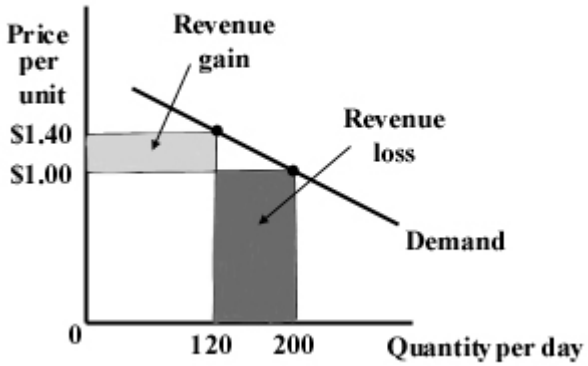


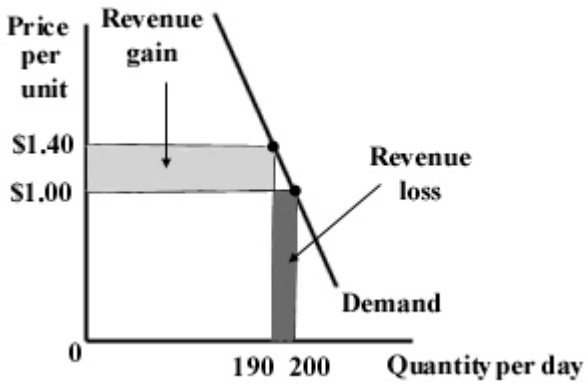
Let's imagine we operate a small canteen in a school.

I might say to you "increasing the price of a can of Brand "X" soft drink from $1.00 per can to $1.40 per can is not a good idea. Our customers will buy Brand "Y" instead."

"At the moment, we are selling 200 cans per day of Brand "X", at $1.00 per can. We are generating $1.00 per can x 200 cans = $200 per day in revenue from sales of Brand "X". I believe that we will only sell 120 cans per day if we increase the price of Brand "X" to $1.40 per can; resulting in a daily revenue of $1.40 per can x 120 cans = $168."

"The revenue we gain from increasing the **price** per can ($0.40 x 120 = $48) will not be enough to offset the revenue we will lose from the decrease in the **quantity** of cans we sell ($1.00 x 80 = $80)."

I show you my reasoning, on a Supply and Demand diagram (shown above). Implicit in my reasoning is my belief that Brand "X" has a close substitute in Brand "Y", and that Brand "X" is **price elastic**.



You, however, are more in touch with teenage trends and fashion than I am.

You reply "Brand "X" is really popular at the moment. I believe we can increase the price to $1.40 per can. We will lose very few sales".

You show me your analysis (shown above) of the market for brand "X". An increase in price to $1.40 per can will only cause a loss of 10 cans in sales per day. The revenue gain from the increase in **price** ($0.40 x 190 cans = $76) will more than compensate for the revenue loss caused the decrease in **quantity** sold ($1.00 x 10 = $10). You have correctly noticed that Brand "X" is **price inelastic**, and that an increase in price will generate **more net revenue**.