Consumer Choice

How a consumer allocates a limited budget.

Economics

Utility is maximised when marginal utility per unit of money is equal across all goods.

$$MUx / Px = MUy / Py$$

MU/P higher for X — **Buy more X**

Reallocate.

Equal ratios — **Optimum reached**

Price of X falls — **Buy more X**

Ratio changed.

THE COMMON MISTAKE

× Buying whatever has the highest total utility

✓ Comparing marginal utility per pound

Total utility ignores price and how much you already have. The decision is always about the next unit.

> Diminishing marginal utility is why the tenth cup of coffee is worth less than the first, and why demand curves slope down.