

Towards a quasi-Lamarckian theory of institutional change

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Abstract

The paper emphasises two flaws in mainstream economics: the failure to understand human behaviour and the belittling of transaction costs. By stressing the role of knowledge, institutions and path dependence, new institutional economics has provided a powerful answer to these shortcomings. Nevertheless, a number of questions remain open. In particular, path dependence is far from being a continuous process. Its dynamics and its irregularities are by and large unexplained. Hence, a strong need for a convincing evolutionary theory of environmental change.

This paper does not deny the validity of the Darwinian view applied to the theory of the firm and of competition in a free-market economy. It is however maintained that the natural-selection process that characterises the Darwinian approach is ill suited to describe economic evolutionary processes. It is shown that a combination of functional analysis and natural selection may indeed be a better solution, for it solves some of the puzzles raised by the public choice school without violating the fundamental tenets of the neo-institutional approach. Still, although this combined view may well explain why the institutional features are retained by the system, it does not clarify why they are introduced in the first place.

A third possibility is thus put forward in the second part of the paper, where a new evolutionary theory is suggested. Within this framework, agents are assumed to behave according to their preferences within the existing rules of the game. At the same time, new ideas and sometimes new ideologies may influence their behavioural patterns. The combination between needs and ideologies generates environmental change, especially if so-called “ideological entrepreneurs” are able to transform latent and shared beliefs into an institutional project and enforce it.

Towards a quasi-Lamarckian theory of institutional change

1. Flaws in mainstream economics

If one were to define the major event that has characterized economic science during the past twenty years, many would probably refer to the crisis of the mainstream perspective. Despite increasingly sophisticated attempts to model agents' behaviour within exogenous institutional frameworks, so as to come to terms with apparently puzzling phenomena of the real world, exercises in optimization and policy engineering have lost much of their appeal. Instead, the dynamics of institutions has continued to acquire an increasingly important role as the key-issue of economic analysis. And of course, the evolutionary analysis of property right systems has been accepted to a larger and larger degree as the essential tool of economic investigation. Even well-known champions of past conventional views, such as the IMF or the World Bank, admittedly slow at abandoning constructivist policy making, have shown little contrition in trying to build up a new facade and even taking the lead in "applied" institutional economics, albeit with some inflection towards social masterminding.

There is no need to recall that the inadequacies of the traditional pattern became particularly evident after its failure to understand development and transition, to explain technological change, let alone comprehend the business cycle. The orthodox misfortunes in these areas are well known and very little disputed. Nevertheless, the deep weaknesses of the old view are perhaps better appreciated by referring to two conceptual flaws, which still affect current controversies and may explain why bad habits are so hard to die¹. The first of such flaws concerns the understanding of human behavior; the second refers to the nature of transaction costs. The remaining part of this section briefly discusses the nature and implications of these two issues, whereas the rest of the paper tries to draw some lessons from the orthodox failures in order to develop insights towards a new theory of institutional change.

¹ Among such bad habits one may recall the strong and sometimes very authoritative support for restrictions on capital movements, banking regulation, anti-trust intervention, enhanced harmonization in many areas of the economic activity. More generally, attempts to impose top-down legislation are on the rise, as the ongoing EU "Constitutional Experience" confirms.

1.1 Human behaviour and ethical principles

Mainstream economic investigation has usually treated agents as if they were optimizing machines, thereby neglecting thorough analysis of how human beings actually behave. Emotions, culture, ideologies, lack of time, poor information, ever changing budget constraints have often been considered a nuisance, rather than the core economic question. This led of course to bad scholarship, for economic action is far from being a mechanical decision-making process. And it also warranted the false belief that economics can do without clearly defined ethical fundamentals, such as those provided by the principle of self-responsibility and thus individual liberty; leading to the respect and enforcement of voluntary exchange. As a consequence, it is hardly surprising that self-conscious technocrats have been feeling justified in putting forward allegedly amoral proposals, with the purpose of securing more or less arbitrary policy goals disguised in terms of social efficiency. Although for entirely different reasons, they were successful; since the diffusion and persistence of state or super-state intervention in modern societies has met only occasional resistance.

Equally important, this view induced too many observers to concentrate on the wrong issues. Since individuals try to enhance their welfare by reducing scarcity and expanding choice², one should expect research to concentrate on how to create suitable conditions for growth, and opportunities to choose. Unfortunately, this is hardly what the very many exercises in model building have done when indulging in the description of fictitious agents in a static world. In particular, from a normative viewpoint the mainstream view has led to the dangerous illusion of economics being concerned with social systems dedicated to the creation of measurable wealth, forgetting about individuals pursuing their own preferences. The purpose of traditional economic investigation has thus become the study material growth *per se*, rather than freedom to choose and to act³. Given the stock of knowledge and resources, one has been far too ready to accept that if

² It is of course true that most individuals behave so as to enhance their satisfaction, given past mistakes, expectations about present and future circumstances, possible changes in preferences. But these efforts to improve one's own living conditions are by all means a different and much wider notion than that featured by a maximizing machine.

³ Ironically, no growth theory has been developed, though. Exogenous growth approaches are about residuals, the nature of which changes according to the various versions of this theory. Whereas endogenous growth visions assume that the acquisition of knowledge increases with past knowledge and/or investment. But the acquisition of knowledge requires of course time and effort. And these theories fail to explain why individuals are induced to spend

more collective wealth or higher efficiency could be attained by disrupting the otherwise spontaneous state of affairs, then interference is not only admissible, but even desirable. The lack of explicit approval on the part of the individual plays a minor role.

1.2 Transaction costs and institutional change

The second fault with established economics lies with the unsatisfactory treatment of transaction costs, i.e. the "costs associated with the transfer, capture and protection of rights" (Barzel, 1997). By ignoring such costs and/or misreading their role, orthodox economists have ended up by fully appreciating the nature of the market system. The analysis of the ideal features of a perfectly functioning world populated by imperfect individuals - the so-called Nirvana (planned) economy - has overshadowed the questions raised by illegitimate and defective rules of the game. In the end, undesirable outcomes have been interpreted as market failures, rather than institutional shortcomings.

The recent emphasis on institutions has fortunately encouraged the economic profession to reassess and appreciate the importance of transaction costs in all their implications. To various degrees, most economists today acknowledge that the reduction of economic and political transaction costs are the basis of all efforts to reduce the scarcity constraint and thus enhance personal well-being. Put differently, the link between knowledge, transaction cost and institutions is no longer questioned.

As a result, in a free society individuals discover and agree on enforcing the rules of the game that ease the acquisition of knowledge, including the expansion of cooperation. That is, property rights evolve in order to reduce transaction costs. On the contrary, in societies that deviate from the principles of individual freedom, activities are bound to be driven by two different dynamics. Those who fear to be victims of coercion are likely to allocate their efforts and resources in order to escape violence, for the fruits of enhanced knowledge cannot be fully appropriated. While those who expect to benefit from the exercise of violence try to develop knowledge in order to increase the returns to violence, enhance their use of it, and develop cooperation accordingly. It follows that in societies where economic freedom is limited property-right assignments tend to

time and energies to this purpose; and why they often decide not to.

become the object of a bargaining process driven by interest groups and by expectations about future rent-seeking opportunities. The rules of such a bargaining process will of course be affected by the power and composition of the different organizations, and thus by the dynamics of individual freedom (or lack of it).

