Lecture 6:
Consumer Behavior

- Utility
- Diminishing Marginal Utility
- Indifference Curve
- Budget Line

Ref:
1. Economics (8e), Roger A. Arnold

Utility

- A measure of the satisfaction, happiness, or benefit that results from the consumption of a good.

<u>Total Utility</u>:

The total satisfaction a person receives from consuming a particular quantity of a good.

<u>Marginal Utility</u>:

The additional utility a person receives from consuming an additional unit of a particular good.

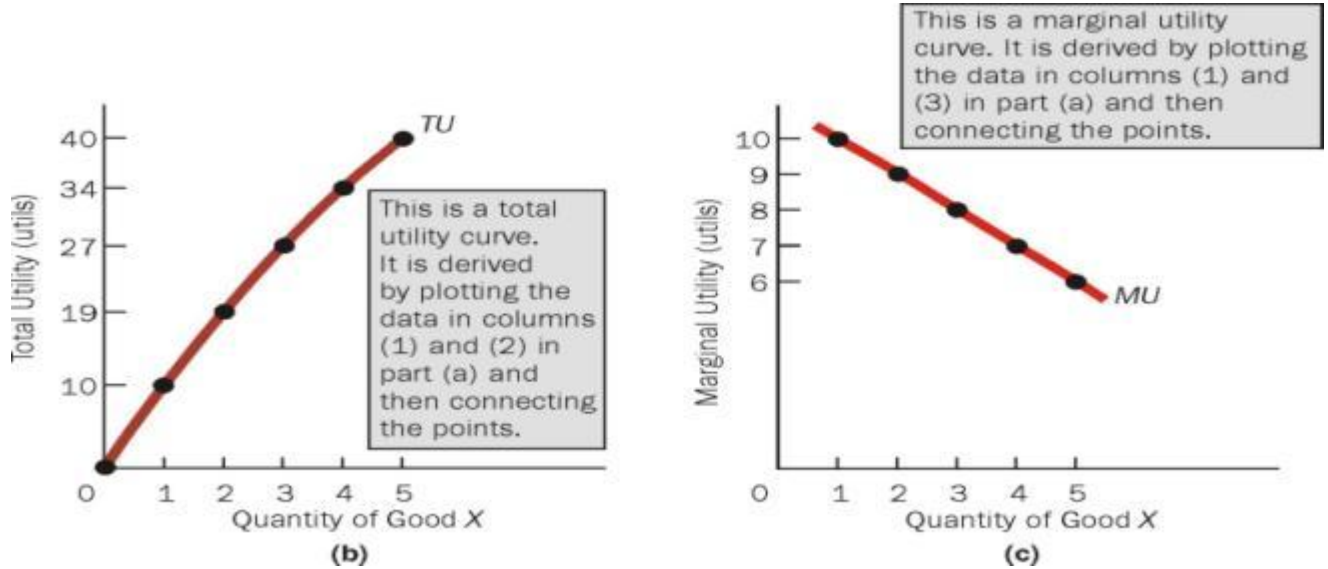
<u>Law of Diminishing Marginal Utility</u>:

- The marginal utility gained by consuming equal successive units of a good will decline as the amount consumed increases.

Total Utility, Marginal Utility, and the Law of Diminishing Utility

(1) Units of Good X	(2) Total Utility (utils)	(3) Marginal Utility (utils)
0	0	—
1	10	10
2	19	9
3	27	8
4	34	7
5	40	6

(a)

