



*Sociality in Economics:  
It's Not Just About Markets*

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# Impersonal Market Exchange

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“It is not from the benevolence of the butcher, the brewer or the baker, that we expect our dinner, but from their regard to their own interest...

It is the necessary, though very slow and gradual, consequence of a certain propensity in human nature which has in view no such extensive utility; the propensity to truck, barter, and exchange one thing for another.”

Adam Smith, *Wealth of Nations*, 1776.



# Example: The Oral Double Auction

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- Features of the oral double auction:
  - Costs and values are dispersed among the individuals.
  - Institutional rules for trading are well-defined.
- Individuals choose purposefully.
  - Interacting non-cooperatively and impersonally, a market of individuals simultaneously maximizes:
    - (1) An individual's return *intentionally* and
    - (2) The aggregate social gains from exchange *unintentionally*.
      - "an end which was no part of his intention" (Smith, 1776)
- "The most significant fact about this (price) system is the economy of knowledge with which it operates, or how little the individual participants need to know in order to be able to take the right action" (Hayek, 1945).



## A Puzzle?

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“How selfish soever man may be supposed, there are evidently some principles in his nature, which interest him in the fortune of others, and render their happiness necessary to him, though he derives nothing from it except the pleasure of seeing it.”

“Nature, which formed man for that mutual kindness, so necessary for their happiness, renders every man the peculiar object of kindness, to the persons to whom he himself has been kind.”

Adam Smith, *The Theory of Moral Sentiments*, 1759

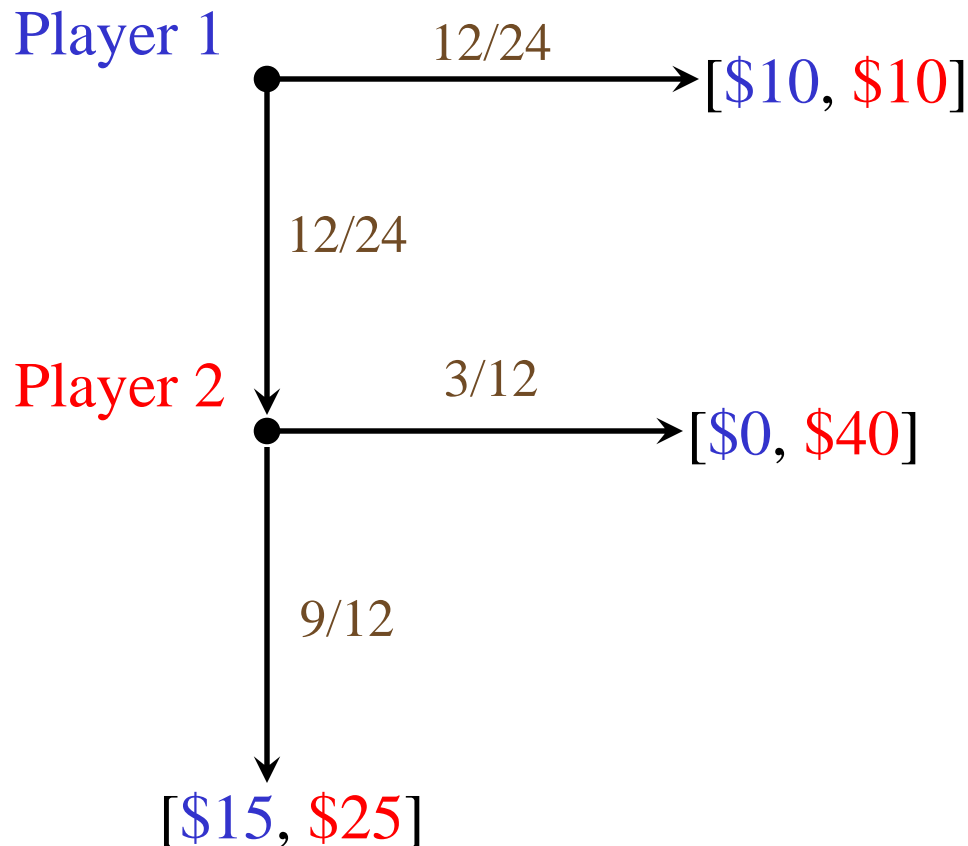


## A Puzzle?

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- Can intentional non-cooperative behavior coexist with intentional cooperative behavior?
- If they do coexist, why do they coexist?

# “An Investment Game”



- Self-regarding behavior would predict what outcome?
- What are the socially efficient outcomes?
- How do people interact when anonymously paired in a one-shot situation?
- Are Player 1's irrational?  
 $.75 \times \$15 + .25 \times \$0 = \$11.25$
- What do Player 1's (2's) believe when they play right?  
Play down?



