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North Carolina's Price-Control Laws
Harming Those They're Meant to Help

Dr. Roy Cordato

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The Macon Series

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This report on price-control laws is the second in a series of annual research papers from the John Locke Foundation devoted to explaining the principles of free markets and applying them to current controversies in North Carolina. The Nathaniel Macon Research Series was created with the generous financial support of David R.Carr Jr. of Durham, in memory of his friend and business partner George W. Brumley III, who was a strong believer in the crucial role that robust, unfettered markets play in advancing human progress and promoting a free society. The Macon Series will examine closely the fiscal and regulatory policies of the state and whether they help or hinder individuals seeking to create or expand businesses and economic opportunities in North Carolina. The series is named after Nathaniel Macon, a North Carolinian and close political ally of Thomas Jefferson who served as Speaker of the House and U.S. Senator during the first few decades of the American Republic. Macon frequently argued, "That government is best which governs least."

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The Heart of Free Enterprise

The heart of free enterprise is the price system. If market participants do not have the legal right to adjust prices to reflect changes in economic conditions — consumer preferences, resource supplies, technology changes, capital costs, interest-rate changes, and a host of other factors, many of which cannot even be objectively specified — it would be a fallacy to even describe the system as capitalist.

Government-imposed price regulations in most market economies do not typically apply to all prices or even most prices all the time. Instead, such regulations usually apply to particular industries under particular circumstances.[1] Furthermore, price controls usually do not define exact prices that must be charged but set either precise maximum or minimum prices, such as the minimum-wage law. They may also specify pricing guidelines, like North Carolina's price-gouging law.

The state of North Carolina levies differing forms of price regulations on a range of what would otherwise be free-market activities (see "North Carolina's Price-Control Laws," adjacent page). These include controls on wages, gasoline, interest rates, and an unspecified number of prices during disasters and states of emergency. The purpose of this paper is to explain why a free and flexible price system is so important to both social order and the efficient allocation of goods, services, and resources in a free society. Particular emphasis will be placed on North Carolina's laws meant to regulate prices and the negative effect that these regulations have on both markets and the well-being of the citizens of the state.

Price-Control Laws in North Carolina

The state of North Carolina has several laws that are meant to thwart market participants' ability to freely establish prices for products or services that they are either selling or buying. The reasons for having these laws vary. Most are presumably meant to protect con-

North Carolina's Price-Control Laws

"An Act to Protect Consumers from Extreme Pricing Practices"

This is the act that established North Carolina's "price gouging" law to control price increases during declared disasters.

"Price gouging" laws tend to exacerbate shortages of high-priority items such as gasoline and ice.

Minimum Wage

North Carolina's minimum wage of $6.15 per hour will be effective on January 1, 2007. It will be illegal for an employer to offer a wage (the price of labor) that is less than $6.15 per hour to potential workers.

The effect of minimum-wage laws is to increase unemployment for very low-skilled workers.

Usury Laws

These laws set the maximum interest rates that lending institutions are allowed to charge for loans.

The most important impact of these regulations has been to outlaw those businesses — often called payday lending institutions — that make funds available primarily to low-income people toward the end of pay periods.

Minimum Pricing for Gasoline

This legislation is officially titled the "Gasoline Marketing Act." Except for certain specified circumstances, it forbids below-cost pricing for gasoline.

Its effect is to deprive consumers of especially low prices and inhibit entrepreneurial activity and competition in gasoline retail.

sumers from prices that are "too high." On the other hand, the state's newly enacted minimum-wage law is meant to protect employees from the possibility of being paid wages — i.e., prices for their labor — that are "too low." There is also the state's minimum pricing law for gasoline, which is based on the idea that the price of gasoline can be too low. Behind all of these laws is the presumption that under some circumstances the free market will generate a "wrong" price for certain products, and that politicians and bureaucrats can know the "right" price.

Price Gouging — When Prices Are "Too High"

North Carolina's current law against what the legislation refers to as "extreme pricing practices" during "states of disaster, states of emergency, or abnormal market disruptions" was passed by the General Assembly in July of 2006.[2] This version of the law was enacted in the wake of Hurricane Katrina to expand on the state's original price-gouging law, which was enacted in 2003. The 2003 law only applied to the specific geographical area that the state government had officially declared to be in a state of disaster. Because of this, complaints of gasoline price gouging in the aftermath of Hurricane Katrina could not be investigated because there was no state of disaster declared in North Carolina. The new law extends to "abnormal market disruptions," which would presumably apply to situations like the Hurricane Katrina disaster. One of the definitions of an "abnormal market disruption" is that it is accompanied by a declared state of disaster or emergency made by the President of the United States, "whether or not the dec-

> *All these laws presume that in some circumstances the free market will generate a "wrong" price for certain products, and that politicians and bureaucrats can know the "right" price.*

laration … applies to North Carolina.” As defined in the legislation, the products and services that come under this law are quite vague and open ended. They include “any merchandise or services which are consumed or used as a direct result of an emergency or which are consumed or used to preserve, protect, or sustain life, health, safety, or comfort of persons or their property.”

During disasters, when markets need to adjust as quickly as possible to changed conditions of supply and demand, price-gouging laws slow the process of recovery and prolong the agony.

What actually constitutes “an extreme pricing practice,” called “price gouging” in the 2003 law, is only slightly better defined, although as will be discussed below, the definition has nothing to do with sound economic theory and shows no consideration of what constitutes efficient price formation or the role of prices in an economy. Under the statute a person is guilty of price gouging if, with “knowledge and intent,” a price is charged that is “unreasonably excessive under the circumstances.” The statute goes on to state that determination will be based on two criteria, which presumably would help a court determine what is and isn’t “unreasonable.” The price increase would not be considered “unreasonable” or “extreme” if it could be “attributable to higher costs imposed by the seller’s supplier or other costs of providing the good or service during the state of disaster.” The second criterion looks at whether the prices a seller is charging may have been exceptionally low in the 60 days previous to the disaster declaration. If it was, then a significant price increase during the disaster also may not be considered “extreme.’

The statute is still quite vague, however. For example, it does not specify how much of a price increase can be justified on the basis of an increase in costs. Also, in the second criterion, the law states that an average of prices for only the previous 60 days will be examined, with no indication of how that average should be calculated.

But while the law's vagueness makes it difficult for businesses to comply with it, that isn't the real problem from an economics perspective. As will be discussed below, these kinds of laws actually harm consumers. During times of disaster, when markets need to adjust as quickly as possible to changed conditions of supply and demand, price-gouging laws slow the process of recovery and prolong the agony.

Penalties for violating the state's price-gouging laws can be quite severe. Each violation has a maximum penalty of $5,000, and "injured parties" may seek compensation.

Minimum Wage — When Prices Are "Too Low"

A wage is the price that an employee charges an employer for his services. Therefore, minimum-wage laws are price-control laws that set a minimum price that employers and employees can agree to as compensation for labor services. Until recently, North Carolina's minimum-wage law was simply an endorsement of the federal minimum wage, set at $5.15 per hour. In the summer of 2006, the state's general assembly passed legislation raising the minimum by $1.00 to $6.15 per hour.[3]

Laws Against Usury Lending — When Prices Are "Too High"

North Carolina has very extensive regulations defining caps on interest rates that may be charged by banks and other lending institutions.[4] These laws define maximum interest rates that can be charged over different ranges of loan amounts and for different time frames. The caps are set quite high and therefore do not impinge on the day-to-day operations of most banks or other financial lending institutions.

