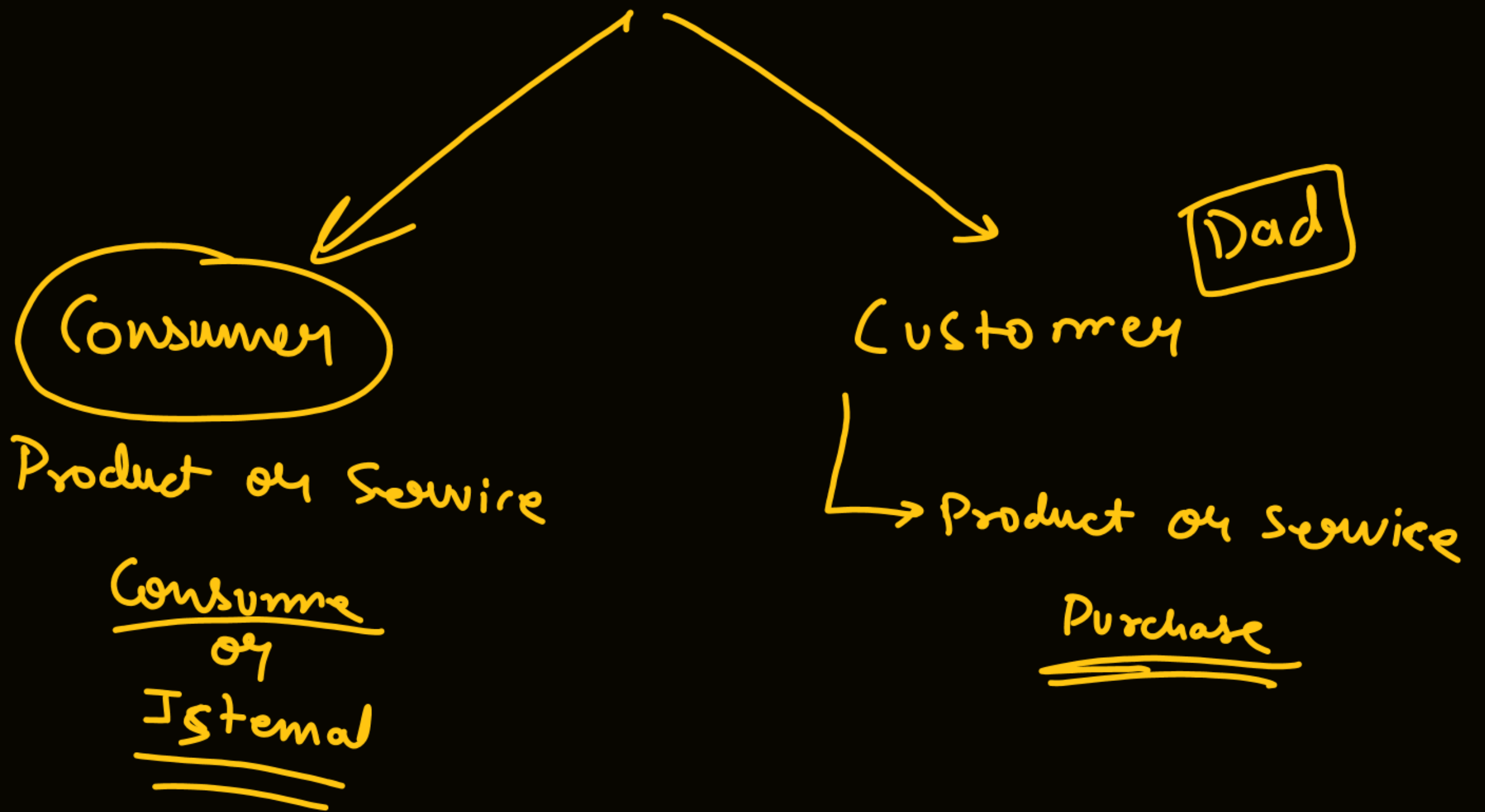


Class 11th | Economics



CONSUMER EQUILIBRIUM

LECTURE - 1



INTRODUCTION

A consumer is the main decision-maker of consumption pattern (A consumer is one who buys goods and services for satisfaction of wants) He takes decisions with regard to the kind of goods to be purchased in order to satisfy his wants. The main objective is to get maximum satisfaction from spending his income on various goods and services. A consumer is generally understood as an individual. But in reality, consumer consists of individuals or group of individuals or institutions.

During Shopping

Foreigners : It's Expensive

Indians : Aap Abhi Rakhiye Hum
Thodi Der Me Aate Hain.



INTRODUCTION

The aim of this chapter is to make you understand: How does a consumer maximize his satisfaction from consumption of goods and services. As the resources are limited in relation to unlimited wants, a consumer has to follow some principles or laws in order to attain the highest satisfaction level. The two main approaches to study consumer's behaviour and consumer's equilibrium are:

- Cardinal Utility Approach (or Marshall's Utility Analysis or Marginal Utility Analysis)
- Ordinal Utility Approach (or Indifference Curve Analysis or Hicksian Analysis)



CARDINAL UTILITY APPROACH

People consume different goods and services in order to maximise the satisfaction level. However, to do this, it is necessary to determine quantum of satisfaction obtained from a particular commodity. Under the Cardinal Utility Approach, the concept of "Utility" is used to attain the Consumer's Equilibrium.



