Introduction and Overview
James I. Sturgeon

Introduction

This is a summary of the approach to institutional economics at the University of Missouri-Kansas City [UMKC]. It includes a brief historical background of the economics department, the scope (syllabi) of the material covered, and sketches of models used to explain the theory and methods in the approach. Taken together the papers in this session and the following one result from the institutional economics workshop at UMKC and seek to cover significant areas included in our approach.

Historical Background

It is likely that the Department of Economics at UMKC has the longest uninterrupted program in which institutional economics is taught and required. Since 1946 (64 years ago) undergraduate students have taken Institutional Economic Theory as part of the major. When the masters program began circa 1950, Advanced Institutional Economics was required. In 1992 the Ph.D. program began and both Advanced Institutional Economics and the Colloquium in
Political Economy were required. Further, comprehensive exams for the MA included both institutional theory and the Ph.D. requires Political Economy, Institutional Theory, post-Keynesian theory, as well as the interrelationships of these.

The department began in the mid 1930’s. Abba Lerner started his US career at the then University of Kansas City as did Eugene Altschull. In 1946 that John Hodges was hired as department chair and immediately began building a program that placed institutional economics at its center. Hodges was an enduring force in the department, remaining chair until 1972, when he was forced to retire per then existing university rules. He continued teaching until age 79.\textsuperscript{1} Like many of his generation of institutionalists Hodges published little, but influenced many.\textsuperscript{2} Under his guidance hundreds of students became interested in economics and especially institutional economics. He helped create the Foundations courses in Physical and Social Sciences, taught the Foundations of Social Science course and hired both Mike Wagner, another Ayres student, and Gene Wagner, Mike’s cousin.\textsuperscript{3} Joe Brown, also a student of Ayres, came to UMKC in 1966 and remained until he died in 1978. W. Robert Brazelton, a post-Keynesian with a significant interest in the institutional, approach was hired in 1963 and taught until 2000. John Ward, an MA student of Brown at Toledo and Alex Kondonassis at Oklahoma was hired in 1969.\textsuperscript{4} I arrived in 1977. Peter Eaton, my friend, colleague and co-conspirator for the last 30 years arrived a year later. Our program has been blessed to have Eaton in charge of econometrics, statistics and empirically grounded research.\textsuperscript{5} In the early 1990’s Ben Young and Mike Kelsay joined the faculty as lecturers, both got MA’s for UMKC before completing Ph.D.’s at Oklahoma and Tennessee, respectively. Doug Bowles a UMKC MA and Ph.D. began with the Center for Economic Information in the late 1990’s and now is the Director of the Social Science Consortium [SSC]\textsuperscript{6} and Research Associate in the CEI. He also teaches courses
in economics and the SSC. James Webb joined the department as a fellow in the late 1990’s and now teaches a Ph.D. course in the SSC as well as being the director the Pragmatism Seminar.

In the mid-1990’s we began expanding the Ph.D. program. At that time, anticipating the retirement of four faculty, we developed a plan to enhance the development of the Ph.D. program grounded in institutional and post-Keynesian approaches. That plan was executed in 1999 when Randall Wray and Mathew Forstater were hired and following soon thereafter, Frederick Lee, Stephanie Kelton, Erik Olsen, and Linwood Tauheed all of whom are institutionalists or post-Keynesians. John Henry joined the department in 2002 after retiring from the California State University-Sacramento. Wray and Kelton were his students there before going on to Washington University-St. Louis (Wray) and Cambridge University (MA) and New School for Social Research (Kelton). William Black joined the department with a joint appointment in the Law School in 2006. He had previously taught at the LBJ School and University of Santa Clara after being Deputy Director of the Federal Savings and Loan Insurance Corporation where he exposed the Savings and Loan crisis.

An unusual strand in the history at UMKC is that the Institutionalist tradition was also present in the School of Administration (now know as the Bloch School of Business and Public Administration). Neel Proctor, Reverdy Gliddon, and others were mainstays in that school for many years. Bill Frederick was also there and was dean of the school before moving to the University of Pittsburgh. There is still an Institutionalist influence via Phil Crossland, a student of Greg Hayden’s, though it is not as strong as it once was.

From the early 1950’s until now there have been at least two intellectual descendants of Veblen teaching at UMKC. This is one key to the continuity of the program. Of course many departments have had an Institutionalist influence in the last 100 years. Regrettably, too many
have come under the pressure of homogeneity and the tradition has been reduced or eliminated at many departments

A Survey of UMKC Approach

Next is a condensed survey of the constituent elements of what is taught. The course materials include grounding in Veblen, Commons, Ayres, Dewey, Pierce, and others, as can be seen by looking at the course syllabi in Appendix 2. We assign Geoffrey Hodgson’s book, *The Evolution of Institutional Economics*, as both a source of information and for critique. Of course we draw on the work of many others too numerous to enumerate here. It is probably the case that Veblen and Dewey have a greater influence in our approach than Commons or Mitchell. Yet, Commons work is an integral part of our approach, especially strategic and limiting factors, futurity, reasonable value, the importance of policy and direct involvement in community issues. Thus, we disagree with Yngve Ramstad’s view on two points, 1) that Commons’ methodological approach and conceptual apparatus are incompatible with the work of Veblen and Dewey, especially as relates to the dichotomy of culture, and 2) that Commons has been rendered inconsequential by institutionalists or “Veblenian” institutionalists.

We teach pragmatism as the philosophical foundation of institutional theory. The most significant point involved here is that behavior (the interrelationship of knowing, doing and valuing) is habit based and involves complex transactions and cultural relations. We teach a theory of behavior grounded in Dewey’s *Human Nature and Conduct*, Veblen’s theory of instincts, the work of Joe Brown in extending the use of social psychology especially as found in the work of Muzifer Sheriff and Robert Hood, and the modern concept of psychological control theory found in the work of William Powers. The latter is employed specifically in the theory of consumption and institutional adjustment.
We also stress that institutional economics is not inductive, as some believe. Rather, drawing on Pierce and Dewey, we teach that the process of establishing “knowledge” involves, in quite specific ways, the interaction of abduction, induction and deduction as explicated by Pierce\textsuperscript{11} and Dewey.\textsuperscript{12} This is briefly summarized in the Knowing—Doing—Valuing model in Figure 2 below. It is presented in more detail in James Webb’s paper and his other work.\textsuperscript{13}

Since change is at the center of institutional analysis, how that change occurs is central. The principles of institutional adjustment are an important part of our approach. These principles, made explicit by Foster,\textsuperscript{14} are extended to run throughout what we teach and are surveyed below.

We teach a theory of class and a theory of consumption found in *The Theory of the Leisure Class*. The former is extended and enhanced with some new concepts such as the “Skills Matrix.” Doug Bowles will present this in a paper in the next session. The latter is extended through the work of Galbraith and Bill Williams and is treated below.\textsuperscript{15} We do not teach Veblen as sardonic, a man from Mars, or envious of the cosmopolitan elite. For example, conspicuous consumption, pecuniary emulation, pecuniary canons of taste and conspicuous waste are not treated as a satire or figments of Veblen’s imagination, but as concepts born of actual human behavior. We teach a theory of production that begins in the work of Veblen and Commons and runs through the work of John Munkirs, and includes the theory of resources of Zimmerman and Peach. Shortened versions of our approach to consumption and production theory are given later in this paper. Next is a sample of some of the main theoretical elements of our approach.

**Theoretical Framework – The Veblenian Dichotomy**
A principle of institutional economics is that human activity is organized by institutions. Extending and modifying Veblen’s distinctions the Veblenian Dichotomy has been developed into an analytical framework.\textsuperscript{16} We use the Veblenian dichotomy as the theoretical center piece of our approach. Analytically, institutions are separated into two primary aspects: instrumental and ceremonial. Both are treated as aspects of human behavior and used to analyze the functioning of the economy. Figure 1 illustrates the major components of the Veblenian dichotomy as we teach it. From what follows in this and the other papers it will be clearer the extent to which the dichotomy influences and inspires our work.

Notice that the dichotomy is lodged in the concept of culture. For the social sciences this is a revolutionary concept because it resolves many mysteries of humanness, thus extending the secular revolution begun in early times. The concept does three things, 1) it squares with Darwinism, i.e., group elaboration and transmission of cultural traits to other members of the group and new generations and a process for adaptation to new conditions, 2) it explains the diversity of human societies that is greater than the individual differences and 3) it explains the amazing stability and persistence of this diversity.