Where these laws have had a binding effect has been in niche areas of lending; i.e., in special cases, most prominently in what are called "payday lending" institutions. Payday lenders are in the business of advancing money to people for short periods of time, typically 15 to 30 days. They provide a service that traditional lending institutions are not willing to offer, but it is one that their customers both want and find valuable. More will be said about the impact of these price controls on these establishments and their customers, but their ultimate effect has been to put payday-lending institutions out of business in North Carolina, thereby denying their customers a service that they both want and need.

> *Price-control laws capping interest rates put payday-lending institutions out of business in North Carolina, thereby denying their customers a service that they both want and need.*

The Motor Fuel Marketing Act — When Prices Are "Too Low"

At the other end of the spectrum from North Carolina's price-gouging law is the "Motor Fuel Marketing Act." The act prohibits the sale of motor fuels below cost when the intent is to "injure competition." The law states that:

> "It shall be unlawful where the intent is to injure competition for any motor fuel merchant or the affiliate of any motor fuel merchant to sell with such frequency as to indicate a general business practice of selling at a motor fuel outlet any grade, brand or blend of motor fuel for less than the cost of that grade, brand or blend of motor fuel."[5]

Below-cost pricing of gasoline, then, is illegal when the intent is "to injure competition." But it is clear that most pricing decisions made by a business are meant to "injure" their competition. Businesses that are not legally protected monopolies, like electric utilities or the Post Office, always set prices in an attempt to convince actual or potential customers to patronize them and not their competition. For example, the law states that it is not unlawful to charge below costs for gasoline if "the price is established in good faith to meet or compete with the lower price of a competitor." What else could this possibly mean other than to convince customers not to patronize the competitor, whose price you are attempting to meet or compete with? If a business is successful in attracting customers away from its competitors, then it will indeed "injure" its competition. The point is that nearly all business activities in an open market are meant to "injure" competition — those includes pricing decisions, advertising decisions, product quality decisions, and even location decisions.

A careful study of business history shows that there are no real-world examples of monopolization through predatory pricing.

Why is this particular approach to "injuring" one's competition considered to be a problem? What needs to be considered is that this statute is part of North Carolina's antitrust laws. Its purpose is to prevent or punish what is known as "predatory pricing." The theory of predatory pricing states that a firm can gain monopoly power in a market by pricing below its costs — i.e., take losses — for an extended period of time, thereby luring away its competitors' customers and driving its competitors out of the market. Once this is done, the successful "predator," now safe from competition, will flex its monopolistic muscle, raising prices to monopoly levels in order to earn abnormal profits. Presumably the predator business, by earning monopoly profits, would more than recoup any losses incurred during the process of driving its competitors out of the market. This theory will be addressed in more detail below, but a careful study of business history shows that there are no real-world examples of monopolization through predatory pricing.

Specific penalties for violating this statute are not defined. If a business is found to be in violation of the law, the Attorney General may seek "injunction and/or civil penalties."

Why Are Prices Important?

There are very few phenomena in our lives that we confront more consistently and regularly than prices. If we stop for a cup of coffee on our way to work in the morning, we face a price; to buy gas or groceries we are confronted by prices. In fact, all market transactions, from purchasing an ice cream cone to buying a new house involves confronting, considering, and either accepting or rejecting prices. Furthermore, this process of confronting and accepting or rejecting prices may occur dozens or even hundreds of times in a single day. For instance, imagine one trip to a supermarket. As we go up and down each aisle choosing what we will purchase for the week, we are constantly looking at different products, checking out their prices, checking out different prices for the same item across brands, comparing these prices to what we may have seen in other stores or in advertisements for other stores, and deciding, based on these prices along with our budget and our overall desire for the item, whether or not to make the purchase. The point is that prices are pervasive in out lives. Even by watching TV, listening to radio, and driving past billboards we are informed of prices.

> *Even though prices are pervasive, few people understand the role of prices in allocating resources and establishing not only economic order but ultimately social order.*

Furthermore, in all of our lives we are not only payers of prices but we are also recipients of prices paid. In fact, it is the prices that we are paid — wages and salaries, prices of stocks that we sell, or interest on investments we make — that allow us to pay the prices we do for the goods and services we want. In other words, in our economic lives we are, and indeed we must be unless we are to live only on the charity of others, both buyers and sellers. It is our market activities as sellers that ultimately gives us the wherewithal to be buyers and consumers.

Despite this pervasiveness of prices in our everyday life, very few people understand the role of prices in allocating resources and establishing not only economic order but ultimately social order. This includes, unfortunately, the vast majority of policymakers who establish laws meant to regulate prices.

What Is a Price?

In order to understand what a price is, we must first understand exchange, since first and foremost prices are what make exchanges and trade possible. We trade with others in order to get what we desire without having to directly produce it ourselves. In a world with no money — i.e., a barter society — we directly exchange goods and services for goods and services. In every exchange that is made voluntarily, both parties to the exchange are giving up something that they prefer less for something that they prefer more. This is why voluntary exchange is said to be a "positive sum game": both parties to the exchange are made better off.

A common misperception is that exchanges are or should be based on equal value. No exchange is; people always prefer (value) what they get more than what they give up.

In this world of barter, the price paid is the quantity of the good or service that is given up in exchange for the good or service that is preferred. For example, if chicken farmer Bill exchanges a dozen eggs for a pound of cheese with dairy farmer Tom, the price of a pound of cheese for Bill is a dozen eggs, and the price of a dozen eggs for Tom is a pound of cheese. The price is the mutually agreed upon terms of exchange by which both parties end up being made better off, from their own perspectives. A common misperception is that exchanges are or should be based on equal value. The fact is that no exchange is based on an equal evaluation between the two parties. People always prefer — that is, they *value* — what they are getting more than what they are giving up.

Nothing changes when money enters the picture. Money is a "medium of exchange." It makes exchange easier because there does not have to be a direct "coincidence of wants" in order for exchange to occur. With money, if farmer Bill wants a pound of cheese, he does not have to find someone with cheese who wants eggs in order to obtain what he wants. He simply needs to find someone selling cheese for the universally accepted medium of exchange, i.e., money. Money allows more exchanges to be made and therefore allows more people to get what they want — improving social well-being for everyone. In this sense money, far from being the root of all evil, is the root of prosperity. Without it social welfare could barely advance past a subsistence level.

> *Exchanges are acts of cooperation between buyers and sellers. Prices are what facilitate this cooperation. Prices offered and accepted by buyers and sellers reveal terms of agreement.*

Every act of exchange is an act of cooperation between a buyer and a seller, and prices are what facilitates this cooperation. Prices that are offered and accepted by buyers and sellers reveal terms of agreement. This implies that when people are allowed to offer and accept any price they want for what they are either selling or buying, the chances of coming to an agreement and therefore improving the well-being of both parties are maximized. When the prices that are allowed to be offered or accepted are restricted, as in the case of the

North Carolina laws mentioned above, the possibility of reaching a mutually acceptable price that would make both parties better off are reduced. In this sense all forms of price restrictions have the potential of blocking some exchanges from being made and therefore are likely to reduce overall social well-being.

