TRANSACTION COSTS, EMBEDDEDNESS, AND THE EX ANTE DISTRIBUTION OF QUASI RENT[1]

Bruno Varella Miranda

Master in Administration – University of São Paulo

bvarella@yahoo.com.br

Maria Sylvia Macchione Saes

Department of Administration – University of São Paulo

ssaes@usp.br

This work relates the ex ante distribution of quasi-rent to the notion of embeddedness. Since the mid-1970s, the governance perspective (Klein; Crawford; Alchian, 1978; Williamson, 1985, 1996; Klein, 2002) has been dedicated to explaining the mechanisms used for the ex post protection of quasi-rent. Aspects related to the ex ante distribution of this value, however, are neglected in the literature. In the following pages, it is argued that the use of an abstract conception of the market from the governance perspective contributes to the adoption of heroic assumptions, and consequently to inattention to the issue of distribution. In particular, the theory assumes that agents are fully capable of determining ex ante what the reward is for their contributions in a cooperative relationship (Klein, 2002; Williamson, 1991). This paper questions this assumption, as well as the design used by the market governance perspective. More specifically, it posits that the difficulty of obtaining the relevant prices for specification of the quasi-rent increases as specific investments are made. As a result, the incentives offered to agents in a cooperative relationship can differ from their actual contribution to the achievement of a goal. Two main consequences derive from the theoretical redefinition of the interaction space of economic agents: i) enrichment of the idea of "transaction cost", with the use of the idea of the existence of "costs of using the price mechanism" (COASE, 1937); and ii) the effective integration of the concept of embeddedness to the perspective of governance.

---

[1] This work was supported with funding from the National Council for Scientific and Technological Development (CNPq). We appreciate the valuable comments of Ana Celia Castro, Ricardo Abramovay, and Rubens Nunes. Errors and omissions are the sole responsibility of the authors.

I. **The Problem**

This work relates the ex ante distribution of quasi-rent to the notion of embeddedness. The existence of quasi-rents results from the realization of specific investments, corresponding to the difference between the asset's value to the purpose which led to specialization in production, and its best alternative use (Klein; Crawford; Alchian, 1978, p. 298). Since the mid-70s, there has been growing understanding about the mechanisms of ex post protection of quasi-rent (Klein; Crawford; Alchian, 1978; Williamson, 2005). Distributional aspects, however, have been neglected by the literature. The reasons are varied: we can point out the emphasis on efficiency in comparative institutional analysis, or the belief in the capacity of governance structures to ensure order.

Regardless of the reason given, it relates to the scenario in which theory is presented. In other words, neglect of the distribution aspect is due to the market concept in the literature. Analysis from the governance perspective (Williamson, 1985, 1996) has been developed in an environment similar to that designed by neoclassical economics. Characterized by its abstract nature, this idea of the market contributes to the maintenance of heroic assumptions: it is assumed, for example, that individuals are always able to define ex ante the rewards derived from participation in a cooperative relationship (Klein, 2002; Williamson, 1991).

This paper questions this assumption. Going further, it argues that the governance perspective disregards elements of the scenario that it intends to analyze. The consequences of the existence of variability among the assets are a prime example. By reducing the number of stakeholders in produced assets, the performance of specific investments contributes to greater difficulty in defining the quasi-rent. Consequently, the distribution of gains from a cooperative relationship is not influenced exclusively by the organizational arrangements described by the governance perspective.

The illustration of the distributive problem does not only imply a redefinition of the notion of market used by the market governance perspective; derived from the scenario in which it is inserted, the interpretation of the idea of transaction cost is also enriched. In particular, it is possible to recover a little-explored aspect of the Coasean contribution, namely the existence of costs of discovering relevant prices (Coase, 1937).

Under this new perspective, the notion of transaction costs is not limited to the characteristics of the exchange, instead assuming a broader character which highlights the interaction between individuals and the markets.

The recognition that coordination is the basis for conscious interaction in the economic sphere, not a response to the constraints of an abstract system, is essential to identify the distributive problem. Obtained through the operation of specific arrangements, specializing in the collection and dissemination of information, the relevant prices may be unavailable to many agents. In such cases, the definition of ex ante rewards may differ from the actual contribution of individuals. The stability of a cooperative relationship could thus lead to results different from those predicted by economic theory.

