

# Non-neoclassical economics from late 19<sup>th</sup> century to 1930s

- Historical school of economics
- Institutional economics (or institutionalism)
- Austrian school of economics
- From 1930s on, neoclassical economics has marginalized these schools, but from 1890s to 1930s, they had been very popular among economists.
- From modern perspective we call those currents as non-orthodox, heterodox (approaches to economics), since neoclassical economics is treated as orthodox.

# ‘Heterodox economics’: late 19th/early 20th century

- Late 19th century and first 3 decades of the 20th century
- Time of PLURALISM IN ECONOMICS
  - neoclassical economics (itself divided into 2 camps – Marshallian and Walrasian)
  - Historical school of economics
  - Institutional economics
  - Marxian economics
  - Austrian school of economics

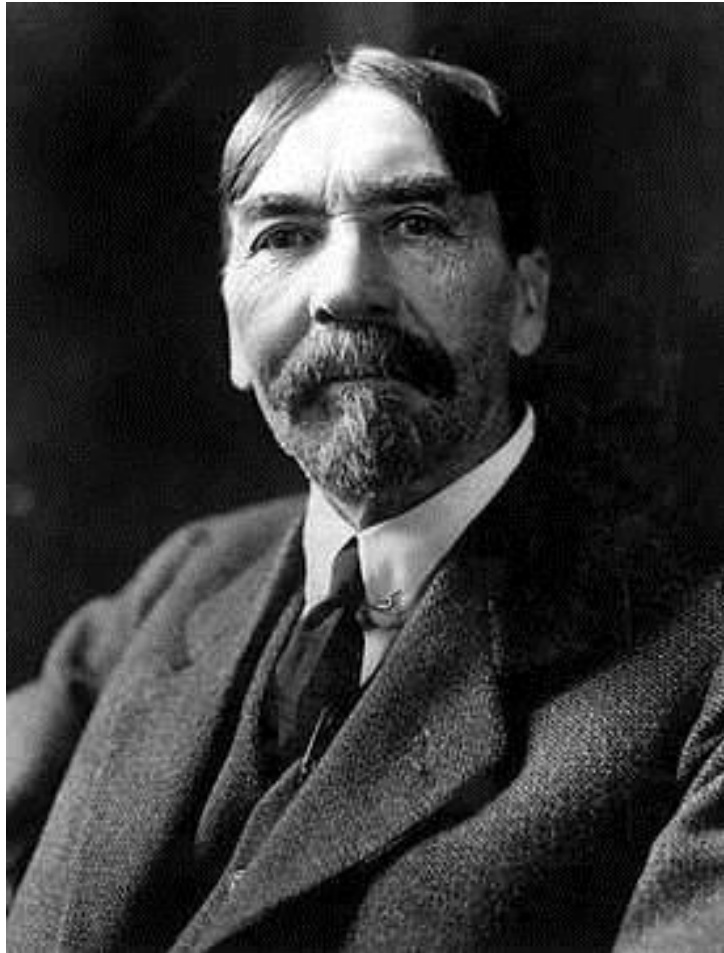
## ‘Heterodox economics’: late 19th/early 20th century

- Neoclassical economics since 1940s has become mainstream, orthodox approach – other currents have been marginalized
- Some of them survived as heterodox schools (Marxian econ., Austrian school), others died out (Historical school), yet others have been largely transformed (‘Old’ Institutionalism into New Institutional Economics)
- But the mainstream was influenced (sometimes much) but the heterodox approaches

# Old Institutional Economics

- Mainly US economists
- Marginalized in 1940s by neoclassical school
- Quasi-institutionalism (G. Myrdal, J. K. Galbraith) – 1950s-1970s
- Revival through synthesis with neoclasical/mainstream economics – New Institutional Economics (since 1980s)

# Thorstein Veblen (1857-1929)



# Thorstein Veblen (1857-1929)

- *Theory of the Leisure Class*, 1899
- ‘the most original and penetrating economic and social critic of American capitalism that the United States has ever produced’.
- Unusual style of writing; terms like ‘conspicuous consumption’, ‘leisure class’, ‘captains of the industry’, ‘predatory instinct’ etc.
- Economist and sociologist
- Veblen’s economics:
  - Criticism of neoclassical economics
  - Analysis of capitalism
  - Possible scenarios of the future development of capitalism

# Criticism of neoclassical economics (NE)

- Wanted to abolish the entire structure of neoclassical economics and rebuild a unified social science from economics, anthropology, sociology, psychology and history.
- According to Veblen, NE is not scientific due to several reasons

# Veblen's criticism of Neoclassical Economics

NE is not scientific because:

a) Based on the wrong assumption, that there is a harmony in the economic system

While in real economies:

1. there are monopolies;
  2. prices are higher than competitive prices;
  3. competition among large corporations leads to wars among countries;
  4. and the actions of captains of industry lead to mass unemployment and depressions.
- Is this criticism valid?



