**CHAPTER THREE**

**Approaches to Economic Sociology**

**3.1 Political Economy**

Political economy was the original term used for studying production and trade, and their relations with law, custom, and government, as well as with the distribution of national income and wealth. Political economy originated in moral philosophy. It was developed in the 18th century as the study of the economies of states, or polities, hence the term political economy.

In its contemporary meaning, the study of the conditions under which production or consumption within limited parameters was organized in nation-states. Political economy refers to different, but related, approaches to studying economic and related behaviors, ranging from the combination of economics with other fields to the use of different, fundamental assumptions that challenge earlier economic assumptions:

 Political economy most commonly refers to interdisciplinary studies drawing upon economics, sociology, and political science in explaining how political institutions, the political environment, and the economic system—capitalist, socialist, or mixed—influence each other. The Journal of Economic Literature classification codes associate political economy with three subareas: the role of government and/or power relationships in resource allocation for each type of economic system, international political economy, which studies the economic impacts of international relations, and economic models of political processes. The last area, derived from public choice theory and dating from the 1960s, models voters, politicians, and bureaucrats as behaving in mainly self-interested ways, in contrast to a view, ascribed to earlier economists, of government officials trying to maximize individual utilities from some kind of social welfare function. An early and continuing focus of that research program is what came to be called constitutional political economy.

 Economists and political scientists often associate political economy with approaches using rational-choice assumptions, especially in game theory, and in examining phenomena beyond economics' standard remit, such as government failure and complex decision making in which context the term "positive political economy" is common. Other "traditional" topics include analysis of such public policy issues as economic regulation, monopoly, rent-seeking, market protection, institutional corruption, and distributional politics. Empirical analysis includes the influence of elections on the choice of economic policy, determinants and forecasting models of electoral outcomes, the political business cycles, central-bank independence, and the politics of excessive deficits.

 A recent focus has been on modeling economic policy and political institutions as to interactions between agents and economic and political institutions, including the seeming discrepancy of economic policy and economist's recommendations through the lens of transaction costs. From the mid-1990s, the field has expanded, in part aided by new cross-national data sets that allow tests of hypotheses on comparative economic systems and institutions. Topics have included the breakup of nations, the origins and rate of change of political institutions in relation to economic growth, development, backwardness, reform, and transition economies, the role of culture, ethnicity, and gender in explaining economic outcomes, macroeconomic policy, the environment, fairness, the relation of constitutions to economic policy, theoretical and empirical.

 New political economy may treat economic ideologies as the phenomenon to explain, per the traditions of Marxian political economy. Thus, Charles S. Maier suggests that a political economy approach "interrogates economic doctrines to disclose their sociological and political premises.... in sum, [it] regards economic ideas and behavior not as frameworks for analysis, but as beliefs and actions that must themselves be explained."

In the political economy perspective, states’ interests are less unitary and more subject to internal and external political pressures. Its views are related to the general model of regulation that comes from economics. Economics starts out from the position that free trade is always good because of the theory of comparative advantage. Adherents to this theory wonder why governments ever undertake protectionist measures. Political scientists and sociologists generally start with the opposite view: that various constituencies in society prevent state actors from entering into free trade agreements centered on negative integration. Scholarly attention has focused on which national interest groups favor of trade and which oppose it. In the case of international economic agreements, exporters (i.e. multinational corporations, or as some call them, transnational corporations [hereafter TNCs]) generally favor more open markets, and local producers who are totally dependent on the national market favor closed markets.

The relative size and weight of these groups in a particular society affect the ability of governments to enter into international economic agreements.

There are two basic variants of this thesis. One emphasizes that sectorial interests predominate, while the other views class interests as pivotal. In the former approach, firms in particular sectors, like steel and sugar that have been negatively affected by opening up boundaries to imports oppose participation by their governments in trade pacts. Similarly, those that would benefit from exporting, like airplane manufacturers and computer firms, favor such pacts. Governments may pursue trade openings for their major exporters and protectionism for those that might be hurt by open markets. Another approach focuses attention on capital and labor, seeing firms and workers as pitted against one another. Capital would theoretically prefer to have open product and capital markets so it can seek out the highest possible returns. Labor would prefer to keep capital captive. Since labor is the least mobile of resource endowments, it is the most likely to pressure governments to protect industry.

