The role of culture and institutions in economic history: can economics be of any help?*

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"… economists are notoriously uninterested in how people actually think or feel." Paul Krugman, *Development, geography, and economic theory* (Cambridge, Mass. 1995) 74.

Introduction

In 1996 *The Economist* published an article in which it was claimed that Goering, who supposedly reached for his gun every time he heard the word culture, would have an aching hand today.[1] *The Economist*, as usual, was right. References to culture have indeed become *en vogue* even amongst economists. Of course they have not taken over mainstream economics, but in many analyses so-called proximate causes, like presence and nature of the forces of production, and technology, have been losing pre-eminence to ultimate causes like culture and institutions. It is too early yet to talk of a cultural turn in economics but there clearly are signs of change.[2] The theme of this conference, the place of culture in economic history, therefore, is well chosen. But personally I think there is no harm in

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[1] *The Economist*, "Cultural explanations. The man in the Baghdad café", November 9th 1996, pp. 25-32.
[2] For literature see R. Klump, ed., *Wirtschaftskultur, Wirtschaftsstil und Wirtschaftsordnung. Methoden und Ergebnisse der Wirtschaftskulturforschung* (Marburg 1996); V. Kunz, "Kulturelle Variablen, organisatorische Netzwerke und demokratische Staatsstrukturen als Determinanten der wirtschaftlichen Entwicklung im internationalen Vergleich", Kölner *Zeitschrift für Soziologie und Sozialpsychologie* 52 (2000) pp. 194-225 and H. Siegenthaler, "Geschichte und Ökonomie nach der Kulturalistischen Wende", *Geschichte und Gesellschaft* 25 (1999) pp. 276-301.

broadening the subject and include economic and political institutions. I do not mean to say that these are a *direct* and *unequivocal* reflection of culture.[3] On the contrary, I think that this is hardly ever the case. But mostly culture and institutions are so strongly intertwined that it is extremely difficult, as well as not very enlightening, to try and disentangle them. Institutions do have dynamics and logics of their own that cannot directly be reduced to the culture of the individual participants involved, but on the other hand, they simply cannot be understood nor explained without reference to that culture. In a sense culture can be regarded as the software of institutional arrangements that, in turn, play a big part in determining culture.[4] However awkward this may be for the theoretician: we are discussing a tight and dialectical relationship between elements that are almost impossible to keep apart. Institutions as structures and culture as their software in the end are two sides to the same coin.[5] I will come back to this point repeatedly.

This article will be fairly idiosyncratic. In the end it is the result of my search, as an historian writing a book on the rise of the West, for general information about the role of culture and institutions in promoting or hindering economic growth. In my reading on the rise of the West I found numerous references to the role of culture and institutions. It does not always, however, become clear how exactly to interpret, assess, and combine them. So I thought that throwing a glance at the literature on these themes by economists or theoretically informed economic historians might

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[3] As North, for example, suggests in D.C. North, *Structure and change in economic history* (New York 1981) pp. 59–60 and in D.C. North, *Institutions, institutional change and economic performance* (Cambridge 1990) p. 137 and as does Landes in his discussion with me in *Itinerario. European Journal of Overseas History* 23 (1999) 8-16, p. 8.

[4] A very interesting analysis of the effects of economics on culture can be found in R. Sennett, *The corrosion of character. The personal consequences of work in the new capitalism* (New York and London 1998).

be of some avail. The more so as these topics are vigorously debated by them. This article in no way pretends to be exhaustive. Nor does its author pretend to be an expert in economics. I just want to shed some light on some problems involved in trying to integrate culture and institutions in studying a specific question in economic history: why was the Western world the first region in the world to have modern economic growth? I believe my remarks have a wider application than only this specific topic. In this article the following topics will be discussed: Culture and institutions in current economics and economic history; The role of culture, institutions and the state in explanations of 'the rise of the West'; The role of culture in explanations of the rise of the West: some methodological comments; Economics on the role of culture; Economics and institutions; Institutions and the explanation of "the rise of the West"; Institutional economics; Institutional economics, economic history and "the rise of the West"; An attempt to integrate culture, institutions and the state in economics. At the end of the article I will present some concluding remarks

Culture And Institutions In Current Economics And Economic History

It does not take much effort to show that culture and institutions are on the rise in economics and economic history. Economics has increasingly been plagued by unease with the so-called "mainstream approach" that many feel has turned into a kind of higher cryptology, with a sophistication in methods that is only matched by a lack of realism in presuppositions. An increasing number of critics is claiming that economists do not have the slightest idea what is going on in the real world, and that economics,

[5] F. Fukuyama, *Trust; The social virtues and the creation of prosperity* (New York and London 1995) p. 34: "…values and ideas shape concrete social relationships and vice

purportedly a social science, has nothing informative to say on that world.[6] With the bluntness that has become characteristic of current scholarly debates the end of economic man and of economics has been proclaimed and talk about a crisis of economics is rife. By paying more attention to culture and institutions one hopes to mitigate this crisis. So-called "institutional economics", in its old as well as in its new variety, has played a major role in this development. The best-known exponent of this approach undoubtedly is North, who won a Nobel prize for his work. But I could also refer to Coase, another winner of the Nobel prize, whose article on the nature of the firm already dates from 1937, and to Williamson. Two other people who spring to mind, as they, like North, have a very direct influence in economic history, are Chandler and the political scientist Olson.[7] Not surprisingly the primary focus of the work of all these authors has always

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versa."

[6] For the claim that something is fundamentally wrong with economics see, for example, G.P. Brockway, *The end of economic man* (New York and London; 3e edition 1995); E. Engelen, *De mythe van de markt. Waarheid en leugen in de economie* (Amsterdam 1995); R. Heilbroner and W. Milberg, *The crisis of vision in modern economic thought* (Cambridge 1995); T.W. Hutchinson, *Knowledge and ignorance in economics* (Oxford 1977); A. Klamer and D. Colander, *The making of an economist* (Boulder 1990) and P. Ormerod, *The death of economics* (London 1994).

[7] For introductory information on the new institutional economy see J.S. Cohen, "Institutions and economic analysis" in: Th.G. Rawski, ed., *Economics and the historian* (Berkeley 1996) pp. 60-84; J.N. Drobak and J.V.C. Nye, eds., *The frontiers of the new institutional economics* (San Diego and London 1997); B. Gustafsson, ed., *Power and economic institutions. Reinterpretations in economic history* (Aldershot and Brookfield 1991); Th. van de Klundert, *Groei en instituties. Over de oorzaken van economische ontwikkeling* (Tilburg 1997); J. Maloney, *What's new in economics?* (Manchester 1992); North, *Structure and change*; North, *Institutions, institutional change and economic performance*; M.C. Olson, *The logic of collective action* (Cambridge 1965); M.C. Olson, *The rise and decline of nations* (New Haven 1982); M.C. Olson and S. Kähkönen, eds., *A not-so-dismal science. A broader view of economies and societies* (Oxford 2000); W. Plumpe, "Gustav von Schmoller und der Institutionalismus. Zur Bedeutung der historischen Schule der Nationalökonomie fur die moderne Wirtschaftsgeschichtsschreibung", *Geschichte und Gesellschaft* 25 (1999) pp. 252-275; J.J. Vromen, *Economic evolution. An enquiry into the foundations of new institutional economics* (London and New York 1995) and Cl. Wischermann, "Der property-rights

been on the role of institutions in economic life, in the case of Olson primarily on the state. But they also have been instrumental in introducing culture into economics. That is especially the case with North, who increasingly stresses the significance of culture, or as he prefers to say "ideology."[8] But these scholars are part of a wider trend. Temin is right on target when he claims that in economics it has become kosher to talk about culture.[9] Concepts like "business culture", "corporate culture", "identity" or "synergy" have become stock in trade in discussions about modern economic life. Fields like economic anthropology or economic psychology have come into existence. In the Netherlands, one of the most corporatist countries in the world and the homeland of the "poldermodel," thinking about economics has always been heavily institutional and impregnated by cultural considerations. But matters have become even "worse": the Dutch economist who was cited most, by far, last year is Hofstede, famous for his publications on cultural differences and their impact on economic organization.[10]

This shift toward cultural and institutional explanations is even more blatant in general discussions on economic development. I just mention the debates on "Asian values," "Japan Incorporated", the economic order and policy of the Newly Industrialising Countries, the Anglo-Saxon model and the Rhineland model, or trust as a source of economic progress. Even a hard-nosed economist like Alan Greenspan maintains that capitalism is a matter

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Ansatz und die "neue" Wirtschaftsgeschichte", *Geschichte und Gesellschaft* 19 (1993) pp. 239-258.

[8] See North, *Structure and change* and *Institutions, institutional change, and economic performance*, in the index.

[9] P. Temin, "Is it kosher to talk about culture?", *The Journal of Economic History* 57 (1997) pp. 267-287. For that wider trend see the literature referred to in note 2.

[10] G. Hofstede, *Culture's consequences. International differences in work-related values* (Beverly Hills and London 1980) and G. Hofstede, *Cultures and organizations: software of the mind* (Maidenhead, Berkshire England 1991).

of culture, not of human nature.[11] The American scholar Lawrence Harrison has probably found the smallest nutshell when he simply states: “Underdevelopment is a state of mind”.[12] The most influential works in this field have not always been written by top professional economists. But then, how many professional economists nowadays write for a wider audience and play *any* role in public intellectual debate? Publications like those by Fukuyama, Putnam, Huntington, and, most recently, Harrison and Huntington, however, are widely read and extremely influential.[13] Mainstream classical economics is far from dead and one can also find scholars who, instead of turning to culture or institutions, think economics could profit from paying more attention to geography, ecology or demography.[14] The new approaches have not taken over the discipline, but they surely are making important inroads.

