

## **Katrina and the Social Organization of Disaster Recovery: Dissolving a Theoretical Antinomy**

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### **Abstract**

This paper explores the social organization of disaster recovery, using Hurricane Katrina to supply context for the theoretical effort. That effort distinguishes two contrasting models of political economy. The conventional model treats the state as a unitary actor that stands outside the economy and uses policy instruments to shift society to some different equilibrium. The alternative model treats the state as comprised of numerous loosely connected actors that operate inside the economy, with policy measures emerging out of interaction among differing desires and beliefs held by the various participants. This alternative model presents a different understanding of state policy, both in ordinary times and in the extraordinary times represented by natural disaster.

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## **Katrina and the Social Organization of Disaster Recovery: Dissolving a Theoretical Antinomy<sup>1</sup>**

The devastation Hurricane Katrina left in 2005 when it struck the Gulf Coast of Louisiana and Mississippi is still in plain view. The present population of New Orleans is only about half its earlier size, and several parts of the city remain vacant or nearly so. Such observations as these have spawned many claims that the policy responses to Katrina have been inadequate or even obstructionist. To be sure, the observation of what seems to be a slow pace of recovery does not by itself warrant a claim of inadequacy or obstruction. Without a suitable theoretical framework to address the pace of recovery, such observations are only *post hoc* or historicist claims. The presentation of such a theoretical framework is the prime object of this paper and with Katrina used to provide context for that framework.

The core of this theoretical effort entails dissolution of a theoretical within the orthodox model of political economy. In that model, political activity is distinct from and orthogonal to economic activity. The position of the state is analogous to that of a mechanic repairing an automobile. While observers might disagree about the quality of the mechanic's work, they would agree that the mechanic is distinct from the automobile. Dissolution of this model creates an alternative model where there is interdependence and not separation between political and economic spheres of activity. This difference in models matters in two respects. First, all human action reflects the economizing efforts of participants to achieve more desired states of affairs. Second, political activity, just as economic activity, is polycentric and not

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hierarchic in nature. The earlier portions of the paper explain the theoretical distinction between these alternative orientations toward political economy; the later portions explore some of the ways in which inapt theoretical formulations can promote inapt policy responses by misdirecting analytical attention and policy effort, using recovery from Katrina to supply context.

### **Time, Theory, and Recovery from Disaster**

Any judgment that an historical episode of recovery is unduly sluggish can avoid the *post hoc*, historicist trap only by employing some theoretical framework that can render intelligible those observations. A particular episode of recovery can reasonably be described as being unduly sluggish only if it can be plausibly shown that recovery could have proceeded more swiftly under some alternative institutional arrangement, as noted in Vining's (1984) examination of the problem of detecting faultiness in economic performance. Any such theoretical framework must, moreover, start from the obvious point that recovery from any type of disaster takes time. A basketball player who suffers fractures of leg and hip from a collision with a car will not be playing basketball a month later. Several months will have to pass before recovery is complete. It is no different for societies and their recoveries from disaster. An interim observation that recovery has not yet been completed might just represent impatience on the part of the observer, though it could also indicate that something is impeding the process of disaster recovery.

It is a convenient mental exercise to assume that recovery from disaster would restore the pre-disaster configuration. This is the common approach of

exercises in comparative statics: an equilibrium configuration is shocked by disaster, and recovery denotes the time interval until the initial configuration is restored. Within this conceptual framework, recovery is purely a matter of restoration or reconstruction. This framework is easy to work with, but it might also be far off-base. Much of New Orleans is below sea level and was rendered habitable only through massive water-related projects combined with subsidy programs to promote construction. It's quite possible that Katrina has changed the perceptions of hazard that many people sense about living below sea level, in which case New Orleans would not attain its pre-Katrina configuration under even the most efficient of recovery scenarios

Recovery takes time, yes, but also there should be no presumption that recovery is capable of restoring the *status quo ante*. The basketball player with the fractured leg might recover so as to be the same player as before the accident. However, the fracture might have been so severe that he will no longer be able to move as swiftly or jump as high as before. Where the player initially averaged 20 points and 10 rebounds a game, the post-recovery level of performance might garner only eight points and four rebounds. This weaker performance would not indicate that something was amiss in the recovery process. If anything were amiss, it would have been the erroneous beliefs that were held about the player's potential for recovery.

