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Competition and business strategy in historical perspective

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Abstract

A review of theories of competition and business strategy over the last half-century reveals a fairly linear development of earlier work by academics and consultants into efforts to understand the determinants of industrial profitability and competitive position and, more recently, to add a time or historical dimension to the analysis. The possible implications of the emergence of a market for such ideas are also discussed.

Full text

Headnote

A review of theories of competition and business strategy over the last half-century reveals a fairly linear development of early work by academics and consultants into efforts to understand the determinants of industry profitability and competitive position and, more recently, to add a time or historical dimension to the analysis. The possible implications of the emergence of a market for such ideas are also discussed.

"Strategy" is a term that can be traced back to the ancient Greeks, for whom it meant a chief magistrate or a military commander in chief. The use of the term in business, however, dates only to the twentieth century, and its use in a self-consciously competitive context is even more recent.

After providing some historical background, this essay focuses on how the evolution of ideas about business strategy was influenced by competitive thinking in the second half of the twentieth century. The review aims not to be comprehensive but, instead, to focus on some key topical issues in applying competitive thinking to business strategy. Particular attention is paid to the role of three institutions -Harvard Business School and two consulting firms, the Boston Consulting Group and McKinsey & Company-in looking at the historical development and diffusion of theories of business competition and strategy. The essay concludes with some discussion of how the emergence of a market for ideas in this broad domain is likely to affect future developments in this area.

Historical Background

Until the nineteenth century, the scope for applying (imperfectly) competitive thinking to business situations appeared to be limited: intense competition had emerged in many lines of business, but individual firms apparently often lacked the potential to have much of an influence on competitive outcomes. Instead, in most lines of business -- with the exception of a few commodities in which international trade had developed- firms had an incentive to remain small and to employ as little fixed capital as possible. It was in this era that Adam Smith penned his famous description of market forces as an "invisible hand" that was largely beyond the control of individual firms.

The scope for strategy as a way to control market forces and shape the competitive environment started to become clearer in the second half of the nineteenth century. In the United States, the building of the railroads after 1850 led to the development of mass markets for the first time. Along with improved access to capital and credit, mass markets encouraged large-scale investment to exploit economies of scale in production and economies of scope in distribution. In some industries, Adam Smith's "invisible hand" was gradually tamed by what the historian Alfred D. Chandler Jr. has termed the "visible hand" of professional managers. By the late nineteenth century, a new type of firm began to emerge, first in the United States and then in Europe: the vertically integrated, multidivisional (or "M-form") corporation that made large investments in manufacturing and marketing and in management hierarchies to coordinate those functions. Over time, the largest M-form companies managed to alter the competitive environment within their industries and even across industry lines.¹

The need for a formal approach to corporate strategy was first articulated by top executives of M-form corporations. Alfred Sloan (chief executive of General Motors from 1923 to 1946) devised a strategy that was explicitly based on the perceived strengths and weaknesses of its competitor, Ford.² In the 1930s, Chester

¹ Alfred D. Chandler Jr., *Strategy and Structure* (Cambridge, Mass., 1962) and *Scale and Scope* (Cambridge, Mass., 1962).
² See Alfred P. Sloan Jr., *My Years with General Motors* (New York, 1963).
³ Chester A. Barnard, *The Functions of the Executive* (Cambridge, Mass., 1938). First published 1938; 2nd ed., 1965.

Barnard, a top executive with AT&T, argued that managers should pay especially close attention to "strategic factors," which depend on "personal or organizational action."³

The organizational challenges involved in World War II were a vital stimulus to strategic thinking. The problem of allocating scarce resources across the entire economy in wartime led to many innovations in management science. New operations-research techniques (e.g., linear programming) were devised, which paved the way for the use of quantitative analysis in formal strategic planning. In 1944, John von Neumann and Oskar Morgenstern published their classic work, *The Theory of Games and Economic Behavior*. This work essentially solved the problem of zero-sum games (most military ones, from an aggregate perspective) and framed the issues surrounding non-zero-sum games (most business ones). Also, the concept of "learning curves" became an increasingly important tool for planning. The learning curve was first discovered in the military aircraft industry in the 1920s and 1930s, where it was noticed that direct labor costs tended to decrease by a constant percentage as the cumulative quantity of aircraft produced doubled. Learning effects figured prominently in wartime production planning efforts.

World War II also encouraged the mindset of using formal strategic thinking to guide management decisions. Thus, Peter Drucker argued that "management is not just passive, adaptive behavior; it means taking action to make the desired results come to pass." He noted that economic theory had long treated markets as impersonal forces, beyond the control of individual entrepreneurs and organizations. But, in the age of M-form corporations, managing "implies responsibility for attempting to shape the economic environment, for planning, initiating and carrying through changes in that economic environment, for constantly pushing back the limitations of economic circumstances on the enterprise's freedom of action."⁴ This insight became the rationale for business strategy—that, by consciously using formal planning, a company could exert some positive control over market forces.

However, these insights on the nature of strategy largely lay fallow for the decade after World War II because wartime destruction led to excess demand, which limited competition as firms rushed to expand capacity. Given the enormous job of rebuilding Europe and much of Asia, it was not until the late 1950s and 1960s that many large multinational corporations were forced to consider global competition as a factor in planning. In addition, the wartime disruption of foreign multinationals enabled U.S. companies to profit from the postwar boom without effective competitors in many industries.

⁴ Peter Drucker, *The Practice of Management* (New York, 1954), 11.

A more direct bridge to the development of strategic concepts for business applications was provided by interservice competition in the

U.S. military after World War II. In this period, American military leaders found themselves debating the arrangements that would best protect legitimate competition between military services while maintaining the needed integration of strategic and tactical planning. Many argued that the Army, Navy, Marines, and Air Force would be more efficient if they were unified into a single organization. As the debate raged, Philip Selznick, a sociologist, noted that the Navy Department "emerged as the defender of subtle institutional values and tried many times to formulate the distinctive characteristics of the various services." In essence, the "Navy spokesmen attempted to distinguish between the Army as a 'manpower' organization and the Navy as a finely adjusted system of technical, engineering skills—a 'machine-centered' organization. Faced with what it perceived as a mortal threat, the Navy became highly self-conscious about its distinctive competence."⁵ The concept of "distinctive competence" had great resonance for strategic management, as we will see next.

