Notes on Charles Lindblom's The Market System

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Events of the last three decades make conceptualising market systems vital and there is surprisingly little inter-disciplinary exchange on this. We need to know scope and limitations of market systems. We need a general account of them, so we can then explore meaningfully the 'varieties of capitalism' that we see.

Lindblom asks too, rhetorically, why have there been no serious attempts by democracies to abolish the market system? We need to explain uniformity of opinion in favour of market system.

1. On Coordination

Lindblom explores the basic dichotomy of coordination versus command as a means to organise needed and desired activities in society.

Market systems coordinate activities, including resource allocations and production decisions, through mutual interactions of buyers &sellers. In doing so, incentives for continuous improvement and mutual cooperation are often entailed.

Market systems are remarkably effective at coordination of all manner of 'performances' - tasks and services in chains of production of value. We are often too focused on the periodic failures of coordination that result in disruptions and shortages. Coordination is mutually beneficial but not purely voluntarily. In free markets, each economic actor is, in a practical sense, rendered rather unfree by competitive pressures - at least in the short to medium term. It is the customer who is made king by competition.

A market system is not limited to 'economic activities' – in Lindblom's words, think society, not economy. Much coordination of activities - of performances - is not done on the basis of a direct economic transaction. The family unit, networks of friendships, voluntary community mutual help, represents a very large part of the total coordination that happens in any society.

Ongoing, endless mutual adjustment is a key feature of a market system (and indeed of any effective conversation - and speakers routinely correct misunderstandings as rapidly perceived. Responsiveness in markets is an extension of natural social responsiveness. It is the large scale of organisations, and hierarchy within them that leads to a loss of responsiveness). Coordination then is more responsive, efficient, in the face of continuous change & the limitations of inevitably imperfect information.

When we view economic activity at the level of the everyday transactions between individuals we see this at work. Yet in our studies of business, and in media reporting, there is an elite bias in the focus on leadership and 'command & control'.

Lindblom provides the example of a Milan coffee house and the chain of coordinated performances that bring beans from around the world and to deliver the coffeehouse experience. It is much richer perspective when we think of a set of coordinated performances rather than to focus merely on the 'marketplace'; which is nonetheless vibrant and interesting.

There is much more cooperation than competition in a market system. There is a global market system despite there being no global government. No government has achieved similar feats of coordination. There is diffusion of participation and control. As a result there is better use made of ideas and insights. In command systems, by contrast, there are many veto points. Adaptability is enhanced in market systems.

2. States and markets

Government is a major contributor to the development and stability of a market system & is a frequent disruptor. A strong state may enforce the logics of voluntary market coordination - commanding that no other societal actor result to force (actual or, for instance, through market dominance) to command certain economic outcomes. All states resort to making some commands. Some may extend this to the economy at large, with often problematic outcomes.

Democracies have market systems, but the reverse causality is certainly not assured. That is, market systems need not always lead to democracy.

Market voting (for goods & services / specificity) & political voting (for processes, intentions, individuals & teams).

At least in the economic arena, competitive markets therefore provide a mechanism for masses to make elites more accountable.

3. Managing conflict

Markets keeps people busy and leaves them with less time to fight and engage in destructive pastimes out of boredom or a sense of hopelessness.

More importantly though, market systems provide a simple decision rule in dealing with scarcity: endemic shortages of things that people would like to have. The simple rule of *quid pro quo* is: you can have want you want up to the value of what other people will pay you for what you have or you can do

This eaves the big distributional issue unresolved. Yet scope for entrepreneurship etc makes for relative social peace, compared to most other means of assigning assets of value to people. It also provides a clear incentive to both creativity and sociability.

4. Firms

Lindblom refers to companies as islands of command in a sea of market-based cooperation.

Why do firms exist? Efficiency of decision-making, in the context of mobilisation of mass resources? When does command work better? The costs of a command-based approach?

Further issues explored include:
Ownership of enterprise – private, state, collective
Separation of ownership and control – managerial elites, diffused shareholders (and, increasingly large proportion of communities)
The privileged position of firms – limited liability etc
The state as risk manager of last resort

5. Limits to the market domain

Societies rarely permit the 'maximum domain' of markets. Lindblom points out, for instance, that most societies would not permit a trade in orphans. Neither in modern societies can people sell themselves or their children into slavery (it was permitted often in the past, including in Japan).

