

Economics 881
Theory of the Market Process II
Spring Semester 2017
Tuesdays 1630-1910
Music & Theater Bldg. 1002

Professor Richard E. Wagner
Office: Mason Hall D115
Hours: Tuesday afternoons
Email: rwagner@gmu.edu
Home: mason.gmu.edu/~rwagner

This course explores some of the material you will have studied in your first-year theory classes, only it does so by examining that material through a different analytical window. Rather than theorizing in terms of conditions or states of equilibrium, it theorizes in terms of *non-equilibrium processes* of continual change or development. These alternative analytical orientations are not antagonistic; they are non-commensurable. They can both be employed, only not at the same instant.

Equilibrium theory posits a set of mutually consistent choices and seeks to give a coherent explanation in terms of contemporaneous data. This type of theory is illustrated nicely by the various proofs of the existence of a competitive equilibrium. It seeks to explain observed data through the method of comparative statics, with this method being “interpreted” as portraying history through its comparison of alternative states observed at t_1 and t_2 .

By contrast, *non-equilibrium theory* take the interval $[t_1-t_2]$ as comprising the relevant unit of observation. This difference in analytical orientation brings in its analytical train several differences in the construction of economic theories. Theory pertains directly to history, as against being interpreted as history. Economic theory pertains to movies, as it were, and not to snapshots taken at different instants, and with differences in the snapshots interpreted as history.

To recur to an image I have used on several occasions, the analytical object of non-equilibrium theorizing is to explain the orderliness of a crowd of pedestrians leaving a stadium, and not that of a parade. The analytical method for doing this is the plausible reasoning of emergent dynamics (which has nothing to do with differential equations), and not the demonstrative reasoning of comparative statics. In other words, we do not start with data to be explained by comparative statics, because the relevant data emerge through economic interaction among market participants. So-called data are the objects of theoretical explanation, and not the starting point for explanation.

Where equilibrium theory inserts exogenous shocks into a situation to generate change, non-equilibrium theory treats change as an ordinary and emergent feature of interaction among economizing agents and their plans. For a process-oriented social theory, exogenous shocks to a social system are rare, perhaps as illustrated by a meteor strike. What are described as exogenous shocks within the confines of equilibrium theory are manifestations of the

continual clashing of plans that are a feature of open-ended processes of creative interaction.

Equilibrium theory focusses on resource allocations and reduces economics to acts of choice. Non-equilibrium theory focusses on processes of human interaction and their governance, with resource allocations being emergent by-products of those processes. Furthermore, non-equilibrium theory operates through complex ecologies of networks, in contrast to the field-based simplicity that characterizes equilibrium theories. I should also note that I do not regard the two types of theorizing as entailing a choice between right and wrong. To the contrary, I regard them as entailing a distinction between the foreground and the background of a theorist's mind.

Course Format

The class will meet 14 Tuesdays during the semester; starting on 24 January and ending on 2 May. There will also be no class on 14 March, as this is during the week of spring break. The first two sessions will be devoted to methodological preliminaries. The remaining 12 sessions will be divided into three units of four sessions each, described as micro, meso, and macro.

The course will proceed in a lecture-discussion format. How much lecture and how much discussion is to be determined. I don't work with detailed scripts, as I like classes to have improvisational character. How the semester unfolds will be an emergent quality of classroom interaction.

While this course takes an emergent dynamic pass through some of the material covered in your first-year theory classes, the course's emphasis is on the social and not the individual level. The relationship of individuals to society is one of parts-to-whole. This relationship is not one of addition, because the whole of something entails greater phenomenal complexity than any of the parts out of which that whole is constituted. You cannot get to society through a simple summation over individuals, once you recognize that structured patterns of relationships have significant analytical work to do, and with those structured patterns having arisen through prior interaction.

I regard advanced graduate courses as venues for exploring new lines of thinking where we are looking for ways to articulate what has not yet been articulated, and not as venues for explaining what is widely regarded as settled knowledge. Like Shakespeare in *Tempest*, I embrace the idea that the past is merely prologue. You need to survey what is regarded as settled, but doing this serves only to provide a point of departure for scholarly work. Our primary course objective is to create new text; mastering old text is but a secondary by-product. Hence my classroom approach is one of "joint inquiry" and not "mental transfer" from me to you.

You will gain further insight into this distinction if you look at the earlier part of my essay “James Buchanan and Me: Reminiscing about a 50-Year Association,” which was published in 2013 in the *Journal of Public Finance and Public Choice* and is available on my SSRN page.

While it is important to read widely, I don’t supply lengthy reading lists though I will suggest enough material to keep you busy during the semester. I also hope you read other materials as well and, more significantly, mix those readings with your imaginations to generate new insights that might lead to interesting analytical places. In my judgment, students become too accustomed to reading published work with an eye to taking exams. I suggest that you cultivate the practice of reading with an eye that continually looks for new ideas that you can articulate, as against absorbing old ideas that you can recollect.

Course Substance

Two books and four papers will serve as textual material for the course, with additional references to be mentioned during the semester. The books I have ordered, available in paperback, are:

- Jason Potts, *The New Evolutionary Microeconomics*, and
- Richard E. Wagner, *Mind, Society, and Human Action*.

The four papers that I also regard as textual material are:

◦ Oscar Morgenstern, “Thirteen Critical Points in Contemporary Economic Theory,” *Journal of Economic Literature* 10 (1972): 1163-89. While I don’t find all these 13 points to be so critical, I think some of them are. Furthermore, Morgenstern was a thoroughgoing Austrian theorist, despite thinking economic theories should be reduced to axioms. Furthermore, each of you will have three short writing assignments (in addition to a longer assignment) where your task will be to write something patterned after one of Morgenstern’s points.

◦ Rosolino Candela and Richard E. Wagner, “Pareto’s Theory of Action: An Alternative to Behavioral Economics,” available on my SSRN page and forthcoming in *Il Pensiero Economico*. While the course’s object of analysis is society, that object is approached through individual action. This paper provides some different insights into conceptualizing individual action.

◦ Jason Potts and Kathleen Morrison, “Meso Comes to Markets,” *Journal of Economic Behavior and Organization* 63 (2007): 307-12. In place of the standard micro-macro dichotomy, Potts and Morrison insert a meso level which contains organizations and institutions. I think their analytical insertion opens into fruitful analytical possibilities.

◦ Richard E. Wagner, “A Macro Economy as an Ecology of Plans,” *Journal of Economic Behavior and Organization* 82: 433-44. This paper takes an alternative, network-based tack toward the material of orthodox macro theory. Interaction among agents generates structure and data, and these in turn influence the actions of agents. Within the theoretical framework this course pursues, the micro-macro relationship is interactive and emergent and not independent and additive.

Course Structure

Part I (two sessions) Methodological Preliminaries

- Potts, Chs. 1, 2.
- Wagner, Chs. 1, 2.
- Morgenstern (1972).

Part II (four sessions) Micro Theory: Human Action, and the Emergence of Structure

- Potts, Chs. 5, 7.
- Wagner, Chs. 3, 4.
- Candela and Wagner (forthcoming).

Part III (four sessions) Meso Theory: Emergent Structure and the Shaping of Human Action

- Potts, Ch. 6.
- Wagner, Chs. 5, 6.
- Potts and Morrison (2007).

Part IV (four sessions) Macro Theory: Systems Theory and Parts-to-Whole Relationships

- Potts, Chs. 3, 4, 8.
- Wagner, Chs. 7, 8.
- Wagner (2012).

Your Work and My Appraisal of it (Grading)

Each of you will submit three short essays. Each of these essays will be patterned after one of Morgenstern's (1972) points, with each of these essays due the final session of the relevant class unit. These should be limited to five

pages of double-spaced text, in addition to including suitable references. You will also present your essays orally during that final session. Each of these essays will count for 20 percent of your course grade.

You will also submit a research paper that will count for 30 percent of your course grade. These must be prepared in standard manuscript style (double spaced) and must not exceed 15 pages, excluding references. These are due by 1630 on 16 May, which is the time that is assigned for our final exam, though I will not give a final exam. You can submit your papers electronically.

