Market failure and government policies assignment

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Market failure and Government policies A case in which prices are unable to adequately adjust to reflect changes in supply or demand. Market failure may occur due to unexpected disruptive events such as wars or natural disaster, or due to economic barriers such as trade restriction or monopolies. Market failure occurs when freely-functioning markets, fail to deliver an efficient allocation of resources. The result is a loss of economic and social welfare. Market failure exists when the competitive outcome of markets is not efficient from the point of view of society as a whole.

This is usually because the benefits that the free-market confers on individuals or businesses carrying out a particular activity diverge from the benefits to society as a whole. An economic term that encompasses a situation where, in any given market, the quantity of a product demanded by consumers does not equate to the quantity supplied by suppliers. This is a direct result of a lack of certain economically ideal factors, which prevents equilibrium. Types of market failure 1. Externalities (positive and negative) 2. Merit and De merit goods 3. Public Goods 4. Monopoly Power 5. Inequality 6. Factor Immobility 7. Agriculture

Reason of Market Failure Externalities An externality is an effect of a purchase or use decision by one set of parties on others who did not have a choice and whose interests were not taken into account. Negative externalities (e. g. the effects of environmental pollution) causing the social cost of production to exceed the private cost. Ex. pollution, generated by some productive enterprise, and affecting others who had no choice and were probably not taken into account. Positive (or beneficial) externalities (e.

g. the provision of education and health care) causing the social benefit of consumption to exceed the private benefit.

For instance, each infected person who takes drugs eliminate diseases helps all of society, not just the Drug company who provide the medicines. ? ? Imperfect information means merit goods are under-produced while demerit goods are over-produced or over-consumed. ? The private sector in a free-markets cannot profitably supply to consumers pure public goods and quasi-public goods that are needed to meet people's needs and wants ? Market dominance by monopolies can lead to under-production and higher prices than would exist under conditions of competition ?

Factor immobility causes unemployment hence productive inefficiency One cause of market failure is the immobility of factors of production. There are many types of factor immobility, occupational and geographical immobility, capital immobility, land. ? Equity (fairness) issues. Markets can generate an ' unacceptable' distribution of income and consequent social exclusion which the government may choose to change. ? With inequality, markets can generate an ' unacceptable' distribution of income and consequent social exclusion which will cause allocates inefficiency. Market Failure Results in: Productive inefficiency: Businesses are not maximizing output from given factor inputs. This is a problem because the lost output from inefficient production could have been used to satisfy more wants and needs ? Allocate inefficiency: Resources are misallocated and producing goods and services not wanted by consumers. This is a problem because resources can be put to a better use making products that consumers value more highly Government Intervention Regulatory actions taken by a government in order to affect or

interfere with decisions made by individuals, groups, or organizations regarding social and conomic matters. Taxes such as changes in VAT and excise duties can be used to raise the price of demerit goods and products with negative externalities designed to increase the opportunity cost of consumption and thereby reduce consumer demand towards a socially optimal level. Subsidies to consumers will lower the price of merit goods such as grants to students to reduce the internal costs of staying on in full-time education and subsidies to businesses employing unemployed workers on the New Deal programme.

They are designed to boost consumption and output of products with positive externalities ??? a subsidy causes an increase in market supply and leads to a lower equilibrium price (see the separate revision focus article on producer subsidies). http://www. aaec. ttu. edu/Faculty/aabenson/aaec2305/Lectures/ch18. pdf http://tutor2u. net/economics/revision-notes/a2-micro-market-failure-introduction. html Five approaches have been taken to Solving the problem of externalities government-imposed taxes and subsidies, private bargaining and negotiation, legal rules and procedures, ale or auctioning of rights to impose externalities, and direct government regulation. Taxes, subsidies, legal rules, and public auction are all methods of indirect regulation designed to induce firms and households to weigh the social costs of their actions against the benefits. Finally I'll like to conclude that One important point to bear in mind is that the effects of different forms of government intervention in markets are never neutral ??? financial support given by the government to one set of producers rather than another will always create “ winners and losers”.

Taxing one product more than another will similarly have different effects on different groups of consumers. Five approaches have been taken to solving the problem of externalities Government-imposed taxes and subsidies: ??? Taxes such as changes in VAT and excise duties can be used to raise the price of demerit goods and products with negative externalities designed to increase the opportunity cost of consumption and thereby reduce consumer demand towards a socially optimal level. Subsidies to consumers will lower the price of merit goods such as grants to students to reduce the internal costs of staying on in full-time education and subsidies to businesses employing unemployed workers on the New Deal programmed. They are designed to boost consumption and output of products with positive externalities ??? a subsidy causes an increase in market supply and leads to a lower equilibrium price (see the separate revision focus article on producer subsidies).