

Virginia Viewpoint

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Nobility at George Mason University

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Summary

With a second Nobel Prize recipient, the George Mason University department of economics has established a worldwide reputation to which our once most prestigious colleges and universities can now only aspire. Perhaps it should be a cause for optimism that if undergraduate students at GMU can grasp that markets outperform government, there may yet be hope for an aging self-anointed elite mired in the New Deal.

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Congratulations to Professor Vernon Smith! He is the second George Mason University economist to win the Nobel Prize in Economic Science – the highest professional award any economist can win. Like his GMU colleague James Buchanan, winner of the 1986 Nobel Prize, Vernon made his indelible mark on economics by successfully challenging some of the profession's dogmas and stale assumptions.

Vernon invented experimental economics. Rather than repeat textbook accounts of how markets work – accounts that Vernon discovered did not persuade many of his students – he constructed real markets in laboratory settings. He gave students real money that became theirs to keep or to spend as they chose in the laboratory on various assets and items that he designed.

His findings are as important as they are unmistakable. Most fundamentally, he discovered that free markets work *better* than their textbook models. Unlike in textbooks, markets do not need a large number of sellers to be competitive. Only a small handful of sellers – as few as four – ensure vigorous competition. In other words, free markets are not seriously beset with problems of monopoly. Also contrary to textbook doctrine, efficient and competitive outcomes do not require that any buyer or seller be fully informed about the state of the market. All each party needs to know is his own preferences and abilities.

Turns out, then, that critics of free markets are right to insist that textbook economics inadequately explains real-world markets. But Vernon showed that this correct observation leads to quite a surprising conclusion – namely, that real markets outperform, rather than underperform, their textbook cousins.

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Another important, and unexpected, finding in Vernon's lab is that people are generally more cooperative than economists had previously assumed. Rather than cheat or short-change others (even when these others will never be able to identify the greedy malefactors), an encouragingly large number of people will play fair and cooperatively. This finding is immensely

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important. It shows that private, cooperative solutions are possible in many situations that were previously thought to require government taxation and regulation.

Vernon, however, has done more than demonstrate that markets and other private arrangements work surprisingly well. He has also used his lab experiments to discover the best ways of creating markets where none yet exist. For example, Vernon's work is a key for government officials seeking ways to reduce airport-runway congestion at peak travel times. In his lab, Vernon crafted a system of auctions that airport managers can use to allocate landing slots among different airlines. If implemented, the delays that we passengers endure would be fewer and shorter.

Similarly, Vernon is now hard at work studying markets for electricity. Already he has incurred the wrath of California Governor Gray Davis, who dislikes Vernon's demonstration that California's recent electricity crisis was not caused by deregulation. Vernon's scientific conclusion is that too much of that state's electricity market remains under the inept thumbs of government bureaucrats. His findings point to greater deregulation as the best means of ensuring reliable and inexpensive supplies to electricity users.

Vernon, of course, does not work alone. While he is a pioneer, he readily acknowledges that his remarkable achievements were made possible only because he is surrounded by excellent colleagues who share his deep understanding of economics and his commitment to scholarly integrity. As the late economist Peter Bauer once remarked, "a voice is rarely effective without an echo," and Vernon's colleagues have not only been effective in echoing and amplifying his message, but in themselves creatively advancing the reach of experimental economics.

Consequently, in 2001 when we sought to bring Vernon Smith to George Mason University, we courted not only him but also six of his colleagues. Of course, since the arrival at GMU of "the magnificent seven" (as several of us now affectionately refer to Vernon and his team), the stature of our already notable economics department has grown tremendously. And so, too, has the enthusiasm of our faculty and students.

George Mason University's department of economics has long been distinguished by its commitment to interesting and relevant scholarship. This commitment was crucial to enticing Vernon and his team to our University. We have no wish to be a second-rate Harvard. Instead, we have become one of the world's finest economics faculties by rewarding creative research that challenges accepted dogmas and in the process we lead the way in showing that markets almost always outperform government.

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(Donald J. Boudreaux is chairman of the department of economics at George Mason University, and a member of the Board of Scholars of the Virginia Institute for Public Policy, an education and research organization headquartered in Potomac Falls, Virginia. **Permission to reprint in whole or in part is hereby granted, provided the author and his affiliations are cited.**)

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