# Question 12

***The economic downturn has forced many food and beverage outlets to compete more aggressively as customer tighten their belts. The Hard Rock Café is usually advertising a recession menu – two set lunches for the price of $12.80 for the price of one – on Mondays to Tuesdays. Even hawker stalls and coffee shops, stalwarts of good, cheap fare, have had to shave up to $1 off to $3.50 meal.***

***The Strait Times, 21 Aug 2001***

**Distinguish between price elasticity of demand, income elasticity of demand and cross price elasticity of demand. (12)**

Elasticity of demand is the measurement of the responsiveness of the change in quantity demanded due to the change in a variable influencing it. These variables are different for all three types of elasticity – The price of the good for price elasticity; the income of the consumer for income elasticity; the price of other goods for cross elasticity. These different concepts can be distinguished from several perspectives as will be seen in this essay.

One differing factor would **be the implications of the co-efficient of the respective types of elasticity of demand**. In the case of Price Elasticity, a negative elasticity would refer to both an inferior good and normal. On the other hand, for income elasticity, the same would refer to an inferior good and for cross elasticity it would refer to a complement good. For positive elasticity, this would refer to a giffen good for price elasticity, normal good for income elasticity and a substitute good for cross price elasticity.

Another differential would be **the factors affecting the value of elasticity of demand**. For price elasticity, the factors that would determine the value of the elasticity of demand would be the time period for decision making, the proportion of income spent on it, the of number of substitutes for the good available in the market and the income of consumers may also affect it. For income elasticity, a consumer’s income would obviously be the biggest factor affecting it. As the consumer’s income increases, the good may turn from luxury to normal and finally inferior. As for cross price elasticity, the nature of the usage of the products would be a major factor such as whether they are complements or substitutes. If the relationship of the two goods is highly interdependent, the value of the cross elasticity of demand would be elastic.

**The usage of the concepts for each concept is different from each other.** For price elasticity, firms may use them to derive price strategies. As for income elasticity, it is mainly used to explain how consumers may respond to a price change as a result of a change in their incomes. Finally, for cross price elasticity, this helps to provide information on market conditions and the relationships of goods.

However, there is a similarity between these concepts as how the **magnitude of elasticity is measured for the 3 concepts of elasticity of demand.** Basically, the bigger the value of the elasticity, the more elastic it is and the smaller the value, the more inelastic it is.

In conclusion, as the 3 concepts of elasticity of demand differ in their influences and implications, the uses of these concepts can be of great use by having a good understanding of these concepts.