
Original Research Article

Understanding the popularity of luxuries: The Veblen effect and consumer behavior

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Abstract: This study aims to investigate the reason for inverse relationship between price and demand of luxuries. We used both qualitative and quantitative analysis to understand the mechanism of basic reason -Veblen effect. We concluded four reasons: high quality of product, satisfaction of consumers' vanity, necessity for socialization, uniqueness of product. We also mentioned the notice points of this analysis in conclusion.

Keywords: Luxuries; Law of demand; Veblen good; Veblen effect

1. Introduction

The price of the goods has always been a key concern for consumers. The law of demand indicates that when other factors are constant, the higher the price, the lower the quantity demanded^[1]. This inverse relationship has been widely accepted and well-established as a fundamental principle of economics. It applies to a wide range of goods today to some extent. For example, when apples' price increases, our demand for apples will decrease. The sensitivity of quantity demanded to change in price might be different for different kinds of goods, but the inverse relationship between price and quantity demanded still holds.

However, there are notable exceptions to this rule. In our daily lives, there are some very expensive goods that are popular among consumers, and luxuries are very significant examples. Luxuries are even more popular when they are more expensive. This contradicts the standard downward-sloping demand curve. This study investigates the uncommon demand patterns observed in luxury markets through the synthesis of theoretical paradigms and empirical case studies. Specifically, it aims to elucidate the microeconomic mechanisms underpinning Veblen consumption and derive actionable implications for luxury industry strategists.

The luxury industry experienced a period of exceptional value creation. Over the past five years, this industry has overperformed the general market. However, when it comes to 2025, the growth significantly slows down. Consumers of luxury are becoming more diverse, and they focus more on the luxury experience rather than the luxury goods themselves.^[2]

Thorstein Veblen's^[3] concept of "conspicuous consumption" provides a foundational framework for understanding this trend. He stated that purchasing luxury goods is a signal of wealth and social status, rather than necessary needs. Subsequent scholars, Bagwell and Bernheim^[4] further examined the conditions where Veblen Effects arise from the desire to achieve social status by signaling wealth through conspicuous consumption and found that luxuries are sold at higher prices to consumers who want to show their wealth.

About the Veblen Effects, many scholars have their own research. Agrawal et al.^[5] conducted a mathematical model to quantitatively perform the sensitivity analysis and obtain the optimal price for Veblen products. Satheeshkumar et al.^[6] conducted a case study on Apple iPhone, analyzing the reason of the demand curve of iPhone when its price is very expensive, and stated that customers of Apple iPhone measure the satisfaction not by the utility value, but by the social status and value.

Moreover, in more recent studies, Zhu^[7] and Liu^[8] both deeply analyzed the reason for the consumption of Veblen goods and the impact of this type of consumption. Furthermore, they both critically assess conspicuous

consumption, and Liu also suggest consumers develop healthy consumption habit.

2. Methodology

To investigate the unique demand patterns of luxury goods and the underlying mechanisms of the Veblen effect, this study adopts a comprehensive approach that combines theoretical analysis with empirical observations. The methodology is designed to provide a nuanced understanding of consumer behavior in the luxury market.

The theoretical foundation of this study is rooted in Veblen's^[3] concept of "conspicuous consumption", which posits that luxury goods serve as signals of wealth and social status. This phenomenon obviously does not follow the law of demand. In other words, when the price goes up, the quantity demanded for these goods also goes up. They are called Veblen goods.

This kind of goods usually includes fancy cars, jewelry, and other luxury items. It can be clearly seen that there exists a positive relationship between price and quantity demanded which violates the law of demand^[9]. And the consumption of luxuries is very common in our daily lives, therefore it is worth analyzing the cause of this phenomenon.

This study examines several well-known luxury brands to understand how their pricing strategies and brand positioning influence consumer perceptions and demand. These case studies provide rich insights into the role of conspicuous consumption and social signaling in the luxury market. To further explore the mechanisms behind the Veblen effect, this study also incorporates both qualitative and quantitative methods to provide a comprehensive analysis. The data was collected through a survey of consumers who had purchased luxury goods in the past two years. The survey aimed to measure consumers' perceptions of luxury goods, their willingness to pay higher prices, the driving factor for the purchase, and the extent to which they associate luxury purchases with social status and daily demand. The survey results were analyzed using statistical methods to identify patterns and correlations between price sensitivity, brand loyalty, and social signaling.

In addition, this study analyzed historical sales data to observe the relationship between price changes and sales volumes. This empirical analysis revealed that, consistent with the Veblen effect, higher prices were often associated with increased sales, particularly for high-end luxury brands. This finding underscores the importance of exclusivity and social signaling in the luxury market, as consumers are willing to pay a premium for goods that convey a sense of status and prestige.

