[A] Reason for (or Why) Government Intervention in the market economy’

Introduction

In a free market economic system, scarce resources are allocated through the price mechanism where the preferences and spending decisions of consumers and the supply decisions of businesses come together to determine equilibrium prices. The free market works through price signals. When demand is high, the potential profit from supplying to a market rises, leading to an expansion in supply to meet rising demand from consumers. Day by day, the free market mechanism remains a tremendously powerful device for determining how resources are allocated among competing ends.

Intervention in the market

The government may choose to intervene in the price mechanism largely on the grounds of wanting to change the allocation of resources and achieve what they perceive to be an improvement in economic and social welfare. All governments of every political persuasion intervene in the economy to influence the allocation of scarce resources among competing uses.

1. What are the main reasons for government intervention?
2. The main reasons for policy intervention are:
3. To correct for market failure
4. To achieve a more equitable distribution of income and wealth
5. To improve the performance of the economy
6. When the lives of the citizens are in danger

• Disease outbreak like in Corona Virus situation
• Natural disaster (E.g.……………………………)
• etc.

[B] HOW Government Intervention in the market economy’ (Method of Intervention)

1. Government may control prices
   • price control,
   • price ceiling/maximum price
   • minimum price
2. Control the market using
   • tax (indirect)
   • subsidy
   • ensure competition
   • becoming a competitor
3. providing public goods
4. welfare
5. minimum wage
6. Ensure economic development & growth

(NB: these are not government functions but **tools** to deliver specific function) of protecting the citizens

NOTES:

**Price Ceilings**

A price ceiling occurs when the government puts a legal limit on how high the price of a product can be. In order for a price ceiling to be effective, it must be set below the natural market equilibrium.

When a price ceiling is set, there will be a shortage. For the price that the ceiling is set at, there is more quantity demanded than quantity supplied. Inefficiency occurs since at the price ceiling quantity supplied the marginal benefit exceeds the marginal cost. This inefficiency is equal to the deadweight welfare loss.

If a price ceiling is set, then there must be a way to assign who gets the low supply of the product. Since there is a legal limit on the price, the price can’t simply be raised. There are several ways this is done without raising the price:

**Lottery:** One way to distribute a product for which there is a shortage is to draw names out of a hat. In some states there is a high demand to be able to hunt for moose, but the government has a limit on the amount of permits it gives out. Often these states have a lottery and if you are lucky enough to get drawn, you can try your luck at finding and shooting a moose during the season.

**Black Market:** For those lucky enough to get some of the short supply, they are often better off selling what they have obtained to the demanders that will get more benefit out of it. In some cities there have been ceilings put on the apartment rent. While the demand for apartments increases, the rent remains the same. When some renters are ready to move, they sublease their apartment instead of ending their contract. If they were renting for R500, but someone is willing to pay R1000, then the subleaser can continue paying R500 and pocket the extra R500 he gets from the subleasee.

**Historical Use:** Sometimes the government will allow the consumers that were already consuming to continue consuming. This would be hard to do since after the price ceiling there will be many more people claiming they have consumed in the past. Also, the quantity supplied is decreased which will even leave some of the historical consumers wanting.

**Subsidy**

A subsidy is a form of financial assistance paid to a business or economic sector. Most subsidies are made by the government to producers or distributors in an industry to
prevent the decline of that industry or an increase in the prices of its products or simply to encourage it to hire more labor.

The graph about illustrates the subsidy effect. From the graph we find that when government giving subsidy, the supply will shift right to the subsidy effect curve. The price will decrease and the quantity will increase.

Advantage of subsidy is they result in lower price for the consumer. Although government implements the price ceiling to set the minimum price, subsidy also have their value in the market.

On the other hand, when government giving subsidy, national will have to be paid from tax revenues and therefore result in higher tax.

**Minimum price** help consumers buy the good which their need, it is helpful for consumer get the goods. It makes sure certain goods which could be scarce, especially when cheap, are available all times.

Nevertheless, some necessary product cannot set at the lower price because when the price is cheaper, the producer will reduce the quantity of the product even leave the industry. When that time the supply will less than demand, there will have a shortage. At the same time the price also will increase. When occur this situation, government adopt to give subsidy to the producer that producer will satisfy on the revenue and continue produce the product and consumer will allow buying it in the price. Cause win-win situation between producer and consumer.

**Maximum price/Price ceiling**

Government just uses this to ensure affordability of staple or essential goods by setting a price ceiling. Or the government can remove tax on those food items, as long as these good does not branded. For instance, this can be seen in retail shops like spar...where you can see SPAR RICE, SPAR MEAL, SPAR BREAD
What is Public Sector?

public sector consists of governments owned and controlled enterprises/organisations/institutions or publicly funded agencies, enterprises, and other entities that deliver public programs, goods, or services. It is not, however, always clear whether any particular organization should be included under that umbrella.

Criteria to help define the boundaries:

• The concept of public sector is broader than simply that of core government and may overlap with the not-for-profit or private sectors. For the purposes of this guidance, the

• public sector consists of an expanding ring of organizations, with core government at

• the centre, followed by agencies and public enterprises.

• consisting of publicly funded contractors and publicly owned businesses, which may be,

• but for the most part are not, part of the public sector.

Public sector organizations may exist at any of four levels:

• International (multistate entities or partnerships).
• National (an independent state).
• Regional (a province/state within a national state).
• Local (a municipal-level body such as a city or count
  District
• Metropolis

Core government

consists of a governing body with a defined territorial authority. Core governments include all departments, ministries, or branches of
the government that are integral parts of the structure, and are accountable to and report directly to the central authority — the legislature, council, cabinet, or executive head.

**Government Agencies**

consist of public organizations that are clearly a part of the government and deliver public programs, goods, or services, but that exist as separate organizations in their own right — possibly as legal entities — and operate with a partial degree of operational independence. They often, but not necessarily, are headed by a board of directors, commission, or other appointed body.

**Public enterprises are agencies**

that deliver public programs, goods, or services, but operate independently of government and often have their own sources of revenue in addition to direct public funding. They also may compete in private markets and may make profits. However, in most cases the government is the major shareholder, and these enterprises partly follow the acts and regulations that govern the core government.

**State businesses are government owned and controlled businesses (or parastatals)** that sell goods or services for profit in the private market.

Although they do not deliver in some cases what would be considered public programs, goods, or services, they are considered part of the public sector.

**Public contractors** are legally independent entities outside government that receive public funding — under contract or agreement — to deliver public programs, goods, or services as their primary business. Due primarily to their limited public control, these organizations usually would be classified as not for-profit or private sector entities.