

# Neoclassicism, Marxism, Institutionalism: Revisiting the broad schools of economic thought

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## Abstract

This paper examines each of the key schools of economic thought that have been employed in the history of the development of modern economic theorizing, that is, *Neoclassicism*, *Marxism* and *Institutionalism* with a view to providing a better understanding of these traditions of economic thought.

It highlights their basic provisions, philosophical underpinning, methodological approach and limitation in economic theorizing. This paper argues that each of these traditions of economic thought have collectively enriched the study, prediction, analysis, explanation and scientific generalization about empirical regularities and economic phenomena. While each one may be more suitably applied in different contexts or particular circumstance, approaches that emphasize social structures are as important as those that stress their economic equivalents in the study of economic phenomena and human interaction and exchange.

That is, to achieve a holistic study and analysis of economic phenomena, the spatial, temporal and sectoral variations in human interaction and exchange dictates that approaches that emphasizes social character to the exclusion of the economic or vice versa might not be appropriate.

**Keywords:** Neoclassicism; Marxism; Institutionalism, economic theorizing, history of economic thought

## 1. Introduction

Modern economic thought emerged between the 18<sup>th</sup> and 19<sup>th</sup> centuries as the western world began its transformation from a predominantly agrarian society to an industrialized one. Modern economic theorizing is often credited to Adam Smith for his 18<sup>th</sup> century treatise *The Wealth of Nations*. Since then three broad schools of economic thought are identifiable viz: the neoclassical approach which is often regarded as the mainstream or orthodox economics school, the structuralist approach with its prominent Marxist variant<sup>1</sup> and, the institutionalist approach.

Also, within the social science and humanities, four broad philosophical approaches to economic theorizing have been identified and employed by researchers in different contexts. These are empiricism, positivism, humanism and structuralism (see Johnston, 1986; Holt-Jensen, 1988). Empiricism is a philosophical approach that emphasizes the importance of sensory experience as the principal source of knowledge. In contrast to rationalism which emphasizes the importance of reason as the primary source of knowledge independent of experience, empiricism stresses the primacy of experience over reason (see Smith, 1996; Meyers, 2006).

The positivist philosophy is an empiricist account of science which is built on the foundation of empiricism (Hooker, 1975; Benton and Craib, 2011). The philosophical foundations of empiricism and positivism are similar, however while the former holds that knowledge is based exclusively on sensory experience, the latter not only shares a similar view, but goes further to subject the information from the experience or observation to logical and mathematical treatment. Zammito (2004) notes the implicit assumption of this philosophical school is that the singular method for attaining valid knowledge is through the natural science. Humanism on the other hand, is a renaissance movement in philosophy towards a more human-centred approach with the conviction that humankind can best improve the circumstances of their lives by thinking and acting for themselves, especially in the exercise of their capacity to reason (Relph, 1981). It is a system of thought which attaches prime importance to human rather than divine or supernatural matters.

Structuralist ideas in social thought developed in opposition to the humanist tradition of the 1950s and early 1960s (Peet, 1998). It is a philosophical school that emphasizes that explanation for observed phenomena cannot

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<sup>1</sup> Other traditions within the structuralist school are structuration theory by Anthony Giddens (1976; 1979) and critical realism by Roy Bhaskar (1975; 1979).

be produced through empirical study of the phenomena alone, but must be sought in general or overarching system or structures which underpin all phenomena but are not identifiable within them. As opposed to empiricists, positivists or humanist philosophies, structuralist philosophical perspective holds that human conscious explanations and overt behaviour cannot be taken at face value as conclusive evidential warrants or objects of scientific analysis. They must necessarily be investigated beyond surface structures to discover the real structures which account for the variety of observable phenomena (Johnston, 1986).

These philosophical approaches are closely associated with the broad schools of economic thought earlier mentioned as will be examined in subsequent sections. The purpose of this paper is to examine each of these schools of economic thought and to highlights their basic provisions, philosophical underpinning, methodological approach and limitation towards a better understanding of these traditions of economic thought.

## 2. The Neoclassical School of Economic Thought

Neoclassical economics is incontrovertibly the most prominent tradition of economic thought (Hodgson, 1992; Finlayson et al. 2005). This prominence may be attributed to its long intellectual history and its unified and rigorous approach to solving a variety of practical and theoretical problems (Gowdy, 2009). Neoclassical economics is overwhelmingly grounded on the positivist philosophy principally logical positivism (Katouzian, 1980; Seligman, 1969). This is founded on Auguste Comte's principle that all forms of valid knowledge are based on scientific evidence, as empirical facts are the major objects of knowledge (Agboola, 2015). Thus, two broad distinctions within neoclassical economics are positive economics and normative economics (Friedman 1994; Weston, 1994). On this note, Blaug (1992) documents David Hume's foundational distinction between positive and normative statements as statements that border on the realm of facts, objectivity or science and, statements that border on the realm of value, subjectivity or art respectively. Similarly, Weston (1994) highlights John Neville Keynes' distinction between positive economics, normative economics and the art of economics.

