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**Market Perfection and the Case of Property: Methodological shortcomings of  
Economic Positivism**

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**Abstract:**

*The intersection between valuation practice and market theory is examined. Implications of the perfect market assumption are explored and applied to the pricing of land. Some emerging currents in economics and property are related to the problem of the market as a pricing mechanism for land.*

*It is found that the formal assumption of market perfection, despite from being broadly recognised as extremely rare in practice, creates complex problems for the pricing of land. Whilst neoclassical economics is largely grounded on the assumption of perfect markets, developments such as institutional economics and the theory of monopolistic competition attempt to bridge the gap between economic theory and positive reality. The paper concludes that these approaches are positively superior but tend to ignore fundamental considerations that led to the original adoption of perfect markets as the basis for economic theory. Implications for valuation theory are examined as well as methodological implications for the direction of property research and the meaningful development of the body of knowledge of the discipline.*

**Key words:** market theory, institutional economics, valuation theory, market efficiency

## 1. Introduction:

It would be trite to attach a citation to the notion that property value is the result of supply and demand, so great is the penetration of the language of the market within the property industry. For this reason, there would appear to be little point in enquiring into the significance of the relationship between property valuation and market theory. However, the behaviour and merit of the market within economic theory is a complex thing, not without considerable debate (Rosendaum 2000). There exist any number of schools of economic thought, and even within that subset referred to as mainstream, there are substantial deviations in thinking (Joseph Wayne Smith 1999; Self 1999). The Chicago School may dominate as the intellectual descendants of Alfred Marshall, but it has its subsets, while the Austrians have a distinct tradition, and there are also monetarists, neo-Keynesians, perhaps paleo-Keynesians, institutionalists and equilibrium theorists, to name a few. While each of these operates within the same basic market framework, they each have a host of reasons why all the others are wrong. Outside the mainstream almost anyone who can woo a publisher can write an economics and most of them who do wheel out a litany of reasons for distrusting the mainstream theorists.

Within this mass of theoretical discord the Marxists have shrunk substantially in significance since the fall of the Berlin Wall. While it remains an easy slur to label anyone who is critical of the mainstream body of theory as Left, a socialist, or even a Marxist, the reality does not support it. Lawrence Boland's (1988; 1992) systematic demolition of Marshallian economics is entirely worked on the internal logical errors of the theory. It does not convey any socialist agenda and does not bother with the complex political economy of Marx in order to show in how many places mainstream economics is based on logical contradiction. Others, such as Jones (1976) or Working (1927) have investigated the empirical support for market theory and have found it lacking. Jones in particular is of interest, because he represents a curious class of economic scholar who recognises that positive economic theory is not positive, yet upholds it as worthy of unqualified support. This hints of ideology. Between Jones and Working, both the supply and demand functions have been shown to be problematic, yet the market continues to hold sway as the centre piece of economic thought and it will be shown that this is largely due to the reality of market imperfection.

## 2. Economic theory and the practice of pricing

Property valuation on the other hand is a practical pursuit. While the economist uses theory to explain price, the valuer must use the best available tools to predict it. In a sense, the very tools of the valuer suggest the uselessness of economic thought for practical price determination. The economist would recommend the creation of demand and supply schedules from careful observation, yet the valuer has little place for these. The economist would explain supply using the intricate curves of the marginalist theory of the firm, but the valuer would side with Milton Friedman (1953) who noted half a century ago that the theory did not square with anything the firm ever did, or indeed could do. Friedman argued strongly that the conventional scientific objective of modelling actual causalities in order to understand and use phenomena when applied to economic events is "... *is fundamentally wrong and productive of much mischief*" (Friedman 1953). Skitmore and Runeson (2006) bridged this issue when they argued that "*although neoclassical microeconomic theory provides a useful means of analysis, it offers little for the practice of pricing.*" Their work echoes economists such as Odd Langholm (1969) who investigated pricing practice and found that marginalist theory was never used in practice. The property valuer is very interested in understanding the practice of pricing but despite using the language of supply and demand, but does not use their methods.

