

Sociology 120  
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Tu-Th 3:30-5:00  
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Office Hours: 1-3 Tu or by appointment  
Barrows 452

## Economy and Society

The financial crisis that began in the fall of 2008 is still with us. Unemployment remains high and the economy is slow growing. Families at the bottom of the income distribution find themselves more vulnerable than ever before. Middle class people who owned a home have seen the value of their homes drop dramatically. By last count, 28% of all homeowners owed more on their houses than they are worth. For those of you who started college in 2008 and are on track to graduate this spring, the labor market looks grim.

All of this cheery news ought to make some of you wonder, how did this all happen? What can we do to get out of this situation? Is there anything that can be done to make sure it does not happen again?

The obvious place to look for answers to these questions is economic theory. But, for those of you who have taken introductory economics classes, such theories do not seem up to the task. At the core of microeconomics is the idea that markets operate according to principles which make the kinds of things that have happened impossible. In a world with perfectly rational actors, with perfect information, operating in markets where prices constantly adjust to supply and demand, economic bubbles and sudden and long lasting crises are impossible.

While there is a lot of economics about how market failure occurs all of the time (Keynesian economics, information economics, transaction cost economics, institutional economics), the political arm of the field that is dominant (with few exceptions, the conservative think tanks that churn out policy recommendations for politicians) continues to sell market fundamentalism as the cure for everything. Indeed, at this moment, all across the world, politicians and their advisers have agreed that the main problem standing in the way of recovery is too much government spending and not enough operation of market forces. It is thought that governments cannot run deficits (deficits caused by a lack of economic activity to fund the central tasks of governments like health care, pensions, education, and infrastructure) because financial markets won't let them. The Republican Party has embraced market fundamentalism by arguing that the way to get us out of the recession is to cut government funding, lower taxes for the wealthy, and get rid of regulations that govern the environmental, banking, and labor. While

one cannot blame the economics profession for all of this, the fact remains that their main theory, neoclassical economics, is the one that is at the core of this economic policy.

Having said that, I want to say upfront that I am a big fan of market society. Market society has produced a better standard of living and longer and healthier lives for large numbers of people here and around the world. It continues to create transformative products that make our lives more interesting, meaningful, and more healthy and secure. But, in order for us as a society to get out of this current mess, it is necessary to construct an alternative theory, one that begins with the idea that the government and markets are joined at the hip, that market actors do not behave as neoclassical theory suggests, and that proposes to understand the conditions under which markets can create dangers, dangers that should be regulated in order to prevent catastrophic damage to all citizens.

My view is that sociology can play a positive role in these discussions. This can work in two ways. First, sociologists are well placed to de-bunk economists' myths about how particular markets work independent of social relations and government intervention. This act of de-bunking should be popularized to make citizens aware of how important government and ongoing social relationships are to the functioning of the economy. Indeed, modern markets depend on government, civil peace, and law to exist (something most academic economists would now agree with).

Sociologists can provide some set of theoretical tools to make sense of many of the conundrums of the modern world economy. The existence of social structures in and around markets and the intervention of government in markets is not that surprising. The interesting question is, when do these interventions result in positive outcomes for society and when do they result in negative outcomes? Economists historically have viewed these features of markets as bad and indicating market frictions or inefficiencies. They have tended to emphasize the good effects of markets over the bad and asserted that getting rid of government and social ties of all kinds between market players would aid in creating efficient outcomes. But even here, more recently economists have come to the opposite conclusion, that networks, firms, institutions, and governments have important and mainly positive roles in economic development.

