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The Roots of the Global Financial Crisis Are in Our Business Schools

Robert A. Giacalone
Fox School of Business and Management, Temple University,USA

Donald T. Wargo
Department of Economics, Temple University,USA

Abstract. In discussing the $1 trillion bailout of the U.S. Financial Institutions, virtually every Member of Congress and almost every government official—including Fed Chairman Ben Bernanke and President Obama—has blamed the crisis on the "greed and irresponsibility of Wall Street". Almost all of the financial executives involved in the crisis, from CEOs to middle managers, are products of our business schools. Additionally, there is a high correlation between the recent unethical behavior of a number of multinational corporations and the number of MBA holders in their top ranks. As a consequence, many critics are convinced that there is something wrong with our business schools. This paper presents the causes and consequences of what ails business school students and graduates today: the toxic teaching of bad management theories. These theories—grounded in the assumptions of economics—include determinism and materialism, the cult of profit maximization and a pessimistic view of human nature as totally self-interested. By teaching these theories, business schools are inculcating values of materialism and greed that create a life-long pursuit of money and status. This makes it all too easy for business managers to choose expediency and short-term profits over ethical behavior. Further, these materialistic values create higher levels of depression, anxiety and psychological disorders as well as make our students less cooperative and more anti-social as individuals long after they leave academia.

Keywords: critique of business school teaching, values education, business ethics, economic assumptions, behavioral economics.

1. The Global Financial Crisis and the Resulting Recesssion

Even as the U.S. Government was rescuing the largest American banks and A.I.G., Inc.—the world's largest insurance company—from bankruptcy, it was simultaneously blaming the global financial crisis on the "greed and irresponsibility of Wall Street." We are going to learn more of the details of how this greed and irresponsibility led to the near-collapse of the entire U.S. financial system (and crippled the financial systems of other countries) from the on-going Congressional, FBI and Securities Exchange Commission investigations and from forthcoming popular business books and academic studies. These inquiries will most likely reveal some of the same behavior that has come to light in the collapse and $180 billion bailout of A.I.G., Inc.

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2. AIG's Insolvency Was Caused by Its Fianancial Products Division

A.I.G. Financial Products was a tiny unit, whose *average* employee salary and commissions were $1,000,000 per year. However, this division committed the parent company to over $500 billion in credit default swaps—extremely risky financial derivatives. *The New York Times* reported that, "In the case of A.I.G., the virus exploded from a freewheeling little 377-person unit in London, and flourished in a climate of opulent pay, lax oversight and blind faith in financial risk models. It nearly decimated one of the world's most-admired companies, a seemingly sturdy insurer with a trillion-dollar balance sheet, 116,000 employees and operations in 160 countries" (Morgenson 2008).

3. Wall Street Bankers and Excessive Risk-Taking

Further, U.S. Treasury Secretary Timothy Geithner has said "This financial crisis had many significant causes, but executive compensation practices were a contributing factor. Incentives for short-term gains overwhelmed the checks and balances meant to mitigate against the risk of excess leverage. By outlining these principles now, we begin the process of bringing compensation practices more tightly in line with the interests of shareholders and reinforcing the stability of firms and the financial system" (Labaton 11 June, 2009).

Mr. Geithner made these comments during the announcement of the appointment of Kenneth R. Feinberg, the highly-respected attorney who presided over the World Trade Center victim compensation, to oversee the pay of the employees at the seven largest U.S. companies rescued by the American government. These companies include A.I.G., Citigroup, Bank of America and the automotive companies GM and Chrysler. Geithner further said the administration would seek legislation to give more authority and promote more independence for the corporate committees that set compensation for top executives. The regulations would be similar to a provision in the Sarbanes-Oxley law of 2002 which responded to a spate of accounting scandals by giving more authority and imposing more exacting standards on the audit committees of corporate boards. Mr. Feinberg stated that the guidelines he will create should be used as a model for the entire financial services industry.

President Obama has also criticized the financial industry for its recent excesses. During the unveiling of his June, 2009, proposals for extensive reform of financial regulatory oversight, he stated that a "lack of oversight" allowed what he called "wild risk-taking" by financial institutions. This includes the banking system, the insurance companies and what has been called the "shadow banking system"—unregulated investment banks and hedge funds. He said this risk-taking led to "very dangerous" conditions that imperiled the global economy (Labaton 17 June, 2009). Millions of responsible and hard-working Americans, according to President Obama, have endured enormous suffering through job losses and

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foreclosures caused by the general irresponsibility of the financial industry and the resulting credit crisis and recession.

4. Will These New Regulations Be Enough to Change Wall Street?

On the other hand, Joseph Nocera, the senior financial columnist for the New York Times, feels these measures won't be enough. "With the big banks, there is always a degree of moral hazard because they simply can't be allowed to fail the way other companies can. Market discipline—or better corporate governance—just isn't enough; even when a bank's management is aligned with shareholders, they aren't necessarily aligned with taxpayers. So it falls on the government to find ways to change the compensation incentives that encouraged the kind of crazy risk-taking that got us into so much trouble" (Nocera 2009).

According to Nocera, there are three major problems in the structure of the banking industry that need remedying. First, there is an individualistic "eat what you kill" mentality. Thus, successful traders at banks still feel entitled to huge bonuses even if their bank lost billions. Second, reforming the compensation structure at the top will not fix this culture. There must a more systemic change to the entire compensation program. Third, once the regulations were modified to allow traditional banks to become investment banks and stock traders, banking evolved from a staid, conservative industry to one driven by enormous greed. Of course, enormous greed leads people to take enormous risks. It seems clear to us that Mr. Nocera is talking about a need for cultural and organizational change at financial institutions—less greed, more ethical behavior. Let us consider how that unethical behavior is encouraged and how change might be effected.

