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INSTITUTIONS AND  
THE CHALLENGE  
OF KARL POLANYI:  
ECONOMIC  
ANTHROPOLOGY  
AFTER THE  
NEOINSTITUTIONALIST  
TURN

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# **Institutions and the Challenge of Karl Polanyi: economic anthropology after the neoinstitutionalist turn<sup>1</sup>**

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## **Abstract**

In this paper, I reflect on ‘the neoinstitutionalist turn’ in the social sciences and its significance for the Polanyian tradition in economic anthropology. Recent trends in economic thought see the debates about the place of economic theory that engaged Karl Polanyi as obsolete, made redundant by the development of New Institutional Economics and their application to such questions. Even within economic anthropology this viewpoint has gained some ground. In this paper, I argue that this notion is mistaken.

In the following argument, I first introduce Polanyi’s role in these debates. Subsequently, I discuss the ‘neoinstitutionalist turn’ itself. Then, taking Douglass North’s response to Polanyi as a paradigmatic example, I argue that New Institutionalism suffers from serious conceptual deficiencies.

Therefore, I caution against the view, expressed among others by Acheson (2002), that economic anthropology could or should become an empirical appendage of the New Institutionalism. Instead, I argue for an alternative I associate with Earle (2002) and Gudeman (2012): the New Institutionalism can be useful only if incorporated selectively into existing economic anthropological research programmes, so that anthropology might encompass institutionalism rather than be swallowed by it. Therefore, ‘Polanyi’s challenge’ remains relevant to economic thought within and outside anthropology.

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## Introduction: Karl Polanyi, institutionalism, and the twin debates

The figure of Karl Polanyi (1886–1964) looms large in any discussion of what anthropological theory can contribute to the comparative study of economic systems from past to present.<sup>3</sup> Polanyi was not only an unusual figure in being both a theorist of economic anthropology and a researcher in economic history, despite the usually considerable intellectual and methodological distance between these two fields of study. More importantly, he provided perhaps the most influential and authoritative formulations of two major points of contention in the rivalry between the methods of economics and anthropology for the study of historical economies: the debates known as the primitivism-modernism debate and the formalism-substantivism debate. Each concerns an analytically separate theoretical and methodological problem, but in practice they are closely linked. Moreover, they have a common origin in the debates of the German Historical School in the late 19th and early 20th century: the *Methodenstreit* between Carl Menger and Gustav Schmoller over economic method and the debate between Eduard Meyer and Karl Bücher about the nature of the ancient economy.<sup>4</sup>

Without fully reviewing the vast literature on both debates, one can briefly summarise them as follows: the *Methodenstreit*, and subsequently its incarnation in Polanyi's work as the formalism-substantivism debate, concerns the question whether the study of premodern economies (and perhaps any economy) is best done according to the 'formalist' deductive and mathematically oriented methods of classical and neoclassical economic theory, or whether it rather requires an approach based in historical and anthropological interpretation of specific historical cases, from which generalisations can subsequently be made. In its original 19th century form, it was primarily a question of deduction based on economic theory versus induction based on comparative empirics alone, and apart from Polanyi this is how it has mainly been remembered in economic history (Nardinelli and Meiners 1988). Polanyi, however, extended this discussion much further by formulating his own 'substantivist' approach, based in anthropological theory, as a conscious alternative to approaches based on the then prevailing theories and methods of economics.<sup>5</sup>

The primitivism-modernism debate, by contrast, concerns the more specific question to what extent premodern societies (however defined) were institutionally similar enough to those of contemporary capitalism so that the concepts and theories based on the study of the latter can be fruitfully applied to the former. This was the bone of contention for Meyer and Bücher, in their case regarding ancient Greece (see Bang 1997). But in practice, of course, it is very difficult to say anything about the applicability of economic theory to a specific case without engaging in debates about which theoretical approach to economics is the correct one, as commentators on Polanyi have often found. Central to both debates, in any case, is "the question of the applicability of modern economic theory to non-market economies" (Humphreys 1969: 181), and it is for this that Polanyi is mainly remembered by economic historians and economists (cf. North 1977, see also below).<sup>6</sup>

<sup>3</sup> I draw in this discussion on Dale (2010).

<sup>4</sup> See respectively e.g. Louzek (2011), Reibig (2001) and Wagner-Hasel (2011) for discussions of the particulars of these debates.

<sup>5</sup> Note that in the Polanyian anthropological context, 'formalism' therefore came to mean using the mainstream of the discipline of economics as basis of inquiry into past and present economic formations, rather than the more specific meaning used in debates on economic methodology, where it commonly refers to an (excessive) reliance on mathematical models (McCloskey 1989; Blaug 1999). In this paper I will use the term in the former sense.

<sup>6</sup> Polanyi was not the only major anthropologist participating in such debates: see also e.g. Sahlins (1972, 2000) and Schneider (1974). However, in the historiography of premodern economic history he is beyond doubt the most influential representative of the alternative to reliance on economic theory. See also the discussion below.

Briefly surveyed, Polanyi's interventions into these debates were as follows. For him, the application of the conventional economic methods of his day (Menger's marginalism as the foundation of neoclassical economics) rested on an unsupported conflation of two different meanings of the economic: the 'formal' one of economising, a description of maximisation as a means-ends relationship, and the 'substantive' one, concerned with the empirics of how the production and distribution of goods was organised in a particular economy (Polanyi 1957: 243). His critique of this conflation then in turn formed the basis for his critique of the 'modernist' interpretation of economic history. This is evident in Polanyi's opinion of how the modernist viewpoint depends on formalist assumptions.

In the modernist perspective, all societies have sufficient commonalities in market-oriented individual rationality that the same theories and concepts can be applied to any historical case, only the empirical specifics being different. This modernism is based on a particular conception of markets that reduces the economic to choice in a market-like setting: any economic system under conditions of scarcity requires means-ends maximisation and therefore will be describable in terms of conventional choice theory designed for the study of market exchange. As one economic historian of antiquity recently put it, the market in economic theory is "nothing more than the abstract intersection of supply and demand for scarce goods and services. Economics is relevant wherever you cannot have your cake and also eat it" (Jongman 2014: 29).

Against this view, Polanyi denied the relevance and universality of scarcity and with it the universality of choice theory. Scarcity is for him a category specific to market exchange, the *result* of markets rather than their precondition: in societies where markets were not the primary 'mode of integration', such as most premodern ones, Polanyi argued, scarcity is not particularly relevant. Such societies have other forms of integration than individual choice in a market setting, and the operative rules are not those of individual utility maximisation but given social norms of social reproduction and preservation (Polanyi 1957). "Aristotle was right: man is not an economic, but a social being. He does not aim at safeguarding his individual interest in the acquisition of material possessions but rather at ensuring social good will, social status, social assets. Man's economy is, as a rule, submerged in his social relations", as he put it in one famous essay (Polanyi 1968: 65).

To summarise Polanyi's argument polemically, then, market exchange was not the main mode of integration in most of economic history, and this refutes the modernists; and the assumption of scarcity and the universal applicability of choice theory falls with this observation, thereby refuting the formalists. In *modern* society, Polanyi conceded, society is embedded in market exchange as the dominant mode of integration, and quite consistently, he was willing to accept the applicability of marginalist and neoclassical economic theory to our present circumstances. But for the comparative study of premodern societies, before the 'great transformation' that made land, labour, and capital fully commodified (Polanyi 2001 [1944]), a different theoretical approach was needed: the substantivist one, based on anthropological theory. And this forms the bridge between his anthropological critiques and his relevance for economic history, especially that of the premodern world.

