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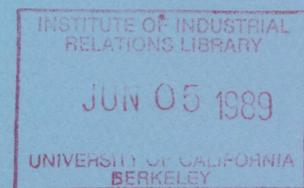
WHAT CAN ECONOMICS LEARN FROM  
INDUSTRIAL RELATIONS?

by

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This is the first draft of a paper to be given at a symposium on "The Economic Approach to Human Resource Management and Industrial Relations" to be held at the 1988 meetings of the Industrial Relations Research Association.

Possessing a powerful model of human behavior, economics over the years has persistently expanded the range of phenomena that it seeks to explain. Among the recent additions to its intellectual empire is the new "economics of human resource management" (E/HRM), which applies various economic concepts --human capital, agency theory, transactions costs--to the analysis of employment relations in organizations. E/HRM is to be welcomed as a harbinger of a more practical and factual orientation in labor economics. But as the gadfly in this gathering, I will argue that E/HRM also has various faults that could be remedied by drawing methodological insights from fields E/HRM is seeking to supplement or replace, particularly industrial relations.

The bulk of this paper outlines the disciplinary origins of industrial relations, whose roots lie in the 19th century clash between the classical and the German historical approaches to economics. Out of that dispute came various attempts at theoretical synthesis, including Weberian sociology, Marshallian economics, and American institutionalism. Along with pressing social problems of the day, these formed the intellectual matrix from which industrial relations developed. Although rarely given in any detail, industrial relations had at its core a set of methodological precepts: institutional holism, factual and behavioral realism, historical specificity, and comparative analysis. Lest the reader not be inclined toward methodology, let me hasten to say that the paper not only explains these terms in detail but in its final section gives concrete demonstrations of how they can be applied to improve the quality of work presently being done in E/HRM and in labor economics more generally.

#### THE METHODENSTREIT

The Enlightenment was that great movement of the 18th century which viewed reason and natural law as the organizing principles of the universe. The task of science was to uncover the eternal and self-evident truths that underlay the ever-changing phenomenal reality of human beings and their world. A utilitarian

offshoot of the Enlightenment was classical economics, which deduced economic laws from the postulates of a universal homo economicus. In 19th century Germany, however, economics followed a different trajectory. The Historical School stressed that economics could never be reduced to a set of universal laws because each nation's economy was inextricably part of a larger social totality composed of historically and culturally unique values and institutions. To the Germans, classical economics was nothing more than a rationalization of English capitalism's trade policy and individualistic ethos ("Smithianismus") and, as such, had little to offer them. Instead, they extolled historical and comparative research to uncover the distinctive properties of national economic systems, although there was little agreement on whether this would lead to the discovery of universal laws governing systemic evolution. (Cassirer 1951) {1}

One of the intellectual strands that made up the historical school was the Romantic movement, which began in Germany in the late 18th century in reaction to the Enlightenment. Romanticism emphasized diversity over uniformity and stressed the idiosyncracies, rather than the similarities, of individuals, cultures, and nations. In scholarship as well as art, the movement spurred the "quest for local color, revulsion against simplicity, distrust of universal formulas, and antipathy to standardization." (Lovejoy 1942:293) Another strand came from Kant, among whose contributions to the historical school was his radical dualism: Human beings are both physical (real) and spiritual (ideal) beings, and to study them requires distinct methods--the natural science of biology as well as the science of culture and values. This led to skepticism that social science could develop deductive general laws on the model of physics and to enthusiasm for detailed empirical study of human history in all its concreteness. Both contributed to the historical school's tendency to favor facts and "feel" over theory. Kant also was the source of Hegel's idealistic belief that facts could be arranged into larger wholes pervaded by a single

essence or moral spirit that could be grasped through intuition or the "higher criticism." Although the German economists eschewed theoretical speculation of the grand Hegelian sort, they were enamored of the idea that economic institutions operated according to their own historical and cultural logic. {2}

Finally, and at a more mundane level, economics in Germany had long been imbued with practical concerns as a result of its close association with the state. The cameralist economists of the 17th and 18th centuries were employed as princely economic advisors and also taught applied principles of administration, finance, and policy. As Germany began to industrialize in the 19th century, their successors--the historical economists --continued the tradition of public service and concern with governmental policy. The historical economists were statisticians and ardent nationalists, intent on devising government programs that would hasten Germany's industrialization with a minimum of social friction. Hence they rejected free trade and laissez-faire as inappropriate to the needs of their late-developing nation. Instead they favored protectionism, both in trade and in social policy, a stance that led Bismarckian Germany to adopt some of the world's first social insurance programs. Although their critics called them "socialists of the chair" for their advocacy of moderate reform (including support for trade unionism), the historical economists--operating individually and through their Verein für Sozialpolitik--nevertheless exerted considerable influence on the policies of the conservative Prussian government.

Thus, the practical orientation of the German economists meshed with the other elements that composed their approach. Designing a national system that would promote industrialization required detailed factual knowledge of Germany's economic institutions as well as those of its competitors. To judge whether a foreign practice could be unbundled from its native socioeconomic nexus one had to be familiar not only with economics but with other disciplines ranging from law to politics to history. Moreover, the German economists made a virtue out of

political necessity by rejecting the trade prescriptions and anti-statist individualism of classical economics. But in so doing they threw out the baby--analytic theory--along with its normative bathwater. Some might see this as a simple (and simple-minded) favoring of fact over theory. But it was instead consistent with the historical school's idealistic version of empiricism, in which factual data were gathered in an attempt "to absorb causal relationships into meaningful systems" that varied across time and space. This contrasted to the approach of the classical economists, who "looked upon particular cases as instances of a general law" and tried "to reduce ostensibly meaningful systems to a causal basis" through the empirical reification of those laws. (Parsons 1949:485) More than a practical preference for induction over the deductive method of classical economics, the German approach was based on a different conception of human action and social reality. (Sheehan 1966)

Given these differences, conflict was inevitable. It erupted during the famous methodenstreit (debate over method) that occurred in the 1880s between Gustav Schmoller, then dean of the historical school, and Carl Menger, the famed Viennese economist whose marginal utility theory helped launch the neoclassical movement. {3} Menger is widely regarded as having been the victor in the debate due to Schmoller's unwillingness to concede a role for analytic theory. Yet Menger failed to deflect key criticisms of Schmoller, thus leaving unresolved several points in dispute. What were the issues?

One was whether economics (and other social sciences) required a methodology different from that used in the natural sciences. Following J.S. Mill, Menger argued that all science -- economics included -- had as its aim the discovery of laws from which the solution to any disciplinary problem could be deduced. Not being different in principle from the natural sciences, the social sciences had no need of a special methodology. Schmoller took the Kantian position that the social sciences were unique because they dealt with objects who possessed

consciousness and free will; these gave socioeconomic phenomena distinctive properties. In particular, said Schmoller, these phenomena were infused with spiritual, moral, and cultural values that varied across time and place. Hence specific economic behavior could not be predicted from a universal, ahistorical model of economic man.

