

# Institutional economics

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# The « institutional turn » in social sciences

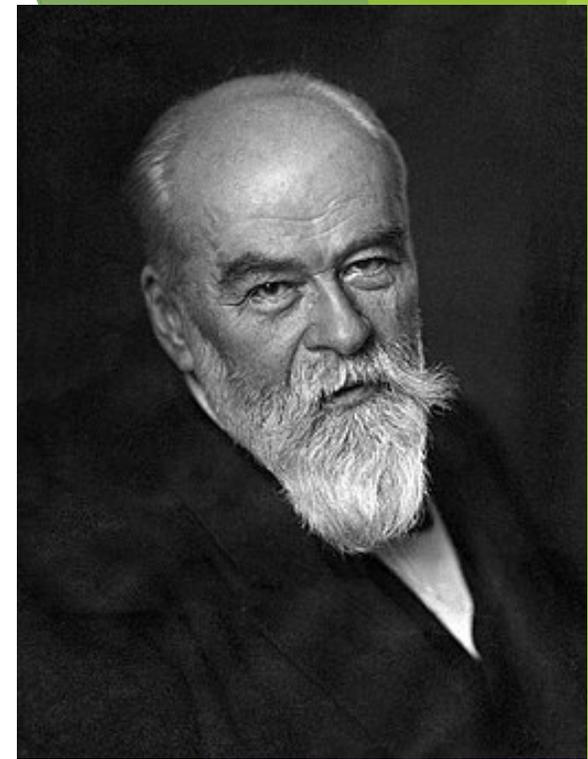
- ▶ Politics
- ▶ Sociology
- ▶ History
- ▶ Geography
- ▶ And... Economics

# A field with a contrasted history

- ▶ Original American « Institutional economics » (1900-1940), influential in the US
- ▶ ... marginalized by the dominance of neoclassical theory (1940-1980)
- ▶ Until the fast development of « New institutional economics » since the 1980s
- ▶ In parallel with the modernization of the tradition of « old » institutional economics, specially in Europe

# The German historical school

- ▶ “Institutions, of a political, legal or economic nature” form “a framework or mould for the action of successive generations”
- ▶ Institutions : **“a set of habits and rules of morals, custom and law... which are consistent with each other and which constitute a system”**
- ▶ Examples : property, slavery, serfdom, marriage, the market, money, industrial freedom
- ▶ Organs : personal aspect of institutions; marriage is the institution, family is the organ
- ▶ Associations, corporations, communes, firms, the State - are organs, i.e. organizations



Gustav  
von Schmoller  
(1838-1917)

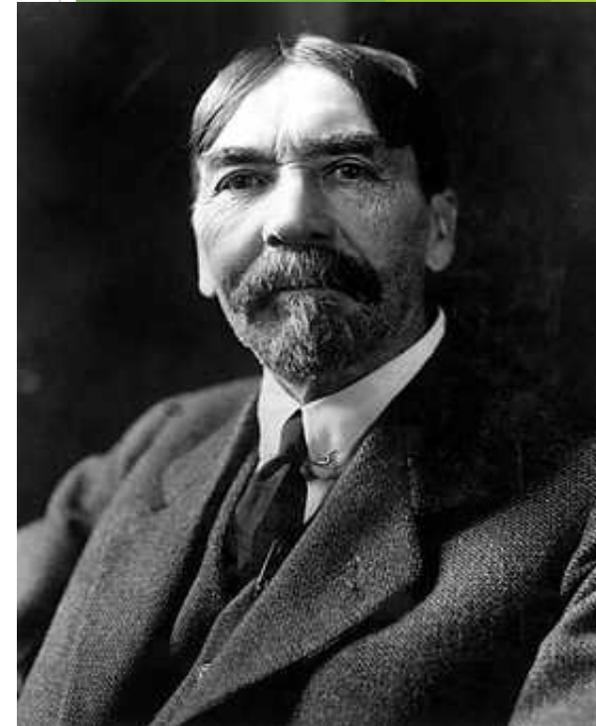
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# Original American Institutional Economics

# Veblen: an evolutionary institutionalism

- ▶ A critique of « neo-classical economics »: its teleological bias, and its neglect of the role of institutions
- ▶ Economics should become an evolutionary science, concerned with the change of institutions
- ▶ Institutions are *prevalent habits of thought and action*, inherited from the past and never in full accord with the requirements of the present
- ▶ A tension between the change of technology and the inertia of institutions
- ▶ “A theory of a process, of an unfolding sequence” (vs equilibrium approach)
- ▶ Cumulative causation: cause → effect