Economic history is normally understood as the evolution of such rules following various path-dependent processes (North 1990, 1994). At one extreme one can imagine a free society, where individuals continuously revise the institutional framework in the light of the new technologies available, so as to reduce transaction costs. In turn, the new rules of the game ease the acquisition of new knowledge and the application of innovative technologies; while lower transaction costs enhance cooperation and welfare. At the opposite extreme, the incentives to acquire knowledge become weaker and weaker in societies with limited economic freedom. And institutional evolution may even lead to higher transaction costs, if by doing so (a) the dominant coalitions believe they can increase their rents, or (b) the victims succeed in raising the cost of being exploited.

Nobody would dispute that much of the real world is actually far away from both extremes. But relatively little attention has been devoted to the nature of the path-dependence processes that have departed from the principle of unconstrained freedom and have led to the intermediate cases⁴. Starting from Quigley (1961) valuable contributions have forcefully described why and when civilizations or societies have prospered or declined by analyzing the interplay between economic performance, political organizations and institutional evolution. Nevertheless, the origins and the evolutionary rules of institutional dynamics remain unexplained. Although we know that change can be affected by accidents and path-dependent processes, it is still unclear why and when shocks have a lasting impact, why and when a path-dependent process may be deviated or lose its impetus and eventually die out. In this perspective, section 2. questions the institutional and public-choice approaches to the evolutionary process. Section 3. looks at the possibility of analyzing institutional evolution from a Darwinian viewpoint and concludes by suggesting instead a Lamarckian interpretation. Section 4. examines some of the ensuing implications, while the final paragraph sum up the main results.

⁴ Among the exceptions, see de Jasay (1985).

2. On the economics of institutional change

Institutional economics posits that agents behave by following their preferences (income, profits, leisure, power, etc.). Such behavior is affected by property rights, which in turn are established and enforced as a result of the interaction among individuals or groups of individuals involved in activities of economic relevance. Institutions provide the broad guidelines within which new assignments may be conceived and effected. It follows that the agents' ability to create new property-right structures depends on the existing rules of the game (institutions).

Consistent with the old institutional approach (Veblen, 1898), it is usually accepted that the rules of the game constrain agents in the short run. In the long run, however, agents may and do affect institutions⁵. This is generally perceived as a gradual process, whereby informal institutions, which incorporate deeply rooted and widely shared cultural values, are gradually transformed into the formal rules of the game. As a consequence, the ideal timing of institutional change should not be much different from that of cultural change, or from the dynamics of commonly perceived needs. That is usually slow, as much of the neo-institutional literature reminds us. When differences become significant the dichotomy between formal and informal rules generates uncertainty, frictions and also opportunities for illegal activities⁶. Economic instability and political turbulence are almost inevitable.

There are two rather *ad hoc* exceptions to this general claim: "institutional shocks" and "representational redescriptions". They both account for interruptions of the path-dependent processes and differ according to what happens after the interruption. The former applies to interruptions after which a new path dependent process sets in. The latter to pauses, after which the

⁵ This is known as "institutional hysteresis". See Setterfield (1993), who suggests a synthesis between the old and the new institutionalist schools.

⁶ See Pejovich (1999) for a in-depth analysis. Fiori (2002) on the other hand draws attention to the problem of defining informal rules in a world of rapid change, where individuals experience the "acceleration of time". Although these are unquestionably crucial issues, their implications are of less relevance to this very section and will be discussed at a later stage.

process resumes.

In particular, institutional shocks refer to those historical moments when institutions undergo a radical change, generally after a violent event (like a war). Of course a shock may describe why the context after the shock is different from before the shock. But explains neither why, nor the causal process which led to shock.

The representational-redescription hypothesis assumes that individuals reassess their mental habits only once in a while. Behavioral patterns are therefore altered only when the new habits are completely acquired⁷, so that changes occur only once in a while. This is not quite the same as a shock, but it explains why path dependence is not necessarily a smooth process. It is still consistent with the idea whereby institutional change is ultimately the result of gradual cultural evolution. But it argues that change appears to be irregular, as it depends on the features and frequency of representational redescriptions.

Not unlike the institutional-shock idea, however, the representational-redescriptions view is also vulnerable to critique. First, it provides a new description of institutional change, but no explanation: that is, there is no attempt to reveal why and when mental habits are altered⁸. Second, it is still inconsistent with a large body of empirical evidence. In fact, institutional change is usually the product of elites, rather than of a spontaneous bottom-up process whereby new individual behavioral patterns lead to new rules of the game. Indeed, one may even argue that the introduction of the new habits is far from spontaneous. Otherwise it would be hard to explain why interest groups and intellectuals make so many efforts to influence public opinion.

2.1 Rent-seeking and the public-choice view of path dependence

Despite the shortcomings mentioned earlier, path dependence is currently the major explanation - or, according to the argument of this paper, the most popular description - of institutional change. It is also commonly accepted that path dependence is driven both by the efforts to create and exploit rents, and by the opportunities to reduce transaction costs and thus raise efficiency. According to the public-choice approach the first mechanism dominates, whereas institutionalists are less

⁷ See Denzau and North (1994) and, more generally, the survey offered by Fiori (2002).

⁸ Among others, Hirshleifer (1977 at 17) made the same point when criticizing modern neoclassical economics.

pessimistic, but vague. Assessing under which conditions the former set of effects prevails upon the other (or viceversa), and how they interact, remains an open question.

Still, even if one accepts the standard view, the relationship between institutional change and rent-seeking activities is not entirely satisfactory. Rents can be already in place as a result of the normative process within the existing institutional context; or they can be an option for the future, especially if potential rents seem to be more or less compatible with the current rules of the game. In both cases, however, interest groups do not fight so much in order to change the rules of the game, but rather to create and appropriate rents within a given institutional framework. This is understandable, since altering institutions can be too expensive or simply counterproductive. In democratic settings small interest groups would be easily resisted by public opinion, whereas encompassing coalitions would have limited interest in expanding rent-seeking beyond a relatively low threshold. On the other hand, in totalitarian environments the incumbent coalitions are already in control of the law-making process, and therefore have no need to change the rules that allow them to exercise almost unlimited discretionary power.

Once again, according to the traditional view the customary aim of pressure groups is not to change institutions, but to exploit the opportunities for rent-seeking. Hence, within a weak institutional setting - i.e. one where property rights can be more or less arbitrarily re-assigned through the legislative process - the fight for rents and privileges will be intense. And the chances to further encroach upon the rule of law will be greater.

In a word, according to the public choice viewpoint, interest groups are to be held responsible for most institutional failures. In particular, property rights fail to be assigned on purpose, so as to elicit demand for bureaucratic regulation. Or they are assigned inefficiently, because the purpose is to favour or protect interest groups, rather than to reduce transaction costs. One way or another institutions are bound to weaken more or less quickly under the pressure of the dominant interest groups. Speed turns out to be a matter of economic or historical accident.