Hence the importance of adding the notion of embeddedness to the study of conscious coordination. This work accomplishes the task in two steps. First, it demonstrates the potential for integration between the structural approach (Granovetter, 2005; Uzzi, 1996) and the governance perspective. Next, it highlights the potential opened by the contribution made by Beckert (2007) toward deepening the study of the relationship between embeddedness and economic organization. Closer to the original idea of Karl Polanyi, this proposal assumes that embeddedness corresponds not only to participation in social networks, but to a complex combination of political, ideological, and social factors able to stabilize a market (Beckert, 2007).

The next section describes the evolution of the concept of transaction costs starting from the pioneering contribution of Coase. Subsequently, parts III, IV, and V discuss the abstract concept of markets used by the governance perspective, highlighting the limitations provided by its adoption to the study of economic organization. Special attention will be paid to the effects of the existence of specific assets used in a scenario with homogeneous goods. Finally, section VI discusses the desirability of adding the notion of embeddedness to the analysis of conscious coordination.

II. The notion of transaction costs: from Coase to Williamson

The evolution of a concept in the social sciences reflects the choices of those who employ it. These are difficult to understand when analyzed individually, influenced as they are by the theoretical framework that they challenge. An illustrative example is the idea of "transaction costs": Ronald Coase does not define them with precision in "The Nature of the Firm," but merely enumerates the activities that determine their existence. When referring to the existence of "costs of using the price mechanism," he relates (i) the discovery of relevant prices, and (ii) the negotiation and conclusion of contracts (Coase, 1937, p. 390).

Although the content of "The Nature of the Firm" is open to interpretation, some of its aspects are undeniable. More than a rupture, Coase proposed an amendment to neoclassical economics; in practice, he extended the logic of efficiency to conscious coordination. Furthermore, the existence of costs to use the price mechanism is recognized in a scenario similar to that designed by the Walrasian paradigm. The emergence of the firm would result from the comparison between the costs of organizing activities with the help of the "invisible hand" or under the orders of an individual.

It is not easy to determine what functions are performed by the entrepreneur in the Coasean firm. Likewise, the effects of the existence of these costs on the daily lives of individuals are rarely explored in "The Nature of the Firm." Evidence throughout the text demonstrates the concerns of Coase, for example calling attention to a statement by Usher, for whom "[...] the successive buying and selling of partly finished products were sheer waste of energy" (Coase, 1937, p. 391). As a result, contract costs would derive from expending time in negotiations to finalize the exchange.

Some lines prior, Coase argues that the assumption that all relevant prices are known by individual actors is not supported by observation of the real world. This conclusion leads him to point out the cost of discovering such information as the most obvious among those he lists (Coase, 1937, p. 390). The amendment he proposes to neoclassical economics thus goes beyond the recognition that using the price mechanism is not free; Coase questions the ability of agents to obtain the data transmitted by operation of the "invisible hand."

It is only after decades of neglect that "The Nature of the Firm" begins to exert influence on social scientists. To a large extent, the Coasean explanation for the problem of externalities accounts for the increased interest in his work. Since the 1960s, there have been a considerable number of interpretations of Coase's legacy. One is the governance perspective (Williamson, 1985, 1996), whose explanation for economic organization is based on the contribution of a number of authors. This approach is underpinned by names as diverse as Chester Barnard, Friedrich Hayek, Herbert Simon, and Kenneth Arrow, among others.

It would be a mistake, therefore, to equate the governance perspective to the operationalization of the Coasean contribution. Although the arguments of "The Nature of the Firm" inspire Williamson, it is clear that the interpretation for the existence of transaction costs stems from many influences. His arguments do not merely reproduce the logic of the firm as a proxy for the price mechanism, as Coase argued (1937, p. 389). Governance structures that Williamson describes interact with the market, which leads him to say: "[...] the problem of economic organization is properly posed not as markets or hierarchies, but rather as markets and hierarchies" (Williamson, 2002, p. 175).

By recognizing that the firm does not replace the market, the governance perspective makes it possible to study the interaction of economic agents with the scene they inhabit, but that is not what happens. It is rather curious that the main hypothesis put forward by Williamson depends to such a large extent upon the characteristics of transactions.[2] In his approach, the relations of individuals are conditioned by the number of potential partners for a particular exchange. In the presence of specific assets, constant coordination is the rule; when there are no idiosyncratic investments, the "invisible hand" suffices to ensure order.

