An Introduction to Microeconomics
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Lecture - 65
Effect of Change in Price

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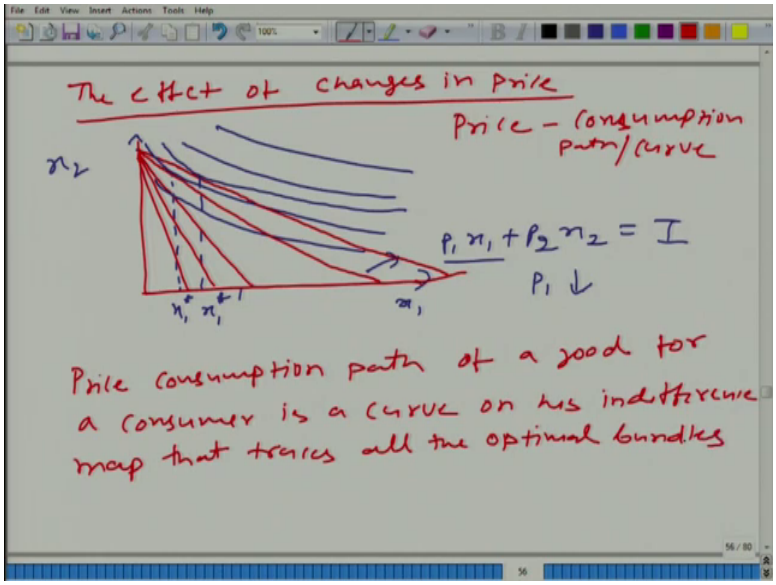

Now let us move to the second step the effect of changes in price. Let me draw some indifference curve let us say this is the budget line. Now what is this budget line this is P 1 x 1 plus P 2 x 2 is equal to I. What we have here is again do not forget the axis this is x 1 axis, this is x 2 axis.

So we are drawing the indifference map and we are getting the optimal bundle using the budget constraint fine. So, what will happen let us say if P 1 decreases?

Student: If the amount of good 1 purchased to increase.

The amount of good 1 ok.

Student: (Refer Time: 01:33).

That is the result.

Student: (Refer Time: 01:35).

That we do not know.

Ok it depends on various factors that we will learn shortly, but what we are certain about is that this budget curve budget line we will rotate in anti clockwise direction pivoted at this point because price of good 2 is not changing. So, it is going to be something like something like this fine.

So, let me draw some one more indifference curve something like this. So, earlier we had this is the x 1 star the new x 1 star let us denote it by dash. So, what is happening in this particular case what is happening the amount of good 1 demanded it has increased, but that is not the idea the idea is to figure out the curve.

That we obtain by keeping everything else fixed in this economy and changing.

Student: Price.

Price of;

Student: Good 1.

Good 1.

And of course, as we change the price of good 1 we will get different budget line.

And correspondingly we will get different consumption bundle the optimal consumption bundle. So, a curve that passes that passes through all these optimal bundle is called.

Student: Price consumption.

Price consumption.

Student: Path.

Path; price consumption path or price consumption curve does not matter. So, let me give you the definition price consumption path of a good for a consumer is a curve of course, curve on his indifference map that traces all the optimal bundles all the optimal bundles for price consumption path of a good for a consumer is a curve on his indifference map that tresses all the optimal bundles for different level of price for good 1.

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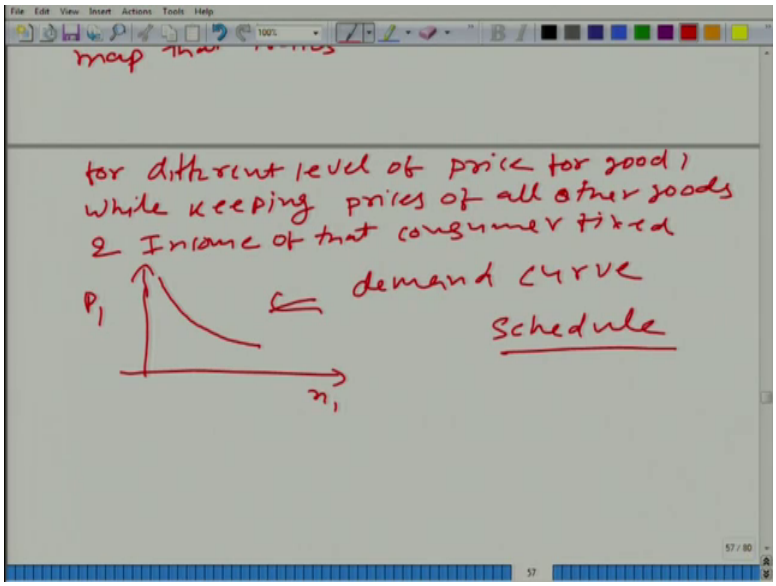

