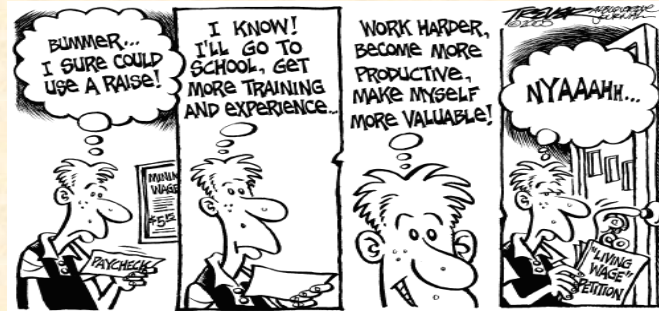


Chapter 6: Price Controls



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Homer versus the 18th Amendment

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Do you think it is a good idea for governments to control prices?

- A) Yes, controlling prices is an essential function of governments
- B) Yes, but only under extraordinary circumstances
- C) No, markets control prices more effectively than governments
- D) No, the government should not intervene in the economy

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Price Controls

- Prices move towards equilibrium in free markets.
- The market will eventually
- Price controls: government-mandated maximum () or minimum () prices.

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Price Ceilings

- Price ceiling: legally established price for a good or service, e.g. rent control.

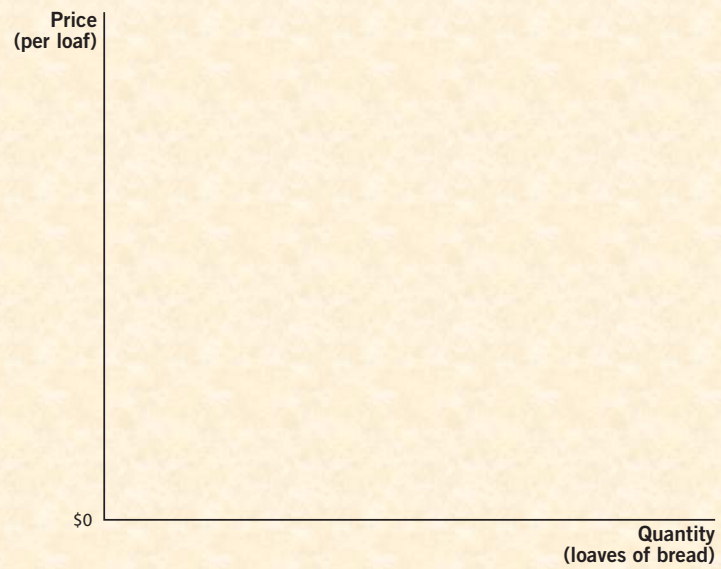
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Recent Price Controls

- Often imposed during war.
- Unintended consequence:
 - Often lead to the creation of markets
- Other ways to circumvent price controls:
 - Reduce the

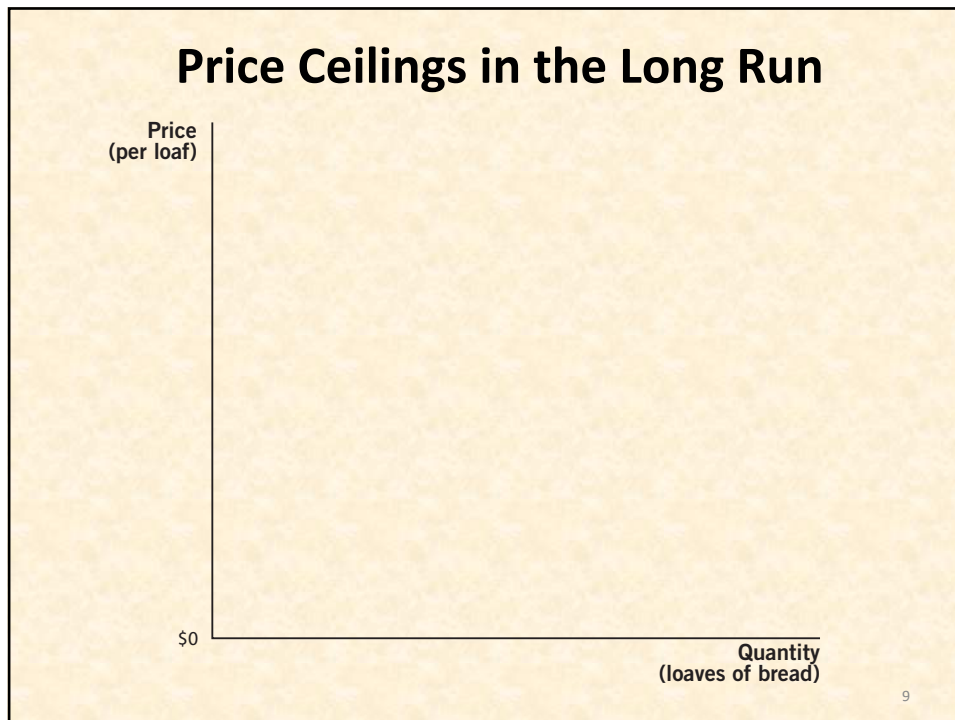
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Nonbinding Price Ceiling



