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BAD FOR PRACTICE – GOOD FOR PRACTICE FROM ECONOMIC IMPERIALISM TO MULTIDISCIPLINARY MAPPING

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Abstract: There is a growing argument that economics can no longer provide any guiding schema for solving current management problems. Economic assumptions even destroy good and socially responsible management practice. In this paper, we analyze two reasons why standard economics can indeed be bad for managerial and political practice. One is the negative influence of wrong assumptions in economic theory building which become self-fulfilling prophecies. Another important factor is economic imperialism. We argue that psychological economics is better for practice than standard economics, but that it is still not good for practice as long as it uses an imperialistic approach. We propose a different research strategy to apply for problem solving in management practice, which we call multidisciplinary mapping. It overcomes the problem of imperialism, not only because it builds bridges between different disciplinary approaches, but also between the knowledge of theorists and the expertise of practitioners. Mapping is useful for realizing. It is good for practice as well as for theory building.

Keywords: economics, psychological economics, multidisciplinary mapping, maps, management practice, theory

INTRODUCTION

Current discussion about corporate scandals, the explosion in management pay and disastrous consequences of the transition process in Eastern Europe has given rise to the question of whether economics might be the wrong theory to solving current management problems. It is argued: economics is bad for practice (e.g. Ghoshal & Moran, 1996). Although the aim of organizational research is to discover, describe order, explain, and predict carefully defined social phenomena that characterize behaviors in organizations, the following examples briefly sketch negative influences of economic research on the practice of management and politics.

Ghoshal (2005), in a posthumously published article, lamented the fact that standard economic theories currently dominating the debate over corporate governance had wrecked good management practices and led to wrong decisions on incentive schemes or counter-productive pay for performance systems. These scandals are interpreted as the consequence of the dominant principal-agent and transaction cost view in corporate governance (see also Adler, 2002; Osterloh & Frey, 2005). The standard economic view is based on the assumption that opportunism is a worst-case scenario. Opportunism is considered to be a prudent consideration for institutional structures (Milgrom & Roberts, 1992; Williamson, 1996). However, prevalence of standard economic assumptions in the training of new managers at reputable MBA

centers leads to a situation in such a conception of human beings as opportunists tends increasingly to become reality. It would appear that the criticism voiced by Ghoshal and Moran (1996) in their frequently quoted article “Bad for Practice: A Critique of the Transaction Cost Theory,” is true: Williamson’s (1985) transaction cost approach is not only wrong but dangerous for guiding management and policy decisions.

Ferraro, Pfeffer and Sutton (2005) state that in the social sciences - unlike physical sciences - theory becomes normative guidance on how to act; the result is a self-fulfilling prophecy. The greater the influence the theories have, the more this is the case. In their view, this is also true of economics. The authors draw on Merton’s definition of a self-fulfilling prophecy as a prediction that “is, in the beginning, a false definition of a situation which denotes a behavior that makes the originally false conception come true” (Merton, 1948: 195).

Kogut and Spicer (2005) analyze the negative impact of economics on the transition process in Russia. They argue that the disastrous development in Russia is the result of the strong institutional ties of economists of Harvard and MIT to the World Bank and the international policy arena. The development in Russia in the nineties is characterized by a picture far worse than in other transition countries, with respect, for example, to the development of life expectancy, infant mortality and living standards prior to the reforms. The authors explain these negative consequences of the reform process in Russia by the dominance of economists and the near total “no-show” of non-economic disciplines like sociology and psychology.

The aim of our paper is firstly to point out why theories, particularly in economics, are often bad for management practice. We argue that being bad for practice is not only a problem of false assumptions but also a methodological problem. The latter problem lies in an imperialistic use of single theories, as is the case with economic imperialism. This problem will not disappear if economic theory is built upon more empirically valid assumptions about human nature. We demonstrate this with the example of the new and strongly growing branch of psychological economics which has questioned some crucial assumptions about standard economics as being endogenous to theory building and thus is clearly better for practice. However, if psychological economics uses the same methodology as standard economics in an imperialistic way; it is still bad for practice. Secondly, we will answer the question: Which research mode is good for practice as well as good for theory building? We propose a different research mode for management research: multidisciplinary mapping. It provides different disciplinary maps to gain insights from the difference between disciplinary views as well as between the views of scholars and practitioners.

ARE ECONOMICS BAD FOR PRACTICE?

In this section we will outline the standard economic model, its critics, and the model of psychological economics to show the methodological procedure of economics and its shortcomings.

