Exchange & Production

COMPETITION,
COORDINATION,
& CONTROL

Third Edition

Armen Alchian & William R. Allen University of California, Los Angeles

Contents

Chapter One

SCARCITY, COMPETITION, AND SOCIAL CONTROL

The Magnitude of the Task of Economic Control 2
Universal Scarcity 2
Costs Are the Best Forsaken Alternatives 4
The Problem of Organizing Production 5
Methods of Organizing Economic Activity 5
Competition, Coordination, and Control 7
Controls, Competitive Criteria, and Survival Traits 8

Attributes of Economic Analysis 9

Summary 10

Questions 11

Chapter Two

CONSUMER DEMAND

The Unit of Analysis Is the Individual 13

Numerical Illustrations 15

The First Law of Demand 15

Demand versus Amount Demanded 16

Personal Use Valuations and Expenditures 17

The Paradox of Value 19

Needs or Amounts Demanded 20

Marginal Revenue 21

Price Change versus Other Factors Affecting Demand 22

Meaning of Change in Price and Change in Quantity 23

Elasticity of Demand to a Price Change 25

The Second Law of Demand 28

Illustrations of the Laws of Demand 29

Estimates of Flasticities of Demand 32

Income Effects on Demand 33

Price Effect on Wealth and Hence on Demand 34 Alleged Exceptions to the Laws of Demand 35 Direct Evidence of Validity of Laws of Demand 36 Pricing Tactics: A Preview 37 Utility-Maximizing Behavior 38

Summary 38

Questions 39

Chapter Three

EXCHANGE

Trade without Surplus Goods 45
Money, Markets, and Middlemen 48
Open Markets and the Costs of Exchange 50
Restraints on Open-Market Competition 51
Ethics of Open-Market Exchange 52

Freedom: As You Like It 53 Criticisms of Methodology 54

Self-interest 54 Summary 54 Questions 54

Chapter Four

MARKET PRICES AS SOCIAL COORDINATORS

Market Demand 58

Market Supply and Demand: Graphic Interpretation 59

Production and Supply 63

Who Pays a Tax? The Answer by Demand and Supply 64

Smog Removal and Land Value 68

Rental and Allocation by Consumer Competition 69

Price Controls, Shortages, Competition, and Discrimination 70

The 1975 National Energy Act: Erroneous Economics but Good Politics? 73

Economic Rent 75

Pareto-Optimal Allocations 76

Summary 77 Questions 78

For Further Study: Futures Markets 81

Are Specialization and Efficient Production "Good"? 156 Reprise and Preview 157 Summary 158 Questions 159	
Chapter Eight	
PRODUCTION BY FIRMS	163
Joint Production 163 Control, Property Rights, and Incentives 166 Substitution, Complementarity, and the Demand for Inputs 173 Summary 178 Questions 178	
Chapter Nine	
BUSINESS FIRMS: OWNERSHIP, CONTROL, AND PROFITS	183
The Business Firm 183 The Corporation 185 Fundamental Sources of Profits 188 Barriers to Entry or Filters? 190 Business Profits 192 Misdefinitions of Profits 194 Summary 195 Questions 196 For Further Study: Interpreting Financial Statements 198	
Chapter Ten	
PRICE TAKERS' SUPPLY AND PRICE RESPONSE TO CONSUMER DEMAND	205
Marginal Revenue Equals Price 206 Market Supply: Aggregated Supplies from All Firms 211 Long-Run Supply Response: Entry of New Firms and Equipment 212 Short Runs and Long Runs 216 Consequences of Wealth-Maximizing Response to Market Demand 217 Some Pricing Tactics 228 Derived Demand 229 Review and Prologue 231 Summary 232 Questions	

Chapter Eleven	
PRICE SEARCHERS	237
Market-Power Price Searcher 237 Price and Marginal Revenue of a Price Searcher 239 Demand Changes and Effects on Output and Price 242 Seller's Search for Wealth-Maximizing Price, Output, and Quality 244 Survival of Best of Actual Activity 246 Monopoly: Open- and Closed-Market Price Searchers 246 Some Price Searcher Pricing Systems 247 Effects of Different Pricing Systems 256 Summary 257 Questions 258	
Chapter Twelve	
COMPETITION AMONG THE FEW	263
Coalitions, Collusion, Cartels, and Firms: An Exercise in Names 263 Collusion among Producers 264 Oligopolies 271 The Law and Market Competition 272 Common Misinterpretations of Modern Business Actions 273 Summary 279 Questions 280	
Chapter Thirteen	
RESTRICTED ACCESS TO MARKETS	283
Political Restraints on Consumers' Market 283 Public Utilities 290 Patents and Copyrights 292 Monopoly Rents: Creation and Dissipation 293 Summary 295 Questions 295	
Chapter Fourteen	
INCOME FROM PERSONAL SERVICES	299
Productive Resources and Incomes 299 Supply of Labor 300 Never Too Few Jobs 304	

Income Differences 309 Observed Differences in Personal Income and Wealth 311 Patterns by Family Size 312 Why Incomes Differ 313

The Poor 318 Technological Progress and Jobs and Wages 320

Summary 322

Questions 323 Chapter Fifteen

LABOR-MARKET INSTITUTIONS

Labor Unions 325

Employee-Employer Bargaining Power 328

Labor-Union Objectives 328 Do Unions Raise Union Wages? 329

Legal Restrictions on Open Markets for Labor 334 Closed Monopoly: Buyers Close a Market to Competing Buyers 337

Summary 339 Questions 340

Chapter Sixteen

Questions 365

Sources of Wealth 344

WEALTH: SAVING AND INVESTING

Property Rights, Growth, and Conservation 345 Investment Activity 347

Demand for Investment: The Most Profitable Pace of Investment 348 Lending 348

Interest Rate and Quantity versus Change in Quantity of Money 355

Competition in the Capital Markets 356 Legal Restraints on Access to Loan and Capital Markets 358

Personal Investment Principles 360 Summary 363

Chapter Seventeen

UNEMPLOYMENT AND IDLE RESOURCES

Numbers of Employed and Unemployed in the United States 371 Who Are the Unemployed? 373

Trends in Unemployment 377 Changes in Structures and Aggregate Demand 378 Fluctuation of Aggregate Demand 381 Economic Fluctuation and Full Employment 382

International Comparisons 383 Summary 383

Chapter Eighteen

Questions 384

THE DOMESTIC AND POLITICAL ECONOMIES

The Nonmarket Domestic Economy 387 Measuring National Income: Value-Added 388

The Scope of Government Economic Activity 392

Public Goods and Government Action 397 Government as an Economic Stabilizer 398

Summary 401 Questions 402

Chapter Nineteen

What Is Inflation? 403

INFLATION

What Causes Inflation? 405

Distinguishing True from Apparent Causes of Inflation 409 Inflationary Redistribution of Wealth 410

Inflation: Taxation without Legislation 413

Living with Inflation 414 Dealing with Inflation 417

Anti-Inflation Monetary Reforms 419

Transient Effects of Changing Inflation Rate on Employment and Production 419

What Can You Do to Reduce Inflation? 420

Recessions Can Occur During Inflation 420 Summary 421

Questions 423 For Further Study: Creation of Money by Bank Deposits and Loans 425

Appendix: Using Math and Graphs 429 Answers to Selected Questions 437

Glossary 461

Index 467