While keeping prices of all other goods and income rates of that consumer is fixed of good 1. Let us put it here of good 1 fine now similarly what we can do we can take this; these optimal bundles and we can represent them in different graph. A graph where on x axis we give the optimal amount of good 1 and on y axis.

Student: Price.

We give price of good 1 and of course, again from here we can figure out because how we are obtaining for different level of price of good one we are obtaining different level of different quantity of good 1 demanded.

So, we can figure out all the pairs and we can draw them. Typically we will get here a .

Student: Downward.

Downward sloping curve;

Student: Yeah.

And this downward sloping curve is nothing, but demand curve or demand schedule.

Remember what did we learn about demand schedule that demand schedule gives us the relationship between price.

Student: (Refer Time: 06:30).

Of a good and;

Student: Quantity.

Quantity demanded for;

Student: (Refer Time: 06:32).

That particular good while everything else in economy is;

Student: Held fixed.

Held fixed so that is what we are talking about here, that everything we are talking about an economy where we have only 2 goods and some consumer. So, income we are keeping fixed and also we are keeping the price of other good fixed. So, then the graph that we get is nothing, but the demand schedule or demand curve or demand function.

Now third thing that we said that we can study here is the effect of change in price of good 2 on quantity demanded of good 1 that we have just learned we have just learned the consumption price consumption path by changing the price of good 1. So, alternatively what we can talk about is the quantity demanded of good 2 with respect to .

Student: Change in price of good 1.

Change in price of good 1 ok. And if we do that what we will know again I am not getting into detail here. Here the cross effect we are talking about.

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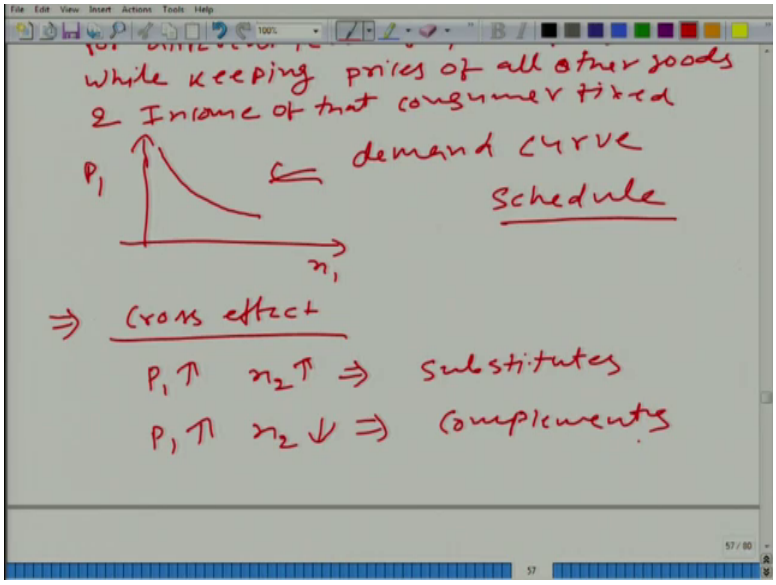

So, let us say P 1 goes up and x 2 as a result x 2 also goes up. What does it mean that good 1 and good 2 are;

Student: Substitutes.

Substitutes.

Student: Substitutes.

Good 1 and good 2 are substitutes. And if P 1 goes up and x 2 comes down then they are.

Student: Complements.

Complements fine that is what we can figure out; is it clear.

Student: Yes sir.