According to Keynes, positive science is the "body of systemized knowledge of what is", normative science is "a body of systemized knowledge relating to the criteria of what ought to be", while the art of economics is "a system of rules for the attainment of a given end". Weston (ibid), on his part posits that positive economics consists of non-ethical true or false claims about economies or aspects of economies whereas normative economics consists of, or refers to, propositions about economics that contain at least one assertion as to what is ethically preferable. He however notes that the putative positive/normative dichotomy in economics is merely a conceptual distinction neither intended as a behavioural standard for economists to avoid advocating ethical positions nor automatically entails the practical possibility of a purely positive, value-free or ethically neutral economics.

Friedman (1953) in his extensive work on positive economics in relation to economic policy argues that normative economics and the art of economics cannot be independent of positive economics as any policy conclusion necessarily rests on a prediction about the consequences of taking an action rather than another. He notes differences of opinions expressed on economic policy are themselves 'positive' statements to be accepted or rejected based on empirical evidence. Thus, in such situations, the outcome of an empirically valid judgment is an indication of consensus on 'correct' economic policy, which depends much less on the progress of normative economics but on the progress of positive economics yielding conclusions that are widely accepted. Friedman (ibid) and Rotwein (1959) contend that the ultimate goal of positive economics is the development of a theory or hypothesis that yields valid and meaningful predictions about phenomena not yet observed. Such a theory is generally a complex combination of two elements; a language designed to promote systematic and organized methods of reasoning and, a body of substantive hypotheses designed to abstract essential features of complex reality.

For Friedman, the language element of a theory has no substantive content; it is rather a set of tautologies that serve as a filing system for organizing empirical material and facilitating our understanding of such empirical material. Thus, when viewed as a body of substantive hypotheses, the criteria for judging a theory is its predictive power for the class of phenomena which it is intended to explain. In this sense, only factual evidence can reveal whether a theory is 'right' or 'wrong' and forms the basis for its acceptance as being valid or its rejection. Thus, Boland (1979) asserts that the only relevant test of the validity of a hypothesis is comparison of its predictions with experience<sup>1</sup>. Friedman further argues that if the hypothesis is consistent with the evidence at

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<sup>1</sup> Friedman (1953) argues that a hypothesis is rejected if its predictions are contradicted frequently or more often than predictions from an alternative hypothesis. Conversely, it is accepted if its predictions are not contradicted i.e. it derives great

hand, its further testing involves the deduction of new facts from it, which are capable of being observed but not previously known and checking these deduced facts against the additional empirical evidence.

However, Caldwell (1980) in a critique of Friedman's essay, points out that there is unanimity amongst philosophers of science in their rejection of the notion that the only goal of science is prediction. According to him, explanation, not prediction, is the goal of science and if science seeks theories that have explanatory as well as predictive powers, then theories that merely predict well may not be satisfactory. Notwithstanding, the positivist stance of neoclassicism is dominant and its emphasis on empirical evidence, objective, descriptive and scientific methodological approach is entrenched in deductivism or hypothetico-deductive mode of enquiry.

Blaug (1992) and Kim (1963) observed that the dominant version of the hypothetico-deductive model of explanation is credited to the work of Hempel and Oppenheim (1948) who argued that all truly scientific explanations have a common logical structure. That is, a deductive model of explanation is a logical structure of argument whereby *an explanandum* or statement about a phenomenon whose explanation is sought is deduced by deductive logic from the *explanans*, which is a combination of a minimum of one universal law and a statement of relevant initial or boundary conditions. In this respect, a universal law is a proposition of the form "in all cases where events *A* occur, events *B* also occur". These universal laws that are employed in explanations are mere hypotheses or conjectures that may be tested by using them to make predictions about particular phenomena or events but which themselves are neither reducible to observations about events nor derived by inductive generalization from individual instances. However, hypothetico-deductivism has been subject to extensive logical scrutiny (see Glymour, 1980; Gemes, 1990; Park, 2004; Gorski, 2004).

