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Summary

During disasters government officials often seek to impose price controls in the name of protecting consumers. However, such controls are counterproductive; they destroy the market's messaging system and cause harm to producers and consumers alike. Price controls make a bad situation worse by adding a political disaster onto a natural one.

Word count: 595

“Price controls are among the worst attacks that a government can levy not only against producers but also against the consuming public.”

Disasters are no excuse for price controls

by *Jacob G. Hornberger*

During natural disasters such as Hurricane Isabel, state officials are often tempted to protect consumers from “price gougers, speculators, and profiteers,” who are selling the things that people need most at what might be considered exorbitant prices. The imposition of a mandatory ceiling on prices of essential items enables state officials to portray themselves as friends of the consumers.

Nothing could be further from the truth. Price controls are among the worst attacks that a government can levy not only against producers but also against the consuming public.

By serving as the market's information-transmission system, the price system is actually the lifeblood of a market economy. Tamper with the price system, and you end up destroying the market economy.

Let's suppose that Isabel knocks out electricity for an indefinite amount of time in a certain part of the state. All of a sudden, the price of candles in that area skyrockets. The soaring price serves to send a vitally important message to consumers in the affected area: “Conserve candles. Use them sparingly.”

By the same token, the rapidly rising price also sends a message to producers: “People in that area need candles. Get them there fast.” The anticipated high profits also send another message to producers: “The faster you accomplish this, the bigger your gains will be.”

As people cut back their consumption of candles (because of the soaring price) and as producers rush additional candles into that area (for the same reason), the price of candles begins to drop. That's a message that tells consumers they can now increase their consumption, while at the same time tells producers that supplies are not as urgently needed as before.

The beauty of the price system is that it works all on its own—that is, without state guidance. In other words, no emergency central planner has to keep track of which items are in short supply and which ones are in abundance. No public-service announcements are needed to advise people what they need to conserve

or to exhort producers on what they need to supply. All that people—both consumers and producers—need to do is rely on the price system to figure out how much they should consume or produce.

What happens if state officials impose price controls in a misguided attempt to protect consumers from “exorbitant” prices? They destroy the market’s messaging system and actually worsen the effects of the disaster.

For example, let’s assume that the pre-disaster price of candles was \$1 per candle. The natural disaster strikes, and candle prices immediately soar to \$20 each. Professing to protect consumers from “price gouging” and “profiteering,” state officials set a price ceiling that prohibits candles from being sold for more than the pre-disaster price of \$1 each.

The state’s intervention throws the market into chaos. The artificially low price obviously sends a distorted message to both consumers and producers. For consumers, the lower price means that there’s no special incentive to conserve candles, and for producers it means that there’s no special need to supply them.

Thus, given that people are consuming candles faster than they should, and given that producers are not rushing to supply more candles to the affected area, the intervention actually makes the situation (a short supply of candles) much worse than it otherwise would be.

By interfering with the price system’s method of sending vital information to consumers, price controls distort the market economy’s ability to allocate scarce resources. Moreover, by hurting the very people they purport to help, price controls add a political disaster onto a natural one.

Mr. Hornberger, JD, is an adjunct scholar to Cascade Policy Institute, a Portland, Oregon think tank, and founder and president of The Future of Freedom Foundation (www.fff.org) in Fairfax, Va.

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Please contact:

Kurt T. Weber
Vice President
Cascade Policy Institute
813 SW Alder Street, Suite 450
Portland, Oregon 97205

Phone: (503) 242-0900
Fax: (503) 242-3822

www.cascadepolicy.org
kurt@cascadepolicy.org