

Lacetera Transcript (revised)

Good afternoon everyone. My name is Nico Lacetera. I'm a professor at the University of Toronto, and today I'm going to talk a little bit about the social and moral support for markets during a pandemic? Let me start with three examples of "vignettes":

Let's consider this woman, called Mary. Mary is following the evolution of COVID19 outbreak in China. She predicts that situation will be similar if not worse in North America. As such, she expects that isolation measures will be in place in North America, too, and many people will work from home. She decides to buy stocks of a company that offers video conferencing services (a "long" position). Two months on, her holdings have greatly increased in value. She decides to sell and realizes a significant financial gain.

Now consider Hannah. She is following the evolution of COVID19 outbreak in China too, and she also thinks it will spread widely beyond East Asia. She decides to invest in stocks of a company that produces a very popular hand sanitizer. Like Mary, she sells her stocks in late March realizing a large gain.

Now let's finally consider Joseph, he holds exactly the same beliefs as Hannah. He decides to stockpile (or hoard) on hand sanitizer, buying bottles and dispensers at relatively low prices from many stores as well as on line. His garage is now full of hundreds of bottles and dispensers. In March, when demand is very high and there is a supply shortage, he starts selling the items online at a significantly higher price than the prevalent one in January. Now, in a sense, these are all expressions of what a capitalistic, market economy, looks like. The self-regulation magic of the price mechanism is such that demand and supply for stocks or for goods will meet, some parties will take advantage of the opportunity, and they will to make a profit.

It is from this kind of entrepreneurial initiatives, among others, that we achieve an efficient allocation of resources while giving individuals and organizations strong incentives to always look for new opportunities, thus eventually driving economic growth and prosperity. And yet, I suspect that some people, perhaps more people, will have a different attitude, even moral judgement, about these three different actions, and these three ways of exploiting an opportunity for profit. And in particular, I suspect what Joseph did, with hoarding hand sanitizers then selling them at high prices after taking them out of stores, might be met with some animus, at least by some of you. And if you share this feeling, it turns out, you definitely aren't alone.

There is a long tradition in the history of thought about the importance of finding some moral limits to market, and about the importance that markets, economic activities rely on social support and respect on some higher moral principles. We can go back as far as the gospels, and in particular, the story of Jesus entering Jerusalem, going to the temple where money traders, commodity traders, are doing their activities, engaging in reasonably mutually beneficial exchanges between them and their customers and yet, Jesus is extremely upset, turns the

tables around, saying you are essentially blasphemous for doing this in the temple. We can go to more recent, although not too recent times, and we can think of Adam Smith the philosopher and economist who introduced the metaphor of the . The Invisible Hand, that is, the idea that competition and the price mechanism efficiently regulate markets and society. But in a previous Treatise, *The Theory of Moral Sentiments*, he claims that higher order values, which he summarizes with the term Justice, are in fact the real pillars of society and the key principle which societies have to abide by; and that the moral pressure of social opinion, to quote his words, guides actions as well in the institutional choices. Even the father of neo-classical economics at the end of the nineteenth century, Alfred Marshall, expressed similar ideas when he considered the role that the moral pressure of social opinion in directing and constraining market activities.

Immanuel Kant (actually it's his birthday today) made the moral distinction between actions and things that have a price, so they're marketable, and those things that have dignity instead, so we cannot assign a monetary value to them. The sociologist Emile Durkheim stressed the social dimension of morality, how abiding by certain moral values of a high order hold societies together. And in more recent years, perhaps one of the major contributions is the one of political theorist Michael Sandel, who focused on the topic of economic justice not just as being about distribution about goods, services and resources, but also about value of things, including to the non-monetary value we assign to these actions and these resources.

I'm going a little fast here but if you're interested in more references I'll be happy to provide them.