As Polanyi himself put it, a new 'general economic history' was required (Polanyi 1977: xxxix). By this he meant a framework that would enable accurate classification and analysis of the full range of forms of economic organisation observable in historical and anthropological sources, including those in which interconnected price-making markets played little or no part. At Columbia, he and his collaborators launched a research programme to this purpose, using

anthropological ideas and methods to examine the nature of markets, trade, and money in a range of ‘primitive’ and archaic societies (Polanyi, Arensberg and Pearson 1957; Polanyi 1966; Polanyi 1968; Polanyi 1977). He saw the embeddedness of markets in antiquity as implying that market exchange was not the primary mode of integration of the provision and distribution of goods, of ‘livelihood’ as he put it, in premodern societies. Rather, the dominant forms of integration were combinations of reciprocity, redistribution, and householding. Central to his critique of the universality of choice theory was therefore what we may call – borrowing from James Carrier – a distinction between markets and the Market. As Carrier puts it:

“People in many times and places have engaged in trade, have given and received objects and services among themselves and with those in neighbouring societies, without necessarily having the notion of the Market. Equally, many people have developed markets, more or less elaborate institutions devoted to facilitating or channelling this trade, without necessarily having the notion of the Market. And again, many people engage in commerce, by which I mean market trade as a significant rather than an incidental part of their economic lives, without thereby developing the notion of the Market.” (Carrier 1997: 26)

I would argue that the difference between them, what Polanyi tried to capture by the term ‘modes of integration’, is a question of *institutions*. For what are the ‘social relations’ into which individual economic behaviour is ‘submerged’ or embedded but social norms and rules, institutions regulating economic behaviour to ensure the provision of ‘livelihood’ according to those same norms and rules? The noneconomic, the anthropological domain of rules, norms, and values, provides the instituting of the economy Polanyi referred to in his famous essay. Polanyi himself made the connection between his critique of the modernist case and the importance of institutional ‘noneconomic’ differences in history explicit:

“(…) the inclusion of the noneconomic is vital. For religion or government may be as important for the structure and functioning of the economy as monetary institutions or the availability of tools and machines (...). The instituting of the economic process vests that process with unity and stability; it produces a structure with a definite function in society (...) it centers interest on values, motives, and policy.” (Polanyi 1957: 249–250)

One could therefore, in contemporary terms, read Polanyi’s intervention in both the formalism-substantivism debate and the primitivism-modernism debate as one and the same *institutionalist* point. At its centre is the methodological argument that understanding comparative economic history involves abandoning market-centric assumptions in favour of a shift to the traditionally anthropological (‘noneconomic’) domain of social institutions and their regulative function for economic behaviour and organisation. Institutional analysis, based on anthropological insights, would replace the economists’ choice theory as the foundation of a comparative approach to economic life (in his substantivist sense) and its relation to the noneconomic.

This point is not original as such. The importance of institutional analysis to Polanyi’s approach to economics has been observed by various authors, so that some have argued he should really be seen as a (previously unrecognised) exponent of the ‘Old Institutional Economics’ (e.g. Stanfield 1980; Hodgson 1993; Maucourant 1995; Gudeman and Hann 2015: 16–19). This recognises also very well Polanyi’s peculiar role as a challenger of so many theoretical fields simultaneously. In

economic history, his primitivist perspective renewed the debates begun by the works of the German Historical School and Max Weber. In (social) anthropology, his substantivism has challenged, and continues to challenge, the dominance of assumptions derived from mainstream economics. But even in economic theory itself, he plays a potentially subversive role, insofar as in his work the Old Institutional tradition in that field can be said to have reached its fullest development, and its fullest range of interdisciplinary application (Rutherford 2011: ch. 8). As much as he was an important economic anthropologist, he also developed anthropological economics.

This insight is important, because it is precisely the image of Polanyi as an institutionalist economist that has in recent years threatened to render him obsolete, now that there is a new competitor on the scene: the *New Institutional Economics* (NIE) and its counterpart in economic history, the *New Institutional Economic History* (NIEH).<sup>7</sup> Although originally developments primarily within the discipline of economics, the core methodologies and ideas of the NIE gave rise to what I will call an ‘neoinstitutionalist turn’ in the social sciences more generally. It is seemingly no longer understanding the price system and getting it right that matters, but understanding institutions and getting *those* right. And in this context, Polanyi’s critique of the modernists and formalists and their lack of interest in the economy as an instituted process in history may seem to no longer have much traction. But is this true?

### **The Neoinstitutionalist Turn**

For some, the twin debates Polanyi was associated with have become irrelevant with the emergence of a new economics-based approach, one specifically aimed at studying institutional variation. The Old Institutionalism of Polanyi falls by the wayside and the New Institutionalism supplants his anthropologically inspired approach. One of the most important figures in this development is Douglass North and his NIEH. More generally, however, one finds this perspective frequently in contemporary reflections on the legacy of the twin debates in economic history. Several recent major studies of the ancient Greek economy are founded on the premise that “the inspiration of the neo-institutional economists allows us to go beyond the old debates between primitivists and modernists or substantivists and formalists” (Bresson 2015; Ober 2015). Many recent works on the economics of antiquity feature the observation that the debate was “sterile”, debased by strawmanning, and that it failed to recognise how both sides could find a common ground in the analysis of historically specific institutions within a larger (mainstream) economic framework focusing on property rights and economic growth (e.g. Saller 2005; Morley 2007).<sup>8</sup> For Elio Lo Cascio the New Institutionalism permits a way to study state and market in the Roman Empire beyond the “heuristically ineffective” models of Polanyian substantivism and “the modernism of Rostovtzeff” alike (Lo Cascio 2006).

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<sup>7</sup> In this paper, I will frequently refer to the New Institutional Economics (NIE) as a whole, but where relevant the specific form given by North, his *New Institutional Economic History* (NIEH), must be distinguished, as it is not in every respect representative of New Institutional theory (Dequech 2002). Also, unlike most NIE theory, it is primarily concerned with historical explanation and is therefore not just economic theory proper. However, these aspects make it particularly suitable as a strong case for the NIE, illustrating the problems with an even more sophisticated formulation of NIE theory than most. See also p. 7 on distinguishing NIE and ‘neoinstitutionalism’.

<sup>8</sup> For a lengthier discussion of the neoinstitutionalist turn, the primitivism-modernism debate and the case of ancient Greece, see Krul and Dale, forthcoming.

Even insofar as economic historians disagree on the relationship between market and state, such debates are increasingly formulated in New Institutional terms. As Koenraad Verboven notes,

“(…) one of the fiercest polemics, for instance, is that between the economic historian Peter Bang and the economist Peter Temin. The latter approaches the Roman economy as market economy. The former sees the Roman economy as a developed ‘bazaar-economy’ and the Roman empire as a predatory ‘Natural State’ in the sense defined by North, Wallis and Weingast.” (Verboven 2014: 75)

In a quite different place and era, Sheila Ogilvie used an analysis of records on Bohemian serfdom in the late Middle Ages to argue against Polanyi’s (and Chayanov’s) critiques of ‘formalism’ and its applicability to premodern economies (Ogilvie 2001). An important part of her argument was to demonstrate that Polanyi and Chayanov, as major critics of the economic fallacy, were wrong. She attributed to both the claim that peasants in these societies made decisions in a qualitatively different way from modern market society, and a way that could not be described using standard economics. Ogilvie tried to demonstrate, on the basis of the records, that even these Bohemian serfs were perfectly able to understand economic concepts and were essentially utility maximising agents. First she showed that the serfs in question used local markets extensively. And secondly, that they used money and understood its use.

Having made this argument, using equivalents of opportunity costs, and so forth, she then emphasises – contrary to simple ‘modernist’ interpretations – that the world of the Bohemian serf was nonetheless a very premodern one. Her formulation of this point, in fact the conclusion of the paper, is particularly telling:

“(…) pre-industrial Bohemia has no claim to be a unique enclave of economic modernity. Its rural economy suffered from lack of information, sparse transactions in many sectors, high risks, frightening insecurity, grinding poverty, and starvation (...) However, available evidence for the estate of Friedland suggests strongly that the obstacles to economic success for Bohemian serfs, and hence those aspects of their economic world on which we must focus, were external and institutional, not inward and cultural.” (Ogilvie 2001: 451)

We see here how ‘institutions’ become a way of navigating between the claims of ‘modernism’, here in the form of attributing market efficiency and performance to a Renaissance servile setting, on the one hand, and the introduction of the ‘cultural’ as an independent variable or relevant constraint, on the other hand.

This is not limited to economic history alone, but it is a wider trend in economic thought about the relation between markets, economic behaviour, and the “social, cultural, and psychological” historical specificities that so interested Polanyi. A recent critical reflection in archaeology declares that

“(…) this seemingly is an appropriate time to challenge old paradigmatic presumptions, given aforementioned declarations that the formalist/substantivist debate is now over, recognition that marketplace exchange and interconnected market systems have a much longer and geographically broader presence than just the last two centuries, and growing awareness, even in some quarters of economics, that there is no such thing today or in history as a completely free, entirely self-regulating market economy. This latter point is key, as it affirms that the

comparative metric long employed to ignore or diminish the importance of markets in the past (because they were embedded in their larger societal and political contexts) was misguided. All economic systems and markets, past or present, are embedded, albeit in different ways and to distinct degrees.” (Feinman 2013: 454)

Moreover, the observation that the problem with Polanyi’s view is the universality of embeddedness (contrary to Polanyi’s own periodisation of this concept) is a commonplace in Polanyi criticism (Barber 1995; Block 2003; Gemici 2008; Beckert 2009). It is also an important component of the convergence between post-Polanyian perspectives and the NIE in other social sciences, for example in the New Economic Sociology (Krippner et al. 2004; Beckert 2003, 2009; Granovetter 1985; Richter 2015; cf. Machado 2011).

