FROM HABITS TO INSTITUTIONS AND BACK: A MODERN INSTITUTIONALIST VIEW ON SOCIOECONOMIC DYNAMICS*

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Abstract

This article revisits institutional economics in the tradition of Veblen and Commons, stressing its value for current debates. It examines how instincts, habits, and institutions interact through circular and cumulative causation, linking individual action with collective rules. This work aims to guide the reader in the circular relationship between habits and institutions, showing how their interaction animates socioeconomic dynamics. Habits grow into institutions, which in turn reshape habits and guide behaviour, creating both continuity and change. The analysis highlights upward and downward effects between agents and structures, showing the constitutive power of institutions in capitalist societies. By focusing on evolution and shared rules, Institutionalism offers distinct lens for understanding socioeconomic order and transformation.

Keywords: Institutional economics; habits; institutions; Veblen; Commons.
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1 Introduction

Institutions are systems of norms and rules, and they are foundational for social and economic life. Their role in the economy was made central in the work of North American economists like Thorstein Veblen (1857-1929), John R. Commons (1862-1945), and Wesley C. Mitchell (1874-1948). They were among the founders of an intellectual movement that came to be known as Institutionalism (Veblen, 1899a; Hamilton, 1919; Commons, 1924; Mitchell, 1914; Rutherford, 2011). This tradition has evolved and expanded through various currents, including radical institutionalism (Dugger, 1988; Almeida & Powell, this volume), legal institutionalism (Deakin et al., 2017; Hodgson, 2025a, 2025b), and post-Keynesian institutionalism (Zalewski, 2019; Lavoie, 2022; Whalen, 2015, 2020, 2022).

Both Institutionalism and post-Keynesianism embrace institutions as an essential theoretical tenet for understanding economic matters. Beyond that, the conceptual bridges between them have been historically complex and, at times, controversial. Keynesian macroeconomics and the neoclassical synthesis sidelined Institutionalism in the 1930s–50s, despite benefitting from the foundational work of institutionalist Wesley Mitchell and his colleagues at the US National Bureau of Economic Research (Mirowski, 2002; Rutherford, 2011). Clarence Ayres (1944) and John Kenneth Galbraith (1987) lamented that Keynesianism gave rise to technocratic management and replaced the institutionalists' political economy, one that addressed the socioeconomic damages of corporate power and inequality. While Keynesianism did dominate postwar policy, some institutionalists (e.g., Gardiner Means) contributed to New Deal policies, and post-Keynesians (e.g., Hyman Minsky) later revived institutionalist themes.

Looking from the perspective of the 1930s, however, in the long run both academic groups seemed to be dead, strafed by the neoclassical synthesis. Well, they are not. One wonders whether they have pondered their bygones while in intensive care. If so, a little mutual sympathy might help them regain strength. This special volume is an opportunity for new generations in both camps to engage in such task.

This paper explores a set of elements – instincts, habits and institutions – that, united by cumulative and circular causation, greatly contribute to the evolutionary character of institutional economics. It aims to guide the reader from habits to institutions and back by tracing how their interplay drives socioeconomic dynamics. By socioeconomic dynamics we mean the ongoing, historically contingent evolution of economic activities shaped by

institutions, habits, and social norms. Section 2 briefly sketches the history of that school of thought. Section 3 looks into the role of instincts, habits and institutions and how they relate to one another with the support of new insights in institutional thought. Section 4 brings our final remarks.

2 Founding fathers and builders of the legacy

Institutional economics emerged in the late 19th and early 20th centuries emphasising the role of institutions, culture, and evolutionary processes in shaping economic behaviour and outcomes. Thorstein Veblen is often credited as its forefather (Tilman, 1996). He developed a theoretical framework in economics that integrated insights from philosophy, psychology, and anthropology (Veblen, 1914). As he argued, human economic behaviour is shaped by evolving institutions and cultural processes. John Commons and Wesley Mitchell are also widely regarded as pivotal figures in the development of institutionalism, each with distinct contributions to the field.

North American institutionalists maintain Veblen's focus on the fundamental role and evolution of institutions, while rejecting the hedonistic psychology that gained currency in marginalism at the time (Veblen, 1899b [1994]; Asso & Fiorito, 2004). They also insist that markets are themselves institutions, greatly shaped by state action (Hodgson, 2015). Preferences are seen as endogenous, not given, and largely shaped by institutional and cultural contexts (Ramstad, 1990). They embrace a problem-solving and empirically driven view of scientific enquiry (Mayhew, 2018).

According to Schneider (2020), institutionalist scholars do not hold on to a previously idealised or teleologically projected economic system. They have, however, shown confidence in the evidence that ruling by pecuniary interests is detrimental to the well-being of many and conflicts with the virtues of careful, democratic deliberation. As a result, laissez-faire capitalism and the corresponding mono-institutional advocacy for free markets that allegedly self-regulate are not their irrevocable references. They tend to envision and consider multi-institutional solutions that, today, would range from centre-left to the progressive end of the political spectrum (Schneider, 2020, item 15).

