## Contents

**Preface** x
**Preface to earlier book** xii

**PART A THE METHODOLOGY OF MICROECONOMIC POLICY**

1 How do economists approach microeconomic policy? 3
   1.1 Introduction: Microeconomics versus macroeconomics 3
   1.2 The scope of microeconomics 5
   1.3 Controversy and the methodology of microeconomic policy 9
   1.4 Conclusion 13
   Reading and references 14
   Questions for review and discussion 14

2 Why do governments need microeconomic policies? 16
   2.1 Introduction 16
   2.2 Nature of microeconomics and policy 18
   2.3 Aims or objectives of microeconomic policy and the role of an economic adviser 20
   2.4 General microeconomic policies for attaining objectives 33
   2.5 The ideal and the politically attainable 40
   2.6 Concluding comments 41
   Reading and references 41
   Questions for review and discussion 42

3 Relevance to business management of microeconomics and microeconomic policy 44
   3.1 Introduction 44
   3.2 The relevance to business management of different approaches to microeconomics 45
   3.3 Business management and the choice of microeconomic perspectives 54
   3.4 The relevance to business management of knowledge about microeconomic policy 55
   3.5 Concluding comments 56
   Reading and references 56
   Questions for review and discussion 57
PART B DEMAND, SUPPLY, MARKETS AND POLICY

4 Competitive markets and price regulation 61
   4.1 Introduction 61
   4.2 Why does the state regulate competitive markets? 64
   4.3 Price regulation in product markets: Some examples 68
   4.4 Price regulation in factor markets: Some examples 80
   4.5 Price regulation in international markets: Some examples 82
   4.6 Concluding comments 89
Reading and references 89
Questions for review and discussion 89

5 Consumers and policy 91
   5.1 Introduction 91
   5.2 Predictive accuracy and testing of demand theory 91
   5.3 Consumer welfare: How is it to be taken into account? 99
   5.4 Market failure, imperfections and consumer protection 106
   5.5 Elasticities of demand and policy 117
   5.6 Conclusion 122
Reading and references 122
Questions for review and discussion 123

6 Costs, supply and policy 125
   6.1 Introduction and overview 125
   6.2 Cost as an operational concept 126
   6.3 The nature of short-run and long-run cost and supply curves 136
   6.4 Learning, externalities and policy 144
   6.5 Market transaction costs and market extension as a source of cost reductions 149
   6.6 Concluding comments 151
Reading and references 152
Questions for review and discussion 153

PART C IMPERFECT MARKETS

7 The behaviour of firms 157
   7.1 Introduction 157
   7.2 The development of theories of the firm 158
   7.3 Why do firms exist? 162
   7.4 Alternative models of firm behaviour 165
   7.5 Policy applications 172
   7.6 Industrial policy 182
   7.7 Conclusion 187
Reading and references 188
Questions for review and discussion 189
## Contents

### 8 Monopoly: Consequences, regulation and prevention
8.1 Introduction 190
8.2 The nature of monopoly 191
8.3 Behaviour of monopolists and its consequences given no entry and the traditional profit-maximizing model 195
8.4 Monopoly behaviour taking potential entry into account 202
8.5 Public action to regulate and prevent monopolies 207
8.6 Private versus public monopolies 210
8.7 Empirical evidence on the impacts of monopoly 212
8.8 Price discrimination and bundling 214
8.9 Conclusion 219
Reading and references 220
Questions for review and discussion 221

### 9 Oligopoly and policy-making
9.1 Introduction 223
9.2 Modelling oligopolistic behaviour 224
9.3 Advertising and oligopoly 231
9.4 Product differentiation 237
9.5 Technical progress and innovation as a competitive strategy 242
9.6 Institutional aspects of oligopoly and of industrial societies 247
9.7 Concluding comments 250
Reading and references 251
Questions for review and discussion 252

### 10 Ownership of enterprises: Public or private?
10.1 Introduction: Does ownership matter? 254
10.2 Public ownership or nationalization 255
10.3 Private ownership 257
10.4 Conclusion 265
Reading and references 265
Questions for review and discussion 266