The remaining 10 percent of your course grade will be based on my evaluation of your contributions to classroom discussions and presentations throughout the semester.

My perspective in evaluating your papers is that I am editing a book (or special issue of a journal, say the *Review of Austrian Economics*) devoted to creating a modern compilation of critical points for economic theory, written from a process-theoretic orientation. I will send you editorial reports on your papers which explain the basis for my evaluations.

I evaluate all your written work by what I judge to be its publishable potential, recognizing that judging that potential is different for five-page essays than for 15-page papers. In either case, a grade of **A** signifies that I think what I have read points in a publishable direction if carried to what I judge to be its destination. A grade of **B** indicates that while you have convinced me that you show good understanding of your material, you have not shown me that you are headed in a publishable direction. A grade of **C** means that I detect some significant holes in your knowledge and understanding of your material. A grade of **F** is a “none of the above” judgment that I hope I don’t have to make. (Various pluses and minuses are also possible grades, and I think that by extrapolation you can attach reasonable meaning to those grades.)

Please note that my interest in the work we do this semester is in helping you to acquire the habits and practices of success. I have no interest in failure. For this reason, I do not accept late work nor do I give incomplete grades. Tardy work and incomplete grades are facets of a repertoire of failure which I will not countenance. If you are scheduled to give a paper at a conference but find you aren’t ready to do so, you won’t be given an incomplete and have the conference rescheduled. So don’t ask for incompletes or turn in late work.

Three Quotations to End the Syllabus on an Advisory Note

First, from Samuel Johnson comes this recognition that fits well with Joseph Schumpeter’s statement that theorizing starts with a pre-analytical cognitive vision that we try to articulate, with varying degrees of success:

Every man has often found himself deficient in the power of expression, big with ideas which he could not utter, and unable to impress upon his reader the image existing in his own mind.

Dr. Johnson describes a situation with which we all have to wrestle in trying to render our intuitive hunches intelligible to others, as well as to ourselves.

Second, from Albert Einstein via Roger Koppl comes this sage counsel:

If we knew what it was we were looking for, we wouldn't call it research, would we?

Research doesn't always yield happy endings. We write many more pages than we publish. The process of writing triggers thoughts that often lead us to recognize that where we thought we were heading isn't such a desirable place after all. So we change our angle of attack. Dead ends, cul-de-sacs, and just plain old frustration are part of the research process, and you must learn to persist in the face of such setbacks.

Third, during my student days I came across this statement from George Shackle's *Uncertainty in Economics* about what it takes to be a good economist (to be sure, Shackle wrote this in the 1950s, when few women studied economics):

To be a complete economist, a man need only be a mathematician, a philosopher, a psychologist, an anthropologist, a historian, a geographer, and a student of politics; a master of prose exposition; and a man of the world with experience of practical business and finance, an understanding of the problems of administration, and a good knowledge of four or five languages. All this is, of course, in addition to familiarity with the economic literature itself.

As for the type of person best suited to the study of economics, Shackle later suggests it is

. . . the outstanding intellectual all-rounder with some leaning towards the arts rather than the natural science side. The person who finds mathematics fascinating without, perhaps, marching through the school course with that instinctive and professional certainty that would mark him as an out-and-out mathematician; who betrays a connoisseurship of words and a delight in language, a gift for expression in English and a sufficient pleasure in the classical languages to awaken thoughts of scholarships, without really promising to become a Porson's prizeman; who can find in

every chapter of the history book the universal and eternal problems of man's dependence on his fellow-men side by side with his rivalry and conflict with them, and can see with the historian's eye the age-long empirical struggle to reconcile self-interest and enlightened compassion; who delights in maps and finds them, perhaps, more interesting than test tubes—this is the potential real economist.

What Shackle describes is more on the order of a lifetime project than something to be accomplished during your few short years as students. But you will have post-student life ahead of you, and Shackle's statement is a lovely summary of an orientation toward economic theory that would allow it to occupy the pivotal position within the humane studies that I think it should occupy.