

Hayek: Price as a signal

Choice, Commerce, and Conflict
Ryan Doody

Review:

The Division of Labor
Marxian Alienation
Smith & Education
Bullshit Jobs

Bullshit Jobs: Why do they exist?

The answer clearly isn't economic: it's moral and political. The ruling class has figured out that a happy and productive population with free time on their hands is a mortal danger (think of what started to happen when this even began to be approximated in the '60s). And, on the other hand, the feeling that work is a moral value in itself, and that anyone not willing to submit themselves to some kind of intense work discipline for most of their waking hours deserves nothing, is extraordinarily convenient for them.

Is Graeber right? Do you agree/disagree?

Bullshit Jobs: Why do they exist?

What's the Argument?

P1 It serves the interest of the ruling class for bullshit jobs to exist.

P2 ???

C Bullshit jobs exist.

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Functional
Explanations

Invisible Hand
Explanations

But first...

Friedrich Hayek

**Friedrich Hayek
(1899-1992)**

**Austrian
Economist**



Contents:

What Is Economics?

Prices (as signals)

Spontaneous Orders &

Invisible Hands

What Is Economics?

What Is Economics?

The Fundamental Economic Problem:

Given the scarcity of resources, what **goods and services** should be **produced** and how should they be **allocated**?

What Is Economics?



On certain familiar assumptions the answer is simple enough. *If* we possess all the relevant information, *if* we can start out from a given system of preferences and *if* we command complete knowledge of available means, the problem which remains is purely one of logic.

What Is Economics?

The Fundamental Economic Problem:

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The Fundamental Economic Problem:

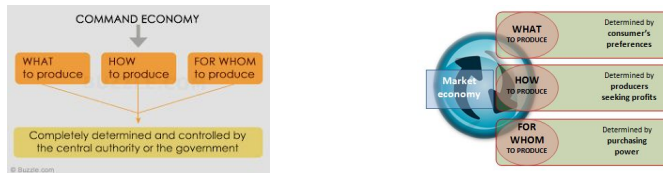
Given the scarcity of resources, what **goods and services** should be **produced** and how should they be **allocated**?

these “data.” It is rather a problem of how to secure the best use of resources known to any of the members of society, for ends whose relative importance only these individuals know. Or, to put it briefly, it is a problem of the utilization of knowledge not given to anyone in its totality.

What Is Economics?

The Fundamental Economic Problem:

Given the scarcity of resources, what **goods** and **services** should be **produced** and how should they be **allocated**?



What Is Economics?

Command Economy vs. Market Economy

Which of these systems is likely to be more efficient depends mainly on the question under which of them we can expect that fuller use will be made of the existing knowledge. And this, in turn, depends on whether we are more likely to succeed in putting at the disposal of a single central authority all the knowledge which ought to be used but which is initially dispersed among many different individuals, or in conveying to the individuals such additional knowledge as they need in order to enable them to fit their plans in with those of others.

Which Is More Efficient? (And Why?)

If we can agree that the economic problem of society is mainly one of rapid adaptation to changes in the particular circumstances of time and place, it would seem to follow that the ultimate decisions must be left to the people who are familiar with these circumstances, who know directly of the relevant changes and of the resources immediately available to meet them. We cannot expect that this problem will be solved by first communicating all this knowledge to a central board which, after integrating *all* knowledge, issues its orders. We must solve it by some form of **decentralization**. But this answers only part

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Decentralization: information is processed locally, distributed across many people.

Spontaneous Order

Spontaneous Order

When the behavior of multiple individuals exhibits a structure that isn't the result of design or control by an individual, government, or agency.



Spontaneous Order

The Invisible Hand

“Every individual... neither intends to promote the public interest, nor knows how much he is promoting it... he intends only his own security; and by directing that industry in such a manner as its produce may be of the greatest value, he intends only his own gain, and he is in this, as in many other cases, led by an **invisible hand** to promote an end which was no part of his intention.”

Adam Smith, *The Wealth of Nations*



Spontaneous Order

In order to produce and allocate goods in the best way, we need **information**:

- Scarcity
- Who wants what



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Supply & Demand



Spontaneous Order

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- Who wants what

The economy is complex and interconnected.

Change of price in one resource ripples out...



Price (as a signal)

What Determines the Price of an Oat Milk Latte?