**Figure 1**

**The Veblenian Dichotomy of Culture and Institutions**
We include in both instrumental and ceremonial behavior is the arts of associated living: the rules, customs, laws, ideologies, accumulated folklore, myths, licenses, policies, and traditions which form the constraints and freedoms of human interaction. These arts are cumulative and developmental, learned, and evolving. If not adjusted to correlate with institutional changes they grow stale and outdated and restrain the ability to compromise, resolve conflict, and ease social tensions. 17

The Enduring Tension

Tension and conflict permeate the fabric of human affairs. They are ubiquitous and enduring. “The Enduring Tension” is a concept we have developed and taught as a principle of Institutional Economics. It is embodied in the tension between the instrumental and ceremonial aspects of economic life. It waxes and wanes under the force borne of technological change and scientific advance. Tension exists on multiple levels and perhaps no problem is more perplexing than the tension between the private and the public domains, between what is good for the
individual and what is good for society. In economics this came into stark relief when the “organic” society of the middle ages began to give way to the more "interdependent” society that followed. With the evolution to a money economy and later a credit economy other powerful avenue is introduced to heighten the tension. The principle of enduring tension enters into the remainder of our approach and specifically it is illustrated below in the theory of production.

**Principles of Institutional Adjustment**

The creative forces of science and technology are an important source of tension and change in economic activity. Change and its analysis are important aspects of Institutional economics, possibly the most important. Change requires adjustment (closer correlation) of ceremonial behaviors to instrumental ones. We teach Foster’s three principles of institutional adjustment, slightly altered, as basis for understanding the process of change in institutions; how institutions adapt to bring their elements into closer correlation. The principles that govern institutional adjustment are applicable to the process of individual behavioral change. Below is an enumeration and explanation of how we use these principles.

1) **Instrumental primacy** is the principle that indicates that change is predicated on the actual ability to do something. This involves technological progress -- additions to the warranted stock of knowledge. Instrumental primacy, as the impetus to adjustment, may be read to mean that one requirement for change is a reasonably accurate perception of what can be done in relationship to what is now being done. This is a critical part of instrumental correlation.

2) **Recognized interdependence** is a principle that specifies that the pattern of adjustment is bounded by the pattern of interconnectedness and interdependency of the institutions/members affected by the change. It is almost axiomatic that
recognized interdependence is more likely to be achieved in institutions that are structured around participation – cooperative interaction, since the participants will be better able to understand their interaction and the consequences of changing them. We assert that the pattern of dependency is, in part, indicated by the Social Fabric Matrix [SFM].

3) Minimal Dislocation deals with the circumstance that adjustments must actually be capable of integration into the remainder of the existing social fabric. The principle discloses the limits, in term of rate and degree, of any adjustment. This does not mean that adjustments are necessarily small, only that there is limitation based on the integration of associated institutions. The social fabric of any institution is finitely elastic at any point of change implementation. The adjustment is more likely to be achieved if the adjustments follow a path with relatively small increments of continuous change. If adjustments are deferred and build to a situation where change involves significant dislocation there will be more resistance as vested interests accumulate around the prevailing institutional structure. This situation is more likely to create the condition of ceremonial encapsulation making adjustments less likely and less susceptible to deliberative processes.

Notice the principles are instrumental in character. This is because adjustment is a change in the relationship or synchronization of ceremonial behaviors to instrumental ones. In other words, while adjustment is an interaction of ceremonial and instrumental behavior, the causative agent is instrumental while ceremonial behavior is the passive and resistive force. There is an enduring tension in these and the successful adjustment of institutions works to reduce this
tension. A lack of adjustment increases this tension. To recognize and to experiment with
different ways of bringing about change requires consideration of the means-ends-consequences
continuum. These can be simulated with the SFM so that actual consequences may be better
anticipated, accepted or avoided. How close that perception is to the instrumental reality is a
critical feature in the adjustment process. This relates to the other processes.

**Means-End-Continuum**

In addition to the three principles above there are two processes involved in institutional
adjustment. The first is the relationship of Means-Ends-Consequences. This process relates to
the problem of selecting actions that will bring about the desired change; including the axiom
that choosing means *is* choosing ends. It is a hypothesis about what to do, but without the
knowledge to do it. The means-ends continuum is deceptively simple, but may sometimes have
complex implications. Means are inseparable from ends because arrival at an end has
consequences for where we can go once we have “arrived.” It is a truism that means are ends and
their continuum is based on seeking to understand the consequences stemming from choosing
alternative means. Institutional theory sees these selections as derived from both instrumental
and ceremonial ways of knowing, valuing, and doing. Both posit a fact based cause and effect
relationship, the former is demonstrable while the latter is not. Selection of means involves
choices. Selection processes are based not only on the ”immediate” consequences of a choice,
but future ones too.

**Deliberation**

Deliberation is a process that precedes choice and action. It is intellectual and examines
the consequences of actions prior to acting; a dress rehearsal as it were. It is an intellectual
experiment in which the consequences of alternative means are extended into the calculable
future. The goal is to sort out alternative paths— their possible consequences, and to evaluate the means with an eye toward directing choices in a way that is consistent with the goal and the instrumentalities of a situation. In the process of institutional adjustment deliberation improves the likelihood of reasonable choices. The analytical process is concerned with discovering whether the possible choices or action plans may prove reliable— warranted. Deliberation involves: a) a felt difficulty, conflict or discrepancy; something is clearly wrong; b) clarification of the specific problem to be solved, c) development of hypotheses concerning the nature of the problem and possible solutions; this means that traditional theories are not to be accepted *a priori* as correct; they may well be a mixture of folk beliefs and facts; d) examination of the logical consequences of proposed hypotheses, a rehearsal in imagination of the possible hypotheses and lines of action. No action has been taken beyond recall. And finally, e) choosing – hitting in imagination upon a line of action that yields overt action.25

Deliberation and choice conjoin with a relevant problem; a reaction or adjustment to a situation that arises to help solve a recognized difficulty. Ideas serve as plans of action because they suggest themselves as problem solvers. The "success" or "satisfactoriness" of a plan of action is to be understood in terms of predicted and actual consequences. In science a general pattern of inquiry has been developed which is competent to integrate and test our ideas about the nature of the world. The hypothesis here is that the rationale of scientific methods is applicable to human behavior (knowing, doing and valuing) and that in a particular situation, by the use of intelligent methods of analysis, one course of conduct can be established as "better" than another. These elements of inquiry for the process include: a) sensitivity to the uniqueness of different situations, b) patience and persistence to carefully formulate the problem, c) creative
imagination to envision new possibilities, d) a bias for objectivity and an ability to discount one's own prejudices, e) the courage to revise one's beliefs in the light of new experience.

In a reasonable or deliberative choice multiple hypotheses may be considered in dealing with a problematic situation. No choice is given precedence over others; meaning that one is just as diligent in looking for knowledge that may question a plan of action as knowledge that favors it. We carefully consider the probable consequences of acting upon one or another hypothesis and criticize our hypotheses or ends by inquiring into the results of the means designed to realize them. When action is intelligent and reasonable, the means are part of the end. Unreasonable choice leads to a path of action in which some preconception, some desire, over-rides all alternatives and secures the sole right of way, usually without benefit of intelligent habits and deliberative processes.

The Flow of Behavior and Institutional Adjustment

It is convenient to condense our analysis of behavior and adjustment to a simplified flow diagram. We use a diagrammatic “model” of the interactive processes of instrumental knowing, doing, and valuing (K-D-V model) and the relationships of each to institutional adjustment. Figure 3 illustrates the flow and logic which underpins institutional adjustment and points to the behaviors that emerge from a process of individual and collective deliberation and choice. In the pragmatic/instrumental view of the life process there is no separation of knowing, doing and valuing. Behavior involves a process of constant adjustment to problematic situations and control of perceptions. In a shorthand form the figure illustrates the relationships among these. The basic structure of the model employs the PIA as well as the processes of deliberation related to choosing means and evaluating consequences. The process of understanding and explicating the underlying social fabric that defines, determines and reveals the context of the problem (area
of adjustment of an institution) under consideration is included in the model in the form of both the processes of inquiry and of judgment as they interact to shape behavior. The contingent rather than determinate qualities of this dynamic process are embodied in the principles of institutional adjustment. These are considered in light of their relation to the adjustment process as indicated in the K-D-V model. The strike point is choosing a means to adjust and the consequences that result from that choice. Actual behavior results in consequences not all of which can be known in advance. Consequences expose error and affirm the soundness of behavior. We argue that the Principles of Institutional Adjustment in tandem with the Social Fabric Matrix increase the likelihood of an improved understanding of the potential consequences and, perhaps more importantly, more timely future adjustments as the consequences, desirable or undesirable, emerge.