It is quite plausible to think that Katrina has operated to shrink New Orleans's post-Katrina configuration and size. Compared with the similar experience with Hurricane Andrew in south Florida in 1992, it is surely implausible

to think that recovery in New Orleans after Katrina would entail the same degree of restoration as it entailed in south Florida after Andrew.<sup>2</sup> Someone notices some dying plants in a garden, and responds by watering them vigorously. This might bring some plants back to life, but it could also kill other plants. Which it does depends on the relevant knowledge that connects action to outcome. To base action on an inappropriate or inadequate theoretical framework could imperil or impede the growth of plants in the garden or the recovery of a city from disaster. The appropriate action to take in the garden depends upon the appropriate theoretical framework that links the health of the plants with the amount of water they receive.

What holds for plants holds for societies as well. Consider the enactment of Prohibition in the United States in 1919 (see, for instance, Thornton 1991). Prohibition did not eliminate the production and consumption of alcohol. It did bring about some modest reduction, as well as a shift to stronger, less bulky forms of alcohol. Mostly though, Prohibition induced changes in the paths and forms of commercial activity; state policy didn't prevent the use of alcohol, but rather changed how people pursued their desires for alcohol. For one thing, violence increased within society because self-help became the only means of settling commercial disputes once the possibility of judicial resolution was eliminated. Furthermore, trust was replaced by suspicion in commercial relationships; after Prohibition an offer to buy alcohol might not be genuine because a sham buyer might be trying to entrap a seller. Disrespect for law and legal authority increased

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<sup>2</sup> With respect to physical measures of intensity, Andrew and Katrina were nearly identical. With respect to estimates of damage, Katrina was about twice as destructive as Andrew.

as many public officials used Prohibition not as a means of enforcing ordinances but as a means for increasing their incomes.

Prohibition illustrates nicely the dependence of policy measures on theories about reality. One possible theory about reality circa 1919 is that most Americans wanted to stop drinking but for some reason could not do so. Any of several lines of argument could be adduced to this effect. One line might reside in a weakness of will, wherein short run desires to drink override long run desires to avoid drinking. Another line might reside in the social nature of much alcohol consumption, which could be represented as a form of prisoners' dilemma. If this kind of theoretical framework were thought to pertain to reality, Prohibition could serve as an instrument to enable most people to achieve states of affairs they genuinely thought more desirable than those in which they were trapped before Prohibition.

If this theory were correct, the period after Prohibition would have been placid and not violent. That theory did not fit reality at all well, so policy worked out strikingly differently from what that theory would have predicted. Some alternative theory about social reality is required. A key feature of that alternative theory would be that some people wanted to use state policy to modify social configurations by forcing other people to stop drinking. Those other people, however, did not go gently into that Prohibitionist night. Prohibition most certainly was not a willful policy choice by some unified state that shifted society in placid fashion to some new equilibrium. Where some political officials supported Prohibition, others opposed it and in so doing took possession of some of the

income flows generated by sales of alcohol. Prohibition cannot be rendered intelligible in terms of a model of hierarchic politics; intelligibility rather requires some model of polyarchic politics. Moreover, the experience with Prohibition during 1919-33 is being repeated in the contemporary drug wars. Policy action emanates from particular nodes within society, and its effect will depend on the types of reception it encounters: where some measures might be widely embraced, others might be resisted and even rejected. The effect of policy measures cannot be gauged independently of an appropriate theoretical framework.

### **Thinking about Political Economy: Contrasting Analytical Frameworks**

A society is a network of human activities where individual participants interact within the context of a variety of conventions and institutions. Those interactions occur within three forums: one is through commercial activity organized through market-based activity; another is through various non-commercial activities that are organized within the precincts of what is generally denoted as civil society; the third is through various offices of government. A disaster shatters this system of relationships, after which those relationships and their associated activities reappear over time as recovery proceeds. How public policy facilitates or impedes that recovery depends upon the real nature and character of that system of relationships. Public policy might impede that recovery or it might promote it. Which it does, and with what intensity, depends on the underlying nature of the social system. A society works through cooperative

interaction among all three forums, and recovery from disaster likewise requires cooperative action among all three forums. But how is that cooperation to be achieved? It is here where theoretical knowledge must come into play, for public policy that is consistent with the underlying character of the societal system will be more effective at promoting recovery than will public policy that is inconsistent with that character.

