

Key Takeaways Lecture 3

Consumer Theory: Definition Meaning and Objective

KEY TAKEAWAYS

- **Consumer theory** is the study of how people decide to spend their money based on their individual preferences and budget constraints.
- Building a better understanding of individuals' **tastes** and **incomes** is important, because these factors impact the shape of the overall economy.
- Though useful, consumer theory is **not flawless**, as it is **based on a number of assumptions about human behavior**.

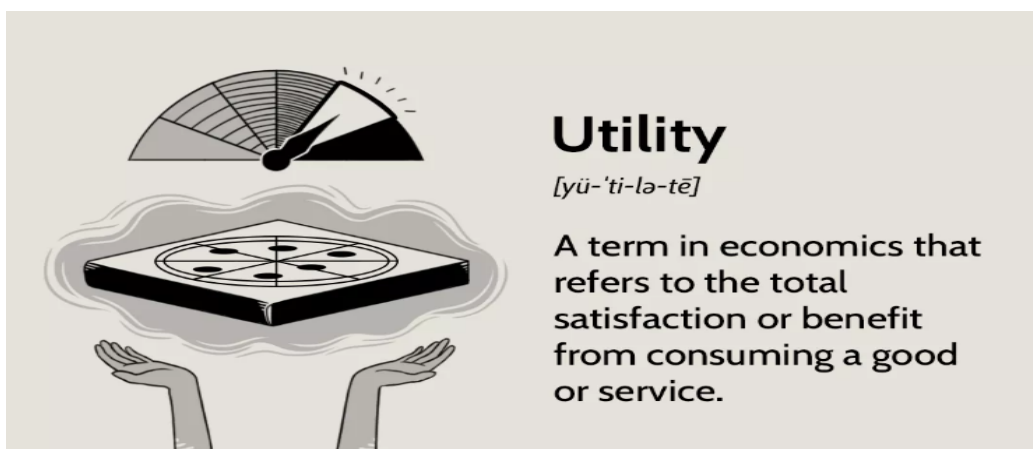


Utility in Economics Explained:

Types and Measurement

KEY TAKEAWAYS

- **Utility**, in economics, refers to the usefulness or **enjoyment** a consumer can get from a service or good.
- Although the concept of utility is abstract, it is a useful way to explain **how and why consumers make their decisions**.
- "**Ordinal** Utility" refers to the concept of **one good being more useful or desirable than another**.
- "**Cardinal** Utility" is the idea of measuring economic value through **imaginary units**, known as "utils."
- **Marginal Utility** is the utility gained by consuming an additional unit of a service or good.



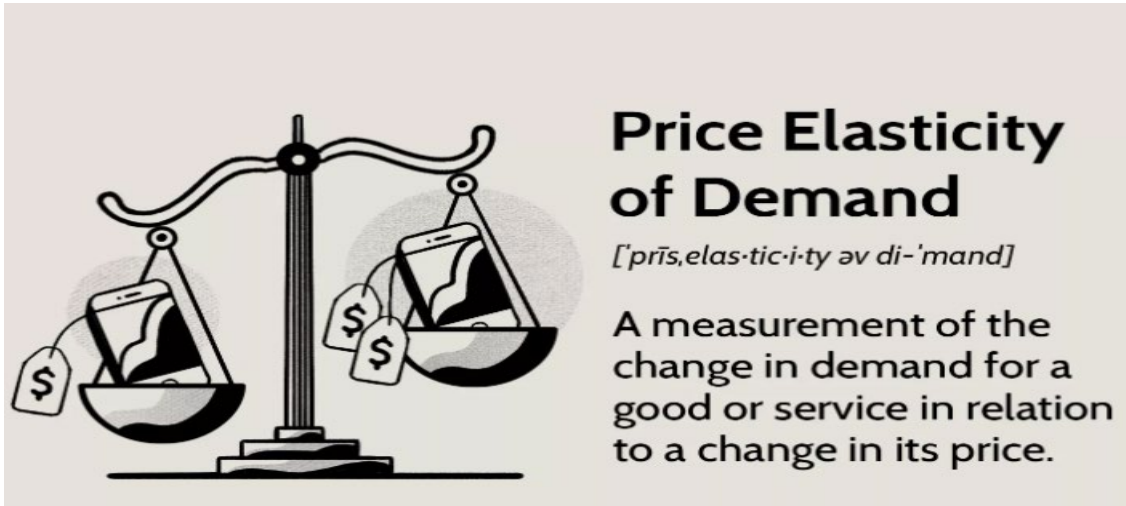
- **Total Utility** the aggregate amount of satisfaction or fulfillment that a consumer receives through the consumption of a specific good or service.

Important:

Economic utility can be estimated by observing a consumer's choice between similar products. However, measuring utility becomes challenging as more variables or differences are present between the choices.

Price Elasticity of Demand:

Meaning, Types



KEY TAKEAWAYS

- **Price elasticity of demand** is a measurement of the change in consumption of a product in relation to a change in its price.
- A **good** is **elastic** if price elasticity is **>1**.
- A **good** is **inelastic** if price elasticity is **<1**.
- A **good** is **unitary elastic** if price elasticity **=1** (price change leads to an equal percentage change in demand).

➡ **An elastic demand** is one in which the change in quantity demanded due to a change in price is large.

An inelastic demand is one in which the change in quantity demanded due to a change in price is small.

- The availability of a substitute for a product affects its elasticity: If there are **no good substitutes** and the **product is necessary**, demand won't change when the price goes up, making it **inelastic**.

