Business Economics

WANTS

- **Definition**: *Wants* refer to any **desire**, **motive**, or **dream** of an individual.
- They can be **elementary (basic)** like food, water, shelter, or **psychological**, such as love, status, or recognition.
- **Wants are unlimited**, but the **means to satisfy them are limited** — this is the fundamental economic problem.

UTILITY

- **Definition**: Utility is the **want-satisfying power of a commodity**.
- It's the **capacity of a good or service** to provide satisfaction to the consumer.
- **UTILITY IS THE BASIS OF CONSUMER BEHAVIOUR.**

💡 **Important Distinction**:

- **Utility = Expected satisfaction**
- **Satisfaction = Actual experience after consumption**

🔁 **1. Form Utility**

- Created when the **form or shape of a commodity is changed** to increase its usefulness.
- ✅ *Example*: Cotton → Shirt, Wood → Chair.

📍 **2. Place Utility**

- Created by **changing the location** of a commodity to where it is more useful.
- ✅ *Example*: Apples transported from Himachal to Delhi.

🕒 **3. Time Utility**

- Created by **making goods available at the right time**.
- ✅ *Example*: Selling ACs in summer, or storing rice for off-season use.

👤 **4. Personal Utility**

- Arises from a **person's individual preferences or needs**.
- Utility changes **from person to person**.
- ✅ *Example*: A stethoscope is useful to a doctor but not to a lawyer.

🧠 **Characteristics of Human Wants**

Wants are the **starting point of all economic activity**. Understanding their nature helps explain consumer behaviours.

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1. ♾️ Wants are Unlimited

- Human wants have **no end** — as one is satisfied, another takes its place.
- Resources to satisfy them are limited, which creates **scarcity**.

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2. ✅ Each Want is Satiable

- A **single want can be fully satisfied**.
- After satisfaction, its utility drops to zero.
- *Example*: Once you're full, you don't crave more food.

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3. 📈 Wants Differ in Intensity

- Some wants are **urgent or basic** (like food), while others are **luxurious or optional** (like designer shoes).
- Intensity affects the **priority** of satisfying them.

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4. 🔥 Utility Depends on Intensity of Want

- The **greater the intensity**, the **higher the utility** of the good.
- *Example*: Water has more utility when you're thirsty.

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5. ⚔️ Wants are Competitive

- Since **resources are limited**, satisfying one want often means **sacrificing another**.
- We must **choose** which want to satisfy — this is the basis of **opportunity cost**.

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6. 🤝 Wants are Complementary

- Some wants **go together**, and satisfying one involves satisfying another.
- *Example*: Car + Petrol, Pen + Ink.

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7. 🔁 A Particular Want May Have Alternative Means of Satisfaction

- One want can be satisfied in **different ways**.

- *Example*: Hunger → Can eat rice, roti, pizza, or pasta.

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8. 👤 Wants are Subjective and Relative

- Wants **vary from person to person**, place to place, and time to time.
- *Example*: A jacket is essential in Kashmir, useless in Chennai summer.

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9. 💸 Wants are Influenced by Various Factors

- Wants change with:
  - **Income**
  - **Taste and preferences**
  - **Advertisement and trends**
  - **Social environment**

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10. 🌱 Wants Arise from Multiple Causes

- They originate from:
  - **Physical needs** (hunger, thirst)
  - **Psychological urges** (love, recognition)
  - **Social obligations** (gifts, festivals)
  - **Economic status** (rich vs. poor wants)

🧩 Classification of Human Wants

Human wants can be classified into **three main categories** based on their urgency, necessity, and nature:

🟢 1. Necessaries

These are **essential for survival** or for **maintaining efficiency** in daily life.
They are **urgent** and must be satisfied first.

🔹 a) Necessaries of Life

- Basic needs required for **existence**.
- *Examples*: Food, water, shelter, clothing.

🔹 b) Necessaries for Efficiency

- Goods that help maintain **productivity and efficiency** in work.

- *Examples*: Uniform for a nurse, spectacles for a student.

🔹 **c) Conventional Necessaries (Social Necessaries)**

- Arise due to **customs, traditions, or societal pressure**.
- These may not be essential by nature but are considered necessary in social contexts.
- *Examples*: Gifts at weddings, formal attire for official events.

🟡 **2. Comforts**

Wants that **make life more comfortable and convenient**.
Not urgent, but they **enhance quality of life**.

- *Examples*: Fan, cooler, washing machine, cushioned furniture.
- Help in **saving time, reducing effort**, or **increasing satisfaction**.

🔴 **3. Luxuries**

Wants that are **superfluous, non-essential, and often expensive**.
Mostly purchased to **show status or wealth**.

- *Examples*: Diamond jewellery, branded watches, luxury cars.
- Do **not contribute to efficiency** — they provide pleasure and status.

