CHAPTER 8 : Efficiency

Key terms

1. Allocative efficiency : occurs when scare resources are used to produce a bundle of goods which satisfies consumer preferences and maximise their welfare
2. Dynamic efficiency : occurs when resources are allocated efficiently over time
3. Productive efficiency : achieved when production is achieved at the lowest average cost
4. X-inefficiency : arising because a firm or other productive organisation fails to minimise its average costs of production at a given level of output

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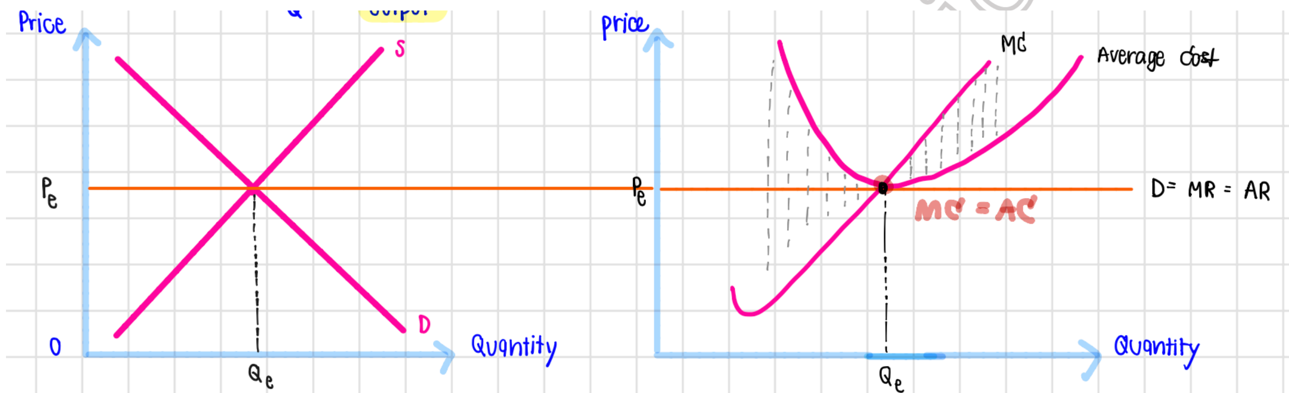
1. **Productive efficiency** : goods and services must be made using the least possible resources and the minimum possible cost

MC=AC

For example , Perfect competition in the market



Characteristics perfect competition

- Many buyers and sellers
- Homogenous products
- Price taker
- No barrier to entry into the market
- Perfect information in the market

1. In perfect competition, firm cannot set price so P = MR =AR
2. MC is additional cost when increasing quantity
3. To find out max profit, MR=MC therefore at this point it can also achieve the lowest cost MC=AC

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2. Allocative efficiency

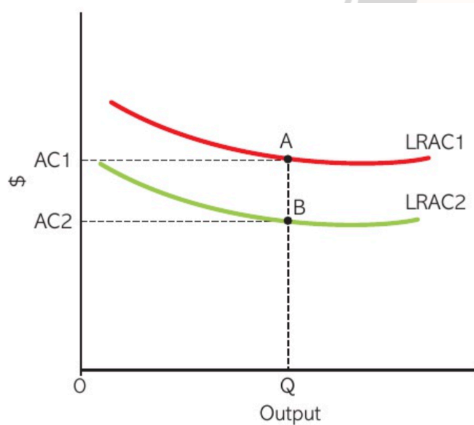
: measures whether resources are allocated to those goods and services demanded by consumers

P=MC

3. Dynamic efficiency

: is an economy when resources are allocated efficiently over time. Dynamic efficiency concerns the rate of investment. Firms invest either to cut costs or to make a new products. Investment can be in research and development, in machinery or buildings or training workers.

Diagram



4. X-inefficiency

: It occurs when a firm is not producing at the lowest possible cost for a given level of output.

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