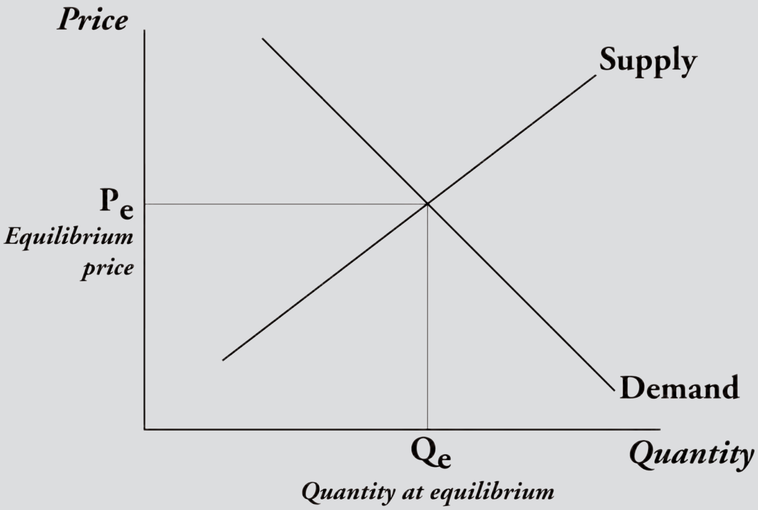
Supply, Demand, and How Prices Promote Social Order

In a memorable Saturday Night Live routine from the 1970s, comedian Don Novello, in his classic role as Father Guido Sarducci, introduced his latest entrepreneurial venture which he called "The 5 Minute University."[6] At his new university the student would be taught in five minutes, including spring break and the graduation ceremony, everything "the average" college student remembers five years after graduation. For example, after two years of college Spanish the typical student remembers *"¡Hola! ¿Cómo está usted? Bien, gracias"* and after being out of college for five years the only thing that the typical college graduate remembers from his economics class are the words "supply and demand."

Unfortunately, North Carolina policymakers who pass laws with the purpose of regulating the prices of goods and services display no greater understanding of how prices are formed than that displayed by a graduate of Father Guido Sarducci's university. They seem to have no idea of how the forces of supply and demand (the amount of money consumers are willing to pay for goods and services and the amount of money producers are willing to sell those goods and services for) interact to establish market prices. Furthermore, they seem to have no appreciation for the fact that prices are not simply arbitrary numbers picked by a seller to put on a price tag. Prices have significant informational importance and can make the difference between social chaos and the harmonious coordination of people's plans.

Diagram 1 is familiar, at least in appearance, to anyone who

Diagram 1



has taken a college or even high school economics class. It shows the familiar "X" formed by an "upward sloping" supply curve and a "downward sloping" demand curve. This diagram is simply a picture showing people's behavior in their roles as buyers and sellers. As buyers of goods and services, the higher the price of something gets, the less of it we are willing to purchase. That is why the "demand curve" (the line labeled "Demand") slopes downward. This is the famous "law of demand."

As sellers, the higher the price that we receive for whatever it is we sell, including our labor, the more we are willing to offer for sale. That is "the law of supply." The "supply curve" (the line labeled "Supply") slopes upward. Of course, both the law of demand and the law of supply take into consideration that other factors — such as personal tastes, momentary fads, transportation costs, and new technologies — will also affect quantities of goods and services that people will be willing to purchase or sell. But when discussing the particular relationship between prices and quantities, these "other things" are assumed to be unchanging. When these other things change, the entire supply or demand curve will shift.

At the intersection of the X (P_e, Q_e) is what is commonly called "market equilibrium." At this price, the amount of the good that people want to sell is exactly the same as the amount that others want to buy. This is referred to as the "market-clearing price." Above the market-clearing price, surpluses will develop — sellers will have product that they want to sell but can't find buyers for. Below the market-clearing price, there will be shortages — willing buyers unable to purchase all that they desire. In an open market where buyers and sellers are free to adjust their price offerings in any direction and by any amount they want, prices will move toward this market-clearing level whenever shortages or surpluses develop. That is why, despite constant changes in technologies, the comings and goings of fads, and all kinds of other market-altering events, persistent shortages or surpluses are rarely seen in a free market.

> *The importance of this spontaneous, voluntary interaction cannot be overestimated. When prices are not allowed to adjust to changing market conditions, chaos can and will ensue.*

That also explains why such shortages and surpluses are common in markets where government regulations do not allow people to negotiate prices freely. For example, it is no coincidence that in the 1970s, when there were legal caps on the price of gasoline and prices were not allowed to rise to their market-clearing levels, long gasoline lines developed and maximum limits were placed on how much gasoline people were able to purchase. On the other hand, even recently where world oil and gasoline demand has been very high relative to supply, prices have been allowed to rise to their "equilibrium levels" so persistent shortages at the gas pump have not developed.

This highlights a key role of freely fluctuating prices, namely to coordinate the plans of market activities — that is, to insure that producers produce in the quantities that satisfy the desires of customers. When price increases alleviate shortages or prevent shortages from ever occurring, or when price cuts reduce oversupplies of goods, order is being established and chaos is being averted. It is important to point out that this happens *spontaneously* through the voluntary interactions of buyers and sellers. In fact, this process cannot be orchestrated or mimicked by government through the use of market regulations or price controls.

The importance of this spontaneous, voluntary interaction cannot be overestimated. When prices are not allowed to adjust to changing market conditions, chaos can and will ensue. Once again it is instructive to turn to the energy crisis of the 1970s, when oil and gasoline markets were dominated by price controls. Prices were kept from rising to their market-clearing levels during key periods where "shocks" in the market made oil suddenly more scarce — namely during the Arab oil embargo of 1973-74 and the Iranian revolution of 1979. These price controls, instituted by President Nixon and continued by President Carter, caused not only severe shortages and long gasoline lines, but a great deal of social unrest. People began to steal gasoline from each other's gas tanks and fights broke out as people waited for hours in lines at gas stations. All of that was the result of price controls.

> *Price controls during the energy crises of the 1970s caused not only severe shortages and long gasoline lines, but a great deal of social unrest.*

While, there have been similar interruptions in oil and gasoline supplies since the 1970s, such as when Iraq invaded Kuwait in 1990, price controls were not imposed and adjustments were made in an orderly manner, avoiding both market and social chaos. This took place because President Reagan eliminated price controls in 1981, and since then prices have been allowed to adjust to dramatic changes in supply and demand.

After Pres. Reagan eliminated price controls in 1981, prices could adjust to drastic changes in supply and demand (such as Iraq's 1990 invasion of Kuwait) without social chaos.