Academic Underpinnings

The Second Industrial Revolution witnessed the founding of many elite business schools in the United States, beginning with the Wharton School in 1881. Harvard Business School, founded in 1908, was one of the first to promote the idea that managers should be trained to think strategically and not just to act as functional administrators. Beginning in 1912, Harvard offered a required second-year course in "business policy," which was designed to integrate the knowledge gained in functional areas like accounting, operations, and finance, thereby giving students a broader perspective on the strategic problems faced by corporate executives. A course description from 1917 claimed that "an analysis of any business problem shows not only its relation to other problems in the same group, but also the intimate connection of groups. Few problems in business are purely intra-departmental." It was also stipulated that the policies of each department must maintain a "balance in accord with the underlying policies of the business as a whole."⁶

⁵ Philip Selznick, *Leadership in Administration* (Evanston, Ill., 1957), 49–50.

⁶ Official Register of Harvard University, 29 Mar. 1917, 42–3.

In the early 1950s, two professors of business policy at Harvard, George Albert Smith Jr. and C. Roland Christensen, taught students to question whether a firm's strategy matched its competitive environment. In reading cases, students were instructed to ask: do a company's

policies "fit together into a program that effectively meets the requirements of the competitive situation"?⁷ Students were told to address this problem by asking: "How is the whole industry doing? Is it growing and expanding? Or is it static; or declining?" Then, having "sized up" the competitive environment, the student was to ask: "On what basis must any one company compete with the others in this particular industry? At what kinds of things does it have to be especially competent, in order to compete?"⁸

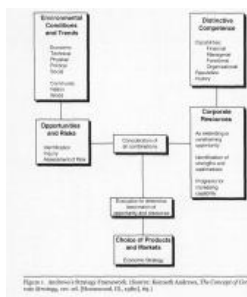
In the late 1950s, another Harvard business policy professor, Kenneth Andrews, built on this thinking by arguing that "every business organization, every subunit of organization, and even every individual [ought to] have a clearly defined set of purposes or goals which keeps it moving in a deliberately chosen direction and prevents its drifting in undesired directions" (emphasis added). As shown in the case of Alfred Sloan at General Motors, "the primary function of the general manager, over time, is supervision of the continuous process of determining the nature of the enterprise and setting, revising and attempting to achieve its goals."⁹ The motivation for these conclusions was supplied by an industry note and company cases that Andrews prepared on Swiss watch-- makers, which uncovered significant differences in performance associated with their respective strategies for competing in that industry." This format of combining industry notes with company cases, which had been initiated at Harvard Business School by a professor of manufacturing, John MacLean, became the norm in Harvard's business policy

course. In practice, an industry note was often followed by multiple cases on one or several companies with the objective, *inter alia*, of economizing on students' preparation time.¹¹

¹¹George Albert Smith Jr. and C. Richard Christensen, *Suggestions to Instruction on Fall for Harvard Business School*, 1963, 2-4.
¹²George Albert Smith Jr., *Policy Formulation and Administration* (Chicago, 1963), 44.
¹³Alfred D. Chandler, Jr., *The Strategy of Corporate Development* (Cambridge, MA, 1962), 15.
¹⁴See Peter L. Johnson, *The Strategy of Corporate Development*, 1963, 15.
¹⁵See Peter L. Johnson, *The Strategy of Corporate Development*, 1963, 15.

By the 1960s, classroom discussions in the business policy course focused on matching a company's "strengths" and "weaknesses" - its distinctive competence - with the "opportunities" and "threats" (or risks) it faced in the marketplace. This framework, which came to be referred to by the acronym SWOT, was a major step forward in bringing explicitly competitive thinking to bear on questions of strategy. Kenneth Andrews put these elements together in a way that became particularly well known. (See Figure 1.) In 1963, a business policy confer

ence was held at Harvard that helped diffuse the SWOT concept in academia and in management practice. Attendance was heavy, and yet the popularity of SWOT - which was still used by many firms, including Wal-Mart, in the 1990s - did not bring closure to the problem of actually defining a firm's distinctive competence. To solve this problem, strategists had to decide which aspects of the firm were "enduring and unchanging over relatively long periods of time" and which were "necessarily more responsive to changes in the marketplace and the pressures of other environmental forces." This distinction was crucial because "the strategic decision is concerned with the long-term development of the enterprise" (emphasis added).¹² When strategy choices were analyzed from a long-range perspective, the idea of "distinctive competence" took on added importance because of the risks involved in most long-run investments. Thus, if the opportunities a firm was pursuing appeared "to outrun [its] present distinctive competence," then the strategist had to consider a firm's "willingness to gamble that the latter can be built up to the required level."¹³



The debate over a firm's "willingness to gamble" its distinctive competence in pursuit of opportunity continued in the 1960s, fueled by a booming stock market and corporate strategies that were heavily geared toward growth and diversification. In a classic 1960 article, "Marketing Myopia," Theodore Levitt was sharply critical of firms that seemed to focus too much on delivering a product, presumably based on its distinctive competence, rather than consciously serving the customer. Levitt thus argued that when companies fail, "it usually means that the product fails to adapt to the constantly changing patterns of consumer needs and tastes, to new and modified marketing institutions and practices, or to product developments in complementary industries."¹⁴

However, another leading strategist, Igor Ansoff, argued that Levitt was asking companies to take unnecessary risks by investing in new products that might not fit the firm's distinctive competence. Ansoff argued that a company should first ask whether a new product had a "common thread" with its existing products. He defined the common thread as a firm's "mission" or its commitment to exploit an existing need in the market as a whole.¹⁵ Ansoff noted that "sometimes the customer is erroneously identified as the common thread of a firm's business. In reality, a given type of customer will frequently have a range of unrelated product missions

or needs."¹⁶ Thus, for a firm to maintain its strategic focus, Ansoff suggested certain categories for defining the common thread in its business/corporate strategy. (See Figure 2.) Ansoff and others also focused on translating the logic of the SWOT framework into a series of concrete questions that needed to be answered in the development of strategies.¹⁷

¹⁷Ansoff, *The Strategy of Corporate Development*, 1965, 15.
¹⁸See, e.g., Theodore Levitt, "Marketing Myopia," *Harvard Business Review* (July-Aug. 1960) 55.
¹⁹See Peter L. Johnson, *The Strategy of Corporate Development*, 1963, 15.
²⁰See Peter L. Johnson, *The Strategy of Corporate Development*, 1963, 15.
²¹See Peter L. Johnson, *The Strategy of Corporate Development*, 1963, 15.

