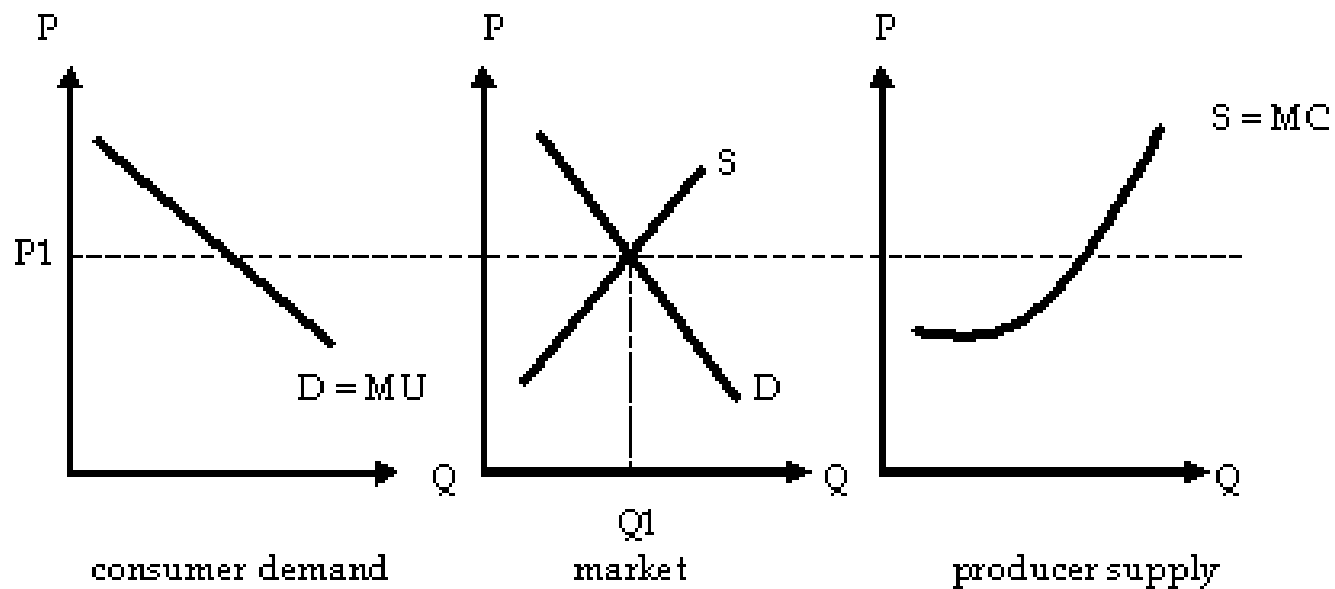


The market can be seen as a group of economic agents, business organizations and individuals who interact with each other in a buyer-seller relationship.

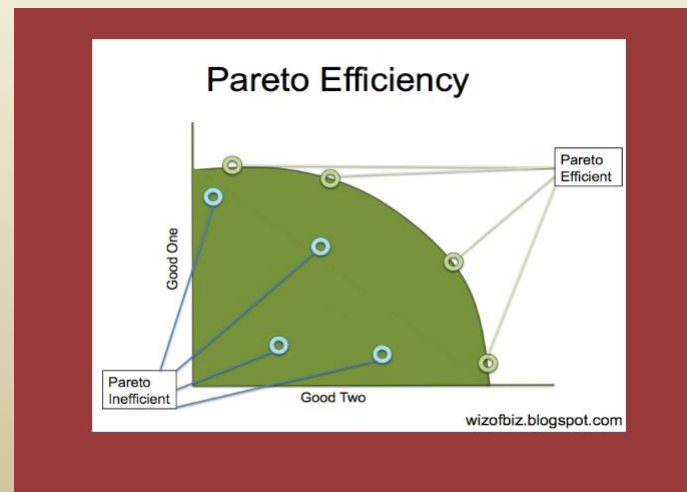


Efficiency occurs when producers provide consumers with the most desired commodities given the resources that are available and the state of technology available in a society.

By extension the market is efficient, or Pareto-efficient when at a given price P the additional cost for producing a product/service is equal to the additional satisfaction for consuming this product/service.

That is where:

$$\underline{MC = MU}$$



Why?

With a fall in the price, the ensuing increase in the quantity demanded reduces MU and increases MC; so neither the consumers nor the producers will agree on a lower price, and vice versa.

In other words, efficient markets are those where the consumer and producer equilibria are matched.

