Review of Chapter 5 Building on Lost Foundations: The Institutional Matrix and Socioeconomic Development by Howard Stein. In *Beyond the World Bank Agenda*, pp.111-46, 2008. Chicago and London: The University of Chicago Press.

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Abstract:

Stein (2008) provides an original institutional economics (OIE) approach to development. He clarifies the concept of institution, and elucidates the stratified causative forces and the part-dependent, cumulative nature of institutional changes. My argument is that more attention should be paid to the valuing system and process in the Stein's formulation of the OIE approach to development.

Keywords: Original Institutional Economics; Institutional Changes; Development

Howard Stein argues that the World Bank development agenda projects a parsimonious neoclassical doctrine onto a complex social and economic reality. In Chapter 5 "Building on Lost Foundations", he attempts to recover "the Lost Foundations", that is, an alternative development vision based on the original institutional economics (OIE) put forward mainly by Gunnar Myrdal.

Myrdal's institutional approach provides an analytical framework that enables the creation of new constructs and theories from a contextualized understanding of development. Development is viewed as a non-linear, anti-teleological process that arises mainly from "policy-induced changes in the social and institutional structures". More specifically, according to Myrdal, development is driven by the dynamics and interplay of six broad categories of the social system, namely, output, condition of production, standard of living, attitudes toward life and work, institutions and policies. The concept of institutions is the most vexing one, the treatment of which is unsatisfactory and misleading in the new institutional economics (NIE) and even sometimes in the OIE. Stein carefully explores the meaning of institution and its relationship with norms, organization, regulation, capacity and incentives. The latter five elements constitute an institutional matrix.

Norms are defined as "socially driven behavioral guidelines concerning what is expected, required and accepted". Norms can be internalized, which then form habits of thought, which in turn become institutions once a sufficient number of people have internalized the habits of thought. Norms are typically enduring as repositories of power, so the challenge of development is to change or deepen norms to alter or reinforce existing habits of thought. Organization is "conceptually (and often legally) recognized entities that combine groups of people with defined common rules and purposes". Institutionalists understand organizations as socially constituted entities embedded within and interacting with a web of norms, rules and beliefs. Organizations have the power to transform human conditions. Regulations define, initiate, support and transform institutions while capacities help constitutive members to achieve their goals within

the confines of rules and purposes. Finally, incentives include not only economic motivations but many other non-material ones, such as reciprocity, wish to avoid social disapprobation and desire for interesting tasks (Fehr and Falk 2002). Moreover, potential reactions to incentives are learned and contextualized. The anatomy of the institutional matrix leads Stein to conclude that institutional changes should focus on "generating new norms of correlated behavior aimed at increasing the generalized standard of living of the population of a country". Changes are path-determinant, that is, the designs for changes are open-ended but linked to the past; changes are neither path independent as in the neoclassical framework nor path-dependent, which would root out the possibilities of reform/change.

Stern's exposition of the institutional approach to development is inclusive and illuminating. The strength of his theorization rests in three aspects: firsts, it provides tremendous analytical clarity to the concept of institution. Institutions not only restrain behavior, a point emphasized in the NIE; they but enable behavior by way of reducing uncertainty and anchoring expectations. Institutions also differ from institutional constructs; the latter often take the form of organizations and organizational changes whereas the former are generally internalized habits of thoughts. Second, Stern stratifies the causative forces driving institutional changes. He insists that human agency is the subject and object of institutional changes. Development involves behavioral and organizational changes, which are a product of evolutions of habits of thought and in turn transform habits of thought. Finally, Stern substantiates the fact that cognition is "expansive and continuous", which provides the basis of circular causation and cumulative changes of institutional transformation and hence the development processes.

Given all the merits of the exposition, I have, however, a quibble, that is, the missing component of instrumental valuing in the institutional change. It is understandable that Stein follows Myrdal's theory, which does not explicitly address the valuing process. However, contemporary Institutionalists have advanced the theory of institutional adjustment to include the valuing process. In Stern's argument, development is not treated as a discourse but simply alluded to as an increase in "the generalized standard of living of the population of a country". Standard of living, or level of living in Myrdal's social system matrix, refers to quality of food and housing, quality and accessibility of medical care, education, provision of public goods and so on. This seems to be problematically narrow and leads to an end-in-point view of development. Sen's capabilities approach to development compares favorably in this regard where expansion of freedoms is the end and means of development (Sen 1999). But more importantly, because development is a normative process, just like any other social system transformation and institutional changes, it necessitates a valuing system and process. OIE has put forward the theory of instrumental valuing, which proposes instrumental efficiency as a valuing criterion. In my view, this should be an indispensible, explicit component of any original institutional theories of institutional changes/adjustments.

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