Despite this gap between economic theory and valuation practice, market theory continues to dominate both economic and business discourse, though it can be shown that these arenas adopt it

for very different reasons. Hidden at the heart of mainstream economic theory is a moral argument (von Kettler 1981; Small 2000), and it is the strength of this moral argument that makes it the necessary focus of economics. By contrast, the practicalities of commerce demand realism ordered towards competitive advantage, in the quest to maximize profitability. Within this realism, the forces of supply and demand are very evident and their manipulation is essential for business success, though they operate on principles that are neither moral (O'Neill 1998), nor scientific (Raffalovich 1999). This paper will explore the tension between the market of economics and the market of the real commercial world and attempt to locate property within it. It will do this by first exposing the connection between economics and moral thought, then secondly, differences between the market of economic theory will be contrasted to actual market, thirdly, the practical implications of the perfect market for property valuation will be examined, fourthly efficient market theory will be compared to perfect markets and applied to property valuation, fifthly, property value as market price will be contrasted to property value as investment value will be considered and finally, emerging issues in economic theory will be canvassed for their relevance for the valuer.

### 3. The Market, Economic Theory and Morality

Kenneth Arrow related the notion of Pareto optimality to equilibrium models to suggest that a competitive equilibrium situation can realise the goal of providing a situation where *no redistribution of goods or productive resources can improve the position of one individual without making at least one other individual worse off* (Arrow 2006, p.25). This aim of providing the best possible outcome for the community is a moral goal. There are several other ways that the moral dimension of the market is apparent.

Many states in the USA have legislation penalising profiteering. Profiteering is not the same as collusion, or restrictive trade practices, it can occur within circumstances that are apparently those of a liberal free market. Profiteering often occurs where transient opportunities enable some market actors to benefit unduly. The community rejects profiteering, despite economic theory seeing it as a vital market mechanism that will stimulate a rebalance of the market. The rejection is based on the vague moral qualm that excessive profit is improper. The very action of the market is directed to reduce excessive profiteering, and support for it is evidence that pricing is a moral issue and the market is a device for realising that moral goal. In practical terms, profiteering creates many dysfunctional distortions as resources may be diverted from useful and productive activities towards those that have excessive benefit/cost ratios.

Emerging economies, such as China, also are recognising the need for legislation to augment the deficiencies of the market, though their experience is instructive. As China adopts the market, it is those with emerging market power that appear to be the major beneficiaries (Gaylord and Levine 1997). The Chinese case reflects the dynamics that is seen elsewhere, the majority of the community object to the practice, but legislation is significantly influenced by the beneficiaries who allow some attention to the issue, but not so much as to eliminate the abuse. This led William Chambliss (1993) to conclude that the law making institutions of both communism and capitalism are considerably more complex than most superficial political theories hold.

The market as an institution for regulating economic relationships can only be evaluated on the quality of the economic relationships that result. All human relationships are evaluated using moral criteria, for that is what morality is about. A moral can be defined as a principle for the appropriate relationships between persons. Since human persons have intellect, will, and hence act from reasoned free choice, the positive content of relationships is freely willed action chosen by the moral actor as the result of reason. For free willed action to be possible, the person must have the power to do otherwise than the appropriate action. The power to do evil is what gives merit to the choice to do good.

In economic relationships, actors often have the power to act in ways that exploit others. The monopolist has the power to choose any price in the marketplace, with the only restraint being the foreknowledge that excessive prices may be resisted by those whose budget limitations may cause them to resist the purchase of a commodity that they would otherwise have purchased. The degree of need in purchasers along with their economic resources become the determinants of price, and where both are great, the vendor can exact a price considerably above any relationship to the legitimate costs and normal profits to supply. This is profiteering, and despite few commentators' attention to it, the fact is that the monopolist has the power to exploit the opportunity, but therefore also has the power to decide not to. This curious fact, that the monopolist has the power, and therefore the freedom, to do either good or evil in setting a price, garners scant interest in most economic theory as the latter assumes a person who is condemned to use intellect exclusively for self-interest. In defining economic man (*homo economicus*) in this way, economics sidesteps the fundamentals of moral freedom and anticipates the worst of human concupiscence and exploitative behaviour.

