**Income Elasticity of Demand**

1. j0213207Define what is meant by ‘Income Elasticity of Demand’
2. Look at factors that influence income elasticity of demand
3. Apply income elasticity of demand to real world examples.
4. On the diagram below illustrate the relationship between income and quantity demanded.

# Income

**Quantity demanded**

2. Using the above idea what do you think is meant by the term ‘**Income Elasticity of Demand**’?

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3. Look at the products below and state whether you think their demand would be **income elastic or income inelastic and state why.**



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1. What is the formula for ‘**Income Elasticity of Demand**’?
2. A person receives a pay rise of $200. His old salary was **$1000** a month now he receives **$1200.** He used to consume **500** units of beer a month but now consumes **550.** Calculate the Income Elasticity of Demand for beer consumption



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1. Another person receives an annual salary of **$120,000.** After a meeting with his boss he receives a pay rise of **$20,000.** His new salary is **$140,000**. He used to go on **2** holidays a year but now he takes **3** holidays a year. Calculate his Income Elasticity of Demand for holiday consumption.



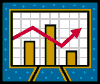
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1. Using the concept of Income Elasticity of Demand in your answer explain why certain businesses do badly when the economy is in trouble. (**recession**)

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1. Therefore which businesses will do well when the economy is **booming** (doing well) and why?

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1. Look at the real world **income elasticities of demand** given in the table below.

|  |  |  |
| --- | --- | --- |
| Good or Service | Elasticity | Comment |
| **Wine** | 2.6 |  |
| **Services** | 1.8 |  |
| **Spirits** | 1.7 |  |
| **Durable Goods** | 1.5 |  |
|  |  |  |
| **Fruit juice** | 0.9 |  |
| **Beer** | 0.6 |  |
| **Green vegetables** | 0.1 |  |
| **Fresh meat** | 0.0 |  |
| **Cereals** | 0.0 |  |
|  |  |  |
| **Tobacco** | -0.1 |  |
| **Bread** | -0.3 |  |

1. Do any of the above values differ from what you expected?

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1. How would you describe the income elasticity of demand for an inferior good or service?



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