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How does Arrow answer arguments such as Friedman’s? Well, Arrow argues five things:

1. The forces of competition are not always so strong, and firms may be able to exercise market power, in the limit as a monopolist.

2. Even if perfect competition exists, and no firm can exercise market power (facing a downwards-sloping demand curve), there is no guarantee that the market allocation of income and wealth will be equitable, even if the market is extremely efficient in transforming inputs into outputs.
3.
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4. Further, market externalities, such as pollution and congestion, mean that firms and individuals may not be paying for all costs they impose on others.

5. And information asymmetries may lead to bad decisions and to deceit: the “lemon” new car, the new pharmaceutical drug.
Means to achieve changed corporate behaviour?

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a.
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b. taxes
c. common-law legal liability — firms can be sued
d. ethical codes

We shall examine these.
Reputation.

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Smith speaks of virtue as the “fine polishing” on the wheels of society, and vice as the “rust” on the wheels.
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The 1998 Nobel laureate Amartya Sen wrote in *On Ethics and Economics* that value judgements are pervasive, that ethics doesn’t subvert economics as a science, that ethics is part of economics as a science.
Game theory and the evolution of fairness

Is it rational to be ethical?
Game theory and the evolution of fairness

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Would we really all be better off if we looked after Number One?
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Darwin’s evolutionary biology was used by others (such as Herbert Spencer, who coined the phrase “survival of the fittest”) to argue that altruism was unnatural and weak.
And recently ...

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There has recently been evidence of the concept of “fairness” among monkeys in the lab, which suggests hard-wiring via evolution in the brain.
Utilitarianism

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2. The *good*: happiness/satisfaction is good.
Criticisms of utilitarianism:

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   — or against duties of truth-telling or promise-keeping
Rights?

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Utilitarianism missing a link to morality of the person.
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<thead>
<tr>
<th>Efficiency v. Equity</th>
<th>Status Quo Ante</th>
<th>efficiency</th>
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<tbody>
<tr>
<td>Less efficiency, greater equality.</td>
<td>Smaller cake, more even slices.</td>
<td>( \cdot A )</td>
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<tr>
<td>Larger cake, more even slices.</td>
<td>Less equal</td>
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<tr>
<td>Efficiency v. Equity or Fairness (lexicographic ordering)</td>
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Consequences?
Confucian Ethics

Kong Zi or Confucius (550–479 B.C.) has influenced over 2000 years of thought in China and beyond.

Master Kong developed the three principles of *Li*, *Jen*, and *Chun-Tzu*.

**Li**: the ideal standards of conduct: religious, moral, and social

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The Silver Rule:
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The Silver Rule:
“Don’t do unto others what you would not like them to do to you.”

Li provides a structure for social interaction
Jen makes it a moral system.
Chun-Tzu

Chun-Tzu (or Junzi, ruler’s son):
the true or virtuous gentleman or person
he who lives by the highest ethical standards,
and displays the five virtues:

1. self-respect
2. generosity
3. sincerity
4. persistence
5. benevolence
Chun-Tzu

Relationships:

- as a son: loyal
- as a father: just and kind
- as a husband: righteous and just
- as an official: loyal and faithful
- as a friend: faithful and tactful

Note: Confucius held that we are inherently good creatures.

Against Christianity: ?
Chun-Tzu

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Against Christianity: ? Original sin.

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see http://www-chaos.umd.edu/history/ancient2.html for
discussion of his disciples Meng Zi and Xun Zi and the schools
of Literati and Legalism and of yin-yang and of Mo Zi.