5. Where Did Wall Street Learn Business?—In American Business Schools

The vast majority of the managers at the insolvent financial firms, along with most other Wall Street executives, learned their trade and their basic outlook on the business world in our business schools, which teach the art of making money. In the course of that teaching, our business schools endorse an ideological framework and worldview that makes money the ultimate good, both from the viewpoint of the individual and from the viewpoint of an employee of a corporation. However, critics of business schools agree—there is something wrong with the business people who are products of our business schools. Pfeffer (2005) cites a number of studies that measure the deleterious effects of business schools on student values and behavior. He believes economic thinking, business school training and the business school environment are the sources of this problem.

Further, Sumantra Ghoshal's critique of business schools and its companion articles in the prestigious journal *Academy of Management Learning and*

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Education identify the corporate and institutional consequences of what they see as "bad management theories". The authors of these articles blame business schools for creating and proliferating these "toxic" theories (Ghoshal 2005; Pfeffer 2005; Hambrick 2005; Kanter 2005; Donaldson 2005; Kilmoski 2005; Nord 2005; Gapper 2005; Mintzberg 2005). These theories have emerged from business school academics over the last thirty years and many respected experts on global management practices agree that these same theories are the causes of the worst excesses in recent management practices in the business world (Ghoshal 2005, p.75).

According to Ghosal, "While within individual fields, such as organization theory or strategic management, authors can and do publish research grounded in very different assumptions and traditions, Friedman's version of "liberalism" has indeed been colonizing all the management-related disciplines over the last half-century. The roots of the ideology lie in the philosophy of radical individualism articulated, among others, by Hume, Bentham and Locke. While the philosophy has influenced the work of many scholars in many different institutions, its influence on management research has been largely mediated by the University of Chicago. It is in and through this institution that "liberalism", as Friedman called it, has penetrated economics, law, sociology, social psychology and most other core disciplines, yielding theories such as agency theory, transaction cost economics, game theory, social network analysis, theories of social dilemmas and so on, that we now routinely draw on both radical individualism and Friedman's 'liberalism', to frame our research and to guide our teaching" (Ghoshal 2005, p. 84).

6. The Vast Influence of the Chicago School of Economic Thought

The legacy of the Chicago School of Thought is the pessimistic, over-simplifying assumptions that underlie our economic teaching and our management theories, according to Ghoshal. These include: 1) the behavioral assumption of radical self-interest of individuals; 2) that morals, other than obeying the law and corporate policy, have no place in corporate management; 3) that profit maximization is the only proper goal of managers and 4) that humans are imperfect and thus we must create organizations that prevent bad people from doing harm as much as enabling good people to do good. However, as Ghoshal points out, unlike theories in the physical sciences, theories in the social sciences are often self-fulfilling. That is, if a cosmologist believes that the sun goes around the earth, this does not change the physical fact. However, a mangement theory that states that individuals are merely self-interested and opportunistic will cause managers to adapt their behaviors and treat them that way. This has been shown, according to Ghosal, to induce employees to acutally become more opportunistic and less trustworthy.

> ....this is precisely what has happened to management practice over the last several decades, converting our collective pessimism about managers into realized pathologies in management behaviors (Ghosal 2005, p. 77).

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Admittedly, there have been a few challenges to Ghosal's viewpoint (e.g., Neubaum et al. 2009). However, despite these contrary opinions, a large number of distinguished mainstream economists, management experts and business journalists have quite recently voiced deeply considered opinions quite similar to Ghoshal's. We will discuss the most important ones in this article and offer some solutions to this "toxic teaching" in our busines schools.

7. The Chicago School of Thought as Ideology, Not Science

Folger and Salvador (2008) believe that theory, research, and teaching based on an assumption of universal, unbridled self-interest are themselves some of the contributing causes of excesses that not only have led to the global financial crisis but inevitably lead to scandal. Further, they think that the central tenent of this approach is more of an ideology than a scientifically grounded basis for research and theory. The central tenet of this school of thought is that when traced to its roots, behavior can have no cause other than self-interest.

8. Evidence of Unethical Behavior: Cheating in Business Schools

McCabe and Treviño have focused the majority of their academic research on ethical behavior by students and by individuals in business organizations. In previous studies, they found significantly higher levels of cheating among undergraduate business students than among their university peers (McCabe and Treviño 1995). Further, their most recent study of over 5000 graduate students at 32 colleges and universities over two consecutive academic years found that 56% of graduate business students—mostly MBA students—admitted to having cheated at least once in the past academic year. Only 47% of their non-business school peers admitted to cheating (McCabe, Butterfield and Treviño 2006).

McCabe and Treviño found that their correlation analysis showed cheating to be associated with perceived peer behavior, as well as the perceived certainty of being reported by a peer, and the understanding and acceptance of academic integrity policies by students and faculty. However, their regression analysis results suggest that perceived peer behavior has the largest effect.

These authors conclude, "In today's post-Sarbanes–Oxley environment, businesses are expected to create strong ethical cultures, to monitor employee conduct, and to create programs and processes (e.g., reporting systems) that support compliance with laws and regulations. At a minimum, business schools should be attempting to do the same. There is some evidence from undergraduate students (McCabe, Treviño and Butterfield 1996) to suggest that having experienced such a culture in school can help to prepare students for their organizational experiences" (McCabe, Butterfield and Treviño 2006).

