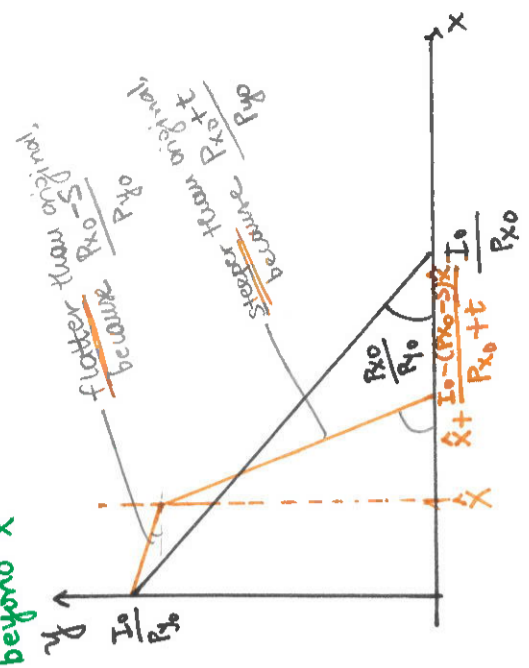


③ UNIT SUBSIDY till \hat{X} , then UNIT TAX (t)

why? Gov restricts consumption of good X beyond \hat{X}



REAL INCOME of X

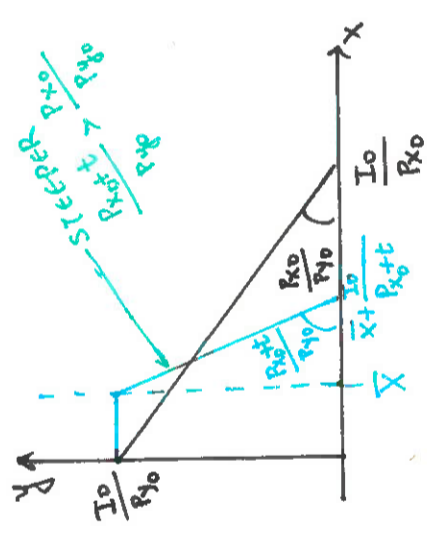
Spent on X at price of $(Px_0 - S)$
 REMAINING NOMINAL INCOME?

$$\frac{I_0 - [(Px_0 - S) \cdot \hat{X}]}{Px_0 + t}$$

KINKED BUDGET CONSTRAINTS

UNDERSTAND REAL INCOME

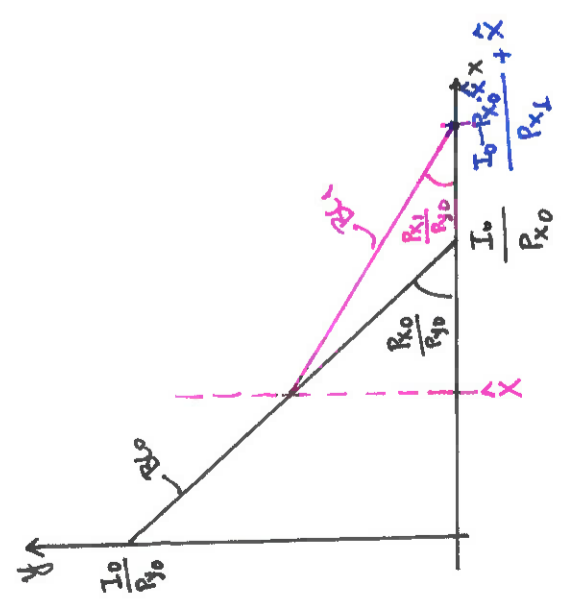
② TRANSFER \bar{X} ; After \bar{X} , UNIT TAX (t) on X...
 why? Gov to ration consumption of good X



REAL INCOME of X

What you consume BEFORE t?
 \bar{X}
 How much less X you can buy?
 $\therefore \frac{I_0}{Px_0 + t}$

① AFTER CONSUMING \hat{X} , $P_x \downarrow \dots$



REAL INCOME of X

What you consume BEFORE the price change?
 \hat{X}
 How much MORE X you can buy with REMAINING income AFTER consuming \hat{X} ?
 REMAINING NOMINAL INCOME

$$\frac{I_0 - Px_0 \cdot \hat{X}}{Px_1}$$

Divide by NEW price to get real income