Within my discipline, economics, the scholar that definitely has considered with more detail the tension and potential contrast between ethical values on the one hand and certain market activities was the recipient of the economics Nobel Prize in 2012, Alvin Roth. He introduced the concept of repugnant transactions. A repugnant transaction is a trade that benefits the parties directly involved, who enter it willingly, without creating any visible cost or what we might call negative externalities on other agents, but these are trades that third parties, or if you want, society disapproves of, and often tries to prohibit or regulate very heavily based on moral grounds. What are these moral grounds, or moral principles that certain societies or parts of society might see as violated or endangered by allowing a particular market transactions? There could be an issue of coercion, undue influence versus certain parties. Or maybe some parties aren't really being benefited, but are being exploited or taken advantage of by participating in a particular trade. Another concern is one of fairness or lack thereof, where we can think of fairness as related to the equal access to certain goods and services that are perhaps considered so essential that they should be available to everybody, for example regardless of their ability to pay for them. But fairness might also refer to the distribution of the gains from a particular transaction, even if available to everyone. And at a deeper level, there is a sense in which certain market activities actually corrupt the dignity of us as humans and as human societies. There are many examples we can consider. Perhaps the ones people mention more often are cases where we put a price on the human body or body parts. Think about paying people to donate their blood, their plasma, or even their organs. Think about commercial

surrogacy, or prostitution. These activities are very often considered coercive, exploitive, and corruptive of human dignity all together. What is interesting is that many of these activities are actually praised if they do not include a price, or at least, they have a positive connotation. People who donate their plasma or blood, in fact people who donate their organs, say a kidney, are considered heroes. Sex, without a price, between consenting adults is in generally considered a beautiful thing, not something that corrupts human dignity.

Other examples in history include child labour, for example, but even lending money for interest, or certain types of insurances contracts, ethical concerns apply to many economic activities. And that's why Alvin Roth again, and I'm quoting him, said we need to understand better and engage more with the phenomenon of repugnant transactions. In the economy, we have to understand folk ideas, common beliefs, common views about what we can do in the market better than we do.

Another interesting case of repugnance markets is not about a particular transaction, but the way that transactions occurs. Consider for example certain pricing practices. called flexible pricing, or price discrimination, which just means applying different prices for the same good or services in different circumstance. If you subscribe to a magazine, the price you actually pay for each single number of the magazine is lower than what you would pay if you bough a single number without a subscription. On an airplane, you might be sitting next to a person who is sitting in a very similar seat, but the prices that you paid are considerably different. There is peaked pricing in electricity systems, there is flexible pricing in car riding systems such as uber and lyft. Where demand is higher at certain moments in the day or because of certain events, they charge a little higher for their rides, just like there are second-hand markets, for example, ticket scalping you can call it, for events such as concerts and sports games and so on and so forth.

Now, here I'm talking really about markets that are not morally controversial...Magazines, airlines, air travel, tickets for concerts and so on. But there are cases where the same pricing practices, which is just letting the market operate in a sense, receive a much different connotation. Let me mention a few examples from Toronto, the city where I live. In 2013 there was a major storm, and a few years after, 2019, last year, there was a fire emergency on one of the subway lines in the city, and in both cases, Uber and Lyft increased their prices by large amounts, because of high demand, just like they were doing in many other circumstances. But the public outrage was significant in those cases because people were in need in that moment and there was a sense that these companies were taking advantage of the situation. A couple of years ago there was a shooting on Danforth avenue, again, here in Toronto, two young women lost their lives and about a dozen other people were injured, and the community organized a charity concert in one of the local concert halls, and the price of a ticket was \$50, the revenues for selling the tickets, would go to the families affected by the shooting. Some people bought a lot of tickets, and they resold them through second hand sites, for higher prices, up to \$500. If you look at the terms used in for example, newspapers for these actions, we see, disgusting, immoral, predatory. Again, a practice in a particular market, that doesn't pose any major moral concerns, in that particular circumstance, can become actually highly morally contentious.