An important and influential direction in the hypothetico-deductivism thesis is the idea propounded by Karl Popper in his falsificationist methodology. Empirical testability is an important criterion for the acceptance or rejection of a theory or hypothesis in economics. Economists hold the view that economic theories or hypothesis must be verifiable or falsifiable against some empirical evidence. The latter principle, credited to Popper (1959, 1969 and 1972) argues that scientific theories, in principle are conjectures that cannot be verified but only falsified by some specific observations contradicting predictions derived from the theories (Haila, 1982). Hence, falsification or refutation is an attempt at logically questioning hypotheses or theories rather than proving or verifying them. It takes the view that science seeks truthful explanations of the interrelation of phenomena and only grows by empirically refuting accepted theories and by proposing new theories which are even more susceptible to refutation (Stanley, 1985). Thus, Blaug (1992) defines falsificationism as a methodological standpoint that regards theories and hypotheses as scientific if and only if their predictions are at least in principle not falsifiable, that is, if they forbid certain acts, states or events from occurring. Yet, a major drawback of the Popperian approach is the difficulty of putting it into practice and many economists have only paid lip service to its usefulness whilst their practice have tended to conform more to the earlier principle of verification (Caldwell, 1982; Hausman, 1985, 1988; Dow, 1997).

Nevertheless, a major criticism that is central to the methodology of neoclassical economics is its extreme formalism and excessive focus on mathematical modeling which critics have attributed to a form of mathematics or physics envy (Blaug, 1992). For Kaldor (1972) abstract mathematical modeling and econometric testing lead nowhere as the careful accumulation, sifting and development of refined methods of statistical inference cannot make up for the lack of any basic understanding of how the actual economy works. This constricted methodology of the neoclassical school, Foldvary (1996) argues, has dominated other rigorous abstract methods such as verbal logic and limits theory to mathematically tractable models with determinate solutions which are often hypothetical constructs with little relevance to the workings of actual economies. Thus, while the application of these techniques sometimes make analysis incomprehensible rather than illuminate it, neoclassical economists have become so enthralled by them as to treat them as ends in themselves

### 3. Marxism

Over the years, economic problems have regularly come to light which cast considerable doubts on the capacity of many of the strands of mainstream economics to explain, or even to address real world events or to facilitate policy evaluation (Lawson, 1997: 3). Rosenberg (1992) in a blunt criticism of mainstream economics argues that economics is an empirical failure which only makes imprecise generic predictions without being able to identify and isolate the major causes of economic phenomena (see also Hoover, 1995; Hausman, 2003).

The many criticisms of the methodology of mainstream economics and the dissenting views of economists on

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confidence if it has survived many opportunities for contradiction.

the empirical relevance of its methodological approaches have led to the rebirth, development and, proliferation of rival and distinct schools of thought in economics (see Mäki, 1990; Lawson, 1995, 1999; McCloskey, 1983, 1994; Fleetwood, 1999). One of such school is the structuralist school of economic thought which comprises the Marxist approach to economic theorizing and constitutes an important component of the broad schools of thought in economics.

Marxism is a socio-economic and socio-political view that borders on a materialistic conception of history. The Marxist approach is based on ideas and practices developed by Karl Marx (1818-1883). There are four distinct and notable themes within the Marxist thesis – historical materialism, the mode of production, the theory of class or class conflict and the labour theory of value (Scott, 1991). As Johnston (1986) submits, Marxism is a structuralist approach to the study of human society which presents observed phenomena as representations of underlying social structures whose base lies in the material conditions of existence. From this premise, the doctrine of historical materialism is developed which in its most rudimentary form states that the development of human society is determined by specific laws of change which are rooted in the social provision of the material means of human existence. The historical element of this doctrine depicts a theory of human history wherein the future is fashioned by past events according to specific laws of evolution, while the materialistic conception views societies as being formed solely for the purpose of collective provision of the material means of existence.

Marx derives much of the inspiration for his historical materialistic approach to the study of human phenomena from the philosophical tradition of German classical idealism and particularly from the earlier work of Hegel (1770-1831) on dialectic (Johnston, 1986; Peet, 1998). Peet (ibid) notes that although Marx derives his dialectical method from Hegel, he rejects its idealistic conception and reverses Hegel's dialectic. While Hegelian dialectic views the process of thinking as an idea which creates the real world or the real world as the external appearance of the idea, for Marx, the idea is nothing else than the material world reflected by the human mind and translated into forms of thought (Marx, 1976). Hence, Marxist materialism is a realist philosophy which asserts the primacy of the material world and views human thought as a reflection of the material world in the mind.

Therefore, Marxist historical materialism is based on understanding the dialectics at work within the structure. This concept of dialectics is presented as a sequence of thesis, antithesis and synthesis whereby conflict between the thesis and antithesis eventually leads to a synthesis that incorporates elements of both the thesis and antithesis, but which later generates its own opposition<sup>1</sup> and thus begins another sequence (Johnston, 1986, 1997). Therefore, the dialectical resolution of conflict is a productive synthesis of the conflicting elements in a definite situation (Peet, ibid). In the context of human society, Marx concur with Hegel's dialectic that the driving force in development is the conflict and opposition between elements.

