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Price Gouging is Not the Problem

by Nick Stearns

Summary

Imposing price controls to protect consumers is one of the worst things government can do in an emergency. Rapidly rising prices signal those outside the affected area to conserve scarce products, and they signal producers to ship more of those products into the affected area quickly. Price controls short circuit such signals, turning a natural disaster into a political one.

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"In reality, price controls are one of the worst things government can do to consumers, even in an emergency."

The "fix what isn't broken" crowd in Salem is at it again. Instead of fixing PERS, reducing traffic congestion, or streamlining government agencies, politicians are spending time pushing Senate Bill 209 which they purport will protect consumers in the wake of a natural disaster, a local ground war or terrorism activities.

Specifically, this bill would target contractors and retailers that charge "unconscionably excessive prices" for services such as property repair, food and water if and when calamity hits. The bill, promoted by Oregon Attorney General Hardy Myers, defines gouging as rates that are 20 percent or more above prices immediately before the disaster hit. On the surface, how could one disagree with protecting consumers from opportunistic profiteers? Aren't Hardy Meyers and his colleagues simply "friends of the consumer"? Scratch that surface a little and you'll see that nothing could be further from the truth. In reality, price controls are one of the worst things government can do to consumers, even in an emergency. As hard as it might be to believe, the price system is the best way for the markets to transmit informationt. It is the key to the market economy. Tamper with the price system, and you end up hurting the very people you wish to protect.

Take a hypothetical example; assume another event like the Columbus Day storm of 1962 destroys windows in homes and buildings in Oregon. Rain is blowing in and people scramble to board up damaged buildings. Overnight, the price of plywood in Oregon spikes. The now-high price of plywood sends a message to consumers in Oregon: "Conserve plywood". At the same time the rise in plywood prices (and potential profit) sends a message to producers, brokers, retailers and other sellers that we need plywood in Oregon and we need it now. The faster the need is met the more profit can be had.

As typical users of plywood reduce their consumption because of the high price and producers race to bring more plywood to the region, the price of plywood drops. The drop in price signals to people that they can now increase their consumption, while at the same time it tells producers that supplies are not as urgently needed as before.

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The free market economy works best when prices are not consciously set by politicians; the system is automatic. There is no need for someone like Meyers to monitor supplies or intervene. If this bill passes, the Legislature will effectively destroy the market in an emergency and make a natural disaster into a political one. In the example above, stores in Oregon would be sold out of $20 per sheet plywood. Imagine homes being destroyed and not being able to buy a sheet of plywood at any price. One might wish for someone willing to sell a sheet or two for $100 each. People might not think that $100 is "exorbitant" if it meant saving their home. While the property of Oregonians is being destroyed, consumers in California or Washington might unknowingly be building playhouses for their kids with cheap plywood. Under this scenario, would SB209 protect you or hurt you?

This is not really that complex. The question is: why is it that so many people, especially journalists and politicians, continue to distrust market based solutions that work while, at the same time, they pursue and embrace interventionist systems and policies that continually fail?

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