The market mechanism responds to the premise of *homo economicus* by providing an environment wherein exploitation is eliminated by force, market force. Market actors in a perfect market are not price makers, they are price takers. The power to exploit has been taken from them in order to realise a moral goal, the elimination of dysfunctional profiteering. Ironically, by removing this economic power to achieve a moral goal, market actors are prevented from acting morally, since their freedom has been removed by market forces, thereby making their acts compulsive, not free (Small 2004). This irony means that despite Marshall formally declaring the science of economics to be separate to morals, its core mechanism, the market, is only intelligible as a moral device, but despite being fully titled the *free* market, its action denies human freedom at its deepest level (Finn 2003). Marshall's argument for a moral-free positive economics was itself a moral argument, in that it argued that a quantitative science could provide policy recommendations that could be used to build a virtuous society. Andrew Yuengert lamented almost a century later, and apparently without having read Marshall, that "*One suspects that it is too much to expect of markets that they will ... create virtuous individuals*" however "*It is perhaps a sign of the extent of moral decay in Western society that they are expected to.*" (Yuengert 1999, p.108).

#### 4. Market Places and Market Functions

(Small 2004) concluded that a free market place was one of the fundamental requirements for moral action in commerce, but recognised the simultaneous necessity for an imperfect market situation. This runs counter to conventional economic wisdom, despite the longstanding recognition that imperfect markets overwhelmingly dominate actual practice (Robinson 1969). The moral defence of the market posits a *perfect* market, and it is on this assumption that most mainstream economics is built (Samuelson 1975). The perfect market was defined by Lâeon Walras as the foundation of economic theory and requires several conditions, among these are perfect knowledge, perfect mobility, a plurality of market participants and commodities for trade that are desired, but not mortally needed (Jaffâe and Walker 1983). Since market solutions to practical commercial problems require a perfect market, a critique of its mechanics is appropriate. Exhibit 1 shows the market functions of supply and demand as they are usually rendered in economics texts, with their characteristic upward and downward respective gradients.

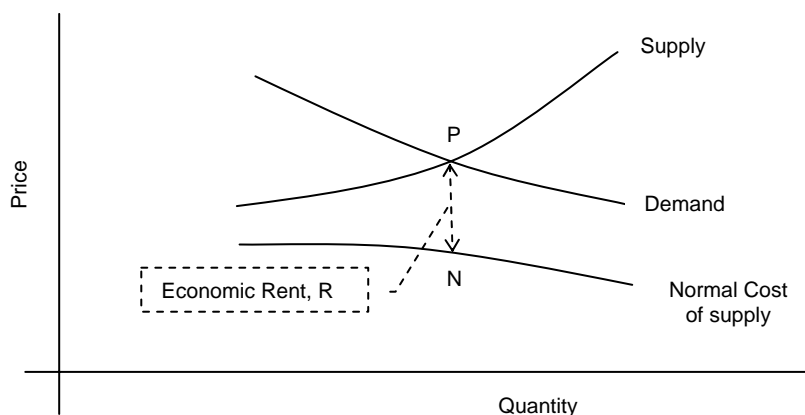
Also on the diagram is a curve representing the normal cost of supply. This important factor has two common definitions. The classical definition is the cost computed by summing all factor costs, including sufficient income, as wages and profit, to the entrepreneur, to satisfy their income needs without being so great as to incline other entrepreneurs to enter into competition. It can be thought of as the risk-adjusted costs and profit distribution for a firm with a stable real share value. Thus defined, it is that objective, quantifiable set of distributions that is the focus of much of the practice

of financial management at the firm level. Due to economies of scale, the normal cost of supply has a mild negative gradient.

The second definition of normal cost of supply equates it to the opportunity cost, or the price that would have to be paid in order to acquire a factor for the purpose of eventual on-sale. This more recent definition has the advantage that it overcomes the problem of land price that will be discussed in a subsequent section, but it can be shown to be problematic. If normal cost is the price that has to be paid to attract a production factor, then one can ask why the pricing for this factor is not simply the result of another perfect market transaction. If it is a perfect market transaction, then its cost, as purchase price, will be the result of its own factor costs. Ultimately, all factor costs regress to those relating to property rights (especially space and raw materials) and those relating to labour (including loadings for skill and entrepreneurship).

In practice, labour factors are related to standard of living costs, and community expectations of appropriate living standards, so they conform to the first definition of normal cost of supply. Competition for employment and the human reality of needing income for life make anything beyond this unrealistic for the vast majority of the population. Property factors, as will be shown below, do not behave in a manner consistent with perfect market pricing. The point is that the adoption of opportunity cost for normal cost of production regresses to actual normal cost to supply for some factors and pricing that cannot be reconciled with perfect market price determination for others. This makes the definition inappropriate in the explanation of perfect market pricing if the latter is to be adopted as universal model for pricing, as it is in economic theory.