# Veblen's criticism of Neoclassical Economics

- b) Equilibrium concept is rather normative (ethical), than positive (scientific)

Is that right?

- c) Assumes that the economy is static, non-evolving entity.

Economists should also study factors they assume to be constant – such as tastes, preferences, technology, organizational arrangements of the society and the economy etc.

Was he correct? Is evolutionary economics possible?

# Veblen's criticism of Neoclassical Economics

- d) Based on the wrong assumptions about the human nature
- According to NE humans are driven by the desire to maximize pleasures and minimize pains. This is hedonistic psychology.
  - This assumption ignores the developments made in psychology, sociology and anthropology. According to Veblen people are guided by a wide array of motives (various instincts, habits, obligations, duties etc.)
  - Is Veblen's alternative workable? What are advantages of NE' concept of human motivation?

# Veblen's analysis of capitalism

- Economics should be a study of the evolving institutional structure of the economy and the society
- He defined institutions as habits of thought that are accepted in the society (or by different classes of society) at any particular time.
- Institutions are widely-shared habits, preferences, norms and the like – in general some kind of a *mental culture* of the society.

# Veblen's analysis of capitalism

- For Veblen, the most important institutions are instincts :
  - parental instinct,
  - instinct of workmanship (of hard work),
  - idle curiosity,
  - instinct of acquisition (greediness, money-grabbing instinct).

# Veblen's analysis of capitalism

- Those instincts create certain tensions in the economy and society.
- Instincts of workmanship and idle curiosity lead to production with great efficiency of high quality products.
- But, the instinct of acquisition (maximization of profits) leads to behavior that benefits only the individual, even though it might have disastrous consequences for the society (lower production, low quality goods).
- In the economy, in every historical period, there is a conflict, tension between the instincts of this two kinds (workmanship and idle curiosity vs. acquisition).

# Veblen's analysis of capitalism

- In capitalism, there are two different habits of thought (institutions):
  - 1) for workers and engineers, and
  - 2) for the businessmen (or captains of industry).
- Instincts of hard work and idle curiosity are prevailing in the class of workers and engineers. Concerned with high production, low prices, high quality.
- Captains of industry (businessmen, owners of capital) are driven mainly by the instinct of acquisition. Concerned with profits, higher prices, restricting the volume of production.
- **So there is a basic, fundamental conflict in capitalism between capitalists and both workers and engineers.**

# Veblen on consumption patterns in capitalism

- Predatory instinct – people want to compete, to be held in high esteem, to be admired etc.
- Predatory and acquisition instincts are realized in modern capitalism by methods of conspicuous consumption and conspicuous leisure.

# Conspicuous activities

- Conspicuous consumption – consumption attracting attention of others, luxury consumption
- Conspicuous leisure – leisure attracting attention of others, often involving some highly priced commodities.
- Do these activities really occur in modern economies?
- Examples?
- Are they bad? Economically?



# Veblen on leisure class

- Leisure class – wealthy class, members do not have to work physically in the productive sector,
- Examples: owners of firms or engaged in ‘money-related’ occupations like high management, banking, finance, law etc.

# Veblen on the long-run tendencies in capitalism

- Patterns of conspicuous consumption and leisure will spread out throughout the society; there will be much waste from those phenomena and advertising and marketing costs will be increasing.
- Increased flow of goods that do not satisfy real human needs.

# Veblen on the future of capitalism

- If the working class and engineers would gain the control of the system, then the progress is possible (in terms of contributing to satisfying real human needs).
- This is possible through a socialist-like revolution.
- The reason for the revolution could be relative poverty of the working class. Discontent on the part of the working class that they can not consume as much as the leisure class.

# Veblen on socialist revolution

- This would be a collapse, an end of capitalism not because of its failures (like growing unemployment, depressions, increasing absolute poverty) as Marx thought, but rather in the effect of its success
- Capitalism is continuously growing, and absolute standard of living is growing, but the relative poverty (inequality) is also growing.

# Veblen on future of capitalism

- Future is not determined, it is open-ended
- Possible visions of the development of capitalism in the long run, according to Veblen:
  1. socialist revolution
  2. technocratic revolution
  3. turn to nationalism and police state
- Have any of these scenarios occurred in modern capitalism? Why or why not?

# Summary of Veblen's thought

1. critic of capitalism and neoclassical economics
2. considered by many as sociologist rather than economist
3. his contribution can be considered as complementary to neoclassical economics
4. his system was literary described with no model or theory in any strict sense
5. his psychology of instincts was soon rejected by psychologists
6. did not influence mainstream economics much, but managed to convince economists to do more empirically-oriented work
7. his conclusions are rather not suitable to empirical testing; writings are a mix of positive and normative statements