Hayek's Insight



- Prices convey **information** (about the supply and demand for the good/service)
- No single person possess all or most of this information; knowledge is **dispersed**
- Prices help **coordinate** the actions of many people

Price (as a signal)



- **Prices** convey information:
 - supply of the good
 - demand for the good
- Allow us to allocate resources where they are **most urgently needed**
- ... without any one individual possessing all of the relevant information

How so?

Price (as a signal)

Example: An increase in the price of oil communicates...



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Price (as a signal)

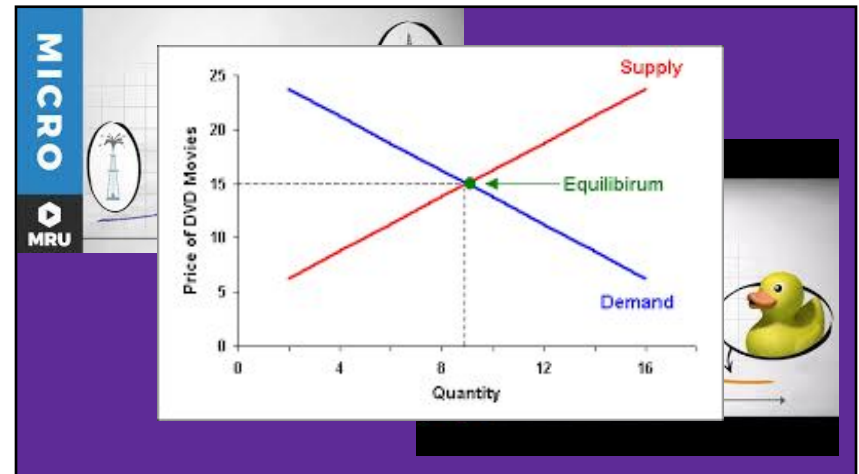
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[To producers]: Sell more oil!

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Result: We reallocate oil from “low value” to “high value” uses.



Price (as a signal)

How does it work?



not know of these events as such, nor of *all* their effects. It does not matter for him *why* at the particular moment more screws of one size than of another are wanted, *why* paper bags are more readily available than canvas bags, or *why* skilled labor, or particular machine tools, have for the moment become more difficult to acquire. **All that is significant for him is how much more or less difficult to procure they have become compared with other things with which he is also concerned, or how much more or less urgently wanted are the alternative things he produces or uses.** It is always a question of the relative

Price (as a signal)

How does it work?



Prices communicate *information* about which goods/services to produce and about how to allocate them, while also providing *motivation* for people to make best use of this information.

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Regulating Prices?

Regulating prices?

Hayek would disapprove



- Markets efficiently aggregate the knowledge possessed by individuals dispersed throughout society
- Government cannot “know” what the market does
- When government interferes, it distorts the information conveyed by prices, leading to **inefficiencies**

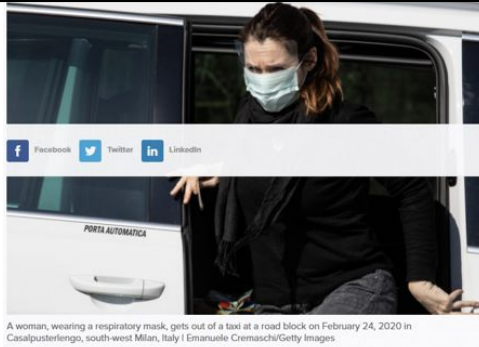
Example:
Should We
Regulate the Price
of Face Masks?



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Price Gouging



A woman, wearing a respiratory mask, gets out of a taxi at a road block on February 24, 2020 in Casalpusterlenigo, south-west Milan, Italy | Emanuele Cremaschi/Getty Images

Online prices skyrocket in Italy amid coronavirus fears

Products such as hand sanitizer have been sold for as much as 7 times the normal price.

The Invisible Hand

The 'Magic' of the Market

Hayek: Think of the market as a giant information-processing machine. It produces prices, which helps coordinate behavior toward (typically) desirable ends.

But it is a machine with *no maker*.

It was not *designed* and no one *controls* it.

How does it work?



The 'Magic' of the Market

Smith: Social effects can arise *spontaneously* from individuals pursuing their own interests (without anyone intending those effects).

