

INSTITUTIONAL ECONOMICS

Ag and Applied Economics/Economics 707

Daniel W. Bromley
Spring 2009

PURPOSE

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 revelation 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 (jurisprudence); 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 that process of becoming.

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 briefly 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.

Readings for the course come from two sources:

1. My book, **Sufficient Reason: Volitional Pragmatism and the Meaning of Economic Institutions**, (Princeton University Press, 2006) provides the primary conceptual grounding for the course. It is for sale at the University Book Store.

2. A reading packet is available at Pigwick Papers, 1401 University Avenue.

EXPECTATIONS

Required reading for each class period is indicated by *. I have also listed Related Readings to offer additional material if you should be interested in pursuing a particular issue in greater depth. The required readings should be read before class and you should come prepared to engage in a discussion about the essential points covered there.

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 paper will count for 60 percent of your grade. The paper will consist of a critique of a **single** article (or book) in the field of your choice in which some economic outcomes or phenomena are allegedly explained. In your paper you are to explicate:

- (1) the conceptual model that was employed;
- (2) the explicit assumptions that were invoked;
- (3) the important assumptions that went unmentioned;
- (4) your confidence in the adequacy of the proffered explanation; and
- (5) how the explanatory model needs to be modified in light of your criticisms.

The paper is to be turned in during class on Monday, April 27, 2009.

OUTLINE and READINGS

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

I. INSTITUTIONALISM

Wednesday, January 21:

Overview

Friday, January 23: (special “make up” class)

- *SR: Prelude
- *SR: Prospective Volition
- *SR: Chapter 2: The Task at Hand
- *Commons: Institutional Economics

Related Readings:

- Bowles: Endogenous Preferences
- Cooter and Rappoport: Were the Ordinalists Wrong?
- Johansson-Stenman: On the Problematic Link Between Ethics and Economic Policy
- Rabin: Psychology and Economics

Monday, January 26:

- *Ramstad: The Institutionalism of John R. Commons: Theoretical Foundations of a Volitional Economics

Related Readings:

- Davidson: Problems of Rationality
- Dwyer: the Alleged Value Neutrality of Economics
- Ramstad: Is a Transaction a Transaction?
- Sen: Rational Fools
- Veblen: The Limitations of Marginal Utility

Wednesday, January 28: (NO CLASS)

Monday, February 2:

- *SR: Chapter 3: Understanding Institutions
- *SR: Chapter 4: The Content of Institutions

Related Readings:

- Coase: The Nature of the Firm
- Coase: The Problem of Social Cost
- Hodgson: The Approach of Institutional Economics
- Kronman: Contract Law and the State of Nature

Mayhew: The Beginnings of Institutionalism
Neale: Institutions
Sen: Markets and Freedom

Wednesday, February 4:

*Ramstad: John R. Commons' Reasonable Value

Related Readings:

Parto: Economic Activity and Institutions: Taking Stock
Putterman: The Firm as Association vs. The Firm as Commodity
Simon: Organizations and Markets
Wilkins: The Neglected Intangible Asset

Monday, February 9:

*SR: Chapter 5: Institutional Change

Related Readings:

Bromley: Economic Interests and Institutions: The Conceptual Foundations of Public Policy
Nelson and Sampat: Making Sense of Institutions in Economic Performance
Rutherford: The Old and the New Institutionalism
Rutherford: Institutional Economics Then and Now

II. FIXING BELIEF

Wednesday, February 11:

*Simon: Rationality in Psychology and Economics
*McCloskey: The Rhetoric of Economics

Related Readings:

Ben-Porath: The F-Connection
Sen: Rationality and Social Choice

Monday, February 16:

*SR: Chapter 6: Fixing Belief

Related Readings:

Davidson: Essays on Actions and Events
Dewey: How We Think

Wednesday, February 18:

*Colander: The Lost Art of Economics
*Stewart: Instrumental Reasoning in Economics

