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# Institutionalism as an Approach to Political Economy

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The title of this article suggests a duality which captures some of institutionalism's essential properties. One unfamiliar with the development of the institutionalist perspective in twentieth-century American economic thought might be tempted to inquire as to whether the distinguishing property of institutionalism pertains basically to its different methodological or philosophical *approach* to the discipline of economics or to its focus upon the broader *political* character of economic life. For institutionalists, of course, the (brief) answer is both. Institutionalism has marched to a different drummer from mainline economics (Keynesian as well as neoclassical) in terms both of the scope and content of its subject matter *and* its methodologies or modes of approaching its substantive concerns.

This article examines "institutionalism as an approach to political economy" from both of these perspectives. First, it gives a comparative review of the institutionalist theory of the evolution of systems of political economy in capitalist development, with focus upon the Veblen-Ayres tradition and contemporary extensions. Here, the emphasis is upon institutionalism's methodological properties, notably, its dynamic and evolutionary approach to analysis of technological and institutional

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change in economic development. Second, it describes the interpenetration of politics and economics in the contemporary political economy, with focus upon the contributions of John R. Commons and J. K. Galbraith. Here, the emphasis is upon the role of political factors in economic life and the conception of the economy as a system of power.

Although references are made throughout to various individuals, in their own right or as representatives of broader themes, essentially we will ignore the intricacies of differentiation among the founding fathers, the late greats, and the contemporary contributors in the institutionalist tradition, and will adopt the technically inaccurate but useful fiction that there exist essential or at least sufficient unity and continuity in their writings to warrant treating them for our present purposes as a group.

### *Theory of Institutional Evolution in Capitalist Development*

As Wesley Clair Mitchell aptly observed nearly a half century ago [1937, pp. 336–37], if the defining property of institutional economics were merely the study of economic institutions, then Adam Smith and John Stuart Mill must be counted among institutionalism's founders. Closer to the mark, as institutionalism's *differentia specifica,* he proceeded to suggest, would be focus upon the cumulative process of evolutionary change in economic institutions. Contemporary perspective would probably lead many to amend this view by placing special emphasis upon the development and transformation from the old-style political economy embodied in the conception, if not always the practice, of competitive market and essentially laissez-faire capitalism to the new-style political economy exhibited in one or another variant of contemporary capitalism.

The perhaps obvious but strategic starting point for an analysis of institutional change is an alteration in methodological perspective, namely, the shift into variables of the data compounded in the *ceteris paribus* assumptions of "orthodox" economic theory. In orthodox price (and national income) theory, the dominant procedure is to construct deductive hypotheses concerning the behavior of selected economic variables from underlying assumptions. These assumptions, typically pertaining to technology, institutions, and social attitudes and motivations, are perceived of as non- or extraeconomic in character. In any event, they are "given," not in the sense that they do not change or cannot be altered for purposes of intellectual experiment (for example, the substitution of the assumption of oligopoly for pure competition), but in the sense that they are typically regarded as beyond the explanatory scope of economic theory. In institutional theory, by contrast, these kinds of data *also* become variables for which hypotheses are to be constructed.

This perspective immediately raises two procedural problems for economists, one of scope, the other of method. If economic analysis is perceived to include technology, institutions, and social attitudes, at least to the extent that changes in them stimulate and interact with changes in the employment and allocation of resources, and the distribution of, fluctuations in, and growth of income, then clearly the scope of the discipline is broadened, and the boundaries with other disciplines become less precise. As to method, how are economists to construct hypotheses concerning economic behavior when the assumptions underlying the analysis have been transformed into issues and variables, changes in which now themselves require explanatory hypotheses?

Probably the dominant answer to this question within the institutionalist tradition is to focus upon technology as the strategic and decisive dynamic factor in economic development and to attribute technological change in large measure to the entire culture or "life process" of society. In this view, technology, key to the development process, obeys its own logic. Economic and political institutions (and ideas) serve essentially facilitative, adaptive, obstructive, or destructive roles in economic and social change. The interconnections between technology and institutions are thus perceived to constitute the dynamics of development, the basic logic of which emerges as the prime concern of institutionalist political economy. This basic idea will now be amplified and illustrated by a series of vignettes on the theory of the evolution of politico-economic institutions from Thorstein Veblen to the present.

### *Thorstein Veblen: From Free Competition to Monopoly Capitalism*

For Veblen [1904; 1919; 1921; 1923; Dowd 1958; 1964], the increasing pace of technological change and improvements in the "industrial arts" since the mid-nineteenth century are perceived as having profound institutional consequences. First, advancing technology stimulates the rise of the corporation to a position of economic dominance, notably in the "key industries" of natural resources, power, and transportation. In part, growing corporate ascendancy is responsive to increasing economies of large-scale production; in part, it simply reflects the singular commitment of the corporate form of business organization to profit and thus its increasing appropriateness in a period of expanding output, population, and markets. Second, the growth of the corporation stimulates other important institutional changes, notably the separation of ("absentee") ownership and management, the expanded business role of credit and financial institutions, and the development of labor unions as business-like attempts to control the supply and remuneration of labor. Third, the combination of technology, credit, and the corporation generates a partially interactive proclivity toward depression and monopoly. On the one hand, the high fixed costs associated with large-scale production, coupled with the technology-based tendency toward lower costs, stimulate cutthroat competition and thereby serve as inducement to monopolization. On the other hand, alternating waves of over- and undercapitalization, stimulated by the corporation and the credit system, are the proximate cause of business fluctuations and depressions (which, in turn, also stimulate monopoly). The modern corporate system, with its trusts, holding companies, credit, price rigging, and salesmanship, thus tends to degenerate into a vast arrangement for "making money" and economic "sabotage," increasingly alienated from the technological forces largely responsible for its emergence and from the "underlying population" as well. Fourth, at the same time, the machine process stimulates workmanlike attitudes and habits of thinking among those occupations and groups (engineers, technicians, production supervisors, industrial workers) most directly associated with technology and production.