2.2 The case for legitimate rent-seeking

Although this view may have some explanatory power under specific conditions, it is not very satisfactory as a general theory. On the one hand, it does not stand the test of history. Property rights have frequently evolved so as to reduce transaction costs. Rents have often been restrained and even

destroyed through institutional competition and/or freedom to move. Violence was not necessarily part of the process. One may surely claim that institutional changes across countries have been affected by rent-seeking games. Nevertheless, the historical pattern has been characterized by steadily decreasing rents, rather than by drifts favoring coalitions interrupted by war events. Moreover, and contrary to the Olsonian view, it is a fact that violent conflicts have often strengthened the incumbent coalitions already in place, rather than weakening them. More important, the public choice approach seems to overlook two important issues, which are the keys to understanding institutional change.

First, rent-seeking coalitions are not always an attack on individual freedom. Their rents may be perceived as legitimate and even desirable. For instance, until the end of the XVIIth century that was certainly the case with Guilds, whereby secrecy, restricted access and exit provided an acceptable substitute for hard to enforce rights on intellectual property in large parts of the world. In less remote times agricultural subsidies and state education to the benefit of selected groups (inefficient farmers and lazy or incompetent teachers, respectively) have enjoyed widespread support in many developed countries, despite their obvious harm to taxpayers' purchasing power. The very fact that the public agrees to subsidize farmers and teachers through general taxation does not mean that the institutional framework has deteriorated. Rather that it has evolved to suit prevailing preferences.

The second point is that the public choice pattern blurs the distinction between individual and coalition behaviour. At first sight it seems plausible to assume that the main character responsible for institutional dynamics is the group, i.e. a set of individuals sharing the same goal. After all, groups, rather than individuals, drive the law-making process. This would also be consistent with the widely studied phenomenon of indifference and disaffection *vis-à-vis* politics in general and elections in particular.

However, modern societies are formed by individuals who try to enhance their satisfaction by pursuing multiple and sometimes conflicting targets at the same time. And such targets need not be constant, of course. Three factors account for this and they all point out to the serious need to reappraise the traditional notion of interest group. One is the fact that today individual long-term planning entails smaller sunk costs than in the past. Hence, the cost of transition from one coalition to the other has decreased. Job mobility across industries has increased continuously thanks to

mechanization and - more recently - computer-operated production processes. The loss of comparative advantage does not necessarily imply long-term, structural unemployment to the same extent as fifty years ago or more, for workers can move from one industry to another with little change in the required skills, as long as they keep abreast of the changing technological requirements⁹. This phenomenon has certainly gained momentum in the very last decades, with important consequences.

Second, and contrary to the past, the notion of individual well-being in developed countries has expanded considerably. Until the end of the XIXth century (and perhaps until the end of World War II in much of Continental Europe) freedom from need was the prevalent concern of individuals: physical security, satisfactory caloric intake and access to basic health were the major concerns of vast layers of the populations. Today, most of our working efforts serve our desire and capacity to enjoy leisure, both from a hedonistic and from an intellectual viewpoint. More so than in the past, it is now our *Weltanschauung* that bears upon our sense of belonging to one or more interest groups; not only monetary returns.

This leads to the third element, which affects the very cohesion and dynamics of a group in modern society. The ability of interest groups to acquire rents tends to increase with the skill to invest resources into industries before the property right structure has been affected through the law-making process. It is obvious that buying a rent after it has been created is likely to be much more expensive than buying the property rights to unforeseen rents. Capital mobility and, more generally, a reduced role for sunk costs in the production process account for this widening gap between the *ex-ante* and the *ex-post* price of the privilege. Hence, effective coalitions are no longer kept together by common interests connected with - and reinforced by - past history and sunk costs, say acquired skills or market power. Instead, interest groups are formed and strengthened by informal rules based on mutual trust, which have been consolidated through repeated games (experience). Member-homogeneity requirements are thus losing grounds to trust and personal ties. And these last elements are highly dependent on what is usually defined as the ability to cooperate,

⁹ On the contrary, globalization has shown that the crucial challenge facing workers today is intra-firm mobility. Trade liberalization has not really changed the structure of comparative advantage as regards industries, but rather as regards the market segment and the stage of production of the firm within the industry. The capacity to qualify for upgrading in skills and to accept at least temporary cuts in the wage rates are the only ways to avoid structural unemployment. Hence, the winning systems are going to be those that will accommodate these new needs faster.

on ethical standards and beliefs as predictors of future behaviour, on emotions. Resilience and commitment to the group are the keywords to lead organizations, whereas teamwork and expected loyalty are the keywords to operate within an organization.

Put differently, it is here maintained that most of the public choice school is referring to - and trying to explain - a world that is no longer the one we are living in. The traditional notion of coalition as an operational device may be obsolete. If so, the public choice pattern is still acceptable from a descriptive viewpoint, but much less valuable for explanatory purposes.

3. A Lamarckian theory of institutional dynamics

The institutional approach and the neo-Austrian School¹⁰ deserve ample credit for having relentlessly emphasized the interplay of institutions and organizations as an essential element to understand individual behaviour and ultimately economic growth. It has thus been possible to overcome the rather simplistic claim maintained by mainstream scholarship, whereby optimization processes drive individuals and growth is to be explained by the accumulation of capital. At last, the fulfillment of Veblen's hopes for the future of economic science seems to be within reach (Veblen, 1898: 376-378).

Nevertheless, as underlined in the discussion so far, economic theory is still unable to put forward consistent and self-contained general evolutionary principles, which do without historical accidents or individual search routines similar to random walks¹¹. Surely, exogenous shocks or the occasional acquisition of knowledge should not be overlooked, for they may indeed play a substantial role in selecting path-dependent processes or enhancing new organizational structures. However, if one tries to explain evolutionary processes by relying heavily on accidental events, one is not really developing or applying an evolutionary theory, but rather working in a context similar enough to historicism, and be likely to be confronted with the same limitations met by Ranke some

¹⁰ The prefix "neo" is intended to emphasize the break provoked by the contributions of Mises (1949, Part I) and Hayek (195X). As early as the 1920s they had started to consider the individual as an agent open to intrinsic changes following outside stimuli, as opposed to - say - Carl Menger and the first generations of Austrian economists, who were reluctant to abandon a hedonistic account of subjective behaviour.

¹¹ See for instance Hirshleifer (1977) and Matthews (1984), especially at 113. At a firm level the best known contribution is of course Nelson and Winter (1982).

150 years ago. Put differently, the search for historical continuity within time periods limited by accidents is a description of the evolutionary question, rather than an attempt to give a satisfactory explanation. In short, there remains a strong need for a persuasive theory to explain how a process evolves in the absence of a shock; upon which conditions and in which way a shock can affect an existing evolutionary process.