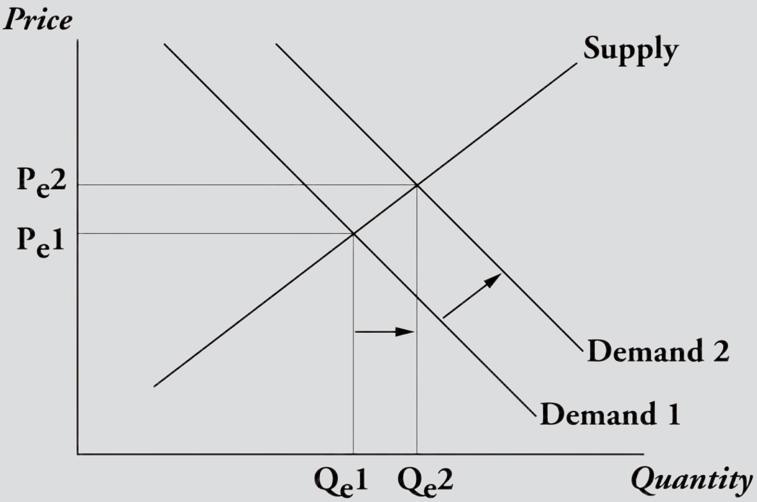
The only exceptions have been during natural disasters when state price controls, commonly referred to as "price-gouging laws," have gone into effect. (These will be discussed at greater length below.)

Beyond Coordination: Sending the Right Signals

Besides the very important function of coordinating supply and demand and eliminating shortages and surpluses, price signals also provide incentives to route resources to where they are most urgently needed. Businesses base their profit and loss accounting on prices. In particular, calculations of profits and losses are based on the prices received for the product being sold (i.e., revenues) and the prices paid for the inputs used to produce the product (i.e., costs).

If people desire a product more intensely, demand for that product shifts up (to the right in Diagram 2) and prices rise. As noted, this price increase prevents shortages of the product from occurring, but it also sends a signal to the producers to produce more of the product to accommodate the consumers' desires. In this case, the higher price means higher profits, which attracts new investments.

DIAGRAM 2



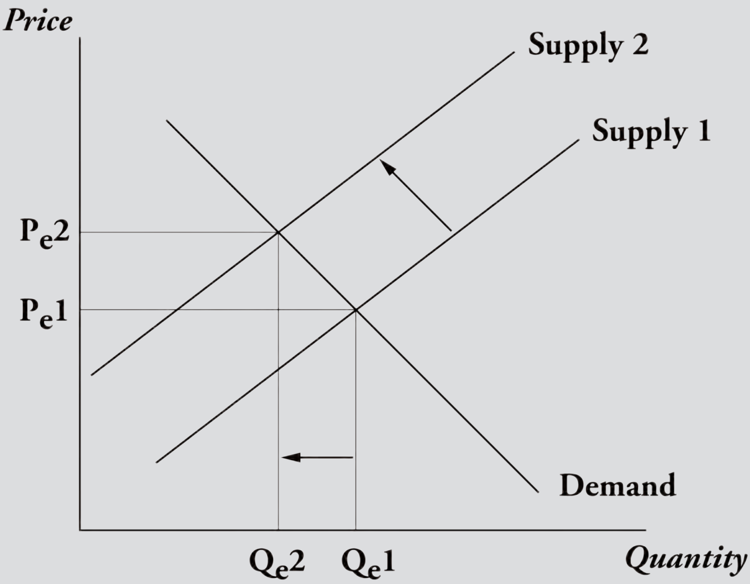
The higher prices, through the system of profit and loss, encourage producers to act in accordance with consumer wants. If consumer desires changed in the opposite direction, this process would work in reverse. The lower prices would discourage additional investment in this product, and resources would flow into the production of goods and services that consumers desire more intensely.

> *Price signals also provide incentives to route resources to where they are most urgently needed. Businesses base their profit and loss accounting on prices.*

Consumers are also motivated to react “correctly” to price changes that are stimulated by changes on the supply side of the market.

For example, if the supply of a resource declines, possibly because of an increase in the price of an important natural resource, shifting

Diagram 3



the supply curve in Diagram 3 to the left, prices will rise. This price increase will not only prevent shortages of the resource from developing, but it will do that by encouraging consumers to conserve on the product that is in shorter supply. At the same time, the higher prices — in this case for the natural resource — and the potential for higher profits that they might bring will encourage suppliers to search out new supplies or suitable substitutes.

Nobel Laureate in economics F.A. Hayek discussed this in his classic 1945 article on the nature and importance of prices called "The Use of Knowledge in Society." One of the most important purposes of this article was to explain how price changes in response to changing realities will, without direction from government, bring about the correct behavioral adjustments throughout the economy.

Hayek uses the example of an increase in the scarcity of tin that causes the price of tin to rise, which in turn generates price and behavior changes throughout all relevant markets. Quoting Hayek:

> It is worth contemplating … a simple and commonplace instance of the action of the price system to see precisely what it accomplishes. Assume that somewhere in the world a new opportunity for the use of … tin, has arisen, or that one of the sources of supply of tin has been eliminated. It does not matter for our purpose – and it is significant in that it does not matter – which of these two causes has made tin more scarce. All that the users of tin need to know is that some of the tin they used to consume is now more profitably employed elsewhere and that, in consequence, they must economize tin. There is no need for the great majority of them even to know where the more urgent need has arisen, or in favor of what other needs they ought to husband the supply. If only some of them know directly of the new demand, and switch resources over to it, and if the people who are aware of the new gap thus created in turn fill it from still other sources, the effect will rapidly spread throughout the whole economic system and influence not only all the uses of tin but also those of its substitutes, and the substitutes of these substitutes, the supply of all things made of tin, and their substitutes, and so on; and all this without the great majority of those instrumental in bringing about these substitutions knowing anything at all about the original cause of these changes. The whole acts as one market, not because any of its members survey the whole field, but because their limited individual fields of vision sufficiently overlap so that through many intermediaries the relevant information is communicated to all.”[7]

The point is that by allowing prices to respond to changes in either supply or demand, market participants are motivated to respond correctly to the new market realities that they face. In Hayek’s example, if the price of tin or the prices or substitutes for tin or the prices of "substitutes for the substitutes" were not allowed to adjust, then shortages would have occurred and improper investments would have been made. If price changing is interfered with or prohibited, consumer and producer behavior will be at odds with true market scarcities.

Laws that regulate pricing behavior cannot repeal the laws of supply and demand any more than the government could repeal the law of gravity. Price regulations can only prevent behavioral changes from occurring that bring human decision-making into line with the underlying realities of resource scarcities and human wants.

> *Price changes in response to changing realities will, without direction from government, bring about the correct behavioral adjustments throughout the economy.*

"Price-Gouging" Laws: Making Natural Disasters Worse

From the perspective of economic science, and particularly the subdiscipline known as "price theory," the concept of "price gouging" or "extreme pricing" or "unreasonable pricing" has no meaning. In fact, none of these terms appear in the index of any of the five most widely adopted principles of economics textbooks used in college classes in the United States.[8] The extent to which this price-control law ignores economic analysis cannot be overstated. It has no grounding in the role of prices discussed above. As noted, while the law specifies several factors that should be used to determine whether prices are illegally high, including facts that are completely irrelevant (such as the average price over the previous 60 days), there is no mention of whether the prices are consistent with actual conditions of supply and demand — which, from an economic perspective, is all that matters.

In reality the main purpose of such laws is to punish sellers who might be pricing according to actual supply and demand conditions. If a seller is charging a price that is truly extreme, higher than buyers are willing to pay, he will make either no sales or fewer sales than he would ideally like to make given his inventory. In other words, it would be a price above the market-clearing price in Diagram 1.

The Special Role of Price Increases During Emergencies and Natural Disasters

In terms of public welfare and social order, it is particularly important to allow the price system to work freely during times of natural disasters and emergencies such as hurricanes or severe weather. During these times, upward pressure is put on prices from both the supply and the demand sides of the market. Prices should be allowed to rise as quickly as possible to reflect these market conditions.

