

## Indifference Curve Analysis:

### Definition of Key concepts

1. **Utility:** refers to the pleasure or satisfaction associated with having, using, or consuming goods and services. The utility inherent in a good derives from whatever qualities a good or services has that gives it want-satisfying capabilities.
2. **Cardinal ranking or measurement of utility:** refers to the notion that the intensity of satisfaction one gains from a consumption or use of a good can be represented by cardinal pattern whereby numerical values (such as 14, 84.9, or 115) are assigned to represent utility. In other words, utility can be measured like we measured numerically like heights and weights.
3. **Ordinal ranking or measurement of utility:** this approach does not require that consumers be able to measure utility in any specific units of measurement but does assume that consumers are able to rank their preferences for different combination (bundles) of the same goods. Ordinal refers simply to the ranking of preferences and nothing else.
4. **The Law of Diminishing Marginal Utility:** *Ceteris paribus*, the marginal utility (the incremental satisfaction that a consumer experience when consuming of a good or service is increased by one unit) derived from consuming a certain good diminishes when the quantity of that good consumed *per of time* increases.
5. **The Budget Line:** Shows the set of all feasible combination of goods and services a consumer can have given her limited income and the market prices of the goods or services at a given point in time.
6. **Indifference Curve:** Shows all the alternative combinations of two goods that yields the *same total* satisfaction and among which the consumer would be indifferent.
7. **The Marginal Rate of Substitution of X or Y ( $MRS_{x/y}$ ):** refers to the amount of Good Y that a consumer will be willing to give up to obtain one more unit of Good X while remaining on a given indifference curve. It measures the willingness of a consumer to exchange one good for another while neither gaining nor losing utility in the process. It is measured by the slope of the indifference cuve.
8. **The Law of Diminishing  $MRS_{x/y}$ :** States that as more of one good, say Good X, is consumed, the amount of the other good (Good Y) that the consumer is willing to sacrifice for one more unit of Good X declines.