

## The Case for the Market

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## Arguments for the market

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## Deontological case for market

- Economic rights as human rights
- Importance of private property
- Necessary for achieving life plans
- Connected to political freedom

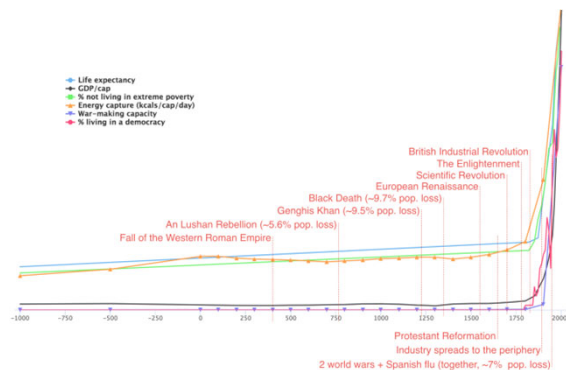
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## Consequentialist case for market

- Invisible hand => efficiency
- Markets & knowledge: price as signal/incentive
- Markets and growth
  - Innovation requires freedom & incentives
- Importance of growth for human flourishing
- Moral & political benefits of growth

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## Impact of economic growth



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## Miracle of compound growth

- Even small positive growth rates make a big difference over time
  - If you raise growth rates by 2%/year, after 50 years, income will be 3x higher
  - If US had grown 1% less/year from 1870 to 1990, it would have same income as Mexico today
- Consider future generations
  - If policies today reduce economic growth, then future will be much worse off than otherwise

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## Development has many positive effects

- Increases life expectancy, health, education, democracy
- Reduces infant mortality, poverty, inequality
- Improves position of women
- See Our World in Data or Gapminder for more statistics

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## Objections

- Rights depend on state
- Problematic origins of property rights
- Markets => inequality (but bad per se? do non-market societies have less?)
- Market failures: monopolies, public goods, externalities, info asymmetries
  - But also government failures

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## More objections

- Economic inequality => political inequality
  - Rich control government through job creation & donations/bribes
- Are cases of high economic growth due to market or state?
  - US/England versus France, Germany, Japan, USSR, China?
- Self-destruction thesis: markets undermine cooperation, work ethic

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## Debate

- Pro: There are some things that should not be bought and sold
- Anti: If you can exchange it freely, then you can buy it and sell it.

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## “Markets in everything”

- \$75,000 from Korean firm for having a baby
- Hire someone to watch you work
- Surge pricing at fast food restaurants
- Bills for emailing with your doctor
- Switzerland pays poor countries to reduce greenhouse emissions
- Operations to surgically lengthen legs
- \$250 for sightings of Supreme Court justices in DC

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## Corrupttour.cz

- World’s First Corruption Tour Company
- Tours of famous sites of corruption in Prague
- Buy a “Master’s of Corruption Administration”

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## Should organs, sex, and other goods be sold?

- Exploitation: take advantage of others' misfortunes
- Misallocation: unfair to sell free tickets to Shakespeare in park
- Corruption: violent video games or pornography might make us bad people
- Semiotic: incompatible with dignity of person or activity

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## Responses

- If you can exchange it freely, why not for money?
- Is objection to the market itself or the type of market? What if added regulations?
- Evidence that market interactions make people more generous, fair
- Ideas of dignity and role of money are culturally contingent

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## Discussion questions

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## 1: Best arguments for markets?

- Which arguments for free markets are stronger - the deontological ones or the consequentialist ones?
- Are Friedman and Hayek more in favor of markets for deontological reasons or consequentialist ones?
- If free markets led to lower growth, would they still prefer them?

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## 2: More economic freedom?

- Many govt regulations actually hurt people
- Occupational regulations. Often you need expensive a license and training to provide simple services. This may just create barriers to entry for the poor and make the services more expensive.
- Zoning regulations. It is very difficult in many places to build dense housing and so housing much more expensive than it could be. People can't even try new medicines.
- Isn't this a good case for more economic freedom?

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## 3. Economic and political freedom

- Friedman argues that economic freedom supports political freedom b/c it means that the govt has less power
- If we limit economic freedom, then the government can use its control of the economy to oppress people. See Orban
- Is Friedman right that economic freedom supports political freedom? How would you object to his argument?

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#### 4. Property rights?

- The case for free markets depends a lot on property rights, but how do we define them?
- Consider IP (intellectual property) like food recipes, fashion, jokes, and tattoos. Do they belong to the inventor? Can others use them?
- Alternatively, we dislike monopolies, but patents create monopolies. You can't play music by Guns n' Roses or the Eagles on Youtube.
- Are we protecting property too much/little?

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#### 5. Inequality and progress

- Hayek famously argued that inequality is a good thing b/c we need rich people to demand new consumer goods that are very expensive.
- Companies wouldn't make things like mobile phones or cars or refrigerators unless they knew that there were wealthy people to buy them.
- But eventually, utopian dreams => luxuries => middle class conveniences => necessities. Now everyone can afford these things.
- In short, inequality not only okay, but good!

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#### Arguments in favor of markets

- Deontological – a fundamental right
- Consequentialist – markets have beneficial effects

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#### Deontological arguments for market

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#### Economic rights as human rights

- Natural liberty to do as we will
- Property important for human dignity
- Economic freedom necessary to achieve life plans
  - You are in control of your life
  - Choice of occupation, how much to charge for your services

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#### Locke's argument

- You can gain property rights over unowned goods by mixing your labor with it
  - You definitely own your own labor
  - Farming virgin land creates value
- But need to leave as much and as good for others
  - Otherwise, you are restricting their natural liberty
  - Does being productive offset this?

