

# NEW MANAGEMENT THEORIES- AN ALTERNATIVE TO THE CURRENT CRISIS?

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## ABSTRACT

*The present paper approaches the current global crisis by means of managerial theories and moral principles. There will be presented a set of economic and political factors which have conducted to the collapse; the accent is put on the moral perspective at the governmental, managerial and individual level, which underlies the development of various management theories. After the analysis of the crisis from different points of view, I will proceed to the study of different management theories, with a special focus on the latest management developments and their capabilities to accelerate the recovery rhythmus of enterprises in order to overcome the crisis and to forewarn us with respect to similar situations in the future.*

**KEYWORDS:** *new management theories, crisis, moral crisis, managerial modernization*

## Introduction

More than 2 years have passed since the sub-prime lending crisis arose in the mortgage sector in the United States. Along with the emergence and expansion of the financial crisis in the developed world it has been broken the illusion of the market being efficient by itself. In this context the statement of Milton Friedman, a promoter and defender of the free market, "I would like that people remember me as a fiend of freedom. By analyzing the history you realize that everywhere where you find economic growth and capitalisms flourish, people live better and longer" proves its inconsistency (Friedman, Friedman, 1980). The structure and dynamics of deregulated finance triggered partially the credit crunch also in the interrelated sectors, which was followed by a generalized crisis at global scale. This unprecedented collapse determines a rethink of financial liberalization. The roots of this fundamental rethinking process go beyond the financial issues, towards management theories and even deeper, tackling the set of values and beliefs of modern societies.

Despite the fact that it is generally known and recognized that the management and its modernization play a crucial role in achieving economic performance and providing sustainability for a company or public system, it is overlooked within the process of implementation of anti crisis measures and restructuring and improvement of the former organization systems. Instead of adopting strategic management solutions, which imply long- term structural changes with effects for a larger time horizon, most of the companies or public administration organisms prefer to adopt solutions which only apparently solve the problem, such as personnel cuts, technical unemployment, loans etc. (Verboncu, Purcaru, 2009). Not many managers and public leaders have acknowledged the wide sphere of competence, action and influence, of which the strategic thinking and management dispose. Therefore not many have tried to rethink the management theories and to adapt them to the requirements and needs of the global society, whose players are countries, companies and individuals.

## Several possible causes and triggers of the crisis

Some economic explanations on the roots of the current crisis provided by both academics and practitioners refer to accumulation of imbalances and lack of suitable rules and regulation of the financial industry: *subprime credits, loan origination practices, new financial products, securitization, rating agencies, leverage, accounting practices, government sponsored agencies as Fannie Mae and Freddie Mac, tax benefits for homeownership, regulation and supervision* (Simon, 2009).

In the US in the last two decades over 6 million people were allowed to buy a house for the first time. This fact was possible just by a loose credit policy. Often mortgages with no down payment (deposit 0) were approved without making any deep research about the income status and credit history of the borrower (Marks, 2009). This is why the defaults on mortgage payments are mostly concentrated on the *real estate subprime market* (Fig.1). The development of the subprime market is tightly connected with the rising house prices. The mechanism is the following: the interest payment for 100% mortgages or mortgages with a small down payment is higher than the regular one because of the increased risk taken by the credit grantor. The prices on the real estate market were steadily growing. Rising house prices enable borrowers to remortgage (refinance) by switching to another agreement with the creditors, in order to get a better interest rate after several years. This means that for the home owners the mortgage represents a smaller percentage of the property and they can contract new credits and the spiral goes further up. This system has conducted to a large number of financial instruments and derivatives, whose value has not relied on the real value, but rather on an artificial, speculated value, much higher than the actual one. Subsequently this speculative market conducted to a bubble, which exploded in 2007/2008 (Simon, 2009). The house prices fell in the last years in the US, which disables the owners to remortgage and in many cases they are even left with negative equity (mortgage debt is greater than the house's value) (Buzelay, 2009).

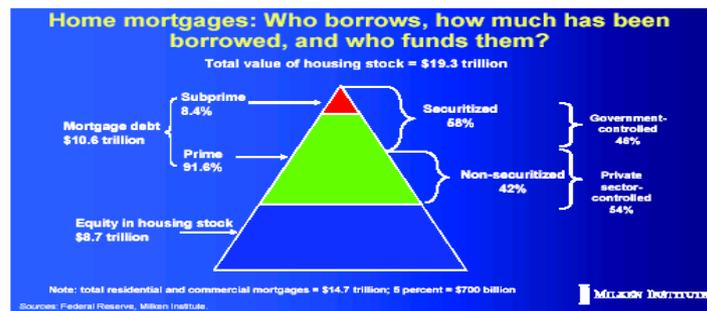


Figure 1 Home mortgages in the US, Source: Barth, J., Yago, G (2009)