CONCEPT OF UTILITY

Although the concept of taste and 'satisfaction' are familiar for all of us, it is much more difficult to express these concepts in concrete terms. For example, suppose you have just eaten an ice-cream and a chocolate. Can you tell how much are you satisfied from each of these items? Probably you can tell which item you liked more. But, it is very difficult to express "how much" you liked one over the other. It is evident, that we need a more quantitative measure of satisfaction. Due to this reason, economists developed the concept of utility.



MEANING OF UTILITY

Utility refers to want satisfying power of a commodity. It is the satisfaction, actual or expected, derived from the consumption of a commodity. Utility differs from person-to-person, place-to-place and time-to-time. In the words of Prof. Hobson, "Utility is the ability of a good to satisfy a want".



IN SHORT, WHEN A COMMODITY IS CAPABLE OF SATISFYING HUMAN WANTS, WE CAN CONCLUDE THAT THE COMMODITY HAS UTILITY.

MEANING OF UTILITY

Utils se measure
karate
hai
unit

How to Measure Utility?

After understanding the meaning of utility, the next big question is: How to measure utility? According to classical economists, utility can be measured, in the same way, as weight or height is measured. For this, economists assumed that utility can be measured in cardinal (numerical) terms. But, there was no standard unit for measuring utility. So, the economists derived an imaginary measure, known as 'Util', utils are imaginary and psychological units which are used to measure satisfaction (utility) obtained from consumption of a certain quantity of a commodity.

cm
Inches



Kg, g, mg



MEANING OF UTILITY

Example - Measurement of satisfaction in utils

Suppose you have just eaten an ice-cream and a chocolate. You agree to assign 20 utils as utility derived from the ice-cream. Now the question is: how many utils be assigned to the chocolate?

If you liked the chocolate less, then you may assign utils less than 20. However, if you liked it more, you would give it a number greater than 20. Suppose, you assign 10 utils to the chocolate, then it can be concluded that you liked the ice-cream twice as much as you liked the chocolate.



20 UTILS = Assume



10 UTILS

MEANING OF UTILITY

One more way to measure utility

Utils cannot be taken as a standard unit for measurement as it will vary from individual to individual) Hence, several economists including Marshall, suggested the measurement of utility in monetary terms. It means, utility can be measured in terms of money or price, which the consumer is willing to pay.



MEANING OF UTILITY

In the above example, suppose 1 util is assumed to be equal to ₹1. Now, an ice-cream will yield utility worth ₹20 (as 1 util = ₹1) and chocolate will give utility of ₹10. This utility of ₹20 from the ice-cream or ₹10 from the chocolate is termed as value of utility in terms of money. The advantage of using monetary values instead of utils is that it allows easy comparison between utility and price paid, since both are in the same units.



₹ 20



₹ 10

1 lakh Rs. ka dede toh bhi
Mai Mummy ke hath ki dal bathi nahi chodunga

MEANING OF UTILITY

“IT MUST BE NOTED THAT IT IS IMPOSSIBLE TO MEASURE SATISFACTION OF A PERSON AS IT IS INHERENT TO THE INDIVIDUAL AND DIFFERS GREATLY FROM PERSON-TO-PERSON. STILL, THE CONCEPT OF UTILITY IS VERY USEFUL IN EXPLAINING AND UNDERSTANDING THE BEHAVIOUR OF CONSUMER”.



EXPLORE MORE ABOUT UTILITY

- **Do not get confused with the dictionary meaning of utility:** The dictionary meaning of utility is given as usefulness. However, to an economist, higher utility does not mean greater usefulness. A commodity may not be useful, yet it may have utility for a particular person. For example, liquor is considered to be harmful for health, yet it may have a high degree of utility for an alcoholic.
- **Satisfaction Vs Pleasure:** Satisfaction must not be confused with pleasure. In fact, satisfaction need not involve actual pleasure. For example, treatment of a patient for his broken arm is a source of great satisfaction for the patient. However, it does not provide him any pleasure as it is merely a relief from pain.
- **Utility is Subjective:** Utility varies from person to person. For example, a thirsty person derives more utility from water in comparison to a person who is not thirsty.

To properly understand the meaning of utility, it is necessary to discuss two of its very important concepts:

(i) Total Utility and Marginal Utility;

(ii) Law of Diminishing Marginal Utility.



TOTAL UTILITY (TU)

Total utility refers to the total satisfaction obtained from the consumption of all possible units of a commodity. It measures the total satisfaction obtained from consumption of all the units of that good.

For example, if the 1st ice-cream gives you a satisfaction of 20 utils and 2nd one gives 16 utils, then TU from 2nd ice-creams is $20+16= 36$ utils. If the 3rd ice-cream generates satisfaction of 10 utils, then TU from 3 ice-creams will be $20+ 16 + 10 = 46$ utils.

TU can be calculated as:

$$TU_n = U_1 + U_2 + U_3 + \dots + U_n$$

Where:

TU_n = Total utility from n units of a given commodity

$U_1 + U_2 + U_3 + \dots + U_n$ = Utility from the 1st, 2nd, 3rd nth unit

n = Number of units consumed

Do Consider it

- 1. The utility derived from the first unit of a commodity is known as initial utility. For example: Utility of 20 utils from the first ice-cream is termed as the initial utility.**
- 2. Total utility is zero at zero level of consumption.**

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