profits, some firms would leave the industry and profits for those remaining would rise. Thus in the long run profits *do* tend to be at the so-called normal or average level.

However, at a given moment of time in a changing, dynamic economy, few firms or industries will be in this long-run equilibrium position. Most will be in the process of making adjustments to the changing circumstances. Thus in some industries, profits will be well above normal, and in others, profits will be well below normal.

It is this fact which leads the firms involved to make the adjustments called for in the service of consumers. The abnormally high profits in some industries are the signal that consumers are calling for more firms to enter those industries. The below normal profits or outright losses in other industries are the signal that consumers are calling for some firms to get out.

The importance of this signal system can be illustrated by the life-history of the ball-point pen. When Reynolds produced the first ball-point pen, he sold it for around $12.95. It is doubtful if, even then, production and distribution costs were as much as one-fourth of the selling price. By any measure known to man, Reynolds was receiving abnormally high profits. However, the signal went out loud and clear and soon every pen company had its ball-point pens and new firms entered the field almost daily. Within a short period of time, the price of the pens had dropped below five dollars. Now I am writing this paper with a pen that I bought with nine others for a total cost of $1.19 for the 10.

Suppose the government, shocked by Reynolds' profits, had insisted on recapturing all of his profits above a return of say 6 per cent on capital and made this a universal rule for the industry. Or suppose that Reynolds' workers had insisted on their wages being increased until his profits were brought down to normal. In either case, the price of ball-point pens might well be still $12.95. But because the abnormally high profits were permitted to serve as a signal to other producers, the results were as we have described them above.

A Vital Set of Signals

The above normal profits then are not "too high" in any value sense, nor are the below normal profits "too low." They are simply signals and very, very important signals as well. In fact, the efficiency of the economy is completely dependent upon their not being silenced or modified.

Nor is this signal system costly to the consumer it serves. Abnormally high profits in some areas tend to be balanced by below normal profits in other areas and the net cost to the consumer is minimal.

If the consumer insists on recapturing the excess profits, surely he is compelled by logic and conscience to indemnify those who are getting below normal profits and the net gain would be of no immediate significance. The price of doing so, though, would be the destruction of the combined signal and incentive system of the free market – and hence his hope for a free and prosperous society.

In the same way, the worker who would demand that wages be tied to profits, that the employer share his excess profits with him, should be compelled by logic and conscience then to take wage cuts whenever his firm is making below average profits. Thus presented, few workers would have much enthusiasm for the arrangement.

In sum, then, we gain little insight into what has happened to profits by asking if some firms are making profits above or below the average. Such deviations from the average are a normal and indispensable part of the functioning of the competitive market economy.

The Concept of Market Structure

We seem now to have thrown out all meaningful ways of evaluating profits, of determining what has happened to profits. Perhaps we should give up in despair and turn our attention to some other problem.

Fortunately, there still remain certain indirect approaches to the problem that do have meaning. Let me go back to a phrase I have used several times, "the competitive market." *It is literally true that profits never can be said to be too high or too low in a competitive market.* In such a market, forces are always at work to bring profits back to the normal level and the net cost to the consumer is minimal.

But what if the markets in which the firms deal are not competitive? What then of profits?

If a given firm has a monopoly of its market, it may be able to make above-normal profits and to make them indefinitely. The signal is going out, but the other firms are prevented by the monopoly power of this one firm from answering the signal. Under these circumstances it is quite meaningful and realistic to say that profits are "too high."

Again, if the firm is selling in a competitive market, but buying its resources (for example, its labor services) from units that are