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## Universal Declaration of Human Rights

### Article 17.

(1) Everyone has the right to own property alone as well as in association with others.

(2) No one shall be arbitrarily deprived of his property.

### Article 23.

(1) Everyone has the right to work, to free choice of employment, to just and favourable conditions of work and to protection against unemployment.

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## Economic freedom and political freedom

- Free market creates diverse centers of power
  - Separates economic and political power
  - If government has both, too powerful
- Democracy connected with free markets
  - All democracies are market economies
  - But not all market economies are democracies

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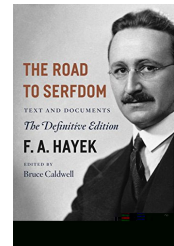
## All democracies have free markets

	Democracy	Authoritarian
Free Market	Almost all industrialized states	Rest of world
Central Planning	None?	Communist states

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## Road to Serfdom

- Compare centrally planned economy
  - State officials hold all economic & political power (USSR)
- Central planning requires strong restrictions on behavior
  - Needs to prevent free exchange
  - Hayek: central planning leads to totalitarianism



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## Consequentialist arguments for market

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## Invisible hand

- “It is not from the benevolence of the butcher, the brewer, or the baker that we expect our dinner, but from their regard to their own interest.” – Adam Smith
- If individuals allow to buy and sell as they please, then producers will find most efficient ways of producing what people want and everyone will benefit

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## Efficiency

- First theorem of welfare economics – competitive markets lead to efficient allocation of resources
  - Pareto efficient: no one can be made better off without someone being made worse off
- Second theorem of welfare economics – can use lump sum transfers and the market to achieve any Pareto efficient outcomes
- Footnote: Strong assumptions required

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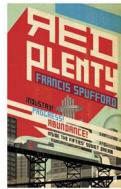
## Markets and knowledge

- Prices spread knowledge quickly & cheaply
  - A signal wrapped inside an incentive
- Consider a disruption in the supply of tin
  - Fewer tin sheets supplied
  - Price of tin rises
  - Individuals reduce use of tin and seek substitutes
  - Higher prices motivate producers to enter market
- People don't need to know any of this

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## What about the alternative

- USSR doesn't want to use prices and markets to allocate goods
- Central planners will mandate a more rational allocation of resources than the "chaos" and lack of plan with markets



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## Consider the scope of the problem

- "In the USSR at this time [1960s] there are 12 million identifiably different products (disaggregated down to specific types of ball-bearings, designs of cloth, size of brown shoes, and so on). There are close to 50,000 industrial establishments..."
- Now we need to make sure that we produce the right amount of each good and get it to the right place at the right time

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## Growth

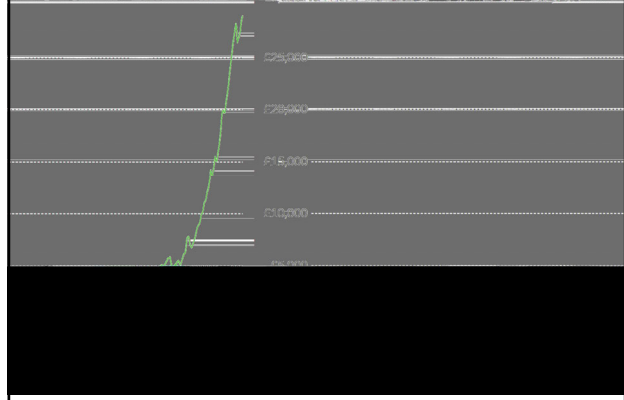
- Robert Lucas – "Once you start thinking about growth, it's hard to think about anything else."
  - We are 17 cm taller than our preindustrial ancestors, we live much longer lives
- Markets seem to promote growth
  - Incentives for efficiency and innovation
- But do historical episodes of growth fit?
  - England, US, Germany, USSR, Japan, Korea

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## GDP per capita in England

Adjusted for inflation and measured in British Pounds in 2013 prices.

Our World in Data



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## Moral consequences of markets

- Growth leads to democracy, civil rights, social tolerance, commitment to fairness
  - Is there more discrimination against minorities when economy is stagnating or growing?
  - Consider political consequences of Great Depression – fascists and communists increase in popularity
- Virtuous and vicious circles: growth => good consequences => growth

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## Objections

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## Is it a natural right?

- Property rights depend on state to provide laws and protection
  - Definition of property (eg, IP, tattoos, recipes, jokes)
  - Enforcement of contracts
  - Punishment of trespassers
- Problems with initial allocations – leaving enough and as good for others

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## Inequality

- Markets create inequality
- Is inequality bad per se?
- Hayek's response
  - Utopian dream => luxuries => conveniences => necessities
  - Who will buy the first cell phone, TV, or refrigerator for \$10K or \$100K?
  - Every innovation needs to start somewhere

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## Market failures

- Monopolies: higher prices and lower supply
- Public goods underprovided
  - Infrastructure, education
- Informational asymmetries
  - Eg, healthcare, used cars
- Externalities: overproduction of bads
  - Producer doesn't pay all costs of production: pollution

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## Government failures

- Just because market fails, doesn't imply that government intervention better
  - What are incentives of bureaucrats/pols?
  - How much knowledge do bureaucrats/pols have?
  - Rent-seeking: efforts by industry to lobby for better treatment
- Be careful of comparisons between real X and ideal Y

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## Next time

- Case for state control of market
- Polanyi: markets are not natural
- Business too powerful