

Answer on Question #60653 – Economics – Microeconomics

1. Illustrate a shift in the demand curve for Bordeaux wine and explain the likely shift factors for the wine, Assume the supply of Bordeaux remains unchanged. Illustrate the impact of a shift in demand for Bordeaux wine on its price.

Solution.

Let us construct the graph to illustrate the shifts of the demand curve for Bordeaux wine graphically.

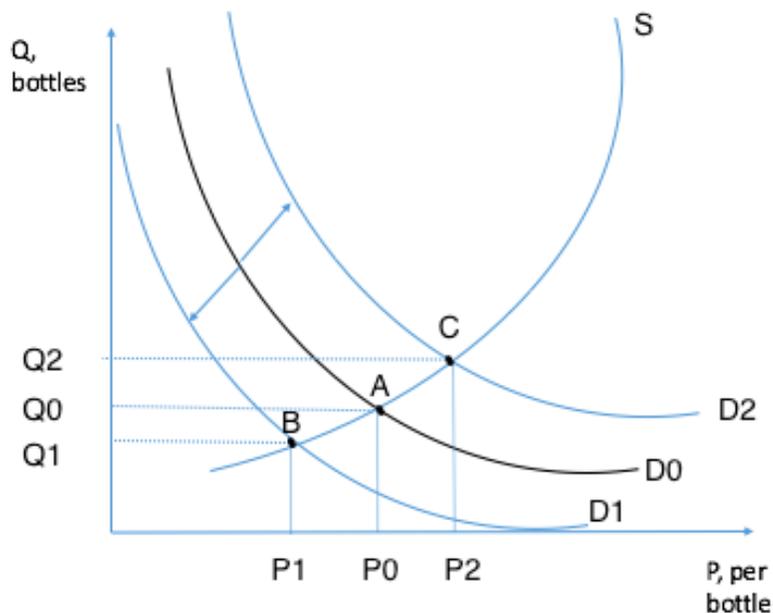


Figure 1. Illustration of the shifts of the demand curve for Bordeaux wine.

The curves D_0 , D_1 , D_2 represent different demand levels; the curve S represents level of supply. Points A , B , and C represent the equilibrium. P_0 , P_1 , P_2 represent the certain wine price levels, whereas Q_0 , Q_1 , and Q_2 represent certain quantity of wine bottles, respectively.

- a) **Shift factors.** As can be seen from the Figure 1, the demand curve for the Bordeaux wine (D_0) could be shifted either to the left (curve D_1 ; decrease in demand of wine), or to the right (curve D_2 ; increase in demand of wine). These changes could be caused by various factors.

First, let us describe those factors influencing *decrease in demand* (curve D_1 ; shift to the left) for Bordeaux wine:

→ a fall in income of the customers;

- a fall in the price of a substitute (another red wine, e.g., Cabernet, Merlo);
- a rise in price of the complement (e.g., meat, cheese)
- decrease in population;
- customers' expectations that the price of the wine would fall in the future
- changes of the customers' preferences and tastes (e.g., a huge governmental social campaign warning that drinking alcohol harmfully influences one's health)
- changes in season and weather (e.g., it is not likely that many people would drink Bordeaux wine when it is extremely hot temperatures outside)

It should be noted that the shift of the demand curve would be influenced by the wine customers' income only in case we assume that Bordeaux wine is a normal good.

Second, let us describe those factors influencing *increase in demand* (curve D_2 ; shift to the right) for Bordeaux wine:

- a rise in the customers' income
- a rise in price of the substitute (another red wine, e.g., Cabernet, Merlo)
- a fall in price of the complement (e.g., meat, cheese)
- increase in population
- customers' expectations that the price of the wine would rise in the future
- changes of the customers' preferences and tastes (e.g., a popular advertising campaign showing that it is "cool and fashionable" to drink Bordeaux wine)
- changes in season and weather (e.g., Christmas time, when people tend to drink hot red wine with spices)

b) Impact of the shift of the demand on the wine's price.

As can be seen from the Figure 1, decrease of the demand for the Bordeaux wine shifts the demand curve D_0 to the left (D_1), and the wine's price decreases from P_0 to P_1 . However, increase of the demand for the Bordeaux wine shifts the demand curve D_0 to the right (D_2), and the wine's price increases from P_0 to P_2 .