THE NEW ECONOMIC SOCIOLOGY

A READER

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Chapter 1

THE SOCIOLOGICAL VIEW OF THE ECONOMY

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AFTER SPENDING eighteen months among the Yanomamo of northern Brazil, Napoleon Chagnon (1968) described them as a fierce people respectful of quick tempers and casual violence. After spending a bit longer among the bond traders of Salomon Brothers, Michael Lewis (1987) described them as a guileful people respectful of quick wits and casual deception.

These peoples have different sorts of economies—systems for producing that with which they sustain life. They have different mechanisms for socializing the young. They have different cosmologies, or frameworks for making sense of the world. Both cosmologies tie social customs and physical objects to something bigger than society itself, in one case to a spirit world, in the other to a corpus of natural laws. The Yanomamo envision a world of departed ancestors that exists immediately above the visible sky and trace economic conventions (chest-beating contests) and physical objects (yams) to specific mythical ancestors. The bond traders envision a roster of social and physical laws that transcend time and space, and trace conventions (arbitrage) and objects (blowfish sushi) to specific laws. In each tribe, the average man on the street may not know everything about the ancestor spirits or scientific laws that govern the world, but he trusts that the experts know.

As a social scientist, what would you want to know to predict an episode of chest beating or bond trading? Chest beating and bond trading are economic behaviors, to be sure, for they determine how much of the group's resources one can claim. To predict an episode of either, it would help if you understood the basics of the local cosmology, embodied in customs and rituals. Is it broadly mystified, religious, philosophical, or rational? What are the established social roles—hunter, warrior, trader, investor? What is the meaning of the particular custom within the local cosmology? Is the chest beater or bond trader engaged in a show of plumage, of force, of business savvy? What is the wider role of the custom—to display a penchant for violence, to raise capital? The more you know, the better you will be at predicting episodes.

For the purpose of prediction, the concept of self-interest, which is at the center of most theories of economic behavior, does not get you very far. The Yanomamo and the bond trader may be self-interested, but their behavior is

largely shaped by social institutions. Chest beating can only be understood in the context of the tribe's very particular cosmology. It is not that the Yanomamo warrior is a puppet of his culture. He reinterprets, challenges, and builds on his culture. He jokes about the ancestors who rule the earth and sky, rails at those ancestors when life treats him poorly, and devises new theories of fertility and weather. But the cosmology provides the lens through which he sees the world and the starting point for cultural change. The same goes for the bond trader. What the trader does makes sense only in the context of her special cosmology. She knows of no other way to interpret experience than through the lens of natural laws. She may chuck it all to join a Buddhist monastery, but she is not likely to question the laws of gravity or of supply and demand.

It is not just that the bond trader is rational and the Yanomamo belongs to a deluded cult that, incidentally, consumes a local hallucinogenic substance in large quantities. Economic practices also vary widely among modern, rationalized societies. Bond traders in Tokyo, Paris, and New York see the world through rationalized lenses, but through very different rationalized lenses. The same spirits do not rule the worlds of the Ndembu and the Yanomamo, and likewise the same laws of supply and demand do not obtain in Tokyo and New York. People in all of these places may be self-interested, but the concept of self-interest is of little use in explaining why people behave differently in different places.

Sociology's Distinct Approach to Economic Behavior

Economic modernization can be seen as a series of societal projects. There was the project of developing intercontinental trade routes, spearheaded by Europe's East India trading companies and colonizing monarchs. There was the project of building large-scale factories with wage labor forces nearby, spearheaded by early industrialists in Massachusetts and Manchester. There was also the project of divorcing the economy from society and polity, spearheaded by capitalists and politicians but also by philosophers and social observers. As Karl Polanyi argued in *The Great Transformation* (1944), British industrialization depended on the *idea* that the economy could be wrenched free of society—that a free labor market could be constructed by breaking traditional links between lords and serfs—as well as on the concrete public policies and capitalist practices.

One manifestation of the intellectual side of the project of splitting economy from society was the division of economics and sociology into distinct disciplines. In the nineteenth century, the dividing line between economics and sociology was difficult to draw. Most of the people who are now part of sociology's heritage studied economic behavior, and called themselves economists. Karl Marx was interested in how capitalism emerged from feudalism; Max Weber in how religious institutions hastened the development of capitalism; Émile Durkheim in the consequences of the division of labor. Empirical studies typically showed that the economy was not a distinct realm—that it was enmeshed in social life. In their struggle against this idea, economists increasingly turned to abstract theorizing in which they modeled behavior "as if" the economy could be treated as a world apart.

Sociologists continued to see economy and society as intertwined, but even sociologists came to accept the emerging division between the disciplines. Sociologists were inductive, deriving theories of social behavior by observing behavior. Economists were deductive, deriving theories of economic behavior from the axiom that self-interest drives individual behavior.

Economics thus came increasingly to resemble physics. As Paul Krugman (1994, xi) jokes, "An Indian-born economist once explained his personal theory of reincarnation to his graduate economics class. 'If you are a good economist, a virtuous economist,' he said, 'you are reborn as a physicist. But if you are an evil, wicked economist, you are reborn as a sociologist."' For the economist, the pinnacle of the academic pyramid had become the most pristine science with the most immutable laws. Economists spelled out how people would behave if they followed pure principles of self-interest. Like physicists, they thought they were identifying universal laws. Like philosophers, they imagined an ideal world and worked out the details of how people would behave in it. They came to play the role that prophets played in another age, conjuring up a perfect world and its rules of behavior.

Sociology became increasingly empirical, based on in-depth studies of communities and corporations and sectors of the economy. Robert and Helen Lynd's *Middletown* (1929) depicted the changed economic institutions, changing network structure, and slowly changing culture of an average American city circa 1925. Philip Selznick's in-depth study of the agency established to fight Appalachian poverty during the depression, *TVA and the Grass Roots* (1949), showed how officials and corporations could subvert public policy's economic goals. C. Wright Mills's *The Power Elite* (1956) showed that power was becoming increasingly concentrated in business, government, and the military and that links between the elites in those sectors were increasing. Meanwhile Digby Baltzell's *The Protestant Establishment* (1964) showed the declining exclusivity of the Protestant elite and the rise of other groups in business and society. William H. Whyte's *The Organization Man* (1956) showed that corporate customs made middle managers conformist and complacent, undermining the work ethic and entrepreneurialism that Max Weber had described among capitalists. In these and other studies, sociologists found economy and society inextricably enmeshed, but left it to economists to theorize economic behavior.

Since about 1980, both sociologists and economists have been challenging this division of intellectual labor, in which economists explain economic behavior using deductive models and sociologists explain all other kinds of

social behavior using inductive methods. Economists see economic behavior as shaped by society. Sociologists see family relations, religious systems, and political institutions as shaped by economics. And in particular, sociologists see social processes shaping economic behavior, not only at the margins, but at the center.

Sociologists began to explain economic behavior in terms of the same four social mechanisms they had observed shaping all sorts of social behavior. These mechanisms entered the common lexicon under the terms *institution*, *network*, *power*, and *cognition*.

Sociology's core insight is that individuals behave according to scripts that are tied to social roles. Those scripts are called conventions at the collective level and cognitive schemas at the individual level. Conventions and schemas make sense within a wider institutional framework, be it rational or religious or mystical. These conventions and schemas shape individual behavior, and so predicting economic behavior is a matter of comprehending conventions, schemas, and institutions. But prediction requires more than that, because conventions change. Understanding why they change is job one, and change can usually be traced to institutions, power, networks, and cognition. Economic *institutions* offer broad prescriptions for behavior. Institutions are sustained by occupational, industrial, and community *networks* that define social roles. *Power* shapes the evolution of new customs, when the powerful sanction the behavior of others and when they shape legal institutions. At the individual level, *cognition* is the carrier of conventions—it provides the schemas through which we make ongoing sense of conventions and through which we challenge them.

This anthology outlines the sociological view of economic behavior. It is divided into four parts, each focused on one of the social mechanisms that sociologists have discovered at the root of economic behavior. Each of the four groups of readings traces one social mechanism from its intellectual origins through studies that demonstrate its importance to studies that show how it meshes with the other mechanisms.

In this introductory chapter I endeavor to show that sociologists see these mechanisms as operating together to produce economic behavior patterns. I do so because it is easy to miss the forest for the trees. The economist Michael Piore describes economic sociology as "an enormous hodge-podge of ideas and insights, existing at all sorts of different levels of abstraction, possibly in contradiction with one another, possibly just incommensurate, without a basic theory or structure to sort them out, or order them" (1996, 742). This is a fair critique, to the extent that individual studies tend to focus on one of the four mechanisms, holding the others constant, and tend not to describe the big picture. Sociologists evaluate the effect of networks by artificially holding power constant just as physicists estimate the effect of gravity by holding atmospheric pressure constant. But sociologists have in fact been working toward an integrated theory of how economic customs

arise and change. All four of these mechanisms play roles in that theory. My goal is to shine some light on that integrated theory.

Institutions

In common parlance people use *institution* to refer to sectors of society—the *institution* of organized religion. Sociologists use the term when talking about particular conventions, some defined by law and some by tradition. Institutions range in complexity from simple customs of exchange to elaborate modern states. The American state is, in the end, a huge agglomeration of smaller conventions, some informal and others codified. Institutions, large and small, shape human behavior not only by providing behavioral scripts, but by representing the relationships among things in the world—between the local totem and the harvest, or between antitrust and progress. For sociologists as for anthropologists (Geertz 1983; Douglas 1986), conventions and routines influence behavior in rationalized societies much as they do in mystified and religious societies. While social life in modern settings may be organized around ideas of progress rather than around ancestor worship, the individual makes particular decisions based on convention, just as she did when it was frog totems and not mathematical formulas that ruled the world. Today we reenact most conventions with an understanding of their rational purposes, but this is not to say that we actually make rational calculations every time we act. Our conventions may revolve around rationality and self-interest, but they are conventions just the same.

Networks

We learn how to be warriors, bond traders, teachers, witch doctors through social networks. What do you do when a buyer fails to pay, or when a drought fails to succumb to incantations? The prescriptions come from networks of others. *Network* theory builds on early French sociologist Émile Durkheim's idea that social location shapes identity and behavior. Your network influences how you behave and your understanding of how people in other roles should behave. Role behavior is defined by conventions, which take the form of conditional prescriptions for behavior; to wit, *if* you are a chief information officer in a large automobile company, *then* you should advocate the transfer of the firm's purchasing function to a Web-based bidding system. Other actors in your network define how you should dress (Brooks Brothers or loincloth), talk, comport yourself, and respond to bids for bonds. Social networks are the carriers of new economic practices and new ideas of what it means to be rational and efficient. Social networks also reward role-appropriate behavior, such as making good on a promise to sell bonds at a certain price, and sanction behavior that breaks norms, such as larceny.

Power

Karl Marx first defined *power* not merely as coercion, but as the ability to shape how others view the world and their own interests. From the dawn of capitalism, successful entrepreneurs and managers have defined economic conventions by proselytizing, telling the world that the best way to run a business is their way. Success itself gives these people the authority to define what rational behavior is. Economic power also goes hand in hand with the political power to determine public policies that shape how people see their interests and how they can behave. For instance, in chapter 16, William Roy finds that at the beginning of the twentieth century, a group of financiers who wanted to consolidate American manufacturing shaped the American view that oligopoly is natural and large firms are more efficient than small ones. In this way, power shaped the public policies that govern competition between firms and the pricing conventions of firms. This sort of power over economic institutions and economic norms operates through political networks, industry networks, and professional networks that serve as the conduits for new policy ideas and business strategies.