Undeniably economic history too is witnessing an increasing sensitivity to cultural and institutional matters. Expressions like “institution”, “transaction costs”, “property rights”, “interest group”, “logic of collective action”, “visible hand”, “human capital”, “social capital”, and “trust” pop up in almost every text in the field. The situation in the Netherlands is no exception to this rule, as shows in work of, for example, Davids, Noordegraaf, De Vries and Van der Woude, Van Zanden and Van Riel.[15] In this article references to

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[11] L.E. Harrison and S. P. Huntington, eds., *Culture matters: How values shape human progress* (New York 2000).
[12] L.E. Harrison, *Underdevelopment is a state of mind* (Cambridge Mass. 1985).
[13] Fukuyama, *Trust*; R. Putnam, with R. Leonardi and S.Y. Nanetti, *Making democracy work. Civic traditions in modern Italy* (Princeton 1993); S. Huntington, *The clash of civilisations and the remaking of world order* (New York 1996) and Harrison and Huntington, *Culture matters.*
[14] See for example P. Krugman, *Development, geography and economic theory* (Cambridge Mass. and London 1995) and J. Sachs, “Notes on a new sociology of economic development” in: Harrison and Huntington, *Culture matters*, pp. 29-43.
[15] C.A. Davids, *De macht der gewoonte? Economische ontwikkeling en institutionele context in Nederland op de lange termijn* (Amsterdam 1995); L. Noordegraaf, *Overmoed uit onbehagen. Positivisme en hermeneutiek in de economische en sociale geschiedenis*

economic history will be confined to literature addressing the question of what made “the West” grow rich, while “the rest” stayed so much poorer. In debates on this problem the role of culture and institutions has always been prominent, and it still is. Again, that does not mean they monopolise current explanations. Materialism still has its staunch defenders in scholars like Blaut, Frank and Snooks.[16] Explanations that emphasize geography and ecology are presented by, to name a few, Diamond, Pomeranz and Sanderson.[17] Demography plays a big role in the analysis of, for instance, Macfarlane and North and Thomas.[18]

The role of culture and institutions including the state in explanations of “the rise of the West”

As indicated, as an explanation for the rise of the West, culture has always been popular**.** Landes, in his book - of which, I am afraid, more copies were sold during the last two years than of all other books on economic history together - flatly claims that “the Weber thesis” is correct

(Amsterdam 1991); J. de Vries and A. van der Woude, *The first modern economy: success, failure and perseverance of the Dutch economy, 1500-1815* (Cambridge University Press 1997) and J.L. van Zanden and A. van Riel, *Nederland 1780-1914. Staat, instituties en economische ontwikkeling* (Uitgeverij Balans 2000).

[16] J.M. Blaut, *Eight eurocentric historians* (New York 2000); A.G. Frank, *ReOrient. Global economy in the Asian Age* (Berkeley 1998); G.D. Snooks, *The dynamic society. Exploring the sources of global change* (London and New York 1996); idem, *The laws of history* (London and New York 1998). In J.R. Goody, *The East in the West* (Cambridge 1996) and E.L.Jones, *Growth recurring. Economic change in world history* (Cambridge 1988) as well a more materialist approach is favoured, or in any case one in which not too much is made off culture.

[17] J. Diamond, *Guns, germs and steel. A short history of everybody for the last 13.000 years* (London 1998); K. Pomeranz, *The great divergence. China, Europe, and the making of the modern world* (Princeton 2000) and St.K. Sanderson, *Social transformations. A general theory of historical development* (Oxford and Cambridge 1995).

[18] A. Macfarlane, *The savage wars of peace. England, Japan and the Malthusian trap* (Oxford 1997) and D.C. North and R. Thomas, *The rise of the Western world. A new economic history* (Cambridge 1973).

and that culture makes all the difference.[19] Fukuyama refers to Weber approvingly on various occasions and has written an entire book on trust and social virtues in the creation of prosperity.[20] Sowell has already published three best-selling volumes in which cultural factors receive prime coverage when it comes to explaining prosperity.[21] A similar focus can be found in Fromkin's work.[22] Jay presented a series on BBC TV, now just appearing in print, which also focuses on culture and institutions as the explanation for the Western road to riches.[23] In France Peyrefitte wrote two books on economic development in which culture, or as he prefers to say "*mentalité"* appears as the major explanatory factor for Western prosperity.[24] The Indian economist Deepak Lal wrote a complex book on the impact of factor endowments, culture, and politics on long-run economic performance. And the list could go on. Apparently there is a wide range of cultural features that count as distinctively Western.[25] Again, maybe not all of these authors count as the *crème de la crème* of serious scholarship, but their works sell. And they are not alone: respected scholars like Goldstone, Hall, Jacob, Mann, and the late Gellner, are not loathe to enthusiastically voice their opinion that there is something special to Western culture that is good for Western economy.[26]

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[19] D.S. Landes, *The wealth and poverty of nations. Why some are so rich and some so poor* (New York 1998) 516.
[20] Fukuyama, *Trust*. I want to emphasise that Weber is much less of an idealist than most of his followers make him. See R. Collins, *Weberian sociological theory* (Cambridge 1986).
[21] Th. Sowell, *Race and culture; Migrations and cultures; Conquest and cultures* (New York 1994, 1996 and 1998).
[22] D. Fromkin, *The way of the world* (New York 1998).
[23] P. Jay, *Road to riches or The wealth of man* (London 2000).
[24] A. Peyrefitte, *Du miracle en économie. Leçons au Collège de France* (Paris 1995) and A. Peyrefitte, *La société de confiance. Essai sur les origines et la nature du développement* (Paris 1995).
[25] Deepak Lal, *Unintended consequences. The impact of factor endowments, culture, and politics on long-run economic performance* (MIT 1998).
[26] E. Gellner, *Plough, sword and book. The structure of human history* (Glasgow 1988); J.A. Goldstone, "Cultural orthodoxy, risk, and innovation: the divergence of East and West

Similar claims have been made for Western institutions. It will not come as a surprise that North claims that the rise of the West was caused by its more efficient economic institutions.[27] Notwithstanding their idiosyncrasies, he and Thomas can be included in the large group of scholars who believe that the rise of the West basically was the rise of capitalism, and who tend to identify this with the rise of "the market."[28] Overall capitalism can be defined by the presence of private property, private enterprise, commodification, the allocation of goods and services via a market, and a drive for capital accumulation. Some kind of political backing, obviously, is a necessary precondition for this mode of production, as it is for any other. In (early) modern capitalism that backing increasingly tended to be provided by the state that defined and protected property. As economists strongly influenced by neo-classical thinking, North and Thomas and a large group of kindred spirits tend to identify capitalism with a *specific kind* of market economy, to wit, one that is characterised by perfect and free competition and all that implies, like fully defined property rights, the presence of a large number of individual actors, market clearing and price-taking. Of course its markets were never operating perfectly and completely unhampered, but the West came closest, and in its rise ever closer to this ideal. This view is shared by many scholars in the field. Landes is only one

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in the early modern world", *Sociological Theory* 5 (1987) 119-135; J.A. Goldstone, *Revolution and rebellion in the early modern world* (Berkeley 1991); J.A. Hall, *Power & liberties. The causes and consequences of the rise of the West* (Oxford 1985); M.C. Jacob, *Scientific culture and the making of the industrial West* (New York and Oxford 1997) and M. Mann, *The sources of social power. Vol I. The history of power from the beginning to A.D. 1760* (Cambridge 1986).

[27] For North's claim that institutions explain the great divergence see his *Institutions, institutional change and economic performance,* 3-10 and *Rise of the Western world,* chapter *1.*

[28] North and Thomas, *Rise of the Western World*.

of the most recent and most outspoken among them.[29] On the other hand there are a lot of opponents to this identifying of the rise of the West with the rise of perfect and free competition. They too tend to blame or praise "capitalism" for Western economic supremacy and prosperity, but for them this capitalism is not tantamount to the 'ideal' market economy that is so dear to mainstream economists. One could think of scholars like Wallerstein, Braudel, Pomeranz, and various Marxist authors.[30] Widely differing as these interpretations of the political economy of the West may be, they all put heavy emphasis on the fact that *institutionally* the West was unique and that this was fundamental in its rise.

In line with the "Smithian" view of capitalism, there are authors who connect the rise of the West to the presence of free competition in all walks of life, not just in the sphere of economics. As Mann puts it, in the various Western countries that were heirs to the last European empire, that of the Romans, the sources of social power - political, ideological, economic, and military - were not monopolised.[31] This is supposed to have promoted a specific, Western dynamism and individualism, strengthened by a family structure in which already at the beginning of the early modern period nuclear families were the rule. In this perspective Western society was socially and geographically more mobile and open than other major societies

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[29] Landes, *Wealth and poverty*; Fromkin, *Way of the world*; Jay, *Road to riches*; E.L. Jones, *The European miracle. Environments, economies and geopolitics in the history of Europe and Asia* (second edition; Cambridge University Press 1987) and G*rowth recurring*; J.P. Powelson, *Centuries of economic endeavor. Parallel paths in Japan and Europe and their contrast with the third world* (University of Michigan Press 1994) and N. Rosenberg en L.E. Birdzell, *How the West grew rich: the economic transformation of the industrial world* (New York 1986).

[30] F.Braudel, *Civilisation matérielle, économie et capitalisme, XVe-XVIIIe siècle* (Paris 1979); Pomeranz, *Great divergence* and I.M. Wallerstein, *The modern world-system I. Capitalist agriculture and the origins of the European world economy in the sixteenth century* (New York 1974). For a classic marxist approach see for example the work of M. Dobb. His ideas are discussed in Gustafsson, *Power and economic institutions*, pp. 38-40.

