Consumer Demand and Elasticity

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Course

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AutoEdge consideration to relocating their manufacturing process to America and increase the price of its good will affect their sales. Consumer demand is some products that a customer is willing and able to buy. AutoEgde manufactures engines and transmission parts. These are luxury goods. Elasticity is concerned with interpreting how price changes with the demand of a good or service (Ahuja 2008). The following discussion will evaluate whether elasticity of auto parts is; relatively elastic, relatively inelastic, unitary elastic, perfectly elastic or perfectly inelastic.

Perfectly elastic: this applies to goods whose demand is profoundly affected by a small change in its sale. When the price falls by a small margin, the demand rises to infinity but if the price increases by a little, the effective demand falls to zero. These goods are not common in real-life situations.

Perfectly inelastic: these are products whose demand does not change even when the price changes. When the price increases, the demand is the same as when the price falls. An example is medicinal drugs. If the price of vaccine falls, the consumer will not purchase more of it and when the price rises, the customer cannot but less than the quantity required. These goods are used in specific amounts.

Unitary elastic: the demand of these products changes in equal proportion to price changes. When the price increases by 10%, the demand of the good will increase by 10% and when the price decreases by 10%, the effective decrease in the sales will be 10%. An example of these goods is clothes. The demand for clothes changes accordingly to price changes because consumers have a limit on the number clothes they have. They cannot go too low or too high.

Relative elastic: in this concept, the change in demand is usually larger than the difference in price. When the price falls, the demand increases by a higher percentage and when the price rises, the effective demand decrease by a lower rate. For example, the price falls by 10%, the effective demand increases by 20% and when the price rises by 20%, the sales fall by 30%. This concept is used to explain the behavior of luxury goods. According to Ahuja, the price changes highly affect the demand because consumers can do without the product. These luxury goods are homogeneous hence they can easily be substituted. When AutoEdge relocates to America, they are likely not to get high sales unless they decide to lower their prices lower than that of the competitors.

Relative inelastic: this describes a relationship in which the percentage change in price and demand differ. The change in sales is usually lower than in price. This concept applies to essential goods such as food products. When the prize in pizza increases by 20%, its demand decreases by 10% and when the price falls by 30%, its demand increase by 20%.

From the above discussion, the elasticity of auto parts is relative elastic. If the company decides to go back to America, they need to know the current price of auto parts. It’s evident that increasing the price a small percentage will decrease the demand by a higher percentage. For the company to make profits, they will have to reduce the price below that of the competitors. Making profits is a challenge due to the current financial struggle of the company. The best decision would be to relocate slowly, that is, as they are rebuilding the company in the USA, manufacturing in South Korea should continue. The sales made in South Korea will help them control loses in America. The high unemployment and interest rates will also decrease the production cost.

Reference

Ahuja L. “Macroeconomics”. (2008). New Delhi: S. Chand.