Notes on Chapter 5

Marginal Utility and Consumer Choice:

We discussed how Utility is synonymous to satisfaction. We emphasized that in economics we are concerned only with market–derived contributions to our happiness or utility. We introduced Utils as a measure of utility. We stressed that utils are simply a hypothetical measure which can be used to rank commodities and should never be used to do interpersonal comparison of utility. We discussed the difference between Total Utility and Marginal Utility. We talked about the Law of Diminishing Marginal Utility and showed the relationship that exists between Total Utility and Marginal Utility. We talked about the Water-Diamond Paradox and how it is the marginal utility which determines the value/price of a product not the total utility. We used several examples and tables to understand how we make product selections under a fixed budget. As a byproduct we get some insight regarding the Law of Demand. We showed that as the price of a product falls, the MU/P ratio increases and makes the product more attractive. This then leads to a reallocation of our spending and we buy more of that product. We discussed the MU/P Equalization Principle and emphasized its importance. We finished the chapter with a discussion of Consumer Surplus.