With respect to the analysis of state policy, there are two polar models for characterizing state action within a social system of political economy. These models differ both in how they explain the establishment of orderly social relationships and in how they explain the reestablishment of those relationships after some natural disaster. The orthodox or conventional model of political economy treats the state in hierarchic fashion as an agent of intervention that acts through policy to shift society from one equilibrium to another, as conveyed cogently in Persson and Tabellini (2000). The alternative model treats the state in polycentric system as a form of order that contains multiple participants who differ both in what they know and in what they desire; state policy action emerges out of interaction among interested participants, and is not adequately conceptualized as some act of choice. This model of political economy is portrayed in Ostrom (1997) and Wagner (2006). I denote the conventional model as hierarchic political economy and the alternative model as polycentric political economy.

*Hierarchic political economy.* The hierarchic orientation envisions social organization in bifurcated and additive fashion. By this, I mean that market and civil society are construed conceptually as standing apart from the actions of polity.

A good deal of social organization is secured through interaction among individuals within the precincts of market and civil society. These interactions are guided by the institutional rules or framework we denote as private property and freedom of contract. Within this institutional framework, people establish commercial enterprises, invent new products and services, and generate new types of commercial relationship and enterprise. They also participate in such components of civil society as churches, clubs, and various types of non-profit organization. With respect to market and civil society, political economy theorizes about how overall societal coordination emerges without there being any person or office who is charged with securing that coordination. In this respect, political economy is the study of self-organizing systems, in that individual action that is aimed at local and personal interests secures systemic coordination all the same.

Within this conventional, hierarchic orientation toward political economy, the state is conceptualized as a higher-level agent or organization that acts independently of and stands apart from the market and civil society. The content of state activity, moreover, is typically separated into two components along the lines described by Buchanan's (1975) distinction between the protective and productive facets of state activity. The protective facet treats the state as acting to maintain the framework of private property and freedom of contract within which the processes of market and civil society proceed; here the state enforces the rules of just conduct within which self-organization within society is secured. The productive component treats the state as acting to fill what by some theoretical models are described as holes or gaps in the network of self-organized

relationships. This is the domain of public goods theory, where the claim is advanced that markets and civil society will fail to provide such goods. States thus act to fill those holes in the social fabric that is otherwise woven through self-organized interaction within the arrangements of market and civil society.

This conceptualization entails a bifurcated or hierarchic model of social organization. That part of society denoted by market and civil society is self-organized through the competitive generation of networks of relatively local interaction. No authority plans the overall pattern of the system of social relationships, for this pattern is an emergent property of that localized interaction. The remainder of society as represented by state action, however, is organized in hierarchic planning fashion outside the precincts of market and civil society. The state is treated as acting globally and thus stands outside of and above the actions that constitute market and civil society.

Panel A of Figure 1 illustrates the hierarchic side of this theoretical antinomy. The state is portrayed as a completely connected network, which means that the state acts as a single entity. Moreover, the state stands apart from the market economy and intervenes into the market, as illustrated by the double arrow that connects state and market. The state is an organization that *acts on society* by shifting it from one equilibrium to another. Market enterprises act according to the economic theory of markets, and from its global vantage point the state acts to fill gaps in the market order.

*Polycentric political economy.* By contrast, the polycentric model of political economy asserts that there is no such locus of action that stands outside of and

above the ordinary people and their interactions which constitute market and civil society. This alternative vision locates the acts of government on the same plane of societal activity as the acts of all other people and organizations within society. Government is not an entity that acts independently of market and civil society, but rather denotes a subset of participants within the precincts of market and civil society, albeit participants who face somewhat different rules of action and interaction than other participants.

In other words, the state is an order and not an organization; moreover, it is an order in two respects. In one respect, state denotes not a unitary, goal-directed firm but rather is a portmanteau concept that denotes a large number of distinct enterprises that often are antagonistic with other state enterprises. In the other respect, state enterprises do not act independently of market and civil society but rather interact with enterprises established within the market and civil society. Society cannot be captured by simple addition across independent entities denoted by state, market, and civil society, for the resulting patterns of social activity depend significantly on the interactions among its various participants, and of the institutional framework within which that interaction occurs. State agencies and offices act within society as part of the self-organizing motion of society, and do not stand outside of society and act on it. This distinction between government as *acting within society* rather than *acting on society* leads to significant differences in the understanding of the operating features of alternative organizational patterns of political economy.

Panel B of Figure s a transformation of Panel A, where the political enterprises in Panel A have commingled with the market enterprises to produce Panel B. Moreover, political enterprises no longer speak with one voice, as it were, but operate in polycentric fashion just as do market-based enterprises. State policy now arises from multiple sources in polycentric fashion and not from a singular source in hierarchic fashion. Each triangle can be a source of policy, and those sources might sometimes conflict while at other times supporting other sources of policy. One implication of this alternative vision is that market-state relationships can play out differently in times of normalcy than in times of disaster. In particular, state actions that might be innocuous in times of normalcy might impede the restoration of normalcy after disaster.

One of the more significant differences between these contrasting models of political economy is their treatment of the *structure of social relationships*. Within the hierarchic model, social structure is irrelevant because what matters can be expressed satisfactorily in aggregate terms. The state is a unitary actor that imposes on society to generate some desired result. Within the polycentric model, however, social structure is of central importance. For one thing, state action entails structured patterns of activity, where actions by one state agency might support actions by another state agency while at the same time conflicting with actions of a third state agency. Moreover, state agencies don't act on the market in some aggregate or indiscriminate fashion, but act on particular nodes within the network of market relationships. For a polycentric political economy, social

structure is of vital significance as aggregate observations emerge in bottom-up fashion through structured patterns of interaction.

### **A Sidebar Pertaining to Ontology and Epistemology**

It should be noted that this distinction between alternative models of political economy is ontological and not epistemological. The nature of the object to be examined takes precedence logically over the procedures for generating accurate observations about that object. The two panels of Figure 1 portray two distinct objects. It is, of course, always possible to collect observations and apply them to an inaptly selected object. The experience with Prohibition illustrates what can happen when this is done. So, too, do the failures of communism, which entailed an inapt ontological vision of social reality, as explained in Roberts (1971) and amplified in Boettke (1993).

Much economic theory conceptualizes its object as if it were a marching band whose members stand in an equilibrated relationship to one another. The classical model of competitive equilibrium treats society as if it were an award-winning marching band, where all participants are in step and in tune. All the conductor-state has to do is select the tune and proscribe the direction of march. The band members then follow the conductor's instructions by maximizing their utilities in response to the announced market-clearing prices.

To be sure, economists mostly recognize that actual societies don't fully resemble the award-winning marching band that is described by the orthodox model of competitive equilibrium. Market failures are recognized to be present.

Some members of the band might get out of step or lose their place in the music they are playing. The empirical problem of political economy as it is ordinarily conceived is to reach a judgment as to just how closely the actual, observed band corresponds to the award-winning band. This question is posed in the form of empirical inquiries into the significance of various deviations from the model of perfect competition.

In contrast, the polycentric model of political economy recognizes that ontologically a society is nothing like a marching band. Accordingly, it is pointless to compare actual societies against a marching band. Societies and marching bands are both orderly social formations. However, source of order differs as between the two. The order of the band is established by the conductor; the order of the society emerges out of the un-orchestrated interactions among the participants. The challenge for public policy is not to try to make society look like an award-winning marching band, for a society in its nature is incapable of being converted into a marching band. Any effort to transform society into an image of a marching band is a recipe for disaster and tyranny, as the experience with communism illustrated. Society is rather like the motion of pedestrians along a city sidewalk, a contrast that is elaborated in Wagner (forthcoming). That motion is generally orderly but never fully. An observer would never confuse the movement of pedestrians with the movement of the members of the marching band. And only some deluded utopian theorist would think of trying to make the flow of pedestrians look like a marching band.

This ontological distinction involves recognition that the processes that generate order among the pedestrians are different from those that generate order among the band members. The problem of securing order among band members is distinct from the problem of securing order among pedestrians. Too much water can kill some plants while allowing other plants to flourish. In similar fashion, policy prescriptions that are suitable for improving the performance of a marching band may degrade the orderly movement of pedestrians; for instance, band members rehearse while rehearsal is nonsensical for pedestrians. The problem of securing good order for a marching band is a problem of planning, wherein the planner acts first and the band members respond by fitting themselves into the plan. This setting, however, does not apply to the orderly movement of pedestrians. Good order for pedestrian movement is not a problem of planning, though it might involve some state participation as in designating crosswalks; however, the contribution of the crosswalks to the orderly movement of the pedestrians will depend on how well they mesh with the desires of pedestrians. Crosswalks that don't help pedestrians accomplish what they want to accomplish will be impediments that pedestrians will ignore and avoid.

