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Most of us are moral most of the time - and so are our markets

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EASTER MONDAY isn't a bad day to observe that there's a lot more morality in economic activities than most people - including economists - realise.

A new book, Moral Markets, edited by the neuroeconomist Paul Zak, and published by Princeton University Press, argues that most people behave ethically most of the time.

"Just as most human beings have an intact and active moral compass, so, too, does economic exchange, the child of human minds, have a vigorous moral dimension," Zak writes.

Most economic exchange, whether with people you know or with strangers, relies on character values such as honesty, trust, reliability and fairness. And a set of shared values is essential to the functioning of modern economies.

That's the first sense in which markets are moral, Zak argues. The other sense is that market exchange itself can lead to an understanding of what constitutes fair exchange, and in this way build social capital in the community. Research has shown that the values that create social capital are a potent stimulus for economic development.

"Exchange is inherently other-regarding," Zak says. "Both you and I must benefit if exchange is to occur. In this sense exchange in markets is virtuous: one must consider not only one's own needs but also the needs of another."

Where does our sense of morality or possession of "values" come from? It's bred into us. Humans are a highly social species - we are "hypersocial apes" - and gauge our own and others' behaviour against social expectations that are manifest as values.

Neuroscientific research has generally failed to support Immanuel Kant's notion that morality is learnt by rational deduction. When viewing immoral acts, nearly all humans have a visceral, emotional and rapid neural response.

In many cases even children have similar reactions. So we don't need to learn what's right and wrong. Most of us know it - or better, sense it - immediately.

"These moral emotions have been localised to evolutionarily old areas of the human brain," Zak says. Many moral decisions, including market decisions, have both cognitive and emotional components.

This is not an attempt to sanctify capitalism. It's an attempt to understand how markets actually work and put back into the story important elements left out of the economists' conventional model, with its focus on supply and demand

and price, and its lack of emphasis on "institutions" (which include the moral values of the participants).

As the book observes, the presence of values such as trustworthiness, fairness and honesty is so common it goes largely unnoticed. But it's not smart to take them for granted.

The authors say they fully acknowledge the role of self-interest as a critical ingredient in what makes markets work. But "pure, unbridled self-interest does not a market make". You need self-interest and moral values ("moral" values are those that concern our relations with others).

Nor are the authors seeking to imply that other, non-market systems for organising economic activity lack values. Indeed, if those systems are to work they'll require their participants to exercise moral values.

The authors aren't suggesting that people in market economies never lie, cheat or steal. Their goal is to explain why people don't do so more often.

Exchange in markets requires the solving of fundamental problems of co-operation and reliability. Our external institutions, such as the law, often intervene when individuals and firms lapse from a given standard, providing reinforcement of our value-based expectations.

The law, and the constant threat of its enforcement, is critical in providing the predictability and stability needed for markets to work. Yet the law very often can be seen as a means of reinforcing values which are internally motivated.

What's more, most of us abide by certain internally motivated values even in situations where we aren't certain what the law requires, or where we know there's no chance we'll be caught disobeying the law. More often than not, external enforcement is not required.

The widespread belief - held also by many economists - that markets are amoral is not only mistaken but also dangerous because it sometimes leads policy-makers to "reform" institutions in ways that don't maximise the benefits of values.

Values-based approaches, where they work, provide private, internal institutions that come at a far lower monetary cost than government-enforced laws and other externally enforced institutions.

And overreliance on external institutions - such as monetary incentives or disincentives - may in some cases crowd out the spontaneous workings of values. Sometimes monetary reward is a poor substitute for duty, honour or professionalism in encouraging people to do the right thing.

It's a shocking thought, but it's true.

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