

# INFORMING THE CONSUMER IS STRENGTHENING THE ECONOMY

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## ABSTRACT

Adam Smith's assumption that consumers are rational and knowledgeable in their buying decisions is examined in this paper, along with the views of other prominent economists. It is concluded that this assumption is incorrect, though consumers are clearly somewhat rational and knowledgeable. The detrimental effects of the lack of consumer product knowledge are thus recognized in a few scenarios as examples.

Although, this would be a very valid conclusion for this paper, the paper follows this topic of Smith's faulty assumption for the purpose of making improvements of our economic system. The conclusion that organizing to enlighten consumers can correct for Smith's faulty assumption is proposed as a solution to many of the inequalities of our present free market system. Some details on the effective way to organize for consumers are mentioned.

Keywords: Consumerism, economics, information economy, corruption.

## A VERY SHORT HISTORY OF ECONOMICS

### *What would Adam Smith think of economics today?*

There is a Presidential election on the horizon this year. People from many different perspectives are taking positions on economic policies. Consistently, they refer to theories proposed by now famous economists such as Adam Smith [North, 1995], Karl Marx [Britannica,2008] , John Maynard Keynes [Kangas, 2008], and Milton Friedman [Wikipedia, 2008]. I believe that these theorists were more in agreement than disagreement, and that they are largely misunderstood in this regard. All of them are social scientists, who have dedicated their minds to the scientific method and applying it to economics. As a rule, economics is a social science, in which we are attempting to predict the behavior of people. People by nature are very complicated and somewhat unpredictable. So, in the realm of social sciences it is necessary to predict behavior by averaging in order to be able to generalize at all. Sometimes, we are unable to explain generalized patterns of behavior, and other times we can only do so by analyzing scenarios of human behavior. In economics, we are usually analyzing scenarios in the marketplace. The science itself was born out of the work of Adam Smith in his book, "The Wealth of Nations." For the most part, economists since Smith have not disagreed

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with him. They have mostly improved upon his theories and interpreted them in different ways. That is one of the purposes of this paper.

One of Adam Smith's assumptions, in making his theory of supply and demand, was that people are knowledgeable as to the value and overall impact of their buying decisions. This assumption was a necessary premise to his understanding of how free markets use prices to properly allocate resources, and direct economic activity to be more efficient and productive. According to his theory interfering with the free market interferes with the efficiency of the economy and has many other deleterious effects.

### ***Other Economists Improve on Adam Smith's Theories.***

Other prominent economists after him, like Karl Marx and John Maynard Keynes, would find this free market system susceptible to many kinds of problems. In Marx's times, the free market system created large fluctuations of unemployment and work force dislocation that resulted in instability to the general economy. Also in Karl Marx's times workers often received subsistence, or below subsistence wages, and suffered unhealthy working conditions. This was crucial to understanding Marx's surplus value theory.

According to Marx, the capitalist charged a surplus value for manufactured goods, above his costs and a fair return for his efforts. He was able to do this because he was in a more powerful negotiating position than the worker or the buyer of his products. The powerful negotiating position he enjoyed allowed him to offer subsistence wages, because the worker might not have any other option than working under such conditions. Capitalists could, on the other hand, offer these positions to many workers. To clarify, this is not to say that the worker didn't have any leverage in choosing one job over another. It was just that the capitalist usually had more leverage because he could choose between many workers, especially when the unemployment cycle resulted in many desperate workers. This is related to the reasoning behind outlawing monopolies. The capitalist, who is the only provider of a certain product, has so much negotiating power from his position that the free market pricing system can not function.

John Maynard Keynes was well read in both Marx and Smith, but he had perspective to add to this conceptualization of economics. Keynes understood how the business cycle leads to suffering and economic instability. In his studies he even invented the study of macroeconomics. But, he was not satisfied with understanding it; he was concerned with solving the problems of the great depression. Unlike Marx, Keynes didn't believe in Marx's simplistic solution to this problem, namely communism. So, he came up with adjustments to the free market system, based on comparisons with socialist economic systems. It would include raising government spending, while lowering taxes in times of economic recession, and lowering government spending, while raising taxes during economic expansion and inflation. As always seems to be the case, political leaders would misunderstand these applications of Keynesian theory, resulting in misguided economic policies.

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### ***A Renewed Belief in Free Market Economics***

It would not be until much later, though, that politicians would change their misguided policies for a very opposite approach, based on the theories proposed by economists like Milton Friedman. Friedman elaborated in many different situations, how government intervention into the pricing mechanisms of the free market consistently made for less efficient and productive economies. Although this was consistent with Keynesian economic theory on the whole, in details it differed. It also resulted in different economic policies by those politicians that would attempt to understand those theories. Many of the Western democracies would implement campaigns of privatization of the economy. One country after another went from using large state run companies to manage certain types of industries, to selling them off to private interests. Going along with Milton Friedman's approach, many countries began deregulating their economies as well.