### **Coordination, Pricing, and Economic Calculation**

The economic theory of a market economy explains how the market prices that emerge through trade in the presence of private property operate to generate coordinated patterns of economic activity. To be sure, the purest form of that theory, which is characterized by the theory of general competitive equilibrium,

presents a society that looks as if it were a marching band. While that ontology mischaracterizes its object, the self-organizing qualities of private property and market prices are fundamental truths of the economic theory of markets, even though there is continuing controversy over the empirical extent to which that coordination is secured.

The economic theory of markets, however, treats only a subset of all economic relationships, those that are organized through private property and free exchange. We can use this theory to understand the coordinated network of activities through which hotels have food delivered to service their restaurants and nearby fishing boats are stocked with bait and gear. All of these activities are coordinated within a decentralized system of market-based arrangements without any person or office being in charge of the coordination. What this theory doesn't allow us to do is explain the full range of societal coordination because governmental activity is absent. In this respect, conventional political economy embraces a theoretical antinomy. On one side, market participants act on the basis of localized knowledge to generate societal patterns that no one intended directly to create. This is the spontaneous order of the market. On the other side, political entities act in unitary fashion on global knowledge to do such things as plug what are regarded as holes in the market order and to otherwise facilitate some notion of societal well-being.

Orthodox political economy embraces this theoretical antinomy by injecting the state as a conceptual imposition onto the market economy and civil society. This reflects what Resnick (1994) calls the centralized mindset, in which order is

attributed to some specific ordering agency when it really arises through some process of self-organization; it is also equivalent to justifying Prohibition by embracing a prisoners' dilemma model. Once it is recognized that state action likewise is self-organized, because there is really no option to self-organization for contemporary levels of social complexity, any more than there was genuinely an option to implement communist planning, a question arises of how such state action relates to the action organized within the precincts of market and civil society.

The alternative orientation, which is elaborated in Wagner (2007) and which was central to the classical Italian approach to public finance during roughly 1880-1940, is to treat all relationships in society as transactional in nature and governed universally by local and divided knowledge.<sup>3</sup> With respect to the preceding picture, deliveries of food and guests to the hotels in the city come over roads that are maintained by governments. The harbor may lie at the mouth of a river, so the ability of boats to move in and out depends on a government agency to keep the harbor clear of silt deposits. The conceptual challenge is how to incorporate such governmental activity into this societal portrait. Relationships among market entities are directly transactional in the exchange of service for money or other consideration. When political entities enter, the relationships are still transactional, only not directly so. The central point, however, is that the political component of social organization does not occur through social-level planning but through

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<sup>3</sup> This Italian approach has been surveyed recently in Domenicantonio Fausto (2003) and earlier in James Buchanan (1960). For an extensive treatment of Pareto in relation to this Italian tradition, see Michael McLure (2007). For a wide-ranging surveys of fiscal sociology, see Jürgen Backhaus (2004) and Juan Cainzos (2006).

networks of exchange relationships of an indirect sort. This very indirectness creates potential clashes among entities that come into contact with one another. Disaster recovery provides added scope for such possible clashing.

The orthodox ontology leads to a sequential mode of analysis, in which people write the first draft of the manuscript of social life, as it were, through their efforts in the precincts of market and civil society, and with the state subsequently revising and polishing the manuscript. The alternative, polycentric ontology leads to a coeval or simultaneous mode of analysis, in which the manuscript of social life is generated through continual interaction among participants within the precincts of market, state, and civil society. What is of particular significance is that the value of political activity can be calculated only in light of how that activity is refracted through market activity. Economic calculation requires prices as tools of calculation. But prices emerge only in the presence of alienable property. Collective property is inalienable. The internal economy of the state cannot generate prices. Prices can arise only within that part of society where property is alienable, and which is denoted as the market. Thus in a technical sense the state must act parasitically upon the market economy, as recognized both by Maffeo Pantaleoni (1911) and Joseph Schumpeter (1918).<sup>4</sup> Political entities must use market prices as calculational aids even if they make incomplete use by staying within the state as against joining the market.

Would it be worthwhile for some enterprise to supply trailers to provide temporary housing while reconstruction is taking place? A market-based firm would make this calculation of cost and gain based on predictions about the effect

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<sup>4</sup> For some elaboration of this parasitical theme, see Wagner (1997).

of such choices on the firm's net worth. A political enterprise faces the same problem of calculation in making such a choice. However, the inalienability of ownership means that the various dimensions of net worth cannot be reduced to some scalar magnitude but appear only as a vector of characteristics, as explained in Auteri and Wagner (2007). In this respect, a FEMA (Federal Emergency Management Agency) official might well conclude that his administrative headache from managing temporary trailers might exceed whatever relevant dimension of gain he might sense, even though the owner of a profit-seeking enterprise might conclude differently because the increase in enterprise value was judged to more than offset the added administrative cost.

