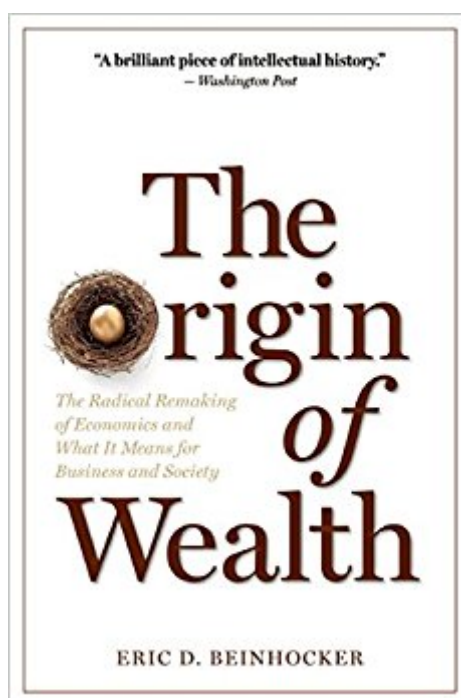


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# The Origin Of Wealth: The Radical Remaking Of Economics And What It Means For Business And Society



## Synopsis

Over 6.4 billion people participate in a \$36.5 trillion global economy, designed and overseen by no one. How did this marvel of self-organized complexity evolve? How is wealth created within this system? And how can wealth be increased for the benefit of individuals, businesses, and society? In *The Origin of Wealth*, Eric D. Beinhocker argues that modern science provides a radical perspective on these age-old questions, with far-reaching implications. According to Beinhocker, wealth creation is the product of a simple but profoundly powerful evolutionary formula: differentiate, select, and amplify. In this view, the economy is a "complex adaptive system" in which physical technologies, social technologies, and business designs continuously interact to create novel products, new ideas, and increasing wealth. Taking readers on an entertaining journey through economic history, from the Stone Age to modern economy, Beinhocker explores how "complexity economics" provides provocative insights on issues ranging from creating adaptive organizations to the evolutionary workings of stock markets to new perspectives on government policies. A landmark book that shatters conventional economic theory, *The Origin of Wealth* will rewire our thinking about how we came to be here--and where we are going.

## Book Information

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## Customer Reviews

Eric D. Beinhocker is a Senior Fellow at the McKinsey Global Institute. Fortune magazine named him a Business Leader of the Next Century, and his writings on business and economics have appeared in a variety of publications, including the Financial Times.

I can't recall having ever read an author with the clarity of exposition and the depth and breadth of erudition that is demonstrated by Dr. Beinhocker in this book. It is an impressive work. The opening sentence of the book asserts that "the field of economics is going through its most profound change in more than a hundred years." Since much of the book directly addresses and analyzes that change and its implications, I think the book could have more accurately been entitled *The Evolution of Economic Theory*. He notes "the two fundamental questions that economists have grappled with throughout the history of their field: how wealth is created and how wealth is allocated." Adam Smith in his *The Wealth of Nations* (published 1776) directly addressed both these questions and, with some elaboration by others, established the basic notions of the Classical Period of economic theory; most of these concepts are still accepted today. Adam Smith and his peers considered themselves philosophers, not scientists, and never attempted to reduce their ideas to mathematical expression. Roughly a century later Leon Walras wanted to change that, he wanted to make economics a science and to make quantitative economic predictions possible. So Walrus set about converting economic ideas into the language of mathematics. He devised a set of equations that represented the equilibrium of cleared markets. Production--how the stuff in the markets was created--was just assumed to have happened, and omitted from the representation. He made other simplifying assumptions. "Walrus's willingness to make trade-offs in realism for the sake of mathematical predictability would set a pattern followed by economists over the next century." Joseph Schumpeter, with his thinking undistorted by trying to produce numbers, brought forth an entirely different vision of how an economy functions, and emphasized the heretofore largely neglected production side of the economy. Schumpeter put entrepreneurship and technical change front and center as the primary source of productivity improvement and therefore wealth creation. He saw the economy as never in equilibrium, always in a state of dynamic change. Schumpeter's ideas were valid and persuasive, but his failure to put them into mathematics held them back from getting the affirmation they deserved. Most economists were still trying to describe economic phenomena in a mathematical language that was inadequate to the task, resulting in the need for simplifying but unrealistic assumptions. The three that stood out was, first, that people were always economically rational in their behavior, second, that the economic system was in equilibrium, and third, that innovation--both technical and behavioral (social) change--were not considered part of the system (considered to be exogenous variables). Robert Solow, a Harvard-trained professor at MIT, won the 1987 Nobel Prize by producing a model of a dynamic economy driven by technical change. [This whole history is a good illustration of "the rule of the tool": the idea when one possesses a tool there is a strong tendency to want to use it whether or not it is

