

**CONFLICT BETWEEN INDIVIDUAL AND COMMUNITY** Finally, Locke's critics have argued that his argument assumes that human beings are atomistic individuals with personal rights to liberty and property that flow from their individual nature independently of their relations to the larger community. Because these rights are assumed to be prior to and independent of the community, the community can make no claims on the property or freedom of the individual. However, critics claim that these individualistic assumptions are completely false: they ignore the key role of caring relationships in human societies and the demands of caring that arise from these relationships. Locke's critics point out that human beings are born dependent on the care of others; as they grow, they remain dependent on the care of others to acquire what they need to become able adults. When they become adults, human beings still depend on the caring cooperation of others in their communities for virtually everything they do or produce. Even an individual's liberty depends on others. The degree of liberty a person has depends on what the person can do: the less a person can do, the less she is free to do. However, a person's abilities depend on what the person learns from those who care for her, as well as on what others care to help her to do or allow her to do.

Similarly, the property that a person produces through labor depends ultimately on the skills acquired from those who cared for him or her and on the cooperative work of others in the community, including employees. Even one's identity—the sense of who one is as a member of the various communities and groups to which one belongs—depends on one's relationships with others in the community. In short, the individualistic assumptions built into Locke's view of human beings ignore the concrete caring relationships from which a person's identity and the possibility of individual rights arise. People are not atomistic individuals with rights that are independent of others; instead, they are persons embedded in caring relationships that make those rights possible and that make the person who and what he or she is. Moreover, critics continue, people are morally required to sustain these relationships and to care for others as others have cared for them. The community can legitimately make claims on the property of individuals and can restrict the freedom of individuals precisely because the community and the caring it has provided are the ultimate source of that property and freedom.

### Quick Review 3.2

#### Weaknesses of Locke's Views on Rights

- Locke does not demonstrate that individuals have natural rights to life, liberty, and property.

- Locke's natural rights are negative rights, and he does not show that these override conflicting positive rights.
- Locke's rights imply that markets should be free, but free markets can be unjust and can lead to inequalities.
- Locke wrongly assumes that human beings are atomistic individuals.

## 3.3: Free Markets and Utility: Adam Smith

**OBJECTIVE:** Assess key arguments associated with Adam Smith's utilitarian view of free markets

The second major support for free markets derives from the utilitarian argument that free markets and private property will produce greater benefits than any amount of government interference could. In a system with free markets and private property, buyers purchase what they want at the lowest prices they can find. Therefore, it will benefit private businesses to produce and sell what consumers want and to do this at the lowest possible prices. To keep their prices down, private businesses will try to cut back on the costly resources they consume. Thus, the free market, coupled with private property, ensures that the economy is producing what consumers want, that prices are at the lowest levels possible, and that resources are efficiently used. The economic utility of society's members is thereby maximized.

Adam Smith (1723–1790), called the father of modern economics, is the originator of this utilitarian argument for the free market.<sup>48</sup> In his major work, *The Wealth of Nations*, Smith wrote that when private individuals are left free to seek their own interests in free markets, they will inevitably be led to further the public welfare by an **invisible hand**:

By directing [his] industry in such a manner as its produce may be of the greatest value, [the individual] intends only his own gain, and he is in this, as in many other cases, led by an invisible hand to promote an end that was no part of his intention. . . . By pursuing his own interest he frequently promotes that of society more effectively than when he really intends to promote it.<sup>49</sup>

### 3.3.1: The Invisible Hand of Market Competition

Smith's invisible hand is market competition. Every producer seeks to make a living by using private resources

to produce and sell those goods that the producer perceives people want to buy. In a competitive market, a multiplicity of such private businesses must all compete with one another for the same buyers. To attract customers, therefore, each seller is forced not only to supply what consumers want but also to drop the price of goods as close as possible to “what it really costs the person who brings it to market.”<sup>50</sup> To increase his or her profits, each producer will pare costs, thereby reducing the resources consumed. The competition produced by a multiplicity of self-interested private sellers serves to lower prices, conserve resources, and make producers respond to consumer desires. Motivated only by self-interest, private businesses are led to serve society. As

Smith stated the matter in a famous passage in *The Wealth of Nations*:

It is not from the benevolence of the butcher, the baker, and the brewer that we expect our dinner, but from their regard for their own self-interest. We address ourselves not to their humanity, but to their self-love, and never talk to them of our own necessities, but of their advantages.<sup>51</sup>

### 3.3.2: Government Plays No Role

The best policy of a government that hopes to advance the public welfare, Smith claimed, is to do nothing: to let each individual pursue his self-interest in “natural liberty” so that he is free to buy and sell whatever he or she wishes.<sup>52</sup> Any interventions

#### Adam Smith’s Market Mechanism

Smith argued that a system of competitive markets allocates resources efficiently among the various industries of a society.<sup>53</sup> He presented a classic supply and demand model.

#### Demand

The process starts with consumer demand.

- When consumer demand of a certain commodity is high enough that the supply is not enough to meet it, buyers bid the price of the commodity upward until it rises above what Smith called the *natural price* (i.e., the price that just covers the costs of producing the commodity, including the going rate of profit obtainable in other markets).
- Producers of that commodity then reap profits higher than those available to producers of other commodities.
- Higher profits induce producers of those other products to switch their resources into the production of the more profitable commodity.

#### Supply

#### Utility

in the market by government can only serve to interrupt the self-regulating effect of competition and reduce its many beneficial consequences by creating either surpluses or shortages.