That led to the second disputed issue: whether the assumptions of homo economicus should be made more realistic and inclusive. Schmoller argued that economics had to broaden its scope in two directions: first, to include the latest findings from other social science disciplines like psychology and anthropology, and second, to incorporate the study of values and of custom as these bore on economic life. Schmoller was pushing here not only for interdisciplinary realism but for a kind of holism in which individual economic choice was determined by social institutions whose logic or "spirit" had to be incorporated into economic analysis. In other words, individual behavior was embedded in a larger totality whose features could not be abstracted from without producing a distorted image of reality. {4} In reply, Menger asserted that economic theory had no need for either realism or psychologism. It dealt with only one "side" of human behavior -- economic need satisfaction-- and to isolate this behavior it had to abstract from all other considerations. As for holism, Menger insisted that only individuals had goals and values; that changes in individuals caused changes in society, not the converse; and that the study of custom and values was something that lay outside the scope of economic theory (in modern parlance, preferences are exogenous). {5}

Thirdly, Schmoller criticized the deductive method used by the classical economists (and by Menger) because it started from incomplete premises and so was applicable only to particular aspects of social reality. Claiming that he was not opposed to deduction per se, but only to deduction based upon "superficial and insufficient principles," Schmoller called for "more exact

observation" of facts, statistics, and institutions so as to build more accurate economic theories. {6} Here Menger hit back hard, claiming that Schmoller did not understand the purpose of abstract theory. At best, said Menger, Schmoller's inductive approach would lead to "realistic" theories based on the structure of actual economic institutions as they were affected by various disturbing influences. But these were the very factors that deductively-derived analysis abstracted from to produce what Menger called "exact" theory. (in Gide & Rist 1948:401; in Burger 1987:147)

Finally, the methodenstreit examined the relationship between history and economics. Schmoller argued that each nation's socioeconomic system was a historically unique configuration of institutions whose structure and essence changed over time. That was the diachronic perspective: economics had to be concerned with how systems developed their features as well as the conditions that caused those features to change. Any theory that held historical and comparative factors constant, said Schmoller, would see only the recurrent --rather than the unique and dynamic -- features of economic life, and could be no guide to the future. {7} Again, said Menger, Schmoller misunderstood the method of economic abstraction, the difference between realistic and exact theories. "History, to be sure, has the task of making us understand all sides of certain phenomena, but exact theories have the task of making us understand only certain sides of all phenomena." (in Burger 1987:146) That is, history was the study of concrete reality, whereas economic theory took a synchronic approach that abstracted from reality so as to isolate its timeless and universal aspects.

#### SYNTHESES

Both disputants had valid points: on the one hand, that classical theory lacked historical realism and a sense of the dynamic and organic character of economic systems, and on the other, that analytic deduction was a more reliable

tool for organizing and predicting facts than the realistic intuition of inductive idealism. But although the streit ended without reconciliation, economists over the next forty years made various attempts to bridge the theoretical gap, not only in Germany (Weber, Sombart, and Schumpeter) but also in England (Marshall) and the United States (the institutionalists).

Germany: The most sophisticated synthesis came from Max Weber, who, while deeply sympathetic to Schmoller's ideas, nevertheless was one of his most effective critics. Weber had studied economics under Karl Knies, a leader of the historical school, and he later held Knies's chair in political economy at Freiburg. But Weber emerged from a long depression at the turn of the century by writing a detailed critique of his old teacher, who, he thought, had made a fundamental mistake in rejecting analytic theory. In a 1908 letter to Schmoller on the occasion of the latter's seventieth birthday, Weber made the same point: "The scientific needs of the different generations in the sphere of our discipline oscillate between theoretical and historical knowledge--as you have often enough acknowledged... [but] it is now perhaps high time to concentrate on the theoretical aspect." In private correspondence written that same year, Weber was less diplomatic, noting that Menger "vastly overrates himself, but he has very substantial merits and he was right on important points of the matter at issue, even in the dispute with Schmoller." (in Schon 1987:59, 62) Yet while Weber had great respect for Menger and for neoclassical theory, he had his own ideas about the latter's epistemological status. {8}

Weber (1975b) held the neo-Kantian position that, although economics superficially resembled the natural sciences, its theory was constructed along completely different lines. Because economics dealt with "cultural beings endowed with the capacity and will to take a deliberate attitude towards the world and lend it significance", it could not avoid issues of value and meaning --of interpretation--that never arose in the natural sciences. (in Schluchter

1988:25). Moreover, rather than transcending history, economic theory took existing elements of historical reality and enhanced them into what Weber called an "ideal type", a "limiting concept with which the real situation or action is compared." Hence economics presented "an ideal image of events ... under conditions of a society organized on the principles of an exchange economy, free competition, and rigorously rational conduct." Rather than being a universal law, Weber saw homo economicus as a prime example of the ideal type: an enhancement of characteristics displayed by modern Western (nontraditional and rationalistic) societies. As such, the model demonstrated "what course human action of a certain kind would take if it were strictly purposive -- rationally oriented, undisturbed by error or emotions, and if, furthermore, it were unambiguously oriented toward one single, especially an economic, purpose." (in Cahnman, 1964:116; Weber 1949:44,90; Loewith 1970)

Although Weber dubbed Menger's conflation of natural and social science a "naturalistic prejudice," he defended the use of ideal-typical abstraction in classical economic theory. Only by abstracting from the psychological and historical details of reality could economists produce predictive theories, said Weber. Like Menger, he thought that Schmoller misunderstood the distinction between exact and realistic theory: "Concepts are analytical instruments for the intellectual mastery of empirical data... [they] are not ends but are means to the end of understanding phenomena." (in Schon 1987:61-3) Schmoller's induction could at best, said Weber, only lead to realistic theories--those that classify empirical patterns and data sequences--never to exact or predictive ones. {9}

On the other hand, Weber (1949:91-4) criticized the tendency of economic theorists to forget (or not realize) that their constructs were ideal types deduced from historical reality. Homo economicus was a product of specific values and institutions (e.g., the Protestant ethic) present only in modern societies and constrained by other values and institutions within those

societies. Indeed, the heart of Weber's work was his analysis of the factors that fostered rationalization and disenchantment in modern life. It was precisely because Weber saw these as the dominant trend in industrial society that he claimed that "the approximation of reality to the theoretical propositions of economics [is] a constantly increasing one." (in Schon 1987:61) Hence Weber believed that economic theory could serve not only analytic purposes but also historical understanding. But he did not intend to turn Schmoller on his head and make economic theory a substitute for economic history. To Weber, they were complements, not substitutes, the one "using empirical data illustratively" and the other "utilizing theoretical concepts as ideal limiting cases." (in Schluchter 1988:23) Unlike crude induction, theoretically-informed historical and comparative research could show not only when institutions were unique, but also when they were not. {10}

Finally, Weber's focus on values suggested a way of resolving another disputed issue. Weber firmly believed that social and economic action was carried out by individuals and did not occur through holistic determinism as propounded by the historical school. At the same time, he thought that social values and institutions had real consequences because they had meaning in the minds (today, choice sets) of individuals. Collective entities like families, firms, governments, and unions were defined by Weber (1947:107-119) as "probabilities" that inclined individual behavior in a particular direction. According to his biographer, Weber "asserted the importance of ideas and of the individual against the collectivism of the Marxists and the social evolutionists [including the historical school], but he also emphasized the social foundations of individual action much as Marxism had done." (Bendix 1962:68) Weber's synthesis of structure (society) and individual choice (economy) implied that social institutions and values were conceptual material not only for sociologists and historians but for economic theorists as well. {11}

Britain: Events unfolded differently in Britain, where the German influence was relatively weak in the late 19th and early 20th centuries. Because historical economics was, to some extent, a rationalization for trade and social protectionism, British economists had less interest in it than those in other nations. As the world's entrepot and most advanced industrial power, Britain's prosperity was tied to free trade. Moreover, the nation's trade unions were relatively well-established as was the practice of labor market regulation and social reform.

