

Value and Exchange: Two Windows for Economic Theorizing

Richard E. Wagner

Department of Economics, 3G4
George Mason University
Fairfax, VA 22030 USA

Abstract

This essay introduces a symposium on value and exchange as alternative organizing concepts for the pursuit of economic theorizing. These concepts pertain to two distinct conceptual windows through which economic phenomena can be examined. The immediate inspiration for this symposium was Meir Kohn's (2004) articulation of the distinction, a distinction that in turn was central to James Buchanan's (1964) articulation. Furthermore, this distinction is central to the divergent orientations toward economic theorizing that were set forth in the early 1870s by Carl Menger and Léon Walras.

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The following symposium was inspired by the publication of Meir Kohn's (2004) distinction between value and exchange as distinct research programs for the organization of economic analysis. The value paradigm characterizes economic observations as equilibrium observations of maximizing action. In contrast, the exchange paradigm characterizes economic observations as processes of development, wherein the world we experience is generated through interaction among those who participate in it. Kohn also notes that many scholars have tried to straddle the two programs through the employment of hybrid theorization, but concludes that this hybrid is indigestible.

As Kohn notes, his claim hearkens back to James Buchanan's (1964) argument that the object that economists should study is not well represented by problems of maximization, and is better represented by problems of exchange and conflict. The differences in theoretical vision articulated by Buchanan and Kohn are reminiscent of the differences in vision articulated by Léon Walras and Carl Menger. What Kohn describes as the value paradigm was given cogent articulation by Walras, and the subsequent post-Walrasian development offered a theoretical window through which all economic phenomena were envisioned as equilibrium states with maximizing agents.

In sharp contrast to Walras, Menger examined economic phenomena through a different window through which the observations were of on-going processes of development, and where the individual agents (or at least a good number of them) were adventuresome explorers in combinatorial space. The

Walrasian and Mengerian visions of economic phenomena point in opposite directions, much as do the two parabolas X^2 and $-X^2$ once you get away from their neighborhood of common origin. These divergent directions, moreover, were recognized by Menger even if not, perhaps, by Walras. In one letter to Walras, where Menger responded to Walras's argument that they were kindred spirits analytically speaking, Menger stated: "There is indeed a resemblance between us. There is an analogy of concepts on certain points but not on the deeper questions."¹ The deeper questions to which Menger referred entail the use of two distinct windows for conceptualizing the object that economists examine.

Windows for Apprehending the Object of Economic inquiry

Economists study the object denoted as economy. Just how this object is conceptualized, however, requires preceding theoretical articulation. A chair or a worm can be apprehended directly by the observer, but an economy cannot. It can be apprehended only within or through some theoretical framework. The Mengerian, or exchange in Kohn's formulation, framework for doing this differs markedly from the Walrasian framework, or value in Kohn's formulation. The object's appearance and qualities depend on the window through which it is examined. An economy is not directly apprehensible, but rather is constructed through a preceding act of conceptual inquiry.

Economic models typically postulate closed and not open concepts. Closure brings tractability, but only by rendering many phenomena unintelligible.

An equilibrium system requires closed concepts, so the creative injection of novelty can be accounted for only as exogenous shocks or, equivalently, as stochastically predictable events. Within this closed framework, people don't truly make choices and have adventures. They face a list of enumerated options in the presence of a well-defined utility function, and the outcome is inexorable, similar to involuntary reflexes. It is interesting in this regard to reflect upon the dislike most economists express for models that have multiple equilibria.

An alternative that comes into play when working with open concepts is to recognize that multiple equilibria speak not to structure but to process. We stand here today, and tomorrow will emerge through interaction among the various choices we make. In the presence of closed concepts, people will make the same choice each time and tomorrow will be the same tomorrow each time. This is what equilibrium signifies, and a model with multiple equilibria is an irritant for such a conceptual presumption. With open concepts, however, people face genuine choices, in which case they could make different choices if it would have been possible to relive the scene multiple times. With everyone in the same position, multiple histories could have emerged. There are thus several tomorrows that could emerge out of today, depending on the particular choices people make and the resultant interactions that are set in motion. The social world can be rendered intelligible without being genuinely predictable.