Veblen's founding approach drew on pragmatist philosophy—Peirce's focus on the practical consequences of ideas, James' instinct-habit psychology, and especially Dewey's

emphasis on institutional habits of thought and action*. Veblen (1898) also argued that economics should be an evolutionary science, and consistent with the insights of Darwinism. Institutions and culture evolved along Darwinian lines of explanation, in which habits and institutions stood as units of selection. Their evolution, however, was not to be reduced to biological terms. Veblen (1919, p. 243) suggested that changes in "the institutional fabric are an outcome of the conduct of the individual members of the group", whilst "these institutions act to direct and define the aims and end of conduct". In the works of Veblen and Commons there is evidence of both upward and downward causation: individuals create and alter institutions, which, in turn, mould and guide individuals.

By the 1930s in America, however, pragmatist philosophy had been eclipsed by forms of positivism, instinct-habit psychology had been displaced by behaviourism, and the use of evolutionary and Darwinian ideas in the social sciences had lost favour (Degler, 1991). Three major intellectual pillars of Veblenian economics were attacked or abandoned. This led to a theoretical crisis within institutionalism as a whole. Commons (1934) endeavoured to provide a theoretical framework for institutional economics, but his efforts failed to overcome those sweeping shifts (Chasse, 2017). At the same time, Mitchell was pioneering work in the systematic use of data to understand large-scale economic fluctuations and changes. Rather than considering static equilibrium positions, he proposed a dynamic way of understanding aggregate oscillations as resulting from human actions, habits, and thoughts. Mitchell's studies of business cycles, his development of statistical methods, and his leadership in establishing the NBER since the 1920s helped institutionalism to consolidate its approach of combined theoretical insight, detailed descriptive work, and data-driven analysis. But the zeitgeist of economics was about to shift radically.

The Second World War helped to change the character of economics. It gave greater prominence to the neoclassical paradigm of maximisation under constraint, and more prestige to mathematics and formal modelling (Bernstein, 2001; Mirowski, 2002). The rise of the "neoclassical synthesis" of Walrasian general equilibrium analysis with a pseudo-Keynesian macroeconomics marginalised institutionalism (Rutherford, 2011). The neoclassical interpretation of conspicuous consumption, for instance, began with Harvey Leibenstein (1950), and later conventional models introduced abstractions that distorted Veblen's institutional and evolutionary framework (Salles & Camatta, 2020). In addition to

* The reader interested in exploring the philosophical foundations of Institutionalism is referred to the works of Mirowski (1987), Bush (1987, 1989), Waller (1988a), Rutherford (1990), and Kilpinen (1998).

such external intellectual and political shifts, as Rutherford (2011) argues, Institutionalism lost ground also because of its internal theoretical fragmentation and the movement's inability to present a unified alternative to the neoclassical synthesis. While the founders had developed rich conceptual and descriptive frameworks and applied analyses of institutional processes, they struggled to articulate a unified theoretical alternative that could compete with the mathematical precision, generality and predictive claims of neoclassical economics.

Despite its decline of influence after 1945, institutional economics survived. Leading postwar figures such as Clarence Ayres, John Kenneth Galbraith, Simon Kuznets, Gunnar Myrdal, Karl Polanyi and Robert Heilbroner were greatly responsible for its promotion (Klein, 1993). The evolution of institutionalism is evident not only through these influential figures but also through enduring collective efforts. In the USA, a large group of institutionalists established the pioneering *Association for Evolutionary Economics* (AFEE) in 1965. Two years later, they launched the *Journal of Economic Issues* (Rutherford, 2001). In 1979 the *Association for Institutional Thought* (AFIT) was formed as a sister organisation by a group of AFEE members who thought they should focus on the foundational principles of institutional economics (O'Hara, 2000). Institutionalist have also been involved with other heterodox and plural associations like the *Society for the Advancement of Socio-Economics* (SASE), the *Association for Social Economics* (ASE), the *European Association for Evolutionary Political Economy* (EAEPE), and the *Association for Heterodox Economics* (AHE). And they have published their works also in journals like the *Forum for Social Economics*, the *Review of Social Economy*, the *History of Political Economy*, and the *Journal of Institutional Economics*, among many others.

