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The Institution, the Economy and the Market: Karl Polanyi's Institutional Thought for Economists

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ABSTRACT *This paper aims to clarify the logical structure of Karl Polanyi's concept of institution, especially with regard to his most important contribution to political economy—the conception of self-regulating markets as institutions. Although Polanyi did not provide a well-developed concept of institution, this article argues that such a concept exists in his work. Moreover, there is in Polanyi's work a sophisticated institutionalist account of the self-regulating market that has been largely overlooked as Polanyi does not present it explicitly. Analyzing the economy as an institutionalized process, as Polanyi does, reveals that the market is neither a natural nor a spontaneous phenomenon—a conclusion that runs counter to conventional economic thinking. Polanyi's approach enables us to view capitalism (the 'market society' in Polanyi's language) through a highly specific cultural fact: the fiction of the self-regulating market. This institutional perspective needs to be reassessed beyond new-institutionalist theoretical constructions.*

> The human economy … is embedded and enmeshed in institutions, economic and noneconomic. The inclusion of the noneconomic is vital. For religion or government may be as important for the structure and functioning of the economy as monetary institutions or the availability of tools and machines themselves that lighten the toil of labor. (Polanyi, 1957, p. 250)
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> The supply-demand-price mechanism, … (which we popularly call the market), is a … modern institution of specific structure, which is easy neither to establish nor to keep going. (Polanyi, 1977, p. 6)

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1. Introduction

Economists have not paid much attention to Karl Polanyi (1886−1964), whose classic work *The Great Transformation* (1944) questioned the universality and the spontaneity of 'rational' economic behavior. If today Polanyi has acquired some legitimacy among eminent economists, it is because they are finding it more and more difficult to establish the scientific basis of a discipline that lacks empirical content. One simply needs to recall, for example, the failure of the shock therapy policies recommended by economic and political advisors following the collapse of the Soviet Union, or the total surprise with which the outbreak of the financial crisis of 2008 and the subsequent socio-economic crisis were met by almost all professional economists.[1] But once the social construction of the principal rules that structure economic life is recognized as decisive, once it is admitted that the founding rules of market organization do not emerge spontaneously from the atomistic decisions of rational optimizing agents, and once the self-regulation of markets is recognized as a fiction, a legitimate space opens itself up to institutional analysis.

Although Polanyi never developed the concept of institution in a wholly comprehensive way, this paper aims at unearthing his conception of institution. We want to show that the notion underpins his oeuvre even if his analysis has not been widely appreciated by economists, principally because he did not explain it unambiguously. Our objective therefore is to clarify the logical structure of his concept of institution. We shall focus on his discussion of the self-regulating market. In doing so, we shall engage in a mental exercise in order to show that there is in Polanyi's work a very deep and significant institutionalist account about the workings of the market as an institution. As Polanyi states time and again: 'market economy is an institutional structure'.

We begin, in Section 2, by explaining Polanyi's institutional logic, making use of the '(dis)embededness metaphor'. In Section 3, we demonstrate the theoretical relevance of the Polanyian perspective for any economist concerned with the concepts of institution and self-regulating market. Finally, in Section 4, we illustrate the contemporary relevance of Polanyi's institutional thought at a time when we are living through one of the deepest crises of capitalism. As we will show, the Polanyian relationship involving institution and economy is not compatible with the New Institutionalist Economics (NIE).

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[1]Nobel laureate and former chief economist of the World Bank Joseph Stiglitz (2002, 2006) has been severely critical of the World Trade Organization, the International Monetary Fund and the World Bank. These organizations, he contends, are driven by an unwarranted confidence in the superiority of the market in all situations. Stiglitz's own theoretical research suggests that imperfect information and information asymmetries render markets incapable of self-regulation, and that certain kinds of collective action can improve the functioning of markets. It is from this perspective that Stiglitz (2001) wrote a laudatory preface to a recent American edition of *The Great Transformation.* The lessons of Polanyi's work, Stiglitz argues, can help us to avoid the disastrous consequences that ensued from the adoption of neoliberal policies in the 1990s.

2. Karl Polanyi's Institutional Logic: The *(Dis)embedded* Economy

2.1. Some Background

In 1939, the collapse of 19th century European civilization, governed by the liberal economic order, had cataclysmic consequences for the entire world, namely the demise of democracy in most of the States of continental Europe. This constitutes the very object of Polanyi's institutional thought, as revealed by the subtitle he gave to the original edition of *The Great Transformation: The Political and Economic Origins of Our Time*. Polanyi wanted his analysis to have broad application, to be concerned with the 'changing relationship between economy and society'. He described the book as a 'narrative' written from the viewpoint of 'human institutions'—that is to say a history understood according to central principles that determine social organization (Polanyi, [1944] 2001, p. 4). Studying institutions in this framework reveals the meaning of an essentially human design.

According to Polanyi (1957, p. 249), 'The instituting of the economic process vests that process with unity and stability; it produces a structure with a definite function in society.' The economic process, in other words, consists in a system of social relations and in shared rules and beliefs, which reveal continuity and impose constraints on individuals while at the same time opening up opportunities to them. 'Institutions,' he writes, 'are embodiments of human meaning and purpose ... On the institutional level, regulation both extends and restricts freedom; only the balance of the freedoms lost and won is significant. ... [T]he privileged ... talk of slavery, while in effect only an extension to others of the vested freedom they themselves enjoy is intended' (Polanyi, [1944] 2001, pp. 262−263). Hence, markets should not be conceived as distinct entities from institutions, as some New Institutionalists would have it, because markets are activities that are institutionalized in a specific way.[2] Institutions also should not be defined negatively (and too simplistically) in contrast to markets, as constraints on markets from the outside such as social regulations that limit economic agents' scope for action. Institutions have to be understood as *socially* constructed entities in which economic processes are culturally codified in such a way that the fluidity inherent in economic movements acquires stability. This involves understanding the specificity of the culture of the market where it is present.