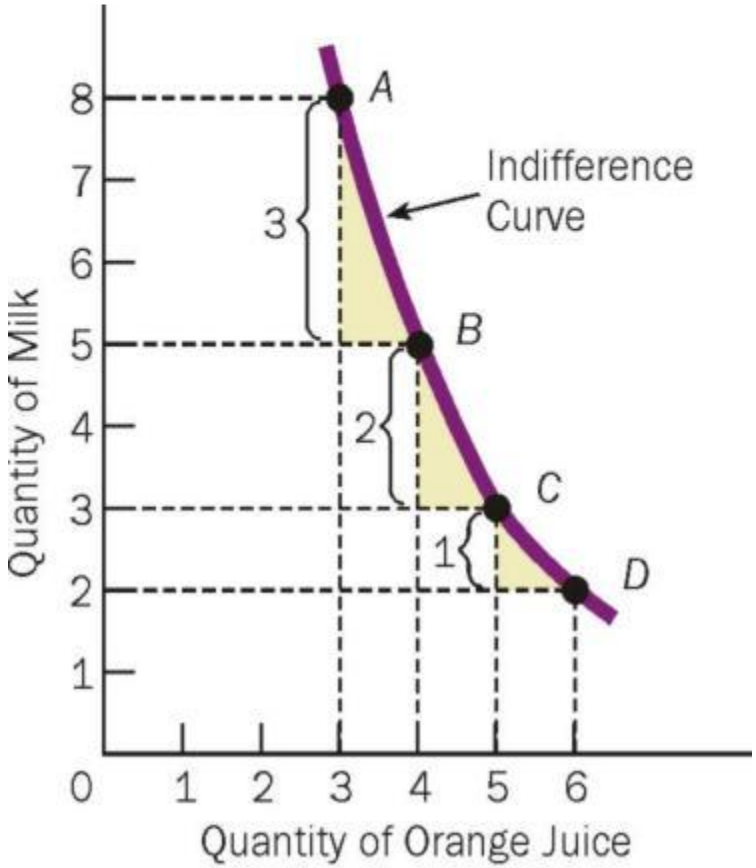


An Indifference Set and an Indifference Curve

An Indifference Set

Bundle	Milk (units)	Orange Juice (units)
A	8	3
B	5	4
C	3	5
D	2	6

(a)



(b)

Characteristics of Indifference Curves

1. Indifference curves are downward-sloping (from left to right)

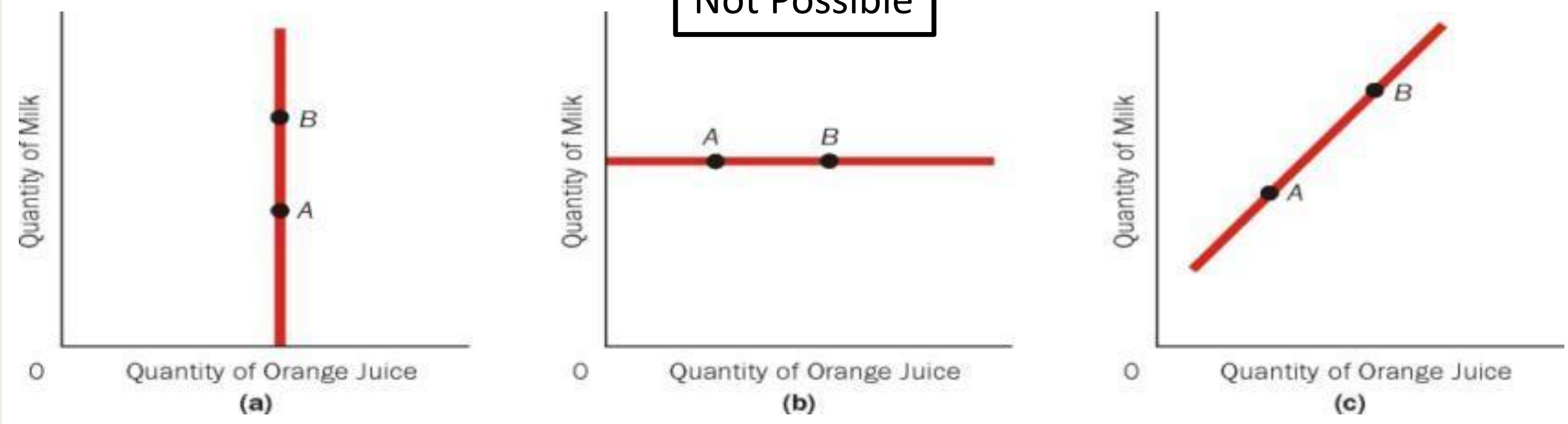
2. Indifference curves are convex to the origin

