

Review Notes – Consumer Budget Constraints

- What does a consumer know?
 - Observes a large number (N) of goods that he could buy.
 - Each good has a price.
 - The consumer has a limited income.
 - He chooses an allocation of goods for each of the N goods.
 - The simple two good model
 - Budget constraint
 - $p_1X_1 + p_2X_2 \leq M$
 - meaning? graphically?
 - Budget Line
 - $p_1X_1 + p_2X_2 = M$
 - meaning? graphically?
 - intercepts of the BL?
 - opportunity cost of the two goods?
 - Slope of the budget line
 - How do we know what the slope equals?
 - The budget line in slope intercept form
 - Algebraically
 - Shifts in the budget line
 - Changes in prices
 - Changes in income
 - What does the budget line look like with:
 - Taxes
 - Subsidies
 - Rationing
 - A black market
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