

INSTITUTIONAL ECONOMICS

Ag and Applied Economics/Economics 707

Daniel W. Bromley
Spring 2007

My purpose here is to help you develop an understanding of the institutional foundations of an economy. Much of advanced work in economics concerns the study of economizing and economizing behavior, while little of it concerns the extent to which an economy is socially constructed. The economy is not some magical and spontaneous entity created by divine inspiration with the goal of producing efficient allocations and happy people. Rather, the economy is built up from the convergence of three imperatives: (1) the need for collective rules of conduct arising from conflicts of interest, driven by scarcity, and enforced by the moral sanctions of collective opinion; (2) the need for rules of conduct arising from conflicts of interest, driven by scarcity, and enforced by the organized sanctions of state-sponsored coercion; and (3) the need for rules of conduct arising from conflicts of interest, driven by scarcity, and enforced by the accounting logic of profit and loss. In other words, the economy is the social realm in which ethics, jurisprudence, and economizing meet. The economy is always in the process of becoming. Here we learn about how that process works.

One understands the economy by understanding its ethical, legal, and economizing components. Institutional economics starts from the view that economizing behavior by individuals and firms is but a mechanistic facet of the more complex structure that gives rise to constellations of costs and benefits which inform that behavior. One cannot understand the economy by studying economizing behavior. One can only understand the economy by seeing that economizing behavior is grounded on prior ethical choices embodied in legislation, administrative rules, and jurisprudential decrees. Because there are an infinity of Pareto optimal outcomes—one for each possible structure of endowments and institutional arrangements—the efficiency doctrine of neoclassical economics is entirely self-referential and without recommendatory credibility as against other norms of individual or collective action—Kantian obligation, procedural transparency, equity (or Rawlsian justice).

Because economics is a policy science, it is important that one gain an understanding of the epistemological basis for policy prescriptions advanced by economists. And because economics is an empirical science, it is essential that the three classes of claims advanced by economists—descriptions, predictions, prescriptions—be capable of empirical testing. Many prescriptive assertions are predicated on a flawed application of deduction—a method of analysis that often fails to offer clear explanations for observed economic outcomes. Under deduction, one usually encounters not explanation but rather justification of (and a rationalization for) those outcomes that appear to be consistent with the circular concept of efficiency. The central concern here will be to gain an understanding of how applied economists come by the beliefs and assertions that they advance as truth claims about what is best to do (“optimal” or “efficient”) in the policy arena. We will see that all public policy is

nothing but institutional change. With that in mind, we will explore the “new” institutional economics and will contrast its reliance on the circular concept of efficiency with classical institutional economics. This classical approach to the study of economic institutions will draw, in the main, on the approach of John R. Commons—an approach that stresses the legal foundations of capitalism, reasonable valuing, prospective volition, and the pragmatic evaluation of truth.

My book, **Sufficient Reason: Volitional Pragmatism and the Meaning of Economic Institutions**, provides the primary conceptual grounding for the course. Other required readings are presented as elaborations of points made in **Sufficient Reason**.

II. EXPECTATIONS

Each class period will have one (rarely two) required reading(s) (indicated by *). The other readings are optional. Students will be assigned the responsibility of opening each class by offering a 10-15 minute exegetical account of the required reading for that period. These assignments will be made in advance. If there are two readings required for a period, two assignments will be made. The purpose of these opening comments is to launch us into a coherent discussion for that class period.

In addition, there will be 10-12 **gobbets** over the course of the semester. These writing opportunities entail the careful response to—or elaboration of—a question or statement. There is a one-page maximum length to the gobbets. The average score for the gobbets will comprise 40 percent of your grade.

You will write a **research paper** of not more than 15 pages in length. The specifics of the research paper will be spelled out in class. The paper will count for 60 percent of your grade. The research paper is due in class, Wednesday, May 2nd.

My book **Sufficient Reason** is for sale at the University Bookstore. To avoid any appearance of profiting by having you buy my book, I will donate \$5 to the Taylor-Hibbard Club for each book purchased.

In addition, a reading packet is available at Pigwick Papers, 1401 University Avenue.