3. Indifference curves that are farther from the origin are preferable because they represent larger bundles of goods

4. Indifference curves do not cross (intersect)

Indifference curves are downward-sloping

Not Possible

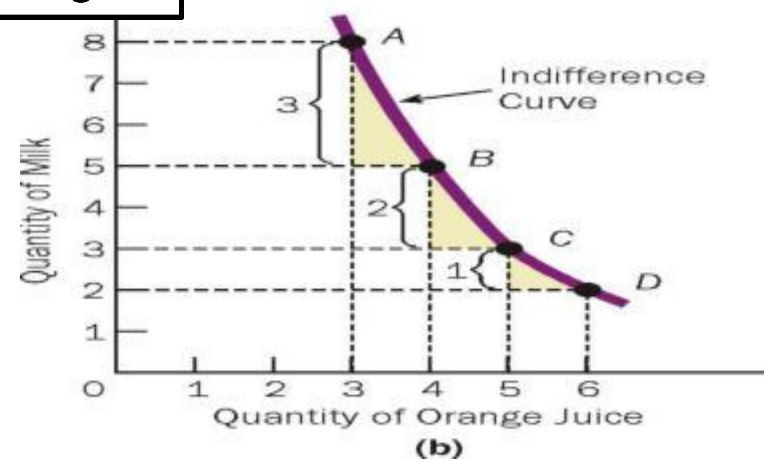


Possible and Logical

An Indifference Set

Bundle	Milk (units)	Orange Juice (units)
A	8	3
B	5	4
C	3	5
D	2	6

(a)



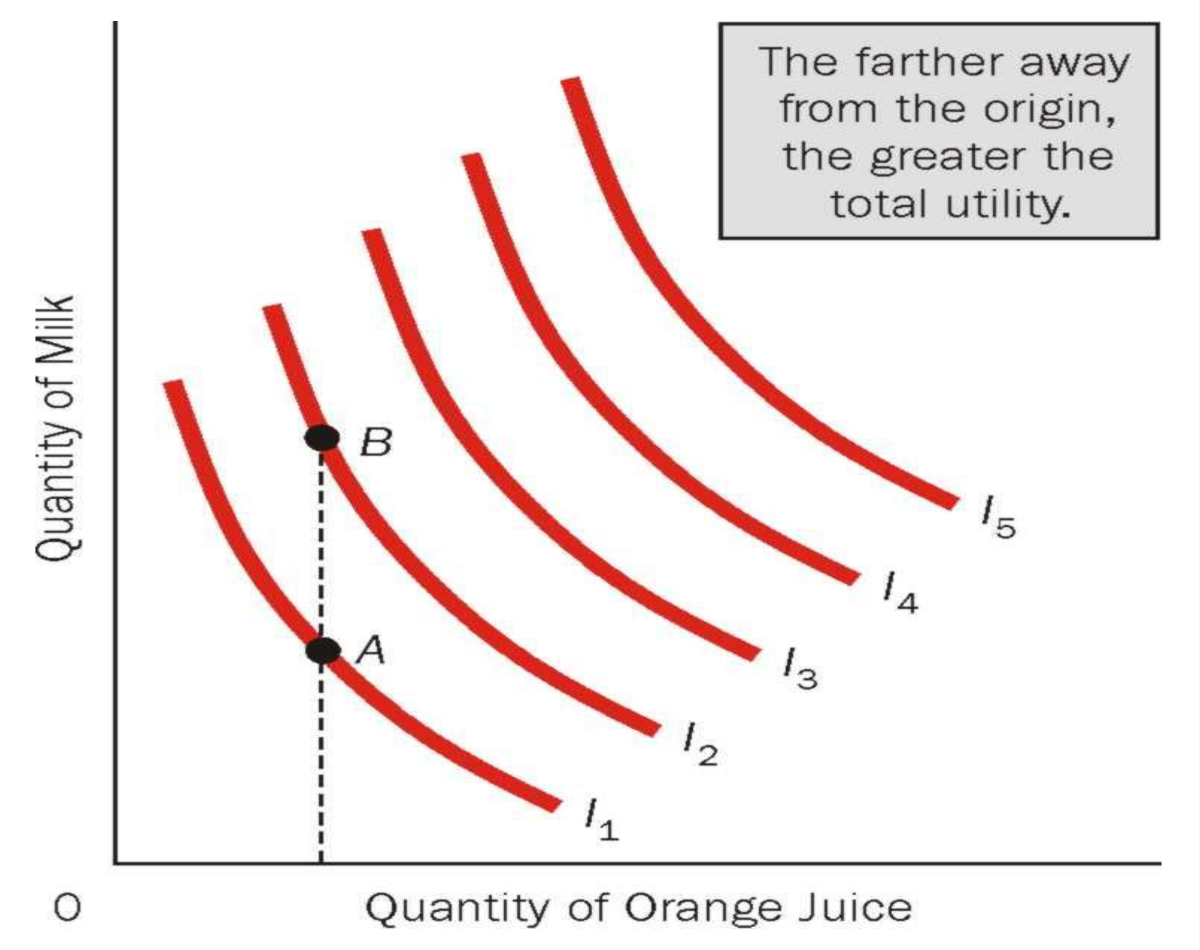
Indifference curves are convex to the origin