[31] Mann, *Sources of social power*, pp. 22-33.

in the world. The diffusion of social power is also thought to have caused, and been caused by, the existence of a so-called “civil society”, another popular topic in discussing the uniqueness of the West. There society had countervailing power against government. Despotism *and* under-government were thereby ruled out, with all the beneficial effects that it is supposed to have had for development and growth. In such conditions, with a network of mutual arrangements and a government that was held in check, trust could arise, which could also enhance opportunities for growth.[32] It will be obvious that scholars who do not buy the story of the West as the home ground of perfect and free competition, will have their doubts about all this talk about mobility, dynamism and voluntary co-operation as well.

Discussing institutions inevitably leads to discussing the state, the super- and supra-institution in the Western world. Two features are mentioned in almost every analysis of the question to what extent it could have helped the West in acquiring its leading position. The first one is its *state system*, the second one the *nature of the individual states*. Again, overall, two lines of interpretation can be distinguished. One in which the Western state is regarded primarily as lean and clean and gravitating towards *laissez-faire*, and one in which emphasis is laid on its strength and its tendency to interfere in the economy. So we are confronted with literature in which “weak” governments and “strong” governments, *laissez-faire* and mercantilism, fight for prominence in explaining the rise of the West.[33]

These few examples more than suffice to show that references to culture and institutions abound in analyses that try to explain the economic phenomenon called the rise of the West. They also suffice to show that these references are anything but unproblematic. A closer look is needed at

[32] P.H.H. Vries, “Governing growth: a comparative analysis of the role of the state in the rise of the West”,*Journal of World History* 13 (2002) 67-138

what is meant by culture and institutions and how they are supposed to influence the economy. In trying to answer the last question we obviously will take a look at economics to see whether this discipline can be of any help to historians.

The role of culture in explanations of "the rise of the West": methodological comments

Culture has become a buzzword among social scientists and historians. It is not that long ago that it was still rejected as a notoriously vague category that serious scholars had better avoid. I will not bother to try and answer the question - that is unanswerable anyhow - what culture *really* is and just start from the definitions I encountered in the literature. Landes, who makes extremely far-reaching claims for the role of culture in economic history in saying that it makes all the difference, puts surprisingly little effort into defining it. To him in the end it amounts to "the inner values and attitudes that guide a population."[34] Huntington, who together with Harrison wrote a manifesto *Culture matters: how values shape human progress,* describes culture as "values, attitudes, beliefs, and underlying assumptions prevalent among people in a society."[35] Fukuyama defines it as "inherited ethical habit."[36] North seems to prefer the expression "ideology", by which he means "the subjective perceptions (models, theories) all people possess to explain the world around them."[37] Olson distinguishes between two kinds of culture: marketable human capital or personal culture, and public-good

[33] See for an analysis of both these points of view, ibidem.
[34] Landes, *Wealth and poverty*, 516.
[35] Huntington in Harrison and Huntington, *Culture matters*, XV.
[36] Fukuyama, *Trust*, 34.
[37] North, *Institutions, institutional change and economic performance*, 23.

human capital, that is knowledge about what public policy should be.[38] For the sake of convenience and to exclude no interpretation that I have come across, I opted for an extremely broad definition, to wit the socially acquired set of dispositions of a group of people with regard to describing, interpreting and valuing the social and natural world.

Those who fear that introducing culture into debates on economic development is a sure recipe for vagueness can find ample confirmation in texts that deal with the emergence of modern economic growth in the West. Unclear interpretations of the concept abound. Its precise meaning is often left unspecified, distinctions according to place and time are often lacking. Authors do not hesitate – as Huntington does for the contemporary world[39] - to call civilisations "Christian", "Confucianist" or "Muslim", and then take this to have extremely far- reaching consequences for their economic performance. It would have been very surprising indeed if no author would have tried to see some connection between Christianity and the specific economic feats of the Western, Christian world. And indeed many did. Some to emphasise that in the Christian conception the world is regarded as something that may be used and changed. Others to emphasise it functioned as a basis for trust among co-religionists.[40] That Protestantism, and especially Calvinism, has been credited with special effects in the realm of the economy needs no further comment. Neither does the *topos* that Confucianism in China, Islam in the Muslim world, and Hinduism in India,

[38] M.C. Olson, "Big bills left on the sidewalk: why some nations are rich and others poor" in: Olson and Kähkönen, *A not-so-dismal science*, pp. 37-60, p 52.
[39] Huntington, C*lash of civilisations*.
[40] See for Christianity as a provider of, among other things, trust Hall, *Power and liberties* and Mann, *Sources of social power.* For its supposedly different attitude towards nature see Landes, *Wealth and poverty,* pp. 58-59. For a fierce critic of the idea that Christianity would in any way have been conducive to economic growth, see D. Cosandey, *Le secret de l'Occident. Du miracle passé au marasme présent* (Paris 1997) pp. 23-32.

were bad things from an economic point of view.[41] As Japan industrialised relatively early, its culture almost had to be a kind of exception to the Asian rule, and indeed positive interpretations of it are not lacking.[42]

Fortunately, I am tempted to say, reference to culture does not always hover at so lofty heights. Going through the literature one can collect a whole list of more specific and concrete cultural traits that are supposed to have played a leading role in creating economic growth in the West. To begin with those features that are summarised under the concept of a (good) work ethic: frugality and industriousness, thrift, tenacity, patience.[43] Then there is of course “rationality”, a word with a very wide meaning. For Weber, in whose work it is a central concept and whose work has been immensely influential - and for mainstream economists! – it means thinking in terms of the methodical, calculable and the predictable.[44] Its highest materialisation in early modern Europe appears to have been double-entry bookkeeping, but it was expressed in an overall inclination to “measure” reality.[45] The meaning of the word “rationality” often, I think incorrectly, tends to be widened to comprise the whole gamut of characteristics expected of an entrepreneur. Here Schumpeter’s characterisation of the entrepreneur, especially in capitalism, as the creative destructor comes to mind.[46] It then also encloses “risk taking” and a feel for innovation. Jay claims that “risk” is a Western word and that Western society was a society of risk-taking entrepreneurs.[47]

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[41] I only refer to Landes, *Wealth and poverty,* the chapters on the history of China and the Muslim world, and his remarks on India and the Weber-thesis.
[42] *Ibidem*, chapter 22 on Japan’s industrialisation.
[43] See for example Landes, *Wealth and poverty,* chapter 29 and M. Egnal, *Divergent paths: how culture and institutions have shaped North American economic growth* (Oxford 1996) “Preface” and “A concluding note.”
[44] Collins, *Weberian sociology*, chapter 2.
[45] A.W. Crosby, *The measure of reality. Quantification and Western society, 1250-1600* (New York 1997).
[46] J.A. Schumpeter, *Capitalism, socialism and democracy* (New York 1942).
[47] Jay, *Road to riches,* TV broadcast.

There are, however, other scholars who think that it was risk-avoidance and manipulation of the economy that laid the ground for Western wealth.[48] Other traits I have come across - all smacking heavily of the American way of life - are competitiveness and individualism, acceptance of success and consumption, a positive attitude toward change, dynamism and mobility. To end this list that has no pretence of being exhaustive but just hopes to present the most important items, I want to mention trust and confidence, cultural capital, literacy and scientific culture.[49]

The big "civilisational" concepts, exemplified *par excellence* in religions or belief-systems, also reflect *par excellence* the vagueness that cultural interpretations are accused of. They are (too) large, diffuse, under-specified. When it comes to categories like Christianity, Protestantism, Calvinism, Hinduism, Confucianism et cetera, the question simply cannot be suppressed what exactly it is that makes them assets, or liabilities, for an economy. How exactly to connect lofty things like religious beliefs to such prosaic matters like production? Not surprisingly opinions differ widely on how to interpret the putative connections and to show that they really exist. Interpretations of the supposed effects of Christianity on economic development vary immensely, from those who think it was one of the most important assets of the West, to those who see no connection at all, to those who think the effects were much more often negative than positive.[50] Opinions are not so extremely diverse when it comes to the debate on

[48] See for this thesis for example the way Braudel defines capitalism in his *Civilisation matérielle* and Pomeranz, *Great divergence,* chapter 4.

[49] For literature on the rise of the West, apart from that mentioned in this article, see P.H.H. Vries, "The rise of the West in economisch perspectief ", *Theoretische Geschiedenis* 25 (1998) 291-321 and idem, "Recente en toekomstige pogingen the rise of the West te verklaren", NEHA Bulletin 15 (2001) 18-34. The shortest overview of the role that culture is supposed to have played in the rise of the West is provided by the reviews of Blaut in his *Eight eurocentric historians*.

Calvinism and capitalism, but here too scholars are torn on the question of the connection – if any - and its exact nature, as the immense literature on the Weber-thesis proves. The same applies to the relationship between Confucianism and economy.[51]

This is not the place to solve these riddles. What is clear, however, is that in this context the easy macro descriptions should at least be disaggregated and transformed into manageable categories that can be defined in an empirically meaningful sense. Cultures are very diffuse and comprise various sub-cultures. They change and interact with what is going on in the world. Much more attention should be paid to looking for good, empirical indicators. What should concern us here are their implications for practical life, not their spiritual principles. This not only applies to religion but also to the many references to Western rationality and the scientific inclinations of the Westerner.

Giving an operational definition of the small "traits" at first sight might seem to be easier. Although on second thought appearances may be very deceptive. How do you determine empirically that one culture has a better work ethic than another one? How do you measure thrift on a society-wide scale, or mobility? Fundamental categories like trust are also hard to pin down precisely. Where measuring is so extremely difficult, it is not clear how authors can be so adamant in their claims that the West had so much of these good things that it, and not any other advanced region in the world, would be the first one with modern economic growth. Especially as so little systematic comparative research has been undertaken.[52]

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[50] In case anybody would want to know, I think the last group has history on its side. See note 40.

[51] I only refer to Harrison and Huntington, *Culture matters* chapters 16 to 20.