The Standard Economic Model and its Critics

The standard economic model of homo oeconomicus is characterized by the following assumptions (e.g. Frey, 1999):

- Action is centered in the individual (methodological individualism). Everything that happens in institutions and society can be traced back to the actions of individuals.
- A strict distinction is to be drawn between preferences (i.e. values which form the basis of motivation) and restrictions (i.e. external stimuli of action and constraints on the scope for action).

- An individual's preferences are given and inalterable (Becker & Stigler, 1977). The individual's actions are determined entirely by restrictions.
- Only self-interested, not pro-social, preferences are assumed to exist. The preferences of other people do not concur with one's own preferences.
- The cognitive perception of restrictions is identical in all individuals.
- Individuals behave entirely rationally. They are able to determine their own maximum utility according to their own preferences within given restrictions.

It is on the basis of these assumptions that the standard economic model is applied to all spheres of life, for instance, to the family, drug abuse, abortion, criminality, art, sport, religion, and suicide. This is tied to the withdrawal (or, better, the ejection) of psychology from economics, which for Schmolders (1962) for instance, was still part of economics. Neoclassical standard economics has thus developed an imperialistic understanding of itself as the "queen of the social sciences" (Hirshleifer, 1985; Becker, 1976), a view which has provoked significant aggression and criticism among neighboring social sciences. Criticism of standard economics refers chiefly to these assumptions. In particular, this is about the assumptions regarding the cognitive and motivational characteristics of homo oeconomicus.

The criticism of the assumptions about the cognitive characteristics of homo oeconomicus is the least controversial. They go back to Simon (1955, 1956) and have led to the idea of bounded rationality as a consequence of people's limited capacity to process information. In contrast to the discussion of his cognitive characteristics, the criticism of the assumptions regarding the motivational characteristics of homo oeconomicus is controversial. One bone of contention is the assumption of self-interest, which has been significantly intensified in the transaction cost approach by the assumption of opportunism as the "seeking of self-interest with guile" Williamson (1985: 56). This argument is the backbone of the criticism of self-fulfilling prophecy: If institutional designs (e.g. measurement and incentive systems or selection processes) as well as expectations and frames are directed towards selfishness, people will react as if everybody is an opportunist. A framing and crowding-out effect of intrinsic motivation will take place.

Psychological Economics and its Critics

Psychological economics is a combination of economics and psychology.¹ It is concerned with the systematic divergence of human actions from the standard economic model of homo oeconomicus while retaining economic methods (e.g. Camerer & Loewenstein, 2004; Camerer & Malmendier, 2004; Frey & Benz, 2007; Kahneman, 2003; Mullainathan & Thaler, 2000; Rabin, 1998). It questions the 'homunculus oeconomicus' in three ways: through the issues of (1) bounded rationality, (2) bounded self-interest, and (3) the bounded utility concept.

(1) Bounded rationality: The findings of psychological economics go far beyond the vague concept of bounded rationality as applied in institutional economics. These show that divergences from the expected maximization of utility follow systematic conditions, which are dealt with under the term "decision anomalies." It is largely with this term that Kahneman and Tversky (1979; 1986) have founded the psychological economics branch of research.² Important decision anomalies include:

- Framing: the perception of a decision situation depends on the presentation of the situation.
- Anchoring: the appraisal of outcomes is influenced such that the first anchor is held against the final judgment, and new information is given less consideration as a result.

- Availability bias: individuals rely chiefly on easily gained information.

These decision anomalies contribute to a self-fulfilling prophecy effect: If the prevailing information you get leads you to an opportunist frame you will design institutions as if all or most people were opportunists. Empirical evidence shows that even experts are subject to these decision anomalies. In situations of great uncertainty, experts are more strongly affected by these decision anomalies than lay people, because they trust too much in their models and past data (Griffin & Tversky, 1992). In an experiment, the Economist (1984; 1995) found that dustmen were able to make better long-term predictions about economic development than ministers of finance.

(2) Bounded self-interest: In contrast to the assumptions of standard economics, numerous empirical results indicate that in many situations, people behave against their own interest in an intrinsically motivated prosocial manner. Intrinsic motivation is directed towards activities which are performed for their own sake rather than for any reward (Deci & Ryan, 1985; Frey, 1997; Osterloh & Frey, 2000). Extrinsic motivation, in contrast, is aimed instrumentally at activities which are not valued for their own sakes. They are, rather, undertaken for a desired reward or to avoid a penalty. Standard economic approaches deal exclusively with extrinsic motivation.

