Public Goods and Publicly Provided Private Goods

WHAT ARE WE TALKING ABOUT TODAY

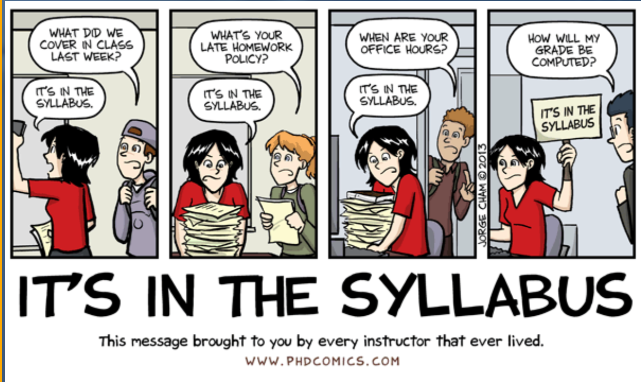
PUBLIC GOODS

PUBLICLY PROVIDED PRIVATE GOODS

DISCLAIMER

This is a new Course, and although I have spent an awful lot of time to develop it, it has not been tested on real students - even worse on real Hult students.

Don’t forget!



Public Goods

Pure and impure

Rival Consumption & Exclusion

To distinguish between private and public goods, we need to ask two basic questions.

i. Does the good have the property of rival consumption?

ii. Is it possible to exclude any individual from the benefits of the good (without incurring great costs)?

Rival consumption means that if a good is used by one person, it cannot be used by another. **Non-rival consumption** refers to cases in which one person's consumption does not detract from or prevents another person's consumption.

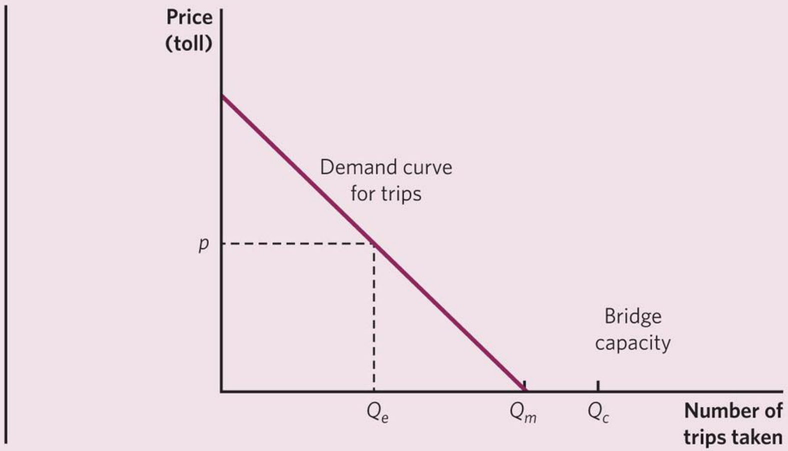
The second question relates to the property of **exclusion**. Can someone be excluded from the consumption of a good. If exclusion is impossible (or too expensive), then the use of price system is impossible because consumers have no incentive to pay the price.

Theocharis Papadopoulos

Underconsumption, undersupply and user fees

If consumption is non rival but exclusion is possible, market might lead to **underconsumption** as the marginal benefit is higher than the marginal cost (zero). But if there is no charge there will be no incentive for supplying the good. In this case, inefficiency takes the form of **undersupply**.

FIGURE 5.1



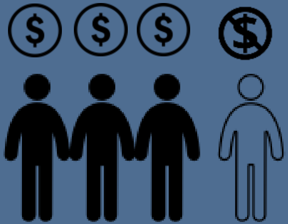
If exclusion is possible, even if consumption is non-rival, governments often charge **user fees** to those who benefit from a publicly provided good or service. For example toll roads, airline ticket tax.

User fees are often thought of as a fairer way of raising revenues, as those who use the public facility the most (and presumably benefit the most) pay the most.

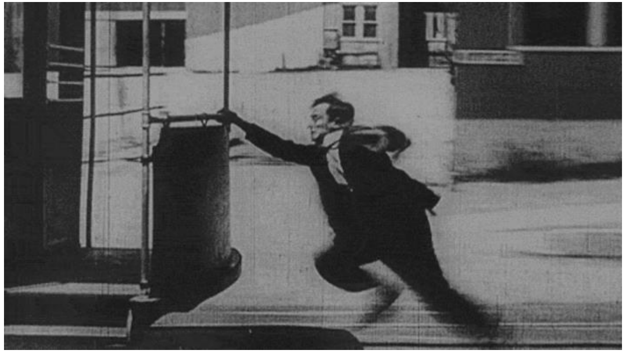
However when consumption is non-rival, user fees introduce and inefficiency.

