

THE PUBLIC SECTOR

The Micro Economy Today, 11th Edition
By Bradley R. Schiller

Chapter 4

I. The Nature of Market Failure

A. The economy's invisible hand can lead to the production of:

B. Graph of PPC to illustrate



C. Market Failure occurs when:

D. Thus, market failure establishes an economic basis for:

II. Causes of Market Failure

A. Public Goods

1. Private goods:

2. Public goods have TWO characteristics:

a.

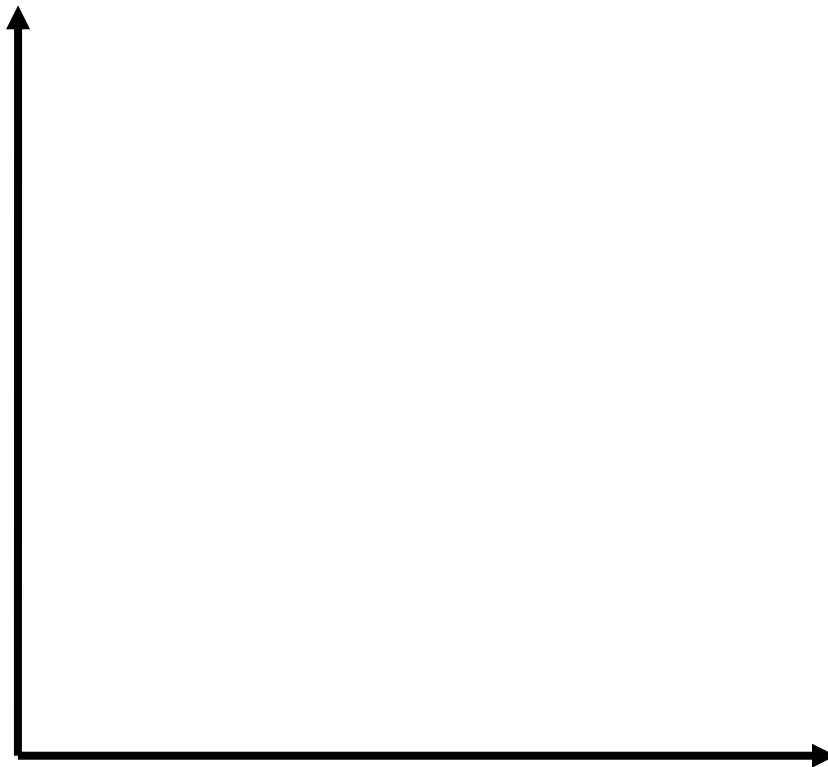
b.

3. The “Problem” with Public Goods

4. Implication: For public goods, the link between _____
and _____ is broken.

=>

5. PPC graph to illustrate



6. Solution:

B. Externalities:

1. External Costs

a. Example:

b. Implication: Goods with external costs will be _____ -
_____ in a market setting.

2. External Benefits

a. Example:

b. Implication: Goods with external benefits will be _____ -
_____ in a market setting.

3. Potential Solutions

a.

b.

C. Market Power

1. Definition:

2. Source:

3. The Problem: A firm with market power will:

a.

b.

4. Potential Solution

D. Inequity

1. In a market-based economy, incomes (and thus goods and services) will be distributed _____ .

2. Does this market-generated distribution of income violate society's view of _____ ?

3. The principal mechanism for income redistribution is the:

a.

b.

4. Merit goods: