



Price control is price dictatorship ¹

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The price of a commodity is an indicator of both its value or usefulness to society (demand side) and its availability or scarcity (supply side). Thus, when a product or service is deemed useless by the consumers, say telegram or personal pager, then its price based on the willingness to pay of the consumers, will be zero or near-zero. At that price, no service provider will supply the service. The result will be clear: there will be no more telegram or paging companies.

On the other hand, when a commodity or service is deemed very useful to society but it is freely available, or the supply is unlimited, like air, then the price for its consumption will be zero. Luckily, the supplier of that service – nature – does not demand any monetary compensation. But there are certain places and instances where air is very thin if not absent and hence, people will have to buy a “bottle or tank” of air for them to survive, like those in scuba diving or those climbing Mt. Everest or other very tall mountains.

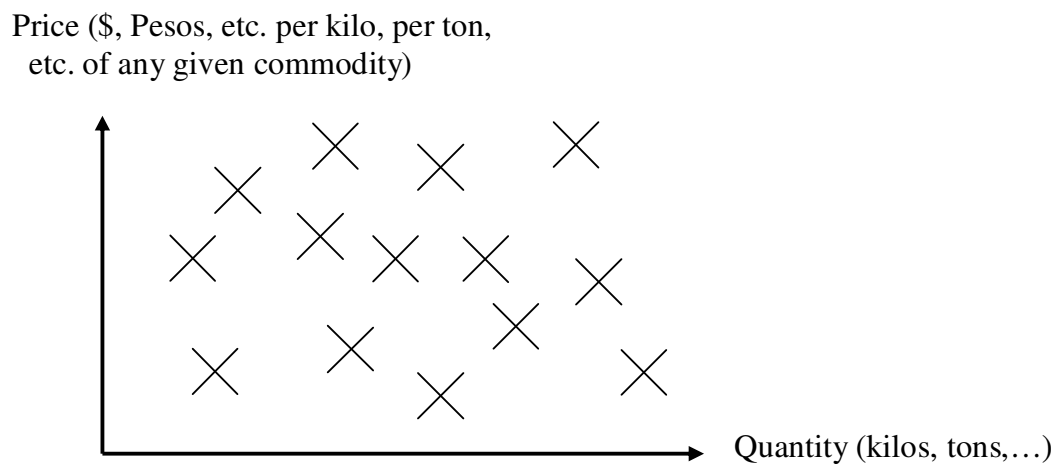
Price, therefore, is a beautiful mechanism that tells people and producers what products and services are most- or least- demanded by certain groups of consumers in a particular place in a particular time. It is necessary therefore, that pricing of commodities and services be left as freely and spontaneously as possible to allow both producers and consumers, both sellers and buyers, to adjust to each other. If the price is too high, consumers can walk away and the sellers will not sell anything and go bankrupt even temporarily. If the price is too low, producers will not supply and consumers will buy nothing that they need and they will be the end-losers.

¹ This is a slightly longer version of a paper of the same title by the author posted in http://www.thelobbyist.biz/column_detail.php?id_article=976&id_category=25

And since there are various qualities for the same generic commodity group, say different sizes and colors, different taste and uses, for tomatoes, then there will be many “equilibrium” prices for each category of commodities. Having a “single price” for tomatoes since they are all the same tomatoes anyway, is not possible. Product differentiation and heterogeneity immediately removes the “homogeneous product” criteria in establishing a perfectly competitive market.

So a situation of various combinations of supply curves (upward sloping) and demand curves (downward sloping) is possible and what is happening in real life, as shown in this graph.

Graph 1. Multiple equilibrium price for heterogeneous or non-similar quality products.

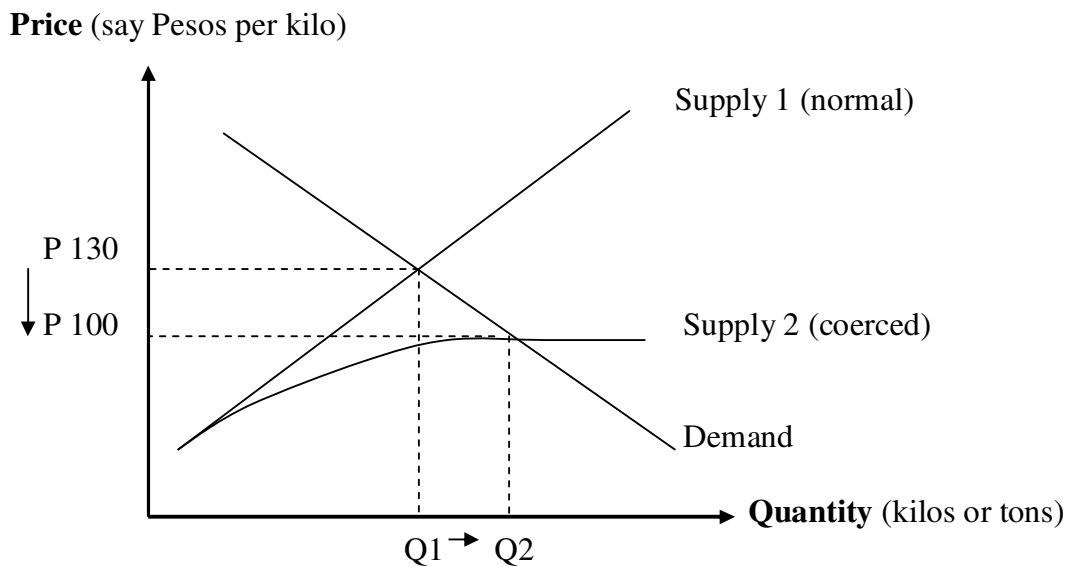


The idea of controlling the price of anything is born out of various motives, from humanitarian and pure public service, to political rent-seeking and pure envy. Price regulation and control is a clear proof and explicit signal that an economy is not free, that pricing of the regulated commodity is highly politicized. Price control is also a naked and blunt proof that there is price dictatorship: the price dictators decide at what price the producer and/or seller of a final product or service can sell, even though the same price dictators do not decide nor dictate the price of all inputs and intermediate products and services needed to produce that final product or service.