AFEE sponsors a few awards that support work in the institutionalist tradition. The *Veblen-Commons Award* honours major contributions to institutional economics since 1969. Among its recipients are scholars well-known in the post-Keynesian tradition, such as Jan Kregel, Geoff Harcourt, and Hyman Minsky. The Clarence E. Ayres Scholarship is awarded since 2013 to an international researcher for contributions to institutional economics. And starting in 2012, the James H. Street Scholarship has been annually awarded for contributions to economic development research in Latin America within the Institutionalist tradition, with a few Brazilian scholars among its recipients. Some of them helped establish the Institutionalist Economists initiative in 2023 and then the *Brazilian Association for Research in Institutional Economics (EINST)* in 2026.

There is obviously much more to be said about the century-old institutional tradition in economics. We refer readers interested in delving deeper into the topic to the works of Rutherford (1994, 2011), Hodgson (1999, 2004) and Almeida & Brites (2022). For what concerns us here, Institutionalism has maintained its core commitment to understanding how institutions evolve through the reciprocal causality between individual habits and collective rules and mores. The works of Veblen, Commons, and their successors provide analytical tools for examining the circular and cumulative processes through which economic behaviour and institutional structures continuously reshape each other. It is to this foundational relationship between habits and institutions that we now turn.

3 Circular and cumulative causation: from habits to institutions and back

In spite of not having produced a consistent, unified set of principles or theories, institutionalists are grouped by sophisticated and multifaceted analyses of institutions, often inspired by important parts of the work of the founders (Schneider, 2019). Such internal plurality leads any attempt to bring together key elements of institutionalism to have multiple entry points and uneven connections. We will therefore focus on a set of ideas from Institutionalism that seem reasonably aligned. They link what economists might call the nano level, which precedes and explains individual decision-making, to the meso and macro levels, which deal with the formation of collective patterns and, eventually, national aggregate outcomes (Pessali, 2016).

At the most granular level, institutionalism emphasises the role of habits as the fundamental constituents of individual behaviour. Deeply intertwined with human instincts and reason, they form the bedrock of individual agency. Habits, when widely shared, grow into institutions. Institutions are agents of stability, but not static backdrops. They are dynamic structures built and lived by individuals, who are at the same time instructed by institutions. This mutual shaping of agents and institutions through an upward and downward dynamics generates distinct transactional patterns that are the very essence of social and economic organisation. These dynamics consider the idea of emergent properties. The identifiable levels thus retain relative independence, while affected by the reconstitutional effects that occur between them.

Preferences and rationality, for instance, must be explained. Preference formation is inherently a social learning process. By observing others, following group norms, and

internalising the ideals embodied in social rules, individuals learn notions of acceptable reasoning and conduct, proper and preferable goals and outcomes (Ramstad, 1990). As Veblen (1899a) famously illustrated, the desire for status and the emulation of the leisure class profoundly influence what individuals come to regard as necessary or desirable. Recent scholarship has further examined, for instance, how psychological processes of imitation, belief formation, and social learning shape consumption practices (Almeida, 2014; Almeida & Luz, 2023; Camatta & Salles, 2024; Camatta et al. 2025). In this way, social institutions decisively mould individual tastes and behavioural patterns.

Individual choices thus cannot be understood in isolation from the institutional environment in which they take shape. The following subsections develop this argument step by step. First, by examining agency through instincts, habits, and reason, we see how individual conduct emerges from the interplay between inherited dispositions and socially built patterns. Second, the transition from habits to rules reveals how repeated behaviours crystallise into institutions that provide stability and guidance. Third, we turn to transactional patterns, where circular and cumulative causation links individual actions to broader processes of social organisation. Fourth, we explore the two-way dynamics between agents and institutions, showing how institutions act and are acted upon individual behaviour. Finally, we address the power of institutions in modern capitalist societies as they shape preferences, distribute opportunities, and reproduce—or challenge—existing structures of inequality.

3.1 Agency: instincts, habits and reason

Human agency involves tacit beliefs and motivations that are not subject to full, conscious deliberation. As pointed by John Dewey (1922), human action starts with raw impulses or instincts. These are inborn tendencies to act in response to stimuli. According to Veblen (1914), instincts are innate psychological tendencies that drive human behaviour. Of course, some notion of such primal prompts is present in many other sources. For instance, they do not escape John Maynard Keynes' perception of "animal spirits" (Keynes, 1936) driving human action.

Instincts are not fixed behaviours; they are dispositions. As such, they can be aroused by circumstances and specific sensory inputs. Instincts are not congenitally structured or refined, but plastic proclivities activated and shaped through social interaction and institutional embedding. They can also be suppressed or diverted. Important details on this

theme remain controversial within Institutionalism (Almeida, 2015), not only the familiar issue of weighting nature and nurture. Indeed, many of our dispositions and much of our personality are formed after birth. But the importance of socialisation does not deny the role of instincts (Hodgson, 2010). They are necessary for socialisation to begin its work.

