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# Observations on a Conversation: Reply to Commentary

by Elena Esposito

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Zhuangzi and Hui Shi were roaming around and got to a bridge above the Hao River. "The minnows swim around so free and easy," said Zhuangzi, "that's how the fish are happy." Hui Shi said: "You are not a fish, whence do you know that the fish are happy?" Zhuangzi replied: "You aren't me, whence do you know that I don't know the fish are happy?"<sup>1</sup>

To observe observation, as we know, produces a lot of puzzles - not only when you disagree, but especially when you agree. The commentaries in this issue show it clearly. This is not surprising and not at all unwelcome, since the premise of the discussion is the mutual intrasparency of the perspectives involved. Intrasparency, however, should not be an obstacle for conversation, and here I will try to take it a step forward. Actually the debate shows how conversation can make this intrasparency productive, and even result in a different kind of insight – I am very grateful to all participants for it.

In different ways, all commentaries express the same criticism. The criticism actually relies on two types of correlated doubts: the first about the ability of observation theory to adequately deal with the blindness of observers, the second about the authentic specificity of second order observation.

That the observer presents "a certain blindness," we know at least since William James<sup>2</sup> - the point here is how and in which form he can be aware of it, and how theory can take this into account. Sarah Quinn describes convincingly the "systematic not seeing" of certain groups in financial markets, which is due not simply to the fact that "some elements fade away in the social distance", but much more radically to the fact that "systems of observation are systematically skewed" towards some interests and cannot or don't want to see others.<sup>3</sup> Flaminio Squazzoni notes that observers tend to

<sup>1</sup> Cited from A.C. Graham, *Chuang-Tzu. The Inner Chapters*. Indianapolis: Hackett, 2001, 123.

<sup>2</sup> "The spectator's judgment is sure to miss the root of the matter, and to possess no truth. The subject judged knows a part of the world of reality which the judging spectator fails to see, knows more while the spectator knows less" [James 1899, 114].

<sup>3</sup> Quinn's critique refers to the fact that Wall Street "chooses" not to see what it doesn't see.

drastically simplify their observational field, producing a systematic imperfection of observation. David Stark – with Yogi Berra – explicitly raises the issue of observation theory’s own blind spot, confronting it with the practices that traders consciously use to try to see their own blindness (reflexive modeling). Can observation theory deal with these phenomena?

The second objection concerns the distinction between first order observation and second order observation: are they really so different that the transition to second order can establish a different way to describe finance, its processes, and its relationship with society? What is empirically the difference? Stark asks, and it is a fundamental question, how and when second order observations are different from “multi-sided first order observations.” Squazzoni remarks that mutual observation happens regularly in markets, usually on the basis of prices (whose movements have primarily the function to allow investors to infer the orientation of other investors). Quinn asks on what social scientist can found their claim of "looking at more things" than the observed agents. When and why does the normal observation of the world and of the others become (also) a second order observation?

I will try to reply jointly to both objections, starting from the difference between the two observation orders. The difference can be expressed in a formula, as always a little oversimplified: first order observation is used to see things, second order observation is needed to see that one does not see. At the end of his work a second order observer doesn’t know more about the world, but should be able to move in the world in a more competent way.

Observing the world is the task of first order observation, and since a second-order observer is always also a first order observer the relationship with objects remains a prerequisite. Also a first-order observer knows very well that he is not alone. He knows that there are others who also observe the world and see things that he does not see, or see his same objects from another perspective. He also knows that their perspective can be relevant: first because he cannot see everything, and then because he can never be sure of not being wrong. A first-order observer observes others to learn more about the world – he realizes a "multi-sided first order observation" in order to arrive at a wider knowledge of the world, including what he sees *plus* what the others see. Ideal for this observer would be being able to take the perspective of the others in such a way as to integrate in his own image of the world what he would

This is a different problem – socially highly important but theoretically easier. If you choose not to see, somehow you have already seen, and then Wall Street can decide to “look up and in, instead of out and down” – with the very serious social consequences we all know. Here, though, the problem is the ineffectiveness of controls or the prevalence of private interests, not primarily the blindness of observers.

see if he were in their position (in space and in time). In this idealized world, traders would then be able to access the models of other traders (Stark). They could actually behave “as if” they were standing outside the market (Squazzoni).

As David Stark points out, this is impossible, because you cannot enter the head of someone else. Moreover, even if you could, you would find many assumptions you do not share or you don't understand (not everything the other sees is useful or interesting for me). You must then introduce many correctives (encodings and decodes, interpretations and attempts at understanding), which can be very complicated, but don't mark the transition to the second order.