- The more of one good that an individual has, the more units he or she will give up to get an additional unit of another good; the less of one good that an individual has, the fewer units he or she will give up to get an additional unit of another good.

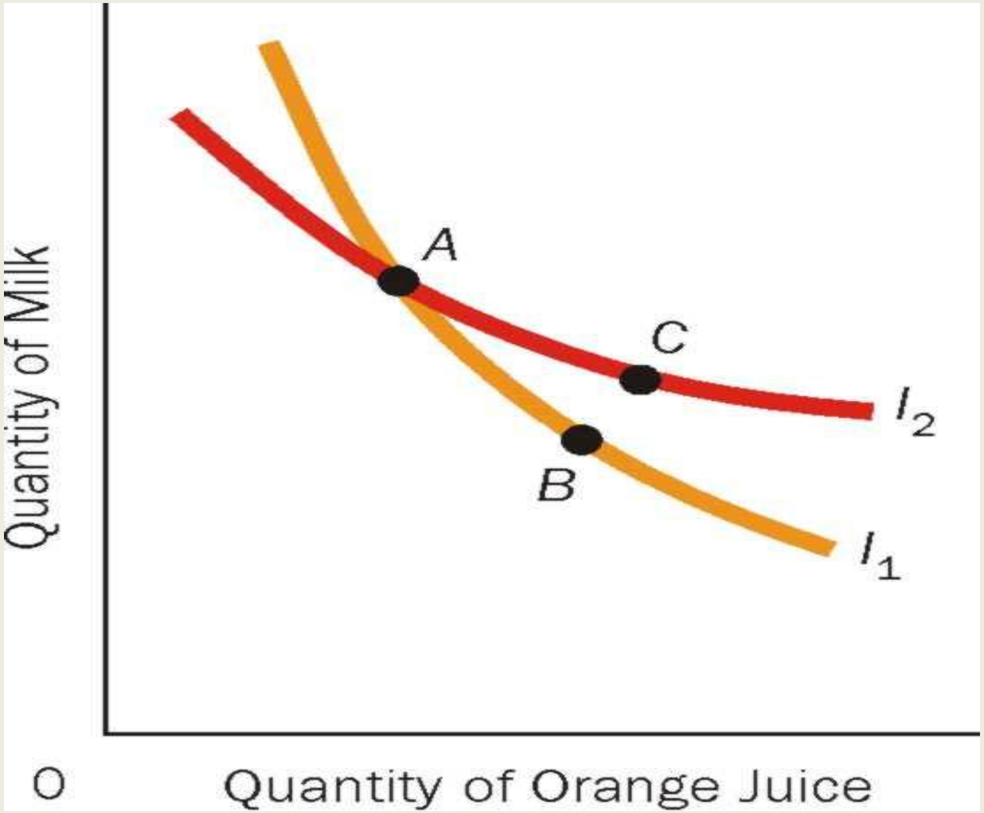
- Marginal Rate of Substitution:

The amount of one good an individual is willing to give up to obtain an additional unit of another good and maintain equal total utility.

