

Title: "The Science of Success: How Market-Based Management Built the World's Largest Private Company"

Author: Charles G. Koch

Publisher: John Wiley & Sons, Inc.

Length: 194 pages

Price: \$24.95 (hardcover)

Reading time: 3 hours

Reading rating: 3 (1 = very difficult; 10 = very easy)

Overall rating: 4 (1 = average; 4 = outstanding)

It is hard to argue with the success of Koch Industries, Inc. (KII) over the past 50 or so years. According to Charles G. Koch, author of *The Science of Success*, the book value of the company has grown 2000-fold since he first joined his father's company in 1961. But the principles and philosophy behind the growth of that company are often debated, even (or perhaps especially) today.

Koch's explanation for KII's success is the strategy he calls Market-Based Management (MBM). The basic premise of MBM is to apply the principles of a free and prosperous society at the level of a firm. There are several elements to MBM, but the most basic keys are 1) an understanding of how value is created and 2) humility about the source and nature of knowledge.

The study of economics has always had its detractors, but Charles Koch is not among them. His contention in *The Science of Success* is that an understanding of economic action is vital to an understanding of business. He credits his successes to an understanding of concepts such as opportunity cost, the sunk cost fallacy, comparative advantage, the subjective nature of value, and how prices are determined by the interaction of marginal costs and benefits. He blames his failures on ignorance or denial of those concepts – he argues that business owners and investors ignore economics at their own peril.

But Koch applies concepts beyond what is found in a typical economics principals course. He notes the importance of knowledge in business and society, and how knowledge tends to be dispersed among people doing different tasks at different times, and important knowledge often belongs to what the Austrian School economist Friedrich Hayek called "the man on the spot," i.e. a worker or consumer who is aware of circumstances that are unknowable to the managers and bureaucrats who try to direct them. He emphasizes that property rights are a crucial precondition for efficient production and gainful trade, and that property rights are a means of harnessing self-interest and thus drive productive, peaceful exchange.

The characteristic feature of *The Science of Success* is its focus on the power of incentives and their relationship to the effective use of knowledge. Koch applies this focus to exchange outside the organization (i.e. dealings with customers and business partners) and also to dealings within the organization. A considerable amount of space is

devoted to understanding how the people within your organization, employees at every level, can create more value when their knowledge is taken advantage of and they are given an appropriate amount of autonomy to act on their knowledge. Further, the author emphasizes the importance of providing workers with appropriate incentives to act in ways that benefit the organization. When the incentives are properly aligned, what economists call the principal-agent problem is diminished.

Perhaps more important than my description and evaluation of the book is the evaluation of the business professionals I teach in WCU's MBA program. I assigned *The Science of Success* last semester to MBA students on a trial basis. The overall response was impressive: the more business experience a student had, the more he or she got out of the book. This book does little to help a student understand abstract concepts; it is for the professional who wants to understand how the seemingly abstract world of economic study actually applies to the business world.

Stephen Miller is an assistant professor of economics in the College of Business at Western Carolina University. His interests include political economy and Austrian School economics. For previously reviewed books, visit us at our website at www.wcu.edu/cob/.