3. Analysis

Before analyzing the cause, we should first figure out what characteristics make Veblen goods different from goods that follow the law of demand. A Veblen good is normally a luxury product, which is commonly exclusive and a status symbol. In addition to its outstanding quality, having a luxury product is a symbol of wealth and power in the present society. Furthermore, Veblen goods can increase the fame of a person. All these intangible benefits make Veblen goods different from other goods. For example, a pair of Air Jordan basketball shoes might make other people think that you are fashionable, even the price of the shoes might be ten times as expensive as a pair of normal brand good-quality basketball shoes.

As for the cause of this phenomenon, firstly, price is usually a criterion to measure the quality of goods. For many consumers, higher-priced products are perceived as higher quality, even if this is not always true. Veblen goods usually have the highest price compared to other goods in the same category, therefore in some consumers' minds, Veblen goods have the highest quality, which will increase the utility or benefit of the goods. Veblen goods sometimes truly have higher quality than other goods to some extent. For example, Rolls-Royce has wonderful ride comfortableness compared to cars like Toyota or Volkswagen. It is understandable that people are willing to spend more money on better-quality goods, and it is a cause for this phenomenon.

Secondly, Veblen goods can satisfy the vanity of some consumers. In the market, due to income constraints, affluent people are a major part of consumers of Veblen goods. For these people, they can obtain a high level of material life easily, hence they are more than willing to purchase Veblen goods to obtain their additional utility. Due to its exclusive nature, by purchasing a luxury item, they can show off to others and hence be envied by others, which will make them happy and satisfy their vanity. For example, driving a Lamborghini to a party might get attention from everyone. To some extent, it is much more important than the quality of the good itself, which makes them willing to pay a premium on the utility of the good. The higher the price, the better the vanity is satisfied, which makes them more willing to purchase this Veblen good. In contrast, if the price declines, the exclusivity of the good decreases and reduces their willingness of purchasing the goods.

In addition, Veblen goods are sometimes necessary for socialization. As mentioned before, Veblen goods are mainly sought after by affluent people. For this group of people, they might need to attend many fancy business lunches and high-end parties for work demands. Veblen goods are necessary to participate in this kind of socialization to some extent, such as an Armani suit or a Chanel handbag. In this situation, Veblen good is a kind of tool or a 'threshold' to integrate into the group, which is necessary and important for affluent people. The price of the good, at this time, can show the level of 'threshold'. The higher the price, the higher the 'threshold', which is attractive to affluent people.

At last, uniqueness is also a contributing factor to the purchasing of Veblen goods. The quantity supplied of Veblen goods is usually small, and they also have limited edition items, which makes it much more difficult to purchase them. It is common that we are more willing to purchase a unique product that others are not able to buy, which is also a symbol of status, wealth, and power. In reality, the price often has a positive relationship with uniqueness. In other words, a good with a higher price is usually more unique. It is the reason for the phenomenon that when the price increases, the demand also increases.

4. Conclusion

The preceding analysis has identified four key factors contributing to the popularity of luxury goods. However, we should also notice that though Veblen good has some special characteristics which result in the positive relationship between its price and demand, different from the demand law, there are also some common characteristics for Veblen goods. Specifically, the substitution effect still exists for Veblen goods, implying that an increase in price should, in theory, lead to a decrease in demand. Nevertheless, in the case of Veblen goods, other factors such as social signaling, exclusivity, and the perception of quality often overshadow the substitution effect, thereby leading to the observed positive relationship between price and demand.

Furthermore, it is important to consider the differential impact of price changes on various consumer segments. For average consumers, a reduction in the price of Veblen goods might result in a marginal increase in demand. However, it is essential to note that even at reduced prices, these goods remain largely unaffordable for the majority. For instance, a Lamborghini, even at half of its original price, is still beyond the reach of most consumers. This led to the growth of demand among these people being negligible. The primary consumers of Veblen goods are typically affluent individuals, who care about different factors of consumption compared to average consumers. For affluent buyers, a decrease in the price of Veblen goods will lead to a significant decrease in demand. This is because the exclusivity and prestige associated with high prices are diminished when their cost becomes more accessible as mentioned above, thereby reducing their allure. The decline in demand among affluent consumers is significantly more effective than the marginal increase in demand among average consumers.

It is also vital to emphasize that the analysis of Veblen goods is only applicable within a reasonable range of price fluctuations. In other words, the quantity demanded cannot rise infinitely when price increases. Affluent people's wealth is also limited. If the price exceeds the threshold that even the majority of affluent people found

the price prohibitive, the demand will definitely decrease.

In conclusion, while the analysis has shed light on several key characteristics of Veblen goods, there remain many aspects that are worth further investigation. Future research in this area could provide valuable insights for luxury industries seeking to refine their strategies and for policymakers aiming to guide consumption behavior effectively.

About the author

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