Consider the case of gasoline before and after a hurricane. What is typical in such conditions is that consumers, in anticipation of the hurricane, tend to hoard gasoline by purchasing much more than they will need for any reasonable length of time following the hurricane. A family with three cars may run out and fill all three cars' tanks and may also fill extra containers in anticipation of shortages in the hurricane's aftermath. If prices are allowed to rise as the demand increases, this "hoarding" behavior will become increasingly more expensive and therefore discouraged. In other words, the higher price encourages conservation right at the time when it is most needed. This will leave more gasoline in the tanks at the gas stations where it is available for those who really need it both before

> *The term "price gouging" doesn't even appear in the index of any of the five most widely adopted principles of economics textbooks used in college classes in the United States.*

the hurricane and during its immediate aftermath, instead of in the tanks of cars that are sitting in people's garages or driveways.

Ultimately these higher prices are what prevent shortages and closed gas stations. The higher prices brought about in times of emergency are not about the exploitational greed of businesses but rather about protecting consumers from the hoarding behavior of their fellow citizens. Also, the higher prices help to ration what could turn out to be reduced supplies over time. For example, if gas stations' tanks cannot be restocked in the immediate aftermath of the storm, possibly because of flooding or road damage, the gasoline that is *conserved* (as opposed to hoarded) prior to the storm will be available during this period. And assuming that prices continue to be allowed to efficiently reflect the conditions of supply and demand, shortages will not develop.

This points to one of the ways that price-control laws during time of disaster make the disaster worse. People hoard goods — gas, ice, bread, milk, etc. — in anticipation of shortages in the aftermath of the hurricane. The price-control laws, by keeping prices artificially low in the face of increased demand and reduced supplies, guarantee that these shortages actually occur by encouraging the wasteful and ultimately harmful behavior that a free market would discourage.

A free price system would also encourage the appropriate behavior on the supply side. While higher prices discourage hoarding on the part of consumers by increasing profits, they also encourage the generation of more supply by producers and sellers.

Higher prices during emergencies aren't about the exploitational greed of businesses but instead are about protecting consumers from the hoarding behavior of their fellow citizens.

Economist James Doti tells of one incident from his time as a graduate student at the University of Chicago in the 1950s that highlights this supply-side response.[9] He tells of a particularly bad snowstorm in the city where everyone flocked to neighborhood grocery stores for the usual supplies of milk, bread, batteries, etc. Most of the stores did not raise their prices and soon ran out of supplies. There was one store, however, that was well-stocked and was able to stay open throughout the entire storm. This store chose to double all of its prices. Instead of hoarding supplies, shoppers purchased only what they absolutely needed to get them through the storm. But beyond this, with the higher profits that the grocer earned, he was able to hire neighborhood kids to make trips with sleds to a warehouse where they picked up the supplies needed to keep the store open.

> *Higher prices and the increased profits they bring about create incentives for people inside and outside the affected area to try to find ways to fill the supply gaps as soon as possible.*

Whether or not the law or some politician wants to call this "price-gouging" behavior is irrelevant. The fact is that by choosing to double his prices, the grocer made life during that particular storm in that particular Chicago neighborhood better, not worse. While his competitors did not raise their prices and had to shut their doors to customers in need, the store that doubled its prices continued to serve the community throughout the entire ordeal.

It should also be noted that if all of the area stores had raised their prices, available supplies would have been greater and the general price increase would have been less. In other words, overall prices during the snowstorm would not have needed to be doubled in order to clear the market. The reality is that higher prices and the increased profits that they bring about create an incentive for people both from inside and outside the affected area to try to find ways to fill the supply gaps, and to do it as soon as possible while the crisis and the temporary profit opportunities exist.

Price-gouging laws like the one implemented in North Carolina short-circuit the market process and its beneficial effects. First, by keeping prices lower than their market-clearing levels, they encourage overbuying by consumers. This occurs at a time when conservation is needed the most. By encouraging overbuying, they induce shortages of critical items, such as ice, gasoline, batteries, and basic food supplies.

It should also be noted that price-gouging laws do not help low-income families. Instead they benefit those people who can get to the stores or gas stations first, before the shortages occur. This, in fact, is not likely to be lower-income, working-class families with both husband and wife having to work. Instead, it is more likely to be those people who can either afford to take time off from work or have one spouse at home who is able to take the time and get to the store.

> *Price-gouging laws do not help low-income families. Instead they benefit only those people who can get to the stores or gas stations first, before the shortages occur.*

During the gasoline shortfalls brought about by Hurricane Katrina, the latest amendments to North Carolina's law had not yet been passed. As noted, until July 2006, when these changes were put in place, the state's price-gouging law applied only to areas where a state of emergency or disaster was declared. This meant that prices in North Carolina were allowed to adjust freely to the dramatic reductions in gasoline supplies. Because gasoline venders at the wholesale and retail levels were not fearful of raising prices to levels that they thought appropriate, gasoline customers made it through the crisis able to purchase the gasoline they needed, albeit at higher prices. In other words, there were no long gasoline lines and no rationing.

In Georgia, however, where the governor used emergency powers to invoke price-gouging laws, long gasoline lines were common.[10]

In addition to encouraging wastefulness on the part of the consumer and causing shortages, price-gouging laws also prolong the hardship suffered by the population during the aftermath of a disaster. They do this by reducing the rewards (profits) for increasing supplies. If, for example, a convenience store is forced to use the average price that it sold the ice for during the 60 days previous to the emergency as a reference point, what incentive is there to do as the grocer did during the snow storm in Chicago — find innovative ways to restock its supplies? The fact is that the price during any previous time period is irrelevant to the appropriate price during and after the storm.

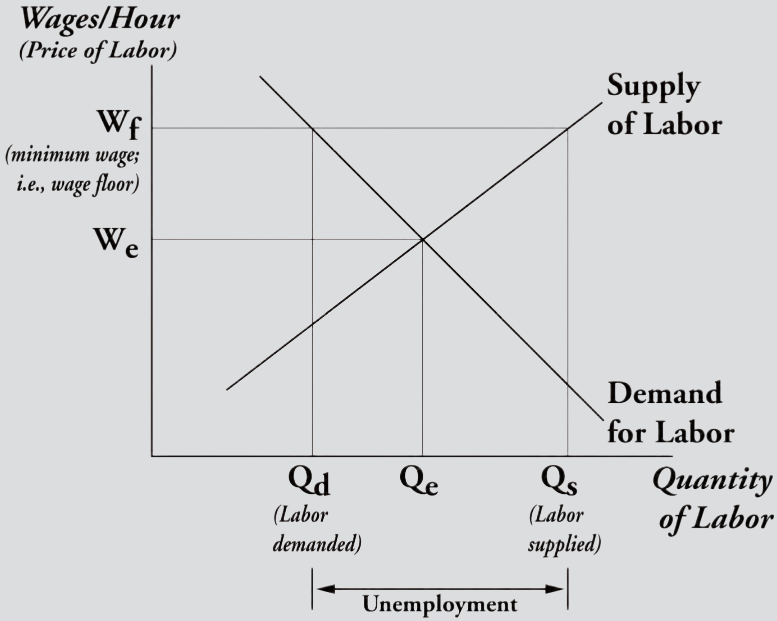
> *Price-gouging laws also prolong the hardship suffered by the population during the aftermath of a disaster. They do this by reducing the rewards (profits) for increasing supplies.*

In order for prices to do their job in a market, they must be able to adjust to reflect the supply and demand conditions of the moment. The price of the product in the past is irrelevant and completely arbitrary as a benchmark for public policy.