The main reason for this outcome is the scenario into which Williamson introduces his theory. The governance perspective uses an abstract conception of markets, similar to that adopted by neoclassical economics. In them, agents have full access to the relevant price and can define what is at stake in a transaction. Problems of

[2] According to Williamson (1985, p. 18), the efficiency of economic organization stems from the alignment between the characteristics of the transaction—with an incontestable focus on the specificity of assets traded—and the governance structure chosen by the parties.

an allocative nature result from the absence of guarantees for idiosyncratic investments. In other words, conscious coordination is not due to a deficiency inherent in the pricing mechanism; the idiosyncrasy of an asset, after all, is related to the number of people interested in acquiring it.

One of the consequences of using an abstract conception of markets is the emphasis that the governance perspective gives to the analysis of ex post contracting.[3] Considering the adoption of the efficient alignment hypothesis (Williamson, 1985), it is natural that attention is drawn to the protection of specific investments. Conscious coordination, seen as a response to the possibility of cheating, involves agents interacting in the market under similar conditions. Cooperating means establishing a framework that allows the realization of mutual gains, which adapts itself according to circumstances.

There is a remarkable contrast between the definition of "transaction costs" submitted by the governance perspective and the ideas discussed by Coase. In "The Nature of the Firm," the existence of "costs to use the price mechanism" also relates to events of an ex ante exchange. One in particular is little explored in most interpretations of the Coasean legacy, namely the process of discovering relevant prices. The reason, according to Williamson (2002, p. 180), is that Coase's argument does not survive the comparative institutional analysis.

This is certainly the case when the market in which the theory is inserted is similar to that described by the Walrasian paradigm. A closer look into the interaction space of economic agents, however, results in a different outcome. The next section discusses the design adopted by the perspective of governance, pointing out the

---

[3] Although also relating the existence of transaction costs to activities undertaken ex ante, the governance perspective pays scant attention to the preparation, negotiation, and protection of formal agreements. To a large extent this is due to the adoption of the efficient alignment hypothesis, which ultimately determines beforehand the result of contractual negotiation. Not coincidentally, Williamson (1991, p. 277) argues that the central problem of an economic organization is related to the "adaptation," an action clearly linked to the ex post dimension of the transaction.

inadequacy of this abstract view. The role of conscious coordination in the existence of an environment that allows the most varied forms of exchange will be emphasized.

III. The governance perspective and its setting

Markets do not emerge spontaneously. As shown by a growing literature (North, 1991; Grief, 2008; White, 1981), the conjunction of several factors explains their emergence. The operation of a complex bureaucratic apparatus shows that behind the assumptions adopted by neoclassical microeconomics are plenty of flesh and blood individuals. It is curious, then, how markets are described by most economists. Although the degree of abstraction used varies, representations such as the Walrasian auctioneer cause surprise at first sight.

The revival of early economic thought helps in understanding this option. Thanks to the philosophical commitment of questioning the government's role in the organization of society, the discipline fathered by Adam Smith specializes in discussing the allocation of resources in a decentralized system. As a result, the price mechanism, a structure independent of any particular human will, is the principal vector for the formation of a desirable balance. No matter if it lacks compassion for the baker, the butcher, or the brewer: the supposed ability of self-regulating economic system makes selfishness a social virtue.

Claiming that the king should not opine on every aspect of daily life, however, does not imply the conclusion that a society is better when nobody has the final word. Adam Smith himself, in Book V of "The Wealth of Nations," recognizes that certain activities may be performed by state authority. Limiting the role of the state is justified by the existence of obvious advantages in dispersing the decision-making prerogative according to the relative ability to take it. The logic of division of labor applies to the provision of institutions; the benefits of specialization will also apply to the production and application of rules.

Varying needs also explain the considerable presence of organizational diversity. The latter, far from responding only to the challenges posed by spontaneous phenomena, enables human society. Exemplifying this are organizations that enable the functioning of price mechanism: numerous arrangements, specialized in information processing, provide relevant information to agents. The abstract description of the markets thus exposes only the outcome of a complex process of social interaction. The "invisible hand," whose name suggests a mechanism independent of human action, depends on conscious coordination.

Although it is possible to study various issues without scrutinizing this dynamic, uncritical abstraction obscures fundamental issues. Behind a market considered "efficient," actual arrangements abound; whether a stock exchange, a marketplace, or a department within a firm, there are many structures dedicated to data transmission. Established by humans, they do not work for free, nor are they perfect. In other words, someone pays the bill for their maintenance, and likewise influences their characteristics. The identification of these organizations reveals important aspects of everyday economics.

What is, more specifically, the role played by conscious coordination in shaping an environment similar to that considered by most economists? The example of the stock exchange is illustrative. Responsible for the organization of markets similar to those predicted by the model of perfect competition, it relies on a considerable bureaucratic structure. Its existence emerges from the interest of thousands of agents in the assets it trades, which explains the division of operating costs. The information it provides, therefore, reflects the interests of those who demand it.