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9. Elite Busines Schools Agree That There Is a Problem

Additional support for our hypothesis has come from elite business schools themselves. In recent years, more than 40% of the graduates of the top business schools have entered the world of high finance. These schools are beginning to wonder what role they had in the global financial crisis. “It is so obvious that something big has failed,” says Ángel Cabrera, dean of the Thunderbird School of Global Management. “We can look the other way, but come on. The CEOs of those companies, those are the people we used to brag about. We cannot say, ‘Well, it wasn’t our fault’ when there is such a systemic, widespread failure of leadership” (Holland 2009).

Jay O. Light, the dean of Harvard Business School, argues that there have been imbalances both on campuses and in the economy. “We lived through an enormous extended period of financial good times, and people became less focused on risks and risk management and more focused on making money”, he said. “We need to move that focus back toward the center”. Further, Rakesh Khurana of Harvard Business School states, “A kind of market fundamentalism took hold in business education. The new logic of shareholder primacy absolved management of any responsibility for anything other than financial results” (Holland 2009).

10. Today’s Business Executives are Merely “Hired Hands”

Rakesh Khurana is Associate Professor of Organizational Behavior at Harvard Business School. His recent book, *From Higher Aims to Hired Hands,* is an extensively researched and deeply pondered history of American business schools, with prescriptions for improving them. Khurana shows that at the outset, the founders of business schools intended to create training for professional managers in the mold of doctors and lawyers. Unfortunately, today’s elite schools have abandoned that noble vision and have become merely peddlers of a very profitable product—the MBA—with students being treated as customers (Khurnana 2007).

> While today’s college presidents, faculties and administrators express dismay at the utilitarian and careerist outlooks of their students, their institutions offer no effective counterforce. As Harvard’s Lewis observes, “Students become customers to be placated, rather than whole beings challenged to stand on their own” (Khurana 2007, p. 367).

Khurana further feels that the failure of educational institutions to train managers as professionals in the true sense of the word has had disastrous consequences for business and for the individuals themselves. The essence of professions, he contends, lies in their status as communities with shared knowledge, standards of practice and norms of conduct. In sum, professionals

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practice discipline, self-restraint and a willingness to renounce self-interest to preserve the good name of the professional community and to advance the greater good.

> …By demoting managers from professional stewards of the corporation's resources to hired hands bound only by contractual requirements and relationships, business schools thus helped create the conditions and standards of behavior through which the market-based mechanism of stock options was turned into an instrument for defrauding investors, jeopardizing the livelihoods of employees and undermining public trust in managers and corporations (Khurana 2007, p. 374).

Khurnana contends that teaching in today's business schools has lost not only the religious framework of the modern university's founders but also has no shared agreement on basic societal values and morals. There are two important consequences to this. The first is that the stated missions of today's universities are nothing more than empty rhetoric—"leadership" or "excellence". Secondly, the universities are now apt to turn out "loose individuals"—persons who feel they are not constrained by social norms, including ethical norms and who have no allegiance to institutions such as nations, firms or jobs. According to Khurana, then, we should therefore not be surprised at the rise of corporate malfeasance. This is because the corporate world is now structured such that managers are merely hired hands who buy and sell corporate assets. Even CEOs are now hired hands who are loaded with stock options and golden parachutes that make sure their loyalty is to the shareholders and not the customers, employees or the community. However, the current structure has an extremely high personal price. It makes it impossible for work and careers to have any real meaning.

> Ultimately, from the viewpoint of an aspiring manager, the most pernicious effect of agency theory's perspective on management has been to drive out any possibility of managers' deriving meaning from their work or creating meaning for others, for that matter. As sociologists, anthropologists and psychologists all recognize, human beings seek meaning; it is as fundamental to human existence as the search for material sustenance. In traditional societies, religion, family and community satisfied this need for meaning (Khurana 2007, p. 382).

An attachment to the institution of religion, or family or community brings with it answers to the questions, "Who am I?" and "What is the good life and the moral life?" Conversely, when the purpose, behavior and constraints of managers are defined solely by "maximizing shareholder value", it implicitly leads to amorality. This is because it is erroneous to claim that the dictum to maximize shareholder value is a value-free dictum. Rather, that dictum actually directs the manager to choose profits over people whenever there is a conflict between profit maximization and ethical considerations.

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11. Unethical Business Practices and Recessions

The book *Animal Spirits* (2009) by Akerloff and Shiller provides additional support for our hypothesis that "toxic teaching" in our business schools creates an underlying culture of selfishness and greed. George Akerlof of the University of California at Berkley is the recipient of the 2001 Nobel Prize in Economics. Robert Shiller of Yale is the author of the best-selling book about financial markets, *Irrational Exuberance,* and one of the founders of the field of behavioral economics. Their collaboration uses the insights of behavioral economics to challenge two economic myths: 1) the myth of individuals as rational utility maximizers and 2) the myth of the reigning free-market ideology of the past thirty years. According to Akerlof and Shiller, so long as humans in the real world do not fit the descriptive assumptions of neoclassical economics—that people are essentially rational, well informed and unemotional in their economic decisions—then government must play a regulatory role in certain important areas.