In the 1960s, diversification and technological changes increased the complexity of the strategic situations that many companies faced, and intensified their need for more sophisticated measures that could

be used to evaluate and compare many different types of businesses. Since business policy groups at Harvard and elsewhere remained strongly wedded to the idea that strategies could only be analyzed on a case-by-case

basis in order to account for the unique characteristics of every business, corporations turned elsewhere to satisfy their craving for standardized approaches to strategy making.¹⁸ A study by the Stanford Research Institute indicated that a majority of large U.S. companies had set up formal planning departments by 1963.¹⁹ Some of these internal efforts were quite elaborate. General Electric (GE) is a bellwether example: it used Harvard faculty extensively in its executive education programs, but it also independently developed an elaborate, computer-based "Profitability Optimization Model" (PROM) in the first half of the 1960s that appeared to explain a significant fraction of the variation in the return on investment afforded by its various businesses.²⁰ Over time, like many other companies, GE also sought the help of private consulting firms. While consultants made important contributions in many areas, such as planning, forecasting, logistics, and long-range research and development (R&D), the following section traces their early impact on mainstream strategic thinking.

The Rise of Strategy Consultants



The 1960s and early 1970s witnessed the rise of a number of strategy consulting practices. In particular, the Boston Consulting Group

(BCG), founded in 1963, had a major impact on the field by applying quantitative research to problems of business and corporate strategy. BCG's founder, Bruce Henderson, believed that a consultant's job was to find "meaningful quantitative relationships" between a company and its chosen markets.²¹ In his words, "good strategy must be based primarily on logic, not ... on experience derived from intuition."²² Indeed, Henderson was utterly convinced that economic theory would someday lead to a set of universal rules for strategy. As he explained, "[I]n most firms strategy tends to be intuitive and based upon traditional patterns of behavior which have been successful in the past.... [However,] in growth industries or in a changing environment, this kind of strategy is rarely adequate. The accelerating rate of change is producing a business world in which customary managerial habits and organization are increasingly inadequate."²³

In order to help executives make effective strategic decisions, BCG drew on the existing knowledge base in academia: one of its first employees, Seymour Titles, was formerly a lecturer in Harvard's business policy course. However, it also struck off in a new direction that Bruce Henderson is said to have described as "the business of selling powerful oversimplifications."²⁴ In fact, BCG came to be known as a "strategy boutique"

because its business was largely based, directly or indirectly, on a single concept: the experience curve (discussed below). The value of using a single concept came from the fact that "in nearly all problem solving there is a universe of alternative choices, most of which must be discarded without more than cursory attention." Hence, some "frame of reference is needed to screen the . . . relevance of data, methodology, and implicit value judgments" involved in any strategy decision. Given that decision making is necessarily a complex process, the most useful "frame of reference is the concept. Conceptual thinking is the skeleton or the framework on which all other choices are sorted out."²⁵

²⁵Experience with Experience Curves, no date given. This article discusses the importance of the experience curve in the competitive behavior of firms. It is based on the work of Bruce Henderson, who developed the concept of the experience curve. Henderson, Bruce. *The Logic of Business Strategy* (Cambridge, Mass., 1979), p. 1. Henderson, Bruce. *Experience Curves* (Cambridge, Mass., 1979), p. 1. Henderson, Bruce. *Experience Curves* (Cambridge, Mass., 1979), p. 1.

BCG and the Experience Curve. BCG first developed its version of the learning curve-what it labeled the "experience curve"-in 1965-- 66. According to Bruce Henderson, "it was developed to try to explain price and competitive behavior in the extremely fast growing segments" of industries for clients like Texas Instruments and Black and

Decker.²⁶ As BCG consultants studied these industries, they naturally asked why "one competitor outperforms another (assuming comparable management skills and resources)? Are there basic rules for success? There, indeed, appear to be rules for success, and they relate to the impact of accumulated experience on competitors' costs, industry prices and the interrelation between the two."²⁷

The firm's standard claim for the experience curve was that for each cumulative doubling of experience, total costs would decline by roughly 20 to 30 percent due to economies of scale, organizational learning, and technological innovation. The strategic implication of the experience curve, according to BCG, was that for a given product segment, "the producer... who has made the most units should have the lowest costs and the highest profits."²⁸ Bruce Henderson claimed that with the experience curve "the stability of competitive relationships should be predictable, the value of market share change should be calculable, [and] the effects of growth rate should [also] be calculable."²⁹

From the Experience Curve to Portfolio Analysis. By the early 1970s, the experience curve had led to another "powerful oversimplification" by BCG: the "Growth-Share Matrix," which was the first use of what came to be known as "portfolio analysis." (See Figure 3.) The idea was that after experience curves were drawn for each of a diversified company's business units, their relative potential as areas for investment could be compared by plotting them on the grid.

²⁶Bruce Henderson explained that, within certain versions of the "experience curve," BCG's experience curve "measures all costs including material, administration, research and marketing and know-how through technological development and product evolution. It is also based on such raw data as unit volume, unit cost, and unit price." Henderson, Bruce. *Experience Curves* (Cambridge, Mass., 1979), p. 1. Henderson, Bruce. *Experience Curves* (Cambridge, Mass., 1979), p. 1. Henderson, Bruce. *Experience Curves* (Cambridge, Mass., 1979), p. 1.

BCG's basic strategy recommendation was to maintain a balance between "cash cows" (i.e., mature businesses) and "stars," while allocating some resources to feed "question marks," which were potential stars. "Dogs" were to be sold off. In more sophisticated language, a BCG vice president explained that "since the producer with the largest stable market share eventually has the lowest costs and greatest profits, it becomes vital to have a dominant market share in as many products as possible. However, market share in slowly growing products can be gained only by reducing the share of competitors who are likely to fight back." If a product market is growing rapidly, "a company can gain share by securing most of the growth. Thus, while competitors grow,

the company can grow even faster and emerge with a dominant share when growth eventually slows."³⁰

²⁷Figure 3. BCG's Growth-Share Matrix. (Source: Adapted from George B. Borch, Jr. and Thomas H. Borch, *Competing Against Time* (New York: 1988), p. 11.)

Strategic Business Units and Portfolio Analysis. Numerous other consulting firms came up with their own matrices for portfolio analysis at roughly the same time as BCG. McKinsey & Company's effort, for instance, began in 1968 when Fred Borch, the CEO of GE, asked McKinsey to examine his company's corporate structure, which consisted of two hundred profit centers and one hundred and forty-five departments arranged around ten groups. The boundaries for these units had been defined according to theories of financial control, which the McKinsey consultants judged to be inadequate. They argued that the firm should be organized on more strategic lines, with greater concern for external conditions than internal controls and a more future-oriented

approach than was possible using measures of past financial performance. The study recommended a formal strategic planning system that would divide the company into "natural business units," which Borch later renamed "strategic business units," or SBUs. GE's executives followed this advice, which took two years to put into effect.

²⁸Conley, "Experience Curves as a Planning Tool," 10--11.

