3 Market failure – Part 2

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)		
indirect tax	间接税			
subsidy	补贴			
maximum price	最高限价			
shortage	短缺			
minimum price	最低限价			
regulation	管制			
state provision	政府提供			
Government failure	政府失灵			

Recall

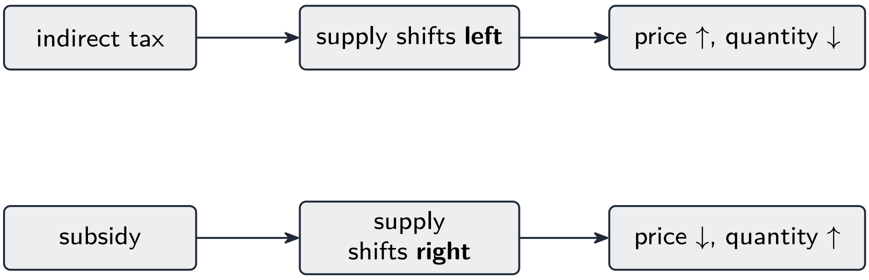
In **Part 1** you met market failure, externalities, and public, merit and demerit goods. Part 2 looks at how the **government** tries to fix market failure.

New ideas

■ 1 Indirect taxes and subsidies

- an **indirect tax** 间接税 is a tax on spending. It raises a firm's costs, so the supply curve shifts **left** — the price rises and the quantity falls. Governments tax **demerit goods** (like tobacco) and goods with negative externalities;
- a **subsidy** 补贴 is a government payment to producers. It lowers their costs, so

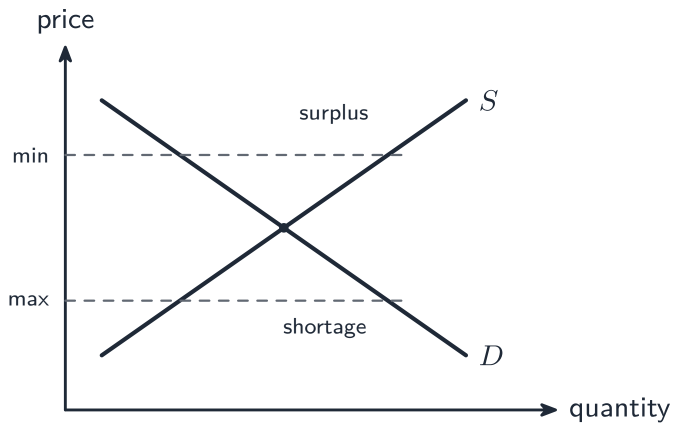
supply shifts **right** — the price falls and the quantity rises. Subsidies are used for merit goods and positive externalities.



Micro-check. State what an indirect tax does to the **price** of a good. [1]

■ 2 Maximum and minimum prices

- a **maximum price** 最高限价 is a legal top price set **below** equilibrium (for example rent control). The quantity demanded is greater than the quantity supplied, so there is a **shortage** 短缺;
- a **minimum price** 最低限价 is a legal bottom price set **above** equilibrium (for example a minimum wage). The quantity supplied is greater than the quantity demanded, so there is excess supply.



Micro-check. A maximum price is set below the equilibrium. State what this causes. [1]

■ **3 Other methods, and government failure**

- **regulation** 管制 — rules and laws, such as bans, age limits and pollution limits;
- **state provision** 政府提供 — the government supplies the good directly (schools, hospitals).

But intervention does not always help. **Government failure** 政府失灵 is when the government's action makes the use of resources **worse** — for example, a maximum price can create an illegal black market.

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

Watch out: an indirect tax shifts supply *left* (price up, quantity down) — used on demerit goods; a subsidy shifts supply *right* (price down, quantity up) — used on merit goods. A maximum price (below equilibrium) → shortage; a minimum (above) → surplus. Government failure = the cure makes things worse.

Practice

3.1 State the effect of an **indirect tax** on (a) supply and (b) the price of a good. [2]

3.2 State **one** type of good a government would **subsidise**, and why. [2]

3.3 A government sets a **maximum** price below equilibrium. State what this causes. [1]

3.4 A government sets a **minimum** price above equilibrium. State what this causes. [1]

3.5 Give **one** example of government failure. [2]

3.6 Challenge. A government puts a high tax on cigarettes. Explain how the tax reduces the quantity bought, and one reason it might still fail to cut smoking much. [2]