Change depends in part upon a perception of the objective circumstances of possible achievement. Meeting the contours and requirements of instrumental function depends upon the relative strength and depth of the layers of ceremonial imagination and practice. If enough of these can be peeled back an adjustment toward more instrumental correlation is more probable. Recognized interdependence and minimal dislocation depend critically on the participant’s perception. Instrumental reality may be seen as unacceptable because it will cause too much change in existing status relations. Whatever the outcome, a prerequisite to institutional adjustment is the perception of a gap between what is instrumentally possible and what is being done. Synchronization of tools and tool-using behaviors, what Veblen called the machine process, is a process of deliberate or rational behavior, i.e., seeking to synchronize the instrumentally possible with the institutionally actual. The absence of this creates a stretch or tension in the social fabric or institutional collage.27
Individual action

The significant facts of human behavior are not found in instinct or reason, but in habit. Individual habit may be thought of as equivalent to institutions and the process of institutional adjustment and individual adjustment are amenable to the same principles, i.e., habit adjustment is the individual counterpart to institutional adjustment. Adjustment begins with a change in perception leading to a change in behavior; an adjustment of habit. The ease of adjustment depends on habit structure and tenacity. In part a change in habit is a process of discovering and adjusting to error in knowledge and judgment. Institutional adjustment depends in part upon a perception of the objective circumstances of possible achievement. Yet, only individuals can perceive. The psychology of perception asserts that behavior is the control of perception. For example, the ability to control perception and adjust it to meet the contours and requirements of instrumental function depends upon the relative strength and depth of ceremonial practice interacting with instrumental capability; the strength of the tension between them.

We draw from Commons in defining an institution as “collective action in control and liberation of individual action” to help analyze individual action in the context of institutional adjustment. The adjustment process also embodies the idea of progress defined as the enhancement of alternatives in a problematic situation. Control and liberation of individual actions expand alternatives. Actions in the context of institutional adjustment flow from valuations of alternatives in a problematic situation. Adjustments arise as part of the patterns of social arrangements and derive from the transactional activities of individuals with each other and their environs. Perceptions are controlled by habits and habits are formed by the inchoate interaction of the mass of instincts present in human abilities with the total environment and experience of the individual.
Individuals acquire their values from both the instrumental and the ceremonial forces of a social process. Instrumental values are experiential in character since they are formed by experiment, trial and error. Dewey made instrumental values directly related to science. “... without physics, chemistry, and biology a grounded empirical theory of valuation, capable of serving as a method of regulating the production of new valuation was out of the question. With no adequate knowledge of physical conditions and propositions regarding the relationships to one another, the forecast of consequences of alternatives by was impossible.”32 This lodges intellectual habit and instrumental values in experiential processes capable of being verified by the consequences emerging from their application to action.
Figure 2
Simplified Model of Institutional Adjustment in Relationship to Instrumental Knowing, Doing and Valuing
Ceremonial values are dictum in character and are formed by the transmission of traditions, beliefs, and habits that are deemed necessary, revered, and faithfully taught to oncoming generations. Ceremonial norms justify and sanctify power, authority, class inequality, rank, status, superior/subordinate relationships, prosperity codes and the like. Norms and mores teach belief in the correctness of the ceremonies which in turn forms a network reinforcing the validity of each other. The method of knowing and arriving at the validity of ceremonial values involves tradition, appeal to authority, “self-evident” truths.

Instrumental values, based in instrumental logic, exhibit the ability to adjust and adapt as knowledge and experience change. However as they change the put pressure on ceremonial values. Problems create stresses and tension in the value structure. The tension may be thought of as a two way stretch in the value structure—a tension between the two ways of valuing, instrumental and ceremonial that cannot be indefinitely sustained. When the tension reaches a breaking point either the instrumental process of value formulation is stalled or the ceremonial values will crumble.

This is illustrated below in Figure 3. The illustration points to the process of increasing tension between the two ways of valuing. The tension is applicable to the process of individual habit adjustment and formulation. As intellectual habit and instrumental processes expand they put pressure on the ceremonial values which are inherently unchanging because they are dictum in nature. For behavior to change at this point a break or adjustment in ceremonial values is required. This may lead to an expansion of the application of intelligence to the process of habit formation. If the dictum values do not change the process of habit formation continues to be lodged in ceremonial practice and it arrests the ability of individuals to adjust to changing circumstances. This may push the value structure to the breaking point. This is also a possible
pivot point in the lessening of tension and conflict or it may be a flash point that explodes into social conflict.

**Figure 3**
Schematic of Two-Way Stretch in the Value Structure

---

**Production and Consumption**

From this admittedly abbreviated explication of some of the main analytic components we turn to an application to production and consumption. We present a somewhat detailed discussion illustrating the Institutionalist approach to these common topics.

**Theory of Production**

A theory of production is predicated on a theory of resources. We teach the Mitchell, Zimmerman, Peach theory of resources, i.e., the functional/dynamic/evolutionary theory in which knowledge is the key to unlocking the usefulness of neutral stuff. This theory is well
known to institutionalists and we present it only briefly here using Figure 4 below. This figure is
drawn from Zimmerman with only slight modification. The theory is a fundamental part of
institutional economics and is consistent with the approach taken by Veblen, especially in “The
Nature of Capital” and Commons in his analysis of natural and social “scarcity.”

**Figure 4**
A Diagram Illustrating the Functional Theory of Resources

*A brief digression on the theory of cost*

The usual concept of cost is lodged in the disutility of labor and scarce resources. True economic
costs are losses in efficiency as recognized under the force of the instinct of workmanship, not the
pecuniary cost of labor. If the former is used then wages and profits are what it takes to entice labor or
entrepreneurs, respectively, to participate. These are then used as the measure of cost. But it is silly to
think of the activities necessary for life as costs. Cost may better be understood as a function of the
instrumental and ceremonial activities involved in production. Instrumental costs are more in the manner of
investments in the future of the life process while ceremonial costs are in the nature of diversions from the application of work to the growth and maintenance of the life process to those in the nature of invidious distinction and distribution of unearned income.

**A Veblen/Commons Theory of the Firm and Business Fluctuations**

Next are two theoretical formulations for analyzing production and its fluctuations. First is a theory of the firm followed by a theory of modern welfare—business fluctuations.

The theory of the firm we have developed is based on both Veblen and Commons. Like Veblen our theory begins with specific propositions, 1) the modern system is built on a pecuniary basis of purchase and sale with an eye toward profit accounted for in monetary terms, 2) aggregate profits net to zero if prices are driven to cost and the machine process runs on an uninterrupted basis. The first is related to intangible property and goodwill the second to the business cycle. We teach that Commons’ theory of the going concern, consisting of two interconnected and interrelated parts—a going plant and a going business, represent an extension of Veblen’s conceptualization of business enterprise. Further, Commons’ theory of reasonable value lodged in the legal system is a compliment to Veblen’s theory of technological/pecuniary value lodged in differential advantage and exploit.

The modern theory of the firm is found in moving from physical concepts of accrual to pecuniary concepts. Moving away from corporeal property, which is less a pecuniary process, to intangible property, which is none other than the pecuniary process itself. The materials come and go with a rapid turnover by depreciation, obsolescence, and consumption, but that which renews and improves is the traditions, customs, and innovations handed down from one generation to the next in the evolving character of transactions. People come more and more to exhibit the instinct of workmanship in the manipulation of markets and of human need for the purpose of obtaining a profit. Property is largely the monetary capitalization of earning power, and this capitalization is modern capital. Intangible assets are pecuniary privileges of business
arising only from control of supply and power to withhold supply if prices are not satisfactory. Earnings capacity is based upon an expected repetition of business transactions along a flow of time.

Production by the firm is shaped by two very different, but interrelated parts. Veblen articulated the difference between industrial and pecuniary employments and extensions there from. Industrial activities are related to workmanship, they are serviceable and functional; instrumental and associated with the industrial arts and science. Pecuniary activities are distributional, frequently predatory, related to vendibility; ceremonial and associated with cultural myths embedded in prosperity codes, magic, force and fraud. Business enterprises control the industrial arts for pecuniary ends. The industrial arts, though, are due to the cumulative evolution of the community’s stock of knowledge and thus, created by the community as a whole.

A beginning point is the separation of the productive process from the forces controlling that process. It is not difficult to grasp the distinction between making goods and making money so that in a system of business enterprise, making goods becomes a by-product of making money. Since these different types of activity have different consequences for economic welfare their distinction is an expression of the tension between the social interests of making goods and the “individual” interest in making money. Quoting Veblen:

The vital point of production with him [the businessman] is the vendibility of the output, its convertibility into money values, not its serviceability for the needs of mankind. A modicum of serviceability, for some purpose or other, the output must have if it is to be salable. But it does not follow that the highest serviceability gives the largest gains to the business man in terms of money, nor does it follow that the output need in all cases have other than a factitious serviceability.
Goods are a required part of the ordinary activities of life and thus this separation is between the life process and the production process. It is what Veblen called the first degree of separation between the general welfare and the purposes for which the business enterprise is animated, a separation of the interests of producers and consumers.

