Student Name:

12 August 2010 Total Possible Marks: 11

Income Elasticity of Demand

Complete in pen or pencil and hand into your teacher when ready. Each multiple choice question carries one mark. Select one answer only.

_ 1 1. Income elasticity of demand is defined as

The responsiveness of demand following a change in the income of consumers

_ 1 2. When demand for a product is income inelastic, the percentage change in quantity demanded is [A]less than the percentage change in income

_ 1 3. The income elasticity of demand for a normal good is always

positive / greater than zero

_ 1 4. It was estimated in 2003 that milk has an income elasticity of demand of -0.6. What can be concluded about milk from this information?

That milk is an inferior good because the income elasticity of demand is negative

_ 1 5. An income reduction of 15% causes Geoff to increase his purchases of minced beef by 10%. Which of the following statements is most likely to be correct?

- ○ A. The income elasticity of demand for minced beef is -2/3 and ground beef is a superior good
- ○ B. The price elasticity of demand for ground beef is -1.5 and ground beef is a normal good
- ● C. The income elasticity of demand for minced beef is -2/3 and ground beef is an inferior good
- ○ D. The price elasticity of demand for ground beef is -2/3 and minced beef is a normal good

_ 6 6. The income elasticity of demand for private dental services, rental movie services, and private (or own) label clothing available in supermarkets have been estimated to be +2.5, +0.8, and -1.5 respectively.

Write an answer interpreting these coefficients for income elasticity

Private dental services and rental movie services are normal goods where quantity demanded move in the same direction. The income elasticity for dental treatments appears to be a luxury because Yed>+1. For example a 10% rise in income might lead to a 25% increase in demand. Rental movie services appears to be a normal necessity. The demand for private-label clothing in supermarkets is estimated to fall when income rises i.e. an inferior good. With an inferior good, income and quantity demanded move in the opposite direction.