Criteria	**Cardinal Utility (Marshall)**	**Ordinal Utility (Hicks & Allen)**
Utility Measurement	Measurable (utils)	Ranked (ordinal)
Nature	Classical / Neo-classical	Modern
Tools Used	TU, MU, Equi-MU, Consumer Surplus	IC, MRS, Budget Line
Realism	Less realistic	More realistic
Substitution & Income Effect	Ignored	Included
Graphical Tool	MU curve	Indifference curve

Law of Diminishing Marginal Utility

Based on the fact that while total wants of a person are unlimited, each single want is satiable.

As a consumer consumes more and more units of a good, the intensity of his want for the good goes on decreasing.

Finally reaches a point where the consumer no longer wants it.

Assumptions

1. Cardinal
2. Rational consumer
3. Independent utility
4. MU of money is constant – unrealistic

Exceptions to **Law of Diminishing Marginal Utility**

- Money
- Addictive
- Rare collections

📘 **Consumer Surplus (CS) – Detailed Notes**

🔹 **Definition:**

Consumer Surplus is the **difference** between the **maximum price a consumer is willing to pay** for a good and the **actual price paid** in the market.

Alfred Marshall's Definition:
"Excess of the price which a consumer would be willing to pay rather than go without a thing over that which he actually does pay."

🔹 **Formula:**

Consumer Surplus (CS)=Willingness to Pay−Actual Price Paid\text {Consumer Surplus (CS)} = \text {Willingness to Pay} - \text {Actual Price Paid}
Consumer Surplus (CS)=Willingness to Pay−Actual Price Paid

Or for multiple units:

CS=Total Utility (TU)−Total ExpenditureCS = \text {Total Utility (TU)} - \text {Total Expenditure}CS=Total Utility (TU)−Total Expenditure

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🔹 **Origin / Basis:**

- Concept is **derived from the Law of Diminishing Marginal Utility**.
- Consumers get **less satisfaction** from each additional unit but pay the **same price** for all units.
- The **gap between utility and price** for each unit adds up to consumer surplus.

🔹 **Graphical Representation:**

- **Demand curve** represents marginal utility (willingness to pay).
- **Market price** is a horizontal line (actual price).
- **Area between demand curve and price line**, up to the quantity purchased, = **Total Consumer Surplus**.

🔹 **Consumer Surplus and Demand Curve Relationship:**

1. **Closely Related to Demand Curve:**
    - The demand curve shows what consumers are **willing to pay**.
    - The area between the **demand curve and price line** represents **consumer surplus**.
2. **Total Consumer Surplus in Market:**
    - The **total area under the demand curve and above price level** = **sum of individual surpluses** of all buyers.
3. **Price Change Impact:**

✅ **When price falls:**

- **Existing buyers** get more surplus (they pay less).
- **New buyers** enter the market and also gain some surplus.

❌ **When price rises:**

- Consumer surplus **shrinks** due to higher cost and potential exit of some buyers.

📘 **Ordinal Utility Approach & Indifference Curve Analysis**

🔹 **Developed By:**

- **J.R. Hicks** and **R.G.D. Allen**

🔹 **Concept Type:**

- **Ordinal Utility** → Utility cannot be measured in numbers (like utils)
- Instead, it is **ranked or ordered** based on consumer preference
  (e.g., Combo A is preferred over Combo B, but not by "how much")

🔹 **Indifference Curve (IC):**

Also called: **Iso-Utility Curve** or **Equal Utility Curve**

- A curve that shows **different combinations of two goods** that give the **same level of satisfaction** to the consumer.
- On any IC, the consumer is **indifferent** between combinations.

📈 **Properties of Indifference Curves:**

1. **Downward Sloping**
   – To maintain the same utility, if you consume **more of one good**, you must **give up some of the other**.
2. **Convex to the Origin**
   – Due to **diminishing marginal rate of substitution** (MRS falls).
3. **Higher IC = Higher Utility**
   – More is preferred to less.
4. **ICs Never Intersect**
   – Each IC represents a **unique level of utility**.

🔁 **Marginal Rate of Substitution (MRS):**

The rate at which a consumer is **willing to substitute** one good (Y) for an additional unit of another good (X), keeping total satisfaction constant.

🔸 **Formula:**

$MRS_{xy} = \frac{MU_y}{MU_x} = -\frac{\Delta X}{\Delta Y}$

- It is the **slope of the indifference curve**.
- MRS usually **declines** as the consumer substitutes more of X for Y.

⬇️ **Why MRS Diminishes? (2 Reasons)**

1. **Satiability of Wants**
   – As the consumer has more of good X, their **intensity of want for X falls**.
2. **Imperfect Substitutes**
   – Most goods cannot perfectly replace each other, so the consumer is **less willing** to give up a good as it becomes scarcer.

🔁 **Perfect vs. Imperfect Substitutes:**

Type of Goods	MRS Behaviour	IC Shape
Perfect Substitutes	Constant MRS	Straight line
Imperfect Substitutes	Diminishing MRS (realistic)	Convex to origin

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🧠 **Why This Approach Is Better:**

- No unrealistic measurement of utility in numbers.
- Captures **real consumer behavior** more accurately.
- Can explain **substitution and income effects**.