Free rider problem

When exclusion is not possible individuals are reluctant to contribute voluntarily to the support of public goods. This is known as the **free rider problem**.

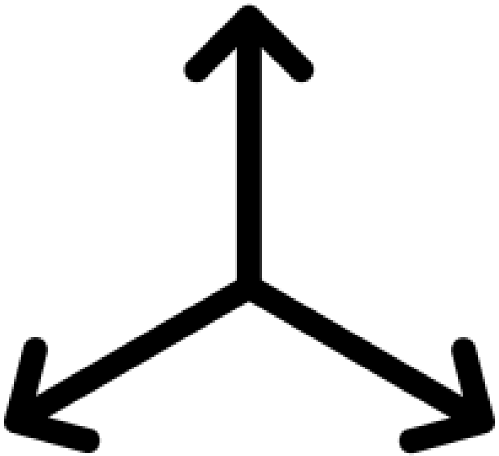


In a few cases non-excludable public goods are provided privately. Usually when there is a large single consumer whose benefit is so large that it pays for him/her to provide it.



Although the “selfish” nature of humanity is in the core of the free rider problem, recent studies in experimental economics have suggested that economists might have overemphasized it.

Spectrum of Goods

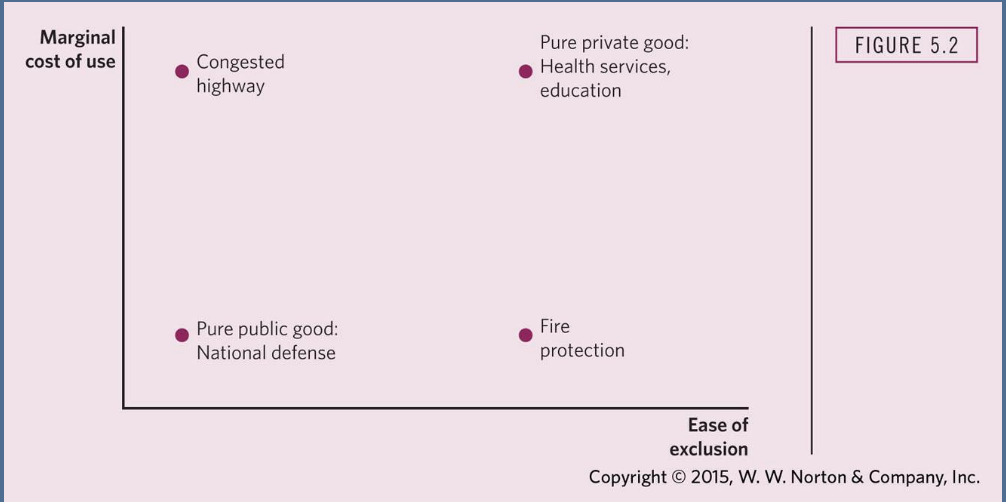


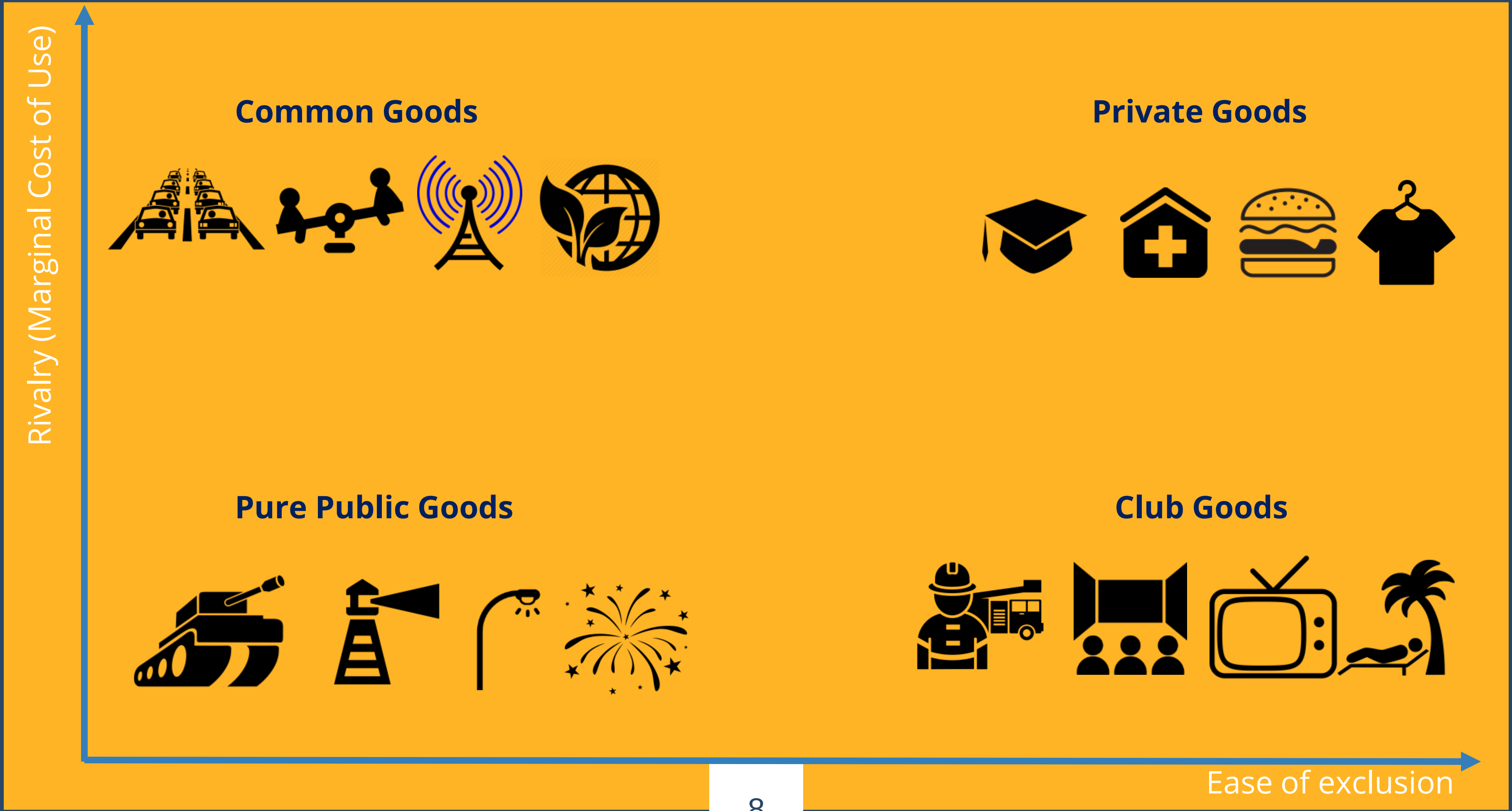
Generally, **private goods** have the properties of rival consumption and excludability.

Goods characterized by non-rival consumption and for which exclusion is impossible are **pure public goods**.

Goods characterized by either non-rival consumption or excludability are **impure public goods**.

- Goods characterized by non-rival consumption and excludability are also known as **club goods**.
- Goods characterized by rival consumption and non-excludability are also known as **common goods**.




Rivalry (Marginal Cost of Use)
Common Goods
Private Goods
Pure Public Goods
Club Goods
Ease of exclusion

Global and Local Public Goods

The benefits of some public goods are enjoyed only locally - by those living in a particular community. These are called **local public goods**.

However more and more public goods are **global public goods**, the benefits of which accrue to anyone in the world. Global environment, global health, global knowledge, and global security are some of them.

Collective Action

Whenever there is a public good, there is need for **collective action**. Within a country, the national government provides for national public goods (e.g. national defence), and local governments provide for local public goods (e.g. street cleaning).

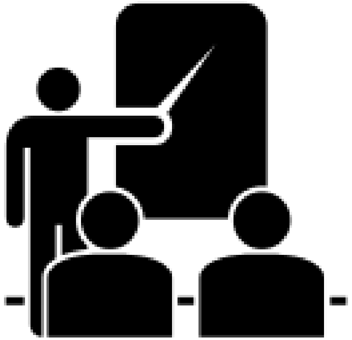
However there is no global government. Still, the international community comes together to address those global public goods, through treaties, agreements and international organizations.