### **IMPROVING ON ECONOMICS BY REALLY USING ECONOMICS**

#### ***What Would Milton Friedman Think of Deregulation's Latest Effects?***

It is impossible to know for sure if Milton Friedman would have agreed to the type of deregulation that has been happening in recent years in his native United States of America. Many blatant environmental and human rights abuses, among other types of abuses, have occurred as a result of the lack of regulation. Maybe Friedman would have pointed to the corruption of big government as the root cause of the problem, or maybe he would have recognized a limited role of government to regulate in some areas. Nonetheless, a political debate has ensued with one side proposing more protection through regulation, and the opposite side proposing less regulation for a more productive economy, at the expense of allowing more abuses of the system [Yasumoto, 2000]. At present financial analysts can actually calculate an estimated cost of regulations, and other socially responsible legislation. A good example of this is the cost of divesting from those involved in the genocide in Sudan. The UC Regents and State Pension Plan of California have done so as part of their divestment plan. On the other hand, it is more difficult to calculate the costs of the toxins routinely consumed as part of the normal diet. Even so, the richest families in the country have their children eating these foods. This has been documented in many studies, such as the recent study carried out on Mercer Island near Seattle, Washington [Schneider, 2008]. This community is the richest neighborhood in the highest per capita metropolitan area in the country. Still, the pesticides found in children's saliva here are among the most toxic used inside and outside of the country. The study serves as an example that flies in the face of belief that consumers know what they are getting, and as proof of the negative results due to this ignorance.

#### ***Opening the Economic Debate to Outsiders***

This paper proposes that this debate, in which we are supposed to choose between regulations to protect us or economic growth, is a fundamentally flawed debate; and that a deeper look has to be made to understand all the options available. There are many

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aspects of a society and its government's policies that can be adjusted for better results in areas of concern such as the environment, economics and human rights. Just as we are complex, the way we analyze ourselves should be complex and consider all the relevant details. Such a discussion includes overturning established assumptions that we find are flawed by closer observation. Who is to say that society is always better off having, for example, a higher GDP? If we were to end up with plenty of expensive products and most of them were so toxic that they shortened our life spans, are we better off being poorer? GDP or any other economic indicator cannot truly represent our well being. Unfortunately, this paper will not be able to go into the depth necessary to reevaluate or evaluate all of economics and all the options for improving our system. We will focus on one aspect of economics: Adam Smith's assumptions of self-interested rationality and maximization in the market.

Milton Friedman's arguments for less government intervention into the marketplace take us back to Smith's view that the market naturally regulates itself. But, as mentioned before, this is a social science, and not a physical science, dealing with human psychology. Human psychology is complex as there are many reasons why people choose to do what they do. This is really the central issue in predicting the economic behavior leading to the study of economics in the first place. Smith's assumption that people must make knowledgeable buying or selling decisions in order for his theory to work, begs the question, "Are people knowledgeable in these decisions?"

### ***A New Debate Based on Knowledge***

Knowledgeable? People are not even rational. Or to put it more diplomatically, it is part of the human condition that we are limited in knowledge and only sometimes rational. The answer can only be qualified as to degrees of knowledge, because people always have some knowledge but lack knowledge of most things, at the same time. So, this breaks down the argument that the law of supply and demand is some sort of absolute law, even though it should be obvious that no human law is absolute.

Hoping to give insight into how information is used and distributed in an unsymmetrical manner between consumers and producers. So, I carried a very simple survey. Whenever I went to go out to eat I asked, "What is the best thing you have, ... and what is the worst? Of course, I waited for the answer for the first part and then asked the second part. Every other time I asked for the best thing first and then asked for the worst thing as above. But, the other times I asked for the worst thing first. Out of twenty times total, everyone answered as to what the best thing was. One fourth of the total, or five times, they answered in some way to the question of what was worst, two times when I asked about worst first and three times when asked last. Fifteen times, or three-fourths of the time, they wouldn't answer what is the worst thing they had. Of course, there is always something that one considers to be the best and always something that is considered to be the worst. For whatever reason information was given about the best and not so much about the worst, however subjective the information itself was. What was not subjective was the clear bias to give good information about a product and not give bad information about a product. The sad thing that comes to my mind is that we are used to this bias and people around me even found it rude for me to ask what the worst

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product was. The consumer is afraid to ask the producer the real questions about their product and expects little information. This is at the heart of the problem. So, what can we do?

