

Department of Economics
University of Toronto
2009/2010

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ECO380: MANAGERIAL ECONOMICS I: COMPETITIVE STRATEGY

Course web site: http://www.economics.utoronto.ca/serrano/teaching/eco380_fall09/eco380.html

LECTURES: Section L5101

Tue 5:10pm-7pm, Room LM 158

DESCRIPTION OF THE COURSE: This course will address a number of issues about industrial organization in order to assess what determines the competitive advantage of firms and their business strategy. We will cover the following topics: product differentiation, firm and entrepreneurial entry, organization of the firm (franchising, vertical integration and mergers), economics of banking and market structure, price discrimination and retail sales, and the economics of innovation and patents. The aim of the course is to build a toolkit of economic strategic concepts adaptable for different purposes in a variety of situations as well as to enhance the critical thinking of the student.

TEXTBOOKS: There is no textbook that covers all the materials for this course. Complementary readings for this course are the following two books:

- [McAfee] McAfee (2002), *Competitive Solutions*
- [BN] Branderburger and Nalebuff (1998), *Co-Opetition*

The complementary readings will be useful to link the topics of industrial organization we cover in class with real life business case studies. Other book you can check at the library: [CP] Carlton and Perloff, *Modern Industrial Organization*

COURSE OUTLINE: (*) Means mandatory reading of all the paper; (**) Means mandatory reading introduction and conclusion.

1. Introduction, Industry Analysis and Competitive Advantage

(*) BN, ch. 1 and 2, ch. 5

(*) McAfee, ch. 1, 2, 3 and ch 4.

CP, ch. 7

2. Product Differentiation and the Product Life Cycle

(*) McAfee, ch. 4 and ch. 5

Klepper, Steven (1996). "Entry, Exit, Growth and Innovation over the Product Life Cycle." *American Economic Review* 86, No. 3. (June 1996), pp. 562-583.

3. Entry: General insights and economics of density and logistics

(*) BN, p. 70-86. and p. 236-247

(**) Holmes, T. (2006), "Walmart and the Economics of Density", Working Paper, University of Minnesota.

(*) McAfee. Entry barriers p. 11-16. Deterring entry p. 44-45

Aghion, P. and P. Bolton, "Contracts as a Barrier to Entry," *American Economic Review* (1987), 388-401

4. Entrepreneurship

(**) Holmes, Thomas (1990). "A Theory of Entrepreneurship and Its Application to the Study of Business Transfers." *Journal of Political Economy*, vol. 98, No. 2, pp. 265-294.

(*) Lazear, Edward. (2004) "Balanced Skills and Entrepreneurship." *American Economic Review*, Vol. 94, No 2, pp. 208-211

(**) Lazear, Edward. (2003) "Entrepreneurship" IZA Discussion Paper No. 760. April 2003.

Astebro, T. and Serrano, C. (2007). "Teamwork." Working paper, University of Toronto.

5. Franchising

(*) Caves and Murphy (1976). "Franchising: Firms, Markets, and Intangible Assets." *Southern Economic Journal*, Vol. 42, No. 4 (Apr. 1976), pp. 572-586.

(**) Mathewson and Winter (1985). "The Economics of Franchising." *Journal of Law and Economics*, Vol. 28, No. 3. (Oct 1985), pp. 503-526.

(**) Gallini and Lutz (1992). "Dual Distribution and Royalty Fees in Franchising." *Journal of Law, Economics & Organization*, Vol. 8, No. 3. (Oct, 1992), pp. 471-501.

6. Vertical Integration: Double Marginalization and the Hold-up Problem

(*) BN, p. 91-103

(*) McAfee, ch. 7; Double marginalization p. 154-157; Holdup problem, p.289-294
CP, ch. 12

7. Mergers and Market Structure: General insights

(*) McAfee, ch. 6

Varian, Hall. Chapter on Non-cooperative Game theory, Cournot, Bertrand, etc. Intermediate Microeconomics: A Modern Approach.

8. Economics of Banking, Financial Stability and Market Structure

(**) Boyd, J., and G. De Nicolo, (2005). "The Theory of Bank Risk-Taking and Competition Revisited", Journal of Finance, 60, 1329-1343.

(**) Boyd, J., G. De Nicolo, and A. Jalal (2009). "Bank Competition, Risk and Asset Allocations". IMF Working Paper WP/09/143.

Diamond, Douglas W. (1984). Financial intermediation and delegated monitoring. Review of Economic Studies 51 (July): 383-414

Diamond, Douglas W., and Dybvig, Philip H. (1983). "Bank runs, deposit insurance, and liquidity", Journal of Political Economy 91 (June): 401-19

Jimenez, G., J. Lopez and J. Saurina, (2007), How does competition impact bank risk taking? working paper, Bank of Spain and Federal Reserve Bank of San Francisco.

(**) Martinez-Miera, D. and Repullo, R. (2008). "Does Competition Reduce the Risk of Bank Failure". Working paper, CEMFI. <http://www.cemfi.es/~dmartinez/files/MMR22jm.pdf>

(**) Stiglitz, J. E., and A. Weiss (1981). "Credit Rationing in Markets with Imperfect Information", American Economic Review, 71, 393-410.