And this brings us, first, to the scenarios I mentioned at the beginning of this talk, and obviously, to the current pandemic. Because even in this case, we've seen how otherwise perfectly acceptable markets, perfectly acceptable practices, can be very contentious.

As we know, the COVID outbreak led to a huge spike in the demand for certain products, sanitizers, wipes, face masks, also some more complex health-related items such as ventilators. This high spike in demand inevitably led to a supply shortage. Demand was much higher than the available supply for certain products. There have been several accounts of people hoarding these products and selling them at many times the normal price, but online and offline. In some cases, wipes were going for more than \$200. It was a vast public outrage, almost everywhere in the world and that led to several regulatory restrictions or legislative provisions, there are websites you can report evidence of price gouging, there are also price caps implemented, the shutting down of certain vendors for particular items, more than a million it turns out on e-commerce platforms, as well as outright public production or control of production for example, for sanitizers, as a way to speed up supply and reduce the difference between demand and supply and keep the prices low. And the public outrage was really driven by moral concerns, moral outrage altogether. Especially for two main reasons.

One, there was a sense that these vendors were taking advantage of scared, uncertain frantic consumers at the worst possible time. They were essentially taking away these goods from stores and reselling them for much higher prices. Many people were also concerned about the fairness of such actions and pricing practices in terms of an equal access to goods, not everyone could afford at that point wipes, or masks, or sanitizers. Unfairness in the sense of unequal distribution of gains, this was a way to transfer essentially, gains towards profits, and those are unequal burdens. It turns out that low skilled, low salary workers, are the ones who are less able, less likely to work from home, in safer conditions, and are more in need of some protections in terms of hygiene products, and they're the ones who, because of price hikes, might be less likely to be able to buy and use these products.

On the other hand, if you take a purely economic approach, and in fact, several economists colleagues are still embracing this view in this circumstance, the view is very different. There is a much more positive view of letting the market work its magic, including price hikes, at least in the short term. Spikes in demand generate shortages, that's one of the arguments, and this leads to rationing, some people will not be able to buy these products because they won't be available. So who should have them? First come first serve? Should there be any other rule? Who establishes these rules? And that's where prices without any regulation are for. Without any explicit regulation, prices solve the imbalance between demand and supply by reducing demand because of the high prices. And the high prices are such that those who value a particular good the most, and have the willingness to pay a higher price, will obtain the goods. High demand and high prices will motivate more producers and sellers to make these products available to the public, so there will be more competition because of this higher incentive to produce. This will naturally push prices to the normal or competitive level, and there will be more products on the market. It might also mean that to produce more, the unit price of

production goes up. Need additional equipment, additional workers, you might use less efficient plants and so on, and so higher prices just compensate for higher cost. And so, going back to the demand side, higher prices are also a signaling device for otherwise irrational or too anxious consumers who would go and buy too much of a product and stockpile them. And so by having higher prices, they are less likely to do that.