[52] One can harbour serious doubts whether it will ever be possible for historians to conduct the kind of empirical research that is done by those who research contemporary relations

Moreover, it is far from obvious how the various traits that are supposed to have set the West on its specific trajectory, can be combined in one consistent story-line. I will restrict myself to just a few examples. How exactly to combine the thesis that the virtues of the bookkeeping *petit bourgeois* (being frugal and industrious, thinking in terms of the calculable and the predictable, avoiding risks) are conducive to economic growth, with the thesis that it is *entrepreneurial* virtues (like a willingness to take risks, deal with uncertainty and look for innovation) that have this effect? The bookkeeper can easily become the enemy *par excellence* of the entrepreneur, although Sombart thought they both were part of the history of *Der Bourgeois.*[53] Taking risks and venturing into the unknown can be very *sensible* in that this is the only way to keep abreast in a competitive environment. Personally, however, I would not call it *rational.* You simply cannot calculate and predict that what you are about to do is the right thing to do. Risk, according to the prevailing definition, might be measured, in the sense that ideally one could insure oneself to make it less risky, but uncertainty cannot, and innovating is by definition uncertain.[54] To give but one, final, example of conflicting interpretations: traits like competitiveness, individualism, mobility and dynamism, are not always easy to combine with trust and confidence. Institutional economists have not by accident focused on the question how co-operation of economic actors can be accomplished

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between economics and culture. See for example Klump, “Wirtschaftskultur” and Kunz, “Kulturelle Variablen.”

[53] W. Sombart, *Der Bourgeois: zur Geistesgeschichte des modernen Wirtschaftsmenschen* (München 1913). Compare the remarks in R. Grassby, *The idea of capitalism before the industrial revolution* (Lanham and Oxford 1999) pp. 47-59.

[54] For the “irrationality” of risk taking and especially of acting in a context of uncertainty see R. Brenner, *History. The human gamble* (Chicago and London 1983) and Goldstone, “Cultural orthodoxy, risk, and innovation.” For the current definition of risk and uncertainty see also H. Pellikaan and W. Hout, eds, *Economische modellen en politieke besluitvorming. Inleiding in de rationele–keuzetheorie* (Bussum 1998) pp. 56-60.

where it might, at least in the short run, often be more rational to be a free rider.

These (apparent?) inconsistencies form an additional, but forceful reason to try and figure out the exact mechanisms that are supposed to make all these cultural traits into explanatory variables in a story about economic growth. Many of them tend to be regarded as good because they are considered good from a *moral* point of view – somehow we like people to work hard, to save, to be individualistic, et cetera - and we tend to think that behaviour of that kind ought to be rewarded. But that does not necessarily mean that these private, moral virtues would be public, *economic* virtues too. Individuals usually work for personal net income, however defined, not for gross national product. Normally they do not really bother about GNP. If they do, that, by the way, might be a very forceful cultural factor in explaining why some countries have had such high growth rates.[55] Activities that are economically rational from a personal point of view and increase or even maximise a private income, *can* be socially inefficient. Smith's optimistic interpretation of the working of the invisible hand is simplistically over-optimistic, even in the best of all markets. Individual behaviour can very well be rational from the perspective of personal self-interest but irrational from the perspective of economic development.[56]

It does not take an awful lot of imagination or technical economic schooling to think of situations in which one or more of the character traits mentioned above indeed might foster economic growth. But, and that is the problem, it does not take much imagination either to think of circumstances in which they would *not*. Hard work can delay mechanisation and economic

[55] One might think for example of Japan's industrialisation, the German "Wirtschaftswunder" after World War Two, and the economic recovery of the Netherlands during that same era.
[56] Maloney, *What's new in economics,* p. 104.

innovation. It can, by the way, become irrational, as Weber already knew. There is nothing rational, in an economic sense, for people who have accumulated more than they can ever spend, to continue working. Any entrepreneur faces the problem that he can never maximise profit and utility both at the same time. But, why does Bill Gates continue working? His time *must* be scarcer than his money. What we call thrift today may be under-consumption tomorrow. Becoming a Mafioso definitely is a risky enterprise, but would Schumpeter endorse it? Being rational and calculating can be a brake on innovation. Individualism and a thoroughly rational approach can lead to a lack of trust or co-operation. National economic mobilisation can create growth, but it can also create havoc, for example when it turns into fierce nationalism and war.

What could be more rational when one is confronted with predicaments like these than to turn to economics? Might one not expect that this most prestigious of all social sciences could help us and tell what cultural traits are beneficial to growth, and in what circumstances? After all explaining economic growth ought to be its major field of interest.

Economics on the role of culture

Economics as a discipline has never been noted for its interest in culture and anyone who has ever leafed through economics textbooks can confirm that almost all the concepts we have just referred to, are completely lacking there. In a way, however, the popular critique that economics neglects culture is completely beside the point: the whole field of economics is “subjective”. It is entirely about choosing on the basis of the preferences you have and the restraints you see. “Value”, its central concept, is not an objective category but a subjective one, just like “commodity”, “labour” and

“labour force”, “money” et cetera.[57] According to mainstream economics the value of a good or service, from the consumer’s point of view, is the extent to which it satisfies a want. We then speak of utility. From the producer’s point of view the value of a good would be the extent to which it generates profit. The wants of consumer and producer themselves are regarded as data: to the economist they are as they are. The *primum movens* in economics, the *reason* people want to acquire goods or produce them in the first place, is outside economics. The much-discussed rationality of the *homo economicus,* and of the economist, normally only considers the ordering of the means, not of the ends. In the range of preferences there must be some order. If not, you cannot say anything systematic about them. Mainstream economists take that order to be rational, which implies, in the “thin” meaning of the word, that it is complete and transitive, and in the “thick” meaning, that the preferences are also ordered according to effectiveness and efficiency. The goal of this ordering is maximalisation. The consumer is supposed to be a maximiser of his utility, which of course depends on what *his* preferences are. With the producer things are less complicated. He is supposed to be a profit maximiser, which means that, in principle, it can be *objectively* verified whether this goal has been reached. So he can even be rational in the thick meaning of the word. Economists start from the premise that any rational person would want to maximise utility and profit. Which implies that consumers and producers know - or at least act as if they knew - what they want and how much they want it as compared to something else. Notice that this concept of rationality is adaptive, being rational is making the best of the situation as it is and in principle being able to do that unequivocally.

[57] For the subjective nature of economic facts see, for example, F.A. Hayek, *The counter-revolution of science. Studies on the use and abuse of reason* (New York 1952) chapter 3.

Differentiating between thin and thick rationality, is talking about method. One can also differentiate between the different fields of reality to which rational-choice theory might be applied. Economists preferably discuss their *homo economicus,* busy with optimising his economic pleasures and minimising his economic pains, i.e. basically making a pecuniary cost-benefit analysis. One might of course go further and apply the principle of economic reasoning, with its thick or thin rationality and its pleasure-and-pain principle, to a much wider range of subjects. Considering, for example, how far one may get in analysing marriage *as if* it were a rational choice, and in that sense an economic activity. Think of the work of Becker and others who promote the economic approach to human behaviour more in general. But even in these types of approaches culture, although fundamental, still is external: a set of given, stable preferences. Economics does not bother why culture is as it is. It focuses on looking at the world from the vantage point of describing, explaining, and predicting rational choices made in a given setting.[58]

In principle there is nothing wrong with such a formalistic approach that postulates utility and profit maximising. The proof of the pudding should be in the eating. If not, then economics is not an empirical science. That point of view might be defended, but in the end I personally doubt whether that would be very fruitful. Well then, how fruitful are this set of premises and the models built on it in confronting the reality of economic history? Let us begin our short evaluation with the individual decision-maker, the atom of economic analysis. In the real world producers often, for one reason or another, do not want to be maximisers but prefer to be satisfiers, or, to think

[58] G.S. Becker, *The economic approach to human behavior* (Chicago 1976). My analysis of rational-choice in mainstream economics is inspired by Engelen, *Mythe van de markt,* passim and Pellikaan and Hout*, Economische modellen en politieke besluitvorming*, chapters 1, 2 and 3.

in terms of a target-income, market share or continuity. Neoclassical economists, rightly, often react to such objections that in a situation of competition you will be forced to be rational, otherwise you will be wiped out. That may very well be true, *in a situation of fierce competition*. These, however, are anything but universal. Consumers in their turn may not always make the best choices, but then, neo-classical economists will suggest, they will have to pay dearly for their irrationality. Again that may very well be true. But historians know that not everybody in the past – or in the present – seems to mind.

But let us suppose an economic agent *wants* to be rational, *could* he? Even in the best of all worlds being rational is a hell of a job. Economists admit that in real life, rationality very often is beyond the grasp of decision-makers who nevertheless have to make some decision. There is a wide range of possible reasons for that. I just mention having too much or too little relevant information, lacking time and/or resources to make all the necessary calculations, and operating in a situation of risk or uncertainty. In practice this means that economists know that individuals are hardly ever rational in the formal, thick, cost-benefit sense, even in the so-called modern, calculating times we are now living in. Suggesting that whatever people have chosen, reveals their preferences, and is therefore “rational,” deprives the concept of all meaning. The rationality of the individual actor is not only “bounded” by his personal abilities or proclivities. Making rational choices also implies being in the position to be able to strictly compare and order options and having any options. It implies comparability or preferably calculability, freedom to act and the availability of alternatives. It is hard to be systematically rational and, for example, produce efficiently, when the environment is constantly changing, when there is no yardstick to compare

the things you want, when you are not allowed to choose, or when there simply is nothing to choose, only one pub in the entire town.