Equally important was the fact that British economics from the 1880s through the 1920s was dominated by the figure of Alfred Marshall, who was more sensitive to the ideas and approach of the historical school than were his neoclassical contemporaries. Like Weber, Marshall sought to reconcile opposing views, although the two men started from opposite places: the one as a self-styled "disciple of the historical school" and the other as heir to the English analytic tradition of Smith, Ricardo, and Mill. However, Marshall's reconciliation did not produce an original synthesis but instead a kind of "schizoid" eclecticism, in which the ideas of the indigenous English and German historical schools were tacked on to the body of mainstream theory (Blaug 1968:426; Coats 1954). Marshall's evaluation of the German contribution was glowing, almost effusive, but he buried much of it in footnotes and appendices, where it posed less of a problem for theoretical consistency. {12}

Thorstein Veblen criticized Marshall's work for its "preconception of normality"--its underlying vision of a static system of normal exchange equilibrium (1919:177). Indeed, this was the dominant motif in Marshall, who was, after all, the man who brought marginalism and equilibrium analysis to the English-speaking world. Yet at the same time Marshall insisted (sounding a lot like Veblen) that the underlying model for economics was "biological", not mechanical, and that the discipline's main concerns were "dynamical," not

statical. Although a description of economic structure could ignore dynamic factors, said Marshall, an explanation "must deal with the forces that brought that structure into existence" (1961 II:48). This was a far cry from comparative statics. But despite his acknowledgment that the economy was changing over time (and despite his own vast knowledge of ancient and modern economic history), Marshall had no historical theory to offer other than a gradualism (natura non facit saltum) that implicitly ruled out the relevance of a dynamical approach. True, an historical element can be found in Marshall's theory of wants: a rising standard of living creates higher-order wants that build character and values which, in turn, permit future improvements in the standard of living (I:83-91). And Marshall credited the German economists for emphasizing the breadth of human character with which economics is concerned, including the moral and social aspects of economic life (I:768, 783). But these are recondite ideas in Marshall's work. He did not explore their methodological implications, no doubt because he saw that if wants and values are made endogenous, then utilitarianism is endangered along with the whole structure of economic abstraction. {13}

Not only was Marshall ambivalent about methodology, he also sent out mixed messages on policy issues. Though hardly a doctrinaire advocate of laissez-faire, he nevertheless stressed the limits and dangers of state intervention and, as compared to the German economists, gave little attention to public policy. He admitted the importance of nonmarket factors but thought that they were overshadowed by competitive forces. Organized labor, for example, received scant treatment in his work. Although Marshall was not unsympathetic to trade unionism, he rarely offered opinions in print. In private letters he said that he considered unions to have been "the greatest of England's glories," but he disliked their "class selfishness" with its inhibiting effect on economic progress. In 1897, five years after Andrew Carnegie had ousted unions from his

Homestead plant, Marshall wrote, "If I were a working man I would wish for no better or more hopeful conditions of life than those which prevail at the Carnegie works now..." (in Pigou 1925:396-9).

In brief, Marshall acknowledged the criticisms of the historical economists but did so in a way that left the core of his own work untouched. In so doing, he cut short the development of a British historical school; critique was absorbed, defused, and forgotten. Although he respected facts and common sense and was skeptical of "long chains of reasoning," Marshall did not attempt the theoretical synthesis that Weber aimed for, nor did his work contain the practical detail or reforming zeal of the American institutionalists. (I:773)

United States: The institutionalists derived a good deal of their vigor and cohesiveness from the sense of being part of a renegade movement outside the mainstream of economics in the United States. No one in the American mainstream (with the possible exception of J.B. Clark) was as eminent and at the same time open-minded as Alfred Marshall. Although lines were not yet firmly drawn when the first wave of institutionalists--including Richard T. Ely, Edwin R.A. Seligman, and Henry Carter Adams--appeared in the 1870s and 1880s, acrimony roiled the profession when the second wave--Thorstein Veblen, Wesley C. Mitchell, and John R. Commons--crested during the three decades after 1900.

Another element unifying the institutionalists were ideas taken from the German historical school. A large number of American social scientists in the late nineteenth century did graduate work in Germany, where they were impressed by the intellectual and practical achievements of the historical school. Of 116 American economists and sociologists surveyed by Henry W. Farnam in 1906, 59 had studied in Germany and 20 had received their doctoral degrees there. More than 80 of Farnam's respondents specified the most important influence on their thinking, and of these 30 mentioned the historical school, 23 the historical and scientific method, and 8 the theory of state intervention, which was of

considerable importance in bolstering young American economists' rejection of the laissez-faire strand in economic theory. (Herbst 1965:131)

Like Germany, the United States was an industrializing nation beset with numerous urgent problems to which, it was felt, economic theory did not offer satisfactory solutions. The institutionalists sought to reshape economic theory into a tool for solving those problems--not only the "labor question" and unemployment, although those were central, but also industrial regulation, municipal ownership, public administration, and trade protection. Germany was proof to them that state intervention need not hinder economic efficiency. They were also impressed by how their German counterparts combined scholarly and practical interests; the Verein fur Sozialpolitik served as a model for the American Economic Association, which Ely and other institutionalists founded in 1885. This was two years before passage of the Interstate Commerce Act--on the eve of a new era of governmental regulation in the U.S.--and the founders angered their more conservative colleagues by including a phrase in the AEA's opening statement that read, "We regard the state as an agency whose positive assistance is one of the indispensable conditions of human progress." (Ely 1886:35) Conservative economists viewed this as socialistic; even mainstream moderates like Frank W. Taussig (1886:37) complained that "if the economists of the old school belittle the importance of the state, those of the new school are in danger of succumbing to a temptation to exaggerate it." One might note that it was not by coincidence that the German-born citizens of Wisconsin supported efforts by Ely and Commons to make the state and its university a laboratory for testing Prussian programs and ideas.

The German influence extended to more theoretical realms. Despite considerable differences among them, the leading institutionalists each expressed strong doubts about the scientific status of economics. Commons, who praised Weber's neo-Kantian ideas, maintained that economics could not be built

on the same foundation as the physical sciences because of man's "volitional psychology," which gave purpose and meaning to human activity. Social science, he said, had to acknowledge the "concerted but conflicting action of human wills in an historical evolution of determining what is workable," else it would produce "a concept of society as the natural growth of a mechanistic equilibrium." A volitional economic theory, Commons asserted, started with preferences--"the purpose for which the artificial mechanism in question was designed"--and then went on to see whether those purposes were obstructed in reality and, if so, how they adapted and made the economy into "a moving, changing, process." (1934:719,733; 1924:376). Like the Germans, then, Commons thought that economic theory was shaped by historical contingency. {14}

This was Veblen's jumping off point for his pungent evolutionary critique of economics; in a nutshell, that it was a "taxonomic science" which ignored economic evolution and lacked a causal theory of institutional change (1919: 67, 232). Wesley Mitchell--Veblen's student--thought that economic theory was tied to a transient set of institutions as well as to an ideal-typical view of human nature, one that was "not so much an account of how men do behave as an account of how they would behave if they followed out in practice the logic of the money economy". But Mitchell was uncertain whether economics could ever construct its scientific method along the lines proposed by Weber. In an address to the American Statistical Association at the end of World War I, he thought it likely that human behavior was dominated by irrational and illogical factors, leaving economics "more like metaphysics than like mechanics, more like theology than chemistry." (1937: 51, 371)

Writing in 1926, when American institutionalism was near the end of its second phase, the movement appeared to Schumpeter (then still in Bonn) to be caught up in a replay of the methodenstreit that had taken place in Europe forty years earlier. "Change the relative emphasis put upon statistical and historical

materials in this picture, and we have, even to details, the position that Schmoller held throughout his life." (in Mitchell 1937:37) True, the Americans resembled Schmoller in some respects, and they did produce more statistical than historical research. But not too much should be made of this latter point. Mitchell (1969:596), the great quantitative institutionalist, was an advocate of historical studies ("they help to emancipate us from the schematic and superficial view of human nature of the classical economists"), while Ely, Commons, and their students published a slew of Schmollerian monographs on labor history; in fact, they founded that discipline. {15} But a more important flaw in Schumpeter's assessment was his failure to acknowledge how far American institutionalism had gone beyond Schmoller: first, by elaborating the synthetic approach developed by Weber and others; and second, by mixing into that synthesis some uniquely American ideas, such as those derived from pragmatism.