One alternative future, which Veblen hedged with numerous caveats, is the dispossession of the absentee owners and the construction of a new industrial order devoted to maximum production, led by this new technical aristocracy. To prevent this, and to support their growing imperialist adventures emanating from the worldwide quest for markets and profits, the "vested interests" may well increasingly turn to the political system. According to Veblen, the underlying population has a tendency toward subservience and emulation of the capitalist and corporate rich in any event. This, combined with feelings of nationalism and patriotism, which are stimulated by war or war preparations and are manipulated by political leaders, can be a powerful deterrent to social reform. Protection of the vested interests and the corporate system by the state, however, has its price. Political and military leadership, reflecting precapitalist virtues and values, may well not rest content serving as handmaidens to business enterprise; what begins as business control over the political system can evolve into a sort of authoritarian fascistic political control over business as well as society at large. Whatever the prospective outcome of the conflict between these two rather speculative alternatives, institutional evolution in systems of political economy seems inevitable. The long-run prospects for the relatively unregulated capitalism of circa 1870–1920 in the Veblenian vision seemed slim. In brief: "It seems possible to say this much, that the full dominion of business enterprise is necessarily a transitory dominion. It stands to lose in the end whether the one or the other of the two divergent cultural tendencies wins, because it is incompatible with the ascendancy of either [Veblen 1904, p. 400].

*Clarence Ayres: From Absolute Capitalism to Limited Capitalism*

In his writings, notably those of the 1940s and early 1950s [1944; 1946; 1952], Ayres continued and elaborated upon the Veblenian themes of the creative impact of technological change upon industrial growth and technology's corrosive effects upon economic and political institutions. His analysis of the prospective shift from the "money power" system under "absolute capitalism" to economic planning under "limited capitalism" exhibits an interesting blend of institutionalist and Keynesian perspectives as well as a valuable exercise in the evolution of systems of political economy.

In *Absentee Ownership,* Veblen had described the view that corporations create capital equipment and tools from accumulated savings which would otherwise have remained idle as part of the "folklore" of political economy [1923, p. 86]. The idea that saving is the proximate cause of investment and thereby technological change and economic growth, Ayres contends, is the reverse of the actual situation. Although saving and "money capital" (and thereby capitalists and capitalism) no doubt serve a permissive or facilitative role in economic development, it would be more accurate to say that technological improvements, embodied in investment or capital goods, generate the increases in national income which thereby enable saving to rise.

Still, the orthodox analysis of the saving-investment relation has provided a powerful rationale for capitalism and capitalists, a sort of "divine right of capital" which has helped sustain absolute capitalism and its property and power relations in a manner reminiscent of the role that the concept of the divine right of kings played in helping to sustain absolute monarchy in an earlier era. Increasingly, however, the actual situation has eroded popular belief in this "legend" and thereby in the moral authority of capitalist institutions. The experiences of the 1920s and 1930s, Ayres suggests, indicate that saving can easily be excessive relative to investment and that the functioning of capital, credit, and bond markets will not automatically equate saving and investment at full employment. This problem does not emanate merely from market imperfections, but is rooted in more fundamental structural and institutional factors. Notable among these, first, is a tendency toward insufficient consumption and excessive saving generated by income inequality; second is the rise of the corporation, which has increasingly separated savers from investors at the same time that it has encouraged internal financing of investment.

The solution, identified prospectively by Ayres, and of course retrospectively by others in the post–World War II period, is a shift to a limited capitalism analogous to limited or constitutional monarchy. The central problem of Ayres's absolute capitalism is its institutional obstruction to sustained economic growth. The central institutional innovation of limited capitalism lies in removing this obstruction through "planning for stability" [1952, pp. 186ff.]. Its essential mechanism would be a redistribution of income (although not of wealth) through a reform of the Social Security system, namely, an extension of "its benefits to the entire population irrespective of their earnings and even of their other independent income" [1946, p. 100] sufficient to generate a level of mass purchasing power supportive of full employment levels of aggregate demand. Limited capitalism would not require a radical reform of either the market system or of corporate and property power. It would require, however, a strategic institutional change wherein government would compensate for or offset the destabilizing proclivities of the private market economy. In Ayres's view, it would also require a reduction in income inequality as the price for sustaining a prosperous overall economy and thereby prosperity levels of profits and property income as well as the essential institutional features of market capitalism.