## Ethical Application

### Government Intervention

The view that government interventions in the market are not beneficial seems to be the view that Abbott Laboratories adopted when it objected to Thailand's decision to manufacture Abbott's patented drug. Abbott argued that the high prices it put on its drugs were necessary to recover the high costs of developing them, and if companies could not charge these high prices they would no longer have any incentive to continue developing new drugs, which would induce a shortage of new drug development. When Thailand's government intervened in the drug market by taking Abbott's patented drug, then, it interfered with Abbott's ability to recover its costs and, to some extent, removed Abbott's incentive to continue developing new AIDS drugs, thereby potentially lowering the future supply of new AIDS drugs. Thus, in the long run, the government's intervention in the drug market was hurting its own people. Government interventions in the market, Smith argued, will almost always end up harming consumers.

### 3.3.3: Interpreting Adam Smith

In the early twentieth century, economists Ludwig von Mises and Friedrich A. Hayek supplemented Smith's market theories by an ingenious argument.<sup>54</sup> They argued that not only does a system of free markets and private ownership efficiently serve to allocate resources, it is in principle impossible for the government or any human being to allocate resources with the same efficiency as the market. Human beings cannot allocate resources efficiently because they can never have enough information nor calculate fast enough to coordinate in an efficient way the hundreds of thousands of daily exchanges required by a complex industrial economy. In a free market, high prices indicate that additional resources are needed to meet consumer demand, and they motivate producers to allocate their resources to those consumers. The market thereby allocates resources efficiently from day to day through the pricing mechanism. If a government were to try to do the same thing, von Mises and Hayek argued, it would have to know from day to day what things each consumer desired and what materials each producer would need to produce the countless things consumers desired, and it would have to calculate how best to allocate resources among interrelated producers so as to enable them to meet consumer desires. Von Mises and Hayek claimed that the infinite quantity of detailed bits of information and the astronomical number of calculations that a government would need to make would be beyond its capacity. Thus, not only do free markets allocate goods efficiently, it is impossible for government planners to duplicate their performance.

**COMMODIFICATION, OR HOW FREE SHOULD FREE MARKETS BE?** Although Smith argued that everyone should be left free to buy and sell whatever they want in markets that are free of any government intervention, many have countered that government should be allowed to set limits on what is bought and sold in markets. The word "commodification" was coined by those who suggest that not everything should be turned into a marketable commodity. To "commodify" something is to treat it as, or turn it into, an item that can be bought and sold (a commodity). Should we be free to commodify whatever we want? For example, many people would like the U.S. government to allow the open sale of sexual intimacies, but since selling sex is illegal in all states but Nevada, sex workers secretly market their services online and in the Yellow Pages as escorts. Others would like the government to allow people to freely buy and sell hard drugs (cocaine and heroin) as do Spain, Mexico, Portugal, and Italy.

**THE KEY ASSUMPTION OF PRIVATE PROPERTY** Although Adam Smith did not discuss the notion of private property at great length, it is a key assumption of his views. Before individuals can come together in markets to sell things to one another, they must have some agreement about what each individual owns and what each individual has the right to sell to others. Unless a society has a system of private property that indicates who owns what that society cannot have a free market system. For this reason, Adam Smith assumed that a society with free markets would have a private property system, although he gave no explicit arguments showing that a system of private property was better than, say, a system where all productive resources were owned in common by everyone or by government. Earlier philosophers, however, had provided arguments in support of a private property system that, like Smith's own arguments for free markets, were based on utilitarian considerations. In the thirteenth century, for example, philosopher Thomas Aquinas argued that society should not rely on a property system in which people own all things in common. Instead, society would prosper best if its resources were owned by individuals, who then would have an interest in improving and caring for those resources. A private property system, Aquinas argued,

is necessary to human life for three reasons. First because every man is more careful to procure what is for himself alone than that which is common to many or to all: since each one would shirk the labor and leave to another that which concerns the community. . . . Secondly, because human affairs are conducted in more orderly fashion if each man is charged with taking care of some particular thing himself, whereas there would be confusion if everyone had to look after any one thing indeterminately. Thirdly, because a more peaceful state is ensured to man if each one is contented with his own. Hence it is to be observed that quarrels arise more frequently where there is no division of the things possessed.<sup>55</sup>

## Commodity Markets: Human Babies and Human Organs

As you might expect, not everyone shares the same opinions on commodification. Here we'll look further into two types of commodity markets: one for human babies and one for human organs. Where will you stand?<sup>56, 57, 58, 59, 60, 61</sup>

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Judge Richard Posner, who sits on the U.S. Court of Appeals for the Seventh Circuit in Chicago, and co-author Elisabeth Landes wrote an article entitled "The Economics of the Baby Shortage." The authors pointed out that more couples who want to adopt a baby exist than babies up for adoption. They suggested that this shortage could be fixed by starting a baby market in which available babies could be sold, and couples who want to adopt babies could buy them.

One argument suggests that Posner and Landes's proposal for expanding the free market for babies is a good idea:

In such a baby market, a shortage of babies would cause their price to rise, and rising prices would lead to more babies being put up for sale and fewer couples stepping up to buy them, which would solve the shortage. Mothers who could not care for their children due to poverty would also benefit.

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In the view that Aquinas proposed, private property is not something that is naturally produced when labor is mixed into things, as Locke claims. Instead, private property is a social construct, an artificial, but beneficial, social institution that we create and that can be shaped in numerous ways. These utilitarian arguments in favor of a private property system over a system of common ownership have often been repeated. In particular, many philosophers have repeated the argument that, without a private property system in which individuals get the benefits that come from caring for the resources they own, individuals would have no incentive to improve those resources or make them as productive as possible.<sup>62</sup> A private property system is best because it provides incentives for individuals to invest their time, work, and effort in improving and exploiting the resources they own and whose benefits they know they will personally receive.

### Quick Review 3.3

#### Additional Support for Adam Smith

- Hayek and von Mises argued that government should not interfere in the market because a government cannot gather and process the vast amount of information necessary to allocate resources as efficiently as a free market.
- Smith, like Thomas Aquinas, assumed that, according to a utilitarian argument, a system of private property would lead to better care and use of resources than would common ownership.

