Photograph by Radhika Chalasani/SIPA Press

Recent Studies

China, branding, antitrust, layoffs, globalization, and inflation.

Venturing in China

David Ahlstrom, Garry D. Bruton, and Steven S.Y. Lui,
"Navigating China's Changing Economy: Strategies for Private Firms,"
Business Horizons, Elsevier Science, January/February 2000.
www.elsevier.nl/inca/publications/store/6/2/0/2/1/4/index.htt

Private enterprise in China is flourishing, with about a million companies operating today. But an overseas entrepreneur must overcome formidable obstacles to create a successful enterprise or joint venture. It generally takes *guanxi* (connections) to make a business thrive. Many advisors suggest that cultivating a few key bureaucrats in Beijing will do the job. But economists David Ahlstrom and Steven S.Y. Lui, of the Chinese University of Hong Kong, and Garry D. Bruton, of Texas Christian University, suggest it's the provinces where the real decision-makers are.

China, they argue, should be thought of not as a unified economy, but as a market comparable to the European Union, with some centralization, but also with strong regional devolution. Fully half of Chinese government spending is done by the provinces, and provincial bureaucrats

Martin Morse Wooster
is an associate editor of *The American Enterprise*, a visiting fellow at the Capital Research Center, the education book reviewer of *The Washington Times*, and a contributing editor to *Reason* and *Philanthropy*.

control most of the land. Other government officials are well known for demanding "fees" for protecting factories at night.

These bureaucrats, say the authors, can be dealt with in several ways. Some can be given shares in the new enterprise. Others can be hired as managers, if they can deliver connections. Another good idea is to hire the former village elder who judges local disputes. Even if he's retired, the elder is well respected and can cut through a great deal of red tape.

Charity also helps. The Chinese have long been impressed by people who help the unfortunate. Gifts of schools and community centers build a reputation with local people, especially government officials. One firm donated 100,000 textbooks for middle schools — and found its building permits speedily processed.

Selling Brand Management

Frederick E. Webster, Jr., "Understanding the Relationships Among Brands, Consumers, and Resellers," *Journal of the Academy of Marketing Science*, Sage Publications, Winter 2000.
www.bus.miami.edu/ams/journal.html

For decades, companies have thought the best way to build brands was through "pull" — extensive national advertising designed to show consumers that their brands offered value beyond those of generic competitors. But with many value-minded consumers preferring off-price products, brand equity is on the decline. Successful brands, explains Frederick E. Webster, Jr., a management professor at Dartmouth's Tuck School, can't just pull consumers in — marketers also have to "push" them to retailers.

Many of the great 20th-century brands, including Ford Motor, Frigidaire, and Goodyear, were built through a combination of strong dealer support *and* intensive national advertising. Dealers stocked these brands and promoted them, because they knew manufacturers would offer strong support through advertising and reliable technical assistance.

But many companies implemented brand manager systems that sharply divided the advertising management from corporate sales force management. That division, Mr. Webster argues, makes less and less sense, since this system favors the consumer over the retailer. Successful enterprises, including Procter & Gamble and Intel, know that strong cultivation of retailers ensures that their brands are sold in a way most appealing to consumers.

A more effective strategy is to create field brand managers who have responsibility for both brand promotion and the regional sales force. "A strong brand without strong trade support is an impossibility," Mr. Webster writes, "as is a strong retailer relationship that is not supported by a brand valued by end-users."

Antitrust Law Before Microsoft

William E. Kovacic and Carl Shapiro, "Antitrust Policy: A Century of Economic and Legal Thinking," *Journal of Economic Perspectives*, American Economic Association, Winter 2000.
www.vanderbilt.edu/AEA/jep.htm

The recent Justice Department antitrust suit against Microsoft has some arguing that the federal government is returning to the "trust-busting" tactics of the past. But George Washington University law professor William E. Kovacic and University of California (Berkeley) economist Carl Shapiro suggest antitrust law has evolved a great deal since the Sherman Antitrust Act became law in 1890.

Antitrust law has gone through five phases:

1. Early years (1890–1914). The Supreme Court rules that Standard Oil and American Tobacco are monopolies but allows other big firms (Du Pont, International Harvester) to remain intact. In 1912, the Court rules that a railroad terminal in St. Louis has to open the terminal to all shippers, an important precedent later used to create "equal access" laws for network industries.

2. Laissez-faire (1915–36). The Court, in its most lenient state, fails to order a U.S. Steel breakup and, in 1927, rules that the FTC has no authority to order Eastman Kodak to sell anticompetitive assets.

3. Increased activism (1936–72).

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Congress outlaws price discrimination with the Robinson-Patman Act (1936) and, in the Celler-Kefauver Act (1950), forbids companies to consolidate assets even if the consolidation doesn't create a dominant firm. The Court prohibits mergers that would create firms with a 4.5 percent market share.

4. Increased leniency (1973–91). With the notable exception of the AT&T breakup (1982–84), the courts, under the influence of noted "law and economics" scholars Robert Bork, Richard Posner, and Frank Easterbrook, offer firms more freedom to merge. But at the same time, the courts use factors other than market share, including long-term contracts with suppliers and R&D and advertising budgets, to determine whether a merger is anticompetitive.

5. Synthesis (1992–). Under the Clinton Administration, the courts and the Justice Department use game theory and other technical methods to reject mergers. They increasingly grant leniency to the first member of an alleged cartel to provide incriminating information against rivals. In 1999, for example, the Justice Department levies $750 million in fines — more than has been assessed in all cases since the Sherman Act's creation — against BASF AG and Hoffman-LaRoche Ltd. for fixing vitamin prices, after Rhône-Poulenc SA gives up the conspirators.