MINIMUM-WAGE LAWS: HARMING THE MOST DISADVANTAGED WORKERS

As noted, North Carolina has recently raised its minimum wage to $6.15 per hour. The new minimum is scheduled to go into effect on January 1, 2007. That is one dollar higher than the federal minimum of $5.15 per hour. Regardless of what the minimum is, the economic analysis is the same. Minimum-wage laws harm those workers among us who are the least educated and lowest skilled.

Diagram 4



The Unemployment Effect

A minimum wage is known as a price floor. What minimum-wage laws seek to do is keep the price of labor (i.e., wages) from falling below a certain level. As with all laws meant to keep prices above the price that would be established by actual supply and demand conditions, minimum-wage laws cause surpluses. In this case, what is being sold is labor.

The term commonly used for a surplus of labor is "unemployment" (see Diagram 4 for the standard graphical analysis in terms of supply and demand). But the best way to think about the effects of the minimum wage is to think of what wages are really about and how decisions about hiring and not hiring are conceptualized outside the context of the traditional supply-and-demand diagrams.

In deciding to hire anyone, an employer must answer a fundamental question: *Will the value of the productive output of the potential employee be greater than the cost of hiring him or her?* From a pure business perspective, this is the only way a hire can be justified. Because of this, minimum-wage laws price certain people out of the labor market.

With mandated employer taxes such as those required for Social Security and Medicare, at a wage of $6.15 per hour it will cost a potential employer about $7.00 per hour to hire a new employee. What that means is that everyone whose skills are such that they cannot generate more than $7.00 per hour's worth of productive output will be unable to find work. That will not, of course, affect college graduates, accountants and skilled manual laborers such as electricians and plumbers. It will instead affect those in society who have little education and little or no job experience — teenagers, high school dropouts, etc.

> *Each increase of 10 percent in the minimum wage results in an estimated 2.9 percent decrease in the likelihood that a low-skilled worker will find employment.*

Recent empirical estimations by two Duke University economists suggests that for each increase of 10 percent in the minimum wage, there will be a 2.9 percent decrease in the likelihood that a low-skilled worker will find employment.[11] For an increase in the state's minimum wage from $5.15 to $6.15 per hour, the trade-off implies a 5.5 percent decline in the chances that a low-skilled worker will find employment. In other words, the minimum-wage increase has placed one more obstacle in the path of those low-skilled workers who already start out severely disadvantaged in the marketplace.

Unemployment statistics for North Carolina suggest that even the federal minimum wage of $5.15 per hour has had a negative impact. For 2004, the most recent data available, the difference between the general unemployment rate and the unemployment rate for teenagers and younger African-Americans — two categories of workers that contain the least educated and lowest skilled in society — is quite significant. While North Carolina's overall unemployment rate for that year was 5.4 percent, the teenage unemployment rate was 19.2 percent. While the unemployment rate for African-American teenagers is not available, it was clearly much higher than the overall teenage rate because the unemployment rate for white teenagers was only 14.3 percent. The unemployment rate for 20-to-24-year-old African-Americans was 18.7 percent.

In preventing very low-skilled workers from entering the labor force, minimum-wage laws deny them the opportunity to move up the economic ladder.

Those are all categories of workers that the economic theory predicts would be adversely harmed by the minimum wage. There is little doubt that these numbers would be significantly lower in the absence of a minimum wage.

As with supporters of other kinds of price-control laws, advocates of minimum-wage laws ignore the economic analysis and the idea that there is any relationship between productivity of the worker and wages paid. They buy into the myth that people's wages can simply be raised by government decree without any change in workers' productivity. By assuming that increasingly higher minimum wages will cause no one to be unemployed, they are making one of two assumptions, both of which are absurd. They are assuming either that there is no one in the labor force whose skills are so low that they cannot command the higher wage or that employers simply ignore worker productivity when considering the wages they have to pay.

Removing the Economic Ladder

In preventing very low-skilled workers from entering the labor force, minimum-wage laws deny them the opportunity to move up the economic ladder. For most poorly educated young workers, work experience is more important than salary level. On-the-job experience and training are what ultimately allow them to climb the economic ladder to better-paying jobs.

Low wages define poverty, but they do not cause it. Wages, like other prices, reflect underlying realities. In this case, the underlying reality being reflected by low wages is that there are many people in North Carolina whose skills are so low that they cannot command a market wage that is higher than $5.15 or $6.15 an hour. The market wage is the messenger that conveys this reality.

If policymakers are truly concerned about helping those earning the lowest incomes in the state, the first question that they should ask relates not to their wage but to their skill level. Why is it that there are non-teenage workers whose skills are so low that they cannot command a “living wage” (to adopt the phrase used by supporters of higher minimum wages)? The answer to this question is beyond the scope of this paper. But clearly the focus should be shifted to issues related to educational reform and how institutions might be rearranged to better facilitate the acquisition of marketable skills and work experience.

North Carolina’s Usury Laws and the Ban on Payday Lending

As noted in the opening section of this paper, North Carolina has caps on interest rates. But since most of these rates are set quite high, the caps are well above the market-clearing rate for loanable funds, so they do not have an impact on the day-to-day availability of most loans. If this situation were viewed in terms of supply and demand, the interest-rate cap would be above the rate that the market would set. In such cases no shortages are generated. An important exception to this has been what are called "payday lending" institutions.

Payday lenders are in the business of advancing people money for short periods of time, typically 15 to 30 days. They provide a service that traditional lending institutions are not willing to offer and that their customers both want and find valuable.

How does it work? First the borrower needs to be gainfully employed with a steady paycheck. The lender accepts a personal check from the borrower with a promise that he will not cash the check until a specified time, usually 15 to 30 days into the future. In exchange for the check, the lender gives the borrower an amount of cash that is worth less than the check's face value. For example, the borrower may write a check for $300 to the lender and receive $255 in exchange. The borrower receives the cash he needs today and the lender earns $45 on the transaction 30 days later. The fee varies according to the amount borrowed. Fifteen dollars per $100 borrowed is typical. Check-cashing companies typically receive 10 percent of the amount of a personal check, so payday lenders receive an extra 5 percent for waiting as long as 30 days before cashing the check.

Payday lenders' charges may be high relative to conventional loans, but they help people avoid even higher late-payment charges or penalty fees for returned checks.

Opponents of payday lending are quick to point out that these fees amount to annualized interest rates of close to 400%, thereby violating North Carolina's legal interest-rate caps. For this reason a special "payday lending law" was passed in 1997 creating an exception for payday lending businesses and allowing them to operate.[12] That law expired in 2001 and was not renewed, once again outlawing these businesses under the state's usury laws. As an ardent opponent of these businesses, North Carolina Attorney General Roy Cooper has stated, "We've fought payday lending at every turn and now we're putting this industry out of business here in North Carolina."[13] But as with all price-control laws, usury laws tend to harm those whom their proponents claim to be protecting.