Akerlof and Shiller provide us with a great insight into the correlation between unethical management practices and recessions. They show how each of the past three U.S. recessions, including the curent one, involved corruption scandals. Further, these scandals played a role in determining the severity of each of these recessions (Akerlof and Shiller 2009, p. 29).

According to these authors, the Savings and Loan crisis, which was precipitated by deregulation and enabled by the junk bond financing of Drexel Burnham's Michael Milken, contributed significantly to the duration and severity of the 1991 recession. Likewise, in the 2001 recession, the bursting of the dot-com stock bubble and the accounting scandals at Enron, WorldCom, Health South, Adelphia and other public corporations destroyed faith in financial markets and contributed greatly to the recession. "People became fed up with financial markets in general and this attitude inhibited the economy far more than any other exogenous factor one can imagine operating at the time" (Akerlof and Shiller 2009, p. 35).

The current recession, which began in December, 2007, and has already become the worst recession since the Great Depression, was caused in large part by the collapse of the Collateralized Debt Obligations (CDOs) backed by sub-prime mortgages. A host of players cooperated in corrupt practices in the issuance and sale of these securities. Financial giants like Lehman Brothers and the debt rating agencies such as Standard and Poors contributed, as did independent and unscrupulous mortgage brokers, who sold mortgages to people who clearly couldn't afford payments and even entered fraudulent financial information on applications. The CDO disaster has already contributed to both the length and severity of the current recession, not to mention the human suffering it is causing as a result of foreclosed homes and lost jobs.

It is clear, according to Akerlof and Shiller, that the business cycle is connected to fluctuations in personal commitment to principles of good behavior

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and predatory activity. This is partly because in financial bubbles, enough individuals tend to think that "everyone is getting away with it" and therefore also engage in unethical behavior. However, financial innovation and cultural changes also create opportunities for corruption to arise. The invention of new financial instruments, understood neither by the general public nor by regulators, make it difficult to foresee potential negative consequences. Furthermore, beginning with the administration of Ronald Reagan and up to and including the current Global Financial Crisis, an extreme bias existed not only towards *laissez faire* government but also towards deregulation and lax enforcement of existing regulations. This opened the door for the aggressively competitive and predatory activities that brought us to this current recession (Akerlof and Shiller 2009, p. 39).

12. Are Business Schools Really to Blame? Yes!

Following the dot-com stock crash and the massive business scandals beginning in 2001 (Enron, WorldCom, Health South et al.), some soul searching took place at American business schools. Thoughtful schools felt their responsibility for shaping the practices and morals of their students. Many business schools introduced or expanded business ethics courses. A similar self-reflection is occurring again in the wake of the most recent global financial crisis. On the other hand, there are defenders of business schools, such as Francesca Di Meglio of *Business Week*, who state that many of the perpetrators of the latest crisis did not attend business schools, so they feel it is a stretch to blame the schools for turning out amoral executives (*The Week*, 12 June 2009, p. 46).

Unfortunately, what we will call the "DiMeglio Defense" is just plain naïve, according to Gillian Tett. Tett is the chief of global financial markets coverage for The Financial Times, the world's leading business newspaper. Her recent book, *Fool's Gold: How the Bold Dream of a Small Tribe at J.P. Morgan Was Corrupted by Wall Street Greed and Unleashed a Catastrophe,* recounts, in exhaustive detail, exactly how Collateralized Debt Obligations were invented at J.P. Morgan and then how they spiraled out of control to create the global financial crisis (Tett 2009).

Tett reports that the creators and purveyors of the Collateralized Debt Obligations that brought the financial world to its knees were in fact almost exclusively MBAs or economics graduates of the world's elite business schools. These degrees were the price of entry to J.P. Morgan and the other Wall Street investment banks that effectively engineered the global meltdown.

Tett holds a doctorate in Social Anthropology from Cambridge University, so she takes a multi-disciplinary view of the crisis. Like many other critics, she contends that the single-minded pursuit of money to the exclusion of any wider social goals was one of the main causes of the financial crisis and what is wrong with the world of finance. In most societies, according to Tett, elites try to

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maintain their power not simply by garnering wealth, but also by dominating the mainstream ideologies, in terms of both what is said and what is not discussed. Social 'silences' serve to maintain power structures, in ways that participants often barely understand themselves, let alone plan. This ideological dominance is exactly what ocurred in the recent rounds of deregulation, beginning with Ronald Reagan and culminating in George W. Bush's administration (Tett 2009, p. 252).

Tett's discussion of ideologies is especially informative to our hypothesis. As the size of the derivatives market ballooned into the billions, J.P. Morgan leveraged manpower, money and aggressive tactics for attacks against various attempts to regulate the derivatives industry during both the Clinton and Bush administrations. Using libertarian ideologies espoused by economists like Friedman and Hayek, the banking lobbyists persuaded Congress, the Securities and Exchange Commission and two administrations that investment bankers could police themselves. They were significantly aided by Fed Chairman Alan Greenspan, who lobbied in Congressional hearings for increased deregulation in financial markets and vigorously espoused the belief that free markets would self-regulate (Krugman 2009; Goodman 2008). In line with this, we feel it is important to point out that Alan Greenspan was not just an advocate of Milton Friedman's libertarian philosophy, but a worshipful disciple of Ayn Rand, author of *Atlas Shrugged* and founder of the philosophy of selfishness called "Objectivism" (Tett 2009).