**Exhibit 1: Market function gradients**



In most practical imperfect market situations, the intersection of supply and demand yields a price that clears the market, but provides an economic rent to the supplier. This economic rent is the gap  $R$  between the price point  $P$  and the normal cost to supply  $N$ . Financial management attempts to maintain this rent at a level that is just below that likely to induce effective competitors to enter the market by using tools such as marketing and branding (Wilson and Keers 1990). The result is relatively stable monopolistic competition. The economic rents enhance the profit of the firm creating super-normal profits, and these are capitalised into real equity growth. The fact of real equity growth is proof of the existence of stable economic rents, that is, stable imperfect markets.

The perfect market, if it existed, would have a very different appearance. Paul Samuelson (1975) recognised that the familiar supply and demand gradients are not native to perfect markets, but are entirely an artefact of market imperfection. He argued that if purchasers did have full knowledge and were not obliged to buy, then they would know the normal cost of supply for a given quantity of product. With this knowledge and freedom, they would not buy until a supplier, also with the aid of full knowledge, saw that it would be possible to supply at the normal cost of supply and earn a

reason personal income. The supplier would be adequately enticed into the market, and the purchasers would recognise the suitability of the price. Likewise, any supplier who considered profiteering would know that inflated prices would result in zero sales. In Samuelson's view, both the supply and demand functions would collapse onto the normal cost of supply in a perfect market, that is, they would display a modest negative gradient. The logic of Samuelson's observation is irrefutable, though it does not auger well for the integrity of a system of economics that claims to be built on the morally solid perfect market, while in reality using critical gradients that can only exist in the contrary market form.

Once the reality of the imperfect market is accepted, much of the remaining theory that makes up the body of mainstream economics is more sustainable as the behavioural expectations of *homo economicus*. This is not to say that the mainstream corpus of theory free of considerable logical problems elsewhere, as Lawrence Boland has taken pains to exhaustively demonstrate (Boland 1992; Boland 1997). It does suggest that Joan Robinson (1969) was on the right track, as demonstrated by the current emphasis on monopolistic competition. It does mean that economics is not amoral, as its proponents like to assert (Boettke 1998), but is immoral if the liberal market is claimed to achieve a moral end in the tradition of Marshall, since the moral claim is false.

The redeeming feature of economic theory is that it does supply the framework for appreciating the moral objectives of the community with respect to commerce. If price approaches the point where it would be in a perfect market, then objectively a moral and economic good is realised. Competitive liberal markets do achieve this to varying degrees, which can be a political objective. In some cases, morally conscious market participants do choose not to use their market power to exploit opportunities, and it has been argued that it is the unsung prevalence of this type of commercial behaviour that has enabled market economies to survive for this long (Phelps 1975).

Actual markets do display characteristics that suggest a positively inclined supply function and a negatively inclined demand curve. The extent and nature of these functions appears to be based on factors that receive scant attention in mainstream economic theory. The supply curve is the easiest to deal with. Higher prices mean higher profits and can induce less efficient suppliers into the market. In this way it has little to do with the complex computations of the marginalist theory of the firm, but still retains a minor dimension related to production costs, at least in the short term. Before leaving supply and the theory of the firm, it should be noted that even if the theory of the firm is accepted, at its core is dependence on demand, through the marginal revenue function. Although contrary to Say's law, this is the reasoning of anyone who has ever considered entrepreneurial activity: the first question is what a commodity will sell for, and from this are removed costs to test if sufficient profit will remain to make the venture worthwhile. It is also illustrated in the residual valuation method, where *en globo* land value, as price expectation of the vendor, is computed by starting with the end realisation, that is, the eventual effective demand, expressed as the price that purchasers will be willing to pay for the final developed space.

The demand function is also based on human decision making that runs counter to the popular explanation of mainstream economic theory. Demand is usually explained as a utility function, with some purchasers attaching a higher utility, and hence price, to a commodity than others. The aggregate utility/price behaviour of the community then becomes a monotonic negative gradient function with quantity. It is telling that while this explanation has logic, when Samuelson (1975) explained demand price behaviour, he talked in terms of the "money votes" potential purchasers were in a position to give in order to acquire a thing, not utility comparisons. This reflects the greater importance of *effective* demand, rather than *physical* demand in economics. While the difference may appear slight, Amataya Sen (1981) showed how it was literally the difference between life and death for victims of major famines who did not have the economic *entitlement* (as available money), despite considerable demand for food.