The pragmatic philosophers--Peirce, James, Mead, and Dewey--shaped the ideas of the institutionalist economists to an extent that is hard to conceive given the current relationship between economics and philosophy. In part, this was because pragmatism was well-suited to a critique of intellectual orthodoxy. Drawing their inspiration from Darwinian rather than Hegelian evolution, the pragmatists held that scientific progress occurred as a result of diversity and chance developments, a view that tolerated eclecticism and historical contingency but devalued mechanism, consistency, and universal laws. Moreover, the pragmatist credo -- that the truth of an idea is judged by its practical consequences --reinforced the German-derived emphasis on policy and facts as opposed to abstract, deductive theorizing. Although institutionalism was condemned for excessive description and fact gathering, at its best it combined the pragmatic emphases on chance and facts to produce--as in the work of Wesley Mitchell--a statistical approach to empirical research that has its modern counterpart in applied econometrics. Despite his scepticism about the scientific

status of economics, Mitchell (who founded the National Bureau of Economic Research) thought that socioeconomic data and statistical measurement held the greatest promise for aligning economics with the natural sciences. {16}

Unlike their colleagues in Germany, the pragmatists were imbued with the Anglo-American ethos of rational individualism but they also acknowledged that individuals were shaped by social institutions and so rejected the political implications of historical individualism. Efforts to resolve this tension led to their emphasis on habit, which plays a key role in pragmatist thought as an alternative to rational choice and decision. Not only do habits cause past choices to constrain a person's present ones, they also have social and cultural dimensions. Dewey called them "customs" (and later "attitudes")--a concept that was the foundation for the field of social psychology established by James, Dewey, and others. The key problem for social psychology, said Dewey, is to recognize conduct as an "interaction between elements of human nature and the environment, natural and social forces in man as well as without him" (1922:108)

These ideas deeply influenced the institutionalists. First, they formed the basis for the charge that mainstream economics lacked psychological realism. Against the rationality and atomism of homo economicus--Veblen's (1919:73) "homogenous globule of desire"--the institutionalists stressed the customary and irrational aspects of human behavior. Not only Veblen, but also Commons and Mitchell (1914), read widely in the new literature of experimental and social psychology and there found considerable support (sometimes explicit, as in the work of McDougall and Dewey) for the view that the psychological foundations of economics were oversimplified and inadequate.

Second, the pragmatic view permitted the institutionalists to go beyond what Hayek (1942) called the "methodological collectivism" of German economics -- in which social phenomena exist independently of individuals --to develop a more synthetic and optimistic view, one that combined structure and volition.

Veblen, for example, argued that economists had to study institutions because "human conduct takes place under institutional norms... the individual's conduct [is] hedged about and directed by his habitual relations to his fellows in the group [and] these relations, being of an institutional character, vary as the institutional scheme varies." On the other hand, Veblen stressed that "the growth and mutations of the institutional fabric are an outcome of the conduct of the individual members of the group", leading Veblen to define institutions as "settled habits of thought common to the generality of men." (1919:239-43)

Commons arrived at similar conclusions using different concepts. For Commons the basic economic relationship was the transaction between two individuals, which gave rise to his focus on conflict, power relationships, bargaining, and good will. Transactions are subject to the working rules of going concerns or institutions. But although institutions have their own internal logic and must be studied on their own terms, they are expressions of collective action and so are subject to change through human volition. Commons defined economics as the study of human will acting in collective organizations. Although this might appear a more cryptic version of the Weberian synthesis (and Commons acknowledged his debt to Weber), it contains a distinctively American strain of optimism. Commons (1934:733, 1950:132) saw the growing bureaucratization of modern society in a positive light. Through "progressive individualism", society not only becomes "greater than the sum of its parts [but] the personality of each organized individual is higher and more capable than the personality of unorganized individuals." Commons conceived modern history as a "moving process [of] changing alternatives open to individuals," this a far cry from Weber's dark musings on the lack of values and meaning -- other than rationality itself -- in modern, rationalized society.

Finally, the institutionalists were less hostile to analytic theory than the German economists, partly because the bulk of their work was published after the

methodenstreit, when synthesists like Weber, Sombart, and Schumpeter had appeared on the scene. Yet institutionalism's eclectic spirit had deep roots in American pragmatism. As far back as 1880, Berkeley's Bernard Moses-- a New Englander and the first American economist to receive his doctorate in Germany--argued that economists must "use a variety of methods in arriving at his conclusions...the deductive method of the classical school and the historical method of Roscher." (in Dorfman 1949:96) Moreover, the Americans were less likely than the Germans to view mainstream economic theory--with its largely English origins--as a pernicious foreign import. Whatever the explanation and despite their present reputation, the institutionalists were better trained in economic theory and--with the exception of Veblen, who was sui generis on this point--offered more constructive criticism than the German economists. {17}

Commons, for example, although he practiced the inductive method of deriving concepts like transaction and collective action from detailed histories and case studies (his mentor, Ely, was an early proponent of the "look-and-see" method) nevertheless claimed that his goal was not to replace existing theory but instead to expand and improve it. "The problem now is not to create a different kind of economics--'institutional' economics--divorced from preceding schools, but how to give collective action, in all its varieties, its due place throughout economic theory." (1934:5) Commons was well-versed in economic theory and applied it in a conventional fashion in his studies of regulation, money, debt, and other subjects.

But it was Mitchell who came closest to developing a synthetic approach, one intended to sharpen economic theory and make it more realistic by constant confrontation with facts, both quantitative (statistical) and qualitative (behavioral and historical). Although Mitchell criticized for being too much of an inductivist, he was well aware of the pitfalls in excessive

description. He criticized Schmoller (whom he otherwise greatly admired) for rejecting theory and naively believing that "only by inductive work could progress be had in the social sciences." (1969:573) On the other hand, he found fault with his friend Veblen for failing to use objective data or to state his ideas in testable terms. (1937:302) Mitchell's own heavy reliance on data, and his method of "passing back and forth between hypothesis and observation, each modifying and enriching the other," were a sharp departure from the deductive tradition of armchair theorizing, of which he was critical:

I don't think I do classical economics injustice when I say that it erred sadly in trying to think out a deductive scheme and then talked of verifying that. Until a science has gotten to the stage of elaborating the details of an established body of theory, say ...filling in a gap in the table of elements - it is rash to suppose one can get an hypothesis which stands much chance of holding good except from a process of attempted verification, modification, fresh observation, and so on. (in Gruchy 1947:268)

Although Mitchell's jab politely was aimed at the classics, he also meant it to apply to contemporary economics. It is well to remember that as late as the 1930s reliable economic data was scarce and sparsely used in economic research. Mitchell did much to remedy both of these problems. (Kuznets 1963)

#### INDUSTRIAL RELATIONS

The institutionalists had their greatest impact on the field of industrial relations and labor economics. This is usually attributed to the Commons legacy but there are more basic explanations, chiefly that mainstream theory was at its weakest in explaining labor market anomalies: the persistence of unemployment and wage differentials, the unspecified labor contract, and the intrusion of noneconomic forces into the labor exchange. More than most of the applied fields in economics, labor economics overlapped other disciplines because both the traders and the commodity traded in labor markets--human effort--were more likely to be affected by purely non-rational social and psychological factors than, say, stockbrokers or hogs (but see Shiller 1984). Moreover, labor markets were studded with institutions like trade unions whose collective logic was not

fully captured by extrapolating from individual behavior. {18} Finally, labor economics was a field in which practical issues were salient and unavoidable. The labor question, broadly defined, was arguably the most pressing problem in American society throughout the first half of this century, long after most other nations had adapted to trade unionism and the modern welfare state.