Alchian (1950) had already shown that decisive insights into the economic behavior of agents could be obtained by regarding economics as the human branch of sociobiology. More recently, Vromen (1995) has drawn attention to the role of the Darwinian approach, both in its pure version (natural selection) and in its best-known variant (adaptive learning), and offered an interesting synthesis to be applied to microeconomic analyses. The following paragraphs do not discuss the validity of the Darwinian view when applied to the theory of the firm and of the competitive process in a free-market economy. Instead, they try to show that the same view cannot be employed to explain environmental change without falling into the traps discussed earlier on. A new theory will therefore be suggested.

3.1 The Darwin-Wallace approach

Darwinian natural selection is based on the unintentional, more or less successful transmission of genes to subsequent generations. Selection depends on how the phenotypes (i.e. behavioral features and patterns embedded in the genes) respond to the environmental conditions, so that the genes associated with the most suitable phenotypes have a higher probability of being transmitted to future generations. The selection process is concluded when the relevant agents acquire a stable set of genes and therefore show constant and predictable behavioural patterns. Minor shocks (mutations, in the Darwinian vocabulary) play a secondary role and eventually die out. Almost by definition, they are unable to eclipse the current reproductive process¹². Their interference with the

¹² Temporary changes in the phenotypes may occur and are explicitly mentioned in Darwinian theories. In particular, the so-called neo-Darwinians maintain that mutants do affect phenotypes. Mutants cannot be inherited, though; because they are not taken into account by the replicators (genes as carriers of features from one generation to the other).

Hence, mutants may generate cyclical behaviours, following the life of the temporary phenotypes, each of them lasting no more than one generation. But since these minor shocks have no consequences for the replication process, stationary processes (path dependence) are observed.

incumbent behavioural patterns is therefore limited in time, and depends on the outside conditions (the environment), which is in turn defined in terms of structural shocks.

Structural changes tend to be ignored by natural scientists, who are more interested in studying how the species react to environmental changes. This is of course acceptable from a methodological viewpoint, for their work emphasizes the process itself, rather than the origin of the process. Such neglect becomes however embarrassing in the domain of economics, where agents' behaviour can hardly be considered to be independent of the environment¹³ and the causality mechanisms are crucial.

Put differently, the (neo-)Darwinian frame is indeed a workable premise to study mainstream issues in comparative-dynamics contexts, where the environment can be taken for granted and the emphasis is on comparing equilibria - whatever that means in economics - in various environmental situations. There is nothing new about this. Although from different perspectives, neoclassical economics (after Marshall) and Austrian economics (before Mises) had already provided the typical research programs consistent with the Darwinian boundaries, whereby voluntary action is almost completely ruled out. Agents behave like machines or hedonistic creatures, so that they are suitable to a natural-selection approach. In particular, no social explanation beyond path dependence is required, since agents turn out to be the object of a mechanical process ruled by what could be defined as social genes, outside conscious human control. And it is hardly worth mentioning that in this light natural selection also justifies exercises in forecasting, simulation and, more generally, policies designed to "invade" the social organism, should the incumbent path-dependent process (driven by natural selection) appear to be heading towards undesirable results. Similarly, attempts to smooth or accelerate the natural process may instead be encouraged, should the outcome of the process be deemed desirable.

3.2 Neo-Darwinian functional analysis

One can imagine two possibilities of overcoming the objections raised by the application of

¹³ Put differently, in the social sciences natural selection should no longer apply to the organism, but to the environment. And contrary to biology, Darwinian equilibria make little sense in economics. Since there is no doubt that Walrasian equilibria are pure fantasy and that the driving force of agents' behavior is indeed the discovery and exploitation of disequilibria.

Darwinism to the social sciences - and economics in particular. This paragraph deals with the first, which borrows heavily from functionalism. While the analysis of the second objection is developed 3.3 and leads to ideas closer to the Lamarckian view.

As pointed out earlier on, the natural-selection mechanism is appealing from a neo-institutional viewpoint, because it provides powerful support to the path-dependence hypothesis. Still, it is vulnerable as a plausible operational principle *per se*, when applied to any social science, including economics. In another context Elster¹⁴ observed that the critique put forward at the beginning of section 3. may be overcome if natural selection is no longer understood to be the driving force of an evolutionary process, but it is interpreted as a way to check the features of a functional process; the latter being the true engine of the evolution of the rules of the game. As will be shown shortly, and if plausible, this proposed (neo)Darwinian functional perspective might actually kill two birds with one stone. It would provide an alternative to the neoclassical and proto-Austrian projects. And it would also answer some problems typical of the public choice literature without questioning the basic tenets of neo-institutional economics.

To this purpose, let us recall the two environmental levels mentioned in these pages: the institutions *stricto sensu* (the rules of the game that constrain the law-making process) and the features of the different property-right assignments - including enforcement - that can be observed within a given institutional framework. Now, according to a functional interpretation of the institutional evolutionary process, property rights may be understood to be assigned so as to fulfill the targets pursued by the rent-seeking interest groups. And institutions develop in order to achieve and secure results after the natural selection process has confirmed that the results obtained are close enough to expectations. In other words, Darwinian-integrated functional evolution takes place according to what could be defined a random walk with a drift, characterized by ratchet effects. The drift originates from the functional elements. The ratchet effect reflects the (natural) selection mechanism that secures intermediate results and rules out regressions. While the random walk describes the search for appropriate rent-seeking arrangements.

Within this context, occasional external influences can be regarded as being the effect of mutants. Although they affect outcomes, they do not interfere with the fundamental behavioural

¹⁴ Quoted in Vromen (1995, ch.5).

patterns. For the replicators are assumed to transmit only the elements that are consistent with the target of the coalition, and neglect accidental conduct. Put differently, selection progresses in an environment that depends on a rent-seeking functional mechanism, as described by the public-choice approach.

To sum up, the evolutionary rendering of the public-choice approach implies that societies are led by a relatively small number of interest groups driven by rent-seeking purposes. Interest groups are kept together on mutual trust and repeated interaction, rather than common industrial interests¹⁵. Each coalition experiments different strategies and tactics in order to create and exploit rents within a given institutional framework. Since information is incomplete and uncertainty cannot be eliminated, the blind-search efforts are sometimes successful, sometimes ineffective or possibly counterproductive. This may lead to unexpected modifications in the agents' behaviour, especially as far as the victims of the rent-seeking game are concerned. Their reactions may take different forms: revolution, migration, innovation, structural changes¹⁶. Natural selection provides the rent-seeking groups with signals about the *ex post* (functional) desirability of their action. If rents are perceived to be high enough, then property rights stabilize and so do institutions. If not, the search goes further on and is carried out in part by the previous coalitions, in part by those which have been able to come to the surface as a consequence of the natural-selection process. It follows that the target of the coalitions and the very balance of power among the various interest groups may change through time. And one can plausibly claim that the natural selection process turns up to be responsible both for the definition of the feasible (lasting) rents and possibly for environmental change, too.

Surely this does not mean that the evolutionary process becomes self-contained or fully endogenized. Indeed, the outcomes of the discovery process can hardly be predicted, as the very nature of the human being suggests and as we know from observation of the real world. Nevertheless, this theoretical framework allows to speculate when efforts to acquire new knowledge may be greater, when pressure to choose with one's own feet is more intense, and when rent-seeking efforts are likely to be more (or less) successful.

