LESSON 5 – DEMAND

Understanding Consumer Behaviour

Slide 1 – Introduction

Good morning everyone.

So far, we've built the foundations of economics:

- Scarcity
- Choice
- Opportunity cost
- Economic systems
- The circular flow of income

Now we begin microeconomics properly.We shift our focus to individual markets. And we start with one of the most fundamental concepts in economics: Demand.

Slide 2 – Why Demand Matters

Every day, people make purchasing decisions.

Whether it's buying food, choosing a school, paying for transport, or subscribing to a service. In each case, price influences behavior.

But price is not the only factor. Economics aims to understand: How do consumers decide how much of a good or service to buy? This is what demand explains.

Slide 3 – Definition of Demand

Demand is defined as: The quantity of a good or service that consumers are willing and able to buy at a given price over a given period. There are three key components in this definition:

1. Willingness to buy

Consumers must actually want the product.

2. Ability to pay

Consumers must have sufficient income or purchasing power.

3. Price

Demand is always considered in relation to price.

If any of these are missing, there is no effective demand.

Slide 4 – The Law of Demand

The law of demand states that:

As price increases, quantity demand decreases, all else equal. This gives us the familiar downward-sloping demand curve. But why does this relationship exist? There are two key explanations.

Slide 5 – Substitution Effect

The first is the substitution effect.

When the price of a good increases, consumers switch to alternatives.

For example, if the price of private school fees rises, some parents may switch to state schools.

Consumers always seek to maximize value. So, when one good becomes relatively more expensive, substitutes become more attractive.

Slide 6 – Income Effect

The second explanation is the income effect. When prices rise, consumers' real purchasing power falls. Even if their nominal income stays the same, they can now afford less.

So, they reduce consumption. This effect is particularly strong for goods that take up a large proportion of income.

Slide 7 – Demand Curve

Let's now look at the demand curve itself. There are three key features:

- Price is on the vertical axis
- Quantity demanded is on the horizontal axis
- The curve slopes downward

This curve represents the relationship between price and quantity demanded. However, it is important to note one assumption: Ceteris paribus — meaning all other factors are held constantly. This is crucial. Because if other factors change, the entire demand curve shifts.

Slide 8 – Movement vs Shift

We must distinguish between the movements along the demand curve. This is caused by a change in price.

Shift of the demand curve

This is caused by changes in other factors.

This distinction is essential for exam questions and real-world analysis.

Slide 9 – Factors Affecting Demand (Shifts)

Let's now explore the main factors that shift demand.

1. Tastes and Preferences

Advertising, trends, and social norms can increase or decrease demand.

2. Income

For normal goods, demand rises as income rises.

For inferior goods, demand falls as income rises.

3. Prices of Related Goods

Substitutes: if the price of one rise, demand for the other increases

Complements: if the price of one rise, demand for the other decreases

4. Expectations

If consumers expect prices to rise in the future, demand may increase today.

5. Population and Demographics

An increase in the number of consumers increases demand.

These factors shift the entire demand curve to the left or right.

Slide 10 – Application: Education Demand

Let’s apply this to a real-world context — education.

Demand for private schooling depends on several factors:

- Household income
- Perceived quality of state schools
- Cultural values
- Expectations about university access

Now consider a policy like a tax on private school fees. If fees rise, quantity demand will fall — this is a movement along the curve. However, demand may also shift if other factors change. For example, if state schools improve significantly, demand for private schools may fall even further. This distinction is crucial in your VAT research.

Slide 11 – Why Demand Matters for Policy

Understanding demand is essential for governments.

It helps them:

- Plan public services
- Set taxes
- Regulate prices

If demand is highly responsive to price — meaning it is elastic — then small price changes can lead to large behavioral changes. If demand is inelastic, price changes have little effect. This has major implications for policy effectiveness.

Slide 12 – Summary

Let’s summarize.

Demand is the quantity consumers are willing and able to buy at a given price. The law of demand states that price and quantity demand are inversely related.

This is explained by:

- The substitution effect
- The income effect

Demand curves show this relationship. Changes in price cause movements along the curve. Changes in other factors cause shifts in the curve.

Slide 13 – Conclusion

The key takeaway is this: Demand is not random.

It follows predictable patterns based on incentives and constraints. By understanding demand, we can better predict how consumers will respond to changes in prices and policies.

Next lesson, we will study supply — how firms respond to prices. And together, demand and supply will allow us to understand how markets actually determine prices.

Thank you.