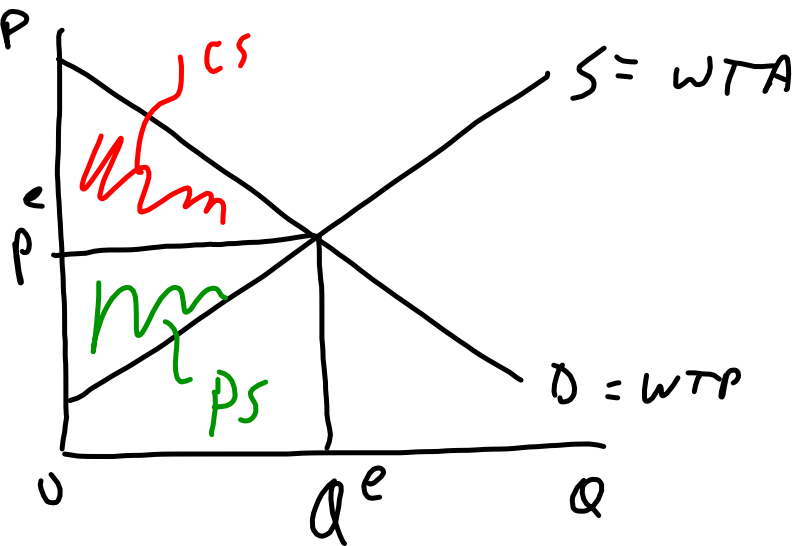


Chapters 7+8 -

markets - allocate resource
maximize efficiency

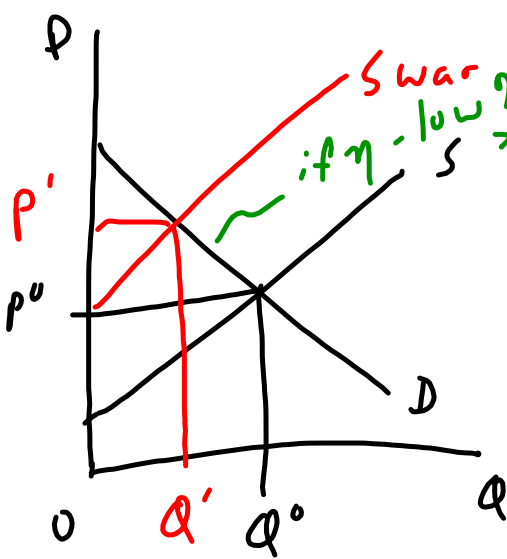
Fig 7 Ch 7

WTP - reflects all D
WTA - reflects all resource cost



Value of a market $\rightarrow PS + CS =$
National Income Accounts $(P^e \cdot Q^e)$

Resource misallocations - examples



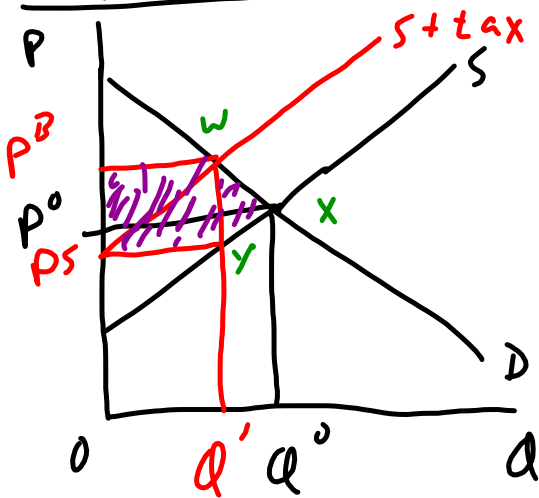
"War on drugs" interdiction & penalties

Becker →
 Expected value of activity (EV)
 States of nature
 Not caught $\pi > 0$
 Caught $F < 0$
 Probability Caught P_c
 Prob. Not Caught $(1 - P_c)$

$$EV = (1 - P_c) \cdot \pi + P_c \cdot F$$

P_c - policy variable & $F \rightarrow EV \downarrow \rightarrow S \downarrow - \pi \uparrow EV \uparrow$

