

COB Review by Stephen Miller for 3/19

Title: "The Undercover Economist: Exposing Why the Rich are Rich, the Poor are Poor – and Why You Can Never Buy a Decent Used Car!"

Author: Tim Harford

Publisher: Oxford University Press

Length: 288 pages

Price: \$26.00 (hardcover)

Reading time: 5 hours

Reading rating: 8 (1 = very difficult; 10 = very easy)

Overall rating: 4 (1 = average; 4 = outstanding)

One of the most basic principles of economics is that voluntary exchange makes both buyers and sellers better off. Monetary prices facilitate such exchanges, so long as they are allowed to rise and fall as market conditions change. Economists like to call those changing conditions “Supply and Demand.”

In *The Undercover Economist*, Tim Harford uses one fascinating example after another to illustrate this well-established yet underappreciated concept. The *Slate* Columnist begins by simply explaining what markets are and how they work, beginning with the market for a cup of coffee. Harford’s sense of wonder and enthusiasm can turn a seemingly mundane topic, like the price of coffee, into an exciting inquiry. The powerful insight behind the book, though, is that even apparently simple goods are incredibly complex once you scratch the surface.

Why does a large cup of coffee cost more than a small one? The author explains that for the coffee shop owners, the cost difference is minimal. It scarcely takes more land, labor and capital to pour a 20 ounce cup than a 12 ounce one. Are sellers just greedy monsters, then? Harford argues that they are not – that by selling different sizes and flavors the coffee shop is of course improving its profit, but it is also offering more value to consumers. The large cup of coffee may be marked up in one sense, but in another the small cup has been marked down. Customers who are unwilling to pay a premium for large, fancy espresso drinks still have the option to pay much less for a small, plain one. The underappreciated notion here is that choice really does make people better off. If Starbucks only offered Venti Mocha Lattes, then many customers would be left out.

The author argues that this strategy of what economists call price discrimination is almost always a good thing for consumers. Those who are willing to pay a premium for features and convenience gain choices, without any choices being lost to those who are not. Problems mostly arise when voluntary exchanges are not allowed. In Harford’s analysis, this often takes the form of allowing people to have for free what they would otherwise pay for.

In economics this is often called the “tragedy of the commons.” Harford gives an example of public roads, where in most cases drivers do not pay for road construction and

maintenance based on how much they travel, but rather through fairly indirect forms of taxation. In the author's terms, taxes force people to pay an average price rather than a marginal one. The result in urban areas is daily traffic jams. The solution to traffic congestion is not, according Harford, to just raise the price of driving, but to *raise it in a particular way*. Simply charging higher highway taxes or registration fees will raise the average price paid by everyone. But that will only have a minimum effect on traffic. The trick, Harford explains, is to charge drivers more *at the margin*, which means to charge the most to those who drive the most. The example the author gives of marginal pricing is London's toll law implemented in 2003, that created a "congestion charging zone," requiring the equivalent of a \$9 charge per day to drive into the city's center. In the following year, the number of private vehicle trips into London fell by a third, while the numbers of bus passengers and cyclists increased.

The book proceeds on with example after example, from a public library in Cameroon to fluctuation in Grolsch Brewery shares, consistently conveying the importance of price and the benefits of voluntary exchange. It is an easy, but excellent read for anyone interested in economics; for casual readers it is superior to a typical college economics textbook. Harford has translated much of the difficult and jargon-rich language of economics into a highly intuitive and insightful discussion of everyday life.

Stephen C. Miller is a professor of Economics in the College of Business at Western Carolina University. His interests include Public Choice Economics and Political Economy. For previously reviewed books, visit us at our website at www.wcu.edu/cob/.