

# CHALLENGING THE RELEVANCE OF BUDGET LINE IN PRATICAL LIFE AND RE-DRAWING IT

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## **Abstract:**

The basic objective of Research is to critically analyse the established facts or theories and propound new one that serve the mankind in this dynamic world . This article is an attempt in the direction of propounding a new structure of Budget line which fits into the practical life.

The presently accepted concept of budget line is based upon an assumption that the Budget line shows all possible combination of two goods that consumer can buy if he spends the whole of his given sum of money on his purchase at the given prices. Thus it is a concept based upon an assumption.

But our practical life is not based upon assumption, and according to me the budget line does not satisfy the real practical life situation if a consumer. As in our practical life we have to buy hundreds of goods with our given income, the prices of which are also dynamic and at times we also purchase goods on which are beyond our income or budget.

This article critically analyses the concept of Budget line and propounds a new Budget Line that would be more relevant in our practical dynamic life.

Keywords: Budget line, relevance, propound, dynamic, critically, concept, practical theories.

## **Introduction :**

Modern world is dynamic and the theories and concepts which are based and established on the foundation stone of some assumptions which make us step into a static world have little impact on our practical life. Assumption and assumption based upon assumption to prove our theories right reflects Economics more as an Assumptive Science. In our real life we don't have the shield of assumption to prove our concept as right .

This article challenges the concept of budget line on point to point basis. Its concepts are challenge by practical life limitations and lastly a new budget line, which I call as the practical application of budget line is our dynamic life.

Thus in this practical dynamic world, where assumptions have no space, where our needs, prices of goods and our income keep changing every now and then, we get a very interesting practical price line /budget line which keeps on moving up and down rising and falling like innumerable waves of the sea.

**Literature Review:**

The concept of Budget/ price line is a very celebrated concept in Microeconomics. So very little effort has been made in the direction of challenging its practical application.

The Budget Line/ Set, Slope and Shift / Microeconomics, by Smriti Chand.

The article defines and explains the concept of Budget line, Budget set, Algebraic Expression of Budget Line, Slope of the Budget Line, Price Ratio, Shifts in the budget line, effects of change in the relative prices of goods on Budget line, etc.

But the article is silent on the relevance of Budget Line in this practical dynamic world, where a consumer has multiple of choices to make with his given income.

## 2. Budget Line: Notes on Budget Line, Space Changes and Slope

By J. Singh

This articles opens up claiming that the concept of budget line is essential for understanding the theory of consumer's equilibrium and further consumer's equilibrium can be explained by introducing it into indifference curve analysis and after explaining the concept of budget line establishes that the slope of the budget line is equal to the ratio of the price of two goods.

but again it remains unanswered that what practical relevance will it make if we base assumptive theories to prove other assumptive theories.

### 1- The Budget Line – Priciples of Microeconomics.

by E. Hutchinson-2017.