Such views are part and parcel of the larger neoinstitutionalist turn in which NIE concepts and theories have become a powerful new way of thinking across various disciplines of the social sciences, from economic history to sociology and anthropology. This term has been used previously to indicate the increasing popularity of NIE-type approaches in political science (Aspinwall and Schneider 2000), where it is tellingly synonymous with the ‘neo-institutionalist turn’, but it can be extended more broadly to the contemporary fashion for institutional analysis and borrowing of NIE concepts or terminology in the social sciences. Within this turn, it is possible to define as many as four different sub-neo-institutionalisms, from rational choice NIE to historical, sociological, and even discursive neo-institutionalism (Schmidt 2010). I will not concern myself here with these specifics, but rather focus on the more general point: the ubiquity of the term ‘institutions’ in contemporary social science writing, usually invoked under the slogan that “institutions matter”. While this does not say very much on its own, it is a way of representing approaches that go beyond simplistic rational choice sociology or neoclassical economic models as well as the descriptive traditions often seen as ‘lacking in theory’ (as the Old Institutionalists tend to be perceived by the New – see Rutherford 1994).<sup>9</sup> Searching for ‘institutions matter’, one finds hundreds of social science journal articles containing this phrase, largely written in the last 15–20 years. Of course, the concept of an institution is much older, and this tells us little about *how* institutions matter. This is where the NIE comes in, for it has contributed a great deal to the definition of institutions and thereby the popularity of the turn. The neoinstitutionalist turn is therefore best understood as those trends in social science in which ‘institutions matter’ is taken as the explanatory research core and where NIE theory in one or another form is the theoretical context.

In order to understand the relationship of Polanyi’s work to this turn, the most significant author is probably the late Douglass C. North. With his colleagues, he has perhaps done more than any other to develop the New Institutional approach into a wide-ranging and ambitious theoretical framework whose scope extends across the social sciences as a whole (North 2005; North, Wallis, and Weingast 2009). The New Institutional Economics can be seen as the systematic theoretical development of these insights: the importance of market failure and transaction costs on differences in market structure, and subsequently the study of how social norms, rules, and conventions lead to political economic structures, such as property rights regimes and political regulations, that

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<sup>9</sup> An early and influential economic example of this claim that “institutions matter”, intended as a ‘theorised’ critique of neoclassical orthodoxy and influenced by the work of North, is Burki and Perry (1998). For the World Bank, it is one of the main lessons learned from the failure of the so-called “Washington Consensus” over no less than the last fifty years (World Bank 1999: 1). See also Rodrik, Subramanian and Trebbi (2002).



engender higher or lower levels of such transaction costs and market failures. At the heart of the NIE approach is therefore what Eggertsson (1990: xiii) has called the “successive endogenization” method: First, economic institutions such as property rights are taken as exogenous and modelled for their effect on market transactions, then the structure of market exchange is endogenised with property rights still exogenous, and finally, social and political institutions are endogenised by reference to reduction of transaction costs. Douglass North’s NIEH is arguably the furthest extension of this process of successive endogenisation, as in his most developed work, entire social-institutional structures (“artefactual structures”) are the result of trade-offs under uncertainty between markets and other allocation systems, mediated by both formal (legal and political) and informal (cultural, social, and tacit).

### **North, Polanyi, and Successive Endogenisation**

One of the clearest examples of how this successive endogenisation approach has developed explicitly as a rival to the Polanyian research programme – and its anthropologically rather than economic theory derived institutionalism – is North’s discussion of Polanyi in his 1977 paper on ‘the challenge of Karl Polanyi’ (North 1977). “Anthropologists, sociologists and historians”, North argued in this paper, “have long challenged the relevance of economic theory to the analysis of past societies” (ibid.: 703). However, this theory, defined in this paper as the “wealth-maximizing behavioural postulate”, has survived among neoclassically oriented economic historians because they have generally been unconcerned by the implications of such theoretical background choices. One cannot directly test them anyway, “the proof of the pudding is in the eating” (ibid.: 703–704). Polanyi, he said,

“(…) cannot be so lightly dismissed, and if his spirit does not haunt the new economic historians, it is because they are probably not even aware the ghost exists (…) Polanyi contends that markets have only dominated resource allocation for a brief span of history centering on the nineteenth-century Western world. Before that time (…) other allocative systems have characterized economic organization and these other systems are not grounded in economizing behaviour.” (North 1977: 703–704)

North is ambivalent about the value of this viewpoint. He explains Polanyi’s theory of ‘transactional modes’, which include – besides market exchange – reciprocity and redistribution, and how for Polanyi these last two were the dominant or characteristic modes of the economies of premodern societies. Markets dominate only in the most recent historical period, and even then only outside Soviet-type societies. In this, he rightly notes, Polanyi opposes both the neoclassical and the Marxist approaches. Each of these represents an opposed social force within modern market society, a society that has only emerged out of the Industrial Revolution. For North, “it is easy to find fault with Polanyi’s analytical framework” (North 1977: 706). Indeed, “there are numerous parts of his analysis that show a failure to grasp elementary economic principles” (ibid.). Economic theory, in other words, is not on Polanyi’s side. And yet North is deeply impressed by the significance of this challenge. For

“(…) the stubborn fact of the matter is that Polanyi was correct in his major contention that the nineteenth century was a unique era in which markets played a more important role than at

any other time in history (...). To the extent that economic theory was confined to the analysis of markets, the tools of the economist were (...) irrelevant to an understanding of the ancient world (...). Economic historians have not even begun to account for such non-market allocative systems, and until they do, they can say very little about societies in which markets had very limited allocative effects.” (North 1977: 706–707)

He takes as good a definition of embeddedness as one could wish for from Polanyi directly:

“The key to Polanyi’s system is the view that economic organization is embodied in society in the sense of ‘having no separate existence apart from its controlling social integument’ (...). Transactional dispositions of natural resources, labor, produce and services are expressions of socially defined obligation and relationships.” (North 1977: 708)

The consequence being that

“(...) the kinship, status, hierarchy and political or religious affiliations which underlie these economic structures are not explicable in terms of economizing behaviour – one can only understand them and therefore the functioning of the economy by ‘in depth’ studies which are social, cultural, and psychological in origin.” (North 1977: 708)

This brings us to North’s own solution. To answer the challenge of Karl Polanyi means two things: firstly to shift the emphasis of research to the study of premodern economic history – that is to say, the economic history of the period before the Industrial Revolution and the dominance of the market as allocation system – and secondly to give an explanation of the nature and functioning of the alternative allocation systems that dominated in the premodern era. The answer to this challenge must be based in ‘economic theory’, as North put it, rather than exclusively in the “social, cultural, and psychological” explanations that Polanyi favoured: those types of explanations and in-depth studies that have defined the domain of an independent theoretical tradition in economic anthropology both before Polanyi and since.

The economic theory in question is no longer to be the simple extension of neoclassical economics to the past that Polanyi dismissed as the ‘economistic fallacy’ (Polanyi 1977: 25–26). Rather, it is to be the NIE, in this form also known as transaction cost economics. Explanations in terms of transaction costs would challenge the claim of anthropologists – who were Polanyi’s main sources of theoretical and empirical inspiration to grasp the domain of the ‘social’: the socio-political structures and cultural norms in which these economic structures were embedded. As North put it in the final sections of his paper:

“Polanyi conceived the custom, kinship arrangements, status, etc., to be fundamentally a result of non-economic forces whereas [North’s view is] consistent with an explanation that they evolved as ways to reduce transactions costs (*sic*) (...) It was Karl Polanyi’s intuitive genius that he saw the issues. A transactions-cost approach offers the promise of providing refutable explanations for these ‘transactional modes’ (...). We can and should be able to predict the direction of institutional change [though] the precise form it will take is still beyond the scope of the state of the art.” (North 1977: 715–716)

It is no exaggeration to say that North’s NIEH research programme, as he continued to develop and extend it over the subsequent four decades or so, is visibly outlined here and as nothing less than an

answer to the challenge of Karl Polanyi. For present purposes, this insight is not so much important for a better understanding of North's work (although I believe it necessary for that). More importantly, it shows how the neoinstitutionalist turn in the social sciences, based on the logic of successive endogenisation, is in one of its most influential forms a conscious effort to relegate Polanyi to the ranks of the obsolete economic theories. One could summarise North's 1977 paper as arguing that Polanyi asked the right questions of the economic historians of his day, but that whatever theories he developed to answer those questions, the NIEH can do better. In fact, that for North the NIE(H) approach has a domain of application potentially overlapping with all the social sciences as a whole, and his simultaneous insistence that typically 'non-economics' questions like those posed by Polanyi are best answered by 'economic theory', by which he meant NIE theory, has led some critics to view him as one of the primary exponents of economics imperialism in contemporary economic thought (Fine and Milonakis 2009).

