


# Chapter 1

## From Old Institutional Economics to New Institutional Economics: A Short History

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### ABSTRACT

*Since different kinds of economics thoughts have been explored, few have been as peculiar as Old Institutional Economics (OIE) and New Institutional Economics (NIE). It is curious that almost every stream criticizing mainstream economics has a left wing. OIE, not a big fan of this, criticizes neoclassical economics/mainstream economics, given it arose in the US. OIE had no sense to left wing, on the contrary, it created an effect criticizing neoclassical economics in its core. Unlike OIE, NIE has many common points with neoclassical economics. NIE has several new aspects different from neoclassical economics, as it has chosen a completely different path than OIE. In this chapter, authors scrutinize circumstances that led to OIE, and what separated OIE and NIE. A brief, successively historical aspect is also provided.*

### INTRODUCTION

Institutionalism is very important for an economy. It covers every shape of our lives. It is in economic institutions, organizations, labor and monetary institutions, property rights, legal institutions, economic actors etc. Institutionalism had affected great economists such as Marshall, Smith, and Mill. But none of them gave such significant focus like USA's institutionalism and like the great philosopher Veblen. This study aims to submit a brief history about the origins of institutionalism.

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Naturally, many of the scholars know that institutionalism has a broad history, but may one elaborate its historical path, it shall be called as Old Institutional Economics (OIE) and New Institutional Economics (NIE). By giving a historical background of the transformation from OIE to NIE, the origins of OIE and its path from today to future will be illuminated. This chapter will cover several aspects of OIE. Firstly, the author will discuss the origins of Institutional Economics in the US which was commenced with Veblen. The chapter proceeds by mentioning the other great contributors of OIE like Mitchell and Commons. Secondly, the author will scrutinize NIE whilst mentioning the three important contributors to NIE, Ronald Coase, Oliver Williamson and Douglas North.

The reason why these great economists and their contributions are being discussed is that the institutional economics history has a wide range. Mentioning the great contributors of each school of institutional economics will provide the readers a thorough history of these two different schools.

## **BACKGROUND**

Since neoclassical economics became an imperial feature, OIE has started by criticizing it. Because, neoclassical economics – frequently called as mainstream economics – is a phenomenon to explain all economics events. Mainstream economics moreover claims that it can explain all other events, all not necessarily in economics. Economic thought sometimes takes a fresh breath, in which case, some new thoughts emerge when it cultivates the pressure of a dominant ideology. So is Old Institutional Economics (OIE). The main ideology of OIE is naturally institution then. So, what is institution?

*Institutions are the kinds of structures that matter most in the social realm, they make up the stuff of social life. The increasing acknowledgement of the role of institutions in social life involves there cognition that much of human interaction and activity is structured in terms of overt or implicit rules. Without doing much violence to the relevant literature, we may define institutions as systems of established and prevalent social rules that structure social interactions. Language, money, law, systems of weights and measures, table manners, and firms (and other organizations) are thus all institutions. (Hodgson, 2000, p. 2).*

Institutions are embedded in human life. Since the beginning of known history of the human settlements, all cultures have created many institutions. All of them are related with both social and economic life. No matter how social life seems to be separated from economics, in fact, it is very much embedded in economics. As Hodgson clearly states that language, money, law, etc. are related with the market. If one needs and wishes, all institutions can be addressed by economics. So, either OIE or NIE is focused on how these institutions affect our lives. Of course, their approach to scrutinize the institutions are different from each other.

## **A HISTORICAL PATH OF BOTH INSTITUTIONALIST SCHOOLS**

The titles like ‘the role of institutions in economics process’ are just the tools to make an easy expression. This reminds that more econometrics studies are seen in economics. They presume there is no institution in economics, and then they consider institution as if there would be ‘pure economics’, namely

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