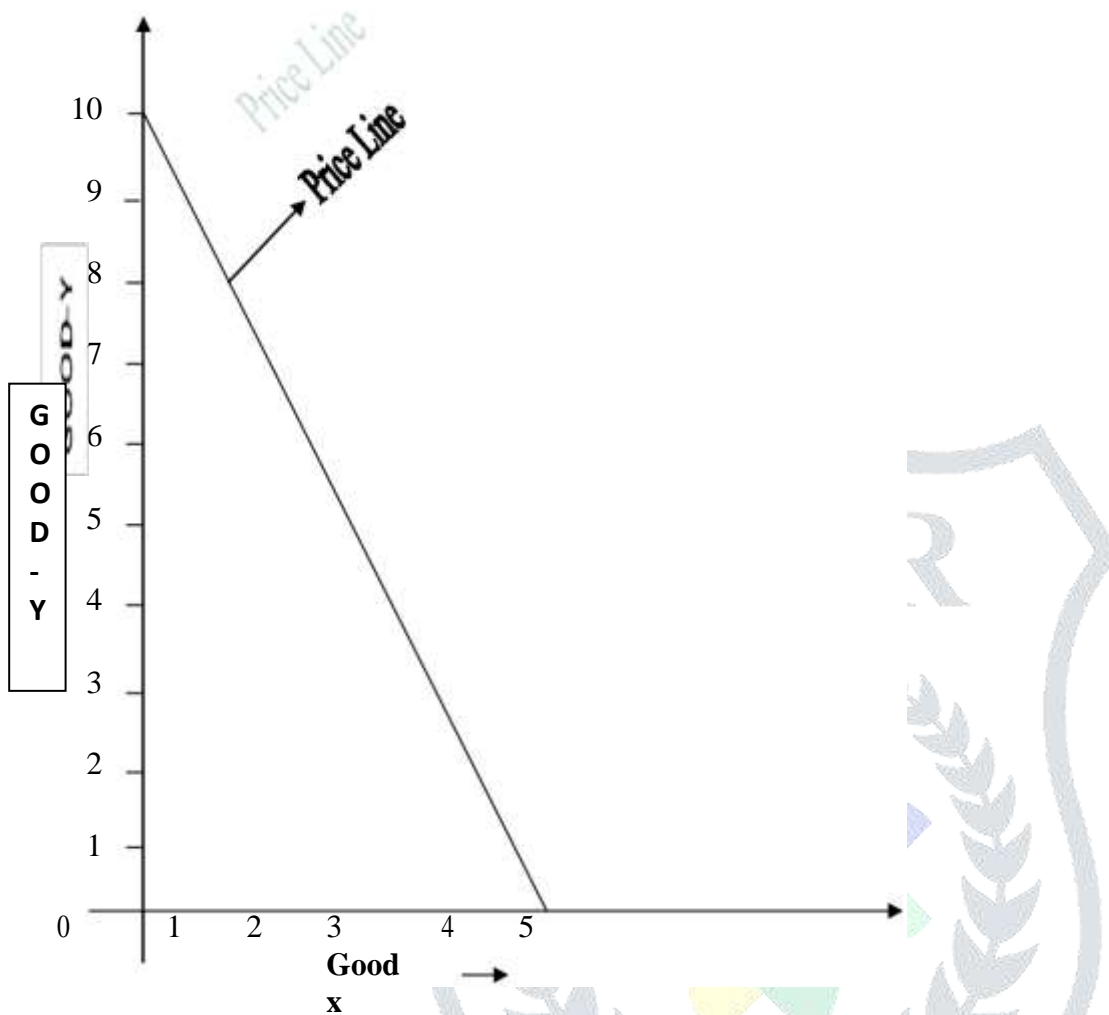
In this book, Principles of Microeconomics topic-6, consumer theory, the concept of budget line is explained further price ratios, recreation of budget lines with price and income changes are effectively dealt with. Again it is silent on the grounds of challenging it on practical relevant ground.

Methodology: Logical criticism , logical conclusions from day today practical dynamic life examples are taken into consideration and new budget line/ lines are redrawn which fits into the dynamic practical life of a consumer making it more relevant.

### **The Relevance of Price Line/ Budget Line in practical life.**

The price line represents the prices of the goods and the consumer's money income. It shows all those combinations of two goods which the consumer can buy spending his given money income on the two goods at their given prices.

Suppose ,I have an income of Rs. 500 per day to spend on goods x and y. let the price of the goods x in the market be Rs 100 per unit and that of good y be Rs 50 per unit. If I spend my whole income on only these two goods I would buy 5 units of goods X or 10 units of good Y. If, I tend to spend my entire income on either one of these two goods respectively, I shall get a straight line joining 5 x and 10 y is drawn we get, what is called as the budget line.



