

Study Materials For BA (Hons.) Economics

Part – 1

Paper – Subsidiary

Topic – Utility Analysis

Introduction

The term utility in Economics is used to denote that quality in a good or service by which our wants are satisfied. In, other words utility is defined as the want satisfying power of a commodity.

Assumption of utility analysis

Cardinal utility analysis of demand is based upon certain important assumptions.

- 1- The utility analysis is based on the cardinal concept which assumes that utility is measurable and additive like weights and lengths of goods.
- 2- Cardinal or Utility is measurable in terms of money.
- 3- The marginal utility of money is assumed to be constant
- 4- The consumer is rational who measures, calculates, chooses and compares the utilities of different units of the various commodities and aims at the maximization of utility.
- 5- He has full knowledge of the availability of commodities and their technical qualities.
- 6- He possesses perfect knowledge of the choice of commodities open to him and his choices are certain.
- 7- They know the exact prices of various commodities and their utilities are not influencing by variations in their prices.
- 8- There are no substitutes.

Features of utility analysis

- A- **Subjective:** - The utility is subjective because it deals with the mental satisfaction of a man. A commodity may have different utility for

different persons. Cigarette has utility for a smoker but for a person who does not smoke, the cigarette has no utility. Utility, therefore, is subjective.

- B- Relative: - The utility of a good never remains the same. It varies with time and place. The fan has utility in the summer but not during the winter season.
- C- Utility and usefulness: - A commodity having utility need not be useful. Cigarette and liquor are harmful to health, but if they satisfy the want of an addict then they have utility for him.
- D- Utility and morality:- The utility is independent of morality. Use of liquor or opium may not be proper from the moral point of views. But as these intoxicants satisfy wants of the drunkards and opium eaters, they have utility for them.

Concept of Utility Analysis

Total utility: - Total utility is the sum of utility derived from different units of a commodity consumed by a household. Supposing a consumer four units of apple. If the consumer gets 10 utils from the consumption of first apple, 8 utils from the second, 6 utils from third, and 4 utils from the fourth apple, then the total utility will be $10+8+6+4 = 28$.

Marginal utility: - The Marginal Utility is the utility derived from the additional unit of a commodity consumed. The change that takes place in the total utility by the consumption of an additional unit of a commodity calls marginal utility.

Average utility: - average utility is ratio of total utility and total good or commodity consumed by a consumer or household