The parasitical character of political catallaxy can be illustrated with reference to the social organization of rebuilding after such a disaster as Katrina. Not all plans for rebuilding can be enacted at once. Some plans will attain precedence over other plans. To provide a simple illustration, suppose 100 people have plans for reconstruction projects, while there are ten construction firms. To further simplify the illustration, assume each reconstruction project requires equal time to complete and that all construction firms are equally proficient. What results is a sequential situation where reconstruction proceeds ten jobs at a time until all 100 projects have been completed.

But what will be the order of reconstruction? The theory of markets gives a simple answer: those projects that owners value more highly will be pursued before those that the owners value less highly. Within the market framework of economic calculation, moreover, higher valued projects will be those where owners

project higher net present values. Therefore, a market economy will promote an orderly pattern of reconstruction where projects with higher net present value take precedence over projects with lower net present value, as based on the expectations of owners. Market prices create a simple metric to guide reconstruction.

The market process also can accommodate sudden changes in valuation despite nominal contractual commitments to the contrary. Someone might have obtained the services of a construction firm prior to such a disaster as Katrina, and so would have contractual entitlement to that firm after Katrina. Yet some alternative project might be valued more highly by its owner. The prior contract does not compel the less valued project to be undertaken first. It only alters some of the terms and conditions of contractual renegotiation. If the project is worth more to the new bidder than to the initial bidder, scope exists for the new bidder to get the old bidder to agree to change places in the construction queue.

In other words, market institutions provide an orderly process for organizing rebuilding, wherein projects that are valued more highly by their owners will be undertaken before projects that are valued less highly. Furthermore, all market participants will agree with this relative ranking of projects by value, because a disagreement can be tested by offering to pay more to move into an earlier position in the queue. Someone who fails to offer more to secure an earlier position is thus tacitly agreeing with the market-generated ranking of value.

Where do governments fit into this process of rebuilding? The pure theory of a market economy adopts the social ontology conveyed by Panel A of Figure 1.

Panel B conveys different insight into the process of rebuilding. There, it can be seen that state presence raises two types of issue. One type concerns the place of political enterprises within the overall queue of reconstruction projects. The other type concerns the impact that state policy action might have on the sequence and timing of market-based reconstruction; political agencies might alter such reconstruction through regulatory actions.

With respect to the first type of issue, state projects must compete against market-based entities for position in the queue. Of the 100 reconstruction projects, suppose 30 belong to state entities. Those entities must bid against market entities for positions in the queue. In doing so, political entities must necessarily engage in forms of economic calculation, though only parasitically and not directly. In offering a higher payment to advance in the queue, a market-based firm judges that the value added to the enterprise by earlier completion exceeds the added cost. A political enterprise is making the same form of judgment, only cost takes on a different form because the inalienability of ownership means that the various elements of cost cannot be reduced to a scalar measure of net present value. A political official likewise judges by comparing costs and gains, only these take the form of a vector of characteristics whose components can be valued differently by different public officials. Where some public officials might place high value on expressions of desire for temporary housing by potential residents, other officials might place higher value on their belief that trailers constitute blight on the landscape.

All choices, whether made by politically-based or market-based officials, reflects judgments about the value of options. It would certainly be normal to expect people to differ in how they appraise those options. Nonetheless, the alienability of ownership tends to create a focal point on enterprise value that is not present for political enterprises. Hence, choices by public officials reflect more of a personal calculation of cost and gain, in that they will tend to weight characteristics by personal valuations rather than by market valuations. With respect to positions in the queue for reconstruction, an increase in the bid offered by political agencies will be paid by taxpayers as against lowering the net worth of managers of the political enterprise. This line of analysis would generate some presumption that political enterprises would figure more prominently in the queue of reconstruction activity, due to their different economic position. Thus government would tend to rebuild more rapidly than market-based enterprises because of the different arrangements for economic calculation.

With regard to the second type of issue, governments can also influence the pattern of market-based reconstruction. Within the pure market economy, the order and pace of rebuilding is determined by the willingness of owners to bid for construction firms. State activity, however, can modify this process, both by changing the order within the queue and by changing the pace of recovery. The pure market form of recovery could entail state support for general relief payments. These would be payments without strings to support reconstruction. Within this framework, it would be fine if one person used some of that relief payment to buy a higher place in the queue of reconstruction, while someone else acted in the

opposite manner. The state relief payments would not interfere with the market process but rather would support it.