### **The Neoinstitutionalist Turn and Economic Anthropology**

As one might expect of a field perhaps more marked by the legacy of Polanyi than any other, the neoinstitutionalist turn has engendered occasional enthusiastic support but also considerable resistance in economic anthropology. Nonetheless, few major NIE theorists have concerned themselves much with anthropology. Although reviews of NIE literature often include anthropology as one of its sources in the social sciences (Klein 1999: 456; Menard and Shirley 2005: 2), this is not supported by the actual bibliographical data of major texts in NIE theory. Even in the case of North and colleagues, explicit references to anthropology virtually disappear after his encounter with Polanyi, with the exception of a few passing observations on Johnson's and Earle's (2000) work on the emergence of chiefdoms and hierarchies in small-scale societies (North, Wallis, and Weingast 2009: 52–53). Other theorists like Oliver Williamson, being closer to the economic mainstream, consider anthropology to be simply outside their domain of research (Hodgson and Gindis 2007: 378). Finally, on one occasion Harold Demsetz used the work of the anthropologist Eleanor Leacock to defend an NIE-based theory of the emergence of property rights (Demsetz 1967). However, he did so by transforming her work into the conceptual apparatus of the NIE and thereby assuming much of what Leacock sought to contest (Gudeman 2012: 79–83; see also below). A possible exception is Elinor Ostrom; although her work is clearly situated within the NIE paradigm, the way it provided an influential rejoinder to Garrett Hardin's rational choice institutionalism and his scepticism about the viability of the commons (Ostrom 1990; Hardin 1968), together with her interest in the institutional and social specifics of commons as field sites place her in some ways closer to the practices of anthropology than any other major NIE author (see also Hann 2014; Donahoe 2009). Even so, her work has been hailed together with that of North and others as an example of how the neoinstitutionalist turn can be good for anthropology (Acheson 2011).

This latter view, that the neoinstitutionalist turn should apply to economic anthropology as well, is subject to an ongoing controversy in the field. Within the subdiscipline, there are different viewpoints: some reject the NIE approach altogether, others accept it, but do not necessarily agree with each other on what this acceptance implies in theoretical or methodological terms. A brief review of some representative examples of these differing views may help shed light on what is at stake in the New Institutionalism debates. The first aspect of importance is that as in other domains

of economic thought, the neoinstitutionalist approach is seen by sympathisers as particularly attractive because it offers a way to go beyond the twin debates and respective positions associated with Karl Polanyi.

We find, for example, in as early as Stuart Plattner's influential 1989 handbook in economic anthropology the observation that

“(...) the contributors of this book can in fact identify with both sides of the [substantivist-formalist] debate (...). The relevance of market theory to tribal society must be demonstrated, not assumed. On the other hand, we understand that all humans exercise economic choices, subject to their local institutional constraints.” (Plattner 1989: x)

In essence, this contains nothing fundamentally different to North's statements on the same subject.<sup>10</sup> This takes us to the theoretical core of the neoinstitutionalist turn as it has affected economic thought beyond economics itself. This core consists of a powerful combination of choice theory borrowed from economics with the insight that ‘institutions matter’. The strengths and weaknesses of the neoinstitutionalist turn beyond economics itself derive from the combination of these core propositions. Plattner's observation also shows how easily this combination can come to seem as obvious an answer to the dichotomies of the Polanyian debates as it did to North and similar authors with a background in economics. In a different but comparable vein, Douglas (1986, 1995) recasts the structure-agency problem of autonomy in group structures as a case of institutions creating constraints on individual choice, in a way immediately reminiscent of (and modelled on) the approach of the NIE. For her this constitutes a way of overcoming the ‘methodological individualism’ that is an important component of what Polanyi described as the economistic fallacy.

More recently, the collection of papers on New Institutionalism and economic anthropology edited by Jean Ensminger (2002) has provided us with two different types of sympathetic views to the neoinstitutionalist turn in economic thought. The one is an enthusiastic reception of NIE theory by James Acheson, whose previous work had already defended the utility and necessity of the New Institutional approach for economic thought (Acheson 1994). The other contribution, written by Timothy Earle, expresses a more complex picture: although, as we have seen, his work is one of the few examples of economic anthropological literature used as a reference point in the work of North, Earle himself has a more ambivalent attitude to the implications of NIE theory, even while remaining generally in agreement with the notion that the neoinstitutionalist turn is helpful insofar that ‘institutions matter’. Earle's perspective is particularly interesting because it rather attempts to reconcile the Polanyian and the neoinstitutionalist approach, while rejecting some of the stronger NIE-based claims in North's work.

Looking at it in more detail, we could use Acheson's and Earle's respective contributions as typological representatives of two different ways of integrating the neoinstitutionalist turn with the traditions of economic anthropology. Acheson's discussion focuses on transaction cost economics itself, how it works, and the ensuing recognition that “a very large number of social and cultural factors affect transaction costs” (Acheson 2002: 29). As Acheson notes, at the heart of this is the insight that markets are usually incomplete and imperfect and that therefore institutions are needed to “secure expectations”, which in turn “constrain choices and open opportunities” (ibid.: 30). Most

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<sup>10</sup> The collection also includes contributions from James Acheson and Allen Johnson, among others.

interesting is the section suggesting how economic anthropologists might use this theory. Polanyi is (among others) invoked as an example of studying ‘market rules’ in this vein, with reference to his work on the early empires (ibid.: 38; Polanyi, Arensberg and Pearson 1957). Personal ties and social relations of various sorts can be reconceived as “substitutes for information” (Acheson 2002: 39) and all sorts of phenomena from hybrid economic organisations to ‘ethnically homogeneous middlemen groups’ can be seen as savings on transaction costs via endogenous enforcement of contracting and trust-building (ibid.). This builds on the work of Janet Landa and Jack Carr (e.g. Carr and Landa 1994). Although Acheson rejects Williamson’s rational choice interpretation of neo-institutionalism, insofar as he does not think that institutions and organisational forms are solely rationally ‘chosen’ on the basis of transaction costs, he suggests with Mary Douglas that this assumption can be corrected by treating degrees of opportunism as a constraining variable, itself endogenously emerging from group structures and norms (Acheson 2002: 43–44).

In concluding, Acheson observes critically that transaction costs cannot be measured, and that this is a serious drawback for the NIE approach. Most significantly, he sees it as an advantage for anthropologists: because there is also no consensus on how norms and rules (institutions, in North’s jargon) are generated and because there is a need to extend NIE analysis to non-market and non-modern (or non-Western) settings. Economic anthropology is, for Acheson, well placed to fill that gap. He seems to suggest practitioners should take the NIE as their methodological point of departure and fill in the missing empirical information on sources of institutional variation within this framework of institutions, organisations, and constraints (ibid.: 50). Along these lines, economic anthropology becomes an empirical component of the NIE.

Earle’s article is about “how the extent of commodity distribution in non-mercantile and non-capitalist economies reflects the organizational character of political economy in these societies” (Earle 2002: 82). This is the main question in dispute between the substantivist and the neoinstitutionalist paradigm: what is the relationship between social and political institutional order and particular economic structures and behaviours, especially market ones? With this question, Earle points to the heart of the matter. As he argues, the NIE approach would lead one to predict that with increasing development of state structures (North’s ‘chiefdoms’) the consequent reduction in transaction costs would show corresponding increases in volume of exchange. But this is not the case: there is no linear relationship between exchange and expanding institutional organisation (ibid.: 83, 87). Instead, commodity flows in early societies are the dependent variable of political organisation in the sense that chiefs and leader figures are to greater or lesser extents, or in different ways, able to acquire goods for maintaining their status or prestige, and this class reproduction is the independent variable (ibid.: 92). In some sense, this is the opposite of Acheson’s vision and that of the neoinstitutionalist turn as doing away with the old debates in anthropology and economic history. Notably, Earle explicitly sees Polanyi’s premise, here formulated as the “insight that a basic dimension of human institutions is economic” and that a “typology of exchange mechanisms that would be... embedded in specific social forms”, as the right point of departure for the economic anthropological study of premodern political economy (ibid.: 95). The NIE’s transaction cost approach becomes a special case of a more general approach based on “the particular means that mobilize and invest surplus”, and Earle envisions a “new economic anthropology in which institutional economics becomes placed in the comparative perspective of historical and archaeological studies and of the evolution of human societies” (ibid.: 98).