In mainstream economics your window of opportunities simply is a function of your budget. In reality it is conditioned by the entire context in which you live. The choices people make, whether we consider them rational or not, economic or not, never are individual choices made in a vacuum. They are made in societies with a certain culture, certain institutions and a specific history. In real life these play a fundamental role in every decision-making process. That does not necessarily make them irrational. On the contrary, it can very well make them rational in the context of a set of overall preferences. In every society the economic is "embedded" in culture, even in capitalist society where the economic is said to have been more detached from society than in any other type of society. Even now there are many cultural reasons for not allowing activities that would be profitable or satisfy wants. Even now there are values that overrule the economic. As we see for example in laws against dealing in drugs and weapons, or against child labour. Culture as a shared set of dispositions focuses the perceptions and preferences of people and thereby acts as a filter in the process of economic decision-making.[59] It cannot be excluded from economic analysis.

The mainstream economist could of course say, well that is all very fine but that does not change the fundamental premise that in the short term culture is a datum, something the economist finds embodied in the preferences of his producers and consumers but need not research as such. Apart from the fact that the economist sticking to this point of view would not understand much of what happens to his/her endogenous variables, the historian or anybody interested in reality could then reply that in the longer

[59] Fukyama, *Trust*, 34 and North, *Structure and change,* p. 49, where ideology is called "an economizing device."

term culture definitely is not a datum. Preferences change. An economic historian cannot ignore this and the reasons for it. If changes in preference were always caused by changes in the economy, i.e. if they could be seen as *endogenous*, the economist would still have the possibility to completely do his/her own thing. There would be no necessity to go outside economics. But that is not the case. Changes of preferences not only are most of the time unexplained in economics, most of the time they are inexplicable in economic terms. Culture is the context in which you can be rational. It is not in itself rational or irrational, but a-rational: the glass through which you can look rationally or irrationally but that in itself is neither. One could claim that "In such an environment one could maximally satisfy certain needs", but that doesn't make that environment or these needs rational.

All these comments must not be interpreted as suggesting that a rational-choice approach, whether it proceeds along thick or thin lines, would be useless and not informative. Far from, it only has to be applied in a sensible way. As a point of departure the presupposition of rationality is far more plausible than the presupposition of irrationality. Looking at economic decision-making as a process of rational choice under constraints, to me still is by far the most fruitful approach, not only in economics but in every sector of life where people try to reach a specific goal and apply a specific strategy.[60] Besides, we are dealing with a model here. That it has been turned into a sterile dogma is not its fault. I have always been in favour of a research strategy that tries to find the logic in what people are doing. That implies trying to find out a) what they themselves think they are doing b) why they are doing it - i.e. what their *reasons* and the *causes* behind these reasons are - and c) what *the effects* are of their acting as they did, in the

short as well as in the long term, intentionally and unintentionally.[61] This requires having a thorough knowledge of the context in which people are operating and the ways in which they think. Only then can one see what *they* might regard as rational. This suggests that even if there might be some truth in the claim of some scholars that the fundamental concepts of economics and its rational-choice approach are universal, there is even more truth in the assertion that it is does not make much sense to use them without any specification of time and context. In different contexts the meaning or impact of rationality, value, preference, goods, services, labour et cetera can be so different that they become empty categories that must be filled in with "local knowledge."[62]

What has been discussed so far, basically, is a set of premises of mainstream, (neo-) classical economics. As institutional economics plays a prominent role in this article because of its increasing popularity in economics and economic history, some specific comments on it are in order. I will confine myself to North, as he is the institutionalist who, as far as I know, has most clearly pronounced himself on the role of culture in macroeconomics, although, as indicated, he would rather speak of "ideology" than of "culture**."** He regards culture as the informal base of institutions, and thinks it is more fundamental than institutions and more difficult to change. Although he started from a neo-classical position, he feels increasingly uneasy about its strict rationality-postulate and expects to be

[60] I can completely agree with the stance taken in D.N. McCloskey, "The economics of choice: neoclassical supply and demand" in: Rawski, *Economics and the historian*, 122-158.
[61] See for this approach R. Boudon, *Theories of social change* (Cambridge 1991) and J. Elster, *Explaining technical change* (Cambridge 1983) chapter 3.
[62] See for example Engelen, *Mythe van de markt*, p. 83, and Heilbroner and Milberg, *Crisis of vision*, pp. 110-111.

able to learn a lot about how people really think from cognitive science.[63] It is only to be welcomed when an economist thinks that culture is so important in economics that this discipline needs “a theory of ideology” and that human thinking and decision-making should be analysed much further. But that theory still is, as North himself admits, wishful thinking. And, I think, it will always be. What gains exactly one might expect for studies of macro-economic development from explorations into cognitive science is as yet unclear. Suppose for the sake of argument that “a theory of ideology” would ever emerge, and that cognitive science would bring new insights, would it then be possible to integrate this into economics in such a way that for economists culture would become an endogenous factor, i.e. that economic variables could explain cultural variables? Maybe in some cases and some contexts, but overall I do not believe for a moment that this might work, and in any case North, nor anybody else, has yet shown it to work. The less culture can be deduced from economic data, the more it will continue to be an exogenous factor in economic theory and the more the economist, and the economic historian, will have to depend on knowledge of the extra-economic.

Taking culture into consideration definitely enriches economics, but it doesn’t make culture part of economics. Economists do not have any privileged knowledge *as economists* about how and why a specific culture comes into existence. The reasons for having a specific culture – to put it somewhat deceptive, as it suggests you rationally choose your culture - are not necessarily and not even primarily economic. Economic developments can of course have a big impact on culture, as for example the current process of globalisation shows. But we simply do not know when they do

[63] North, “Prologue” in: Drobak and Nye, *Frontiers of new institutional economics*; idem *Structure and change* and *Institutions, institutional change and economic performance*.

and when they don't, or how exactly the connection will work out. It is not inconceivable that economists, of whatever variety, might tell us what type of culture would be conducive to economic growth or indicate what could bring about such a culture.[64] In their line of reasoning in the end that would have to be a culture that values economic rationality in the two widely differing meanings of the term we used here, that is being efficient and being innovative. That is – to end our long detour in search for help in economics - all that mainstream economists and institutionalists can teach historians about culture and economic growth. Both "rationalities" are important in economic life. How to bring about the first type of rationality, at least in principle, is not very mysterious. But Schumpeter definitely was right when he claimed that in capitalism growth is created by a gale of perennial, creative destruction, i.e. by constant innovation. Before capitalism this gale may have been only a soft breeze but still: in any competitive environment producers always have had to be on the alert and willing to innovate, that is, go *beyond* known constraints and so to say create their own environment. Economics has not (yet?) produced a theory of economic macro-inventions. What we have is a set of empirical generalisations at best.[65] Whatever else may be needed for an economically efficient and innovative culture to emerge and exist, it will never thrive without an adequate institutional context. Let us therefore turn to the place of institutions in economic life, economic history and economics.

[64] See, for example, Harrison and Huntington, *Culture matters*, chapters 20-22.

[65] J. Mokyr, *The lever of riches. Technological creativity and economic progress* (New York and Oxford 1990); G. Clark, "Economic growth in history and theory", *Theory and Society* 22 (1993) pp. 871-886 and J. Mokyr, Innovation and its enemies: the economic and political roots of technological inertia" in: Olson and Kähkönen, *A not-so-dismal science*, pp. 61-91.

Economics and institutions

Economic choices are always embedded in a cultural and institutional setting, just like they on the other hand exert their influence on them. Taking this into consideration is what makes these choices rational *in real life*. We have commented upon culture as a factor in individual economic behaviour and seen how fundamentally it conditions this behaviour. Culture, however, only becomes influential on a macro level and in a structural way, and more easily to pinpoint in its effects, when it "solidifies" in institutions. The culture of an individual or even a group does not matter very much in general economic history when it is not braced by some kind of institution. But then, institutional economists stress, it can become extremely important. It creates a new set of constraining and enabling factors, next to the "ordinary" economic data like technology or factor endowments. What then can historians discussing the role of institutions, in general or with regard to the rise of the West in particular, learn from economics?

If the frequency with which the word "institution" is used in recent economic publications is something to go by, it has become even more of a buzzword than culture. It is even claimed that there is a whole branch of the discipline that goes by the name "new institutional economics", where the "new" is meant to indicate that there always has been a branch of economics where institutions were deemed important.[66] It appears to be not really a separate branch of economics, but rather a particular set of concerns. It generally focuses on transaction costs and property rights, /political economy and public choice/ quantitative economic history (usually in institutional micro-economic context)/ cognition, ideology and the role of path-dependency.[67] Be that as it may be, one might expect it would not be

[66] See for example Gustavsson, *Power and economic institutions*, "Introduction."
[67] Drobak and Nye, "Introduction" in: iidem, *Frontiers of new institutional economics.*

hard to find a definition of this new key concept and a small synthesis of the main findings of this type of economics.

North's work would be the obvious place to look for such a definition. He defines institutions in terms of formal rules (laws, constitutions, rules), informal constraints (conventions, codes of conduct, norms of behaviour) and the effectiveness of their enforcement, all of them instrumental in structuring economic life. In this definition he distinguishes between the rules of the game and the players, i.e. organizations. Enforcement of the rules is carried out by third parties (law enforcement, social ostracism), second parties (retaliation) or the first party (self-imposed codes of conduct).[68] Other scholars include the players and regard them too or even primarily as institutions. From this point of view it is only logical to also include the state, the super- and supra-institution that, even in "minimalistic" interpretations of its tasks, functions as arena of collective action, where government provides infrastructure, formulates the rules and acts as referee when it comes to applying them. Davids presents an even more encompassing definition. To him the concept "institution" stands for the structures that in the course of time develop in economic interaction between individuals. They are the power of custom.[69] In this article I will, for the sake of convenience, use a very broad definition that encloses all the features mentioned in this paragraph.[70]

The importance of culture for institutions thus defined, is evident. Culture, i.e. in any case somebody's culture, is at the basis of institutions. Formal rules, informal constraints and enforcing agencies: they all refer to peoples' conception of how things ought to be done. They are expressions,

[68] North, "Prologue."
[69] Davids, *Macht der gewoonte*.

or in any case results, of how people see themselves, other people and the world. Organizations, including governments, are interest groups. So what they do is heavily influenced by the interests they have chosen to defend. Which is often related to culture and, by the way, hardly ever focused on increasing GNP in the long run. This does not mean one can simply deduce institutions from individual reasons and choices. They clearly have a status, dynamics, and logic of their own. The same applies to organizations. But it would be silly to deny that these are heavily intertwined with culture. Every economic order – as well as every political order - *implies* a cultural order.