Cognition

Sociologists use the term *cognition* to refer to the psychological process of making sense of the world and its social conventions. Max Weber and Émile Durkheim articulated theories of social psychology as part of their theories of economic behavior. For them, the human mind is programmed to develop categories, causal frameworks, and maps of the world. Rather than looking for a single human cognitive archetype, Durkheim and Weber were interested in how "human nature" varies across social settings. Weber saw that many social systems produce individual psyches oriented to tradition rather than progress. He traced both the traditional and the modern psyche to the structure of religious institutions. In sociology, but also in cognitive psychology, behavioral economics, and cognitive science, the idea that core aspects of the psyche are situational rather than hard-wired has become commonplace. Economic sociologists are particularly interested in how ideas of rational self-interest vary with exposure to what Erving Goffman (1974) called different "frames" for understanding the world. For Goffman as for cognitive psychologists, cognitive frameworks are situated in individual consciousness, but they are shared among groups of people exposed to common institutions. Bond traders share a culture that shapes individual cognitive structures, and the same can be said for Yanomamo warriors. In modern social systems, people are exposed to different frameworks—market efficiency, economic justice, and so on (Boltanski and Thevenot 1991)—in different realms.

Why does economic sociology need a fourfold theory? A change in only one of these factors may result in a change in economic conventions, but the other factors matter along the way. Take the question of why America's largest companies reversed course in the 1970s and 1980s, abandoning a guiding business strategy of diversification for one of core competence. In 1970, big firms were buying companies in other industries to diversify their assets. General Electric bought NBC, and R. J. Reynolds bought Nabisco. By 1990, big firms were buying others in the same industry to take advantage of their core managerial competence—Daimler bought Chrysler. How did this shift happen? Neil Fligstein and Linda Markowitz (1993) and Gerald Davis, Kristina Diekmann, and Catherine Tinsley (1994) trace the changes. A change in legal *institutions* opened the way for the change in business conventions, when the Reagan administration relaxed antitrust enforcement to permit firms to buy related businesses. The spread of the core-competence strategy also depended on the rise of a *network* of institutional investors and securities analysts who came to define de-diversification as in their own interest, because it was easier to evaluate companies that were not diversified. They used their market *power* to reduce the value of diversified conglomerates, inviting hostile takeover artists and CEOs to restructure big corporations. Core competence hinged as well on the force of an existing *cognitive schema*, of managerialism, which gave managers and investors a shorthand for understanding the core-competence model and for challenging the corporation-as-portfolio schema behind the conglomerate. Managerialism defined executive expertise in an industry as key to a firm's success in that industry, providing a rationale for the core-competence firm. Take away any one of these factors and the American firm might still be structured much as it was in 1970. Can the change be explained by the superior efficiency of the new model? Perhaps it was more efficient in some cases, but it spread even to companies that had been very successful with the strategy of diversification, and thus efficiency alone did not drive the process. The social redefinition of corporate efficiency was at work.

What do we know about how these four mechanisms shape economic behavior? Next I trace the evolution of each idea since its inception by previewing the selections from this anthology and outlining their particular contributions. The anthology is organized around the four sociological camps that have focused on these mechanisms, but each section highlights work that brings in insights from the other schools.

Institutions and Economic Action

Human nature surely plays a role in determining behavior, as economic theory suggests, but it cannot easily explain variation across societies and over time in how people behave. Differences across societies, it goes without say-

ing, can only be explained by something about society itself—by customs, institutions, resources. Society shapes the behavior of the individual. A newborn placed in the fold of Ndembu warriors will become a Ndembu warrior, and the very same newborn will become a bond trader among bond traders, a Catalan merchant among Catalan merchants, and a Calvinist preacher among Calvinist preachers. We know this from common sense more than from research, because university regulations prevent us from randomly assigning newborns to different tribes.

What we do know from previous research is that human behavior is highly predictable on average. You cannot always predict whether a particular Yanomamo will dig for yams this afternoon, but you can say with some certainty that in general the Yanomamo will dig for yams, and bond traders will trade bonds. To understand when and where these things will happen, you must grasp the logic underlying economic conventions. Is yam digging linked, in practice and in the minds of the natives, to the weather, to the days of the week, to the mood of totemic spirits? And bond trading? James Duesenberry's famous quip—"Economics is all about how people make choices; sociology is all about how they don't have any choices to make" (1960, 233)—captures this quality of social context. In these cases, it is not that the Yanomamo and the bond trader do not choose, but that they choose within cosmologies rather than across them.

Peoples' understandings of social customs are shaped by how the institutions around them express social order generally. When European institutions were broadly religious, they expressed social customs as an imperfect reflection of God's will. Kings, for instance, were thought to be chosen by God's own hand. Rationalization led to institutions that express social customs as an imperfect reflection of natural physical and social laws. Presidents, for instance, are thought to be chosen by the will of the people, because political philosophy defines democracy as humankind's natural state.

In religious and rationalized societies alike, people trace customs to something bigger than society itself. Rationalized societies trace customs not to the will of God but to physical and social laws inscribed in mathematical formulas. In each kind of society, people seek to divine the character of these exogenous forces by observation and epiphany. Thus, people read reason into the social practices they experience and understand worldly phenomena in terms of broader frames offered up by culture. Those of us born into a rationalized world spontaneously understand a thunderstorm with natural laws (low-pressure fronts) and not with spirit forces (displeased frog sprits) or the will of God. Comparative studies of capitalist societies show that they vary almost as richly in terms of causal imagery as do religious societies. Among societies oriented to salvation, institutions can direct human behavior toward prayer, warfare, or fulfilling a God-given calling. Among societies oriented to progress, institutions can direct human behavior toward market competition, coordination by large business groups, or state industrial planning.

In 1776, Adam Smith suggested that economic laws dictate that there is one best way to organize economic life. Trial and error would, he argued, reveal the details to nations. This suggested that modern societies would converge on one optimal set of economic institutions and behavior patterns. That assumption is now part of modern common sense, but comparative studies of capitalism do not bear it out. Some (Guillén 2001; Whitley and Kristensen 1996) find that different industrial systems have different comparative advantages, and suggest that countries are probably best served by recognizing and building on those advantages. Others (Fligstein and Byrkjeflot 1996) suggest that alternative market forms rely on different logics—labor markets, for instance, may rely on the logic of vocationalism or on that of managerialism—and that differences across countries may represent functional alternatives rather than, as Adam Smith might have argued, different stages in the evolution of rationalization.

Many similarities in economic conventions among rationalized societies, students of comparative capitalism argue, can be traced to mimicry or to the need to exchange goods and services across borders on common terms rather than to economic laws that make only one sort of fiscal policy (Campbell 2000) or incorporation law (Roy 1997) effective.

If America's economic conventions represent but one among many possible ways of efficiently organizing things, then understanding what shapes those conventions becomes an important sociological problem. Game theorists in economics explain differences in economic conventions across nations and over time with the idea of multiple Nash equilibria. How can economic systems generate different economic conventions, either over time or across space, even when all participants are behaving rationally? In a set of transactions that is repeated, the behavior of individuals may change from one round to the next (see Gibbons 1992). In consequence, given the parameters of the game and the stage of the game, different economic conventions may emerge.

Economic sociologists take a different view of why economic institutions differ across nations, why particular institutions persist, and what causes institutions to change. On the issue of why different kinds of economic systems arose in the first place, institutional analysts from political science and sociology argue that history has given different societies different material to begin with (Campbell 1998; Hall and Taylor 1996). For instance, in the late nineteenth century the French state planned and sponsored a network of railroads that linked Paris with all of the outlying regions, while the American state subsidized a handful of transcontinental railroads but left it to states and towns to subsidize various local and regional lines. Today the French state has a nationalized network of state-of-the-art high-speed trains that mirrors the network it planned in the nineteenth century, and the American state reluctantly subsidizes a semiprivate rail system with but one, slow, "high-speed" route. Why these persistent differences in the ways railways

are planned and run in the two countries? They stem in part from the fact that with the threat of invasion from all sides, France had by the 1700s established an absolutist military regime and a corps of engineers to build roads, canals, and then railroads to its perimeter. The descendants of that corps still plan railroads. The United States had little in the way of a central state, and no pressing military need for a similar transport system in the 1700s (Dobbin 1994). Thus early institutional differences in nations shaped economic patterns.

On the issue of why different kinds of economic institutions persist, economic sociologists argue that institutions such as laws governing property typically survive until someone directly challenges them. "Path dependence" has been the most recent shorthand among sociologists and political scientists for describing how systems retain essential characteristics over time (Campbell 1998; Hall and Taylor 1996; Stark 1992). Once a group or nation goes down one path, toward antitrust or state industrial planning, for instance, future paths will necessarily lead off from that first choice. Different ways of organizing economies tend to be sticky, or resistant to change, and many different approaches may prove sufficiently efficient to persist. The institutional economist Douglass North, who won the Nobel Prize in economics in 1993, adopted the idea in his book on institutions and institutional change (North 1990). Social institutions that arise for reasons of chance survive to shape future economic behavior. The idea is not incompatible with game-theorists' idea of multiple equilibria, but the focus is on how institutions shape basic forms of rational behavior.

Max Weber suggested that institutions persist not only because they develop structural inertia but because they come to make sense to people, and that understanding what kind of sense they make is the key to understanding why they persist. Weber insisted that sociologists take what anthropologist Clifford Geertz later called the "native's point of view"—that they explore the meaning of social conventions to the people practicing them. Understandings of particular behaviors, it turns out, vary widely even across rationalized societies. Take cartels. In late-nineteenth-century Britain they were understood to be an efficient mechanism for coordinating industries. The government backed cartels as the wave of the future. Yet in the United States they were labeled an evil private invention that threatened both economic growth and democracy (Dobbin 1994). Joining a cartel meant something very different in Britain than it did in America.

Most customs have an implicit meaning, and enacting them in context reinforces that meaning. The Ndembu circumcision custom signifies the tribe's belief that the local totem increases fertility when invoked at the onset of adolescence. The custom of antitrust enforcement signifies the tribe's belief that price competition begets progress. These customs are usually enacted without much explanation, because everyone understands their meaning. Even anthropologists catch on pretty quickly. Both customs build on

wider cosmologies, representing specific causal relationships between the tribal totem and fertility or between "market mechanisms" and progress. Weber insisted that we try to understand the meaning of customs to the groups who practice them, for people only practice customs that make sense to them. This is not to say that customs necessarily have the intended effects, and they may in fact serve functions that are invisible to those who enact them (Weber 1978, 4).

On the issue of why economic institutions change, Weber argued that change could originate in politics, in the law, in religious ideals. The model of change that most sociologists embrace is built on the idea of punctuated equilibrium that Stephen Jay Gould (1989) sketches for the biological world and Stephen Krasner (1984) adapts for the social world (and see Fligstein 2001). Customs tend to persist until something shakes up the social system, opening up the possibility of change. New customs are often worked out in power struggles, and they may or may not be more efficient than those they replace. The jury is still out, for instance, on whether the core-competence firm is ultimately more efficient than the diversified firm it replaced. Institutionalists from the field of economics (e.g., Williamson 1975) initially argued that institutions evolve toward increasingly efficient forms—that history is efficient when it comes to institutions. But even economic institutionalists (North 1990) have increasingly argued that change may be shaped by power and happenstance as well as by efficiency. Change in economic customs may more closely resemble random mutation than teleological progress.