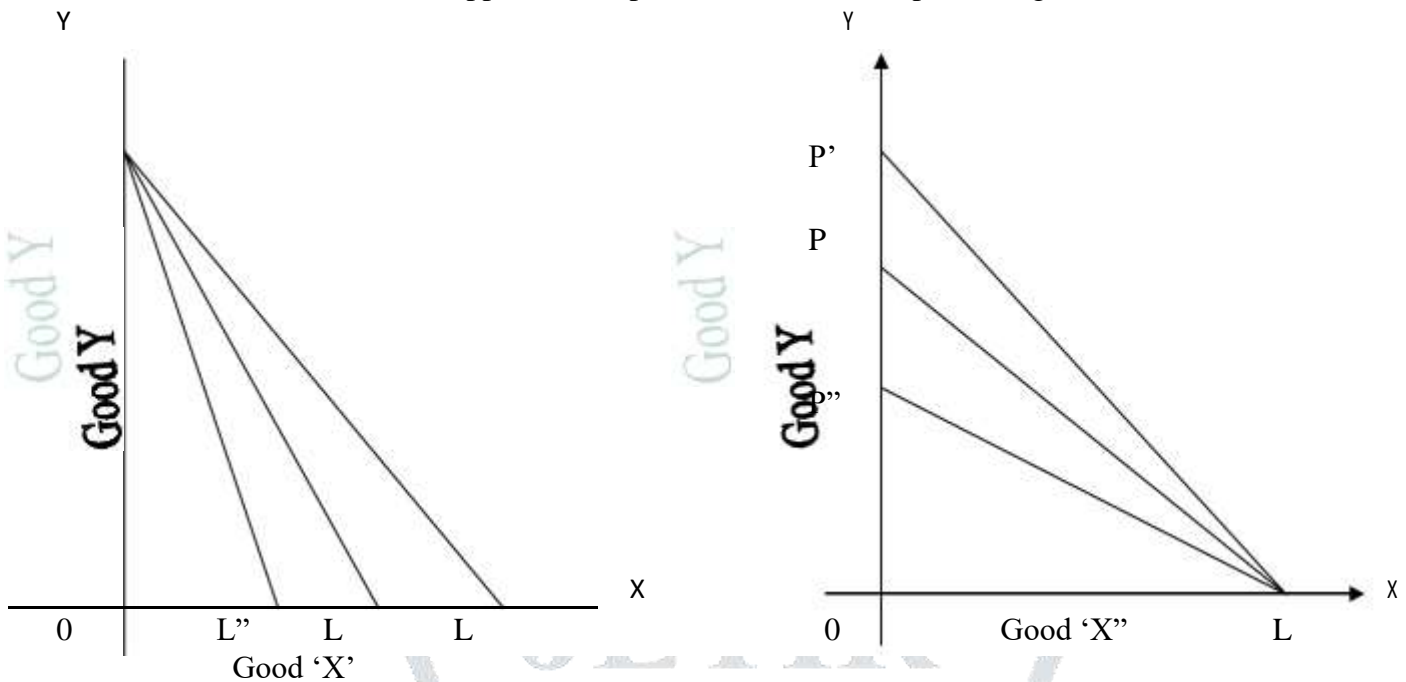
### Limitations :

The concept of price line under the assumption that I have to spend my entire income upon only two goods X and Y holds good. But the moment I step into the practical world out of the theory, I find it impossible or rather improbable to draw the budget line with my given income when in reality I have to buy scores of goods and services as well. More over in practical life we cannot spend the whole of our income on a single or a couple of goods. If I need bread, butter, clothes, tooth brush, paste, petrol, pen and so on what will be the shape of my budget line, will it be a straight line, several parallel lines, or a grid of lines intermingling with each other .

So I find it irrelevant in practice while drawing my own budget line because: with the assumption that whole of the given income is spent on given goods and at given prices if the consumer has to choose among from all those combination which lie on the price line.

In this dynamic world the prices of goods keep changing so in a day while I shall prepare a budget line even for only two goods I shall find that the prices of goods have changed meanwhile I drew the price line with previous prices.

Now what happens to the price line if either the prices of goods



Suppose the price line in the beginning is  $PL$ , given certain price of the goods  $X$  and  $Y$  and a certain income suppose the price of  $X$  falls and price of  $Y$  remains unchanged. Now with a lower price the consumer will purchase more quantity of  $X$  than before with his given income. Let us suppose that at lower price of  $X$ , we get a new price line  $PL^1$ .