The example of the stock market is certainly not unique. Many existing arrangements are dedicated to decoding information and providing the relevant price to agents. Their organizational characteristics may differ considerably: compare a marketplace and a specialized department within a company. Nothing obscures, however, the similar functions performed in everyday society. It is the set of these structures that enables the existence of something like the price mechanism, and hence the success of neoclassical microeconomics in explaining a number of issues.

Many must be wondering what the difference is between the organizations listed above and those considered from the governance perspective. Based on the description given by Williamson (1991), it is possible to identify a series of contrasts. The main one corresponds to the nature of the organizational phenomenon analyzed in each case. Under the logic proposed by Williamson, conscious coordination responds to the characteristics of an abstract system. Heir to the prevailing market concept in neoclassical economics, it is limited to questioning the capacity of that environment to ensure order given the existence of specific assets.[4]

In other words, the governance perspective introduces idiosyncratic investment to a reality accustomed to standardized goods. The result is that Williamson (1991, p. 279), although proposing to study conscious organization in the social sphere, considers it a kind of last resort. Costs are assumed, it is true; but they do not restrict the dissemination of information in the economic system. Adapting the criticism of Hayek (1948, p. 45) to the Walrasian paradigm, the governance perspective sees the market as a system where "everyone knows everything."

The addition of new elements to a scene so dependent on its assumptions, however, has important ramifications. When entering variability into its model, the governance perspective changes the scenario devised by the Walrasian paradigm. The participation of a large number of individuals, the central feature of the markets described by neoclassical economics, gives rise to relations based on the exchange of idiosyncratic assets. It would therefore be insufficient to question the realism of the premises adopted by comparative institutional analysis; going beyond, we seek to identify the blind spots arising from this option.

IV. Relevant prices and asset specificity

What explains the existence of costs for discovering relevant prices? When trying to identify them, Williamson (2002, p. 180) concludes that the Coasean hypothesis is inconsistent with the comparative institutional analysis. However, his

---

[4] Besides asset specificity, Williamson (1985, 1996) argues that frequency and uncertainty are explanatory variables of economic organization. Their use for empirical ends, however, is limited, so idiosyncratic investments are still the main factor considered in efforts to legitimize the governance perspective.

conclusion reflects the characteristics of the theory on which the discussion is based. As in the treatment of other topics, including the advisability of integrating the notion of trust to organizational studies (Williamson, 1993a), what is observed is the strengthening of the analytical framework of governance perspective. Much is said about previous theoretical choices, but rather less about the desirability of strengthening the framework being challenged.

Guiding resource allocation, prices do not result from a spontaneous phenomenon, but rather derive from the organizational effort of the agents. Their availability is conditional on the features of arrangements that they discover, as well as resulting expenses. The costs of discovering relevant prices, identified by Coase, can be interpreted as a consequence of the operation of the "invisible hand." They complement, in this way, Williamson's (1985, 1996) view that associates transaction costs with the governance of transactions.

The specificity of the process of price discovery is important in its direct relationship with the individual. Going beyond concern with the characteristics of the exchange, it is necessary to understand who participates in it and how it fits into the scenario in which they live. Personal skills should be considered, as well as the interaction of agents with the surrounding organizational structures. It is worth noting this dynamic based initially on the fundamental hypothesis presented by the governance perspective. In other words, the elements of this theory are embedded in a more realistic description of the market in order to highlight the distributional problem

The identification of the existence of costs to the discovery of relevant prices raises the question: who incurs them? Selfish agents will pay the bill only if they obtain corresponding benefits. Conceivably, therefore, the free transfer of information will not occur in a setting populated by agents similar to *homo economicus*, unless the costs of protection are prohibitive. The search for minimizing the costs of discovery similarly motivates the emergence of diverse organizational forms.

The typical market described by the Walrasian paradigm, characterized by the interaction between a large number of agents, is organized around the marketing of identical assets. Broad participation allows the sharing of costs of discovering relevant prices. The result is the realization of a scenario similar to that provided by neoclassical economics, both in allocative and distributive terms. The recognition of organizational arrangements behind the "invisible hand" does not affect this conclusion; adapting the argument of Coase (1937), costs incurred are justified according to the logic of efficiency.

