

What is meant and how can government attempt to correct it?

Government



What is meant by market failure and how can government attempt to correct it? Market failure occurs when there is no economic efficiency within a market. Whereas government intervention is put in use when a market may not always allocate scarce resources efficiently in a way that achieves the highest total social welfare. Monopolies are one of the main causes of market failure. Monopolies are firms whom have eliminated all, if not, most competitors within that market leaving them with most control within that market.

The main reason why monopolies are negative within the economy is because they dictate pricing. After having eliminated most competitors, they then can start to charge whatever price they want for a product as the consumers can't go elsewhere. As well as having increased the price of a product, they now have caused a limit in choice for the consumer. This is because the consumer can't go for a cheaper product within that market as the monopoly has gotten rid of competition, thus leaving the consumer with high prices to pay at a limited choice.

Another reason is because monopolies only have profit maximisation in mind. Profit maximisation is when a firm determines the price and output level that returns the greatest profit. Although the firm is maximising its profits, monopolies are allocatively inefficient. Monopolies tend to become complacent over time because pricing power, not gains from efficiency or innovation, drive profits. This means that due to the fact that they have stripped consumer surplus and experiencing vast profits, they are simply not allocating resources efficiently simply to do with its size.

As a firm gets larger, it is more difficult for managers to be on top of every single thing that occurs within the company. Unnecessary waste could be caused meaning they aren't allocating the finite resources efficiently, which isn't beneficial in any economy. Due to a lack of innovation and efficiency, this also causes allocative inefficiency as they now have to compete on efficiency and new technology, which affects markets in negative manners.

Walmart invested over one billion dollars to lose within the first year, by making prices of products incredibly cheaper than its competitors which drove them out of business, then increased prices in order to make back the losses and make huge profits whilst having removed all if not most competition. This is known as predatory pricing and is now very difficult to achieve because the governments noticed what had happened within that market and had to intervene in order to control market share within markets.

Governments have now set a limit of 25% market share so that monopolistic behaviour doesn't occur within a market, thus allowing other smaller business to compete or even simply enter for new businesses to enter. This is beneficial because firms will now have to compete on efficiency and innovation, so the push of new technology through research and development creates a higher efficiency within a market as firms will now try to keep costs low instead of taking consumer surplus like monopolies. Inequality plays a large factor within causing market failure.

This is because differences in wealth and income of different groups lead to a wider gap in living standards between households. Thus the division of rich and poor. Society itself may not find too much inequality acceptable. Those <https://assignbuster.com/what-is-meant-and-how-can-government-attempt-to-correct-it/>

who are born into a rich background are more likely to be rich later in life, whereas some who are born into a poor background are a lot more likely to live a life of poverty. This is because those with richer backgrounds will have better education and up bringing thus increasing the chances of success later in life. In a free market, this isn't the case.

It is thought that all individuals have the opportunity to succeed. But, because of misallocation of resources in a free market economy this isn't always the case. The way the government try to tackle this issue and making the gap smaller is normally by imposing a larger tax on the rich and create government programs which transfer this income to the poor. These are normally known as welfare benefits, unemployment benefits, public schools, NHS and some sort of support for economic development in poorer communities where unemployment and poverty is very high.

Welfare benefits are very beneficial in spreading income to poorer people as they now have money to spend and inject back into the economy which also stimulates it but also increases their opportunities in life as they can afford things like gym memberships which make for a healthier and fitter labour force. However, nowadays, people have gotten lazy and inherited this life of living on benefits. This isn't beneficial for the economy in the slightest as they are people who are capable of working and add to the labour force but choose not to as they believe they live an easier life by given money for free by the tax payer. Public schools are put in place because it gives those with a poorer background a chance to be educated and more possibilities for the future. This increase in possibilities could lead to them from escaping a life of poverty, thus decrease gap between rich and poor. NHS is also one of the

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best healthcare systems devised, because it gives the chance for those who cannot afford to pay for doctors and hospital bills if anything were to happen, which leaves the economy with healthier people or simply people who can be treated when ill for free.

However, this comes out of the tax payers pocket and seems very unfair for those who pay and never need to use NHS whereas there are some who don't work and choose to, you can almost say 'milk it'. Even though some choose to abuse it, NHS has had more positive outputs into the economy as it keeps the labour force treated of any injury or illness making for a more efficient labour force thus preventing market failure. A market may fail due to externalities.

Externalities are benefits or costs which come from economic activity and affect someone other than those who are actually engaged in that economic activity and are not taken into account fully in the price we pay. Due to the fact that they aren't taking into account of the price they are a form of market failure because the amount of the activity carried out, if left to the free market would not be an efficient use of resources.

One of the main negative externalities which affects is pollution, for example, a city where manufacturing industries are based would be the cause of the pollution and poor environment as they pollute the air which we breathe, the rivers by dumping chemical waste and kill wild life. If a government weren't to intervene then these externalities would become so severe that our atmosphere and environment could come to be so polluted that people become ill and die. These people are the labourers of that economy and if

work force starts dying out this leads to a loss in production as people would need to be treated.

Thus, eventually leading to market failure. One way the government can resolve this is by setting regulations for example, a ban. Another way is by determining whether it's a negative or positive externality, and if it's negative, impose a tax, if positive, a subsidy. A tax on negative externality would correct market failure as the cost for it is now being taken into account in the price. Overall, as we can see the government has devised many different forms of policies in order to prevent market failure.

Monopolies, inequality and externalities are some of the main reason to explain why market failure occurs, however the government has overcome this. For example, with monopolies, they realise one business having most percentage of market share wasn't beneficial to the market and consumers as there simply wouldn't be any competition and an exploitation by that firm so they set a maximum of 25% market share so that there would be fair competition and competing with prices in order to offer the consumer the best possible price and product.