Taxation and Government Intervention

Chapter 7-1

Laugher Curve

Two economists meet on the street.

Q. How's your wife?

A. Relative to what?

Producer and Consumer Surplus

- ***Consumer surplus*** – the value the consumer gets from buying a product less its price.
- It is the area underneath the demand curve and above the price an individual pays.

Producer and Consumer Surplus

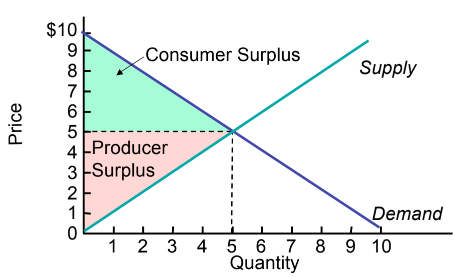
- ***Producer surplus*** **–** the value the producer sells a product for less the cost of producing it.

- It is the area above the supply curve but below the price the producer receives.

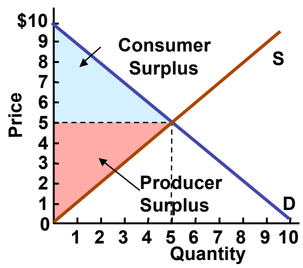
Producer and Consumer Surplus

- The combination of consumer and producer surplus is as large as it can be at market equilibrium.

Producer and Consumer Surplus



Producer and Consumer Surplus



CS = ½(5x5) = 12.5 = Area of blue triangle

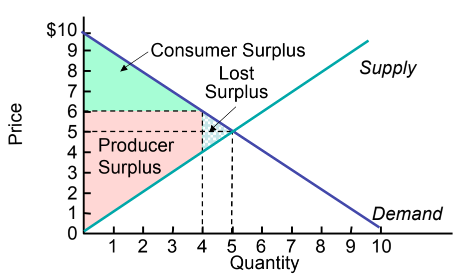
PS = ½(5x5) = 12.5 = Area of red triangle

The combination of producer and consumer surplus is maximized at market equilibrium.

Producer and Consumer Surplus

- The combined consumer and producer surplus falls when price is above market equilibrium.

Producer and Consumer Surplus



Producer and Consumer Surplus