### *J. K. Galbraith: From Market Economy to Planned Capitalism, Corporate Model*

Many economists in the institutionalist tradition have examined planning as an evolving supplement or substitute for market processes. For Ayres, as already implied, planning "is itself a manifestation of the technological process." It is problems resulting from "institutional obstruction" to technological change that stimulate the emergence of economic planning, and it is institutional innovation to overcome such obstruction (for example, macroeconomic policy to promote stability) that constitutes planning's strategic dimension [1952, p. 192]. In a singularly "modern" essay written in the mid-1930s, to cite a second example, Mitchell attributed the growing departure from laissez-faire and emergence of early varieties of government planning (piecemeal, emergency, and stabilization planning) since the late nineteenth century to an interwoven complex of changes in technology, economic and political organization, and social attitudes. Of special interest is his view that economic progress itself, under capitalist auspices—through growing interdependence, exhaustion of natural resources, increasing incidence of depressions, and growing concentration in income, wealth, and economic power—conduces to a perceived need for enlarged government control, guidance, and planning in economic life [1937, pp. 103–36].

In his recent works [1971; 1973], Galbraith has identified an evolutionary process of development of economic planning in postwar America as something approximating a capitalist version of a planned economy. In the Veblen-Ayres tradition, the corporation is perceived as the locus of this trend, and technological change as its underlying dynamic imperative. The most visible and profound evidence of change in twentieth-century America, especially since the beginning of World War II, Galbraith asserts, has been "the application of increasingly intricate and sophisticated technology to the production of things" [1971, p. 1], notably in the several hundred large-scale corporations which dominate the "decisive part" of contemporary industry [1973, p. ix]. The consequences of these technological changes—the increasing commitment of time and capital, the greater inflexibility of this commitment, the increased need for specialized manpower and organization—have reduced the reliability of market relations and thereby have made corporate planning "imperative." In order to function effectively in the new technological environment, large corporations must be able to anticipate—*and control*— both consumer demand and their sources of supply, at remunerative prices and costs, as well as the sources of supply of corporate saving for investment. The various strategies for accomplishing this (for example, sales promotion, vertical integration, internal corporate financing) constitute nothing less than the supersession, suspension, or control of the market and its replacement by planning. Corporate planning, in turn, is supplemented and reinforced by appropriate government action, notably the regulation of aggregate demand, the provision of trained manpower through the educational system, the underwriting of new capital and technology, and, to some degree, the promotion of wage-price stability.

In response to his critics, Galbraith readily accedes that this system of political economy "is not the formal planning of the socialist state. It is a more informal and much less fully developed apparatus. . . . [It] does not have a system of overall coordination; . . . discrepancies in performance exist between different sectors. . . . Nor is the planning complete; market influences are not fully excluded. . . . But it is planning by organizations with the requisite power. . . . [A significant part of the economy] is becoming increasingly subject to the power of the productive apparatus, specifically the great corporation" [cited in Sharpe 1974, pp. 96–100]. And it is this kind of emerging planning system, not the impersonal governance of market forces, which is coming increasingly to characterize and control the allocation of resources in contemporary capitalism.

### *Gunnar Myrdal: From Market Economy to Economic Planning, Contemporary Welfare State Model*

For Galbraith, drawing primarily upon American experience, the locus of power and change has been the large-scale corporation. For Gunnar Myrdal, sketching in broad strokes the process of politico-economic change in the rich countries in the Western world over the last half century, the focus is upon the emerging democratic welfare state, that is, a state with fairly clear and developed responsibility for the promotion of such social goals as full employment, equality, economic development, and minimum standards of income, health, education, housing, and so on. As does Galbraith, Myrdal believes planning has become "a necessity" [1960, p. 62]. Planning is distinguished from mere intervention into market relations, however, by identifying it with "conscious attempts by the government of a country—usually with the participation of other collective bodies—to coordinate public policies more rationally in order to reach more fully and rapidly the desirable ends for future development which are determined by the political process as it evolves" [1960, p. 23]. The typical process of development has been that intervention has led to planning in this sense of rationally coordinated public policies: when measures turned out to be more than temporary, when policies had important unanticipated secondary or countervailing effects, when different interventions or policies turned out to be inconsistent or raised administrative difficulties.

State interventions into market forces, in turn, have developed by a process of "cumulative causation." As Allan Gruchy aptly puts it, "an original or primary change will cause secondary reactive changes which will reinforce the primary change and cause the social process to move further in the same direction taken by the primary change" [1972, p. 181]. For example, modern technology and organization have increased the scale of economic activity and created opportunities for organizational control over markets. This development "compels the state to large-scale measures of intervention." Intervention becomes "necessary" to prevent social disorganization and exploitation [Myrdal 1960, pp.32–33]. But just as private intervention stimulates state intervention, so too does the derivative state intervention encourage further departure from reliance upon market forces. This occurs directly, by developing an institutional and organizational infrastructure (for example, collective bargaining), and indirectly, by tempering the potentially dislocating features of the original changes, thereby permitting their continued growth and extension.

Another "typical cumulative process of circular causation" [Myrdal 1960, p. 36] is found in the transformation of social attitudes. Changes in technology and institutions partly explain adaptations of attitudes. But attitudinal changes, especially during periods of domestic or international crisis, have dissolved old taboos (for example, regarding the gold standard, the categorical imperative of the annually balanced budget, the sanctity of private property) and have made people more economically sophisticated and "rational," thereby contributing to their insistence on expanding private and public control over their economic destinies. Similarly, with the spread of democratic institutions, based on industrialization and urbanization, it became inevitable that larger numbers of people would press for large-scale redistributional reforms, thereby strengthening the basis for fuller participation in the economic and political life of the community by the lower end of the income and power strata.