But as international business practices become more complex, can regulators determine precisely which corporate practices are anticompetitive? Can regulators create rules that ensure a stable and predictable base for designing business plans? The recent Microsoft and American Airlines antitrust cases, the authors conclude, "place a premium on the ability of the antitrust system to do both of these things."

Taking the Pain out of Layoffs

Gary Charness and David I. Levine, "When Are Layoffs Acceptable? Lessons from a Quasi-Experiment," *Industrial and Labor Relations Review*, New York State School of Industrial and Labor Relations, Cornell University, April 2000.
www.ilr.cornell.edu/depts/ilrrev/

The most painful part of a manager's job is laying off workers. Economists Gary Charness, of Spain's Universitat Pompeu Fabra, and David I. Levine, of the Haas School of Business at the University of California (Berkeley), suggest there are proven methods to make layoffs less painful.

Mr. Charness and Mr. Levine asked several hundred workers in Silicon Valley, Vancouver, and Toronto to rate three scenarios: "gentle layoffs" (four weeks' pay, severance based on seniority, outplacement assistance), "harsh layoffs" (two weeks' pay, no other benefits), and "labor hoarding" (no layoffs and frequent relocation).

Based on the survey, Mr. Charness and Mr. Levine offer bosses the following suggestions:

Keep workers informed. Workers are more likely to accept a layoff if they're told far in advance that hard times might be coming. Among the more acceptable reasons for laying off workers: a downturn in product demand and technological change.

Share the pain. Laid-off workers are more likely to trust a CEO who takes a pay cut during a downturn. Conversely, workers don't mind when their boss receives a substantial compensation package in good times, as long as executive compensation is tied to corporate performance.

Labor hoarding isn't necessary. In the New Economy, most workers don't expect jobs for life, particularly if the price of a lifetime job is having no control over where one lives.

What workers do expect is to be treated respectfully and be given as much information as possible about why a layoff is occurring.

Globalization Makes You Happy
Ronald Inglehart,
"Globalization and Postmodern Values," *Washington Quarterly*, MIT Press, Winter 2000.
www-mitpress.mit.edu/journal-home.tcl?issn=0163660X

Looking for a suitable place to invest? Ronald Inglehart, director of the University of Michigan's Institute for Social Research, suggests that one way of predicting which Third World countries will become stable democracies is to see how happy their residents are.

Mr. Inglehart directs the World Values Survey, which has, since 1970, polled people in 40 countries about their state of well-being. Based on 30 years of survey research, he argues that countries pass through three stages of economic development:

1. Authoritarianism. When poor people feel unable to control their lives, they express their unhappiness as a desire to replace democracy with a strong leader who will bring order out of chaos. This was the general condition of the world in the 1930s and is still the norm in ex-Soviet nations. In the 1990 survey, a majority of the residents of the Communist nations of Eastern Europe and the USSR were unhappy, an important signal that the Soviet Union was doomed. By 1995, Russians registered the unprecedented low score of -12, which meant that nearly all Russians "were unhappy and dissatisfied with their lives." Russian discontent, Mr. Inglehart predicts, means hard times in the near future for Russia and the other former Soviet republics.

2. Materialism. Until a nation's GDP reaches $10,000 per person (comparable to Ireland and South Korea today), most citizens are primarily concerned with making money through hard work and sacrifice for the future.

3. Postmaterialism. Once a nation's GDP crosses the $10,000 per capita barrier, "postmaterial" values prevail, including tolerance for different lifestyles, an interest in "exotic things and cultural diversity," and an increasing distaste for bureaucracy. Postmaterial societies also tend to be stable democracies. Increasing happiness, Mr. Inglehart argues, is an important clue that voters will prefer democracy, since voters tend to trust political systems under which their lives improve. He predicts that Mexico is likely to become a democracy, since its residents are as happy as Spaniards and Italians. And the Chinese, thanks to the wealth that comes through increased trade, "show a predisposition to democracy that will probably surprise most observers."

Inflation: Dead and Loving It
W. Michael Cox and Richard Alm,
"The New Paradigm," 1999 Annual Report, Federal Reserve Bank of Dallas.
www.dallasfed.org/htm/pubs/annual/arpt99.html

Even with today's steady prices, there's always a possibility that inflation will come back. But Federal Reserve Bank of Dallas chief economist W. Michael Cox and *Dallas Morning News* business writer Richard Alm suggest that one lesson of the 1990s is "the upper limit for non-inflationary [GDP] growth might be a full point higher" than economists of 1990 foresaw. Economic forecasters would do a better job if they simply studied price levels instead of examining other warning signs for inflation, they say. "We cannot assume," they write, "that strong GDP or vigorous demand makes a spike in prices inevitable."

The old economics taught that there was a "rivalry" among consumers for goods and services, and that increasing demand too drastically would lead to scarcity and inflation. But many products in the New Economy, such as information and entertainment, don't disappear or degrade with use, so increased demand doesn't lead to scarcity.

Moreover, in the New Economy, most producers have high R&D costs that rapidly amortize once their goods are produced in mass quantities, ensuring "high fixed and low marginal costs." A pharmaceutical manufacturer might invest $350 million in a new drug that costs a penny a pill to produce. Thus the average cost of one pill is $350 million and of 10 million pills $.04. Similar economies of scale occur in other New Economy products, such as software, electronics, and CDs, and in network industries, such as telecommunications, electricity, and natural gas. +