

Econ-Hub **Rapid Revision** Classes

Market Economics

Elasticity of Supply Analysis

Unit [2] - BOOK [3]

Theory Recap Material [TRM]

2027 A/L Edition

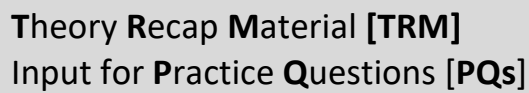




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[04 marks]

Price (Rs.)	Quantity Supply [Qs]
10.00	100
12.00	140

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[TRQ: 3] State the range of Price Elasticity of Supply (PES) scenarios (or types), outlined based on the PES Coefficient values

[05 marks]

[illegible]

[TRQ: 4] 'It is said that, as quantity supplied increases, the behavior of price elasticity of supply coefficient, along all typical upward sloping linear supply curves is not the same' Explain briefly

[04 marks]

The price elasticity of supply (PES) at a given point on a supply curve is estimated using the point PES approach. The formula for which is presented as follows

$$\text{Point PES} = \frac{\Delta Q_s}{\Delta P} \times \frac{P}{Q_s}$$

The element on the left of the above formula indicates the slope or reciprocal of the slope of the supply curve. In terms of a linear supply curve the value of the slope (or reciprocal of the slope) shall remain the same (or consistent).

However, the price elasticity of supply coefficient value tends to gradually increase or decrease as quantity increases, along certain upwards sloping linear supply curves. This is because the component on the right in the above formula keeps changing in a specific manner, as per intersect of the supply curve, while the overall elasticity type remains consistent. The two main forms of such supply situation can be outlined as follows:

- Supply curve with a positive quantity axis intercept: **PES is constantly less than one** (inelastic), but coefficient value **rises** as **quantity increases**.
- Supply curve with a negative quantity axis intercept: **PES is constantly more than one** (elastic), but coefficient value **diminishes** as **quantity increases**.

Graphical Illustration [Additional]

[TRQ: 5] State the specific situations in which the price elasticity of demand coefficient is consistent (fixed) along the entire supply curve (or function)

[03 marks]

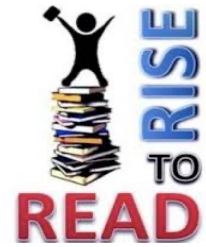
[TRQ: 6] Outline the behavior of the price elasticity of supply coefficient, along a nonlinear supply curve, sloping upwards from left to right

[04 marks]

[TRQ: 7] State the main determinants of price elasticity of supply for a given good

[04 mark]

Special - Theory Recap Questions [STRQs]: SPECIALLY DESIGNED FOR FURTHER learning & clarifications



STRQ [19]

- (A) Briefly explain what is meant by the concept 'Price Elasticity of Supply' (02 marks)
- (B) Identify the different **types** of price elasticity of supply situations (05 marks)
- (A) The process of measuring the proportionate responsiveness of **quantity supplied**, i.e. **percentage change** in quantity [%ΔQs] to a given **percentage change** in **price** [%ΔP], while **other factors** (Non-price factors) affecting supply **remain constant** within at a point of **time**; can be identified as price elasticity of supply.

In other words the flexibility or sensitivity of quantity supplied to a given change in price of the product under consideration. In simple terms, what will be the percentage change in quantity supplied of a certain product when the price of that product changes on a percentage basis (i.e. when price increases or decreases).

The process of calculating price elasticity of supply

General Approach

$$\text{PES} = \frac{\text{Percentage Change in Quantity supplied}}{\text{Percentage Change in Price}}$$

Point Price Elasticity of Supply
[Point PES]

Arc Price Elasticity of Supply
[Arc PES]

$$\text{Point PES} = \frac{\Delta Q_s}{\Delta P} \times \frac{P}{Q_s}$$

$$\text{Arc PES} = \frac{\Delta Q_s}{\Delta P} \times \frac{P_1 + P_2}{Q_1 + Q_2}$$

- (B) The answer obtained from the formula of price elasticity of supply is known as the price elasticity of supply coefficient. This coefficient value can **range from Zero (0) to Infinity**. The price elasticity of supply coefficient value constantly takes a positive form, due to the positive or direct relationship between price and quantity demanded of a certain product