Another important role in the crush of the financial instruments and subsequently the crush of global economy is assigned to the *Credit Rating Agencies*. Their importance increased exponentially along with financial globalization and the risk carried by different financial assets was tightly linked with the rating scores issued by these Credit Rating Agencies. Several authors have tried to identify the conflicts of interests which might occur in the rating issuance activity (Marzavan, Stamule, 2009). Thus these conflicts have a large impact on the quality of the rating issuance activity and in many cases led to overrating companies. The defenders of the Credit Rating Agencies bring into spotlight the theory of

“reputational capital” which would constraint these Agencies to act completely independently and provide accurate information. The economic history has already proven the inconsistency of this presumption by considering other cases of corruption in big financial companies, such as Arthur Andersen, which was one of the “Big five”.

By conducting a simple calculation, it can be easily proved that the value of subprime loans in default represent just 3% of the GDP, which couldn't solely provoke such a deep global crisis (calculation based on data from Milken Institute, <http://www.milkeninstitute.org/>). Even the multiplier effect can not completely endow credibility to this hypothesis: “increase in stocks, decline in sales and profits in the building industry and then the crash was felt throughout the overall economy by slowing investments and consumer spending shrinking the aggregate demand and the GDP, increasing unemployment etc.” (Simon, 2009, pp.189)

Other authors come up with *political explanations*: US has overestimated its capacity of intervention on the world map. Therefore the latter has exceeded its funds and run out of resources, not being able anymore to take action on parallel fields. The poor and emerging countries point at the developed countries as at the origin of the crisis. Though *not many authors have analyzed the crisis from the moral perspective*, from the point of view of the values, standards and beliefs promoted by modern societies. The following chapter aims to approach the crisis from the aforementioned perspective.

### **Is the economic crisis a moral issue?**

Supposedly we can distinguish between moral issues, such as abortion, domestic violence, other family related topics etc. and other type of issues like trade, politics, business administration etc. The present paper's objective is to switch this perspective by removing the barriers of these two categories and letting them converge. *The first step* in order to pursue is to look at government's engagement in the society by dint of the regulations imposed by the latter and their sweeping consequences in the society's organization.

In respect with the current crisis almost everything is a matter of justice or injustice induced by the government and therefore a moral issue. “Government is active in the economy in the way it sets tax policies, allows banks to offer mortgages to people who can afford little or no down payment, and is now sending money to taxpayers to try to stimulate a faltering economy even though the money it distributes is borrowed (as debt) from future taxpayers.

The economic crisis that government is now trying to solve or alleviate, in other words, is not an innocent accident.

It is the fruit of a great deal of injustice—the injustice of government piling up public debt and encouraging individuals, businesses, and financial institutions to do the same”(Skillen, 2008). Financial institutions, guided by the goal of profit maximization, no matter if sustainable or not, kept multiplying risk and leveraging debt. As a consequence the objects of trade are not based on their real value, but on a speculative one, much over evaluated. The outcome of this helix is an inflation of values, which finally conducts to market failure and system's collapse.

John Plender reports in 2008 in Financial Times about the income *inequality in the US income distribution* and the huge gap between rich and poor people. He argues that this gap is not just a result of sharp competition, globalization, innovation in high technology and healthy return of investments, but also a result of a weak oversight and tax policy. Having said this he relates in his article to some figures: the pre-tax income and the post-tax income for the low, middle and high income families. Late 70s the post-tax income of the richest households was 8 times higher than that of middle income households and 23 times higher

than the lowest fifth. By 2005 those ratios grew respectively to 21 and 70. Considering this issue from the angle of growth of the pre-tax income, we have the following outcome: between 1979 and 2005 the pre-tax income for the low- income households grew by 1.3 per cent a year, middle incomes by less than 1 per cent a year, while those of households in the top 1 per cent grew by 200 per cent pre-tax and, more strikingly, 228 per cent post-tax (Plender, 2008). Cumulating these statements it is drawn an unquestionable conclusion: all the measures taken by administrative institutions induced a *deeper gap between social classes*. Simultaneously the American media and opinion leaders induced through all communication channels the idea of fulfillment of the *American Dream*, that everything was possible by being ambitious and perseverant, even the acquisition of a house. The American leaders encouraged the idea of purchasing a real estate property, taking into account the increased stability in the local communities that this kind of acquisition would have brought about. The irrational exuberance and extravagant expectations of the Americans were enhanced by the low interest rates for credits and mortgages and became reality, even if just for a short period of time, followed by a disruptive downfall. Irresponsibly people with low incomes “have taken out a low-or-no-down-payment mortgage at the encouragement of irresponsible lenders at the encouragement of those responsible to regulate financial institutions” (Plender, 2008, p.7). Everyone hoped (speculated) that ever-rising real estate prices would give their owners ever-increasing equity, allowing them to go ever further into debt to keep the consumption game going” (Skillen, 2008).

