

A CONCEPTUAL FRAMEWORK FOR INTERPRETING HUMAN HISTORY

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The objective of this essay is to recombine many elements familiar to economic historians into a new approach that suggests a different understanding of the process of economic change and specifically of the course of human development. Social orders, as defined here, specify clear social boundaries to the human prospect and alterations in the boundaries create a new social order. The three social orders are 1) primitive societies, 2) limited access social orders or natural states, and 3) open access social orders. The shift from primitive societies to natural states was a shift from the limitations imposed by humans being confined to exploiting an existing resource base to the human ability to expand the resource base, a development which served as the source of modern civilization. The shift from the natural state to the open access society was made possible by the scientific revolution that eliminated the specter of diminishing returns and made the potential enormous productivity increase realizable by creating the competitive conditions of Adam Smith and the dynamic model of creative destruction implied by the Schumpeterian vision which together with the growth in the stock of knowledge produce the open access society. It could, however, be achieved only by creating in political and economic markets the institutional conditions for impersonal exchange. The fundamental building blocks for this approach are 1) consciousness and the development of beliefs, 2) the characteristics of human exchange, 3) the pervasive role of violence in history and 4)

the consequences of evolving specialization and division of labor throughout human history.

The first building block is essential because our understanding of the world around us is a function of the way the mind and brain interpret the external environment. Economics is correctly characterized as a theory of choice, but economists have neglected to analyze how we arrive at the choices we do. Consciousness in humans is self awareness in time and space and is the source of all the wonders of human creativity and of human "depravity." Whether the belief system is characterized by religious fundamentalism, Marxism, or the more eclectic choice theoretic framework economists assume, its nature is at the heart of the choices humans make which underlie human development.

Throughout most of human history and still today, personal exchange, characterized by individual contact and repeat dealings with the other party, has colored and shaped political, economic, and social exchange. This aspect of human interaction appears to have evolved into a genetic feature of human behavior over the three million years humans were hunter/gatherers and produced innate cooperative behavior in small group interaction and correspondingly distrust of "outsiders" and large group interaction. The antithesis, impersonal exchange, required fundamental institutional/organizational change to permit large group interaction among individuals and groups with no personal knowledge of each other.

Violence and the pervasive threat of violence either to gain access to resources or to protect resources underlie the structures humans create throughout human history.

The fourth building block is the institutional/organizational consequences of specialization and division of labor and is essential to more productive economies. As Adam Smith enunciated in 1776, specialization and division of labor underlies the increasing size of markets and therefore is the source of the Wealth of Nations. The specialization in knowledge that results from this structure is the underlying source of productivity increase and therefore economic growth.

These four fundamental building blocks interact with other features in the human experience--specifically aspects of the physical environment, climate and geography--, to shape the features of the first two social orders. It is only in the last millennium that humans have evolved a complex environment; the shift from the physical to the human environment as a basic determinant of the human condition is a major part of my story.

I

The origins of the first social order-primitive society--must focus on the physical changes in humans that led to language. Erect stature, the transformation of vocal chords, and increasing brain size were essential elements. Here our story can build on Merlin Donald's work, The Origins of the Modern Mind. Language permitted more complex social organization, predominately family and clans that produced primitive specialization based on sex in which men hunted and women gathered. The chronological changes--fire, tools, and weapons--- altered human relationship to animals and indeed it is hypothesized led to extinction of some large mammals. The artistic expression as evinced in the caves of Lascaux also demonstrated evolving human creativity. Population growth was very slow although local concentrations may have been responsible for diminishing

returns to hunting/gathering. A hunting/gathering economy is limited to small size units and extracts from the resource base it does not, however, add to that base.

II

We have characterized this order as the "natural State" because it combined a set of features that were consistent with the genetic predisposition of personal exchange. As a consequence it produced a social structure which has proven to be almost impervious to fundamental change. Evolving out of the enormous productivity change inherent in humans creating resources rather than simply exploiting the existing resource base, it permitted growth and a wide diversity of political, social and economic structures. The development of agriculture led to permanent settlement and the growth of specialization in production and exchange. A consequence was an hierarchical social structure in which elites evolved at the apex of commerce, trade, agriculture, as well as religion and particularly military organization. The evolution of religions provided the basic belief system that dictated the social structure and the nature of the elites. The state was made up of an interdependent group of such elites whose well-being rested on restricting entry into each of the occupations so that rents would accrue from the monopoly position of the elites. Well specified property rights defined the overall structure including the recognition of privileged rights of elites and the restricted rights of the great majority who were outside the elites. The resultant rents bound the interest of elites to the current dominant coalition. Any threat to the existing coalition threatened the rents of all elites because a breakdown in social order reduces everyone's rents. In addition the rents provide incentives for policies that increase stability and trade. The wide diversity of natural states reflected the path dependent pattern in diverse physical environments and

diverse competitive conditions. A major source of change internal to the natural state was the evolution of military technologies which at times favored larger political structures (the evolution of the nation state) and at others small political entities (such as feudalism). A wide diversity of both political and economic organization ensued in different settings. Capitalism, socialism, communism, fascism have all been natural states as have oligarchies, single dictators, and even limited democracies.