Once demand is understood as the subjective willingness to commit a sum of money towards the acquisition of a good, then the actual mechanics of the marketplace becomes accessible. Giffen

goods, those for which the demand curve has a positive gradient, become intelligible as instances where, amongst other things, price can be viewed as the most reliable indicator of attractiveness. The radical subjectiveness of the demand function suggests that it does not so much exist objectively, but rather originates as the personal demand functions of individual potential purchasers, even if it can be experienced as appearing to be objective (Benassy 2006). All this reinforces the more classical position that demand creates supply, leading suppliers to recognise that an important way to enhance profits is to groom individuals' personal demand functions to the point where purchasers are willing to commit greater sums to acquisition of a particular good. In this view, marketing is more demand management than information, a perception that is not without a long tradition of popular support (Packard 1957).

## **5. The Perfect Market and Property Valuation**

Property presents an additional challenge to the notion of the perfect market and possibly explains part of why valuers do not use market theory in practical valuations. If a perfect market in property were to price the land component at the normal cost of supply, the price of land would be zero, because the fundamental resource, land, has no cost of production. This runs counter to common experience, where in many markets the land value within a property asset represents the major component of value. Quite simply, the existence of land value is sufficient proof that land markets cannot be perfect. That is, every sale of land represents a situation where the purchaser accepts the practical necessity of paying a price for land that bears no necessary relationship to its cost of supply. This can only happen when the conditions for a perfect market are violated, and some reflection on the nature of land reveals that most of them are. This recognition led Adam Smith (1778) to conclude that for practical purposes land always behaved as a monopoly. That is, land pricing follows mechanisms that are the antithesis of perfect market competition. This explains why the valuer cannot apply a theory to land that was designed to apply, at least in part, to perfect market pricing.

The major techniques of valuation do provide important insights into the question of pricing. The residual method has already been mentioned, leaving the comparable sales method, capitalisation and summation methods. The summation finds most application as a check method and merely recognises that real property is usually a combination of land that is ultimately priced comparatively, and improvements, for which labour costs, competitive forces and pricing legislation all play a part in pricing. Applying a summation approach recognises that improvements only have value to the extent of their depreciated replacement cost, hence, capital growth lies with land. It is of no further interest here.

Valuing by comparable sales is perhaps the most important single valuation strategy, and even informs the practice of the other methods. The valuer does not so much establish the value of the property, as fit it into the fabric of values that makes up the whole market. The comparable sales method has no fundamental regard for costs, only relativities. While the valuer is careful to only consider comparable properties marginally better or worse than the subject, the integration of the approach over the entire market effectively connects every property, from the best to the worst. For the valuation of land, it recognises that land value can be thought of as a continuous value surface stretched over a spatially defined market. In this way, it is a practical reflection of David Ricardo's nineteenth century observation that property gets its value relatively from its marginal advantage over the least attractive land in use (Ricardo 1817).

The capitalisation method, or income approach, hints at the priority of rents over property values in causal priority. This has been experimentally validated (Small and Oluwoye 1999). Conceptually, it implies that for income producing properties, it is not the physical characteristics so much as the financial possibilities that carry value. Significantly, the capitalisation method ignores the notions of supply and demand completely, all that is required is an estimate of rent and a rate of return. While it is possible to construct arguments connecting rents and yields to supply and demand for rental space and investment property, these are tenuous and indirect. The direct facts provide ample scope

for the task of deriving price. In this way, price can be understood more directly than is possible using economic theory, making the application of the latter strained and unnecessary.

## 6. Efficient Markets and Perfect Markets

Eugene Fama (1965; 1970) proposed the Efficient Market Hypothesis (EMH) to explain the behaviour of equity prices. Often the expressions efficient market and perfect market are used synonymously, however Fama's efficient market also makes notions of supply and demand unnecessary by focusing on the efficiency of information flows in price setting. Financial securities, such as equities, exist primarily as the promise of a set of future cash flows. Their value is purely in terms of the anticipated future revenues, making value equal to the present value of the future returns (Wilson and Keers 1990). Like land, they can be considered to have no physical cost, even though common practice associates an acquisition price to them. They may be considered to be a form of property right, where the property in question is purely a set of expected cash flows. All property rights, including real estate, taxi licenses and radio spectrum, are valued in a similar way under similar notional parameters, that is, even if the initial payment is connected with acquisition of some tangible capital asset, the value of the asset is primarily associated with its capacity to provide future cashflows rather than with its intrinsic construction.