Until the 1930s, labor economics and industrial relations were synonymous terms. The field was a *mélange* whose dominant element came from economics, although it also covered industrial sociology, personnel administration, labor law, labor history, and industrial psychology. But except for psychology, none of these had yet developed into specialties firmly rooted in disciplines outside of economics. For reasons too complex to discuss here, sociologists and historians largely ignored labor issues, while business and law school faculties competed with labor economists for authority over the other areas. Among others, Gordon Watkins, Sumner Slichter, and Joseph Willits wrote widely on personnel administration, while John Commons, William Leiserson, and David Sapos all were recognized labor law experts. {19}

The academic division of labor [sic!] began to change during the late 1930s. With the rapid growth of unions and of labor market regulation, industrial relations emerged as a distinct, interdisciplinary area of study. By the end of the war it had its own research institutes, professional organizations, journals, and degree programs. Although a few of these programs were housed in economics departments, the bulk were found in new, interdisciplinary schools and departments of industrial relations. Labor economics was central to postwar industrial relations, but it no longer defined the field. Other disciplines now staked out claims for a piece of the intellectual action and as a result, labor economics in the 1940s and 1950s became slightly less eclectic than it had been. Some labor economists viewed this as a small step in the right direction. But most remained oriented to other disciplines and actively involved in practical

affairs. Hence they chose to remain under the industrial relations umbrella.

In these and other respects the industrial relations economists, or neorealists as Kerr (1983) calls them, strongly resembled their institutionalist forebears. They were thoroughly familiar with economic theory but dissatisfied with its lack of realism, impracticality, and normative conclusions. But rather than junking the whole apparatus, as Schmoller did, they persistently attempted to remedy perceived theoretical problems. One way this was done was by mastering the facts about how labor markets operated, collecting new data when these facts were missing, and then amending or correcting theory when it failed to fit. That was Lester's (1946) approach in the debate with Machlup, and Ulman (1955) did much the same thing in his critique of Friedman. A second approach was to revise economic theory by taking insights from other disciplines and from comparative and historical research. This was the thrust of the Inter-University Study of Labor project, under whose aegis numerous works were produced that emphasized the historical and cultural limitations of economic theory. {20} Social and industrial psychology continued to be a source of critical ideas about economic rationality in the labor market, although the link was overshadowed by the the industrial relations economists' critique of the human relations school, which turned on the alleged failure of the Mayoites to acknowledge unions, social conflict, and other structural issues. Indeed, the structural perspective--that unions, government, and other institutions had to be studied on their own terms and not reduced to individual maximizing--constituted a third approach, exemplified in Dunlop's (1958) writings on industrial relations systems and their web of rules. Finally, the industrial relations economists shared with the German economists, the Fabians, and the early institutionalists a reformist political outlook that included an abiding concern with policy issues, sympathetic identification with the labor movement, and direct participation in public affairs. {21}

As is well-known, the industrial relations field began to lose numbers and intellectual luster during the 1960s, which reflected (at least initially) not the decline of the labor movement and the welfare state but rather their success, institutional stability, and public acceptance; the historical mission of the reformers seemed to have been accomplished. At the same time, intellectual currents began to shift within labor economics and other economic fields: "soft" (synthetic, interdisciplinary, realistic, structural, fact-laden) was out; "hard" (pure, elegant, individualistic, theory-driven) was in. {22}

The ascendance of the hard approach had more to do with the stress on mathematical tractability and sophistication that went along with computerization than it did with quantification in the sense of empirical "number crunching." In fact, one of institutionalism's legacies was the data-oriented style of labor economics research carried out at the NBER by Freeman and his students. But that no longer was the route to professional prestige. As Leontieff (1982) tabulated it, two-thirds of the articles published in the American Economic Review between 1977 and 1981 contained no data whatsoever. Given that economics had long been the mother discipline of American industrial relations, it was, perhaps, inevitable that intellectual trends in the former would register in the latter. As a result, the field of industrial relations today is "harder" than before, at least in the United States. {23}

#### A VITAL LEGACY

This is not to say that the old industrial relations disappeared without leaving a trace. As noted, the NBER approach is a heritage of that tradition. Moreover, labor economists still value a "feel" for labor market institutions and arguably know more about developments in cognate disciplines than other economists. A strong practical orientation remains within labor economics as does an awareness that institutions have to be approached on their own terms. Also, here and there one finds an awareness that received theory has

limitations: historical, cultural, and analytical. There is even scattered evidence that the methodological pendulum is swinging toward greater eclecticism and realism. Japan's superior economic performance is sparking renewed interest in institutional analysis. And a growing number of labor economists are employed in business and other professional schools, where an emphasis is placed on case studies, field research, and practicality. The new economics of human resource management (E/HRM) is a direct result of that development and represents a promising trend. But it is not without problems. The remainder of this paper shows how methodological insights from industrial relations can raise the quality of research in E/HRM and in other parts of labor economics. {24}

Empirical Realism: Knowing the facts about labor market institutions and keeping theory close to empirical reality were key parts of the industrial relations tradition that should be preserved. Facts not only are needed for the verification of theoretical predictions but--as in their "stylized" form--are elemental substances from which theories are derived. Although, as Friedman argued, a theory's assumptions do not have to be realistic, realism nevertheless improves the chances of predictive accuracy. Unfortunately, recent work in labor economics shows a tendency to rush into print theories based on partial or faulty factual knowledge; only later do the grim empiricists come to clean up the mess wrought by Occam's razor and ceteris paribus.

Take, for example, the risk-shifting version of implicit contract theory. Popular during the 1970s, it eventually broke apart on hard factual reefs: the limited incidence and scope of real wage protection (e.g., COLAs) and of income replacement for unemployed workers, both in its public (UI) and private (SUBs and severance pay) forms. The same may yet be the fate of efficiency wage theory, the alternative proffered during the 1980s. After a spate of theoretical elaboration, the factual problems are starting to surface. Neither the turnover nor the monitoring versions of the theory have held up to empirical scrutiny

(Leonard 1987)--not even at Ford Motor (Raff 1988)--and the adverse selection version, while correct, is an old story (Weiss 1966; Mortensen 1970).

Admittedly, some of these problems stem from the unavailability of facts, especially corporate personnel records and other demand-side data. These would permit more extensive testing of the myriad competing theoretical claims that lie at the core of the E/HRM literature-- in particular, whether the shape of wage profiles is better explained by agency theory or by specific human capital, and whether wage structure stability is the result of efficiency wages, human capital, or other factors. (Lazear 1979; Parsons 1986; Katz 1986; Murphy and Topel 1987) The fault, however, does not entirely lie with secretive firms or the BLS. As Leontieff's study suggests, today it simply is more convenient and prestigious for academic economists to do theory than to secure new facts. Hence there are fewer surveys and case studies of the sort that were regularly reported in the old industrial relations literature. Still, even if more data were dug up, they wouldn't solve problems created by sheer ignorance of facts, such as those concerning the features of the UI system or the causal relation between the NLRB's contract bar rule and contract durations; some of our most able theorists have repeatedly gotten this last one wrong. (Hall & Lillian 1979; Aoki 1984; Williamson 1985) {25}

Institutional Analysis: Institutions are another part of the industrial relations tradition that need to be reemphasized within E/HRM and labor economics, not only as background facts but as theoretical complements to individuals and prices, the fundamental units of conventional analysis. Institutions can be reincorporated at two levels--as terms in individual choice sets and as structures that undergird market economies--always keeping in mind, however, that they possess their own logic and histories.

Terms derived from social institutions--norms, attitudes, customs--are included in the utility functions of all individuals. Rather than accepting

these as given, industrial relations economics made them objects for study and attribution. Mainstream analysis, on the other hand, typically abstracts from these terms or reduces them to maximizing behavior, thus creating purely economic man who, says Sen, "is close to being a social moron" (1982:99). Social moronism might be a good approximation to reality in some instances, but it is a misleading oversimplification when applied to E/HRM issues, the study of which could be improved by taking seriously social institutions and social research.