In presenting his historical materialist analysis of society within a conceptual framework, Marx focused on the dialectics of *the mode of production* as the resolution of the contradictory opposites that is inherent in capitalism. Scott (1991) note that Marx characterized human history by identifying four basic modes of production which corresponds to the distinctive evolutionary stage of human society, viz: ancient (primitive communism), feudal, capitalist and communist. Mode of production according to Marx is a historically specific complex of social relations through which human societies collectively produce their material means of existence (Burris, 1987). It consists of two elements; the *material forces of production* and the *relations of production*. The former comprises the physical means of production (land, raw material, machinery etc) and labour power, while the latter defines the distribution of ownership over the productive forces between different groups or classes in the society. That is, it addresses the conditions within which the productive forces are brought into operation.

Therefore, central to Marxism is the analysis of the critical role of the economic structure of capitalist society and the contradictions inherent in it which constitutes the determinants of human consciousness and being. For Marx, a capitalist system is characterized by a tendency for capitalists to maximize the rate of profit by the exploitation<sup>2</sup> or appropriation of the surplus value of labour, i.e. the part of the value created by labour in excess

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<sup>1</sup> Each synthesis becomes the next thesis and so there is no permanent resolution as each synthesis contains within itself the roots of its own destruction (Johnston, 1997). Marx applied the dialectical method to analyse the contradictions inherent in capitalism which arises as a consequence of the alienation of labour power from its fruits and the resultant decline in the capitalist's rate of profit.

<sup>2</sup> Social relations are conceived as relations between classes centred on the extraction of surplus labour time or exploitation. Societies are exploitative when uncompensated surplus labour or its products are taken from the direct producers, the exploitation process being an arena of struggle, the dominant using a combination of economic, political and ideological force, and the dominated resisting through overt means like social organization, rebellion and hidden means like reluctant compliance (Peet, 1998:82).

of the cost of labour. Capitalists aim to maximize profit while keeping the cost of labour as low as possible through investment in *dead labour* – equipment, machinery and technological development. This difference between the capitalist's selling price and the cost of labour is the *surplus value* which is the source of the capitalist's profit. However, this arrangement soon generates conflict or antagonism between labour and capital since the consumption of the proletariat (the working class) is constrained by their limited resources which reflect the increased disparity in capital concentration within a class of the society. Hence, this leads to over-production or under-consumption since the market comprises a substantial percentage of the working class whose resources are constrained and thus a subsequent fall in the capitalist's rate of profit (Johnston, 1986).

Essentially, Marx's theory of socio-economic change centre on the conflict between the material productive forces and the relations of production (Hodgson, 2001). Therefore, this crisis or contradiction between the forces of production and the relations of production inherent in the capitalist system will necessitate a transition to a new mode of production. In other words, the production relations which initially encouraged the development of the productive forces soon creates an inter-class antagonism which eventually leads to a hindrance in their further development. Consequently, the contradictions within the capitalist system are circumvented by the creation of new relations in production which supplants the prevailing mode (Scott, 1991; Peet, 1998).

Another feature of human social life which Marxism aims to uncover in the general laws of history is class division of society which reflects the antagonism of the division. Social class, according to Scott (1991) is not simply a passive category to which individuals are assigned; rather it is the basis upon which the entire consciousness of the individual, their interests, ideas, aspirations and actions are shaped. Levine (1998) notes that Marxism conceptualizes class in terms of the relationship of individuals to the structure of ownership or paid labour, i.e. classes are defined in relation to their position in the production process. According to Marx (1976) the defining characteristics of the relationship between labour and capital can be understood by the exploitative nature of the capitalist production system. In this sense, exploitation results from the power that the relations in production bestow on one class at the expense of the other. Levine (1998) and Scott (1991) observe that 'exploitation' has a specific meaning in Marxist economics and is derived from Marxist labour theory of value.

Building upon Adam Smith and Ricardo's theory of value, Marx drew a distinction between the *use value* and *exchange value* of a commodity and designated labour as use value, and labour power (the actual commodity transacted between the employer and employee) as exchange value. He argued that the labour power which the capitalist purchases has both a market price and an underlying value which is the *socially necessary labour time for its (re)production*. However, labour has a unique ability to create value in excess of its reproductive requirements, which is referred to as surplus value. Hence, the appropriation of this surplus value by the dominant class in the relations of production is described as exploitation and forms the root of basic inequality and class struggle in capitalist society (Scott, 1991; Mandel, 2002; Derek, et al 2009).