A different situation emerges when the assumption of identity of the assets is abandoned. The individual cost of discovering relevant prices increases with the increasing level of specificity of the assets traded, due to the inability of existing organizations in the typical market of perfect competition to translate the information spread throughout the economic system into rewards for individuals. Consequently, the agents establish alternative arrangements, incurring costs. A firm could, for example, create a specialized department to collect data to guide their decisions.

That does not mean that the information provided in the typical Walrasian market is useless in an exchange of idiosyncratic assets. This obviously follows as a reference to the parties; the definition of quasi-rent, however, depends upon the establishment of alternative organizational arrangements. Other factors, such as agent skills, are also important. In fact, Coase (1937, p. 390) draws attention to the role of specialists in obtaining information. Moreover, the individual costs of discovering relevant prices can differ considerably according to participation in social networks (Uzzi, 1996).

As a consequence, the relationship between producers and final buyers is frequently indirect. The data used by the contractor results from its ability to obtain them, or the establishment of a specialized arrangement. The producer of an asset, on the other hand, may be unable to estimate market demands, and thus the resulting reward. The cost of obtaining the information is the main reason, insofar as it can be prohibitive to many individuals. The incentives for adaptation thus derive from the action of a "visible hand" that allocates responsibilities and rewards.

Considering the possibility that agents are opportunistic (Williamson, 1985, 1993b), nothing guarantees that information unavailable to the partners in a transaction is transferred. Rather, the apparent stability of a contractual relationship may mask the incompatibility between their contributions and rewards. Likewise, similar organizational arrangements may have varied relationship patterns. The hypothesis of efficient alignment would not show more than "the tip of the iceberg"; behind the efficiency of a governance structure, there would be room for opportunism.

Put another way, since one party holds relevant knowledge about price and is able to translate it into incentives, it is expected that the result of cooperative action be efficient. These arrangements, however, may lead to individual economic outcomes different from those predicted by the perspective of governance. Behind the hypothesis of efficient alignment, heterogeneity would predominate; the difference of this problem to matters traditionally addressed by the literature, and the relevance of the concept of embeddedness for its study, will be the topic of the next sections.

V. Information and conscious coordination

The evolution of the concept of "transaction cost" in economic literature has observed, to a large extent, the limitations imposed by the Walrasian paradigm. Beginning with the pioneering contribution of Coase (1937), several authors presented their own interpretations of the term. In previous sections it was argued that the governance perspective, equating the idea to the costs arising from the use of contracts, presents an impoverished picture of reality.

A notion derived from the scenario used by analysts, the idea of transaction cost loses much of its force when it emerges from an unrealistic view of the market. The main consequence of this option is the assumption made about the nature of the economic organization: instead of a willful act of economic agents, this is seen instead as a response to the constraints of an abstract system. The hypothesis of efficient alignment is an excellent example; although Williamson (1991) strives to add greater complexity to its interpretation for constant coordination, the difficulty in transposing this attempt to an empirical basis is evident.[5]

Still, it would be wrong to consider that the recognition of the existence of costs of price discovery is impossible in an abstract setting. Coase does so in "The Nature of the Firm," which is the embryo of the theories of the firm which emerged later. Nearly five decades later, Cheung (1983) follows the example of correlating this category of

---

[5] As previously stated, the main studies on the governance perspective are limited to drawing a relationship between asset specificity and the choice of organizational form. For a list of empirical applications, see Shelanski; Klein (2005) and Richman; Macher (2006). For a critique of the application of some of these studies to the theoretical content of the governance perspective, see Carter; Hodgson (2006).

transaction costs to the problem of measurement. With respect to the difference in perspective, it's worth noting how the discovery and minimization of the costs of discovering relevant prices occur in his work.

By and large, Cheung offers four reasons for the costs of discovering relevant prices. One is the cost of getting to know the price of each component of a product (Cheung, 1983, p. 7). A consumer would incur unnecessary—and often prohibitive—costs in negotiating the amount corresponding to each share of a good being acquired, a situation no better than allowing one firm to be responsible for providing a single price for the product. Cheung explains that it is advantageous to leave the negotiating to the producers, since they are specialists.

What Cheung does not explicitly state is the reciprocal nature of the problem. In a world inhabited by atomized individuals, the difficulty for the consumer in determining the relevant prices of each component that he acquires is similar to that faced by owners in determining their contribution to the total asset value. Although owners may be experts capable of obtaining the relevant prices at a low cost (Cheung, 1983, p. 7), there is no guarantee that this is the case. In fact, the ability to produce a given good does not necessarily imply the ability to determine its value.