*The second step in my approach of the crisis as a moral issue* consists in shifting the perspective and turning the attention to *managers and leaders*, strategy setters of big companies, which play a crucial role at the macroeconomic level and are major contributors to the well fare of the global economy or, on the contrary, at its collapse. These managers and leaders are mostly graduates of big American and Western European business schools and in their way of acting and managing the business one can recognize major influences of different management theories, most of them achieved during the study. Attempting to trace back to the roots of the current crisis one can point to the management theories taught in the famous, high ranked business schools. I want to emphasize the belief that *management education*, especially that one delivered in top business schools attended by top managers, *contributed to the systemic failure of leadership and management that led to the current global crisis*. One reason in claiming causality between the current crisis and management schools is that the *management theories* taught in these universities *do not foster responsibility and accountability and do not focus on value-based leadership and management*. Ethics is not central in the management education and scholars are told to focus on the big picture and to take all the necessary measures in order to reach the organization’s main objective, mostly profit maximization. “By studying the arts, culture, history, literature, philosophy and religion, people develop their powers of critical thinking and moral reasoning. Business schools don’t develop those skills [...] which is why MBAs made the shortsighted and self-serving decisions that resulted in the current financial crisis” (Poldony, 2009, p. 45). These management principles are reflected also in the way the business schools advertise their study programs: one of the main criteria for the preparation of the schools’ and programs’ rankings relies on the “guaranteed” incomes -guaranteed by the degree- of the former graduates from the programs. This practice reinforces the idea that their only goal is to teach students how to make a lot of money, by any price. As a reaction to the big scandals, in which graduates from high ranked business schools were involved, such as the fraud by giants like Enron, some universities tried to reconsider their curricula and introduce subjects aimed to develop the soft skills, not only the technical ones, to focus on social responsibility and to use more qualitative methods. These topics unfortunately still represent a minor field of study, often considered not essential for one’s management

education. Some experts came up with the proposal to introduce in business schools a code of conduct and to set up a committee which monitors graduates' adherence to it. If necessarily, this committee has the right to withdraw the degree of those who break its rules. The problems faced by management education (many researchers believe that business schools are fostering unethical, self interested and even illegal behavior by their graduates being therefore harmful to society), which should be a solution of the problem, rather than a part of it, have their roots in the obsolete principles, that they promote, which do not correspond anymore to the society's needs and economic, social and political reality.

*The next step* in approaching the crisis as a moral issue leads the research *towards individuals and their values and beliefs in the modern society*. Lord Griffiths, vice chairman of Goldman Sachs International, portrayed at the lecture he delivered in October within the Academy of Economic Studies of Bucharest on the topic of the global crisis, the modern societies very suggestive as having replaced their God with the Market and its rules. Under these circumstances we can take into consideration some theories that relate a certain type of "market slavery" and "money slavery" (McGehee, 2009). During his speech Lord Griffiths approached another very important aspect regarding the causes of the social crisis that we are undergoing that refers to the steady appetite and even addiction to consumerism shown by individuals in modern societies. One can ascertain an ongoing process of "Despiritualization" of modern societies and a migration of spiritual values towards material ones.

### **New management theories and their role in the current crisis**

If we compare the changes that incurred in the last 50 years in technology, life style, geopolitics etc. with the management theories, the latter ones seem to have advanced in a much slower rhythm. If we ask a manager of the 60s to analyze the current management practices, he will be surprised by the supply chains in real times, the ability to offer non-stop service to the clients etc, but in the same time he will ascertain that not much changed in the management principles that ruled 50 years ago. Therefore I can state that management change did not cope with the social, technological, political change. Hierarchies are not so sharp anymore, but they still exist. The normal employees are more educated and instructed, but they still obey the decisions of the managers. In many organizations the goal of the company is not embraced by employees. In this context aroused the question: did the modern management theories reach a peak, which doesn't need to be passed? Or we should expect a revolution in the management theories, in order for this to be brought in line with the technological and social progress? (Hamel, 2007)

The new management theories appeared as a reaction to dysfunctions in the system. A fundamental issue for a company and its role in society is connected to the setting of strategic objectives. According to the majority of the new management theories a major difference appears by the *definition of the company's goals*: the main goal of a company is not the profit, but the creation of values for the society and its members (customers). Therefore the *profit is just a normal consequence of creation of values and bringing satisfaction to people*.