### 3.3.4: Criticisms of Smith's Free Markets

Critics have attacked Smith's classic utilitarian argument in defense of free markets and his assumptions regarding private property on a variety of fronts.

## The Criticism of Unrealistic Assumptions

The most common criticism of Smith's defense of free markets is that the argument rests on unrealistic assumptions.<sup>63, 64</sup>

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### Monopoly Prices Do Not Necessarily Move to Lowest Levels

Critics claim that Smith's argument assumes that the impersonal forces of supply and demand will force prices down to their lowest levels because the sellers of products are so numerous and each enterprise is so small that no one seller can control the price of a product. This assumption was perhaps true enough in Smith's day, when the largest firms employed only a few dozen workers and a multitude of small shops and individual merchants competed for the consumer's attention. However, today many industries and markets are completely or partially monopolized, and the small firm is no longer the rule. A monopolized industry is one with a very few sellers. In these monopolized industries, the few large enterprises are able to set their own prices, so it is no longer true that prices necessarily move to their lowest levels. The power of the industrial giants enables them to keep prices at artificially high levels and production at artificially low levels.

Many observers have pointed out that patents create a form of monopoly. When a company is issued a patent for a drug it has developed, it alone has the right to sell that drug, so it has a monopoly in that drug. If the drug is able to cure a prevalent disease, then the company will likely be able to set the price for that drug as high as it wants to set it. In a free market, there are no limits on the price a monopolist can charge for its drugs.

### Producers Do Not Carry All Costs

### Profit Is Not a Universal Motive

## Ethical Application

### Monopoly and High Prices

As we saw in the case of Abbott Laboratories, which had patents on certain drugs that could treat AIDS, the price at which the company sold its AIDS drugs was so high that the drugs were out of reach for people in poorer countries such as Thailand. Abbott set the price of its AIDS drug Kaletra, for example, at \$7,000 a year in most countries, and at \$2,200 a year for Thailand. Other patented AIDS drugs could be sold for as much as \$12,000 a year by companies that had patents that gave them a monopoly on those drugs. In monopolized free markets like these, prices do not move to their lowest levels as Adam Smith suggested they would.

**MORALITY, EFFICIENCY, AND JOHN MAYNARD KEYNES** The market system of a society makes humans selfish, and this widespread selfishness then makes us think the profit motive is natural.<sup>65</sup> It is the institutions of capitalism that engender selfishness, materialism, and competitiveness. In actual fact, human beings are born with a natural tendency to show concern for other members of their species (e.g., in their families). A major moral defect of a society built around competitive markets, in fact, is that within such societies this natural benevolent tendency toward virtue is gradually replaced by self-interested tendencies toward vice. In short, such societies are morally defective because they encourage morally bad character.

As for the argument of von Mises and Hayek—that human planners cannot allocate resources efficiently—the

examples of the French, Dutch, and Swedes have demonstrated that planning within some sectors of the economy is not quite as impossible as they imagined.<sup>66</sup> Moreover, the argument of von Mises and Hayek was answered on theoretical grounds by socialist economist Oskar Lange, who demonstrated that a “central planning board” could efficiently allocate goods in an economy without having to know everything about consumers and producers and without engaging in impossibly elaborate calculations.<sup>67</sup> All that is necessary is for the central planners to receive reports on the sizes of the inventories of producers and price their commodities accordingly. Surplus inventories would indicate that lowering of prices was necessary, whereas inventory shortages would indicate that prices should be raised. By setting the prices of all commodities in this way, the central planning board could create an efficient flow of resources throughout the economy. Yet, even

the critics of von Mises and Hayek must acknowledge that the kind of large-scale planning that has been attempted in some communist nations—particularly the former Soviet Union—has resulted in large-scale failure. It appears that planning is possible only if it is but one component within an economy in which exchanges are, for the most part, based on market forces.

#### Quick Review 3.4

##### Criticisms of Smith's and Keynes's Arguments

- Smith's arguments rest on the unrealistic assumption that there are no monopoly companies.
- Smith's arguments falsely assume that all the costs of manufacturing are paid by the manufacturer, which ignores the costs of pollution.
- Smith's arguments falsely assume that human beings are motivated only by a self-interested desire for profit.

### The Influence of John Maynard Keynes

The most influential criticism of Smith's classical assumptions came from British economist John Maynard Keynes (1883–1946). In turn and over time, elaboration on and criticism of Keynes's theories have evolved as well.

#### The Keynesian Criticism of Adam Smith

Smith assumed that without any help from the government, the automatic play of market forces would ensure full employment of all economic resources, including labor. If some resources are not being used, then their costs drop and entrepreneurs are induced to expand their output by using these cheapened resources. The purchase of these resources, in turn, creates the incomes that enable people to buy the products made from them.

Thus, all available resources are used and demand always expands to absorb the supply of commodities made from them (a relationship now called *Say's Law*). Since Keynes, however, economists have argued that, without government intervention, the demand for goods may not be high enough to absorb the supply. The result is unemployment and a slide into economic depression.

Keynes argued that the total demand for goods and services is the sum of the demand of three sectors of the economy: households, businesses, and government. The **aggregate demand** of these three sectors may be less than the aggregate amounts of goods and services supplied by the economy at the full employment level. This mismatch between aggregate demand and aggregate supply will occur when households prefer to save some of their income in liquid securities instead of spending it on goods and services. When, as a consequence, aggregate demand is less than aggregate supply, the result is a contraction of supply. Businesses realize they are not selling all their goods, so they cut back on production and thereby cut back on employment. As production falls, the incomes of households also fall, but the amounts households are willing to save fall even faster. Eventually, the economy reaches a stable point of equilibrium at which demand once again equals supply, but at which there is widespread unemployment of labor and other resources.

