MARKETS & MORALITY

THE TWO MORALITIES OF OUTLAWING PRICE GOUGING

When economists criticize anti-price-gouging laws, they need to do so in moral terms.

BY DWIGHT R. LEE

Economists have long criticized anti-price-gouging laws by arguing that market prices are the most effective means for people to communicate their need for help after a major disaster. (See "The Problem with Price-Gouging Laws," Spring 2011.) This criticism is about as popular as criticizing Jesus for being a lousy carpenter. For most people, price gouging is primarily a moral issue, not an economic one, and the economic argument against outlawing it has been ineffective. Although I agree with the economic argument, I do not believe it can be made widely persuasive without confronting the view that it is immoral for some to profit from the misfortune of others.

Granted, economists can use their supply-and-demand diagrams to demonstrate that preventing price increases for items that disaster victims need will result in outcomes that harm the very people we want to help—hardly a moral outcome. For most people, however, morality is more about *intending to achieve* desirable outcomes than actually *achieving* them. Economists' best hope for making an effective case against anti-price-gouging laws requires considering two moralities—one intention-based, the other outcome-based—that work together to improve human behavior when each is applied within its proper sphere of human activity. Unfortunately, the intention-based morality creates strong support for anti-price-gouging laws that render both moralities less effective at motivating help for disaster victims.

TWO DIFFERENT MORALITIES

For most people, the morality of helping others involves helping them intentionally by making a personal sacrifice. For example, we would consider it a moral act for a man to have risked his own life by diving into an icy, fast-moving river to save a 4-year-old boy, even if that child was Adolf Hitler. On the other hand, a drunk in a motor boat would receive no moral credit if he unwittingly saved a little girl by catching her up in the boat's mooring line and dragging her safely to shore. His actions saved the girl's life, but he did not intend to, or make a sacrifice to do so. I refer to the morality of intentionally making a sacrifice to help others as "magnanimous morality." It is a morality we are programmed to approve of with strong emotions—and rightly so.

There is tremendous value in magnanimous morality in situations where people are well informed about the interests and circumstances of others, and have genuine concern for them. That knowledge and concern are restricted to relatively small groups, such as families, friends, and those with whom we have frequent, direct, and mutually beneficial interactions. Magnanimous morality operates within the small groups to motivate a significant amount of help and reciprocity that does not depend on formal contracts. It is a morality that fosters close relationships that provide much of the joy and meaning in our lives. This is the morality that is essential to the creation of what Nobel laureate economist James Buchanan called "moral communities."

We should not let the benefits we realize from our moral communities, and magnanimous morality's emotional appeal, obscure the fact that we also depend on cooperation with large numbers of complete strangers scattered all over the globe. As Adam Smith noted in *Wealth of Nations*, "In civilized society [each of us] stands at all times in need of the cooperation and assistance of great multitudes, while [one's] whole life is scarce sufficient to gain the friendship of a few persons." So the question is, how do we explain the global cooperation upon which

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we all depend, *but which no one intends*, and is essential to what Buchanan called a "moral order"?

The unintended cooperation that extends far beyond the few people we have direct contact with and care about is something that economists know a lot about, and it is fundamental to their understanding of how extended social orders operate. Smith famously described this cooperation as an "invisible hand" that orders human affairs. Paraphrasing Smith, multitudes of strangers, each motivated primarily by self-interest, will act in a manner that serves their collective interests. This cooperation among strangers is something that economists find extraordinarily impressive and it is critically dependent on a moral foundation, as suggested by Buchanan's term "moral order." The moral foundation upon which the invisible hand depends requires respecting the rights of others and abiding by general rules such as those necessary for impersonal market exchange. This rule-obeying morality does not require taking action to intentionally help others; it just requires people to avoid actions that harm others by violating their legitimate rights. So for obvious reasons it is not nearly as emotionally compelling as magnanimous morality, and I refer to it as "mundane morality."