Related Readings:

Hall and Taylor: Political Science and the Three New Institutionalisms

Samuels: The Coase Theorem and the Study of Law and Economics
Samuels: The Relation Between Legal and Economic Processes
Vatn and Bromley: Choices Without Prices Without Apologies

Monday, February 23:

* SR: Chapter 7: Explaining

Related Readings:

Field: On the Explanation of Rules Using Rational Choice Models
Field: The Problem with Neoclassical Institutional Economics

Wednesday, February 25:

*Samuels: The Legal-Economic Nexus

Related Readings:

Dahlman: The Problem of Externality
Rutherford: J.R. Commons' Institutional Economics
Whalen: John R. Commons' Institutional Economics: A Re-Examination

Monday, March 2:

*SR: Chapter 8: Prescribing and Predicting

Related Readings:

Mishan: How Valid are Economic Evaluations of Allocative Changes?
Tversky and Kahneman: Rational Choice and the Framing of Decisions

Wednesday, March 4:

*Posner: A Pragmatist Manifesto

Related Readings:

Ramstad: A Pragmatist's Quest for Holistic Knowledge

Monday, March 9:

*SR: Chapter 9: Volitional Pragmatism

Related Readings:

Hoover: Pragmatism, Pragmaticism, and Economic Method
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 11:

*Bromley: Reconstituting Economic Systems

Related Readings:

Hurst: Law and Markets in United States History
Mishan: The Folklore of the Market
Schmid: Legal Foundations of the Market

SPRING BREAK

III. VOLITIONAL PRAGMATISM AT WORK

Monday, March 23

- *SR: Chapter 10: Thinking as a Pragmatist
- * Ogilvie: Whatever is, is Right? Economic Institutions in Pre-Industrial Europe

Related Readings:

Philp, et al.: Preferences, Power, and Determination of Working Hours
Saraydar: The Conflation of Productivity and Efficiency in Economics
Stone: Causal Stories and the Formation of Policy Agendas
Tribe: Policy Science: Analysis or Ideology?

Wednesday, March 25:

- *Burawoy: The State and Economic Involution
- *Olson: Why Some Nations are Rich and Others Poor

Related Readings:

Fiori: Alternative Visions of Change in Douglass North's New Institutionalism
Stiglitz: Whither Reform?

Friday, March 27: (special "make up" class)

- *SR: Chapter 11: Volitional Pragmatism and Explanation

Related Readings:

Biddle: Purpose and Evolution
Chasse: John R. Commons and the Democratic State
Mandelbaum: Purpose and Necessity in Social Theory

Monday, March 30: (NO CLASS)

Wednesday, April 1: (NO CLASS)

Monday, April 6:

- *Lin: The Needham Puzzle: Why the Industrial Revolution did not Originate in China?
- *Mokyr: The Industrial Revolution and the Economic History of Technology

Related Readings:

Hodgson: Economics and Institutions

Wednesday, April 8:

*SR: Chapter 12: Volitional Pragmatism and the Evolution of Institutions

Related Readings:

Bromley: Regulatory Takings
Bromley: Constitutional Political Economy
Hallowell: The Nature and Function of Property
Sax: Some Thoughts on the Decline of Private Property

Friday, April 10:

*Anderson: The Economics of Dowry and Brideprice

Related Readings:

Drury: Locke and Nozick on Property
Pollak: For Better or Worse
Williams: Kant's Concept of Property

Monday, April 13:

*SR: Chapter 13: Volitional Pragmatism and Economic Regulations

*SR: Chapter 14: Sufficient Reason

Related Readings:

Bromley: The Ideology of Efficiency
Nelson and Winter: An Evolutionary Theory of Economic Change

Wednesday, April 15: (NO CLASS)

Monday, April 20:

*Bromley: The Economic Reach of the State: African Development Reconsidered

*Kuran: Why the Middle East is Economically Underdeveloped

Related Readings:

Yousif: Development Growth and Policy Reform in the Middle East & North Africa

Wednesday, April 22:

SUMMARY AND REFLECTIONS

IV. RESEARCH PROJECTS

Monday, April 27 – Wednesday, May 6:

Research Reports

BIBLIOGRAPHY

- Anderson, Siwan, "The Economics of Dowry and Brideprice," Journal of Economic Perspectives, 21(4):151-74.
- Ben-Porath, Yoram, "The F-Connection: Families, Friends, and Firms and the Organization of Exchange," Population and Development Review 6(1):1-30, March 1980.
- 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. "The Economic Reach of the State: African Development Reconsidered." October, 2008. (mimeo).
- 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.
- Bromley, Daniel W., "The Ideology of Efficiency: Searching for a Theory of Policy Analysis," Journal of Environmental Economics and Management 19:86-107, 1990.
- Bromley, Daniel W. "Regulatory Takings: Coherent Concept or Logical Contradiction?" Vermont Law Review 17(3):647-82, Spring 1993.
- Bromley, Daniel W. "Reconstituting Economic Systems: Institutions in National Economic Development," Development Policy Review 11:131-51, 1993.
- Bromley, Daniel W. "Constitutional Political Economy: Property Claims in a Dynamic World," Contemporary Economic Policy 15(4):43-54, October 1997.
- Bromley, Daniel W. "Markets," Encyclopedia of Political Economy, vol. 2: L-M London: Routledge, 1999.
- Burawoy, Michael, "The State and Economic Involution: Russia Through a China Lens," World Development 24(6):1105-1117, 1996.
- Chasse, John Dennis, "John R. Commons and the Democratic State," Journal of Economic Issues 20:759-84, September 1986.
- Coase, Ronald, "The Nature of the Firm," Economica 4:386-405, 1937.

- Coase, Ronald, "The Problem of Social Cost," Journal of Law and Economics 3:1-44, 1960.
- Colander, David, "The Lost Art of Economics," Journal of Economic Perspectives, 6(3):191-98.
- 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.
- Davidson, Donald. Essays on Actions and Events, Oxford: Clarendon Press, 2001.
- Davidson, Donald. Problems of Rationality, Oxford: Clarendon Press, 2004.
- Dewey, John. How We Think, Mineola, NY: Dover.
- 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.
- Field, Alexander J., "The Problem with Neoclassical Institutional Economics: A Critique with Special Reference to the North/Thomas Model of Pre-1500 Europe," Explorations In Economic History 18:174-98, 1981.
- 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.
- Hodgson, Geoffrey M., Economics and Institutions Cambridge, England: Polity Press, 1988.

- Hoover, Kevin D. "Pragmatism, Pragmaticism, and Economic Method," in: Contemporary Issues in Economic Methodology, ed. by Roger Backhouse, London: Routledge, 1994 (ch. 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.
- Kronman, Anthony T., "Contract Law and the State of Nature," Journal of Law, Economics, and Organization 1:5-32, Fall 1985.
- Kuhn, Thomas S., "Objectivity, Value Judgment, and Theory Choice," in: Readings in the Philosophy of Science ed. by B. A. Brody and R. E. Grandy, Englewood Cliffs, NJ: Prentice Hall, 1989. (pp. 356-68).
- Kuran, Timur. "Why the Middle East is Economically Underdeveloped," Journal of Economic Perspectives, 18(3):71-90, Summer 2004.
- Lin, Justin Yifu. 1995. "The Needham Puzzle: Why the Industrial Revolution Did Not Originate in China?" Economic Development and Cultural Change, 43(2):269-92.
- Mandelbaum, Maurice. Purpose and Necessity in Social Theory Baltimore: Johns Hopkins University Press, 1987.
- Mayhew, Anne, "The Beginnings of Institutionalism," Journal of Economic Issues 1(3):971-98, September 1987.
- McCloskey, Donald, "The Rhetoric of Economics," Journal of Economic Literature 21:481-517, 1983.
- Mirowski, Philip, "The Philosophical Bases of Institutional Economics," Journal of Economic Issues 21(3):1001-1038, September 1987.
- Mishan, E. J., "How Valid Are Economic Evaluations of Allocative Changes?" Journal of Economic Issues 14:143-161, March 1980.
- Mishan, E. J., "The Folklore of the Market," Journal of Economic Issues 9:681-752, December 1975.
- Mokyr, Joel. 2001. "The Industrial Revolution and the Economic History of Technology: Lessons from the British Experience, 1760-1850," The Quarterly Review of Economics and Finance, 41:295-311.
- Neale, Walter, "Institutions," Journal of Economic Issues 21(3):1177-1206, September 1987.