In actuality, state activity acted to change the order of reconstruction and to slow its pace. For instance, FEMA refused to allow temporary housing in trailers and in so doing surely slowed the pace of reconstruction (Sobel and Leeson 2007). A market based firm would have allowed such temporary housing, provided only that it added to the firm's net present value. In rejecting temporary housing, FEMA was necessarily engaging in economic calculation, only of a different form due to FEMA's position within the parasitical part of the social ecology where ownership is inalienable.

### **Markets and the Constitution of State Policy**

Recognition that some state actions can complement the market economy while others can degrade it brings to mind the theory of *ordnungstheorie*, literally translated as "order theory" but not a genuinely translatable term. This theory was a version of what has since become known as constitutional political economy (Vanberg 1988) Buchanan (1990), in that it operated with a bi-level analytical framework. The constitutional level concerned the establishment and maintenance of rules of just conduct; the operational or action level concerned the patterns of human activity and organization that emerged through interaction among people when those interactions were constrained and shaped by the framework of constitutive rules.

One of the significant constitutional features of this analytical framework is expressed by the principle of *market conformability* (Eucken 1952).<sup>5</sup> This principle did not exclude government participation in economic activity. Rather it held such participation to a standard of market conformability. This standard is a constitutional principle which asserts that state action should be consistent with the constitutive principles of a market economy, and most certainly not violate those constitutive principles. This framework allows plenty of scope for state action in response to natural disasters, provided only that it does not undermine or sabotage the operation of the market economy.

The meaning of market conformability is perhaps best seen by an illustration Eucken used, the distinction between tariffs and quotas. Within the standard theory of international trade there is no distinction. Whatever reduction in imports a tariff can achieve can also be achieved by a quota. A 20 percent tariff on silk blouses might reduce imports by one million per year; say from three million to two million. If so, the same reduction could be achieved by imposing a quota of two million. This orthodox conclusion, however, is incomplete because the quota sabotages the operation of market processes while the tariff does not, at least so long as the tariff doesn't reach heights that promote smuggling along with police-style reactions to that smuggling. With the tariff domestic buyers can still choose the foreign suppliers they prefer, and the pattern of reduction in imports is worked out through interaction among the buyers and sellers of silk blouses.

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<sup>5</sup> For a perceptive comparative treatment of Eucken and Max Weber, see Rath (1998). For a collection of essays on Eucken-like themes, see Leipold and Pies (2000). For a textbook statement of this theme in English, see Kaspar and Streit (1998).

In contrast, the quota destroys the ability to buyers and sellers to work out their preferred pattern of import reduction. It does this by making the pattern of reduction a matter of state action. With a quota, some state officer acquires the power to determine which sellers are able to import blouses and how many. This power, in turn, expands the scope for venality in politics. Quotas require licenses to import, and the number of licenses awarded will be less than the number that suppliers will request. Some non-market method of selection will replace the market-based method of selection. Suppliers will compete among themselves for quota allotments, and in doing so will engage in various efforts at domestic lobbying.

When disaster relief takes the form of general cash vouchers, state policy is market conformable. State policy is supporting the self-organizing capability of market arrangements to promote recovery. In contrast, programs that impose requirements of state planning, as by stipulating some order of precedence or by specifying standards of construction, are not market-conformable. Such policies both distort and impede the self-organizing capabilities of market arrangements, both distorting and slowing recovery.

This constitutional approach to state policy was articulated to deal with a tension that arises once it is recognized that policy measures emerge within society and are not impositions from outside society. That tension concerns how to maintain an open market order in the face of possibly strong pressures to bias that order through closures of various forms. The requirement of market conformability was one approach to keeping this tension in reasonable check. Within this setting,

state activity generally plays a supporting and not a leading role in the economic organization of society. Supporting roles are important for any drama, of course, but they are supporting roles all the same. Stated differently, the politics of bureaucracy arises in response to market activity, as against being the generative source of market activity (Mises 1944) (Tullock 1967). Market relationships are the primary source of information about valuation, and with the state occupying a position in the background and not in the foreground.

If Panel B of Figure 1 were presented in 3-D fashion, the state triangles would be shown in the background and the market circles in the foreground. This is the normal societal arrangement in market-based societies, and this arrangement stands in stark contrast to that of the communist societies of recent history. It is, however, an understandable part of human nature for those in supporting roles to desire more prominent roles. Disasters can provide such opportunity. This can be seen by elaborating on the geography associated with Panel B, which shows only a local geography.