Again, if the price of good  $X$  rises, and that of good  $Y$  remains unchanged then the consumer will buy less of good  $X$ , according to our assumption, we get a new price line  $PL^2$ . Similarly if the price of good  $Y$  falls and that of good  $X$  remains unchanged we get a new price line as in fig (b). as  $LP^1$ .

If the price of good  $Y$  rises and that of good  $X$  remain unchanged we again get another price line  $LP^2$  denoting less quantity of good  $Y$  being bought by the consumer.

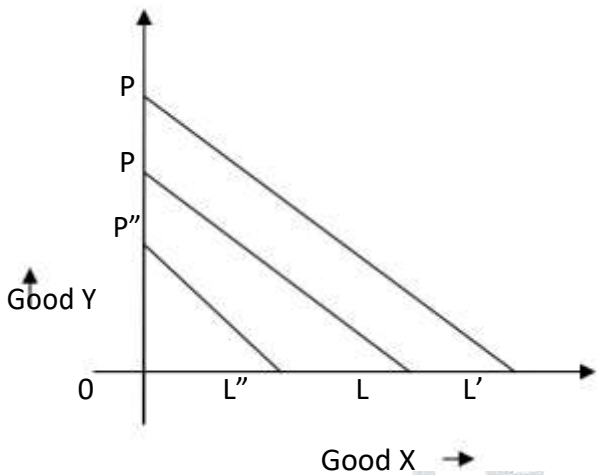
Limitations: Again the moment we test this concept out of the domain of assumption I find it if not totally, then partially true on these grounds:

1. If I am a labourer and with the given income I choose two goods bread and potatoes, then with a fall in price of potatoes, shall I buy more potatoes or will be guided by Giffen's Law to purchase a superior good say eggs or meat with my real income being risen due to fall in price of potatoes. So, to hold one theory true by assumption we are holding another theory untrue.

2. If the two goods I choose with my given income are paying the fees of a doctor and that of buying medicines as per the prescription of the doctor.

If the doctor will lower his fees how and why shall I avail more of his services with his fallen fees again, if the price of medicine falls, shall I buy more medicines than what is required to justify the concept of price line.

3.If, I am a rich man and the price of a luxury good out of the two luxurious goods that I have chosen falls then shall I buy more of that good or will be guided by the Veblen effect. Again to justify the assumption of price line the theory of Veblen shall have to be axed. Now the question is, what happens to the price line, if the income changes while the price of goods remain the same. The effect of change in income on the price line is shown in fig(c).



let PL be the initial price line given

certain price of goods and income if the consumer income falls and price of goods x and y remain unchanged then the price line will shift downwards from PL to P<sup>2</sup>L<sup>2</sup>

on the other hand if the income of the consumer increases and that the price of goods

x and y remain unchanged then the price line

will shift outwards from PL to P<sup>1</sup>L<sup>1</sup>, because a lower income will purchase a proportionately smaller quantities of both goods X and Y and vice-versa.

It is clear from above that the price line will change if either the price of goods change or the income of the consumer changes.

Thus, the two determinants of the price line are: a) the price of goods and

b) the consumer's income to be spent on the goods.

**Limitations:**

1.The concept of price accept the part of the law of demand as long as it suits it, to prove it true. It admits the fact that with lower income lesser quantity of a good is demanded and when the price of a good falls, its demand rises and vice versa, but it fails to recognise that there are other determinants to our demand other than income of the consumer and the price of the goods concerned. The other determinants such as our tastes and preferences, the price of related goods, fashion, reputation of the goods purchased etc. are totally ignored in the determinants of price line.

2. If the two goods that I choose for my price line are edible oil and bread and if there is a rumor in the market that edible oils are adulterated shall I still purchase more of it at lower prices? These arguments can be brushed inside the carpet by another powerful shield of economics that is calling them as exceptional cases, but the reality is that in our real practical life we don't have the shields of assumptions and exceptions. We have to face the world right as it is. Assumptions and assumptions based on assumption to prove our theories right makes economics an Assumptive Science, but a study loses its significance if it is just to be preached and not



practiced .For example, to prove that circum navigation of the earth is not possible I shall ask you to assume that the earth is not round but flat my absurd theory will be proved but what good on earth will such a theory serve. Similarly, for understanding the concept of budget line or price line it is essential to understand the theory of Consumer's Equilibrium and for the understanding of the price line we have to depend upon the concept of Indifference Curves. Indifference Curves', significance rests upon other assumptions and so on. Assumptions based upon assumptions erected the multistoried building of economic theories but it rests upon a weak foundation and that is assumption.

