

Syllabus for ECON 106I Organizational Economics

Spring 2017, Department of Economics UCLA

Time and Location:

Lec 1 Monday and Wednesday, 9:30am – 10:45am, Pub Aff 2270

Lec 2 Monday and Wednesday, 11:00am – 12:15pm, Pub Aff 2270

Instructor:

Moritz Meyer-ter-Vehn

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Office Hour: Monday and Wednesday, 2pm – 3pm, Bunche Hall 9365

Grader:

Vladimir Pecheu

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Office Hour: Tuesday, 11am – 12pm, Bunche Hall 2250

Overview:

This course is about the economics of the modern firm in theory and practice with an emphasis on personnel economics, that is, the economic theory of careers and human resource management. It prepares students for a wide range of careers in which they will be faced with the challenge of advising or managing firms. Such careers include positions in management of firms themselves or management consulting firms. The class covers theoretical models as well as empirical evidence and case studies that illustrate the concepts introduced in the context of actual companies. Outside industry experts will moderate the case discussions and relate the topics discussed in class to their real life jobs.

One of the most important results in neoclassical economics you learnt in Econ 11 and 101, the first welfare theorem, states that under “perfect competition”, individual utility maximization leads to socially optimal outcomes. The assumptions of this theorem are frequently violated in practice. Sometimes, firms have market power and can overcharge customers, pushing low-value customers out of the market. In other ex-ante competitive situations, the realization of economic benefits requires parties to invest into their relationship, but once such investments are sunk the counter-party might renege on the agreement; for instance, a new employee may need to relocate his family across the country for a new job, but then the employer may renege on the promised career opportunities. In yet other situations, the quality of goods or especially services may be hard to specify or ascertain, and consequently underprovided; simply put, if my wage does

not depend on the quality of my work, why try so hard? This problem is accentuated in modern work environments with highly specialized tasks, where the observable quality of the final product cannot easily be traced back to the individuals who contributed to it.

But rational economic agents do not need to sit idly by in the face of these problems. If a local cheese factory has natural monopsony power to buy local farmers' milk, it may make sense for the farmers to cooperatively own this factory. When a firm's operations become too intertwined with a supplier that neither can live without the other, and long-term contracts cannot specify the relevant contingencies in the face of uncertainty, it may make sense for the firms to integrate vertically. And in personnel economics, we can interpret the vast variety of employment relationships, from tenured government employees with fixed salaries, to bonus-driven sales people, to completely independent contractors, as institutional attempts to provide incentives for high-quality work in varying circumstances. Other institutions, such as reputation mechanisms on Uber (or indeed on Bruinwalk) help consumers share information and provide incentives for good service.

Prerequisite:

We will use some game theory, as well as basic calculus and probability theory. Intermediate Microeconomics, Econ 101, is a prerequisite for this course. Game Theory, Econ 106G, is useful but not required. Economics of Technology and e-Commerce, Econ 106T, is complementary but not required.

Final Exam:

Saturday, June 10th, 3:00pm – 6:00pm

Grading:

The grade for the class will be based on two problem sets with formal questions (10% each), two case-studies write-ups (10% each), class participation, especially in the case study discussions (10%), and the final (50%), which will include both essay and formal questions. I encourage you to work together on the problem sets and the case-study write-ups; you can submit your solutions in groups of up to four students. You cannot copy answers from other groups. The exams are closed-book and everyone works by themselves.

Textbook:

Paul Milgrom and John Roberts, "[Economics, Organization and Management](#)" - this book is available at the UCLA Book Store and two presence copies are available at the College Library.

There are other supplementary books/articles that are helpful for this class.

- Donald Campbell, "[Incentives](#)"
- Sytse Douma and Hein Schreuder, "[Economic Approaches to Organisations](#)"
- Luis Garicano and Luis Rayo, "[Why Organizations Fail: Models and Cases](#)"
- Henry Hansmann, "[The Ownership of Enterprise](#)"

- Peter Kuhn, “Personnel Economics” forthcoming
- Edward Lazear, “[Personnel Economics](#)”
- Louis Putterman and Randall Kroszner, “[The Economic Nature of the Firm](#)”
- John Roberts, “[The Modern Firm](#)”

Case Studies:

I have put together a course pack of 4 Harvard Business School case studies at <http://cb.hbsp.harvard.edu/cbmp/access/61690326> that you will need to purchase for \$17.

Class Outline:

Introduction: Examples and Class Logistics

- Milgrom, Roberts 1
- Roberts 1

Economic Organization and Efficiency

- Milgrom, Roberts 2
- Douma, Schreuder 1

Coordination through Markets and Management

- Milgrom, Roberts 3-4
- Douma, Schreuder 2-3

Incentive problems in markets and organizations (~2 classes)

- Milgrom, Roberts 5-6
- Douma, Schreuder 4

Incentive Contracts (~2 classes)

- Milgrom, Roberts 7-8

Ownership

- Milgrom, Roberts 9
- Hansmann 1-5

Case Study “Family Feud: Andersen vs. Andersen”

Employment (~3 classes)

- Milgrom, Roberts 10-12
- Lazear 2-5, 8, 9

Case Studies “Safelite Carglass” and “Lincoln Electric”

Organization of Firms (~3 classes)

- Garicano and Rayo

Case Study “Challenger”