In the first degree of separation the business enterprise produces goods, manipulates prices, engages in increasingly adroit of salesmanship, and eventually sells the goods to a consumer, an end user. The enterprise does not necessarily begin with what consumers may find serviceable, but what can be sold. A manipulation of the prices and the sale of goods are the tasks to which managers turn their most acute attention. This starting point is important, but less consequential than when production entities evolve to a second degree of separation.

The second degree of separation, which is often overlooked, occurs when the larger use of loan credit is added to process of making money, not on the vendibility of goods *per se*, but by speculation in the financial capital said to be necessary to create the industrial capital that produces the goods. This is the process of creating, buying and selling business capital, which is mostly of the nature of credit and its instruments. Here managers turn their attention to the creation and manipulation of property (asset) values. The value of an asset may be comprised of two parts, tangible and intangible. Tangible or corporeal value is simply the money cost of physically reproducing the asset. The intangible value of an asset is the pecuniary valuations by businessmen. Determining the intangible value of the asset is derived directly from the customs of businessmen who own the asset. As far as we know Veblen was the first to integrate intangible property and goodwill into a theory for determining asset value.

We seek to capture the main components of the firms in both the “real and financial” sectors in Figure 5 below. Notice that we add Commons’ transactional analysis to the theory. The argument
is that the type and structure of transactions affects the value of property and degree to which differential advantage emerges. It is not a stretch to argue that managerial transactions, in particular, are compatible with Veblen’s concept of differential advantage. The transactional structure reflects the relative strength and control between instrumental or pecuniary values in the operation of the firms and sectors and sets the relationships both within the firm and among/between firms. Thus as the credit system expands financial sector firms acquire a more influential position vis-à-vis real sector firms. As the second degree of separation expands it increases the strength of managerial transactions between the sectors.

There is little tangible property associated with firms in the financial sector. A few building and a variety of business machines represent the greater part of it. Intangible property is by far the most important in this sector. It rests on the grounds of differential advantage stemming from favorable access to information associated with the ordinary activities of finance as well as a stock of esoteric knowledge possessed by employees, all of which yields an asymmetry of information resulting in the myths of financial potency embedded in the prosperity code of the culture. The value of this intangible property is a function of the community’s degree of credulity or confidence in the reputation of the separate firms and the sector as a whole and is booked as goodwill.

Intangible property, the most common form of which is capitalized as goodwill, is of no use to the general community. Rather it is an accounting mechanism for the distribution of control of the community’s production power. More precisely intangible property is the right to fix prices by withholding from others what they want but do not own. This ability in turn stems from and requires a differential advantage, in part rooted in the extension of credit. Said credit, mostly in
**Figure 5**
Integration of Commons Going Concern and Transactions and Veblenian Elements of Business Enterprise

- **Real Sector Firms**
  - **Going Concern**
    - **Going Plant**
    - **Going Business**
      - **Machine Process Engineering**
        - **Industrial Employments**
          - **Technological Efficiency**
            - **Make Goods Consumers/Serviceability**
    - **Purchase & Sale Finance**
      - **Pecuniary Employments**
        - **Financial Efficacy**
          - **Make Money Producers/Vendibility**

- **Financial Sector Firms**
  - **Going Concern**
    - **Going “Plant”**
    - **Going Business**
      - **Machine Process Financial Instruments**
        - **Technical Pecuniary Employments**
          - **Distributional Management**
            - **Invent/Refine Financial Instruments**
              - **No End Consumer**
    - **Purchase & Sale Finance**
      - **Pecuniary Employments**
        - **Financial Reputation**
          - **Make Money Producers/Vendibility**

- **Transactions**
  - **Bargaining**
  - **Managerial**
  - **Rationing**

- **1st degree of separation**
- **2nd degree of separation**
the form of bonds, debentures and stocks, permits the control of tangible property, including the industrial apparatus of production.

In the real goods sector goodwill may have value in those activities related to the goods in question. Consumer perceptions of the reliability, content, and effect of goods play a role in the increase or decrease in goodwill, as do differential advantages such as patents, trade secrets, copyrights, etc. It seems clear that intangible property and goodwill are of the nature of make-believe. They rest on the putative nature of business valuation which in turn rests on the power, prestige, and status of that better class of citizens known as captains of industry and finance. The classical theory of production attributes production to the self-sufficient individual overlooking the fact that there is no isolated self-sufficient individual. Production, with no exception, is a socially organized and structured activity. Thus when it is time to book the value of goodwill it is marked as a property right of an abstract “individual” owner, the rights of which have been ratified by a legal fiction.42

The Theory of the Business Cycle

The modern theory of the business cycle has emerged because the last hundred and thirty years have exhibited significant differences from previous periods, especially those described above. Before business principles came to dominate everyday life, privation was not so much a matter of high prices (social scarcity), as of “natural scarcity.” When business enterprise was confined to commerce it had scant impact on livelihood – but when it became the basis for industry (under the regime of the machine process) it came to impact the general welfare. Thus, as Veblen argued, the theory of general welfare is lodged in an analysis of the variation in business activity. Business forces create periodic and frequent oscillation between good times
and hard times even though the average material well being may be at a higher mark due to the penetration of the machine process.

In the new order, welfare is a considered a question of price. Business cycles are phenomenon of business principles – of prices and capitalization. The latter is a creature of financial credit. Finance proceeds on the basis of 1) solvency, and 2) goodwill. It does not follow that a period of depression is followed by one of exaltation (prosperity). An era of prosperity is an era of rising prices. At first this may seem mistaken, i.e., it is more commonly thought that an era of prosperity is an era of increasing output. While this is often thought of as prosperity in modern practice, dominated as it is by pecuniary valuation, it is not. Rising output means falling prices and increased putative profits are due to rising prices.43

Creating the expectation of increased profit is required for loan credit to be extended. Output can rise for a period of time without falling profits, but must eventually reverse. It is not to be forgotten that aggregate pecuniary profits are zero if the machine process runs on an uninterrupted basis, no uncollateralized credit is extended, and no government debt or fiat money is issued. Adjustments of expected “nominal” to “actual” value of business capital, based on actual earning capacity, are ongoing and instability results because of the adjustment process of the valuation of old investment versus new. Business capitalization is on the basis of profit yielding capacity and the business is rich or poor based on the balance sheet.

Crisis, depression and exaltation are phenomena of price disturbance. Therefore the traffic in vendible capital becomes the pivotal factor in the modern situation in business and industry. Since industry waits on business, fluctuations in vendible capital impact the general welfare and the stability of the system of economic activity. Mechanical sequence and the concatenation of the branches of industry – inter-industrial relations – are tied together by
contracts (of a pecuniary nature) for future performance. So that in the end business depression and prosperity are in their first incidence psychological facts, just as is price movement.

Following Veblen and Mitchell a report of actual profits less than expected profits is a leading indicator of the end of a period of exhalation and the beginning of the writing down of the intangible value carried on the books in the form of goodwill or other means of accounting for the inflated values due to speculation in non-serviceable vendibiles. The decline in value is seen as a loss of wealth and a depression of the propensity to consume, and the well-known Keynesian like consequences, among others, ensue.

We may visualize the emergence of degrees of separation and the modern business cycle as illustrated below:

- Handicraft (H)
- Market trading (T)
- Machine Process (MP)
- Business Capital (BC)
- Goodwill (G)
- Intangible Property (IP)
- Financial Capital (FC)
- Uncollateralized Credit (UC)
- Speculation (S)
- Business capital price (BCP)
- Financial Liquidation (FL)
- Exaltation (E)
- Depression (D)

\( H \rightarrow T \) is a situation where the producer/trader is directly involved with both the means of production and the channels of distribution. This represents the period prior to the emergence of the modern business system. A modest division of labor, small-scale production, modest if any differential advantage, goodwill or intangible property is typical.

As the machine process (MP) evolves out of this earlier form of production it is related to and controlled by the valuation of business capital (BC), just as the handicraft system was
immersed in a system of trading and commerce. MP and BC co-evolve and the latter comes increasingly to depend on goodwill (GW) and intangible property (IP). Here the first degree of separation exacerbates the valuation process between the machine process and business capital. Since this is a separation in the production/consumption continuum, i.e., between the interests of consumers and producers it is also a separation of means and ends as it relates to the expansion the tension between pecuniary and instrumental valuation.