In addition to helping someone get through a short-term financial crises, payday lending can provide some people a chance to save money. An April 2000 PBS report[14] cited a case of a bus driver who borrowed $250 from a payday lender to make a car payment on time. As the report noted, "the $37.50 fee he paid was cheaper than the late fee on his car payment." Furthermore, PBS noted that "the rates are higher than credit card fees … but cheaper than the cost of writing bad checks." In other words, the costs may be high relative to conventional loans, but they allow people to avoid even higher late payments and penalty fees that banks and stores charge for returned checks.

Payday lenders' critics may use expressions like "predatory lending" and "legal loan-sharking," but they know they can't accuse payday lenders of defrauding their customers.

The attorney general, self-proclaimed "consumer advocacy" groups such as the N.C. Justice and Community Advocacy Center, and the American Association of Retired People (AARP) have consistently been in favor of using North Carolina's price controls on interest rates as a tool to keep payday lending illegal. But in fact, they are thwarting the will of the very ones they claim to be protecting. While it is common for opponents to use expressions like "predatory lending" and "legal loan-sharking," they are not charging that payday lenders are defrauding their customers, promising a product and not delivering, or breaking their legs when payments are late. In fact, from all appearances payday lenders in North Carolina provided a service that customers freely chose to purchase in full knowledge of the terms of agreement. Furthermore, it is clear that people who used the service did so because they felt that it offered them benefits that they could not otherwise obtain.

North Carolina's Floor on Gasoline Prices: Can Gas Prices Really Be Too Low?

While most people would not argue that a gasoline station could possibly charge too little for a gallon of gas, the North Carolina General Assembly disagrees. North Carolina's "Motor Fuel Marketing Act" prohibits pricing gasoline for less than it cost the merchant to purchase the gasoline, when the "intent or effect" is to "injure competition."[15]

Like other forms of price control, this law makes very little sense. First, it should be reiterated that the intent, if not always the effect, of all truly competitive behavior is to "injure competition." In other words, what businesses in an open market attempt to do, through advertising, product innovation, location decisions, and pricing policies of all kinds, is convince customers to buy from them rather than others in the market. To the extent that they are successful, those others — i.e., their competition — will be injured. In fact, if they cannot respond effectively they may even go out of business. In other words, to complain that a business is pursuing strategies that may injure competition is to complain about the competitive process itself.

> *To complain that a business is pursuing strategies that may injure competition is to complain about the competitive process itself.*

So what is the problem with below-cost pricing as a specific tool of attempting to "injure competition"? The idea behind this law is to prevent what is known as "predatory pricing." A strategy of predatory pricing implies that a business, in this case a gas station, will charge below cost in order to drive its competitors out of the market. Once that occurred, the gas station would then have a monopoly and would raise its prices to monopolistic levels, ultimately harming consumers. While this strategy, on its face, may sound like it should be a public-policy concern, the fact is that, as an actual business strategy, predatory pricing is impossible to sustain.[16]

Obviously, from a consumer's perspective, the prospect of having several gas stations so aggressively competing for their business could only be considered a windfall.

Unfortunately, the idea that predatory pricing is a common business practice and something that needs to be thwarted by legally prohibiting below-cost pricing is a myth that is widely held by the general public. As one economist has noted:

> [The predatory pricing businessman] is a significant figure in the public's perception of economic affairs and undoubtedly exerts a very considerable influence on its attitude toward economic matters in the large, particularly its view of the government's role in economic policy ... The economic literature, on the other hand, accords this ubiquitous character no such front and center role on the economic stage. Indeed, the standard theoretical analysis in this area treats predation as a form of ... irrational ... behavior and thus *an unlikely occurrence in the real world.*[17] (Emphasis added.)

Why is Predatory Pricing an Unlikely Business Strategy?

Predatory pricing is a very risky approach to overtaking one's competition in the market. First, in order to pursue the strategy, a business must be in a position to sustain losses for an indeterminate length of time. Unless a gas station is starting from an initial position where there is already little or no competition in the market — i.e., unless it is already a monopoly — then it is unlikely to have been earning very high profits over a long enough period to build up a "war chest" of revenues to carry it through a sustained period of losses. In other words, unless the gas station is starting from the monopoly position that it would be seeking by invoking a predatory strategy, it would not be in the economic position necessary to carry out the strategy.

The actual effects of North Carolina's Motor Fuels Marketing Act prohibiting the below-cost pricing of gasoline are to harm competition and to keep prices high.

But having a war chest would only be the first problem. There are other uncertainties. For one, there is no way of knowing how its competitors might respond. Instead of simply rolling over and leaving the market, competing gas stations might respond in kind, matching or even beating the low prices. In other words, an aggressively competitive "predatory" pricing strategy on the part of one gas station in an area may simply trigger a price war among several gas stations, increasing the cost of the predatory strategy. Obviously, from a consumer's perspective, the prospect of having several gas stations so aggressively competing for their business could only be considered a windfall.

The final hurdle and risk would come with success. As unlikely as this is, assume that the gas station succeeded in its strategy and drove all other gas stations out of the area. Its purpose wasn't simply to be the sole gas station in the market but to be able to charge monopoly prices and earn high monopoly profits. But by doing this it would simply be inviting new competition to enter the market. Clearly it is quite easy for new gas stations to enter a market. By charging noncompetitive prices, the predatory gas station would simply be creating profit opportunities for other entrepreneurs to open up new gas stations. In other words, in order to fend off new competitors, it would have to refrain from taking advantage of its monopoly position. This is part of the reason why, as the quote above notes, economists consider predation to be simply irrational behavior. The point of taking losses during the predation process is so that those losses can be made up for with exorbitantly high prices and profits once the monopoly position is established. But by actually carrying out the plan, the high profits earned by the predator simply invite other entrepreneurs to enter the market, creating new competition to take the place of the businesses it sought so hard to drive out of the market in the first place.

A Legitimate Tool of Competition

The actual effects of this law are to harm competition and to keep prices high. While the use of below-cost pricing as a method for monopolizing the market makes no economic sense, it can and might often make sense as a legitimate tool of competition. For example, a new start-up gas station in an area may want initially to charge prices that are below its cost to entice existing customers in the area away from gas stations that they are currently patronizing. The idea is not only to get the customers to buy their gas but, since gasoline is usually sold as part of a larger convenience-store or even fast-food operation, to bring them in and expose them to the new store's other products. The cheaper gas is a way of introducing them to the rest of the operation and the other product lines being offerer. New entrants into a market are automatically at a disadvantage because they are an unknown quantity and also have to overcome the existing

> *Below-cost pricing laws aren't about protecting competition but protecting existing gasoline stations from competitors, with the real losers being the gasoline-buying public.*

loyalties of customers. What these below-cost pricing laws do is protect the existing firms from aggressive new competitors.

But even if a gas station is not a new entrant, it may want to use, at least for a period of time, a below-cost pricing strategy simply as a way of attracting new customers into its business and exposing them to other products — to get them to buy a cup of coffee, a snack or even a meal. They may believe that, by offering an item such as gasoline at a price that would not generate a profit, they may enhance the overall profitability of their entire operation through additional sales of other items where the profit margin might be greater.

