

## Applied Economic Analysis

MBA 710

Section 1

TTh 5:30-6:45 PM

BEH 105

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Fall 2005

**Text:** *Microeconomics for Managers* and *Student's Companion to Microeconomics for Managers* by David M. Kreps, Norton, 2004.

**Office Hours:** TR 3:30 to 5:00 PM and by appointment

**Objective:** Students who successfully complete this course will begin to think the way an economist thinks. You will understand how markets work and how firms price goods and services under various market structures. You will understand the nature of incomplete information problems – adverse selection and moral hazard – and how to protect against these problems when dealing with others. Finally, you will see how the basic tools of microeconomic analysis provide insight to business decisions. Learning objectives include (1) Critically analyze an industry and a specific firm within an industry; (2) Synthesize important relationships across business disciplines; (3) Apply economic and behavioral concepts to strategy formulation, (4) Be able to assess and manage business risk; (5) Explain and apply analytical constructs to business problem solving; (6) Design organizations to make and implement specific business decisions under given performance requirements; and (7) Recognize the special opportunities and challenges presented by the global business environment.

**Evaluation:** The course evaluation for each student involves two separate components. First, 10 homework assignments are due at the Tuesday class. I drop the three lowest scores. Students will work in study groups of four (4) and each study group submits a homework assignment. Second, each student will take the three in-class exams. The first two exams are given in the Thursday class. The final exam is not comprehensive, but only covers the material not covered in exams 1 and 2. The final exam is given during the final exam week. While I prefer to maintain some flexibility, I propose weighting the component parts as follows: 35% for the graded homework assignments, 15% for the somewhat shorter first exam, and 25% each for the last two exams.

**WebCT:** This course is a WebCT course. I will post the course outline, homework assignments, other handouts, and so on at the WebCT site. You can access this site 24/7, except for scheduled maintenance on the system and unexpected downtimes due to technical glitches.

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**Academic**

**Dishonesty:** Academic dishonesty (e.g., cheating and plagiarism) will not be tolerated. At the instructor's discretion, a student suspected of academic dishonesty may receive an F for the course and be expelled from the class. Additional penalties, up to expulsion from the University, are possible.

**Disabilities:** The UNLV Disability Resource Center (DRC) houses the resources for students with disabilities. If you have a documented disability that may require accommodations, you will need to contact the Disability Resource Center (DRC) for coordination in your academic accommodations. The DRC is located in the Student Services Complex (SSC), Room 137. Their numbers are: (702) 895-0866 (voice), (702) 895-0652 (TTD) and (702) 895-0651 (fax). For additional information, please visit the following web address: <http://www.unlv.edu/studentlife/drc>

**Course Outline**

	<b>Topics Covered</b>	<b>Assigned Readings, Practice Problems, and Homework Problems</b>
<b>Week 1</b>	Thirty takeaways What motivates workers? Economics and organizational behavior Why study microeconomics? GM truck coupons example	Chapters 25 and 1. Economic Tutorial. Practice Problems: 1.1. Homework 0 (not graded). Survey (not graded).
<b>Week 2</b>	Marginal analysis: four puzzles <ul style="list-style-type: none"> <li>Should developer build more luxury boxes?</li> <li>Selling seats at a soccer game</li> <li>Profitability and product lines</li> <li>Should "Fredonia" export steel?</li> </ul> Demand and Supply: First look	Chapters 3 and 2. Practice Problems: 2.2, 3.3, 3.4, and 3.10. Homework 1: 3.9. Homework 0 due.
<b>Week 3</b>	Demand: Second look <ul style="list-style-type: none"> <li>Demand and inverse demand</li> <li>Market demand and demand facing firm</li> </ul> How well do firms know their demand? Demand elasticity: Invariance measure <ul style="list-style-type: none"> <li>Marginal revenue and demand elasticity</li> </ul> Consumer choice: Bangs for the buck <ul style="list-style-type: none"> <li>Marginal analysis</li> </ul> Indifference curves: Equal bangs for the buck Budget lines: Constraint on total bucks	Chapters 4 and 5. Practice Problems: 4.4, 4.10, and 4.14. Homework 2: 4.8 and 4.13. Homework 1 due.
<b>Week 4</b>	Porsche retailing problem in US market Two-step distribution and double marginalization <ul style="list-style-type: none"> <li>Does direct marketing to public prove superior?</li> </ul> Why do we observe retailers? <ul style="list-style-type: none"> <li>Up-front fees: Having your cake and eating it too</li> <li>Enter psychology: Is it fair?</li> </ul> Back to Porsche problem Why laws protect franchisees?  <b>Exam 1 (Weeks 1 to 3)</b>	Chapters 6. Practice Problems: 6.1. Homework 2 due.
<b>Week 5</b>	Surplus extraction <ul style="list-style-type: none"> <li>Third-degree price discrimination</li> <li>Second-degree price discrimination</li> <li>First-degree price discrimination</li> </ul>	Chapters 7. Pricing with Market Power: Notes. Practice Problems: 7.1, 7.6, 7.8, 8.1, and 8.5 Homework 3: 7.2