The Achesonian perspective, in which economic anthropology is fully integrated into the New Institutional research programme and therefore accepts the implications of the neoinstitutionalist turn to their fullest extent, has encountered a good deal of resistance within economic anthropology. In most cases, the NIE and its ambitions seem to have been simply ignored or dismissed as yet another case of Western economic theory inapplicable to non-Western societies.<sup>11</sup> This should come as no surprise, since economics and anthropology are barely in communication with each other in general (Pieters and Baumgartner 2002; Cosgel 2006). However, one significant economic anthropologist who has engaged with NIE theory at length is Stephen Gudeman. Taking from Polanyi the dual model of the economy – embedded and disembedded – but projecting this onto all economic formations, somewhat along the same lines as the Polanyian economic sociologists cited above, Gudeman has argued against the explanatory universalism of NIE theory. In fact, although Gudeman’s argument is more explicitly phrased as a rejection of the work of major NIE authors, his reasoning is quite similar to Earle’s in some respects.

For Gudeman, the NIE’s rational choice implication that institutional arrangements are, at some stage or in some way, ‘chosen’ so as to minimise transaction costs is to neglect the dimension of mutuality *as opposed to market* in the economy. Since transaction costs apply only to market exchange in the first place, being expressed in prices, the assumption of the universality of the implications of transaction cost economics is based either on serious omission or circular reasoning (Gudeman 2012: 83–84, 96).<sup>12</sup> He has also extensively criticised the work of Janet Landa and her application of NIE theory in an anthropological context (indeed the same works referred to in Acheson’s plea for the neoinstitutionalist turn). Landa’s hope – typical for the enthusiasts – was that the turn would lead to the “unification of the social sciences” (Landa 1994: 38). Against this ambition, Gudeman has argued that her attempt to explain paradigmatic cases of economic anthropology such as the *kula* trade in terms of rational choice and transaction costs constitutes “colonizing” local practices (Gudeman 2012: 121).

For Gudeman, it is evident that forms of ‘mutuality’ like the *kula* trade cannot be explained by or reduced to institutions that minimise transaction costs, just as Polanyi saw reciprocity as irreducible to economic behavioural principles (Polanyi 1957: 47). But for Landa, it is equally evident that they must be, if they are to be explained at all. In this context, it is interesting to note that this explanation in Landa’s work of Polanyian reciprocity as an institution to reduce transaction costs is not new. The debate between Gudeman and Landa is mirrored by an earlier debate, none other than the confrontation between North and the challenge of Karl Polanyi: in his 1977 paper, North already suggests that what Polanyi sees as evident cases of reciprocal economic behaviour could be explained by transaction cost economics along just these lines (North 1977: 713–715). Given this observation, and also given the polar oppositions and the tone of the polemicising in the above debates in contemporary economic anthropology, we are here not so far removed from the formalism-substantivism debate after all. The neoinstitutionalist turn seems to contain more of a ‘return of the repressed’ than its exponents have imagined. But such parallels do not, of course,

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<sup>11</sup> Ensminger (1998) suggests that the neoinstitutionalist turn has had a considerable impact on the work of evolutionary and paleo-anthropologists, but – aside from her own work and that of Acheson – relatively little on ‘sociocultural’ anthropology. She ascribes this to the influence of postmodernism, but also to the intellectual heritage of Anthony Giddens and Pierre Bourdieu. Polanyi is not mentioned.

<sup>12</sup> Gudeman thus considers the NIE to be part of ‘mainstream economics’ as much as its neoclassical rival. Another important argument is that both economic paradigms rely on assuming the universality of instrumental reason and commensurability (Gudeman 2012: 52–54). I will not discuss the latter here, but return to this observation about the use of rationality below.

settle the question: does this approach really allow us to go beyond the Polanyian debates, and achieve a step towards unifying the social sciences? Should economic anthropologists all be New Institutionalists now? Or are Earle and Gudeman right that any incorporation of the neoinstitutionalist turn must take Polanyi's own form of institutionalism, as expressed in his interventions into the twin debates, into account?

### **Economic Anthropology on the Crossroads between Polanyi and North**

As I have sketched it here, the Acheson approach subsumes economic anthropology into the NIE(H) research programme, where its main purpose is to provide empirical and in-depth studies that evidence which particular institutions operate as constraints in particular cases (past or present). The Earle-Gudeman approach can be said to be the reverse: it sees NIE as a special way of looking at the effects of institution formation on exchange, but which in its direct implications – at least in North's version – is likely to be misleading. The NIE(H) provides potentially useful tools for thinking about exchange, but cannot stand on its own as an explanatory theory, let alone substitute for the existing intellectual heritage of economic anthropology in the study of nonmarket production and exchange of goods. For this approach, the Polanyian comparative study of different kinds of embeddedness, in Earle's case given a Marxist flavour with an emphasis on class reproduction and surplus flows, is the general case and the NIE is subsumed within that. This leaves us with the original question posed by North in his 1977 paper contrasting the two schools of thought: can NIE(H) theory answer the challenge of Karl Polanyi, at least for the purposes of economic anthropology?

To answer the question, we must look more closely at a number of points of tension within the NIE paradigm itself. I will focus here on three aspects of NIE theory that are potentially hazardous for economic anthropologists inclined to follow Acheson's path: the market, rationality and choice, and indeterminacy. All three reveal aspects of the institutionalist turn that, I shall argue, show that economic anthropologists would be wiser to follow Earle and Gudeman's road. However, I want to make clear in advance that this should not imply a wholesale dismissal of NIE theory. I take Earle's point to be an important one: economic anthropologists *do* do well to engage with New Institutionalism, even if it is because it will become increasingly inescapable in the social sciences. The best means to achieve this is to look for ways to integrate it into existing theoretical contexts, while (as both Earle and Gudeman assert in different ways) there remain reasons for scepticism about the stronger theoretical claims of the NIE tradition. In this perspective, the neoinstitutionalist turn can be integrated as a potentially useful set of tools rather than a substitute for traditional anthropological argumentation, but only if its nature and limitations are properly understood, and its domain of application given the thought it deserves. By the following critical discussion of North's NIEH as a paradigmatic case of New Institutionalism, at least insofar as its influence has affected anthropology, I hope to contribute to finding ways to achieve this more fruitful synthesis.

#### *The Market*

One of the frequent criticisms of the New Institutional paradigm is that it takes market exchange as a point of departure: it explains how institutions and nonmarket hierarchies relate to market exchange, but does not explain the origins or function of market exchange itself (Ankarloo and Palermo 2004). This applies in particular to the work of Oliver Williamson, for whom as we have

observed the historical and anthropological dimensions of the rise of capitalist society are not of interest. Williamson's famous statement that "in the beginning there were markets" is indeed the premise of his work (Williamson 1975: 20). This stands in stark contrast to the primitivism-substantivism of Polanyi, for whom tracing the origins of modern market society was one of the primary goals, indeed to the point of equating capitalism with the emergence of price-making, autonomous market exchange as such (Bell 2002). Moreover, Polanyi made an important distinction in the comparative analysis of historical economies between money, markets, and trade, something not apparent in the Williamsonian approach that conflates them all anachronistically into 'The Market' (Carrier 1997).

In the case of North, the picture is more complex, but the same fundamental problem reappears in a more indirect way. North's 1977 essay makes it clear that the challenge of Karl Polanyi was for him as much to show that the NIE approach could account for *nonmarket* forms of allocation as for the rules of operation of market exchange. Moreover, North was – although trained in economic theory – an economic historian and therefore put the historicity of economic phenomena at the centre of his work, unlike Williamson.<sup>13</sup> Directly following on his discussion of Polanyi's embeddedness viewpoint, North points out (correctly) that one implication of Polanyi's argument is that exchange and trade must not necessarily imply "economic motivation" – meaning a profit motive.

It is clear to North that Polanyi's definition of markets is a very specific one, namely the *price-making market*. The absence of this type of market exchange, with its independent endogenous logic of supply and demand, in premodern economies is the cornerstone of the latter's analysis of economic historical differentiation.<sup>14</sup> Polanyi importantly distinguished markets *per se* from what he called 'price-making markets', one in which supply and demand act as independent forces to determine the relative prices of goods and which is integrated, or tends to integrate, into a larger system of market exchange (Polanyi 1957: 255; Stanfield 1999: 214–215). As North points out, this seems to apply to markets with "a large number of buyers and sellers, a variety of goods, an agreed-upon medium of exchange and an enforced set of property rights" (North 1977: 710). For North, it is the latter that is decisive: the property rights arrangements (and their enforcement) determine transaction costs (information costs, measuring costs, and so forth) and thereby the viability of such markets compared to other forms of exchange. The salient point is that "the costs of defining and enforcing property rights (...) lead to non-price allocation of many goods and services today (...) transactions costs in the ancient past would have been an insuperable barrier to price-making markets throughout most of history" (*ibid.*: 709–710).