Evidence exists to support this division of interests. One way to bring both theories together is to recognize that sector and factor interests could coincide. So, low-skill, labor-intensive industries confronted with high and rising import penetration would mobilize both firms and workers to support protection. Theorists who begin with the idea that a particular country has a trade regime because of its mix of economic activities have to consider how those activities have changed in order to explain why governments have shifted policies. A number of provocative arguments have been made. One argument is that as trade barriers have decreased, both capitalists and skilled workers view exporting as an opportunity and therefore press their governments for more trade agreements. This produces a kind of “virtuous circle” for support of free trade. This argument seems of greater relevance to more developed than to less developed countries. In the case of less developed countries, another set of arguments has been made. Scholars argue that governments have taken the relative failure of import substitution strategies and the relative success of the open Asian countries as impetus to shift from trade protectionism to trade openness. It turns out that there is little evidence to support this view. Most less developed countries still have organized opposition to such shifts in policy among both capital and labor. Their governments often changed policies in the face of substantial opposition. A more promising line of research to explain the interest in open trade among less developed countries looks at political factors. Some of these are domestic, like the capacity of the local bureaucracy to act autonomously from key interest groups and the existence of democracy. Others are international.

Here, scholars have emphasized the role of U.S. hegemony, the fall of communism, and the push to economic liberalization by IGOs like the Organization for Economic Cooperation and Development, the World Bank, and the International Monetary Fund.

 The international economic environment has provided ideological and material support to push free trade and financial deregulation. The epistemic community of international aid and economics organizations has pushed the view that the path to economic growth is more market and less regulation. Both carrots (i.e., trade access to developed countries and international investment) and sticks (requirements from the IMF and the World Bank to open markets in exchange for aid) are used to open markets.

**3.2 Organizational Theory**

Organizational theory is the sociological study of formal social organizations, such as businesses and bureaucracies, and their interrelationship with the environment in which they operate. It complements the studies of organizational behavior and human resource studies.

For a number of reasons there exists a clear affinity between organization theory and economic sociology. One reason for this, no doubt, is that sociologists of organization often analyze economic organizations; another is that organization theory was to incorporate much of industrial sociology when this field disappeared in the 1970s. And, finally, roughly during the 1990s, business schools often hired sociologists to teach organization theory. Three schools or perspectives in organization theory have been of much importance to economic sociology: resource dependency, population ecology, and new institutionalism. The basic idea of resource dependency is that an organization is dependent on resources in its environment to survive. This perspective, as especially Ronald Burt has shown, can be of some help in understanding how the economy works. At the center of Burt’s work on resource dependency is his concept of structural autonomy, or the idea that a corporation has more room to maneuver the fewer competitors it has and the more suppliers and the more customers there are. That a corporation has more power if it is in a monopoly position is clear; from this it follows that suppliers as well as customers are less powerful the more competitors they have. If Corporation A, for example, has only one supplier and one customer, both of these can wield quite a bit of power over Corporation A. Using a huge input–output data set for the nation’s industry, Burt has also shown that the idea of structural autonomy has some support in empirical reality; in brief, the more structurally autonomous a corporation is, the more likely it is that profits will increase (Burt 1983).

Population ecology, as opposed to resource dependency, uses as its unit of analysis not the single corporation but whole populations of organizations. That these populations go through fairly distinct phases of growth and decline has been shown through a number of empirical studies, many of which are highly relevant to economic sociology since the organizations being studied are often economic organizations. Population ecology also looks at competition between organizations and the processes through which new organizational forms become accepted. The fact that population ecology typically looks at large populations of organizations means that relatively high powered statistical methods are used. There is, however, little theoretical renewal going on in population ecology, and unless this changes, this perspective risks being exhausted in a few years.