A dynamic relationship exists between intrinsic and extrinsic motivation. Under certain conditions, extrinsic motivation can crowd out intrinsic motivation. This leads to what have been termed the hidden costs of rewards; the existence of these hidden costs is well supported empirically by both laboratory experiments and field studies (Frey & Jegen, 2001). These show that, under certain conditions, external interferences (like pay for performance or monitoring) can crowd out pro-social intrinsic motivation (Frey & Oberholzer, 1997; Stukas, Snyder & Clary, 1999).³ The crowding-out effect provides a theoretical and empirical well-founded explanation for the self-fulfilling prophecy of the assumption of opportunism. If this assumption is introduced exogenously into theory building as an a priori, as is the case in orthodox economics, then organizations will be designed to monitor and induce their members with carrots and sticks. Their preferences will change from intrinsic to extrinsic or even opportunistic.

(3) Bounded utility concept: In standard economics, it was, until recently, the case that only observable acts ("revealed preferences") could be the object of economic study - but not what was subjectively perceived. In this view, individuals' expressions of their subjectively felt utility, their happiness or their life satisfaction cannot be trusted (Samuelson, 1938). However, a dramatic change has occurred in recent years. A variety of methods have captured how happy individuals feel, which determinants are decisive for this, and what the measurable consequences arise from this are (for an overview, see Frey & Stutzer, 2002a; 2002b). Happiness research has brought about a near-revolutionary change in economics. It captures those determinants of subjective life satisfaction or individual welfare that are the most important. Some of these clearly contradict the assumptions of standard economics, such as:

- Wealth makes people happy, but to a lesser extent than such factors as health or an occupation. It is not the absolute but the relative level of wealth that matters.
- The most important factor of unhappiness is unemployment, even when income remains the same.
- Individuals evaluate their utility over the long term falsely.

- People in democratic countries are, other circumstances remaining the same, happier than in authoritarian societies. They are happiest when they are able to be directly active in democracy through the use of initiatives and referendums.

Psychological economics can contribute more and richer insights for the awareness and shaping of companies and societies than standard economics and its empirically false “homunculus oeconomicus”. It considerably reduces negative self fulfilling prophecies. The question arises: Does it avoid being bad for practice?

WHY PSYCHOLOGICAL ECONOMICS CAN BE STILL BAD FOR PRACTICE

Psychological economics is less bad for practice than orthodox economics because it has made some critical assumptions about human nature endogenous to theory building. In particular, it shows that pro-social behavior is empirically relevant and can be the basis of institutions which strengthen social responsibility. However, psychological economics uses a similar methodology as orthodox economics and thus runs the danger also of being not good for practice for five methodological reasons.

Firstly, as orthodox economics, it takes as starting point formal models, in which just a few variables are systematically analyzed. The standard economic model continues to serve as a frame of reference for the analytical and the empirical research. Like standard economics, it proceeds from a restricted number of assumptions, which are formulated within mathematical models. Some of these variables are introduced endogenously into theory building, but most variables are still introduced exogenously, such as rational behavior in most experiments which investigate pro-social preferences, for instance. The economist Mayer (1993: 53) criticizes this procedure as the “principle of the strongest link”. It is the background to the frequent accusation that these models are rigorous but not relevant. Significant variables which do not fit the model are ignored. At best, contextual conditions are included ex-post as “weak links” in the form of unsystematic, arbitrarily occurring ad-hoc reflections. These ad-hoc reflections stand for the most part in stark incongruity to the strict output of the model’s results and the claim to give valid prescriptions to practitioners.

Secondly, for many scholars, psychological economics is identical to experimental economics. Most empirical work in psychological economics is done as laboratory experiments, in which very few variables are artificially isolated and changed under controlled conditions. Though external validity is very questionable, a lot of scholars claim to derive prescriptions for practitioners (Mullainathan & Thaler, 2000).

Thirdly, the key to explaining observed actions is only sought where the disciplinary lamp is shone. The insights of other disciplines are not systematically incorporated. Also, the perspectives and viewpoints of practitioners are seen as insignificant. Their potential for reflection is underestimated. This is astonishing, given the results of research on the value of laypeople’s insights. As in standard economics, the results of research into practice in psychological economics are made available without there being any feedback into the research process. This problem has been extensively discussed in the field of knowledge production using the term Mode 1 as opposed to Mode 2 (Gibbons et al., 1994). Mode 1 research neglects that much of practice in most fields remain only partially understood scientifically and that technological and social practice and scientific understanding often coevolves (Nelson, 2006; Starbuck, 2006; Stokes, 1997).