For the standard NIE perspective on 'markets versus hierarchies' the choice between market contracting and hierarchical non-price structures is between the twin poles in an efficiency tradeoff (Williamson 1996). North here appears to extend this concept of markets and other 'allocation systems' (in North's jargon) as a choice within a tradeoff structure to Polanyi's distinction between price-making markets and other 'modes of integration' (in Polanyi's terms). For North, the NIE version of the economics approach can be extended to viewing the 'choice' for one or another of these transactional modes as a response to transaction costs. It should be noted, especially in light

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<sup>13</sup> Other NIE-oriented economic historians such as Avner Greif use slightly different methods than North, but come to similar theoretical conclusions. See e.g. Greif (2006).

<sup>14</sup> Polanyi's argument has the caveat that the period of Hellenistic Greece to the heyday of the Roman Empire was, for him, characterised by such markets. Polanyi therefore, quite consistently, considered those societies as of one piece with modern 'capitalism' (Polanyi 1977: 273).



of Earle and Gudeman's criticisms of NIE theory, that roughly from North (1981) onwards he dropped the Williamsonian rational choice assumption that the terms of such tradeoffs can be deduced from efficiency criteria. So what determines the 'choice' of institutional arrangement? While North is keen to reject conventional rational choice explanations, he ultimately finds no alternative to "players of the game" who choose for the purpose of "lining their pockets" (see North 2005: 79). While pointing out that the literature differs on the precise nature of the firm (a hierarchical structure, a legal fiction, a joint production arrangement), North agrees with all that it is a "wealth-maximizing institution which substitutes for price-making markets". And so, North says, "*it is reasonable to assume that the forces that lead to the substitution of firms for markets today may also help us to explain the variety of forms of economic organization in past societies*" (North 1977: 711, emphasis added).

In other words, the neoinstitutionalist choice theoretical approach can, by extension, explain the past 'choice' for nonmarket forms of allocation. If firms substitute for markets in order to maximise wealth, given the constraints necessitating a tradeoff between them, North seems to argue, why should not other allocation systems be just like firms and also choices within a wealth-maximising tradeoff? It is reasonable to assume that the forces of competition, motivation, or whatever may be involved are no different in past societies as in the present, insofar as this type of institutional choice is concerned. Firms or other nonmarket allocation systems act in this framework as substitutes for price-making markets (leading to the 'nonprice allocation' referred to), which therefore serve as a benchmark. Even insofar as North concedes Polanyi's empirical claim regarding price-making markets in premodern history, i.e. even in their absence, a wealth-maximising motive is still assumed in the 'choice' between allocation systems. So although North does not presume that wealth maximisation necessarily determines choices *within* institutional orders (see the section on rationality and choice below), it is an underlying assumption of his approach that this does hold in the choice *between* such orders, i.e. in the 'choice' of (powerful) elites, organisations or individuals to maintain or alter institutional arrangements.

In all this, institutional orders, especially of a 'non-Market' (in Carrier's sense) nature, can in this framework *only* be explained insofar as they are *substitutes* for the actually efficient free market, that consummation devoutly to be wished. As Francesco Boldizzoni observes:

"The term 'substitutes' is not neutral and indeed here does not mean 'alternatives'. Substitutes expresses the idea that the natural allocation system is the market, and the others are surrogates for it, intervening when conditions are imperfect and unfavourable. In other words, according to North, it is not the emergence of market systems that requires explanation, but why other institutions 'allocate resources in place of markets.'" (Boldizzoni 2011: 22)

The contrast with Polanyi is obvious.

The point of North's approach is to show that the economics approach can explain such allocation systems, their institutional structure and the direction of change. But, as Daniel Ankarloo suggests, given the above problem, North can only do this by assuming the very market relations he has just denied:

"This is due to the fact that institutions evolve as rational responses to relative price changes, by, albeit 'constrained', micro-rational economic men, in his model. But such calculation cannot explain the origins of the market. Calculating what to buy only makes sense when there

already are commodities on the market to buy (...). North fails to acknowledge the fact that the 'free' individual – the micro-calculating consumer – is the result of capitalist markets, rather than the other way around. In North's theory this individual has no history, and that is a critical limitation on his program of 'history matters'. This problem of neoclassical theory is not solved at all. It is inherited." (Ankarloo 2002: 19)

### *Rational Choice and Bounded Rationality*

To comprehend fully how this is a problem for the NIE, we must turn to the problem of rationality in neo-institutionalist analysis. Here the NIE is a more divided field, because approaches to rationality modelling vary widely within New Institutionalism. For this reason, Thrainn Eggertsson has distinguished those New Institutional approaches based on traditional rational choice models (such as Williamson's) from the ones that prefer concepts of bounded rationality and satisficing (such as North's), calling the former 'neoinstitutionalist' and the latter NIE proper (Eggertsson 1990: 8–9). Most likely, this only proliferates terminological confusion. I will here concentrate on the latter case, because it is more interesting and more in line with what anthropologists are familiar with: the contextual and imperfect nature of cognition and the effects of culture and belief systems acting as constraints on the pursuit of rational self-interest. It seems likely that these 'concessions' on North's part to the critics of rational choice economics have helped enhance the influence of his approach in the social sciences.

Brian Donahoe's discussion of what he calls 'situated bounded rationality' and its importance for a possible convergence between New Institutional theory and economic anthropology is a good example in this regard (Donahoe 2009). In examining the operation of this concept within an anthropological but NIE-oriented framework, it is his intent to "point out the common ground among certain powerful theoretical approaches that are often seen as irreconcilable and mutually exclusive", where no less than "the key to that reconciliation lies in a critical refinement of a central concept of the new institutionalism, that of bounded rationality" (ibid.: 2). North's last major works stood out in particular for their spirited defence of bounded rationality approaches against Williamsonian rational choice (e.g. North 1993), and Donahoe suggests that this constitutes a potential point of synthesis between the concerns of economic anthropology and NIE theory. In light of Earle's suggestion to find such a synthesis in which the neoinstitutionalist turn is incorporated, without 'colonising' as Gudeman put it, this is a salient remark. It is therefore essential to obtain clarity about what this methodological principle, bounded rationality, really does in North's work.

Although the framework of bounded rationality was developed by Herbert Simon and others many decades ago (Simon 1959), it has only recently with the institutionalist turn and with the growing influence of evolutionary models and behavioural economics become a more mainstream application to economic thought (e.g. Gigerenzer and Selten 2002; Denzau and North 1994; Pagano 2000; Ostrom 1990; Crawford and Ostrom 1995). The central premise is to view individual choice as a case of constrained satisficing, the achievement of a 'good enough' level of utility under conditions of uncertainty, rather than utility maximisation (optimisation) under conditions of perfect information in which risk is probabilistically assessed. Since there can be a great variety of different constraints operating on choice via informational limitations, and since belief systems, ideologies, and mental models of the world (correct and mistaken) affect choice when uncertainty exists, this allows a much greater scope for the incorporation of such 'cultural' elements in behavioural models than traditional rational choice approaches do. As Donahoe notes, this changes

the concept of rationality employed from a substantive one – adherence to the formal criteria of rationality such as transitivity and completeness of preferences, etc. – to what he calls a processual one where the context is particularly significant (Donahoe 2009: 5–6). This dovetails with the use of cognitive theory and psychology in economic models – something explicitly excluded by conventional rational choice theory – to the effect of seeing human choice behaviour as primarily guided by heuristics rather than calculation (Tversky and Kahneman 1974; Gilovich, Griffin and Kahneman 2002).<sup>15</sup>

It is not a coincidence, I think, that a great part of North's last theoretical monograph is dedicated to the importance of cognitive science for situating institutionalised behaviour. Although Donahoe's main frame of reference for NIE theory is the work of Elinor Ostrom, I will therefore rather use Douglass North as example of what I mean, since the latter has repeatedly written about the importance of cognition and bounded rationality for his project to answer Polanyi's challenge (North 1993, 2005; Mantzavinos, North and Shariq 2004). The chain of argumentation in the most developed stage of the NIEH runs from cognitive limitations, inherited as evolutionary baggage, to the formation of belief systems and ideologies and the need for social order, and these jointly give rise to respectively informal and formal institutions (laws and norms), which finally define the 'rules of the game' of self-interested pursuit of advantage in markets or substituting economic arrangements. Insofar as NIE theorists accept the bounded rationality approach, then, they open up a greater room for convergence with anthropology than the more rational choice efficiency-oriented approach associated with Williamson and public choice theory. For Donahoe, this kind of bounded rationality approach is

“(...) based on the recognition that human behavior emerges out of and can only be understood in the context of an individual with evolved predispositions that are culturally mediated, in interaction with his/her social, cultural, and physical environment. This is very much in line with processual and practice-based approaches in anthropology.” (Donahoe 2009: 13)

However, I am less optimistic about the possibilities of such convergence than Donahoe. For reasons of space and scope, I cannot go into the evolutionary argument that is also important to his discussion, the use of bounded rationality in the more non-neoclassical forms of New Institutionalism Donahoe refers to is problematic. The problems with rationality tie directly into the problem of indeterminacy in NIE theory. They revolve around the same problem: the more flexible a theory becomes, the less explanatory work it can perform. This was traditionally the argument for rational choice. In rejecting the conventional utility maximisation approach, the alternatives – such as bounded rationality – are often burdened with impossible expectations.