- Contrary to Smith's view, some government planning and regulation of markets is possible and desirable.
- According to Keynes, Smith wrongly assumed that demand is always enough to absorb the supply of goods.
- Keynes' views were challenged when government spending did not cure high unemployment but created inflation.

### 3.3.5: Social Darwinism

Nineteenth-century social Darwinists added a new twist to utilitarian justifications of free markets by arguing that free markets have beneficial consequences over and above

those that Adam Smith identified. They argued that economic competition produces human progress.

Those individuals whose aggressive business dealings enable them to succeed in the competitive world of business are the fittest and, therefore, the best. Just as survival of the fittest ensures the continuing progress and improvement of an animal species, Spencer argued, so too the free competition that enriches some individuals and reduces others to poverty results in the gradual improvement of the human race. Government must not be allowed to interfere with this stern competition because doing so would only impede progress. In particular, government must not lend economic aid to those who fall behind in the competition for survival. If these

#### Charles Darwin and Herbert Spencer

The doctrines of **social Darwinism** were named after Charles Darwin (1809–1882), who found that the various species of living things were evolving as the result of the action of an environment that favored the survival of some things while destroying others. Even before Darwin had published his theories, philosopher Herbert Spencer (1820–1903) and other thinkers had already begun to suggest that the evolutionary processes that Darwin described were also operative in human societies.<sup>68, 69</sup>

#### Charles Darwin's Theory

Darwin said, "This preservation of favorable individual differences and variations, and the destruction of those which are injurious, I have called **natural selection** or the **survival of the fittest**." The environmental factors that resulted in the **survival of the fittest** were the competitive pressures of the animal world. As a result of this competitive struggle for existence, Darwin held, species gradually change because only the fittest survive to pass their favorable characteristics on to their progeny.

#### Herbert Spencer's Theory

economic misfits survive, they will pass on their inferior qualities and the human race will decline.

The shortcomings of Spencer's views were obvious even to his contemporaries. Critics were quick to point out that the skills and traits that help individuals and firms advance and survive in the business world are not necessarily those that help humanity survive on the planet. Advancement in the business world might be achieved through a ruthless disregard for other human beings. The survival of humanity, however, may well depend on the development of cooperative attitudes and the mutual willingness of people to help each other.

The basic problem underlying the views of the social Darwinist, however, is the fundamental normative assumption that *survival of the fittest* means *survival of the best*. That is, whatever results from the workings of nature is necessarily good.

The fallacy, which modern authors call the **naturalistic fallacy**, claims that whatever happens naturally is always good. However, it is a basic failure of logic to infer that what is should be and that what nature does is what it ought to do.

In spite of its many shortcomings, many business people today firmly believe in a version of social Darwinism. That is, many business people believe that businesses must compete for their lives in an economic environment in which only the strong will survive. Modern versions of Spencerism hold that competition is good not because it destroys the weak individual, but because it weeds out weak firms. Economic competition ensures that the so-called best business firms survive and, as a result, the economic system gradually improves. The conclusion of modern social Darwinists is the same: government must stay out of the market because competition is beneficial. This is one of the reasons why many business people object to government assistance to troubled businesses, or bailouts. During the last several decades, when very large businesses were failing and it looked like they might have to close and lay off all their workers, the U.S. government stepped in and provided those businesses with enough money to bail them out of their troubles. This happened during the 2008–2009 recession when government provided over \$700 billion to prop up dozens of banks, insurance companies, automobile companies, and other businesses. Social Darwinists objected that all this did was preserve weak and inefficient companies that should have been allowed to go under.

### Quick Review 3.5 Views of Herbert Spencer

- Evolution operates in society when economic competition ensures the fittest survive and the unfit do not, which improves the human race.

- If government intervenes in the economy to shield people from competition, the unfit survive and the human race declines, so government should not do so.
- Spencer assumes that those who survive in business are "better" people than those who do not.

## 3.4: Free Trade and Utility: David Ricardo

**OBJECTIVE:** Analyze comparative advantage as a foundation for free trade among nations

We have so far focused on the arguments for and against free markets as they might operate within a single nation. But utilitarian arguments have also been advanced in favor of free trade between nations. Adam Smith's work, *The Wealth of Nations*, in fact, also discussed the benefits of free trade. There he wrote:

It is the maxim of every prudent master of a family, never to attempt to make at home what it will cost him more to make than to buy. The tailor does not make his own shoes but buys them from the shoemaker. . . . What is prudence in the conduct of every family, can scarce be folly in that of a great kingdom. If a foreign country can supply us with a commodity cheaper than we ourselves can make it, better buy it of them with some part of the produce of our own industry, employed in a way in which we have some advantage.<sup>70</sup>

Adam Smith's point here is simple. Like individuals, countries differ in their ability to produce goods. One country can produce a good more cheaply than another and it is then said to have an **absolute advantage** in producing that good. These cost differences may be based on differences in the following:

- labor costs
- workers' skills
- climate
- technology
- equipment
- land
- natural resources

Suppose that because of these differences, our nation can make one product for less than a foreign nation can, and suppose that the foreign nation can make some other product for less than we can. Then, clearly it would be best for both nations to specialize in making the product each has an absolute advantage in producing and to trade it for what the other country has an absolute advantage in producing.

But what if one country can produce everything more cheaply than another country?

### David Ricardo's Example of Comparative Advantage: England and Portugal

British economist David Ricardo (1772–1823) is usually credited with showing that even if one country has an absolute advantage at producing everything, it is still better for it to specialize and trade. In his major work, *On the Principles of Political Economy and Taxation*, Ricardo used the example of England and Portugal to show that even if England is better than Portugal at producing *both* cloth and wine, it is still better for both England and Portugal to specialize and trade.<sup>71, 72</sup>

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#### Foreign Trade from England's Perspective

According to Ricardo, "England may be so circumstanced, that to produce the cloth may require the labour of 100 men for one year; and if she attempted to make the wine, it might require the labour of 120 men for the same time. England would therefore find it in her interest to import wine, and to purchase it by the exportation of cloth."