Indifference curves that are farther from the origin are preferable because they represent larger bundles of goods



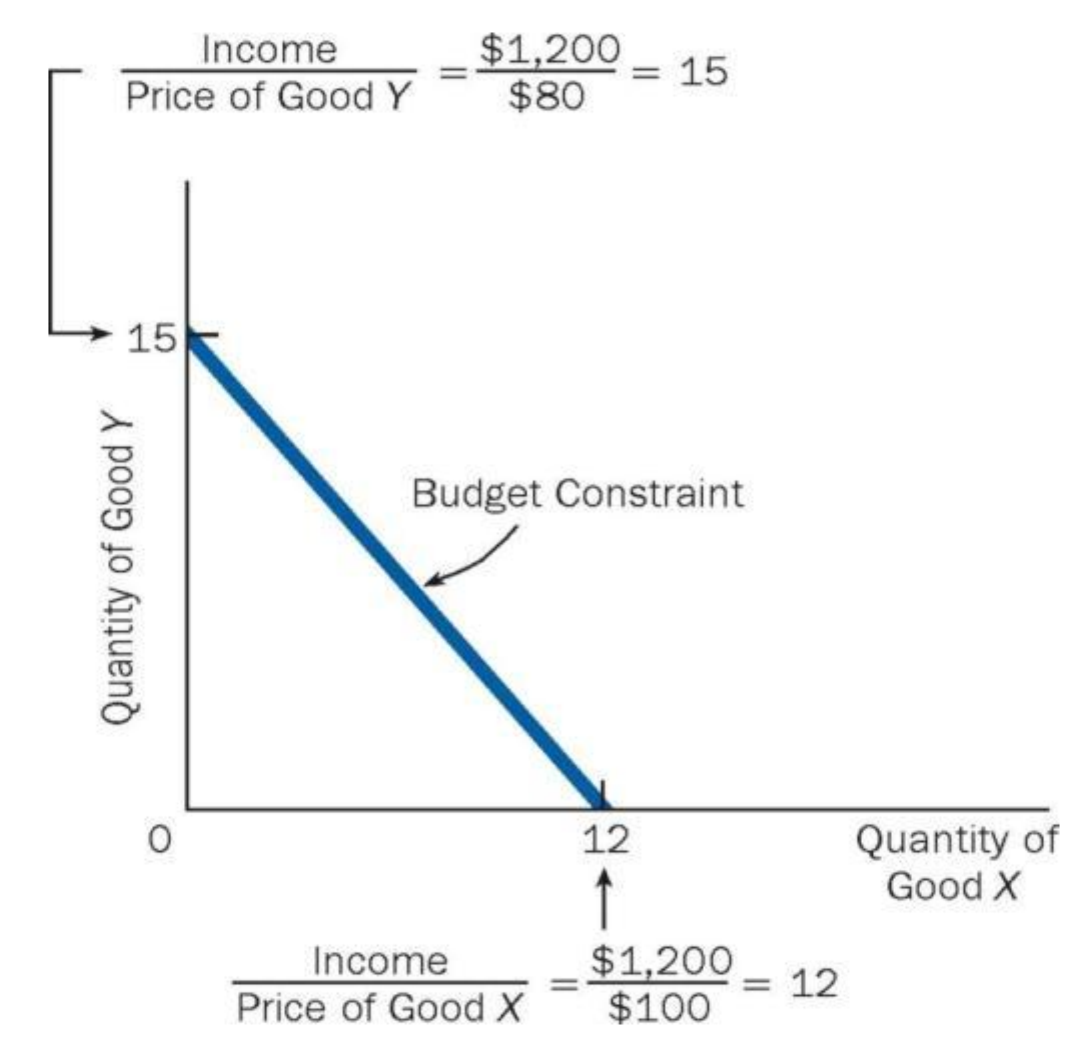
Indifference curves do not cross (intersect)