Through interaction with the environment and social experience, instincts gradually transform into habits (James, 1890). In fact, much instinct cannot manifest itself without the help of culture and socialisation (Mayhew, 2018). An artist or an academic may spend hours perfecting a painting or an article, not just for profit but because the creative process is still active. Society can shape such instincts and create a shared habit of thought that conditions them. For instance, in a heavily profit-driven corporate environment, the creative propensity may be stifled as work corresponds to hitting production or sales targets rather than to meaningful creation. Or, as in Keynes' example in the particular field of investment decisions, there is a "spontaneous urge to action rather than inaction" (1936, p. 161), which becomes channelled into widespread optimism and herd behaviour.

Unlike instinct, a habit is a propensity moulded by environmental conditions and transmitted culturally rather than biologically. Veblen and the pragmatists regarded habit as an acquired proclivity or capacity, which may or may not be actually expressed in current behaviour. A similar interpretation of habit as a disposition is found in modern psychology, even when not explicitly or essentially grounded on pragmatist foundations (Gardner, 2014; Wood & Rünger, 2016; Carden & Wood, 2018). Brain imaging studies on human subjects (Poldrack et al., 2001) show that the formation of habits involves a shift away from parts of the brain associated with conscious, declarative memory and goal-setting (the medial temporal lobe and pre-frontal cortex) toward areas associated with procedural memory and context-triggered responses (the basal ganglia).

Repeated behaviour is important in forming a habit. But habit and behaviour are not the same. A habit is a potential behaviour stored in a cognitive representation of a cue-action response (Fleetwood, 2019). It instils a disposition to engage in previously adopted or acquired behaviour or thoughts, triggered by a cue—an apt stimulus or context. It may exist even if it is not manifest in behaviour all the time. Knowing a language or riding a bicycle are embedded in our habits and triggered by specific circumstances (Hodgson, 2010). To be sure, habits do give thoughts and actions stability. They are not fetters, though. As John Dewey (1922) argued, habits can be modified to accommodate the needs of evolving circumstances.

As Hodgson (2020) explains, individuals also have inherited or acquired abilities that enable reasoning. Reason is a faculty or capacity for conscious thought and deliberation used to navigate complex situations, create options and ponder alternatives, and to adapt behaviour. It allows individuals to critically assess and, at times, modify their habits when confronted with novel circumstances or perceived challenges. Reason does not emerge or operate in isolation, though. Instead, it springs from and builds upon ingrained habits. After habits first shape reason, their coupled operation is the source of mutual reshaping along life experiences (Bromley, 2006). Instincts and habits are primary. The capacity to choose, and to reason about choices, comes after the formation of crucial habits of cognition, thought or behaviour (Veblen, 1914; Dewey, 1922; Hodgson, 2009). For instance, a person used to pay cash might behave unlearnedly when introduced to credit card payment. Habits of impulsive spending easily emerge, leading to debt accumulating. In the absence of short-term consequences, this behaviour can be easily rationalised as a proper way to fund consumption. Impulsive spending becomes a habit, as with consumerism. Later, a new, unlearned situation arises when debt, interest charges, or financial stress must be faced. Reason is called upon to ponder the long-term consequences of such spending habit. A conscious decision then acts to reform the established habit (e.g., budgeting, switching back to cash payments, or using debit cards, and adjusting to all related rules that come with the new choice). As new spending habits are formed, new ways of reasoning about financial management and payment methods also emerge. A new habit-reason combination is formed.

Accepting habits to affect behaviour does not demote reason or belief. Yet habits of thought are the foundation of both reasoning and beliefs. Habits act as filters of experience and the substratum of intuition and interpretation. From the perspective of pragmatist philosophy, Jamesian psychology and Veblenian institutionalism, they are the grounding of both reflective and non-reflective behaviour (Hodgson, 1997). This does not make belief, reason or will any less relevant or real. But it cannot be ignored that all deliberations, including rational optimisation, rely on habits and rules (Vanberg, 2004).

3.2 Institutions: from habits to rules

In social reality, institutions are a class of entities. Therefore, in order to identify and differentiate between things that are institutions and those that are not, a concise taxonomic description is necessary. A taxonomic definition is a nominal definition that deals with a population of entities that share some common attributes (Hodgson, 2019). Before engaging

in lengthy analytical work, there must be some agreement among scholars on the type of object to be analysed.

The concept of an institution is broad, but not all-encompassing. Not all social structures are institutions. Social structures include sets of relations that may not be codified in discourse, such as demographic or gender structures (Hodgson, 2020). They may affect behaviour, but not necessarily through the operation of shared social rules.

There are different kinds of institution. Like the class "mammal" in animal categories, the class institution covers many different types. Therefore, the category institution needs to be divided and subdivided. Broadness of meaning does not make it an illegitimate term. It simply means that sub-divisional definitions are also required, as typical with taxonomy. Many writers, for instance, seek to differentiate between "formal" and "informal" (North, 1990), "regulatory" and "normative (Cole, 2017), "legal" and "non-legal" (Llewellyn, 1925), or "market" and "non-market" institutions (Arrow, 1974).