really appropriate to the task at hand. The result is often that the task is modified to fit the tool. It is often illustrated by the observation that when you give a small boy a hammer is just turns out that nearly everything needs bashing. The transistor was invented in the 1940's. This technological discovery made the digital computer possible, and by the latter part of the century had put an entirely new tool in the hands of analysts, largely removing much of the pressure to modify the task to fit the tool.] The digital computer opened the door to new powers of analysis, and lessened the need for simplifying assumptions made to allow any quantitative analysis at all. The computer is capable of simulating most phenomena, providing versatility to quantitative analysis heretofore not available using conventional mathematics. Complex systems--systems in which the macro behavior emerges from the interaction of the fundamental agents--could be simulated and therefore studied. The economy is a prime example of a complex, adaptive system in which the fundamental agents are people and institutions that through their behavior and interaction produce the macro behavior of the total system. For the first time the goal of deriving macroeconomic behavior as an emergent property of microeconomic activity is in sight. Beinhocker discussed in depth the implications of these events, and provided substantially more color than this brief summary here. He discussed the properties of networks as they affect economic behavior, cognitive phenomena and the unreality of the rational man, and the dynamics of systems with feedback. He illuminated many of the ideas and implications of the economy as a complex system by describing actual computer simulations of various types. He notes that "Complexity Economics is still more of a research program than a single, synthesized theory . . ." These first two parts of the book focused on the evolution of economic theory. He also mixes in a kind of running tutorial on the terminology and often very surprising properties of complex systems. The third part addressed how evolution creates wealth. It begins with a description and illustration of the generic evolutionary process itself, including a fairly detailed presentation of the story of our biological evolution. He makes the point that the evolution of our economic system and creation of wealth are analogous processes. It seemed to me that while it is of some gee-whiz interest that the generalized patterns were the same, the specific mechanisms were so different that the fact of algorithmic or schematic similarity added very little real understanding of the economic process itself. He notes that economic evolution is driven by the coevolution of changes in physical technologies, social technologies--how people organize and set rules, and business plans--how people behave to exploit the technical and social innovations. The rest of the book is devoted to the detailed description and analysis of these three elements. It is very exhaustive, but at a high level of abstraction. For example, there is little or no discussion of the actual technological innovations in our history (except that of making stone tools, which is included

to make a point about the properties of invention). He examines all these phenomena from many different angles which I will make no attempt to summarize. Beinhocker is a master of inductive reasoning, going from the detailed reality to abstract patterns. His grasp of the consilience of the many dimensions of economic behavior is impressive, and the range of his interests and knowledge is downright astounding. I will admit that my reaction on my first reading of the initial chapters was negative: I thought he was painting a negative picture of past economic thinking with the intent of resurrecting it under new labels as new thinking. I was wrong, although I think much of old thinking has held up better than he seems to sometimes imply. But this profound book leaves little doubt that digital-computer-enabled Complexity Economics has and will open the window of our understanding of the creation of wealth very much wider than it has ever been.

One of the best books I've ever read. For me, it brought a lot of disparate observations into focus and provided a plausible and nearly universal explanatory model; e.g., evolution, self-organization & entropy, management in a high risk research environment, funding basic research, portfolio approach to project selection and management, top-down vs. bottom up initiatives, strategic vs. opportunistic approach to growth, philosophy of governance and its execution, etc., etc. etc. My only negative was the early denigration of the so-called "standard" approach to economics, which I always considered to be an evolutionary process, just like in any scientific endeavor; i.e., a work in progress in which there is a continuous flow of new data, which evokes an on-going stream of new insights, which are then integrated into its knowledge base.

I am absolutely crazy about this book. I'm really interested in the intersection of behavioral economics, evolutionary psychology, policy and traditional macroeconomic theory. In particular, I've always known something was unsatisfying about classical economic theory...but this book gives voice to an evidence based, full-throated critique of classical economics that really expanded my mind. It also contains some very specific insights about how to harness an evolutionary process in a company or in government in order to unleash innovation and productivity. Brilliant.

This book was fascinating to me and really led to my subsequent reading of, evolution of cooperation as well as various books on complexity and behavioural finance. I think it's always a measure of praise when a book induces an individual to go back and read the references versus just move on to the next book on the pile. For the unfamiliar (which was me) Beinhocker starts the book out with description of various computational models of simple economic systems that seem

almost trivial. The results are the emergence of complexity and patterns that are of extraordinary depth. The emergence of distributions of wealth from things like sugarworld are fruit for extended discussion as are the results of tit for tat results. These computational experiments that were collaborative efforts are still not fully acknowledged as of value to many economists, which continues to shock me, given the richness and patterns one can discern and associate with empirical results we see in the real world. The book continues with straightforward build up of feedback loops that are frequently encountered and fitness surfaces that we all march on. The issues of local and global peaks and the S curves of innovation that one can associate with the calculus of exploration on these imagined fitness surfaces are tackled clearly. In some sense the origin of wealth might be misleading, I read this book a while ago so I don't recall what my motivation was for buying it (I think I was looking for a more neo-classical economic commentary on economic growth), but the results are a fantastic overview of the emergence of complexity and the non-linear dynamical systems that we operate in. Books like this give strong insight into the arguments for multiple equilibrium and the non-linearities when perturbing initial conditions (which should serve as humbling evidence that luck is often why we end up where we do). This book takes a while to get through but is really a great starting point, whether anticipated or not, for looking at things differently. It opens up perspective on the evolution of what seem to be simple systems and remind us that if simple systems which resemble our societies have propensity to evolve like non-linear dynamical systems, the results of a more precisely defined computational system really can't follow equilibrium economics and math (frankly crisis and all we've been through recently should make that pretty intuitive). But this should be read by all who want to get a flavor of the complexity and behavioral aspects of modern economics.

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