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B.A.Part -1
Paper-2
Topic :- **Consumption Function**
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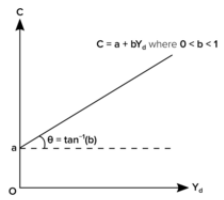
Consumption Function

In economics, the consumption function describes a relationship between consumption and disposable income. The concept is believed to have been introduced into macroeconomics by John Maynard Keynes in **1936**, who used it to develop the notion of a government spending multiplier.



C= a+b.Yd

Graphical representation of the consumption function, where a is **autonomous consumption** (affected by interest rates, consumer expectations, etc.), b is the **marginal propensity to consume** and Yd is **disposable income.**

Psychological Law of Consumption:

The Keynesian concept of consumption function stems from the fundamental psychological law of consumption which states that there is a common tendency for people to spend more on consumption when income increases, but not to the same extent as the rise in income because a part of the income is also saved. The community, as a rule, consumes as well as saves a larger amount with a rise in income.

Keynes' psychological law of consumption is based on the following propositions:

- When the total income of a community increases, the consumption expenditure of the community will also increase, but less proportionately.

- It follows from this that an increase in income is always bifurcated into spending and saving.

- An increase in income will, thus, lead to an increase in both consumption and savings. This means that with an increase in income in the community, we cannot normally expect a reduction in total consumption or a reduction in total savings. A rising income will often be accompanied by increased savings and a falling income by decreased savings. The rate of increase or decrease in savings will be greater in the initial stages of increase or decrease of income than in the later stages.

The gist of Keynes' law is that consumption mainly depends on income and that income recipients always do not tend to spend all of the increased income on consumption. This is the fundamental maxim upon which Keynes' concept of consumption function is based.

Further theories on the shape of the consumption function include James Duesenberry's (1949) **relative consumption hypothesis**, Franco Modigliani and Richard Brumberg's (1954) **life-cycle hypothesis,** and Milton Friedman's (1957) **permanent income hypothesis.**

Some new theoretical works following Duesenberry's and based in behavioral economics suggest that a number of behavioural principles can be taken as microeconomic foundations for a behaviorally-based aggregate consumption function.