9. Price Discrimination

(*) BN, Bundling p. 250-253. Complexity p. 222-227

(*) McAfee, ch 11

CP, ch. 9 and 10

Varian, Hall. Chapter on Price Discrimination. Intermediate Microeconomics: A Modern Approach.

10. Retail Sales

- (**) Aguirregabiria, V. (1999) "The Dynamics of Markups and Inventories in Retailing Firms," *The Review of Economic Studies*, Vol. 66, pp. 275-308.
- (*)Hendel, I. and Nevo, A. "Sales and Consumer Inventory", joint with Igal Hendel, NBER Working Paper No. 9048, forthcoming *The RAND Journal of Economics*
- (*) Pesendorfer, M. (2003). "Retail Sales: A Study of Pricing Behavior in Supermarkets." *Journal of Business*. Vol 75, No. 1. pp. 33-66.
- (*) Villas-Boas, J.M. (1995) "Models of Competitive Price Promotions: Some Empirical Evidence from the Coffee and Saltine Crackers Markets," *Journal of Economics and Management Strategy*, Vol. 4, pp. 85-107.

11. Patents, Innovation, Management of Patents and Copyrights [Dec 1]

CP, ch. 16

- (*) Arrow (1962) "Economic Welfare and the Allocation of Resources for Invention," in Richard R. Nelson (ed.), *The Rate and Direction of Inventive Activity: Economic and Social Factors*, NBER
- (*) Gans and Stern (2003). "The Product Market and the Market for Ideas: Commercialization Strategies for Technology Entrepreneurs." *Research Policy* 32, 2003.
- Gallini, N. and B. Wright, "Technology Transfer Under Asymmetric Information," 21 *RAND Journal of Economics*, Spring 1990, 147-160.
- Gallini N. and Winter, R. (1985). "Licensing in the Theory of Innovation." *RAND*, vol. 16, No. 2. (Summer 1985), pp. 237-252.
- (*) Hendricks, K. and Sorensen, A. T. "Information Spillovers in the Market for Recorded Music." NBER Working paper No. 12263.
- (**) Pakes, A. and Schankerman (1986). "Estimates of the Value of Patent Rights in European Countries During the Post-1950 Period." *The Economic Journal*, Vol. 96: No. 384, pp. 1052-1076.
- (**) Pakes, A. (1986). "Patents as Options: Some Estimates of the Value of Holding European Patent Stocks." *Econometrica*, Vol. 54, No. 4.
- (**) Serrano, C., "The Market for Intellectual Property: Evidence from the Transfer of Patents", Working Paper, University of Toronto.

GRADING AND EVALUATION:

- There will be three problem sets. Problem sets due dates are posted on them. Problem sets represent 10% of the course grade.
- There will be two one-hour long (approximately) term tests. Term tests represent 40% of the course grade. They will not be cumulative.
- There will be one final exam, which is cumulative, representing 50% of the course grade.

Requests for re-grades will need to be in writing within one week of the term test or problem set being returned. To ensure consistency, I or the TA will re-grade the entire test or problem set, not just a single question. Students are responsible to know both the material of the problem sets, the assigned readings and the one covered during lectures. Collaboration on problem sets is strongly encouraged, but copying the answers from somebody else is not allowed and will be considered plagiarism.

IMPORTANT DATES (tentative dates):

- Oct, 6: Problem set 1 in webpage
- Oct, 20: Term Test 1
- Nov, 3: Problem set 2 in webpage
- Nov, 17: Term Test 2
- Nov, 24: Problem set 3 in webpage
- TBA: Final exam

SCHOLASTIC DISHONESTY: According to the Faculty of Arts and Sciences policy, any act of scholastic dishonesty entails a 0 for the particular assignment and exam or the course. See the Faculty of Arts and Sciences policies for further details on scholastic dishonesty and related matters.

MISSING EXAM AND ASSIGNMENTS POLICY: If you miss one mid-term test during the Fall term, your term test grade will be based on the final exam of the course. If after missing a test you miss another term test, you will earn a zero on it. You may consider re-taking the course when you are able to complete the required work. If you miss to submit a problem set on time, then your grade will be reduced by 25%. If you miss to submit a problem set within 24 hours of the deadline, then you will receive a zero.

E-MAIL POLICY: I will reply to email within 24 hours, except on weekends, with the following provisions:

- The question should require a one (or two) sentence response (maximum). If it takes more, office hours are the more appropriate venue
- I will never answer emails that request information that can be found on the website or the syllabus
- I will not reply to emails concerning grading. For such matters, office hours are more appropriate
- It is also (strongly) preferable that you use a utoronto email address: My spam filter is set to maximum. Moreover, university policy stipulates a preference for these email addresses.
- Always identify yourself, course and section in your email.
- Please do not send attachments of any kind.
- Please do not submit term work by email.

I should note, however, that I encourage you to provide course feedback and comments via email, if you wish.

PREREQUISITES AND EXCLUSIONS POLICY:

Prerequisites: ECO200Y5 or ECO206Y5
ECO220Y5 or ECO227Y5 or (STA250H1 and STA257H5) or (STA257H5 and STA261H5)
Exclusions: ECO310Y5

You must contact Robbie Innes at rinnes@chass.utoronto.ca for enrolment and prerequisite issues.