As the money/commercial economy evolves into the credit economy the manipulation of business capital prices becomes a more ordinary and common activity of business. It is the manipulation of business capital prices; stocks, bonds and derivatives thereof, that become the preferred, higher status, activity of those in control of the business. Business capital becomes a source of speculation. It becomes financial capital (FC), and is created by the extension of more and more uncollateralized credit (UC), (based on the value of goodwill/intangible property as a source of future earnings) and is related to speculative activities of many types. Since the end user of financial credit is not the general community but other speculators, the second degree of separation on the production/consumption continuum emerges and adds to the complexity and over valuation of assets. The second degree is the focus of modern welfare in which we lodge the theory of business cycles. Since high and volatile prices represent good times and speculative opportunities, a period of exaltation ensues leading to a tension between and separation of instrumental and pecuniary asset valuations. This is frequently exacerbated by fraud. In the modern period the weapon of choice for both speculative gain and fraud is accounting. This weapon becomes increasingly complicated and more the intangible property of a professional class in possession of esoteric knowledge of the ways and means of its manipulation. This in
turns makes the system more susceptible to a growing body of asymmetrical information, more speculation and enticing opportunities for criminals.

In part due to expanded production, the possibility for which is created by the extension of the machine process, and in part due to the inflation of the value of intangible property values, the valuations are eventually unsustainable. Firms report profits below expectations. A period of devaluation begins along with financial liquidation and a decline in the value of intangible property (prices). The path of the economy, both cyclically, and secularly, may be symbolized as follows:

\[
\text{MP} \rightarrow \text{BC} \rightarrow (1^\text{st} \, \circ \, \uparrow) \rightarrow \text{GW/IP} \rightarrow \text{E/FC} \rightarrow \text{UC} \rightarrow S \rightarrow (2^\text{nd} \, \circ \, \downarrow) \rightarrow \text{FI} \rightarrow \text{FL} \rightarrow \text{D}
\]

As the system of modern welfare evolves it is subject to decay brought on by the separation of means and ends and the increasing number of activities that become subject to pecuniary valuation. This extension contaminates the instinctual heritage, e.g., workmanship becomes contaminated by business habits. Business cycles become increasingly subject to financial considerations and valuations and the tension between the instrumental and pecuniary (ceremonial) forces is either adjusted or the system becomes increasingly unstable.

**Consumption – A Theoretical application**

In *The Theory of the Leisure Class* Veblen employed the concepts of: pecuniary emulation, conspicuous consumption, conspicuous waste, and pecuniary canons of taste. Much of the flavor of his view of consumption is conveyed by these concepts. He viewed consumption as having both instrumental and a symbolic or ceremonial functions; the latter being the most
significant measure esteem. The above concepts capture the ceremonial aspect of consumption and place it in the realm of display rather than the instrumental (serviceable) function.

Ceremonial functions as evolved in the U.S. economy have taken on a pecuniary character and significant amounts of production and consumption are devoted to display as a measure of worth. It was less the instrumental aspects of goods, their ability to enhance the aggregate life process taken materially, but the ceremonial aspects that shaped the character of consumption patterns.

Consider the following passage from *The Theory of the Leisure Class* as illustrative.

Goods are produced and consumed as a means to the fuller unfolding of human life; and their utility consists, in the first instance, in their efficiency as means to this end. The end is, in the first instance, the fullness of life of the individual, taken in absolute terms. But the human proclivity to emulation has seized upon the consumption of goods as a means to an invidious comparison, and has thereby invested consumable goods with a secondary utility as evidence of relative ability to pay.47

Functionally consumption is not an end in itself (as is assumed in standard theory), but part of a continuum. We teach it as part of an evolutionary process, as man always acting—producing—consuming—producing—consuming in a continuum of means-ends. Nor do we assume rational and efficient consumers. Mitchell’s “Backward Art of Spending Money” is useful in driving this point home. Wants are not fixed nor taken as primary data, i.e., outside the scope of economic inquiry. Goods are not treated as homogeneous but as bundles of attributes.48 The attributes are differentiable as instrumental and ceremonial. So that goods are bi-valent and consumption is most commonly bundles of both ceremonial and instrumental attributes that are frequently inseparable by consumers. We express this in shorthand as below.

\[ C = f(I, C) \]

\( I \)nstrumental attributes, \( C \)eremonial attributes

And then point to several attributes that may be included in these more specific functions depending upon the good under consideration. General categories of these include:
Ca = f (c, pe, cw, pct) where c = conspicuous, pe = pecuniary emulation, cw = conspicuous waste and pct = pecuniary canons of taste.

Ia = f( clp, d, e, s, rc ) where clp = contribution to life process, d = durability, e = efficiency, s = safety, and rc = re-creational capacity

Next is a theoretical example of what we teach to theoretical of what we teach to the theory of consumption. Consider the Giffen paradox, so called. It is a paradox in the standard theory of demand since it gives rise to an increase in consumption of a good when its price increases. Paradoxes frequently reveal theoretical deficiencies. In institutional theory Giffen is no paradox at all, since it is capable of analysis using a theoretical argument based in habit adjustment and perception. Suppose ones diet consists of meat and potatoes in amounts just enough to maintain basic nutritional requirements. If the price of potatoes increases it is impossible to consume the same amounts in the new situation. The situation is problematic for the retention of the old pattern of consumption and requires an adjustment to the new circumstances. Yet, before the required adjustment is possible several things are required. First, there must be the actual perception that a change in diet is required. Reduced to its simplest form an individual is faced with four interrelated conditions.

1) an instrumental function - in this case a minimum number of nutrients for a subsistence diet (some combination of meat and potatoes such that the price to nutrient ratio (p/n) is lower for potatoes than for meat,

2) a preference (ceremonial) function – in this case a preference for meat over potatoes of at least the combination of the previous situation,

3) a budget limitation/limiting factor such that no more can be spent on the two than previously, and
4) a perception of the need to adjust based on the above.

The latter does not require a particular adjustment only a perception of that one is needed. The individual may prefer to remain with the habits and patterns of behavior of the previous situation, but the environmental conditions have changed such that it cannot. The situation can be analyzed as follows. From the K-D-V model, if meeting the instrumental function is the action chosen at the conclusion of the process, the adjustment of habits begins. The individual has perceived the instrumental requirement of maintaining a sufficient number of nutrients for basic requirements; the presence of felt difficulty and an adjustment to it. If the difficulty is passed through the comb of deliberative inquiry and if the warranted stock of knowledge allows for proper judgment of the diet, one may act to adjust to meet the instrumental function. These results in an increase in consumption of potatoes and a reduction in meat: because it is the only way to get enough nutrients to forestall malnutrition. In the alternative, one may decide to meet the preference (ceremonial) function first. This does not mean immediate starvation, but it does involve malnutrition. Note that there is no necessity of an immediate perception of the instrumental consequences. In fact it may take a while to notice that one cannot eat as much meat as before. Nonetheless this choice would lead to an increase in meat and decrease in potato consumption. The simplicity and homeliness of the example should not reduce its importance in understanding human behavior. It may be applied to any level of finite budget constraint, type of instrumental function and preference function. It need not be limited to a “necessities of life” situation. For example, a family with two cars one cheap and one expensive (say a Ford and a Porche) faced with replacing one, but also with an increase in the price of the cheap one.

Further, it illustrates that habit adjustment involves a tension, a stretch in the value structure. In the above example the tension is between the two sources of habit formation. It involves the
instrumental value function (nutrition) and the ceremonial function (preference for meat over potatoes). The two-way stretch creates a situation where either the preference function cannot be sustained over time and will eventually either adjust or the individual will starve. This is the equivalent of an institution being unable to adjust. The simplicity and homeliness of the example should not reduce its importance in understanding human behavior. It may be applied to any level of finite budget constraint, type of instrumental function and preference function. Further, it illustrates that habit adjustment involves a tension, a stretch in the value structure. In the aforementioned example the tension is between the two sources of habit formation. It involves the instrumental value function (nutrition) and the ceremonial function – preference for meat over potatoes. This two-way stretch creates a situation where either the preference function cannot be sustained over time and will eventually either adjust or the individual will starve. This is the equivalent of an institution being unable to adjust. Note also that the concept of limiting factors (Commons) is the equivalent of a “budget constraint” and strategic factors are interwoven into the process by which one adjusts the tension and habits involved in the changed situation. Also note that it does not take much to add an increasing reliance on “consumer debt” to this approach. The “budget constraint” is eased by adding the capacity to incur debt as a means of payment. This is also a path to tie consumer behavior to producer behavior during the course of the business cycle. This is not treated here, but is a part of the approach we take in teaching institutional economics.

**Conclusion**

This admittedly incomplete overview of the Kansas City approach provides a guide to what we teach and to the other papers in this and our other session. We do not purport to cover the field in the papers nor in what we teach in our classes. Much in the field is omitted but what
we cover does, we think, prepare students for further work. We recognize that our approach is not without deficiencies and most certainly is not without deserved criticism. Yet, it does strive to preserve, improve, and extend an important body of economic thought and it this we seek the continued assistance of our colleagues, critics and fellow travelers.
This appendix is not complete. I have put it together on the basis of memory and a few papers I have in old files. I need to do some archive work to finish it. It does have some serviceability even as an incomplete guide to the people associated with the department.