A considerably higher degree of flexibility and creativity characterizes new institutionalism, or the kind of organization theory that has emerged around the work of John Meyer. A fundamental thesis in this approach is that rationality is often only a thin veneer and that organizations usually look the way they do for other than rational reasons. There also exist more or less distinct models for what a certain type of organization should look like, and these models are typically diffused through imitation. Since new institutionalism has such a flexible core, it can be used to analyze a variety of topics, in contrast to population ecology, which is considerably more limited in scope.

**Competing Theories of Organization**

As organizations are implemented over time, many people experimented as to which one was best. These theories of organizations include Bureaucracy, Rationalization (Scientific Management), and the Division of Labor. Each theory provides distinct advantages and disadvantages when implemented.

1. **Bureaucracy Theory**

**Weber's ideal of bureaucracy**

Efficiency and teleological arguments in Weberian bureaucracy

Max Weber believed that an ideal bureaucracy consists of six specific characteristics: hierarchy of command, impersonality, written rules of conduct, advancement based on achievement, specialized division of labor, and efficiency. This ultimate characteristic of Weberian bureaucracy, which states that bureaucracies are very efficient, is controversial and by no means accepted by all sociologists. There are certainly both positive and negative consequences to bureaucracy, and strong arguments for both the efficiency and inefficiency of bureaucracies.

 Weber’s theory of bureaucracy claims that it is extremely efficient, and even goes as far as to claim that bureaucracy is the most efficient form of organization. Weber claimed that bureaucracies are necessary to ensure the continued functioning of society, which has become drastically more modern and complex in the past century. Furthermore, he claimed that without the structured organization of bureaucracy, our complex society would be much worse off, due to the fact that society would act in an inefficient and wasteful way. He saw bureaucracies as organizations driven towards certain goals, which they could carry out efficiently. In addition, within an organization that operates under bureaucratic standards, the members will be better off due to the heavy regulation and detailed structure. Not only does bureaucracy make it much more difficult for arbitrary and unfair personal favors to be carried out, it also means that promotions and hiring will generally be done completely by merit.

Weber most definitely saw bureaucracies as goal-driven, efficient organizations, but one must not come to the quick and incorrect conclusion that he saw no downfalls to bureaucracy. He recognized that there are constraints within the bureaucratic system. First of all, he realized that bureaucracies were ruled by very few people with very large amounts of unregulated power. This tends to lead to a situation of oligarchy, whereby a limited number of officials become the political and economic power. Furthermore, Weber considered further bureaucratization to be an “inescapable fate,” due to the fact that it is supposedly superior to and more efficient than other forms of organization. Weber’s analysis of bureaucracies led him to believe that they are too inherently limiting to individual human freedom and he feared that people would begin to be too controlled by bureaucracies. His rationale comes from the knowledge that the strict methods of administration and legitimate forms of authority associated with bureaucracy act to eliminate human freedom.

Regardless of whether or not bureaucracies should be considered positively efficient or too efficient to the extent that they become negative, Weberian bureaucracy tends to offer a teleological argument. A theory, in this case bureaucracy, is considered to be teleological if it involves aiming at specific goals. Weber claimed that bureaucracies are goal-oriented organizations, which use their efficiency and rational principles to reach their goals. A teleological analysis of businesses leads to the inclusion of all involved stakeholders in decision-making. The teleological view of Weberian bureaucracy postulates that all actors in an organization have various ends or goals, and attempt to find the most efficient way to achieve these goals.

There are several additional features that comprise a Weberian bureaucracy:

* It is possible to find the utilization of hierarchical subordination in all bureaucratic structures. This means that higher-level offices supervise lower level offices.
* In bureaucracies, personal possessions are kept separate from the monies of the agency or the enterprise.
* People who work within a bureaucracy are usually trained in the appropriate field of specialization.
* Bureaucratic officials are expected to contribute their full working capacity to the organization.
* Positions within a bureaucratic organization must follow a specific set of general rules.

When a bureaucracy is implemented, they can provide accountability, responsibility, control, and consistency. The hiring of employees will be an impersonal and equal system.