Considering mundane morality as the moral foundation of the "invisible hand" may not seem like a promising way to develop a moral defense for price increases after a major disaster. While mundane morality and the invisible hand may appeal to economists as an effective way of helping victims of disaster, few non-economists consider it a compelling alternative to magnanimous morality as a decent way to help the victims. Even many of those who are aware of the argument that higher market prices generate desirable outcomes decry price increases after a disaster on moral grounds. For example, Michael Sandel, a Harvard political philosopher who has spent his career examining the issues of morality and justice and is highly praised as a leading authority on public morality, acknowledges arguments that price increases create incentives for distant suppliers to provide needed goods and services to those in the disaster area. In his 2009 book *Justice*,

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he dismisses those arguments, however, by claiming that "the outrage at price-gougers is more than mindless anger. It gestures at a moral argument worth taking seriously.... Outrage of this kind is anger at injustice." Sandel continues,

> In times of trouble a good society pulls together. Rather than press for maximum advantage, people look out for one another. A society in which people exploit their neighbors for financial advantage in times of crisis is not a good society.

Economists should take Sandel's argument seriously by recognizing that his moral argument for helping our "neighbors" after a disaster is more compelling emotionally than any economic argument that ignores moral concerns. But the popularity of Sandel's case against "price gouging" is inseparable from his failure to recognize its moral flaw: the inability of magnanimous morality to generate cooperation over an extended society without the help of the mundane morality of the market. The moral case against anti-price-gouging laws is that those laws undermine the ability of both magnanimous and mundane morality to help disaster victims.

MAGNANIMOUS MORALITY HELPS, BUT IT'S NOT ENOUGH

Anyone bringing food to a neighbor harmed by disaster would be understandably condemned if she demanded payment for her service. But after a disaster, those who have suffered damage need help that requires the coordinated effort of a very large number of geographically dispersed people, almost all of whom are complete strangers. Only by accepting the belief that all those strangers can be considered neighbors to the disaster victims (in the sense of knowing and caring for them) can we expect them to provide effective disaster relief motivated by love alone. Sandel defends this belief by criticizing Dennis Robertson's 1956 argument that "if we economists mind our business, and do that business well, we can ... contribute mightily to the economizing, that is to the full but thrifty utilization of that scarce resource Love, ... the most precious thing in the world." Sandel, in his 2012 book *What Money Can't Buy*, dismisses that limit on love because "it ignores the possibility that our capacity for love and benevolence is not depleted with use but enlarged with practice." He supports this possibility with an example of a loving couple whose love deepens because they use rather than hoard it. But this deepening of love for a loved one is hardly the same as expanding love over a multitude of people you don't know.

Granted, many people who live far from the disaster area and know none of the victims nonetheless donate food and other needed items through their churches and other charitable organizations. Those people are to be applauded for their magnanimous morality and the genuine help they provide. But it should be recognized that this help is insufficient for two reasons: First, even though almost everyone wants the victims of a disaster to be helped, there is a strong temptation to let others provide the help, and large numbers fail to resist that temptation. Second, even if magnanimous morality motivated all of us to donate, our donations would be adequate only if guided by a tremendous amount of information. We, or the relief agencies to which we contribute, may know that the victims need plywood, generators, food, bottled water, flashlights and flashlight batteries, gasoline, and many other things. But how much do the victims value more plywood relative to more generators, or more gasoline, or more of a long list of other things? Any hope for donating the combination of goods that provides the most help would require that each donor have information on the circumstances and preferences of the victims, as well as the amount others are donating of particular items. Without that information, victims would receive excessive amounts of some goods while receiving inadequate amounts of others.

Magnanimous morality plays an important role in helping disaster victims, but it cannot provide the information and motivation needed to provide the amount and combination of help they need. Indeed, if it were enough, suppliers would be *unable* to increase prices after disasters and no purpose would be served by laws outlawing such increases! Everyone who seriously sees helping disaster victims as a moral undertaking should be interested in how the mundane morality of markets adds to the moral means of this undertaking by supplementing and enhancing the effectiveness of efforts motivated by magnanimous morality. It is at this point that the economic argument against anti-price-gouging laws can be made effectively.

A SOCIETY THAT PULLS TOGETHER

Clearly we want victims of natural disasters to be able to communicate persuasively with those best able to provide the help they need. With technological advances in recent years making instant global communication widely available at low costs, it is easy to overlook that the most effective way for people—no matter what their situations—to inform many millions of others of their need for assistance is through market prices.