Although many writers have recognized the significance of the works of Marx for economic theorizing in the explanation of important macroeconomic phenomena of capitalist economies, such as the rate of profit, periodic depressions, value of labour etc (Moseley, 1985, 1997; Mohun, 1994; Foley, 2000), Marxism has been a subject of enormous criticisms. For instance, Veblen (1897), whilst acknowledging the relevance of Marxist materialistic interpretation of history in explaining social development, argues from an evolutionary economics perspective that an explanation of the operative force at work is lacking in Marxism as there is no explanation of the causal mechanism of how individual attitudes, purposes and behaviours are influenced by social structures or institutions. He contends that Marxism lacks an adequate theory of human agency as it denies human discretion and effort at seeking a better adjustment but conceptualizes man as the creature of circumstances.

Similarly, Peet (1998) opines that Marxist structuralism is an overly abstract, totalizing and deterministic conception of human existence which does not provide an adequate consideration of the autonomy of human consciousness. Giddens (1981: 88) note that Marx's view of the superiority of production over other aspects of social life is untenable. According to him, the fact that material production is a necessary means of sustaining human existence does not imply that social organization of production is more fundamental to the explanation of the persistence or transformation of societies than any other institutional form. From a neoclassical economics viewpoint, Samuelson (1971; 1992) a blunt critic of Marx argues that Marxian theory of land rent and his transformation problem<sup>1</sup> is grossly misconceived and lacking in logical coherence (see also Glick and Ehrbar,

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<sup>1</sup> Karl Marx's transformation hypothesis relates to the transformation of the value of a commodity based on the socially necessary labour time expended on its production (in line with his labour theory of value) into the competitive price of the market place. The transformation problem is the problem of finding a general rule to transform the values of commodities into Marxian prices of production, defined as cost plus profit at the average rate. Karl Marx gave an arithmetic illustration of

1987). Blaug (1990) further argues that Marx's theory does not provide definite predictions which follow as logical deductions from the empirical premises of the theory. He maintains that most of Marx's conclusions do not only follow logically from his premises, but also have been contradicted by empirical evidence.

One distinct criticism of structuralist approach and by extension Marxism is offered by Hodgson (1999). According to him, structuralism fails to acknowledge the role of a special type of social structure, i.e. institution and its influence on agents' action and intentions. Hodgson (2006) argues that institutions are the kind of structures that matter most in the social realm as they make up the substance of social life. Hodgson (2004) further notes that institutions unlike social structures do not only enable and constrain agents' intention and action but can also condition and shape such intentions and actions.

#### 4. Institutionalism

An assessment of the history of economic thought reveals widespread attempts at incorporating issues bordering on institutions within the economics discipline. The most apparent example is that of the American institutionalist tradition of Veblen, Mitchell, Commons and Ayres. However, prior to that, institution had been an important element of political economy. Rutherford (1994a) posits that institutional analyses of various kinds are evident in the earlier works of classical economists such as Adam Smith and J. S. Mill; members of the English, German and American historical schools; members of the Austrian school such as Menger, von Weiser and Hayek.

Nevertheless, Thorstein Veblen is arguably the pioneer of the field of knowledge that has come to be known as institutional economics. Langlois (1989) notes Veblen's early methodological writings are perhaps the major source of the old institutional economics (OIE) tradition. Prior to 1918, institutional economics was not a distinct school of economic thought, although Veblen's works had attained popularity in America by that time (Hodgson, 2004). However, the term, 'institutional economics' was not brought to the public attention of the economics discipline until 1919 by Walton Hamilton in an American Economic Association conference paper (Rutherford, 2001).

Thus, institutionalism became a significant element in American economics and reached its peak in the interwar period; it however suffered from decline and fragmentation leading to its estrangement from the mainstream of economics (Foster, 1991; Hodgson 2004). Foster (ibid) notes that contrary to impressions gained in some historical accounts of economic thought, institutional economics was indeed the principal and dominant school of economic thought during this period and was widely taught and exerted a strong influence on policy. However, it was displaced and supplanted by the neoclassical economics school following the Second World War by the latter's resolute and vigorous aspirations for economists to be regarded as scientists and thus the rejection of the normative priorities of the institutional economics tradition in favour of the positivism of mathematical logic represented in neoclassicism.

According to Hodgson (1998, 2004) OIE was relegated due to the profound methodological shift in social science from an institutional economics approach that emphasizes analytical description or explanation and a holistic and evolutionary view of the economy in favour of a neoclassical approach that stresses mathematical formalism, prediction and scientific generalization about empirical regularities. Hence, Hodgson (ibid) notes that behaviorist psychology and positivist philosophy displaced the instinct psychology and pragmatist philosophy upon which early institutionalism had been built. Consequently, in comparison, institutionalism was regarded as technically less rigorous and thereby inferior.