Fourthly, it is characteristic of this type of research that it neglects aspects of synthesis in favor of analysis. The requirements of discipline-based knowledge with the requirements of business and policy practice are left to the practitioner. It follows the IKEA model: Take it home yourself and put it together yourself (Mintzberg, 2004, p. 47). This is particularly disadvantageous to management science, which, like other problem-oriented fields of research such as engineering sciences, jurisprudence, environmental sciences, proceeds explicitly from the concrete questions of practice rather than from problems defined within the discipline. Management practice pays no attention to disciplines (Steinmann & Schreyögg, 2005). Its nature is “a-disciplinary”.

Fifthly, psychological economics and orthodox economics both claim to be the “queen of social science”. This goes so far that the results of other social disciplines, like social psychology, are mostly ignored, though these disciplines deal with similar questions and apply similar empirical methods. But any form of disciplinary imperialism restricts scientific progress.

As a consequence, psychological economics, like standard economics, is very often rigorous, but not relevant for problem solving outside the laboratory. Although psychological economics is clearly better for practice than standard economics, it still is not good for practice.

FROM ECONOMIC IMPERIALISM TO MULTIDISCIPLINARY MAPPING

What must a research strategy look like if it is to be good for practice while at the same time overcoming the frequently discussed trade-off between rigor and relevance (e.g. Donaldson, 1995; Huff, 2000; Pettigrew, 2001, Stokes, 1997)? We suggest the research strategy of “multidisciplinary mapping” and give reasons why it is most appropriate to support at the same time problem solving in management practice and scholarly understanding of research questions.

Maps are theoretically based reference anchors, offering precise terminology with regard to specific contents. They provide frames for action to start from (Fiol & Huff, 1992; Weick, 1990), without determining action. Maps describe navigation devices that may solve a given problem, but offer no guarantees for doing so. Maps are a vehicle for transferring theoretical insights to scholars from other disciplines without using a theory-specific language. Thus, they enable better communication between different disciplinary approaches. Dogan and Pahre (1991) show empirically that the most important innovations in social science took place at the borders between single disciplines. Maps help practitioners to analyze their problems more systematically. Although maps use a precise terminology, they neither establish causal laws or regularities, nor do they offer “blueprints”. Instead, maps can be used as different “walking sticks” to reveal possible unintentional consequences of intended actions (Roethlisberger, 1977). They can also be used as different “talking sticks” in argumentation processes to consider propositions and to come to an agreement (Scherer & Dowling, 1995). What is crucial, maps do not claim to translate theoretical insights gained by one discipline (e.g. orthodox or psychological economics or psychology) into instructions for practitioners in the form of a “tautological transformation” (Popper, 1959). Rather, they provide frames of reference in order to throw spotlights on the territory.

Multidisciplinary mapping is the provision of different disciplinary maps which provide orientation in a complex territory. The aim of multidisciplinary mapping is to gain insights from the differences between these different maps and to exploit these differences. What matters is to provide practitioners and scholars from other disciplines with findings from different theoretical approaches in a language they understand so

that they can triangulate methods and models with respect to their problems (Van de Ven & Johnson, 2006; Starbuck, 2006). Thus, we propose multidisciplinary mapping as an effective method for leveraging the different knowledge contributions that practitioners and scholars make with regard to the question of what is good for practice and theory building.

CONCLUSION

A theory that is socially responsible and good for practice must have no truck with imperialism of any kind. Instead, it must sensitize scholars as well as practitioners to the broad range of views and issues involved. We examine that “multidisciplinary mapping” reduces the overconfidence of scholars in their models, and supports practitioners to express their problems and experiences in a more precise terminology. Multidisciplinary mapping addresses the dual purpose of management studies: to achieve a deep understanding of the research question for creating scientifically meaningful research, while at the same time advancing problem solving in management practice. Thus not only is multidisciplinary mapping good for socially responsible practice, it is also good for theory building.

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NOTES

¹ Psychological economics is often referred to in the Anglo-Saxon world as behavioral economics. However, this description is misleading. In psychology, the term ‘behaviorist’ denotes a scientific approach which exclusively investigates observable stimulus-response relationships (e.g. Watson, 1913), and disregards internal psychological cognitive and motivational processes.

² C.f. Rabin (1998) gives an exceptional overview of this branch of research.

³ Variable and performance-related rewards are not negative in principle, c.f. Frey (1997) and Frey & Osterloh (2002). Where extrinsic motivation predominates in an activity, variable pay produces a positive total effect on performance. However, variable pay always costs more than it appears to at first glance, because the hidden costs of reward must be added to the monetary costs of variable pay. This effect was demonstrated in detail by a vignette experiment involving professionals by Weibel, Rost and Osterloh (2007), which looked into the “black box” of cognitive and motivational processes.