This criticism does not extend to Donahoe himself, who rightly observes the difference between evaluation of rationality by an objective but exogenous criterion, in this case evolutionary fitness as measured by responses to ecological challenge, and the more common approach that is derived from economics and has dominated the neoinstitutionalist turn in economic thought. As he observes:

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<sup>15</sup> It should be understood here that rational choice theory does not require that humans are actually optimising calculating agents, only that they can effectively be modelled *as if* they are. This reduces the psychological content of the theory to utility maximisation and excludes consideration of mental states (Satz and Ferejohn 1994). That latter claim is the one under contention in the bounded rationality literature. See Gul and Pesendorfer (2008) for a critique of the psychological approach and a defence of rational choice economics excluding psychological concerns.

“(…) the most significant difference between this heuristics-based vision of bounded rationality and the ‘heuristics and bias’ and ‘optimization under constraints’ approaches critiqued above is that the simple heuristics model is based on ‘ecological rationality,’ in which the criterion for rationality is adaptive success via fit with the environment, whereas in the other applications of bounded rationality, the criterion defining rationality is still some assumed ‘true’ or ‘pure’ or ‘real’ disembodied and decontextualized pure form of economic rationality.” (Donahoe 2009: 9)

But it is this latter form that remains, seemingly as a utility maximising substitute for rational choice, the dominant approach for those NIE theorists like North who reject conventional rational choice (e.g. North 1993; Mantzavinos, North and Shariq 2004). I therefore focus my critique on that version, where I suspect convergence is less likely to take place along the lines of synthesis suggested by Timothy Earle and where the risk of ‘economics imperialism’ is considerably greater.

As Alexander Rosenberg points out, the usual justification in neoclassical economics for ignoring procedural rationality is that the substantive form of rational choice has sufficient explanatory power that further knowledge is irrelevant. Indeed, in some interpretations the *point* of rational choice is to remove all consideration of what happens inside the mind: rational choice provides a set of axioms which are necessary for this kind of behaviourist analysis of human behaviour. (Rosenberg 1992: 116–120; Gul and Pesendorfer 2008). In the case of the former justification, the obvious problem is that the rationality criteria have often been shown to be violated in practice. Whether the explanatory value of rational choice in economics is sufficient to overcome such problems is, to say the least, controversial. It is against this argument that North appears to aim his criticisms. Yet, on the latter justification, utility maximisation is irrefutable because *true by definition*; any behaviour can always be redescribed as maximising some property. The only relevant criterion, then, is whether this assumption leads to testable predictions and so to improvements in knowledge, which is again controversial (Hogarth and Reder 1986, 1987; Hausman 2012).

Now recall how, on my reading, the theoretical core of the institutionalist turn is the combination of traditional microeconomics and choice theory, with its implications for free and well-ordered markets taken as a normative benchmark (what Carrier and Miller 1998 call ‘virtualism’), with the emphasis on social-institutional context that was hitherto left to other social sciences such as anthropology. From this perspective, North’s emphasis on investigating the sources of procedural rationality (and its possible failure) only makes sense if he had already rejected the assumption that humans can be usefully modelled as if they conform to substantive rationality *and* the claim that they actually conform to it, at least sufficiently for theoretical purposes. North often seems to indicate that this is in fact his view. But if the processes of learning and cognition are to give content to human intentionality, then the more content it has, the less any choice theoretical framework recognisable from conventional microeconomics will work, and therefore the less its implications or justifications are available to New Institutional theory. This is why most economists reject any venture into cognitive science, neuroscience, or developmental biology.

The use of cognitive science can, at most, explain how imperfect information came about; it does not (yet) provide us with sufficient knowledge to know, in given environmental conditions, what choices individuals will make. For this we are left once again with some theory of rationality. This, in turn, leads us back to the strong assumptions and their interpretation, according to which utility maximisation is either wrong or by definition true, and in both cases of questionable use. Hence,

North's recourse to 'bounded rationality', a solution used for these purposes, simply isn't one. This explains North's hesitation when introducing the chapters on cognitive science: "The rationality assumption is *not wrong*, but such an acceptance forecloses a deeper understanding of the decision-making process in confronting the uncertainties of the complex world we have created" (North 2005: 5). We are not told what kind of 'deeper understanding' this is, and whether it should affect the rationality assumption or not, the same one he has called "devastating for most of the major issues confronting social scientists and is a major stumbling block in the path of future progress" (ibid.). He wants us to recognise the importance of uncertainty and its implication that we must study beliefs and institutions. While cognitive science is tasked with giving us beliefs, nothing connects beliefs and preferences other than a final resort to bounded rationality. Bounded rationality in turn consists of an application of rational choice under strong constraints, which is why North calls institutions and beliefs constraints. Yet, rational choice must take, holding tastes constant and for a given cognitive capacity, beliefs and preferences as a given.

That these justifications are not compatible with each other does not appear to occur or matter to North. In each case, he accepts one or the other of these claims because they provide justifications that are convenient relative to other theories. The anti-rational choice perspective is justifiable for North when used against neoclassical and neoinstitutionalist 'efficiency' models, and the rational choice perspective is justifiable when it confirms the validity of the conclusions of conventional microeconomics. These conclusions are in particular the explanatory power of assuming utility maximisation of some sort and its contribution to testability and prediction; as well as the normative desirability of 'free and efficient' markets as modes of social cooperation, and that such markets are a necessary but – given the problem of getting the institutions right – not sufficient condition for achieving lasting economic growth or other desirable welfare effects.

This problem appears more generally in the institutionalist literature, although most evident in North simply because he has written most explicitly within the NIE framework about the theoretical questions involved. If anything, North's work gives more room for cognitive constraints and the centrality of belief structures than is common in New Institutional writing. But as Ben Fine and Dimitris Milonakis write in a critique of North's approach to rationality:

"(...) with frequent reference to the work of Herbert Simon, and others working on (ir)rationality from the perspective of the individual's cognition and system of beliefs, North is most readily interpreted as always reconstructing social theories of ideology through the prism of methodological individualism, of agents making sense of their external environment by interacting with, and internally contemplating it (...). As it were, ideology, etcetera, is complicated; we do not have a complete theory; so the focus will be on one effect alone (...) [But] there is one essential mechanism that straddles all of the analytical levels – *individual pursuit of self-interest with an as-if market mechanism prevailing throughout society*. This is already explicit in the gains from behaviours such as cheating, but for institutional impediments. But it penetrates everywhere, even to the determinants of ideology, with every principle having its price (...) *ideology* becomes a truly marvellous and powerful explanatory factor. For it encompasses whatever is not explained by rationality (which has itself been extended by appeal to market imperfections)." (Fine and Milonakis 2003: 558–563)

On the one hand, North insists on bounded rationality and 'institutions matter' because both are ways of incorporating the social context of economic behaviour without reducing such phenomena to parameters of rational self-interest alone. Yet, on the other hand, like many New Institutionalists,

he still relies on the choice theoretical foundations of mainstream economics, especially microeconomics, to understand *how* institutions and choices interact in an ‘as-if market’, so that agents turn out to be constrained pursuers of self-interest after all. In non-rational choice New Institutionalism, as the case of North illustrates, a paradox emerges: where bounded rationality differs from constrained optimisation, it cannot do any explanatory work, and where it has to do explanatory work, it devolves into constrained optimisation. Hence, North’s attempts at escaping this dilemma by introducing undefined exogenous factors: ‘ideology’, or evolutionary imperatives, or simply a rather hand-waving “complex mix of beliefs and institutions” (North 2005: 44). Ultimately, he is therefore forced to reintroduce conventional microeconomics and choice theory through the back door. That these issues are difficult to disentangle is undeniable, but it is not clear how the neoinstitutionalist turn offers any more determinate solutions to the problems posed by rational choice theory than existing anthropological traditions. This then brings me to the discussion of indeterminacy in the neoinstitutionalist turn in general.