The identification of this peculiarity of the human interaction process is important because it illuminates a central aspect of economic discourse. Since the beginnings of the discipline there has been concern about the alignment between the contribution of each individual within the system and corresponding reward. Nearly two centuries after Adam Smith's contribution, Alchian and Demsetz (1972, p. 778) argue that productive cooperation achieves better results when this question is properly considered.

The coexistence of this concern with the assumption of full knowledge of the relevant prices, however, led to a predictable outcome: limiting the possibilities for cheating in the daily economy. Room was left for the theoretical treatment of problems such as adverse selection (Akerlof, 1970) or shirking (Alchian, Demsetz, 1972). Both of these issues are characterized as representing a breach of promise. In both cases, the individual violates an agreement, either by offering a good with different characteristics from those which were agreed or by working less.

Not coincidentally, from the theoretical point of view, the success of coordination has been synonymous with conscious fulfillment of promises previously made. In a world where everyone is able to define what to expect from partners, indeed there isn't much more to do. The impression one gets is that the arrangements operate automatically as a result of the participants' harmony.[6] Minimizing the costs of governance becomes the primary goal; one even assumes that decisions in a chain are based solely on the search for efficiency (Arruñada, 2002).

It is important, in order to complete this section, to contrast the problems typically handled by the governance perspective with the content discussed over the last few pages, a discussion reaching beyond the mere fulfillment of promises; we sought to show that access to information made available by the "invisible hand" is not automatic. When one considers that the price mechanism is the result of numerous bureaucratic structures operating simultaneously, it is clear that the transfer of data can be a problematic issue. Cognitive, cultural, and institutional peculiarities, among others, determine the outcome of this process.

VI. Embeddedness and economic organization

The notion of embeddedness is incorporated into the new economic sociology through the contribution of Granovetter (1985). Its origin shares similarities with the idea of "transaction costs": Karl Polanyi, the term's pioneer, does not define it precisely. Not surprisingly, there is a considerable wealth of interpretations about what embeddedness means. This lack of consensus, recognized by Smelser and Swedberg (1994, p. 18), led to proposals such as Zukin's and DiMaggio's (1990), which identified four approaches to embeddedness, namely: cognitive, cultural, structural, and political.

[6] The definition of reputational capital provided by Klein (2002) is illustrative. According to Klein, the calculation of reputational capital would result from the estimate of future earnings derived from a cooperative relationship. Holdup, accordingly, would result from the perception that cooperation would yield a lower return than the alternatives available. However, it is worth questioning the value of spending on alternative governance structures in a context where maximizing agents have full knowledge of what the future holds for them.

Among the dimensions of embeddedness described by Zukin and DiMaggio, that which can most easily adapt to the governance perspective is the structural approach (Granovetter, 2005; Uzzi, 1996). Ironically, this movement arises from Granovetter's (1985) criticism of Oliver Williamson's research program. Both proposals, however, far from representing irreconcilable points of view, have considerable potential for integration. To a large extent, this possibility is owed to the identification of the pattern of relationships between the actors as the central variable for the explanation of economic outcomes (Granovetter, 2005).

It is no stretch to identify the benefits derived from integrating Granovetter's ideas to the governance perspective. The importance of broadening the notion of transaction costs makes the insertion of a network a central variable to explain the acquisition of information. Uzzi (1996) demonstrated this by analyzing a market approaching the model of perfect competition; the structural approach, therefore, finds fertile ground even with the retention of an abstract market conception.

Maintaining the hypothesis of efficient alignment is not an impediment to theoretical integration. Granovetter's criticism (1985) focuses on the impression that, for Williamson, vertical structures would be able to mitigate all the problems arising from conscious coordination. A different situation emerges when new problems are identified in the original status quo; the issue of distribution would most certainly benefit from the analysis of networks and their effect on the individual costs of discovering relevant prices.

It is worth noting that the structural approach does not explore fundamental ideas found in the original formulation of the idea of embeddedness. According to Beckert (2007), the interpretation provided by Granovetter differs substantially from the way in which Polanyi incorporates it in his work. Far from equating markets to producers' networks, Polanyi considered them as full social institutions, reflecting a complex mix of politics, culture, and ideology (Beckert 2007, p. 9), hence the need for a careful analysis of the area of economic interaction of individuals.

The full understanding of the economic results does not only depend on assessing the pattern of relationships between the agents; going further, it is essential to understand how these individuals—or organizations—fit into the broader context, as well as the characteristics of this context. Beckert (2007, p. 11) identifies three coordination problems, which are: i) valuation of goods; ii) competition among agents; and iii) cooperation, derived from the risk inherent in the transaction.