### PART D FACTOR MARKETS AND POLICY

### 11 Labour markets
11.1 Introduction: The scope of manpower policy 269
11.2 The functions and achievements of labour markets 269
11.3 The competitive labour market 271
11.4 The economics of information 276
11.5 Unemployment 281
11.6 Labour market legislation 284
11.7 Military personnel 288
11.8 Conclusion 291
Reading and references 291
Questions for review and discussion 291
<table>
<thead>
<tr>
<th>Chapter</th>
<th>Title</th>
<th>Page</th>
</tr>
</thead>
<tbody>
<tr>
<td>12</td>
<td>Human capital and social policy</td>
<td>293</td>
</tr>
<tr>
<td>12.1</td>
<td>Introduction: The scope of human capital theory</td>
<td>293</td>
</tr>
<tr>
<td>12.2</td>
<td>Human capital, the life-cycle and social policy</td>
<td>294</td>
</tr>
<tr>
<td>12.3</td>
<td>Income distribution and human capital theory</td>
<td>298</td>
</tr>
<tr>
<td>12.4</td>
<td>Training markets: How are skills obtained?</td>
<td>300</td>
</tr>
<tr>
<td>12.5</td>
<td>Finance for human investments: Can individuals borrow for human</td>
<td>304</td>
</tr>
<tr>
<td></td>
<td>investments?</td>
<td></td>
</tr>
<tr>
<td></td>
<td>The predictions of human capital theory: What are its implications</td>
<td>306</td>
</tr>
<tr>
<td></td>
<td>for training policy?</td>
<td></td>
</tr>
<tr>
<td>12.6</td>
<td>Conclusion: Has human capital theory been successful?</td>
<td>310</td>
</tr>
<tr>
<td>Reading and references</td>
<td></td>
<td>311</td>
</tr>
<tr>
<td>Questions for review and discussion</td>
<td></td>
<td>311</td>
</tr>
<tr>
<td>13</td>
<td>Trade unions</td>
<td>313</td>
</tr>
<tr>
<td>13.1</td>
<td>Introduction: What is the problem?</td>
<td>313</td>
</tr>
<tr>
<td>13.2</td>
<td>Why do unions exist?</td>
<td>314</td>
</tr>
<tr>
<td>13.3</td>
<td>The objectives of unions and professional associations</td>
<td>322</td>
</tr>
<tr>
<td>13.4</td>
<td>Unions as monopolies</td>
<td>323</td>
</tr>
<tr>
<td>13.5</td>
<td>Union bargaining and constraints</td>
<td>325</td>
</tr>
<tr>
<td>13.6</td>
<td>Unions: Restrictive labour practices and efficiency</td>
<td>330</td>
</tr>
<tr>
<td>13.7</td>
<td>Conclusion: Is there a need for government intervention?</td>
<td>333</td>
</tr>
<tr>
<td>Reading and references</td>
<td></td>
<td>335</td>
</tr>
<tr>
<td>Questions for review and discussion</td>
<td></td>
<td>335</td>
</tr>
<tr>
<td>PART E</td>
<td>PUBLIC CHOICE</td>
<td></td>
</tr>
<tr>
<td>14</td>
<td>Do votes determine policies? A public choice perspective on policy</td>
<td>339</td>
</tr>
<tr>
<td>14.1</td>
<td>Introduction</td>
<td>339</td>
</tr>
<tr>
<td>14.2</td>
<td>A taxonomy</td>
<td>340</td>
</tr>
<tr>
<td>14.3</td>
<td>The performance of political markets</td>
<td>344</td>
</tr>
<tr>
<td>14.4</td>
<td>Economic models of politics</td>
<td>346</td>
</tr>
<tr>
<td>14.5</td>
<td>Economic models of bureaucracy</td>
<td>351</td>
</tr>
<tr>
<td>14.6</td>
<td>The optimum size of the public sector</td>
<td>358</td>
</tr>
<tr>
<td>14.7</td>
<td>Economic models of bureaucracy and the size of the public sector</td>
<td>364</td>
</tr>
<tr>
<td>14.8</td>
<td>Improving efficiency within the public sector</td>
<td>367</td>
</tr>
<tr>
<td>14.9</td>
<td>Methods of controlling bureaucracies</td>
<td>369</td>
</tr>
<tr>
<td>14.10</td>
<td>Conclusion: Votes, policy and methodology</td>
<td>370</td>
</tr>
<tr>
<td>Reading and references</td>
<td></td>
<td>371</td>
</tr>
<tr>
<td>Questions for review and discussion</td>
<td></td>
<td>372</td>
</tr>
<tr>
<td>15</td>
<td>The contract state</td>
<td>373</td>
</tr>
<tr>
<td>15.1</td>
<td>Introduction: Controversy and the choice set</td>
<td>373</td>
</tr>
<tr>
<td>15.2</td>
<td>The scope of public procurement policy: Some difficulties of</td>
<td>374</td>
</tr>
<tr>
<td></td>
<td>definition</td>
<td></td>
</tr>
<tr>
<td>15.3</td>
<td>Policy objectives: What are the aims of government procurement policy?</td>
<td>378</td>
</tr>
</tbody>
</table>