Polanyi's writings and the 'substantivist school' he founded remind us that there are various means of inscribing market practices in history, according to political, ecological, technical, religious, societal and cultural specificities, not to mention the existence of societies without markets.[3] Contrary to what has come

[2]Oliver Williamson (1975), a pioneering representative of the New Institutionalist view, explains institutions as optimal solutions to various problems that the market alone cannot solve.

[3]In 1953, at Columbia University, Karl Polanyi, Conrad Arensberg and Harry Pearson launched the *Interdisciplinary Research Project on the Institutional Aspects of Economic Growth*. The main result was the publication of *Trade and Market in the Early Empires* in 1957. Polanyi's chapter on 'The Economy as an Instituted Process' established the 'sub-

to be the conventional view among economists, we ought to distinguish the institution that we call 'market' from the institution of money, since the obligations inherent in social interactions are not fundamentally economic in nature (Polanyi, 1957). Polanyi ([1944] 2001, pp. 21, 237) even asserts that the widespread error of the 1930s was to conceal the socio-political nature of the gold standard as an institution that was, in reality, a set of rules that aimed at reproducing a hierarchy between classes and nations. More generally, the denial of the social nature of the gold standard was the expression of the liberal ideology that believes it possible to render the economic sphere autonomous in terms of both facts and ideas.

2.2. Markets and the Embeddedness Metaphor

Polanyi ([1944] 2001) characterized 'market society' as a 'myth' and the idea of the self-regulating market as a 'stark utopia'. For him, the 'free market' admired by the classical economists—Malthus and Ricardo were among his favorite targets—and their successors is unrealistic and unfeasible in practice: it has never been achieved in the history of humankind precisely because it requires treating land, labor and money as if they were profit-making commodities. However, while these entities may have a price, unlike true commodities they are not originally produced for sale: they are, respectively, nature, people and social relations (Servet, 1993), and none of them can be fully subjected to the demands of the market without being destroyed. Allowing the market mechanism to organize labor, land and money as real commodities would result in the annihilation of society or even of humankind itself. For Polanyi, the biggest danger is not economic in nature: it is neither that the self-regulating market is capricious (i.e., volatile), nor that it produces chronic economic crises. The biggest threat is the eradication of social institutions. In this sense, labor, land and money are 'fictitious commodities' because they are merely treated as if they were produced for sale on the market, even though they are not. To be more precise, the impossibility of wholly commodifying land, labor and money—the Achilles heel of the self-regulating market in Polanyi's view—leads to 'counter-movements' where humans spontaneously organize to protect themselves and their environments from the threat of the fiction of the self-regulating market. Regarding the development of markets during the 19th Century, Polanyi ([1944] 2001, pp. 3–4) warned in an often-quoted passage that:

> Such an institution [i.e., the self-regulating market] could not exist for any length of time without annihilating the human and natural substance of society; it would have physically destroyed man and transformed his surround-

stantivist' approach as a forceful challenge to the prevailing orthodoxy in economic anthropology, which uncritically applied the principles of neoclassical economics to non-market societies. Substantivism, as advanced by the Polanyi group, posits that the differences between pre-modern and modern economies are substantial enough to render the vocabulary of mainstream economics inapplicable and misleading in the study of ancient and tribal societies (Dalton & Köcke, 1983, p. 26).

> ings into a wilderness. Inevitably, society took measures to protect itself, but whatever measures it took impaired the self-regulation of the market, disorganized industrial life and thus endangered society in yet another way.

Polanyi understood the dynamics of 19th Century civilization as a tension between the two main organizing principles of modern society. Each had its own aims and methods (i.e., policies) and its own support in definite social forces. The first principle is the principle of economic liberalism. Its aim is to establish the self-regulating market using *laissez-faire* methods and free trade. This principle was supported by the bourgeois classes. For Polanyi, economic liberalism is the organizing principle of a society engaged in creating a market system. Polanyi regards the economic liberalism of the early 19th century as the ideological foundation behind the rise of the market economy. He saw economic liberalism and the market system appear as inseparable parts of a single whole, the second being an embodiment of the ideas formulated by the first. Like Karl Marx, Polanyi considers the market economy and the principle of economic liberalism to be two sides of the same coin. However, the causal relationship is included in Polanyi's account. It is not the (market) economy that gives rise unilaterally to an ideology (the principle of economic liberalism) as a secondary superstructure. The ideology of economic liberalism is a critical element in the rise of the market economy. Due to the identification of the principle of economic liberalism as an ideological foundation of the market economy, Polanyi is able to criticize both with the same set of arguments: the arguments mobilized against the one can be extended as a critique of the other.

The second principle is social embeddedness, which aims to safeguard human beings and nature through market regulation. This movement has no stable base. It was supported in an *ad hoc* way by those who were affected by the destabilizing effects of the first principle: the working class, peasants, merchants, and so on. At various levels of political organization (community, church, industry, State), people act against the dislocations and the disruption of traditional social institutions caused by the functioning of the market system. The rise of markets drove the population from the countryside to the cities, and gradually forced all participants in the economic system to adapt their mode of action to the dictates of self-regulating markets and its corollary features (self-interest, capitalist accounting, pecuniary calculation, and so on). Polanyi interpreted legislation regarding public health, factory conditions, labor unions, social insurance, public utilities, municipal services and trade union rights in Victorian England as countervailing measures to check the societal effects of the unfettered expansion of markets. He noted that on the European continent, governments of widely different political complexions enacted similar measures, including the protection of industries and agriculture threatened by ruinous competition. By embedding the market in society through such spontaneous social movements, social actors attempt to respond to movements towards allegedly self-regulating markets by codifying markets in both a legal and a social sense.