<p><b>Week 6</b></p>	<p>Relationship between averages and margins  Profit maximization</p> <ul style="list-style-type: none"> <li>• Total revenue and total cost</li> <li>• Average and marginal cost</li> <li>• Average and marginal revenue</li> </ul> <p>Marginal revenue equals marginal cost: Cost and efficient scale of production  Cost minimization</p> <ul style="list-style-type: none"> <li>• Isoquants: Many ways to “skin a cat”</li> <li>• Returns to scale</li> <li>• Marginal analysis</li> <li>• Average cost and returns to scale</li> </ul>	<p>Chapters 8 and 9.  Practice Problems: 9.1, 9.8, 9.9, 10.1  Homework 4: 8.7  Homework 3 due.</p>
<p><b>Week 7</b></p>	<p>Profits today, tomorrow, and next year</p> <ul style="list-style-type: none"> <li>• Short-run and long-run cost functions</li> </ul> <p>Durable assets</p> <ul style="list-style-type: none"> <li>• Accounting depreciation and income statements</li> </ul> <p>Know how</p> <ul style="list-style-type: none"> <li>• Experience curve</li> </ul> <p>Total Quality Management (TQM)  Perfect competition and supply: Second look  Firm supply</p> <ul style="list-style-type: none"> <li>• Marginal analysis</li> </ul> <p>Firm to market and competitive equilibrium</p> <ul style="list-style-type: none"> <li>• Short and intermediate run</li> <li>• Long run</li> </ul> <p>Entry and exit and the long-run supply</p> <ul style="list-style-type: none"> <li>• Accounting and economic profits</li> </ul>	<p>Chapters 10 and 11.  Practice Problems: 11.1, 12.1, 12.5, 12.6  Homework 5: 9.2  Homework 4 due.</p>
<p><b>Week 8</b></p>	<p>Competitive markets and efficiency  Defining and dividing the surplus</p> <ul style="list-style-type: none"> <li>• Producer surplus</li> <li>• Consumer surplus</li> </ul> <p>Competitive markets maximize total surplus</p> <ul style="list-style-type: none"> <li>• Government’s slice: Introduction</li> </ul> <p>Efficiency versus equity  Government’s slice: More details  Tax in competitive market</p> <ul style="list-style-type: none"> <li>• (Dead weight) loss of surplus</li> </ul> <p>Tax on monopolist  Price supports  Price ceilings  Regulation and deregulation</p>	<p>Chapters 12 and 13.  Practice Problems: 13.1, 13.3  Homework 6: 11.2  Homework 5 due.</p>
<p><b>Week 9</b></p>	<p>Individual decisions and uncertainty  Risk aversion and anomalies  Expected utility model: Intuitive</p> <ul style="list-style-type: none"> <li>• Certainty equivalents: Valuing gambles to certain payments</li> <li>• Risk-aversion behavior</li> <li>• Risk-seeking behavior</li> </ul> <p>Anomalies to expected utility model</p> <p><b>Exam 2 (weeks 4 to 8)</b></p>	<p>Chapters 15 and 16.  Practice Problems: 15.1, 16.1  Homework 6 due.</p>