In support of our contention, Tett reports that Mark Bricknell, one of J.P. Morgan's leaders in the banking industry's extended lobbying efforts, found derivatives so "thrilling" precisely because they were outside the purview of regulation. "I am a great believer in the self-healing power of markets," Bricknell often said, "Markets can correct excess far better than any government. Market discipline is the best form of discipline there is" (Tett 2009, p. 32).

13. The Death of The Chicago School's "Self-Regulating Free Market" Hypothesis

As the crisis has persisted into the end of 2009, most economists have concluded that the Friedman, Hayek and Greenspan ideology of self-regulating, efficient markets has now been proven disastrously wrong. A leading proponent of this ideology, Alan Greenspan testified October 24, 2008, before a Congressional Committee investigating the financial crisis, admitting the worldwide financial crisis had left him "in a state of shocked disbelief…I made a mistake," he said, in assuming "that the self-interest of organizations, specifically banks" would keep them from taking on excessive risk (*The Week,* 7 November 2008). Unfortunately, according to extensive interviews Tett conducted with the J.P. Morgan team, the creators of these financial derivatives lack regrets similar to Greenspan's—they blame everyone else (Tett 2009, p. 247). Consequently, the public has good reason to fear this lack of remorse, since these businessmen and women are now working at, and leading, other investment banking firms.

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14. How Self-Interest Destroys Great Companies

We contend not only that the free market hypothesis is fatally flawed, but also that selfishness destroys great companies. Management guru Jim Collins' latest book, *How the Mighty Fall,* deals with great companies that have recently declined precipitously. From his firm's research data on thousands of companies, Collins selected for study eleven once-great companies that had declined significantly, some to the point of bankruptcy. These included well-known firms such as A&P, Circuit City, Merck, HP and Motorola. Collins concluded that organizational decline "is largely self-inflicted…I've come to see institutional decline like a staged disease: harder to detect but easier to cure in the early stages, easier to detect but harder to cure in the later stages. An institution can look strong on the outside but already be sick on the inside, dangerously on the cusp of a precipitous fall" (Collins 2009, p. 3).

We introduce the model that Collins and his team have constructed from their research because it has significant lessons to teach us about the global credit crisis and also important lessons for educators of business ethics. The decline and/or fall of once great companies has five stages.

Stage 1: "Hubris" (Excessive Pride), Born of Success
Stage 2: Undisciplined Pursuit of More
Stage 3: Denial of Risk and Peril
Stage 4: Grasping for Salvation
Stage 5: Capitulation to Irrelevance or Death

According to Collins, these five stages are not independent of one another but are interconnected. "Stage One Hubris leads to Stage Two Overreaching, which sets the company up for Stage Three, Denial of Risk and Peril" (Collins 2009, p. 68). Hubris encompasses behaviors such as viewing success as deserved—rather than earned or even fortuitous—and that the success is entirely due to the firm's leadership. This leads the company to feel they can succeed at any venture, no matter the risk.

The second stage of the disease is an obsession with growth for growth's sake. This is a huge mistake, according to Collins. "Public corporations face incessant pressure from the capital markets to grow as fast as possible, and we cannot deny this fact. But even so, we've found in all our research that those who resisted the pressures to succumb to unsustainable short-term growth delivered better long-term results by Wall Street's own definition of success, namely, cumulative returns to investors" (Collins 2009, p. 54).

However, just the opposite occured in the firms that caused the global financial crisis, according to Collins. One of the defining markers of Stage Two is the placing of personal interests above organizational interests. This was exactly the culture of Wall Street just before the crash. "People in power allocate more for themselves or their constituents—more money, more privileges, more

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fame, more of the spoils of success—seeking to capitalize as much as possible in the short term, rather than investing primarily in building for greatness decades into the future" (Collins 2009, p. 64).

Stage Three is the denial of risk. In the current crisis, the housing bubble was inflating at unprecedented rates that were clearly not sustainable. However, it is clear that the large financial institutions neither seriously thought that housing prices would decline nor risk-managed the possibility that they might.

Collins presents empirical proof that hubris and greed destroy good companies. Conversely, his research shows that the positive leadership qualities of humility and prudence are leadership traits that make good companies great. Therefore, we feel that holistic ethical education in our business schools can have a great impact on counteracting some of the factors that Collins' research shows can destroy a company. This includes instilling the positive traits of humility, patience, sustainability and prudence over hubris, overreaching, greed and recklessness.

15. The Personal Consequences of a Materialistic Value Orientation

It seems clear to many critics that business schools endorse materialistic greed and financial well-being over all other goals. That focus on profit and the acquisition of wealth as the most important purpose in business changes the *weltanschauung* of their students (Giacalone 2004). They often become primarily driven to achieve power, status and money. The result of this orientation, which is pervasive yet concealed, is business people who value material success and status as a top priority in their lives and who as a result are quick to choose money over ethical behavior.

Furthermore, we contend that individuals with a Materialistic Value Orientation will have psychological problems, family dysfunctions, health problems and possibly personal financial problems. The evidence for this is voluminous and robust. (See Kasser and Kanner 2004.) In the bigger picture, the damage is in how these attitudes are then major contributors to social problems that undermine the fabric of our society. These attitudes even contibutrute to world discord, as the exportation of American materialism emphasizes the gulf between the "haves" and the "have-nots" around the globe.

16. The Neuroeconomic and Psychological Consequences of Money

As we previously mentioned, Treasury Secretary Geithner pointed to misguided compensation packages as one of the major causes of the global financial crisis. His criticisms are quite accurate, since money can be the motivation for very unethical and aberrant behavior.