According to the *Japanese new management theories* there are 3 fundamental questions that an employee or entrepreneur must answer:

- What is the goal of your life?
- Why your organization should exist?
- What is love?

Especially the third one might appear very surprising, illogical and useless in a business context for an entrepreneur, but the explanation for its existence is that nothing can be created without love, not even a sustainable company. Without having clarified the

answers at the aforementioned questions, the work can not be focused towards creation of value. The Japanese theories are built on the following statement: Management without philosophy is a lethal weapon; philosophy without management is worthless. These theories highlight the importance of the philosophy which stays behind the business and advice against the “money rush” as a primary way of action.

There are many American and western European authors whose books approach the future of management. Hamel, Savage, Shirky, Ridderstale and Nordström and many others promote management principles such as: development of the companies after the model of the “*communities of purpose*”, whose members are driven in their activity by passion and the individual objectives overlap with the company’s ones. The organizations of the future should be characterized by *a high degree of transparency, informality and flexibility, dulling of the hierarchies up to their disappearance, special attention and respect for the spiritual needs of individuals, creation of the conditions for the collaborators to develop their creativity and therefore to innovate*, time management which enables associates to enrich and enlarge their sphere of action, focusing also on other activities than the core activities, which they enjoy and foster the personal development, going behind the routine of day to day work. The well known schema 70:20:10 (time dedicated for core activities: innovative activities for the benefit of the company: activities for the personal development) should become normality in the organization of the future.

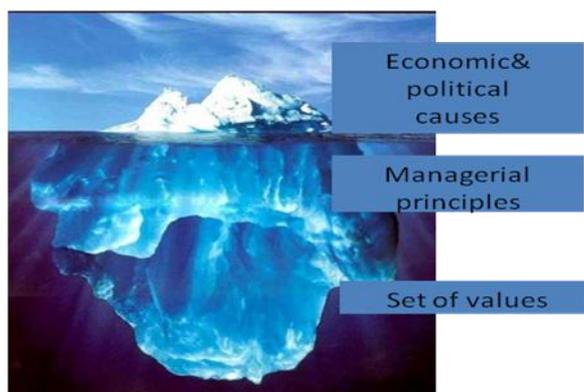
Recent theories argue for the *fractal organization*, which is inspired from the chaos theory (Savage, 1996) and features autonomy and coordination. In this kind of organizations each member acts independently and owns his unique characteristics, but the organization’s features are recognized at a smaller scale in each of its members. Each element has the capacity for self optimization, self design, self organization and self creation, but always in the larger framework of the organization. In order to overcome the new challenges, the organizations need to display the flexibility of the organic networks and systems and not the inflexibility of the hierarchical systems (Isaac& Herremans, 2009). An organic organization relies on trust, general participation in the decision making process and a high degree of regeneration through creative methods.

As one can remark the new management theories refer to and emphasize much more those aspects which have been disregarded in the classic management theories. At this time, in the present social order, setting a main objective of a company different from the financial one appears as a utopia or at least unrealistic. The crisis that we are undergoing is just a first signal of the need for “moral reconstruction” and establishment of a new scale of values .The business principles have to be reconsidered and reformulated. If modern societies fail to react accordingly, the future will probably disclose other unpleasant events.

## **Conclusion**

The current crisis calls up an analysis in a larger framework. After referring to the visible, cognitive causes of the crisis that the global world undergoes, the present paper aimed to step further with the research by revealing the fundamentals, the core explanations, which actually underlie the economic and political ones. The ongoing research attempted to approach the invisible, hidden part of the iceberg (Fig.2). The economic and political causes represent just the visible peak of the iceberg, while the moral and emotional values substantiate the current collapse of modern society and its proficiency and efficiency to administer and manage the economic, political and social system. This set of emotional values is strongly embedded in the management theories, on the basis of which executives manage their business and build up the business strategies and tools. It is

aimed to bring forward the moral aspects of the crisis and to highlight the fundamental role played by these principles which actually back up the managerial theories. The opinion and decision makers have to reconsider their management principles, in order to successfully overcome the challenges that they face and to develop sustainable businesses. As a consequence of this, the management theories will undergo essential changes and achieve improvements.



**Figure 2. The “Crisis’s iceberg”**

There are many immoral, irresponsible decisions by governments, businesses and individuals in the current crisis. Unfortunately considering their reactions and measures there is reason to doubt that the aforementioned actors are prepared to give up the false belief that there is a quick and easy road to prosperity.

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