When disaster victims communicate their need for help through higher prices, that information is noticed immediately by those specializing in providing the help as quickly and cheaply as possible. The help requested cannot typically be completely satisfied by local suppliers, but higher prices reach distant suppliers and motivate them to incur the higher costs of redirecting their attention from local markets to where the need is greatest. The higher prices are also noticed immediately by consumers outside the disaster area who are also purchasing items more urgently needed by the disaster victims. The outside consumers respond by reducing their consumption of those items, making more available to the disaster victims.

Of course, increased prices for the things needed to deal with a disaster are not necessary to inform the millions not directly affected that the needs of victims for many items are greater than their own. That general information is available instantly from the Internet, television, Facebook, or Twitter—but they do not inform individuals how much more valuable each of those items is to disaster victims, or how much they should increase the amount supplied, or reduce the amount consumed, of particular items the victims need. Neither do those sources of information contain strong incentives for people to act on the information. Market prices provide detailed information and incentives to suppliers and consumers of needed products. That information and those incentives are necessary for each actor to make decisions that best accommodate disaster victims, given the decisions that other actors are making. Market prices inform suppliers of just how much disaster victims value additional units of goods and provide the suppliers with an incentive to expand the amount supplied as long as their marginal costs are less than the values victims receive from the additional supply. Consumers not directly affected by the disaster respond to the higher prices by reducing their consumption of goods as long as their sacrifice is less than the additional values made available to the disaster victims, as reflected in market prices. And higher market prices also motivate disaster victims to share with each other. Victims are all better off when each refrains from consuming more of scarce goods when the additional consumption is worth less to one victim than to others. This is what market prices give each victim the information and incentive to do.

Market prices inform suppliers of just how much disaster victims value additional units of goods and provide the suppliers with incentive to expand the amount supplied, so long as marginal cost is less than marginal benefit.

Because of higher market prices after a major disaster, millions of people can coordinate their decisions to produce more and share more of what victims want, and provide it in amounts the victims desire at the higher prices. This is an impressive example of how, in Sandel's words, "[i]n times of trouble a good society pulls together." This degree of social cooperation could never be achieved by magnanimous morality alone, although it can help. Indeed, volunteers motivated by magnanimous morality work more effectively in conjunction with the mundane morality of markets. In response to the help provided by volunteers, market prices adjust to shift market activities into areas relatively less served by volunteers. Market prices also provide information that can direct volunteer efforts to where they do the most good. Why would anyone concerned with the morality of helping disaster victims as much as possible want government to obstruct the help that only the mundane morality of markets can provide them, and reduce the effectiveness of the help provided by the magnanimous morality of volunteers by imposing anti-price-gouging laws?

Some will respond to this question by expressing concern that markets allow the wealthy to out-compete the poor for the help they need. Space permits only a few words on this concern in this article. First, the poor do receive benefit from the additional goods and services that are directed into disaster areas by market incentives. Second, those who are seen not to be benefiting sufficiently from market activity are best helped directly through charitable activity, not by hampering everyone's ability to communicate their need for help through markets with anti-price-gouging laws. And third, restricting the rationing of assistance by prices increases the importance of rationing by political influence and social connections. The poor are not likely to benefit from this rationing any more than they would from price rationing. Indeed, the influence of the wealthy almost surely gives them more access than the poor to the limited amount of products available at artificially low prices.

CONCLUSION

The strong economic case against anti-price-gouging laws will be widely dismissed on moral grounds unless economists present their case within a moral framework. The most effective way of doing this is by recognizing that there are two moralities, one based primarily on intentions (magnanimous morality) and the other based primarily on outcomes (mundane morality). When those moralities operate within their proper spheres of human activity, they work together to motivate the most help to victims of disaster. Our instinctive desire, however, is to hamper the mundane morality of markets with anti-price-gouging laws in the naive hope that magnanimous morality can do the job of both. The unfortunate result is to reduce the contribution of both moralities to provide the help needed by victims of disaster. R

READINGS

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