The mixed economy and externalities

Edexcel IGCSE Economics 4EC1 sections 1.1.5-1.1.6 full package

Topic 3 at a glance

> Markets and the state share the work; where markets fail, the state steps in.

- 4EC1 spec sections 1.1.5 and 1.1.6.
- The externality diagram reuses the shared market model.

Private and public sectors

Private sector

owned by individuals and firms

aims mostly at profit

Public sector

owned by the state

aims at **welfare** and services

The three questions

> In a mixed economy both market and state answer them.

- Market: prices and profit signal.
- State: health, education, public goods.

Market failure

> When markets misallocate, governments intervene.

- Inefficient allocation of resources.
- Too much or too little against the social optimum.

Public goods and free riders

> No one pays, so no private firm supplies: the state must.

- Non-excludable: no one can be stopped from using it.
- Non-rival: one person's use does not reduce another's.

Privatisation

Group	Effect
consumers	lower prices if efficiency is passed on; higher if a monopoly results
workers	job losses from efficiency drives
businesses	new profit opportunities
government	a one-off sale receipt, then lost dividends

External costs and benefits

External costs	External benefits
pollution	education
congestion	healthcare
environmental damage	vaccinations

Social cost and social benefit

1. **Social cost** private cost + **external cost**
2. **Social benefit** private benefit + **external benefit**
3. **Example** private cost 20 + external cost 6 = social cost 26

Decision

An external cost lifts social cost above private cost.

Over-production, drawn

> The market makes 100; society wants 92: 8 too many.

- MSC $=$ MPC $+$ 6 per unit.
- Label MPC, MSC, MSB and the gap.

Data response: plastic bags

> A 97% fall: 7.6 billion bags became about 228 million.

- 5p charge from October 2015; 10p from May 2021.
- Bags block drains, harm wildlife, last centuries.

Data response: is a charge best?

For the charge	Against
use fell about 97%	5p is not the true cost
cheap: shops collect it	bags for life: more plastic
private cost nearer social	ignores packaging

Check yourself

Question	**Answer**
Two features of a **public good**?	non-excludable, non-rival
Define **privatisation**.	public to private ownership
Social cost =	private + **external cost**
Market vs optimum quantity?	100 vs 92: 8 too many