Sociological thinking about institutions has evolved significantly since the time of Weber, particularly with the realization that different sorts of rationalized institutions have prospered alongside one another. Chapters 2 through 7 explore that evolution. In *The Protestant Ethic*, Weber traces the new spirit of capitalism among Calvinists, and the conventions of hard work and saving, to a new religious ethic—showing how a religious movement could produce rational economic conventions. In chapter 3, John Meyer and Brian Rowan discuss how new management conventions diffuse across fields of organizations, along with supporting rationales of efficiency. In chapter 4, Paul DiMaggio and Walter Powell build on this idea to show how three important mechanisms of diffusion operate, among networks of professionals, of business executives, or of organizations and the government agencies that regulate them. In chapter 5, Viviana Zelizer explores how the convention of child factory labor was put to an end by a social movement, which offered a new definition of the role of childhood in industrial society. In chapter 6, Richard Whitley explores the origins of different national "business systems" in East Asia, and the public policy institutions and private economic conventions that go along with them. Finally, in chapter 7, Gerald Davis, Kristina Diekmann, and Catherine Tinsley trace how a change in business conventions came about in large American firms, as the portfolio/conglomerate model was replaced by the core-competence model.

Where New Institutions and Customs Come From

Chapter 2 is an excerpt from Max Weber's *The Protestant Ethic and the Spirit of Capitalism*. Weber was a professor of economics in Germany, but with the publication of *The Protestant Ethic* he became one of the founders of modern sociology. Weber wondered how capitalism could arise in Europe out of the conservative economic traditions of feudalism and Catholicism, which did little to encourage people to work hard or to save. He found that those customs originated in early Calvinism, which taught predestination, or the idea that one's destiny in the afterlife was fixed prior to birth. What you did in life could not win you salvation, but it could signal your fate. God gave everyone an earthly calling—work to be done in His name—and demanded self-denial and asceticism. Commitment to these ideals might signal that one was destined for heaven. The idea of God's calling led Protestants to devote themselves to their work, whatever it was. Asceticism led them to save, for they were not to squander money on trinkets or religious icons. Devotion to work and saving became enduring customs—they became institutionalized. The customs spread even beyond the boundaries of Protestantism, and endured even when Protestantism took a new course that placed less emphasis on the calling and on asceticism.

In *The Protestant Ethic*, in his various studies of the world religions (1951, 1952, 1958, 1963), and in his opus on capitalism, *Economy and Society* (1978), Weber tried to understand the customs found in different social systems, the thinking behind those customs, and the forces that lead to changes in customs. Some (e.g. Novak 1993) argue that Catholicism was not so different from Protestantism and promoted the same kinds of behavior, but what was novel about Weber's ideas was not so much his particular argument as his vision of society. For Weber, the beliefs that underlie customs sustain them. In Calvinism, the belief in predestination—the belief that one is destined for heaven or hell at birth—sustains the custom of asceticism, because asceticism is thought to be a sign that one is bound for heaven. Weber argued, extending the concept, that in modern firms the belief in professional expertise sustains the custom of hierarchical authority. In *The Protestant Ethic* Weber explained how well-entrenched economic customs could change, as related parts of the social system change. In this case, a shift in religious beliefs was key, but Weber argued that changes in other parts of the social system—beliefs, political power, scientific knowledge—could lead to changes in economic conventions.

The Institutionalization of Rational Myths

Chapter 3 is John Meyer and Brian Rowan's seminal 1977 article sketching an approach to organizational sociology rooted in Weberian ideas. Weber

argued that concrete economic customs made sense to people within the framework of a wider cosmology. Meyer and Rowan's "Institutionalized Organizations: Formal Structure as Myth and Ceremony" depicts how modern organizations adopt structures and practices that symbolize rationality and fairness. Their question: How do new ideas and practices spread among organizations to shape our understandings of progress?

When Meyer and Rowan's piece was first published, the prevailing view of the firm followed Adam Smith's thinking about national economies—that economic laws determined "best practices" for business and that those best practices would evolve everywhere eventually. If organizations looked alike, it was because they were subject to the same economic laws. If they had accounting departments and strategic planning teams and performance evaluations, it was because each organization had found each practice to be efficient. Meyer and Rowan described the rationalized practices found in organizations in terms of "myth and ceremony." Organizations adopt practices that embody myths of rationality with the goal of symbolizing their commitment to efficiency to the world. Organizational entrepreneurs who invent new practices often promote them directly to those in their networks and more widely in management magazines, through cover stories on quality teams or empowerment. New practices became "institutionalized"—taken for granted—as this process proceeds. New practices must conform to the wider understanding of what is rational, and so it is easier to sell certain kinds of practices in Osaka than in Omaha. In Meyer and Rowan's world, firms come to look alike because they jump on the same bandwagons, not because each discerns the (same) optimal way to organize itself.

How Fields Spread Rational Myths

In 1983, Paul DiMaggio and Walter Powell built on this idea, sketching the networks through which new rational customs diffuse among organizations—political networks, professional networks, and networks of firms. Schools were coming to look more like one another, and so were hospitals, auto factories, and charities. A growing body of standard practices could be found in each field. Like Meyer and Rowan, DiMaggio and Powell described the driving force behind institutionalization as social—managers of auto factories did not independently invent the same business practices; they copied those practices from leading firms.

Copying of organizational practices usually follows one of three patterns. Sometimes public policy encourages organizations to adopt new conventions ("coercive isomorphism"). For instance, federal regulations dictate that schools must meet certain standards, or give certain tests (Meyer and Scott 1983). Sometimes professional networks that span organizations promote new conventions ("normative isomorphism"). For instance, finance managers promoted the portfolio approach to corporate diversification in which

the firm held a portfolio of different businesses (Fligstein 1990). Sometimes managers cannot figure out how to best proceed to achieve their goals, so they copy practices of successful organizations ("mimetic isomorphism"). For instance, American automakers copied Japanese production techniques after Japan made inroads into America's auto market. Mimetic isomorphism can have the character of a cargo cult, in which the tribe builds a wooden replica of a cargo plane in the hope that the replica will bear forth the same goods the real plane bore. Through these three processes, organizations within a sector come to look more and more alike.

Key business strategies often spread through mimetic isomorphism, and as Heather Haveman (1993) shows in a paper titled "Follow the Leader," firms that are defined as industry leaders due to high growth or sheer size are more likely than others to be copied by their peers. Among savings and loans, when industry leaders diversify into real estate or into commercial loans, other firms follow their lead. The very definition of what a savings and loan is is changed in the process.

The sectoral differences in management that DiMaggio and Powell describe have declined over the last few decades, with the rise of a more generic model of organizing (Meyer 1994). Social service agencies increasingly have CEOs, and hospitals increasingly have mission statements. But DiMaggio and Powell would surely see this as the natural extension of the process they document, as isomorphism increases across sectors as well as within them.

Meyer and Rowan and DiMaggio and Powell have charted how rational conventions spread through the forest of organizations to alter notions of rationality. The quality management movement, for example, turned the tide against the earlier movements of Taylorism and Fordism to encourage production workers to help design the production process (Cole 1989). The movement helped spread the idea that worker participation in job design could be more efficient than a strict division of labor between those who design assembly lines and those who work on them. To call the underlying idea of empowerment a rational myth is not to say that there is nothing to it, but rather, to suggest that such ideas diffuse much as customs diffuse in religious or mystical social systems.

For DiMaggio and Powell, as for Meyer and Rowan, new customs diffuse only when they accord with existing cognitive schemas. If the idea of school vouchers succeeds in the United States, it will be because Americans are inclined to think that public bureaucracies breed inefficiency and that the corrective is private competition.

Revolutions in Rational Customs

Chapter 5 excerpts one of Viviana Zelizer's rich Weberian analyses of how modern economic conventions came to be—in this case the convention of banishing child labor from factories. Zelizer's study shows how rationalized

roles can be altered. Under early capitalism, children sold their labor by the hour, just as adults did. They had no special role in the factory, and they had no special role in the family, in that every able member contributed his or her labor. Social institutions of all sorts supported this view of the role of children. Life insurance for children was designed to replace children's income. Foster parents favored older boys because of their earning potential. The courts compensated parents of children killed in accidents for the child's lost wages. Early capitalism had rationalized the role of children in parallel to that of adults.

Between 1870 and 1930, children's advocates sought to remove children from industry, changing the meaning of childhood. They described childhood as a sacred category, defining children's value to parents as primarily emotional rather than economic. This crusade succeeded, altering the treatment of children across realms. Most forms of child labor were outlawed. Life insurance for children was redefined to provide parents with compensation for their grief over the loss of a child. Adoptive parents came to favor baby girls, who were inferior earners but superior objects of emotional attachment. The courts awarded grieving parents compensation for their emotional loss rather than for the loss of their child's income. Weber had argued that change in economic institutions can come from many different corners. Zelizer shows that a new rational myth of childhood emerged out of a social movement. The agents of this change were social reformers with a new interpretation of childhood, just as the agents of change in Meyer and Rowan's depiction of organizational life are management consultants with new rational myths of management. In the new myth, children are an asset we invest in for the future rather than a source of labor for the present. In Zelizer's study, rationalized economic conventions can change form entirely, and if those changes persist, we attach rationalized significance to the new form just as we had attached rationalized significance to the old form. The abolition of child factory labor has the feel, in retrospect, of something that was natural and historically inevitable. But child factory labor represented a natural and efficient economic convention at the time, and the redefinition of childhood simply represented another rational interpretation of the role of the child, as worker-in-training through schooling rather than apprenticeship.

National Institutions and Business Recipes

In chapter 6 Richard Whitley's "national business system" approach does for the world's different forms of capitalism what Max Weber did for the world religions, sketching the principles underlying each form. Weber had shown that under Protestantism, Catholicism, Hinduism, Buddhism, and Judaism, different religious logics of salvation corresponded to different prescriptions for how to behave. Whitley finds that there are many different

sorts of capitalist economic systems, each with its own conventions and its own logic of rationality.

Whitley begins with national economic and political institutions that affect the firm. National institutions offer a particular social construction of the economy—a particular understanding of the relationships between state and industry, buyer and supplier, finance and industry. They also offer concrete conventions for raising capital, buying components, offering goods for sale, and so on. Within each nation, every industry faces a unique kind of business environment, and successful "business recipes" are those that are best suited to the environment. A winning business recipe for telecommunications may fail miserably in a year or two as the environment changes.

Each industry faces unique circumstances, but general patterns can be seen within each nation. Japan, Hong Kong, Korea, and Taiwan illustrate. Because they operate on very different principles, these economies favor different sorts of business recipes (see also Hamilton and Biggart 1988; Johnson 1982; Cumings 1987; Westney 1987). For instance, the principal economic actors are quite different in these countries, for historical reasons, and the different sorts of actors correspond to different recipes for the pricing of parts. The primary economic actors have been the *kaisha*, or large corporation, in Japan; the *chaebol*, or family-controlled conglomerate, in Korea; and the Chinese Family Business (CFB) in Taiwan and Hong Kong. Cross-shareholding in Japan means that there is typically little competition among parts suppliers, each of whom is formally connected to a buyer. Suppliers are more likely to compete in Taiwan and in Hong Kong, where firms are smaller and where connections between them are weaker. In the end, these business systems depend on different logics, and they create efficiency in different ways. Whitley focuses on the logics underlying these different business systems, but others focus on how new business conventions come about and alter those logics (Gao 1977; Stark 1992).