Crossing Indifference Curves are inconsistent with Transitive Preferences

The Budget Constraint

All the combinations or bundles of two goods a person can purchase given a certain money income and prices for the two goods



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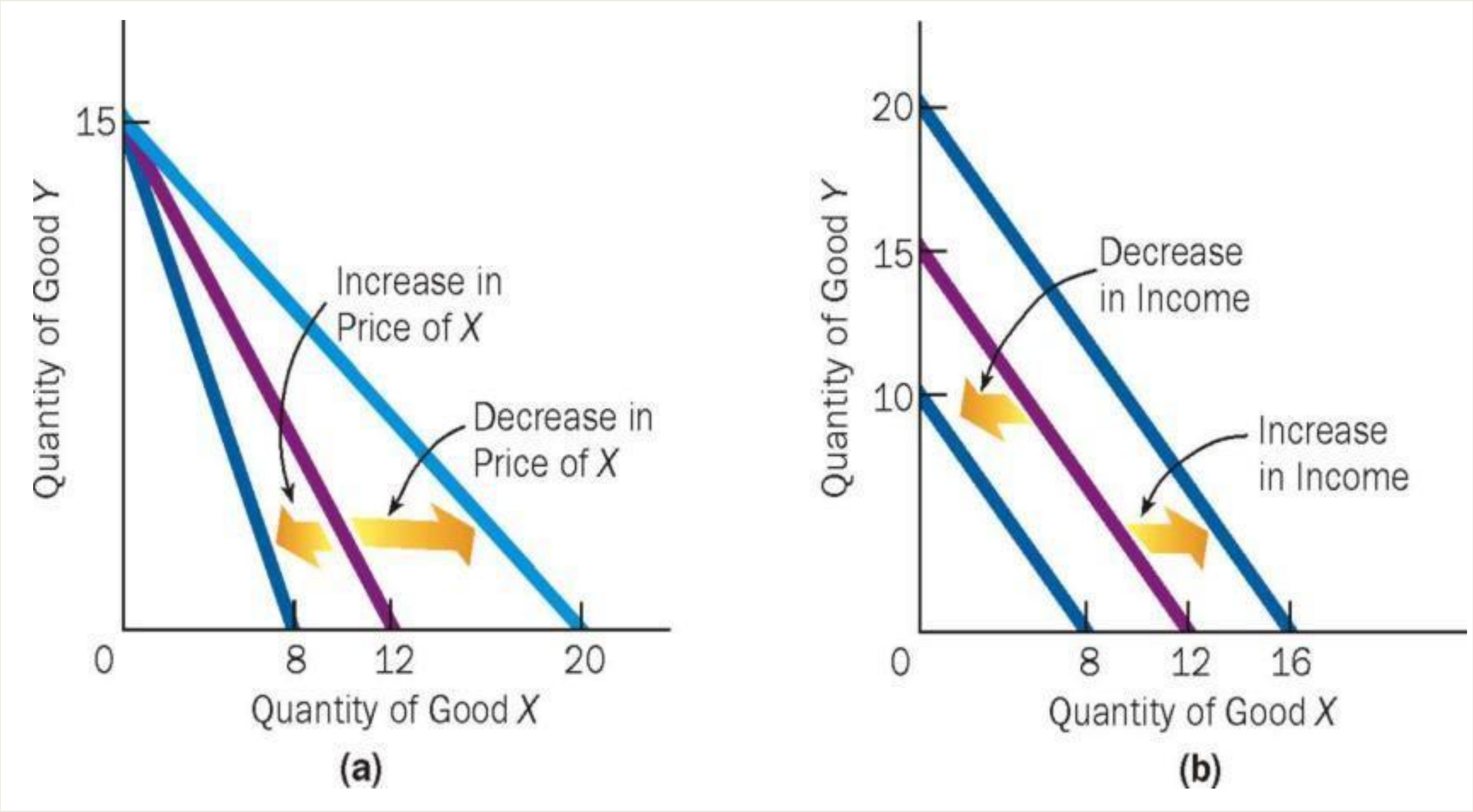
Changes in the Budget Constraint



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Consumer Equilibrium