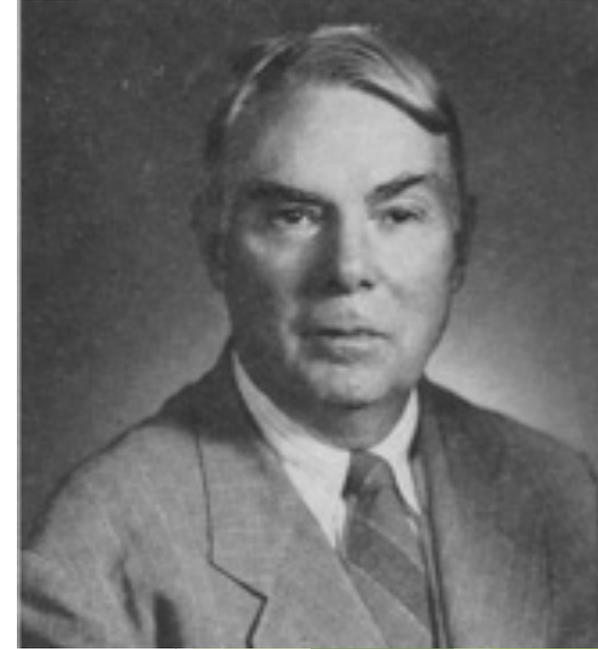
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Thorstein  
Veblen  
(1857-1929)

# Institutions: a veblenian view

- ▶ Centrality and ambiguity of institutions in history
- ▶ Institutions constitute factors of order but also possibly disorder
- ▶ They embody knowledge but also ignorance
- ▶ They are subject to
  - ▶ Historical drift
  - ▶ Conversion
  - ▶ Forgetfulness of origins



Walton  
Hamilton  
(1881-1958)

# Commons: an organizational theory of institutions

- ▶ The institution is ‘collective action in restraint, liberation, and expansion of individual action’, or ‘collective action in control of individual action’
- ▶ Going concerns and their working rules compose institutions
- ▶ Society is made of a great number of going concerns (the family, the corporation, the trade union, the trade association, the state)
- ▶ Three types of “transactions”, managerial, bargaining, rationing
- ▶ The “common law method”: legitimate authorities decide conflicts, forming the working rules (for the time being) of a given concern
- ▶ Futurity : individuals act in the present institutions on the basis of their views of the future
- ▶ Search for a “reasonable capitalism”

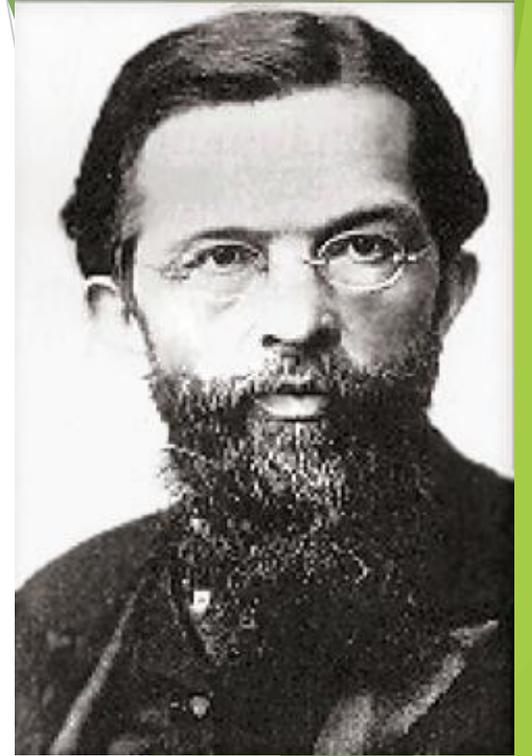


John Commons  
(1862-1945)

# The Austrian school

# Menger: pragmatic and organic institutions

- ▶ Two types of institutions : the first of deliberate, ‘pragmatic’ origin, the second of spontaneous, ‘organic’ origin
- ▶ Organic institutions: money, law, language, markets, communities, the state
- ▶ Individuals strive for personal interest, follow certain rules, others imitate them if they meet success; the unintended result is organic institutions
- ▶ A combination of methodological individualism and of Adam Smith’s « invisible hand »



Carl Menger  
(1840-1921)

# Hayek: two classes of orders



Friedrich Hayek  
(1899-1990)

	Organizations	Spontaneous orders
Type of order	Simple, « made »	Complex, evolved
Direction	Yes	No
Objectives	Yes	No
Rules	Finalized	Non finalized (eg law)
Coordination	Deliberate	Unconscious, unplanned

Spontaneous orders: society, the market

The major error of socialism or of « constructivist » views: to deal with spontaneous complex orders as if they were organizations

