How Much Rationality Does the Model Assume?

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<u>How much rationality do we assume in the model</u>
of slack:

- Households maximize utility subject to
budget constraint → households <u>do the best they</u>
can given their income / wealth.

- Households take as given & therefore
anticipate the price of services → prices
<u>follow price norms</u> that are by definition
understood & followed by everybody

- Households take as given market tightness
& therefore anticipate correct market
tightness → <u>a lot of rationality required w/</u>
heterogeneous agents → can introduce statistical
agency instead-

⌐ If government announces <u>tightness x,</u>
and households max. utility given x,
then x will be realized

→ | statistical agency
   government provides <u>correct forecast</u>
   (which is their objective)

⌐→ households do best they can b/c they use correct x.