### *Robert Solo: Ideology's Role in the Evolution of American Political Economy*

Social scientists from Alexis de Tocqueville and Karl Marx to present-day writers have observed and commented on differentiating properties of the American experience, including dimensions of American political economy which distinguish it from the patterns of European capitalism. Marx, for example, commented that despite robust American economic development in the nineteenth century, the existence of an open frontier and public policies conducive to fairly widespread landholdings and small-scale farming worked to delay the emergence of a modern industrial capitalist economy, characterized by the confrontation of a small, property owning capitalist class and a large, propertyless proletariat. Myrdal has recently observed that departures from laissez-faire and movement toward the advanced, participative welfare state have been slower in the United States than in Europe. "The process of national integration" in the United States, he suggests, "has still a considerable distance to go before identification, solidarity, and participation reach the levels common in the other Western countries." After rejecting a country's size, relative youth, and degree of personal mobility as explanations, Myrdal focuses upon cultural heterogeneity and "separatistic loyalties" emanating from the diverse backgrounds of immigrant groups and upon the more legalistic and bureaucratic structure of social relations in America [1960, p. 99].

In a recent work embracing the entire sweep of American history, Robert Solo [1974; Peterson 1976] examines the role of *ideology* as a strategic explanatory factor in the evolving relations between the political authority and the market system. *Ideology,* defined as "any coherent idea (or set of ideas) as to what ought to be with respect to some field of choice and action" [Solo 1974, p. 18], can and does lag obstructively behind social change. However, because man is a learning and valuing creature, ideology can also be an autonomous spearhead or initiator of change. Furthermore, when a former, obstructive ideology dissolves through the corrosive force of the changing pace of events and is transformed into a new ideological perspective, that new perspective itself can become a powerful force for change [Solo 1974, p. 8]. Thus, political policy "*is an expression of a prevailing ideology*" and "*policy change reflects ideological change*" [p. 23]. Explanation and prediction of policy changes require identification and prediction of prospective ideological changes. The role and impact of ideology, Solo avers, vary with different types of choice processes. Within organizations, for example, ideology has the greatest import in *authoritative decisions,* that is, decisions made by individuals in authority (who are responsible for explaining and justifying those decisions) *for* the organization. *Composite choices,* which reflect the diversity of interests and views of the members of the organization (established, for example, by voting) are more likely to represent compromise than ideological clarity. In the American political system, the Supreme Court "exemplifies authoritative decision and articulates an ideology. Congress and the President exemplify composite choice, reflecting a balance of pressures" [Solo 1974, p. 40].

At the outset of the American political experience, the dominant ideology was a blend of nationalism and property- and market-oriented liberalism. Although a European transplant, the liberal ideology flourished and persisted in American soil for two key reasons: the absence of a feudal and medieval heritage, and the fact that American liberalism was a *pre*industrialization phenomenon—it was able to take deep roots prior to the disruptive effects of the capitalist industrialization process.

In the first great phase of the evolving American political economy, roughly until the Civil War, the central issue facing the young republic was the locus of political authority, that is, "whether the political system was to take the form of decentralized authority exercised by quasi-sovereign states or whether power was to be centralized in the federal government" [Solo 1974, p. 51]. The Constitution, far from resolving this issue, had divided authority between the federal government and the states, and among the president, Congress, and the judiciary within the federal government. In this period, the interests of property and wealth reflected in the liberal ideology were best represented by a strong federal government that would provide a solid infrastructure (internal free trade, national banking, security for property and enforcement of contracts) for development of the market system. In this context, the Supreme Court, acting in concert with the prevailing ideology, took the lead in social reform and change to remedy the lag of institutions behind ideology. In a series of landmark decisions (*Marbury* v. *Madison,* 1803; *McCulloch* v. *Maryland,* 1819), it revolutionized the power structure of the American political system by spearheading the drive to centralize political authority in a strong nation state.

In the second phase of American political economy, from roughly the end of the Civil War to the depression of the 1930s, massive industrialization, and its attendant technological and institutional changes, created problems and perceived needs that the prevailing ideology of laissez-faire liberalism was unable to accommodate. Thus, crisis and need called for institutional reforms that conflicted with the dominant ideology. In this context, ideology was an obstructive force, lagging behind new technology and institutions. Congress and the president (agencies of composite choice) led in the thrust for reform, characterized by piecemeal efforts to expand the scope of public action. The Supreme Court (the agency of authoritative decision), firmly reflecting the dominant ideology of laissez-faire liberalism, fought against and succeeded in aborting federal efforts to control prices, wages, hours, employment conditions, and production. Throughout this period, ideology played a powerful constraining role. That it was able to do this, "even in opposition to rational pragmatism and the pressures of interested groups" [Solo 1974, p. 154], is an indicator of its tremendous power and widespread acceptance. Only the combination of massive depression, war, the internationally derived imperative of economic growth, and the organizational revolution was finally sufficient to cause the process of social change to break loose from the tenacious hold of obstructive ideology exemplified by the functioning of the Supreme Court from roughly 1860 to 1935.

The years since 1935 have been characterized by institutional experimentation and ideological transition, facilitated by the collapse of the Supreme Court's powerful commitment to the traditional liberal ideology. Institutionally, public policy has gone beyond the mere "housekeeping function" of the pre–New Deal era (maintaining the institutional infrastructure for individual choice and market relations) to the "offset function" (offsetting poverty, inequality, bargaining disadvantages, insecurity, and, most notably, instability and unemployment). Ideologically, this has been reflected by a "New Deal Credo," rationalized by Keynesian economics and focusing upon the offset function, and by postwar Supreme Court decisions reflecting the needs of organization and the need to protect the individual in an organizational society. What is needed now, Solo contends, is a movement, institutionally and ideologically, beyond the offset function phase to a new phase of "systems planning," wherein the public sector initiates, plans, organizes, and manages "complex activities in pursuit of goals selected through the process of political choice" [Solo 1974, p. 371] and thus confronts the challenges and opportunities for collective achievement in such areas as race, urban development, inflation, and growth.

