

## Price Elasticity of Demand

- ① defn - PED measures the degree to which the Qty of a product demanded responds to a price change
- ② GR - law of demand states that given CETERIS PARIBUS, the Qty demanded increases (↑) as price decreases (↓)
- ③ Exceptions to GR
  - ↳ price changes for different products affects demand in different ways
  - ↳ demand curves for different products with different degrees of elasticity are all DOWNWARD SLOPING but have different slopes/shapes
  - ↳ the STEEPER the slope the more inelastic the demand as the slope is closer to approaching a vertical/perfectly inelastic slope
  - ↳ see graph...

ELASTIC DEMAND - is one in which a PRICE CHANGE brings about a GREATER THAN PROPORTIONAL CHANGE in Qty. demanded by consumers  
↳ i.e. - a small price change is likely to have a large impact of Qty demanded

INELASTIC DEMAND - price changes have little effect on Qty. demanded  
↳ i.e., small price change likely to have little or no impact on Qty demanded

FORMULA - 
$$\text{price elasticity of demand (Ed)} = \frac{\% \Delta Q_d}{\% \Delta P}$$

- ↳ IF coefficient Ed is  $> 1$  THEN demand is ELASTIC
- ↳ IF Ed is  $< 1$  THEN demand is INELASTIC
- ↳ IF Ed = 1 THEN demand is UNITARY ELASTIC

## Characteristics that help determine Elasticity

### ① luxury OR necessity?

↳ GR - necessary products have INELASTIC DEMAND  
b/c demanded regardless of price

### ② number and/or availability of substitutes

↳ GR - the greater the number of close substitutes  
the more ELASTIC the demand as price increases  
drive consumers to several alternatives

### ③ Percentage of income/budget available to spend on product

↳ GR - small % of income/budget means price changes  
are not likely to greatly impact Qty. demanded  
- i.e., INELASTIC

### ④ Length of time since price change

GR - short term - unlikely to impact demand thus inelastic  
b/c no substitutes / knowledge of  
substitutes / convenience ...

- long-term - time for market to respond / increase in  
substitutes / knowledge of substitutes

- buying patterns adjust

- i.e., more ELASTIC as time passes

\* not all factors required to determine a products elasticity  
... one may be sufficient