

**ECONOMICS FOR FINANCE**  
**Chapter 2 Unit 2: Market Failure**

**Questions**

1. Define 'market failure'
2. Why do you think markets are inefficient?
3. Distinguish between demand-side market failure and supply side market failure.
4. What is meant by 'market Power'? How does it cause market failure?
5. Define externalities. Do they reflect in market prices? Why?
6. Define externalities. Why are they considered as a source of market failure?
7. What are the features of externalities?
8. Why do economists use the word 'external' to describe third-party effects that are harmful or beneficial?
9. Distinguish between positive and negative externalities.
10. What do you understand by externalities in consumption?
11. Distinguish between production externalities and consumption externalities
12. Give two examples each of positive and negative consumption externalities
13. Distinguish between unilateral and reciprocal externalities
14. Explain with examples how positive production externalities are received in production and consumption
15. Explain with examples how negative positive production externalities are received in production and consumption
16. Explain with examples how positive consumption production externalities are received in production and consumption
17. Explain with examples how negative consumption are received in production and consumption

18. Explain why environmental pollution is regarded as a source of market failure.
19. How can social costs be differentiated from private cost?
20. Can social costs be less than private costs? Illustrate your answer
21. What is the consequence of a negative externality on price and output? Illustrate your answer
22. How does the presence of positive externality influence price and output?
23. 'The problem of negative production externality though serious, does not usually float up much' Why?
24. Explain the distinction between marginal private cost, marginal external cost and marginal social cost.
25. What are the components of marginal social benefit?
26. When does social cost exceed private cost? Give two examples
27. When does social benefit exceed private benefit? Give two examples
28. Explain the context in which private cost and social cost diverge?
29. Define 'socially optimal output'. How is it achieved?
30. Explain with the help of a diagram how negative production externalities cause loss of social welfare?
31. Explain the concept of 'deadweight loss'
32. Explain, with the aid of examples, the main characteristics of private goods.
33. Explain, with the aid of examples, the main characteristics of public goods.
34. Identify a 'pure public good' using the criteria for identification
35. Identify a 'pure private good' using the criteria for identification
36. Explain 'free rider problem'. Give examples.
37. 'Private goods do not have free rider problem'. Elucidate
38. Explain the rationale behind efficient allocation of resources for the production of private goods.
39. Explain how non excludability in consumption of public goods affects their production?

40. Public goods do not use up extra resources as additional people consume them. Why?
41. 'Private goods conform to the settings of market exchange' explain
42. "Public goods do not conform to the settings of market exchange" Why?
43. What criteria are used to distinguish between pure and impure public goods?
44. Explain the term quasi public goods
45. What is the market outcome for Consumption goods which are rival but not excludable?
46. Describe the term 'Tragedy of Commons'
47. Define common resources. Why are they overused?
48. Discuss the importance of distinguishing between private costs and social costs.
49. Describe, using examples, common access resources
50. Describe the concept of 'Global Public Goods'
51. What are the implications of free rider problem?
52. 'Complete information assumed by perfect competition is a myth' explain
53. Why are health and education not pure public goods?
54. Describe why markets have incentives to produce private goods?
55. Why do markets fail to produce public goods? Illustrate your answer.
56. Distinguish between different types of public goods.
57. Explain, with the aid of examples, the main characteristics of merit goods.
58. Describe the free rider problem associated with public goods. What would be the outcome? Give examples
59. Appraise the role of incomplete information in generating market failure.
60. Define 'Asymmetric information'. What consequence does it have?
61. How does asymmetric information lead to adverse selection?

62. Define Moral Hazard. How is it different from adverse selection?
63. 'Asymmetric information, adverse selection and moral hazard affect the ability of markets to efficiently allocate resources and therefore, lead to market failure' Explain