Although the classical perspective encourages efficiency, it is often criticized as ignoring human needs. Also, it rarely takes into consideration human error or the variability of work performances (each worker is different).

1. **Scientific Management**

The scientific management theory was introduced by Frederick Winslow Taylor to encourage production efficiency and productivity. Taylor argues that inefficiencies could be controlled through managing production as a science. Taylor defines scientific management as "concerned with knowing exactly what you want men to do and then see in that they do it in the best and cheapest way." According to Taylor, scientific management affects both workers and employers, and stresses the control of the labour force by management.

Taylor analyzed how to maximize the amount of output with the least amount of input. This was Taylor’s attempt to rationalize the individual worker.

1. Divide work between managers and workers

2. Provide incentive system (based on performance)

3. Scientifically trained workers

4. Create a science for each individual’s responsibilities

5. Make sure work is done on time/efficiently

There are problems that arose out of scientific management. One is that the standardization leads workers to rebel against mundaneness. Another is that workers may reject the incentive system because they are required to constantly work at their optimum level, an expectation that may be unrealistic.

1. **Rational system perspective**

In a rational organization system, there are two significant parts: Specificity of Goals and Formalization. Goal specification provides guidelines for specific tasks to be completed along with a regulated way for resources to be allocated. Formalization is a way to standardize organizational behavior. As a result, there will be stable expectations, which create the rational organizational system.

1. **Division of labor**

The division of labor is the specialization of individual labor roles. It is often associated with increasing output and trade. According to Adam Smith, the division of labor is efficient due to three reasons: occupational specialization, saving from not changing tasks, and machines taking the place of human labor. Occupational specialization leads to increased productivity and distinct skill. Also, Smith argued that human and physical capital must be similar or matched; if the skill of workers were matched with technological improvements, there would be a major increase in productivity.

Although the division of labor is often viewed as inevitable in a capitalistic society, there are several specific problems that may arise. They include a lack of creativity, monotony, and lack of mobility. Creativity will naturally suffer due the monotonous atmosphere that the division of labor creates. Doing the same routines may not be for everyone. Also, employees aren’t familiar with other parts of the job. They cannot assist employers of different parts of the system.

**3.3 Population Ecology Theory**

Population Ecology Theory incorporated the individual, population, and community as units of analysis to look at the death of organizations (firm mortality) and the birth of new organizations (organizational founding), as well as organizational growth and change. In effect, Hannan and Freeman theorize about a complete ‘life-cycle’ for an organization.

The formal conceptual definition of Organizational population ecology theory is, a theoretical and empirical approach that uses insights from biology, economics, and sociology, and employs statistical analysis to try and understand the conditions under which organizations emerge, grow, and die. Briefly, it is the analysis of an organization using human life cycle terms and principles.

And, in the field of organizational studies, Population Ecology Theory is seen as an alternative to the dominant adaptation perspective. Simplified, it’s the idea that environment affects organization structure, failure, and success.

There are numerous hypotheses or sub-theories within Organizational Population Ecology Theory. Among these the following sub-theories are dominant

 1. Inertia and change

2. Niche width

3. Resource partitioning

4. Density dependence

5. Age dependence

Population Ecology Theory has over the years become one of the central fields in organizational studies, and is known for its empirical, quantitative character within each description of sub-theories of Population Ecology.

1. **Inertia and Change**

This hypothesis posits that organizations that are both reliable and accountable are those that can survive (favored by “natural selection”). A negative by-product, however, of the need for reliability and accountability is a high degree of inertia and a resistance to change. The readings suggest that a key prediction of population ecology is that the process of change itself is so disruptive to organizations that it will result in an elevated rate of mortality.

Conflicting and complementary theories about inertia and change seem to be fundamental to the research organizational population ecology. Given the limits on organization-level adaptation, most of these broader changes thus come from the entry of newly founded organizations and the selective replacement of unfit organizations. Hence, scholars in the organizational theory field, have spent considerable effort on understanding the effects of inertia and change on the mortality rates of organizations. As Baum points out, Structural Inertia Theory addresses to main questions: 1) how changeable are organizations and 2) is change beneficial to organizations?