# A Solution to the Puzzle

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- Efficiency in **impersonal** exchange is based upon non-cooperative behavior.
- Efficiency in **personal** exchange requires reciprocity.
  - **Positive reciprocity**: Rob responds, non-simultaneously and with like acts, when Kyle has transferred goods or favors to Rob.
  - **Negative reciprocity**: Rob punishes Kyle for “cheating” on an exchange by failing to return reciprocity.



## Or is there really even a puzzle?

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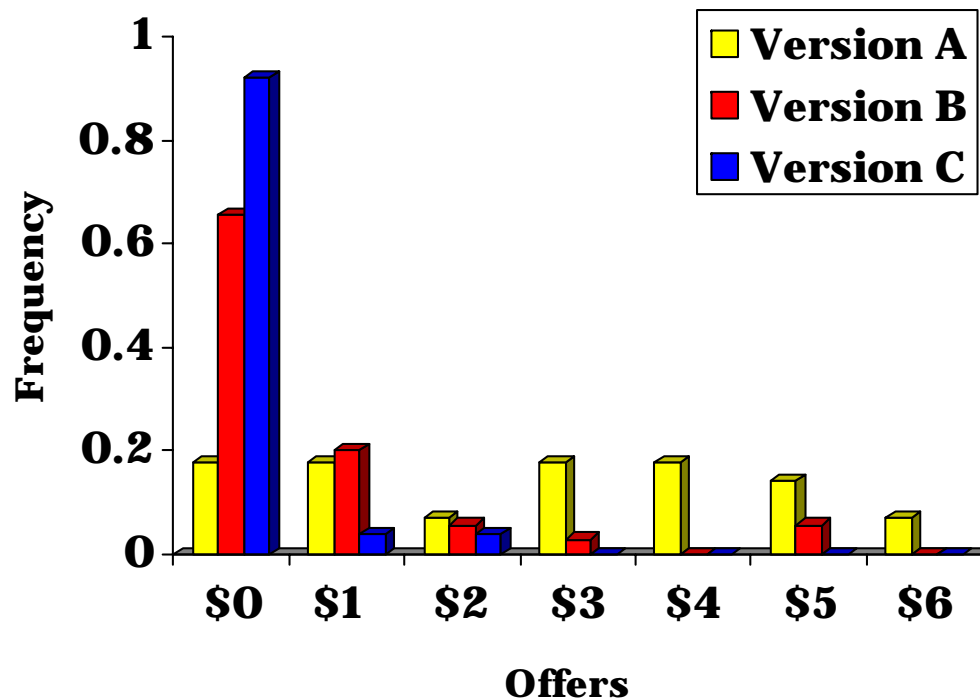
“If we put it concisely that by saying that people are and ought to be guided in their actions by *their* interests and desires, this will at once be misunderstood or distorted into the false contention that they are or ought to be exclusively guided by their personal needs or selfish interests, while what we mean is that they ought to be allowed to strive for whatever *they* think desirable.”

Hayek, *Individualism: True and False*, 1945



# “Dictator Game”

- Player 1 anonymously splits \$10 between himself and Player 2. The decision is final.
  - Version A: Monitor knows how Player 1 splits the \$10.
  - Version B: Player 1 also acts anonymously with the monitor.
  - Version C: Version B + Player 1 earns the money as the dictator.





# The Challenge

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“Part of our present difficulty is that we must constantly adjust our lives, our thoughts and our emotions, in order to live simultaneously within different kinds of orders <exchanges> according to different rules.

If we were to apply the ... rules of the micro-cosmos <personal exchange> ... to the rules of the macro-cosmos <impersonal exchange>, as our instincts and sentimental yearnings often make us wish to do, *we would destroy it.*

Yet if we were always to apply the rules of the extended order <impersonal exchange> to our more intimate groupings <personal exchange>, *we would crush them.*

So we must learn to live in two sorts of world at once.”

F. A. Hayek, *The Fatal Conceit*, 1988.



# Examples of Not Meeting the Challenge

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- Applying rules of impersonal exchange to personal exchange.
  - How long will your friend remain your friend if you *never* return like benefits?
    - Pure self interest in personal exchange will crush the friendship.  
“Friends don’t do that to friends.”
- Applying rules of personal exchange to impersonal exchange.
  - Only knowing his own circumstances, an individual cannot observe all of the gains from trade that a market a maximizes.
  - Furthermore, an individual’s experiences reinforce the concept that doing “good” enhances gains from personal exchange.
  - Hence, the individual is prone to distrust the market and led to believe that “good” can be done by intervening in markets.
  - An example: **Minimum wages**.



# Why Experimental Economics?

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“The curious task of (experimental) economics is to demonstrate to men how little they really know about what they imagine they can design.”

F. A. Hayek, *The Fatal Conceit*, 1988.



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