### *The Interpenetration of Politics and Economics*

If the evolutionary process of development in politico-economic institutions is the primary theme in the institutionalist approach to political economy, then the *interpenetration* of politics and economics in the institutional structure and behavior of contemporary society runs a close second. This felicitous expression, apparently coined by J. M. Clark in a seminal paper in the mid-1950s, conveys pointedly the idea that as a result of social change not only have former conceptions of boundaries between politics and economics broken down, but also "each discipline, and practice, enters inevitably into the field of the other." On the one hand, within "official" government, economic processes and interests "shape political issues and measures"; government policy, in turn, "increasingly shapes the course of economic affairs." On the other hand, economic and political characteristics are combined in the economic governments or "nominally private bodies that carry on economic affairs" [Clark 1957, pp. 226–27; Hamilton 1957]. Consequently, polity has become a process for economizing as well as a system of authority and power, while economy has become a system of power as well as a process for economizing. Some of the major methodological and theoretical implications of the resulting amalgam will now be described briefly by reference to two prominent contributors to the institutionalist tradition: John R. Commons and Galbraith.

### *John R. Commons: The Political Economy of Collective Action*

For Commons, institutional economics was perceived as virtually synonymous with the political economy of collective action. Collective action, which Commons viewed as expanding and liberating as well as controlling individual action, ranges ubiquitously from unorganized custom to organized private and public "going concerns." In contemporary capitalism, the dominant organizational forms of collective action are corporations, labor unions, and political parties. Because collective action has been present in economic thought (although generally ignored or deemphasized) from the mid-eighteenth century to the present, the intellectual problem is not to substitute a new, institutional economics for mainstream thought, but to create a "rounded-out Political Economy," so as "to give collective action, in all its varieties, its due place throughout economic theory" [Commons 1934, p. 5].

Collective action, as does individual action, begins with scarcity "as universal for all economic theory" [Commons 1934, p. 6]. But scarcity for Commons goes beyond the biological and psychological dimensions of Herbert Malthus and the Austrians, respectively, to the *"proprietary* scarcity" connected with intangible property in contemporary capitalism (that is, to the ownership power to control things, notably to restrict supply), "enforced by working rules of government and by the collective action of corporations and labor unions" [Commons 1950, p. 94]. Traditional economics, by focusing upon such relatively bloodless and essentially man-to-nature or man-to-himself concepts as utility, commodity, and exchange, in the main was able to slight the institutional dimensions of economic activity. In the traditional view, scarcity leads to individual, economizing choices. In a world of mutual interdependence, choices are coordinated through market exchange relations, with static equilibrium and market values as the theoretical results.

By contrast, institutional economics focuses upon man-to-man actions or *transactions,* classified as bargaining (transactors as legal equals), managerial (transactors as individual legal superiors and inferiors, for example, foreman and worker), and rationing (transactors as collective legal superiors and inferiors, for example, a legislature and the citizenry, a labor union and its members). Ownership thus "becomes the foundation of institutional economics" because ownership interacts with scarcity to create conflicts of interest which are "predominant in transactions." But transactors are mutually interdependent as well as conflicting. Because of mutual interdependence, Commons rather optimistically believed, the "alienation and acquisition, between individuals, of the *rights* of future ownership of physical things" would be "negotiated between the parties concerned, according to the working rules of society," thus creating not equilibrium or "harmony," but at least a certain "security of expectations" or "order" [Commons 1934, p. 58].

This negotiational process, in turn, rests upon "sovereignty," that is, "the changing process of authorizing, prohibiting, and regulating the use of physical force in human affairs" [Commons 1934, p. 684]. In the United States, the system of courts, ultimately the Supreme Court, serves as the arbiter and determiner of the application of society's negotiational working rules. "The Court thus becomes an authoritative faculty of Political Economy for the United States" [Commons 1934, p. 712]. Its rulings (and those of the administrative commissions, which have absorbed much of the Court's functions in economic regulation since the mid-1930s), "correlating law, economics, and ethics," come to represent "reasonable values." This is so not because they constitute market equilibria, but because they are based on the distinctly human qualities of "conflict of interests, mutual dependence, and the rules of order deemed necessary to keep industry agoing with due regard to public and private interests" [Commons 1934, p. 719]. In brief, the mainstream sequence would be:

Scarcity → Economizing Choice → Market Coordination → Equilibrium and Market Values

Commons's revised institutionalist sequence would be:

Scarcity → Ownership and Power Conflicts → Negotiation under Sovereignty → Created Order and Reasonable Values

