

Brief Review

1. Price elasticity of demand is the responsiveness of a product's quantity demanded to changes in the product's price. When demand is elastic, a given percentage change in price causes a larger percentage change in quantity demanded. When demand is inelastic, a given percentage change in price causes a smaller percentage change in quantity demanded.
2. Demand is perfectly elastic when the price of a product is constant at all quantities demanded. Demand is perfectly inelastic when the quantity demanded of a product is constant at all prices. Demand is unit-elastic when a percentage change in price causes an equal percentage change in quantity demanded.
3. Price and total revenue have an inverse relationship when demand is elastic but a direct relationship when demand is inelastic. When demand is unit-elastic, total revenue is constant, regardless of price.
4. Four factors affect the price elasticity of demand of a product: the portion of consumer incomes the product accounts for, access to substitute products, whether the product is a luxury or a necessity, and the amount of time that elapses after a price change.
5. Other demand-related elasticity concepts include income elasticity, which measures the sensitivity of a product's quantity demanded to a change in consumer income, and cross-price elasticity, which measures the sensitivity of a product's quantity demanded to a change in another product's price.

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1. Price elasticity of supply is the responsiveness of a product's quantity supplied to changes in the product's price.
2. When supply is elastic, a given percentage change in price causes a larger percentage change in quantity supplied. When supply is inelastic, a given percentage change in price causes a smaller percentage change in quantity supplied.
3. Price elasticity of supply is dependent mainly on the production period. In the immediate run, supply is perfectly inelastic, meaning, a change in price has no effect on quantity supplied. In the short run, supply may be elastic or inelastic.
4. In the long run, price elasticity of supply depends on the industry's use of resources. In a constant-cost industry (not a major user of any one resource), supply in the long run is perfectly elastic, with a constant price at all possible quantities supplied. In an increasing-cost industry (a major user of at least one resource), the long-run supply is very elastic, with price rising gradually at higher quantities supplied.

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1. For various reasons, governments sometimes choose to intervene in markets to override the "invisible hand" of competition. Price controls are one form of intervention and take the form of price floors and price ceilings.
2. Setting a price floor, or a minimum allowable price, in a competitive market tends to cause surpluses.
3. Setting a price ceiling, or a maximum allowable price, in a competitive market tends to cause shortages.

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1. Spillover effects are the external effects of economic activity that arise because no market exists in isolation.
2. Spillover effects can be negative or positive. Spillover costs, such as pollution, are the harmful effects of producing or consuming a product. Spillover benefits, such as those associated with education, are the positive effects of producing or consuming a product.
3. Governments often step in to see that public as well as private costs and benefits are accounted for. Governments might, for example, intervene with taxes to correct an oversupply in the case of spillover costs or with subsidies to correct a shortfall in the case of spillover benefits.
4. Public goods are products whose benefits cannot be restricted to certain individuals. Governments often step in to provide these goods rather than leave them to private markets. Governments can also attempt to turn such goods into private goods by defining new types of property.