Each national business system embodies a different conception of how capitalism operates—of the different collective actors involved (family-owned businesses versus monolithic firms) and the relationships among them. For Whitley, each system has a logic that comes to shape how individuals think about their own behavior; in consequence individuals have different cognitive maps of the economic world, and groups have different customs that accord with those maps.

How Rational Myths Emerge

In chapter 7, Davis, Diekmann, and Tinsley (1994) build on the insights of Meyer and Rowan and of DiMaggio and Powell about the role of fads in popularizing new business practices. They explain the shift from the conglomerate to the focused firm that came about in the 1980s as corresponding

to a new myth of corporate rationality. The old prescription for how a firm should be run, based in portfolio theory, suggested that huge firms should spread risk through diversification. The challenger model, based in classical managerialism, suggested that huge firms should instead focus on the activities that their management teams are best equipped to manage—on the core industry and kindred industries. This chapter exemplifies the theoretical integration of the new economic sociology, because it uses ideas from institutional, network, power, and cognitive theories.

When the Reagan administration relaxed antitrust law, a change in *institutions* made it possible for firms to switch from diversifying acquisitions to same-industry acquisitions. The new core-competence model of the firm depended on the growing *power* of institutional investors, who control large blocks of stock and who dislike conglomerates because their prospects are difficult to assess. A *network* of hostile takeover specialists developed the model of buying and breaking up the large conglomerates that institutional investors had undervalued. The new strategy was compelling to business because it came along with a familiar *cognitive* framing—that firms should specialize in industries that made the best use of management expertise. Davis and colleagues thus build an explanation of this shift in corporate strategy that depends on all four of the core insights of economic sociology.

The chapters in the institutional section focus on how economic conventions come to be and on what makes them change, emphasizing how our understandings of conventions support them. Economic institutions and conventions provide broad frameworks for understanding the world, and this can be seen in the differences between Catholicism and Protestantism as Weber depicts them in chapter 2. They also provide concrete scripts for how to behave, and this can be seen in the work of John Meyer and Brian Rowan, who describe how new conventions spread across organizations that hope to appear rational and to be rational. For DiMaggio and Powell, dominant firms, professional groups, and nation-states promote new management conventions, contributing to the evolution of conventions. Zelizer shows how one rational convention—child factory labor—was altered forever, when a social movement succeeded in redefining the role of childhood in capitalism.

Whitley carries Weber's ideas in another direction, exploring the logics underlying different forms of capitalism just as Weber had explored the logics underlying the different world religions. For Whitley, each national business system depends on a peculiar set of economic customs, which reinforce one another and which thereby produce a sort of self-sustaining system. Finally, Davis and colleagues show how a change in business conventions can depend on the confluence of *powerful* actors introducing a new strategy, a *network* promoting the strategy, regulatory *institutions* that permit the change, and a *cognitive* framework that legitimates the new strategy.

Networks and Economic Conventions

Max Weber documented the daily customs, and wider institutions, found in different societies. He asked how economic conventions differed between feudal Catholicism and urban Protestantism, and how people's understandings of the world sustained those different conventions. For Weber, conventions survive only because people attach meaning to them—because they make some sort of sense to people. So to understand a society, he sought to grasp the logic running through its conventions and institutions. For Weber, conventions, institutions, and their meanings drive social behavior.

Émile Durkheim tackled society from another angle, trying to understand different sorts of societies through their networks and roles. For Durkheim, social and economic conventions were held in place by social networks. Social networks varied dramatically among the societies Durkheim studied, from the tribes of the South Pacific to the industrial societies of early-twentieth-century Europe. These differences were rooted in the division of labor. In tribal societies, gathering food, making clothing, and building shelters were common tasks. Men and women typically performed different tasks, but that is as far as the dividing up of tasks went. Shared experience was the glue of social life. Tribesmen identified with fellow tribesmen.

In industrial societies the tasks of everyday life were divided up, among ranchers, farmers, factory workers, railwaymen. People who shared an occupation shared common experiences. They learned the everyday routines of the job from the occupational network, and came to identify with that network and its routines. Occupation became a primary role. Interdependence was the glue of social life—ranchers and railwaymen may have had little in common, but they depended upon one another.

Network theorists build on Durkheim's core ideas about the importance of social milieu and of role. Interpersonal networks provide behavioral scripts, or conventions, suggesting, for instance, that managers should "empower" workers by giving them more autonomy. Those networks convey cultural frameworks—chunks of tribal cosmology—so that the new convention of "empowerment" arrives complete with a new theory of human motivation.

The five chapters that follow Durkheim's develop two themes. The first three explore how networks generate and reinforce the very economic conventions that the institutional studies in the first section document. In chapter 9, Mark Granovetter builds on Durkheim's insight that networks establish economic conventions and sanctions. The norm against price gouging is enforced informally by members of an industry network; a seller who is known for price gouging in times of scarcity will lose customers in times of plenty. Alejandro Portes and Julia Sensenbrenner, in chapter 10, build on Granovetter's idea that social networks enforce economic norms via informal sanctions, and show how those norms can have positive effects for the community. In chapter 11, Eric Leifer and Harrison White argue that producers choose from a set of socially defined market roles—price leader, luxury brand, volume discounter—each with a set of off-the-shelf conventions.

The final two chapters explore the structural effects of networks. They explore how networks produce concrete economic advantages that most economic theories ignore. In chapter 12, Ronald Burt's *Structural Holes* shows how missing links in networks create patterns of information asymmetry. People with ties that span these gaps have economic advantages. In chapter 13, Brian Uzzi shows that both intimate and arms-length ties to banks shape the interest rates that small businesses receive on loans. Taken together, these studies provide a striking picture of the role of networks in establishing business customs, in sanctioning firms that do not abide by accepted business practices, and in creating economic advantages for firms.

How Social Milieu Shapes Economic Roles and Behavior

Émile Durkheim pioneered the study of modern occupational networks. Durkheim's *The Division of Labor in Society*, excerpted in chapter 8, charts the origins of the division of labor and explores how social attachment was restructured with industrialization, as individuals developed primary attachments to their occupational groups rather than simply to their local communities. For Durkheim, the glue that held society together was now people's interdependence rather than their common situation. Identification with a group of peers remained important, but those peers now consisted of an occupational group at large.

Durkheim understood social attachment to differ between primitive societies without differentiated roles and modern societies where roles were highly differentiated. Under feudalism virtually everyone was a peasant and the basis of social attachment, and of identity, was the fact that serfs' lives and livelihoods were shared. In complex societies with elaborate divisions of labor an individual's identity was connected to an occupational community of others, many of whom the individual never met. Benedict Anderson (1983) would later call the modern nation an "imagined community," comprising people who identify with others they have never met.

Durkheim saw that in modern societies, identity was formed by religious affiliation and by nationality but also increasingly by occupation. Managers and workers, professionals and bureaucrats thus behave according to occupational scripts. Durkheim documented the increasingly fine-grained economic conventions that emerged in modern societies. He showed that occupational networks were becoming the source of the economic conventions and meanings that Weber saw at the heart of modern economic behavior. The division of labor generated a complex web of overlapping occupational networks, each with elaborate socialization processes that conveyed particular customs of work.

How Networks Constrain Economic Behavior

Sociologists have long been interested in why people behave according to economic conventions. Institutionalists, from Weber forward, have argued that customs that are socially defined as self-interested are not hard to explain. In rationalized societies, people believe they should act in their self-interest and are always on the lookout for new ways to behave self-interestedly. Economic customs that are socially defined as altruistic are harder to explain, but network theorists argue that we follow altruistic customs because we are embedded in social networks. Our reputation, prestige, and future capacity to buy and sell depend on our behavior in a network of peers.

Chapter 9 is Mark Granovetter's erudite "Economic Action and Social Structure: The Problem of Embeddedness," which in 1985 gave the new economic sociology a theoretical shot in the arm, challenging two extreme views of economic behavior and proposing a middle ground in the tradition of Durkheim. Sociology's oversocialized conception of economic behavior (Wrong 1961) suggested that we follow norms like lemmings following the crowd. Neoclassical economics' under-socialized conception of economic behavior seemed to suggest that individuals are atomized decision-making machines unaffected by culture and socialization.

Granovetter proposed instead that individual economic choices were embedded in social context. Workplace and professional networks shape behavior, determining the kinds of economic behavior people can imagine and constraining the kinds of economic behavior they can pursue. Granovetter thus explains how rational actors can decide to abide by economic conventions even when doing so costs them money.

To illustrate, Granovetter tackles Oliver Williamson's "transaction cost" theory from institutional economics, which addresses the conditions that encourage a firm to merge with its supplier rather than to use the open market to obtain supplies. Williamson argues that a firm will merge with its supplier (will "vertically integrate") where it is efficient to do so; in particular, where the supplier has the opportunity to price-gouge. Granovetter counters that suppliers often abide by the norm against price-gouging, because their reputations and identities depend on this convention. Networks, moreover, often punish price-gougers by denying them business. Thus firms do not have to buy suppliers who might have the chance to price-gouge, because social networks discourage gouging.

Granovetter's theory melds elements of the neoclassical economic view, that people are self-interested maximizers of income, with elements of the sociological view, that social milieu shapes behavior. In Granovetter's model, for instance, it may be rational in the long run for a seller to follow social norms about pricing even when, in the short run, those norms impinge on her profits. Francis Fukuyama's bestseller *Trust: The Social Virtues and the*

Creation of Prosperity (1995) builds on Granovetter's idea that trusting social networks confers economic advantage on a society by obviating the need for extensive regulation, generating spontaneous cooperation and assistance, and making economic relations collaborative rather than legalistic.

How Networks Produce Social Capital and Reinforce Conventions

Granovetter argues that people's social networks can constrain them to abide by economic conventions, such as that against gouging. Chapter 10 is Alejandro Portes and Julia Sensenbrenner's "Embeddedness and Immigration: Notes on the Social Determinants of Economic Action," which builds on Granovetter's idea of embeddedness coupled with the idea of "social capital." French sociologist Pierre Bourdieu introduced the idea that social networks offer a type of "capital" for achieving economic ends. James Coleman (1990) in sociology and Robert Putnam (1993) in political science later built on the idea. Like Granovetter, Portes and Sensenbrenner show that social networks can promote economic conventions that serve the community even if they do not serve individual interests, narrowly construed. Like Granovetter, they challenge the view that people make economic decisions in isolation and show that conventions persist because networks come to expect members to abide by them.

Portes and Sensenbrenner distinguish mechanisms through which social capital can confer advantages on group members. *Reciprocity exchanges* involve the trading of virtual chits across economic exchanges. By doing good for someone else, you place them in your debt and you can expect them to do good for you in the future. *Bounded solidarity* (Durkheim 1933) refers to solidaristic bonds that tie communities together and cause them to support members in need. *Enforceable trust* refers to group sanctioning of behavior, following Granovetter's idea that malfeasance and bad faith will become known to the group and will be punished in subsequent exchanges.