Scholars have strived to come up with an encompassing definition of "institutions" that could appease the predicaments of disagreeing views (Mayhew, 2008). Geoffrey Hodgson, as one of those engaged in this pursuit (2006, 2025b, 2019), has come to conclude that a near-consensus has been reached around a taxonomic definition of institutions (Hodgson, 2025c). They are systems of established and prevalent social rules that structure social interactions.

The addition of an etymological layer to this taxonomic definition may help enhance our understanding. The word "institution" has Latin roots that intertwine. "*Instituere*" is a verb composed of "in-" (meaning "into, in, on") and "*statuere*" (meaning "to set up, to establish, to place"). "Status" is the root of "*statuere*", and means "standing, position, arrangement". But status has commons roots with "*struere*", from which "structure" derives. And "*institutio*" is a noun that refers to "a disposition, arrangement, order", and also to "instruction, education; a system".

With these etymological inputs, Hodgson's taxonomic definition can be slightly thickened. Accordingly, institutions are systems of social rules that have been *set up* and have achieved a stable *standing* or *arrangement* within a society, and whose principles or contents are *transmitted* and *learned*, thereby *structuring* the interactions of individuals within that society. Systems of language, money, law, academic curricula, the inflation-targeting role of central

banks, scientific methods, property rights regimes, and enduring forms of organisations are thus institutions.

In turn, rules comprise behavioural norms, social conventions, and legal regulations. The term rule refers to a directive or disposition that on situation X do Y, or rather do not do Z. Beyond this regulative attribute over actions, a rule can also be constitutive (interpret phenomena W as being Q). Rules do not have to be widely or deeply known to be enforceable. The common acceptance of authority is, in many cases, what is required. Most of us are aware of only a tiny fraction of legal regulations. Yet they are enforceable, in part because many people respect the judicial system's authority. That is, they must be rules in actual or potential use, not merely rules in form.

There must also be some commitment in the community to follow rules (Gilbert, 2001). The term "socially transmitted" means that the replication of such rules depends upon a developed social culture and some use of language. Institutional economists and pragmatist philosophers, in the tradition of William James (1890), Thorstein Veblen (1899a) and John Dewey (1922), argue that institutions work only as far as the rules involved are embedded in shared habits of thought and behaviour.

The prevailing rule structure informs and beacons the way for action through morals, values, interpretative patterns, incentives and constraints. When individuals are motivated to follow particular institutional norms or rules, accordant thoughts and practices become habitual. Those norms and rules are thus reinforced. From this viewpoint, habits are the constitutive material of institutions, providing them with enhanced durability, power and normative authority. Individuals may then rationalise these actions in terms of preference or choice. According to this view, conscious choices are generally the outcome of habits, rather than the other way around. Hence preferences or dispositions may be moulded by institutional circumstances, which helps explain the normative power held by custom (Hodgson, 2010).

Habits are both problem-solving and sources of institutional inertia. In part, this explains how habits and changing circumstances relate. For instance, some habits are responsive to environmental pressures and adapt when conditions change. Consider the example of payment habits: when someone develops budgeting practices or switches from credit to debit cards in response to debt problems, these new habits emerge from genuine problem-solving needs. Other habits persist even when their original circumstances disappear. Authority, tradition, and social reinforcement typically drive such inertia. The

conspicuous consumption patterns Veblen analysed often follow this track—habitual expenditures that continue not because they address current challenges, but because they have become embedded in status relations and social hierarchies. This distinction helps explain why institutional change encounters differential resistance, as explained by Waller (1988b).

The distinction points to additional dimensions of the problem. The identification of what solves a problem, or when a problem is solved, for instance, also depends on habits and thus becomes the target of competing interests. This is also sparked by questions about whose problem has been solved, or about what new problems have been created by the solution of the old problem. Individuals experiment and learn, giving rise to new potential habits, which are then evaluated, institutionalised, and transmitted (Hodgson, 2004). This results in a framework in which institutional patterns are neither rigid nor purely individualistic. They evolve through recursive interactions between reasoning, social embedding, and valuation. Whether similarities in the channels of such a circular flow of stability and change are contingent on a particular time and space or singular across them is an open question (Waller, 2022). But institutionalists usually frame changing and ossified habits as operating within some kind of "collective action in control"—the organised going concerns that can either facilitate or resist institutional change, as Commons would call them.

