Intermediate Microeconomics

Part I: Welfare Economics

INTRODUCTION

Lecturer: Ivan Mitrouchev

Université de Strasbourg

Fall 2021

DEFINITION

▶ What is **welfare economics**? A contemporary definition:

"Welfare economics is the part of economics that deals with evaluating states of the world and formulating recommendations for policies that would improve the well-being of society as a whole. It covers not only a body of policy advice but, arguably more important, a body of principles on which such evaluations and recommendations should be based."

(Backhouse, Baujard and Nishizawa 2020)

▶ From a standard approach, welfare economics is a part of **microeconomics**
  ▶ from *individual* to *social* welfare:
    ▶ Preference $\implies$ utility $\implies$ individual welfare $\implies$ social welfare

DEFINITION
○

POSITIVE/NORMATIVE ECONOMICS
●○

LEARNING OUTCOMES
○

REFERENCES
○○

ASSESSMENTS
○○

INFORMATION
○○

THE POSITIVE/NORMATIVE DISTINCTION IN ECONOMICS

So far, you have been familiar with *positive* (or *descriptive*) economics:

► *Consumer theory*: how individuals choose their consumption bundles (the ones which maximise their utility subject to their budget constraint)

► *Producer theory*: how firms choose their level of production (the one which maximises their profit)

► *General equilibrium*: how prices are formed on the market (supply and demand)

The goal was to describe how (theoretically speaking) the market works.

Now a natural question which follows is:

► *Is it a good thing* that individuals and firms behave this way?

► Or, is the market "efficient"?

This is the subject matter of *normative* economics **(what this course is about)**.

THE POSITIVE/NORMATIVE DISTINCTION IN ECONOMICS

- ▶ *Positive* economics: what *is*. Examples:
    - ▶ Why is it difficult to find a taxi on a rainy day in New-York?
    - ▶ What is the relationship between inflation and unemployment?
    - ▶ What are the conditions under which a general equilibrium can be reached?
    - ▶ Etc.

- ▶ *Normative* economics: what *should be*. Examples:
    - ▶ Should inequalities be reduced, and if so, why?
    - ▶ Is the market efficient, and according to what criterion?
    - ▶ Is it a "good thing" to legalise cannabis?
    - ▶ Etc.

While *positive* economics is about either theoretical or empirical results, *normative* economics is about theoretical results that are derived from some principles that should be accepted (e.g. "efficiency is a good thing").

Typically, how do we define what is best for society? This does not involve judgements of *fact* but judgements of *value*.

LEARNING OUTCOMES OF THIS COURSE

- Introduce the analytical methods of (micro-)economics in order to assess individual and social well-being

- An introduction to the main results of welfare economics
  - The two theorems of welfare economics
  - Some problems of aggregating individual preferences
  - Some problems of externalities

REFERENCE: OUR TEXTBOOK

▶ Hal R. VARIAN (2014), Intermediate Microeconomics: A Modern Approach, WW Norton & Co., 9th edition (available on Moodle)

▶ **Readings:**

- ▶ **Session 1:**
  - ▶ Chapter 3 (Preferences)
  - ▶ Chapter 4 (Utility)
- ▶ **Sessions 2 and 3:**
  - ▶ Chapter 32 (Exchange)
- ▶ **Session 4:**
  - ▶ Chapter 34 (Welfare)
- ▶ **Session 5:**
  - ▶ Chapter 35 (Externalities)

ADDITIONAL REFERENCES

During the sessions, I provide additional references (in blue) that we will not have time to cover in this course, for example:

▶ Materials on the foundations of welfare economics

▶ Alternative measures of well-being

▶ Some contemporary debates in welfare economics

▶ And more...

These readings are *optional*.

If you want to have a broader knowledge than what is covered in Varian (2014), you are more than welcome to read the additional references!

All these references can be found on the Moodle page of this course.

TALKS

Sessions 6 and 7 are devoted to talks about a topic of your choice related to welfare economics.

The idea is that you give talks about what we will not have time to cover in this course, because such a content is extremely broad and can lead to very insightful discussions.

Here are some suggested topics (but you can propose your own):

▶ "Happiness measurement"
▶ "Ordinal *versus* cardinal utility"
▶ "Inequalities and redistribution"
▶ "Voting paradoxes"
▶ "Welfare economics and ethics"
▶ "The tragedy of the commons"

The grade of the talk is common to the group

▶ Weight: 25%

WRITTEN EXAM

Session 8 is devoted to a one-hour written exam

- ▶ Save the date: the 24/11/2021 from 3:00PM to 4:00PM
- ▶ Based on everything we will cover during this course
- ▶ Weight: 25%

The other 50% grade is covered by Mr Munier's Part II of this course (that will take place in December)

INFORMATION

- ▶ I put the lecture slides on Moodle **only after** I cover the content in class
- ▶ So you may take additional notes that are not included in the slides (comments, explanations of calculus and of graphs, etc.)
- ▶ Questions about the course: mitrouchev@unistra.fr
- ▶ Office: A322 (*please send me an e-mail if you want to arrange an appointment*)

Questions? Let's start!

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