

# Microfoundations in Management Studies

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## Abstract

Little consensus exists on the definition of microfoundations in management studies. This paper proposes a simple definition of microfoundations in management studies from a practical point of view as comprising involvement of and interactions between individuals that entail value creation at a firm. This involvement should include every individual within an organization. For interactions to be successful in terms of value creation, both leadership and common goals (visions and missions statements) are important. This definition will be supported by drawing on the literature and practical examples to illustrate its functional effectiveness and practicality. Since this definition, with its description and examples, includes important factors of organizational performance, practitioners could use it while planning, reviewing, and implementing strategies.

**Keywords:** microfoundations, organizational performance, value creation

## Introduction

As Barney and Felin (2013) state, little consensus exists on the definition of microfoundations in the fields of organization theory, management, and strategy. There are different views such as applying individual concepts at the firm level and focusing on the role of structure and simple rules in

dynamic environments. As Devinney (2013) states, there also exist different perspectives, ranging from arguments that microfoundations are a distinctive theoretical paradigm (Barney and Felin , 2013) to a skeptical extreme that compares microfoundations to the failure of economics in linking microeconomic foundations to macroeconomic theory (Winter , 2013 ). However, clarification in this regard has progressed owing to the proposition by Barney and Felin (2013 ), who argue that social aggregation and emergence need to be emphasized while discussing microfoundations. Building on Barney and Felin (2013 ), this article aims to propose a simple definition of microfoundations from a practical point of view, namely, that of value creation at a firm, since a firm's primary purpose is to create value (Nonaka and Toyama , 2007 ). Since this definition, with its description and examples, comprises important factors of organizational performance, it could be useful to practitioners who have to promptly struggle with real problems, which may undergo daily, dramatic changes, while planning, reviewing, and implementing strategies.

## **Definition of Microfoundations in Management Studies**

### **Involvement of and Interactions between Individuals at a Firm**

In agreement with Foss and Lindenberg (2013) , I propose that microfoundations must involve individuals. In addition, drawing from the work of Barney and Felin (2013) , I contend that interaction between individuals should also be included in the definition of microfoundations, the rationale being that it is equally important for value creation in a firm. This wider view incorporates the assertion by Nonaka and Toyama (2007) that value can be created when one person perceives and interprets reality differ-

ently as compared with other people. Therefore, I propose that involvement of and interactions between individuals as part of the process of value creation at a firm should be adopted as the definition of microfoundations in management studies from a practical viewpoint. A theory that incorporates the idea of microfoundations, as defined in this study, is the goal-framing theory proposed by Foss and Lindenberg (2013) and Lindenberg and Foss (2011).

In my view, the dynamic model of a knowledge-creating company proposed by Nonaka and Toyama (2005a) and Nonaka and Toyama (2007) also includes microfoundations as defined in this study. A successful practical example incorporating microfoundations seems to be the methodology utilized by Kazuo Inamori, the founder of Kyocera, who is known as the “God of Management” (Kagono and Yoshimura, 2012). Kyocera, which started with 28 employees in 1959, has consistently maintained a high profit ratio for more than 50 years. As requested by the Japanese Government, Kazuo Inamori, as the president, has also rebuilt Japan Airlines, which had gone bankrupt (Inamori, 2013). Inamori’s methodology, too, seems to include microfoundations, i.e., it utilizes the involvement of individuals and their interactions for value creation, as his methodology (named “Ameba Keiei” in Japanese) divides a firm into small organizations with a self-supporting management accounting system. This system ensures common management by a leader and other members of the small organization to enable each individual to function as a lead actor, suggesting that each individual acts like a manager with discretion and responsibility - a driving force in improving firm performance. About 400 companies have been advised in implementing the Inamori methodology, after which these companies greatly improved their performances (Inamori, 2010). Under this definition, social

interactions that lead to group-level pathologies such as social loafing, as stated in Barney and Felin (2013) , should be excluded from microfoundations because these interactions do not seem to foster value creation. Components of the definition will be discussed in greater detail below.

### **Individual should be the Stopping Point**

Barney and Felin (2013) point out a strand of argument alleging that microfoundations lead to infinite regress. However, in my view, neither the goal-framing theory (Foss and Lindenberg , 2013; Lindenberg and Foss , 2011) , nor the dynamic model of a knowledge-creating company (Nonaka and Toyama , 2005a) , nor even the Inamori methodology (Inamori , 2010) lead to infinite regress, but, apparently, place the individual as the stopping point, i.e. , the final discrete unit of action. Therefore, along with Barney and Felin (2013) , I argue that the individual should be the stopping point. Since reducing explanations to sub-individual levels of genes and brain activity is not likely to contribute to understanding the process of value creation, I agree with Barney and Felin (2013) , who state that such reductionism is not likely to fully inform the very practical day-to-day activities and behaviors of managers and individuals in organizations.