# Cultural evolution

- ▶ A process of selection which is neither natural nor artificial
- ▶ Rules are initially individual innovations, when adopted by larger groups they lead to distinct cultural traditions
- ▶ They spread through imitation and group selection (decline or absorption)
- ▶ Rules that are more beneficial to the global spontaneous order survive and take root
- ▶ Praise of the British common law model

# Critics of Hayek

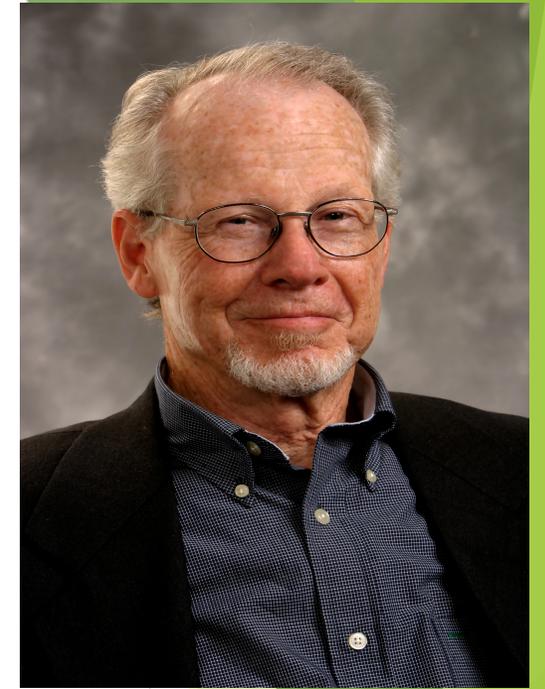
- ▶ Dichotomous model of orders
- ▶ Romantic anglophilia
- ▶ Ignorance of the interdependence between capitalism and socialism (Schumpeter, 1946)
- ▶ Tensions between political and economic liberalism

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# New Institutional Economics

# Williamson: Transaction costs economics

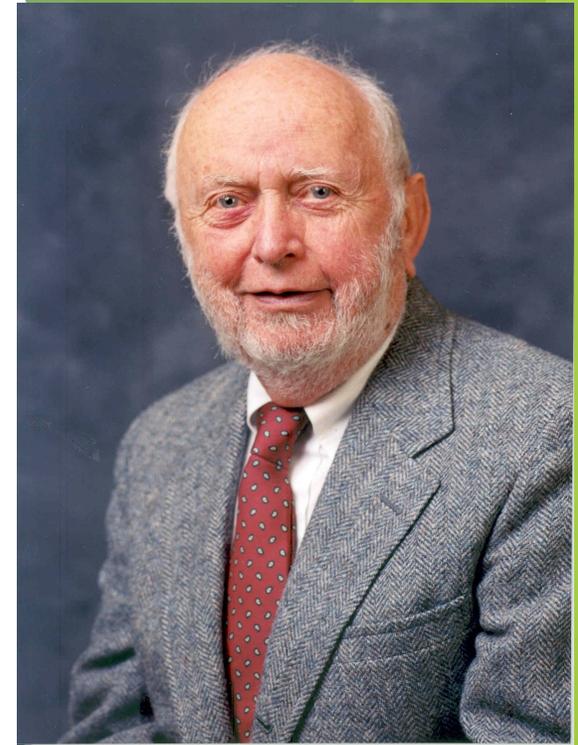
- ▶ Complementary to orthodoxy
- ▶ Inspired by Coase, « The nature of the firm », 1937
- ▶ « New institutional economics » 1975
- ▶ Mains institutions of capitalism: the market, the hierarchy (the firm), hybrids
- ▶ An efficiency approach: the choice between governance modes results from economizing on transaction costs



Oliver Williamson  
(b. 1932)

# North: the rules of the (economic) game

- ▶ Institutions
  - ▶ formal constraints (rules, laws, constitutions)
  - ▶ informal constraints (norms of behaviour, conventions, and self imposed codes of conduct)
  - ▶ and their enforcement characteristics
- ▶ Institutions are “rules of the game”, organizations are the players
- ▶ Holders of power determine formal institutions, which are not based on efficiency
- ▶ Institutional change is essentially gradual; formal rules may be changed fast, but not informal rules; transfer or imitation of institution is not a sufficient condition for good economic performance



**Douglass North  
(1920-2015)**

Mental models and ideologies  
(beliefs)