From the perspectives of both the classical theory of democracy and the classical and neoclassical theories of the competitive market, Commons's revised sequence would seem defective as well as vague. On the one hand, it would substitute governance by pressure groups and the negotiations of various private and public governments for genuine, one-man, one-vote majoritarian democracy [Dahl and Lindblom 1953, pp. 504–507]. On the other hand, it would substitute an elusive bargaining process among restrictionist and monopolizing economic power groups for market choice and coordination under a beneficent competitive regime. In Commons's view, both types of criticism miss the point. Drawing upon his own extensive personal experience as well as on intensive study of history, law, and administration, Commons contended that the negotiational, organizational political economy is the way contemporary collective capitalism works. The realistic alternative to organizational pluralism is not the economic individualism of classical theory, he averred, but the monopolizing proclivities of corporate monism. The most likely alternative to national bargaining in political life is not classical democracy, but some variety of totalitarian dictatorship. (Both Soviet-style communism and fascism, he observed, eliminate or emasculate the autonomy of labor unions, corporations, and political parties.) The basic rationale for encouraging and attempting to improve on the emerging and imperfect contemporary collective capitalism stems not from its tendency toward optimality or perfection (classical competition and classical democracy are superior on that score), but from the fact that it appears to be the only workable alternative to politico-economic forms (Soviet communism, fascism) that would destroy liberal and democratic values outright.

Commons was basically optimistic concerning the continued development and strengthening of what he called emerging "reasonable capitalism" or "collective democracy," characterized by an "equilibrium of economic power" among conflicting interests and classes. But that optimism was qualified by recognition of the power, yet internal disruption, created by "banker capitalism" (so-called because of the enhanced role of financial interests in twentieth-century corporate activities, notably in mergers and holding companies) and the appeals amid the dangers of the external ideologies and systems of fascism and communism. As to communism, Commons held that "Marx was even more nearly correct for the United States than he was for Russia or Italy." Massive industrialization, coupled with the surge to dominance of the large-scale corporation (facilitated by friendly Supreme Court decisions in the late nineteenth century and financial innovations in the twentieth, for example, the holding company), radically reduced the role of small proprietors, who were the "bulwark of American individualism," and created an industrial labor force of wage and salary workers, "the foundations of Communism or Fascism." Small businessmen and farmers are ground "between the upper and nether millstone of modern technology and business depressions. On the one side big business is absorbing their markets. On the other side wage-earners are demanding higher wages and shorter hours. . . . The conflict is irrepressible." As private property becomes corporate property, and individualism becomes "corporationism," as illustrated in the depths of the depressed 1930s, the "remaining small proportion of farmers become revolutionists by defying the courts and sheriffs in their attempts to foreclose mortgages" [Commons 1934, pp. 880–81, 885–86].

As to banker capitalism, Commons recognized that conflicts occur between classes or groups as well as between individual transactors, as evidenced by the fact that classes organize and consolidate "for concerted action according to similarities in economic interests" [Commons 1934, p. 109].

*Power,* he emphasized, is fundamentally a "question of class war, or class struggle, breaking out in strikes, lockouts, and even in military revolutions." Although these classes are many, rather than one or two, collective bargaining between organized labor and organized capital is the "major economic issue" to which other organizations and classes (farmers, bankers, merchants, and so forth) must "conform their policies and methods" [Commons 1950, pp. 262, 266].

Until the massive depression of the 1930s brought remedial action by government, an altered role for the Supreme Court, and a strengthened position for organized labor relative to capital, there is no doubt that American political as well as economic institutions strongly reflected the dominant position of propertied and financial interests and the large-scale corporations. Indeed, at least up to the depression, both legislatures and "voluntary private associations of laborers, farmers, small business men, and political parties" were "getting weaker and weaker in America" [Commons 1934, p. 898]. Still, Commons held, there are fundamental contrasts between American and European capitalism, notably, greater abundance, extension of stock ownership, promotion from within the ranks, and greater tolerance of small business, both because of small business efficiency in some areas and fear of political repercussions to monopoly. These factors, combined with the labor legislation of the New Deal and the resulting improved bargaining position for organized labor, supported Commons's qualified hope that a "balance of power between self-governing corporations and unions" and a "constitutional government of balanced equilibrium of propertied and unpropertied classes, capable of holding its own against military despotisms, may be foreseen on the American field" [Commons 1950, pp. 263, 268].

*John Kennth Galbraith:*
*Power and the Planning System*

In Commons's approach to political economy, corporations and labor unions are perceived as private economic governments. Individually, and in negotiation with one another, they comprise legislative, executive, and judicial components; formulate and administer policy; rule vast economic empires; seek legitimation of their rule; demonstrate complex relations between leadership and "citizens"; exercise moral and economic, if not physical, sanctions; and make treaties and strike pacts with each other. At the same time, government, especially administrative commissions and the Supreme Court, is intimately and inextricably involved in the administration of public economic policy and the economic activities of the "private" sector generally, notably the adjudication of disputes between and formulation of working rules for corporations and labor unions. The conflicting economic interests of groups and classes constitute the basis and determine the content of public policies, and economic breakdowns and economic class struggles serve as the root causes of wars and revolutions.

As Commons recognized, "*political* economy" is not merely a matter of governance; it is also fundamentally a question of power, of dominance and subservience in the determination and legitimization of goals, rules, and policies. From this perspective, politics and economics cannot be distinguished in terms of (overlapping) "sectors" of national life, "private" and "public," but only as alternative approaches to or ways of looking at society; and political economy implies thinking of economic activity as a power system as well as an economizing process.

