

In Praise of Profit

We've all heard the exhortation "People before profits." My goal here is to show that in a freed market (not a corporatist economy), there need be no conflict between treating people well and earning profit. On the contrary, profitability in the market would depend on being sensitive to what people want.

We first must recognize that the pursuit of profit, or gain, is the defining feature of *all* purposeful human action, as Ludwig von Mises taught. It makes action what it is. Whenever one acts — whenever one chooses an end and the means to achieve it — one seeks to improve one's condition, that is, to replace one (coming) state of affairs with another that the acting person prefers. If I am hungry (or anticipate soon becoming hungry) and I prepare a meal, I have taken steps to create a state of satisfaction because I prefer that condition to the one that would have come to pass if I had not acted.

All action is of that nature. The actor replaces situation B with situation A. The end sought may be egoistic, altruistic, or something else. What counts is that, for whatever reason, the person *wants* the end. This applies to Mother Teresa as much as to an acquisitive materialist. They want different things, perhaps for different reasons, but *they* want them, and so they act. (This is not to be confused with psychological egoism, the idea that we are all self-interested.)

It is already implicit in what I've said that if an action is successful — if the end is achieved — the actor experiences a profit. How so? Assuming the person has not made a mistake (which is always possible), he or she prefers the end to whatever was given up or forgone to obtain it — this is the price, or the opportunity cost. Mises called this gain "psychic profit." We are not talking about market transactions only. Alone on an island, when Crusoe decides to make a net so he can catch more fish, the "price" he pays includes giving up other uses of his time, including leisure, and other uses of the materials.

By nature, then, all action aims at profit, and all successful action is profitable. No one would undertake an action expecting to give up what one prefers in exchange for what one does not prefer. In fact, one *can't* do it. To act is to demonstrate one's preference under the circumstances. (Thus, Mises held that the analysis of features common to all human action is a conceptual, or a priori, matter.)

Those who condemn profit as an unjust gain need to reevaluate their position in light of the foregoing. Remember, in analyzing profit, I am assuming a freed market, that is, an economy based on individual liberty and free enterprise without special privileges from government. The conclusions drawn here cannot be automatically applied to the current corporatist economy, in which people are able to make profits that would be unavailable in

a freed market.

For example, if a corporation is highly profitable because it sells drones to the government, we shouldn't applaud the company for its competence in the marketplace. The corporation's activities are not aimed at pleasing consumers making free choices, but rather at pleasing government officials who obtain their revenue by force (taxation).

In free-market transactions, just as with individual actions, the parties each seek a state of affairs that is preferred over others they might achieve with their resources. If Olivia gives an orange to Alexander in exchange for his apple (assuming no coercion or fraud), we must conclude that they evaluate the products differently. Olivia prefers the apple to the orange, and Adam prefers the orange to the apple. Both profit — though the gain cannot be measured or quantified, because it is subjective and ordinal. Presumably, no one would condemn this dual profit.

When goods are exchanged for money, however, some people see the situation differently. For one thing, only the receiver of money is said to profit. But that is wrong. If Olivia buys the apple from Alexander for two dollars, we still must conclude that she prefers the apple to whatever else she could have bought with the two dollars. That gain is her profit.

Nothing is changed if we imagine that Adam paid only one dollar for the apple. Olivia still prefers the apple to her other alternatives for the money. She of course would like to pay less, just as Alexander would like to charge more. But the agreed-on price satisfies both parties. There are no grounds for criticizing Adam for his profit. (If Olivia insists on paying less, Alexander might find someone who is willing to pay two dollars. If Alexander insists on charging more, Olivia might find someone who is willing to charge only two dollars. Hence the importance of free competition.)

Mises and his student Israel Kirzner used the term *entrepreneurial profit* for the gains made from spotting price discrepancies in the market. If an alert person sees that apples are selling for a dollar apiece in one part of the market and two dollars apiece in another part, she can profit by buying in the former and selling in the latter. Her dollar profit is her reward for alertness; there was nothing to stop anyone else from doing what she did. But note that her profit will be fleeting. Her buying apples in the cheap market will drive up the price there, while her bringing additional apples to the dear market will drive down the price there. Soon there will be one price and no entrepreneurial profit.

The story is the same with more complicated enterprises. If consumers are willing to pay more for an item than it costs to gather the factors of production and assemble it, some part of the return for some period of time will be pure entrepreneurial profit resulting from a formerly unnoticed price discrepancy. That abnormal profit will attract competitors until the return is more in line with other industries.

Price discrepancies can be seen as knowledge errors: resources are undervalued with respect to their potential. Entrepreneurial activity consists in spotting and correcting such discrepancies. Profit is the reward for that service, but after the error is corrected, the profit disappears.

The upshot is that in the absence of government privilege, profit — psychic or monetary — is legitimate and praiseworthy. In a freed market, profit is an inducement to serve others and a sign that they are being well served.