Chapter 5:

•Elasticity: Responsiveness of QD or QS to one of its determinants
•Price elasticity of demand: Measures how much QD responds to change in price
-Said to be elastic if QD responds substantially to changes in price
•Influence on the price elasticity of demand:
-Availability of close substitutes: Goods with close substitutes are more elastic, because it is easier to switch from that good to others (EG. Eggs not elastic)
-Necessities v Luxuries: Necessities tend to have more inelastic demands (EG. Doctor visits), Luxuries have more elastic demands (EG. ↑Price of yacht=substantial change in demand)
-Definition of the market: Narrowly defined markets tend to have more elastic demand than broadly defined markets, since it is easier to find close substitutes
(EG. Food is broad=inelastic, Ice cream is narrow=elastic)
-Time horizon: Goods tend to have more elastic demand over a longer period of time (EG. When the price of petrol rises in short term demand will fall only slightly, whereas over a longer period of time they will switch to full efficient cars)
•Price elasticity of demand (midpoint method)=

$$\frac{[Q2-Q1]/[[Q2+Q1]/2]}{[P2-P1]/[[P2+P1]/2]}$$

•Total revenue= Price x Quantity
-If demand is elastic, ↑P=↓Revenue
-If demand is inelastic, ↑P=↓Revenue
-If demand is unit-elastic, ↑P=No change in Revenue
•Income elasticity of demand: Measure of how QD responds to change in consumer's income=

$$\frac{\%\ \Delta \text{ in QD}}{\%\ \Delta \text{ in Income}}$$

-Normal good: Higher income=↑QD (luxuries tend to have higher income elasticities)
-Griffin good: Higher income=↓QD (EG. Public Transport)
•Cross price elasticity of demand: Measure of how much QD of one good responds to a change in price of another good

$$\frac{\%\ \Delta \text{ in Q of Good 1}}{\%\ \Delta \text{ in P of Good 2}}$$

-Substitutes: > than 0 (EG. Hot dogs and hamburgers)
-Compliments: < than 0 (EG. Computers and computer software)
•Price elasticity of supply: Measures how much QS responds to a change in P of that good=

$$\frac{[Q2-Q1]/[[Q2+Q1]/2]}{[P2-P1]/[[P2+P1]/2]}$$