Portes and Sensenbrenner illustrate the cases of bounded solidarity and enforceable trust in immigrant communities. In the case of bounded solidarity, ties among members of an immigrant community cause them to stand together behind a community member who is threatened. This creates, for instance, a kind of premium-less insurance pool for legal expenses. In the case of enforceable trust, immigrant groups often establish informal financial networks and rotating credit associations. Having no legal hold on members, these groups depend on informal sanctions such as the threat of ostracism from the business community. Enforceable trust succeeds to the extent that members depend on others in the community for business and for future loans. This kind of social capital safeguards lenders while providing credit to group members who might not qualify for loans from traditional lenders. In other words, strong in-group networks can serve to enforce such conven-

tions as loan repayment. For Portes and Sensenbrenner, then, social networks create, convey, and enforce economic conventions.

How Market Networks Produce Roles

Institutionalists argue that corporations copy very specific practices—deconglomeration—from their competitors. Sociologists who look at producer markets as networks argue that market networks also generate an array of conventional roles. Market roles are themselves institutionalized. Firms deliberately choose from among these roles, often in an effort to find a market niche that will shield them from competition. For network theorists of markets, the configuration of market roles (large-volume, low-cost manufacturer; elite, low-volume producer) is itself routinized and recognizable across industries. CEOs do not really create market strategies de novo, they adopt one socially defined market role or another.

In chapter 11, Eric Leifer and Harrison White (1987) expand on White's (1981, 2002) network theory of markets, in which sellers follow the customs for pricing that are established by other sellers rather than discovering what "the market will bear" by trial and error. Sellers look to their peers for signals about how to set prices, how to determine quantities produced, and how to assess the trade-off between quantity and quality. For White, it does not make sense to think of markets, pace neoclassical economists, as composed of atomized producers paying attention only to the price signals coming from buyers.

In "A Structural Approach to Markets" Leifer and White show that producers define their identities relative to those of other producers. They choose from roles such as price leader, luxury brand, and volume discounter. These roles, like the occupational roles Durkheim describes, come with a set of prescriptions for how to behave—that is, economic conventions. The roles are based, in large part, on a socially established menu of decisions about quality, quantity, and price of the product. Whereas the economist Michael Spence (1973) argued that in labor markets, people signaled their productivity with educational attainment, White argues that in production markets sellers send signals to other sellers to mark their market territory. A new frozen pizza maker signals her niche by her prices, quantities, and quality, and she chooses that niche based on her perception of the niches that existing producers have left open. The identity, or strategy, she selects—inexpensive but chic, or the best that money can buy—soon locks her into a market position.

Like the institutionalists, network theorists show that individuals draw their strategies from customs rather than making rational calculations, from scratch, in each situation they face. White goes one step further, arguing that even the dimensions on which economic actors distinguish themselves from the crowd are determined by convention (see Bothner 2000). They are institutionalized. While for Granovetter a producer is constrained to follow the convention against gouging by concern over his reputation among buyers, for Leifer and White a producer is constrained by the behaviors—the business strategies—of other producers.

How Network Position can Confer Social Capital

In the tradition of Durkheim, Ronald Burt and Brian Uzzi are concerned with how one's network provides information about roles, reputations, and economic opportunities. This information can confer economic advantage, and it can shape pricing decisions. For Burt, "structural holes" in social networks create information asymmetries—imbalances of information among individuals or firms—and opportunities. Economists George Akerlof (1970) and Joseph Stiglitz (2002), who shared the 2001 Nobel Prize in economics with Michael Spence, have explored the consequences of information asymmetry but have not seen it as a feature of networks. Akerlof's famous paper "The Market for Lemons: Quality Uncertainty and the Market Mechanism" (1970) illustrates the problem of information asymmetry with the market for used cars. Information asymmetry depresses the prices that buyers are willing to pay for used cars, because while each seller knows whether he has a good machine or a lemon, buyers must operate on the assumption that all cars on offer are lemons.

Burt focuses on network structures, arguing that there are "structural holes" in all social networks—missing links that create information asymmetries. Where (B) knows both (A) and (C), who are strangers, (B) may be able to take advantage of his position. The headhunting industry works on this principle, with headhunters connecting dissatisfied executives with firms in search of personnel. The headhunter is rewarded for his network position in the form of a commission. *Structural Holes* shows that one can profit from spanning a hole in a network. Burt's theory has obvious practical implications, for it suggests that people should tap into diverse networks to maximize their economic opportunities. Mark Granovetter's 1974 book, *Getting a Job*, illustrates one way in which structural holes create opportunities. In his study of how people actually make the connections that get them jobs, Granovetter finds that people typically find jobs through weak social ties rather than through strong ones. Strong ties tend to produce overlapping information. If you are looking for a job and you ask all of your current coworkers, you will discover that they know about the same job openings. If you search through weak as well as strong ties, asking your college friends, your dentist, and your dry cleaner, you tap into wider networks of information and are more likely to land a job.

Burt's theory of structural holes helps to explain many economic phenomena that others have not been able to explain. Firms that cooperate with industry peers do better than those that do not, and this has long been put down to collusion. Network theory suggests that there may be more to it. Ingram and Roberts (2000) find that hotels make more money when their

managers have many friends among their competitors, because those friends pass on overflow clients and exchange information about the market. Wayne Baker's *Networking Smart* (1994) and *Achieving Success through Social Capital* (2000) have brought such insights to an audience of managers seeking to understand how to make the best strategic use of networks.

How Network Ties Influence Prices Paid

Burt's theory of structural holes suggests that networks can create information asymmetries that advantage the well connected. Brian Uzzi's structural studies of networks and pricing demonstrate that network connections shape reputations and thereby influence pricing. Economic sociologists have sometimes been criticized for not studying the most important economic phenomenon, price. In chapter 13, Uzzi does just this in an award-winning study that combines ethnographic analysis with quantitative analysis of data on bank loans to small firms.

Do firms with similar profiles pay the same interest rates, regardless of their ties to the banks they borrow from? Common sense and conspiracy theory suggest that close personal ties might get you lower rates. Uzzi shows that it is not so simple. It is true that firms with close personal ties to banks receive favorable rates, but it is firms that have both close ties and arm's-length ties that receive the best rates. Close social ties encourage banks to share resources, but arm's-length ties give them objective information about a firm's creditworthiness. Both kinds of network ties help firms. Uzzi and Lancaster (forthcoming) find an equally interesting pattern of relations between networks and prices in the legal industry. Close ties lower prices (legal fees), as in banking, but corporate board ties increase the prestige and expertise of a law firm in its prospective client's eyes, and thus raise legal fees.

Network theorists have developed a number of different insights about economic behavior. Durkheim argued that networks create behavioral norms—conventions—for occupational groups and for firms. Like institutionalists, Harrison White is concerned with how customs make sense to people, and hence he focuses on how concrete interpersonal networks provide individuals with examples of how to behave rationally—scripts for how a luxury producer, or a volume discounter, should play the game. Granovetter shows how networks influence reputation and identity and thereby cause members to adhere to economic conventions. Portes and Sensenbrenner stand on Granovetter's shoulders to show that dense networks can enforce such norms as loan repayment and thereby substitute for legal sanctions. Ronald Burt and Brian Uzzi develop structural theories of networks, asking how networks shape reputations and transmit economic information.

Following the chapters on network theory is a group of chapters that emphasizes how power influences economic conventions. For institutionalists, people use power to promote the business strategies and regulatory institutions that they want to see adopted. Thus, according to Davis and colleagues, in the 1980s and 1990s institutional investors and securities analysts had the power to lowball stock in diversified firms, pressuring such firms to join the core-competence bandwagon. Network theorists see corporate power being used to (*a*) sanction firms that practice malfeasance, according to Granovetter, (*b*) prevent potential competitors from entering markets, according to Leifer and White, and (*c*) gain advantage over isolated firms, according to Burt. In the coming section, the focus is on how the powerful are able to influence (*a*) public regulation of markets and (*b*) business conventions.

Power and Economic Conventions

Like institutionalists, power theorists try to explain how economic conventions arise. They ask how power shapes conventions. Karl Marx's analyses of feudalism and capitalism inform most contemporary power theories. His economic sociology was rich and variegated, but the idea that has most influenced contemporary economic sociologists stems from his observation that under capitalism as under feudalism, people seldom perceive the exercise of power. Serfs accepted their positions as part of the natural God-given order. Workers accepted *their* positions as part of the natural pecking order under capitalism, in the belief that aptitude and fate separated assembly-line workers from Henry Ford.

Marx's idea was that power relations are obscured by ideology. It is not the threat of force that is the key to power, but the capacity to cause people to see certain economic conventions as natural and inevitable. Powerful individuals, firms, and countries promote their favored economic conventions not merely as such, but as good for society at large. Once a country, a firm, or a tycoon has convinced the world of the efficacy of a new public policy or business strategy, that policy or strategy is held in place not by the sustained exercise of power, but by its own self-evident efficacy (Lamont 1989).

Power theory has increasingly come to parallel institutional theory, in that both build on the idea that we read utility into the social conventions and institutions that surround us. When we see antitrust law in action, we develop explanations of it as a necessary component of an efficient market. We do not naturally think of it as the legacy of a nineteenth-century power struggle among different groups. Charles Perrow's (2002) *Organizing America: Wealth, Power, and the Origins of Corporate Capitalism* takes this approach to its highest form by arguing that large-scale capitalism emerged not because it was more efficient than small-scale production, but because a wealthy few wanted to dominate the economy. What drove the evolution of huge firms was not the democratic striving for plenty, in Perrow's view, but the striving of a small group for control over the economy.

The four selections in the third section of the anthology treat two broad issues. The chapters by Karl Marx, Neil Fligstein, and William Roy explore how the powerful devise policy institutions and business conventions to serve their own interests, framing those institutions and conventions as neutral and efficient. In *The German Ideology*, Marx argues that modern states were built to reinforce the power of capitalists but that they survive under the guise of democracy and freedom of opportunity. Marx saw the rhetoric of democracy and freedom as a smokescreen for a system of economic regulation designed to enrich owners of firms and impoverish their employees. The chapters by Fligstein and Roy exemplify how power theorists now use Marx's insight in combination with institutional and network insights. In each, power played a role in the initial formulation of a new business convention, networks helped to diffuse that convention, and institutionalization (meaning-making) helped to ensure that it would become taken for granted. Fligstein shows that management subgroups have struggled over control of the modern corporation, with sales managers wresting control from production managers and finance managers, in turn, wresting control from sales managers. Roy shows how early financiers used power to win control over large portions of American manufacturing and how they consolidated huge firms in many industries. In chapter 17, Bruce Carruthers takes up a second theme prominent in economic sociology, showing not that power helps to shape core ideas about rational behavior, but that economic decisions are shaped by power and politics. In the early British stock market, sellers of stock preferred to sell to others in their political party to keep important corporations in the hands of their political cronies.

How Coercion Shapes Economic Scripts

Karl Marx was interested in how the world that people encounter shapes not merely their economic behavior but also their ideas. In *The German Ideology*, excerpted in chapter 14, Marx critiqued contemporary philosophy for being based entirely in abstract thought rather than in human experience, and sketched a theory of human history based in the evolution of production and of class relations. In Europe, lords had exploited serfs under feudalism, masters had exploited workmen under guild production, and capitalists now exploited wage laborers under capitalism. Each system portrayed these relations as natural and just, for God chose lords and kings under feudalism, the master craftsman earned his position by the sweat of his brow under guild production, and the factory owner won his position with cunning under capitalism.

