ECO550 Week 2 Check Your Understanding Submission
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  \* Chapter 3: Problems 3, 4, and 7
Chapter 3 -Problem 3 Answer:   The Olde Yogurt Factory has reduced the price of its popular Mmmm Sundae from $2.25 to $1.75.   As a result, the firm’s daily sales of these sundaes have increased from 1,500/day to 1,800/day.   Compute the arc price elasticity of demand over this price and consumption quantity range.
Arc Price Elasticity = (Q₂ - Q₁ / P₂ - P₁) \*   (P₂ + P₁ / Q₂ + Q₁)
Q₁ = 1500
Q₂ = 1800
P₁ = 2.25
P₂ = 1.75
Answer: [(1800 - 1500)/(1.75 – 2.25)] \* [(1.75 +2.25)/ (1800 + 1500)]
(300/-.5) \* (4/3300) = 1200/-1650 =   -.7272

Chapter 3 -Problem 4 Answer:   The subway fare in your town has just been increased from a current level of 50 cent to $1.00 per ride.   As a result, the transit authority notes a decline in ridership of 30 percent.
        \*   Compute the price elasticity of demand for subway rides.
Answer:   Price Elasticity of demand =   %∆Q / %∆P = .30/ (.50/1.00) = .30/.50 = .60
        \* If the transit authority reduces the fare back to 50 cents, what impact would you expect on the ridership?   Why?
Answer:   Price Elasticity of demand =   %∆Q / %∆P = .30/ (1.00/.50) = .30/.20 = .15
Because the elasticity of demand is less than 1, it is

considered inelastic.   Therefore, an decrease in price would be a decrease in revenue.
Chapter 3 -Problem 7 Answer:   In an attempt to increase revenues and profits, a firm is considering a 4 percent increase in price and an 11 percent increase in advertising.   If the price elasticity of demand is -1.5 and the advertising elasticity of demand is +.06, would you expect an increase or decrease in total revenues?
Answer:   Because the price elasticity of demand is -1.5 the absolute values of the price elasticity of demand is elastic.   Therefore, with a 4% increase in price, there would be a decrease in quantity sold.   The reduction in quantity would then cause a reduction/decrease in total revenue.   Although the firm is considering a 11% increase in advertising, the advertising elasticity is substantially less than the price elasticity of demand.   If the advertising elasticity was higher, sales would be more responsive.   Because sales responsiveness is quite low, it would not pose an increase in revenues.   Therefore, looking at both elasticity of demand given, I would expect a decrease in total revenues based on their current considerations.

      \* Chapter 4: Problems 5, 6, and 7

  \* Chapter 4 -Problem 5 Answer:
Original equation transformed:
Log Q = -2.15log6280P + 1.05logA + 3.70logN
  \* Determine

the point price elasticity of demand for Tweetie Sweeties
      \* -2.15
  \* Determine the advertising elasticity of demand
      \* +1.05
  \* What interpretation would you give to the exponent of N?
      \* N’s elasticity would be +3.70

  \* Chapter 4 -Problem 6 Answer:
  \* Determine the price elasticity of demand
      \* -2.74
  \* Determine the income elasticity of demand
      \* +.461
  \* Determine the cross price elasticity of demand
      \* 1.909
  \* How would you characterize the demand for haddock?
      \* Because the price elasticity of demand’s absolute value is > than 1, It is probable that the quantity/demand would decrease.
  \* Suppose disposable income is expected to increase by 5% next year.   Assuming all other factors remain constant, forecast the percentage change in the quantity of haddock demand next year.
      \* Because income does affect the demand of items, the increase in the elasticity of demand of income could increase the quantity of demand for haddock with a slight increase in demand.

  \* Chapter 4 -Problem 7 Answer:
  \* Determine the point price and income elasticities for household furniture.
      \* The point price elasticity is   -.48
      \* The income elasticity is +1.08
  \* What interpretation would you give to the exponent

for R?
      \* The elasticity for exponent R would be +.16.
      \* Why do you suppose R was included in the equation as a variable?
        \* I think that R was included in the in equation because it gives an idea of the value of private residential construction per household.   This is important because it shows the value of the homes.   If you were looking at residents that were $70,00 versus homes that were $200,000, it would be a significant difference in the value and type of furnishings in those homes respectfully.
  \* If you were a supplier to the furniture manufacturer, would you have preferred to see the analysis performed in physical sales units rather than dollars of revenue?
      \* If I were a supplier to the furniture manufacturer, I would prefer to see the analysis of the physical sales.   Although the dollar amounts are important, it is more important to see what is actually moving.   It would make more sense to invest in items that are moving instead of those things that are collecting dust in the warehouses.
  \*   How would this change alter the interpretation of the price coefficient, presently estimated as -.48%?
      \* I think if I were able to refine what really would needed, it would definitely affect the elasticity of demand for the products that are being provided.