

CH 3 - Preference

Luke Lu • 2026-02-09

Consumer Preference Model

Info – Consumer Preference Model

- Model of what and how much consumers purchase
- Model of a choice between alternative

Effect on the model

- Price
- Preference
 - Weak axiom of revealed preference: if choosing between A, B , if one of the two becomes unavailable. The remaining choice must contain A to remain a rational choice.
- Income/Budget

Info – Budget

1. Equation

- M = income
- p_i = price for product i
- q_i = quantity for product i

$$M = p_1 q_1 + p_2 q_2$$

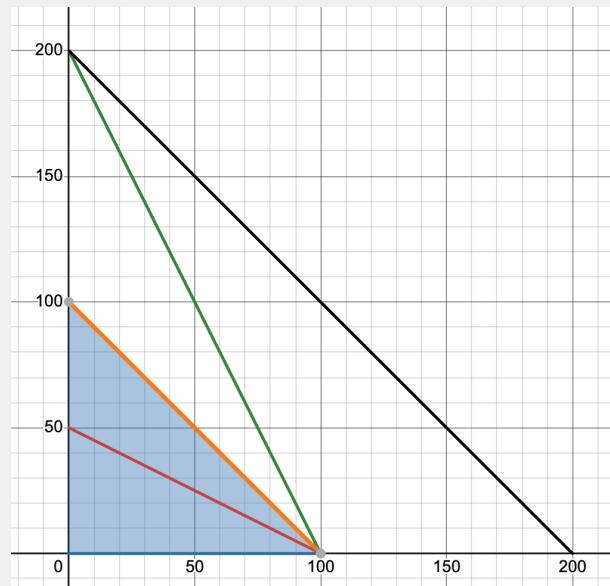
→ M is the amount of money allocated for this specific decision

Note that the goal is to gain the most amount of happiness from the given budget.

Example allocation:

- Salary
 - ▶ Spending
 - Shopping
 - ▶ Saving

2. Graph



Area below the curve is the Inefficient distribution of budget.

On the line suggests the optimal distribution of budget.

The slope $\frac{p_2}{p_1}$: good 2 costs $\frac{p_2}{p_1}$ good 1 ⇒ opportunity costs

Orange: original line

Green: p_2 decreases

Red: p_2 increases

Black: M increases

 **Info – Preferences**

Preference often/always intangible and non-numeric.

Force intangible to have inherent structure like numbers

“Happiness” ~ “Utility”

An assumption is that of diminishing marginal utility, but still positive