The point is that these are legitimate pricing strategies aimed at better satisfying customer wants and enhancing the overall success of the business. They are part and parcel of the dynamic and rivalrous competitive process, and to outlaw these practices harms consumers. In reality this law is not about protecting competition but protecting existing gas stations from competitors, with the real losers being the gasoline-buying public.

"Now let me state the present rules,"
The lawyer then went on,
"These very simple guidelines,
You can rely upon:
You're gouging on your prices if
You charge more than the rest.
But it's unfair competition if
You think you can charge less!

"A second point that we would make
To help avoid confusion...
Don't try to charge the same amount,
That would be Collusion!

"You must compete. But not too much,
For if you do you see,
Then the market would be yours –
And that's Monopoly!"

– Excerpt from "Tom Smith and His Incredible Bread Machine," by R.W. Grant [18]

Conclusion

The excerpt from R.W. Grant's classic poem captures the wrongheadedness behind North Carolina's price-control laws. The fact is that it is impossible for lawmakers to improve on the prices that are arrived at through the interplay of supply and demand in the marketplace. Every free exchange makes both parties better off. Every exchange that is prevented because the government has outlawed the price that would bring about agreement between potential trading partners harms those parties by preventing them from pursing a course of action that would improve their well-being. Hence, North Carolina's so-called price-gouging laws harm people by creating shortages of products just at the moment when consumers need them the most; minimum-wage laws cut the lowest-skilled workers in our society out of the labor market, relegating them to the unemployment lines and welfare roles and keeping them from gaining a foothold on the bottom rung of the economic ladder; the state's usury laws reduce access to needed finances for those in the state who are the least financially secure; and the state's prohibition of below-cost gasoline prices harms consumers by, in some instances, causing prices to be higher than they otherwise would be and by reducing competition. In every case, the people who are harmed by the laws are those that, presumably, the laws are designed to help.

The only posture that state, local, or federal governments should take with respect to prices is to stay out of the way. Prices that are freely agreed to in the marketplace prevent shortages and surpluses and also convey information about consumer preferences as well as product and resource availabilities. Ultimately prices direct productive activities in ways that are most consistent with societies' wants and needs. In doing that, those same prices coordinate plans and prevent both market and social chaos. For these reasons, price controls of any kind are anti-social and inconsistent with the goal of creating a free and prosperous society.

End Notes

1. Socialist economies, like China or the former Soviet Union, are exceptions, as are price controls during war-time in more capitalist systems. A time in the United State that fits neither of these examples was during the 1970s, when President Nixon invoked his "wage/price freeze" in a futile and ignorant attempt to "fight inflation."

2. House Bill (HB) 1231, "An Act to Protect Consumers From Extreme Pricing Practices," General Assembly of North Carolina, found at *www.ncleg.net/Sessions/2005/Bills/House/HTML/H1231v4.html*.

3. HB 2174, "Raise minimum wage," General Assembly of North Carolina, *www.ncleg.net/Sessions/2005/Bills/House/HTML/H2174v5.html*.

4. "North Carolina Consumer Finance Act," *www.ncleg.net/EnactedLegislation/Statutes/HTML/ByChapter/Chapter_53.html*, *www.ncleg.net/EnactedLegislation/Statutes/HTML/ByChapter/Chapter_24.html*.

5. The latest, amended version of the act (March 2005) can be found at *www.ncga.state.nc.us/Sessions/2005/Bills/Senate/HTML/S986v1.html*.

6. Found at *lazowska.cs.washington.edu/scienceforum/tsld085.htm*.

7. F. A. Hayek, "The Use of Knowledge in Society," *The American Economic Review*, Vol. 35, No. 4, Sept. 1945. Reprinted in *Hayek, Individualism and Economic Order*, (Chicago: University of Chicago Press), 1948, quote found on pp. 85-86.

8. In order of rank: Campbell McConnell, *Economics*, 16th ed, (Chicago: Richard D. Irwin, Inc) 2005; Gregory Mankiw, *Principles of Economics*, 3rd ed. (Boston: South-Western Publishing Co.) 2004; Carl Case, *Principles of Economics*, 7th ed. (Upper Saddle River, N.J.: Prentice Hall, Inc.) 2004; William Baumol amd Alan Blinder, *Economics: Principles and Policy*, 9th ed. (Boston: South-Western Publishing Co.) 2005; Roger Miller, *Economics Today*, 12th ed. (Boston: Addison, Wesley, Longman, Inc.) 2004. Rankings provided by Monument Information Resource, "College Textbook National Market Report."

9. James L. Doti, "Capitalism and Greed" in James Doti and Dwight Lee, ed., *The Market Economy: A Reader* (Los Angeles: Roxbury Publishing) 1991, p. 4.

10. Christopher Boyce, "Panic buying fuels gas lines," *Columbus Ledger-Enquirer*, September 1, 2005.

11. Peter Arcidiacono and Tom Ahn, "Minimum Wage and Job Search: What Do Employment Effects Really Measure?" Employment Policy Institute, August 2004, *www.epionline.org/study_detail.cfm?sid=75*.

12. SL 1997-391, "An Act to Regulate Check Cashing Businesses," *www.ncga.state.nc.us/Sessions/1997/Bills/Senate/HTML/S312v3.html*.

13. Roy Cooper, North Carolina Attorney General, "Pay Day Lending on the Way Out," press release, March 1, 2006, *www.ncdoj.com/DocumentStreamerClient?directory=PressReleases/&file=paydaylenders3.06.pdf*.

14. "Payday Lending," Online News Hour, April 3, 2000, *www.pbs.org/newshour/bb/business/jan-june01/payday_04-03.html*.

15. "The Motor Fuel Marketing Act," *www.ncga.state.nc.us/Sessions/2005/Bills/Senate/HTML/S986v1.html*.

16. See Roland H. Koller II, "The Myth of Predatory Pricing: An Empirical Study," in Yale Brozen, ed., *The Competitive Economy* (Morristown, N.J.: General Learning Press) 1975, pp. 418-428. The most infamous alleged monopoly "predator" was John D. Rockefeller's Standard Oil in the late 19th Century. Serious research into Standard's pricing behavior, however, demonstrates that even this, the most notorious "example" of predatory pricing in U.S. business history, has no basis in fact. See "Predatory Price Cutting: the Standard Oil (J.J.) Case," *The Journal of Law and Economics*, Vol. 1, 1958, reprinted in Brozen, ed., *The Competitive Economy*, p. 380.

17. *Ibid.*, p. 418.

18. R.W. Grant, from "Tom Smith and his Incredible Bread Machine," *www.vex.net/~smarry/oldbbs/bread.html*.

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About the John Locke Foundation

The John Locke Foundation is a nonprofit, nonpartisan public policy institute based in Raleigh. Its mission is to develop and promote solutions to North Carolina's most critical challenges. The Locke Foundation seeks to transform state and local government through the principles of competition, innovation, personal freedom, and personal responsibility in order to strike a better balance between the public sector and private institutions of family, faith, community, and enterprise.

To pursue these goals, the Locke Foundation operates a number of programs and services to provide information and observations to legislators, policymakers, business executives, citizen activists, civic and community leaders, and the news media. These include the foundation's monthly newspaper, Carolina Journal; its daily online news service, CarolinaJournal.com; the Locke Letter, a quarterly newsletter for donors; regular events and conferences on important public policy issues; and research reports of varying lengths on topics facing state and local governments.

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