Stark's “attention networks” are located at this level, and in fact he openly declares that they are guided by objects: the purpose of the construction is to articulate a “interobjectivity” that deals with the problem of mutual intrasparency of observation perspectives. I cannot get into the head of the other and I can access his observation only indirectly: through what he tells me, through the traces he leaves (the spread plot), through the objects he observes (the ticker) or also observing the objects he or others close to him were attentive to. But I am always using the perspective of the others to expand my knowledge of the world, bridging gaps or correcting errors.

Second-order observation, on the other hand, is as we know observation of observers. What does it mean, if the other is by definition inaccessible? The point here is that there is no need of the other to be accessible, the enigma is only apparent. Intrasparency cannot be overcome, but there is no need to overcome it in order to get to a more complex and articulated form of observation. The observer does not see someone else's observation, but can observe it – obviously always from his perspective and according to his categories (and with his blindness). Second order observation is no access to an alien world, it is an articulation of one's own world. What one faces is not the outside world by itself, but how this outside is seen from within. In terms of systems theory: what the system accesses is not the environment “as it is” (a kind of autonomous truth) but always its hetero-reference, the way the system sees the environment - what is outside the system. Referring to observers: the observer does not see what others think, only what he can imagine that others think – which can be more or less different from what he himself thinks (and this can happen in many different forms).

This is however not a small difference. It indeed changes the whole sense of observation, entering a new quality of variety and complexity – above and beyond dissonance. You don't need to be in disagreement to be different – you are different even when you resonate, when you say the same or look at the same object, because your motives, categories and interests will inevitably be different. If I understand it,

my world will be enormously more complex, even if it remains closed and idiosyncratic as the one of first order observers.

Second-order observation, as we said before, is not needed to see more, but to see that you do not see, i.e. to see blindness (your own blindness and the blindness of others). As von Foerster says: “If I *don't see* I am *blind*, I am *blind*; but if I *see* I am *blind*, I *see*” [1981, 290]. What do I see? Obviously not the world through the eyes of the others, which is still inaccessible. I always see only what I see, and don't see what I don't see. But I learn to better manage my actions and relationship with others, I'm better able to obtain information, and different information, from the stimuli I receive, I can transform my lack of information into a different source of information. I can for example learn to differently process acoustic stimuli and information that come from the others, and build a way of orientation which needs less images. An aware blind man can move around the world with great competence, precisely because he is and remains blind.

The same happens in the relationship with others: instead of regarding the inaccessibility of the perspective of the others as a limitation, I can start to consider it as an advantage. I won't try then to translate it more or less imperfectly into my perspective (looking for an identity), but I will use the increased complexity deriving from the fact that it is and remains different, in a form that can provide me with information (always and only in my categories, always and only within my perspective – using the difference).

The curious form of “interobjectivity” provided by ratings is located at this level – and is independent of the fact that their assessments are correct or not, or that the observers deem them to be correct.<sup>4</sup> I can even think that ratings are wrong and know that the others think the same, but if I want to competently work in finance I must continue to observe them and to draw information from them - not in order to know how the world is, but in order to observe what the others (in their own way) observe.<sup>5</sup>

What does it mean on a more concrete level? Let's take reflexive modeling. As Beunza and Stark [2012] show, the trader who practices it sees to some extent his own blindness. In Wittgenstein's words: “the idea [...] is like a pair of glasses on our nose through which we see whatever we look at. It never occurs to us to take them off” [2001, 103] – at most, as wary traders, one can try to see what one sees with the

<sup>4</sup> Sarah Quinn very rightly reminds us of the unilateral selectivity of ratings.

<sup>5</sup> A very different condition from the “as-if-outside” attitude described by Flaminio Squazzoni. The observer is completely and consciously inside the observed world – so much that he even exploits this position to get information. In the much discussed Paulson's case, his advantage would have been not simply looking at what the others see (and act differently), but acting on what they see (and look at what happens).

different glasses used by others. One remains at the level of first-order observation, which works until a case of resonance occurs, where the mutual short-sightedness of traders does not cancel out each other but add up, leading to a condition of general blindness, which the observer can no way control.

The reflexivity of second-order observation, though, would suggest a different approach: to try to take the glasses off and check if you can see something different. Presumably you will be more careful to where you go and how you move, will trigger other sensors (hearing, touch), will communicate with others on other channels. You will access then a different and more radical “diversity of viewpoints,” that does lead not only to correct one’s errors by integrating the perspective of others, but to correct the very claim to be able to see, integrating it with the knowledge of one’s own blindness: a sort of diversity from view itself. It would mean not trying to correct one’s own models supplementing them with other models (as far as you can know them), but reflecting on the use of models itself and on their consequences: on view in general and on other points of reference.