Compensation provides a case in point. Rather than being a purely economic process, organizational pay setting to a significant extent is socially determined, as the industrial relations economists knew so well (e.g., Dunlop 1957). Recent research on equity theory, for example, bears this out. Workers are found to gauge pay differentials according to cultural and organizational norms of fairness. (Weick et al. 1976; Carrell & Dittrich 1978) When wage dispersion exceeds these norms, effort is reduced and turnover increases. (Mowday 1983; Pfeffer & Blake 1988) Even the pay of top corporate executives is significantly affected by social factors, such as the reinforcement of hierarchical authority in large firms or the maintenance of equity between CEO salaries and the pay received by outside board members. Indeed, these factors are found to outperform conventional economic predictors of managerial pay. (Simon 1957; O'Reilly et al., 1987) Although a few economists have begun to reincorporate social institutions into compensation theory (Akerlof 1980,1982; Frank 1984), progress in this area has been glacial. Ancient conundrums like industrial wage differentials might fruitfully be explored along these lines.

Until quite recently mainstream economics ignored institutions because it perceived them as islands of irrationality impeding the free flow of market transactions. By contrast, those working in the industrial relations tradition saw (and still see) institutions as part of the stream: theoretically inseparable from it and, in many cases, functional to its continued movement.

Social norms, customs, and laws form what Durkheim (1933:206) called "the noncontractual relations" of contract. One abstracts from them at the risk of misunderstanding how markets--including labor markets--work. The so-called new institutional economics (NIE), which combines agency theory and transactions costs, is presently reviving many of these ideas, paying close attention to the structural foundations of markets and giving credit to the ideas of earlier institutional theorists like Commons. (Williamson 1985; Langlois 1986) But with the exception of research on internal labor markets, NIE has not had much impact on labor economics. That is unfortunate, because there are nuggets within the NIE that could enrich E/HRM and labor economics and bring them closer to work presently being done in other social science disciplines (and to previous work in industrial relations). For example, relational exchange--an NIE concept that analyzes the noncontractual aspects of long-term economic relationships--has the potential to explain a host of fascinating and critical issues: the role of trust in the workplace; the characteristics of Japanese versus American personnel management; the social and cultural bases of labor exchange; and the economic logic of a governing web of rules. However, these issues remain largely unexplored in E/HRM and labor economics. {26}

NIE is gradually forcing economists to consider the economically desirable properties of governments, firms, social customs, and even trade unions; hence it is to be credited for restoring respectability to institutional analysis. But NIE often achieves its results by rationalizing institutions and reducing them to the logic of individual maximizing behavior. By contrast, the industrial relations tradition insisted that institutions be studied on their own terms: paying close attention to their actual evolution and operation, and not assuming (the fallacy of composition) that they are merely the sum of their parts. One does not have to dredge up ancient tomes to see the value of that approach. For example, recent research on union objectives has shown that the expected utility

model--however well it might predict individual behavior--poorly explains the behavior of unions. (Pencavel 1984, 1985) The determination of union goals is better approximated by studying the institutional characteristics of a union and its environment: the level, timing, and extent of bargaining; internal union structure; and the union's use of norms and benchmarks. Institutions also figure prominently in the new comparative macroeconomics, which considers the same variables as Pencavel but also incorporates political factors affecting wage setting, such as the terms contained in implicit "social contracts", the integration of organized labor into government, and other measures of corporatism. (Bruno & Sachs 1985; Flanagan et al. 1983; Helliwell 1988)

Time and Place Specificity: The comparative approach to studying institutions was strongly emphasized in industrial relations, but it is as yet not central to E/HRM. Admittedly, E/HRM's willingness to peer into the institutional boxes marked "firms" and "unions" marks an advance over the narrow price-theoretic concerns of mainstream theory. But in unpacking the contents of those boxes--internal labor markets, hierarchy, union goals--E/HRM has tended to follow the mainstream practice of abstracting from time- and place-specific elements. Hence E/HRM emphasizes the universal and rational features of employment institutions, although these factors are becoming less relevant to understanding economic growth and competition. With increased speeds of technological diffusion and similarly rationalized economies, the competitive edge among the advanced nations today depends on the particular and fine-grained features of their institutions. Evidence from comparative studies of firms in similar industries using identical production technology shows significant national differences--in worker and employer attitudes, management structure, and personnel practices and customs--which in turn are related to differing productivity levels. (Dore 1973; Form 1976; Maurice et al. 1984; Lincoln et al. 1978, 1986; Melman 1958) These national variations in what might

be called "x-efficiency" are important yet E/HRM virtually ignores them.

Abstracting from time and place has also caused E/HRM to produce theories that, perhaps unwittingly, rationalize American practices of recent vintage. Implicit contracts and efficiency wage theory "explain" in efficiency terms the phenomenon of wage rigidity-cum-temporary layoffs. But if the phenomenon is rational, given assumptions about risk preference or monitoring and turnover costs, why is it that American wages are more rigid and temporary layoffs more prevalent today than before the 1930s? Why do modern Japan and Europe have less wage rigidity and fewer layoffs than the U.S.? (Mitchell 1986; Sachs 1979; Gordon 1982, 1983; Piore 1986) Either risk preferences or turnover costs considerably vary over time and place (if so, this itself deserves study) or, what is more likely, national employment practices result from factors omitted by the theories. The latter suggests a more nuanced form of efficiency: a nation's employment practices are at best efficient adaptations to an historically contingent set of national institutions. Ignoring these leads to overly rational and even chauvinist theories.

Industrial relations included the study of labor and economic history because it recognized that institutions--unlike markets--have histories, and that these influence an institution's response to ongoing environmental change. {27} That historical focus, however, is largely missing from E/HRM, leaving E/HRM theory functional but static, largely unconcerned with how institutions change. And when E/HRM does deal with questions of origins and evolution, it gives too much weight to efficiency incentives. That shrouds our current institutions in an aura of permanence and closes off inquiry into normative and policy questions concerning institutions.

Take internal labor markets, for example. E/HRM attributes their origins to the emergence of firm-specific technology and other organizational idiosyncracies that created asset specificity in employment relationships. But

actual (rather than assumed) historical events occurred in precisely the opposite direction: Technology (broadly defined) today is less firm-specific than in the 19th century, when spot markets for labor were, however, more prevalent. Machines and other production technology now are available from national vendors and so firms do not have to design and craft their own, as in the past. Also, rules and procedures in modern bureaucratic organizations are more similar today than 100 years ago, when firms were stamped by the identities of their owner-operators and work routines were unstandardized. Hence it is unsurprising that historical studies of internal labor markets in Japan and the United States have found that in neither case were efficiency incentives alone strong or obvious enough to employers to generate internal labor markets. Employers adopted those structures when pressured by unions, government, and changing social norms. Moreover, those forces have grown weaker during the last fifteen years, particularly in the U.S., and as a result employers in both nations are now trying to restructure and shrink their internal labor markets. (Jacoby 1985; Gordon 1985; Deutschmann 1987)