This distinction between open and closed concepts is directly relevant for the treatment of coordination in economic theory. A focus on closed concepts leads to coordination being explained through some hypothesized equilibrium. A

parade illustrates the use of closed concepts to explain coordination. A parade is a coordinated movement of people, and with the coordination achieved by a parade marshal. Things can sometimes go wrong in a parade, and these would represent exogenous shocks to the marshal's plan. For instance, a horse might drop some dung that was neither cleared nor observed by a following trumpet player. On planting his left foot in the dung while executing a right turn, the trumpeter slips and falls, sending some of the other band members collapsing into a heap. The parade is delayed momentarily and then continues, the exogenous shock absorbed into an error term that accounts for the above-average duration of that particular parade.

Alternatively, consider the systematic movement of people leaving a stadium or theater. This movement is likewise coordinated, only it is not coordinated by some parade marshal. With the parade, every participant's location at each moment during the parade will be pre-determined by the parade marshal, save only for disruptions caused by exogenous events. With the spectators leaving the stadium or theater, no such pre-determination is present even though the participants arrive at their desired destinations pretty much as they anticipated. It would be a metaphorical stretch to account for this outcome "as if" it were orchestrated by a parade marshal. It has none of those features of orchestration, and to invoke "as if" is to parade ignorance as knowledge. But this is where working with closed concepts leads. The alternative is to work with open concepts. In this case, coordination is rendered intelligible through some conjunction of intentional action by participants as mediated by such things as

conventions regarding courtesy and police barricades, among other things. Occasionally a fight will break out and every so often someone will fall and get trampled a bit. These are intelligible events in the aggregate, but they are not the products of a pre-coordinated parade. They are rather emergent phenomena that arise out of interaction.

Theorizing about people is different from theorizing about termites or trees, because with respect to people we live inside the objects we theorize about. For termites or trees there is no option but to theorize from the outside looking in, and the only test of reasonable theorizing must be some measure of the coherence between theoretical predictions and observed outcomes. In contrast, the humane sciences can also call upon theorizing from the inside looking out. Indeed, much social theorizing can only be done from the inside looking out. The claim that people seek to be effective in applying means to the pursuit of ends is not a conclusion of outside observation and inference, but rather is a feature of our self-awareness. To be sure, theorizing from the inside looking out is an instrument that must be used with care, for a danger that comes with it is that it can turn into a battle among contending prejudices and intuitions. Yet there are many statements about successful human action that can be rendered intelligible in terms of a pure logic of choice because such a logic maps directly into a logic of successful conduct—and we know from the inside that people do not seek to fail at what they try.

Economic models are vehicle for conveying stories. For models that employ closed concepts, those stories must be conveyed in the passive voice.

People don't do anything in those stories, for they are simply whipped into line by some utility function and market mechanism. Markets clear and people are naturally forced to optimize as their utility functions dictate. What is portrayed is a society without life or action. The open concept alternative allows stories to be conveyed in the active voice. People actually do things, and with market phenomena of various types emerging out of those actions and interactions. People choose one course of action while rejecting others. In the process they participate in generating the world they experience. To be sure, ex post from the outside looking in any choice can be portrayed through a closed formulation of utility maximization. But that construction isn't recognizable to participants, for from an inside position looking outward people face and make choices, and it is the interaction among such choices that generates the social world we experience.

Process vs. Structure: Distinguishing Foreground from Background

Equilibrium is a sensible even if perhaps peculiar notion to apply to an individual, for it merely signifies coherence in a person's planned pattern of conduct regarding the employment of means in the pursuit of ends. It is an entirely different matter to apply notions of equilibrium to societies. A society is not an acting creature from which we would expect coherence, but rather is an arena within which acting creatures interact. It's true that societal processes unfold in generally orderly fashion, though not always and never completely. People seek to be successful in action, and have over the years developed

various customs and conventions that facilitate such success. While there is a good deal of permanence in social life, particularly over relatively short periods of time, there is also a good amount of turbulence. The challenge for social theorizing is to render intelligible social life and social patterns in such a setting of continual and turbulent development.

Any analytical framework that distinguishes between universal principles and particular instances of those principles that can take on multiple guises is one that will involve both process and structure. Structure speaks to the universally recognizable features of the actions, both inventive and repetitive, that occur within society. It is possible simultaneously to embrace the recognition in Ecclesiastes that there is nothing new under the sun and the assertion of Heraclites that you can't step into the same river twice. Both process and structure (or equilibrium) provide useful analytical orientation, but there is a question of which occupies the foreground. In the view through the Mengerian window, the foreground is occupied by process.