Appendix 1

Institutionalists Associated with UMKC as faculty or Ph.D. graduates, 1946 – 2010

John Hodges, 1946-1986, University of Texas (1938) Ayres

Mike Wagner, University of Texas (1950), Ayres

F. Eugene Wagner, 1959 – present (UKC, Syracuse), Hodges,

Joe Brown, 1966-1978, University of Texas (1953), Ayres

Reverdy Gliddon University of Texas (1955), Political Science, Ayres

Neel Proctor (Texas A & I, LSU), Brown

Ted Brannon University of Texas (1950’s), Ayres

William Frederick University of Texas (1950’s) Ayres

John Chitwood, University of Texas (1960’s) Gordon

William D. Williams, 1998 – 2004 (University of Denver, Union Graduate School) Foster

James Sturgeon, 1977- present, also MA, 69, Oklahoma (Hodges, Brown, Peach, Reese)

Wray Tool, Henry, Minsky (Cal State, Washington University, St. Louis)

Kelton (Henry, Wray, Nell)

Forstater (Heilbroner)

Brazelton (Dow}

Todorova (UMKC)

Parada (UMKC)

Scott (UMKC)
Nikinia (UMKC)
Kaboub (UMKC)
Tauheed (UMKC)
Bowles (UMKC)
Appendix 2

Syllabi for Institutional Economics Courses at UMKC

Syllabus
Institutional Economic Theory
Economics 451
University of Missouri-Kansas City
Department of Economics

Introduction
Institutional Economic Theory builds on knowledge that has emerged and is emerging from a number of areas including social psychology, sociology, anthropology, and even some of the physical sciences. It will probably be of assistance to you in grasping the content and implications of the institutional way of thinking to be reminded from the beginning that it cannot be best understood as a mere modification of conventional economic and social thinking, but rather, represents a significantly different way of thinking about man, the economy, social activities generally, and human economic and social potentials.

Reading Requirements
C. E. Ayres The Theory of Economic Progress (TEP)*
Brian Arthur, "Positive Feedbacks In the Economy" Scientific American, Feb. 1991 (BA)*
Robert Montgomery, "Historical Fact" Unpublished Paper (RM)*
Thorstein B. Veblen "Why is Economics Not and Evolutionary Science" (TBV1)*
_____, "The Limitations of Marginal Utility" (TBV2)*
_____, The Theory of the Leisure Class (TBV3)*
_____, The Barbarian Status of Women (TBV4)*

The acronyms in parenthesis following each reading are used below in the reading guide.

Please note that other readings will be suggested during the course. These will be "recommended" and will sometimes be the source for discussion.

*Available electronically at
http://cas.umkc.edu/econ/economics/faculty/sturgeon/451webpage/index.html
**Available at
http://www.jstor.org/view
Reading and Course Outline

This outline is presented as a suggestion of the broad outline of the course, but, more importantly as a guide to the reading of the textual materials. Please note the Key which is used to refer to a specific textual source.

TEP, C. E. Ayres *The Theory of Economic Progress*
V1, Thorstein B. Veblen "Why is Economics Not and Evolutionary Science"
V2, Veblen, "The Limitations of Marginal Utility"
V3, Veblen *The Theory of the Leisure Class*
V4, The Barbarian Status of Women
RM, Robert Montgomery, Historical Fact
BA, Brian Arthur, Positive Feedbacks In the Economy
PD, Paul David, Clio and the Economics of Qwerty

I. Economic and Social Thought in Historical Perspective -- an Overview
   Standard Economics
      Pre-classical and Classical/Neo-classical
      Keynes and Keynesian
      Socialist Reaction, including Marxism
   Reactions and Criticisms of Classical/Neo-classical
   German Historical School
   Institutionalist Thought

   Reading – Week 1
   TEP, Chs 1-4
   V2

II. The Nature and Characteristics of Theory and Theoretical Systems
   Points of view - static, taxonomic - dynamic, evolutionary paradigms, theories,
   frame of reference
   Method - Methodology
   Science and Sciencing
   Selected Confoundings

   Reading -- Week 2
   V1
   RM

III. Institutional Theory as a Way of Thinking: Basic Concepts
   A. Introduction

   Reading – Week 3
   TEP, Preface & 1962 Introduction
   V3, Introduction, Chapter 1

   B. The Concept of Culture

   Reading – Week 4
   TEP, Ch 5
   C. The Veblenian Dichotomy
Reading – Weeks 5 & 6
   TEP, Chs 6-9
   Waller
IV. Institutional Theory of . . . .
   A. Resources and Production

Reading – Weeks 7 & 8
   BA
   PD
   Munkirs
   B. Consumption

Reading – Weeks 9 & 10
   V3, Chapters 2-7.
   V4
   C. Value
      Reading – Weeks 11 – 1
      TEP, Ch 10
   D. Progress
      Reading – Weeks 13 – 14
      TEP, Chs 11-13
      V3, Chapters 8-14.
Syllabus
Capstone Colloquium in Economics
Economics 499
University of Missouri-Kansas City
Department of Economics

Course description:
As the capstone of the undergraduate degree in Economics, this course gives students an opportunity to integrate and apply their knowledge of the theory and methods of economic analysis acquired in this and previous program coursework to the problems of economic development in a major metropolitan region. Major components of the course include:

1. Readings, lectures, and class discussion in the theory and practice of urban economic development
2. An 8 - 10 page writing assignment, conforming to the requirements for designation of this course as “writing intensive”
3. Training in the use of Geographic Information Systems (GIS) software
4. A group project entailing preparation of an economic development proposal for a specified urban neighborhood
5. A midterm and a final exam

Textbooks:

Supplementary Readings:

Writing assignment:
The detailed requirements for the case study writing assignment will be provided as a separate document. Original writing assignments will be critiqued, evaluated for grade, and returned to students for rewrite, if required. Failure to submit a required rewrite will result in a zero grade. So that students may anticipate the instructor’s expectations as to the level of work required for a given grade, the rubric used by the instructor for writing assignment critique and evaluation is attached to this syllabus. Students are encouraged to make use, as necessary, of the College of Arts & Sciences Writing Center (see attached information sheet). Writing assignments submitted late will be assessed an immediate penalty of 5 percent, followed by an additional penalty of 5% per week (calculated as 1 point per week day, Mon Fri).
Training in GIS software:
At least two class periods early in the semester will be devoted to training in the use of Geographic Information Systems (GIS) software in the Urban Research Lab (314 Haag Hall). The goal of this training will be to give students the capability to optionally employ GIS and descriptive data mapping in their group projects.

Group project:
Students will be assigned to groups by the instructor. Using methods derived from course materials and lectures, and in consultation with the instructor, each group will formulate and present to the class a viable economic development proposal for a defined neighborhood, district, or community of the Kansas City metropolitan region. The proposal will be produced as a written report and turned in for grading. The group’s project grade will include evaluation of the class presentation. Details of the requirements for this project will be provided as a separate document.
Required readings discussed in class

- Hodgson, Geoffrey *The evolution of institutional economics* (Available at UMKC bookstore and other sources)
- Dewey, John *Human Nature and Conduct* (Available at UMKC bookstore and other sources)
- Ken Dennis, Boland on Friedman, *Journal of Economic Issues*, September, 1986
- John Dewey, *The Quest for Certainty*, Chapters 1, 3 & 7.*
- Veblen, Thorstein *The Theory of Business Enterprise*
- _____, "The Limits of Marginal Utility”*
- _____, "Why is Economics Not an Evolutionary Science”*
- _____, "The Instinct of Workmanship and the Irksomeness of Labor"*
- _____, "The Barbarian Status of Women"*
- _____, “On the Nature of Capital”*

Background readings considered prerequisites

- Paul David, “Clio and the Economics of QWERTY,” *AER*, May 1985.**
- Clarence E. Ayres *The Theory of Economic Progress*
- Robert Montgomery, "Historical Fact" Unpublished Paper*

* Available electronically at course Website
** Available at jstor (see below for address)

Course Outline

**Method and philosophy of knowledge**

Hodgson, Chs 1-3
Veblen, "Why is Economics Not an Evolutionary Science"
Robert Montgomery, "Historical Fact" Unpublished Paper
Ken Dennis, Boland on Friedman, *Journal of Economic Issues*, September, 1986
John Dewey, *The Quest for Certainty*, Ch 1-3 & 7
Theory of human behavior
Hodgson, Chs 4, 9
Dewey, Parts One & Two
Ayres, Ch 5
Veblen "The Instinct of Workmanship and the Irksomeness of Labor"

Historical footings, theoretical concepts and principles
Hodgson, Chs 6 – 8, 12, 14 - 18
Ayres, Ch. 1-4.
Veblen, The Theory of Business Enterprise
Veblen “The Limits of Marginal Utility”
Veblen "The Barbarian Status of Women"

Theory of valuation
Hodgson Chs 10
Dewey, Part Three
Ayres, ch 10
John R. Commons, Institutional Economics: Its Place in Political Economy, pp. 649-692
Yngve Ramstad, “‘Reasonable Value’ vs. ‘Instrumental Value’”

The process of change, adjustment and progress
Hodgson Chs 19- 21
Dewey, Part four
Ayres, Ch 11-13
Foster, "The Theory of Institutional Adjustment"
Course Plan

Colloquium means an extended and organized conversation. The class begins with a discussion of several topics: historical, theoretical and applied. Students will participate in these discussions and will write a paper chosen from the topics below that will be presented to the class. The final version should be near publication quality. Each student will choose or be assigned one or more chapters or articles to summarize and discuss in class. An outline and notes should be available (in paper and electronic form) one week prior to discussion. Political economy is vitally concerned with the ongoing nature of the relationship between groups in the community. Hence, each student is expected to devote 8 hours over the semester to community involvement. Avenues for this involvement and its verification will be explained later in the course.

