Demand And The Consumer

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INTRODUCTION

It is essential for the business managers to have a clear understanding of the following aspects of the demand for their products:

- What are the sources of demand?
- What are the determinants of demand?
- How do the buyers decide the quantity of a product to be purchased?
- How do the buyers respond to the change in a product prices, their income and prices of the related goods?
- How can the total of market demand for a product for a product be assessed and forecast?

These questions are answered by the Theory of Demand.

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Demand

INTRODUCTION:

Demand is the force that drives all business, without a demand for its goods or services, a firm is doomed to failure.

MEANING OF DEMAND:

The amount of a commodity or service which a buyer is willing and able to purchase at a particular set of prices during a given period, is called demand.

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Important Determinants of The Demand

1. **Price of the goods**: The first and leading determinant of the demand for good is price. Usually, higher the price of goods, lesser will be the quantity demanded of them.

2. **Income of the buyer:** The size of income of the buyers also influences the demand for a commodity. Mostly it is true that "larger the income, more will be the quantity demanded".

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3. Prices of Related Goods: The prices of related goods also affect the demand for a good. In some cases, the demand for a good will go up as the price of related good rises.

The goods so inter-related are known as substitutes, e.g. radio and record player.

In some other cases, demand for a good will comes down as the price of related good rises. The goods so inter related are complements, e.g. car and petrol, pen and ink, cart and horse, etc.

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4. Tastes of the buyer:

This is a one-sided factor. A commodity may not be purchased by the consumer even though it is very cheap and useful, if the commodity is not up to his taste or liking.

Contrarily, a good may be purchased by the buyer, even though it is very costly, if it is very much liked by him.

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5. Seasons prevailing at the time of purchase: In winter, the demand for woolen clothes will rise; in summer, the demand for cool drinks rises substantially; in the rainy season, the demand for umbrellas goes up.

6. Fashion: When a new film becomes a success, the type of garments worn by the hero or the heroine or both becomes an article of fashion and the demand goes up for such garments.

7. Advertisement and Sales promotion: Advertisement in newspapers and magazines, on outdoor hoardings on buses and trains and in radio and television broadcasts, etc. have a substantial effect on the demand for the good and thereby improves sales.

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Types of Demand

Joint demand: When several commodities are demanded for a joint purpose or to satisfy a particular want.

E.g. Milk , sugar and tea dust are jointly demanded to make tea. Similarly, we may demand paper, pen and ink for writing. Demand for land, labor, capital and organization for producing commodity is also a case of joint demand.

Composite demand: The demand for a commodity which can be put to several uses is a composite demand. In this case a single product is wanted for a number of uses. For example, electricity is used for lighting, heating, for running the engine, for the fans etc.

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Direct and Derived demand:

The demand for a commodity which is for direct consumption, i.e. Demand for final good, is called direct demand, e.g. food, cloth, etc. Direct demand is called **autonomous demand.**

When the commodity is demanded as a result of the demand for another commodity or service, it is known as the derived demand or **induced demand.** For example, demand for cement is derived from the demand for building construction; demand for tires is derived from the demand for cars or scooters, etc.

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Law of Demand

- The law of demand is one of the important law of consumption which explain the functional relationship between price and quantity demanded of a commodity.

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- "Other thins being equal, the amount demanded increases with a fall in price and diminishes with a rise in price."
- According to Ferguson, "Other things remaining constant, the quantity demanded varies inversely with price i.e. when price falls demand expands or (rises) and when price rises, demand contracts or (falls).
- Marshall's law of demand describes the functional relationship between demand and price.

  It can be presented as $Qd = f(P)$
- This functional relationship is inverse and negative because larger quantity is demanded when price falls and smaller quantity will be demanded when price rises.

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Explanation of the law of demand with the help schedule and diagram

Schedule:

Price of Commodity (P)	Quantity Demanded (Qd)
50	100
40	200
30	300
20	400
10	500

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Paragraph

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- From the above schedule we observe that at a higher price of *Rs*.50 per unit of commodity the quantity demand i.e. 100 units and at a lower price of *Rs*.10, the quantity demand rises to 500 units.
- This shows a inverse relationship between price and quantity demanded.

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Diagram and its explanation

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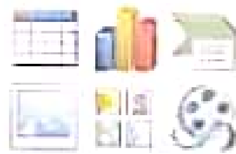

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Assumption of the Law of Demand

The law of demand is based on the following assumption or conditions:

(1) **No change in consumer's income:** Consumer's income must remain unchanged because if income increases consumer may buy more even at a higher price invalidating the law of demand.

(2) **No change in the size of population:** The size of population are assumed to remain constant. As such changes are sure to affect demand.

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(3) **No change in consumer's taste, preference, habits and fashions:** If the taste changes then the consumer's preference also will change which will affect demand. When commodities go out of fashion then demand will be low even at a low price.

(4) **No change in price of related goods:** Related goods may be either substitutes goods or complementary goods. Law of demand will be true only if prices of these goods do not change. Accordingly Qd of Pepsi will change due to change in its price if and only if the price of Coca Cola does not change.

