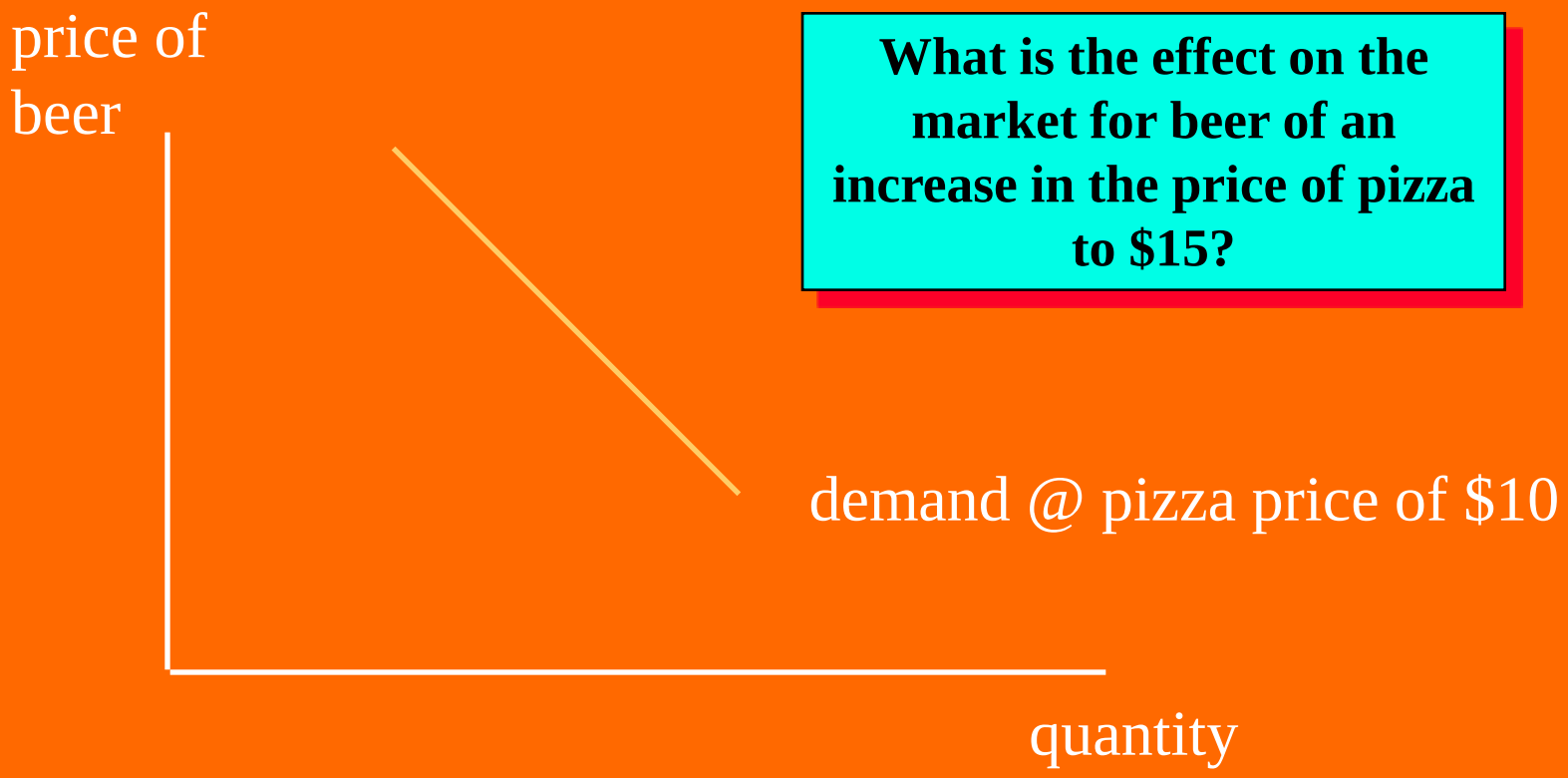
Market for spaghetti

Complements defined

Complements: Two goods are complements if an increase in the price of one of them causes a decrease in the demand for the other.

