# 3 Market failure – Part 1

Name: ______________ Class: __________ Date: ____________

## Vocabulary 词汇

*Write each word three times.* 把每个单词抄写三遍。

| English | 中文 | Write it 3 times (English) | | |
|---|---|---|---|---|
| Market failure | 市场失灵 | | | |
| allocate | 配置 | | | |
| externality | 外部性 | | | |
| third party | 第三方 | | | |
| negative externality | 负外部性 | | | |
| social cost | 社会成本 | | | |
| private cost | 私人成本 | | | |
| positive externality | 正外部性 | | | |
| public good | 公共物品 | | | |
| national defence | 国防 | | | |
| free-rider problem | 搭便车问题 | | | |
| merit good | 优值品 | | | |
| demerit good | 劣值品 | | | |
| information failure | 信息失灵 | | | |

## Recall

In topics 1–2 you saw markets set prices and usually work well. Bring this with you:

- A market lets buyers and sellers meet, and the price guides them.
- But the result is not always best for **society** as a whole.

At AS we study **market failure** —when a free market makes too much or too little of a good.

## New ideas

### 1 What market failure is

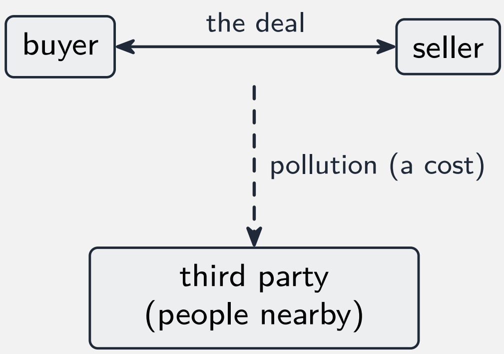
**Market failure** 市场失灵 is when a free market does not **allocate** 配置 (share out) resources efficiently —**too much** or **too little** of a good is made. Then the government may step in to fix it.

**Micro-check.** State what is meant by market failure. [1]

### 2 Externalities

An **externality** 外部性 is a cost or a benefit that falls on a **third party** 第三方—someone who is not the buyer or the seller.

- a **negative externality** 负外部性 (like pollution from a factory): the **social cost** 社会成本 (to everyone) is bigger than the **private cost** 私人成本 (to the producer), so the market makes **too much**;
- a **positive externality** 正外部性 (like a vaccination that protects others too): the market makes **too little**, because buyers ignore the benefit to others.




**Micro-check.** A factory pollutes a river. Is this a negative or a positive externality? [1]

### ■ 3 Public, merit and demerit goods

- a **public good** 公共物品 (street lighting, **national defence** 国防) cannot shut out non-payers, so private firms make no profit and supply none —the **free-rider problem** 搭便车问题;
- a **merit good** 优值品 (like education) is **under-consumed** —people buy too little;
- a **demerit good** 劣值品 (like cigarettes) is **over-consumed** —people buy too much, because of **information failure** 信息失灵 (they misjudge the harm).


**Micro-check.** Is education a merit or a demerit good? [1]

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**Watch out:** a *negative* externality (pollution) → social cost > private cost → market makes *too much*; a *positive* externality (vaccination) → market makes *too little*. Merit goods are under-consumed; demerit goods over-consumed.

## Practice

**3.1** Explain what is meant by **market failure**. [2]

**3.2** A factory's smoke harms people living nearby. State the type of externality, and whether the market makes too much or too little. [2]

**3.3** Explain why private firms will not supply a **public good**. [2]

**3.4** State whether each is **under**- or **over**-consumed: (a) a merit good; (b) a demerit good. [2]

**3.5** Give one example of (a) a merit good and (b) a demerit good. [2]

**3.6 Challenge.** A coal-burning power station causes pollution. Explain why the free market produces *too much* electricity, using the ideas of private and social cost. [2]