I can fill in our analysis with some historical description of the diverse patterns of development of natural states. Take the classical world. The belief systems that evolved from the temple society of Egypt, where the pharaoh was both the ruler and a god, to the Jewish order that developed in Israel, to the triumph of Christianity in the Roman world all defined the social structure. In contrast to primitive societies settled agriculture necessitated a much more complex social and economic organization. Exclusive property rights must be established to exclude non-members of the community from sharing in the output generated by community action. Violence potential both within and between political-economic units was a critical underlying influence upon the structure and hence performance of economies in the ancient world. While geographic constraints determined viable size of political units those constraints must be melded with the characteristics of military technology to explain the internal control structure and the consequent structure of property rights that evolved.

Did the industrial revolution produce radical alteration in the structure of economies? In terms of technological change and substantial increase in productivity the answer is yes. In terms of institutional/organizational structure the answer is not necessarily. Most economies still today are natural states. Even with radical alteration in

productivity potential, the domination of political and economic markets by elites that restrict entry characterizes most societies. Indeed the common feature of all the foregoing stories is that their structure is built on limited entry into both economic and political markets. The result is some growth in productivity and economic expansion and a resolute resistance to fundamental change in the social order. But realizing the potential of the technological development made possible by the scientific revolution required large and therefore impersonal markets and such fundamental change required a shift from personal to impersonal exchange-a movement that ran counter to the innate genetic predisposition-and had to be built around the creation of impersonal social/economic structures and the effective establishment of the rule of law.

III

Open access societies are characterized by competition in both economic and political markets which results in monopoly rents being temporary in character and therefore providing the actual setting for the kind of competitive order that was extolled in the neo-classical model. Missing, however, was an understanding of the necessary institutional specifics to realize the welfare implications of that model. This social order embodies a combination of the welfare features of Adam Smith's competitive market with the dynamic features of Joseph Schumpeter's "creative destruction" economic order. Necessary conditions are the interplay of economic and political institutions that will prevent monopoly in either market and impersonal exchange which will permit the economies of large scale production necessary to realize the potential of modern technology. Access is not dependent on personal relationships with the government. In politics, people have rights by virtue of being citizens, not by virtue of their relationship

with those in power. Open access orders are capable of legally supporting a wide variety of organizational forms. Most organizations, even those that are ostensibly voluntary, rely on some aspect of third party enforcement and are thus contractual organizations. Third party enforcement enables individual organizations to develop highly articulated and sophisticated internal structure and external relationships with individuals and organizations. The creation of effective economic, political, and social organizations through the use of contractual third party forms by the state dramatically reduces the coordination problems inherent in such large institutional/organizational structures.

Our understanding of the gradual development of open access societies in the western world owes much to Avner Greif's pioneering studies first of the Genoese and Mahgribi traders in Mediterranean trade in the twelfth century and then his description of the Community Responsibility System that provided an intermediate step from personal to impersonal exchange. In the former case he detected systematic differences in the organizational structure of Mahgribi and Genoese traders traceable to contrasting individualist versus collectivist behavioral beliefs. Islamic traders developed in group social communication networks to enforce collective action. Such networks did not lend themselves to the impersonal exchange that arises with the growing size of markets and diverse ethnic traders. The Genoese, in contrast, developed bilateral enforcement mechanisms which entailed the creation of formal legal and political organizations for monitoring and enforcing agreements-an institutional organizational path that permitted and led to more complex trade and exchange. The Community Responsibility System made entire communities responsible for the actions of its merchants, thereby supporting long distance trade and providing an intermediate step to the polity eventually

undertaking third party enforcement of contracts. In both stories it is the interaction of evolving economic and political institutions that is the key to the story. The Dutch and then the British exploited the potential of greater political and economic freedom.

Both the British and the Dutch began their overseas adventures by creating corporations. The first British joint stock company was the Russian company formed in 1553, followed by the African company. Both the British and the Dutch created East India Companies. These corporations were pure natural state creations with charters granting them all the traditional monopoly privileges, but they also were impersonal bodies granted perpetual life by a polity. There was a tension and an asymmetry between a mortal state creating an immortal organization. A perishable state cannot guarantee perpetual rights. A state had to be envisioned whose definition as an organization extended beyond the personal exchange perception of a state identified with specific individuals. A changing perception of the state was the gradual result; A constitutional government replaced the personal individual royal person. It was this interplay between economic change and political change that gradually evolved the elements of an open access political economy. With my colleague Barry Weingast I tell a part of this evolution in the case of Britain. (cite)

Why is this transition so difficult and why is it possible for open access states to slide back into Natural states? The ubiquitous effort of entrepreneurs to protect themselves from the uncertainties inherent in a competitive market makes the attempt to establish secure monopolies a constant in history, as Adam Smith reminded us several centuries ago. In his Rise and Decline of Nations, Mancur Olson maintained that periodic revolutions were essential to prevent the development of special interest groups that

would throttle growth by creating monopolies. The modern history of Argentina demonstrates how easy it is for societies to regress. Because the road to secure monopoly requires at least the acquiescence of the polity, it is that body that is the key to the maintenance of an open access society. We know all too little about the dynamics of political change. Where open access societies have persisted, such as in the United States, the reason has been the creation of adaptively efficient institutions which in the face of the uncertainty that characterizes the human condition have encouraged trial and error experimentation (a position argued by Friederick Hayek, who first recognized the uncertainty that pervades our future). The antithesis characterized the Soviet Union with the inevitable consequences.