#### Foreign Trade from Portugal's Perspective

### 3.4.1: Ricardo's Argument for Comparative Advantage

Ricardo's argument for comparative advantage asks us to imagine a world consisting of only two countries: England and Portugal. We first see that Portugal has an absolute advantage in making both wine and cloth, since it can produce both products more cheaply than England can.

Note that after specializing and trading, both countries have *more* of both products than either had when they did not specialize or trade. Specialization in comparative advantages increases the total output of goods countries produce, and through trade all countries can share in this added bounty.

### 3.4.2: Comparative Advantage and Globalization

Ricardo's ingenious argument has been hailed as the single most important and most meaningful economic discovery ever made. Some have said it is the most surprising and counterintuitive concept in economics. Comparative advantage is, without a doubt, the most important concept in international trade theory today and is at the heart of the most significant economic arguments people make when they argue in favor of globalization. In fact, it is the key argument for globalization and free trade. All the arguments politicians and economists make in favor of globalization and free trade come down to Ricardo's point:

## Comparative Advantage in Foreign Trade

As you go through the data, figure out why and how each country can benefit from foreign trade.

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	100 Barrels of Wine (Cost in Worker-years)	100 Rolls of Cloth (Cost in Worker-years)
England	120	100
Portugal	80	90

It costs England the labor of 120 workers toiling one year to produce a certain amount of wine (let us arbitrarily assume that amount is 100 barrels), while it costs Portugal the labor of only 80 workers to produce the same amount of wine over the same time. Meanwhile, it costs England the labor of 100 workers for one year to produce a certain amount of cloth (let us arbitrarily assume that the amount is 100 rolls), while it takes Portugal only 90 workers to produce the same amount of cloth over the same time.

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globalization is good because specialization and free trade boost total economic output, and everyone can share in this increased output.

### Quick Review 3.6

#### Free Trade: Support for Globalization

- Free trade is advocated by Smith, who showed that everyone prospers if nations specialize in making and exporting goods whose production costs are lower for them than those costs are for other nations.
- Free trade is advocated by Ricardo, who showed that everyone prospers if nations specialize in making and exporting goods whose opportunity costs to them are lower than the opportunity costs other nations incur to make the same goods.
- The arguments of Smith and Ricardo provide support for globalization.

### 3.4.3: Criticisms of Ricardo

Although most economists accept Ricardo's basic argument as correct in theory, many question whether his utilitarian argument applies in practice to today's real world. Of course, Ricardo makes a number of simplifying assumptions that clearly do not hold in the real world—such as that there are only two countries making only two products with only a fixed number of workers. But these are merely simplifying assumptions Ricardo made to get his point across more easily, and his conclusion could still be proved without these assumptions.

Other assumptions, however, are not so easy to get around. Ricardo assumed the following:

1. The resources used to produce goods (labor, equipment, factories, etc.) do not move from one country to another. Yet today multinational companies can, and

easily do, move their productive capital from one country to another.

- Each country's production costs are constant and do not decline as countries acquire new technology or expand their production (i.e., there are no *economies of scale*). But we know that the costs of producing goods regularly decline as companies expand production and develop ever better production technologies.
- Workers can easily and without cost move from one industry to another (from making wine, for example, to making cloth). Yet, when a company in a country closes down because it cannot compete with imports from another country that has a comparative advantage in those goods, the company's workers are laid off, suffer heavy costs, need retraining, and often cannot find comparable jobs.

These are core reasons why many U.S. workers (and their unions) today reject key aspects of globalization and free trade.

## Ethical Application

### Non-transferability of Jobs

U.S. workers of Swingline had to bear significant burdens and costs when the manufacturer closed its factory in New York and moved to Mexico. A few years later, Swingline workers in Mexico suffered a similar fate when the company moved to China.

**INTERNATIONAL RULES SHIFT THE BALANCE** Finally, and perhaps most important, Ricardo ignored international rule-setters. International trade inevitably leads to disagreements and conflicts, and so countries must agree to abide by some set of rules. Today, the main organization that sets the rules that govern globalization and trade is the WTO, although both the World Bank and the International Monetary Fund also impose rules on countries that borrow money from them. Critics claim that these organizations impose requirements that harm poor developing countries while benefiting the wealthy developed nations and their businesses.

It is difficult to say how telling these criticisms are. Many people today continue to be enthusiastic supporters of global free trade, repeating Ricardo's comparative advantage argument. Many others have become harsh critics of globalization. Indeed, there have been continuing and violent demonstrations against globalization on the streets of cities around the world, many of which have directly affected important meetings of the WTO.

## Ethical Application

### International Rules and Balance

When the World Trade Organization (WTO) rules were being negotiated, poor countries had few patent laws so they had often copied the drugs their people needed, but that U.S. drug companies had developed and patented in the U.S. Abbott Laboratories and other large U.S. drug companies contributed millions of dollars to U.S. politicians and successfully got the U.S. government to seek worldwide acceptance of the patent protections they enjoyed in the United States. As a result, when the WTO agreements were finalized, the United States insisted that all WTO countries had to recognize and enforce drug patents for 20 years. Because developing countries did not have the resources to engage in the expensive research needed to invent new drugs, enforcing drug patents would not benefit them. On the contrary, recognizing drug patents would force developing countries to pay the drug companies for the drugs that they had been freely copying. Nevertheless, developing countries went along with the requirement that they enforce drug patents because the WTO offered them the chance to sell their exports in the markets of the United States and other industrialized nations, by far the largest markets in the world. In the end, the patent rules of the WTO forced the poor people of developing nations to pay about \$60 billion a year to the drug companies of the rich industrialized nations.<sup>73</sup> Thailand, as we saw, attempted to get around these expensive requirements by using an exception allowed by the TRIPS rules of the WTO.