A central concept for this course is what has been called the machine question. We will attempt to elucidate the impact of this question on economic and social thought and on economic change and welfare.

1. Types of Political Economy
   a. Classical -- Neo-Classical – Smith to Marshall and possibly beyond
   b. Marxian
   c. Institutional
   d. Keynesian - Post Keynesian
   e. Others

2. Philosophical Foundations and Methodological Issues
   a. Moral Sentimentalism - Aristotle to Aquinas to Newton
   b. Dialectics - Dialectical Materialism
   c. Instrumentalist - Evolutionary
   d. Logical positivism
   f. The nature of scientific and theoretical change

3. Theoretical Concepts and Controversies
   a. Problems & issues - what are the issues, how do we frame the questions
   b. Markets, price, capital, value
   c. Change, adaptation, adjustment, progress
   d. Employment, investment, consumption
   e. Policy formation and implementation
   g. Income distribution
   h. Economic order, growth and progress
   i. The nature of money and capital
j. Social and economic class

4. Policy Issues in Political Economy
   a. Taxation, equity and growth
   b. Weal and Welfare
   c. Investment and productivity
   d. Human capital, race and class
   e. Markets, Control, Planning & Organization
   f. Trade and Global economy

Readings
- Available electronically at (Look in Courses - Readings) at
  http://cas.umkc.edu/econ/economics/faculty/sturgeon/688webpage/index.html

** Available electronically at (Look in Courses - Readings) at
  http://www.jstor.org/jstor/

Books
James Caporaso & David Levine Theories of Political Economy
Karl Polanyi The Great Transformation
Adam Smith An Inquiry into the Nature and Causes of the Wealth of Nations
David Ricardo The Principles of Political Economy and Taxation
John S. Mill Principles of Political Economy
Karl Marx Theories of Surplus Value
    , Das Kapital
John M. Keynes The General Theory of Employment, Interest and Money
Milton Friedman Capitalism and Freedom
F. A. Hayek The Road to Serfdom
J. K. Galbraith A Life in Our Times
M. C. Howard & J.E. King The Political Economy of Marx
Michael Perelman Classical Political Economy
Marc Tool Essays in Social Value Theory
C. Wright Mills The Power Elite
G. William Domhoff The Power Elite and the State
John R. Commons, Institutional Economics: Its Place in Political Economy* (in part)
John Dewey, The Quest for Certainty
Thorstein Veblen, The Theory of Business Enterprise*
    , The Theory of the Leisure Class*
C. E. Ayres The Theory of Economic Progress*

Articles
John R. Commons, "Institutional Economics" *
J. B Davis "Distribution in Ricardo's Machinery Chapter", History of Political Economy (HPE), Fall 1989
Paul David, “Clio and the Economics of QWERTY,” American Economic Review (AER), May 1985,**
Robert Montgomery, Unpublished Paper*
Ben Seligman "The Impact of Positivism on Economic Thought" *HPE*, Fall 1989
Ken Dennis, Boland on Friedman, *Journal of Economic Issues, (JEI)*, September, 1986
Wassily Leontief, "Theoretical Assumptions and Nonobserved Facts," *AER*, 1971.**
T. Veblen “The Limitations of Marginal Utility”* 
_____, “The Limits of Marginal Utility”* 
_____, "Why is Economics Not an Evolutionary Science"* 
_____, "The Instinct of Workmanship and the Irksomeness of Labor"* 
_____, "The Barbarian Status of Women"* 

More readings will be announced as the class proceeds

**Electronic Resources**

1. The electronic site for this class is:  
   [http://cas.umkc.edu/econ/economics/faculty/sturgeon/688webpage/indexl](http://cas.umkc.edu/econ/economics/faculty/sturgeon/688webpage/indexl)


3. [http://www.marx.org](http://www.marx.org)

4. [http://cepa.newschool.edu/~het/home.htm](http://cepa.newschool.edu/~het/home.htm)


7. [http://csf.colorado.edu/pkt/](http://csf.colorado.edu/pkt/)
Endnotes

1 Hodges was killed in an automobile accident while returning home from the airport.

2 He wrote a review of Abba Lerner’s review of *The Theory of Economic Progress*, but Fritz Machlup, then editor of the *American Economic Review*, rejected it. See James I. Sturgeon & Hartwell Byrd, *Journal of Economic Issues* 19xx for background on this and to read the review.

3 Mike Wagner taught the Foundations course for several years before he moved to the University of the Pacific. Gene Wagner then taught it until the late 1990’s when the College faculty decided to remove it from the general education requirements for undergraduates.

4 Over the years several institutionalists have been on the faculty either as visitors or non-tenure track full time members, including, Ben Young, Ivan Weinal, Mike Kelsay, Bill Williams, James Webb. Several others earned degrees including John Munkirs, James Sturgeon, Ben Young, Martin Stack, Ivan Weinal, Tom Hale, Linwood Tauheed, Doug Bowles, Myles Garlind, Jairo Parada, Robert Scott, Fadel Kaboub, Zadravka Todorova, and several in progress.

5 His shop, the Center for Economic Information, now in its 15th year, is a model for empirically based applied institutional economics. It is drawn on what may described as a Mitchell/Commons approach to establishing an empirical research program that informs and helps shape public policy. Doug Bowles presence in that shop adds a strong measure of institutional interdisciplinarity. Their work is focused on the Kansas City metro area. The latest example of this is the Green Impact Zone, a major community development program created with the cooperation of City, State and Federal governments and funded mostly through the Economic Recovery Act of 2009. It is not a stretch to say that the presence of this approach to teaching and use of econometrics and empirical research has been an indispensible strand in the fiber of our program. Heterodox programs that have a narrow application of economic statistics and statistical methods would perhaps best understand this importance.

6 The Consortium is a co-discipline in the Ph.D. program. It has a significant Institutionalist influence and is the most often chosen by economics students.

7 We find Hodgson’s work helpful as a survey of the landscape and an expansion of the source material for instruction. We find it to have several errors. The most significant of these are his 1) nearly complete misunderstanding and misrepresentation of Veblen’s instinct of workmanship and theory of pecuniary motive, 2) dismissal of Commons as confused and confusing, 3) apparent misunderstanding of Ayres and his influence (e.g., his lack of recognition of the influence of Ayres on future generations of institutional including, Foster, Junker, Peach, Reese, Hodges, Brown and many others. This later is understandable perhaps since there is not too much written work of these scholars, but there is some and there is also recourse to oral histories and interview of relevant sources.

8 See Course Syllabi in Appendix 2.

9 This work sought a way to “marry the cultural level with the social psychological (individual level)” as Brown expressed it. His work is found an unlikely place, the *Final Report to the Ford Foundation on Programs in Urban Science*. 1964. The two way stretch in the value structure is a model derived from Brown and Hood.

10 William T. Powers *Behavior: the Control of Perception*

11 See Charles S. Pierce “How to establish our beliefs” and Making our ideas Clear, in

12 See John Dewey, *Logic: the theory of inquiry*


See William Waller, The Evolution of the Veblenian Dichotomy, *Journal of Economic Issues*, March 1982. I came of age on C. E. Ayres’ version of the Veblenian Dichotomy, but gradually came to Foster’s view. The main force in changing my thinking was the Principles of Institutional Adjustment. Bill Williams had a lot to do with it and those who knew Bill or his work will recognize his influence on this paper.

Institutionalists are familiar with this theoretical construct and no further explanation of it is included here.

