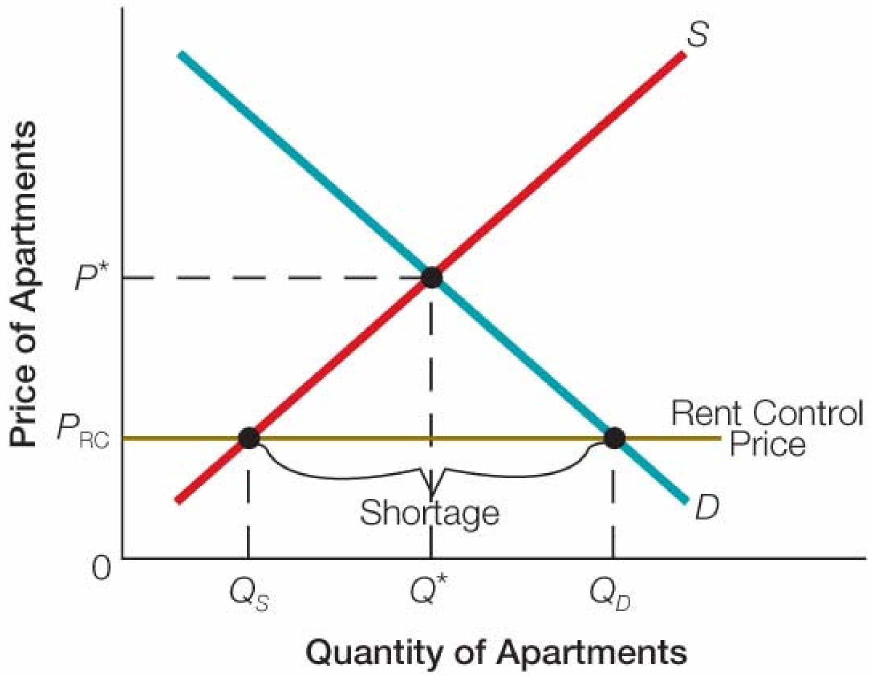
SECTION 4.3 PRICE CONTROLS

- Although nonequilibrium prices can occur naturally, reflecting uncertainty, they seldom last for long. Governments, however, may impose nonequilibrium prices for significant time periods.
- Price controls involve the use of the power of the governmnent to establish prices different from the equilibrium prices that would otherwise prevail.
- The motivations for price controls vary with the market under consideration. A **price ceiling**, or maximum price, is often set for goods deemed "important," like housing. A **price floor**, or minimum price, may be set on wages because wages are the primary source of income for most people.
- An example of a price ceiling is rent control. Under rent control the price (or rent) of an apartment is held below market rental rates over the tenure of an occupant. When an occupant moves out, the owner can usually, but not always, raise the rent to a near-market level for the next occupant.
- Rent controls distort market signals and lead to shortages and often do not help the intended recipients – low income households.
- Because living in rent controlled apartments is a good deal, one that would be lost by moving, tenants are very reluctant to move and give up their governmentally granted right to a below-market rent apartment.
- Rent controls constrain the rents received by landlords to below-market levels, the rate of return on housing investments falls compared to that on other forms of real estate not subject to rent controls, reducing the incentives to construct new rental housing. Where rent controls are truly effective, there is generally little new construction going on and a shortage of apartments that persists and grows over time.
- Since landlords are limited in what rent they can charge, there is little incentive to upgrade maintain rental apartments in order to get more rent. In fact, there is some incentive to avoid routine maintenance, thereby lowering the cost of apartment ownership to a figure approximating the controlled rental price.
- Rent controls promote housing discrimination. With rent controls, there are likely to be many families wanting to rent a controlled apartment, some desirable and some undesirable in the landlord's view, because the rent is at a below-equilibrium price. The landlord can indulge in his "taste" for discrimination in favor of "desirable" renters without any additional financial loss beyond that required by the controls.