It seems to me that sociology, with its emphasis on understanding the empirical world can maintain a healthy skepticism about both the positive and negative aspects of market society. By theorizing what those might be, sociology can provide citizens and policymakers with tools to analyze particular market building projects with an eye towards understanding when social relations and government intervention appear to contain seeds of rent seeking (i.e. privilege incumbent firms in a market or government officials who control market access and thus give them the opportunity to seek out higher profits than is their due) and when they appear to aid positive economic growth. They can help us understand when markets contain too little social structure or regulation. So, for example, markets that are constantly whipsawed by rapid price swings usually suffer from too little information, not too much and as such are open to speculation. Markets are a form of social power and the real question is whether or not one group

gets to benefit from the distribution of goods and services produced in a disproportionate fashion.

My goal is for you to leave this course with a set of intellectual tools to analyze real markets. These tools will make you able to read the newspaper more intelligently, participate in political life in a more knowledgeable way, and understand how the organization you work for (whether public or private) fits into the broader set of markets and government in which it is situated.

This course is set up to first consider and then refute most of the main neoclassical assumptions about how markets work. We consider empirical examples that illustrate the problems of neoclassical theory. Then, we turn to explicating a sociological view of markets.

We use that sociological perspective to try and analyze the rise and fall in the market for the securitization of mortgages. This perspective causes us to question many of the conventional wisdoms about what happened. We consider how this crisis has spread around the world. We end by considering what the collapse of the housing market means for the future of the American economy. The financial crisis has generated lots of press. If you want to listen to one version of the crisis, I recommend “The Giant Pool of Money” that aired on NPR’s This American Life.

<http://www.thisamericanlife.org/radio-archives/episode/355/the-giant-pool-of-money>

If you like movies, I suggest “Inside Job”, Charles Ferguson’s Academy Award winning documentary about the crisis. If you want a gripping fictional account (light on the analysis, but heavy on the drama), see “Margin Call.”

We then consider the problem of how capitalism is organized differently in the developed and developing world. We show how the American model of capitalism, based on the idea that firms should maximize shareholder value, has not spread much beyond the U.S. and Great Britain.

### **Class format**

This class is set up as a lecture class. My lectures use the readings as their main source of information. The class assignments will be drawn from the readings and lectures as well. The good news is that we will have Graduate Student Instructors (GSIs) and run sections with a maximum of 25 students. This means that it will be possible for you to learn quite a bit in this class if you work at keeping up with the class on a week to week basis. Here is what I suggest. Learning is often about repetition. Multiple exposures to the same material in different settings and with different ways of absorbing the material make it more likely that you will grasp it.

In practice, this means you must do the readings before class. While you may not totally understand them, it will make the lectures more comprehensible. Then, you should go to section.

Section will allow you to discuss what was said and ask questions about what you did not understand. The writing assignments and exams will further push you to express for yourself some of the issues at stake in the material. If you do all of this, you will be in a position to get the most out of the class.

## **Readings**

There are two required texts:

N. Fligstein. The Architecture of Markets, Princeton University Press, 2001.

B. McLean and J. Nocera. All the Devils are Here. Penguin. 2010.

There will be a reader available at University Copy Service (2455 Channing Way, 549-2335 located at the south end of Sather Gate Shops passage). I will also post the readings on B Space if you do not want to buy a reader.

## **Course Assignments**

Your grade will be based on your attendance and participation in section (10%), two short papers that will be conceived and written in section (20% each for a total of 40%) and two exams, one an in class midterm (25%) and one a final exam (25%).

We are fortunate in this class to have GSI sections. That means you will have the opportunity to discuss the materials in the class, twice a week, with a GSI. Section attendance is required and attendance and participation will count for 10% of your grade. Sections will begin meeting the week of January 23-26 (the second week of class). Sections will not meet the week after the mid term exam (Feb. 27-March 1). GSIs will schedule their office hours once the semester begins. They will hold office hours beginning the second week of classes.

One of the Sociology Department's initiatives in adding GSIs to a class was to try and give students the opportunity to write more sustained papers. The main task of going to section is to give you an opportunity to ask questions about and discuss the material. But, there will be two short papers in the class that will be discussed in section. Each paper will be 5-7 pages long, double spaced and worth 20% of the grade. The section meetings will be set up for you to choose a topic, discuss it with the GSI, and produce an outline for the paper. The paper will be integrated into studying for the exam. Indeed, the topic of your paper will certainly be part of your preparing for the exams.

