BY: DR. SHAILESH KR. SINGH
ASSISTANT PROFESSOR (GUEST)

Ref. No.: DBC/BE **Date:** 25 July, 2020

B.COM. PART 1

CORE CONCEPT OF BUSINESS ECONOMICS

Cardinal Vs. Ordinal Utility Approach

Utility refers to the satisfaction that a consumer obtains from the purchase and use of commodities and services. According to economics there are two theories that are able to measure the satisfaction of individuals. These are the cardinal utility theory and the ordinal utility theory. There are a number of differences between the two in the methodologies that they use to measure consumption satisfaction. The article that follows offers a clear explanation on each type of theory and highlights the main differences between cardinal utility and ordinal utility.

Cardinal Utility-Cardinal utility states that the satisfaction the consumer derives by consuming goods and services can be measured with numbers. Cardinal utility is measured in terms of ***utils*** (the units on a scale of utility or satisfaction). According to cardinal utility the goods and services that are able to derive a higher level of satisfaction to the customer will be assigned higher utils and goods that result in a lower level of satisfaction will be assigned lower utils. Cardinal utility is a quantitative method that is used to measure consumption satisfaction.

Ordinal Utility- Ordinal utility states that the satisfaction the consumer derives from the consumption of goods and services cannot be measured in numbers. Rather, ordinal utility uses a ranking system in which a ranking is provided to the satisfaction that is derived from consumption. According to ordinal utility, the goods and services that offer the customer a higher level of satisfaction will be assigned higher ranks and the opposite for goods and services that offer a lower level of satisfaction. The goods that offer the highest level of satisfaction in consumption will be provided the highest rank. Ordinal utility is a qualitative method that is used to measure consumption satisfaction.

What is the difference between Cardinal and Ordinal Utility?

Cardinal and ordinal utility are theories that are used to explain the levels of satisfaction that a consumer derives from the consumption of goods and services. There are a number of differences between the methods in which either measure consumption satisfaction. While cardinal utility is a quantitative measure, ordinal utility is a qualitative measure. Using Cardinal utility a customer can assign a number to a product that when consumed was able to satisfy their needs. Using ordinal utility a customer can rank the products according to the level of satisfaction that was derived. Further to this in cardinal utility it is assumed that consumers derive satisfaction through consumption of one good at a time. However, in ordinal utility it is assumed that a consumer may derive satisfaction from the consumption of a combination of goods and services, which will then be ranked according to preference.

Summary:

Cardinal vs Ordinal Utility

• Utility refers to the satisfaction that a consumer obtains from the purchase and use of commodities and services. According to economics there are two theories that are able to measure the satisfaction of individuals. These are the cardinal utility theory and the ordinal utility theory.

• Cardinal utility states that the satisfaction that the consumer derives by consuming goods and services can be measured with numbers.

• Ordinal utility states that the satisfaction that the consumer derives from the consumption of goods and services cannot be measured in numbers. Rather, ordinal utility uses a ranking system in which a ranking is provided to the satisfaction that is derived from consumption.

• While cardinal utility is a quantitative measure, ordinal utility is a qualitative measure.

• In cardinal utility, it is assumed that consumers derive satisfaction through consumption of one good at a time. However, in ordinal utility it is assumed that a consumer may derive satisfaction from the consumption of a combination of goods and services, which will then be ranked according to preference.

UTILITY ANALYSIS:

A subset of consumer demand theory that **analysis** consumer behavior and market demand using total **utility** and marginal **utility**. The key principle of **utility analysis** is the law of diminishing marginal **utility**, which offers an explanation for the law of demand and the negative slope of the demand curve.