



# Merits & Demerits of Governmental Intervention on Pricing System with Emphasis on Controlling Organization Role

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## ABSTRACT

**Objective:** The issue of government intervention in pricing has always been discussed by experts and economists, and various theories has been proposed by supporters of closed economy and opponents of government intervention in the pricing (open economy). Generally, the role of government has been very crucial in facing price control policies in the development of national industry, or in destruction and lack of competitiveness of industry and economic backwardness. However, government's non-intervention in pricing and lack of attention to the prices of goods and services at various times, such as: Natural disasters, wars, etc will have many deleterious effects and may even lead to public discontent. In unusual conditions the governments as the main policy makers in the field of economy must take necessary measures in supporting people particularly the vulnerable ones against unreasonable fluctuations in commodity and service prices and control inflation through different tools such as payment of subsidies, and avoid the rise in prices of goods and services. It has a crucial role in establishing social justice and equitable distribution of income. **Methodology:** Studying the economy of the country after the glorious Islamic Revolution indicates the presence of government in the market and special attention of the authorities to the pricing of goods and services at various times, such as during the Sacred Defence period, development period and targeted subsidies law enforcement period. **Results:** Since the intervention of governments in pricing in normal circumstances is not justified and it may have various consequences such as lack of competitiveness of national products in the international arena, reduction of the private sector's motivation to invest in the production, the existing bureaucracy in pricing system by the government and the lack of attention to market supply and demand mechanism, faces the government's success with some doubts in achieving the goal of affordable consumer goods and continuity in this process causes reduction in supply due to lack of interest of the producers in competing with the prices provided by the government which ultimately leads to economic under development because of the lack of private sector participation. **Conclusion:** Hence it is tried to explain and describe the role of regulatory agencies to access the Resistive Economy policies purposes with an increasing domestic production approach in order to access international markets, domestic and foreign investment attraction, transparency and healthy economic and distribution systems and pricing, utilizing up-to-date market supervision methods with some advantages and disadvantages of government intervention in pricing.

## 1. Introduction

Economists have always been discussing about the intervention in the pricing from the far past, and today the intervention of government to create progress and development is inevitable. In general, there are two types of views in this regard as the economic freedom and command economy. However, note that the delimitation and the size of government interventions in pricing is also investigable and based on the specific economic conditions, the issue

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of intervention or non-intervention in the pricing can have positive and negative effects on the economy of a country. The foundation of the theory of economic freedom, or economic liberalism is based on the ground that economic decisions as much as possible must be made by the private sector and activists in the field of economy and governmental agencies or organizations apply minimal intervention in economic affairs (Perkins et al., 2001).

This belief is based on the overall support of the market economy and private property in the micro and macro-economic issues, including issues related to the production, although economic liberalism can support government regulations and laws up to a certain point, but when the government intervention in the market, creates restrictions on free trade and competition, it opposes with it. In other words, in the classical view government must have the minimum intervention in the economic affairs (Krier and Montgomery, 1973).

Of course, this group seeks an unlimited market by the government, and believes that government has a vital role in providing public goods, in contrast, some are proponent of command economy that is just the opposite of the theory of economic liberalism. Command economy view is proposed against open economy and it refers to an economic system which is formed according to the order of a non-private institution or organization which is the executive of governmental policies and mainly includes systems such as the socialistic economic system and governmental economy (Wood, 2002).

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## 2. Materials and methods

In general, command economy is the same as command pricing, command economy fans believe that with the arrival of the government in the field of pricing, the double pressure is prevented from the consumers in the face of price fluctuations (Poulton et al., 2006). Due to the sensitivity of the issue of government intervention in pricing and its impact on growth and development of different economic sectors given that the pricing policy in terms of economic efficiency in that sector while providing consumers needs can also adopt the path of growth and prosperity and lead to economic development and entrepreneurship or on the other hand destruction of economic enterprises and disturbance of the profitability of industry and production (Gal, 2004). Therefore, one of the most dramatic examples of government intervention in the economy, is command economy or price controlling of goods and services. However, government intervention in economic affairs is not a new phenomenon and study of the history of different countries suggests this fact. According to the conducted studies the history of pricing goes back to middle ages which was about lowering the price of bread (Ismet et al., 1998).