Behavioral Realism: Industrial relations took from the German school and from pragmatism the idea that theory had to be based on psychological facts rather than assumptions about economic rationality. Although behavioral issues are particularly important to understanding employment relationships, there is little evidence that E/HRM has been affected by recent research in cognitive psychology that questions the behavioral precepts of economic theory. {28} The new psychology has found that expected utility maximization models do not accurately forecast behavior and that economic decisions are often only quasi-rational. (Kahneman et al. 1982; Russell & Thaler 1985) People ignore high consequence events of low probability--not purchasing flood and earthquake insurance, for example--unless they have previously been exposed to them (Kunreuther et al. 1978). That raises serious questions about the psychological

adequacy of key E/HRM concepts, such as reputation effects in agency theory and the disciplinary consequences of efficiency wages. In each case, the average worker will reason that the odds are low that the firm will treat her unfairly or dismiss her for cause, so why should firms (knowing this) treat workers fairly or workers not shirk? The new psychology also stresses that search and choice under uncertainty are not entirely rational but instead are guided by heuristic "frames." These have been shown to explain behavior of interest to labor economists, including bargaining, arbitration, and money illusion. In the case of wage cuts, the illusion results from social norms of fairness, a finding that reinforces Durkheim's point concerning the economic centrality of custom, mores, and law. (Kahneman et al. 1986)

Another feature of the industrial relations tradition was a willingness to make its behavioral assumptions explicit, as in the dispute over human relations. But with a few notable exceptions {29}, labor economists today either are unconscious of their beliefs about human nature or unaware that there might be alternatives to Hobbesian views. Opportunism and shirking exist, to be sure, but there is also reason to think that human beings can enjoy work and be trusted to perform it with discretion. While there is a risk of being Pollyanna, there is also the risk--rarely considered in the E/HRM literature--that pessimistic expectations will be self-fulfilling because individuals resent being tightly controlled. In the workplace, as Fox (1974) reminds us, low trust begets low trust. Thus while firms on the cutting edge of human resource management are seeking to minimize hierarchy and promote self-managing teams, E/HRM is rationalizing traditional forms of organization and authority. {30}

The E/HRM literature also makes assumptions about work motivation that are inconsistent with empirical studies of the subject. The heavy emphasis on compensation issues in E/HRM stems from an implicit judgement that employees are extrinsically motivated, chiefly by pecuniary rewards. But psychological

research shows the equal or greater importance of intrinsic motivation --competence, self-determination, self-esteem--and the factors that promote it, including job design and management style. Pay can be an effective motivator for some persons in some situations, but it can also undercut intrinsic motivation or otherwise stymie performance. (Lawler 1971; Staw 1976) Although compensation theory is the most developed area in E/HRM at this time, it would be hubris to suppose that E/HRM offers much of practical use even on that topic, let alone others (but don't tell that to the professional school deans).

#### CONCLUSIONS

As Weber wrote in his birthday letter to Schmoller, intellectual needs oscillate between generations. After two decades of movement away from the industrial relations tradition, it is time for labor economics again to develop a more empirical, realistic, and eclectic approach to its subject matter. That does not mean, however, giving up the theoretical precision which has been gained in recent years. Just as Weber's work combined the best of old and new, so too is it possible to develop a more synthetic approach in labor economics. Despite its faults (which are remediable), E/HRM is a step in the right direction.

But there still is far to go. Economists are adept at arguing the irrelevance of other disciplines or of evidence that does not fit maximization models. They can always claim that market competition or learning effects will iron out any observed departures from rationality. The strength of neoclassical theory--and also its profound weakness--is its ability to rationalize nearly any fact that confronts it. Young economists acquire these habits of mind early in their training. A recent survey of graduate students in economics found that only 13 percent had intellectual interactions with students or scholars in other disciplines; well more than half thought it unimportant to have a thorough knowledge of the economy. (Colander & Klamer 1987)

In light of those figures and of our discipline's intellectual history --the rarity of good eclectic work like that done by Marshall or Mitchell or Schumpeter--I admit it may be overly optimistic to imagine that a brilliant new synthesis lies just over the horizon. It might be possible, but it is not probable. One hundred years ago Walter Bagehot observed that "Political economy is an abstract science which labours under a special hardship. Those who are conversant with its abstractions are usually without a true contact with its facts; those who are in contact with its facts have usually little sympathy with and little cognisance of its abstractions." (in Coats 1954:146) Although the two sides have come a good deal closer since then, it is sobering to consider how far apart they still are, a distance that R.A. Gordon (1976) measured in his call for "relevance with as much rigor as possible." Perhaps this is the most which can reasonably be asked of the new E/HRM: that it preserve the concern for facts and relevance that is the legacy of the industrial relations tradition.

## Notes

1. In this article I lump together the so-called "older" (Roscher, Knies, Hildebrand) and "younger" (Schöller, Brentano, Wagner) historical schools, despite differences within and between them. Stage theory, for example, was propounded by Hildebrand but rejected by Knies and Schöller. See Schumpeter (1954).

2. Here, for those who wish to pursue it, is the link between the historical school and Marx. Veblen (1919:260) classed them as two branches (right and left) of the Hegelian tree. The German economists in varying degrees were antipathetic to Marx's revolutionary beliefs and to his idea that capitalism followed laws of motion analogous to natural laws. This objection to Marxian scientism--that it conflated nature and society--presaged the Frankfurt School of Adorno, Horkheimer, and Habermas. Yet when Menger's former students, Hayek (1942) and Popper (1957), wrote their critiques of "historism", they lumped the German school together with Marx. Although this was inaccurate, the German economists were not entirely innocent of the charges levelled against them because of their vagueness on the scope for individual volition in cultural totalities. There also was an authoritarian, statist virus in Romanticism from which the historical school was not entirely immune. Hence its stress on the rights of society and its cult of the state (as in Adolf Wagner's unfortunate phrase "state socialism") can be viewed as precursors of Nazism, although there was more to both movements than that. Note that the historical school was popular in Japan, another statist late developer, and that mechanical stage theories still pervade Japanese Marxian economics. (Albritton 1986; Iggers 1965)

3. The debate was set off by Menger's Economic Investigations (1883), which criticized Roscher and Knies. Schöller wrote a scathing review of it, leading Menger to write another book, The Errors of Historicism in German Economics (1884), after which still more articles were published by both men. At times the debate got quite nasty. Schöller said, "Menger is a clever fellow but lacks a broad education; hence the one-sidedness of his economic views. He fancies the one little room of theory with which he is acquainted is the whole structure of political economy" (in Mitchell 1969 II:115). Menger called Schöller a scientist "the totality of whose halfways original knowledge consists in the primordial sliae of historical-statistical material." (in Burger 1987:259) Schöller's earliest works were detailed histories of craft and merchant guilds.

4. There is a similarity here to von Ranke's historicist ideas. Although he is best remembered for his emphasis on facts, Ranke stressed that facts should be placed in intuitively-derived structures that he called "ideas." Von Laue (1950:115) said of Ranke that "in order to perceive the mysterious throbbings of the 'idea', he strained all the faculties of his mind, reason, emotion, and intuition."

5. Schöller was attacking, and Menger defending, the utilitarian postulate of the randomness of ends. For Schöller ends were determined by cultural and historical factors and so were legitimate research topics, whereas for Menger they were random elements that interfered with the deductive method. Menger said that he would never dream of abstracting from anything but the insignificant, disturbing elements. But, as Rogin (1956:482) remarked, "the important point [of the dispute] is that of significant abstraction." See also Boehm-Bawerk (1890).

6. By induction Schöller meant detailed institutional studies, including historical and comparative ones. In later years, he took a more nuanced position, claiming that "Induction and deduction are both necessary for the science, just as the right and left foot are needed for walking." Schöller said he was not "opposed to the practice of deduction as such, but ... it is too often based upon superficial and insufficient principles, and other principles derived from a more exact observation of facts might very well be substituted for these." (in Gide & Rist 1948:401) In his Principles (I:29), Marshall approvingly quotes these same words in a chapter on methodology.