Mechanisms like imitation, conformism, conditioning, cognition, and others of deontic basis, like a sense of moral obligation, are also subtle and pervasive inducers (Hodgson, 2003; Dequech, 2024). To understand human motivation in general, and rule-following in particular, there is a strong case for bringing in insights from psychology, as Veblen (1899a) and others have argued (Hodgson, 2020; Hermann, 2023). Mechanical reaction to incentives has always been an unsatisfactory basis for that. *Mutatis mutandis*, the same is true for insights from law, political science, sociology, anthropology and philosophy. There is also a place for evolutionary ideas to help explain the underlying genetic, developmental and cultural workings of human motivation. Their interplay with institutions deserves further study (Hodgson, 2010). Modern societies with agrarian surpluses, for instance, make selection drift away from survival (Waller, 2022) toward stratification and comparative status, as Veblen's (1899a) ideas about conspicuity suggest.

3.3 Transactional patterns, circular and cumulative causation, and social organisation

Institutionalism has strong ties to pragmatist philosophy. It sees knowledge as contingent, evolving, being shaped by experience and human interaction as a tool for problem-solving. The truth or validity of knowledge is determined by its practical effects and its usefulness in real life (Peirce, 1878). As knowledge evolves, its ultimate test lies on "whether it serves directly to enhance human life on the whole-whether it furthers the life process taken impersonally" (Veblen, 1899a, p. 67).

To deal with the problem of ensuring the means of our survival, we build knowledge with practical applications toward engendering and organising necessary resources. Veblen (1914), for example, identified historical stages in the evolution of our mode of social organisation. It started with simple social institutions, based on family and tribal ties, in an economy structured around subsistence activities. Private property and the division of labour then emerged, attended by violent disputes and the rise of social hierarchies. This grew into relations of servitude, in an economy based on agricultural work and lacking significant advances in knowledge. Still, with some growth in manufacturing and trade, a new stage came forth with the progress of industry and mass production. This is when Veblen draws attention to a forceful distinction between industry (producing goods and services) and business (making money). Business belongs to an idle class who profits off other people's labour.

These stages illustrate Veblen's view regarding the technological and institutional changes that marked major eras. On the one hand, technological progress has altered production methods, which then require a new institutional line-up to make them viable, such as changes in property rights, labour organisation, and social consent of new hierarchies. On the other hand, institutions have steered, accelerated or inhibited technological change. As they can influence agents and their habits of thought, the way a community sees the priorities and distributional effects of pursuing and adopting a technology is an institutional matter (Pessali & Fernández, 2006).

Commons further stressed the effects of institutions on social organisation, its advances and setbacks, with the concept of transaction. Seen by Commons (1931, pp. 652) as the fundamental unit of economic activity, a transaction is defined as the "alienation and acquisition, between individuals, of the rights of property and liberty created by society,

which must therefore be negotiated between the parties concerned before labor can produce, or consumers can consume, or commodities be physically exchanged". This means that previous negotiations are needed to erect and legitimate rights and obligations that come to be collectively accepted. As acceptance grows, recurrent interactions generate transactional patterns, which are the foundations of social organisation: they bring order along with self-reinforcing routines and expectations.

Indeed, Commons (*idem*, p. 649) defines institutions as

> collective action in control, liberation and expansion of individual action. Collective action ranges all the way from unorganized custom to the many organized going concerns, such as the family, the corporation, the trade association, the trade union, the reserve system, the state.

Such going concerns thus hold some critical mass of shared habits to bring forth an idea, policy, value or other. They also hold, or strive to hold, some bargaining power to transact with other parties in order to control, liberate or expand social actions.

As a result, transactions bear on conflict resolution, dependence balance and durable order, all of which have distributional implications. Uneven bargaining powers and their abuse can be damaging. A better balance of powers tends to produce order from which all sides may benefit and, thus, refrain from changing. In any case, the recurrence of a set of orderly transactions feeds back on itself, serving as a guide for future transactions. Causation becomes circular and cumulative, as suggested by Gunnar Myrdal (1944, 1957) and Veblen (1899a), in ways that are historically contingent and socially embedded. Transactional stability, however, does not mean social paralysis. Indeed, it can provide the timely conditions for other changes. The ongoing, historically contingent evolution of human activities shaped by institutions, habits, and social norms, i.e. its socioeconomic dynamics, is seen in how we organise and reorganise society (Hamilton, 1953; Peach, 2003; Jo, 2011).

3.4 Agents and institutions: upward and downward dynamics

Satisfaction and discontent with the *status quo* are substrates of institutional inertia and change. Their causes and intensifiers are varied, as suggested earlier. But how does this circular and cumulative movement between agents and institutions occur? One account is given by the dynamics of constitutive and reconstructive effects between them.

The dependence of institutions on habits partially roots institutions in people's dispositions. Institutions are structures that people encounter, and those same people are the producers and keepers of institutions. In this way, institutions are both objective structures

"out there" and subjective sources of agency "in people's heads". The agent and the structure, although distinct, are linked in a spiral of interaction and interdependence, reinforcing and reconstituting each other. Individuals create and alter institutions, while institutions, in turn, mould and guide individuals.

