When Markets Can’t be Relied Upon

Video Transcript

As part of their quest to study how humans deal with scarcity, economists have noticed that some goods and services are produced by private enterprises while others are produced by government.

In the United States, which is considered to have a mostly market economy, more than 90 percent of children are educated in public schools, which are owned and operated by government; other countries considered less market-oriented than the United States allow families to choose, and use tax money for, privately-owned schools. Some local governments own all the equipment and directly hire personnel to provide trash service, remove leaves in the fall, and plow roads in the winter; others contract with private companies or allow their residents to directly secure these services.

Economists debate the most appropriate way to provide for certain goods and services. Should government or the market and private enterprise have responsibility? In seeking an answer to this question, economists have focused on whether market incentives can be relied upon to ensure that useful and necessary goods and services will be supplied.

Economists have identified circumstances where markets cannot be relied upon. Think about national defense. It involves training personnel in the use of weapons, providing for those weapons, and prioritizing missions. Every individual within a nation’s boundaries benefits from the security provided by national defense. If a billion dollars is spent on national defense, every person enjoys a billion dollars-worth of national defense. The fact that your neighbor gets a billion dollars of benefit in no way reduces the billion dollars of benefit you enjoy as well. We call this nonrivalrous consumption.

Another fact about national defense is that as long as someone is living in the country being defended, that person cannot be prevented from enjoying that security. No one in a country can be stopped from consuming its national defense. This is called nonexclusive consumption.
Economists refer to goods that are nonrivalrous and nonexclusive in consumption as public goods. And, it makes sense that a public good has to be produced by government. Why? Were a group of civic-minded people to voluntarily provide for national defense, many others would choose not to help pay for it, even though they see the benefit. The result could be that too little national defense would be produced, and might ultimately not be produced at all. National security could be severely compromised if government taxation was not providing for national defense.

Following this logic, national defense is a public good that should be produced by the government. But what of other services that the government currently provides, or is called upon to provide. Do they meet the criteria for being a public good?

About this transcript:

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