### *Indeterminacy*

To my mind, the greatest problem for the institutionalist turn, one which can be said to cover the problems discussed above (and indeed more, such as the evolutionary dimension I do not discuss here), is its indeterminacy. In short: if everything depends in an indeterminate way on institutions, then the institution concept does no explanatory work. That this may be a problem is already indicated by the vagueness of the popular phrase “institutions matter”, because it does not say how they matter or for what purpose. In the rational choice version of this approach, the hypothesis about the causal chain is at least fairly straightforward: those institutions will be chosen, or will evolve, that minimise transaction costs within a particular temporal bound. However, transaction costs have not so far been found to be directly measurable, only subject to very broad estimations (e.g. Wallis and North 1986), and transaction costs apply not just in the process of exchange, but also prior to it, which further complicates matters. Moreover, this approach falls foul of the same critiques that all rational choice approaches to economics do, such as their lack of realism, and it does not capture much of the informal social or cultural content of institutions that makes them so particularly salient as a cause of institutional variation (this was Polanyi’s point).

However, the ‘irrational choice’ approach of North and colleagues as well as of psychologically oriented economists like Daniel Kahneman suffers from the opposite problem. Since there is a virtually limitless number of ways that institutions, ideology, beliefs, and habits can act as constraints on the operation of choice, and since the particulars of the cognitive limitations of individuals are not well-known beyond their general use of heuristics and biases – that is, we cannot deduce from that literature which specific heuristics and biases will be in operation at a given time – there is no predetermined way at all to move from institutions to a clear hypothesised causal chain in this explanatory framework.

This is not just a problem of bounded rationality in institutionalism. It applies more generally to the approach itself. As mentioned, the slogan ‘institutions matter’ does not tell us *how* they matter, and this is no small omission. As Gudeman has pointed out, to rely on transaction costs to explain nonmarket situations is a circular reasoning, and it is dubious whether transaction costs can in any case be sufficiently directly measured. The notion that informal and formal rules constrain individuals offers no behavioural prediction in the absence of strong assumptions about the choice behaviour of those individuals. But where such strong assumptions are permitted, as in the Coase-

Williamson tradition, the behavioural predictions of NIE theory are as wrong in light of behavioural and experimental economics as their neoclassical predecessors' predictions and assumptions were. Neither greater realism of assumptions nor a synthesis with other social sciences is reached. Finally, in taking the isolated individual's choice behaviour as the point of departure, that defining methodological principle of microeconomics even North was unwilling to give up, all economists – institutional or otherwise – are confronted with this dilemma: *either* to choose mathematically tractable and predictive simplifications that are not borne out, *or* to attempt to integrate such methodological individualism with institutional and interpersonal context, in which case both tractability and determinacy become impossible (Varoufakis 2014; Fine and Milonakis 2008).

We must therefore conclude that North's original hope that the NIEH should be "amenable to testing" and that "we can and should be able to predict the direction of institutional change" has not been fulfilled, and moreover cannot be fulfilled on the basis of his theoretical analysis (North 1977: 707, 715). The more work has to be done by institutional variables, the less anything in particular is predicted by the theory, and therefore the less directly refutable or testable it becomes. Since I am not a Popperian, this problem does not worry me a great deal. But it does point out the more philosophical problem that the literature in the institutionalist turn, at least as most applications to other social sciences hitherto are concerned, faces a stark dilemma: either to go for the Williamsonian route of rational choice institutionalism, which has clear directions of prediction but is unlikely to give realistic explanations, or to go in the direction of North and others, and to be left with no definite explanatory theory at all, since virtually anything is variable in this approach.

For economic anthropology, this implies that Earle and Gudeman are right to question the ability of New Institutional Economics to live up to the expectations of its enthusiastic importers in the social science. There is nothing inherently wrong with anthropologists considering transaction costs, or using a framework in which institutions are defined as rules and act as constraints, or to consider how such frameworks contribute to overcome collective action problems. But such can only be done in the context of a larger theoretical framework within which these concepts become tools, and the Achesonian road of using NIE theory as such a framework in its own right is likely to disappoint the high expectations the proponents have of it. Equally, the combination of institutional analysis with bounded rationality that defines the more 'heterodox' forms of NIE theory, such as North's later works, may not be better at steering between the Scylla of indeterminacy and the Charybdis of irrelevance than the more straight-laced Williamsonian approach. Donahoe's discussion of the relevance of such approaches to anthropology is a good example of how only careful methodological considerations can allow one to escape this trap.

### **Conclusion: the persistence of Polanyi**

If I am right that the tools and concepts made fashionable by the neoinstitutionalist turn will only prove useful to economic anthropology if employed in synthesis with theory from the anthropological tradition itself, the question arises what theory that would be. Here, I would return to Polanyi. Like many economic historians, I have some reservations about specific claims about premodern economic history. His acceptance without question of the dominant economics of his day to explain capitalist society (though not to justify it) seems, in retrospect, as big a mistake as his tendency to read modern principles of socialist economic organisation – planning, social

regulation – into antiquity. As mentioned in the introduction, in the neo-Polanyian revival there has been a tendency to address these problems in Polanyi’s work by the thesis of the ‘always embedded’ society: the argument, based on Polanyi’s concepts but not his actual viewpoint, that *every* economy is institutionally embedded in social and cultural norms and relations that determine its particularities, and that therefore the disembedded market is simply an illusory notion (Block 2003). Gudeman’s (2012) universal duality of the economy, between mutuality and market, has a similar structure.

This approach is not a helpful alternative to the neoinstitutionalist turn because it raises the same problem of indeterminacy as that faced by the New Institutionalists. If everything is embedded, embeddedness does no more explanatory work than institutions do in applications of NIE theory. What we can take from Polanyi are not so much his own answers but his questions, the challenge taken up by North, which should interest economic historians and anthropologists alike. This challenge is manifold. Firstly, his contributions to the twin debates, his substantivism and his primitivism, remain relevant as long as the institutionalist turn is beset by conceptual problems. Polanyi challenges us to understand economic systems first and foremost from the viewpoint of the organisation of production and distribution (substantivism), and to see them as historically strongly differentiated phenomena, rather than assuming a series of minor variations on imperfect markets (primitivism).

Secondly, Polanyi also challenges us – to some extent *malgré lui* – to understand (micro)economics properly, but in understanding it, to see the limits and context of its application. To understand choice theory is also to comprehend that it is not so much wrong as meaningless to say that, as one economic historian was quoted earlier, “economics applies wherever you cannot have your cake and also eat it” (Jongman 2014). Polanyi challenges us to ask *which* economics applies, and to question the assumption that reference to conventional economic theory automatically raises an argument’s explanatory value.

Finally, Polanyi challenges us to renew the research programme that he undertook at Columbia University: the systematic comparative study, in the longer run, of the origins of capitalist society out of the differentiated institutional structures of premodern economies. As Sally Humphreys noted, Polanyi sought to do so by “proceeding from a substantive definition of the economy to an empirical study of the place of the economy in society, without any theoretical presuppositions about the function of the economy.” (Humphreys 1969: 199) This need not involve accepting Polanyi’s view that individuals in premodern societies were less concerned with material want satisfaction, or that modern capitalist society is primarily characterised by the structure of market exchange. But we can still take from Polanyi as our most important challenge the development of a “new science of comparative economics.” (ibid.: 207)

This would be one that includes the tools of NIE and traditional choice theory but recognises their limits. One important direction of research would be to take Polanyi’s intuition to see market exchange as itself as an ‘institution’. This would involve rejecting the common perspective that sees markets in history as more or less impoverished instances of The Market. It would regard them as the product of specific and varying social-institutional conditions, showing cycles of rise and decline in the *longue durée*, instead of regarding institutions as at best complements to the Market in the style of North.<sup>16</sup>

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<sup>16</sup> One promising work in this direction is Van Bavel, forthcoming.



The greatest significance of this challenge is that it offers a great opportunity for the reconciliation of economic history and economic anthropology, which has been long rendered impossible by the dominance of neoclassical methods in the former field and a lack of theoretical agreement in the latter. The purpose of Polanyi's interventions in the twin debates I have discussed in the beginning of this paper was to affect such a synthesis, or at least to pave the way for one. This is what I see as the implication of the Earle-Gudeman approach to the neoinstitutionalist turn for economic anthropology.

If the ship of New Institutionalism is likely to run aground on the shoals of indeterminacy, it would be good if the small rescue vessel, economic anthropology, can take the stranded economists and economic historians on board and steer them towards a common destination that is still worth reaching. And if that vessel should be haunted by the ghost of Karl Polanyi, as Douglass North once suggested, this may not be such an unwelcome presence. There will be other ghosts, of course (Marx and Weber come to mind), but this particular one may persist longer than those who would exorcise him.

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