The embeddedness metaphor is essential to understanding Polanyi's institutional logic. Although Polanyi uses the term 'embeddedness' only twice in

The Great Transformation, it is, according to Fred Block (2001, p. xxiii), '[t]he logical starting point for explaining Polanyi's thinking [and] his most famous contribution to social thought.'[4] Yet, despite its centrality in Polanyi's oeuvre, *The Great Transformation* contains neither a definition nor an extended discussion of the metaphor. In some way, this omission may explain first, the number of interpretations—and misinterpretations—that the metaphor has provoked, and second, the 'enormous confusions' (Block, 2001, p. xxiii) that it has generated.[5] For Polanyi, the metaphor serves two purposes: first, it expresses the broad idea that economy as a whole (and not only the market) is not autonomous, as it must be in conventional economic theory, but rather it is subordinated to politics, religion, culture and social relations; and second, it points 'to the need for regulative intervention into the market to compensate for socially problematic effects of the market system' (Beckert, 2006, p. 37).

The growing number of spheres of social life that were subjected to market mechanisms was, as we have noted, the source of 'counter-movements'—forms of social resistance. This social resistance generated institutions that are concrete, multiply-determined objects that could combine different social processes simultaneously. Polanyi used the metaphor of embeddedness as a kind of shorthand for this dialectical method of studying institutions. The dialectic he describes can be fatal in the sense that counter-movements, which are mostly necessary to the simple continuation of social life and even the very survival of markets, can destroy social cohesion. If, for example, the birth of the New Deal in the United States was the very expression of a counter-movement that rooted the economy in a democratic way, other counter-movements that emerged at the same time, such as authoritarian and fascist regimes in most of continental Europe sought to make market alienation absolute (Polanyi, 1935). In a striking passage Polanyi ([1944] 2001, p. 32) points out that 'in order to comprehend German Fascism, we must revert to Ricardian England.' Fred Block (2001, p. xxv) invokes the metaphor of a giant elastic band to illustrate what Polanyi is getting at: attempts at enhancing market self-regulation raise the degree of tension as the band is stretched; as this tension continues, the band will eventually break (i.e., social breakdown) or retract (i.e., the market will go back to a more embedded state).

[4]Most authors, after noting the two occurrences of the metaphor in Polanyi's magnum opus, overlook the references to it that appear elsewhere in his work; see Polanyi (1947; 1957; 1977, pp. 9, 53); Polanyi & Rostein (1966, pp. 60, 81); Polanyi *et al.* (1968, pp. 118−119). The precise inspiration for the metaphor is not known, though various hypotheses have been put forth (see Beckert, 2007; Block, 2001, p. 24, n. x; Dale, 2011).

[5]The unsettled status of the concept is substantiated by the abundant literature on it. See, for example, Barber (1977, 1995); Beckert (1996, 2003, 2007); Block (2003); Dale (2011); Gemici (2008); Granovetter (1985, 1993); Krippner (2001); Krippner *et al.* (2004); Lie (1991).

2.3. The Fiction of the Self-Regulating Market and the Disembeddedness Metaphor

One of Polanyi's aims was to understand the history of the influential fiction of the self-regulating market idea. He recognized market society as a myth and the idea of the self-regulation of markets as a stark utopia. Nevertheless this fiction functions as an ideological tool that influences the behavior of individuals and, as a result, influences social relations and deeply transforms society. According to Polanyi's ingenious outlook, 19th century Western society was fundamentally different from what preceded it in the sense that the later period was dominated by a utopian belief in a self-regulating market, a belief that is a performative representation of reality. This utopian belief—this fiction—plays an important role not only in describing real-world economies and markets, but also in framing them.[6] This reading of Polanyi's work enables us to discard the misleading and sometimes naïve interpretations which attribute to him the view that the market did materialize in the utopian form envisaged by the classical and neoclassical economists.

Indeed, Polanyi is often understood to be saying that the 19th century economy (defined narrowly as a self-regulating market) was really no longer embedded in society but was successfully disembedded from society and came to dominate it. No less a figure than the French historian, Fernand Braudel (1992, pp. 225–229), reads Polanyi in this way. Other scholars have claimed that Polanyi was still too beholden to classical economics in his understanding of markets and failed to conceptualize economic relations as necessarily embedded in wider institutional processes (see for example, Barber, 1977, 1995; Gemici, 2008; Krippner, 2001; Lie, 1991; Randles, 2003). Our interpretation allows a nuanced reformulation of the influential reading put forth by Block (2003), who maintains that there is a deep contradiction within the text of *The Great Transformation*, reflecting a shift that occurred in Polanyi's theoretical framework midway through the composition of the book. Block surmises that Polanyi wanted the *Great Transformation* to influence the discussion of the post-war debates, and therefore sought to complete the book relatively quickly, before resolving all internal inconsistencies. To explain Polanyi's shift, Block argues that Polanyi experienced something akin to an epistemological fracture during his time in the United States, causing him to abandon his earlier Marxian framework in favor of a socio-economic theoretical position grounded in the theory of fictitious commodities and the 'always embedded economy'. According to Block, only time

[6]Performativity refers to the idea that science in general—economics for our purposes—shapes economic reality rather than describing how it works. Speaking about 'the performativity of economics', Michel Callon (2007) argues that economics (broadly construed to include accounting, marketing and related disciplines) has played two essential roles in the creation of modern markets. First, economics frames the world in terms of markets and makes it calculable. Second, economics creates calculative agencies that make use of the newly-framed world in order to act in rational ways. At certain times and places, he argues, the world of the formula is actualized in such a way that it can be said that the formula describes and represents the world correctly.

prevented Polanyi from revising the manuscript of *The Great Transformation* to resolve this contradiction. The final result of Block's analysis is that the metaphor of disembeddedness is merely a residue of Polanyi's older adherence to Marxism and thus should not be given importance.