¹⁵ See the argument put forward at the end of section 2.2.

¹⁶ This term usually refers to a variety of phenomena, the most important of which are the migration from one industry to another, (de)urbanization, lower propensity to work, illegal activities.

There is no doubt that this functional approach, which has been here integrated by a neo-Darwinian selection mechanism, satisfies mainstream requirements in at least two respects. First, it is consistent with optimization strategies (e.g. constrained rent-maximization); and its outcomes are subject to formal modeling, especially if the result of the discovery process is conceived as a probability distribution, subject to suitably specified environmental variables. In addition, institutional developments are also consistent with the public-choice paradigm, since the rent-seeking groups remain the driving forces behind the rules of the game.

The difference between this view and that presented in paragraph 3.1 is straightforward. From a Darwinian perspective, evolution was more or less a linear process outside human control, driven by the given environment towards an inescapable equilibrium situation. On the other hand, in this latter case, evolution takes shape as a discontinuous process subject to interference by rent-seekers. Institutions evolve in order to lock in the outcomes deemed to be desirable by the rent-seekers themselves. In particular, and contrary to a Darwinian view, no pre-defined social target can be identified. There is however a pre-defined process, whereby property rights are upheld if they serve the interests of the dominant coalitions, discarded otherwise.

Although appealing to many neo-institutional economists, this functional neo-Darwinian attempt to interpret evolution still suffers from one major weakness. For this enhanced functional theory does explain why institutional features are retained by the system, but does not clarify why they are introduced in the first place. In contrast with its biological version, it would be hard to figure out a teleological engine role for social functionalism. From a subjectivist viewpoint there is no doubt that individuals hardly know what they are aiming at, apart from satisficing, which would not be a very useful notion from this viewpoint. As mentioned earlier on, much of our economic activity outside consolidated routines refers to the application and discovery of new knowledge. The outcome of this process remains however by and large uncertain. Hence, a teleological version of economic functionalism does not seem to reflect individual behavior. Similarly, if one accepts the theory about interest-group formation and activity put forward in section 2.2, it appears that teleological functionalism does not apply to coalitions, either. For it does not explain how interest groups get together and how their targets are selected.

In the end, it is not surprising that the environment changes by accident, as a result of the mistakes made by the incumbent coalitions. This amounts however to some kind of a residual

answer. If so, this underscores our ignorance of the evolutionary process, rather than our knowledge. Not to mention the fact that this thesis runs against historical experience. Although with the benefit of hindsight, it would be very hard to claim that history has developed according to accidents and mistakes. These may have played a role in determining the exact moment of change, or the leaders of change. But it would nevertheless be very hard to claim that history is just a sequence of accidental mistakes.

3.3 A quasi-Lamarckian approach

The Lamarckian stance differs from natural selection in that economic agents may modify their features (phenotypes) during their lifetime as a consequence of outside stimuli. And at least some of the new features can then be transmitted genetically¹⁷. It is worth mentioning, however, that in this context transmission regards processes (behaviours) more than outcomes. Put differently, from the evolutionary viewpoint upheld here what matters is the way agents behave (processes) rather than the outcomes of their action. Actions are of course important when evaluating the behavioural processes and their consistency with the so-called maximizing principle. Thus, results are unquestionably the main object of the transfer of information. But the object of the evolutionary process as commonly understood is about decision-making criteria and constraints, rather than about the representation of sets of outcomes¹⁸. Indeed, institutions are not designed to deliver pre-defined results, but to allow people to look for and develop behavioural patterns that may lead them

¹⁷ To be precise, the environment does not play a meaningful role in the strictest version of Lamarckism, whereby organisms acquire their new phenotypes following some built-in drive towards perfection. The environment becomes however more relevant in neo-Lamarckism, according to which the environment forces the organism to adapt. For the sake of simplicity we shall keep referring to Lamarckism, even when the use of the prefix "neo" would be more appropriate.

According to the orthodox Lamarckian view genetic transmission is ruled by the use/disuse of the organ by the agent. On the contrary, from the viewpoint presented here use/disuse implies more or less successful transmission of a cultural heritage. It creates or weakens inertia through memory. Disuse cancels memory only in the very long run, though; and organs are not altogether destroyed. As a consequence, old behavioural patterns can be retrieved with relative ease, as long as their memory persists.

Furthermore, it is not necessarily true that repeated use reinforces the organ, as Lamarck would have argued. Rather, it is here claimed that within a social framework repeated use does contribute to inertia, but may also lead to decay and increased rigidity *vis-à-vis* external modifications. This two deviations account for the qualifications ("quasi") in the title of the paper and of the present paragraph.

¹⁸ This differs of course from the functionalist approach, which focuses on results, since natural selection takes place with reference with the suitability of the outcomes compared with the goals to be attained.

to hoped-for, frequently ill-defined results.

In turn, accessible technologies, ideologies, culture, habits influence decision-making criteria. Although culture and habits depend heavily on shared moral values and evolve slowly, ideologies may be introduced much more quickly. Therefore, and contrary to the neo-institutional tenet, whereby tensions are provoked by fractures between formal and informal rules of the game, here the strains are assumed to take place because of ideological breaks and their different impact on different groups of people. For instance, in societies where internal mobility is limited individuals react according to classes, possibly to industries or to input factors (e.g. industrial workers opposing landowners). Where mobility is greater - as is the case in most of today's developed world - tensions arise also according to the different permeability of the various generations to novelty. Hence, one would predict that in societies where youth leave the family earlier, the young generations are more inclined to accept new environmental proposals - but also quicker to abandon them and fall back on the previous institutional arrangement. Whereas in communities characterized by stronger interpersonal bonds (extended families) the new proposals may find it harder to break through, since change presumes shared consensus. But then it leads to deeper ratchet effects, for the whole system of interpersonal relationships is affected more or less permanently and reversals are therefore more difficult to occur.

Put differently, the evolutionary path takes the following steps. Given the technology, agents behave according to their preferences within the existing rules of the game, both individually and as members of coalitions. At the same time, they continuously undergo more or less clearly-perceived stimuli that might lead them to change their preferences and their behavioural processes: new ideas and sometimes new ideologies, or moral suggestions perceived as new ideologies. The rate of success of the allegedly new ideologies depends on their ability to meet latent needs and justify action without soliciting unbearable opposition. It often happens that the same ideological motion affects different strata of the population for different reasons; or that the new elites consider a shared ideology a suitable means to acquire power. Whatever their motivation, the institutional environment changes - if it does change - according to the nature of the combination between needs and ideologies.