Economists very often bring examples like rent control and too high minimum wages are an example of failure of regulation, where rent control leads to a lower supply of apartments for rent, or lower maintenance, and therefore quality, and minimum wages when they are too high, increase unemployment for example. So in general, this view points out to some benefits of letting the market operate freely even in these circumstances. So overall we see very different views, each of them you might see people giving credit to. Some of the proposals that have been advanced, even implemented, are trying to compensate these trade-offs. Price caps, as mentioned earlier, might be a way to avoid issues of exploitation and unfairness, but they lead to rationing and so they generate another problem. You can imagine to contain prices, and impose price caps, perhaps give a compensation or a subsidy to producers so they can have the extra profit needed to have the incentive to produce more. This solves the unfairness issue because prices are more affordable, but creates another fairness issue, as we are essentially transferring potentially public resources to private producers in the form of extra profits. You can also go the way to give grants to consumers to buy those products, those who can't afford them otherwise. But again, this would be a transfer of resources, and an unequal distribution of the gains. In some places, for example, local governors, have introduced public production, or the seizing of certain factories to convert to the production of certain goods. But again, how feasible is this? How efficient is this? How slow or how fast will public production occur. Who's going to pay for it? Are we going to pay for it, in taxes and so on? Where is the gain? Overall, what I wanted to point to with this consideration is that, the consideration of repugnance, so of the moral concerns towards markets, is not free. It implies trade-offs. And this is probably the greatest lesson that Alvin Roth, with his work on repugnance left us with. There are conflicts between different values that we need to somehow balance. And what from a scholarly and a policy point of view, but also from the point of view of citizens, it's important to really consider all these values, and also to consider that repugnance and moral concerns are a combination of different values and so another crucial aspect here is understanding what values are particularly salient in particular situation. Are we caring especially about exploitation of consumers? Are we caring about fairness in terms of access, or in terms of distribution? Of gains? And what is more important is going to drive a particular institutional response. And this is why understanding precisely what we care about, the values we care about as a society, will lead to different decisions. And this is also why for many these transactions from regulation of prices during a crisis, but those other transactions, paying for plasma, paying for blood, commercial surrogacy, we see different countries, different jurisdictions, having different legislations, because there are different trade-offs, to solve here.

What is important, however, is that, and this is a point I care about, in a situations like the current one, mutual trust and coordination among organizations, public authorities, is of paramount importance. It is hard to believe that you can achieve this level of coordination, for

example, in complying with social isolation rules and social distancing, without the social support for certain private actions and institutional choices. And that's why we really need to consider these concerns, and moral and social dilemmas, in depth, to find solutions that maintain trust and cohesion. This is always important, but is particularly relevant in these days.

Let me close with a couple of notes. First, if I had more time, which I don't, I would address another transaction where repugnance plays a major role and is particularly relevant in this context, and this is the supply of blood plasma. As it turns out, the plasma for patients who fully recover from COVID-19 is being considered for testing for some therapies for COVID, hyper-immune therapies as well as serum therapies. However, paying for plasma is illegal in most countries around the world, in Canada. Not in the US, where it's legal, and not in Germany, where it's allowed. But in many other countries. However, one might argue that in order to incentivize those who have recovered from COVID-19 to supply their own plasma, maybe paying them, because of the relevance and the social value of their plasma, paying them to incentivize and donate, might actually be a good idea. For a welfare improving idea, to create benefits for society. Here we have another hard moral and institutional nut to crack. If you're interested, I'd be happy to talk more about that.

Let me close up with a couple of readings or viewing suggestions relating to this. There is an Italian novel, it is actually one of the two Italian texts in the Western canon, it's called *The Betrothed* by Alessandro Manzoni. It's a historical novel taking place in 17th century Milan and among many other things, Manzoni describes the protests because of price hikes for bread in Milan due to poor harvest, a supply shortage essentially. And the flip-flopping of public authorities between cutting prices on the one hand and then leaving prices freely, leaving the market to operate freely led to more public unrest, seems quite related. There is also a theatrical play by Eduardo de Filippo, an Italian playwright, it's called *Napoli Milionaria*. Sometimes in English it goes with *Street-Side Story*. It's also a movie, and the play was recently proposed at the Stratford festival last summer. This is the story of the moral and human price that a family had to incur for engaging in hoarding and selling products that were scarce during the Second World War in Italy, at very high prices, engaging in black market activity essentially.

And if I may, I would like to conclude with a final thought with my late grandfather and namesake, because he used to own a small store in an Italian village, selling many different things, and again during World War II he had the opportunity to take advantage of the scarcity and shortages of the goods he would otherwise sell, by increasing prices substantially. He decided not to, and decided to take his own share of pain in that particular contingency, because of his own moral values, but also because he cared about the small society he was living in.

So, I leave you with this thought, and thank you so much for listening. I hope you all stay safe and healthy.