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The same face of the two Smiths: Adam Smith and Vernon Smith

Maria Pia Paganelli

Trinity University, One Trinity Place, San Antonio, TX 78212, United States

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ABSTRACT

Going from personal to impersonal exchange seems to be a relevant feature that allows humans to develop complex societies and grow prosperous. Adam Smith's idea of moral imagination, embodied in the impartial spectator and achieved through sympathy, may integrate and complement today's evolutionary biology and experimental economic explanations, providing the missing key as to how we generate and internalize those rules of conduct that promote fair and cooperative behaviors.

How do we go from personal to impersonal exchange? How do we go from cooperation among kin to cooperation among strangers?

Economic theory today explains the presence of cooperative behaviors and other-regarding behavior in terms of evolutionary biology and/or utilitarianism. Cooperation makes us evolutionarily fit, and it is in our interest to cooperate, at least in the long run. We create complex human society through this evolutionary process and through the internalization of the rules that allow us to trade successfully with strangers. These explanations are correct but fall short of explaining *how* we generate, internalize, and institutionalize those rules of cooperation that allow us to go from personal to impersonal exchange. Adam Smith's ideas of moral imagination, sympathy, and innate desire to be both praised and praiseworthy may offer a possible way to integrate and complete these explanations.

The idea to use Adam Smith and some of the literature of his time to integrate the picture of human behavior emerging from experimental economics originates with Vernon Smith. In 1998 Vernon Smith introduced *The Theory of Moral Sentiments* (TMS) – the "other" book of Adam Smith – into the experimental literature. Vernon Smith used TMS to help explain some experimental results with human and non-human primates and how those results relate to evolutionary biology. Given the depth of the insights and the stature of Adam Smith, Vernon Smith was followed by many more economists, and now TMS is relatively commonly seen in the experimental literature. This article is an attempt to develop the argument that Vernon Smith originally proposed.

E-mail address: maria_paganelli@yahoo.com

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In particular, I suggest integrating Adam Smith's ideas of sympathy, moral imagination, and praiseworthiness with the current explanations deriving from experimental results to possibly create a more complete picture of why and how humans cooperate, trust each other, and grow prosperous in industrialized societies. By this, by no means do I mean to diminish the importance of the traditional explanations based on self-interest. Nor do I mean to juxtapose self-interest to something else. Self-interest is and remains a major driving force of human cooperation. Other-regarding preferences and/or a moral sense do not substitute for self-interest in any respect, but they may integrate and fill the gaps in explanations of human cooperation among strangers that are based exclusively on self-interest. Additionally, in considering this, by no means do I mean to indicate that what I suggest is *the* only explanation. I simply propose an argument as *a* possible explanation. Adam Smith's analysis does not seem to contradict the existing explanations offered by evolutionary biology and neuroscience. His analysis seems relevant because it may integrate and potentially complete them. Another couple of caveats are due. First, the description of Adam Smith's views, provided herein, is instrumental to the explanation of problems we face in today's literature. Smith's primary concern was not about evolution or evolutionary biology as we know it today. Nevertheless, as Vernon Smith has demonstrated, Adam Smith can be successfully used, even if out of context, to help us understand questions we face today. Vernon Smith chooses to look at Adam Smith as a possible source for answers, and I choose to follow his line of thought because in many ways Adam Smith asked similar questions to the ones we ask today. Adam Smith's broad Scottish Enlightenment background incorporates and merges knowledge and insights and it may offer us different perspectives and answers that may be otherwise hard for us to see. Secondly, I will use the word *sympathy* not as a synonym of altruism or benevolence but in its Smithian meaning: as a *mechanism* through which we relate with others. The specific forms this mechanism takes will be discussed below.

If the analysis provided here is sound, the results are relevant for at least three reasons. First, because it shows the importance of moral imagination, praiseworthiness, and a sense of fairness in developing and sustaining complex commercial societies and the importance of commercial society for increasing not only prosperity but also cooperation. Second, because by understanding the process through which we generate, internalize, and institutionalize rules of cooperation we may be in a better position to understand how we can reach prosperity and cooperation. And finally, it highlights opportunities to integrate the *homo economicus* of our economic analysis, as Vernon Smith's suggests, with some of the insights of the underappreciated depths of economic and social understanding in the 18th century, offering a potentially more complete picture of human behavior.

The paper develops as follows. The first section describes some of the hypotheses used to explain cooperative behaviors in the existing literature. It is followed by the explanation of how Adam Smith may help us understand the mechanism through which we may be able to move from personal to impersonal exchange, namely the internalization of rules of cooperation achieved through sympathy, reducing the transaction costs present in complex anonymous societies. The Smithian explanation is subdivided into three sections: the generation and internalization of cooperation at the individual level, at the social level, and the institutionalization of the rules of cooperation which may be seen as a feedback mechanism caused by and causing increasing cooperation. The final section of the paper briefly examines some limitations for developing cooperation.

1. Vernon Smith and economic experiments

Vernon Smith fathered the branch of economics that uses human (and non-human) subjects in experiments to understand economic behavior. Despite accusations of "mechanicism" (Lee and Mirowski, 2007), Vernon Smith has increasingly and more vocally demonstrated interest in a broad and full view of human beings, looking at the 18th century as one of the possible sources of understanding and alternatives to the strict utilitarian mode (Smith, 2003, 2008, 2010).

In experimental results in industrialized countries, cooperation and fairness are routinely observed. Cooperation and fairness may vary with the degree of anonymity, as subjects respond to incentives. Nevertheless, even with complete anonymity, a relevant amount of cooperation and fairness is observed (see for example Hoffman et al., 1996; Cox and Deck, 2005; Cherry et al., 2002).[1] Additionally, cooperation and fairness are also observable in many foraging societies across the globe, although in different forms from the ones observed in industrialized countries. Fairness seems to be universally present among humans, even if it varies with different incentives and across cultures (Henrich et al., 2004). Interestingly, similar experiments done with non-human primates also show some level of cooperation and "fairness." Non-human primates help each other in getting food and reciprocate the help received. They get upset if one gets an "unfair" share: if one primate undeservedly gets a larger portion or tastier food, the other primate screams in protest (de Waal, 1996, 2003; de Waal and Berger, 2000; de Waal and Luttrell, 1988; Brosnan and de Waal, 2003; Jansen et al., 2006).

These experimental results show much more cooperation than economic theory predicts. So why do we cooperate so much? Smith (1998) presents a positive and negative reciprocity story using the behaviors of non-human primates to shed light on the origins of some human behaviors. Cooperation evolves, in part, when I punish you if you do not cooperate

[1] In a regular dictator game, where one player is given a positive amount of money and is asked to share it with another player, subjects share monetary rewards over 80 percent of the times. In a dictator game where it is known to all parties that dictators have to earn the stakes to be shared (by answering correctly GMAT questions), subjects do not share as much (between 20 and 30 percent of the offers are nonzero offers). With the complete anonymity of a double blind procedure, a hard-core of 3–5 percent of the offers remains nonzero.