## 3.5: Karl Marx and Justice: A Critique of Free Markets and Free Trade

**OBJECTIVE:** Interpret Marxist views on the impact on workers of free trade and free markets

Karl Marx (1818–1883) is undoubtedly the harshest and most well-known critic of private property institutions, free markets, and free trade and the inequalities they may create. Marx lived during the Industrial Revolution. He saw all around him the wrenching and exploitative effects that industrialization had on the laboring peasant classes of England, Europe, and the rest of the world. In several works, he described the suffering and misery that capitalism was imposing on its workers: exploitative working hours, pulmonary diseases and premature deaths caused by unsanitary factory conditions, 7-year-olds working 12 to 15 hours a day; 30 seamstresses working 30 hours without a break in a room made for 10 people.<sup>74</sup>

Marx claimed that worker exploitation was merely a symptom of the underlying extremes of inequality that capitalism produces. According to Marx, capitalist systems offer only two sources of income: sale of one's own labor and

ownership of the *means of production* (the buildings, machinery, land, and raw materials by means of which we produce goods and services). Because workers cannot produce anything without access to the means of production, they are forced to sell their labor to the owner in return for a wage. The owner, however, competes against other businesses and so tries to minimize all his costs, including the cost of labor. The owner lowers wages to the point where workers receive only what they need to subsist. Workers therefore do not receive the full value of their labor. The difference (or “surplus”) between the full value of their labor and the subsistence wages they receive is retained by the owner and is the source of the owner’s profits. Thus, the owner is able to exploit workers by appropriating from them the surplus they produce, using as leverage ownership of the means of production. As a result, those who own the means of production gradually become wealthier,

and workers become relatively poorer. Capitalism thus promotes an inequality that is inconsistent with justice.

Marx, however, did not use the term *unjust* to describe the way the capitalist takes the surplus value that workers produce. In fact, he claimed that the terms *just* and *unjust* are generally used by capitalists to describe what is, and what is not, in their own interests. The capitalist, he wrote, will even “assert that the present-day distribution is ‘fair.’”<sup>75</sup> So the terms *just* and *unjust*, and *fair* and *unfair*, Marx asserted, are nothing more than “obsolete verbal rubbish” and “ideological nonsense.”<sup>76</sup> Instead of saying that the surplus value the capitalist takes from workers is an “injustice,” Marx said that it is “robbery,” “theft,” “embezzled,” “usurped,” and “the loot of other people’s labor.” So although Marx did not use the term *injustice*, it is clear from his use of these other terms (*robbery*, *theft*, etc.) that he thought it was in fact unjust for the capitalist to take the surplus value that workers produced.<sup>77</sup>

## Marx’s View on Alienation

According to Marx, capitalist economies alienate workers in four ways.<sup>78, 79, 80, 81, 82, 83, 84</sup>

### 1. Capitalist Economies Alienate Workers from Their Own Productive Work

In capitalism, a worker is forced to work for someone else and serves under the supervision and control of someone else. Because the purpose of his work is to make money for the owner of his workplace, it is not designed to be a fulfilling form of productivity and to satisfy his own needs:

In what, then, consists the alienation of labor? First, in the fact that labor is external to the worker, i.e., that it does not belong to his nature, that therefore he does not fulfill himself in his work, but denies himself in it, has a feeling of misery rather than satisfaction, does not develop freely his mental and physical energies but is physically exhausted and mentally depressed . . . His labor, therefore, is not voluntary, but forced—forced labor. It is not the gratification of his need, but only a means to gratify needs outside his work. Its alien nature shows itself clearly by the fact that work is shunned like the plague as soon as no physical or other kind of coercion exists. Lastly, the external character of labor for the worker appears in the fact that it is not his own, but someone else’s, that it does not belong to him, that in it he belongs, not to himself, but to another.

### 2. Capitalist Economies Alienate Workers from the Products of Their Labor

### 3. Capitalist Economies Alienate Workers by Denying Them Control

### 4. Capitalist Economies Alienate Workers from Themselves

### 3.5.1: Alienation

The living conditions that capitalism imposed on workers contrasted sharply with Marx's view of how human beings should live. In Marx's view, capitalism and its private property system creates *alienation* among workers. Marx used the term *alienation*—which means separation or estrangement—to refer to the condition of being separated or estranged from one's own true self or one's own true nature. Marx believed that it was the nature of a human being to be self-determined and able to satisfy one's true needs; that is, to be in control of one's life and able to fulfill one's true human needs. If a person lost control over her life and the ability to be fulfilled through the satisfaction of her human needs and was instead controlled by some external power and forced to meet its needs, this person was alienated from her own nature. Marx's fundamental

criticism of capitalism was that it alienated workers by robbing them of control of their lives and forcing them to satisfy needs that were not their own.

**A PRICE ON EVERYTHING** A key cause of alienation, Marx claimed, was the way that capitalist societies come to see everything in terms of their market prices.

Marx might have pointed out that when the managers of Swingline considered moving the factory to Mexico, they did not think about their relationships with their workers. All that mattered to them was whether they would make more money in New York or in Mexico. Instead of thinking about their connection to the people around them, these managers used an "egotistical" calculation to figure out whether the cash payment of moving to Mexico was greater than the cash payment of staying in New York.