In fact most of the times such stimuli are ineffectual. But when they fall upon a particular

combination of attitudes characterized by widespread dissatisfaction¹⁹, they generate substantial environmental change. Two elements are thus worth stressing. On the one hand the effectiveness of what could be named "ideological entrepreneurship", that is the ability to transform latent and shared beliefs into an institutional project and possibly enforce it. Hence, leaders matter; and so do failed leaders, for the opposite reason. On the other hand, it should be recalled that the nature of dissatisfaction changes over time as well as across regions. For instance, at times and areas where civil war is more likely, totalitarian projects have a higher probability to succeed, even if the prospects for income growth can be severely damaged. And at times where income growth has been faster and less homogeneous, envy intensifies and a new system based on state welfare principles and redistribution become acceptable; even to the "rich", whose main problem is not to be the object of envious sentiments (Schoeck, 1966). Of course, all this does not allow any precise prediction about environmental change. But it does offer an explanation, rather than just a sheer description.

From the viewpoint of institutional evolution, two sets of implications follow. At the higher level, institutional change (i.e. the evolution of the overall environment, excluding the technological features) becomes dependent on the development of individual phenotypes, which are in turn influenced by ideologies and expectations. By and large, when a system delivers in accordance to expectations (e.g. in terms of GDP growth, employment, opportunities, political freedom, personal ambitions to attain power), the incumbent institutional framework strengthens and competing ideologies find it harder to create new powerful and widely shared phenotypes. On the other hand, when the system does not meet expectations or needs, new ideas have a better chance to make an impact and create more room for new property-right assignments. Whether these new assignments are actually enforced and whether they affect the system in a direction conducive to enhance individual well-being is of course another matter.

Therefore, formal institutions do not change as a direct consequence of informal rules or rent-seeking pressures, but rather according to the shared ideological tenets. These tenets may well be the result of coalitions' pressure and have to be compatible with the cultural heritage of the population. That is, informal institutions are more like a constraint than as a cause. And rent-

¹⁹ As Schoeck already made clear in his work (1966), envy also plays an important role, perhaps even dominant.

seeking actions are no longer the prime cause of institutional evolution. By pursuing this line of reasoning one can also note the difference between the quasi-Lamarckian evolutionary theory and the neo-institutional position as regards intentionality, which characterizes the latter²⁰, but not Lamarckism. From this perspective the supporters of intentionality maintain that individual and groups display some kind of (bounded) rational behaviour, so that they systematically search for the institutions which best serve their purposes; and ideologies, if at all, make an impact only when they justify a given institutional environment. Not surprisingly, this rings a functionalist bell again. As aired earlier on, the viewpoint proposed here suggests that the institutional environment does not change according to a specified goal. Individuals may have (vaguely defined) goals, but not society, for there is no basis for saying that society is an active agent *per se*. It is however true that agents' interaction is influenced by shared moral principles as well as envy. And it is often times the task of the intellectual to induce people to believe what is acceptable, to draw the line between rightful and shameful envy in the various domains of human activity²¹. If so, the crucial question then is to assess when and what kind of ideas succeed in affecting the institutional environment; in which way changes occur and how they affect future evolution.

At a lower level (artificial assignment and forced transfer of property rights, following successful rent-seeking activities) it is plausible to posit that the law-bargaining game is a learning process driven by a small number of fairly simple rules:

(a) coalitions and law-makers discover what kind of legislation can be passed or eliminated by means of a piecemeal process based both on past experience and acquired knowledge. This means that targets are assumed to be selected once suitable processes have been accepted and agreed upon. Similarly, evolution in the processes tends to prevail on target selection when assessing the cohesion and effectiveness of a pressure group. This does not rule out that theories can be conceived whereby targets only matter. Indeed, this is what the whole public-choice approach is

²⁰ It may be worth pointing out that intentionality is also a distinctive feature of adaptive learning processes. Indeed, this is one of the two points of contact between natural selection and adaptive learning. Another area of similarity regards target-driven behaviour. In both natural selection and adaptive learning individuals continuously evaluate, select or discard results, rather than behavioural patterns. See also Vromen (1985: 119-121) for a summary of the differences between the two views.

²¹ See Raico (2002, ch.X) for a recent appraisal of the debate on the active/functional role of intellectuals.

about. But it does rule out that a target-driven process is compatible with any biological/evolutionary explanation.

(b) the nature of the environment is crucial, for it affects phenotypes permanently, until a new change occurs. Hence, successful action to acquire rents - or to reject rent-seeking attempts - will have to include efforts to alter the environment and elicit appropriate reactions; for instance, from public opinion or rival interest groups. This is where the balance between formal and informal institution may play an important role, even if more complex than what many neo-institutionalists would claim. Deeply rooted informal institutions ease target-driven rent-seeking action, as long as the rules of infra-group behaviour are solid and well specified. The opposite holds true when the gap between formal and informal rules is profound, for in this case it is harder to discipline those ready to betray the group and free ride on state action. Whereas when formal institutions are soft and informal institutions are shaky, the nature of the rent-seeking process within the environment plays the central role in shaping an interest group and its activity.

(c) The temptation to carry out top-down legislation is likely to intensify with the so-called "acceleration of time"²². This phenomenon will not enhance the legitimacy of top-down legislation, but might reduce frictions between the formal and the informal rules, since the latter will find it difficult to form and settle down in a short period of time, i.e. before preferences and technological opportunities change substantially again. As a result, they turn out to be weak and sometimes ill-defined. On the other hand, the gap between the existing property right structures and the cultural expectations of the individuals may widen. Although people find it harder and harder to stop politicians and bureaucrats from taking advantage of their discretionary power, *ex post* resentment with respect to law-making intensifies and demands for new political actors increases. As the political market becomes more contestable, the net benefits of rent-seeking decline. It follows that more attention will be devoted to rent-seeking at a global level, where contestability is lower because institutional competition is stifled; and also to achieving more economic freedom at a local level, except for those areas where shaping the cultural environment is still possible.

²² This term comes from the neo-institutional jargon and describes a situation whereby societies fail to absorb quickly enough - and to adjust *vis-à-vis* - the substantial and frequent changes in the environment. As a consequence, informal rules do not come to the surface, let alone consolidate. See also the argument presented in section 2.

4. Some implications

Contrary to other avenues of investigation, this quasi-Lamarckian view lays emphasis on when and to which extent the environment - shared ideologies and accessible technologies - affects individual behaviour. As mentioned earlier, individuals interact within the given environment by considering what they perceive to be ethic preferences, realistic targets and ambitions, shared moral rules (legitimate modes of social interaction and thus cooperation). In particular, modifications brought about by the environment are successful only if other requirements are met, both in the environment itself and in the individuals' phenotypes, which in turn can be modified by changing the notion of morality and, more generally, by introducing new ideologies. In turn, the environment evolves under the impulse of what have been defined as ideological entrepreneurs (see par. 3.3), under whose influence individuals develop new behavioural features. Eventually, when the current behavioural traits of the agents are no longer compatible with the previous rules, new rules of the game are introduced.

The difference between this quasi-Lamarckian view and the neo-institutional approach is straightforward. According to the neo-institutional view, individuals affect the environment as informal rules are gradually translated into formal rules through a process similar to natural selection. As a consequence, path dependence leaves little room for changes in individual demeanor and loses much of its explanatory power when informal rules are ill-defined or fragile; which is indeed what happens when time "accelerates".