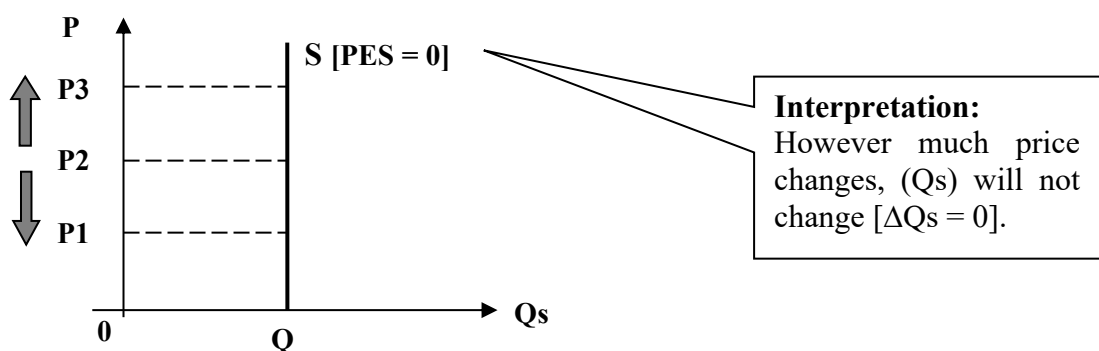
Due to this positive relationship between price and quantity supplied, both the denominators (bottom) and the numerator (top) of the PES formula always becomes is a positive value.

Range of Coefficients

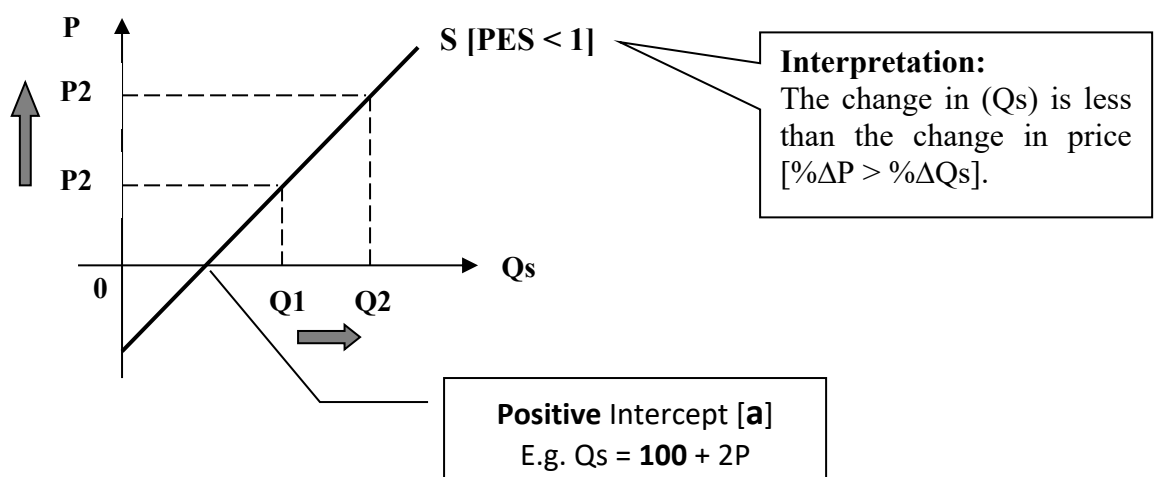
Types of price elasticity of supply coefficients

Formula	PES Coefficient	Types of Price Elasticity of Supply
$\% \Delta Q_s = 0$	$PES = 0$	Perfectly Inelastic Supply
$\% \Delta Q_s < \% \Delta P$	$PES < 1$	Inelastic Supply
$\% \Delta Q_s = \% \Delta P$	$PES = 1$	Unitary Elastic Supply
$\% \Delta Q_s > \% \Delta P$	$PES > 1$	Elastic Supply
$\% \Delta P = 0$	$PES \rightarrow \infty$	Perfectly Elastic Supply