For Marx, the modern state imposed laws favoring capitalists on a society in which the vast majority were not capitalists, and it did so under the rhetoric of democracy rather than under that of capitalist domination. In so doing, Marx argued, states made capitalism seem natural and just when it was in

reality neither. Today power theorists rarely portray the nation-state as a tool of capitalists, but they have built on Marx's idea that states impose a particular set of rules, regulations, and institutions shaping economic life—a set of "property rights," in the language of institutional economists. These property rights are not dictated by economic laws, but are worked out by powerful groups. In support of the idea that economic laws do not dictate public policy, comparative studies of capitalism, such as Richard Whitley's "business systems" studies (chap. 6), demonstrate that there are many ways of organizing a capitalist economy efficiently.

Thus while today's power theorists accept the idea that capitalism is more efficient than other economic systems, they argue that power relations produce different forms of capitalism. From institutional theory (Meyer, Boli, and Thomas 1987; Berger and Luckmann 1966; Wuthnow 1987) they draw insights about why we believe that there must be "one best way" to organize economic activity under capitalism. The modern worldview depends on a scientific cosmology in which the world we experience is produced by universal laws governing nature and the economy. Those laws determine the best way to design a bicycle, just as they determine the best way to design a semiconductor market. When we encounter a bicycle, we presume that trial and error have produced the best possible outcome. We think about semiconductor markets in the same way.

For power theorists, people come to take for granted, and to interpret as rational, the economic conventions that surround them. Power shaped those conventions in the first place.

How Management Factions Shape Corporate Strategy

Neil Fligstein's *The Transformation of Corporate Control* brings to bear Marx's insights about power struggles among competing elite factions, found for instance in *The Eighteenth Brumaire of Louis Bonaparte* (1963), in explaining changes in leadership and strategy among America's largest corporations. Fligstein explores power struggles within management groups seeking to gain control of large corporations. His foil is Alfred DuPont Chandler, America's preeminent business historian who in *The Visible Hand* (1977), told the story of the evolution of corporate control from the perspective of business efficiency. Early firms were run by managers with backgrounds in production. Later, sales and marketing managers took over, as the axis of competition among firms shifted from production to marketing. Later still, finance managers took over, as firms shifted focus from sales and marketing to diversification. Chandler treats these changes as part of the natural progression of the modern firm.

Fligstein finds that these changes were the result of a series of power struggles among management factions. Each group succeeded in taking control of the large corporation by convincing investors that their management spe-

cialty held the key to corporate efficacy. The shift from sales to finance management was kicked off in 1950 when Congress passed the Celler-Kefauver Act, making it difficult for firms to acquire others in related businesses. Finance managers responded with a new business model, later reinforced by portfolio theory in financial economics, in which the large firm should not act like a marketing machine in a single sector, but like an investor with a diversified portfolio. Finance managers now argued before corporate boards and investors that the diversified conglomerate was the way of the future and that they, finance managers, were best qualified to manage conglomerates. They thereby came to displace experts in sales at the helms of the biggest corporations.

What now makes this story more compelling than Chandler's argument that the conglomerate prevailed because it was more efficient than the one-trick pony is that the one-trick-pony (the "core-competence" firm) has risen again. Today the smart money is on firms that focus on one or two businesses; investors argue that *they*—not corporations—should diversify their portfolios as they see fit; and it is difficult to find advocates of the portfolio theory of the firm. As Davis and colleagues show in chapter 7 (and see Fligstein and Markowitz 1993), "core competence" arose because institutional investors and securities analysts found it hard to place a value on the conglomerate and used their power (to rate firms and to invest funds) to raise the stock prices of firms that operated in a single industry. Power played a role in the rise of the diversification strategy, and in its demise as well.

How Capitalist Factions Shaped Corporate Strategy

Fligstein's work brings together insights from power theory (a power play for control of large corporations was central), from network theory (a network of finance managers was key), and from institutional theory (new business customs became taken for granted) to explain shifts in corporate conventions—firm structure and strategy—over the course of the twentieth century. William Roy, in *Socializing Capital: The Rise of the Large Industrial Corporation in America* (1997), excerpted in chapter 16, brings together these same three elements to explain a wave of mergers at the beginning of the twentieth century that produced huge industrial enterprises and a business model based on economies of scale.

In explaining the rise of finance managers with their conglomeration strategy, Fligstein finds that antitrust amendments circa 1950 changed the balance of power between different sorts of managers within the firm. In Roy's case, the initial enforcement of antitrust in 1897 had an unanticipated effect on the balance of power between large and small firms. Roy shows that it was not only economies of scale that gave big firms an edge, as Alfred Chandler (1977) contended, because small firms merged into big firms even in industries that could not benefit from economies of scale. Instead, Roy argues, when antitrust prevented firms from joining together to set prices, large firms demanded that smaller competitors sell out or face certain death in price wars. It was not that large firms were more efficient than small firms, it was that they had the power to threaten them after antitrust prevented firms from banding together to set prices.

The irony of early antitrust law was that while it was designed to prevent the concentration of economic power by outlawing collusion, it encouraged mergers. Small firms could no longer set prices together, but they could merge into a bigger firm that could set a single price. The huge concentrated firm, then, was born out of an unanticipated coincidence of public policy and private power. Public policy fostered price competition, and large firms forced their smaller competitors to sell out. Americans soon came to take the huge industrial enterprise for granted, and to presume that large firms are large because they enjoy economies of scale. Drawing on institutional theory, Roy argues that people came to believe that the huge oligopoly emerged for reasons of efficiency rather than for reasons of power.

Fligstein shows how power (among finance experts) shaped the rise of the diversified conglomerate and contributed to our taking it for granted as efficient. Roy does the same for the huge oligopoly at the dawn of the twentieth century, showing that power has an ongoing effect—once a power struggle establishes a new business convention (the oligopoly), we come to believe it must be efficient, and this belief sustains it. In this case, the theory of scale economies was articulated to reinforce the oligopoly. Thereafter, people believed that firms were big because big was efficient, not because medium-sized firms had gobbled up small rivals by threatening price wars—by exercising power.

How Political Alliances Shape Exchange Patterns

Bruce Carruthers's *City of Capital: Politics and Markets in the English Financial Revolution* (1996), excerpted in chapter 17, examines the role of power from a different angle. Rather than looking at how power shapes business conventions, Carruthers looks at how politics shapes trading. A tenet of price theory in economics is that each seller chooses the buyer offering the highest price. Carruthers looks at English stock trading in the early 1700s to show that politics influenced sellers' choices of buyers. Stockholders in politically important companies often chose to sell to other partisans even when it meant that they would not get the best price. There were strong political battle lines in place in the early 1700s, and large companies exercised significant influence over political decision-making. Who controlled the East India Company was of some political consequence. Carruthers finds that stockholders with strong political leanings tended to sell to partisans. Sellers might lose money by refusing to sell to their political rivals, but that is exactly what they did.

Carruthers's study carries forward an important tradition in economic sociology of showing that political motives influence economic behavior (see Zelizer 1988). In Granovetter's terms, Carruthers finds that stock traders are embedded in a wider political context that shapes their behavior—that traders are not isolated machines driven by price alone. If this is true in the pristine realm of stock trading, Carruthers implies, it is surely true throughout economic life.

From the muckraking stories of collusion among early railway barons and oil magnates to journalists' tales of accounting scandals among corporate giants at the dawn of the twenty-first century, most journalistic accounts caution that power must not infiltrate business dealings. For most economic sociologists, power is a regular part of economic life. Modern regulatory institutions and business conventions are shaped in the first place by power relations. This is particularly evident in the United States, where industries are typically regulated by former captains of industry (Useem 1984). The studies included in this part suggest that business conventions and forms we take entirely for granted as originating in the search for efficiency—the oligopolistic manufacturing firm and the diversified conglomerate—were shaped by power struggles.

Cognition and Economic Conventions

Whether they focus on the effects of institutions, networks, or power, economic sociologists share a common set of social psychological assumptions. Durkheim spelled out the core ideas, and they are now shared not only by economic sociologists but by many sociological constructionists, cognitive psychologists, organization behavior theorists, cultural anthropologists, cognitive scientists, and behavioral economists.

These ideas are different from those underlying mid-twentieth-century American economics, which began with the premises of methodological individualism and self-interest. Under methodological individualism, behavior can be traced directly to human nature—to instinct. The instinct of greed trumps other instincts. People are naturally calculating—conniving, even—and systematically so. In premodern societies, the story goes, superstition and myth interfered with the rational pursuit of self-interest, but at heart people were always self-interested. The idea was that you could explain economic conventions with a small set of mathematical formulas that capture how self-interest is played out. Those formulas were written by nature. Social structures evolve to allow people to pursue their self-interest—they do not alter human instincts, they facilitate them. Society, then, is merely the individual mind writ large.

Sociologists have taken the opposite view, that the human mind is society writ small (Douglas 1986). Individual consciousness comes to reflect social

institutions. Social institutions take many different forms, and the differences come about by chance. Tribes worship frogs because the local environment is inundated with frogs. Or they worship at the altar of public transport planning (in France) because in the eighteenth century, their state built royal roads to bring troops to the front. Consciousness comes to reflect institutions that arose by historical happenstance. Because history has produced many different kinds of societies, it has produced many different cognitive structures. For sociologists, while the survival instinct may be innate, much of what people view as innate, self-interested, economic behavior is scripted by convention rather than by biology. Much of it is learned rather than hardwired by our genes.

The degree to which behavior is learned, rather than innate, varies by species. Horses leave the womb ready to walk. Tortoises leave their eggs with all the tools they need to get along. But much human behavior is learned, and the interesting differences across groups are, ipso facto, learned. Socialization theory and cognitive psychology offer starting points for thinking about what underlies these differences, better starting points than mid-twentieth-century microeconomics, which is based in the idea that humans have universal goals (Teutonic luxury cars) and universal scripts for how to achieve them (Stanford MBA followed by McKinsey). After all, in some settings people are socialized to pursue the goal of appeasing the ancestors by the means of sacrificing small animals. Most economic theories now stipulate that goals vary—that your goal may be Zen tranquility rather than the BMW 745—but retain the idea that the means to achieving goals are more or less part of human nature. This may be where economic sociology differs most starkly from neoclassical economics—in the idea that the scripts for achieving goals are social phenomena that become embedded in cognitive schemas. The idea is that scripts are no more given by nature than goals are.

Social institutions create mental maps of the world in individuals. Some call them schemas, others frames (Goffman 1974), others cultural tool-kits (Swidler 1986). Institutions produce broadly similar cognitive frameworks across members of a society. These frameworks encompass categorization schemes, maps of relationships among things, and maps of causal processes.

This view of the human psyche is widely shared among sociologists. Not only Durkheim, but Weber and Marx saw human actions, motives, and understandings as reflecting social structure. Weber (1978, 4) turned this observation into a methodological dictum, arguing that to understand social action, one must understand its meaning to the actor. The social scientist may think that a price reduction has an objective meaning, but she will not understand it unless she understands what it means to the actor (Schutz 1970). While economists' belief in methodological individualism dictates that they must trace behavior to human nature, Weber insists that we must trace behavior to its socially constructed meaning.