Block's interpretation was criticized by Kari Polanyi-Levitt (2006), who argues that there is no strong evidence of a shift in Polanyi's thoughts during the writing of *The Great Transformation*. She contends that the metaphor of disembeddedness plays an essential role in the critical parts of Polanyi's arguments and therefore cannot be set aside without eliminating the central part of Polanyi's argument. In her view, the apparent contradictions in *The Great Transformation* are not contradictions, but expressions of the contradictions that exist in the self-regulating market system itself. Polanyi argues that the disembedded economy is a fiction and at the same time that this utopian project was partially achieved. So, there is no contradiction. There is merely a tension that Polanyi saw in the real world, a tension between the two main organizing principles of modern society: economic liberalism and social embeddedness. Since the market society was ultimately impossible, its implementation had to result in crisis and failure. Thus, the *a priori* contradiction that Block tries to set aside must be regarded as an integral part of Polanyi's thesis. We agree with Polanyi-Levitt that Block's interpretation fails to understand the uniqueness of the 19th century, which Polanyi explicitly described as a particularly distinctive episode in the history of Western society. Indeed, after his supposed epistemological break, Polanyi continued to emphasize that 'the working of the economic system here not only "influences" the rest of society but actually determines it . . .' (Polanyi, 1977 p. 12).[7]

The reason for Block's mistake is relatively easy to understand. Polanyi, like Karl Marx and Max Weber, believed that the 19th century Western world was essentially different from all earlier economic forms: for it was characterized by the institutionalization of economy as the driving sphere of social development. Hence, there is, within capitalism, a singular dependence of society on economy. Three years after the publication *of The Great Transformation*, this insight led Polanyi (1947) to the idea that the market mechanism created the illusion that economic determinism—the market mentality—was a general law for human society. The difficulty that arises from Polanyi's work is not, as Block contends, connected to Polanyi's earlier adherence to Marxism, but concerns the need to acknowledge a critical turning point that shaped the Occidental socioeconomic system (Maucourant, 2010).

In fact, Polanyi demonstrates that at the beginning of the 19th century a radically singular economic society emerged, which amounted to a total rupture with those societies that preceded it, be they primitive or archaic. It emerged first in England and then spread to the rest of the Western world. It was 'economic' in the distinctive sense that people's lives were organized around pecuniary gain instead of around the need to survive, as it was in all previous societies. What

[7]The writings in the posthumous collection from which this quotation is drawn date to the early 1950s.

was radically new in this system was that the economy was no longer embedded in traditional social institutions based on social patterns such as age, sex, kinship and marriage; the principle of economic liberalism attempted to embed society in an autonomous economy, with the self-regulating market serving as the 'fount and matrix' of the social system. In earlier societies, individuals subordinated their economic action to social institutions. The division of labor was determined precisely by such social institutions; technology, productive equipment and accumulation played relatively limited roles; and competition was social rather than economic. Market exchanges existed but markets were peripheral to the economic system; subsistence production was a more important feature of the system than production for sale. There was no separate sphere of economic activity: the economy was embedded in society in such a manner that the economy cannot be accurately studied apart from the tissue of relationships that constitute the entire society. However, at the beginning of the 19th century the economy became disembedded from traditional social institutions and imposed the constraints of its own particular organizational form and development on diverse areas of social life. In contradiction to what was the case in earlier forms of society, instead of the economic system being embedded in social relationships, these relationships were now embedded in the economic system.

What is essential in this process is that without the purposeful efforts of the early English political economists such as Ricardo and Malthus among others, and without systematic, protracted and sometimes tempestuous interventions on the part of the State, the utopian belief in a self-regulating market could never have emerged and developed. For Polanyi, the institutionalization of the belief in utopian self-regulating markets was possible only as a result of the activities of economists and the State. (In the case of the State, this active involvement included the regular exercise of violent physical force.) In a famous passage of *The Great Transformation*, Polanyi ([1944] 2001, pp. 145−147) argues:

> There was nothing natural about laissez-faire; free markets could never have come into being merely by allowing things to take their course. ... [L]aissez-faire itself was enforced by the State. The 1830s and 1840s saw not only an outburst of legislation repealing restrictive regulations, but also an enormous increase in the administrative functions of the State, which was now being endowed with a central bureaucracy able to fulfil the tasks set by the adherents of liberalism. ... [L]aissez-faire was not a method to achieve a thing, it was the thing to be achieved. ... The road to the free market was opened and kept open by an enormous increase in continuous, centrally organized and controlled interventionism. ... Thus even those who wished most ardently to free the State from all unnecessary duties, and whose whole philosophy demanded the restriction of State activities, could not but entrust the self-same State with the new powers, organs, and instruments required for the establishment of laissez-faire.