### **Every Individual in an Organization Should be Involved**

The goal-framing theory (Foss and Lindenberg , 2013) states that the top management as well as a broad scope of organizational members are involved in realizing an organization's goals. The dynamic model of a knowledge-creating company (Nonaka and Toyama , 2007) states that the scope of individuals involved encompasses every individual in the organization and not just a small group of elites. Further, the Inamori methodology (Inamori ,

2010) utilizes this methodology, stating that every individual should be a lead actor. These instances imply that every individual in an organization should be involved for value creation. Additionally, involvement of every individual in an organization could bring about more efficient use of resources. In other words, if only the top management or a small group of elites are involved, many other human resources are not well utilized since these uninvolved human resources tend to be under-motivated - a situation that the management allows to persist despite the fact that motivation seems to be critical for value creation according to the goal-framing theory (Foss and Lindenberg , 2013) . In contrast, under the Inamori methodology (Inamori , 2010) , which divides a firm into small sub-organizations, human resources seem to be well motivated since everyone can participate with responsibility and discretion.

### **Importance of Leadership for Successful Interaction of Individuals**

For interactions between individuals to successfully lead to value creation, leadership is very important. The goal-framing theory (Foss and Lindenberg , 2013) states that leadership has strategic importance due to the existence of a top-down process that elevates the goals of leaders and makes them influence employee goals. This prioritization of leader goals reflects the fact that leadership can foster the employees' motivation to take individual responsibility for reaching collective (i. e. , leaders') goals. This type of leadership has been identified as transformational leadership in, for example, Grant (2012) . The dynamic model of a knowledge-creating company (Nonaka and Toyama , 2005a) states that leadership plays various roles in the knowledge-creation process, such as (1) providing a vision , (2) developing and promoting the sharing of knowledge assets , (3) creating,

energizing, and connecting *ba* (a shared context in motion, in which knowledge is shared, created, and utilized) , and (4) enabling and promoting the continuous spiral of knowledge creation. Under the Inamori methodology (Inamori , 2010) , the leadership capabilities of a leader in the small organization is critical, since the leader has discretion and responsibility, similar to the president of a small or medium-sized firm. He plays a central role in the small organization, along with a self-supporting management accounting system that utilizes a profit-loss per hour table, which is an easy-to-understand table expressing the basic principle of management - namely, if sales are maximized and costs are minimized, value added (which is the difference between sales and costs) would be maximized.

### **Importance of Common Goals (Visions and Missions Statements) for Successful Interactions between Individuals**

For interactions between individuals to successfully lead to value creation, common goals (visions and missions statements; “ Keiei rinen ” in Japanese) are also very important. For example, the goal-framing theory (Foss and Lindenberg , 2013) states that, for increased value creation, both the top management and other organizational members should be included in a normative goal framework that expresses the desire to act appropriately in the service of an organization. Such a goal framework alone can sufficiently motivate the organizational members to engage in a truly collaborative activity; Lindenberg and Foss (2011) call this “ joint production motivation ” , wherein individuals see themselves as part of a joint endeavor, each with his or her own role and responsibilities, and as a result , (1) generate shared representations and tasks , (2) cognitively coordinate cooperation and choose their own behaviors in terms of joint goals, and (3) exert intelligent ef-

forts to reach joint goals. This theory (Lindenberg and Foss , 2011 ; Ashforth and Johnson , 2001) also states that a common direction can be achieved by utilizing a vision and mission statement that is consensually supported by the top management and focuses on a common purpose. An example of a mission, given in Foss and Lindenberg , 2013 , is that of LEGO, which asserts the firm's intention is " to help children develop their creativity and learning skills through constructive play. " The dynamic model of a knowledge-creating company (Nonaka and Toyama , 2005) includes a knowledge vision, which stems from the fundamental ontological question of the firm's *raison d'être*. The knowledge vision should inspire the intellectual passion of organizational members, thus encouraging them to create knowledge. An example of such a vision, given in Nonaka and Toyama , 2005, is that of Eisai, which is simply " human health care. " This vision allows Eisai's employees to recognize that the company sees itself as being on the side of patients and their families, and not that of doctors or pharmacists. Under the Inamori methodology (Inamori , 2010) , the mission (" Keiei rinen " in Japanese) of Kyocera is as follows: " Pursue happiness of all employees, both physically and mentally and contribute to the progress and development of society. " By this mission, Kyocera's *raison d'être* became clear, and consequently, employees began to work hard to achieve the common direction as if they themselves were managers (Inamori , 2010) .

### **What is a Firm ?**

A firm is an entity that produces goods and services (Odagiri , 2010) . Therefore, not only private enterprises but also nonprofit organizations, such as international organizations, universities, independent administrative agencies, and incorporated foundations, can be considered firms because

those organizations, too, seek to create value, which is a firm's primary purpose (Nonaka and Toyama , 2007) . An additional rationale is that practitioners in nonprofit organizations also have to promptly struggle with real problems that may involve daily, dramatic changes in the course of planning, reviewing and implementing strategies.