Institutions and the explanation of "the rise of the West"

Economic history from the very beginning has always paid attention to institutions. Before the cliometric revolution, it was, if anything, more institutional than economic. It primarily was economic history with economic theory left out. With the New Economic History it was just the other way around. It by and large was economic history (in a neo-classical mould) with history (including culture and institutions) left out. One would expect the new institutional economics to be very informative for historians who constantly refer to institutions in their explanation of economic phenomena.

In debates on the rise of the West we constantly come across references to institutions, as we already pointed out. It is, for example, claimed that in the West markets were more competitive and/ or free than elsewhere, that property rights were better protected, transaction costs lower. To mention only those institutional traits one might think are fairly easily measurable. Surprisingly a good operational definition of the variables

[70] For various contemporaneous authors and their definitions, apart from those already mentioned, see Cohen, "Institutions and economic analysis"; Van de Klundert, *Groei en*

in case and a systematic measurement of them, are mostly lacking, even for such a fundamentally quantitative factor as transaction costs. Where measurement is so difficult, it is very daring or simply imprudent to state that “the West” had more of an advantageous institution than “the rest.” I will not dwell on this but just make one comment with regard to the work of North, who makes very wide-ranging claims with regard to the role of institutions in Western economic hegemony: he does so without making *any* systematic comparison whatsoever with regions outside Western Europe or beyond the period between 900 and 1700, not in his 1973 book, which is hardly surprising, but neither in any of his later publications. The hypothesis *that* institutions matter, can best be illustrated by comparisons.[71] The question *how* exactly they matter, of course then still has to be settled.

The huge problems involved in defining and “measuring” institutions will surely not be innocent to the fact that there are such immense differences between various interpretations of the political economy of the West and its relation to western economical supremacy. Nowhere this is more evident than in the way in which capitalism and its role in the rise of the West are interpreted. Almost all the big narratives on how the West became economically different are spun around a concept of capitalism as an institutional framework. But that’s about where agreement ends. There is an old and still dominant, tradition of seeing the rise of the West as a process of emancipation towards perfect and free markets. It is the emergence of fair competition between all economic agents involved with as little interference from outside forces as possible that is supposed to have done the trick. In the West the state and pressure groups presumably interfered less with the market than they did elsewhere and so helped, willingly or unwillingly, in

instituties “Inleiding”, and Van Zanden and Van Riel, *Nederland 1780-1914*, “Inleiding.”
[71] See for a fine example Olson, “Big bills.”

making it more efficient. Overall there is a tendency to very easily identify unfettered competition between individuals, firms, and states, with growth.[72] But as already indicated, there is also an impressive array of scholars who, I think with more good reason, claim that as a description of what actually happened in the West, this is simply not true. To them, distortion of the market and interference, have always been the normal state of affairs, even when capitalism was at its height. Wallerstein's modern world-system may be capitalist according to him, but it definitely would not be to Adam Smith and his followers.[73] Braudel goes as far as to characterise his Western capitalism as "the anti-market."[74] Pomeranz in his book on the great diverging of the economies of Europe and China, asserts that imperfect competition, coercion and collusion were far more characteristic of the economy of early modern Western Europe than full competition and *laissez-faire,* and even contends that in the Smithian sense of the word China was more capitalist than Europe.[75] In short, in these and kindred interpretations, Western economies have never even come close to the ideal of free and perfect competition and, what is more, that apparently hasn't been a handicap. Monopolistic and oligopolistic competition much more than perfect competition, mercantilism much more than *laissez-faire,* characterized early modern Europe and prepared its *démarrage*. That applies even to the nineteenth century. Surprisingly enough when it comes to the role of constant competition between Western nations, almost *all* scholars tend to agree. It is regarded as conducive to economic growth. The immense disadvantages of this competition in terms of war, protectionism, increases

[72] In this context it is striking that Landes in his *Wealth and poverty* is not in favour of free trade. See index under "comparative advantage."
[73] Wallerstein, *Modern world-system,* see the index under "capitalism."
[74] Braudel, *Civilisation matérielle*, I, p. 8, and II, p. 9 and pp. 196-197.
[75] Pomeranz, *Great divergence,* chapter 2.

in transaction cost et cetera, apparently are regarded as more than compensated for by the advantages.

This tension between an emphasis on competition and non-interference on the one hand, and on protection and interference on the other hand, is repeated in discussions on the mobility and openness of Western society. The view that Western development is directly linked to the status of Western society as a mobile and open society, the most popular one, competes with the view that this must be taken with a heavy grain of salt or even denied. Braudel is an explicit supporter of the latter interpretation. To him Western society wasn't more mobile and open than let's say China or the Ottoman Empire. There, at least in principle, a much more meritocratic structure existed, with less aristocracy and more careers open to talent. Capitalism as he sees it, could develop because capitalists, as he defines them, were protected by the political elite and had the possibility to quietly accumulate.[76] There is a related difference of opinion when it comes to the effects of having a thriving civil society. In most of the stories on the rise of the West such a society, which is considered to be a high-trust society, figures prominently as a "good thing." But dissenting voices claimed, even before Olson had analysed the problem from a more theoretical point of view, that what in a positive vein can be described as "a thriving civil society," can easily derail into a society where pressure groups become vested interests and block innovation.[77] Even democracy need not necessarily be a good thing, at least not for economic innovation.[78] As

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[76] Braudel, "À propos des origines sociales du capitalisme" in: R. de. Ayala and P. Braudel, eds., *Les écrits de Fernand Braudel, II*, (Paris 1997) pp. 359-371.
[77] Mokyr, "Innovation and its enemies"; Olson, *Rise and decline of nations*; Olson, *Logic of collective action*; Kunz, "Kulturelle Variablen."
[78] See the previous note; R.J. Barro, *Determinants of economic growth* (Cambridge and London 1997) and E. Weede, *Economic development, social order and world politics* (London and Boulder 1996) passim, especially chapters 6 and 8.

indicated interpretations that stress individualism or mobility as typically Western do not always combine easily with interpretations that focus on trust.[79] Big differences of opinion when analysing what kind of state is conducive to growth have already been signalled. I would only want to add that scholars not only disagree about what kind of state promoted growth in the West, but also hold very different viewpoints on the role of the state in explaining why “the rest” didn’t rise. That, for example, is blamed by some on totalitarianism or oriental despotism, by others on under-government![80]

So we hear dissenting voices when it comes to institutions and their role in the rise of the West. The point is that the competition, non-interference and small-government narrative as well as the protection, interference and big-government narrative - and all their derivatives – *as such* can be construed in a plausible way. Although they can, of course, not both be *factually* true. Again one would expect economics as a discipline to be of help in getting out of this predicament. Scholars who present the rise of the West as based on the rise of “the market” and of *laissez-faire* can have ample recourse to economic theory to make their account plausible. They have mainstream economics at their side. Those who claim that in the rise of the West it was not perfect and free competition that was instrumental but its “opposites”, monopolistic and oligopolistic practices, collusion and coercion, and a large role for the state, face a more difficult task. But they too can find some support in economic theory. Think for example of Schumpeter and various Marxist scholars as Dobb.[81] This again induces us to delve

[79] See, for example, Weede, *Economic development*, pp. 12-13.
[80] For an overview see Vries, “Governing growth.”
[81] Schumpeter, *Capitalism, socialism and democracy*, and Th.K. McCraw, “Joseph A. Schumpeter. Capitalism, socialism, and democracy”, EH. NET Review, on eh.net-review@eh.net. For Dobb’s ideas see Gustafsson, *Power and economic institutions,* pp. 38-40.

somewhat deeper into economic theory, more specifically into institutional economics.

Institutional economics

The simple fact that a group of economists has emerged who are known as (new) “institutionalists,” suggests that mainstream economics was not institutional, or in any case not institutional enough. To a certain extent that simply isn’t true. Mainstream economics is institutional in its very essence. The point is that in the end it only acknowledges, and deals with, a very restricted and specific set of institutions. It only feels really at ease when discussing a fully competitive market that is left to its devices. Mainstream economists have always taken this as their point of departure. The more situations deviate from the model of perfect and free competition, the more *ad hoc* they operate**.** In the end, all adaptations and refinements notwithstanding, the only thing economic theory can systematically = deductively handle, is a system based on Smithian premises and tending towards equilibrium. But even such a “free-market system” cannot exist *in vacuo*. Its functioning presupposes a large set of institutional and cultural underpinnings. Without them competition and *laissez-faire* turn into chaos and anarchy. A market economy is something that has to be created and maintained and that people have to find worthwhile. It presupposes, and creates, a specific order. It is not the state of nature, nor is it a necessary, “logical” phase in history. In fact “the rise of the market” was an extremely complicated, hazardous and tortuous process. These comments also apply to non-fully competitive markets and to all kinds of systematic government interference; they too have to have a base in institutions and thereby in culture.