Binding Price Ceiling





Price Ceilings: A Thought Experiment

- Suppose that legislation was passed that placed a 50 cent price ceiling on each
- What can we learn from this?

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Review Question: Price Ceiling on Bread

Question	Explanation
Will there be more or less bread for sale?	
Will the size of a typical loaf change?	
Will the quality change?	
Will the opportunity cost of finding bread change?	
Would you buy illegal bread if you could?	

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What Effects Do Price Ceilings Have on Economic Activity?

- Two real-world examples:
 - Rent control and price gouging

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Over half a million now waiting for apartments in Stockholm

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Poll Everywhere Question 2

- In times of national disaster, many suppliers take advantage of the situation by increasing the price of necessities in shortage, e.g. food, water, power & gas. This is known as price gouging. What is the appropriate government response?
- A) Price gouging should be illegal. The government should use price controls to ensure that all citizens have access to necessities.
- B) Allow price gouging to continue. Higher prices will give producers an incentive to increase supply of necessities

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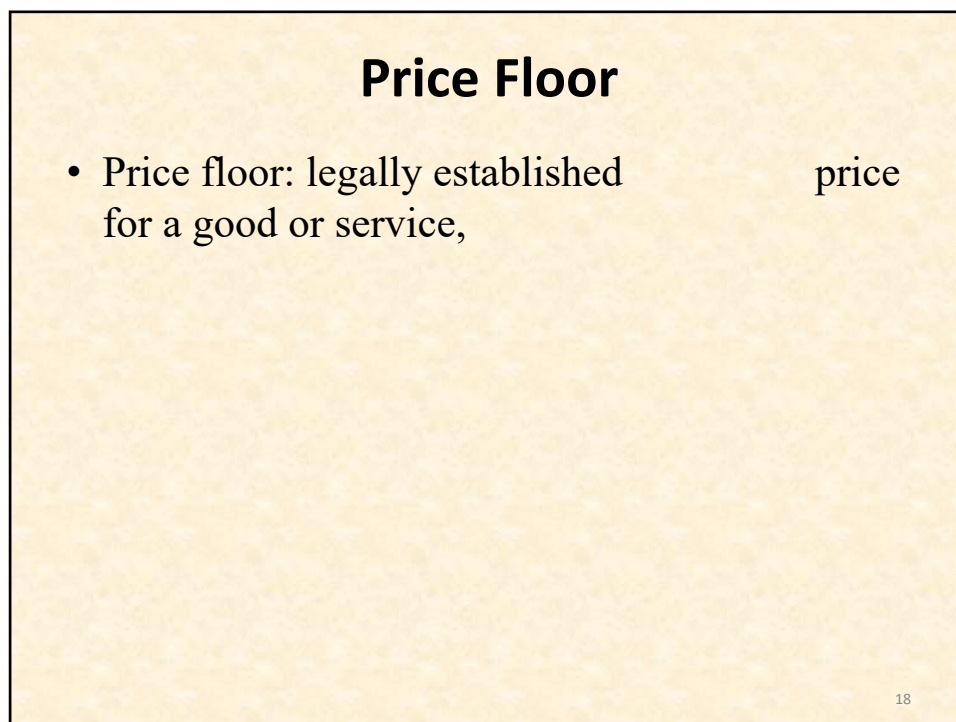
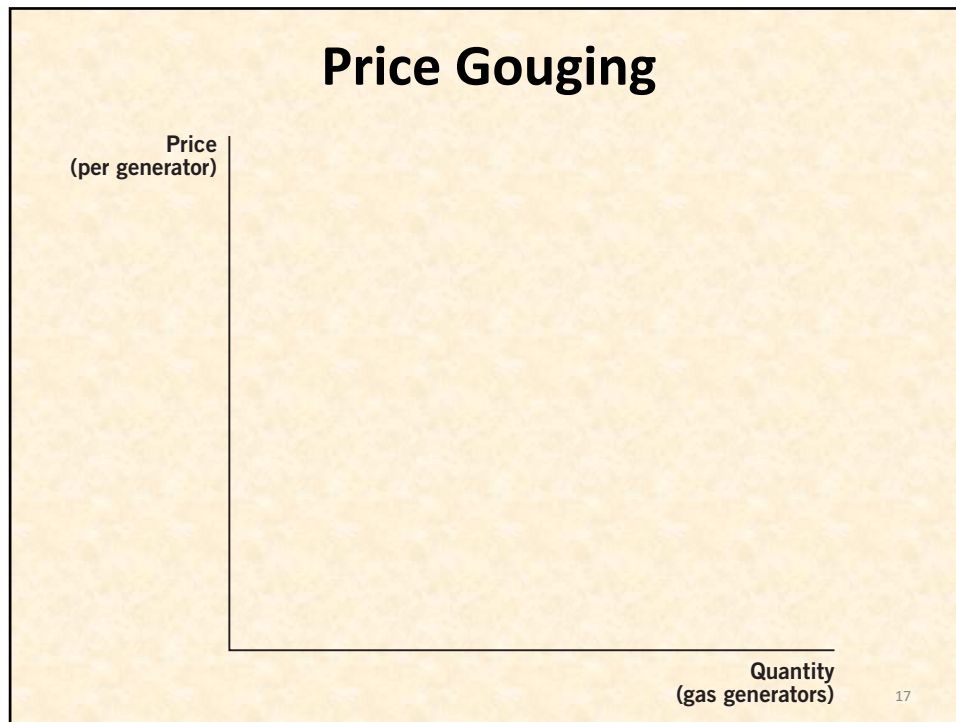
Price Gouging in The News