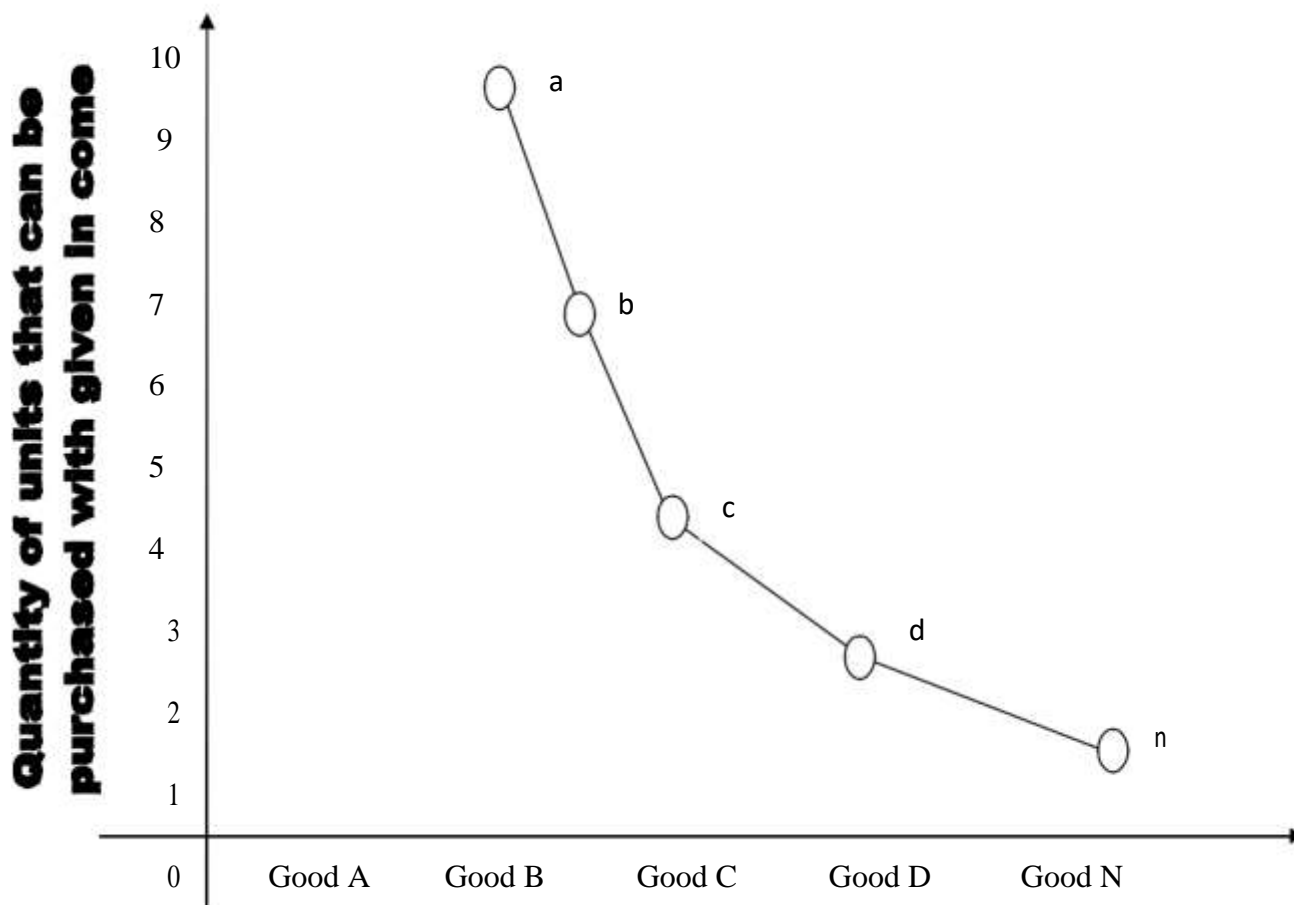
### **THE SHAPE OF PRACTICAL PRICE LINE:**