The four chapters in the part on cognition trace the evolution of this sociological idea, that cognition is driven by social conventions and their meanings to the group. In chapter 18, Durkheim examines pre-modern religious systems to find that the social classification of things and beings and the social construction of causal processes are fundamental to human nature. In Chapter 19, excerpted from Peter Berger and Thomas Luckmann's *The Social Construction of Reality*, the sociological view of objectivation is spelled out—the cognitive process by which we transform subjective interpretations of the world around us (as driven by the spirit world, or by laws of nature) into hard objective realities. Chapter 20, James March and Herbert Simon's "Cognitive Limits on Rationality," sketches how members of organizations develop rationalized routines for solving problems, and how they come to apply these routines as rationalized rituals to solve problems. Finally, in chapter 21, the psychologist Karl Weick explores cognitive sensemaking within organizations, showing how people explain their own behavior post hoc, to themselves and to others, in socially meaningful terms. We invent meaningful rationales for action after we have acted, simultaneously reinforcing existing rationales and justifying our own behavior.

Origins of the Meaning Underlying Economic Action

Whereas for early economists, the core human trait was self-interest, for Durkheim the core trait was sociality. Economists traced behavior to self-interest, and Durkheim traced it to the group processes of classification and meaning-making. He found these processes in primitive and modern societies alike. Pacific Islanders categorized the world in ways alien to Durkheim, lumping the tribe with the totem, animals with vegetables, and so on. Their categories were based on affinities between things defined by the spirit world. They constructed understandings of causality built on these categories, and based in mystical rather than in rational principles. Yet as in modern societies, the shared constructions of the world they developed structured the psyche.

Durkheim's revelation in *The Elementary Forms of the Religious Life*, excerpted in chapter 18, is that the totem is at once the group's deity and its flag. The totem—be it a frog or a bat—represents the tribe as distinct from other tribes and is also the object of worship. The totem symbolizes the idea that the group is more than the sum of its parts—that there is something transcendental in social life. This insight is the kernel of the social constructionist theory of cognition. For Durkheim, societies trace social conventions to something bigger than society. Tribes that worship their ancestors trace conventions to the spirit world and see what goes on in society as a reflection of the world of the ancestors. Religious societies likewise trace social order and customs to something outside of society—to God.

Durkheim's followers argue that rationalized societies are not so different from religious and mystified societies. Rationalized societies trace social conventions to something outside of society—to laws of nature, economy, and society that are unvarying across time and space. Social constructionists, such as Peter Berger and Thomas Luckmann, who are excerpted in chapter 19, argue that cognitive structures come to reflect social conventions and the universal laws that modern societies define as underlying them. For them, human cognition is a reflection of the surrounding social order. We are rational actors, but only because we live in a universe governed by scientific laws. In a universe directed by frog spirits, our cognitive structures would reflect the frog kingdom. Moreover, rational cognitive orientation comes in as many flavors as mystified cognitive orientation.

The best evidence for this view may come from the historian Albert Hirschman (1977), who has shown that the goals-and-interests framework itself arose relatively recently even in the West, to replace a view of human behavior as driven by a series of innate passions—greed and lust and hunger. Self-interest, it seems, is just one among many lenses through which we can view the modern soul. It is now popular to believe, following historical studies such as Avner Greif's (1993) analysis of early trading patterns, that a modern version of self-interest can be found in antiquity and thus that self-interest is innate and that the inclination to truck and barter is hardwired. It is certainly the case, as Weber (1978) and Richard Swedberg (2002) argue, that elements of modern self-interest can be found in early modern Europe. But Neil Smelser's (1993) review of anthropological evidence suggests that in aboriginal societies, members did not view self-interest as underlying their own behavior and did not create incipient modern markets. That the modern version of self-interest is a product of rationalized societies seems clear. How, then, do specific notions of self-interest arise and evolve?

How Cognition Carries Prescriptions for Economic Behavior

Durkheim did not find much in the way of rational, calculating self-interest among totemic societies, but he did find the same general form of meaning-making that he had seen in modern societies. In both settings, people categorized things to make sense of the world. In both, they traced physical and social patterns to forces outside of society—to a spirit world or to a system of natural laws. For Durkheim, it is human nature to make sense of the world.

In chapter 19, Peter Berger and Thomas Luckmann sketch a social constructionist view of human cognition, a view that has come to shape the other three strands of economic sociology, including the work of Meyer and Rowan in chapter 3, the work of Leifer and White in chapter 11, and the work of William Roy in chapter 16. Their ideas are based in social phenomenology. Berger and Luckmann (1966, 20) say that their task is to grasp "the objectivations of subjective processes (and meanings) by which the *inter*sub-

jective commonsense world is constructed." How is it, in other words, that our subjective "knowledge" of the world comes to have the feel of an objective reality? The fact that our fellows share that subjective knowledge helps to give it the feel of objective fact. Understanding how we come to take for granted the world as it presents itself is key to understanding how economic conventions are stabilized, and how they can change. If everyone around us believes that economic success is a consequence of the local totem's sentiment, of God's will, or of market conditions, we will find that belief compelling and will come to see it as objective knowledge rather than subjective belief. This is how we make sense of the world, as Durkheim contends. We do not see the socially constructed reality around us—the belief in the connection between market conditions and economic success—as a social product. We see it as real. Gravity is what it is, a force of nature (not of the spirit world) as predictable as death and taxes.

Berger and Luckmann find that the inclination to assign objective status to intersubjective reality characterizes human societies. In mystified, religious, and rational settings alike, people know *why* the sun rises and sets just as surely as they know *that* it rises and sets. At the level of cognition, the individual makes causal connections on the basis of the wider system of meaning institutionalized in concrete customs. Americans, for instance, believe that a kind of Darwinian competition among firms creates progress, killing the less efficient and rewarding the more efficient. This is a simple cognitive model that guides behavior. Under Leifer and White's version of network theory, the understanding that you will face stiff competition if you enter a market in a segment with a dominant actor follows from this cognitive model. Leifer and White find that the model leads market entrants to seek niches where there is no competition. Other countries and industries operate with entirely different market customs and cognitive models, many of which are not organized around a Darwinian market. Where the state coordinates business groups, as in Japan, or enforces cartel agreements, as was long the case in Britain and Germany, market customs and cognition take different forms. You might not see it as suicidal to enter a market that already has one very big fish.

Cross-national studies of the human psyche confirm that societies impose very different models of social order on the mind. In psychology, experimental studies have shown that individuals describe the same picture in very different ways, Americans focusing on the subject and Japanese focusing on the context (Nisbett et al. 2001). Hence Americans are more likely to attribute the behavior of others to character, while Japanese are more likely to attribute it to context. Comparative studies of management practices and ideas (e.g. Hofstede 1980) show that across a wide range of countries, orientations to authority, innovation, and cooperation vary systematically. "National character"—sometimes a code word for ethnicity—used to be thought to explain these differences, but scholars increasingly trace them to differences in national institutions (e.g., Whitley and Kristensen 1996). The institution of lifetime employment for managers still prevails in Japan (Dore 2000), and it contrasts starkly with the custom of getting ahead by moving around that prevails in the United States. Such customs shape cognitive orientations and the means people use to pursue goals. How to succeed in business is understood differently in these two settings.

Understanding what the actor has in mind when she acts is important to Berger and Luckmann not only as an intellectual exercise, but because it facilitates prediction. For some forms of behavior, as March and Simon argue in chapter 20, local scripts are highly routinized. But for many, individuals have to draw on the general mental models of action available to them. If you know that the American psyche makes a Darwinian market the driving force of progress, you can reasonably predict that when Americans face a problem of efficiency, they will try to apply the model. And indeed even where economists think market mechanisms will not work—telecommunications, air transport, health care, education—Americans have favored market solutions. Mid-twentieth-century American economics saw such preferences as innate, whereas economic sociologists tend to see them as learned—as nurture, not nature.

How Cognition Shapes Economic Choices

In discussing subjectivity, Berger and Luckmann are implicitly comparing the cognitive frames found in diverse societies or groups. Eving Goffman (1974) popularized the concept of a *frame* as a shared map of reality. Pierre Bourdieu (1977) defines *habitus* as a class-based way of seeing the world. Luc Boltanski and Laurent Thevenot (1991) use the term *justification* to refer to the menu of standard ways of understanding social action. Ann Swidler (1986) uses *cultural tool-kit* to describe the shared cultural components that people use to act on the world and interpret it. The common point is that societies produce broadly different sorts of cognitive orientations—maps of reality. The Ndembu and Kansas tribes have different understandings of how to achieve a good harvest. In economic sociology, studies of cognition have generally taken place at the organizational level rather than at the national level, though in cultural anthropology and, increasingly, cultural psychology the same processes are studied cross-nationally.

James March and Herbert Simon's "Cognitive Limits on Rationality" (1958) stipulates a modern, rational society and explores the role of cognition in organizational decision-making. March, a sociologist, and Simon, a cognitive psychologist and recipient of the 1978 Nobel Prize in economics, sketch two ideas that have been widely used in economic sociology. The first idea concerns the limits of human cognitive capacity in rational decision-making. Managers are seldom able to identify the optimal means to a particular end because of the difficulty of assessing the costs and benefits of each imaginable

strategy. They typically settle on solutions that meet minimal criteria for achieving a goal rather than searching for the ideal solution, "satisficing" rather than optimizing. George Stigler, in a famous essay titled "Economics and Information" from 1961, argued that people search for ways to achieve a goal with perfect efficiency—that they continue to search until precisely the point at which the marginal cost of searching exceeds the marginal benefit to be gained. March and Simon anticipate this argument, showing that decision makers lack the information to judge when further searching is worth the effort. Instead, they argue, people begin the search process with familiar solutions in mind. When faced with a problem, people typically think of an analogous problem from the past and apply the solution used in that case—"What did we do the last time there was a budget shortfall?" They go beyond off-the-shelf remedies only when no such remedy is available.

This brings us to the second idea, which concerns the menu of solutions that organizations offer. Organizations develop all sorts of problem-solving routines, ranging from very precise routines for dealing with common and predictable functions (filling an order) to very general routines for dealing with rare and unpredictable functions (writing a computer program). The routines exist as organizational culture at the level of the firm and as cognitive problem-solving scenarios in the minds of individuals. In chapter 20 March and Simon argue that customs and cognitive frameworks are really two sides of the same coin, for cognitive frameworks reflect the customs individuals encounter in their work organizations. Whereas institutionalists focus on the character of broad institutional systems—religious or scientific, Hindu or Protestant—and on the factors that lead those systems to change, cognitive theorists focus on the individual-level cosmologies or cognitive frameworks that those institutions generate. Institutions and conventions vary across nations, but March and Simon point to important variations even across work organizations in the same nation and industry, shaping workers' cognitive frameworks and hence their knee-jerk reactions to problems that arise.

For March and Simon, people in modern work organizations act rationally, in that they pursue rationalized solutions to problems. You will not encounter many rain dances at IBM. But the nature of human cognition is such that people do not devise optimal solutions for the problems they face. They mostly choose from among the organization's ritual, albeit rationalized, solutions. These rituals have shaped their cognitive structures, offering ready means to particular ends.

How Action Reinforces Cognitive Frames

In exploring the relationship between social structure and individual cognition, Durkheim's followers argue that most human customs are framed as driven by forces outside of society. The human inclination to categorize and

generalize leads people to see the wider universe as the source of social and economic customs. Berger and Luckmann argue that different groups have different meaning systems, and that to understand and predict a social behavior, we must grasp its subjective meaning to the actor. Often this meaning is mundane, for most of what people do is mundane. But how people understand their own actions matters. It matters whether one knocks on a table to bring a meeting to order or to ward off the bad luck brought on by uttering a desire aloud. It matters for predicting behavior.