Polanyi lays particular emphasis on the ongoing pivotal role played by the State apparatus and the legislative process in the 19th century in England to shape the rules governing human beings and nature with a view to constructing apparently self-regulating markets. In other words, these apparently free markets relied on the State to provide the conditions that enabled it to work. These were not only regulations about what constituted fair and free trade, the drafting and fulfillment of contracts, financial regulations and so on: they also involved State management of the supply of money and credit, as well as rules and regulations regarding the provision of land and labor. The latter constituted what Polanyi termed fictitious commodities. In the 1830s and 1840s the liberal crusade resulted in an outburst of legislation passed by the British parliament aiming at repealing restrictive regulations. The key measures were the Poor Law Amendment Act of 1834, which subjected the domestic labor supply to the price-setting mechanisms of the market; Peel's Bank Act of 1844, which subjected monetary circulation in the domestic economy to the self-regulating mechanisms of the gold standard more strictly than had previously been the case; and finally, the Anti-Corn Law Bill of 1846, which opened up the British market to the supply of grain from the entire world.[8]

The process of disembeddedness is central to Polanyi's claim that the 19th century was economic in a very different sense from earlier periods because that process appears as a particular form of social construction by the State and its administrative bodies in which coercive public powers are used to promote practices that adopt an exclusively market-orientated representation of economic world. Under capitalism (market society), all social considerations, motivations, and values originate in the empirically acquired primacy of the market-orientated view of the social world; this becomes autonomous from any conscious efforts at social control. Under capitalism, the connection of economic exchange with some set of social structural and cultural elements in the social system does not take the form of interdependence but rather the primacy of the market economy over the entire social system. The first frames and largely determines the second. This is precisely why Polanyi speaks of disembeddedness with regard to this type of economy. However, if there is disembeddedness, it is a new kind of social organization that makes it possible. Hence, for Polanyi: (i) economic relations are always institutionally embedded; (ii) the institutions that interest the economist need to be understood as socially constructed institutions; and (iii) economists have to analyze how ideological and politico-legal processes are endogenous to modern capitalist organization.

Finally, on account of Polanyi's institutional perspective, the very controversial Polanyian institutional process of disembeddedness appears as a market representation of a social world, a utopian representation that cannot be fulfilled and which is destructive when pursued by society. Yet for at least the past three decades this representation has dominated the economic and political spheres, just as it had in the 19th century.

[8]Polanyi notes that the cruellest part of this process was the commodification of labour. The Speenhamland system sought to mitigate the economic dislocations caused by the emergence of a labour market. But the long-run result of the system was ghastly, only furthering pauperism. The State, accepting what the classical economists regarded as the brute facts of nature, instituted extensive changes in the social welfare system with the New Poor Law in 1834, abolishing the Speenhamland subsidies and imposing stringent and punitive conditions for receiving workhouse assistance.

3. The Economy and the Markets as Complex 'Instituted Processes'

3.1. Institutions and the Confusion between Formal and Substantive Views of the Economy

As John R. Commons (1934) has noted, social science would be impossible if human action was totally unpredictable. Institutions are expressions of the socialization processes that make human behavior predictable and knowledge about social existence possible. Polanyi's institutional view of economic history goes beyond approaches that oppose individual choice to social necessity and that are often laced with ideological biases (Polanyi, 1977, p. xli). An 'institutional analysis' can show how the tension between the social body and individuals can resolve itself. In a series of early papers, Polanyi (1922, 1924, 1925) criticized central planning as incapable of creating a rational account of costs, and developed an alternative model in which institutions organize the functions of production and consumption in a decentralized socialist system. He argued, moreover, that attempts by the State to dictate the needs of society and the means of satisfying these needs are a source of waste and abrogate working class subjectivity, with negative consequences for the achievement of socialist aims. He later attempted to show that Nazism rested on anti-individualist ideology and that fascist ideology is underpinned by the fantasy of the determinism of the whole (Polanyi, 1934). The basis of our knowledge about economic life, then, is not the equilibrium mechanism, as orthodox economics presumes, but rather the concept of the institution that Polanyi shares with thinkers such as traditional American institutionalists.

Polanyi conceives the economy as a social-natural process the major elements of which are 'human needs', 'human work and effort' and 'means of production' (Polanyi-Levitt, 1994). For Polanyi (1957, p. 243), the meaning of economy in its most general or institutional sense 'derives from man's dependence for his living upon nature and social environment'. The 'substantivist' view studies the role of economy within society. It deals with the institutional forms taken by the process of human needs satisfaction in all societies, past or present, actually existing or envisaged for the future; its main concern being sufficiency rather than efficiency. Polanyi insists on the necessity of having such a conception of economy, and he rejects the conventional 'formal' view according to which the economy is limited to a mental process of economization via a rational adjustment between scarce means and alternative ends. In this latter conception, the economy is reduced to a certain psychic arrangement of the human mind based on a decision-making process in a situation of scarcity. As summarized by Polanyi (1957, p. 243), 'The formal meaning of economic derives from the logical character of the means-ends relationship, as apparent in such words as "economical" or "economizing". It refers to a definite situation of choice, namely, that between different uses of means induced by an insufficiency of those means.' Thus, this formalist view of economy is based on an ontological scarcity of means catering to human needs, and the object of analysis is thus the discrete and rational individual who seeks to maximize his gains.

From this point of view, economics—which defines itself as a universal science of choice—is a rationalization of motivations that govern the capitalist world, that of generalized and ahistorical scarcity where markets condition the choices of economic actors. Yet, the livelihood of man may or may not involve the need for choice: 'Custom and tradition, as rules, eliminate choice, and if choice there be, it need not be induced by the limiting effects of any "scarcity" of means' (Polanyi, 1977, p. 27).[9] Thus Polanyi's institutional view of economy is not founded on the notions of scarcity and choice, the basic postulates of the formal approach. Furthermore, economists too often think about the economy in a way that implicitly assumes the homogeneous existence of a market economy, such as most of us inhabit. However, if we are referring to an economy substantially different from our own, we run the risk of distorted or anachronistic thinking. Polanyi challenges the ethnocentrism of the formal view, which implies equivalence between the human economy in general (i.e., 'substantive' economy) and its free market form. This is what Polanyi (1977, Chapter 1) calls 'the economistic fallacy'. This chimera, which grounds the formal view of the economy, classifies all human activity as ends or means, and rationalizes the use of means in the form of a timeless and instrumental rationality. It uncritically equates the human economy in general with its market form. But means and ends depend upon prevailing institutional circumstances in a society; they are mutable possibilities rather than fixed givens. According to Polanyi ([1944] 2001, p. 280), the economistic outlook projects towards the past some categories that would only belong to an idealized market society. As a consequence, it eventually creates an artificial landscape that barely has any resemblance to the original one (Polanyi, 1957, p. 257; 1977, p. 6).