The idea of upward effects says that elements at a lower ontological level affect those at a higher level. For example, flu epidemics reduce economic productivity, voting can change governments, and a firm's innovation can create or erode monopoly positions in an industry. And, as Keynes (1936) discussed in chapter 7 of his *General Theory,* increasing individual savings can collectively lead to a fall in aggregate demand, then in income, and ultimately in overall savings. If lower-level changes can alter a higher-level structure, then it can be said that upward causation is reconstitutive. Agency "in people's heads" is responsible for stabilising a rule or pattern of transactions. It is also responsible for deviating from that pattern, as suggested by Dequech (2017), thus for changing or reconstituting it.

The idea of downward effects says that phenomena on higher ontological levels exercises control on lower-level components, but do not break or intervene in the causal relationships of their activities (Sperry, 1991). For example, people may be motivated to steal by their innate inclinations to self-preservation, but community rules or laws against theft deter them from stealing. As such, higher-level structures can act on instincts and reformulate individual habits, though not determine them. In spite of anti-theft laws and underlying legal enforcement, thefts still occur. Yet, institutions "out there" and other higher-level structures influence people and, to some extent, reconstitute them.

Structures and institutions generally precede individuals (Searle, 1995). We are all born into a world of pre-existing institutions, bestowed by history (Hodgson, 1999; Bromley, 2019). They inform us which desires, needs, knowledge, laws, technologies, and standards of social interaction and status are socially legitimate, for example. No final cause or balancing force, however, leads us to equilibrium, uniformity or singularity.

Variation and, thus, selection are to be expected (Hodgson, 1999). Biological make-up and life experiences are unique. Exposure to a same set of institutions does not warrant identical reactions; exposure to many of them, as regularly happens in real life, warrants some variation. This works for both individuals and societies.

Veblen (1899a, pp. 188) proposed that, in addition to the natural selection of individuals in terms of their fitness, there was a "natural selection of institutions" as well. To

be clear, fitness-based selection bears no relation with optimisation. Certain rules or transactional patterns (e.g. the capitalist labour contract) may ensure the survival of some social groups (those who sell their labour and those who own capital). This is not to say that both groups have selected an institution that maximises their utilities or GDP.

The issue of institutional selection and design is of utmost value to real economies. Economists, for example, recognise that income distribution is affected by institutions, and attempts to alter them can arouse a reaction from established interests (Pessali & Dalto, 2010). Hence, agency can work to boost or block institutional change. Veblen (1899a, 1915) stressed that entrenched elites and vested interests shape institutional endurance or strive to steer change to their benefit. Creation and reform of economic institutions are thus subject to capture. The mono-institutional approach of multilateral organisations, international consultants, and academics toward pro-market policies is often referred to as a case in point (Babb & Kentikelenis, 2018; Kashwan et al., 2019). As noted by MacLeavy (2008), instilling a set of values and social norms in people is a crucial part of this process.

3.5 Institutions and power in modern capitalist societies

The idea that institutions play a constitutive role in individual motivation and behaviour allows for an enhanced concept of power in the analysis of economic institutions. William Dugger (1980, p. 897) described economic power as the "ability to tell other people what to do with some degree of certainty that they will do it". Commons (1934) recognised that all transactions involve an element of power, often the "power to withhold". This power can be used to coerce. The "working rules" of institutions, whether legal or not, determine whose "liberty" (freedom to act) is expanded and whose is "exposed" (limited), inherently involving coercion or its threat. The state, through its legal and enforcement systems, is the ultimate arbiter of these rules, wielding physical coercion. That mounts up to a question of the state's power to empower. As such, it can both enforce the interests of the powerful and work as a vehicle for social transformation and the resolution of collective problems (see Dugger & Waller, 1992; Wisman, 2013).

Veblen's (1921) concept of "industrial sabotage", among others, highlights how the business class (or pecuniary interests) has grown in power over the industrial class (or production interests). This power allows the former, through its control of capital and financial means, to engage in the "conscientious withdrawal of efficiency". This can be described as a deliberate limiting, hindering or redirecting of the industrial system's full

productive capacity not for societal benefit, but to guarantee or increase their own profits and dominance.

But power is not to be seen in connection with coercion or constraint alone. Power is often exercised more subtly, particularly by customs and institutions, as argued by Steve Lukes (1974). He pointed out that lasting power is exerted by orchestrating the thoughts and desires of others. Again, this has not escaped John M. Keynes' (1936, p. 383) perception, as he affirmed:

> The ideas of economists and political philosophers, both when they are right and when they are wrong, are more powerful than is commonly understood. Indeed the world is ruled by little else...I am sure that the power of vested interests is vastly exaggerated compared with the gradual encroachment of ideas.

