

It's Either Bullies or Balance Sheets

Written by Jeffrey Tucker.

A piece of sea bass for \$16 struck me as absurd. That's too much! I bought it anyway. It was delicious. But I was still upset about the price. Nonetheless, the next day I decided to buy some more.

"We sold out of that yesterday."

What can we conclude? I conclude that it was the right price after all. The market cleared. In any case, what gave me the idea that I knew it was too expensive? I bought it. The terms were right, since the buyer and seller agreed. After all, if the store could just charge anything it wanted, the fish would have been a million dollars. If I paid what I wanted, the price would have been \$0. The real-world price is somewhere in between, but where precisely is an experiment in human decision making.

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I thought about a time when I thought a price was too low. I was at the thrift store and found an all-wool double-breasted navy blazer. It was \$5. Online, the same would have been \$500 plus. Bargain right? Well, the thrift store got it for free, so it made money. The price was indeed right.

There Is No Just Price

We have every right to declare what is or isn't the right price for us to part with our own money or goods. But there is no standard beyond that to know the right price of anything. We think we know, but we do not. Prices emerge from markets to tell us something about the world around us. They enable rational calculation. They give rise to profit-and-loss statements that signal to businesses whether they are going about things the right way. They are a social tool to minimize waste and maximize opportunities for living a better life.

A wise man once told me that in this life, you can obey balance sheets or bullies. In the end, those are the only two paths. He was drawing attention to an unavoidable reality in a world of scarcity. All scarce things must be allocated among competing ends. This can be done top-down by people in control, or it can be accomplished bottom-up with the signaling system that emerges from voluntary exchange. The two approaches don't mix well.

Producers Can't Dictate Prices

None can compete with its efficiency, much less displace its indispensable utility in this world.

Of course, prices do not exist apart from human will. They can be played with, but not finally controlled, by producers in the market. There are vast surprises along the way. It's not the case that only the rich thrive in this environment. Who would have thought that the sci-fi machine in old movies that provides instant answers to all questions would eventually be provided for free by one of the world's biggest companies? I'm speaking here of Google, but the same could be said of the many alternative search engines out there.

Who would have thought that the world's largest communication networks — email and social networking — would be free also, funded mostly by selling ad space and premium upgrades? In the same way, most of the world's most useful software is free, as is the cloud-based word processing system I'm using to type this article. So too for the music that filled my living room last night, all selections from the 16th and 17th centuries, all provided to me for free. Amazing.

The price system is a constantly changing kaleidoscope that beautifully merges our subjective imaginations with the gritty realities of the physical world. It is the combination of mind and matter that yields an output — a simple number — that never lies. It gives us that glorious balance sheet that tells you whether you are doing sustainable or unsustainable things. No institution can compete with its efficiency, much less displace its indispensable utility in this world.

Defying Expectation

It is impossible to predict these things.

Who could have known five years ago that physical books would sometimes sell for less than digital books of the same title? This defies every expectation. The physical good is a real thing that you can hold and costs money to make (so much for the labor theory of value). The digital goods need only be made once and then can be sold billions of times. So what is the trick? It comes down to consumer demand. We really like e-books — their convenience and speed of delivery — and are willing to pay for them.

The price system also decides which companies are profitable and which are not. It has nothing to do with the size of the company. If you take in less than you spend, you will eventually go belly up. If you take in more than you spend, you will grow. The vast global network of price formation ultimately reduces to this simple calculation that determines how all the world's resources are used. Every company faces the same constraint. So whether or not these pricing decisions are rational has much to do with the fate of the world.

No Perfect Prediction

State institutions that distort prices, such as wage floors, profoundly affect the profit-and-loss calculation.

The point is that it is impossible to predict these things. No matter how smart the team of experts, how powerful and prestigious the price setters behind the curtain, there will always be surprises out there. That's because no one can fully predict the values manufactured by the human mind, nor know enough about the world to foresee every possible alternative use of a resource that goes into the production process. When economists say that something should be "left to the market," they are really saying that people should be left to work all this out for themselves. This is the only way of dealing with all the uncertainties of this world.

These are some of the insights about the price system that can be drawn from the science of economics. It explains that there is no substitute for the price system. And this is why it is also so enormously dangerous for any society to give power to a central bank to manipulate the price system from the top down. Its decisions about the money supply can't help but be irrational and ultimately destructive to economies and the realization of the common good.

Interventions

The same could be said of a range of state institutions that distort prices, such as wage floors and ceilings, subsidies and penalties for particular companies, and taxes and regulations that extract resources and profoundly affect the profit-and-loss calculation. They all interfere with the fluid functioning of the price system. They all waste resources. They all interfere with the efficiency of the market.

More and more, people of the developed world are seeing the balance sheet replaced by the bully. An example: when the president tells you the conditions under which you can or cannot buy resources outside the borders. That decision should be made by owners, not politicians.

This is harming both our prosperity and our personal liberty to make decisions for ourselves. If the bully can tell the fast food joint what its prices ought to be, the same bully can tell me what I can and cannot eat, what and where I can and cannot drive and where I can and cannot work and under what terms.

The price system, premised on the idea of private property and the freedom to choose, is the best friend liberty and prosperity ever had. The next time someone complains about it, ask that person what he would prefer to take its place.

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