Examrace

Competitive Exams: Consumer Surplus

Explain consumer's surplus with support of figure diagram. What difficulties one faces in measuring consumers surplus

consumer surplus is equal to the difference between the amount of money that a consumer actually pays to buy a certain quantity of a commodity x, and amount that he would be willing to pay for this quantity rather than do without it.

Graphically the consumer's surplus may be found by his demand curve for commodity x and the current market price, which is assumed, he cannot affect by his purchases of this commodity. Assume that the consumer's demand for x is a straight line (AB in below fig) And the market price P. At this price consumer buys q units of x and pays an amount (p) for it. However, he would be willing to pay p1 for q1. P2 for q2, p2 for q3 and so on. The fact that the price in the market is lower than the price he would be willing too pay for initial units of x implies that is actual expenditure is less than he would willing to spend to acquire the quantity q. The difference is the consumer's surplus, and is the area of the triangle PAC in the fig. Below

Thus consumer surplus may be defined as the excess of utility or satisfaction obtained by the consumer and is measured by the difference between what we are prepared to pay and what we actually pay.

Difficulties in Measuring Consumer's Surplus

- The cardinal measurement of utility is difficult: Because it is close to impossible for a consumer to say that the first unit of commodity gave him 10 units of satisfaction and the second unit of commodity gave him 5 units of satisfaction.
- Marginal utility for the same commodity id different to different consumers: Marginal utility for a particular commodity varies from person to person depending upon their income, tastes and preferences.
- Existences of substitutes: In the real world a number of substitutes for a commodity exist, thus making the work of measuring consumer's surplus a complicated task.
- Marginal utility of money is not constant: Marshall based his concept of consumer's surplus on the simplifying assumption that the marginal utility of money is constant. As the consumer buys more and more units of a commodity x, the amount of money with him diminished, in this case, the marginal utility of money is bound to increases rather than remain constant.

- Lack of awareness of different price: It is not possible for a consumer be of the entire demand schedule.