The former financial giant, Lehman Brothers, may fit the characterization of an organization whose long-term survival was based on reliability and accountability. However, Lehman Brothers core change led to overexposure to riskier investment portfolio assets, namely derivative backed securities, and ultimately led to their demise.

1. **Niche theory**

The sub-theory of niche-width distinguishes broadly between two types of organizations: generalists and specialists. From Hannan and Freeman, specialist organizations maximize their exploitation of the environment and accept the risk of experiencing a change in that environment. On the other hand, generalist organizations accept a lower level of exploitation in return for greater security.

Niche-width theory shows that specialization is generally favored in stable or certain environments. However, the main contribution of the niche-width theory is probably Hanna and Freeman’s finding that “generalism is not always optimal in uncertain environments”. Environments that “place very different demands on the organization, and where the duration of environmental states is short relative to the life of the organization” produce the exception.

Thus, Population Ecology Theory attempts to show that different structures in different industries (generalist vs. specialist organizations) are shaped by relevant environments.

However, the niche-width sub-theory seemed to be carrying with it a high degree of inconclusiveness, which may be why it was stated that many scholars abandoned the research.

1. **Resource partitioning**

The resource-partitioning model further develops the relationship between generalists and specialist organizations. This model includes predictions about the founding and mortality rates of both specialists and generalists as a function of market concentration.

The theory can be illustrated by describing two environments. Environment A stands for an unconcentrated mass market and environment B represents a concentrated mass market. In environment B, generalists will always attempt to address the center of the market where most resources peak. After all, in the center of the market these generalists can thrive by exploiting economies of scale.

However, according to Carroll “in environment B, despite the very concentrated generalists market, the resource space outside this market [i.e. in the periphery of the market] is larger than in environment A, where the generalist market is less concentrated”. The abundance of resource in the periphery can then become hospitable to specialist organizations, and the market becomes effectively partitioned. Carroll concluded that “more available resources should translate into better chances of success for specialists when they operate in the more concentrated market”.

In other words, in markets with competition among large generalist, specialists can thrive at the seams, and thus lower their aggregate failure rate.

1. **Density Dependence**

Organizational Population Ecology Theory also predicts that the rates of founding and the rates of mortality are dependent on the number of organizations (density) in the market. This density dependency sub-theory seemed rather intuitive and related to Smith concepts of “supply and demand”. The two central mechanisms here are legitimacy (in other words, does the public recognize or take-for-granted that group of organizations) and competition. Legitimacy generally increases with the number of organizations, but so does competition. The result is that legitimacy processes will prevail at low numbers of organizations, while competition prevails at high numbers.

The organizations founding rate will therefore first increase with the number of organizations (due to an increase in legitimacy) but will reach a peak and then decrease at high numbers of organizations (due to competition). The reverse holds for mortality rates. Thus, the relationship of density to founding rates has an inverted U shape and the relationship of density to mortality rates follows a U-shaped pattern.

1. **Age Dependence**

How an organization's risk of mortality relates to the age of that organization has also been extensively examined. Organizational ecologists have found a number of patterns:

**Liability of newness:** Here, the risk of failure is high initially but declines as the organization ages. As Carroll posits, ‘if age X coincides with the amount of environmental change experienced by an organization, and if the risk of failure Y increases with the cumulative environmental change, then the probability of failure Z will increase with age if environmental change is uncontrolled.

**Liability of adolescence:** The risk of mortality will be low at first as the organization is buffered from failure due to support by external constituents and initial endowments. But when these initial resources become depleted, the mortality hazard shoots up and then declines following the liability of newness pattern. Like a teenager, the organization has neither the protection afforded in early childhood, nor the maturity to be self-sufficient like an adult.

**Liability of aging**: Here, the risk of failure increases with organizational age. This could be due to a liability of obsolescence (a growing external mismatch with the environment).