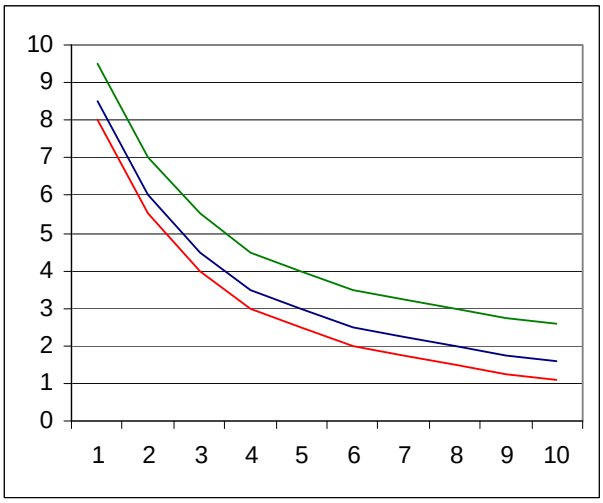
Consumer Evaluation
Indifference Curves
Utility

See the IndifferenceCurves.ppt notes



The original goal was to find a way to express consumer preferences in an ordinal manner—that is, without relying on arbitrary measurements. Utility theory basically requires only that consumers be able to compare bundles of products. Any bundle that contains more of at least one good (and no less of any others) must be preferred. (Otherwise the product becomes a "bad.")

The slope of an indifference curve indicates the rate at which a consumer will trade one product for another: Give up how many units of good Y to gain one of good X.

Indifference curves combined with prices can be used to generate demand curves. So, from a few basic rules about preferences, we can show that demand curves are downward sloping.

Lab Assignment:

1. With paper and pen, show how indifference curves lead to a demand curve. Number each step of your analysis.
2. Show how a change in price leads to an income and substitution effect.
3. Within your team, choose two products and have each person identify the tradeoff/indifference curve for at least three points. Plot the curves separately.
4. If each member of the team was given a fixed bundle of the two products (say 5 units each), would there be an opportunity to trade them with each other so that some people can gain utility without causing others to lose utility?