However, in 1971, a GE corporate executive asked McKinsey for help in evaluating the strategic plans that were being written by the company's many SBUs. GE had already examined the possibility of using the BCG growth-share matrix to decide the fate of its SBUs, but its top management had decided then that they could not set priorities on the basis of just two performance measures. And so, after studying

the problem for three months, a McKinsey team produced what came to be known as the GE/McKinsey nine-block matrix. The nine-block matrix used about a dozen measures to screen for industry attractive

ness, or profitability, and another dozen to screen for competitive position, although the weights to be attached to them were not specified.³¹ (See Figure 4.)

²⁹Figure 3. BCG's Growth-Share Matrix. (Source: Adapted from George B. Borch, Jr. and Thomas H. Borch, *Competing Against Time* (New York: 1988), p. 11.)

Another, more quantitative, approach to portfolio planning was developed at roughly the same time under the aegis of the "Profit Impact of Market Strategies" (PIMS) program, which was the multicompany successor to the PROM program that GE had started a decade earlier. By the mid-1970s, PIMS contained data on six hundred and twenty SBUs drawn from fifty-seven diversified corporations.³² These data were used, in the first instance, to explore the determinants of returns on investment by regressing historical returns on variables such as market share, product quality, investment intensity, marketing and R&D expenditures, and several dozen others. The regressions established what were supposed to be benchmarks for the potential performance of SBUs with particular characteristics against which their actual performance might be compared.

In all these applications, segmenting diversified corporations into SBUs became an important precursor to analyses of economic performance.³³ This forced "de-averaging" of cost and performance numbers that had previously been calculated at more aggregated levels. In addition, it was thought that, with such approaches, "strategic thinking was appropriately pushed 'down the line' to managers closer to the particular industry and its competitive conditions."³⁴

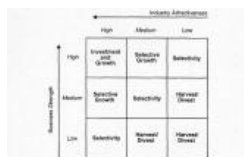


Figure 5. Industry Attractiveness - Business Strength Matrix. (Source: Amabile C. (1984) and Porter M. (1985). Strategic Management: an Integrative Perspective. Englewood Cliffs, N.J., 1984) (24)

extent.³⁶

³⁶Walter R. Starling, "Strategic Management: an Integrative Perspective," Englewood Cliffs, N.J., 1984, p. 100. ³⁷Frederick W. Gluck and William J. Abernathy, "The Strategic Planning Process: an Industry Perspective," *Strategic Management Journal*, 1983, 4, 1. ³⁸A. James Henderson, "Strategic Planning: A Critical Review," *Strategic Management Journal*, 1983, 4, 1. ³⁹Philip H. Hirsch, "Strategic Planning: an Integrative Perspective," Englewood Cliffs, N.J., 1984, p. 100.

experience curve was pinpointed in a classic 1974 article by William Abernathy and Kenneth Wayne, which argued that "the consequence of intensively pursuing a cost-minimization strategy [e.g., one based on the experience curve] is a reduced ability to make innovative changes and to re

spond to those introduced by competitors."³⁷ Abernathy and Wayne pointed to the case of Henry Ford, whose obsession with lowering costs had left him vulnerable to Alfred Sloan's strategy of product innovation in the car business. The concept of the experience curve was also criticized for treating cost reductions as automatic rather than something to be managed, for assuming that most experience could be kept proprietary instead of spilling over to competitors, for mixing up different sources of cost reduction with very different strategic implications (e.g., learning versus scale versus exogenous technical progress), and for leading to stalemates as more than one competitor pursued the same generic success factor.³⁸

In the late 1970s, portfolio analysis came under attack as well. One problem was that, in many cases, the strategic recommendations for an SBU were very sensitive to the specific portfolio-analytic technique employed. For instance, an academic study applied four different portfolio techniques to a group of fifteen SBUs owned by the same Fortune 500 corporation; it found that only one of the fifteen SBUs fell into the same portion of each of the four matrices, and only five of the fifteen were classified similarly in terms of three of the four matrices.³⁹ This was only a slightly higher level of concordance than would have been expected if the fifteen SBUs had been randomly classified four separate times!

³⁹William J. Abernathy and Kenneth Wayne, "Costs of the Learning Curve," *Strategic Management Journal*, 1974, 5, 1. ⁴⁰Frederick W. Gluck and William J. Abernathy, "The Strategic Planning Process: an Industry Perspective," *Strategic Management Journal*, 1983, 4, 1. ⁴¹Frederick W. Gluck and William J. Abernathy, "The Strategic Planning Process: an Industry Perspective," *Strategic Management Journal*, 1983, 4, 1. ⁴²Frederick W. Gluck and William J. Abernathy, "The Strategic Planning Process: an Industry Perspective," *Strategic Management Journal*, 1983, 4, 1. ⁴³Frederick W. Gluck and William J. Abernathy, "The Strategic Planning Process: an Industry Perspective," *Strategic Management Journal*, 1983, 4, 1.

competition" and often leave businesses "vulnerable to unexpected thrusts from companies not previously considered competitors."⁴⁰ Gluck and his colleagues sought to loosen some of the constraints imposed by mechanistic approaches,

proposing that successful companies devise progressive strategies to take them through four basic stages. Each stage requires these companies to grapple with increasing levels of dynamism, multidimensionality, and uncertainty, and they therefore become less amenable to routine quantitative analysis. (See Figure 5.)

The most stinging attack on the analytical techniques popularized by strategy consultants was offered by two Harvard professors of production, Robert Hayes and William Abernathy, in 1980. They argued that "these new principles [of management], despite their sophistication and widespread usefulness, encourage a preference for (i) analytic detachment rather than the insight that comes from 'hands on experience' and (2) short-term cost reduction rather than long-term development of technological competitiveness."⁴¹ Hayes and Abernathy in particular criticized portfolio analysis as a tool that led managers to focus on minimizing financial risks rather than on investing in new opportunities that require a long-term commitment of resources.⁴² They went on to compare U.S. firms unfavorably with Japanese and, especially, European ones.

⁴¹Robert L. Hayes and William J. Abernathy, "Managing the Way We Conceive Ourselves," *Harvard Business Review*, 1980, 58, 10. ⁴²Ibid., 11.