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It is not from the benevolence of the butcher, the brewer, or the baker, that we expect our dinner, but from their regard to their own interest. We address ourselves, not to their humanity but to their self-love, and never talk to them of our necessities but of their advantages (WN I.2.12).



The 'Magic' of the Market

WARNING:

Smith *does not* think that all people are inherently *greedy* or *selfish*.

Market = machine that converts *self-interest* into *mutual gain*.

(But how?)

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Invisible Hand Explanations

Invisible Hand Explanation:

- (1) A certain pattern of human activity arises from the intentional actions of some individuals,
- (2) No one acted with the intention of bringing about that pattern.

Every individual... neither intends to promote the public interest, nor knows how much he is promoting it... he intends only his own security; and by directing that industry in such a manner as its produce may be of the greatest value, he intends only his own gain, and he is in this, as in many other cases, led by an invisible hand to promote an end which was no part of his intention (WN IV.2.9).



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Under certain conditions, *markets* produce *positive social effects*.

But not always.

And spontaneous orders needn't always be positive.



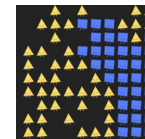
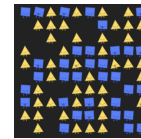
Segregation Model

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Example:

Thomas Schelling's Segregation Model



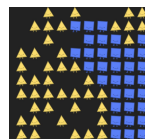
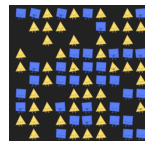
Segregation Model

Thomas Schelling's Segregation Model (<https://ncase.me/polygons/>)

Individuals have a preference to not be a minority in their neighborhood.

In aggregate, as a result of individuals acting on their preferences, segregation emerges.

... even if everyone prefers integration over segregation.



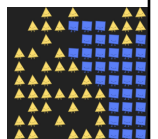
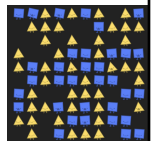
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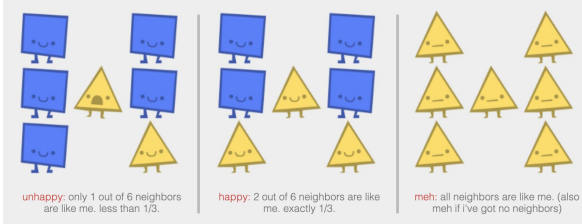


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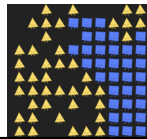
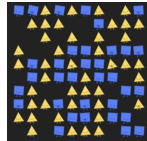


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"I wanna move if less than 1/3 of my neighbors are like me."



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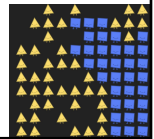
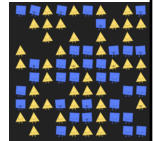
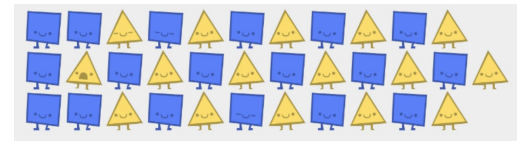
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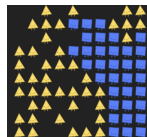
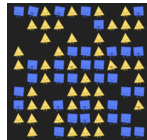
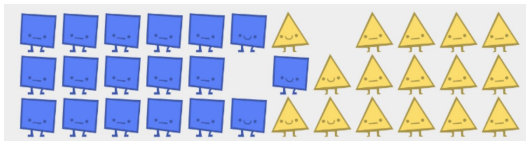
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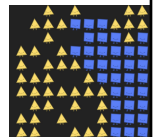
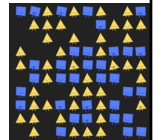


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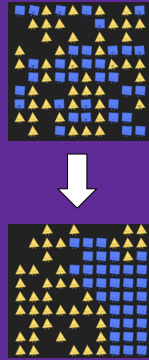
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**Discussion
Question:**
What can be
done?



Segregation Model



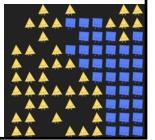
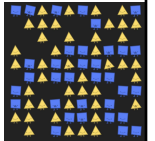
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Lesson:

It doesn't follow from the observation of segregation that people *want* it.

It's not enough for people to want integration. (What would it take?)

Government enforcement. (E.g., forced bussing)



Review:

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Prices (as signals)
Spontaneous Orders &
Invisible Hands

Questions?