Among contemporary economists in the institutionalist tradition, Galbraith is perhaps preeminent in perceiving and examining the evolving American economy as a political and power system. Schematically, we may identify four major kinds of power relations in Galbraith's writings: (1) those between business, especially large-scale corporate, leadership and the general consuming and working public (and, similarly, between political leadership and the citizenry); (2) the internal power relations within the giant corporations, notably, the shift in power not only from owners to managers, but therein, from managers to the "technostructure"; (3) the power relations between the "planning system" and the "market system"; and (4) the power interactions between business and government, exemplified by the "symbiosis" between big business and the public bureaucracy [Galbraith 1971; 1973; Fusfeld 1972]. We have already alluded to the first issue in connection with our earlier discussion of Galbraith's views on the emergence and evolution of corporate planning. In the interest of brevity, we reluctantly refrain from further comment on these matters here and also pass over the much-discussed second issue (the shift in intracorporate power to the technostructure) in order to focus upon the somewhat less familiar remaining two.

Among the remaining issues is the question of power relations between the planning system and the market system. *Power,* Galbraith asserts—defined as "the ability of an individual or a group to impose its purposes on others" [1973, p. 92]—is a central fact in contemporary political economy, rooted in technology and its correlative, corporate organization. But the comparative growth, size, and consequently power of the relatively more organized versus the relatively less organized parts of the economy (and between larger and smaller organizations) is "singularly uneven" [1973, p. 40]. Although the national economy is properly perceived as a continuum ranging from the smallest family farm to the largest corporate behemoth, it is analytically useful to distinguish between two broad sectors. The planning system consists of about one thousand Brobdingnagian corporations producing approximately half of all nongovernment output in manufacturing, power, transportation, finance, and merchandising. The other, the market system, consists of about twelve million smaller firms and farms, in trade, light manufacturing, services, and the arts; it constitutes roughly the "other half" of the national economy.

In terms of power, there are key differences between these two sectors. Both endeavor to control their economic environment, but by different means and with different degrees of success. In the market system, the enterprise is under the control of an individual (in either the proprietorship or the entrepreneurial corporation). Some degree of control over the economic environment exists in the form of product differentiation and local monopoly. Typically, such control is relatively small and tenuous and often depends on collective action or government assistance (for example, resale price maintenance laws, agricultural price supports, government support for collective bargaining) for its initiation or sustenance. The market system, granting its impurities and imperfections, functions more or less in accord with orthodox theory. By contrast, the control over the economic environment exercised by the giant technology-based "mature" corporate organizations in the planning system is both pervasive and powerful. Here, control emanates almost automatically, as a result of large size, supplemented by corporate strategies in such areas as internal financing (to insulate the organization from intrusions of stockholders and creditors), sales promotion, vertical integration, imperialist control over raw materials in Third World countries, multinational operations, and so on. And here, as noted earlier, corporate planning (although by no means the balanced integration of the various corporate plans) has largely superseded the market pricing system as a process for economic coordination.

Furthermore, the market system is part of the environment which the planning system seeks to control, while the planning system is part of an environment which is essentially beyond the control of the market system. Large corporations both sell to and buy from smaller firms, but at prices controlled by the giants. Given the uneven distribution of power between the two systems, the terms of trade between them "will have an insouciant tendency to favor the system that controls its prices and costs and therewith the prices and costs of the other system as well" [Galbraith 1973, p. 51]. In short, inequalities in economic power generate inequalities in income between the two sectors, as the big corporations manipulate prices charged and prices paid to their own advantage. In the absence of "unimpeded mobility" between the two sectors, these differences in the level and security of income can and will persist.

A second issue pertaining to power raised by Galbraith is that of the relations between business and government. Institutionalists, from Veblen to the present, have typically held an ambivalent attitude toward the role of the state and government policy in economic life. On the one hand, many, like Veblen, have taken it as virtually axiomatic that the state heavily reflects the dominant economic and class interests in capitalist society and that government policy, especially prior to the 1930s, essentially favored capitalist, propertied, and corporate interests. On the other, most have viewed the state as partially independent from business interests and thereby capable of at least quasi-independent programs of action, ranging from deterioration into authoritarian and dictatorial control over business as well as society to, under propitious circumstances such as the New Deal, genuine democratic reforms and policies more broadly reflective of the interests and perceived needs of nonbusiness groups and society at large.

Galbraith's contribution to this ongoing debate has been to distinguish between the methods and character of interaction with the state and influence upon public policy of the entrepreneurial, market-oriented enterprise (either proprietorship or corporation), prominent prior to World War II, and the mature corporation of the contemporary planning system. The entrepreneurial enterprise, rooted in the market system, had (and has) essentially a pecuniary relation with government. Under propitious circumstances, especially prior to the 1930s, it bought its favors (tariffs, franchises, mineral rights, tax exemptions) from receptive (and income-maximizing) politicians. Under less propitious circumstances, for example, the New Deal years, these favors would be reduced or (typically temporarily) withdrawn. In any event, it was (and is) not strategically dependent upon the state. The market, not government, was (and is) the main source of its income and wealth; and the temporary interruption of government largesse (assuming, although Galbraith does not make this explicit, the continued existence of market and private property relations) was unpleasant, but not fatal.

