Chapter 2

Demand : Thinking like a Buyer

Perfect Competition := so many buyers & sellers s.t. no individual buyer or seller can influence the price of a product

rational rule : buy until price = MB ≡ MU

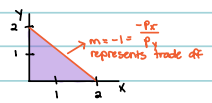
utility := the level of satisfaction a consumer derives from consuming a good | service

marginal utility = $\frac{\text{change in total utility}}{\text{change in quantity}} = \frac{\Delta TU}{\Delta Q}$

Law of Diminishing Marginal Utility (LDMU) := marginal utility ↓ as quantity consumed ↑

maximizing utility := a consumer maximizes utility by equalizing marginal utility per dollar across all goods and spending their entire income

Opportunity Set := all possible combinations of goods a consumer can afford



Budget Line : = all possible combinations of goods that exhaust a consumer's budget

↳ $P_x X + P_y Y = I$

$P_y Y = I - P_x X$

$Y = \frac{-P_x}{P_y}(X) + \frac{I}{P_y}$

demand curve = marginal benefit curve = willingness to pay curve

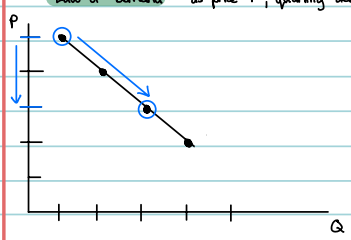
↳ downward sloping due to diminishing marginal utility

Demand := a relationship between the price of a good & the quantity of a good a buyer is willing & able to buy

Quantity Demanded := the amount of a good a consumer buys at a certain price

Demand Schedule := table of price & associated QD according to demand

Law of Demand := as price ↑, quantity demanded ↓



P	QD
1	5
2	4
3	3
4	2

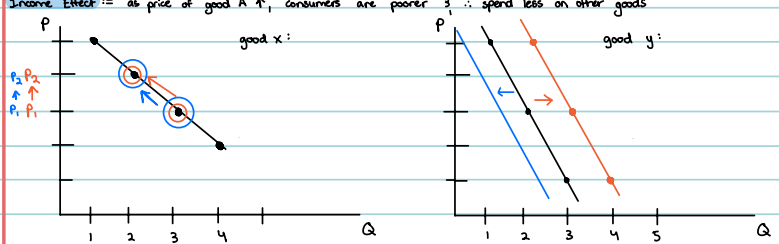
demand function : $Q_d = a - bP$

inverse demand : $bP = a - Qd$

$P = \frac{a}{b} - \frac{1}{b}(Qd)$

Substitution Effect := as price of good A ↑, consumers buy more of substitute good B

Income Effect := as price of good A ↑, consumers are poorer & ∴ spend less on other goods



- wealth : Normal vs Inferior
- preferences
- expectations