

14.121
Fall 2001

Professor F. M. Fisher

Microeconomic Theory I
Outline and Reading List

The central topic of this course is the theory of individual choice, i.e., the theory of the firm and the theory of the household. These theories provide the underpinning for supply and demand curves, and the course will also consider competitive market equilibrium and the theory of monopoly. (Treatment of other forms of market organization is postponed until 14.122).

Note on Schedule: As a rule, lectures will be given on Mondays and Wednesdays, with recitation sections on Fridays. However, this will not always be true. In particular, there will be a lecture on Friday, September 6th unless otherwise announced.

Readings marked with a # are obtainable from Graphic Arts. Readings marked with an asterisk are optional, but you should read at least some of them. Readings marked with a double asterisk give a rather different perspective.

The book entitled, Did Microsoft Hurt Consumers? is on reserve at Dewey Library.

Texts: # F.M. Fisher, Lectures in Microeconomics.

Plus one of the following alternatives:

- a. H. Varian, Microeconomic Analysis (3rd edition)
(New York: Norton, 1992) (A list of errors is in the reading packet).
- b. D. Kreps, A Course in Microeconomic Theory
(Princeton: Princeton University Press, 1990)

Here are the issues:

1) The course runs at a level often higher than my "Lectures", so some other text is desirable.

2) In years past I have assigned Kreps because I thought it easier to read and better on explanations than Varian. But student comments very often say Kreps is too chatty and ask for Varian.

3) Varian is a good book. But it's more formal and closely written than Kreps and hence less insightful. It's also harder for the less mathematically trained.

- 4) Probably the best rigorous text is the Green, Mas-Colell & Whinston, Microeconomic Theory (assigned as optional reading and available on reserve at Dewey Library). But I think students who are not used to fairly sophisticated mathematical argument (which does not necessarily mean advanced mathematics) applied to economics are likely to find this book hard going. Further, the order of topics is quite different

from that of the course. So pick one of Varian and Kreps. You do not need to do the readings in more than one text. Pick the text according to where you think you stand in terms of mathematical comfort. The course follows neither of them really closely. If you can follow Green, Mas-Colell & Whinston you need not do the Varian or Kreps readings.

(Note that Green, Mas-Colell & Whinston is the text for later course in the micro sequence.)

O. Preliminaries: Homogeneous Functions; Constrained Optimization.

Fisher Lectures, pp. 3-6.
Varian, Section 26.8, ch. 27
or
Kreps, Appendix one.

I. Theory of the Firm:

Fisher, Lectures, Ch. III, pp. 25-44.
Varian, chs. 1-6
or
Kreps, ch. 7 and **chs. 19-20.

Fisher Notes on elasticity of substitution.

*Green, J., A. Mas-Colell and M. Whinston, Microeconomic Theory (on reserve), ch. 6.

*Malinvaud, E., Lectures in Microeconomic Theory, Ch. 1, 3.

*McFadden, D., "Cost, Revenue, and Profit Functions," in M. Fuss and D. McFadden (eds.) Production Economics: A Dual Approach to Theory and Applications.

**Nelson, R. and S. Winter, An Evolutionary Theory of Economic Change, Ch. 3-5.

**Williamson, Oliver E., The Economic Institutions of Capitalism MacMillan, 1985.

II. Competition and Monopoly.

Fisher, Lectures, Ch. IV, pp. 44A-56.
Varian, chs. 13-14
or
Kreps, ch. 8, pp. 263-83; ch. 9.

Fisher, "Diagnosing Monopoly," Quarterly Review of Economics and Business, vol. 19, (Summer 1979), pp. 7-33 (reprinted as ch. 1 of Fisher, Industrial Organization, Economics, and the Law, Hemel Hempstead: Harvester Wheatsheaf and Cambridge: MIT Press, 1990).

Evans, D. F.M. Fisher, D. Rubinfeld and R. Schmalensee, Did Microsoft Hurt Consumers?, American Enterprise Institute/Brookings Institution, 2000.

*R. L. Bishop, "The Effects of Specific and ad Valorem Taxes," Quarterly Journal of Economics, May 1968.

III. Consumer Theory

1. Preferences and utility: consumer sovereignty and rationality; axioms on preferences; representation of preferences by a utility function.
2. Utility maximization and demand: the budget constraint; utility maximization; demand functions geometry, examples.
3. Indirect utility and expenditure functions: definition and properties; duality; the Slutsky matrix; geometry of Hicksian and Marshallian demand; consumer surplus.
4. Theory of revealed preference: revealed preference axioms; empirical bounds on consumer surplus.
5. Introduction to Uncertainty Theory.
6. Separable preferences and two-stage budgeting: decomposition of the utility maximization problems; separability and homotheticity of preferences; Hicks aggregation; cost-of-living indices and empirical demand analysis.

Fisher, Lectures, Chapters I, II.

Varian, Chs. 7-10, 11 (lightly)

or

Kreps, Chapter 2.

Fisher Notes on existence and continuity of utility functions.

*Green, Mas-Colell & Whinston, chs. 1-5, 7 (lightly).

*Deaton, A. and J. Muellbauer, Economics and Consumer Behavior, Cambridge University Press, 1980.

H. Houthakker, "The Present State of Consumption Theory," Econometrica, October 1961.

*P. Samuelson, Foundations of Economic Analysis, Cambridge, Harvard University Press, 1947, Chapter 5.

*G. Becker, "A Theory of the Allocation of Time," Economic Journal 75, 1965, pp. 493-517.

Part III continued

**K. Lancaster, "A New Approach to Consumer Theory," Journal of Political Economy 74, April 1966, pp. 132-57.

*C. Blackorby, D. Primont and R. Russell, Duality, Separability, and Functional Structure, (North-Holland, 1978). Introduction.

*H. Houthakker, "Additive Preferences," Econometrica, April, 1960.

- *R. Pollak, "Additive von Neumann-Morgenstern Utility Functions," *Econometrica*, July-October 1967.
- *M. Machina, "`Expected Utility,' Analysis Without the Independence Axiom," *Econometrica*, March 1982.
- *F. Fisher and K. Shell, *Economic Theory of Price Indices*, (New York: Academic Press, 1972), Essay I.
- *J. E. Triplett, "Hedonic Functions and Hedonic Indexes," (Bureau of Economic Analysis, Discussion Paper 3, May 1986).
- *H. Simon, "Theories of Decision-Making in Economics and Behavioral Science," *American Economic Review*, vol. XLIV, 3, June 1959.
- *M. Yaari, "Endogenous Changes in Tastes: A Philosophical Discussion," Hebrew University, 1976.
- **H. Leibenstein, "Bandwagon, Snob, and Veblen Effect in the Theory of Consumer Demand," *Quarterly Journal of Economics*, 64, May 1950, pp. 183-207.
- *C. Blackorby et al, "Homothetic Separability and Consumer Budgeting," *Econometrica* 38, No. 3 (May 1970), pp. 468-72.
- *C. Blackorby and P. R. Russell, "Indices and Subindices of the Cost of Living," *International Economic Review* 19, No. 1 (Feb 1978).
- *L. J. Lau, "on Exact Index Numbers," *Review of Economics and Statistics* 61, (1) February 1979, pp. 73-82.
- **A. Tversky and D. Kahneman, "The Forming of Decisions and the Psychology of Choice," *Science* 21 (30), January 1981, pp. 453-58.
- *H. A. Simon, "Rationality as Process and as Product of Thought," *American Economic Review*, Papers and Proceedings, (May 1978) pp. 1-14.