A taxi license is a reasonable example. At present in Sydney, one can purchase a taxi license for a little over a quarter of a million dollars. The license does not mean the taxi cab itself, which in any case has a value no more than a tenth of the license value. The value of the license is entirely composed of the present value of the net revenue stream that a well run taxi operation will produce, including an expectation of an eventual sale of the license. Its estimation suits discounted cash flow analysis. Historically, taxi licenses were originally given away freely merely to regulate the industry. In this way they were like water licenses up to a few years ago, and the lesson of their capital growth has not been lost on water property investors. Land pricing has similar essential qualities, though the physical asset is considerably more tangible, its value is derived from expected future rents, not costs.

Fama's efficient market hypothesis suggests that capital assets will be priced correctly in a market, depending on the quality of information flow, so that in its strongest form, all information pertaining to an asset will be factored into its market price. This means that there is no possibility of systematic supernormal profits flowing from its acquisition. It assumes knowledge of revenues and risks, as well as an agreed expectation of adequate return, or discount rate. If there is shared knowledge of those factors, both vendors and purchasers will share a common estimate of the value of the asset. The fact of a shared estimate of price is not the same as a perfect market price, it is merely an agreement at a broader level than is usually apparent in a monopoly pricing situation. Consider for example the right to acquire licensing rights to a monopoly trading position. The anticipated revenue stream is the result of monopoly, which will inflate the value of the asset. Both sides may agree on the price, and the purchaser will eventually earn only a normal profit from it, but the price is determined by the financial use-value of the asset, not anything connected with costs to supply.

## 7. Market Value versus Investment Value

It should be evident that property pricing appears to have more in common with investment pricing than commodities amenable to perfect market pricing. The competitive market does have application to products that can be competitively produced using productive factors over which the producer has little pricing control. Assuming the factor pricing is reasonable, the possibility and reality of competition are powerful influences for containing prices within limits acceptable to the community. On the other hand, property and financial assets have a price due to their investment value.

This creates several problems for the valuer. Given that the market is highly imperfect and influenced by complex social and psychological factors (Albert 1997), the underlying investment



value of a property may be masked by an array of market impediments including buyer emotion, incomplete information, irrational use of debt finance and incorrect interpretation of market signals. Some of these may be consciously managed by unscrupulous persons in the property market and evidenced in marketing strategies such as dummy bidding and two tier marketing (Robinson and Reed 2003).

In a buoyant market, demand is fuelled by irrational optimism stimulated mainly by the momentum of the market. This herd mentality is partly based on the evidence of capital gain and the belief that more of the same is immanent. The result is a distorted investment value that invited correction when the growth run is exhausted. In pessimistic markets, such as existed in the early 1990s, the reverse can be the case with investment demand absent except for exceptional opportunities. In each case, it is the error of the market price with respect to a sober investment appraisal that indicates transitory folly in the market pricing. While arguments can be couched in terms of supply and demand, the operative element tends to be demand, but the real dynamics are market pricing errors with respect to underlying investment value. A difficulty for valuers has always been the subjectivity and complexity of evaluating investment value. If the demand function is primarily personal as Benassy has demonstrated, then this is where investment value must originate, as subjective and investor-orientated. It would include aspects that valuers have traditionally avoided explicitly, such as leverage and taxation variables, as evidenced in the API practice notes for Discounted Cash Flow analysis. Despite this, valuers know that the market does respond to leverage and taxation changes, such as interest rate changes or changes to taxation concessions. The reality again appears to place price within the complex realm of investment decision of the potential purchaser, not an objective market price of the physical asset. Even owner-occupied residential purchases can be interpreted as a form of investment, with a utility use value and an expectation of capital gain.

Valuers have been shy of pursuing this area, and it has been taken up by financial investment advisors, despite the latter's lack of specific property expertise. A recognition of the importance for property economists to come to grips with an investment value perspective would appear timely. Valuers currently profess to being able to forecast an immanent market price, but adding an explicit investment appraisal capability may be an important dimension for the practicing valuer.

## **8. Institutional Economics and Pricing**

The emerging interest in institutional aspects of property indicate recognition that traditional economic theory has limited application in the practical commercial world. Austin Jaffe & Demetrios Louziotis (1996) concluded that institutional issues were correlated to property market efficiency, suggesting that property research should focus more on property rights than on econometric modelling in order to understand pricing trends. Dimand and Hardeen's (2003) review of Barbara Wooton's investigation showed how institutional aspects had substantial impact on the pricing of wages, well beyond the parameters suggested by the conventional approaches.