3.2. The Economic Process and Institutions

Although the problematic of the *Great Transformation* is steeped in institutions, the question of how they ought to be incorporated into the study of society was not explicitly addressed by Polanyi in his book. But the work he did for the Columbia Interdisciplinary Project led Polanyi to give content to the notion of institution through the concept of 'instituted process'. According to Polanyi (1957), the economy must be viewed as a process of interaction between man and his

[9]Polanyi's views were inspired by Carl Menger's *Grundsätze der Volkswirtschaftslehre* (1871). According to Polanyi (1977, Chapter 2), only Menger, among the great theorists of the social sciences, avoided the mistake of mixing up the two meanings of the term 'economic', a word that has profoundly distinct roots: 'As Menger (1871, p. 22) explained it, the economy has *two* "elemental directions", *one* of which was the economizing direction stemming from the insufficiency of means, while the *other* was the "technoeconomic" direction, as he called it, derived from the physical requirements of production regardless of the sufficiency or insufficiency of means'. Menger sharply contrasted exchange economies, which were the subject of his *Principles*, with the 'non-civilized' economies, and he distinguished economic action in general (*Wirtschaftend*) from economic action connected to the fact of scarce means (*Sparend*). This distinction has never been pursued in any subsequent presentation of neoclassical economics.

natural and social environment. Such a process results in an ongoing supply of material meant to satisfy human needs, and is the foundation of the method envisaged by Polanyi: institutional analysis has an understanding of the fluid mix of 'economic' and 'social' factors. For Polanyi, to the extent that 'Social activities … form part of the process, [they] may be called economic; … any components of the process may be regarded as economic elements' (Polanyi, 1957, p. 249). Yet, without the concept of institution, the understanding of the economic process, perceived as an alchemy of physical, technical, social and ecological elements, would be limited:

> If the material survival of man were the result of a mere fleeting chain of causation—possessing neither definite location in time or space (that is unity and stability), nor permanent points of reference (that is structure), nor definite modes of action in regard to the whole (that is, function), nor ways of being influenced by society goals (that is policy relevance)—it could never have attained the dignity and importance of human economy. The properties of unity and stability, structure and function, history and policy accrue to the economy through its institutional vestment. (Polanyi, 1977, p. 34; see also Polanyi, 1957, p. 249)

Institutionalizing means shaping economic facts according to certain social relations. The institutionalization of the economic process is essential, for it means that man's survival does not depend on the contingency inherent in his interaction with nature and society (Polanyi, 1977, p. 34). Economy may of course be instituted in different ways from one society to another. So Polanyi ([1944] 2001, 1957) identifies three major patterns, or so-called 'principles of behavior' or 'forms of integration', such as reciprocity, redistribution and exchange (implicitly market exchange), which in combination give economy its unity and stability (i.e., order); that is, the interdependence and recurrence of its parts. To be effective as integrative mechanisms, such forms of integration require 'models' or 'institutional supports' that are respectively symmetry, centricity and the market: reciprocity requires movements between designated symmetrical groupings as in kinship relations; redistribution of goods in and out of a center requires centricity and is generally accompanied by hierarchy; and exchange requires a price-making market system. For Polanyi, these patterns of integration are historical in nature; they do not derive from the summation of individual acts but are conditional on the existence of specific institutions. Nor do they represent stages of development because no particular sequence in time is implied.[10] Furthermore, they work together and their coherence rests in their synergy. Hence there is nothing to be gained by attempting to isolate supposed 'good institutions' in a given system and then to try to reproduce them under another institutional form.

A significant feature of Polanyi's analysis is his insistence on the non-universal nature of market and market rationality. As Polanyi makes evident, the efficiency of each form of integration can be improved though its articulation to

[10]Polanyi rejects as historically untenable Marx's historical 'stages' of Asiatic, feudal and capitalist modes of production based on the predominant labour regime.

the other forms. For example, Polanyi (1957, p. 253) notes that the efficiency of reciprocity increases considerably when it uses redistribution as a subordinate method: 'Reciprocity may be attained through a sharing of the burden of labour according to definite rules of redistribution as when taking things "in turn".' The combination of these regulation mechanisms is essential, for instance, to the understanding of European feudalism, which is marked by important relationship networks among the monarchs, vassals and inhabitants of the fiefs. If it is a historically established fact that, very early in history, reciprocity and redistribution articulated themselves with one another, we sometimes forget the speed with which redistribution got linked to exchange. But it took the market centuries to become the predominant form of integration in Western society.