The primacy of process over structure is conveyed nicely by considering a galloping horse.² Some people looking at snapshots will see all four of the horse's hoofs to be off the ground. Taken as an equilibrium observation, it would have to be concluded that a horse can fly, or at least levitate.³ The snapshot of the flying horse ignores the underlying causal process through which that observation emerged. That process-oriented observation, however, is an insight that appears through the Mengerian window and is obscured when it is viewed through the Walrasian window.

Demsetz and Property Rights in Labrador: Variations on a Theme

Harold Demsetz (1967) advanced his well known claim that private ownership replaces common ownership when the change is economically efficient. Demsetz illustrated his claim with respect to changes in the ownership over animals among Indians living in Labrador. Demsetz's claim, moreover, can be read into Carl Menger's formulation of economizing action. The main story line is straightforward. As trade in furs expanded, quarrels arose among the Indians as they had to travel longer distances and stay away longer to capture their desired game. By establishing ownership over particular beaver huts, quarrels would be reduced and incentives would be provided to refrain from harvesting overly small and young beavers.

This is a nice story to tell, and it is rendered in comparative static fashion, pretty much in the same fashion as all such analyses of institutional change are rendered.⁴ These efforts seek to portray change through successive looks through the Walrasian window. One view shows fur-bearing animals subject to common ownership. The subsequent view shows those animals subject to private ownership.⁵ Both views are presumed to pertain to equilibrated relationships, and yet the views they present differ. That difference must be attributed to some exogenous shock that disturbed the former equilibrium and led to its replacement by the second equilibrium. The analytical trick or challenge is to locate something that can account for this shock. Usually the shock is

attributed to technology. In the case of Labrador, it was an expansion in the fur trade which transformed an abundant supply of animals into a scarce supply.

One notable feature of this approach to the presentation of historical development is that no one is really doing anything in any active voice kind of way. People respond to circumstances thrust upon them, but they don't generate those circumstances. When viewed through the Mengerian window, the same setting would surely play out differently in a number of ways. Those differences, moreover, would in various ways speak to the creation of insight into the process by which this transformation occurred. Any such process would start with felt uneasiness, for a complaint is just an expression of felt uneasiness. Beaver are harder to find, and quarrels among hunters are more common, as are such incidents as broken noses and crushed skulls.

What transpires in the society so described? What kinds of history might have transpired if we were to examine a series of parallel worlds? It is certainly easy enough to imagine those complaints brought before a tribal council, and with some form of property rights to animals being parceled out. Yet it's also easy to imagine other responses to the same initial source of uneasiness and complaint. For one thing, and closest to what Demsetz describes, licenses could have been issued to particular locations, which is a cousin to private property. Alternatively, the tribal council might have tried to limit the harvest of beaver, perhaps by imposing some kind of tax or by imposing quantitative limits, as do fish and game regulations today. The Council might even have undertaken some effort to fashion tastes differently, perhaps by holding opossum festivals to

promote the replacement of beaver by opossum in stimulating the sartorial and culinary desires of tribal members.

Furthermore, it's unlikely that once this issue had been resolved, life would proceed in all other respects just as it had before. The complaint over animals set in motion various processes by which people develop new activities and acquire new capacities. Those new activities and capacities will not generally be forgotten just because people are no longer fighting over beaver. They will surely be put to new uses, promoting emergent changes throughout the society. This, anyway, is how the history would look through the Mengerian window.

The Essays to Follow

The authors of the symposium's essays were not asked explicitly to comment on Kohn's paper. Indeed, they were asked explicitly not to do so. Rather, they were asked to use Kohn's essay as a point of entry for exploring themes of interest to them that happened also to relate generally and broadly to Kohn's thematic regarding value and exchange as providing alternative orientations for economic theorizing.

Robert Axtell notes that neoclassical theory contains a set of mutually supporting presumptions, which together constitute what he describes as the neoclassical sweet spot. These presumptions are that agents are rational and homogenous, that agents don't interact with one another but only act on a market field, and that equilibrium aptly characterizes agent actions. Axtell subsequently argues that agent-based computational modeling offers a platform for exploring

an alternative formulation that avoids the neoclassical sweet spot. Within Axtell's alternative formulation, agents are purposive without being able to read the future accurately as rationality presumes, they interact with one another through networked relationships, and societal formations are evolving and emergent and not equilibrated.