Simplifying enormously, one might say that neo-classical, mainstream economics departs from the following premises in its analysis of the working of the market: 1) the actors are – a large number of - individual agents 2) who act rationally, as *homines oeconomici* 3) in a setting of perfect competition where everyone is a prize-taker and where there are no returns to scale and 4) there is no extra-economic interference that thwarts or distorts the market, so that in the end it will always be cleared. Historians would be very hard-pressed to find an economy that comes sufficiently close to this model for it to be able to say anything non-trivial about that economy. Economists therefore simply have had to try and come to grips with institutions and situations that in the best of all classical worlds supposedly were non-existent. [82]

Economic reality has always had characteristics that deviate from textbook presuppositions and there is no reason to expect that a situation will ever arise where this would not be the case. Let us confine ourselves to capitalism as it really is. In the real, sublunar world there are innumerable mechanisms and visible hands that influence market forces. Simply ignoring them or simply regarding them as distortions or deviations, in the long run turns economic models into scholastic fairy tales. We already discussed the extent to which, in the real world, economic choices can be irrational. Premise number 1, the idea that economic actors are individuals or in any case monolithic decision-makers, also appears to be not very realistic. Not only are capitalist economies characterised by various complex economic organizations that do not figure in the analyses of classical economic thinking and can only with difficulty, if at all, be systematically integrated in its logic of rational individuals. We also come across entities like classes, ethnic groups, or states, that are even less suited to be fitted into the neo-

[82] Compare Gustafsson, *Power and economic institutions,* pp. 11-12.

classical paradigm. With the increase of scale and complexity of the economy, transactions become more complicated and forms of co-operation and co-ordination are called for, as well as informal and formal rulings. These are the things institutional economics focuses on, by and large trying to incorporate them in the neo-classical paradigm. Analysis becomes even more complicated by the fact that “non-perfect” and non-free competition is the rule rather than exception. All in all, *even* in capitalism and capitalist society, we see players, games and referees that are not included in the neo-classical, “ideal type” model. This puts the question of economic order on the agenda.

Apart from economic power - the ability to have things your way because of your economic resources - there is, in theory distinguishable, in practice often interacting - what one might call “political power.” Individuals, groups, organizations, the government, can all “disrupt” the working of the market in the hope of promoting interests or ideals. Their success depends, to a large extent, on their power. Again, this is the case in capitalist economies as well as in all other types of economy history as ever known. This puts the question of political power on the agenda.

Economic order and political power raise colossal problems for anyone wanting to analyse an economy according to the principles of mainstream economic analysis, even in the case of so-called capitalist societies. In other types of society, with other modes of production, these problems usually are even bigger. Not only because there the rational *homo economicus* is even more of a figment than he is in modern capitalism, but also because the institutional and cultural preconditions of mainstream economic analysis are (almost completely) lacking. It is with good reasons that various authors assert that pre-capitalist economies – as well as the economies of (former) communist countries – do not have an economy in

the modern economist's sense of the word, and cannot be studied at all according to the rules of modern economics.[83] The best studies of non-capitalist societies have been written with extremely little attention to ideas of mainstream economics, which does not imply that they cannot be to some extent based on models and on fundamental economic reasoning. Their authors just had to incorporate a completely different societal and cultural logic.[84]

Institutional economics, economic history and "the rise of the West"

Simplifying outrageously and with the bliss of ignorance one might say that institutional approaches are the most systematic effort of economics to engage the challenge presented by order and power. I am not the person, and this is not the place to provide an extensive and systematic analysis of institutional economics as such. I just confine myself to looking whether it can give historians a clue as to which institutions are conducive and which ones detrimental to development and growth and whether it can inform them about origin and function of economic institutions.

The big underlying debate in the study of the economic history of the West, when it comes to institutional preconditions for its economic growth, is whether perfect and free competition or rather non-perfect competition and interference, were characteristic for its political economy, and which of the two was fundamental in explaining its growth. The historian can only conclude that impressive economic growth has been created in situations

[83] See for example Heilbroner and Milberg, *Crisis of vision*, chapter 6.
[84] See for example M.I. Finley, *The ancient economy* (Berkeley 1999, updated and with a foreword by Ian Morris, originally London 1973); W. Kula, *An economic theory of the feudal system: towards a model of the Polish economy, 1500-1800* (London 1976, originally in Polish 1962) and J.L. van Zanden, *The rise and decline of Holland's economy: merchant capitalism and the labour market* (Manchester 1993).

where there was no perfect competition and a lot of interference. It is only natural for him to look for support in economics to decide which of the two explanatory schemes has better credentials. To put it bluntly, that will be of little avail.

When it comes to economic order, there simply is no theoretical model that can systematically compare advantages and disadvantages of both types of economic order – the neo-classical one with its perfect competition or the one characterised by imperfect competition - and pass some general judgment on their efficiency. Reading for example Van de Klundert's book on institutions and growth depressed me, the parts I understood as much as the parts I did not understand.[85] There simply is no such thing as an institutional theory of economic growth that could be of much use in explaining real economic growth as we have witnessed in history. It all depends on the circumstances. On what circumstances and how exactly, economists simply cannot tell us, in any case not better than does common sense. When it comes to political interference, the situation is no different. Everything from a complete *laissez-faire* (the best economic policy is no policy at all) to completely planning and regulating the economy (give the planners the tools and they will finish the job) has at one time or another by one economist or another been hailed as simply the best policy. The range of advices is a clear sign of ignorance.

If there is support for some points of view in these matters, it derives from simple empirical generalizations. When it comes to successful economic performance "well-defined property rights, limited but strong government, the rule of law, fairly open trade, stabile monetary regimes mobility of labour and capital, and a society congenial to invention and

[85] Van de Klundert, *Groei en instituties*.

innovation are all felt to be part of the equation."[86] The state must be efficient and effective and not over-ambitious, as must be its laws.[87] Democracy *to a certain extent* can help.[88] The point with most of these generalizations is that they are either extremely self-evident or tautological, if not both at the same time. It is like my father used to say: "if you don't want to get drunk you shouldn't drink too much." I am still groping for the "too."

Could economists then at least give some clues as to what causes specific institutions to arise and to function as they function? In other words, can economics endogenise institutions? As it cannot do this with culture, and culture is the substratum of institutions, there again is not much reason for optimism. But even little bits might help. To what extent do institutions come into existence and function according to economic efficiency rules, i.e. how far can they be explained in cost–benefit terms? Knowledge about their *causes* and *functioning* would still leave many questions with regard to their *effects* unsettled, but so at least part of what North considers as the most important determinants of economic life would not be completely beyond the reach of the economist.

Endogenising *economic* institutions and thereby economic order in the sense of explaining in general economic terms how (*ceteris paribus*!) they are *caused*, is not so complicated. It does not take a superhuman intellect to understand that perfect competition will be as improbable in reality as it is normal in textbooks. I personally found the work of Schumpeter and Chandler very enlightening in showing how real competition, in this case in a capitalist context, works. Economies of scale and scope, high barriers to entry, innovation and the advantages of being first mover, they all in a fairly

[86] Drobak and Nye, *Frontiers of new institutional economics*, "Introduction," p. XX.
[87] See *World Development Report* by the World Bank 1997, referred to in *NRC-Handelsblad* 26-6-1997.
[88] See notes 77 and 78.

obvious way promote forms of imperfect competition. One must, however, realise that what these authors - and others – provide, are explanations in principle. That means explanations that show how a system (in their case industrial capitalism) works, without being able, and without pretending to be able, to predict how a specific part of it will fare or how it will develop as a whole. They cannot, for example, predict innovations or their success, nor can they indicate who exactly will innovate and innovate successfully. The concrete *effects* of imperfect competition therefore are mostly unpredictable and as such can only be explained ad hoc.[89] One can very well imagine that the existence of specific economic institutions like property rights or even political organizations like the state can be explained in economic-functional terms, in the sense that one can show their economic functionality and functioning. But that is something different from explaining their concrete actual emerging, functioning and effects.

Endogenising political power is even harder. To put it bluntly: impossible. The logic of power simply is not identical to the logic of profit, notwithstanding the fact that they may sometimes overlap. Talking about the state as a provider of goods, or of politicians as operating on a political market offering products to voting consumers, can be nice as a metaphor. It may even be illuminating in some cases. But its suggestion that politics might be a subset of the economy, or political science a specific kind of economics, simply is wrong. Central government, political parties, pressure groups or whatever actors there might be in the field, they all have their reasons for doing what they do and wanting what they want. These, however, often are not economical or not even rational in any meaning of the word. Even central governments in democratic states are hardly ever

[89] Schumpeter, *Capitalism, socialism and democracy* and A.D. Chandler, jr., *Scale and scope. The dynamics of industrial capitalism* (Cambridge Mass 1990).

exclusively or even primarily focused on increasing national wealth. It is rule rather than exception that those trying to make or influence politics have *their* interests and ideals in mind rather than GNP.[90] Politics is not economics and it is not reducible to economics. Even if it were, its market is not a market of buyers and sellers like the market of “normal” goods with its supply, demand and a specific, tangible price.[91] There is an immense difference between voting and ruling on the one hand and buying or producing on the other. The stakes are different, the players are different, and the game that is being played is different. If only because the economy has no government that can take certain decisions that apply to everyone and are binding. If the logic of public choice were the logic of rational choice – which it is not -, it would still not be economics. And if it were economics, it would be economics of the non-perfect and non-free competition type, which means it is complex and under-determined. There is no model that can predict which pressure group will achieve exactly what goal, no model that can predict what a politician will do when in power.[92]

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[90] See for J. Bradford De Long, “Overstrong against thyself: war, the state, and growth in Europe on the eve of the industrial revolution” in: Olson and Kähkönen, *A not-so-dismal science*, 138-167. Gellner’s *Plough sword and book* and Jones’ *Growth recurring* constantly refer to the tension between profit-seeking and rent-seeking. The entire oeuvre of Mancur Olson focuses on the role of interest groups and their harmful effects for GNP in, especially, democracies. This topic also figures prominently in Weede, *Economic development*.

[91] People who compare the political and the economic market in any case pass over the fact that most people in world history have neither had the right to vote nor the right to produce and consume as they wanted!