3.3. The (Self-Regulating) Market as a Complex Historical Institution

Contrary to any 'conjectural history' of the market, Polanyi (1977) shows that we did not move from the local to the domestic market and then on to the external market. Analyzing the work of Weber (1923), who shows that trade between peoples preceded domestic forms of exchange, Polanyi ([1944] 2001, p. 61) suggests that 'The true starting point is long-distance trade, a result of the geographical location of goods, and the 'division of labor' given by location.' According to pure market principles, prices are mainly independent of social relations between different actors. They result from the convergence of a mass of anonymous sellers and buyers. In ancient times, trade was a form of collective action, the expression of reciprocal practices between political units: exchange between social elites is at the origin of transactions that are limited in number and variety. Polanyi (1977, p. 81; 1957, pp. 257–258) emphasizes the acquisition of goods originating in far-away countries as the crucial characteristic of trade. Once political power is organized, systems of redistribution organize commerce. This form of trade is essentially administered, prices being fixed by diplomatic treaties predating the exchange and thus unlikely to be open for discussion or modification through bartering. In addition, trade and exchange do not naturally relate to man's subsistence. Consequently, it does not make human existence dependent on fluctuations in market prices.

At this level, Polanyi does not deny the ancient origins of the marketplace. Instead, he underlines the fact that trade and the use of money predate markets: they 'are as old as mankind; while markets, although meetings of an economic character may have existed as early as the Neolithic, did not gain importance until comparatively late in history' (Polanyi, 1957, p. 257). An essential question of economic history to ask is how trade became linked to the market (Polanyi, 1977, pp. 91–92). Simple practices of exchange do not create a market system: the market gives stability to what would otherwise have only amounted to occasional acts of exchange. This is why the market is an institution, or rather an instituted process, involving a supply-and-demand mechanism in which the movement of goods is controlled by prices (Polanyi, 1977, Chapter 8). The fact that market prices are 'fluctuating or changing' and of a 'competitive nature' is obviously decisive (Polanyi, 1957, p. 269). In such conditions, the market as an institution produces systematic effects that Polanyi designates by the term 'integrative exchange': 'Even price-making markets are integrative only if they are linked up in a system which tends to spread the effect of prices to markets other than those directly affected' (Polanyi, 1957, p. 255). This assertion is of primary importance for the study of early market forms, since the exchanges that form part of this institution must have a minimum of coherence and stability: 'Acts of exchange on the personal level produce prices only if they occur under a system of price-making markets, an institutional set-up which is nowhere created by mere random acts of exchange' (Polanyi, 1957, p. 251). Finally, according to Polanyi, the existence of transactions between individuals involving exchange relations is not the same as a coherent market institution. Consequently, it is impossible to rely on the existence of simple market practices to draw hasty conclusions about the existence of a market system.

4. Polanyian Institutional Thought and Contemporary Prospects in Theory and Practice

One premise represents the starting point of the new-institutionalist perspective: in the beginning, there was scarcity and competition. Thus, Oliver Williamson (1975, p. 20) writes: 'In the beginning, there were markets'. Douglass North's point of view is more complex but not substantially different: the continuous interaction of institutions and organizations, which is the key to institutional change, originates in the scarcity-competition paradigm.[11] In contrast, Polanyi's institutional approach rests on the tension between the radically historical nature of institutions and the universal nature of man's subsistence. Society does not possess an infinite number of different institutions to organize subsistence; but it is entirely possible that there are institutional variations that organize themselves around several fundamental patterns. Economy is not one thing for Polanyi but rather a set of complementary institutions, anchored in history, the study of which must be based on ideal types as the 'forms of integration', that are institutional patterns of redistribution, reciprocity and market exchange. Polanyian institutional analysis aims to demonstrate, as far as possible, the historicity of the constituent features of economic structure.

Although New-institutionalism and the 'substantivist' approach of Polanyi both insist on the centrality of institutions, the two perspectives are fundamentally different. To conceive of economy and markets as institutionalized processes, as Polanyi does, contradicts the belief in the naturalness, the asocial universality and the ahistorical nature of the market. The market regains its fundamental anthropological, historical and cultural plurality. The belief in market as a spontaneous phenomenon, common to conventional economic approaches, masks the profoundly institutional nature of the market, which must be understood in its historical and social context. So, following Polanyi, markets have never been free and self-regulating; they require a set of social relations and institutional arrangements

[11]North (1990, p. 5) draws a distinction between organizations—'groups of individuals bound by a common purpose to achieve objectives'—and institutions—'the rules of the game of a society.' See also North (2005) and North *et al.* (2009).

to enable the allegedly invisible hand to work. In short, without State interventions, markets cannot emerge, expand and survive. Market society thus rests on particular ideological, political and legal arrangements, which are the social requirement of the market as an institution.

The world described in Polanyi's *The Great Transformation* seems strikingly similar, in its fundamental characteristics, to the one we have been living in for the past three decades. As Polanyi argues, the self-regulating market was a fiction, and the attempt to achieve which is the effort to organize society on the basis of *laissez-faire* liberalism, inevitably led to social responses aimed at protecting society from the market. Despite these social responses, the ascendance of market fundamentalism ushered in the catastrophic events of the first half of the 20th century. A similar failure to appreciate the institutional thickness of the market may account for the misplaced confidence in the efficiency of financial capitalism that led to the current economic crisis.

The utopian belief in market self-regulation, which re-emerged about 30 years ago is reflected in an increasing penetration of the market logic at the heart of social life: social protections and public services introduced in the 20th century to protect society from the market have been increasingly privatized throughout the world. At both moments in history—the first decades of the last century and the present neoliberal episode—social reality was shaped by a utopian vision of the self-regulating market and the ideology of market liberalism. In both periods, the movement toward allegedly self-regulating markets was accompanied by counter-movements toward more regulation. If this historical comparison is sound, as we believe, Polanyi's analysis may have much to teach us about the present socio-economic landscape.[12]

Neoliberal economists claim that the current economic dysfunctions are due to policymakers' failure to embrace the capitalist logic, much as the liberals of the 1930s had blamed the Great Depression on monetary laxness. Revisiting the pre-Keynesian approaches of that time, Polanyi, in a true *tour de force*, managed to turn this liberal argument against itself by arguing that a market society cannot operate without debt; he showed that there is no invisible hand that dissolves social antagonisms (Maucourant, 2011).