Chapter 8 - Taxation - costs of taxation



- taxes →
 dead weight loss
 (excess burden)
 excise tax - seller
 collect tax at
 sale
 $(P^B - P^S) > 0$ tax wedge

tax revenue $(P^B - P^S) \cdot Q'$

Cost to economy $P^B W X Y P^S$

Diff $W X Y - CS \downarrow P^B W X P^0$
 $P^S \downarrow P^0 X Y P^S$

But $P^B W Y P^S \rightarrow$ transfer to gov't tax revenue

Efficient tax system
 minimize DWL for tax revenue
 ratio $\frac{DWL}{\text{Tax Revenue}}$

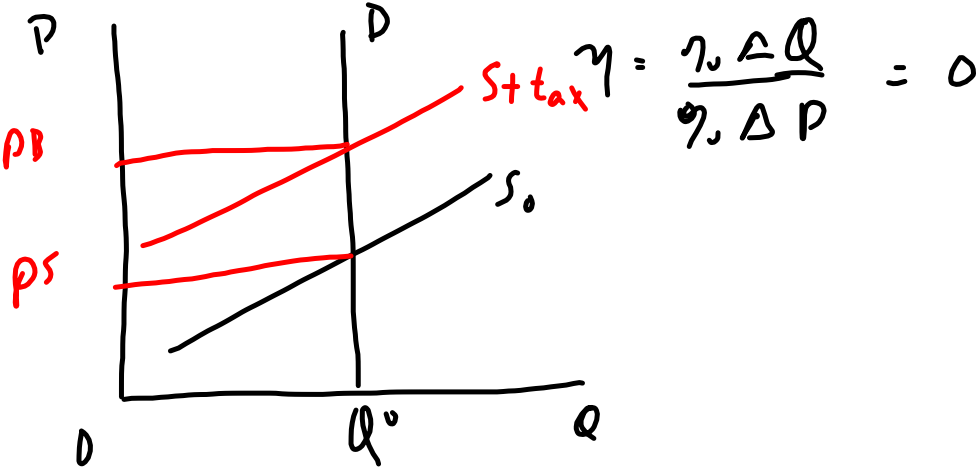
Tax inelastic Demand $\eta = \frac{\% \Delta Q}{\% \Delta P}$
 $\eta < 1 \quad \% \Delta Q < \% \Delta P$ \rightarrow tax added
 so $P \uparrow$

example
 2 goods $i + j$

$$\frac{t_i}{t_j} = \frac{\eta_j}{\eta_i}$$

- tax inelastic good
 more
 inverse elasticity

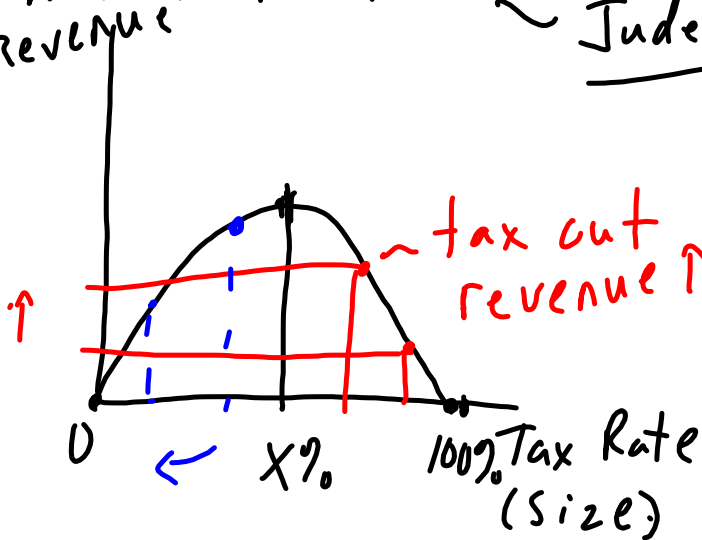
Rule Ramsey Rule
 Frank Ramsey 1920s



"Taxes are bad" → lower taxes
economy grow

Reaganomics early 1980s
trickle down. → taxes on wealthy
- spend more & trickle down.

Arthur Laffer ~ Jude Wanniski



Stuart -
Sweden
1970
 $x \approx 60\%$