With the development of economic relations and highlighted role of public and private sector in the economy, governments have tried to refrain from interfering in the pricing and only "in special circumstances such as natural disasters, wars and so on determine the price of goods and services (Liu et al., 1995). In our country Iran, government has always played a decisive role in pricing and in some cases, because of unfavorable economic conditions, such as: During the imposed war and the years after that, during the implementation of the targeted subsidies, and the hostile international sanctions and economic down turn explain the reason for entering into the market and determining the price of goods and services, and the essential role of government during this period was to prevent illogical raise of the prices and services and control inflation rate with various tools, such as subsidies payment, coupon system, a strong presence in the market through inspection and regulatory systems (Erba and Novakovic, 1995). Due to the effective measures taken by the eleventh government in the economy and reduction of inflation and control of the irrational fluctuations of goods and services it appears that in the current conditions the issue of price controls on goods and services with the goals and key economic indicators such as: economic development, productivity, and reducing the unemployment rate was evaluated and regulatory policy orientation is moved to minimal intervention about essential commodities, therefore, in this paper the impact of government intervention in pricing examined (Jinglian and Renwei, 1987).

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## 3. Discussion and results

### 3.1 The Advantages of Government intervention in Pricing:

Due to the lack of appropriate infrastructure in some industries and remaining negative effect Sacred Defense period, the next governments have always tried to support consumers in various forms such as: Stabilization of prices and preventing its rising (the subject of approval No.6954 of the year 1380 (2001) as a system for supply of goods and services price), supplying and storage of goods according to the market demand, and guaranteed purchase of some strategic commodities and subsidizing basic goods manufacturers. This is a sensitive issue and has a special place in the government of the Islamic Republic of Iran because of the importance of social justice and the elimination of all forms of discrimination and equitable distribution of income and by firmly believing in the ideals of the system, they made a sharp reduction in social class differences (Rujing, 2010).

By the outbreak of Imposed War its influence on the macro-economic issues, the government by playing a strategic role through various tools, such as the coupon system in addition to supplying basic needs of people, it supported consumers especially the vulnerable ones against fluctuations in commodity prices (Daugbjerg and Svendsen, 2011). With the end of eight years of Sacred Defense, the government began the implementation of the first five-year plan of economic development after the revolution and there could be seen some signs of open economy in government policies, although the priority of the government is the organization of the country after the Imposed War with a constructive approach (Lin, 2010). But along with these policies regulatory organizations such as the organization of inspection and monitoring of the distribution of goods and services prices, the Governmental Discretionary Punishments Organization and Consumers & Producers Protection Organization have had a leading role in the process of pricing of goods and services, and always have tried to establish the government intervention in this field of economy with the pricing of goods and services and application of the necessary controls in the process of production and distribution as well as punishment of the offenders (Umali-Deininger and Deininger, 2001). With the rise of the reform government, its most basic concern was to reduce inflation that by taking correct economic decisions and establishing price control and investigation committee under the supervision of the first deputy of the president it could reduce the inflation rate of the construction government in 1384 (2005) to less than 13 percent. (History of political economy, Political Economy Development of Iran)

Investigations about the performance of the ninth and tenth government regarding the above discussion, despite the implementation of the great project of targeted subsidies indicates the need for effective government so provision the pricing of goods and services and according to the relevant legislation "Any increase in the price of goods and services should be coordinated with Consumers & Producers Protection Organization (working group market control approval) In this regard, one of the achievements of the government to prevent the rise in prices of goods and services arisen from the enforcement of targeted subsidies and moderation of the effects of increase in energy carriers price (Perkins et al., 2001).

Since the reasons and achievements of government intervention in pricing were noted, in the next section we will explain the performance of government by investigating the weaknesses of controlling goods and services.

### **3.2 The Disadvantages of Government Intervention in Pricing:**

If the performance of governments in controlling prices of goods and services is evaluated with economic indicators such as gross domestic product, raise of domestic and foreign investment, and employment enhancement , we will in fact, find out the obvious weaknesses of government intervention in pricing, and perhaps "the success of government in achieving the aim of providing a cheaper good to the consumer through determining a price lower than the actual price of the goods is called into question (Perkins et al., 2001).

