AP Micro Review Unit 6: Market Failure and the Role of Government

TOPIC 6.1: Socially Efficient and Inefficient Market Outcomes & TOPIC 6.2: Externalities

Both 6.1 & 6.2 topics and practice questions are covered in our 6.1 & 6.2 PowerPoint and the **AP Classroom 6.2 Daily Video 2 and 3**

4 Types of Externalities Cheat Sheet

Mr. Clifford can support the PowerPoint if you need it

Mr. Clifford's Negative Externality Video on Cigarettes **(per unit tax example)**

TOPIC 6.3: Public and Private Goods

Define whether goods are rival and/or excludable & Explain how the nature of rival and/ or excludable goods influences the behavior of individuals and groups.

- **Private goods:** Rival in consumption (the same unit of the good cannot be consumed by more than one person at the same time) and excludable (the supplier of that good can prevent people who do not pay from consuming it)
- **Public goods**: Non-rival (more than one person can consume the same unit of the good at the same time) and non-excludable (the supplier cannot prevent consumption by people who do not pay for it)
- Due to the **free rider** problem (when goods are non-excludable so individuals won't pay and free-ride off those who do pay), private individuals usually lack the incentive to produce public goods, leaving the government as the only producer.
- Because of free riders, Governments sometimes choose to produce private goods, such as educational services, and to allow free access to them.
- **Commons resources**: Some natural resources (ocean) are, by their nature, non-excludable (anyone can fish and are open access) and rival (only one person can consume each fish caught). Private individuals inefficiently over consume (over fish) such resources. To fix the “Tragedy of the Commons” Governments can tax or regulate the common resource, use tradable licences for the right to use the resources or make it excludable and assign property rights to it.

TOPIC 6.4: The Effects of Government Intervention in Different Market Structures
90% of 6.4 material was learned in previous units. 6.4 just takes all the information we learned and asks what will happen if the Government intervenes using things like per unit or lump sum taxes, per unit or lump sum subsidies, and price ceilings & price floors. The effect of these policies can be different based on the elasticity of the curves and what market structure we are talking about. Therefore, this is VERY cumulative.

This can be the most overwhelming of all the TOPICS, but you will feel better after watching the 4 AP classroom videos (7 min. each) that cover 6.4. There are lots of practice questions as well and this is by far the best way to prepare for this as it is really a review of much of the material we covered all semester.

Remember, government taxes and subsidies can CREATE market inefficiencies "failures" if the market is in equilibrium but can also fix inefficiencies "failures" if there are externalities.

Define government policy interventions in imperfect markets.
Explain (using graphs where appropriate) how government policies can alter market outcomes in perfectly and imperfectly competitive markets.
Calculate (using data from a graph or table as appropriate) changes in market outcomes resulting from government policies in perfectly competitive and imperfectly competitive markets.

- Per-unit taxes and subsidies affect the total price consumers pay, net price firms receive, equilibrium quantity, consumer and producer surpluses, deadweight loss, and government revenue or cost. The impact of change depends on the price elasticity of demand and supply. Cheat Sheet on Elasticity and who pays the Tax
- Lump-sum taxes and lump-sum subsidies do not change either marginal cost or marginal benefit; only fixed costs will be affected.
- Binding price ceilings and floors affect prices and quantities differently depending on the market structures (perfect competition, monopoly, monopolistic competition, and monopsony) and the price elasticities of supply and demand.
- Government intervention in imperfect markets can increase efficiency if the policy correctly addresses the incentives that led to the market failure.
- Government can use price regulation to address inefficiency due to monopoly.
- A natural monopoly will require a lump sum subsidy to produce at the allocatively efficient quantity, where MC intersects with the demand curve
- Governments use antitrust policy in an attempt to make markets more competitive and reduce the market power held by one firm.

Watch and complete the questions from the 4 AP classroom Videos for 6.4 (7 min. each)
Complete (Lump Sum & Per Unit Past AP FRQs to Practice)

TOPIC 6.5 Inequality

The Lorenz curve and Gini coefficient are used to represent the degree of inequality in distributions and to compare distributions across different countries, policies, or time periods. Tax structures can also lead to increasing or decreasing inequality.
Exclusion: You will not be required to Draw the Lorenz curve OR calculate the Gini coefficients on the AP Exam.

Lorenz curve, Gini coefficient and progressive/regressive taxes Cheat Sheet and Practice Questions

AP Classroom Review Videos 6.5 #1 and 6.5 #2 do a nice job reviewing these topics. *Remember, you don't need to draw the Lorenz curve or calculate the Gini coefficient for the exam, so these should be manageable with a brief review.*