

# Economically Sound, Ethically

## Business

"Price gouging" may make sense to economists. But there's more to life than the laws of supply and demand.

By David Futrelle | Nov. 02, 2012

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In the wake of a calamity like Superstorm Sandy, is it fair for businesses — from corner bodegas to gas stations to car services — to jack up their prices, earning windfall profits off the desperation of their customers? There aren't a lot of people who would answer yes to that question; in the midst of the devastation of Sandy, this sort of price gouging seems not only deeply unethical but almost, you might say, treasonous. One disgruntled consumer told CNBC.com's John Carney he considered it a kind of "reverse looting."

So it was hardly surprising to hear New Jersey Governor Chris Christie issue a blunt warning to merchants that price gouging is illegal and brings harsh penalties. "During emergencies, New Jerseyans should look out for each other," Christie said in a statement, "not seek to take advantage of each other." New York Attorney General Eric T. Schneiderman issued a similarly stern warning.

But there's one group of people who don't share the general distaste for disaster profiteering: economists. Why is that? Because what most people call price gouging is, to them, simply an example of the laws of supply and demand working as they should.

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In a capitalist society, after all, prices aren't set according to moral rules or by fiat. To oversimplify a bit, merchants charge whatever they can get away with charging and that won't persuade their customers to desert them for a cheaper competitor. In the wake of a disaster, with supply limited and demand (for everything from gas to transportation to flashlight batteries) high, prices are supposed to rise. That's the invisible hand at work, baby!

And so we've seen a very strange debate take place in the media in recent days. Strange, in that a seemingly unlikely coalition of writers on economic subjects has come out swinging — in defense of price gouging. It's not surprising to see writers with a conservative or libertarian bent take this stance. Libertarian TV personality John Stossel has penned a veritable paean to price gouging for Fox News; a *Wall Street Journal* op-ed invites us to "hug a price gouger" today.

But the gougers have also found an improbable defender in the form of Matthew Yglesias, the lefty-liberal business and economics correspondent for Slate. In a post called "The Case for Price Gouging," Yglesias lays out the basic economic logic for letting supply and demand work its magic unfettered by legal or moral restrictions:

Letting merchants raise prices if they think customers will be willing to pay more isn't a concession to greed. Rather, it creates much-needed incentives for people to think harder about what they really need and appropriately rewards vendors who manage their inventories well.

(PHOTOS: [Capturing Sandy's Wrath](#))

In a follow-up post, he suggested that anti-price-gouging laws were exacerbating the gargantuan gas lines that have grown like mushrooms all over the New York City area in recent days:

If it were possible to earn windfall profits by transporting gasoline into the affected areas, then human ingenuity would be finding ways to do it. But if you restrict retailers to earning merely ordinary profits,

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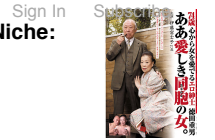
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Libertarian ideologues and liberal business journalists haven't been the only ones trying to make this case to the public. For better or worse, so have the folks at the car-summoning service Uber. On Wednesday, with trains in NYC out of commission and demand for its services high, the company switched to "surge pricing" at twice its normal rate. When riders complained, the company [took to Twitter](#) to explain that "higher prices means more drivers will come out and work. We've seen nearly a 50% increase in supply this morning."

([MORE: What Good Is a Gas Station \(or a Generator\) If Gas Can't Be Pumped?](#))

This Econ 101-style explanation evidently didn't go over well, and the company turned off surge pricing while still paying drivers a bonus. A day later, it turned surge pricing back on again. On Thursday, Uber [tried to explain](#) its position on its blog, essentially casting itself in the role of the helpless victim of economic forces beyond its control:

[I]n order to maximize the number of drivers on the system yesterday, we started paying drivers 2x the fare on all trips — and in the meantime charging riders the standard 1x fare avoiding surge pricing for most of the day after Sandy. Doubling drivers' fares tripled the number of cars on the road and kept them out there far longer. However, footing the bill for higher driver costs came at a significant expense to Uber with over \$100,000 in additional payments to drivers in a single day — something we can't continue indefinitely without breaking the bank ...

Later this morning we will be reverting back to standard Surge Pricing for riders. It is a hard decision, but one we feel strongly about. Without raising the price, there will be less than ½ the number of drivers on the system with several times more demand on far fewer drivers. Without Surge Pricing, Uber would become essentially unusable this week.

Somehow I doubt this explanation will go over any better than Uber's original tweet. Oh, the economics of it makes perfect sense. It's just that right now, with so many people suffering, the cold logic of capitalism seems callous and morally suspect, an affront to basic notions of fairness. Price gouging might, at least in theory, help shrink lines and reduce shortages. But I think most people would rather wait in line than have someone make a windfall profit off their desperation.

At a time when some people have literally lost their lives trying to help others, Uber's not going to get a lot of sympathy for its one day of lost profits.

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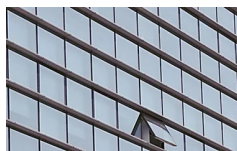
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