

Economics Class 12 Important Question Chapter 2

Theory of Consumer Behaviour

Q1. What does utility mean?

Ans: Utility refers to a commodity's ability and power to meet needs. It is a level of satisfaction associated with economic activity.

Q2. Describe the law of diminishing marginal utility.

Ans: A convex indifference curve results from a declining marginal rate of substitution, which is the answer. Any increase in consumption after a certain point can cause Total Utility (TU) to decrease.

Short Answer Questions 3-4 Marks

Q1. Describe any four factors that affect a commodity's demand.

Ans: The factors that determine demand are as follows:

Commodity price (Px): The demand for any commodity is significantly influenced by its price. Keeping other things constant, the demand will be low if the price of the commodity rises, while the demand will be high if the price of the commodity falls.

Accordingly, for most items, the connection between the quantity demanded and the price is inverse.

Consumer income (Y): Another significant factor affecting demand for an item is consumer income.

Demand for commodities is influenced by changes in consumer income. As income levels rise, so does the demand for everyday items, and vice versa. It demonstrates a direct connection between income and the volume of demand.

Price of related goods: The cost of other commodities, particularly substitutes or complementary, has an impact on a commodity's demand.

Products that can be easily substituted for one another are referred to as substitute goods. For example, tea and coffee. These items are referred to as substitute goods when a rise in the price of tea leads to an increase in the demand for coffee despite no change in the price of coffee. In other words, there is a positive relationship between two substitute commodities. If the demand for another product rises as a result of the price of one.

Complementary products are items that one purchases alongside other items. For example, a car and gasoline. These items are referred to as complementary goods when a rise in the price of gasoline results in a decrease in demand for automobiles. In other words, there is a negative relationship between two complementary products. The demand for other commodities declines when the price of one product rises.

Tastes and Preferences: A commodity's demand is influenced by a variety of factors, including changes in fashion, culture, tradition, and consumer taste and preferences. The demand for a particular good or service fluctuates along with changes in customer taste and preference. In other words, if a customer's taste and preferences are favourable, demand for that good rises; if they are unfavourable, demand falls. As a result, a consumer's taste and preferences are crucial.

Q2. A buyer purchases 50 units of a product for Rs. 4 each. When its price decreases by 25%, demand increases to 100 units. Determine the price elasticity of demand.

Ans: Given:

$$P=4$$

$$Q=50 \text{ units}$$

$$Q_1=100 \text{ units}$$

The fall in price is calculated as:

$$P=4 \times 25/100$$

$$=1$$

$$\Delta P=P_1-P$$

$$= 3 - 4$$

$$= -1$$

Similarly,

$$\Delta Q=Q_1-Q$$

$$= 100-50$$

$$= 50$$

The elasticity of demand is calculated by the formula,

$$E_d = -P/Q \times \Delta Q/\Delta P$$

$$= -4/50 \times 50/-1$$

$$= 4$$

Therefore, the price elasticity is 4

Long Answer Questions 6 Marks

Q1. What are the methods for calculating demand-price elasticity?

Ans: The following are the techniques for calculating price elasticity of demand:

Proportionate or percentage method: Using this method, elasticity is computed as the ratio of the percent change in the quantity needed to the percent change in price.

The formula is shown below:

$$E_d = \% \text{ change in quantity demanded} / \% \text{ change in price}$$

Or

$$E_d = \Delta Q / \Delta P \times P / Q$$

Total outlay method: The elasticity of demand is greater than one if total outlay rises as prices fall, equal to one if total outlay stays the same, and less than one if total outlay falls.

Point or geometrical method: This method evaluates the demand elasticity along different stretches of the same demand curve.

E_d = the lower segment of the demand curve / the upper segment of the demand curve

Q2. How does indifference curve analysis aid in the achievement of equilibrium?

Ans: A consumer is said to be in equilibrium when he experiences the most satisfaction from his purchase. The highest level of satisfaction a consumer may have given their income and pricing is referred to as "consumer's equilibrium." Consumer equilibrium can be explained using the indifference curve method.

The following illustration explains the diagram from above.

(i) AB stands for the budget line.

(ii) It is certain that the equilibrium for consumers will be situated in the same spot on AB.

(iii) The preferences of consumers for different pairings of good x and good y are shown on an indifference map (set of IC1, IC2, and IC3).

(iv) Customers will reach equilibrium when the budget line (AB) is perpendicular to the IC₂.

The consumer's equilibrium position is calculated under the following presumptions:

Rationality: The client is a logical entity. A consumer aims for the highest level of fulfilment with the given resources and prices.

The utility is ordinal: It is assumed that the consumer can rank his preferences according to how happy each product combination makes him feel.

Choice consistency: Another theory holds that consumers consistently make purchases.

Perfect competition: There is perfect competition in the market where the consumer buys the goods.

Total utility: The amount of the good consumed affects the consumer's overall utility.