The first paper will be based on the materials in the first third of the class. It will be due on March 21 in Section. The second paper will be based on the materials on the financial crisis and will be due April 25 in Section. Late papers will be graded down one letter grade per day

late.

There will be two exams each worth 25% of the grade. The exams will contain some multiple choice questions and some short answers. I will provide students with a list of potential questions before the exam. The first exam will be February 23 and the final exam is Friday, May 11, 2012, 7-10 PM (sorry, nothing I can do about that!). The exams are non-cumulative . The first exam will cover the critique of economics and the sociological view of markets. The second will focus on the financial crisis, 2007-2010 and the section on “comparative capitalisms.”

### **Class Sessions and Readings**

Jan. 17 Introduction

Jan. 19 An Introduction to Economic Sociology

Reading: Fligstein, ch. 1

Jan. 24 What does neoclassical theory say about the organization of markets?

Readings: E. Roy Weintraub "Neoclassical economics" and J. Williamson "A Short History of the Washington Consensus".

Jan. 26 Problems of neoclassical theory- I Price theory, and the problem of anonymity, the number of traders, and networks

Readings: W. Baker, "Social structure of a securities market" American Journal of Sociology, 1984, 89: 755-811.

B. Uzzi and R. Lancaster, "Embeddedness and the price of legal services" American Sociological Review, 2004, 69: 319-345.

Jan. 31 Problems of neoclassical theory II- Trust in markets, networks, and institutions and their effect on firm performance

Readings: K. Kashkooli, "Risk, Uncertainty and Market Growth: The Case of E-Bay", Paper presented at the Annual Meetings of the American Sociological Association, Boston, Ma., Aug 4-8, 2008.

B. Uzzi, "The sources and consequences of embeddedness for the economic performance of organizations", American Sociological Review, 1996, 61: 674-698.

Feb. 2 Problems of neoclassical theory III- The role of governments in trade and markets

Reading: N. Fligstein, "Economic transformation of Europe", Ch. 3 in Euroclash: The EU, European Identity, and the Future of Europe, 2008, Oxford University Press, Oxford, Eng.

Feb. 7 Problems of neoclassical theory IV- Property rights around the world: a lack of convergence

Reading: R. LaPorta, F. Lopez-de-Silanes, A. Sheifler, "Corporate ownership around the world", Journal of Finance, 1999, 54:471-517.

Feb. 9 What is a sociological view of markets?- I Pre-conditions for markets

Reading: Fligstein, Architecture of Markets, ch. 2-3

Feb. 14 What is a sociological view of markets?-I (continued) The emergence, stabilization, and transformation of markets

Reading: Fligstein, Architecture of Markets, ch. 3-4

Feb. 16 What is a sociological view of markets?-II How networks index property rights and market structure

Reading: Networks in the Economy: W. Powell and L. Smith-Laurel "Networks and economic life" pp. 379-402 In N. Smelser and R. Swedberg (ed.) The Handbook of Economic Sociology, 2004, Russell Sage: New York.

Feb. 21 What is a sociological view of markets?-III The performativity of economics and economic theory

Reading: D. MacKenzie Ch. 1 "Performing Theory" in An Engine, Not a Camera, Princeton University Press, 2006.

Feb. 23 In class exam

Feb. 28 The Mortgage Securitization crisis: What happened and whodunit?

Reading: N. Fligstein and A. Goldstein "The anatomy of the mortgage securitization crisis." In M. Lounsbury and P. Hirsch (ed.) Markets on Trial: The Economic Sociology of the Financial Crisis, Emerald Press, 2010.

March 1: The alphabet soup of mortgage products

Readings: L. Kendall. "Securitization: a new era in American finance." Pp. 1-16 in L. Kendall and M. Fishman (ed.) A Primer on Securitization. MIT Press: 2000.