Polanyi's theoretical framework can illustrate a structural similarity between the Great Depression of 1929 and the collapse of 2008. To maintain the social foundation of liberal capitalism after the First World War, European countries imposed duties on social wealth for the benefit of various social classes. The return to the international Gold Standard of the pre-First World War implied a sharp rise in financial yields. Increased debt enabled higher levels of aggregate demand to be satisfied in the short run. International credit—at the time more

[12]As Stiglitz (2001, pp. vii–ix) notes, 'Because the transformation of European civilization is analogous to the transformation developed countries face today, it often seems that it is as if Polanyi is speaking directly to present-day issues. (…) The most recent global financial crises reminded the current generations of the lessons that their grandparents had learned during the Great Depression: the self-regulating economy does not always work as well as its proponents would like to believe.'

receptive to political pressure than ever before—postponed the inevitable reconciliation of European imbalances. But if the new elasticity of the financial system put off the resolution of structural issues, it certainly did not solve them. In fact, the ballooning of debt permitted numerous European countries to roll over their previous loans instead of repaying them.

On both sides of the Atlantic, there were mutual benefits in the short term. By controlling European immigration and raising customs duty, the US had a somewhat incongruous high standard of living. Polanyi believed the US ought to have forgiven the war debt 'of'; In fact we have difficultes to understand the english translation probably because of our little understanding. the First World War, even though this would have entailed a decrease in the standard of living of Americans, due to the need to raise taxes. Alternatively, the US could have insisted upon repayment of its war loans, but adopted a more open immigration policy; this too would have lowered the average standard of living. Yet, America 'not only kept its debts, but to safeguard them, it also granted Europe massive loans' (Polanyi, [1933] 2008, p. 348; our translation). In such conditions, the British policy of acceding to creditors' demands that the pound sterling be revalued was inappropriate. Such a revaluation of the pound sterling implied a decrease in domestic prices. However, Britain's 'strong currency' policy could not be efficient, since the planned reduction of wages had failed in 1926. Thus, to maintain the value of the pound sterling, the dollar had to be less attractive. Support of the pound sterling, required an increase the interest rate differential between London and New York (Polanyi, [1944] 2001). This was the goal of the American 'Cheap Money Policy' in May 1927 that led to a transfer of the British imbalance to the US. Even though inflation of the debt was no longer encouraged by the monetary policy, by February 1928 the debt spiral and the stock market frenzy had gone so far that a liquidation crisis was inevitable. As soon as America gave up its credits, the liquidation process started, and this provoked the credit crisis in 1931. Polanyi reckons that prosecuting the war and then attempting to preserve the social order during peacetime heralded a new balance of power. Both led to the accumulation of debt, which was incompatible with the convertibility of currencies to gold. The policy of the creditor nation, i.e. the United States, had serious consequences: the will to sustain a certain type of claims and to closely control immigration both precipitated the global crisis.

Applying Polanyi's main intuition to the current crisis, we may note that neoliberal economists tend to forget that economic elites consider cheap-money policies and the expansion of debt to be necessary to maintain a growth rate that is sufficiently high to preserve their class dominance. This point is crucial to what follows. Had the US chosen a public health policy consistent with its economic power, and had it renounced its reckless acquiescence to demands for financial liberalization and 'free trade', the credit frenzy that occurred during the first years of the present century would not have been necessary. Free trade was a significant cause of the recent debt explosion: it led to the erosion of real wages (a fact not widely acknowledged by the conventional wisdom of the past two decades). China's often lamented trade surpluses—largely the counterpart of the US trade deficit—are the consequence of an accumulation model that is both deindustrializing and finance-based (Gréau, 2008; Jorion, 2007). The pre-crisis growth of the

US economy owed a good deal to technical 'progress' in the financial domain and to the decrease in the relative prices of some imported goods, which balanced out the downward trend in demand that was the inevitable outcome of a redistribution of productivity gains to a very thin social stratum.

The orthodox discourses that carp about financial malpractice conceal the fact that the dysfunctional practices in question are closely linked to the globalization policies advocated by orthodox economists. Had the US economy not contracted debts all over the world and increased the liquidity of its financial paper, it would not have been able to lend with such energy. Had the financial market been less creative and therefore less attractive, the US would have been unable to accommodate global savings. The central bankers were indeed blind to what was going on, but they were also trying to facilitate the dynamics of capitalism, which at a critical moment required low rates of interest and State guarantees on mortgage credits to enable the expansion of debt. Those central bankers had no mandate to induce economic stagnation, indeed depression, which might have shaken, or perhaps even destroyed, the foundation of market society: they were not authorized to let the economy experience the efficiency of the 'invisible hand' in the long term. The parameters for US monetary policy are not set by the President or the Federal Reserve, but by the global constraints of capitalism as it really exists. Lamenting over the increasing private debt, as neoliberals do, as though it were not necessary in the economic framework of the 1990s and after, amounts to pursuing the chimera of market society without recognizing the price of its continuation.

Finally, it seems that only institutionalized arrangements, which build various forms of group actions along with a market-based mechanism, can stabilize class conflicts and other social interests in a sustainable way. Markets do not operate in a social and cultural vacuum. Those institutions, whether in 1929 or 2008, impose economic levies upon society as a whole. The modern financial sector has enabled the level and type of growth that the inequality of our times structurally requires; but such growth has involved ever higher levels of risk which, while yielding considerable private gains in the short run, have generated a serious crisis and a massive socialization of costs in the medium term.

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