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Chapter 2

Elasticities

2.1 The Elasticity of Demand

2.1.1 The Price Elasticity of Demand

- A good's <u>price elasticity of demand</u> measures how much the quantity demanded responds to a change in price.
- Demand for a good is <u>elastic</u> if the quantity demanded responds a lot to changes in price.
- Demand is <u>inelastic</u> if the quantity demanded doesn't respond a lot to changes in price.

<u>Determinants of Price Elasticity of Demand</u>

1. Availability of Substitutes: Goods with close substitutes are more elastic
2. Necessities v. Luxuries: Necessities are more inelastic and luxuries are more elastic
3. Market Definition: Goods in narrowly defined markets are more elastic, and goods in broadly defined markets are more inelastic.
    - Ex. Vanilla ice cream is a narrowly defined good, so it has lots of substitutes.
    - Ex. Food is a broadly defined good, so it has no substitutes.
4. Time Horizon: Goods are more elastic in the long term than the short term

2.1.2 Computing the Price Elasticity of Demand

2.1.3 The Midpoint Method