The relevance of Beckert's proposal lies in the perspective it opens for the study of economic organizations based on multiple dimensions. It is also likely that the deepening of the understanding of the foundations for establishing a market leads to the emergence of alternative hypotheses for the study of economic organizations. Future studies able to scrutinize the complex relationship between the different dimensions of human interaction are likely to provide an alternative to a tool that, even among peers, raises considerable controversy.[7]

For the purposes of this study, it is sufficient to demonstrate that the notion of embeddedness, in its most popular interpretation, is perfectly compatible with the perspective of governance. This task was accomplished by identifying a problem overlooked by the literature, namely the ex ante distribution of quasi-rent. The identification of an inconsistency between the scenario used by Williamson and the adoption of the assumption of asset variability shows that, behind the hypothesis of efficient alignment, heterogeneity is the rule, creating the need for additional ideas for dealing with this reality.

The statement in Beckert's work, however, is crucial for demonstrating a promising line of theoretical evolution. A central variable in explaining the diversity in the results collected by economic agents in their market penetration, embeddedness cannot be limited to participation in social networks, as part of the literature seems to suggest (Uzzi, 1996, Granovetter, 2005). Rescuing the Polanyian legacy will certainly mean focusing attention on the arena of individual interaction and its complex dynamics. The stability of markets is not in fact automatic, but depends on the conjunction of a number of factors. Likewise, several equilibria are possible, so that the perception of order may vary according to analyst expectations.

---

[7] Even among the institutionalists there is no consensus about Williamson's approach. See, for example, Demsetz (1993, p. 166).

VII. Final considerations

In a lecture given at the University of Missouri in 2002, Ronald Coase said that economic analysis needs to change. Comparing it with other areas of knowledge such as biology and physics, he highlighted the resistance of economists to incorporating new ideas into their daily routine. Coase noted that while the thinking of Charles Darwin or Isaac Newton is being replaced by new contributions in their disciplines, the economy remains true to the works of Adam Smith, or textbooks from the late nineteenth century such as those of Alfred Marshall.

While economics' ability to answer a series of problems is undeniable, Coase makes a precise diagnosis of its main limitation. According to the 1991 Nobel Prize winner, economics fails to study the functioning of the economic system as a whole. In the name of formalism, the choice has been to isolate each of the elements of that system as if their relationship would not influence the final results. Not coincidentally, economics has specialized in the generation of data on specific phenomena; the understanding of broader transformations, however, has been precarious.

This article agrees with Coase's diagnosis and seeks to build on it. The solution to this problem, it seems, encompasses the redefinition of the space of theoretical interaction fundamental to the discipline: the market. While the abstract conception of the market prevails, it is only with great difficulty that the blind spots offered by the marginalist analysis can be overcome. The pages above aim to demonstrate that the progressive addition of new elements to the scenario used by economists eventually mischaracterizes it.

The above analysis maintains Williamson's fundamental hypothesis mainly for didactic reasons: the goal, over the last few pages, was to show that the "order" suggested by the governance perspective only materializes when very specific conditions are considered. Adding elements such as the variability of the assets used by the typical scenario in the Walrasian paradigm, however, makes supporting these conditions a rather complicated task.

Clearly, the adoption of an enriched conception of markets—and of the agents involved in the environment—also has implications for the establishment of hypotheses for the study of governance structures used in an exchange. In this sense, the next step should be the specification of hypotheses for the study of economic organizations based on a more realistic scenario. In addition, two topics deserve attention in the future: i) the observation of organizational diversity in the real world, with special attention to the so-called plural forms; and ii) the actual relationship between the conscious organization and the institutional environment.

VIII. References

AKERLOF, George A. The market for "lemons": quality uncertainty and the market mechanism. **The Quarterly Journal of Economics**, Vol. 84, No. 3, 1970.

ALCHIAN, Armen; DEMSETZ, Harold. Production, information costs, and economic organization. **American Economic Review.** Vol. 62, No. 5, 1972.

ARRUÑADA, Benito. The quasi-judicial role of large retailers: an efficiency hypothesis of their relation with suppliers. *In*: BROUSSEAU, Eric; GLACHANT, Jean-Michel. **The economics of contracts:** theories and applications. Cambridge: Cambridge University Press, 2002.

BECKERT, Jens. The great transformation of embeddedness: Karl Polanyi and the New Economic Sociology. **MPIfG Discussion Paper 07/1.** Cologne: Max Planck Institute for the Study of Societies, 2007.