The price line that shows all those combinations of only two goods which the consumer can buy spending his given money income on the two goods at their given prices, holds good in case of a world of an assumption, but in real practical life we come across a situation when we have to make a choice or a series of choices over a range of goods. So, a new practical price line tends to be drawn, which will not necessarily be a straight sloping line touching the two axis .

The Practical Price Line is a line joining the loci of the points that we derive by dividing the income by the price per units of all the goods in consideration, by a consumer, if all the income of the consumer has to be spent on purchasing each one of those goods under consideration.

For example, if a consumer's income is Rs. 1000 and he has to spend his income on a variety of goods having different prices and if the said goods are arranged in ascending order of their prices per unit( that last good in the order will be the good whose price per unit is equal to the income and not more than it because a good with higher price per unit then the income of the consumer will be out of his reach. The quantities of goods that can be purchased with his given income will be according to the table below:

| <b>Goods upon which income is to be spent</b> | <b>Income</b> | <b>Price per unit (rs)</b> | <b>Quantity that can be purchased with given income</b> | <b>Point on practical Price line</b> |
|---|---------------|----------------------------|---|--------------------------------------|
| <b>Good A</b>                                 | <b>1000</b>   | <b>100/ Unit</b>           | <b>10 Units</b>   | <b>A</b>                             |
| <b>Good B</b>                                 | <b>1000</b>   | <b>200/ Unit</b>           | <b>5 Units</b>  | <b>B</b>                             |
| <b>Good C</b>                                 | <b>1000</b>   | <b>300/ Unit</b>           | <b>3.3 Units</b>  | <b>C</b>                             |
| <b>Good D</b>                                 | <b>1000</b>   | <b>400/ Unit</b>           | <b>2.5 Units</b>  | <b>D</b>                             |
| <b>:</b>                                      | <b>1000</b>   | <b>:</b>                   | <b>:</b>  | <b>:</b>                             |
| <b>Good N</b>                                 | <b>1000</b>   | <b>1000/ Unit</b>          | <b>1 Unit</b>   | <b>N</b>                             |