**Institutional framework** of polity and economy



Incentive structure



Organizations



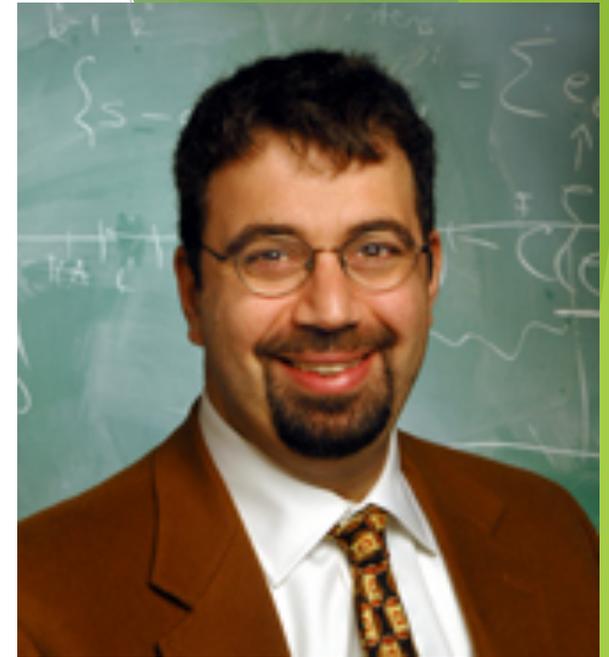
Policies



Performance

# Acemoglu: institutions as the key to economic success

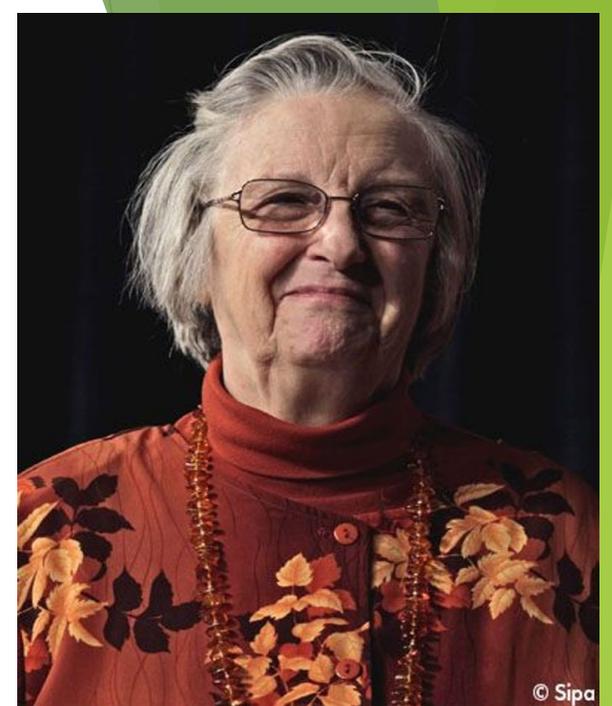
- ▶ Extractive vs inclusive institutions
- ▶ **Inclusive institutions** include secure property rights, law and order, state support for markets; free entry of new businesses; « level playing field », they are linked to political democracy
- ▶ **Extractive institutions in favor of elites** are obstacles to long-term growth
- ▶ Influence of political institutions on economic institutions (vs the « culture » explanation)



Daron  
Acemoglu  
(b. 1967)

# Ostrom : diversity of institutional arrangements

- ▶ Complex and polycentric systems
- ▶ Institutional diversity
- ▶ 3 levels of rules: the operational level, the collective-choice level, and the “constitutional” level
- ▶ Commons’ influence → Rules : understandings by actors of *enforced* prescriptions concerning what actions are *required, prohibited, or permitted*
- ▶ Analysis of common-pool resources: numerous collective institutional arrangements that disprove the « tragedy of the commons »
- ▶ Against institutional panaceas



Elinor Ostrom  
(1933-2012)

# Neoliberal radicalization : « quality of institutions » (2000s)

- ▶ « Good institutions » characteristic of the anglo-american model of capitalism, « bad institutions » typical of other models
- ▶ Good institutions : economic freedom, private property, rule of law, clearly delineated property rights, flexible labor market, shareholder oriented corporate governance
- ▶ Econometric studies : institutional quality/growth
- ▶ Diverting the institutional turn in a neoliberal perspective

# Controversy over neoliberal institutionalism

- ▶ World Bank and the IMF (with their conditionalities), and the OECD, the G7, the World Economic Forum, promoted the adoption of such « good institutions » of the neoliberal model
- ▶ World Bank « Doing Business » Reports
- ▶ But « Global standard institutions » favour the rich over the poor, capital over labour, and finance capital over industrial capital (Chang 2011)
- ▶ « Good institutions → Development » : ignores the reverse causality « Development → Institutional improvement »