However, over the years, another strand of institutionalism known as the new institutional economics (NIE) has developed, not via a re-emergence of traditional institutionalism but mainly from within the neoclassical economics tradition (Hodgson, 1989). Hence, NIE mirrors some of the provisions of the neoclassical school but essentially differentiated from it on some vital theoretical aspects. Rutherford (1989) observes that NIE adopts a purely individualistic approach in line with neoclassicism and one which emphasizes invisible-hand process. Hodgson (2004) also notes NIE places emphasis on the survival of specific institutional forms because they lower transaction costs relative to their alternatives. According to Coase (1984: 230), the distinguishing feature of the NIE School is its use of standard economic theory to analyze the working of institutions and to discover the part they play in the operations of the economy. Thus, Nee (2005) points out that NIE has sought to differentiate itself from OIE by adapting, rather than rejecting, as did the latter, neoclassical economic theory.

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the transformation process in volume III of *Capital* (see Seton, 1957).

Yet, the OIE tradition represents a rich, albeit diverse and disparate school of economic thought which emerged largely out of a critique of mainstream orthodox assumptions. The conventional view is that the two principal publications that lent foundation to the OIE school were Veblen's "*The Theory of the Leisure Class*" and Commons' "*A Sociological View of Sovereignty*" (Samuels, 1998). In the evaluation of institutionalism, OIE can be broadly classified into a Veblen-Ayres and a Commons branch. While both Ayres and Commons derived much of their inspiration from John Dewey, Ayres applied these ideas to a Veblenian tradition whereas Commons developed a rather diverse conceptualization of these ideas in relation to his personal ideas (Hodgson, 2004). Veblen's writings borders on issues such as capitalism, imperialism, foreign policy, business cycle, economic growth and development and, evolutionary theory (Hodgson, 2004).

On the other hand, Commons' interest on issues that borders on law and organizations, labour, importance of property rights, the system of courts, the evolution of common law and the determination of statute law in comparison to the other major writers in the American institutionalist tradition is unrivaled (Rutherford, 1994a; Hodgson, 2004). Commons, like other institutionalists was concerned about orthodox economics failure to incorporate institutions into its theory and attributed this failure to the latter's presumption of harmony of interest on the part of individuals instead of conflict of interest which follows necessarily from the pervasiveness of scarcity. He argues that orthodox theory fails to bring out the need for institutionalized rules to constrain individual behaviour, create order, certainty and security of expectation.

Commons (1893) emphasized the importance of law and property rights in affecting both production and distribution and explicitly challenged the tendency among orthodox economists to take the laws of private property for granted with an assumption that they are fixed and immutable. He argues that property laws are changeable and its evolution is often an outcome of long-term historical processes (Chase, 1986). The unit of analysis in Commons' writing is the *transaction*, which according to him is the ultimate unit of economic activity (Commons, 1931). According to Rutherford (1983, 1994b), Commons' ideas are built around the basic concepts of transactions, working rules and going concerns with his idea of transaction focusing on the various legal relationships arising in economic transactions. Hence, from Commons works on transactions, property rights and organizations, writers have argued there are close links with the NIE School and even suggested that Williamson's (1975, 1985, 1990) idea of transaction costs and economics of organization developed from Commons' ideas on transaction as the major unit of economic analysis (see Rutherford, 1994a; Dugger, 1983, 1996 and Williamson, 1996: 152).

A basic strength of the OIE School which may not be contested is that it provides the foundation for highlighting the importance of institutions in human interaction and as key elements of any economy. As Hodgson (2004) argues, OIE emphasizes the importance of institution in economic life and attempts to understand their role and their evolution. Thus, a common theme in the OIE tradition is the concept of the institutionalized individual. This notion is projected by the idea that the individual is not given but is reconstituted by the institution. In other words, individuals are affected by their institutional and cultural situations and the former do not simply create institutions intentionally or unintentionally, but are rather born into existing institutions and institutions in turn influence the motivations and preferences of the individual. Hence institutions in the context of the OIE School are a social structure which shapes the very preference, purpose, behaviour and disposition of the individual. This view has been described by Hodgson (2003, 2004) as "reconstitutive downward causation".

Thus, institution is the centrepiece of analysis in the OIE thesis. However, it is difficult to ascribe a precise definition to institution in the OIE thesis particularly due to the quite dramatic differences between the methodologies and theoretical directions of its founders (Rutherford, 2000). Notwithstanding, Hodgson (2006) defines institutions as the systems of established and prevalent social rules that structure social interactions.

