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# Institutions in the economy and some institutions of mainstream economics: From the late 1970s to the 2008 financial and economic crisis

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## ABSTRACT

This article examines the relations between institutions and the economy. It highlights the role of institutions in the development of rules and socially constructed systems. It also discusses the impact of institutions on economic agents and the economy as a whole. On the other hand, there are important limits to the influence of the institutions of economics

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outside academia, and institutions in the economy also influence the institutions of economics.

Q KEYWORDS: Crisis finance institutions macroeconomy mainstream economics

Q JEL CLASSIFICATIONS: A11 A14 E02 G01 G10

## Notes

<sup>1</sup>This concept of conventions is intentionally less restrictive than game-theoretic ones. It is, however, more specific than the concepts underlying the analyses of conventions in the American economy by political scientists Blyth (2002) and Nelson and Katzenstein (2014). The nonsuperiority of conventions raises the question of how some rules become part of mainstream economics without being demonstrably superior to one or more alternatives. On this and on the mechanisms through which rules become conventions, see, again, Dequech (2017).

<sup>2</sup>Several references will be provided in the next sections, together with examples of the arguments made in this section.

<sup>3</sup>For Campbell (1998, p. 390), prestigious academic ideas have an advantage when it comes to influencing what he calls paradigms, “broad cognitive constraints on the range of solutions that actors perceive and deem useful for solving problems,” as distinct from “programs” which are “precise, concrete, and policy-specific courses of action and

<sup>4</sup>This issue is discussed in the next sections. Some references will be provided in the next sections, together with examples of the arguments made in this section. Some references will be provided in the next sections, together with examples of the arguments made in this section.

<sup>5</sup>This is a common issue in the literature. Some references will be provided in the next sections, together with examples of the arguments made in this section. Some references will be provided in the next sections, together with examples of the arguments made in this section.

<sup>6</sup>Although this is a common issue in the literature, some references will be provided in the next sections, together with examples of the arguments made in this section. Some references will be provided in the next sections, together with examples of the arguments made in this section.



<sup>7</sup>Fundamental uncertainty is the lack of knowledge resulting from the possibility of nonpredetermined structural changes. Procedural uncertainty results from the contrast between the complexity of the situation and the agents' limited capabilities. See Dequech ([2011](#)).

<sup>8</sup>Dow (2015) did not explain which institutions and conventions were those. Conventions, informal social norms and contracts emerge among private agents, but some institutions are implemented by policy. Perhaps Dow is thinking of reforms implemented in the 1930s (such as the New Deal in the U.S.) and/or the Bretton Woods system. Some policies may aim at reducing instability, but this does not necessarily mean that they are guided by an economic theory that emphasizes fundamental uncertainty or by any other academic theory.

<sup>9</sup>Campbell ([1998](#)) pointed out the influence of mainstream economics on the paradigms employed by actors in the 1970s/1980s but associates neoclassical economics more strongly with free market ideas and less with the kind of Keynesianism that prevailed in the 1950s and 1960s, while I see neoclassical economics as compatible with both.

<sup>10</sup>Among the earlier developers of VaR was Kenneth Bargaide (PhD in economics, Princeton, 1975). For a critique of VaR, see Crotty ([2009](#)).

<sup>11</sup>On the origins and diffusion of the copula method and the influence of mainstream financial economics, see MacKenzie and Spears ([2014](#)).

<sup>12</sup>Confidence in risk-assessment models also underlies proposals for bailing in banks (Dow, [2016a](#)).

<sup>13</sup>Nelson ... of excessive risk taking ... confidence depends ... present discussion ... tion mean that the ... en neglected by m

<sup>14</sup>The re ... p. 177) argued, ... at the time, the agen ... gencies did not seem ... ewhere.



However, S&P, in 2015, and Moody's, in 2017, agreed to pay US\$1.4 billion and US\$900 million, respectively, to settle lawsuits.

<sup>15</sup>The efficient market hypothesis also “provided a compelling rationale for the re-orientation of companies toward shareholder value. ... [T]he science and institutions of finance co-evolved to a degree unknown in most other domains, often with the aid of financial economists themselves’ (Davis, 2009, pp. 20, 22, 56, emphasis added).

<sup>16</sup>Blyth (2002, pp. 169–171) referred to monetarism as a new convention of both the Fed and financial markets. See also the references below to Abolafia ([2012](#)) on legitimation.

<sup>17</sup>According to Krippner (2011, p. 117), “[u]nlike academic monetarists, the FOMC staff was never under any illusion that it would be possible to precisely control the money supply.”

<sup>18</sup>Relatedly, Dow (2016b) examined differences in how policymakers, market players and households frame finance.

<sup>19</sup>On Friedman and funding, see also Van Horn and Mirowski ([2009](#), pp. 166–168).

## Additional information

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