Y. Smith. Chapter 9. "The Heart of Darkness." Econned. Palgrave, 2010.

B. McLean and J. Nocero, Ch. 8 in All the Devils Are Here, Penguin Press, 2010.

March 6 The emergence and expansion of securitization in the housing market in the U.S. 1966-1988

Readings: S. Quinn "Securitization and the state", Paper presented at the Annual Meetings of the American Sociological Association, Boston, Ma., Aug 4-8, 2008;

B. McLean and J. Nocero, Ch. 2 in All the Devils are Here, Penguin Press, 2010.

M. Lewis, Pp. 79-151 Liar's Poker. Penguin, 1989.

March 8 The Rise of the New Mortgage Market and the Origins of Subprime, 1988-2001

Reading: B. McLean and J. Nocero, Ch. 3-5 in All the Devils are Here, Penguin Press, 2010.

March 13 Complex Role of Government as Regulator and Participant, 1966-2010

Readings: B. McLean and J. Nocero, Ch. 6-7 in All the Devils are Here, Penguin Press, 2010.

S. Johnson. "Introduction". 13 Bankers. Pantheon, 2010

March 15 The Rise and Fall of the Subprime Market, 2001-2010

Reading :B. McLean and J. Nocero, Ch. 9,-10, 15-19 in All the Devils are Here, Penguin Press.

March 20: The Spread of the Crisis around the world

Readings: N. Fligstein and J. Habinek "The spread of the worldwide financial crisis".

March 22: Economic Sociology and Making Sense of the Financial Crisis: Questions that remain and the Future of the American Economy

March 26-30 Spring Break

April 3 Characterizing Capitalisms I- The Shareholder Value Conception of the Firm in the U.S.:

Reading: M. Useem, "The rise of shareholder power", ch. 2, Executive Defense, Harvard University Press, Cambridge, Ma., 1993

April 5 Characterizing Capitalisms I (continued)- The Shareholder Value Conception of the Firm in the U.S.:

Readings: M. Useem, "Intensified management of managers", ch. 4, Executive Defense, Harvard University Press, Cambridge, MA., 1993

N. Fligstein "The rise of the Shareholder Value Conception of the Firm", ch. 7 in The Architecture of Markets, 2001.

April 10 Comparative capitalisms II: "Has the world gone to shareholder value?" Overview (hint: the answer is "no")

Readings: PA Hall and DW Soskice, Varieties of Capitalism: The Institutional Foundations of Comparative Advantage, 2001, Oxford University Press, ch. 1.

N. Fligstein, ch. 8 in The Architecture of Markets. (covers related materials)

April 12 Comparative capitalisms II: "Has the world gone to shareholder value?"

Case Study: Japan

Reading: S. Vogel "Routine adjustment and bounded innovation: the changing political economy of Japan" In .W. Streeck and K. Thelen (ed.) Beyond Continuity, 2005, Oxford University Press, Oxford, Eng.

April 17 Comparative capitalisms II: "Has the world gone to shareholder value?"

Case Study: Germany

Reading: M. Albert. p. 99-146, in M. Albert Capitalism vs. Capitalism, 1993, Four Windows: New York, N.Y.

April 19 China: Broad contours of the transition to a market economy

Reading: B. Naughton. Ch. 4 The Chinese Economy: Transitions and Growth. MIT Press: Cambridge, Ma., 2007.

April 24 China: The reorganization of Chinese firms and the growth of the "private" economy

Reading: B. Naughton. Ch. 13 The Chinese Economy: Transitions and Growth. MIT Press: Cambridge, Ma., 2007.

April 26 Sociology and Economic Life: A conclusion Reading: Fligstein, Ch. 10.

