Explain how the existence of externalities (whether from congestion or pollution)...

Literature, Russian Literature

Externalities and Road Transport Economics Insert (s) Externalities and Road Transport Economics

The existence of externalities such as congestion and pollution often negatively affect resource allocation in road transport by distorting the various pricing mechanisms thereby resulting in the less than optimal allocation of resources to the sector. This is particularly attributed to the fact that market prices normally ignore the costs imposed on the third parties and thus the pricing mechanism can never reflect the true social costs of economic activities. In today's world economy, road transport plays a vital role. Condition in which marginal communal costs is equal to marginal communal benefits refer to an efficient balance (Block, 2009, p. 10).

The resource allocation changes through externalities since the market fails to completely fund the external belongings caused by economic actions. Markets prices tend to reflect a price based on the original personal utility, while disregard the payback on the third parties. Therefore, personal costs may deviate from social costs as the pricing means fall short to replicate the social economic actions. When the demand for road uses rises above a given level, additional costs (externalities) such as congestion, pollution may result in increased costs such as increased fuel consumption, increased journey times and other running costs as shown below.

Additionally pricing arrangement results in a sub-Pareto, most select allocation of resources as the marginal cost of an action equals its marginal private cost where equals its cost due to the failure of all relevant effects. The actual price of a product does not entirely resolve its allocation and consequently the purpose of the market to resourcefully distribute resources based on their accurate prices breaks down consequential in a misallocation. Lastly, according to Schmidtchen (2009, p. 30), the continuation of externalities leads to sub-optimal allocation since both too many resources used in processes presenting and uncompensated collective repayment while the return maximizing production is less than the socially best production

References

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