### The Communist Manifesto and Commodity Fetishism

Human interactions, Marx claimed, have been so commercialized and turned into commodities that everyone and everything has its price.<sup>85</sup>

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## Communist Manifesto

## On the Edge

### Marx's Children

The International Labor Organization estimates that 218 million children work today. In developing countries, child workers are common. In the soccer ball industry, for example, child labor continues to be used to stitch soccer balls together in spite of a 1997 industry agreement to end the use of child workers. A 2010 report of the International Labor Rights Forum indicates that child labor occurs in China and India where stitching is done in workers' homes and not in a factory. Geeta, a 12-year-old girl stitcher from Kamalpur in India said, "I have been stitching footballs for as long as I can remember. My hands are constantly in pain. It feels like they are burning."<sup>86</sup> Children must work in a hunched position for five to seven hours to make two soccer balls for 3–4 rupees

per ball (a total of 7.5 to 10 cents). Nike, Adidas, and Puma are among the largest companies that buy soccer balls from Indian manufacturers.

#### WRITING PROMPT

##### Relevance of Marx Today

1. How would Marx explain why there is so much child labor in the world today?
2. What ethical obligations do companies have in order to deal with these issues? Why?

The response entered here will appear in the performance dashboard and can be viewed by your instructor.

Submit

### Child Labor Today

The terrible conditions under which workers—particularly child workers—of the nineteenth century had to labor inspired much of Marx's writing. Yet many of these conditions continue today.<sup>87, 88</sup>

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#### Agriculture

Vintage photo of child workers in China. According to Human Rights Watch, U.S. farm companies have children and teens working for them today.



## Economic Structure and Social Superstructure

The economic structure of a society, according to Marx, consists of the materials and methods it uses to produce its goods and the way it organizes itself to produce those goods. In addition to its economic structure, a society also consists of what Marx called a *social superstructure*, which is made up of society's institutions and fundamental values. Ultimately, history is shaped by economic forces.<sup>89, 90, 91, 92</sup>

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### Economic Structure: Forces of Production

Marx refers to the materials (land, labor, natural resources, machinery, energy, technology) a society uses to produce its goods as its *forces of production*. The societies of the Middle Ages, for example, were agricultural societies in which the forces of production were primitive farming methods, manual labor, and hand tools. In modern industrialized societies, the forces of production are factories; assembly-line manufacturing techniques; steam, electricity, nuclear power, and other power sources; and machinery.

### Economic Structure: Relations of Production

### Economic Structure: Social Classes

### Social Superstructure: Political and Social institutions

### Social Superstructure: Influence on History

### Social Superstructure: Historical Materialism

## 3.5.2: Historical Materialism

Marx did not believe that what was happening to workers in capitalist societies was an accident. He argued, in fact, that the position of workers in modern capitalist societies was the inevitable result of certain historical and economic forces. Given the nature of modern industry, he claimed, it was inevitable that workers should find themselves being exploited by the capitalist owners of the factories in which they were forced to labor. To support his claim, Marx offered a breathtakingly comprehensive analysis of society, which we can only sketch here.

Marx argued that every society has two main components:

- an economic structure
- a social superstructure<sup>93</sup>

## 3.5.3: Immiseration of Workers

Marx claimed that so long as capitalism remained the dominant economic system of modern societies, the lives of workers would not improve. In fact, he claimed, their lives would only get worse. The combined effects of increased concentration, periodic economic downturns, rising unemployment, and declining wages are what Marx refers to as the *immiseration of workers*. The conditions leading to immiseration of workers include the following:

1. Modern capitalist systems inexorably move toward an ever greater concentration of ownership in a relatively few hands.<sup>94</sup> As owners try to expand their businesses so that they can better compete against other businesses, smaller firms are gradually taken over by larger ones. Thus, economic power and

wealth become concentrated in ever fewer hands, increasing inequality.

- Capitalist societies must inevitably experience cycles of economic downturns.<sup>95</sup> Because workers are organized into mass assembly lines, businesses can produce large amounts of goods. As these businesses compete with one another, each tries to produce as much as possible. As a result, firms periodically produce an oversupply of goods. These flood the market, and an economic depression or recession results as the economy slows down to absorb the surplus.
- Marx argued that the pressures of competition lead businesses to do whatever they can to reduce their costs. To reduce their costs, they continually try to reduce the wages of workers, resulting in a gradual fall in wages.<sup>96</sup> Competitive pressures also lead owners to replace workers with cheaper machines, thereby creating rising unemployment.

The solution to conditions leading to the immiseration of workers, Marx believed, was collective ownership of society's productive assets and the use of rational planning to replace unregulated markets (see Table 3.2).

### Quick Review 3.7

#### Marx on Private and Productive Property

- Private ownership of the means of production, or private property, is the source of the worker's loss of control over work, products, relationships, and self.
- Productive property should serve the needs of all and should not be privately owned, but owned by everyone.

**CLASSLESS SOCIETY AS SOLUTION** Marx's answer to capitalism is captured by the popularized statement with which he ends his most famous work, the *Communist Manifesto*: "Workers of the world, unite!" The problems of capitalism arise from the conflict between classes—between the owner class and the worker class—so the only real solution is to get rid of classes. In other words, the way to overcome capitalism is to wipe away its class system and, in its place, establish a classless society. To get to the classless society, Marx thought, required a revolution in which the workers would overthrow capitalist owners. He wrote that workers could achieve their ends "only by the forcible overthrow of all existing social conditions. Let the ruling classes tremble at a Communist revolution. The workers have nothing to lose but their chains."<sup>101</sup>

In the classless society, Marx thought, the means of production would no longer be an owner's private property, but would be collectively owned by all workers. Everyone would contribute according to his or her abilities, and receive according to his or her needs. This would be a society without exploitation, unemployment, poverty, and without inequality. It would be a society "where nobody has one exclusive sphere of activity but each can become accomplished in any branch he wishes, [where] society regulates the general production and thus makes it possible for me to do one thing today and another tomorrow, to hunt in the morning, fish in the afternoon, rear cattle in the evening, criticize after dinner, just as I have a mind, without ever becoming hunter, fisherman, herdsman or critic."<sup>102</sup>

**Table 3.2** Private and Productive Property

Marx did not hesitate to make clear that his views implied that private ownership of the means of production was wrong.<sup>97, 98, 99, 100</sup>