COURSE OUTLINE

SR = SUFFICIENT REASON: Volitional Pragmatism and the Meaning of Economic Institutions

I. INTRODUCTION

Monday, January 22:

- *SR: Chapter 1: Prospective Volition
- Robbins: An Essay on the Nature and Significance of Economic Science

Wednesday, January 24:

- *Philp, et al.: Preferences, Power, and the Determination of Working Hours
- Bowles: Endogenous Preferences
- Dwyer: the Alleged Value Neutrality of Economics
- Pollak: For Better or Worse
- Sen: Rational Fools
- Sen: Rationality and Social Choice

Friday, January 26:

- *SR: Chapter 2: The Task At Hand
- Cooter and Rappoport: Were the Ordinalists Wrong?
- Rabin: Psychology and Economics
- Ramstad: Is a Transaction a Transaction?
- Simon: Rationality in Psychology and Economics
- Veblen: The Limitations of Marginal Utility

Monday, January 29:

- *Rutherford: Institutional Economics Then and Now
- Hodgson: The Approach of Institutional Economics
- Mayhew: The Beginnings of Institutionalism

II. ON ECONOMIC INSTITUTIONS

Wednesday, January 31:

- *SR: Chapter 3: Understanding Institutions
- Hallowell: The Nature and Function of Property
- Putterman: The Firm as Association vs. The Firm as Commodity
- Schmid: Legal Foundations of the Market
- Simon: Organizations and Markets
- Sugden: Spontaneous Order
- Wilkins: The Neglected Intangible Asset

NO CLASS UNTIL February 14th.

Wednesday, February 14:

- *North: Institutions
- Ben-Porath: The F-Connection
- Bromley: Markets
- Coase: The Nature of the Firm
- Neale: Institutions
- Sen: Markets and Freedom

Friday, February 16:

- *SR: Chapter 4: The Content of Institutions
- Coase: The Problem of Social Cost
- Hodgson: Economics and Institutions
- Kronman: Contract Law and the State of Nature

Monday, February 19:

- *Hall and Taylor: Political Science and the Three New Institutionalisms
- *Parto: Economic Activity and Institutions: Taking Stock
- Samuels: The Coase Theorem and the Study of Law and Economics
- Samuels: The Legal-Economic Nexus
- Samuels: The Relation Between Legal and Economic Processes

Wednesday, February 21:

- *SR: Chapter 5: Institutional Change
- Nelson and Sampat: Making Sense of Institutions in Economic Performance
- Rutherford: The Old and the New Institutionalism

Monday, February 26:

- *Ramstad: The Institutionalism of John R. Commons: Theoretical Foundations of a Volitional Economics
- Rutherford: J.R. Commons' Institutional Economics
- Whalen: John R. Commons' Institutional Economics: A Re-Examination

III. VOLITIONAL PRAGMATISM

Wednesday, February 28:

- *SR: Chapter 6: Fixing Belief
- Hoover: Pragmatism, Pragmaticism, and Economic Method
- Ramstad: A Pragmatist's Quest for Holistic Knowledge
- Stone: Causal Stories and the Formation of Policy Agendas

Monday, March 5:

- *McCloskey: The Rhetoric of Economics
- Putnam: The Empiricist Background
- Putnam: The Entanglement of Fact and Value
- Putnam: Fact and Value in the World of Amartya Sen

Wednesday, March 7:

*SR: Chapter 7: Explaining
Field: On the Explanation of Rules Using Rational Choice Models
Field: The Problem with Neoclassical Institutional Economics
Ostrom: Collective Action and the Evolution of Social Norms

Monday, March 12:

*Stewart: Instrumental Reasoning in Economics
Fiori: Alternative Visions of Change in Douglass North's New Institutionalism
Kuhn: Objectivity, Value Judgment, and Theory Choice
Mirowski: The Philosophical Bases of Institutional Economics
Webb: Dewey: Back to the Future
Weston: Toward a Better Understanding of the Positive/Normative Distinction

Wednesday, March 14:

*SR: Chapter 8: Prescribing and Predicting
Bromley: Economic Interests and Institutions
Bromley: Ideology of Efficiency
Mishan: How Valid are Economic Evaluations of Allocative Changes?
Mishan: The Folklore of the Market

Monday, March 19:

*Olson: Why Some Nations are Rich and Others Poor
Saraydar: The Conflation of Productivity and Efficiency in Economics
Stiglitz: Whither Reform?