Publicly Provided Private Goods

Private goods provided by the government

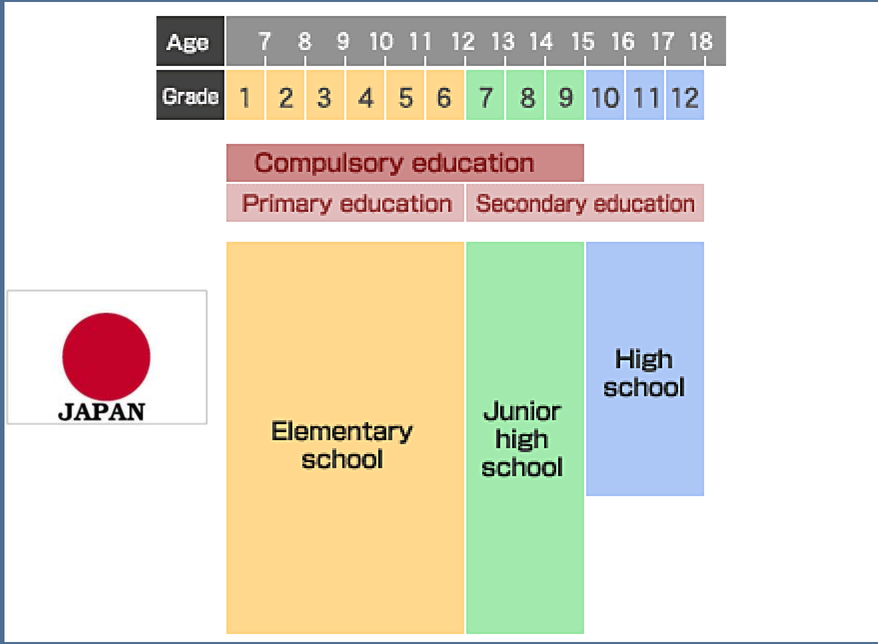
Theocharis Papadopoulos

Publicly Provided Private Goods



Publicly provided goods characterized by large marginal cost associated with supplying additional individuals are referred to as **publicly provided private goods**.

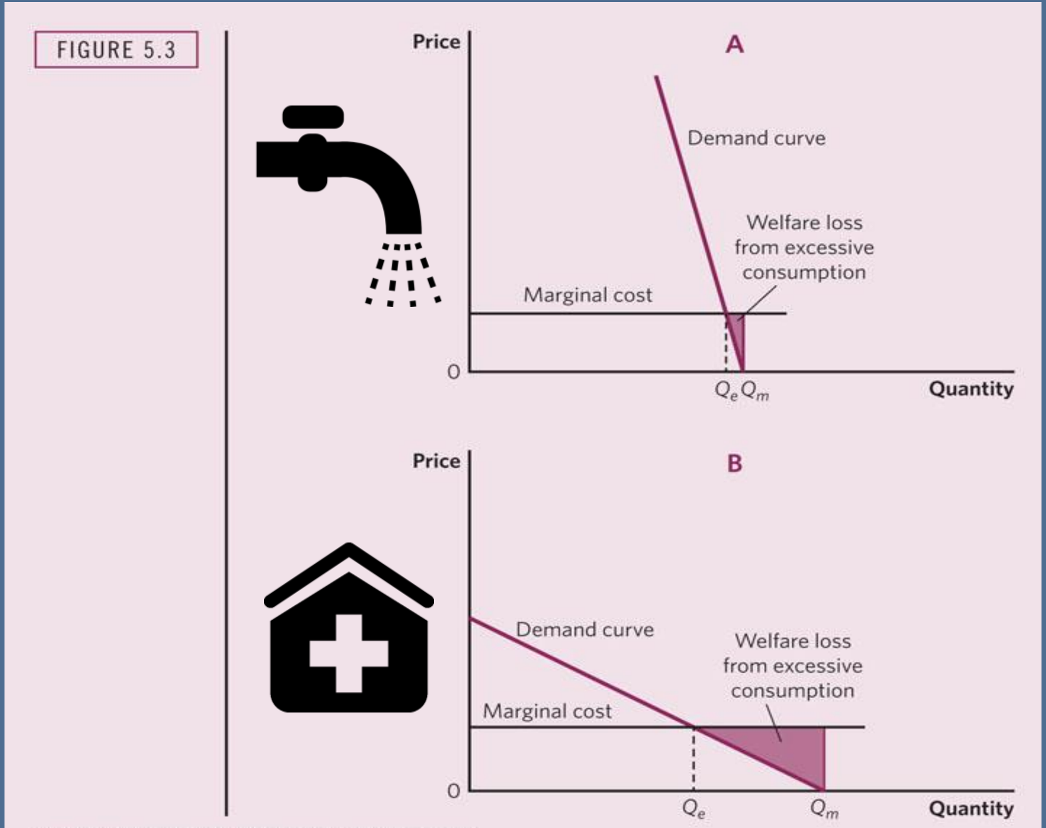
Education is a typical example of publicly provided private good.