CARTER, Richard; HODGSON, Geoffrey. The impact of empirical tests of transaction cost economics on the debate on the nature of the firm. **Strategic Management Journal**, 27, 2006

CHEUNG, Steven N. S. The contractual nature of the firm. **The Journal of Law and Economics**, Vol. 26, No. 1, 1983.

COASE, Ronald H. The nature of the firm. **Economica**, Vol. 4, No. 16, 1937.

COASE, Ronald H. Why economics will change. **Remark at the University of Columbia.** Columbia, Missouri, 2002 Available at: http://www.coase.org/coaseremarks2002.htm.

DEMSETZ, Harold. The theory of the firm revisited. *In*: WILLIAMSON, Oliver; WINTER, Sidney (Eds.). **The nature of the firm:** origin, evolution and development. Oxford: Oxford University Press, 1993.

GRANOVETTER, Mark. Economic action and social structure: the problem of embeddedness. **The American Journal of Sociology**, Vol. 91, No. 3, 1985.

______. The impact of social structure on economic outcomes. **Journal of Economic Perspectives**, Vol. 19, No. 1, 2005.

GREIF, Avner. Coertion and exchange: how did markets evolve. **SSRN Paper Series,** 2008. Available at: http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1304204.

HAYEK, Friedrich. Economics and knowledge. *In*: **Individualism and Economic Order.** Chicago: University of Chicago Press, 1996 [c1948].

KLEIN, Benjamin; CRAWFORD, Robert G; ALCHIAN, Armen. Vertical integration, appropriable rents, and the competitive contracting process. **Journal of Law and Economics**, Vol. 21, No. 2, 1978.

KLEIN, Benjamin. The role of incomplete contracts in self-enforcing relationships. *In*: BROUSSEAU, Eric; GLACHANT, Jean-Michel. **The economics of contracts:** theories and applications**.** Cambridge: Cambridge University Press, 2002.

MACHER, Jeffrey; RICHMAN, Barak. Transaction cost economics: an assessment of empirical research in the social sciences. Durham: Duke Law School. **Legal Studies Research Paper Series**, Research paper No. 115, 2006.

NORTH, Douglass. **Instituciones, cambio institucional y desempeño económico.** México, Distrito Federal: Fondo de Cultura Económica, 1993

SHELANSKI, Howard; KLEIN, Peter. Empirical research in transaction costs economics: a review and assessment. **Journal of Law, Economics and Organization, Individualism and Economic Order,** Vol. 11, No. 2, 1995.

SMELSER, Neil; SWEDBERG, Richard. The sociological perspective on the economy. *In:* SMELSER, Neil; SWEDBERG, Richard (org.) **The handbook of economic sociology.** New York: Russel Sage Foundation, 1994.

SMITH, Adam. **An inquiry into the nature and causes of the wealth of nations.** Indianapolis: Hacket Publishing Company, 1993.

UZZI, Brian. The sources and consequences of embeddedness for the economic performance of organizations: the network effect. **American Sociological Review**, Vol. 61, No. 4, 1996.

WHITE, Harrison. Where do markets como from? **American journal of sociology,** Vol. 87, No. 3, 1981.

WILLIAMSON, Oliver. **The economic institutions of capitalism**. New York: The Free Press, 1985.

______. Comparative economic organization: the analysis of discrete structural alternatives. **Administrative Science Quaterly**, Vol. 36, No. 2, 1991.

______. Calculativeness, trust and economic organization. **Journal of Law and Economics**, Vol. 36, No. 1, 1993a.

______. Opportunism and its critics. **Managerial and Decision Economics**, Vol. 14, No. 2, Special Issue: Transaction costs economics, 1993b.

______. **The mechanisms of governance**. Oxford: Oxford University Press, 1996.

______. The New Institutional Economics: taking stock, looking ahead. **Journal of Economic Literature**, Vol. XXXVIII, 2000.

______. The theory of the firm as governance structure: from choice to contract. **The Journal of Economic Perspectives,** Vol. 16, No. 3, 2002.

______. The economics of governance. **The American Economic Review**, Vol. 95, No. 2, Papers and proceedings of the One Hundred Seventeenth Annual Meeting of the American Economic Association. Philadelphia, PA, 2005.

ZUKIN, Sharon; DiMaggio, Paul. Introduction. *In:* ZUKIN, Sharon; DiMaggio, Paul (eds.). **Structures of capital**: the social organization of the economy. Cambridge: Cambridge University Press, 1990.