Wednesday, March 21:

*SR: Chapter 9: Volitional Pragmatism
Mandelbaum: Purpose and Necessity in Social Theory

Monday, March 26:

*Commons: Institutional Economics
Biddle: Purpose and Evolution
Chasse: John R. Commons and the Democratic State

IV. VOLITIONAL PRAGMATISM AT WORK

Wednesday, March 28:

*SR: Chapter 10: Thinking as a Pragmatist
*Posner: A Pragmatist Manifesto

SPRING BREAK

Monday, April 9:

*Ramstad: John R. Commons' Reasonable Value

Tribe: Policy Science: Analysis or Ideology?
Tversky and Kahneman: Rational Choice and the Framing of Decisions

Wednesday, April 11:

*SR: Chapter 11: Volitional Pragmatism and Explanation
Nelson and Winter: An Evolutionary Theory of Economic Change

Monday, April 16:

*SR: Chapter 12: Volitional Pragmatism and the Evolution of Institutions
Dahlman: The Problem of Externality
Drury: Locke and Nozick on Property
Sax: Some Thoughts on the Decline of Private Property

Wednesday, April 18:

*Lin: The Needham Puzzle: Why the Industrial Revolution did not Originate in China
Burawoy: The State and Economic Involution

Monday, April 23:

*Kuran: Why the Middle East is Economically Underdeveloped
Bromley: Reconstituting Economic Systems
Hurst: Law and Markets in United States History
Yousif: Development Growth and Policy Reform in the Middle East & North Africa

No class April 25

Monday, April 30:

*SR: Chapter 13: Volitional Pragmatism and Economic Regulations
Bromley: Regulatory Takings
Bromley: Constitutional Political Economy
Williams: Kant's Concept of Property

Wednesday, May 2:

*SR: Chapter 14: Sufficient Reason
Johannson-Stenman: On the Problematic Link Between Ethics and Economic Policy
Vatn and Bromley: Choices Without Prices Without Apologies

Monday, May 7:

Research Reports

Wednesday, May 9:

Research Reports

BIBLIOGRAPHY

Required readings are marked with *. The other readings are here for your reference.

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Biddle, Jeff E. "Purpose and Evolution in Commons's Institutionalism," History of Political Economy 22(1):19-47, 1990.

Bowles, Samuel, "Endogenous Preferences: The Cultural Consequences of Markets and other Economic Institutions," Journal of Economic Literature 36:75-111, March 1998.

*Bromley, Daniel W. Sufficient Reason: Volitional Pragmatism and the Meaning of Economic Institutions, Princeton: Princeton University Press, 2006.

Bromley, Daniel W., Economic Interests and Institutions: The Conceptual Foundations of Public Policy Oxford: Basil Blackwell, 1989.

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Burawoy, Michael, "The State and Economic Involution: Russia Through a China Lens," World Development 24(6):1105-1117, 1996.

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*Commons, John R. "Institutional Economics," American Economic Review 21:648-57, December 1931.

- Cooter, Robert and Peter Rappoport, "Were the Ordinalists Wrong about Welfare Economics?" Journal of Economic Literature 22:507-30, June 1984.
- Dahlman, Carl J., "The Problem of Externality," Journal of Law and Economics 22:141-162, April 1979.
- Drury, S. B., "Locke and Nozick on Property," Policy Studies 30:28-41, 1981.
- Dwyer, Larry, "The Alleged Value Neutrality of Economics: An Alternative View," Journal of Economic Issues 16:75-106, 1982.
- Field, Alexander J., "On the Explanation of Rules Using Rational Choice Models," Journal of Economic Issues 13:49-72, March 1979.
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- Fiori, Stefano, "Alternative Visions of Change in Douglass North's New Institutionalism," Journal of Economic Issues, 36(December):1025-43, 2002.
- *Hall, Peter A. and Rosemary C.R. Taylor. 1996. "Political Science and the Three New Institutionalisms," Political Studies, 44:936-57.
- Hallowell, A. Irving, "The Nature and Function of Property as a Social Institution," Journal of Legal and Political Sociology 1:115-138, April 1943.
- Hodgson, Geoffrey, M. "The Approach of Institutional Economics," Journal of Economic Literature, 36(March):166-92, 1998.
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- Hoover, Kevin D. "Pragmatism, Pragmaticism, and Economic Method," in: Contemporary Issues in Economic Methodology, ed. by Roger Backhouse, London: Routledge, 1994 (chapter 14).
- Hurst, J. W. Law and Markets in United States History Madison: University of Wisconsin Press, 1982.
- Johansson-Stenman, Olof, "On the Problematic Link Between Fundamental Ethics and Economic Policy Recommendations," Journal of Economic Methodology 5(2):263-97, 1998.
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