Modern economic institutions are by and large the intended result of authoritative agents like legislators, judges, heads of states, trade associations and business corporations. They design working rules and entitlement regimes with the very purpose of eliciting behaviours and ensuing associated outcomes (Bromley, 2006). Such institutional authority strives to shape not only formal compliance but also the habitual expectations, routines, and valuations that guide individuals' everyday behaviour. Its effectiveness depends on how such attempts interact with socially learned habits and dispositions. Working out the powerful and subtle persuasiveness of institutions becomes a means for change or its impediment.

Ownership of productive or financial resources is a main source of power in modern capitalist societies. It allows owners to command labour in their desired amount, for instance. It also allows them to buy education and communication channels, which are forceful instruments for mass persuasion in current industrial societies (Wisman, 2013). Institutions that eventually result from this effort or that assimilate its pattern of thought reinforce the original distributional status. This is a mechanism that Keynes seemed to regard as independent from the "gradual encroachment of ideas", as suggested in the quote above. Institutionalists see them as interconnected.

Social status is also a major source of power (Veblen, 1899a). Membership in an elite group, like in a clan, family, professional or religious circle, may allow varied levels of control over society's productive resources. Many social orders or hierarchies can result, as illustrated by the variety of capitalist societies (Hall & Soskice, 2001).

That institutions are powerful and vested interests habitually seek to format them does not entail determinism. This is so for at least two reasons. First, each attempt at instilling a working rule meets individuals who live under the influence of different sets of previous

or coexistent working rules, within particular contexts and with varied interpretative resources, or, in other words, it comes across some institutional entropy (Pessali, 2023). This reflects a view of power as a complex social phenomenon where individuals, embedded in their cultural context, both shape and are shaped by institutional structures (Waller, 2017). Second, institutions secure a distributional pattern in transactions. Changes in an institution, thus, involve a possible redistribution of power and resources, as mentioned above. This is usually a source of resistance to change, or institutional inertia (Mahoney & Thelen, 2009). Disputes over power and resources are thus at the very heart of institutions, be it language or money. Distributional conflicts are always latent. When some critical mass of competing interests vies for a new distribution of power and resources, the outcome cannot be entirely predicted. These two elements—entropy and inertia—are sources of uncertainty to institutional change.

Indeed, institutional researchers have long dealt with institutional change and its dynamics. This area deserves intellectual commitment, lest it be guided by mechanistic principles or anachronic approaches to discuss economic development. Even before the literature on economic development was so named in the 1940s and 1950s, institutionalists had already placed institutional and technological changes at the heart of the matter (Mitchell, 1910; Veblen, 1915; Commons, 1934; Salles & Conceição, forthcoming). The dynamics of habits and institutions formation and reformation outlined above, involving upward and downward effects in circular causation, seem better suited to guide our inquiry into economic development (Pessali & Salles, forthcoming).

4 Final Remarks

While institutions have regained a salient place across economics, Institutionalism has maintained its distinctive lens. Contemporary approaches often treat institutions, like property rights or contracts, as fixed constraints on rational agents seeking to maximise utility. In contrast, the Veblen-Commons-Mitchell tradition explored here conceives institutions as dynamic processes that shape what people want and how they think, and vice-versa. We observe individuals cultivating tastes for luxury brands to display social status, pursuing educational credentials for prestige, or choosing eco-friendly products. These are not simply responses to institutional constraints, but the social formation and reformation of preferences through repeated interaction. This mutual shaping of habits and institutions is thus central to understanding socioeconomic dynamics.

Institutionalism views economies as evolving systems shaped by culturally embedded rules, habits, and power structures. Along this line of thought, three key pillars of institutionalism have been highlighted here: (1) Institutions as systems of socially transmitted rules that wield collective power to shape behaviour; (2) Agency as habit-driven, where individual actions are moulded by institutional contexts, and feed back into institutional reinforcement or change—a two-way road of upward and downward effects; and (3) Institutional evolution as resulting from the upward-downward dynamics. All this draws on pragmatist philosophy and Veblen's emphasis on instincts, habits and adaptive knowledge to analyse how the ongoing formation and reformation of transactions guide societies. The recursive relationship between institutions and individuals is the spiral of history.

Ultimately, one enduring contribution of institutional economics lies in its subtle yet powerful perspective. It delves into the realm of rules, ingrained habits, and underlying power structures that shape economic behaviour and outcomes. Rapid changes in technology, extreme financialisation of the economy, hunger and extreme poverty amid the greatest affluence ever seen, and imperatives of environmental sustainability, for instance, cannot be seen as merely technical or market-driven issues. Rather, they result from a profound reshape of our institutions, moulding our patterns of production, distribution, and consumption. If this can be accepted, then institutionalism has a contribution to make.

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