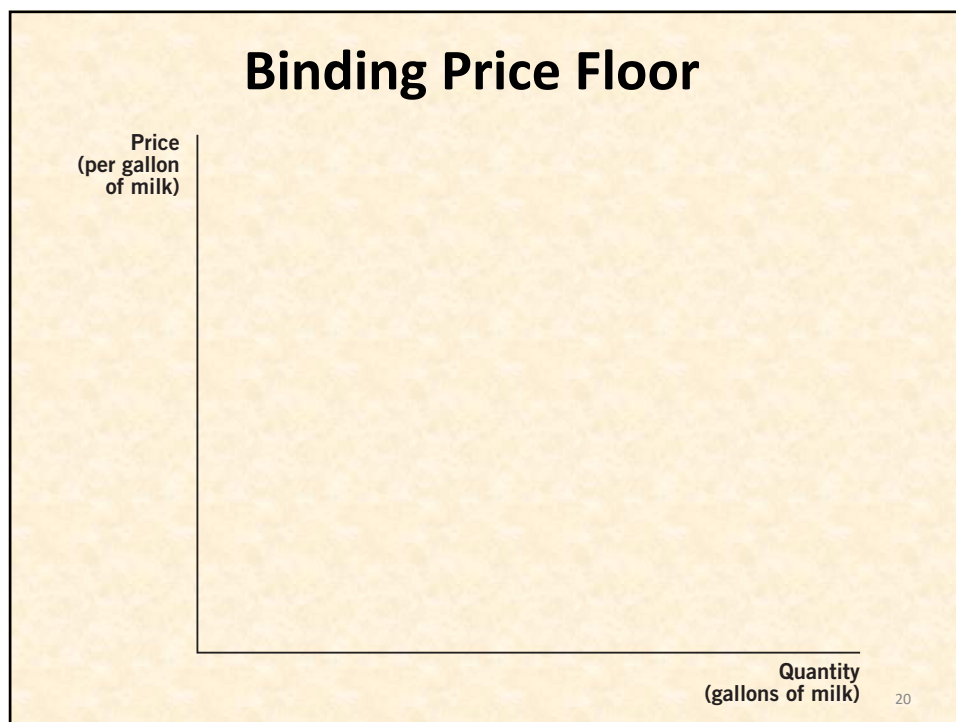
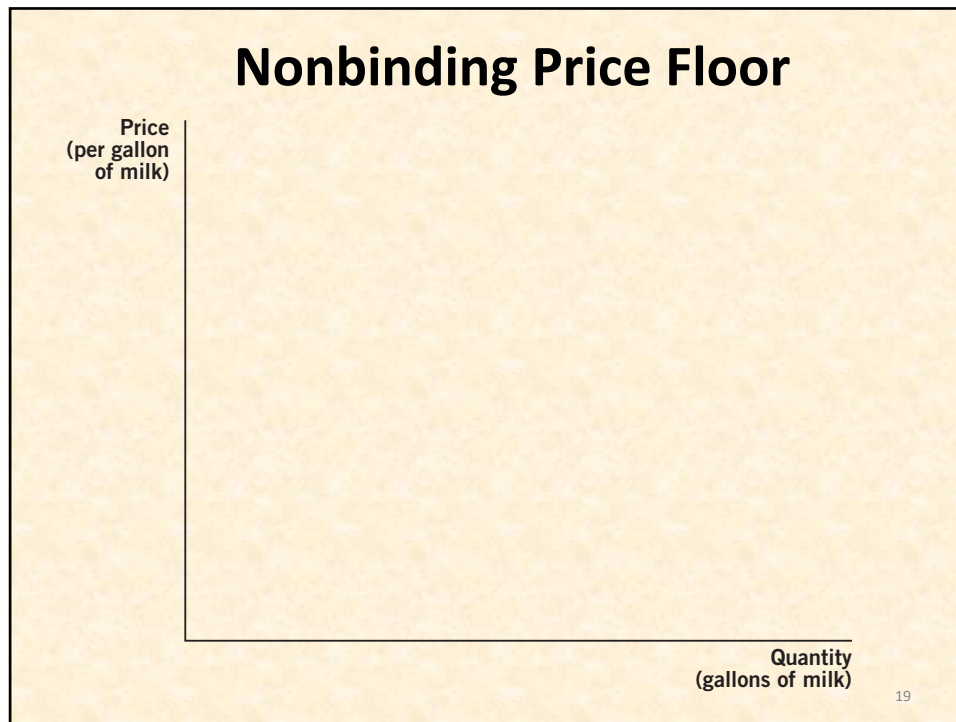
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Price Gouging