This would be a different kind of reflexivity, in which catastrophic resonance effects become much less likely – and complexity much higher. One could reflect for example on model risk and unintended consequences (such as moral hazard): the “extreme events” mentioned by Squazzoni would not appear as surprises but rather as effects of the widespread use of formalized models.<sup>6</sup> Or one could reflect on the way in which the use of models not only affects what you see of the world, but also changes the world itself that you are observing. Such a trader would be able (in Quinn’s image) to look “out and down” at the consequences of his action on people and society. Of course he could never predict what’s going to happen nor what these consequences will actually be, but he could process more information – giving up with no regret the hope to see everything.

According with this attitude, reflexive blindness reflects on itself and produces a different kind of insight, whose reference is not a supposed world outside but the way the others observe. The one who observes better (not necessarily “more” – more than what?) is not the one who sees more things, but the one who is able to adopt more distinct possibly incomparable perspectives. The observation of the blind spot is not the point of arrival but a starting point. Stark is right: a conversation is better than an observation. Or in other words: only communication, not an isolated individual, can realize a really complex observation, where several blindness “irritate” each other.<sup>7</sup>

<sup>6</sup> A typical case in which first-order reference to the world cannot explain what’s going on: these events are and remain so highly unlikely (less than 1 on 1050) that their occurrence is practically impossible – but nevertheless they happen.

<sup>7</sup> The concept of “double contingency” [Luhmann 1984, 148 ff.] expresses this condition.

This holds, and it could not be otherwise, for observation theory itself, which also has its own blind spot and does not overcome it by being aware of it. It can see its own blindness but this doesn't remove it – it simply moves the blind spot to a different level, producing a new blindness it cannot see. This is not a flaw but an inevitable condition one could learn to exploit [Esposito 1992]. It is exploited for example in a conversation like the one presented in this issue of *Sociologica*, which among other things reflexively shows what second order observation could "watch" (Yogi Berra): watch how people outside finance observe how finance observes itself (Sarah Quinn), how economic agents (often knowingly) simplify the complexity of observation (Flaminio Squazzoni), how traders know that they don't know (David Stark). Therefore I wish to thank again the authors who contributed to this conversation in such a productive way.

But there is another blindness that this debate highlighted, which concerns the sociological observation of finance itself. Our debate referred to the figure of Keynesian beauty contest, that for many decades had great success in describing mutual observation in the financial world [Hertz 2000]. But if you reflect on the beauty contest starting from our discussion, you can see that the situation is more complicated – I didn't see it before this conversation.

David Stark<sup>8</sup> remarked quite rightly that in Keynes' strange beauty contest - and in the original situation of finance as well - you don't really understand who wins and what it means to win. If you refer literally to Keynes competition, the jurors are at the same time the real contestants (not the girls, they count for nothing). As observation theory maintains, it is never possible to observe finance from outside. Is the winner the one who guesses how the others vote, hence votes like them? But he is also a juror: he must observe the others, who in turn try to guess how he votes, who votes as they vote. Then if one wins they all win (actually very little), and there is no real winner. But most likely no one wins, because no one knows how to vote. What kind of contest is this?

Actually finance never puts on stage a specific contest like this. Traders are never in an authentic situation of Keynesian beauty contest (nor in a pure situation of second order observation<sup>9</sup>): finance is already in progress, things happen and are observed in order to decide what to do. And there is no single winner; some gain and others lose money. To reason on an abstract Keynesian beauty contest does not make much sense: the contest does not exist as a competition with a possible winner.

<sup>8</sup> On the occasion of a very inspiring seminar at Copenhagen Business School on May 27, 2013.

<sup>9</sup> Or of double contingency.

Nevertheless the debate on it goes on since many decades. As in all cases of patently nonsensical questions, the fact that they are discussed seriously when there can be no solution leads to shift attention to the observer. How is it that a clearly absurd model has been used for decades as a metaphor of the functioning of financial markets? What does this show about the implicit assumptions of the theory of finance, and possibly about the blindness of observation theory itself? The work on these issues must still be done: “it ain’t over ’til it’s over.”

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Abstract: The very productive debate in *Sociologica* shows that second-order observation is not needed to see more, but to see that one does not see, i.e. to see blindness. Reflexive blindness reflects on itself and produces a different kind of insight, whose reference is not a supposed world outside but the way observers observe.

The debate highlights not only the blindness of finance, but also a certain blindness of the sociological observation of finance and even the blindness of observation theory itself. To see it can become an advantage, if inserted in an ongoing conversation.

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*Keywords: second-order observation, blindness, reflexivity, conversation, modeling*

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