	Marx's View	Explanation
<b>Private property</b>	<p>A private property system that allows private control of productive property, he held, is the basis of the alienation, inequalities, and immiseration that characterize capitalist societies:</p> <p>You are horrified at our intending to do away with private property. But in your existing society private property is already done away with for nine-tenths of the population; its existence for the few is solely due to its non-existence in the hands of those nine-tenths. You reproach us, therefore, with intending to do away with a form of property, the necessary condition for whose existence is the non-existence of any property for the immense majority of society.</p>	<p>Marx did not suggest that he wanted people to do away with private ownership of their clothes, houses, or food. That is, he did not object to "the power to appropriate the products of society." However, he did object to private ownership of factories, companies, mines, farms, and other productive property (i.e., the private ownership of <i>capital</i>).</p>
<b>Productive property</b>	<p>Productive property should benefit everyone, and so it should be owned by everyone. To the utilitarian argument that without private ownership of productive assets there would be no incentive for individuals to work, Marx replied:</p> <p>It has been objected that upon the abolition of private property all work will cease and universal laziness will overtake us. According to this, bourgeois society ought long ago to have gone to the dogs through sheer idleness; for those of its members who work, acquire nothing, and those who acquire anything, do not work.</p>	<p>Marx held that productive property should be seen as having a social purpose: it belongs to the whole community and should serve the needs of all. Productive property should not be private, but should be held in common and its fruits enjoyed by all. Marx believed that if there were no private ownership of the means of production, people would still continue to lead productive lives because their desire to be productive and to express themselves through what they make with their hands and minds is an instinct that is built into their very nature.</p>

**Quick Review 3.8****Marx on Immiseration of Workers**

- Capitalism concentrates industrial power in the hands of a few who organize workers for mass production.
- Mass production in the hands of a few leads to surplus, which causes economic depression or recession.
- Factory owners replace workers with machines, which creates unemployment; they keep wages low to increase profits.
- The combined effects of the above cause immiseration of workers.
- The only solution is a revolution that establishes a classless society where everyone owns the means of production.

### 3.5.4: Critics' Views on Karl Marx's Criticisms

Criticisms of Karl Marx include the proposition that principles of justice are hard to define and that justice

requires free markets. Some believe that the benefits of private property and free markets are more important than equality, while others see free markets as able to encourage community instead of causing alienation. Still others argue that immiseration of workers has not occurred.<sup>103, 104</sup>

**Quick Review 3.9****Criticisms of Marx**

- Marx's claims that capitalism is unjust are not provable.
- Justice requires free markets.
- The benefits of private property and free markets are more important than equality.
- Free markets can encourage community instead of causing alienation.
- Immiseration of workers has not occurred; instead, their condition has improved.

**Explaining Critics' Viewpoints**

There are five distinct criticisms of Karl Marx's worldview, and each are explained here.

**Principles of Justice Are Difficult to Define**

Critics have answered the Marxist criticism that free markets generate unjust inequalities by arguing that Marx wrongly assumes that justice means either equality or distribution according to need. This assumption is unprovable, some of his critics have claimed. There are too many difficulties in this way of establishing acceptable principles of justice. Should distributive justice be determined in terms of effort, ability, or need? These questions cannot be answered in any objective way, critics claim, so any attempt to replace free markets with some distributive principle will, in the final analysis, be an imposition of someone's subjective preferences on other members of society. Such an imposition, of course, would violate the (negative) right every individual has to be free of the coercion of others.

## 3.6: The Mixed Economy, New Forms of Property, and the End of Marxism

**OBJECTIVE:** Explain the mixed economy and redefinitions of property that affect the business system

The debate for and against free markets, free trade, and private property continues. Some people have claimed that the collapse of several communist regimes at the end of the twentieth century showed that capitalism, with its emphasis on free markets, is the clear winner.<sup>105</sup> Other observers, however, have held that the emergence of strong economies in nations that emphasize government intervention and collectivist

property rights, such as China and Singapore, shows that free markets alone are not the key to prosperity.<sup>106</sup>

### 3.6.1: The Mixed Economy

Perhaps it is inevitable that the controversy over free markets has led many economists to advocate retention of market systems and private ownership, but with modification of their workings through government regulation that rid them of their most obvious defects. The resulting combination of government regulation, partially free markets, and limited property rights is appropriately referred to as the **mixed economy**.<sup>107</sup>

Basically, a mixed economy retains a market and private property system but relies heavily on government policies to remedy their deficiencies. Government transfers (of private income) are used to get rid of the worst aspects of

#### How Effective Are Mixed Economy Policies?

A comparison of the United States with other countries that have gone farther down the road toward implementing the policies of a mixed economy may be helpful. Sweden, Denmark, Norway, France, Ireland, and Switzerland are all mixed economies with high levels of government regulation. Statistics are readily available comparing these countries to the United States.<sup>108</sup>

#### Comparative Statistics

To begin with, the United States has greater inequality than Sweden, Denmark, Norway, France, Ireland, or Switzerland. Based on the *CIA World Factbook* for 2015, the top 10 percent of all U.S. households receive 15 times as much income as the bottom 10 percent; however, in Sweden the ratio is 6 times, in Norway it is 5 times, in France it is 7 times, in Ireland it is 9 times, and in Switzerland it is 2.5 times. According to the CIA figures, the infant mortality rate of the United States (6.17 deaths per 1,000 live births) is higher than that of Ireland (3.7 deaths), Denmark (4.1 deaths), Switzerland (3.73 deaths), France (3.31 deaths), Ireland (3.74), and Sweden (2.6 deaths). The life expectancy at birth in the United States (79.56) is less than in Ireland (80.56), Norway (81.6), Switzerland (82.39), Sweden (81.89), and France (81.66).