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The most recent research about the effects of money on individuals comes from the fields of Neuroeconomics and Psychology. These studies show just how powerful a force money is. Therefore, it is critically important to take the power of money explicitly into account when thinking about how to best use it as an incentive in management and in how it affects business ethics. Many psychologists and economists present research to show that money can easily become addictive (Layard 2005, p. 225; Peterson 2007, p. 77). This is because the human brain constantly engages in what is called "hedonic adaptation". When we reach a higher level of income, we initially derive satisfaction from it. However, very soon, we adapt mentally and emotionally to that level and need even more money to achieve the same level of happiness. Therein can lie the addiction. By the same mechanisms through which the human brain can succumb to addiction to drugs, alcohol or gambling, people can become addicted to money.

Current theory about the psychological consequences of money characterizes money as both a "tool"—an interest in money for what it can be exchanged for—and a "drug"—an interest in money for itself (a maladaptive function) (Lea and Webley 2006). This theory emphasizes that people not only value money for its instrumentality—that is, money enables people to achieve goals without aid from others—but also for itself—that is, for the totally false sense of control, security and power that it gives (Vohs et al. 2006). Conversely, Price et al. (2002) have shown that physical and mental illness after financial strain due to job loss is triggered by reduced feelings of personal control.

In addition, there is another level of dissatisfaction that the emphasis on profit maximization at business schools creates. Combined with absorbing modern society's emphasis on money and status, there is also now a perception among the younger generations that they will not be better off, nor even as well off, as their parents were. The extensive research on this subject shows that they are, on average, correct (Brookings 2007; Pew 2007). Both this expectation and their relative economic inequality significantly decrease their subjective wellbeing (Luttmer 2005). In response to this frustration, Generation Y is no longer willing to define their life as showing up for work every day to punch the clock. Instead, they want meaningful life experiences and ask what the company can do for them (*Economist,* 2008; *Wall Street Journal,* 2008).

17. Inculcating Materialism and Selfishness through Management Education

In the United States, where business schools were founded, these schools eventually created a multitude of materialistic legacies for future generations of Americans (Leach 1993). The assumptions and legacies still exist today: 1) An institutional legacy of corporations and investment and commercial banks deeply entwined with and influencing business schools, commercial art schools, museums, universities, and the Federal government; 2) The concept of the human

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being as an insatiable, desirous machine or as an animal governed by an infinity of desires—that what is most human about people is the quest for "new" and "more"; 3) The myth of the separate world of consumption as the domain of freedom, self-expression, and self-fulfillment, that consumer moments are liberation, or the means to happiness and 4) The conception of an unbounded consumer market.

We feel these legacies and ideas that we pass on have changed the core values of students who are educated in our business schools. As evidence of this, an Aspen Institute study found that during the two years that students spent in MBA programs, their values changed—enhancing shareholder value became more important and customers and employees became less important (Aspen 2001). Another study has shown that the correlation between firm size and corporate illegal activity becomes stronger as the percentage of top management team members possessing an MBA degree increases (Williams et al. 2000).

These assumptions underlying our business schools' approach accordingly lead to a number of toxic aberrations (Ghosha, 2005). First, they leave no room for ethics, as determinism does not allow for human intentionality—the essence of ethical choice. Second, they have myopically narrowed the purpose of managers to Friedman's dictum of "maximizing shareholder value" (Friedman 2003). Third, their gloomy view of the opportunistic nature of humans leads to more and more controls put on employees actions and less latitude allowed in their decision-making. Unfortunately, the path breaking work of Rose and his research colleagues has shown that this manner of treating employees, particularly in the managers' controlling attitudes and the lack of control of employees over their own actions at work literally makes them physically and psychologically ill and causes them to die prematurely (Rose and Jenkins 1978; Rose and Fogg 1993; Ming, Rose et al. 2004).

18. Summary

In summary, what is the overall impact on our students of this toxic teaching? First, with what we are teaching in American business schools, we are magnifying and exacerbating some destructive social values that exist in our society. These destructive values include materialism and "dog-eat-dog" individual and corporate competition.

Secondly, we are also undermining important human moral values—freedom and hope—by substituting for them the values underlying our current management theories, which are, according to Ghoshal, amorality, determinism and pessimism. We agree with Ghoshal that whereas economics makes a strong claim to objectivity, none of the social sciences is more values-laden than economics and all its derivatives, including much of the theories of modern finance and management (Ghoshal 2005, p. 83).

Thirdly, by emphasizing profit-maximization as the goal of the corporation to the exclusion of all other goals and self-interest as the goal of the individual, we

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are undermining important social values that are essential to keeping the fabric of our society “of a whole cloth”. This emphasis is killing cooperation, compassion, forgiveness, generativity and other important social values.

19. Some Solutions: How Do We Detoxify Teaching in Our Business Schools?

A. Teach Values Educatioin and Weed Out Bad Candidates

We are happy to report that a number of the elite business schools are trying to change their business school teaching. The Aspen Institute, in conjunction with Yale School of Management, has developed a curriculum that aims to train students in how to act on their values at work, including social and environmental values. Thus far, approximately fifty-five business schools are running pilot programs based on this curriculum.

