Preface and Introduction to the Theme

The papers presented in this volume were all presented at a researcher course for Ph. D. students on "New Institutional Economics and the Sociology of Economic and Political Institutions in Developing Countries". The course was co-sponsored by the Nordic Academy for Post-Graduate Research. It was held in March 1992 at Sandbjerg Manor.

The course was organised as an integrated component of the Ph. D. programme on "Political and Cultural Institutions in Development", organised by IDS, Roskilde, and its network partners in Denmark, the other Nordic countries, and India.

Various approaches under the broad heading of *development sociology* or *sociology of development* have for many years drawn attention to the role of economic and political institutions in societal development. The basic idea behind this researcher training course was to confront and compare these sociological approaches with the approaches often referred to as the *new institutional economics* (NIE). The course focused on the major NIE approaches and their particular contributions to understanding and explaining the emergence as well as the functions of selected economic and political institutions. These contributions were compared with the analyses and theories offered by development sociologists.

The NIE approaches have been developed mainly as alternatives or supplements to neo-classical micro- and macro-economics. Unlike other 'institutionalist' approaches, the NIE analyses and attempts to construct theory retain many of the axioms and assumptions of the tradition following Arrow and Debreu, most notably methodological individualism (cf. John Toye's paper).

The basic ideas of the NIE are introduced in the various papers included in this volume. Only a few basic points regarding the perspectives chosen by these approaches - as compared with neo-classical economic theory - will be mentioned in this preface.

In neo-classical economic theory institutions play no major role. Harvey Liebenstein has described their absence in the following manner: "Consider the matter of investment. The standard approach is that investment may be a function of some aggregate such as income and the interest rate. The consequence of investment may be determined by some variable, such as a marginal capital output ratio." Liebenstein goes on to ask what is left out in neo-classical economics. Some of the questions not raised, according to him, include the following: How are banks organised? Are they good at assessing who should get and who should not get loans? In what firms will the investments be made? How are these firms organised? How does the nature of the organisation of a firm determine the consequences of the investment? These are some of the important questions that new institutional economics add to the perspective of neo-classical economics.

To emphasise the basic distinctions between NIE and neo-classical economics the following simplified presentation may be useful as a starting point:

In neo-classical economics:

* Households are assumed to maximise utility;

* The market is assumed to shape economic behaviour;

* Firms are assumed to maximise profits or a utility function comprising both profit and growth.

Now, the points made by Liebenstein and other NIE adherents is that

* The market is not the only institution which shapes economic behaviour. The market is only one aspect of the more comprehensive incentive structure in a society.

* The market - the invisible hand - has little or no influence on intra-firm (and intra-household) behaviour. Intra-firm behaviour is shaped by a completely different governance structure - the visible hierarchy; a vertically integrated system

of transactions organised by the entrepreneur-manager-coordinator.

Using Douglass North we may compare NIE and neo-classical economics in this way:

	Neo-classical economics Rational choice	NIE
Role of institutions	Passive No constrain on choices	Active Guide choices
Assumptions about actors	Fully informed to make correct choices	Incompletely informed
Rationality postulate	Instrumental rationality	Procedural rationality

It could be added to this that the neo-classical model has been applied mainly in the context of highly developed, efficient markets where the unrealistic assumptions have proved their value for generating at least partly valid theory. The NIE assumptions would, most likely, be more useful in less developed societies with highly incomplete and imperfect markets - where institutional factors are particularly important to market development (cf. Jerome Davis' article).

The texts included in the present collection represent only a selection of the lectures and papers which were presented at Sandbjerg. Priority has been given to texts which we believe might be of particular interest to Ph. D. students and graduate students who would like to acquaint themselves with the prospects for applying NIE approaches to development studies. Most of the texts were prepared for this Occasional Paper. They are brief and in some cases tentative (my own contribution in particular). The much longer article by Jean-Philippe Platteau was prepared for publication elsewhere. It is included here to facilitate access to his interesting application of game theory along with other approaches to the study of links bewteen market, social relations and moral norms.

As organiser of the researcher course I would like to thank each of the paper writers for their contribution to this volume.

Roskilde, February 1993 John Martinussen