Today, in general, objects & performances can be bought & sold if:
1. subject to contingent human control
2. scarce
3. obtained without compulsion

Compulsion to maintain acceptable market systems is rather common. We make speak then of a 'chosen domain' of the market, rather the maximum domain that might arise in the absence of state authority. The state becomes a regulator, customer, compeller of transfer payments, insurer. It may compel private contributions to the provision of collective (public) goods; as otherwise a free rider problem would arise. Firms and families also function, in practice, as instruments of compulsion but the scope for such will be more or less constrained by the state.

6. Qualifying the 'quid pro quo' rule

Although it creates incentives to work & innovation, the *quid pro quo* rule that people are free to buy what they want with the money they can earn in the market, it clearly has many problems. Ill-fortune may handicap many, & socially valued actions often go unrewarded. There is also the 'prior distributions' problem: current wealth much influenced by the past. Inheritance is taxed in some countries but not all, and generally there has been a move away from doing so in some economies.

The creation of a welfare state provides minimum (floor) benefits through public choice. Additional benefits may be contracted for through market choice - such as private health insurance. There is a strong economic logic for public coordination and provision of core insurance owing to the efficiency entailed in large insurance pools.

7. Efficiency

Efficiency can be understood here as the ratio of valued outputs to valued inputs.

Knowledge of costs is essential to rational choice & efficiency. Poor allocative efficiency brought down communist regimes and imposes enormous costs on the poor and others. Collective choices, namely most central planning in command economies, entail profound difficulties in weighting costs & benefits.

Allocative choices, devolved, made at the margin (marginal benefits vs costs) are efficiency enhancing.

Efficiency prices (pareto optimality) – gains from trade & specialisation with no forced imposition of costs on others (true even for random initial allocation of resources, abilities etc)

When markets are working well prices ‘correspond to the frequency and intensity of desires’. Efficiency prices change as people change their minds about value. Efficiency prices ‘make cost information universally available’, ‘and they force cost information on every chooser’

Lindblom also discusses ‘motivational efficiency’: contingent specific benefits from entrepreneurial responses to efficiency prices (altruism is not enough).

8. Externalities & inefficiency

Externalities are spillovers, that is, impacts on third parties from an economic transaction between two parties, and for the which the contracted price does not address. There are both negative & positive externalities (the former being, for instance, pollution). Increasingly efforts are made by states to solve negative externalities through markets – trade-able pollution rights etc. This would involve the state in forcing markets to be more efficient.

Government interventions as ‘inefficient’?: whilst market-distorting, efficiency question hangs on the objective & efficacy of the intervention.

Government interventions to secure social justice outcomes often result in new unintended (grey markets’ - such as for sublets on rent-controlled apartments with cash payments that may capitalise the effective subsidy entailed in the rent control. This can lead to a new round of catch-up regulation which leads to further regulatory complexity.

9. Social justice issues

‘too little too late’? – allocative efficiency after initial allocations (prior determinations) of property, abilities etc

Prior determinations (inherited wealth) as consequence of past allocative efficiency (via entrepreneurship, govt interventions etc)

10. Do market systems change personality?

Lindblom proposes questions about whether the culture and practices of market systems render people shallow petty egoists?
Instrumentalism? Degradation of work? Fragmented, commercialised?
Materialism & commercialism: values & self-identity, attainment?
Ethics in markets?

Modern values in contrast to the values of aristocrats, peasants, soldiers
Persuading the masses: spending to influence, create wants

Selling the system? Market & political circularity. Lindblom argued that, historically, elites (royalty, aristocracy etc) conceded spheres of liberty to merchants (entrepreneurs) who together then later feared a universal franchise: leading to investments in education, mass persuasion in the virtues and values of a market system.

11. Firms in politics

Firms & market elites as privileged actors in the political market

Large enterprise & modern democracy: Lindblom is critical of the firm as political actor violating equality precepts.