CHAPTER 14 : MARKET FAILURE

Key terms

1. Social benefit : benefit to the society or the sum of private benefit and external benefit
2. Social cost : cost to the whole society or the sum of private cost and external cost
3. Private benefits : benefits from consumption to consumers or benefit from production to producers
4. Private cost : cost of consumption to consumers or cost of production to producers
5. External cost : negative effects from consumption or production to the third party
6. External benefit : positive effects from consumption or production to the third party
7. Socially optimal output: the level of output where society's welfare is maximized. It is where social cost and social benefit are equal
8. Merit goods: products which generate positive externalities and are under-consumed in the free market e.g. education and healthcare
9. Demerit goods: Products which generate negative externalities and are over-consumed in the free market e.g. alcohol
10. Private goods: Product which is rival and excludable.
11. Public goods : Product which is non-rival and non-excludable. It needs government help to provide
12. Monopoly : A single seller
13. Price fixing : when two or more firms agree to sell a product at the same price

1. What is Market failure?

Market failure : when markets allocate resources inefficiently.

2. Types of market failure

2.1) Externality

: Market fails to take into account all costs and benefits.

↳ There is **overproduction and overconsumption** in some goods which generate external cost e.g. pollution and alcohol.

↳ There is **underproduction and underconsumption** in some goods which generate external benefits e.g. research on medicine and education.

2.2) Information failure

: when consumers and producers do not have equal access to information. It leads to the wrong decision.

2.3) Underconsumption or underproduction of merit goods

: Products which are under consumed in the free market. And, the goods generate positive externalities (Positive effect to the third party)

2.4) Overconsumption or overproduction of demerit goods

: Products which are over consumed in the free market. And, the goods generate negative externalities (negative effect to the third party)

2.5) Public goods

: Product which is non-rival and non-excludable, it is under-provided in the free market. Non-excludable means no one can be excluded from the consumption. Non-rival means the consumption by one person does not reduce the consumption to the next consumer.

2.6) Monopoly

: A single seller has market power to restrict output to push up the price. Then consumers face high prices and low quantities of output in the market.

2.7) Immobility of resources

: Some resources are geographical and occupational immobility.