


**6**  **Government Actions in Markets**

- Can governments cap rents to help renters?
- Can governments make housing more affordable by raising incomes with minimum wage laws?
- The government taxes almost everything we buy.
- But who actually pays and who benefits when a tax is cut: buyers or sellers?
- The government subsidizes some farmers and limit the quantities that other farmers may produce.
- Do subsidies and production limits help to make markets efficient?

© 2010 Pearson Education Canada

---

---

---

---

---

---

---

---

**▶ A Housing Market with a Rent Ceiling**

A **price ceiling** or **price cap** is a regulation that makes it illegal to charge a price higher than a specified level.

When a price ceiling is applied to a housing market it is called a **rent ceiling**.

if the rent ceiling is set *below* the equilibrium rent, it has powerful effects.

**PRICE CEILING - a maximum legal price for the market.**

© 2010 Pearson Education Canada

---

---

---

---

---

---

---

---

**▶ DO RENT CONTROLS HELP THE HOMELESS? PRICE CEILINGS**



Rent controls fix rents below market-clearing levels,

Rent controls sometimes justified by **Robin Hood principle** — take from the rich (landlords) and give to the poor (tenants)

© 2010 Pearson Education Canada

---

---

---

---

---

---

---

---

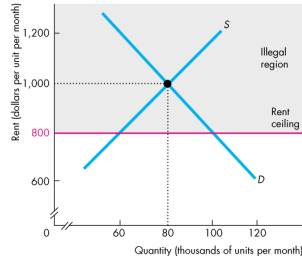
### ◆ A Housing Market with a Rent Ceiling

#### Housing Shortage

The equilibrium rent is \$1,000 a month.

A rent ceiling is set at \$800 a month.

So the equilibrium rent is in the illegal region.



© 2010 Pearson Education Canada

---

---

---

---

---

---

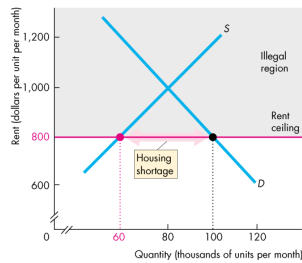
---

---

### ◆ A Housing Market with a Rent Ceiling

At the rent ceiling, the quantity of housing demanded exceeds the quantity supplied.

There is a shortage of housing.



© 2010 Pearson Education Canada

---

---

---

---

---

---

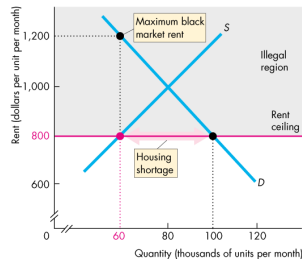
---

---

### ◆ A Housing Market with a Rent Ceiling

- Search activity
- Black markets

With a housing shortage, people are willing to pay up to \$1,200 a month.



© 2010 Pearson Education Canada

---

---

---

---

---

---

---

---

## ▶ A Housing Market with a Rent Ceiling

### Search Activity

The time spent looking for someone with whom to do business is called **search activity**.

When a price is regulated and there is a shortage, search activity increases.

### Black Markets

A **black market** is an illegal market.

Illegal arrangements are made between renters and landlords at rents above the rent ceiling—and generally above what the rent would have been in an unregulated market.

© 2010 Pearson Education Canada

---

---

---

---

---

---

---

---

## ▶ A Housing Market with a Rent Ceiling

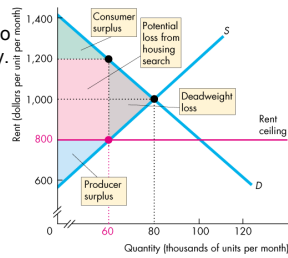
A rent ceiling decreases the quantity of housing supplied to less than the efficient quantity.

A deadweight loss arises.

Producer surplus shrinks.

Consumer surplus shrinks.

There is a potential loss from increased search activity.



© 2010 Pearson Education Canada

---

---

---

---

---

---

---

---

## ▶ A Housing Market with a Rent Ceiling

### Are Rent Ceilings Fair?

According to the *fair rules* view, a rent ceiling is unfair because it blocks voluntary exchange.

According to the *fair results* view, a rent ceiling is unfair because it MAY not generally benefit the poor

A rent ceiling decreases the quantity of housing and the scarce housing is allocated by

- Lottery
- First-come, first-served
- Discrimination

© 2010 Pearson Education Canada

---

---

---

---

---

---

---

---

## DO MINIMUM WAGES HELP THE WORKING POOR? PRICE FLOORS



Minimum wage laws fix wages above market-clearing levels, quantity adjustment takes the form of a surplus of workers. Benefit is higher wages to the employed, but unintended consequence is fewer are employed.

© 2010 Pearson Education Canada

---

---

---

---

---

---

---

---

### A Labour Market with a Minimum Wage

A **price floor** is a regulation that makes it illegal to trade at a price lower than a specified level.

When a price floor is applied to labour markets, it is called a **minimum wage**.

If the minimum wage is set *above* the equilibrium wage rate, it has powerful effects.

© 2010 Pearson Education Canada

---

---

---

---

---

---

---

---

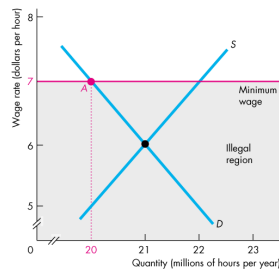
### A Labour Market with a Minimum Wage

The equilibrium wage rate is \$6 an hour.

The minimum wage rate is set at \$7 an hour.

So the equilibrium wage rate is in the illegal region.

The quantity of labour employed is the quantity demanded.



© 2010 Pearson Education Canada

---

---

---

---

---

---

---

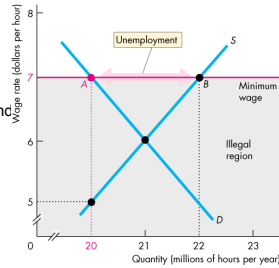
---

### ▶ A Labour Market with a Minimum Wage

#### Minimum Wage Brings Unemployment

The quantity of labour supplied exceeds the quantity demanded and unemployment is created.

The quantity of labour employed is less than the efficient quantity.



© 2010 Pearson Education Canada

---

---

---

---

---

---

---

---

---

---

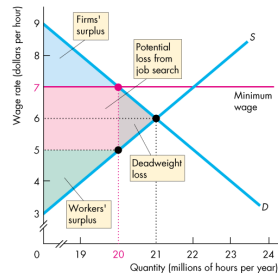
### ▶ A Labour Market with a Minimum Wage

A minimum wage set above the equilibrium wage decreases the quantity of labour employed.

A deadweight loss arises.

The potential loss from increased job search decreases both workers' surplus and firms' surplus.

The full loss is the sum of the grey areas and a part of pink.



© 2010 Pearson Education Canada

---

---

---

---

---

---

---

---

---

---

### ▶ A Labour Market with a Minimum Wage

#### Is the Minimum Wage Fair?

A minimum wage rate in Canada is set by the provincial governments.

In 2009, the minimum wage rate ranged from a low of \$7.50 an hour in New Brunswick to a high of \$10.00 an hour in Nunavut.

Most economists believe that minimum wage laws increase the unemployment rate of low-skilled younger workers.

© 2010 Pearson Education Canada

---

---

---

---

---

---

---

---

---

---