

INSTITUTIONAL ECONOMICS

Ag and Applied Economics/Economics 707

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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 judicial 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 Tuesday, May 4, 2010.

OUTLINE and READINGS

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

I. INSTITUTIONALISM

Tuesday, January 19:

Overview

- *SR: Prelude
- *SR: Chapter 1: Prospective Volition
- *SR: Chapter 2: The Task at Hand

Related Readings:

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

Tuesday, January 26:

- *Commons: Institutional Economics
- *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

Tuesday, 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

Tuesday, February 9:

- *SR: Chapter 5: Institutional Change
- *Ramstad: John R. Commons' Reasonable Value
- *Simon: Rationality in Psychology and Economics

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
- 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

Tuesday, February 16:

- *McCloskey: The Rhetoric of Economics
- *SR: Chapter 6: Fixing Belief

Related Readings:

- Ben-Porath: The F-Connection
- Sen: Rationality and Social Choice
- Davidson: Essays on Actions and Events
- Dewey: How We Think

Tuesday, February 23:

- *Colander: The Lost Art of Economics
- *Stewart: Instrumental Reasoning in Economics
- * SR: Chapter 7: Explaining

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

Tuesday, March 2:

- *Samuels: The Legal-Economic Nexus

*SR: Chapter 8: Prescribing and Predicting

Related Readings:

Dahlman: The Problem of Externality

Rutherford: J.R. Commons' Institutional Economics

Whalen: John R. Commons' Institutional Economics: A Re-Examination

Mishan: How Valid are Economic Evaluations of Allocative Changes?

Tversky and Kahneman: Rational Choice and the Framing of Decisions

Tuesday, March 9:

*Posner: A Pragmatist Manifesto

*SR: Chapter 9: Volitional Pragmatism

Related Readings:

Ramstad: A Pragmatist's Quest for Holistic Knowledge

Hoover: Pragmatism, Pragmaticism, and Economic Method

Kuhn: Objectivity, Value Judgment, and Theory Choice

Mirowski: The Philosophical Bases of Institutionalist Economics

Weston: Toward a Better Understanding of the Positive/Normative Distinction

III. VOLITIONAL PRAGMATISM AT WORK

Tuesday, March 16:

*Bromley: Reconstituting Economic Systems

*SR: Chapter 10: Thinking as a Pragmatist

*Ogilvie: Whatever is, is Right? Economic Institutions in Pre-Industrial Europe

Related Readings:

Hurst: Law and Markets in United States History

Mishan: The Folklore of the Market

Schmid: Legal Foundations of the Market

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

Tuesday, March 23:

*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?

SPRING BREAK (March 27- April 5)

Tuesday, April 6:

- *SR: Chapter 11: Volitional Pragmatism and Explanation
- *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:

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

Tuesday, April 13:

- *SR: Chapter 12: Volitional Pragmatism and the Evolution of Institutions
- *Anderson: The Economics of Dowry and Brideprice

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

Tuesday, April 20:

- *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

Tuesday, April 27:

- *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

Tuesday, May 4:

SUMMARY AND REFLECTIONS

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