In providing the causal and evolutionary explanation for how individual disposition conform to social rules and are reconstituted by the institution, Veblen (1914) made recourse to the psychology of human motivation and the social mechanism of the creation and reproduction of roles. This argument is based on the instinct-habit psychology of human. Instincts, according to Hodgson (2004) are inherited behavioural dispositions that when triggered give rise to reflexes, urges or emotions which are directed to some objective end, while habits are the means by which the pursuit of these ends could be adapted in particular circumstances.

The habit-driven capacity to reflect and reason upon particular situations gives rise to new behaviours and new habits. In turn, the capacity to form new habits aided by both instincts and reason falls into conventional lines, acquires the consistency of custom and prescription and hence takes up an institutional character and form. Institutional adaptation and behavioural norms are then stored in individual habits and passed on to succeeding generations by education, imitation or socialization. Hence, habits or habits of thought are essential to cognition

and provides the mechanism through which individual are able to perceive and understand the world and also a mechanism through which institutional norms and conventions are pressed upon the individual (Hodgson, *ibid*).

Thus, a major thesis in the OIE tradition is methodological collectivism or holism, i.e. the explanation of individual behaviour, action or intention in terms of social, structural or institutional phenomena. Therefore, in contrast to the NIE emphasis on methodological individualism, the OIE is replete with arguments indicating social forces or phenomena that are not a consequence of individualistic behaviour or that are not adequately linked to mechanisms involving individual decision making (Rutherford, *ibid*). As Langlois (1989) contends, the OIE view of methodological holism is established from the observation that individuals do not live in isolation but are influenced by the society in which they live.

However, the OIE School does not embody a single, well-defined body of thought or programme of research and has witnessed enormous criticisms. A widespread and prominent criticism especially from within the NIE camp is the former's lack of theory and overly descriptive methodology. According to Coase (1984) OIE is not theoretical but anti-theoretical. Coase's (*ibid*: 230) dismissive criticism of the OIE tradition is articulated in his statement:

*“Without a theory, they had nothing to pass on except a mass of descriptive material waiting for a theory, or a fire”.*

Coase (*ibid*) reiterates that the distinguishing feature of the NIE School is that they do not only speak about institutions but also employ standard economic theory to analyze the working of these institutions and to discover their influence on the operations of the economy. Similarly, Williamson (1998a) maintains that the difference between the older style institutionalism and the NIE School is that while the former was content with critique of orthodoxy and simple description, the latter affirms that institutions are susceptible to analysis. This emphasis on description and failure to advance a positive research agenda, he observed, led to the collapse of the OIE School.

Rutherford (2000) points out that OIE often appears incoherent, and a little more than a set of individual research programmes with nothing in common other than a questioning of more orthodox theory and method and a dissent from the latter. Thus, while the importance of institution in human interaction is not contentious as well as the lofty position of the OIE School in furnishing our knowledge of the significance of institution, the OIE School does not provide any concise and corroborative methodological or analytical approach for the empirical assessment of its research agenda.

## 5. Conclusion

In the history of the development of modern economic thought, three key schools are identifiable – neoclassicism, structuralism with its prominent Marxist variant and, institutionalism. These traditions of economic thought are also closely related to the four broad philosophical approaches to economic theorizing that are often employed within the social science and humanities, that is, empiricism, positivism, humanism and structuralism.

Without doubt, neoclassical economics represents the most dominant of these key schools of economic thought. Neoclassical economics is strongly grounded on positivist philosophy and places emphasis on empirical evidence, objective, descriptive and scientific methodological approach to solving a variety of practical and theoretical problems. This methodological approach is encapsulated in the neoclassicist hypothetico-deductive mode of enquiry which comprises a logical structure of arguments whereby statements about a phenomenon whose explanation is sought is deduced by deductive logic from a combination of a minimum of one universal law and a statement of relevant initial or boundary conditions (Hempel and Oppenheim, 1948).

However, criticisms of the neoclassical economics school's overdependence on formalism and mathematical modelling in part led to the rebirth, development and survival of rival and distinct schools of economic thought. One of such schools – Marxism, credited to the extensive 19<sup>th</sup> century writings of Karl Marx, is a socio-economic and socio-political view that borders on a materialistic conception of history. It is founded on four distinct and notable themes, that is, historical materialism, the mode of production, the theory of class or class conflict and the labour theory of value (Scott, 1991).

Marxism is a structuralist approach to economic theorizing which presents observed phenomena as



representations of underlying social structures whose base lies in the material conditions of existence and wherein the future is fashioned by past events according to specific laws of evolution (Johnston, 1986). Marx drew substantial inspiration from Hegel (1770-1831) and applied the latter's principle of dialectic to study the *mode of production* and understand the conflicting elements at work in the thesis, antithesis and eventual synthesis of the structure of capitalism.