<b>Week 10</b>	<p>Expected utility model: Formal</p> <ul style="list-style-type: none"> <li>• Required behavior properties and anomalies</li> </ul> <p>Does it make sense?</p> <p>Spreading and sharing risk: Intuition</p> <p>Risk does not always spread</p> <p>Correlation between gambles</p> <p>Efficient risk sharing</p>	<p>Chapters 16 and 17.</p> <p>Practice Problems: 16.2, 17.1, 17.2</p> <p>Homework 7: 15.2</p>
<b>Week 11</b>	<p>Hidden information: Adverse selection</p> <ul style="list-style-type: none"> <li>• “Lemons” market</li> <li>• Signaling and screening</li> <li>• Winner’s curse</li> </ul> <p>Hidden information: Moral hazard</p> <ul style="list-style-type: none"> <li>• Incentives</li> <li>• Risk sharing versus motivation</li> </ul>	<p>Chapters 18 and 19.</p> <p>Practice Problems: 18.1, 19.1</p> <p>Homework 8: Handout</p> <p>Homework 7 due.</p>
<b>Week 12</b>	<p>Porter’s five forces</p> <ul style="list-style-type: none"> <li>• Rivalry (competition)</li> <li>• Potential entrants</li> <li>• Substitute (complement) products</li> <li>• Customer bargaining power</li> <li>• Supplier bargaining power</li> </ul> <p>Industry niches</p> <p>Noncooperative games</p> <ul style="list-style-type: none"> <li>• Strategic-form</li> <li>• Extensive form</li> </ul> <p>Dominance in strategic-form games</p> <ul style="list-style-type: none"> <li>• Does dominance make sense?</li> </ul> <p>Nash equilibrium</p> <p>When does unpredictability pay? Mixed strategies</p> <p>Backward induction in extensive-form games</p> <ul style="list-style-type: none"> <li>• Does backward induction make sense?</li> </ul>	<p>Chapters 20 and 21.</p> <p>Practice Problems: 21.1, 21.3, 21.7</p> <p>Homework 9: 18.2</p> <p>Homework 8 due.</p>
<b>Week 13</b>	<p>Reciprocity and collusion</p> <p>Prisoner’s dilemma and the “folk theorem”</p> <ul style="list-style-type: none"> <li>• Naïve cooperation</li> <li>• Grim cooperation</li> <li>• Tit for tat</li> </ul> <p>Finite and infinite horizons</p> <p>Collusion and oligopoly</p>	<p>Chapters 22.</p> <p>Homework 9 due.</p>
<b>Week 14</b>	<p>Credibility</p> <ul style="list-style-type: none"> <li>• Tying your own hands</li> <li>• Cheap talk</li> </ul> <p>Reputation</p> <ul style="list-style-type: none"> <li>• Trustworthy</li> <li>• Tough</li> <li>• Noise and ambiguity</li> </ul> <p>Monopolist: Credibility and reputation</p> <p>Transaction cost economics</p> <ul style="list-style-type: none"> <li>• Unified governance</li> <li>• Relational contracting</li> </ul> <p>Boundary of the firm</p> <ul style="list-style-type: none"> <li>• Legal embodiment of unified governance</li> <li>• Focus of reputation stake</li> <li>• Focus of specific reputation</li> <li>• Affect expectations and tastes</li> </ul> <p>Ethical behavior</p>	<p>Chapters 23 and 24.</p> <p>Homework 10: 21.4.</p>

<b>Week 15</b>	Thirty takeaways Review and summary	Chapters 25. Homework 10 due.
<b>Week 16</b>	<b>Exam 3 (weeks 9 to 14)</b>	