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THE IMPLICIT MORALITY OF THE MARKET *IS* CONSEQUENTIALIST

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A COMMENTARY ON Joseph Heath (2019), "Is the 'Point' of the Market Pareto or Kaldor-Hicks Efficiency?," ***Bus Ethics J Rev*** 7(4): 21–26, https://doi.org/10.12747/bejr2019.07.04

ABSTRACT

Joseph Heath states that our paper "misinterpret[s]" and so misrepresents his account. The present Commentary corrects the record. Our paper (Cohen and Peterson 2019) outlined Heath's account on his own terms; it explained that Heath distances himself from consequentialism. But then we *argued* that Heath is mistaken and so offered a repaired version of the market failures approach. Our central concern, in the original paper and in this short Commentary, is showing that the economic argument for markets is at the same time ethical, and then being more precise about the ethical consideration that does the work.

A RECENT COMMENTARY by Joseph Heath (2019) on Moriarty (2019) makes passing reference to our paper (Cohen and Peterson 2019). According to Heath, we "misinterpret" and so misrepresent his view in describing the market failures approach (MFA) as fundamentally consequentialist.

The present Commentary corrects the record: Our (2019) paper outlined Heath's account on his own terms; it explained that Heath distances himself from consequentialism, and we quoted Heath on the point: "I am not promoting some sort of welfarist consequentialism" (Heath 2013: 51). But then we *argued* that Heath is mistaken and offered a repaired version of the MFA—one that makes the conse-

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quentialism explicit. What follows explains this point, then focuses on why it matters.

Moriarty (2019) argues that the MFA – and with it the implicit morality of the market – is more accurately formulated with reference to Kaldor-Hicks efficiency. Heath (2019) notes that that would make the MFA utilitarian; he rejects Moriarty's argument, insisting that the implicit morality of the market is Pareto efficiency. For present purposes, we grant Heath his point. But the MFA is nevertheless thoroughly consequentialist (though not utilitarian) even when grounded on Pareto efficiency.

Heath's references to market efficiency and his description of the MFA as "Paretian" amount to two claims:

(i) According to Heath, and consistent with economic theory, the justification for markets is that they generate Pareto efficient outcomes—meaning that agents exchange to exhaust all opportunities to make themselves better off without making others worse off. These exchanges are good – exchange is promoted – according to economic theory because the exchanges result in surplus gains. And when markets are competitive and complete, surplus is maximized. Why is surplus important, why is it to be maximized? Because surplus represents aggregate welfare as understood in economic theory. This is straightforwardly consequentialist.

Our 2019 paper emphasized the role of markets in producing the optimal satisfaction of consumer preferences, but the two ends – maximizing total surplus and producing the optimal satisfaction of consumer preferences – are equivalent, because surplus is a measure of how well an economic system satisfies the preferences of consumers. So, within economic theory, when we say that Pareto improving exchanges make agents "better off," the improvement is realized in terms of individual preference satisfaction and then aggregate surplus. This is all thoroughly consequentialist on both ways of putting it—with reference to surplus/preference satisfaction as the end to be pursued. That said, economists themselves recognize that this is an incomplete conception of social welfare (see Hausman and MacPherson 1996), but it is the part of welfare provided by the market.

(ii) Heath (2014: 101): "[M]arket competition must be governed by a set of rules, restricting the range of strategies that individuals may employ" in order to preserve Pareto efficient outcomes. For example, markets do not produce efficient outcomes when there are monopolies, so market competition must be governed by rules that prevent monopolies. And, when law/regulation do not provide adequate protection, managers are bound by beyond-compliance norms—these norms are Heath's "efficiency imperatives." Heath sees the regulatory scheme and his efficiency imperatives as protecting efficient outcomes, needed to maintain the market's ability to maximize total surplus.

The logic of the MFA is this: the justification for markets – generating Pareto efficient outcomes – at the same time serves as the normative justification for laws/market regulation and beyond-compliance norms, so the commitment to Pareto efficiency is the "implicit morality of the market." And, as mentioned, the commitment to Pareto efficiency is fundamentally consequentialist, as are the laws/market regulations and efficiency imperatives derived from it. This shouldn't be a surprise. Amartya Sen (1988: 39), for example, notes that "consequentialism is implicit but firmly demanded" in references to Pareto optimality.

Heath (2014: 10), however, distances himself from consequentialism, describing efficiency as "an irreducibly normative principle." But here he makes a mistake. Heath (2014: 10) explains that,

> one way of thinking about the Pareto standard is to regard it as a general prohibition on waste, since if it is possible to rearrange the allocation of resources in such a way as to improve one person's welfare without worsening anyone else's, and yet this is not being done, it means that some resources are being wasted under the status quo.

And Heath associates "waste" with allocative inefficiency, a situation in which resources – as Heath (2014: 75) himself says – "are spent producing goods no one wants at the expense of goods that people do want." So, in his own explanation, waste is not wrong in some irreducible or deontic sense, or for some reason not tied to total surplus (equivalently, not tied to the satisfaction of consumer preferences). And so Heath's appeal to the problem of waste does not push the MFA outside of consequentialism.[2] To be sure, Heath could provide a different argument against waste from outside of economics, and such an argument could avoid the consequentialism—but this would come at great cost as it would separate the MFA from its grounding in economic theory.