Following the Lamarckian view, agents change their behaviour after their perception of the environment (much alike the old institutional perspective), which should be understood both in terms of accessible knowledge and of rules. Property rights assignments may be changed within the given set of (higher) rules. Indeed, as long as these changes are consistent with the institutional framework (the rules of the game), property rights modifications should be assimilated to changes in individual's behaviour and patterns of interaction, rather than to changes in the environment. This also regards of course most property-right remodeling to accommodate the needs of new knowledge (e.g. technological progress). At the same time, this view leaves little room for exogenous shocks on the overall institutional context. Surely, the fact one cannot predict how people's preferences and modes of interaction evolve does not mean that institutions change exogenously, as much of the neo-institutional school would claim.

All the above does not rule out the importance of informal rules and of tensions between formal and informal rules. But the features of their interplay need to be reassessed. In particular, the term "formal rules" turns up to be too vague to be useful in this context. As pointed out previously, there exist two kinds of formal rules, one at a lower level (property right assignments) and one at a higher level (rules of the game). At a lower level formal rules are the outcome of coalitions' behaviour, which in the recent decades have been operating according to the nature of the processes, rather than to the features of the outcome. Once again, agents' conduct (widely defined) and the way it can be modified through time is the key issue, so that keeping the coalition together has become more important than focusing on the rent-maximizing targets. In this context informal rules do play a role, in that processes are indeed based on informal rules based on trust and past experience. But the lack of clear informal rules does not necessarily delegitimize formal rules; nor is it necessarily true that formal rules in contrast with informal rules are ineffective. For instance, weak informal rules may well lead to fragile coalitions and therefore to less successful rent seeking, rather than to chaos and uncertainty (as many neo-institutionalists would probably suggest).

At the higher level, it is here denied that informal rules as such lead to a direct change in the constitutional framework; or that top-down legislation is necessarily an act of violence with little respect for societal interaction. When the informal rules of the game matter - i.e. when they are clearly understood and shared by a large enough number of agents - they tend to affect the assignment of property rights within the environment, rather than the environment itself. And when the overall rules of the game do not allow informal contracts to take place, then such rules are simply ignored and the discretionary power of the officials curbed through corruption, political control, or both. Conflicts between informal and formal rules may and do emerge, but become critical only when there exist ideological fractures. That is, when new or old assignments of property rights conflict with the dominant moral rule, politicians are unable to provide consistent policies and the overall formal rules are questioned as a by-product of their ineffectiveness.

4.1 Ideologies and redescriptions

It has been argued in section 3. that the environment changes also as a consequence of morals, i.e. of widely shared moral standards, which affect individual behaviour and ultimately discipline envy. As people react to the existing environment, new needs come to the surface. In turn such new

requirements become acceptable only if supported by a satisfactory ideology. When this happens, the environment undergoes more or less serious change.

Although it is probably wrong to claim that most intellectuals systematically create arguments to support the winning coalitions and thus justify their rent-seeking activities²³, it is however worth reminding that the emphasis should be on a special category of intellectuals - the ideological entrepreneurs. They succeed in anticipating and accelerating new behavioral patterns or providing the needed-for ideology following a rapid change in the patterns. True enough, this is not too far away from the phenomena generated by periods of "representational description" mentioned at the beginning of section 2.. Still, there remains a fairly important difference.

Representational redescrptions refer to when individuals become aware of their new preferences and thus make their behavioural patterns explicit. The origin of the new preferences, the timing and features of the redescription continues however to be unknown. On the contrary, the quasi-Lamarckian view allows us to speculate that old (neglected or elitarian) ideologies - or their revised versions, if not altogether new beliefs - make an impact and legitimize new action (1) when preferences are at odds with the existing environment, (2) when the gap is too wide to be bridged by new phenotypes developed as a result of the stimuli provided by the environment, and (3) when selected interest groups see a large enough potential for rent-seeking to run the risk and lead institutional change, the latter being based upon the agents' expected new behavioural patterns and not necessarily grounded on sets of consolidated informal rules.

To conclude, let us now examine how these insights may help explain what happened in two historical periods where drastic institutional change took place: the end of medieval society in Western Europe and the downfall of the communist regimes in Central and Eastern Europe²⁴.

4.2 The end of feudal societies

Feudal societies were thriving when military aggression was a constant threat, communication and

²³ When this happens, educated and sometimes even erudite individuals have actually replaced intellectuals. In this case, the name of the game is not the creation of an ideology or a system of shared values, but rather the raising the cost of opposition for rival coalitions.

²⁴ Of course, these two short paragraphs have no ambition to be thorough analyses; but rather outlines of two research projects that could be developed according to the theoretical suggestions put forward so far.

transaction costs as a whole were high. Surely, the cost of achieving effective coordination between the centre and the periphery were far superior to the benefits of a centralized kingdom. Hence, local communities remained the only viable form of societal organization. Defense against raiders by means of professionals (heavy cavalry) and justice were the main task of the feudal lord, to be financed by means or trade taxes and *corvées*. Contrary to other institutional arrangements - say, Islam - since the middle of the IXth century hereditary transmission made sure that short-term violent rent-seeking by the lord could be maintained within tolerable limits, although at a cost²⁵.

From a factual viewpoint (description), in the XIIth/XIIIth centuries feudal societies dissolved for three reasons. First, labour mobility reduced the ability to tax, so that the lords could no longer control enough resources to secure adequate defense in case of need. Second, the crossbow made professional cavalry redundant. Third, the sources of wealth and thus power started to shift away from the landowners towards a new class, the merchants.

But from our viewpoint the institutional change could not have occurred if the traditional link between lords and population had not been challenged and morally delegitimized. In this case, there is no doubt that the Church acted as ideological entrepreneur in two respects. It started the diffusion of the Christian message systematically²⁶, in particular as regards the notions of individual dignity and freedom, which of course severed the cultural link between lords and serfs. Running away from the lord was no longer a break of a consolidated societal order, not far away from tribal loyalties, but (among other things) an assertion of individual liberty. New moral standards were thus introduced (later refined and partially changed through the Humanist period). In addition the Church introduced a new type of loyalty, to the emperor and to the king. It was a very strong tie, because it was enforced by God; but *de facto* with very soft obligations, for the king had little

²⁵ The cost was the loss of the original legitimacy for nobility and class differentiation, which was dignity and honour, as these were understood since the Roman times (Werner, 1988). As it soon became clear, the right of birth significantly strengthened the positions of nobility *vis-à-vis* the king, but reduced the incentives to create popular support, which in fact weakened throughout the centuries and shifted towards the king, who had the (divine) legitimacy the lords lacked.

²⁶ Before then, Christendom was an elitarian phenomenon, poorly understood by vast layers of the populations, which retained pagan rites for many centuries. More important, since the time of Constantine the Great the Church and the lay nobility were one; actually the Church belonged to the Prince, in the West as in the East. Indeed, the Church made no effort to change the incumbent framework until a crucial ideological blow was delivered; and the Gregorian Reforms substituted the Pope to the Emperor as the true and only representative of God on earth - or, more precisely, in the Western world. As we know, the East remained faithful to the Constantine.

power to execute any kind of contract upon its peripheral subjects. More aptly, it was more similar to a moral protection of the individual against the local lord, a right to revolt against the baron, rather than a just a change of sovereignty.

