

AN APPLICATION OF ECONOMIC THEORY TO
THE TEACHING OF POLICY AND STRATEGY

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An area of significant difficulty for students in policy and strategy classes is understanding causal relationships in case studies. One approach to providing structure for understanding environment firm relationships is to use the basic concepts of Industrial Organization. Students faced with analyzing policy and strategy decisions in marketing cases tend to feel frustration at the apparent lack of pragmatic theory to guide them. Policies must be considered in light of some normative model if the student is to begin to understand the relationships involved. The authors have bridged this gap of subjective-normative by using the text, American Industry: Structure, Conduct, Performance, 4th Edition, Prentice-Hall, by Richard Caves. The remainder of this paper is devoted to a review of the concepts used from industrial organization and how those concepts are implemented to promote understanding by the student.

Market structure analysis as used by the authors in class, covers the following: (1) Seller Concentration, (2) Product Differentiation, (3) Barriers to Entry in Industry, (4) Buyer Concentration, (5) Fixed Costs—both absolute and relative to variable cost, (6) Growth of Market Demand, (7) Technological Innovation.

Market conduct is identified by examining the firm's potential (likely) policies in five areas: (1) Price Setting Policies, (2) Product Policies, (3) Production Policies, (4) Innovative Policies, (5) Competitive Behavior Policies.

Linkages between the market structure and likely firm behavior in the market place are developed by examining the historical behavior of a firm described in the cases studied. This behavior is then compared to the constraints provided by the market structure. The success or failure of various behavior/market structure combinations, when taken over a series of cases, provides support for the concepts presented. Students are encouraged to examine the reasons behind the variances in their case situations from the text theory. They soon discover that the linkages become less causal the further the firm drifts from the assumption of profit maximization.

Using the approach described above, students generally adapt quickly to the logic of the effect market structure has upon the policies of the firm. The models of price theory taken from earlier courses in economics are typically seen in clearer fashion as they are applied. The presentation of a structure to guide and explain analysis in this complex and unfamiliar area gives the student a logical reference to facilitate understanding.

The third and last link in the chain of causality is performance. The following are the typical measures of performance examined: (1) efficiency, (2) progressiveness, (3) contribution to full employment in economy, and (4) how equitable the firm is in promoting the social and economic distribution of opportunity and wealth in society.

Quite obviously, exact measurement of the above is impossible. Students are encouraged to think about measurement of goals and even goal formulation. How can one promote efficient operation of a firm without a corresponding concept and measurement?

After a background is developed and some working experience gained in industrial organization, students are required to write a paper analyzing an industry using the concepts covered. Students are then assigned to task groups of 3-5 people. This task group forms the nucleus for the student's study group, the case analysis group, and the industry analysis for the remainder of the term. After a short period of initial preparation, the instructor negotiates with each task group and assigns a specific industry for analysis. Student task groups are then given one week to prepare the analysis. During this time, each group must meet with the instructor to review progress. The resultant papers, due the middle of the third week, are typically 10-16 pages long.

The papers are formally presented to other task groups. Depending on class size, presentations to other groups can be altered. Generally a one-hour class period is allocated to the oral presentation of the industry analysis. Both peer and instructor evaluations are used to grade the presentation. The paper is graded by the instructor alone. Each member of the task group receives the grade for the paper based on percentage of total effort as defined by the task group.

Throughout the remainder of the term, students are required to use the structure-conduct-performance analysis on cases where sufficient industry data are present. On occasion, the instructor requires the students to research industry data and perform analysis when the case has inadequate data.