By contrast, the mature corporation, rooted in the planning system and ruled, according to Galbraith, by its technostructure, is both dependent upon government and enters into a symbiotic relationship with it. The planning system, "in fact, is inextricably associated with the state. In notable respects the mature corporation is an arm of the state. And the state, in important matters, is an instrument of the industrial system" [Galbraith 1971, p. 298]. As noted earlier, the giant corporations are dependent upon government, in Galbraith's view, for qualified manpower, education, regulation of aggregate demand, provision of capital, support of technology, and, notably in military production, markets. Consequently, opposition to government's expanded role in the economy (in these areas), so important to the business litany prior to World War II, has quietly evaporated in the age of the mature corporation. On the other hand, the mature corporation has come to influence and control public policy in intricate and subtle ways, notably through symbiosis with the public bureaucracies, especially in military production, facilitated by the tendency for many legislators to ally themselves with the bureaucracy and thus, by association, with the planning system. The symbiosis between business and government extends from the public bureaucracy and the regulatory agencies to societal goals. "The state is strongly concerned with the stability of the economy. And with its expansion or growth. And with education. And with technical and scientific advance. And, most notably, with the national defense. These are the national goals" [Galbraith 1973, p. 311] *and* those of the giant corporations. "A final source of political power for the planning system is organized labor" [Galbraith 1973, p. 161]. Labor-capital conflicts in the big corporations have been greatly reduced by the capacity of the corporations to pass on wage increases in the form of price boosts, by the "psychic identification" of workers in the planning system with the organization, and by the coalescence of corporate goals (for example, big defense budgets, steady employment, high growth rates) with those of organized labor.

### *Concluding Remarks*

The primary focus in this article has been expositional and illustrative rather than evaluational and comprehensive. Some brief comments of critical assessment thus may be in order. First, institutionalist political economy from Veblen to Galbraith does seem to demonstrate at least the unity and continuity implied by the expression "useful fiction" used at the outset of the article to justify treating contributors in the institutionalist tradition as a group. As we examine the views of such economists as Veblen, Commons, Ayres, Galbraith, and Myrdal, it would be misleading as well as ungenerous to deny that, despite individual differences on specific matters, somehow the whole of institutionalist political economy *is* greater than the sum of its individual parts.

Second, it is important to emphasize that the institutionalist approach to political economy, with its focus upon the interblended evolutionary development of technology, institutions, ideology, and economic behavior, group and power conflict, and the interpenetration of politics and economics, does not primarily (although it certainly does in part) offer different answers to the traditional questions of orthodox, economizing-oriented economic theory. Instead, it asks and endeavors to answer no less important but typically different—and larger—questions, notably those pertaining to issues such as discussed herein. Insofar as this is true, institutionalist political economy is essentially complementary to standard economic theory, even when economists of institutionalist persuasion offer their neo-neoclassical and neo-Keynesian colleagues few compliments (and vice versa). Assertions of superiority in debates between institutionalists and their critics—illustrated, for example, by Robert Solow's majestically disdainful concluding comment in his interchange with Galbraith [Solow 1967: "Apres moi, la sociologie"]—often seem to be more reflective of alternative methodological and philosophical perspectives concerning questions to be asked than of the validity of answers to given questions.

Third, ironically, compared to such analysts of institutional evolution as Marx and Joseph Schumpeter, a case may be made for the proposition that many American institutionalists have been *insufficiently* institutional, that they have spread their analytical nets too narrowly rather than too broadly. Although his judgment would probably be tempered somewhat today, notably as regards Galbraith, the main thrust of R. A. Gordon's assessment of the early 1960s retains much merit. Marx and Schumpeter, Gordon observed, "took the entire story of capitalist evolution and possible decline" as their province. American institutionalists have not gone this far with their institutionalism. Typically, their analyses have been framed "within a limited time perspective and with reference chiefly to American conditions. They have therefore not produced the comprehensive, evolutionary, and institutionally oriented theory that they sought. Their perspective in time and space was more limited than they realized. . . . They thought very largely in terms of American economic and social conditions during a few decades. And, in a sense, they did not ask big enough questions, did not equip themselves with the tools to answer systematically the questions that they did ask" [Gordon, in Dorfman 1963, p. 146].

Last, and related to the third point, institutionalist political economy, from its own perspective, might well benefit from closer links with other dissenting or unorthodox approaches (quite apart from maintaining interchange with the general body of economic analysis). With the notable exception of Veblen, institutionalists have kept Marx (and thereby possible insights from Marxian analysis) at arm's length. Despite the obvious parallels between his analysis of capitalist development and that of institutionalism, Schumpeter typically fares no better at the hands of institutionalists. His name appears only once, for example, in Gruchy's comprehensive volumes on institutionalism, in a footnote reference to Mitchell's cycle theory [Gruchy 1972, p. 44; 1947].

More recently, one wonders about the potential benefits of attempting to connect institutionalist analyses in the Veblen-Ayres tradition with the unorthodox studies of such British neo-Keynesians as those of Joan Robinson. Her dissent from the post-Keynesian orthodoxy (somewhat impudently but pointedly labeled "bastard Keynesianism")—including her focus upon income distribution and its relations to consumption and investment, her denial of a marginal product of labor or of capital, her rejection of the concept of equilibrium and substitution of a nonmechanistic process of historical dynamics, and, especially, her insistence upon saving as investment determined rather than the other way around—are remarkably similar to views expressed by Ayres, among others [Kregel 1973]. But, then, if economists in the institutionalist tradition were to establish closer connecting linkages with Schumpeter, Marxian studies, and such contemporary economists as Michal Kalecki, Robinson, and Piero Sraffa, the resulting interaction could well approach what a resurrected Veblen might call a "Grand Union" of dissenting perspectives; and one wonders whether *that* might not be more than the economics profession, if not American society, could reasonably absorb, to use Veblen's apt expression, "just yet" [Veblen 1921, p. 169].

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