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(5) **No change in tax policy of the Government:** The level of direct and indirect tax imposed by the government on the income and goods should remain constant.

(6) **Fear of rise of price in future:** If consumer think that price of good will increase in future they will store it. In other words, the demand of those goods shall increase at the same price. But this law states that demand should go up only if price falls.

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(7) **No Change in quality:** There should be no change in quality for the validity of this law. Say quality of a commodity decreases, its demand will not increase even its price decreases.

(8) **No Emergency:** In case of emergency, i.e. flood, war etc., the demand for a commodity increases without the increase in its price.

(9) **No change in Weather Conditions:** This law is valid only when weather conditions do not change. For example, in case of ice, this law is valid in summer seasons only and it will not valid in winter season as we observe that for ice decreases in winter even with a decrease in price.

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Why Demand Curve Is Negatively Slope

There are following reasons behind it:

1. **Entry of New Buyers:** Fall in the price of a commodity attracts new buyers in the market. The people hesitating to purchase the commodity at higher prices, now start buying it after the fall in price resulting an increase in its demand.
2. **Income Effect:** when the price of a commodity decreases, purchasing power of the consumer increases . Thus more units are demanded at low price with the same amount of money.
3. **Substitution Effect**: When the price of required commodity falls, while the price of its substitute remains unchanged, the consumers feel that this commodity is now relatively cheaper, therefore its demand increases while, on the other hand the demand for the substitute decreases.

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Importance of the Law of Demand

The law of demand plays a vital role in decision-making and forward planning of a business unit. The production planning in a firm mainly rests on accurate demand analysis. The law of demand has theoretical as well as practical advantages.

These are as follows:

1. Price determination: With the help of law of demand a monopolist fixes the price of his product. He is able to decide the most profitable quantity of output for him

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2. Useful to Government: The finance minister takes the help of this law to know the effects of his tax reforms and policies. Only those commodities which have relatively inelastic demand should be taxed.

3. Useful to farmers: From the law of demand, the farmer knows how far a good or bad crop will affect the economic condition of the farmer. If there is a good crop and demand for it remains the same, price will definitely go down. The farmer will not have much benefit from a good crop, but the rest of the society will be benefited.

4. In the field of planning: The demand schedule has great importance in planning for individual commodities and industries. In such cases it is necessary to know whether a given change in the price of the commodity will have the desired effect on the demand for commodity within the country or abroad. This is known from a study of the nature of demand schedule for the commodity.

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Supply

Introduction:

- Supply is an independent economic activity but it is based on the demand for commodities. The managers' ability to make more profits depends upon his ability to adjust the supply to the demand without creating a surplus while at the same time not creating a scarcity that will spoil the image of the company in the eyes of the public.
- Supply is also sometimes inelastic and sometimes elastic.

- The managers have to take wise decisions to maximize the profits of the firm.

MEANING OF SUPPLY:

The product which a seller is willing and able to sell at a particular set of prices during a specific period of time is called supply.

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Determinants Of Supply

1. The cost of factors of production: Cost depends on the price of factors. Increase in factor cost increases the cost of production, and reduces supply.

2. The state of technology: Use of advanced technology increases productivity of the organization and increases its supply.

3. External factors: External factors like weather influence the supply. If there is a flood, this reduces supply of various agricultural products.

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4. Tax and subsidy: Increase in government subsidies results in more production and higher supply.

5. Transport: Better transport facilities will increase the supply.

6. Price: If the prices are high, the sellers are willing to supply more goods to increase their profit.

7. Price of other goods: The price of other goods is more than ‘X’ then the supply of ‘X’ will be increased.

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Law of Supply

- The law of supply states that, other things remaining the same, the quantity supplied of a commodity is directly or positively related to its price.
- According to J.B. Taylor, the higher the price, higher the quantity supplied and lower the price, lower the quantity supplied.
- "Other things remaining unchanged, the supply of a commodity expands with a rise in its price and contracts with a fall in its price."

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- Functional relationship between supply and price.

  It can be presented as $Qs = f(P)$
- This functional relationship is direct and positive because larger quantity supplied when price rise and smaller quantity will be supplied when price falls.

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Explanation of the law of supply with the help schedule and diagram

Schedule:

Price of Commodity (P)	Quantity Supplied (Qs)
5	10
10	20
15	30
20	40
25	50

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- From the above schedule we observe that at a lower price of *Rs*.5 per unit of commodity the quantity supply is low i.e. only for 10 units and at a higher price of *Rs*.25, the quantity supply rises to 50 units.
- This shows a positive relationship between price and quantity supplied.

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Diagram and its Explanation

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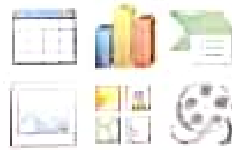

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Assumption of the Law of Supply

(1) **No change in Cost of production:** There should be no changes in cost of production otherwise this law will not valid. For example, if the cost of production increases, price will rise but rise in price will not lead to rises in supply. Therefore, law of supply would be applicable only when the cost of production remains constant.

(2) **No change in technique of production.** This law is valid only if technology remain the same. If technology improves, supply increases while price remains the same or even price may decrease.

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