### ***Outsiders Improving the System from the Inside***

As with Keynes' approach, it seems more practical and more correct to build upon the strengths of Smith's economic analysis, as well as those that followed, then to tear it all down from the base and start over. Besides, it is almost instinctually obvious that we can fix some economic problems by fixing the way that buyers and sellers exchange knowledge. Effectively, we can improve upon the application of economics by making its assumptions true, or truer. This is the information age, wherein the communication and analysis of information has so many new possibilities. There is so much opportunity to improve in this area. Milton Friedman might chime in at this point to warn of the danger of involving government, for reasons of corruption and inefficiency. At the same time Karl Marx would correctly distrust the usual entrepreneur and his government, as they are both for sale. Hopefully, Keynes would come up with the solution I will propose.

We need a different psychology. We need a psychology, political system and economic system of knowledge. What I mean by that is that we need to build a system that promotes people getting correct information. And to do that we have to recognize like Marx and Friedman, that those who typically will promote ignorance about products are most often the producers according to the former, and their cronies in the government, according to the latter. Who else is there? The consumer and the worker both have historically made out worse than businesses in our country, with exceptions, due to the dynamics of negotiations. It is no coincidence that the capitalist makes more money than the laborer, and it is much less of a coincidence that the average CEO of a company makes 500 times what the average worker with his company. Hence, enter the consumer union and the labor union. They have had their place and seemed to have filled a need to negotiate collectively and organize collectively. They have had some successes, but poor people can't seem to get a break from the cycle of poverty, except those that escape to become skilled professionals or business leaders in their own right. On the other hand, as technology advances businesses have taken organization to a whole new level. Business is now global and has successfully organized along these lines, with accountability to the consumer or labor advancing slowly and often retreating.

It might seem like the workers and consumers of the world have been defeated; and at least temporarily, we are defeated every day. I beg you to find just one supermarket without the first pesticide ever outlawed, DDT, on any of its produce. Workers have many rights here, and consumers seem to have many rights. Everything works out fine, if workers in the United States are willing to buy goods manufactured by near slave labor, to make the kinds of ridiculous profits needed to pay CEOs what they make.

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### ***Using the Matrix to Be the Solution***

Fast forward to the present, and to the age of the internet. Now the same roads, of communication, used by the Romans to conquer and establish their empire can be used by those same people they conquered to take it back. The internet and the information superhighway are here and make the disparity between the rich and poor less significant in many areas. Many people can own a computer, even own a website, and have international recognition for that website. For the time being, the globe is one marketplace and is ruled by laws favoring businesses going global over consumer standard interests. But, as the world depends more and more on information technology, the playing field can be made more even. Consumer groups can organize on a global scale, do it more efficiently online, and use that same information technology to find out about the manufactured products they are exposed to. Only, once consumer groups unite along the lines of the internet, it will be much more difficult to break them down, and lie to them about the products in the market. An infrastructure with obvious benefits to society will have been constructed, that people in a relatively free society will resist giving up.

If eventually, as sometimes happens, these consumer groups gain the backing of the law, consumers will be even more protected. But, the most important change that could secure further change and protections for consumers and many other discounted groups is that of access to information. Anyone, given the chance, would most likely prefer a product that didn't have some undisclosed toxin, and the free market would eliminate such common products. By the same token, many people would not accept products manufactured at the expense of the abuses we are only rarely informed of.

What are missing are not the social, political or economic conditions for such organizations to exist. What is missing is the catalyst or the activation energy to start that level of organization so that change happens spontaneously in our society. That catalyst is the insight that starting such an organization is needed, and the initiative to get it started. Building upon what this paper stated earlier, this organization would eventually be self-sustaining because of its usefulness and the need for independence from corrupting forces, such as investor stockholders or sell out politicians. We are basically talking about a non-profit organization whose source of income would not be subject to the approval of businesses or government.

Forming an organization like the one I am proposing is definitely problematic. A person might postulate that if such an organization doesn't exist already there is a natural cause I am overlooking. There already are organizations like the one being proposed, but they fall short of fulfilling the role of the organization mentioned in degree. They are not widespread enough to be available to all. They only address a limited number of consumer issues. And, when they do address consumer issues they do not have specialized or relevant information. Most importantly, these organizations don't provide information in a convenient or usable manner. For example, if you want to find information about a product in regards to allergens you have to go to one website for that allergen, which will not even give information about any particular product if it is available at all. After that, if you want to find out about the safety of a particular children's toy you have to go to another website, where you may find relevant

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information about that toy, though you may not be even able to find the country of origin, or the manufacturer.

One or two websites bringing the others together are needed, that give product specific information. Because so much information is not made available to the public, this site needs to be interactive. This is so that the massive resource of individuals with knowledge about a particular product can contribute that knowledge for the public benefit. Hence, we are talking about a well known website, with organized links to specific areas of interest, product specific search engines and blogs in very specific areas of interest to bring a freer flow of information. I am working on this kind of website now. Care to help? Whether this will raise the Gross Domestic Product of a country or not, it is clear that better information will help us to not waste our money on poor quality products. If a consumer organization can make more correct information available when we need it, we can make the free market system work better for society and raise the standard of living wherever such organizations exist.

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