Thus, an increase in the price of pizza would decrease the demand for beer if the goods were complements.

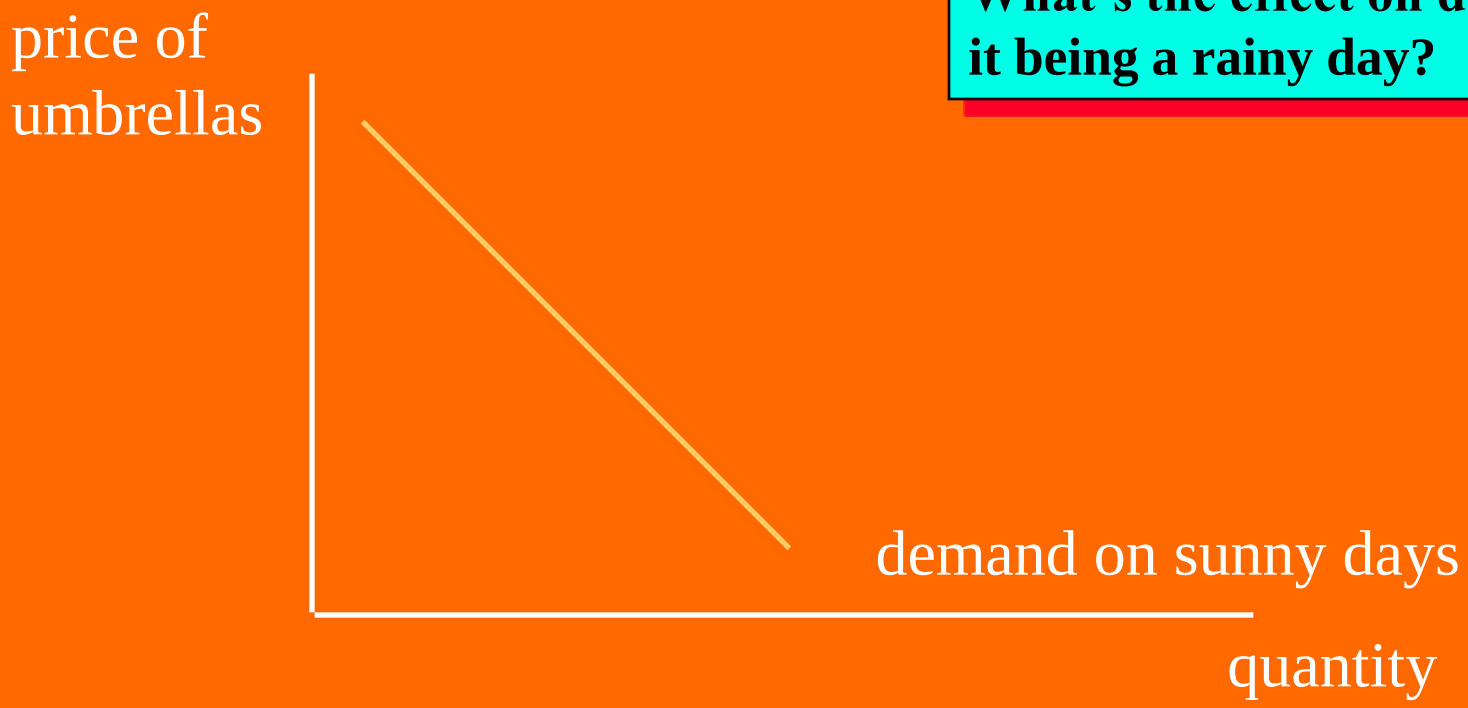
The graph shows the demand curve for beer when pizzas cost $10 each.



What is the effect on the market for beer of an increase in the price of pizza to $15?

The graph shows the demand curve for umbrellas on sunny days.

What's the effect on demand of it being a rainy day?



Market for umbrellas

DEMAND SUMMARY

Demand is a function of own-price, income, prices of other goods, and tastes.

The demand curve shows demand as a function of a good's own price, all else constant.

Changes in own-price show up as movements along a demand curve.

Changes in income, prices of substitutes and complements, and tastes show up as shifts in the demand curve.