Also, Sharon Oster, the new Dean of the Yale School of Management, has called for a renewed focus on the social value of management. “Business creates value in terms of services and products,” she said. “That’s what business delivers, just like medicine delivers a healthy person.” (Holland 2009)

Admittedly, there are students who only care for themselves and for the fast track to the corporate jet and stock options but they should be excluded from business school admission. One institution that already does this weeding out is Berkeley’s Haas School. Peter Johnson, the school’s director of admissions told *Economist.com* that he believes the best approach is to look for applicants who are not only smart, accomplished and ambitious but who also reflect the solid ethical values of the program. “It’s OK to make money, he says, “We just want our students to understand how to do it responsibly” (*Economist.com,* 29 June 2009).

B. Teach Synthesis and Positive Organizational Scholarship

How should we change our business school teaching? Ghoshal recommends a series of far-ranging changes that could, in his opinion, counteract the toxicity of our current business school teaching (Ghoshal 2005, p. 82). One change is his call for “pluralism” in our schools—admitting those whose primary scholarship interests are in synthesis, application and pedagogy and not just analysis. Another recommendation is research into the underlying assumptions of management theorists and how these assumptions bias their theories. A third recommendation is further research and implementation of Positive Organizational Scholarship (“POS”), which is focused on the study of the positive outcomes, processes and attributes of organizations (Ghoshal 2005; Cameron, Dutton and Quinn 2003).

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C. Teach the Insights of Behavioral Economics into Human Nature

Samuel Bowles of the Santa Fe Institute presents further evidence of the need for a new direction in business school ideology. Bowles reviewed all the recent experimental studies in Behavioral Economics and concluded that managerial programs based solely on economic incentives, "may be counterproductive when they signal that selfishness is an appropriate response, constitute a learning environment through which over time people come to adopt more self-interested motivations, compromise the individual's sense of self-determination and thereby degrade intrinsic motivations, or convey a message of distrust, disrespect and unfair intent" (Bowles 2008).

According to Bowles, the latest experimental research shows that people act not only as *homo economicus*—that is to acquire goods and services—but also to constitute themselves as dignified, autonomous and moral individuals. Therefore, incentive systems that rely only on self-interest, often lead to unintended and negative consequences. As we have stated above, the underlying assumptions of contemporary management theory are still those of Economics, the "Queen of the Sciences". Although mainstream neoclassical economic theory still currently assumes humans are solely self-interested in all their actions, a host of experiments in Behavioral Economics are showing these assumptions to be false or at least too simplistic.

Folger and Salvador argue even more vociferously against the assumption of self interest as the base explanation for all human behavior in management theory (Folger and Salvador 2008). After presenting evidence from philosophical literature and the disciplines of management science, social psychology and behavioral economics, they argue that self-interest should be only one of a number of possible theoretical explanations for specific human behaviors. In fact, it should not be the default assumption in explaining human behavior, as this leads to a strong confirmation bias—"If the only tool you have is a hammer, everything looks like a nail". Rather, selflessnes, cooperation, altruism, along with self-interest, should be given equal chances as the accurate model of specific human behavior.

Further, Akerlof and Shiller set forth in great detail the wide range of motivations and behaviors that humans show in making economic decisions. These include not only rational self-interest, but also irrational behavior and non-economic motivations. They term these behaviors and emotions—which are not considered by neoclassical economics—"animal spirits", borrowing a term from John Maynard Keynes, the founder of modern economics. These well-established animal spirits include overconfidence and under-confidence, our sense of fairness, greed and opportunities for corruption, our susceptibility to "money illusion" and the stories handed to us by others that shape our culture (Akerlof and Shiller 2009, p. 176). According to these authors, the economy cannot be adequately explained without incorporating these animal spirits into our models, particularly in times of crisis. We would add that understanding and influencing

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the ethical behavior of individuals in business settings will continue to be lacking until these animal spirits—that is emotions—are taken into account in our models.

D. Finance Needs a Holistic Approach

Gillian Tett also has recommendations for fixing the world of finance that has direct relevance to our business school teaching. She believes that in order to restore sanity to the world of finance, that policy makers, bankers and politicians must adapt a more holistic view of finance—a return to the seemingly dull but traditional banker virtues of prudence, moderation, balance and common sense.

> …In the last two decades, as finance has spun out of control, it stopped being a servant of the economy, but became its master. That must be reversed….money is also a vital fluid that must flow freely and safely throughout our fragile, interconnected world (Tett 2009, p. 254).

E. Make Business a Profession

In a very popular and much-discussed article in *The Harvard Business Review,* Khurana and Nohria (2008) propose one major solution to the problems we have discussed. They argue that we should make business a *profession.* This is what, according to these authors, was the original vision for business schools—that they would be professional schools exactly like medical schools and law schools. Business professionals, as trustees of society's economic resources—like other true professionals—should have a code of conduct that is taught as part of their education. They should also have a governing body of respected members that oversees member compliance to the rules of the profession.

As a matter of fact, Khurana and Nohria take the exact *opposite* position to Milton Friedman's view of managers as solely agents of a company's stockholders. "Managers, in our view, must be agents of society's interest in this endeavor. We further contend that society grants to corporations the status of legal persons in order to hold them accountable for their conduct, as any individual citizen would be … It is thus best for managers to have a higher-order purpose—viewing society as their ultimate client and society's interest in vibrant, sustainable, value-creating enterprises as their foremost objective" (Khurana and Nuria 2008, p. 70).

F. Reformulate the Foundational Assumptions of Economics

Stephen Marglin, in *The Dismal Science* (2008), calls for a solution to "toxic teaching" by reformulating what he calls the "foundational myths" of economics.