7. "There is a new future before political economy", said Schöller, "thanks to the use that will be made of historical matter, both descriptive and statistical, that is slowly accumulating. It will not come by further distillation of the abstract propositions of the old dogmatism that have already been distilled a hundred times." (in Gide & Rist 1948:398)

8. Schumpeter (1954:819) classed Weber as an economic sociologist and praised his contributions to that field, but he disparaged Weber for being ignorant of economic theory. Yet Weber wrote several works on marginal utility that showed his command of, and appreciation for, neoclassical theory. In one of them, Weber (1975a) defended the rationality assumptions of marginalism against Brentano's call for psychological realism. Some consider Weber and Schumpeter both to have been members of the "youngest" historical school, along with Sombart and Spiethoff. See Hennis (1987); Osterhammel (1987); Lane (1956); Machlup (1978); Huff (1984).

9. Weber found it ironic that some German economists wanted to study the historically unique in order to formulate universal laws of economic evolution. That limitation of inductive method is shown in industrial relations' inability to produce a general theory other than Dunlop's (1958) taxonomic approach.

10. Marshall (1961 I:38) made much the same point: "History tells of sequences and coincidences; but reason alone can interpret and draw lessons from them."

11. Economic sociologists have recently reiterated this point as "the problem of embeddedness" (Granovetter 1985). For earlier formulations of the economy as a social system, see Durkheim (1933) or Parsons & Smelser (1956).

12. Marshall said of the German historical school that it was "the most important work done on the Continent in recent times.. they have greatly extended the boundaries of economic theory... It would be difficult to overrate the value of the work which they ... have done in tracing and explaining the history of economic habits and institutions. It is one of the great achievements of our age." (1961 I:767)

13. At times Marshall veered off into holistic determinism of the sort condemned by Hayek and Popper. Economists, he said, "are concerned with individuals chiefly as members of the social organism. As a cathedral is something more than the stones of which it is made ... so the life of society is something more than the sum of the lives of its individual members." Previous economists had "confined their attention too much to the motives of individual action" but now, said Marshall, they regarded the individual "not as an isolated atom, but as a member of some particular ... group" (I:25). But Marshall never linked these points to his main schema. As Wesley Mitchell put it, a "ghost stalks the background of Marshall's analysis." It is "the schematic and superficial view of human nature... embodied in homo oeconomicus." (1969 II:596)

14. Edwin R.A. Seligman, Mitchell's colleague and part of the first wave of institutionalists, said much the same thing back in 1886, when he praised the German economists for "denying the existence of immutable natural laws in economics, calling attention to the interdependence of theories and institutions, and showing that different epochs or countries require different [theoretical] systems." (1886:19)

15. Despite Brody's (1979) antinomy of the "old" and "new" labor history, the two approaches have common roots in Romantic idealism. In the old labor history, gathering an abundance of detailed and often exotic facts was a means to the end of saying something about larger structures, chiefly organized labor and its institutions. In the new labor history, collecting those facts becomes an end in itself, although the facts are sometimes fused into idealist wholes (e.g., working-class culture, Republican virtue, etc.) Note that the field of business history also has German roots--specifically the work of Richard Ehrenberg, who inaugurated the corporate case study approach to economic history--that were transplanted to the United States by Edwin F. Gay and others.

16. Mitchell's friend and teacher, John Dewey (1929:246 et seq.), took this one step further and argued that Kant's dualism could be overcome -- in economics and other social sciences -- by recognizing that nature was no more certain or lawful than human behavior: both contained contingent elements that required a common probabilistic methodology. Statistics rescued induction as a theoretical tool because one could reasonably generalize from inductive data given assumptions derived from the law of large numbers. Note that one of the pioneers in the collection and analysis of economic statistics was Ernst Engel, head of the Prussian Royal Statistical Bureau. Through his international reputation (Engels' law) and the work of his American students, Engels spurred the creation of new state and federal bureaus of labor and commercial statistics in the United States. (Dorfman 1963)

On pragmatism, see Wiener (1949); Mills (1966); Scheffler (1974); and Murphey (1961).

17. With his sarcastic dismissals of analytic theory, Veblen probably came closer to Schmoller than the other major institutionalists. Like Schmoller (whose work he enthusiastically reviewed for American audiences), Veblen denied the existence of a purely economic sphere and decried the absence of dynamic and cultural elements in mainstream theory (1919:67,173). Mitchell recalled that for his former teacher, neoclassical theory was "not so much right or wrong as it [was] beside the point" and that Veblen found it curious that "reasonable men could think such notions plausible or important." (1969 II:652,654)

18. Even judges had a hard time with this one. It took until the 1920s for courts to recognize that unions were not agents for their members and that their contracts established group rules which could not be reduced to a bundle of individual rights and interests. (Lenhoff 1941)

19. Leon Keyserling, drafter of the Wagner Act, did graduate work in economics under Rexford Tugwell and then followed his teacher to Washington in 1933 (Casebeer 1987). My discussion of industrial relations history is based on McNulty (1980), Dorfman (1959), and Strauss (1988).

20. Note, however, that the project culminated in a book (Kerr et al., 1960) whose main point was a variant of Weberian rationalization--that industrial societies were converging on the modern American model (hence lowering the barriers to a wider application of Anglo-American theory).

21. Kerr (1983:303) accurately described the neo-realists of the 1940s and 1950s but gave no sense of their historical significance or intellectual lineage. They "took an interest in the role of power and of politics, as well as of rules of behavior... they wanted to look at things as they really are, to render the precise details of relationships; but they also wanted to connect faithfully theory to practice. They rejected efforts to present complex relationships in an abstract or idealized form... [they] concentrated on typologies or patterns of actions related to time and place rather than on either individual developments or one, central, universal theme. The

attention to reality led to an interdisciplinary perspective.. Policy [also] was a central interest." For a similar view, see Dunlop (1977:280).

22. The "hard" approach has even reached Marxism, as in the recent work of the analytical Marxists. (Roemer 1986)

23. Cappelli (1985) well describes the British approach to industrial relations, which is more inductive, holistic, and case-oriented than the American one, a difference he ascribes to the continuing salience of policy issues in Britain. But it is well to remember that British industrial relations grew up outside of economics -- in sociology, law, and the Webbs. Although the Webbs resembled the institutionalists in many respects, they were more disdainful of analytic theory and, with the exception of the LSE, had little influence within British economics. Hence the absence of labor economics at the center of British industrial relations left it relatively more inductive and descriptive, even in the 1950s and 1960s, and less subject to changing styles within economics, such as the recent shift to "hard."

24. For a sampling of the recent E/HRM literature, see the articles (and citations therein) found in a special issue of Journal of Labor Economics (October 1987).

25. During the 1920s, when there was no bar, about a quarter of all contracts had durations of three years or more. Since World War II, average contract durations have determined bar durations, not the other way around. See Jacoby & Mitchell (1982) and Jacoby (1988).

26. The concept first was outlined by Williamson (1979) and Goldberg (1980). Okun (1981) later dubbed it the "visible handshake." For earlier explorations, see Parsons & Saelser (1956); for recent and suggestive analyses, see Piore and Sabel (1984), Dore (1987), and Williamson (1985).

27. Nelson and Winter (1982) analogize these histories--as encoded in organizational procedures and routines--to Lamarckian genes.

28. An exception here are the behavioral realists that have come out of Carnegie-Mellon, including Herbert Simon and Oliver Williamson. In his Nobel Prize acceptance speech, Simon cited John Commons as a key influence on his thinking. (1979:499)

29. Examples include Akerlof (1984), Leibenstein (1987) and Hogarth & Reder (1987).

30. Compare Walton (1985) or Heckscher (1988) to Jensen & Meckling (1979) or Williamson (1980). Williamson, however, is to be credited for making his behavioral assumptions explicit and for noting, though only in passing, that "calculativeness can get in the way of trust" (1985:406). Some (e.g., Dore 1987) take the Schmoellerian view that these behavioral assumptions are time- and place-specific abstractions from modern American society, although I do not agree with that assessment.

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