Thus, while the rationale or alibi given to institute price regulation and control is to “give justice to the consuming public”, there is great injustice to the same consumers when producers and/or sellers of commodities whose price has been politicized and regulated will be discouraged from producing further. When prices are controlled, producers who can possibly make some “miracle” products at sky-high and “miraculous” costs will be discouraged from innovating and producing those products. Ultimately, it is the public, the consumers, who will be the losers because they will be deprived of enjoying such revolutionary products.

The evils of price control can be depicted below.

Graph 2. Single “equilibrium price” as a result of price control



If there is no price control and price dictatorship, the prevailing buying-and-selling price (or “equilibrium price”) of a particular commodity (say tilapia or onion or potato) will be at P130 per kilo; at that price, an amount equivalent to Q1 (xx kilos) will be bought.

Now government comes in, urged upon by some lobby groups and government politicians and regulators themselves like the idea of playing “hero” in the eyes of vote-rich poor people, and imposes a maximum retail price (MRP) of only P100 per kilo of the same commodity. When there is price control, there is also quantitative control, usually in the behavior of the supply curve. So the supply curve moves from S1 to S2. Consequently, the volume or quantity being demanded by the consumers will increase from Q1 to Q2, as people buy more when the price is cheaper.

This looks cute and is supposed to give credence to the populist thinking that “State intervention is necessary to correct market abuses and market failure”.

But can people expect the “same” quality of a commodity given the distorted and coerced lower price? This does not look possible.

Producers will be discouraged from producing better quality commodities or products that require higher cost of raw materials and intermediate inputs, higher wages for higher labor and technological skills, higher office and plant rentals for cleaner production environment, higher cost of storage and packaging, etc. When the price of the above-mentioned production and marketing costs are uncontrolled, plus there are uncontrolled taxes and fees slapped on them, then the price of the finished product will be controlled later, then it is a perfect formula to discourage production of good quality commodities. Only low quality and mediocre products will be produced and sold at politicized pricing system.

This partly explains why under normal, non-coerced, non-politicized pricing system, there are different prices for different quality products of the same generic category. For instance, there are different prices for different designs and brands of running shoes. And people love this price segmentation or price differentiation for differentiated designs, quality and packaging of products.

Here in the Philippines, price control is seldom practiced, thanks to some sanity in the minds of government regulators and bureaucrats. Unfortunately, that populist and interventionist policy is never erased in the minds of many people in government. That is why in the recently-enacted “Cheaper medicines law” or RA 9502, price control of some drugs and medicines “when national emergencies exist” was included.

This already sends a negative signal to producers of good quality and innovative medicines while sending positive signal to producers and traders of low quality, non-innovative, even counterfeit medicines. Because a “maximum price” to be set by the government through the Department of Health (DOH) and ordered by the President of the country will now be used by the second group of medicine producers and traders as a “target” price. Even low quality and non-innovative drugs can be priced near or at the level set as “maximum price” by the State.

The potential damage of the price control provision in the law, however, can be mitigated if the implementing rules and regulations (IRR) that will be issued will make it not too easy and arbitrary to declare a “national emergency” to justify medicine price control. Thus, certain safeguards that are strict enough should be put in the IRR.

The current [draft IRR](#) prepared by the DOH somehow lists some good and strict criteria before a maximum retail price (MRP) can be declared. Among such criteria are the dozen-plus factors and inputs that contribute to the final price of medicines, like cost of research and marketing, taxes and fees, exchange rate, and so on.

But the composition of the Price Control Advisory Body or Consultative Council was not defined. This writer suggested some [proposals](#) on who should be in that body or council, mainly players from the private sector plus consumers. Since the composition of the body or council is not defined in the DOH draft IRR, it is possible that such body may be packed with lots of government officials, like people from the DOH, DTI, BFAD, DOST, DSWD, NEDA, DILG, and so on.

A definition of what constitutes “national emergency” was also not made in the section on Definition of terms. Again, there is danger that such phrase can be abused by an abusive and corrupt DOH Secretary and President of the country someday. Like threatening the manufacturers and distributors of safe, effective, but “expensive” medicines with “Hey, we will issue price control (or compulsory license) on your most popular and block-buster medicines, unless you pay us...”

This is **not** to say that the current DOH Secretary and President are corrupt and extortionists. This law will stay with the citizens and residents of this country for the

next 20 or 50 years or even longer, unless amended by another law where the price control provision is removed and abolished. The appearance of corrupt and extortionist DOH Secretaries and Presidents of the country in the next 20 or 50 years or even longer, is a big probability considering the bad governance culture and history in the country.

Hence, mechanisms should be instituted to make it difficult for future corrupt and extortionist DOH Secretaries and Presidents to impose medicine price regulation and control arbitrarily. More innovators and inventors of effective, revolutionary and safe medicines should be encouraged to come in. not discouraged with politicized pricing and patent confiscation. With more competition among such type of medicine producers, the public will be protected with quality and affordable medicines.