- Nelson, Richard R. and Bhavan N. Sampat, "Making Sense of Institutions as a Factor Shaping Economic Performance," Journal of Economic Behavior and Organization, 44:31-54, 2001.
- Nelson, Richard R. and Sidney G. Winter, An Evolutionary Theory of Economic Change Cambridge: Harvard University Press, 1982.
- North, Douglass C. "Institutions," Journal of Economic Perspectives, 5(Winter):97-112, 1991.
- Ogilvie, Sheilagh. "Whatever is, Is Right? Economic Institutions in Pre-Industrial Europe," Economic History Review, 60(4):649-84.
- Olson, Mancur, "Big Bills Left on the Sidewalk: Why Some Nations are Rich, and Others are Poor," Journal of Economic Perspectives, 10(Spring):3-24, 1996.
- Ostrom, Elinor, "Collective Action and the Evolution of Social Norms," Journal of Economic Perspectives, 14(Summer):137-58, 2000.
- Parto, Saeed. 2005. "Economic Activity and Institutions: Taking Stock," Journal of Economic Issues, 39(1):21-52.
- Philp, Bruce, Gary Slater and David Harvie. 2005. "Preferences, Power, and Determination of Working Hours," Journal of Economic Issues, 39(1):75-90.
- Pollak, Robert A. "For Better or Worse: The Roles of Power in Models of Distribution Within Marriage," American Economic Review 82(2):148-52, May 1994.
- Posner, Richard A., "A Pragmatist Manifesto," in: Pragmatism, ed. By Louis Menand, New York: Vintage Books, 1997, pp. 417-36.
- Putterman, Louis, "The Firm as Association versus the Firm as Commodity," Economics and Philosophy 4:243-66, 1988.
- Putnam, Hilary, The Collapse of the Fact/Value Distinction, Cambridge: Harvard University Press, 2002.
- Rabin, Matthew, "Psychology and Economics," Journal of Economic Literature 36:11-46, March 1998.
- Ramstad, Yngve, "A Pragmatist's Quest for Holistic Knowledge: The Scientific Methodology of John R. Commons," Journal of Economic Issues 20(4):1067-1105, Dec. 1986.
- Ramstad, Yngve, "Is A Transaction a Transaction?" Journal of Economic Issues 30(2):413-25, June 1996.

