**Som-Lalit Institute of Management Studies**

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## Elasticity of Demand

A tariff is a tax placed on the products of foreign countries sold in India. Assume, there is a 10% tax on foreign-made mobiles. Who would bear the incidence of this tax? Assume that a Korean Mobile and a similar Indian Mobile each sell in India at a price of Rs.20,000. With a 10% tax on Korean Mobile (Rs.2000), the Korean company would like to raise the price of its Mobile to Rs.22000. Whether it can do so or not depend on the price elasticity of demand for Korean Mobile. If the demand for Korean Mobile is relatively inelastic, the quantity demanded will fall very little at the price of Rs.22000. This means that buyers do not find Korean and Indian Mobile to be close substitutes. The incidence of the tax would be on the mobile buyers. On the other hand, if the demand for Korean Mobile is relatively elastic, the quantity of Korean Mobile demanded will fall considerably at the price of Rs22000. This means that buyers will closely substitute between Korean and Indian Mobile. The Korean company will have to charge a price close to Rs.20,000 in India to be able to compete. The incidence of the tariff will be on the Korean mobile companies. In technical language, a tariff on a foreign product that has very elastic demand is called an optimal tariff. The price of the foreign product will rise very less in India if there is high elasticity. Most of the tariff will be paid by the foreign company as reduced profits.

Q.1. What are the different types of elasticity of demand?

Q.2. Explain the situation in which the prices of mobile of the Korean company will be near Rs.22000.

Q.3. Explain the situation in which the prices of mobile of the Korean company will be near Rs.20000.