In his recent Commentary, Heath instead emphasizes deadweight loss to avoid the consequentialism. He (Heath 2019: 23) writes, "It is noteworthy, in this context, that the standard argument made by welfare economists against price-fixing is not that it lowers aggregate social welfare, but that it generates deadweight loss." They differ, Heath (2019: 23) explains, in that "[a] deadweight loss is an unrealized exchange." He continues (Heath 2019: 24),

> This is why, in my discussion, I put so much emphasis on deadweight losses. These represent not just a failure to maximize social welfare. As unrealized exchanges, they constitute Pareto inefficiencies. The regulatory structure that governs the market – most obviously, competition law – is intended to maximize the number of Pareto-improving exchanges that occur.

Deadweight loss is a loss of total surplus; this Heath acknowledges in the passage just quoted. But at the same time Heath claims that deadweight loss represents something else, something further—"an unrealized exchange." But deadweight loss is not an unrealized exchange, it is the loss of surplus *caused by* unrealized exchanges, themselves caused by the inefficient allocation of resources. And the lost exchanges only matter because of the result (the reduction in surplus). So consequentialism again does the work; Heath's reference to unrealized exchanges does not push the MFA onto non-consequentialist ground.

Heath (2019: 23) allows that, if the MFA turned out to be a species of rule utilitarianism, that would not be a "death-knell." We agree. The laws and beyond-compliance norms that constitute business ethics on Heath's approach are grounded on the consequentialist consideration mentioned here, but – with Heath – they can be followed by managers in a deontological way. With Heath (and Christopher

[2] Alternatively, Heath might refer to productive inefficiency, a situation in which resources are underused and/or mis-assigned. The result is that fewer goods are produced thereby lowering preference satisfaction. And, again waste is bad (within economic theory) for reasons tied only to the satisfaction of consumer preferences.

McMahon [1981]), one central insight here is that there are distinctive normative requirements in the business context, derived from the implicit morality of the market. So – and this is a point we emphasized in our paper – acknowledging the consequentialist nature of the MFA does not change the substance of that approach—nothing is lost. The consequentialism (taking consumer preference satisfaction as the sole end to be pursued) is not a problem, though the limitations become clearer (more on this in a moment).

This all matters, to us and for the discipline of business ethics, for two reasons:

(i) Our central concern is showing that the economic argument for markets – the efficient satisfaction of consumer preferences – is at the same time an ethical argument. Heath's work on the implicit morality of the market, building on McMahon, advances this project, but it is essential that we be precise about the ethical considerations doing the work.

And, recognizing that the argument for markets is ethical can shift the dynamic in business ethics: many think of business ethics as advancing ethical arguments in the context of amoral economic activity, but seeing that the argument for markets is ethical pushes us away from this logic. Business ethics, instead, is a matter of weighing the consequentialist ethical benefit of economic activity and markets against other moral arguments/other normative concerns—for both managers and also for broader questions addressed outside of the scope of management.

(ii) Heath (2014: 174) claims that his efficiency imperatives are "pretty much all there is to business ethics." But when we see that regulation and efficiency imperatives in the MFA are all justified in consequentialist terms, tied only to consumer preference satisfaction, the need for further laws and additional beyond-compliance norms becomes clear. We made this case in Cohen and Peterson (2019). One example from that paper: the regulation of benzene to prevent worker exposure to toxic chemicals, outside of and without reference to efficiency considerations. Another example (Jacobs 2019: d3): the Danish government, "worried about the rise of drug-resistant infections, barred veterinarians from selling antimicrobial drugs directly to farmers."

In both examples, regulations (rules) are derived from ethical considerations other than the promotion of consumer preference satisfaction; the MFA cannot account for this. And, with Heath, when regulation is not adequate ethical considerations generate beyond-compliance norms that constrain managerial action—but, again, the MFA could not account for such norms in these two cases.[3] The MFA therefore leaves the manager without needed rules or norms in these two cases.

We should therefore reject the narrow economism Heath promotes; we should reject his suggestion that the market and market behavior could be governed by a commitment to efficiency alone—the position he explicitly adopts (Heath 2014: 199; Moriarty demonstrates this commitment in Moriarty 2019: 4, this is not a misrepresentation of Heath). This economism is inadequate and likely dangerous: a broader set of ethical considerations is needed to ground market regulation and beyond-compliance norms.

The deep irony is that business ethicists should be highly attuned to this economism, those (we) in business ethics should push back against the overly-narrow conception of business ethics grounded on Pareto efficiency, maximizing total surplus, optimizing consumer preference satisfaction. Acknowledging the consequentialism in the MFA is a required first step.

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[3] This critical point addresses Heath's account on his own terms, arguing that efficiency considerations cannot generate an adequate business ethics; we are not addressing questions that Heath brackets, in particular concerns about distribution (as in Sen 1970).

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