Figure 13.8 The First Theorem of Welfare Economics
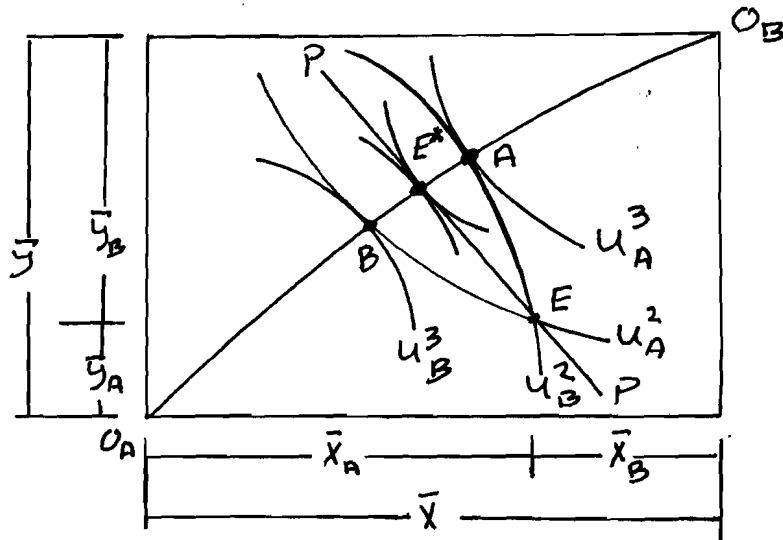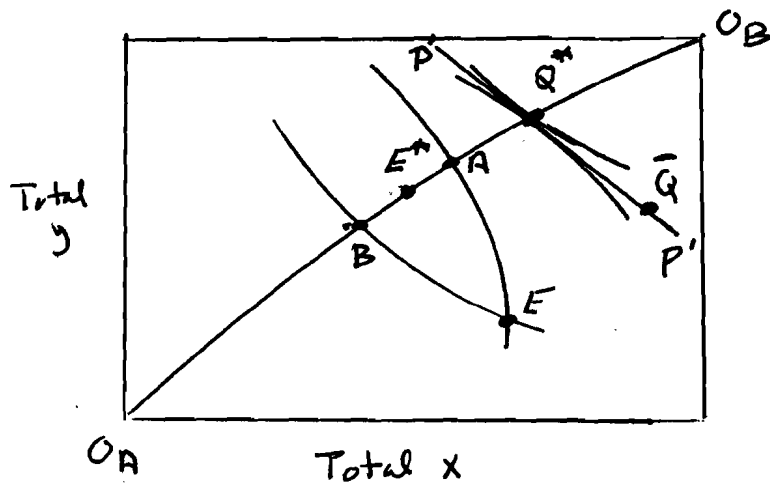

With initial endowments at point E individuals trade along the price line PP until they reach point E*. This equilibrium is Pareto efficient.

Figure 13.9   The Second Theorem of
                 Welfare Economics

If allocation Q^* is regarded

as socially optimal, this allocation

can be supported by any initial

endowments on the price line $P'P'$.

To move from E to, say, $\bar{Q}$ would

require transfers of initial

endowments.

Figure 13.10 Production increases
the number of feasible
allocations.

Quantity of
y

P

y_A ———————— A

x_A Quantity of
x
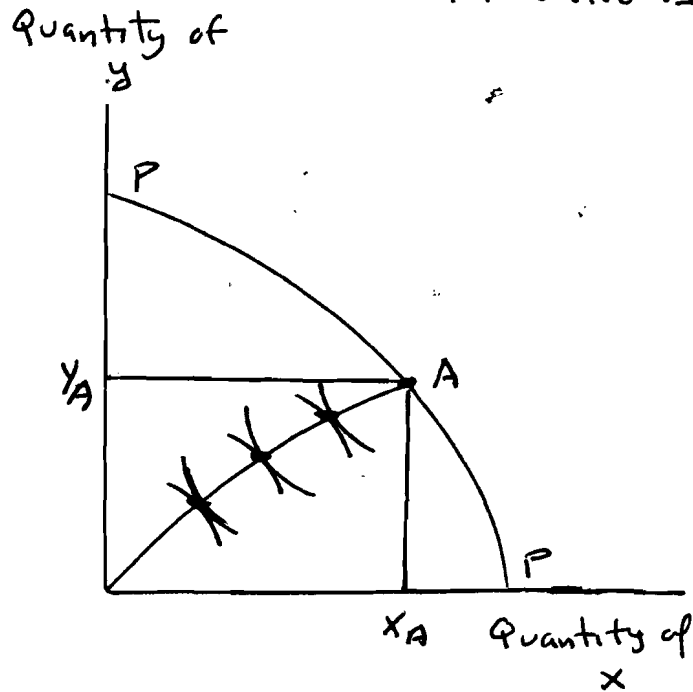
Any point on ~~the~~ the production
possibility frontier PP can
serve as the dimensions of
an Edgeworth exchange Box.