Theocharis Papadopoulos

Overconsumption of publicly provided private goods

If a private good is provided freely by the government there is likely to be overconsumption of the good as individuals will keep consuming it until their marginal benefit is equal to zero.



Theocharis Papadopoulos

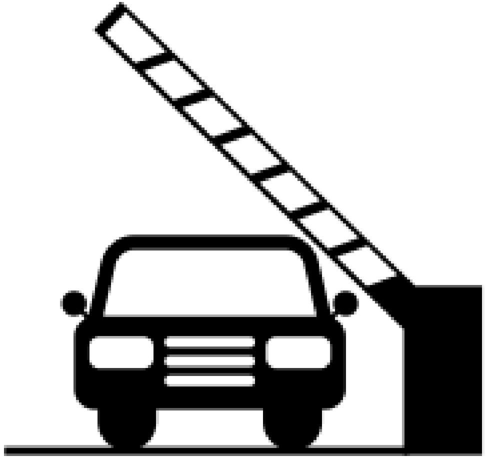
Rationing Publicly Provided Private Goods

Given the inefficiencies arising from overconsumption when no charges are imposed for publicly provided goods, governments often try to limit their consumption. Any method restricting consumption of a good is called a **rationing system**.

There are three main methods of rationing publicly provided goods:

1. User Charges
2. Uniform Provision
3. Queuing

User Charges



Users pay a fee for the good/service.

<u>Advantages</u>

Those who benefit bear the cost

<u>Disadvantages</u>

Results in undercosumption

Administering pricing system adds transaction costs

Theocharis Papadopoulos

Uniform Provision

Governments supplies the same quantity of the service/good to everyone

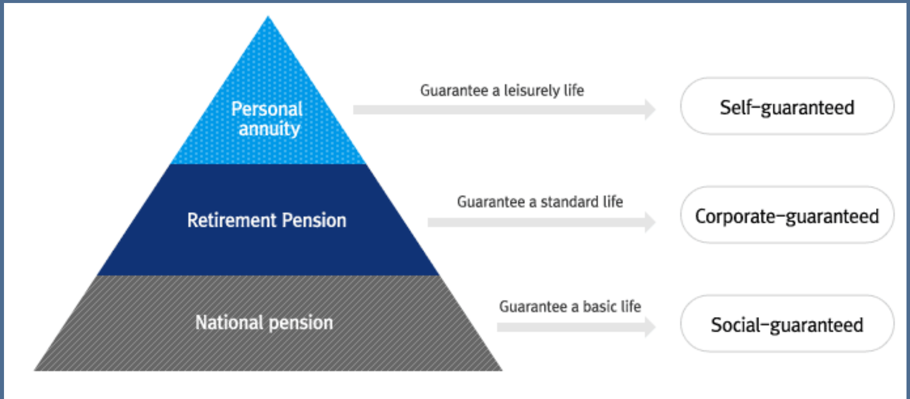
Advantages

Saves on transaction costs

Disadvantages

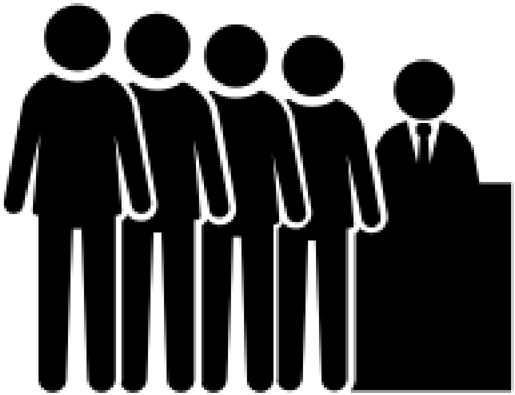
Leads some to overconsume and others to underconsume

High demanders may supplement public consumption, increasing total transaction costs



Theocharis Papadopoulos

Queuing



Rather than charging individuals money for access to publicly provided goods and services, government requires that they pay a cost in waiting time

