Along with recent work by David Galenson, and I hope my own books as well, this book is sure to put cultural economics on the map.

In short, here is an excellent and innovative book with many strengths and no worrisome flaws.

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Economists find it difficult to teach business strategy because they typically use an analytic pedagogy based on models, rather than a softer approach based on cases. The problem with an analytical approach is that MBA students hate it, but the case alternative has shortcomings of its own. You need a very big library of cases to cover all possible situations, and when faced with a novel problem, you have to know which case in your library to draw on for advice.

The best approach to teaching strategy is, of course, an appropriate mixture of cases and models. You have to give students enough cases and examples to teach the lessons of the models, but you also have to provide the students with an analytic framework so that they know how to interpret cases.

It is in this regard that the first part of Sharon Oster’s book Modern Competitive Analysis, entitled ‘The Competitive Environment’ is wildly successful. In these first six chapters, she does to Michael Porter what Jimi Hendrix and The Byrds did to Bob Dylan—cover his songs much better than he did. She puts analytic flesh on the skeleton of Porter’s five-forces taxonomy.

She begins by posing the question, ‘how should we measure success?’ And then presents various measures of industry performance as a segue into profit maximization and Porter’s industry analysis. She then describes the forces moving an industry towards competitive equilibrium, and identifies characteristics that impede the competitive process, thereby allowing firms to earn supra-normal profits. This is a very effective way to teach industry analysis.

A useful design feature of the book are the boxes that that break up the text and summarize material for students, like ‘The larger the Minimum Efficient Scale, the greater the expected wedge between pre-and post-entry prices, and thus the less likely entry is to occur’. These boxed conclusions facilitate studying because a student can skim through the book, and read only the text preceding the boxes of interest.

Most textbooks put this kind of summary information at the end of a chapter, where it is more difficult for students to find the corresponding material. Bravo to Oster for treating readers’ time as if it were a scarce and valuable commodity.

The rest of the book is divided into three sections, ‘Inside the Organization’, ‘Rivalry’, and a concluding chapter on ‘The Planning Process’. These sections not as successful as the first, and even though I will dwell on their shortcomings, I think the first part of the book is a pedagogical gem, and justifies the purchase price by itself.

The least-successful section in the book is the second one, ‘Inside the Organization’. This is unfortunate because under-}

standing the black box of the firm is tremendously important for MBAs, most of whom will end up in middle management. The kinds of questions they will confront are not at the industry-level, but rather, questions of how to motivate subordinates and how to respond to superiors. In short, the kinds of questions addressed by Principal/Agent models. Unfortunately, Oster gives short shrift to the analytical framework of economics here, and instead uses a synthesis of psychology, sociology and economics. This approach will frustrate economists looking for a continuation of the microeconomic approach of the first six chapters.

For example, here are three boxes describing some principles of organizational design:

1. Decentralization generally increases job satisfaction.
2. The organizational structure should complement the social and corporate culture.
3. Delegation of decisions is made easier if there is goal consensus.

Although each of these principles is illustrated with examples, none of these is derived from an analytical structure that students can use in a useful way. Faced with a real problem, these principles are of little value.

For those interested in a cohesive analytical treatment of this material, I would suggest the Rochester paradigm, as embodied in the work of Brickley et al. (1997). They approach the same question with much more useful advice.

1. Make sure that decision-makers have the information necessary to make good decisions; and
2. the incentive to do so.

The Rochester ‘three-legged stool’ has done for organizational design what Porter’s five forces did for the field of strategy. As Oster borrows liberally from other sources, omission of this material is puzzling.

The rivalry section in Oster is alright. She uses game theory to give analytical structure to many good examples in the text. The coverage of the questions and issues is exactly right for an MBA audience, but the analytical approach is shallow and could be better done. I prefer the pedagogy of Dixit and Skeath (1998), but they are not focused on business problems. I think there is what Oster would call entry opportunity on the ‘product map’ of strategy texts, for a text aimed at MBAs that uses game theory to address business questions.

The third edition of the book is not much different than the second. Touted in the preface is new material on network industries, but her treatment of the topic suffers in comparison to Shapiro and Varian’s (1998) Information Rules. Its narrow focus on strategy in a single industry and its consistent microeconomic approach make it much easier to read. Their tight, cohesive text compares favorably to the general, almost reference-like coverage of the strategy field in this book, particularly for teaching purposes. As the strategy field matures, I expect to see fewer general approaches like Oster’s, and more narrowly-focused books like Shapiro and Varian’s.

Nevertheless, there is much in this book to recommend it. She raises all the big issues of business, and summarizes most of the academic literature in a concise and efficient manner. However, her broad, reference-like treatment of the field comes at some pedagogical cost.
REFERENCES


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