

*Institutions and the Evolution of Modern Business*. Edited by Mark Casson and Mary B. Rose. London: Frank Cass, 1998. Pp. 184. \$42.50 (H/C) \$19.50 (P/B).

This collection of eight and half essays makes an important contribution to both the theory and practice of business history. Six essays employ the new institutional economics and evolutionary theory to examine central issues in economic history and economic development as they arose in specific historical contexts in Western European countries. The other two and a half essays, by S.R.H. Jones and the editors (the “half” is a brief, but wonderful introduction), examine and critique the theoretical literature that provides the basis of the new institutional economics, laying out clearly its strengths and its limitations for contributing to our understanding of business and economic history. In doing this, the volume provides a model of how business history should be done.

The collection puts particular emphasis on local and national cultural differences. The point of the study is not simply to note, as is too often the case, that culture influences business. Rather, each essay addresses, either directly or indirectly, the central question of economic history: what has determined the pace and path of economic development? The comparative perspective taken by these essays, with the attention paid to cultural and institutional differences, allows the authors to discuss very concretely the ways that culture has made a difference to the pace and path of economic development.

S. A. Counce’s essay on the development of the Yorkshire woolen industry is a lovely example of this approach. Counce analyzes the social geography of the region as well as the history of individual families to explain the emergence of an internationally competitive industrial district in Yorkshire in the late 18<sup>th</sup> century. This emergence cannot be explained by a local technological shock, local factors of productions, or the introduction of the factory. Access to and participation in markets was critical, but these markets were not disembodied institutions. To the contrary, access to and participation in markets arose from the embeddedness of those markets in local institutions. Households engaged in home production for the market. Their willingness to do so reflected the particular history and geography of the region -- a substantial non-conformist population, a lack of resident gentry, and the existence of a relatively large number of relatively well-off freeholders. The market in which they participated was a very particular institution -- the local cloth hall -- through which merchants provided information to producers. The existence of community, family, and religious ties did not impede market activity but rather supported it by providing a strong reputational incentive to honor one's economic obligations, both legal and not. Local diversity facilitated development. If one strategy, organization, or method of production or distribution did not work, there were others to be tried.

Oliver Westall’s essay on diversity in the organization of the British insurance industry argues that while transactions cost economics can successfully explain the organization of firms at any point in time, an evolutionary approach is necessary to explain why it was that the “optimal” organizational form changed over time and was different for different branches of the industry. He also makes a point with which I am particularly sympathetic, namely that the growth and success of large bureaucratic

organizations over the twentieth century was predicated on significant market power and the ability to limit price competition.

Hans Sjogren's essay uses a comparative analysis of a sample of financially distressed British and Swedish firms to make a similar point about the importance of contextualizing contractual relationships. The contractual relationships between British lenders and the firms to which they lent and Swedish lenders and their borrowers were quite different. Despite this, in both cases, banks were willing to force distressed firms into bankruptcy. This was the case even for Swedish banks, which were themselves shareholders as well as creditors of the distressed firm. Similarly, British banks did not constrain themselves to the arms length relationship that we might presume. In many cases, British banks stepped in to take control and replace the management of distressed firms.

Matthias Kipping's comparison of the development of business consulting in Britain, France, and Germany demonstrates the importance of national political and cultural institutions in the determination of industry structure and growth. It also demonstrates the importance of national differences in the diffusion of ideas, such as Taylorism, about how firms should be organized. This argument complements the recent work of Chris McKenna that shows that consultants themselves were extremely important agents in the diffusion of managerial ideas.<sup>1</sup> Kipping's essay places those consultants into a broader political and cultural context.

Sverre Knutsen's shows how Norway's distinctive culture and political climate influenced Norwegian industrial policy. Norway placed greater emphasis on small banking institutions participating in government networks and the provision of finance to small, regional firms, rather than the creation of large financial institutions that provided capital to a few privileged firms. Thus Knutsen shows that the "optimal" size of firm depends in part on state policy. In a period in which mergers and planet-sized organizations are treated as the only viable enterprises, it is useful to remember that it is often state policies, not economies of scale, that determine whether small, community-based firms can compete.

Mary Rose's essay also focuses on state policy, providing a clear and convincing explanation of why the U.S. maintained higher tariffs on textile imports than did Britain despite their mutual commitment to free trade. Differences in the cost structure of the two industries or differences in culture or ideology cannot explain the tariff differences. Instead she turns to something often ignored by business historians -- political history. She argues that increasing concentration and growth in firm size, combined with a tactical alliance with labor on this issue, allowed the industry to pressure key members of Congress who, in the decentralized political system in the U.S., had disproportionate power over the setting of tariffs. In contrast, the British industry was internally divided, as small and large producers pursued distinct strategies; a much more centralized British state could ignore the interests of a divided industry whose particular needs conflicted with the state's overall policy goals.

In the final essay in the volume, Casson proposes a “cybernetic” model of the economy, in which firms are viewed as specialized intermediaries rather than as production functions. While most economic models explicitly or implicitly assume that intermediation is costless and the ability to intermediate abundant, Casson argues convincingly that intermediation is costly and the ability to do so requires both highly specific information and a well developed reputation for trustworthiness. Thus Casson provides us with the answer to the time-honored question: if you’re so smart, why aren’t you rich? Economists don’t pick up that dollar bill because they don’t realize that knowing that it’s there is valuable information. Virtually all economic models assume that there is no money to be made from intermediation because such opportunities will quickly be arbitrated away. Intermediation is trivial when you view information as free, easy to get, and easy to transfer. But information is none of those things, and without that information, trade doesn’t take place. People who have information that makes trade possible are richly rewarded.

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<sup>1</sup> See Christopher McKenna, "The Origins of Modern Management Consulting," *Business and Economic History*, Volume 24, Number 1 (Fall 1995): 51-58.