## **Other Related Issues**

### **Utilization of Concepts in Other Disciplines**

As Barney and Felin (2013) state, there is an argument that borrowed concepts can constitute microfoundations. However, the goal-framing theory (Foss and Lindenberg , 2013) does not solely comprise borrowed concepts but includes original concepts, such as joint production motivation, despite being based upon cognitive science, behavioral economics, and social psychology. Likewise, the dynamic model of a knowledge-creating company (Nonaka and Toyama , 2005a) does not solely consist of borrowed concepts but includes many original concepts developed from practical experience, although this theory does utilize philosophy. In contrast, the Inamori methodology (Inamori , 2010) was created directly from practical management experience and, therefore, does not utilize concepts borrowed from other disciplines. These three instances imply that borrowed concepts as well as original concepts contribute to value creation. Therefore, a more appropriate description should be that the utilization of concepts from other disciplines could contribute to microfoundations, but is not necessary. Barney and Felin (2013) also point out that some have argued for general or universal theories, in which theoretical concepts and mechanisms across levels and contexts are identical. However, as with Nonaka and Toyama

(2007) , who argue that finding a universal theoretical answer tends to overlook the element of strategy based on practice as it evolved within a particular context, I posit that this type of grand, universal theorizing tends to lack practical value.

### **Microfoundations do not Deny the Role of Structure**

As Barney and Felin (2013) state, there is an argument that microfoundations deny the role of structure as well as of other macro factors such as culture, institutions, and norms. However, goal-framing theory (Foss and Lindenberg , 2013) does not deny the role of structure but emphasizes the importance of governance structures for motivating joint production. In my view, the dynamic model of a knowledge-creating company (Nonaka and Toyama , 2005a) does not deny the role of structure because the knowledge-conversion process, i.e. , the socialization, externalization, combination, and internalization (SECI) process (Nonaka and Toyama , 2005a) , includes both, a multi-layered *ba*, which is an existential place for the SECI process, and the environment as an ecosystem of knowledge. The Inamori methodology (Inamori , 2010) does not deny the role of structure either, but rather emphasizes the importance of small organizations. These examples support the argument that microfoundations do not deny the role of structure, a perspective in keeping with that of Barney and Felin (2013) .

### **Actor is More Appropriate than Level of Analysis**

Greve (2013) distinguishes between level of analysis, which means the particular social unit at which the theoretical argument is posed, and the actor about whom the predication is made. In my view, Greve (2013) also argues that using level of analysis is more appropriate because, for example, in

game theory, the individual actor is the least interesting component of the theory. However, the goal-framing theory (Foss and Lindenberg , 2013) , dynamic model of knowledge creation (Nonaka and Toyama , 2005) , and Inamori methodology (Inamori , 2010) seem to focus on the actor. This indicates that examining individual actors is a more practical window through which the process of value creation can be examined. It should be noted that Greve (2013) states that viewing microfoundations from the actor level is a frequent and, perhaps, understandable interpretation.

### **Reasonable Models of Behavior Could be Close to Behavior Based on a Normative Goal**

Van de Ven and Lifschitz (2013) propose reasonable models of behavior as microfoundations. They view reasonable behavior based on jurisprudence and institutional theory as being collectively-defined appropriate behavior for specific roles and circumstances that can meet collective standards of prudent, reasonable persons. Although these two theories are grounded in different disciplines, such definition of reasonable behavior is similar to behavior based on the normative goal framework in Foss and Lindenberg , 2013 , because normative goals express the desire to act appropriately in the service of an organization and because behavior is based on normative judgment. I also contend that, in both theories, the main actor is an individual whereas the unit of valuation is a collective. In my view, the unit of valuation in Van de Ven and Lifschitz (2013) could be similar to the level of analysis concept in Greve (2013) . Given these arguments, reasonable models of behavior could also include microfoundations as per the definition given in this study, because normative goals can greatly contribute to value creation.

### **Individual Psychology that Duly Emphasizes Habit Could Contribute to Microfoundations.**

Winter (2013) argues that individual-level foundations can be found only in accounts of individual psychology that give due weight to habit. As per the definition in this study, individual psychology that allots appropriate and necessary consideration to habit could contribute to microfoundations if it could meet the criteria as put forward in the proposed definition.

## **Conclusions**

Thus, this study contends that the proposed definition of microfoundations will be of practical use in management studies. Microfoundations do not lead to infinite regress; rather, individuals should be the stopping point. Further, involvement should encompass every individual within an organization, and leadership and common goals (visions and missions statements) are essential for interactions to successfully culminate in value creation. Since microfoundations do not solely comprise borrowed concepts, but can be explained without utilizing concepts from other disciplines, a more appropriate description is advanced that utilizing concepts from other disciplines could possibly contribute to microfoundations, but are not *a priori* requirements. Microfoundations do not deny the role of structure. Further, using the concept of actor is more appropriate than using the concept of level of analysis, which concerns the social unit at which the theoretical argument is posed. In terms of the definition in this study, reasonable models of behavior could also include microfoundations, and individual psychology that considers the significance of habit could contribute to microfoundations if able to facilitate the involvement of and interactions between individuals for the

purpose of value creation at a firm.

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