

## Study Questions and Revised Reading List

### Efficiency and Equity

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### Revised Reading List

#### Part 1 – The Role of Public Policy

##### 1.1 Introduction

##### 1.2 Efficiency and Equity – Welfare Economics

###### 1.2.1 Partial Equilibrium and Efficiency

Katz, Michael L. and Harvey S. Rosen, *Microeconomics*, Second Edition, Burr Ridge, Ill.: Irwin, 1994, pp. 377-385. (<http://oregonstate.edu/~tremblac/katzandrosen.pdf>)

###### 1.2.2 General Equilibrium and Efficiency

► Pindyck, Robert S. and Daniel L. Rubinfeld, *Microeconomics*, Sixth edition, Upper Saddle River, NJ: Pearson Prentice Hall, 2005, pp. 579-584, 590, 604-607.

###### 1.2.3 Equity

Katz and Rosen, pp. 422-426.

► Pindyck and Rubinfeld, pp. 591-593.

###### 1.2.4 When Should the Government Intervene?

► Pindyck and Rubinfeld, pp. 607-610.

### Study Questions

#### Partial Equilibrium and Efficiency

- Define consumer surplus, producer surplus, and total surplus verbally and graphically.
- Explain and show graphically why total surplus is maximized in perfect competition.
- Show how consumer surplus, producer surplus, and total surplus change when price controls are imposed.
- Define deadweight loss and show graphically.
- Explain why society might impose rent control laws even if total surplus falls.
- Show how a rent control policy can actually reduce consumer surplus.
- Illustrate how a federal tax on a good would affect total surplus.
- Define excess burden.

## General Equilibrium and Efficiency

*Note:* PowerPoint slides for the lecture are posted on my website for this topic.

- Define partial equilibrium analysis and general equilibrium analysis.
- Construct a supply and demand model of 2 interrelated markets (i.e., where the goods are complements, goods are substitutes, or 1 good is an input in the production of the other good). Show how a partial equilibrium model understates the effects of a change in price or quantity in one market when there are feedback effects from a related market.
- Explain when a General Equilibrium occurs.
- Define a Pareto efficient allocation.
- State the first and second theorems of welfare economics.
- Define Marginal Rate of Substitution (MRS), Marginal Rate of Technical Substitution (MRTS), and Marginal Rate of Transformation (MRT).
- List the 3 conditions needed for economic efficiency.
- Describe the equalities that must hold for each of the following types of efficiency:
  - Efficiency in exchange.
  - Efficiency in production.
  - Efficiency in the output market.
- Why do competitive markets satisfy the 3 conditions of efficiency? Use equalities to show your answer.
- Suppose that the MRTS for good  $x = 2$  and the MRTS for good  $y = 3$ . Should society change the amount of  $x$  produced and the amount of  $y$  produced? If so, how?
- Explain why an allocation of goods is efficient only if the goods are distributed so that the MRS between any pair of goods is the same for all consumers.
- Practice problems in Pindyck and Rubinfeld, pp. 34-35: #2, 3 (skip the Edgeworth Box; use a chart like 16.1–note that there is more than 1 answer.)

## Equity

- Using a utility possibilities frontier, illustrate that: 1) an efficient allocation need not be equitable; 2) an inefficient allocation may be more equitable than an efficient allocation.
- Define a social welfare function verbally and in equation form.
- State 4 views of equity.
- Critique the idea of social welfare maximization as a method of attaining social goals.

## When Should the Government Intervene?

- Briefly discuss 4 situations in which free markets are not efficient.
- Explain why monopoly power violates the conditions of economic efficiency.
- How does the second welfare theorem relate to government intervention?