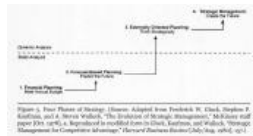
These and other criticisms gradually diminished the popularity of portfolio analysis. However, its rise and fall did have a lasting influence on subsequent work on competition and business strategy because it highlighted the need for more careful analysis of the two basic dimensions of portfolio-analytic grids: industry attractiveness and competi

five position. Although these two dimensions had been identified earlier-in the General Survey Outline developed by McKinsey & Company for internal use in 1952, for example -portfolio analysis underscored this particular method of analyzing the effects of competition on business performance. U.S. managers, in particular, proved avid consumers of insights about competition because the exposure of much of U.S. industry to competitive forces increased dramatically during the 1960s and 1970s. One economist roughly calculated that heightened import competition, antitrust actions, and deregulation increased the share of the U.S. economy that was subject to effective competition from 56 percent in 1958 to 77 percent by 1980.⁴³ The next two sections describe attempts to unbundle these two basic dimensions of strategy. (See Figure 6.)

Unbundling Industry Attractiveness

Thus far, we have made little mention of economists' contributions to thinking about competitive strategy. On the one hand, economic theory emphasizes the role of competitive forces in determining market outcomes. However, on the other hand, economists have often overlooked the importance of strategy because, since Adam Smith, they have traditionally focused on the case of perfect competition: an idealized situation in which large numbers of equally able competitors drive an industry's aggregate economic profits (i.e., profits in excess of the opportunity cost of the capital employed) down to zero. Under perfect competition, individual competitors are straitjacketed, in the sense of having a choice between producing efficiently and pricing at cost or shutting down.

Some economists did address the opposite case of perfect competition, namely pure monopoly, with Antoine Cournot providing the first



definitive analysis—as well as analysis of oligopoly under specific assumptions—in 1838.⁴⁴ Work on monopoly yielded some useful insights, such as the expectation of an inverse relation between the profitability of a monopolized industry and the price elasticity of the demand it faced—an insight that has remained central in modern marketing. Nevertheless, the assumption of monopoly obviously took things to the other, equally unfortunate, extreme by ruling out all directly competitive forces in the behavior of firms.



⁴⁴Frederick W. Clark, "The Structure of Strategic Management," *Management Science*, vol. 33, no. 1, pp. 1-15, 1987.

This state of affairs began to change at an applied level in the 1930s, as a number of economists, particularly those associated with the "Harvard school," began to argue that the structure of many industries might permit incumbent firms to earn positive economic profits over long periods of time.⁴⁵ Edward S. Mason argued that the structure of an industry would determine the conduct of buyers and sellers -- their choices of critical decision variables--and, by implication, its performance along such dimensions as profitability, efficiency, and innovativeness.⁴⁶ Joe Bain, also of the Harvard Economics Department, advanced the research program of uncovering the general relation between industry structure and performance through empirical work focused on a limited number of structural variables --most notably, in two studies published in the 1950s. The first study found that the profitability of manufacturing industries in which the eight largest competitors accounted for

more than 70 percent of sales was nearly twice that of industries with eight-firm concentration ratios of less than 70 percent.⁴⁷ The second study explained how, in certain industries, "established sellers can persistently raise their prices above a competitive level without attracting new firms to enter the industry."⁴⁸ Bain identified three basic barriers to entry: (1) an absolute cost advantage by an established firm (an enforceable patent, for instance); (2) a significant degree of product differentiation; and (3) economies of scale.



been carried out. While the relation between structural variables and performance turned out to be more complicated than had been suggested earlier,⁴⁹ these studies reinforced the idea that some industries are inherently much more profitable or "attractive" than others, as indicated below. (See Figure 7.)

Industry	Return on Equity
Drugs	22.1
Printing and Publishing	13.5
Food and Drug	13.1
Automotive and Coal	11.1
Major retailers and department stores	11.0
Textile mill products	9.3
Beer and Oil	8.8

Figure 7: Differences in the Profitability of Selected Industries, 1955-1959. (Source: Table 10, *Monopoly, Rivalry, and Competition*, 1959, Harvard Business School Publishing, No. 790-090 (1960)).

Harvard Business School's Business Policy Group was aware of these insights from across the Charles River: excerpts from Bain's book on barriers to entry were even assigned as required readings for the business policy course in the early 1960s. But the immediate impact of IO on business strategy was limited. Although many problems can be discerned in retrospect, two seem to have been particularly important. First, IO economists focused on issues of public policy rather than business policy: they concerned themselves with the minimization rather than the maximization of "excess" profits. Second, the emphasis of Bain and his successors on using a limited list of structural variables to explain industry profitability shortchanged the richness of

modern industrial competition ("conduct" within the IO paradigm).



Both of these problems with applying classical IO to business-- strategic concerns about industry attractiveness were addressed by Michael Porter, a graduate of the Ph.D. program offered jointly by Harvard's Business School and its Economics Department. In 1974, Porter prepared a "Note on the Structural Analysis of Industries," which presented his first attempt to turn IO on its head by focusing on the business policy objective of profit maximization, rather than on the public policy objective of minimizing "excess" profits.⁵⁰ In 1980, he released

his landmark book, *Competitive Strategy*, which owed much of its suc

cess to Porter's elaborate framework for the structural analysis of industry attractiveness. Figure 8 reproduces Porter's "five forces" approach to understanding the attractiveness of an industry environment for the "average" competitor within it. In developing this approach to strategy, Porter noted the trade-offs involved in using a "framework" rather than a more formal statistical "model." In his words, a framework "encompasses many variables and seeks to capture much of the complexity of actual competition. Frameworks identify the relevant variables and the questions that the user must answer in order to develop conclusions tailored to a particular industry and company" (emphasis added).⁵¹ In academic terms, the drawback of frameworks such as the five forces is that they often range beyond the empirical evidence that is available. In practice, managers routinely have to consider much longer lists of variables than are embedded in the relatively simple quantitative models used by economists. In the case of the five forces, a survey of empirical literature in the late 1980s--more than a decade after Porter first developed his framework--revealed that only a few points were strongly supported by the empirical literature generated by the IO field.⁵² (These points appear in bold print in Figure 8.) This does not mean that the other points are in conflict with IO research; rather, they reflect the experience of strategy practitioners, including Porter himself.



In managerial terms, one of the breakthroughs built into Porter's framework was that it emphasized "extended competition" for value rather than just competition between existing rivals. For this reason, and because it was easy to put into effect, the five-forces framework came to be used widely by managers and consultants.

Subsequent years witnessed refinements and extensions, such as the rearrangement and incorporation of additional variables (e.g., import competition and multimarket contact) into the determinants of the intensity of five forces. The biggest conceptual advance, however, was one proposed in the mid-1990s by two strategists concerned with game theory, Adam Brandenburger and Barry Nalebuff, who argued that the process of creating value in the marketplace involved "four types of players -- customers, suppliers, competitors, and complementors."⁵³ By a firm's "complementors," they meant other firms from which customers buy

complementary products and services, or to which suppliers sell complementary resources. As Brandenburger and Nalebuff pointed out, the practical importance of this group of players was evident in the amount of attention being paid in business to the subject of strategic alliances and partnerships. Their Value Net graphic depicted this more complete description of the business landscape -emphasizing, in particular, the equal roles played by competition and complementarity. (See Figure 9.)