The emergence of indigenous ownership challenges to western property rights is one instance of economic outcomes being influenced by factors of a social, cultural, or psychological nature. It has led to a shift in interest towards social issues as suggested by Albert (1997) that were largely expunged from the discipline a century ago by Marshall and others. John Davis (2006) recognised this trend towards a broader research agenda for economics that has seen the emergence of several nascent, though promising schools of economic thought, several of which may provide more useful practical direction than the current corpus of mainstream theory.

The notion of *homo economicus* has come under almost constant derision since it was first articulated. Its defence is principally in terms of the supposed usefulness of the theories that flow from its adoption, despite recognising its unrealistic nature (Friedman 1953). Thomas and Rosita Rourke faced this argument head on and noted the economic and social shortcomings of the application of liberal market ideology. They linked it to the anthropology of western modernity, principally the notion of the individual, from which *homo economicus* was developed through

Enlightenment rationalism (Rourke and Rourke 2005). They distinguished between the notion of the individual and that of the person and demonstrated how the acting moral person was the appropriate anthropological basis for the construction of any political system capable of supporting a sustainable culture. Given that the practical economic system is a set of institutions built on a political and cultural foundations (Small 2003), the personalist argument includes a strong economic dimension that is thoroughly explored.

The Rourkes' approach the problem from the perspective of political science, within which economic relationships are a key power source and they present economic evidence covering an extremely wide range, from local small business to the impacts of globalist free trade. This perspective provides an important insight into the nature of the market functions that mainstream economics appears unable to come to grips with. Gregory Gronbacher (1998) argued that only when economics incorporated the anthropology of personalism could it flourish as an autonomous science. Personalism also offers useful tools in inter-cultural dialogue, such as is necessary in the resolution of indigenous ownership disputes with liberal market cultures. It also enables the economic actor to assume a mantle of consciousness appropriate for genuinely human behaviour, rather than the mechanistic self-serving determinism of homo economicus.

The existence of the market functions of supply and demand in practical markets, with their characteristic gradients, has not been doubted as a general tendency, even if they may only exist as attitudes subjectively held by individual market participants. What is not convincing is their origin. The reality in an imperfect market is the imbalance of market power. The degree of need in the respective parties is an index of their weakness in the trading relationship. In most cases, the purchaser has the greater need as most purchases move goods closer to actual consumption and consumption is a response to a physical need or desire. In the majority of cases vendors have a greater likelihood of finding other purchasers, and in any case sale is not connected directly to their human needs. If a baker does not sell pies to one person, she may sell it another, and even though no-sale is an inconvenience or a cost, it is not the same as the hunger of the person who did not buy. The major exception is the sale of labour. The labourer sells labour to directly finance subsistence. If the labourer does not sell labour, in most cases he does not eat, but if an employer does not buy labour from a particular person, she either finds another, or does the work herself.

For both supply and demand, the major determinant of their price/quantity calculus is their power in the trading relationship. Their power is weakened by their own human need, but strengthened by the need of the other. The human need of consumers is a good's utility, the human need of vendors is the urgency of the transaction and its relationship to their own subsistence. John Lie (1993) traced the history of the modern western market economy to "*power and social struggles*" not economic advances *per se*. Thorold Rogers (1884) showed quantitatively that the transition to market commerce in the sixteenth century did not aid the majority of the population of England, despite making England the most powerful commercial power in the world in its time. Fred Harrison (1983) examined the way that technology was used more as an economic weapon through the industrial revolution than simply a means of raising productive efficiency. It shifted the power balance away from labour. In property, Lawrence Raffalovich suggested that "*...in advanced industrial capitalism the power of property is rooted in political, not market relations*" suggesting political/power aspects as key to understanding property, not economic considerations (Raffalovich 1999). Cynthia Watson noted that the major determinant of commercial rents "*the balance of negotiating power between landlord and the tenant*" where the landlord's power was further influenced by access to capital and investment objectives (Watson 1995). Each of these authors identifies power issues as central to understanding the behaviour of the markets they study.

