Introduction to Social Welfare and Efficiency

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What is social welfare?

social welfare $= \sum_{i \in model}$ utility (i)

goal of policy / government maximize social welfare

What is an efficient allocation?

allocation: description of # of goods in model
+ description of what people are doing

efficient allocation. allocation that maximizes
social welfare subject to
tools available in model / structure
of the economy.

Why do we care about efficiency / efficient allocation?

It tells us whether there is a role for

government intervention & policy.

RBC model. always efficient $\rightarrow$ there is
no role for government intervention
$\rightarrow$ there is
no role for monetary policy, fiscal policy.

Matching model: generally inefficient $\rightarrow$ role for
government policy.