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# From social control to financial economics: the linked ecologies of economics and business in twentieth century America

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## Abstract

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This article draws on historical material to examine the co-evolution of economic science and business education over the course of the twentieth century, showing that fields evolve not only through internal struggles but also through struggles taking place in adjacent fields. More specifically, we argue that the scientific strategies of business schools played an essential—if largely invisible and poorly understood—role in major transformations in the organization and

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Administration after World War II. This episode illustrates the increasingly successful claims of social scientists, backed by philanthropic foundations, on business education and the growing appeal of “scientific” approaches to decision-making and management. Finally, we argue that the rise of the Graduate School of Business at the University of Chicago from the 1960s onwards (and its closely related cousin at the University of Rochester) marks the decisive ascendancy of economics, and particularly financial economics, in business education over the other behavioral disciplines. We document the key role of these institutions in diffusing “Chicago-style” economic approaches—offering support for deregulatory policies and popularizing narrowly financial understandings of the firm—that sociologists have described as characteristic of the modern neo liberal regime.

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## Notes

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1. But see Abbott's discussion of the difference between his concept of ecology and Bourdieu's concept of field at <http://home.uchicago.edu/~aabbott/Papers/BOURD.pdf> (accessed July 1, 2010).
2. Note that what is true of economics is also true of sociology and psychology. Witness, for instance, the development of network analysis, largely a by-product of the migration of sociology into schools of business.
3. For instance, when the Harvard Business School was founded in 1908, the medical school had been around since 1782, the law school since 1817, and the divinity school since 1819.
4. The term "behavioral sciences" was explicitly

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MBA growing fastest among advanced degrees. Additionally, Zorn ([2004](#)) has shown that even beneath the CEO level, CFOs have become an important part of the senior executive team and that their backgrounds and training are less likely to come from accounting and more likely resemble the strategic finance and financial engineering taught in MBA programs.

6. The most conspicuous omission in this panorama is, of course, Harvard Business School, which we have excluded for substantive reasons that will become clearer in the remainder of the article. The fact is that in spite of its pioneering role in establishing business education in the United States, Harvard's trajectory in this domain remained quite disconnected from evolutions at other major schools. Harvard's relative autonomy is attributable largely to its size, financial autonomy from the larger university, preeminent status as one of the oldest business schools in the country, and, finally, to the distinctiveness and success of its clinical approach to business education and

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business school systems.

9. Marginal utility theory commonly refers to a set of conceptual and mathematical tools (specifically differential calculus) developed in continental European economics at the end of the nineteenth century to study economic behavior “at the margin” and thereby assess the efficiency of resource allocation.

Methodologically, analytically, and sometimes politically as well, marginalist economists often found themselves at odds with economists advocating more institutional and historical approaches to the economy. The fiercest intellectual battles involved the German (historicist) and Austrian (marginalist) schools of economics, but similar struggles took place also in England, France, and the United States.

10. A member of the Pennsylvania Child Labor Committee, Nearing had been convinced by his work there that local businessmen were responsible for keeping local youngsters in their factories and preventing the passage of laws regulating child labor. During the

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state legislature (which partly bankrolled the university), as well as prominent trustees, and Nearing was promptly fired—one of the many victims of the “academic freedom” persecutions so well chronicled by Furner ([1975](#)). Also see Nearing ([1919](#)). The firing of both Nearing and Patten was officially attributed to their antiwar views.

11. Willits was, in many ways, an example of the consummate academic insider of the interwar period—he worked on Hoover’s Emergency Committee for Employment, helped found and presided over the National Bureau of Economic Research, became dean of Wharton during the 1930s and ended his career as a Rockefeller Foundation official.
12. See, e.g., Bruce [2005](#), on the importance of personnel management concerns in American economics during the 1910s and early 1920s. Also Shenhav [1995](#).
13. Roswell McCrea, who followed Patten as Dean of the Wharton School, argued:

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possible one of search for effective competitive devices, and with no clear vision of the social goal of business activity. And economics, divorced from business, is too likely to spend itself either in closet philosophizing by traditional modes, altogether too little affected with a present interest, or in fortifying predilections regarding public policy with broadly garnered data too remote from the intimate, work-a-day world of fresh experience to yield much more than a crop of articles, books, and book reviews. If schools of business realize their opportunities, the economic theory of the future will grow out of their researches and will be formulated by their teachers. The joining of socially motivated thinking with a knowledge of concrete, shifting reality, such as can be effected in a school of business, may well escape the puttering of the strict vocationalist on the one hand, and the futility of the closet philosopher on the other. The foundations of wise business policy can be laid in this as in no other way." (McCrea 1925, p. 222) The University

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business school, whose pre-Depression mission statement emphasized narrow technical skills, revised it to include the advancement of knowledge on “fundamental questions of economics and philosophy which influence the course of a dynamic age.” The University of Oklahoma’s business school, whose mission statement, prior to 1930, stressed the economic value of its degree, shifted to wanting to “enable [students] to understand the public problems, particularly those having to do with the interrelationships between different businesses, between business and government, and between the employer and employee.” Similar changes could be found at the University of Michigan, New York University, and the University of California.

15. One response from the business world and foundations was to sponsor new economic research institutions, the most important of which was the Committee for Economic Development, a think tank filled with economics faculty and graduates from the University of Chicago, some of them closely

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for two WPA jobs the town government had managed to get.” Bach thought there “must be a better way” for economics (Bach in Gleeson and Schlossman [1995](#)).

17. Interviews carried out by Marion Fourcade with American economists confirmed that as late as the 1970s–1980s, business schools were not considered highly reputable places for young economics graduates to start a career. (The Chicago GSB changed all that.)