Other strategists, however, argued that some very limiting assumptions were built into such frameworks. Thus, Kevin Coyne and Somu Subramanyam of McKinsey argued that the Porter framework made three tacit but crucial assumptions: First, that an industry consists of a set of unrelated buyers, sellers, substitutes, and competitors that interact at arm's length. Second, that wealth will accrue to players that are able to erect barriers against competitors and potential entrants, or, in other words, that the source of value is structural advantage. Third, that uncertainty is sufficiently low that you can accurately predict participants' behavior and choose a strategy accordingly.⁵⁴

Unbundling Competitive Position

"Barry P. Coyne and Somu Subramanyam, 'Unbundling Competition in Strategy,' McKinsey Quarterly, 1994, 40.
Note: Dr. Subramanyam, who is a consultant, has been quoted in the article by Michael E. Porter, 'From Static Structure to Dynamic Strategy,' Harvard Business Review, 1993, 62-76.

The second basic dimension of business strategy highlighted by Figure 6 is competitive position. While differences in the average profitability of industries can be large, as indicated in Figure 7, differences in profitability within industries can be even larger.⁵⁵ Indeed, in some cases firms in unattractive industries can significantly outperform the averages for more profitable industries, as indicated in Figure 10. In addition, one might argue that most businesses in most industry environments are better placed to try to alter their own

competitive positions, rather than the overall attractiveness of the industry in which they operate. For both these reasons, competitive position has been of great interest to business strategists. (See Figure 10.)

"Barry P. Coyne and Somu Subramanyam, 'Unbundling Competition in Strategy,' McKinsey Quarterly, 1994, 40.
Note: Dr. Subramanyam, who is a consultant, has been quoted in the article by Michael E. Porter, 'From Static Structure to Dynamic Strategy,' Harvard Business Review, 1993, 62-76.

Traditional academic research has made a number of contributions to our understanding of positioning within industries, starting in the 1970s. The IO-based literature on strategic groups, initiated at Harvard by Michael Hunt's work on broad-line versus narrow-line strategies in the major home appliance industry, suggested that competitors within particular industries could be grouped in terms of their competitive strategies in ways that helped explain their interactions and relative profitability.⁵⁶ A stream of work at Purdue explored the

heterogeneity of competitive positions, strategies, and performance in brewing and other industries with a combination of statistical analysis and qualitative case studies. More recently, several academic points of view about the sources of performance differences within industries have emerged -- views that are explored more fully in the next section. However, it does seem accurate to say that the work that had the most impact on the strategic thinking of business about competitive positions in the late 1970s and the 1980s was more pragmatic than academic in its intent, with consultants once again playing a leading role.

Competitive Cost Analysis. With the rise of the experience curve in the 1960s, most strategists turned to some type of cost analysis as the basis for assessing competitive positions. The interest in competitive cost analysis survived the declining popularity of the experience curve in the 1970s but was reshaped by it in two important ways. First, more attention was paid to disaggregating businesses into their component activities or processes and to thinking about how costs in a particular activity might be shared across businesses. Second, strategists greatly enriched their menu of cost drivers to include more than just experience.

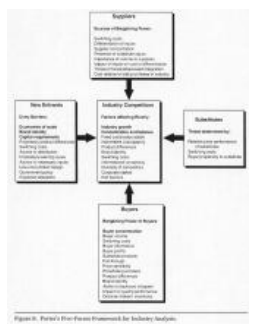


Figure 10: Porter's Five Forces Framework for Industry Analysis

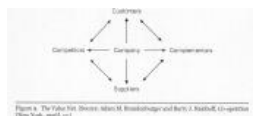


Figure 9: The Value Net (Source: Adam M. Brandenburger and Barry J. Nalebuff, co-authors, 1996, Harvard Business School Press)

The disaggregation of businesses into their component activities seems to have been motivated, in part, by early attempts to "fix" the experience curve to deal with the rising real prices of many raw materials in the 1970s.⁵⁷ The proposed fix involved splitting costs into the costs of purchased materials and "cost added" (value added minus profit margins) and redefining the experience curve as applying only to the latter. The natural next step was to disaggregate a business's entire cost structure into activities whose costs might be expected to behave in interestingly different ways. As in the case of portfolio analysis, the idea of splitting businesses into component activities diffused quickly among consultants and their clients in the 1970s. A template for activity analysis that became especially prominent is reproduced in Figure 11.

Activity analysis also suggested a way of getting around the "tree-- standing" conception of individual businesses built into the concept of SBUs. One persistent problem in splitting diversified corporations into SBUs was that, with the exception of pure conglomerates, SBUs were often related in ways that meant they shared elements of their cost structure with each other. Consulting firms, particularly Bain and Strategic Planning Associates, both of whose founders had worked on a BCG study of Texas Instruments that was supposed to highlight the problem of shared costs, began to emphasize the development of what came to be called "field maps": matrices that identified shared costs at the level of individual activities that were linked across businesses, as illustrated below.⁵⁸

The second important development in competitive cost analysis over the late 1970s and early 1980s involved enrichment of the menu of cost drivers considered by strategists. Scale effects, while officially lumped into the experience curve, had long been looked at independently in particular cases; even more specific treatment of the effects of scale was now forced by activity analysis that might indicate, for example, that advertising costs were driven by national scale, whereas distri

⁶⁵ Porter, *Competitive Advantage*, 33, 37.
⁶⁶ Talk by Arnaldo Hax at MIT on 29 April 1997.

⁶⁷ J. B. Scherer and David Ross, *Industrial Structure and Economic Performance* (Chicago, 1967), 83.
⁶⁸ R. N. Stalk, "Time as Value Stream," *Harvard Business Review* (Spring 1988), 48-55.
⁶⁹ J. B. Scherer, "Sustainable Advantage," *Harvard Business Review* (Sept. 1985), 139-48.
⁷⁰ The first systematic studies of the "Red Queen" effect is generally attributed to L. Vito Lillien, for a time editor, of *Strategic Management* (now *Strategic Theory*) 1 (1973): 1-22.
⁷¹ The primary reference is to James G. March's classic observations in *Structural and Through the Looking Glass* (New York, 1981), but published only 10 years after the Red Queen had been named.
⁷² Stalk, "Time as Value Stream," 48-55.
⁷³ Stalk, "Time as Value Stream," 48-55.
⁷⁴ Stalk, "Time as Value Stream," 48-55.

