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Workshop 2B related to ch. 4

Markets in Action

1. (a) The price elasticity of demand measures the responsiveness of *the quantity demanded / price* to a change in *the quantity demanded / the quantity supplied / price*.

[Delete wrong words.]

- (b) Give the formula for own price elasticity of demand.

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2. In the mid-1990s, the government in the US announced that for every 10 per cent rise in the price of cigarettes, the demand is likely to fall by 6 per cent. If this information is correct, what is the value of the price elasticity of demand for cigarettes?

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3. In each of the following pairs, tick which of the two items is likely to have the more elastic demand. Give reasons for your answer.

- (a) Gasoline (all brands) Shell gasoline

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- (a) Holidays abroad Bread

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- (a) Salt Clothing

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4. The formula for price elasticity of demand is as follows:

$$\frac{\text{Proportionate (or percentage) change in quantity demanded}}{\text{Proportionate (or percentage) change in price}}$$

This can be summarised as (arc price elasticity – note that mid means average):

$$\Delta Q_d / \text{mid } Q_d \div \Delta P / \text{mid } P$$

The following table shows the quantity of a product demanded at two different prices:

<i>P</i>	<i>Q_d</i>
16	25
14	35

- (a) Calculate the proportionate change in quantity demanded when price falls from \$16 to \$14. (Use the first part of the formula, i.e. $\Delta Q_d / \text{mid } Q_d$, to do your calculation.)

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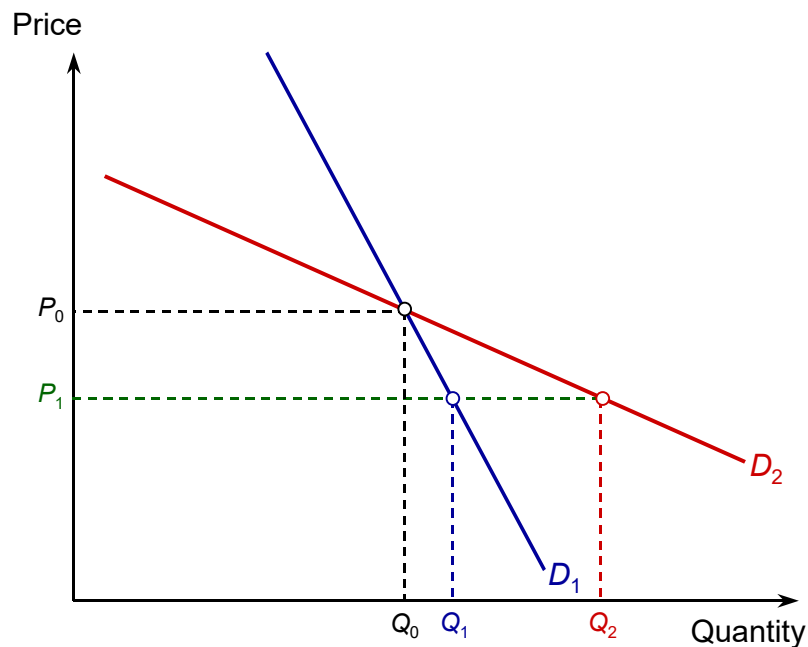
- (b) Calculate the proportionate change in price when price falls from \$16 to \$14. (Use the second part of the formula, i.e. $\Delta P / \text{mid } P$, to do your calculation.)

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- (c) What is the price elasticity of demand between \$16 and \$14?

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5. The following diagram shows two demand curves that cross at a price of P_0 .



Which of the following statements are true?

(a) Curve D_1 is inelastic and curve D_2 elastic. *True / False*

(b) Demand is more elastic between P_0 and P_1 along curve D_2 than along curve D_1 *True / False*

(c) The price elasticity of demand between P_0 and P_1 in the case of curve D_2 is equal to:

$$\frac{Q_2 - Q_0}{\text{mid } Q} \div \frac{P_0 - P_1}{\text{mid } P} \dots\dots\dots \textit{True / False}$$

(d) For any given change in price there will be a larger proportionate change in quantity along curve D_1 than along curve D_2 .
 *True / False*

6. Fill in the rest of the following table – keep in mind that mid means average:

(For the final column use the formula: $\Delta Q_d / \text{mid } Q_d \div \Delta P / \text{mid } P$)

<i>Quantity demanded (000s)</i>	<i>Price (\$)</i>	<i>Total consumer expenditure</i>	<i>Elastic or inelastic demand</i>	<i>Price elasticity of demand</i>
7	13
9	11
11	9
13	7

7. (a) What is the formula for income elasticity of demand?

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(b) Which of the following would you expect to have a demand which is elastic with respect to income? (There are more than one.)

- (i) Flour..... *Yes / No / Possibly*
- (ii) Ready-prepared meals for the microwave *Yes / No / Possibly*
- (iii) Champagne *Yes / No / Possibly*
- (iv) Socks *Yes / No / Possibly*
- (v) Designer jeans..... *Yes / No / Possibly*
- (vi) Electricity..... *Yes / No / Possibly*
- (vii) Bus journeys *Yes / No / Possibly*
- (viii) Insurance..... *Yes / No / Possibly*