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Like most disciplines, economics suffers from a common disease. It has taken its methodology and turned it into a dogma. Therefore, whatever cannot be measured by the tools of economics doesn't count or doesn't exist, Marglin says. He calls for the rejection of 1) the ideology of rational knowledge in favor of one that gives greater weight to experience, or to spirituality; 2) the primacy of the individual in favor of the essential relationships that constitute community and 3) the primacy of the national community in favor of the legitimate claims of local communities. "If we start from a different set of assumptions, we may well discover a different set of priorities for ourselves and for our children" (Marglin 2008, p. 263).

Since each of us is emotionally invested in our own discipline, we all are subject to a myopia that can blind us to the shortcomings of our methodology. This is what Marglin is pointing to in the case of economics. However, even though this short-sightedness is difficult to overcome, one sure way we have found to overcome it is to approach problems with an interdisciplinary methodology. Without going into great detail here, as it is beyond the scope of this paper, we will mention some of the interdisciplinary fields in economics that are yielding valuable insights. These include neuroeconomics, behavioral economics, economic anthropology and economic psychology.

G. Commit to a Culture of Integrity in Business Schools

McCabe et al. (2006) believe that the best solution to unethical behavior is what they call "ethical community building". This moral socialization emphasizes clear communication of rules and expectations, creation of normative pressures, commitment to pro-social values and norms and mutual respect. This approach is the most effective, the authors believe, not only for changing the cheating culture in business schools but also for changing the cheating culture in corporations. "The ethical community-building approach involves creating a 'culture of integrity and responsibility' within the academic program. Such a culture of integrity and responsibility has been found to be effective in undergraduate education and at least some of these ideas should be applicable to graduate business education…. Further, ethical context (climate and culture) has been found to influence ethical/unethical behavior in corporate settings as well" (McCabe, Butterfield and Treviño 2006, p. 302).

H. Teach Character and Virtue in Our Business Schools

Management guru Jim Collins also weighs in on this matter in *How the Mighty Fall* (Collins 2009). His work on corporations that have achieved greatness and remained great and his recent study of once-great corporations that have declined or failed present us with good lessons for business schools. Great leaders—whom he terms his "Level Five Leaders"—are both humble and generous. "Level Five

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leaders are ambitious first and foremost for the cause, the organization, the work —not themselves—and they have the fierce resolve to do whatever it takes to make good on the ambition. A Level Five leader displays a paradoxical blend of personal humility and professional will" (Collins 2009, p. 180).

Further, great leaders instill a culture of important values throughout their organizations: discipline, brutal honesty and patience. They realize and teach that greatness is more important than growth and that constant adherence to the organization's timeless core values is what creates greatness—even as strategies must change to respond to new challenges. These winning virtues are all character traits that we can instill and enhance in a holistic business school education that emphasizes the importance of values.

We believe that values education, spirituality, creating an ethical culture, transcendent belief and connection to something bigger than ourselves, are the most effective antidotes for greed, unethical behavior and status anxiety. Dean Hamer, a world-renowned geneticist has recently done extensive research on spirituality. He contends that by analyzing the genetic makeup of over 1,000 diverse subjects, he has identified a specific "God gene" that influences spirituality (Hamer 2004). He argues that spiritual belief offered evolutionary advantage by providing humans with a sense of purpose and the courage and will to overcome hardship and loss. It also increases our chances of reproductive survival by helping to reduce stress, prevent disease and extend life.

There is strong evidence for the "fitness" value of spirituality from a recent study completed by the Rush University Medical Center in Chicago. Boyle and colleagues studied over 1200 elderly people without dementia in community living facilities. (The average age was 78 +/- 7.8 years.) Each was tested for perception of a purpose in life. These authors report that a number of studies have shown the association of a higher purpose in life with positive psychological outcomes—happiness, satisfaction and self-esteem. However, the researches tested the hypothesis that a higher purpose in life would bring longevity. In a five-year follow-up of their subjects, the researchers found that those with a higher purpose in life had approximately one-half the probability of dying than those with a low score on purpose in life tests. The researchers adjusted or tested for various confounding demographic factors, so age, sex, education, income and race had no effect on the results. "The finding that purpose in life is related to longevity in older persons suggests that aspects of human flourishing—particularly the tendency to derive meaning from life's experiences and possess a sense of intentionality and goal-directedness that guides behavior—contribute to successful aging" (Boyle et al. 2009, p. 577).

Boyle and colleagues also present in this same paper a number of studies showing that a higher purpose in life is associated with lower stress-indicating biomarkers and speculate that this is likely the biological connection. Finally, on the practical side, Giacalone and Jurkiewicz (2003) have provided multidisciplinary perspectives on the relationship between transcendent views and organizational outcomes, both financial and value-related.

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20. Conclusion

Our studied conviction is that great business leaders must have *character* rather than just *charisma*. This is foundational to leadership that creates long-term success in organizations. What is character? It is the basically the practice of virtue. And there are six virtues that are ubiquitous in all the great works of religion and civilization: Wisdom and Knowledge; Courage; Love and Humanity; Justice; Temperance; Spirituality and Transcendence (Seligman 2002, p. 133). Students enter our business schools with at least a minimum practice of these virtues, since they are ingrained in human nature. However, the *praxis* of virtue is strengthened by making them habits. Business schools can go a long way, in our opinion, in inculcating the habit of using these virtues in making business decisions. Then, if they become habits, they will exert greater influence on business decisions than the default option of profit maximization at any cost.

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