Essentially, Marxism focuses on the conflict between the material forces of production particularly *labour power* and the distribution of ownership over the productive forces between different classes in the society. Therefore, central to Marxism is the analysis of the critical role of the economic structure of capitalist society and the contradictions inherent in it which constitutes the determinants of human consciousness and being. However, a distinct criticism of Marxism is the failure to adequately incorporate the role of institutions – a special type of social structure in its analysis.

Institutionalism or OIE represents a rich, albeit diverse and disparate school of economic thought which emerged largely out of a critique of mainstream orthodox assumptions. It refers to the tradition of economics closely associated with Thorstein Veblen, John R. Commons, Wesley Mitchell, and Clarence Ayres. While the OIE School does not embody a single, well-defined body of thought or programme of research, a major idea in the OIE tradition is methodological collectivism or holism. That is, the explanation of individual behaviour, action or intention in terms of social, structural or institutional phenomena (Rutherford, 1994). Langlois (1989) notes the OIE view of methodological holism is established from the observation that individuals do not live in isolation but are influenced by the society in which they live. Essentially, the School emphasizes analytical description or explanation of economic phenomena and takes a holistic and evolutionary view of economic issues (Rutherford, 2000, 2001; Hodgson, 2004a). While, a basic strength of the OIE School is that it provides the groundwork for highlighting the importance of institutions in human interaction and exchange, failure to advance a concise theoretical agenda and overly descriptive methodology are its major drawback. Thus, over the years, a younger school of institutionalism, that is, the NIE School has emerged from within the neoclassical economics tradition largely out of a critique of the atheoretical approach of the OIE School. In contrast to the latter, NIE employs standard economic theory to analyze the working of institutions and to discover the part they play in the operations of the economy.

Each of these schools of thought has their particular provisions, assumptions, philosophical underpinnings and limitations. Nevertheless, these traditions of economic thought have collectively enriched the study, prediction, analysis, explanation and scientific generalization about empirical regularities and economic phenomena. While each one may be more suitably applied in different contexts or particular circumstance, it is argued that approaches that emphasize social structures are as important as those that stress their economic equivalents in the study of human interaction and exchange. That is, for a holistic study and analysis of economic phenomena, the spatial, temporal and sectoral variations in human interaction and exchange dictates that approaches that emphasizes social character to the exclusion of the economic or vice versa might not be appropriate.

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This paper examines each of the key schools of economic thought that have been employed in the history of the development of modern economic theorizing, that is, Neoclassicism, Marxism and Institutionalism with a view to providing a better understanding of these traditions of economic thought. It highlights their basic provisions, philosophical underpinning, methodological approach and limitation in economic theorizing. This paper argues that each of these traditions of economic thought have collectively enriched the study, prediction, analysis, explanation and scientific generalization about empirical regularities and economic phenomena. Keywords: Neoclassicism; Marxism; Institutionalism, economic theorizing, history of economic thought. Against a Marxist, this puts an institutionalist at a disadvantage. Above all, Marxism has an impressive historical scope and a Page 2 powerful analysis of the capitalist system, which I think we should acknowledge as being relevant even today. However, while within institutionalism there is a lack of a consensus over a number of issues, I will try and draw out some unifying points. Both institutionalism and Marxism share this concern, and both schools of thought see agency and structure as irreducible to one another. They are both against the extreme positions, where everything becomes explicable simply in terms of structure, or simply in terms of individuals. (Although some institutionalists and some Marxists have sometimes veered too much towards one or other of these extremes.) Neoclassicism, Marxism, Institutionalism: Revisiting the broad schools of economic thought. A. O. Agboola, Aderemi Olofa, A. Odebode. Sociology. Comparative Economic Organization: The Analysis of Discrete Structural Alternatives. O. Williamson. Economics. Contending Economic Theories book. Read 22 reviews from the world's largest community for readers. A systematic comparison of the three major economic th... Besides the broad comparison of the three major corpus, the book also offers a chapter to explain late neoclassical theorie(s), including game theory, evolutionary theory, social effects of capitalism and behavioral economics. A book that shines on the shelves of economic literature given its interesting and unique approach. ...more. A surprisingly dense book on three of the major schools of economic thought. Took me a very long time to work through it, as it is most definitely academic in tone and therefore not at all a light read. That being said, worth the time investment 100%. Marxist economics is generally seen as belonging to a time long since passed, where fat cat businessmen smoked cigars and wore top hats while cloth cap workers slaved away in dangerous factories for miserable wages that left them living in slums. Here Robert Nielsen explains the various economic schools in a concise and accessible way. If you watch the news on telly, you would be forgiven for thinking there is only one valid economic theory and that theory is the one much loved by the Right and Nu Labour. Well, guess what? It isn't.