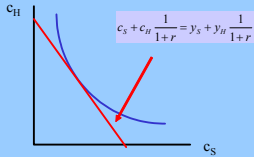


Consumption

Inheritances



The Issue

- Our consumers are selfish, caring only for themselves (and indeed only cared for by themselves).
- Common sense suggests that there are bequests and inheritances.

Some Assumptions

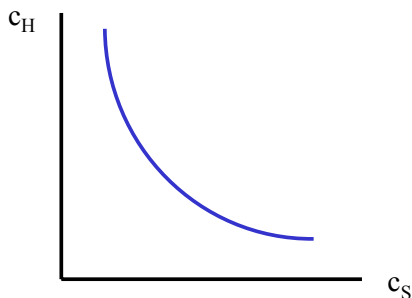
- Two generations
 - Self and Heir
- Income is y_S and y_H .
- The discount rate is r
- Everything is certain

The Key Insight

- People have a preference function

$$U(c_S, c_H)$$

Indifference Curves

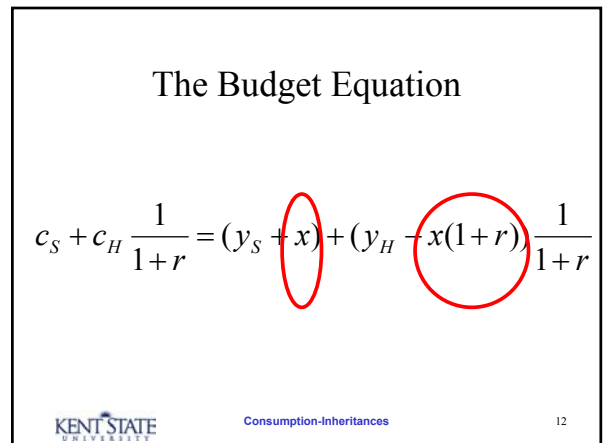
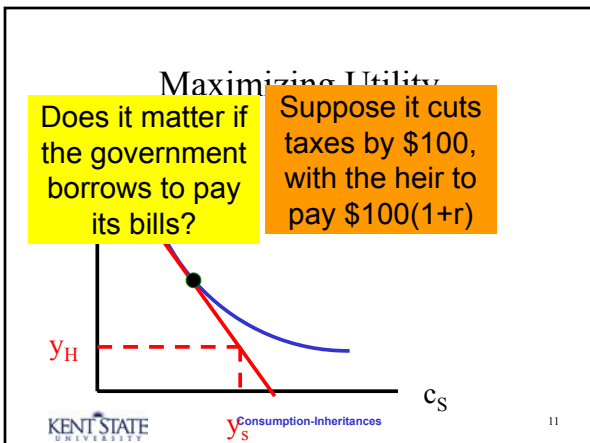
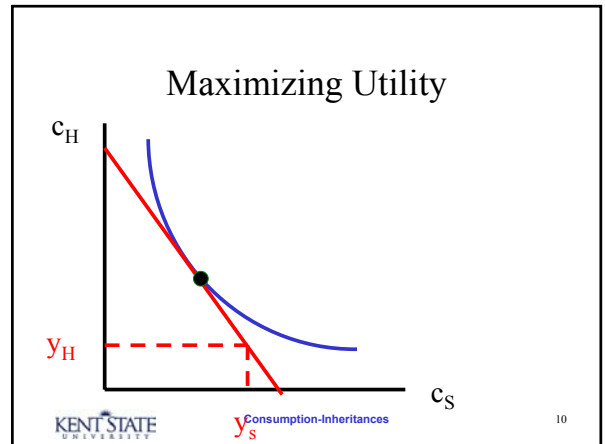
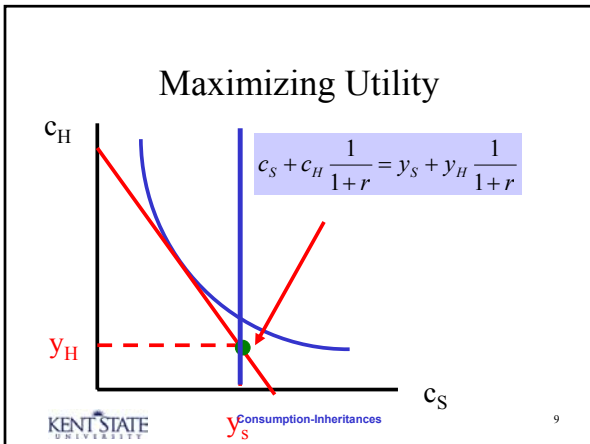
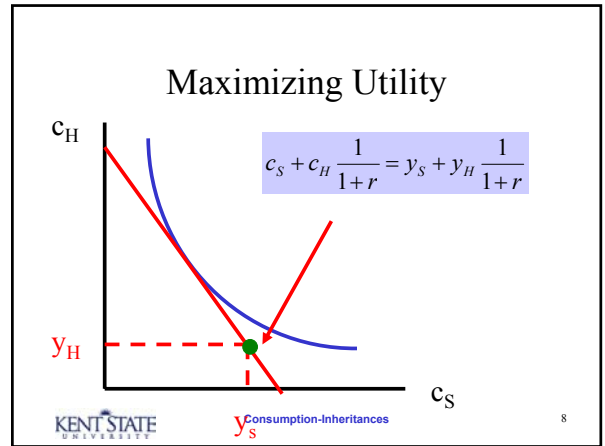
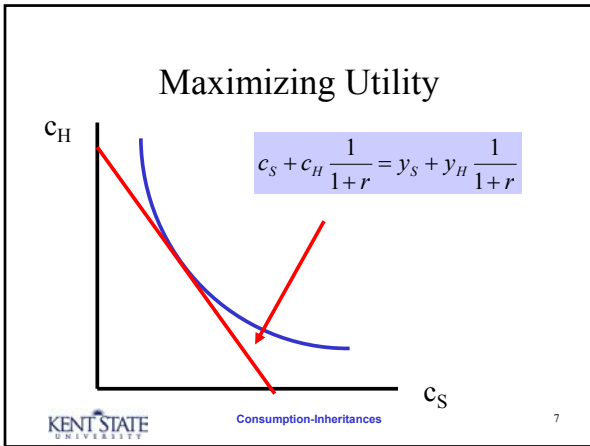


