

A behavioral theory of the firm

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Understanding the Behavioral Theory of the Firm**

Introduction

The behavioral theory of the firm is an approach to understanding how firms make decisions and behave. It emphasizes the influence of human behavior, bounded rationality, and organizational processes on decision-making.

Herbert Simon's Theory of the Firm

Herbert Simon, a Nobel Prize-winning economist, developed the behavioral theory of the firm in his book "Administrative Behavior" (1947). According to Simon, organizations are complex systems where individuals make decisions under conditions of bounded rationality. This means that decisions are made with limited information, time, and cognitive abilities.

Simon's Four Theories of the Firm

Simon proposed four theories of the firm to explain how firms make decisions:

- **Routines and Habits:** Firms develop routines and habits that simplify decision-making and reduce uncertainty.
- **Satisficing:** Firms search for solutions that are "good enough" rather than optimal, given their limited resources.
- **Bounded Rationality:** Decisions are constrained by the cognitive limitations of individuals and the information available.
- **Organizational Goals:** Firms have multiple goals that may conflict with each other, such as profit maximization and employee satisfaction.

The Behaviorist Model of Cyert and March

James Cyert and Richard March expanded on Simon's theory in their 1963 book "A Behavioral Theory of the Firm." They developed a model that includes elements of:

- **Organizational structure:** How responsibilities are distributed within the firm.
- **Standard operating procedures:** Established procedures that guide decision-making.
- **External environment:** Factors outside the firm that influence its behavior, such as competition and regulation.

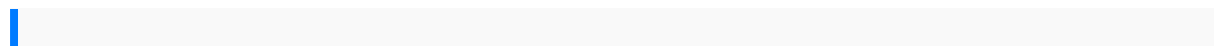
Behavioral Theory vs. Other Theories of the Firm

The behavioral theory of the firm differs from other theories, such as:

- **Neoclassical Theory:** Assumes that firms are rational actors who make profit-maximizing decisions.
- **Keynesian Theory:** Emphasizes the role of demand-side factors in firm behavior, such as investment and consumption.
- **Marxist Theory:** Views firms as part of a capitalist system that exploits workers.

Conclusion

The behavioral theory of the firm provides a more nuanced understanding of firm behavior by accounting for the influence of human behavior, bounded rationality, and organizational processes. It suggests that firms make decisions that are influenced by a range of factors, including cognitive limitations, routines, and organizational goals, rather than acting as purely rational actors.



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