- Ramstad, Yngve, "The Institutionalism of John R. Commons: Theoretical Foundations of a Volitional Economics," in: Research in the History of Economic Thought and Methodology, ed. by. Warren Samuels, Boston: JAI Press, 1990.
- Ramstad, Yngve, "John R. Commons' Reasonable Value and the Problem of Just Price," Journal of Economic Issues, 35(2):253-77, June 2001.
- Robbins, Lionel, An Essay on the Nature and Significance of Economic Science London: Macmillan, 1932.
- Rutherford, Malcolm, "J. R. Commons's Institutional Economics," Journal of Economic Issues 17:721-44, September 1983.
- Rutherford, Malcolm, "The Old and the New Institutionalism: Can Bridges Be Built?" Journal of Economic Issues 29(2):443-51, June 1995.
- Rutherford, Malcolm, "Institutional Economics: Then and Now," Journal of Economic Perspectives 15(3):173-94, Summer 2001.
- Samuels, Warren J., "The Coase Theorem and the Study of Law and Economics," Natural Resources Journal 14:1-33, January 1974.
- Samuels, Warren J., "The Legal-Economic Nexus," George Washington Law Review 57:(6):1556-78, August 1989.
- Samuels, Warren J., "The Interrelations Between Legal and Economic Processes," Journal of Law and Economics 14:435-450, Oct. 1971.
- Saraydar, Edward, "The Conflation of Productivity and Efficiency in Economics and Economic History," Economics and Philosophy 5:55-67, 1989.
- Sax, Joseph L. "Some Thoughts on the Decline of Private Property," Washington Law Review 58:481-96, 1983.
- Schmid, A. Allan, "Legal Foundations of the Market: Implications for the Formerly Socialist Countries of Eastern Europe and Africa," Journal of Economic Issues 26:707-32, September 1992.
- Sen, Amartya, "Rational Fools," Philosophy and Public Affairs 6:317-44, 1976-77.
- Sen, Amartya, "Markets and Freedoms: Achievements and Limitations of the Market Mechanism in Promoting Individual Freedoms," Oxford Economic Papers 45:519-41, 1993.
- Sen, Amartya, "Rationality and Social Choice," American Economic Review 85(March):1-24, 1995.

- Simon, Herbert, "Rationality in Psychology and Economics" in Rational Choice, Hogarth, Robin and Melvin W. Reder (eds.), Chicago: University of Chicago Press, 1987.
- Simon, Herbert A., "Organizations and Markets," Journal of Economic Perspectives 5(2):25-44, Spring 1991.
- Stewart, Hamish, "A Critique of Instrumental Reason in Economics," Economics and Philosophy 11:57-83, 1995.
- Stiglitz, Joseph E. "Whither Reform?" Keynote address for the Annual Bank Conference on Development Economics, Washington, D.C: World Bank, April 28, 1999.
- Stone, Deborah, "Causal Stories and the Formation of Policy Agendas," Political Science Quarterly 104(2):281-300, 1989.
- Sugden, Robert, "Spontaneous Order," Journal of Economic Perspectives 3(4):85-97, 1989.
- Tribe, Laurence H., "Policy Science: Analysis or Ideology?" Philosophy and Public Affairs 2(1):66-110, 1972.
- Tversky, Amos and Daniel Kahneman, "Rational Choice and the Framing of Decisions" in Rational Choice, Hogarth, Robin and Melvin W. Reder (eds.), Chicago: University of Chicago Press, 1987.
- Vatn, Arild and Daniel W. Bromley, "Choices Without Prices Without Apologies," Journal of Environmental Economics and Management 26(2):129-48, March 1994.
- Veblen, Thorstein, "The Limitations of Marginal Utility," in: The Philosophy of Economics ed. by D. M. Hausman, Cambridge: Cambridge University Press, 1984. (chapter 7).
- Whalen, Charles J., "John R. Commons's Institutional Economics: A Re-Examination," Journal of Economic Issues 23(2):443-54, June 1989.
- Webb, James L. "Dewey: Back to the Future," Journal of Economic Issues, 36(December):981-1003.
- Weston, Samuel C. "Toward a Better Understanding of the Positive/Normative Distinction in Economics," Economics and Philosophy 10:1-17, 1994.
- Wilkins, Mira, "The Neglected Intangible Asset: The Influence of the Trade Mark on the Rise of the Modern Corporation," Business History 34:65-95, 1992.
- Williams, Howard, "Kant's Concept of Property," Philosophical Quarterly 27:32-40, 1977.

Yousef, Tarik M. "Development, Growth and Policy Reform in the Middle East and North Africa Since 1950," Journal of Economic Perspectives, 18(3):91-116, Summer 2004.