

Semester: 1/2011
EE 311 Microeconomic Theory
Exercise No. 3: Consumption equilibrium and Applications

1. Assume that you spend 200 Baht each week on movies. There are only two theaters in town: Comedy Theater and Action Theater. A ticket at Action Theater costs 50 Baht each and at Comedy Theater 40 Baht each.
 Show what happens to your budget line under the following (separate) conditions:
 - (a) The government wants to reduce the number of visits to Action Theater and imposes a specific tax of T Baht per ticket.
 - (b) You receive a free ticket to Action Theater.
 - (c) Action Theater offers a special promotion: if you buy two tickets, you get additional tickets at half price, for only the first two tickets.
 - (d) Comedy Theater offers a promotion: if you buy two tickets, you get the third one free, for only the first two tickets.
 - (e) Suppose that you now develop an intense dislike for action movies. Draw your new indifference curves on your diagram in (d) above.

2. Joy is shopping for a new computer. She hears that the Pineapple computer is technologically superior to the IBN computer. However, she asks her friends and it turns out they all have IBN machines which are not compatible with Pineapple. They agree that the Pineapple is better, but they add that at the local software store, the software section for Pineapple seems to be getting smaller and smaller. Based on what she observes, Joy buys a IBN machine. Can you explain her decision?

3. True or False? Explain.
 - (a) "If the consumer is better off, the expenditure index exceeds the Laspeyres price index."
 - (b) "If the Paasche quantity index is less than 1, welfare has declined."

4. Given the following information:

	Good X			Good Y	
	Price	Quantity		Price	Quantity
2009	1	5		2	4
2011	2	6		3	3

Calculate the Laspeyres and Paasche price and quantity indexes as well as the expenditure index. Can you draw inferences about consumer welfare from these indexes? Explain. Do you notice anything unusual about the values you obtained?