



3055 BA SANGAM COLLEGE

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Week 11

LESSON NOTES

School: Ba Sangam College

Year: 11

Name: _____

Subject: Economics

Strand 3	Macroeconomics
Sub Strand 3.2	Government in the Economy
Content Learning Outcome EC11.3.2.1	Justify the need for a government in an economy.

GOVERNMENT IN THE ECONOMY

MARKET FAILURE

The following conditions must be met if the market is to work well without any government actions (that is, the Invisible Hand to bring about Allocative efficiency):

- Consumer sovereignty
- Perfect information
- Perfect mobility
- Perfect competition
- Public goods and Externalities

Market failure

- occurs when the conditions of the market system to work perfectly are not met, so the price system will not achieve allocative efficiency.
- In other words, the result of the market failure is an inefficient allocation of resources. The market failure can be used to justify government intervention.

Intervention available to government may take the form of :

- Taxes
- Subsidies
- Law, control, regulations
- Direct provisions of services/ transfers

Factors That Contribute To Market Failure

1. Inefficiency

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- All firms operate in imperfectly competitive arrangements and perfect competition is not seen in reality.

2. Income Inequality

- The market incomes may not reflect socially desirable outcomes, with the rich getting richer and poor getting poorer. In such cases, inequality is increased and there is a large gap between the rich and poor.

3. Externalities and Public Goods

In real world situation:

- There are goods with external effects on others (that is, associated with externalities).
- There is lack of public goods because the free market has no incentive to produce them as they cannot be sold. This provides justification for government intervention.

4. Price Fluctuations

- The fluctuations of prices in the market lead to the decrease in the firms' confidence in earning profit.
- Therefore, firms are discouraged to produce goods and services resulting in a decrease in total production/output.

Activity

1. Name the Economist associated with Invisible Hand

_____ (1 mark)

2. State three conditions that must be met if the market is to work well without any government actions.

_____ (3 marks)

3. Define Market failure

_____ (1 mark)

4. State **four** ways the government intervenes to solve market failures.

_____ (4 marks)

5. State the tax system that government can use to solve the problem of unequal distribution of income. (1 mark)

6. Define the term Externalities

_____ (1 mark)

7. What do you understand by the term **Public Goods** and state **three** examples?

Examples

(4 marks)

The End