- Price gouging laws
 - Temporary price
 - Usually after a natural disaster
- Consequences
 - Restricted prices can't
 - Severe

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Binding Price Floor in the Long Run

Price
(per gallon
of milk)

Quantity
(gallons of milk)

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Another Thought Experiment: \$6 Price Floor on Milk

<u>Question</u>	<u>Explanation</u>	<u>In pictures</u>
Will the quantity of milk for sale change?		
Will the size of a typical container change?		
Would producers sell below the price floor?		
Are milk producers better off?		

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Poll Everywhere Question 3

- **Do you think there should be a minimum wage?**
- A) Yes.
- B) I don't know. I need more information.
- C) Absolutely not.
- D) I will never have to worry about getting the minimum wage, SO I DON'T CARE.

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Minimum Wage

- Minimum Wage: lowest hourly wage rate that firms may legally pay their workers.
- Reasons behind a minimum wage:
 - Provide a
 - Help working poor who are often unskilled

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“30 Days” Minimum Wage

25

Minimum Wages around the world

Sample of 26 OECD countries

26

Minimum Wage

- The unintended consequence of a binding minimum wage is . Caused by:
 - in quantity demanded for labor
 - in quantity supplied of labor
 - Firms replacing low-skilled jobs with , if possible
 - Firm
 - hours for workers

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Binding Minimum Wage

wage
(per hour)

Quantity
(workers)

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Investing in capital to save labor cost

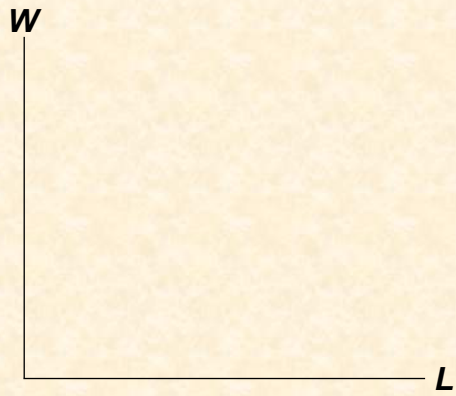
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Review Question

- You are looking for work in Melbourne. The national minimum wage is \$18.29/hour; the market equilibrium wage is \$20/hour.
- A) What wage will you be paid?
- B) Is the national minimum wage a binding or non-binding price floors?
- Suppose the national minimum wage $\uparrow$ from \$18.29 to \$25 (above equilibrium market wage). At \$25, labor demand is 30; labor supply is 50.
- C) Using a labor market diagram, show how this might affect the number of workers employed & indicate any unemployment.

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Answer



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