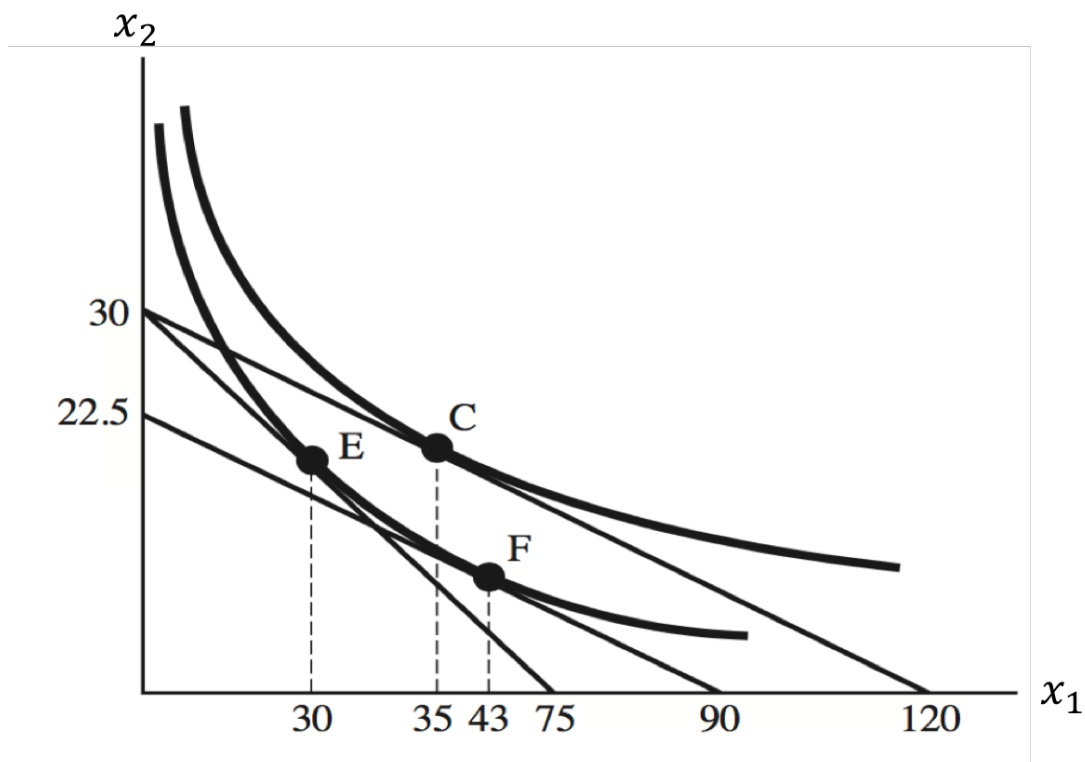


ECON203 Microeconomic Analysis (Session 2, 2018)

Tutorial 2

N.B This is economics – diagrams are always your friend ©

1. Consider the following budget and preference representation for an agent:



The agent has an income of 300, the price of good 1 is 4 and the price of good 2 is 10.

- How much of good 1 does this agent consume?
- If the price of good 1 falls to \$2.50, while income and the price of good 2 stay constant, how much of good 1 will the agent consume?
- How much income must be taken away from this agent to isolate the Hicksian income and substitution effects?
- The total price effect of the price change is to change consumption from the point [] to the point []? (fill in the blanks with the correct answers).
- The income effect corresponds to the movement from the point [] to the point

[] while the substitution effect corresponds to the movement from the point [] to the point [].

(f) Is good 1 a normal good or an inferior good?

2. In completely legitimate and totally non-stalkerish ways, you have been able to compile the following information about a sequence of choices by an agent named Martin:

	x_1	x_2	P_1	P_2
Week 1	12	24	2	1
Week 2	16	32	1	1
Week 3	12	24	1	1

- a) Show Martin's budget constraints for each of the 3 weeks, and indicative indifference curves.
- b) What can you deduce about Martin's preferences? Why?
- c) Indicate the income and substitution effects of the price change for good 1. Explain any surprising results.

3. Feng has this utility function over consumption and leisure: $U = C^3L$. His friend Ha-eun has this utility function: $U = CL^3$. The price of the consumption good is 1, and the hourly wage for working is 4. Neither Feng nor Ha-eun have any non-labour income.

Find Feng's and Ha-eun's weekly income.

[Hints: a week has 7 days of 24 hours each; every hour of leisure means 1 hour not worked; given the price of consumption, income and total consumption have the same value.]