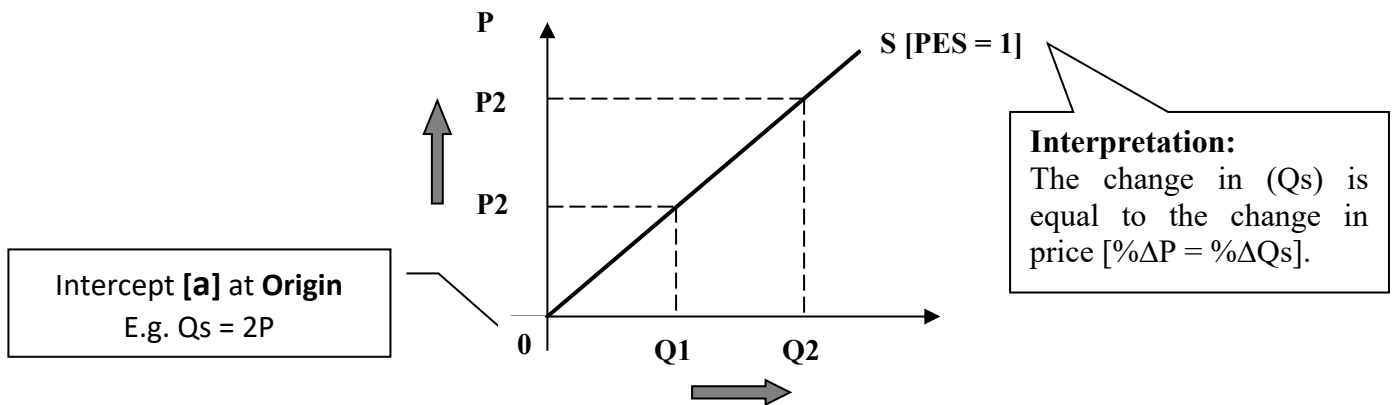
(01) Perfectly Inelastic Supply Curve



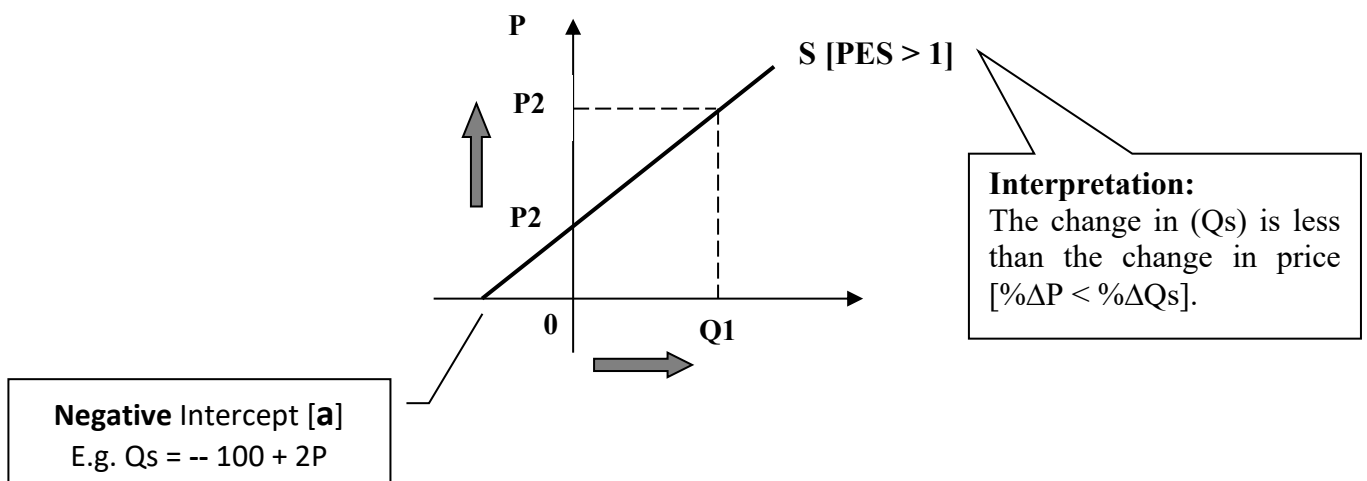
(02) Relatively Inelastic Supply Curve



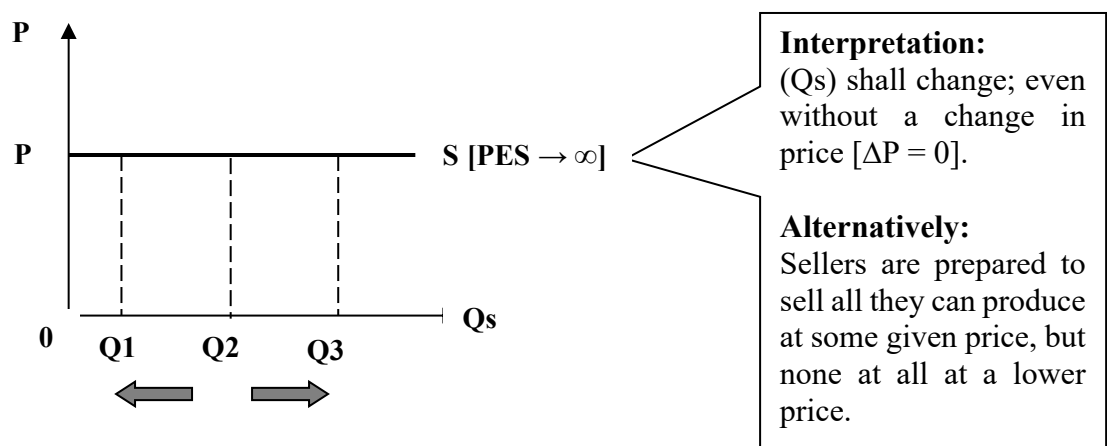
(03) Unitary Elastic Supply Curve



(04) Relatively Elastic Supply Curve



(05) Perfectly Elastic Supply Curve



Ensure to read these **illustrative notes** at least ☐

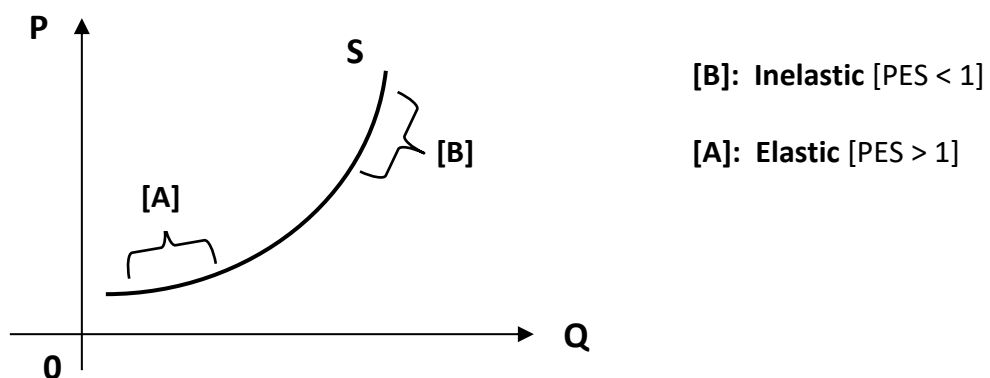
SUPPLY CURVE AND PRICE ELASTICITY OF SUPPLY [PES] COEFFICIENT

The price elasticity of supply behavior along the traditional upwards sloping supply curve tends to vary depending on the nature of the supply curve under consideration. Said PES behavioral variances, can be specifically observed when moving along two main types of supply curve diagrams:

- 1) Non-linear supply curve diagrams
- 2) Linear supply curve diagrams

(1) Non-linear Supply Curve

In a nonlinear traditional supply curve slopping upwards from left to right, PES tends to be **elastic at lower quantities** (output levels) as the firms' are below their full production capacity. While at **higher output levels PES is inelastic** as firms are nearing their full production capacity. Such elasticity behavior is deemed highly realistic.



(2) Linear Supply Curves (Traditional, upwards slopping)

(1.1) Constant value of PES coefficient along the curve

- Supply curve parallel to the price (vertical) axis: PES is zero at all points on the curve [perfectly inelastic curve]
- Supply curve passing through the origin: PES is one or unitary at all points on the curve [unitary elastic curve]
- Supply curve parallel to the quantity (horizontal) axis: PES reaches infinity at all points on the curve [perfectly elastic curve]

(1.2) Consistent elasticity type, PES coefficient changes along the curve

- Supply curve with a positive quantity axis intercept: **PES is constantly less than one** (inelastic), but **rises as quantity increases**.
- Supply curve with a negative quantity axis intercept: **PES is constantly more than one** (elastic), but **diminishes as quantity increases**.

TRQ [20]

State and briefly examine the principal **determinants** of price **elasticity of supply**

(05 marks)

- Production substitutability of production factors or mobility of production factors (number or production substitutes)
- Time period, required make and implement supply decisions (market/immediate time, short term and long term)
- **Nature of the product (ability store or perishability of the product)**
- **Availability of stock or inventory of finished goods and intermediate inputs**
- **Flexibility in production capacity (availability of excess production capacity)**
- **Nature or availability of the main raw materials**

Notes

Study Notes

[illegible]

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