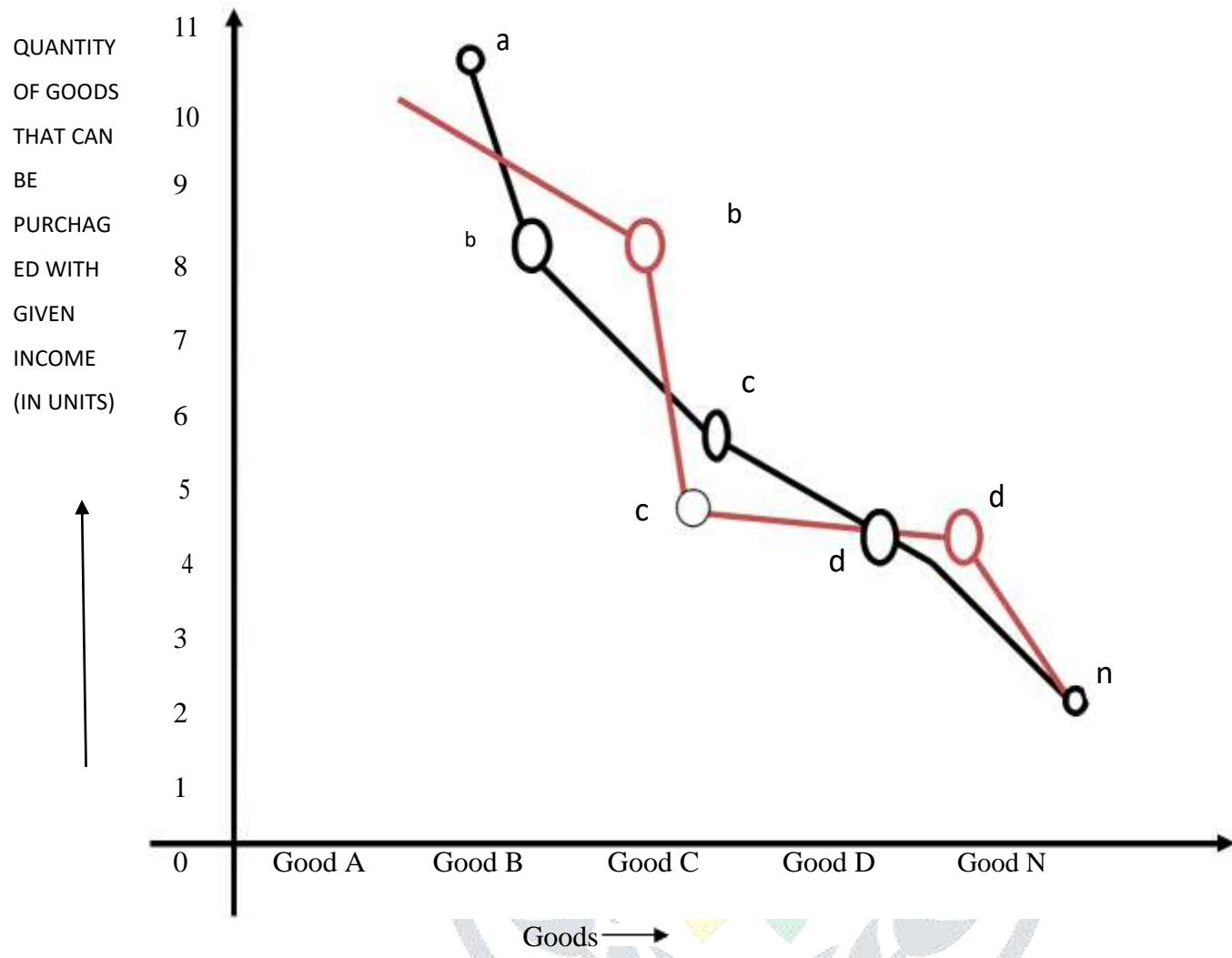
**FIG SHOWING PRATICAL PRICE LINE FOR VARIOUS GOODS**

**Case 1.** If the income of the consumer changes: If the income of the consumer increases, and the price of goods remain unchanged, then the practical price line will shift upwards towards the right. On the other hand, if the income of the consumer decreases and the prices of goods remain unchanged, then the price line will shift downwards, towards the left, indicating the lesser quantity of goods that can be affordable with his fallen income.\

**Case2.** If the prices of good/ goods changes:

If the price per unit of a good/ goods rises and income remains unchanged then the shape of the price line will change towards the left, down wards at the point of the concerned good whose price has risen.

On the other hand if the price/ prices per unit of a good/ goods falls, income remaining unchanged then the practical price line will buldge towards the right at the point/ points of the concerned goods whose prices have fallen.



**Fig: Showing Changed Shape Of Practical Price Line Due To Changes In Prices Income Remaining The Same**



| Goods upon which income is to be spent | Income | Price per unit (rs) | Quantity that can be purchased with given income | Point on practical Price line |
|--|--------|---------------------|--|-------------------------------|
| Good A                                 | 1000   | 120/ Unit           | 8.3 Units  | A'                            |
| Good B                                 | 1000   | 150/ Unit           | 6.6 Units  | B'                            |
| Good C                                 | 1000   | 350/ Unit           | 2.8 Units  | C'                            |
| Good D                                 | 1000   | 380/ Unit           | 2.6 Units  | D'                            |
| Good N                                 | 1000   | 1000/ Unit          | 1 Unit   | N'                            |

### Conclusion:

Thus, in this practical dynamic world when our needs, prices of goods and our incomes keep changing every now and then, the price line that we get will keep on moving up and down rising and falling with the prices of various goods falling and rising respectively like the innumerable waves of the sea.

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