UNIT – II

Consumer behaviour

Cardinal · Ordinal · Indifference · Surplus

Explanatory Lecture Slides

Micro Economics · Major-5 · Semester IV

MICRO ECONOMICS

LEARNING OBJECTIVES

Topics covered in this unit

01 **State the cardinal (Marshallian) theory**

02 **State the ordinal / indifference approach**

03 **Derive consumer equilibrium in both**

04 **Define consumer surplus**

05 **Place income and substitution effects**

06 **Note the limits for a court**

UNIT II · SYLLABUS MAP

How this unit is organised

01	02	03	04	05	06
Cardinal utility	Law of DMU	Indifference	Consumer equilibrium	Consumer surplus	Income / substitution

Cardinal utility

Utility is measurable in utils. Marshall: money is the measuring rod. MU of money constant.

- Useful: MU = λP at equilibrium. Weak: utility is not a thermometer.

Cardinal utility

KEEP	DROP
• MU/P equalisation. • DMU.	• Utils as a real unit.

Law of diminishing marginal utility

Successive units yield less additional utility. Foundation of the demand curve and of progressive taxation (ability-to-pay).

- Exceptions: money, hobbies in a range, addictions. A 6-mark with two uses (demand, taxation).

Law of diminishing marginal utility

USE

- Demand slopes down.
- Progressive tax.

EXCEPTION

- Miser.
- Collector.
- Addiction.

Indifference curves

Locus of bundles giving the same satisfaction. Properties: downward, convex, non-intersecting, higher = better.

- MRS = slope. Convexity = diminishing MRS. A 10-mark of properties + one diagram-sentence.
- Ordinal: we rank, we do not measure. Hicks–Allen.

Indifference curves

MUST

- Downward.
- Convex.
- No intersection.

MRS

- Rate at which Y is given up for X, satisfaction constant.

Consumer equilibrium

Cardinal: $MU_x/P_x = MU_y/P_y = \lambda$. Ordinal: $MRS = P_x/P_y$, on the budget line.

- Interior eqm. Corner solutions exist (the consumer buys zero of one good) — a 6-mark extra.
- A price fall: pivot of the budget line, new tangency, more of X if normal.

Consumer equilibrium

CARDINAL

- MU per rupee equalised.

ORDINAL

- Slope of IC = slope of budget.

Consumer surplus

What the buyer would have paid minus what she did pay. Marshall: area under demand above price.

- Dupuit’s invention; Marshall’s diagram. Uses: tax deadweight, public-works, damages as a story of lost surplus (careful in court).
- A 10-mark: definition, diagram-in-words, two uses, one limit (interpersonal, income effects).

Consumer surplus

USE

- Tax burden.
- Project appraisal.

LIMIT

- Not a rupee the court can always count.

Income and substitution effects

Price of X falls: X is cheaper against Y (substitution) and real income rises (income). Hicks and Slutsky decompose differently — name Hicks, skip the algebra unless asked.

- Giffen: negative income effect of an inferior staple outweighs substitution — the only upward demand that is not Veblen.

Income and substitution effects

NORMAL GOOD

- Both effects increase X.

GIFFEN

- Income effect backwards and huge.

Consumer equilibrium

Cardinal: $MU_x/P_x = MU_y/P_y = \lambda$. Ordinal: $MRS = P_x/P_y$, on the budget line.

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- A price fall: pivot of the budget line, new tangency, more of X if normal.

LANDMARK AUTHORITIES

Cases a KSLU answer should name

CASE

Lucknow Development Authority v M.K. Gupta

(1994) 1 SCC 243

Consumer protection as a legal cousin of consumer surplus — the State as a supplier.

CASE

Indian Medical Association v V.P. Shantha

(1995) 6 SCC 651

Professional services inside consumer law — the ‘consumer’ of microeconomics meets a statute.

CASE

CCI v Bharti Airtel

(2019) 2 SCC 521

Sectoral regulator and competition — consumer welfare is not only a Marshallian triangle.

STATUTE / SECTION MAP

Provisions & materials to quote

Consumer Protection Ac	The statutory consumer.
Sale of Goods Act 1930	Quality — the legal assumption behind a demand curve that trusts the good.
Art. 19(1)(g) / 19(6)	The seller’s freedom, limited.
Competition Act 2002	Consumer welfare as an aim of market law.
Legal Metrology Act 20	The kilo the demand curve thinks it is buying.

WRITE IT IN THE HALL

10 / 16-mark frames from this unit

Q1 Explain the law of diminishing marginal utility. What are its exceptions?

Q2 What is an indifference curve? State its properties.

Q3 Explain consumer’s equilibrium under the cardinal and ordinal approaches.

Q4 What is consumer’s surplus? What are its uses and limitations?

BEFORE YOU CLOSE THE FILE

Unit recap

1. Cardinal: MU/P; ordinal: MRS = price ratio.
2. IC properties: down, convex, no cross.
3. Consumer surplus = willingness minus price.
4. Giffen is income effect beating substitution.
5. CPA 2019 is the legal consumer of this unit.