The Budget Constraint

- The basic budget reality

$$c_H = y_H + (y_S - c_S)(1+r)$$

$$c_S + c_H \frac{1}{1+r} = y_S + y_H \frac{1}{1+r}$$

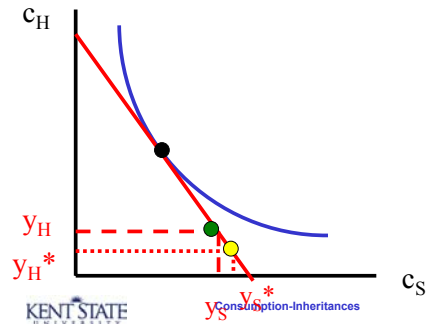


The Budget Equation

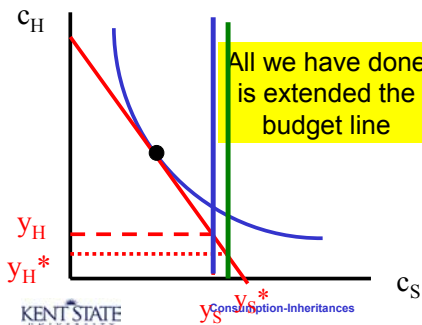
$$c_S + c_H \frac{1}{1+r} = (y_S + x) + (y_H - x(1+r)) \frac{1}{1+r}$$

$$c_S + c_H \frac{1}{1+r} = y_S + y_H \frac{1}{1+r}$$

Government Borrowing

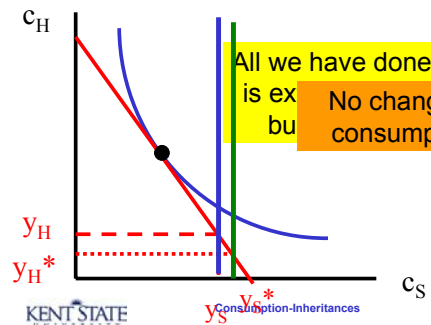


Government Borrowing



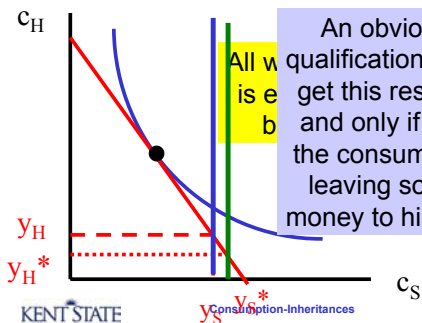
All we have done is extended the budget line

Government Borrowing



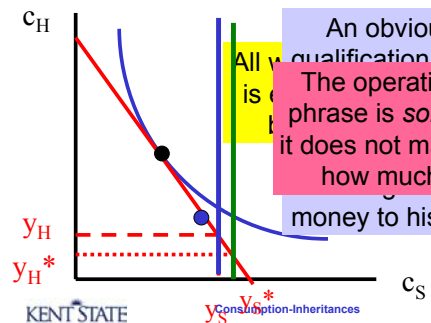
All we have done is extend the budget line. No change in consumption

Government Borrowing



All we have done is extend the budget line. An obvious qualification. We get this result if and only if (iffi) the consumer is leaving some money to his heir

Government Borrowing



All we have done is extend the budget line. An obvious qualification. We get this result if and only if (iffi) the consumer is leaving some money to his heir. The operative phrase is some; it does not matter how much

End

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