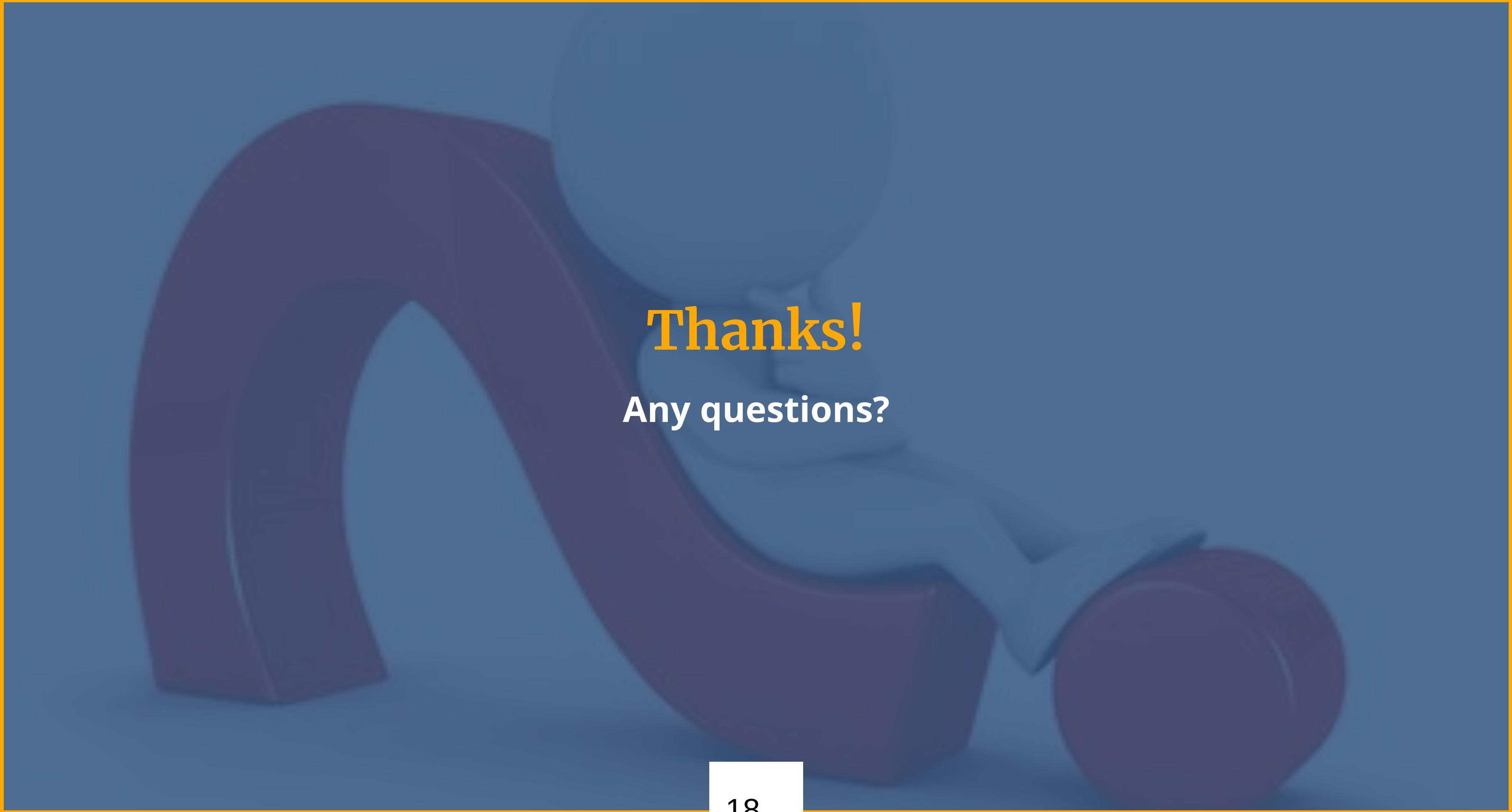
Advantages

Goods (like healthcare) allocated not necessarily on basis of who is wealthiest

Disadvantages

Alternative basis of allocation (who has time to spare) may be undesirable

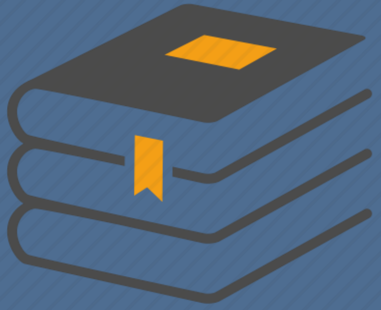
Time is wasted



Thanks!

Any questions?

Bibliography



Stiglitz, J. and J. Rosengard (2015) *Economics of the Public Sector* (4th ed.), W.W. Norton & Company