Even the direction of economic thought itself can be interpreted through the lens of power. If those with greater economic power want to protect their political position it is in their interests to create a system of economic thought that supports it. This view is sociological Marxism (Cuff, Sharrock et al. 1992), but it was empirically validated in the case of twentieth century US economic thought and the development of land-scrip universities in the USA by Mason Gaffney (1994). Gaffney is

definitely no Marxist, but the historical connection between major entrepreneurs, the enterprise of establishing universities in return for potentially valuable land grants and the selection and promotion of economics professors of the right sort makes a strong argument. It would go some distance to explaining why the discipline thrives despite failing to meet its own criteria. Mainstream economics, according to Marshall and Friedman has merit purely on its empirical strength, especially in terms of its predictive ability, yet authors such as Sen (1981), Rourke and Rourke (2005) and Michael Pusey (2003) being examples of studies that demonstrate its failure historically, internationally and within Australia respectively. The evidence failure in the face of continuing rhetoric of potential success would seem to strengthen Gaffney's argument. Apologists for mainstream economics, such as Milton Friedman (1980) usually point to the historical success of capitalism as proof of its superiority. They are careful to avoid noting that while historically GDP per capita is higher for capitalist countries, its impact on the ordinary citizen is usually lost due to excessive wealth polarisation (Rogers 1884) that has only been broken in the last two centuries by the threat of socialism. Without socialism as a viable political threat, Pusey's observations of the plight of middle Australia is fast taking on the same profile as working England in the sixteenth century as studied by Rogers.

A power theory of the market appears to add a degree of realism to the supply and demand functions, without denying their traditional association with utility and the goal of profit maximisation. It recognises that these personal motivations are valid but partial, and adds other more pressing factors such as social, psychological, political and even biological influences which practical experience suggests should be included in the market calculus. A power theory also integrates well with more pervasive cultural themes, such as post modern theory derived from Hegel (Grosz 1990) and the Nietzschean preoccupation with power as the basis for all relationships that pervades much social thought (Foucault 1976). While power may be the best explanation for relationships in western modernity, Rourke's point is that humans are capable of other grounds for action. Karl Zimmerman's (1947) analysis of the rise and fall of great civilisations can be read as an historical analysis of the tendency for cultures to begin and grow under an anthropology of personalism, only to atrophy when the dominant anthropology is transformed into power relations. On this reading, *homo economicus* is symptomatic of an anthropological ideology that has the capacity to do greater harm than that limited to economics and against which indigenous people are currently waging a feeble rearguard battle.

## 9. Conclusions

The valuer is currently in a curious position, as the valuation profession matures as an academic discipline. On one hand, there is the understandable desire to integrate more fully into the parent discipline of mainstream economics. On the other, is the practical fact that economics has never had very much to offer the valuation profession, apart from some general notions that appear to refer to very real and powerful forces in the market place, but just happen to be very different to what the economists says they are.

Milton Friedman told us half a century ago not to take economic theory seriously. Its only value is the reliability of its predictions. It is not meant to an isomorphism that models reality conceptually and mathematically. Its only use is to suggest policies that the community may adopt on the faith that they will produce desirable social outcomes. There appears to be overwhelming evidence that the policy prescriptions do not help who they usually say they will help, the broad community, developing people, the economically marginalised. On this basis it seems to have failed, not only as a conventional science, but also as a predictive art in the Friedmanite mould.

The valuation profession, or more generally the property economics discipline, is yet to recognise that it may in fact be ideally suited to make a key contribution in the reverse direction. Rather than seeking to incorporate economic theory, the property economist is in a position to inform it, to expose some of its more fundamental and practical flaws and perhaps to even advise on their rectification. The property discipline has a speciality that is suited to the task in a most timely way,

that is, its focus on property. The renewed interest in the nature of property occasioned by the political prominence of indigenous ownership has the potential to review the institution of property and in so doing can be used to explore the political, cultural and anthropological foundations of this key component of most economic relationships.

The valuer already knows the immeasurable worth of knowing the full context of a sale, of having a feel for the market. As yet that aspect of the art of valuation has been largely hidden from the light of academic enquiry due to its embarrassingly irrational and non-quantifiable nature, but any good practitioner knows it is the key to professional success. It is time for the methodology of property economics to recognise this reality and in so doing offer mainstream economics direction out of its current unreality as a discipline.

NOTES FOR REVISION: include (Conlisk, Gerstner et al. 1984) to illustrate practical markets, also (Rabin 1998) on irrationality.

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