



The Benefits and Costs

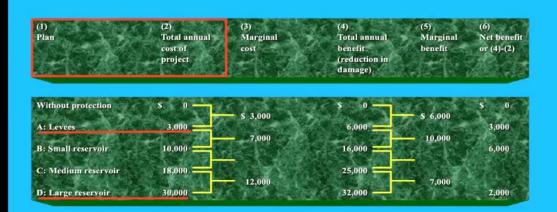
- Benefits: Come from the reduction in damage to the land in the valley in the event of a flood.
- Costs: The loss of satisfaction associated with the accompanying decline in the production of private goods or some other public good.
- Costs can usually be measured simply by the cost of building the project!

The Decision Rule

- Build: If the benefits from the project exceed its costs, we should build the project.
- Don't Build: If the costs exceed the benefits, we should not.

Benefit-Cost Analysis

- Can indicate much more that just whether a public project is worth building.
- It can also help government choose among the best competing alternatives.







Pause the presentation now if you want to do this exercise.



Answer: Compare the marginal cost and the marginal benefit associated with each plan.



Without protection	S 0		\$ 0		S 0 c
A: Levees	3,000	s 3,000	6,000	\$ 6,000	3,000
B: Small reservoir	10,000	7,000	16,000	10,000	6,000
C: Medium reservoir	18,000	9,000	25,000	2,000	7,000
D: Large reservoir	30,000	12,000	32,000	7,000	2,000

Benefit-Cost Analysis

- Shatter the simplistic notion that the best way to make government more efficient is to always reduce government spending
- Key Point: Efficient government does not necessarily mean minimizing public spending.
- Use tools like benefit-cost analysis to efficiently allocate resources between the private and public sectors until no net benefits can be had from further re-allocations of resources.