## Paper Assignments

There will be two paper assignments for this course. The purpose of the papers are for you to be able to explore some topic in more depth. Each paper will count for 20% of the grade for a total of 40% of the grade. Papers that are turned in late will be graded down one letter grade each day they are late. We encourage you to meet the deadlines for the paragraph description for what you are going to do and the outline of the paper. We also encourage you to go to office hours if you are having trouble with the assignments. GSIs will discuss the assignments in Section. Here are the deadlines:

### First paper

Feb. 15 One paragraph describing your project due in Section on Wednesday  
March 5 1-2 page outline of your paper due in Section on Monday  
March 21 5-7 page double spaced paper due in Section on Wednesday

### Second paper

April 4 One paragraph describing your project due in Section on Wednesday  
April 16 1-2 page outline of your paper due in Section on Monday  
April 25 5-7 page double spaced paper due in Section on Wednesday

### First paper

The first paper should be drawn from materials in the course up until February 23 (the mid term exam). I expect that students will write one of three kinds of papers.

1. A synthesis. You may decide that in order to understand better how the materials fit together, it might make sense to write a synthetic essay from the readings. Potential ideas for topics:

A. What are the empirical critiques of neoclassical economics? Why does it matter that neoclassical models do not account for real markets? What does this mean about the potential success of failure of social and political policies based on trying to implement reforms based on creating a neoclassical market?

B. What are the main conceptual tools that sociologists use to describe how markets are structured (i.e. government and law, market institutions that allow markets to generate trust and allow participants to trade, networks, and performativity)? How do these tools produce a more realistic view of how markets work?

C. How do the general political alignments in society (i.e. the relative power of government, business, and labor) operate to structure market institutions? Under what conditions would we expect that capture of market institutions would result in markets that operated to narrowly reward one party or another (i.e. rent seeking)?

2. You might choose to investigate one of the concepts we discussed in the first part of the class more intensely. This might lead you to do some additional reading in order to understand how scholars use some of these ideas. Some examples:

A. Property rights. Who gets to control profits in capitalism is a big topic. Accounting for the large differences in how property rights are constituted in societies over time and level of development is a research industry.

B. The emergence of new markets. What are the roles of existing firms, entrepreneurs, and government in the constitution of new product markets? Where do new ideas come from and how do they spread across firms?

C. The role of academic ideas like those from economics in the creation of new markets. MacKenzie argues that economic ideas helped structure the futures markets. How is it that ideas can be performed in markets? How do these kind of processes work? How do such ideas depend on already existing social structures?

3. You might choose to try and use some of the ideas in a class to understand a particular market in which you might have an interest. Some examples.

A. The use of social networks in Facebook implies a kind of performativity. In the case of Facebook, the model is to directly draw upon the social contacts people have to build a market. But what exactly is the market? How can Facebook make money off of people keeping a Facebook page where they communicate with their “friends” for free? What are the problems that the firm has in creating a stable market by which they can make money?

B. Amazon relies on a different kind of performativity. Instead of measuring a given person’s social network, they use information on what basket of goods that people buy in order to suggest things that you might want to buy. The underlying assumption is that you share tastes with an aggregate of people whom you do not even know. What is the sociology of this kind of product market?

C. Recently, the Justice Department would not allow ATT to merge with T-Mobile. Had the merger gone through, the new company would have been the largest mobile phone company in America. Advocates of the merger stressed that customers would have the advantage of a bigger firm and network. Opponents stressed that consumers would have less choice with the two largest firms controlling over 70% of the US market. Use the sociology of markets to argue

whether or not the Justice Department was right.

D. Why is CEO pay so out of control, particularly since the early 1990s? This suggests that something changed in the market for CEOs around that time that gave them more market power. How might that have worked?

Second paper

The second paper will be focused on the current financial crisis in the U.S. and around the world. Let me suggest a number of topics.