The need to return the time dimension to predominantly static ideas about competitive position was neatly illustrated by the techniques for "value-based strategic management" that began to be promoted by consulting firms like SPA and Marakon, among others, in the 1980s. The development and diffusion of value-based techniques, which connected positioning measures to shareholder value using spreadsheet models of discounted cash flows, was driven by increases in capital market pressures in the 1980s, particularly in the United States: merger and acquisition activity soared; hostile takeovers of even very large companies became far more common; many companies restructured to avoid them; levels of leverage generally increased; and there was creeping institutionalization of equity holdings.⁶⁷ Early value-based work focused on the spread between a company or division's rate of return and its cost of capital as the basis for "solving" the old corporate strategy problem of resource allocation across businesses. It quickly became clear, however, that estimated

valuations were very sensitive to two other, more dynamic, drivers of value: the length of the time horizon over which positive spreads (competitive advantage) could be sustained on the assets in place, and the (profitable) reinvestment opportunities or growth options afforded by a strategy.⁶⁸ At the same time, analyses of business performance started to underscore the treacherousness of assuming that current profitability and growth could automatically be sustained. Thus, my analysis of 700 business units revealed that nine-tenths of the profitability differential between businesses that were initially above average and those that were initially below average vanished over a ten-year period.⁶⁹ (See Figure 13.)

The unsustainability of most competitive advantages was generally thought to reflect the "Red Queen" effect: the idea that as organizations struggled to adapt to competitive pressures, they would become stronger competitors, sending the overall level of competition spiraling upward and eliminating most, if not all, competitive advantages.⁷⁰ In the late 1980s and early 1990s, both academics and consultants started to wrestle with the dynamic question of how businesses might create and sustain competitive advantage in the presence of competitors who could not all be counted on to remain inert all the time.

⁷⁵ George Stalk, Jr., "Time: The New Source of Competitive Advantage," *Harvard Business Review* (July-Aug. 1988), 48-55.

From an academic perspective, many of the consultants' recommendations regarding dynamics amounted to no more, and no less, than the injunction to try to be smarter than the competition (for example, by focusing on customers' future needs while competitors remained focused on their current needs). The most thoughtful exception that had a truly dynamic orientation was work by George Stalk and others at BCG on time-based

competition. In an article published in the *Harvard Business Review* in 1988, Stalk argued: "Today the leading edge of competition is the combination of fast response and increasing variety. Companies without these advantages are slipping into commoditylike competition, where customers buy mainly on price."⁷¹ Stalk expanded on this argument in a book coauthored with Thomas Hout in 1990, according to which time-based competitors "[c]reate more information and share it more spontaneously. For the information technolo-

gist, information is a fluid asset, a data stream. But to the manager of a business . . . information is fuzzy and takes many forms -knowing a customer's special needs, seeing where the market is heading. . . ."⁷²

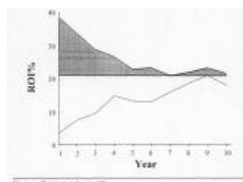


Figure 13. The Limits to Sustainability

Time-based competition quickly came to account for a substantial fraction of BCG's business. Eventually, however, its limitations also became apparent. In 1993, George Stalk and Alan Webber wrote that some Japanese companies had become so dedicated to shortening their product-development cycles that they had created a "strategic treadmill on which companies were caught, condemned to run faster and faster but always staying in the same place competitively."⁷³ In particular, Japanese electronics manufacturers had reached a remarkable level of efficiency, but it was an "efficiency that [did] not meet or create needs for any customer."⁷⁴

For some, like Stalk himself, the lesson from this and similar episodes was that there were no sustainable advantages: "Strategy can never be a constant.... Strategy is and always has been a moving target."⁷⁵ However, others, primarily academics, continued to work in the 1990s on explanations of differences in

performance that would continue to be useful even after they were widely grasped.⁷⁶ This academic work exploits, in different ways, the idea that history matters, that history affects both the opportunities available to competitors and the effectiveness with which competitors can exploit them. Such work can be seen as an attempt to add a historical or time dimension, involving stickiness and rigidities, to the two basic dimensions of early portfolio analytic grids: industry attractiveness and competitive position. The rest of this section briefly reviews four strands of academic inquiry that embodied new approaches to thinking about the time dimension.

⁷⁶ Stalk and Webber, *Competing Against Time*, 100.
⁷⁷ George Stalk, Jr., and Alan M. Webber, "Time's Dark Side of Time," *Harvard Business Review* (Spring 1993), 78.
⁷⁸ Stalk, "Time as Value Stream," 48-55.
⁷⁹ The word of stability is in the spirit of the game theorists, John von Neumann and Oskar Morgenstern, in their pathbreaking book *The Theory of Games and Economic Behavior*, 1944.
⁸⁰ Ibid., 100-1.

Game Theory. Game theory is the mathematical study of interactions between players whose payoffs depend on each other's choices. A general theory of zero-sum games, in which one player's gain is exactly equal to other players' losses, was supplied by John von Neumann and Oskar Morgenstern in their pathbreaking book *The Theory of Games and Economic Behavior*.⁷⁷ There is no general theory of non-zero-sum games, which afford opportunities for cooperation as well as competi-

tion, but research in this area does supply a language and a set of logical tools for analyzing the outcome that is likely-the equilibrium point-given specific rules, payoff structures, and beliefs if players all behave "rationally."⁷⁸

Economists trained in IO started to turn to game theory in the late 1970s as a way of studying competitor dynamics. Since the early 1980s, well over half of all the IO articles published in the leading economics journals have been concerned with some aspect of non-zero-sum game theory.⁷⁹ By the end of the 1980s alone, competition to invest in tangible and intangible assets, strategic control of information, horizontal mergers, network competition and product standardization, contracting, and numerous other settings in which interactive effects were apt to be important had all been modeled using game theory.⁸⁰ The effort continues.

Game-theory IO models tend, despite their diversity, to share an emphasis "on the dynamics of strategic actions and in particular on the role of commitment."⁸¹ The emphasis on commitment or irreversibility grows out of game theory's focus on interactive effects. From this perspective, a

⁹⁴ Ursula L. Lammert, "The Legitimacy and the Rightness of a Promise to Make the Firm's Product Development," *Strategic Management Journal* (April 1994), p. 95.

⁹⁵ For a book-length discussion of commitments, see Paddy Coleman, *Commitment* (New York, 1992). For a discussion of the other modes of dynamic commitment to the market, see, for example, Paddy Coleman, *Strategic and Organizational Commitment* (New York, 1992).

