GOV'T INTERVENT.

(a) Ceiling Prices
(b) Floor Prices
(c) Subsidies & Quotas

expert groups

resource groups

1. Defn
2. GR
3. PURPOSE / EFFECT
4. Graph
5. Examples

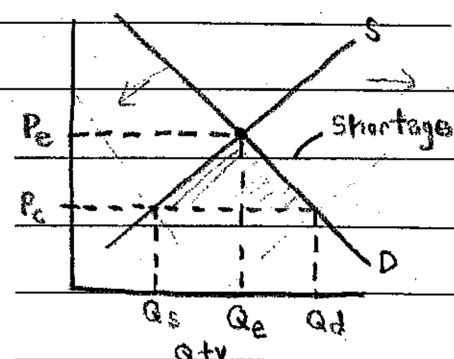
Price Ceilings

equilibrium price artificially high

↳ artificially high prices est. in mkt place – by law

↳ gov't imposed maximum price (illegal to sell above ceiling price)

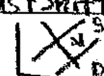
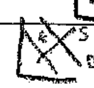
↳ e.g. oil, energy, rent




* Shortages – free mkt. naturally restores to $P_e$ via price increases but intervention thus GOV'T must ~~eliminate another way~~

thus D or S curve must shift

further gov't involvement to induce new equilibrium

1. subsidy to producers 
2. restrict demand? discourage demand 

FACTOR AFFECTING SUPPLY & DEMAND

Quota

## Price Floors

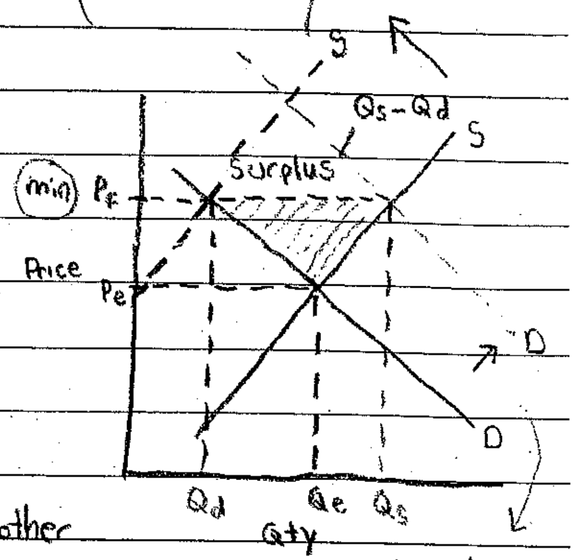
highly under valued products
highly competitive mkts
recessionary/contractionary

↳ Defn – gov't-imposed minimum price as gov't determined mkt. equilibrium price too low

↳ e.g., agricultural products

↳ legal process legislating a minimum price

↳ effect of price floor on market




↳ no longer a free-mkt situation as artificial/gov't intervention

results in disequilibrium b/c of gov't intervention

THUS gov't must further intervene to restore the balance/equilibrium

↓

efficiency? equity? stability?

in a free mkt. situation a surplus would be corrected by naturally lowering prices – another way must be found to rid the market of the surplus

Ont. Advertising

↳ Milk/Produce/Cheese/Eggs

new "Got to have Milk" spots (big fish little fish/standing cow in rubber boots)

i.e. some factor must shift demand or supply curve so new equilibrium price at Pf

e.g., – gov't restrictions on production/production quotas (SUPPLY LEFT)
– advertising/tastes & preferences to ↑ demand (DEMAND RIGHT)

(gov't must become further involved in REGULATING MKT CONDITIONS

~~trade issues~~ / over production (dumping)

## Subsidies and Quotas

* price ceilings & floors — COMMON PROBLEM = less product / economic activity between buyers and sellers B/C price is forced away from price equilibrium

↳ GOV'T INTERVENTION TO COUNTERACT

① subsidies — gov't offerred financial support to a particular industry (e.g. CDN oil despite profit)

② quotas

- lower prices to consumers
- higher revenue to producers
- increased economic activity

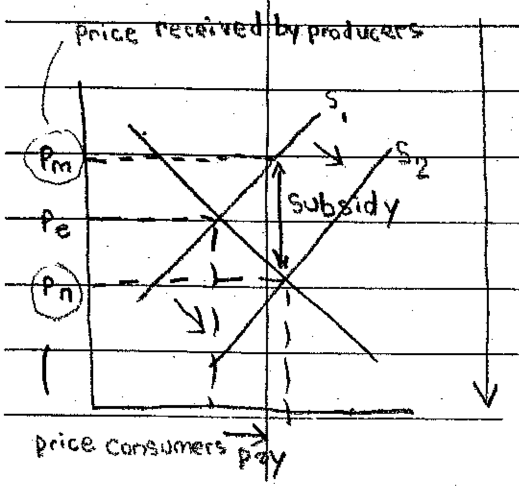
] benefits of subsidy

↳ funded by taxpayer / priorities

↳ props up inefficient / failing business

↳ global economy — barrier to free trade

] drawbacks

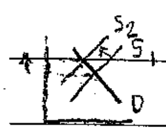



Quotas / help producers generally by restricting amount of product produced by ~~individual producers~~

\ marketing boards administer the intervention / gov't representatives, representatives / producers, sells to retailers / consumers

\ effect = ↑ supplier income by price increase

\ purpose = raise producer income as most effective for inelastic products (e.g. – food production) → characteristically low ~~low~~ incomes → essential product / commodity




\ CRITICISM ① artificially raises equilibrium prices

② actually reduces volume of exchange / economic activity

## Excise Taxes

↳ affect supply side of market

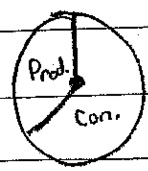
↳ "extra costs" imposed by GOV'T on sale of certain commodities

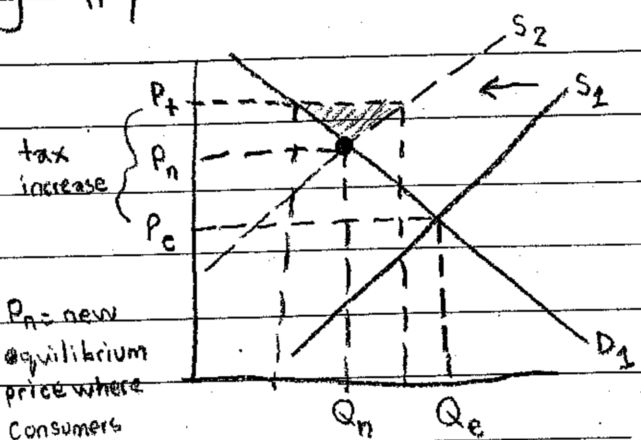
↳ PURPOSE – revenue generation / source for GOV'T
- influence mkt. behaviour / use &/or production of a particular commodity

e.g., liquor, ~~tobacco~~, gas tax, auto air conditioners, other envi. reasons

↳ producer / manufacturer required to pay tax

↳ EFFECT – factors affecting supply – COST OF PRODUCTION ↑




INCIDENCE OF TAX – burden of tax split betw consumer & producer – $P_n$ = new equilibrium price where consumers pay a portion of the tax

INCIDENCE OF TAX varies product by product and major determinant is price elasticity of demand & supply

↳ IF demand INELASTIC THEN likely ... consumer bears the majority of burden

↳ IF demand ELASTIC THEN likely ... producers assume greatest burden

↳ what products? depends on objective of tax
- ① RAISE REVENUE then products w inelastic demand (TR consideration) (tobacco/liquor)
- ② DISCOURAGE CONSUMPTION then products w elastic demand (certain technology in autos)