

Linear fractional relative risk aversion^{*}

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April 23, 2026

Abstract

We characterize the family of utility functions satisfying linear fractional relative risk aversion (LFRRA) in terms of the Gauss hypergeometric functions. We apply this family, which nests various utility functions used in different strands of literature, to monopolistic competition and obtain the profit-maximizing price by generalizing the Lambert W function. We let firm-level data decide whether the RRA in each sector or in the aggregate economy is increasing, decreasing, or constant, which in turn determines whether markups are decreasing, increasing, or constant with respect to marginal costs.

Keywords: linear fractional relative risk aversion; Gauss hypergeometric functions; monopolistic competition; generalization of the Lambert W function; markups.

JEL Classification: D43; D21; D22; D11.

^{*}Earlier versions of this paper have been presented at the ETSG 2025 Milan, the 39th Annual Meeting of the Applied Regional Science Conference, the CAE Research Workshop in International Economics (ETH Zürich), and UQAM. We thank Ikuto Aiba, Swati Dhingra, Peter Egger, Ruobing Huang, and Mathieu Parenti, as well as the participants at these conferences and workshops, for valuable comments and suggestions. Behrens gratefully acknowledges financial support from SSHRC Insight Grant #435-2021-1017. Murata gratefully acknowledges financial support from JSPS KAKENHI Grant Number 24K04845.

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