[92] For a fine and convincing analysis of the difference between the rules of the market as they function in economics and the functioning of politics see Weede, *Economic development*, chapter 2.

An attempt to integrate culture, institutions and the state in economics: Douglass North

This may all sound fairly vague and maybe it is. Why then not look at the work of someone who has really thought this through? This again brings us to North as he has professed his intent to integrate culture, institutions, and the state in what in the end should amount to "a theory of institutional change". According to him in building such a theory three elements deserve special attention: a theory of ideology, that as we saw, and as North himself admits, still is in the wishful thinking stage; a theory of property rights, and a theory of the state.[93] His starting point was firmly neo-classical, which means his explanation how institutions arise, departed from a rational-choice and cost-benefit analysis and supposed they function efficiently. Together with Thomas he tried to empirically implement this approach in a book that basically presents a model in which demography, technology and the size of the market determine relative factor prices, which then are adduced to explain why and how property rights emerged. I don't think that worked. To begin with because their reasoning *presupposes* the existence of markets for various factors of production and a strong market-orientation in a world – Western Europe between 900 and 1700 - where these were anything but omnipresent. That they do so is quite understandable, since a neo-classical approach of whatever variety, including an institutional one, by definition is not able to explain the *emergence* of a market economy. No economic theory can. There is nothing economically inevitable to the market economy and from the point of view of rent-seeking elites, i.e. all the elites in the *Ancien Regime*, it is not even desirable.[94]

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[93] North, *Structure and change*, pp.7-8.

[94] See for example R. Brenner, "Economic backwardness in Eastern Europe in the light of developments in the West" in: D. Chirot, ed., *The origins of backwardness in Eastern*

Claiming that the emergence of property rights can be explained by the fact that in a time of labour scarcity, peasants could strengthen their position on the labour market versus their lords, suggests that this kind of market relations was decisive in determining the strength of various categories of the population. They were not without impact, but the fact that peasants East of the Elbe, who objectively were just as scarce after the Black Death, often were made serfs, and the differences in property rights between for example France and England, indicate that much more than a simple economic market-logic was operating. Sheer power and force played a very important role, and their logic need not be the logic of neo-classical economics. To merit the label "theory of institutional change", moreover, North's ideas are on the one hand too narrow, too exclusively focused on transaction costs and property rights, and on the other hand too wide, when for example he thinks these two elements can basically explain the Industrial Revolution.[95] Fairness requires to say that North has, also in this context, distanced himself from neo-classical approaches by, apart from no longer strictly adhering to the rational-choice dogma, admitting that institutions need not be efficient. A die-hard neo-classicist might defend the thesis that institutions arise because it is the choices of rational actors, whatever their faults, on which institutions are directly or indirectly based. Those that are inefficient will be competed out of existence. The real is the rational so to say.[96] Rightly North does not believe this: there are inefficient institutions because of ideology, inefficient political decision procedures, lock-in and path-dependency.[97] This of course amounts to saying that people do a lot of things that, from the perspective of maximising GNP, they should not be

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Europe. Economics and politics from the Middle Ages until the early twentieth century (Berkeley 1989) pp. 15-52.

[95] See the chapter on the Industrial Revolution in his *Structure and change.*

[96] Vromen, *Economic evolution,* chapter 3.

doing. Which boils down to admitting that institutions cannot be reduced to economic necessities or even to economic logic, but exist for a whole variety of reasons. Especially political or social institutions *need* not even be efficient, as they do not operate in a competitive environment of the kind in which economic institutions have to survive, while on the other hand they can have a huge impact on economic life.

His functional theory of the state in the end boils down to the fact that the state has as its primary function to protect property and enforce rulings that in the best of all world would make the market more efficient. But such a functional explanation does not indicate why the state arose in the first place, nor can it tell us much on why states can behave very differently, and neither is it very informative on the myriad of other things governments have busied themselves with, apart from protecting or not protecting property. If institutionalism, or for that matter any other type of economic approach is not able to endogenise the state in its analysis – and it is not and will never be – it will simply have to admit that, as an economic theory, it does not know how to deal with by far the most important institution, an institution that in OESO countries at the moment has a tax income, to mention but one obvious element of its importance, of between 30 and 50 percent of GNP. I need not go further into this. All these criticisms have already been ushered before.[98] That I make them at all is because they show, at the highest level so to say, that institutional economics is not able to really integrate institutions, culture and "normal" economic analysis into one analytical

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[97] See North, *Institutions, institutional change and economic performance.*

[98] See for example Inleiding to the Dutch version of North and Thomas, *Rise of the Western world,* published as *De opkomst van de westerse wereld. Een nieuwe economische geschiedenis* (Den Haag 1980); Clark, "Economic growth in history and theory"; A.J. Field, "What is wrong with neoclassical institutional economics: a critique with special reference to the North-Thomas model of pre-1500 Europe", *Explorations in Economic History* 18 (1981) pp. 174-199 and Gustavsson, *Power and economic institutions*, pp. 26-33.

scheme. North himself indicates that in his theory of institutional change the motor behind change is largely laying outside economics. Apart from relative prices, he refers to organizational activity and ideology, these last ones both firmly outside the realm of economic reason.

As Gustavsson in his analysis correctly concludes, North does not so much integrate institutions into economics as economics into institutions. This conclusion is valid for all efforts that have been made to bring culture, institutions and the state (back) into economics. They may have widened the range of subjects that are studied by economists, but they have added only very little to the explanatory power of their discipline *as a discipline*.[99] Wittingly or unwittingly they have made it patently clear that when it comes to explaining economic reality, economic theory is extremely impotent and can hardly say anything relevant without the help of detested disciplines like history, sociology, political science or psychology. Institutional economics in the end amounts to a camouflaged admittance of failure by representatives of by far the most arrogant among the social sciences. It would be hard to give a better illustration of this arrogance than the intriguing finding of Klamer and Colander that in 1990 only 3.6% of the graduate students in economics at six top ranking graduate economics programmes in US thought that having a thorough knowledge of the economy was important if you wanted to have success as an economist.[100] Many economists in their dealing with reality remind me of Hegel. This Prussian virtuoso is supposed to have vociferated “so much the worse for the facts”, when somebody pointed at some facts that were not in accordance with his theory.

[99] Gustavsson, *Power and economic institutions,* p. 31.
[100] Klamer and Colander, *Making of an economist,* p. 18.

Concluding remarks

Culture matters in economic history and economics. It does so on three different levels: the level of the choices made by consumers and producers, the level of institutions and the level of the political structure we call the state. If we regard culture as a set of dispositions it predisposes economic actors to make specific choices as producers and consumers and functions as the informal basis of institutions and political systems. At all three levels it has a huge impact on economic life.[101] Neither economic historians nor economists can afford to neglect culture, institutions or the state. Deep in their heart economic historians have always known this. With the cliometric revolution in the 1970s and 1980s, however, it seemed no longer obvious. The New Economic History brought methodological sophistication, a better understanding and use of theories and methods, and various other good things. A Marxist might even be seduced into saying that it was a historical necessity. But to a large extent it meant applying neo-classical theory, which is unrealistic even when applied to the modern western capitalist present with huge amounts of information, to a past, where it is even more unrealistic and even less supported, or held in check, by facts. It is not the kind of economic history that is likely to throw much light on the questions of large-scale development that I think should be at the heart of any economic history that wants to be a form of history. I can only agree with Solow: "Far from offering the economist a widened range of perceptions, this sort of economic history gives back to the theorist the same routine gruel that the economic theorist gives to the historian. Why should I believe, when it is applied to thin eighteenth-century data, something that

[101] Compare Kunz, "Kulturelle Variablen."

carries no conviction when it is done with more ample twentieth-century data?"[102]

The problem, however, is that even those who are willing to admit that culture, institutions and the state must be ingredients of any analysis of macro-economic change, find it very hard to deal with their role in concrete research. How exactly can you measure their importance? What theories to use in referring to their importance? How to pinpoint the exact mechanisms at work? The economic historian looking for help in these matters will probably look at (new) institutional economics, a branch of economics that one would expect to have analysed these problems and that has become extremely fashionable. And, indeed, some work done by institutionalists is very interesting. People like North, Chandler and Olson focus on the right questions. There is a lot to be learned from their books that cannot be learned from mainstream economists. To avoid disillusions, however, it is better not to have too many illusions in the first place. Institutional economists may ask the right questions, they have not come up with a set of systematically interrelated answers that can be integrated in a new paradigm and that allows us to throw away the neo-classical rational-choice approach. To a very large extent culture, institutions and the state continue to be external to their economic explanations. Their emergence, functioning and effects still largely have to be explained by factors outside the economy. Which means they constantly have to be introduced on an ad-hoc basis. To put it in more technical terms, they are not endogenised. The ad-hoc element becomes even stronger because of the role of path-dependency in economic development. This implies that historians will find much less sensational new insights and methods there than they may have expected.

[102] R.E. Solow, "Economics: is something missing": in: W.N. Parker, ed., *Economic history and the modern economist* (Oxford 1986) pp. 21-30.

Even the newest institutional economics in the end boils down to a mainstream economic analysis combined with the advice and an effort to bring culture, institutions the state and history – under the cloak of the better sounding “path dependency” - back in. Apart from the concept of transaction costs there is nothing new from a strictly economical point of view. Do not get me wrong; I am in favour of institutional economics and hold its practitioners in high esteem and appreciate their realism. It would be more than welcome when their openness to other disciplines would find a wide following. But let them be frank: all this simply means that history has hit back with a vengeance. Combining the strict logic of traditional mainstream economics, the insights and research agenda of institutional economics and the careful attention to concrete mechanisms and context that characterizes history as a discipline, is the task ahead. The results will not be as hard as those promised by mainstream economics and the new economic history. But I do not really mind. I have become old enough to prefer being vaguely right over being precisely wrong.