

Elasticity of Demand

Notes

“ELASTICITY OF DEMAND” TARGETS

Knowledge

Reasoning

Skill

THE PRICE ELASTICITY OF DEMAND

The **elasticity of demand** measures how much the quantity demanded will change when other factors change.

1)

2)

3)

4)

<p>Price elasticity of demand = _____</p>
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PRICE CEILINGS ARE INEFFICIENT

When measuring percent changes, you will get a different result depending on which number you start with. The midpoint method eliminates this problem.

1) Formula to find the numerator:

<p>% change in quantity = _____</p>
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2) Numerator formula rewritten:

<p>% change in quantity = _____</p>
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3) Denominator has a similar formula:

<p>% change in price = _____</p>

4) This is the complete formula:

<p>PED = _____ ÷ _____</p>

COEFFICIENT OF ELASTICITY

The values we get when we calculate the price elasticity of demand are called coefficients of elasticity. They tell us the relative elasticity of an item.

- 1) **Coefficient Is Zero**
- 2) **Coefficient Is Between 0 and 1**
- 3) **Coefficient Is 1**
- 4) **Coefficient Is Greater Than 1**
- 5) **Coefficient Is Infinite**

TOTAL REVENUE TEST

Each section of a demand curve has a different elasticity. The Total Revenue Test, which also calculates elasticity, shows how this works.

- 1) **Calculations**
 - A)
 - B)
 - C)
- 2) **Results**
 - A) INELASTIC:
 - B) ELASTIC:
 - C) UNIT ELASTIC:

DETERMINANTS OF ELASTICITY

Several factors help determine whether an item is relatively elastic or inelastic.

- | | |
|---|---|
| <ul style="list-style-type: none"> 1) Items Are Elastic If... <ul style="list-style-type: none"> A) B) C) D) | <ul style="list-style-type: none"> 2) Items Are Inelastic If... <ul style="list-style-type: none"> A) B) C) D) |
|---|---|

CROSS-PRICE ELASTICITY OF DEMAND

Another type of elasticity is the cross-price elasticity of demand, which measures how strongly two substitutes or two complements are related.

- 1) We use a slightly different formula:

<p>Cross elasticity of demand = _____</p>
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- 2)
- 3)
- 4)
- 5)

INCOME ELASTICITY OF DEMAND

Another type of elasticity is the income elasticity of demand, which measures how much quantity changes when consumer income changes.

- 1) We use a slightly different formula:

<p>Income elasticity of demand = _____</p>

- 2)
- 3)
- 4)
- 5)
- 6)