

Webnote 291

Syllabus: Items 66-67

Use the syllabus to understand the
key concepts in relation to items 66-
67 of the syllabus

Market Failure – Public Goods

Features:

(important for definition/explanation)

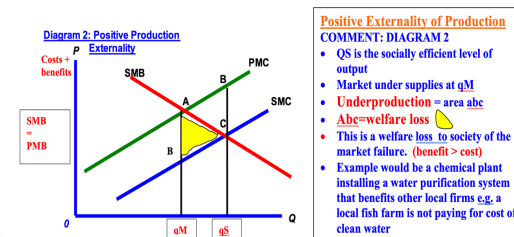
1. Non-excludable
2. Non-rivalrous
3. *Non-rejectable*
(not in syllabus)

Features:

Features:

(important for definition/explanation)

1. Non-excludable – not possible to restrict use of public goods, e.g. street lighting, judicial system
2. Non-rivalrous – users are not competing to use the public good so access to public good
3. (Non-Rejectable – person cannot reject benefit e.g. national defence)



Pure public good:

1. Non-excludable
2. Non-rivalrous
3. E.g. think of police services, judicial service or nuclear defence of a country

Public Goods

Problem:

Solutions:

1. Government Direct Provision: Underprovided – see Diag 2 below where Market equilibrium is below optimal level for society.
2. Government employs the market (firms) to supply the good.

Key problems :

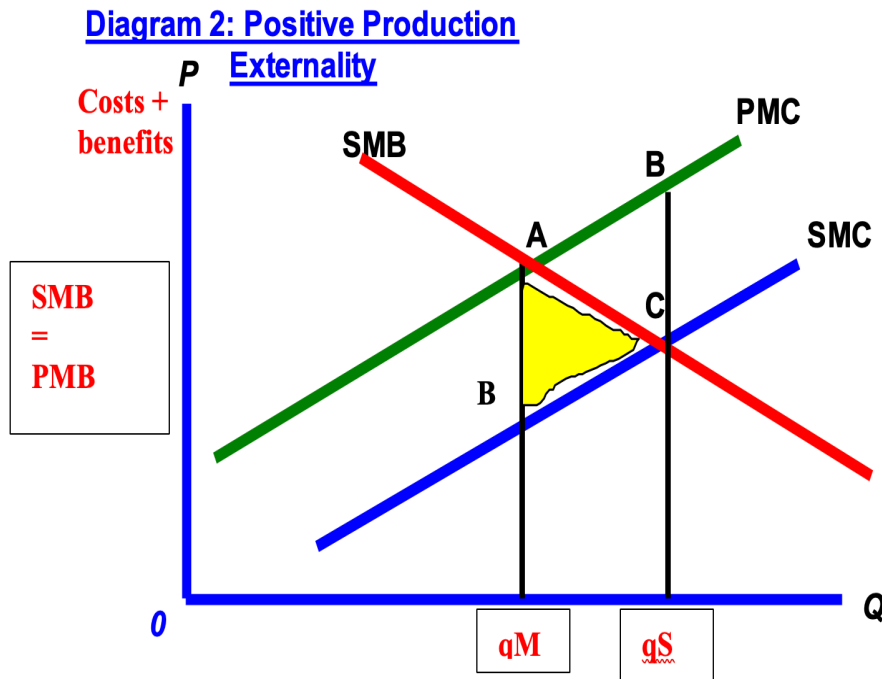
- with public goods are over use e.g. tragedy of the commons
- 'free rider' problem
- Need for direct provision by government e.g. infrastructure roads, street lights etc

Government can use legislation to restrict use e.g. overfishing

Difficult to regulate. Advertising may reduce e.g. need to pay for service e.g. national television licence. This is a legal requirement but many households do not buy e.g. free riding

Government can use direct provision to overcome shortage of public goods where market fails to provide

Public goods + underprovision



Positive Externality of Production

COMMENT: DIAGRAM 2

- QS is the socially efficient level of output
- Market under supplies at qM
- **Underproduction** = area abc
- Abc=welfare loss
- This is a welfare loss to society of the market failure. (benefit > cost)
- Example would be a chemical plant installing a water purification system that benefits other local firms e.g. a local fish farm is not paying for cost of clean water