March and Simon describe how organizational customs persevere as problem-solving routines. Organizations attach them to legitimate cultural frameworks, so that a routine for decision making may be understood in terms of "democracy" or of "expertise," but not in terms of prowess with a six-shooter or of epiphany.

Karl Weick's *Sensemaking in Organizations* (1995) examines how frames for understanding the world are activated and manipulated by individuals. Weick does not see the meaning of an action as tightly wedded to the action itself, but instead sees individuals as operating with a range of interpretive frames. People make sense of much of their behavior retrospectively, using these interpretive frames. To illustrate, Weick cites Garfinkel's study of jury decisions, which shows that jury members tend to select a punishment first, and then make sense of the evidence so that the crime fits the punishment. For Weick, organizational behavior tends to follow the same pattern. People act, and then construct rationales for their behavior using common cognitive/rhetorical elements.

What may be most innovative about the sensemaking perspective is the idea that action shapes cognition—that we make cognitive sense of even our own actions after they have occurred. Decision making is often spontaneous, but we interpret it with customary points of view. This challenges Duesenberry's quip that sociology is the study of why people don't have any choices to make. Weick suggests that people not only choose how to behave, they choose from a range of interpretations of their own actions. It is not that their actions must make sense, but that their accounts of their actions must make sense given the wider system they operate in. When you raise prices for the disk drives you sell to a computer manufacturer, you can say, and think, that your labor costs have risen or that your components are in short supply. You cannot say, or think, that the Lord came to you in a dream and told you to buy your husband a new car.

This brings us full circle, to the issue of how customs and their meanings are articulated. Durkheim suggested that what is constant in the human condition is the inclination to try to make sense of the world by categorizing and generalizing from experience. For Weick and the other students of cognition, basic cognitive frameworks are shaped by experience with social customs. Each individual does not have to interpret customs on her own; rather, each

custom comes equipped with cultural meaning, whether it is the custom of sacrificing a goat at harvest time or the custom of enforcing antitrust law.

The Four Mechanisms in Action: The Creation of the Amicable Merger

Before concluding, I offer a final illustration of how the four sociological mechanisms operate together to shape economic conventions (Dobbin and Dowd 1997, 2000). For economic sociologists, people typically enact economic conventions with little forethought. When conventions are challenged by public policy shifts or by private action, groups often vie to determine which alternative conventions will come to be defined as rational. Who wins depends on both power and networks, but the winning strategy must be accompanied by a cultural and cognitive framing that lines up with existing conceptions of efficiency.

The decline of the cartel and the rise of the amicable merger in railroading is a case in point. Between 1880 and 1910, business conventions in the American railroad industry were revolutionized, as firms went from participating in cartels to merging into regional monopolies. In Britain and elsewhere, cartels survived. What caused the change in the United States?

First, the cartel represented one *institutionalized* economic convention with a clear-cut cultural and cognitive rationale of efficiency. In response to early rate wars, railroaders created cartels and argued that in modern nations with large firms, only cartels could prevent price wars that could destabilize entire sectors.

Second, a *network* of ranchers, farmers, and small shippers formed to fight the cartel, arguing that cartels checked the freedom of small shippers. The breadth of this network gave it the *power* to pass anticartel legislation. It also succeeded because it built on an American way of thinking, found in the Constitution and reflected in popular cognitive orientations, in which concentrated power (whether in the federal government or in private industry) was undemocratic.

Third, when antitrust outlawed cartels, railroads divided into two camps. Financiers argued that firms should respond with amicable mergers, to preserve the value of the many railroads whose stock financiers held. Dedicated railroaders, who owned individual railroads, argued that firms should fight it out in price wars, with the strongest railroad taking the spoils in each region. Financers convinced dedicated railroaders to embrace amicable mergers by dint of their *power*. J. P. Morgan announced that financiers would withhold capital from predatory railroads.

The result was the institutionalization of a new business convention, the amicable merger. The convention was supported by the new theory, and *cognitive framework*, of the natural monopoly, in which price wars were destructive and pointless (consolidation was inevitable) and friendly mergers were the efficient remedy.

Thus in short order, a new equilibrium of business conventions was established. Firms did not coordinate prices in cartels, but when competition threatened to break out, they put their heads together to arrange mergers. Everything about how rational managers should behave vis-à-vis their competitors had changed. A new economic convention had been institutionalized. Was it more efficient than the cartel? Unlikely, as both had the goal of precluding competition. But it came to be seen as more efficient, and the cartel was shortly defined as an irrational relic of history.

This pattern can be seen in the empirical studies by Davis and colleagues (chap. 7), by Fligstein (chap. 15), and by Roy (chap. 16). In each case, a set of business *institutions* is challenged by an emergent *network*, different groups use *power* to try to define the new institutions that will replace the old, and the group that wins links new institutions to a compelling *cognitive* model of efficiency. What results looks to the world like the work of natural economic laws that replace inefficient business conventions with more efficient ones.

Conclusion

If you think about how a Dallas semiconductor manufacturer sets today's price, as economists do, you put yourself in her place and imagine how she perceives supply and demand. What kind of increase in demand would cause her to raise the price, given fixed supply? But if you think about how semiconductor manufacturers set prices in both Dallas and Osaka, as economic sociologists do implicitly or explicitly, you consider how context shapes their decisions. Conventions and institutions explain much of the difference in pricing decisions. You cannot help but ask, for instance, whether without the Department of Defense's early nurturing of chip manufacturers, the Dallas semiconductor seller would even exist. You cannot help but wonder whether, without antitrust law in place, she would think of competition among producers as the main factor influencing pricing. In Japan, you cannot help but ask whether without MITI's tutelage of high-tech industries, the Osaka seller would exist. You cannot help but wonder whether without state support for long-term contracting, the seller would think of a decades-old collaboration with one buyer as the main factor influencing pricing. How the Dallas and Osaka sellers decide on price is shaped by context.

Economic sociology's terrain is the effect of the social on economic behavior. People may make choices that they view as rational, but they do so with the battery of customs and prescriptions that society offers. In Karl Marx's (1963, 15) famous words, "Men make their own history, but they do not make it just as they please: they do not make it under circumstances chosen by themselves, but under circumstances directly encountered, given

and transmitted from the past." The past has presented the Dallas and Osaka chip manufacturers with *different* rational conventions for setting prices. In Dallas it is rational to adjust price to demand; in Osaka it is rational to sustain a beneficial relationship with the buyer. Context also changes over time, and so a given American seller may use entirely different decision rules in 1980 and in 2000.

At the dawn of the twentieth century, the fields of economics and sociology were not far apart. Economists John R. Commons and Thorstein Veblen were preoccupied with explaining how social context determines economic behavior. So were sociologists Émile Durkheim and Max Weber. But by halfway through the century, the two camps had moved apart. Economists interested in how institutions shape real-world behavior had become a rarity, as had sociologists interested in economic behavior per se. Economists developed a theory of perfectly rational, socially isolated individuals. They experienced a sort of collective amnesia about the origins of this endeavor, forgetting that neoclassical theory had been a kind of thought experiment that assumed a single human instinct (self-interest) and imagined a world built up from that one instinct. The field consequently elaborated what Mark Granovetter (chap. 7) calls an "undersocialized" view of human behavior, in which social customs and collective understandings are all but irrelevant in explaining everyday economic decisions. Only stylized economic facts mattered.

Sociologists had been trying to understand how context shapes behavior all along, and from about 1980 they returned to the study of the economy with an array of implements refined in their studies of migration decisions, political choices, career strategies—all manner of social behavior. Forged by the founders of the field, who studied the rise of new economic patterns in the nineteenth century, these tools were refined on the premise that social and economic behavior alike originate not in the individual, but in society.

Sociologists see people as creatures of habit, driven by customs and routines that arise by chance, or by force. Modernity thus does not signal a fundamental shift in the character of the individual. It is not that people followed shamanism, voodoo, and animal magnetism for a hundred thousand years and then suddenly with the Enlightenment became calculating, rational actors. It is that at some point society began to organize customs around rationality rather than around spirituality, and people dropped customs backed by spiritual and mystical significance for customs backed by rationalized significance.

Sociologists thus consider the range of social forces that shape economic customs. This has led to a proliferation of insights under four theoretical tents. Some have built on the insights of Max Weber with an institutional approach that emphasizes the importance of meaningful social conventions. Others have built on the insights of Émile Durkheim and Georg Simmel with an approach linking economic behavior to social networks. Others have

stood on Karl Marx's shoulders to explore how power shapes the emergence of new economic conventions. Still others have built on Durkheim's ideas about our inclination to categorize and make sense of the world and Weber's insights about customs and their meanings to examine how economic conventions become reflected, and made meaningful, in the human mind.

Economic sociologists have found that these four forces operate together to produce and sustain behavioral customs and market structures. Thus economic sociology, like the field of sociology more broadly, is undergoing an unusual sort of paradigm shift. When Thomas Kuhn (1970) observed paradigm shifts in the physical sciences, he saw the gradual replacement of one broad explanatory framework by another. Sociology has historically entertained several competing paradigms at once, and in recent years those paradigms have cross-fertilized to produce a rich theory of social action. In sociological studies of economic life, we increasingly see network ideas conjoined with Marxist ideas about power. We increasingly see ideas about cognition merged with Weberian ideas about institutional structure. Sociology's inductive, empirical method has produced studies that find these four core mechanisms shaping social behavior in all sorts of settings. The field is increasingly coming to see them as part of a single sociological explanation of behavior.

If sociologists have often settled for proving the effects of one element of the fourfold paradigm at once, holding the other elements constant, they have done so for good reason. It is difficult to create a reliable natural experiment in which all four elements are in motion at once, just as it is difficult to observe the effects of gravity, temperature, and wind resistance at once. The evolution of economic conventions is a multifold process, and as in physics, it remains difficult to disentangle the elements except by observing one at a time.

Recent studies sketch how these factors work together. Neil Fligstein's *The Architecture of Markets* (2001), Harrison White's (2002) *Markets from Networks*, and William Roy's *Socializing Capital* (1997) develop synthetic theories of economic life and many of the chapters in this anthology draw on two, three, or even four of these mechanisms. This sociological model of the evolution of economic conventions follows the logic of the model of evolution that biologists now embrace (Gould 1989) in describing evolutionary changes as fairly haphazard rather than as, of necessity, improving on the status quo. As long as random evolutionary changes do not doom a species, they may be sustained in the species. The same goes for the evolution of economic customs. New customs can be sustained so long as they do not lead to economic collapse. For the most part, it is impossible to discern whether a new convention hurts or helps in the aggregate. There are enough successful innovations in technology and management to mask the effects of the innovations that do more harm than good.

That economic conventions are socially produced does not mean that they are entirely random. Economic conventions are subject to natural selection as Darwin described it, to be sure (Aldrich 1999). Grossly inefficient customs

die out, and some take their practitioners with them. Sociologists' comparative studies of capitalism, however, suggest that for any given economic goal, a number of different means may be about equally efficient. If one accepts the premise that there is more than one way to skin most cats, then the whole world of economic conventions is opened to sociological analysis. If inefficiency did not doom the cartel or the conglomerate, it stands to reason that we need to explain what did. This is where sociology's convention-based approach to economic behavior comes in.

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