⁹⁶ See, for example, William J. Starling, John C. Patten, and Robert D. Wiley, "Commitment and the Theory of Industry Structure," *Strategic Management Journal* (1994), p. 100. For a discussion of the other modes of dynamic commitment to the market, see, for example, Paddy Coleman, *Strategic and Organizational Commitment* (New York, 1992).

Commitments to durable, firm-specific resources and capabilities that cannot easily be bought or sold account for the persistence observed in most strategies over time. Modern 10 theory also flags such commitments as being responsible for the sustained profit differences among product market competitors: thought experiments as well as formal models indicate that, in the absence of the frictions implied by commitment, hit-and-run entry would lead to perfectly competitive (zero-profit) outcomes even without large numbers of competitors.⁹⁵ A final attraction of commitment as a way of organizing thinking about competitor dynamics is that it can be integrated with other modes of strategic analysis described earlier in this note, as indicated in Figure

14. The ideas behind the figure are very simple. Traditional positioning concepts focus on optimizing the fit between product market activities on the right-hand side of the figure. The bold arrows running from left to right indicate that choices about which activities to perform, and how to perform them, are constrained by capabilities and resources that can be varied only in the long run and that are responsible for sustained profit differences between competitors. The two fainter arrows that feed back from right to left capture the ways in which the activities the organization performs and the resource commitments it makes affect its future opportunity set or capabilities. Finally, the bold arrow that runs from capabilities to resource commitments serves as a reminder that the terms on which an organization can commit resources depend, in part, on the capabilities it has built up.

Markets for Ideas at the Millennium⁹⁶

⁹⁷ For a more extended discussion of the ideas in this paragraph, see Paddy Coleman, "Commitment and Management: The Role of the Firm's Future," *Strategic Management Journal* (1994), p. 100.

A teleology was implicit in the discussion in the last three sections: starting in the 1970s, strategists first sought to probe the two basic dimensions of early portfolio-analytic grids, industry attractiveness and competitive position, and then to add a time or historical dimension to the analysis. Dynamic thinking along the lines

discussed in the previous section and others (e.g., options thinking, systems dynamics, disruptive technologies and change management, to cite just four other areas of enquiry) has absorbed the bulk of academic strategists' attention in the last fifteen-plus years. But when one looks at the practice of strategy in the late 1990s, this simple narrative is complicated by an apparent profusion of tools and ideas about strategy in particular and management in general, many of which are quite ahistorical. Both points are illustrated by indexes of the influence of business ideas such as, for example, importance-weighted citation counts calculated by

Richard Pascale, admittedly with a significant subjective component, that are reproduced in Figure 15.⁽⁹⁷⁾ A complete enumeration, let alone discussion, of contemporary tools and ideas is beyond the scope of this essay, but a few broad points seem worth making about their recent profusion and turnover. Given the forward-looking nature of this discussion, it is inevitably more conjectural than the retrospectives in the previous sections.

Some of the profusion of ideas about strategy and management is probably to be celebrated. Thus, there are advantages to being able to choose from a large menu of ideas rather than from a small one, especially in complex environments where "one size doesn't fit all" (and especially when the fixed costs of idea development are low). Similarly, the rapid turnover of many ideas, which appears to have increased in recent years, can be explained in benign terms as well.⁹⁸ Thus, some argue that the world is changing rapidly, maybe faster than ever before; others, that the rapid peaking followed by a decline in attention to ideas may indicate that they have been successfully internalized rather than discredited; yet others, that at least some of the apparent turnover represents a rhetorical spur to action, rather than real change in the underlying ideas themselves.⁹⁹

¹⁰⁰ For additional discussion of the methodology employed, consult Richard T. Pascale, *Managing on the Edge: The Art of Strategic Thinking* (New York, 1994).

¹⁰¹ For more evidence that management ideas have become shorter-lived, see Paddy Coleman, Paddy Coleman, John C. Patten, and Robert D. Wiley, "Commitment and the Theory of Industry Structure," *Strategic Management Journal* (1994), p. 100.

¹⁰² For a more extended discussion of the ideas in this paragraph, see Paddy Coleman, "Commitment and Management: The Role of the Firm's Future," *Strategic Management Journal* (1994), p. 100.

It seems difficult to maintain, however, that all the patterns evident in Figure 15 conform to monotonic ideals of progress. Consider, for example, what happened with business-process reengineering, the single most prominent entry as of 1995. Reengineering was popularized in the early 1990s by Michael Hammer and James Champy of the consulting firm CSC Index.¹⁰⁰ Hammer originally explained the idea in a 1990 article in the *Harvard Business Review*: "Rather than embedding outdated processes in silicon and software, we should obliterate them and start over. We should... use the power of modern information technol

ogy to radically redesign our business processes in order to achieve dramatic improvements in their performance."¹⁰¹ Hammer and Champy's book, *Reengineering the Corporation*, which came out in 1993, sold nearly two million copies. Surveys in 1994 found that 78 percent of the Fortune 500 companies and 60 percent of a broader sample of 2,200 U.S. companies were engaged in some form of reengineering, on average with several projects apiece.¹⁰² Consulting revenues from reengineering exploded to an estimated \$2.5 billion by 1995.⁽¹⁰³⁾ After 1995, however, there was a bust: consulting revenues plummeted, by perhaps two-thirds over the next three years, as reengineering came to be seen as a euphemism for downsizing and as companies apparently shifted to placing more emphasis on growth (implying, incidentally, that there had been some excesses in their previous efforts to reengineer).

¹⁰⁴ For a more extended discussion of the ideas in this paragraph, see Paddy Coleman, "Commitment and Management: The Role of the Firm's Future," *Strategic Management Journal* (1994), p. 100.

Much of the worry that the extent of profusion or turnover of ideas about management may be excessive from a social standpoint is linked to the observation that this is one of the few areas of intellectual enquiry in which it actually makes sense to talk about markets for ideas. Unlike, say, twenty-five or thirty years ago, truly large amounts of money are at stake, and are actively competed for, in the development of "blockbuster" ideas like reengineering—a process that increasingly seems to fit with the end state described by Schumpeter as the "routinization of innovation." Market-based theoretical models indicate that, on the supply side, private incentives to invest in developing new products are likely, in winner-take-all settings, to exceed social gains.¹⁰⁴ To the extent that market-based, commercial considerations increasingly influence the development of new ideas about management, they are a source of growing concern.

Concerns about supply-side salesmanship are exacerbated by the demand-side informational imperfections of markets for ideas, as opposed to more conventional products. Most fundamentally, the buyer of an idea is unable to judge how much information is worth until it is disclosed to him, but the seller has a difficult time repossessing the information in case the buyer decides, following disclosure, not to pay very much for it.

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