Firms belonging to efficient markets are said to be perfectly competitive as they supply a market concurrently i.e. there is no competition in the sense of rivalry, while maximizing profits where $MR = MC$

Pareto efficient markets are in a state of equilibrium which is is:

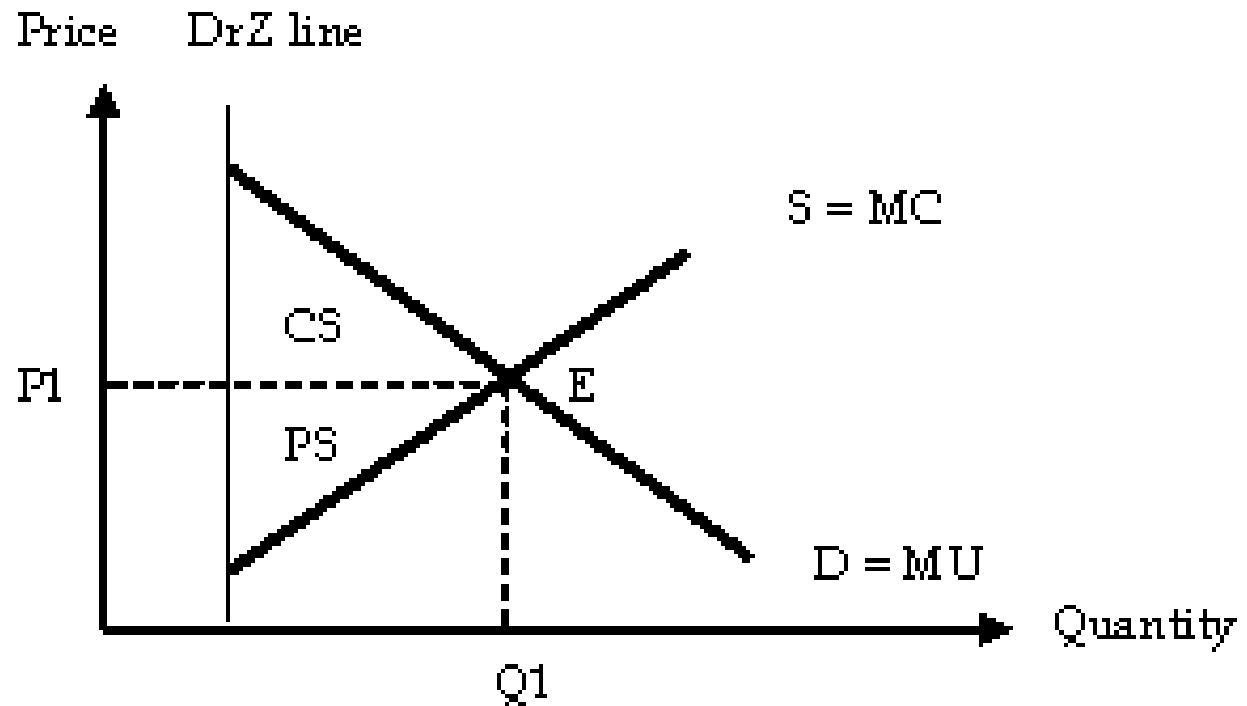
1. Conditional: only when $QD = QS$ can there be price that satisfies both consumers (maximize utility) and suppliers (maximize revenue). That is the equilibrium is the point where $MU = MR$ (for the business organization this point is where $MR = MC$ since the MR curve represents the demand for a product)
2. Temporary: if the conditions determining demand and supply are changed, the equilibrium is upset leading to changes in demand and supply in such a way so as to restore the equilibrium – a *reminder of the laws of thermodynamics! But is it so?*

3. Clearing: there are no shortages of surpluses: everything that has been produced is consumed (and everything the consumers desire has been produced). *But is it so?*
4. Equalizing: that consumer surplus utility (CS) (i.e. the difference between the price paid in the market and the higher price one is ready to pay) and producer surplus utility (PS) (i.e. the difference between the price obtained in the market and the lower price paid to utilize factors of production) are equal.

Efficient markets are ideal markets as they ensure the perfect allocation of resources in the microcircuit

At equilibrium E where $Q_1 = Q_D = Q_S$ holds at price P_1 , $CS = PS$; a Pareto efficient market is absolutely equalizing – *one of the most entrenched and enduring utopian theories!*

DrZ Line:
min
quantity
consumed
/produced



Pareto efficiency means this: envision the situation where you have ordered a pizza at a price that maximizes your satisfaction (consumer equilibrium), that the restaurant has made it with no waste or pollution whatsoever and paid the expected salaries (producer equilibrium), and that you have eaten your pizza, left no crumbs, the plate is clean and your dog is happy!

But is it so?

The question has to be tackled from 2 angles

1: are such ideal markets desirable?

2: are such markets feasible?

Desirability

Yes; anti-trust laws are a prime example of efforts to render markets ideally competitive. The premise is that markets are not as efficient as they should be and thus the state should intervene.

Feasibility

No; the reality of things is that perfectly competitive markets are what they are: an ideal. The reason why they are unfeasible is that human beings that conduct business are in to make money with little regard for other firms (thus seek larger market share) and consumers (thus seek to impose high prices).