What happened for many centuries to follow - more or less until the last decades of the XVIIIth century - was indeed the development of new property right systems within the institutional framework. This was made possible by the ideological message promoted by the Church when the political conditions of the time induced it to take a more active role²⁷. The fact that the Ecclesiastical supremacy was repeatedly challenged should be understood within the process of property-right assignments and reassignments following rent-seeking activities, not as new overall institutional arrangements. The Church was indeed a rent-seeking player itself, which sometimes suffered from the very rules of the game it had introduced when acting as an ideological entrepreneur.

4.3 Patterns in transition economies

There are several theories about the collapse of the Communist regimes that formed the so-called Soviet Empire. Among the two most frequently quoted, one refers to the economic crisis of the area, which failed to grow and meet expectations in the Eighties. The second one refers to an alleged political crisis within the Soviet Union, the collapse of which sparked changes in the other countries of the bloc.

Whatever the true original cause, ten years later most countries of the former bloc abandoned central planning and totalitarian regimes (frequently with regrets). Some of these countries retained a highly centralized political system ruled by autocrats, sometimes in constant conflict with other potential oligarchs. Other countries have made serious progress towards private

²⁷ One could probably locate a new institutional change around the XVIth century, when the Humanist ideology modified again the rules of the game. The previous moral standards had emphasized individual dignity and freedom as a divine gift, to be lost when the divine law was infringed. Of course, it was up to the Church to limit and interpret the boundaries. On the contrary, humanism emphasized individual freedom as a natural right, with no boundaries and constraints.

This message was not new, of course, as Peter Valdo's followers know. But Valdo came too early. The tensions and the expectations of the XVI century were different from those of four hundred years before. That made indeed the difference between Luther and Valdo (apart from their personal qualities in terms of leadership and political connections).

property and sound money. None of them can however be labeled as a truly free-market economy. Indeed, no serious attempt has ever been made in that direction.

In simple terms, the arguments presented here suggest that the communist system collapsed because Gorbachev emerged as an appealing and credible ideological entrepreneur at a moment when the population was asking for new standards which would allow for capitalist affluence and socialist security. Surely, institutional change was not included in Gorbachev's original project. The purpose of the Gorbachevian undertaking was the new definition of property rights within the existing environment, rather than changing the environment altogether. As it turned out, his design was neither new, nor did it make much sense from an economic viewpoint. But it was politically successful because it came at the "right time", as the experience of his successors and of many other leaders in the transition economy confirms. And changed the course of history.

Time and again has it been argued that transition countries are far from being a homogenous bloc. They follow different policies and obtain different results. This is correct. But what is more relevant from an institutional viewpoint is where they are heading. The answer suggested here recommends one should look at the prevailing system moral rules, which rely less on informal norms of conduct than on a more or less agreed-upon ideological framework. For instance, Central Europe seems to be characterized by three crucial moral elements, which are embedded in the new environment, to various degrees modeled after the Gorbachevian somewhat contradictory blueprint (and incidentally, also consistent with the EU federal profile): reluctance to accept personal responsibility, confidence in competent state intervention, strong sense of national belonging. Institutions in that area today are well equipped to accommodate these principles and the day-to-day law-making process follows suit.

Whatever is going to happen in the near future, the crucial question for the social scientist is not about what kind of legislation is going to be passed. The answer to that is relatively easy. Variations across countries will depend on the different intensities across the bloc of the three elements mentioned above, as well as on the policy-makers' ability to comply with those moral principles and possibly deliver according to expectations. More important, we should be asking ourselves about the contestability of the incumbent ideology, *vis-à-vis* eventual new ideological entrepreneurs. In some cases it may well be high. But for a new institutional change to take place, new intellectual leaders must emerge, too.

5. Summary and concluding remarks

This article has emphasized two flaws that affected much of modern economics until today. The illusion that this discipline can be appropriated by amoral technocrats suggesting allegedly neutral, collective-welfare enhancing policies; and the misperception of transaction costs as a consequence of market failures, rather than of institutional deficiencies. These flaws have legitimized state intervention in violation of individual freedom. More important for the purpose of the present paper, they have also inhibited our understanding of institutional evolution, which is currently deemed to be the result of the interplay among rent-seeking groups in a changing and to some extent unpredictable environment. Hence, path-dependence still has remained an unresolved challenge and continues to look more like a descriptive hypothesis than an explanatory tool.

In particular, institutional economists do succeed in explaining economic behaviour within given institutional frameworks, but fail to clarify the main issue, that is the evolution of the environment itself. This becomes apparent especially when one departs from the extreme models - the free society and the totalitarian regime. More generally, institutional economics still finds it hard to break away from the temptation of carrying out comparative-statics exercises in property-right systems. Whereas the reason that have brought about the new rules of the game are described by shocks or redescriptions, but hardly rationalized.

Public choice economics has explained the behaviour of opportunistic groups within an institutional environment, thereby providing a theory for path-dependent processes. The same does not hold for institutional change, though. For the success or failure of interest groups depend on the strength of the institutional framework, rather than on the mechanics of the rent-seeking action. Indeed, not only does history show that institutional changes do not always follow coalitions' pressures, but it also appears that the traditional ways to identify interest groups no longer reflects reality.

This article does share the notion whereby economic is a sociobiological discipline. Nevertheless, it is argued that contrary to what can be claimed for the theory of the competitive firm, the Darwinian legacy, even when included into a functional framework, is of little use for the economics of institutional change. The Lamarckian view differs in that agents are assumed to be vulnerable to outside stimuli, and may modify their behavioural patterns accordingly, transmitting

such patterns from one generation to the other. When the outside pressure is an ideological break, and certain conditions are met, then the institutional environment undergoes radical change. Tensions may and do come to the surface, of course. But rather than being the consequence of frictions between formal and informal institutions, or the outcome of excessive rent-seeking, they tend to be generated by the contrast between the prevailing morality and the individual ethical standards. These may of course be substantial, especially in highly heterogeneous communities.

Surely, although there is no limit to the birth of ideology, new environmental patterns are successfully introduced only occasionally. That is not surprising. Accepted moral principles may change quickly, but not frequently, for the cost of changing them is often high. True enough, that may occur after dramatic and prolonged military events, which usually create widespread tensions, illusions, deep dissatisfaction. For under those circumstances ethical beliefs are weaker, the perceived need for new moral standards is greater and vulnerability to radical ideologies manifest. But if the view proposed in these pages is correct, institutional change does not occur because of the military shock, but only afterwards, and only if the environment successfully anticipates or accommodates the agents' new behavioural patterns. More importantly, even in a long-run perspective, individuals act within a given institutional framework for long periods. Their behavioural rules - including rent-seeking - depend on the moral norms of the system. The analysis of the rules of path dependence can thus be replaced by the inquiry into the dynamics of ideological competition.

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