The intellectual history associated with this problem goes back to Plato and possibly beyond; the modern history to Adam Smith. Smith framed it as private vice/public virtue this tried to construct an alternative view of economic order, one to replace mercantilism. Marx saw the problem as an inevitable struggle between the haves and the have nots. Marshall hoped economic chivalry would reduce the conflict among firms and the public. Veblen framed the problem as an endless stream of distinctions between science and superstition, or more specifically between industrial and pecuniary habits. Keynes saw the problem as a series of fallacies of composition that led to an internal breakdown of economic order; individual rationality leading to irrational aggregate outcomes. Ayres fashioned a dichotomy between technology and institutions, or instruments and ceremonies to get at the problem. Galbraith used the concept of countervailing power to explain why both liberals and conservatives have problems explaining the contemporary U.S. economy, the large corporation, and to show why government activity was needed to help close the gap between the power of the corporation and the ability of the individual to bargain over wages. In the past few years the New Institutionalist approach, led by the work of Oliver Williamson has emerged. For Williamson one main function of the firm is to reduce transactions costs created by opportunism, asset specificity, and bounded rationality.

We teach that the Social Fabric Matrix can be effectively used in analyzing how institutions/habits change. It can reveal quantitative and qualitative aspects of an institution that indicate how and in what direction adjustment is possible or more probable. The Social Fabric Matrix and its uses are extensively examined in *Institutional Theory and Praxis: the Social Fabric Matrix*, Editors, Tara Narinjan, Scott Fulwiler & Wolfram Elsner, Springer, 2009, and are not discussed here.

Foster, *Journal of Economic Issues*, p. 933

Foster’s term was technological determinism. In this chapter it has been renamed it instrumental primacy. The latter is more in line with terminology used to define the Veblenian dichotomy and in light of contemporary usage of technological determinism, is less likely to be misunderstood.


For example, the most reliable way to stop an automobile is to apply the brakes. Few would seriously entertain praying as a means of stopping– at least they would not actually use it very long.

For a more complete explication of deliberation as used in pragmatic philosophy see John Dewey, *Human Nature and Conduct*

The term model is not entirely appropriate, but it serves as a convenient name, better perhaps than flow diagram or figure.
The attempt in the early 19th century to implement the utopian idea of a self-regulating market economy threatened such an upheaval in the U.S. economy and increased the tension and conflict that has endured since. See Karl Polanyi, *The Great Transformation* for an analysis of this.

Here the argument is not significantly different from that made by John Dewey in *Human Nature and Conduct*. It is only in its application to the theory of human behavior as the control of perception that the argument is expanded.

Space does not permit elucidation of this concept. See William T. Powers *Behavior The Control of Perception*, and William D. Williams *The Giffen Paradox*

Ceremonial means are without genuine causal or experimental linkages. Thus selection of such a means has little hope of solving a problem in a way that permits continuity or even of solving a problem. But within the bounds they set, however elastic, there is a required accommodation for a successful adjustment. Progressive change requires adjustment of behaviors to instrumental requirements. Change is not found in reenactment or routine – but by experiment and trial and error. Error is born in unfulfilled expectation. Instrumental behavior involves the correlation of expectation and action, error detection and adjustment. It strives to bring action into correlation with expectation—without prejudice. Ceremonial behavior is imaginary, mis-specified, misplaced or mistaken if – then relations/correlations. Instrumental patterns impose structure and behavior on other patterns, but these impositions are not necessarily known in advance addressed in advance of technological change. Instrumental Primacy can be discerned by the SFM. Since the actual ability to do something is a prerequisite to any adjustment it is necessary to know what is now possible or may soon be possible. The SFM is suitable to this task and can also disclose patterns of power and control in a situation.

Here the term experience is meant as Dewey expresses it, perhaps best in *Art as Experience*, chapter 2, having an experience.

Dewey *Values and nature* (p. 62)

Veblen realized that the classical analysis of Smith *et al.* was deficient for understanding a credit economy. And he set about to create a new theory by figuring out what was going on in actual firms and with actual business practices. More specifically, Veblen built his theory of the credit economy on the testimony and observations of businessmen involved in creating the modern industrial corporation, as recorded in the 1900-1901 industrial reports. The extensive use of credit in the form of corporate securities created a conflict between the old and contemporary definition of capital.

Ibid. Page 658

Ibid. Page 660

The machine era begins with the development of mechanical means of production too extensive to be owned and operated by independent craftsmen. Ownership is thus divorced from operation. Joint stock companies, later business corporations, are created as individuals. Joining Locke and Marx the ideal of the Natural Rights of the individual is the path taken, rather than an alternate path of community control. This was a moment of path emergence or as it turned out path entrenchment. Smith had argued that the division of labor was limited by the extent of the market and therefore the market, including market competition should be extended. Everyman comes to live by exchange and is some measure a merchant and society grows to be commercial society. By following Smith’s idea that competition is necessary to extend wealth we see this interplay as a kind of personal bargaining transaction between buyer and seller. While the handicraft era is past, it is the one in which the roots of economic analysis are set on their path. In the present age the reliance on the old order economic theory is of the nature of a devout observance

We pause to recall Robert Hielbronner’s definition of advertising as “an activity that demonstrates to the young that adults will lie for money.”

Veblen’s theory was gleaned from the evident exploitation of business transactions when left unregulated by law. Commons, taking Veblen’s lead defined intangible property as the present value of the future bargaining power of capitalists, the ability to fix prices. He based his refinement of Veblen on the Supreme Court’s doctrine of Reasonable Value, which he finds in judicial decisions. See Thorstein Veblen, *The Theory of Business Enterprise*, and John Commons, *Institutional Economics: Its Place in Political Economy*, Volume 2, New York: Macmillan, 1934, page 655 and p. 6.

These are found in *The Theory of the Business Enterprise* (1904).

Recall from Commons that managerial transactions are between a “legal” superior and subordinate.

The Supreme Court of the US recognized the concept of intangible property in 1890 when it declared that the reduction of railway rates by the Minnesota Railway Commission was a “taking of property”. In this case what was taken was not corporeal property, but the intangible property of power to fix prices. The court also declared that the taking of property was a judicial, not a legislative question. The definition of Reasonable value has changed over time with the evolving decisions of the courts. This evolution generates new “reasonable” practices which impinge upon the old, until we reach the present contesting concepts of reasonable value in a world that inherits the old, but is compelled by economic maladjustment to evolve a future new out of the obsolescent old. Reasonable value is the evolutionary collective determination of what is reasonable in view of all the changing political, moral, and economic circumstances and the personalities that arise there from to the Court. The process goes on quietly in the pleadings, briefs, arguments, and opinions of lawyers and judges, and it is not until several years have passed that the change can be formulated in a "leading case."

One is put in mind of the wisdom of Milo Minderbinder, Joseph Heller’s black marketeer in *Catch 22*, “It’s a good year for artichokes, the crops are bad.”

Veblen argued that the accumulation of great fortunes was primarily by means of force and fraud. William Black notes the emergence of Control Fraud in the modern era. This is accomplished when crooks come into positions of authority in business. See his book, *The Best Way to Rob a Bank is to Own One.*

Veblen argued it resulted in an increase in warlike activities or the reversion to “Christian values” and the laws of God. The former is an historic path that followed the rise and fall three separate eras of handicraft in Europe and has been notable in the second century of the machine age. The latter precedes the doctrine of Natural Laws and Natural Rights and the liberation of the individual from the tyranny of monarchs and religious dogmas. Reversion to the latter reverses this liberation. Veblen was no advocate of Natural Rights, as his critique of Marx and others readily shows, so his analysis here is not to be interpreted as advocacy. While Veblen appears to have a low opinion of Natural Rights he seems to have an even lower one of God’s Laws. The machine age brought a new concept of efficient causality, one of cumulative sequence free from the anthropomorphic residue of earlier orders. But it does not guarantee progress in the human condition.

Gary Becker’s work, for example, extends the logic of business calculation to the family. Within the movement and direction of economic analysis, governed by pecuniary valuation and a businesslike frame of mind, his conclusions are consistent with Veblen’s. But for Veblen this is a contamination of the most important of all instincts, the parental bent, and pushes the specie toward extinction. Veblen points out in *The Instinct of Workmanship* that our genetic composition was last changed during the last ice age and is incompatible with the institution of business enterprise. In the absence of another mutation, the continued pursuit of business activities will scarcely improve, and most likely will diminish, the specie. Under the progress of business enterprise we become less and less suited to operate the means of production. Business enterprise is more often an activity of calculation (reflex) rather than deliberation (intelligence) and Veblen’s foresaw the likelihood that the specie, or some substantial portion of it, will succumb to its siren song and be swept aside in the evolutionary jousting; a species unable to adapt its basic nature to the matter of fact world.