When the price of a commodity is determined based on market conditions and if competition condition is provided for the desired product the equilibrium price will be the price where supply and demand of a good are equal. If the government make manufacturers and providers to deliver the goods at prices lower than the equilibrium price, it definitely "would reduce the tendency of manufacturers to supply products and thus the amount of goods in the market will be reduced. Government might be able to prevent the supply goods with the desired price of manufacturer through command and control prices but can it be claimed that manufacturer has the previous incentive based on the cost of ,as well as diversity and innovation in the production of goods ?The answer is clear and can be clearly understood that producers seek ways to reduce costs and there by achieve the desired profit, to this aim they will begin low quality production, fraud in produced goods and use of low quality raw materials ,and keeping up with the current circumstances would be inevitable. Other disadvantages of the implementation of the command prices and preventing from rising prices of goods and services and pricing based on market supply and demand system and lack of attention to the production with the desired price of the manufacturer is that the production and supply of the desired good for some manufacturers who produce goods with higher production costs and lack of attention to costs through creating productivity, achieving less profit and economic in feasibility of production leads to reduction of the investment for producing the desired products through the private sector, and this issue in the long-term leads to the imbalance of supply and demand for the desired commodity and in this case ,not only the government's main objective which is to protect consumers is unrealized but also causes another problem as economic under development ,so that by creation of a shortage in the market while a false demand is created through supplier education ,i.e.by applying command price and making the desired product cheaper in some cases ,through demand increase and reduction of supply, consumers show more motivation to purchase that good .However ,increased demand and reduced supply of goods ,depends on the type of goods and their market but existence of a short age in the market is the most important characteristic of this type of intervention in which because of the expectation of people who want to purchase the desired commodity with the determined prices would be unable to access to them.

With the extension of this situation and creation of waiting line to get a desired commodity through command prices, another problem will emerge as the necessity to monitor the equitable distribution, and in order to do this important issue there's a strong need for the presence of the said regulatory organizations. It should be noted in this regard that in the most optimistic situation, the government can properly monitor thee quit able distribution and prevent the discrimination and violation of the rights of the waiting consumers, although due to the shortage, the goods are provided for people who are in the front of the line.

Regardless of this issue, a very important point that is neglected in this process and the government should have a fundamental attention toward it is the issue of consumer's time which lose sits value in such situation and if the consumer's time value is evaluated with money criteria, we find that sometimes the consumers' wasted cost is higher regarding the cost of purchasing goods with the desired cost of the producers ,in fact, consumers are spending more money for the desired commodity compared to the time when the government applies its command price .However ,the above conditions without considering issues such as :rent for having a product as many as possible is official corruption, and under these circumstances ,the price paid by consumers for the supply of goods is the same as the desired price of the government . But there is no doubt that part of the consumers must pay a price higher than the price set by the government because of the lack of demand coverage. In this case, government is considered as a factor of the black market (secondary market).

Spending public funds and resources in terms of budget for regulatory agencies is another disadvantage of government intervention in pricing that with regard to the objections raised in the past if there exist true belief and practice about the system of supply and demand among politicians and decision-makers in economics and pricing in addition to reducing the size of government, it would be possible to take advantage of potential of these organizations by defining new tasks ,including presence in market to prevent contraband items and counterfeit goods ,speculation, monitoring the supply of goods having expiration date and soon.

Regardless of the samples and the objective-historical evidences, addressing the reasons of intervention in pricing is also a complex issue, but according to what was said ,the economic justification for pricing of goods and services is very crucial .Although the claims of governments are essentially "done exclusively with the slogan of intervention in the markets, but in fact unilateral action of regulatory agencies such as the Consumers & Producers Protection Organization, the Governmental Discretionary Punishments Organization have been without studying the nature of the goods and services market, and sometimes" intervene in markets that because of intense competition between producers and suppliers of legally and illegally imported goods the incentive to invest in production is destroyed.