Jason Potts presents an evolutionary account of economic phenomena that is centered on the growth of knowledge. In contrast to Kohn's distinction between value and exchange, Potts's central distinction is between generic and operant levels of analysis. In particular, he argues that exchange is a generic process. By this, he means that exchange emerges out of the rules that people follow. This focus on rules leads to a style of economic analysis that is open ended, process-based, and evolutionary. Potts subsequently elaborates three kinds or levels of rules, and examines the insight this conceptualization offers into market evolution and the growth of knowledge.

Bart Nooteboom explores how embodied cognition, as treated by cognitive scientists, can lead to a methodological interactionism that transcends the common dichotomy between methodological individualism (which treats individuals as autonomous independent of society) and methodological holism (which treats society as sentient). Cognition arises through interaction, both among people and between brain and body within any single person. From this point of departure, Nooteboom explores how embodied cognition can generate insight into the operation of firms and the generation or extinction of trust within organizations.

Erik Reinert notes that Austrian economics originated within a particular Germanic orientation toward social and economic theorizing. After all, Carl Menger dedicated his *Grundsätze* to Wilhelm Roscher, and the flavor of his *Untersuchungen* was equally Germanic in giving analytical priority to the understanding of processes of social ordering. Reinert sets forth some of the contours of what he regards as an Austro-German theory of uneven economic development, and which these days might be labeled evolutionary development economics. The key conceptualization here is that development emerges out of specific activities in networked manner, and some activities and points of origin carry more oomph than other possible activities and points of origin.

Gerrit Meijer explores some of the contributions to economics that are associated with the University of Freiburg. The prime figure Meijer examines is Walter Eucken, though Friedrich Hayek was also associated with the University of Freiburg. Meijer also examines scholarship of the lawyer, Franz Böhm. Together, Böhm and Eucken developed an approach to law and economics in the 1930s that surely rivaled the University of Chicago at the time as a place of high creativity with respect to the integration of law and economics. The type of integration pursued by Böhm and Eucken and their colleagues distinguished between activities organized within market arrangements and the legal framework that shaped and framed those activities.

Alain Marciano likewise explores law and economics, emphasizing differences in conceptualization of their analytical subject matter by James Buchanan and Richard Posner. The primary issue Marciano examines is the

divergent treatments of legal processes by Buchanan and Posner. Where Posner treats legal rule making as an ordinary activity, Buchanan treats it as outside ordinary activity, and consigns it instead to the constitutive level of activity. In this, Buchanan carries forward the Eucken-Bohm orientation described by Meijer, whereas Posner rejects the dichotomy between a market and its framing or constitutive institutions. In doing this, Posner conceptualizes society as a field whereas Buchanan, like Eucken, and the contributors to this symposium for that matter, conceptualizes society as a networked structure or pattern of relationships.

Meijer Kohn closes the Symposium by describing three directions of research for advancing what he designated as the exchange paradigm: (1) intellectual history, (2) theoretical construction, and (3) historical research. These directions, moreover, are not independent from one another. Among other things, the intelligibility of historical experience can be rendered only through the employment of some theoretical framework. Furthermore, our intellectual past contains a good deal of scholarly work that is still valuable because it has not been contaminated by the enormous debris that has been spawned by the now receding but nonetheless century-long predomination of the value paradigm.

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Endnotes

¹ This quotation appears in Sandye Gloria-Palermo (1999, p. 20), and was taken from the correspondence of Walras collected in Jaffé (1965). Further discussion on the divergence between Menger and Walras is presented in Jaffé (1976).

² For a crisp statement of the primacy of process from a philosophical orientation, see Nicholas Rescher (2000).

³ An equilibrium theorist would not assert that a horse can fly, of course, but in doing so he would be speaking outside the framework of the static snapshot that equilibrium theorizing professes.

⁴ For a collection of essays in this vein, see Alston, Eggertsson, and North (eds.) (1996).

⁵ It's not really this simple and apparent, because you can't really just look at a snapshot of people and tell whether their relations with one another are governed by private or common property.