It's conceivable that the relevant society is locally captured by that local geography, perhaps as might be illustrated by a small island society. More common, however, is that the devastated territory is but a small part of a larger territory. In this setting there will typically be significant differences geographically between market-based enterprises and politically-based enterprises. An extreme form of this difference would be for all market-based enterprises to be local, while all political enterprises were national with local branches. A disaster would thus move market-based enterprises farther away from their normal operating

circumstances than politically-based enterprises. Reality, of course is not quite so stark: some market enterprises are branches of national enterprises while some political enterprises are local in nature. Nonetheless, the extreme model captures a significant geographical difference in the institutional impact of disaster.

While a local Wal-Mart can be replenished from Wal-Mart's in unaffected areas, there will be many local commercial operations that have no such outside sources of support to facilitate the restoration of normalcy. Hence, disaster can provide an opportunity for political officials to occupy more of the foreground in the aftermath of disaster because market enterprises have become less robust relative to political enterprises. What matters, then, is the means by which that foreground is occupied. A requirement of market-conformability would limit what could be done while occupying the foreground. Without such a limit, the normal tendency created by the necessarily parasitical position of political action is to engage in planning-types of activities. Hence, political offices would engage in such things as trying to determine the order of construction, making determinations of both when and where. In contrast, the market procedure would allow the affected parties to work out these matters among themselves.

It would be market conformable to give unconditional cash grants based upon quick estimates of damage. The extent to which such grants go to rebuilding houses or rebuilding factories would be worked out by market participants and would not be an object of public policy. Once public policy gets involved in the allocative details of such matters, state planning intrudes on markets, and with it

necessarily comes corruption (Leeson and Sobel 2006), just as a quota necessarily promotes venality in comparison with an equivalent tariff.

### **Peroration: Enterprise Zones and Disaster Recovery**

Within a market-based framework, we would normally expect to find a quickening of the pace of activity in response to such disasters as Katrina. People would do such things as work longer hours and postpone vacations because the restoration of commercial capability has become relatively more valuable. But such market based restoration also depends on public activity of various forms. Under normal times within an on-going and well-working society, clashes among market and political enterprises would seem generally to be relatively minor nuisances, perhaps as represented by Adam Smith's remark that "there is a deal of ruin in a nation." After disaster, however, political entities to a significant extent confront weakened market entities. The danger that comes from this weakness is that society can become more of a planned-type society that acquires some of the infirmities exhibited by the socialist regimes of the recent past. This change comes about because state entities encounter less resistance in occupying the societal foreground than they would encounter in normal times.

Enterprise Zones were originally a British idea that started to gain support in the US around 1980 (Butler 1980). The initial idea was that depressed urban areas could be revitalized by granting some period of relief from regulations and taxes. Enterprise zones now operate within most American states as well as at the federal

level, though are by no means limited to depressed urban areas.<sup>6</sup> While it could be argued that enterprise zones are forms of subsidy that work by promoting some relocation of economic activity, the idea would nonetheless seem to have some potential merit as a market conformable approach to disaster recovery, in contrast to the present form of planning for recovery.

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<sup>6</sup> For a useful link see [<http://www.floridaenterprisezones.com>].

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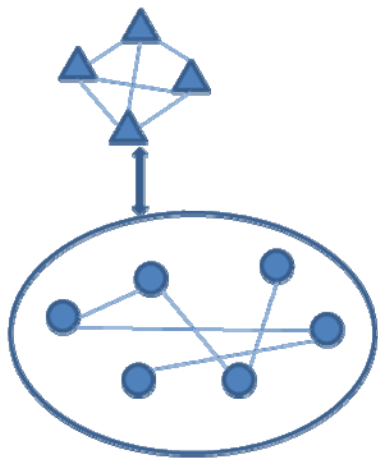
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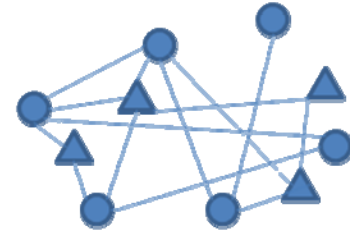
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A: Hierarchic Political Economy



B: Polycentric Political Economy

- Market Enterprises
- ▲ Political Enterprises

Figure 1: Alternative Models of Political Economy