Regardless of then numerous motives of the said organizations to interfere pricing, despite elevate legislations such as the Fifth Development Plan, the policies of Resistive economy served by the Supreme Leader, and Principle No. 44 of constitution, unfortunately, the performance of the regulatory agencies were not aligned with the related regulations. As for example in the ninth chapter of the 44th constitution "competition facilitation and monopoly

prohibition "and in Article 44 it was decided that "any conspiracy through contract, agreement (whether written, electronic, verbal or practical) between the parties that disrupt the competition is prohibited "and then the determination of the prices for buying or selling a product or service and its way of determination in the market directly or controlling the production, purchase or sale of goods or services is mentioned (Principle 44th of constitution), but regulatory organization so sensibly take measure in respect to the measures that is an instance of pricing to protect consumers.

With regard to the proposed items and intervention of the effect of government intervention in pricing in terms of advantages and disadvantages of the subject and in order to increase the domestic production and attraction of private sector investment and for entrepreneurship and economic development which is one of the goals of Resistive Economy policy, some recommendations are presented as follows, with an emphasis on the need to revise the tasks of regulatory agencies and compliance with the mechanisms of market supply and demand and removal of abundant and disruptive regulations:

1. Revising laws and regulations that are disturbing to the production and trade
2. Removing regulatory agencies from the pricing of goods and services and competitive market services on the basis of laws
3. Lack of monitoring the price of insensitive and unnecessary goods and transferring authorization to determine the price of goods and services based on supply and demand mechanism
4. Limiting the pricing of goods and services only "for the exclusive and semi-exclusive markets and cases where the system is subsidized
5. Change in the approach of regulatory agencies of the pricing of goods and services to cooperate with the private sector in order to meet the demands of consumers via the domestic production and creating incentives to attract investment in the production for entrepreneurship in the industry
6. Definition of new job description of regulatory agencies related to subjects such as: preventing false advertising to deceive consumers, preventing the supply of counterfeit goods, constant monitoring on the standard observance of items subject to mandatory standards, playing an advisory role by regulatory agencies for unions and associations for protecting the rights of consumers
7. Facilitating the member ship conditions in the World Trade Organization by limiting intervention in pricing and allowing domestic producers to compete with similar foreign goods
8. The development of the national share in international trade in order to sustain economic development

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#### 4. Conclusion

Since the government of Iran is Islamic Republic and the criteria of government intervention in economic affairs is the interests of the country and the people ,and the final decision is made by the supreme leader, and that the great leader has served the general policies of the system in the form of resistive economy ,hence in this part the policies of the resistive economy related to the role of government regulatory agencies in various economic sectors, with the approach of domestic and foreign investment ,production based on efficiency, transparency of distribution system and pricing (Paragraphs.4, 5, 6, 10, 19, 23, 24 provisions of the Resistive economy policies) will be discussed:

1. Studying the paragraphs (1 to 10) of Resistive economy policies directly points to the role of national production and promotion of production and exports hare with the approach of providing all the conditions and enabling all financial resources and facilities and human and scientific capital to development entrepreneurship and job creation and productivity by maximizing the participation of the public in economic activity by facilitating and encouraging the collective cooperation and emphasis on promotion of income and the role of low –income and middle-class people .And these objectives or the creation of appropriate conditions for the private sector in economic activity, and in this sector the government by providing the conditions for people's investment and managing them to the economy and transferring pricing of goods and services to the private sector on the basis of supply and demand mechanisms provide the transition process from command pricing to free pricing. It should be noted that determining the boundaries of government intervention, doesn't mean the lack of government control in the market, but the government and regulatory agencies in some cases, and when for any reason the balance of supply and demand disappears ,by adopting different policies such as suitable storage in order to supply at times when there is an increase in demand, and in case of supply increase by providing the appropriate facilities and playing an advisory role and providing facilities to establish international markets for exporting goods and services be sides playing a key role in achieving the goals of Resistive Economy policies it can provide its required support for consumers and manufacturers.
2. Clarification and purification of the economy, the distribution system and pricing and updating standards for market supervision and increasing standard coverage for domestic products subject to paragraphs (24,23,19) of Resistive Economy policies which reflects the importance of the role of regulatory and influencing agencies in the field of pricing, that it is necessary to put the development of new and efficient rules and regulations in the distribution and pricing system on the agenda of the ministries an relevant institutions so that besides the realization of resistive economy policies goals, required authority be provided to the private sector for the development of national production and enhancement of investment in order to meet the domestic needs and access to international markets and eventually lead to economic development.

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