# European heterodox institutionalisms

# The French Régulation school

- ▶ Five institutional forms of the fundamental capitalist relations:
  - ▶ Monetary and financial regime
  - ▶ The wage-labour nexus
  - ▶ Forms of competition
  - ▶ Insertion into the international regime
  - ▶ Forms of the State
- ▶ Diversity of capitalisms: eg Amable 2003
  - ▶ Market-based capitalism
  - ▶ Social democratic capitalism
  - ▶ Asian capitalism
  - ▶ Continental European capitalism
  - ▶ South European capitalism

Robert  
Boyer  
(b. 1943)



# The nature of institutions

- ▶ ‘Institutionalized compromises’ between social groups in conflict
- ▶ The emergence of new institutions often follows crises, conflicts or wars, it takes place mainly in the framework of the nation state
- ▶ Imitated or imported institutions are generally transformed in the process : hybridization
- ▶ **Complementarity**, and **hierarchy** of institutions (eg dominance of the wage-labour nexus in Fordism, dominance of the monetary and financial regime in contemporary neo-liberal capitalisms)

# Accumulation regime, mode of régulation

- ▶ The *accumulation regime* corresponds to a pattern of regular growth
- ▶ The *mode of regulation* represents the process of maintaining through time the relative stability of a contradictory system through fluctuations and negative feedbacks
- ▶ Recursive causality between the institutional framework and the modalities of economic growth : institutionalized compromises shape accumulation regimes, but *structural crises* are generally overcome through the restructuring of institutional forms
- ▶ Question of *viability* of an institutional configuration, rather than one-dimensional “performance” (growth)

# Hodgson and the revival of original institutionalism

- ▶ Institutions are systems of established and embedded social rules that structure social interactions
- ▶ Rules are socially transmitted and customary injunctions that « in circumstances X do Y »
- ▶ Organizations are special institutions that involve
  - ▶ (a) boundaries and a distinction between members and non-members
  - ▶ (b) principles of sovereignty concerning who is in charge
  - ▶ (c) chains of command
- ▶ Actor and institutional structure, although distinct, are connected in a circle of mutual interaction and interdependence.



Geoff Hodgson  
(b. 1946)

# From a darwinist approach to legal institutionalism

- ▶ Evolutionary institutionalism: the three main principles put forward by Darwin - variation, inheritance and selection – hold for institutions
- ▶ Legal institutionalism : the fundamental role of law in the institutional setup
- ▶ Capitalism, property, money, markets, and corporations depend on, and are partly constituted by, the state
- ▶ Property is an essential institution, but the theory of property rights deals neither with property (only with possession) nor on rights (it underestimates legal titles sanctioned by the state)

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To conclude

# Common theses in different theories of institutional economics

- ▶ Institutions, and history, matter for understanding the economy
- ▶ Institutions determine the economic system, and influence economic development and growth
- ▶ The neoclassical tradition is unsuitable to approach the question of institutions
- ▶ The problem of *change* is central, different temporalities of change intersect
- ▶ A *process* view is favoured over an *equilibrium* approach
- ▶ Cumulative causality or path dependency are at work
- ▶ *Emergence* - new forms or new processes result from lower levels interactions
- ▶ A positive relation to other social sciences

# A remarkable diversity

- ▶ Differences between Original IE and New IE, and diversity within both groups of theories
- ▶ Methodological individualism vs holism in methodology (but also opposition to such dichotomy)
- ▶ Doctrinal stances in relation to economic liberalism: from a radical critique (German historicism, Régulation theory) to a resolute defense (Austrian school)
- ▶ Preferred social science for interaction: history, sociology, political science,...

# Theoretical and doctrinal differences

- ▶ Analysis focused on institutions established top-down, in a deliberate fashion, or bottom-up, through spontaneous evolution
- ▶ The focus may be on formal or informal institutions
- ▶ The general perspective may be the reform of existing institutions, or their conservation
- ▶ It may be motivated by a critique of capitalism (Veblen) or of socialism (Hayek)
- ▶ Diverse views of human psychology and behavior may be mobilized
- ▶ Various specific institutions may constitute the model for a general theory of institutions: money, the state, law, property, the market, the firm...

# Institutional economics remains a large and diverse family

- ▶ This family includes many differences found in economics in general, some of which are profound
- ▶ However there are many examples of coming closer or overlapping between different theories in that family
- ▶ Debates and controversies between different institutionalist theories contribute to reduce their incomplete character, but does not lead to convergence
- ▶ Differences in institutionalist theories do not exclude elements of complementarity
- ▶ The captivating field of institutional economics is largely open to future developments and new insights

Muchas gracias !