18. There was particular hostility toward Harvard Business School and the academic disciplines. Harvard, the GSIA faculty felt, impressed through expensive neo-Georgian architecture and elegant faculty offices, not intellectual rigor (Leavitt [1996](#), p. 290). The need to differentiate the GSIA from Harvard even manifested itself in the design of the school's physical building, where a culture of austerity dictated that there not even be an elevator, although the institution was on sound financial footing. The GSIA faculty saw this as a badge of true seriousness.

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Magazine Forum, April 27, 1948. In a 1947 article, *The New York Times* applauded Harvard Business School's brief pamphlet *Education for Business Responsibility* as an intellectual turning point for developing a free-market retort to those academics calling for greater governmental involvement in the economy. (Russell Porter, "Stress Social Responsibility as Factor in American Life," *New York Times*, September 7, 1947, p. F1.)

22. See Lagemann [1987](#). Amadae ([2003](#), p. 38) dates the sharp shift to the right of the Ford foundation policies and intellectual agenda from the replacement of Paul Hoffman by H. Rowan Gaither, Jr., as president of the Ford Foundation in 1953. Under the latter's leadership, the Ford foundation decisively reoriented its activities toward national security and the arguably rather anti-democratic vision of a society managed by experts. Also see Tadajewski ([2009](#)).

23. According to an internal review (Wheeler [1965](#)) the Ford Foundation spent about \$19

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funding the school. Again, to highlight the significance of these amounts, Harvard Business School's main fund from alumni donations had totaled \$2.5 million from 1908 to 1959.

24. The idea that Harvard would not be part of the Ford Foundation program would have threatened the legitimacy of all of Ford's reform efforts. Though Ford ended up supporting HBS more heavily than any other school, our evidence suggests that foundation officials remained much more hands-off in their dealing with the institution, using the connection essentially as a way to legitimate their involvement in business education and treading carefully around the tight personal connections between HBS and the board of the Ford Foundation. As one member of the foundation's program on business education described the situation: "[T]hat first year and a half or so was a continuing sort of running skirmish between Don [Donald David, Harvard Business School former dean who went on to become executive

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was directed largely toward increasing the school's endowment and diffusing its case study method, whereas everywhere else the foundation was much more actively pushing schools to embrace a social science model. HBS was thereby essentially able to maintain its clinical focus and mute any attempt to change its program, while other schools rapidly moved toward professionalization along scientific-academic lines.

25. The AACSB was originally set up in 1917 by the founding deans of the leading business schools to help spearhead the professionalization of business education and management as a profession. In the 1950s, the organization shifted its focus to serve as an accrediting institution for business education. Still, it was relatively weak and increasingly perceived as irrelevant by the better business schools.

26. See <http://www.tepper.cmu.edu/about-tepper/history/the-b-school-change-agents/carnegie-connections/index.aspx>.

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how this led him to such a radically non-behavioral hypothesis as rational expectations. (I once tried to discuss this with Herb, thinking of it as an instance of the enormous, productive influence he had on all of us, but he took offense at the suggestion)” (McCallum [1999](#)).

29. A similar story would play out later at the Chicago GSB, where behaviorism faced the strong opposition of economists (Van Overtveldt [2007](#)).

30. The Chicago GSB was renamed the Booth School of Business in 2008. However to avoid anachronism, we use its old name throughout this article.

31. Hayek, however, taught in the Committee on Social Thought, having failed to secure an appointment in the economics department.

32. Over the years, the Chicago economics “nebulae” would end up providing a host of Mont Pèlerin recruits, such as Gary Becker.

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34. See, for example, Nelson ([1987](#)), Noll ([1985](#)) on the deregulation movement, and Mercurio and Medema ([1997](#)) on law and economics in the United States.
35. Starting in 1959, the investment bank Merrill Lynch, whose officials had developed an interest in modern financial theory, supplied the GSB with a series of grants to set up the Center for Research in Security Prices (CRSP). Over a period of 22 years, the center would receive a total of \$1 million. The CRSP was devoted mainly to gathering the prices, dividends, and rates of return of all stocks listed and trading on the New York Stock Exchange since 1926.
36. See MacKenzie [2006](#); Whitley [1986](#). Other achievements of financial economics—all based on the view of efficient financial markets—did not fare much better: the capital asset pricing model (Sharpe [1964](#)), for instance, held that the only optimal portfolio was the entire market—which analysts found unhelpful at first.

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US business schools, these figures hovered around 45 %, with the notable exception of Harvard (30 %). (authors' calculations)

38. The accountants were perhaps the most creative. They borrowed from Friedman's appeal to Popper in his "methodology of positive economics," as well as from their Rochester colleagues' ventures into "positive political theory," to craft a new science they dubbed "positive accounting."

39. When an activist investor group or corporate raider seeks to purchase a firm through a hostile takeover they typically need to remove the old board members in order to vote in favor of the takeover. One often used tactic is the nomination of an alternate slate of directors who are presented to shareholders. Since most shareholders are interested in receiving the higher price being offered by the hostile takeover firm, shareholders will often vote in favor of the new slate of directors. Directors on this new slate are chosen on being favorable to the takeover event and

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Golden parachutes, which guarantee multi-million dollar payouts to CEOs in the event of a takeover, are defensible, in Jensen's view, since shareholders still benefit when a firm is taken over.

41. Michael Jensen, "A Helping Hand for Entrenched Managers" *Wall Street Journal*. (Eastern edition). November 4, 1987, p. 1.
42. Industrial settings were another place where these ideas evolved (see [Shapin 2008](#)).
43. These citations studies show that marketing, management, operations research, and especially accounting and finance cite economics heavily, but that the reverse is not true.

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