1. Describe the financial instruments involved in the financial crisis including mortgages, sub prime mortgages, mortgage backed securities, cdo, and cds. How was the crisis created by the production of these instruments?
2. Discuss how the banking industry became focused on the mortgage industry. Why did this happen? How did investment banks become more like commercial banks and savings and loan banks (and vice versa)? What was the role of the federal government and the government sponsored enterprises in this process?
3. Is there anything that the regulators could have done to prevent the crisis that eventually happened? If so, what? If not, why not?
4. Why did the U.S. mortgage crisis spread across the developed world? Why has the crisis been so slow to resolve itself?
5. What was the role of banks and consumers in the housing bubble? Do you think that one side or the other are to blame, or both? Should the government have done more to stop the crisis? If so, how were they going to overcome their 50 year support for home ownership in the U.S.?

### Writing Short Papers

In this class, I am asking you to write two short papers. Since many of you have had little experience formulating your own work, it is useful for me to provide some guidelines for these assignments. I am asking that you do this in three stages: a one paragraph description of what you want to do, a 1-2 page outline of your paper, and a final paper that will be 5-7 pages of double spaced text.

The first thing you need to decide to do, is to choose a topic. I have given you some ideas about potential topics in my other handout. Feel free to use these topics or to supply one of your own. You will discuss topics in Section with the GSIs and they will offer collective advice to guide the group. You should also feel free to go to office hours with the GSIs to ask them to help you focus your topic.

Writing a single paragraph about a potential topic is more difficult than you think. Such a paragraph should begin by proposing what your question is. This will require you to situate the question in some issue. The paragraph should begin by introducing the issue. Then it should turn to outlining what the various perspectives are on the issue. Finally, it could list the topics necessary to discuss in order to arrive at a conclusion. One way to get a good idea about your paragraph is that it should look like an abstract to a paper (go to the readings and you will find some abstracts). To the degree that you have a thesis that you will defend, that should be included in your paragraph. The paragraph should be no longer than 200 words.

The next assignment is an outline. An outline should focus on deciding the topics of the sections of the paper. So, all of your papers should contain a one or two paragraph introduction describing the issue and what you intend to do (a slightly longer version of the one paragraph which you have already written). Then, you should construct the main sections of the paper. What these will be, will depend on exactly what your topic is. You should tell us in your outline what the sections are and what the main points are. Then, the paper should have a conclusion. A 5-7 page paper will have 10-20 paragraphs. If two are in the introduction and one is the conclusion, then that leaves you with 7-17 for your main sections. One way to think of an outline is to think about what are the major points that each paragraph or set of paragraphs will try to make.

One question you might have is do you need to find other references besides the materials in the reader and books? It is certainly possible for you to use only the materials prepared for the class. I am happy to have you find additional materials if it makes sense for your topic. In such a short paper, I would discourage you from going out to find too much material. If you find

yourself citing more than five sources not in the readings, that probably means you have gone too far. If you are having problems with this, please speak to the GSIs.

The final paper should have the following format. I would like you to have your name, the class title, and a title for your paper at the top of the first page. I also ask that you use section headings like “Introduction” and “Conclusion” to separate the parts of the paper. Finally, you should cite sources in standard academic fashion. If you have a direct quote, end it with the name of the author, the year of the publication, and the page number of the quote in parentheses after the quote. If you are citing a source as an authority, put the name of the author and the year of the publication in parentheses at the end of the sentence. Here are some examples.

“The rain in Spain falls mainly on the plain” (Jones, 2011: 54).

The rain in Spain falls mainly on the plain (Jones, 2011). (Here, this is not a quote but a conclusion based on the text.)

Jones (2011: 54) says that the rain in Spain falls mainly on the plain.

I expect you to include a bibliography at the end of the paper that includes full citation to your sources. Your paper could have between 5 and 10 citations depending on the topic. The bibliography will not count against your 5-7 pages of text.

If you have any questions about the content of your paper or its format, please go to office hours or Section to ask your GSIs. If you are looking for more literature that they cannot help you on, please sign up for my office hours.