section 4.3
Exhibit 1

Rent Controls

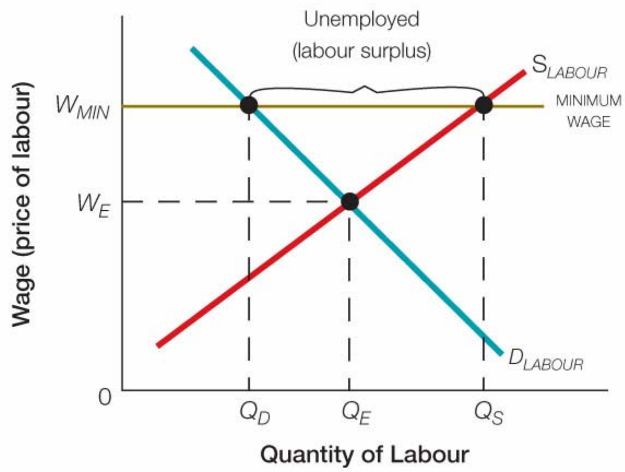


The impact of a price ceiling (a rent-control law) set below the equilibrium price is a shortage.

- An example of a price floor is the minimum wage. Provincial and territorial governments in Canada have made it illegal to pay most workers an amount below a legislated minimum wage.

section 4.3
Exhibit 2

The Unemployment Effects of a Minimum Wage on Low-Skilled Workers

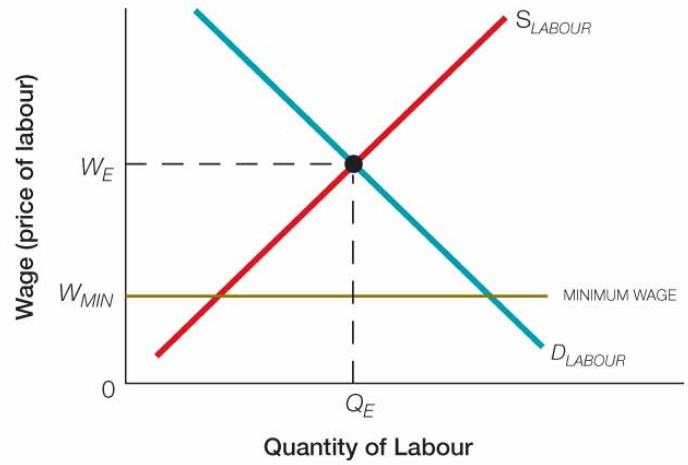


The impact of a price floor (a minimum wage) set above the equilibrium price is a surplus—in this case, a surplus of low-skilled workers.

- Because it would produce willing workers who will be unable to find jobs, an increase in the minimum wage would create a surplus of low-skill workers.
- Those who continue to hold jobs with the same hours and working conditions after the minimum wage is imposed will gain. But minimum wage laws do create some unemployment, and the unemployment is concentrated among teenagers.
- The analysis does not "prove" minimum wages are "bad." There is an empirical question of how much unemployment is caused by minimum wages, and some might believe that the cost of unemployment resulting from a minimum wage is a reasonable price to pay for assuring that those with jobs get a decent wage. But they do impose a cost, and it falls not only on unskilled workers and employers, but also on consumers of products that were made more costly by the minimum wage.

section 4.3
Exhibit 3

The Unemployment Effects of a Minimum Wage on Skilled Workers



There is no impact of a price floor on the market for skilled and experienced workers. In this market, the price floor (the minimum wage) is not binding.

- When markets are altered for policy reasons, it is wise to remember that actions do not always have the results that were initially intended **- unintended consequences** or secondary effects of an action that may occur along with the intended effects. The unintended effects may sometimes completely undermine the intended effects. For example, rent controls reduce vacancy rates, increase discrimination, and lead to the deterioration of the quality of rental housing units, and the minimum wage increases unemployment and decreases fringe benefits.