

Economics 70362: Industrial Organization II

Spring 2009

Professor Jensen

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Office Hours: Wednesday; and by appointment.

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Classes: Tuesday, 4:00 – 6:30 pm, 600 Hesburgh Library

Required Text: The Theory of Industrial Organization, Jean Tirole.

Recommended Texts:

International Handbook of Industrial Organization (Volumes 1, 2, and 3). The first two volumes are dated, but still have some value – especially in providing overviews.

Modern Industrial Organization, Dennis Carlton and Jeffrey Perloff (an undergraduate text with an extremely thorough coverage of IO, easy to read).

Course Objectives:

This course has two objectives. One is to provide a survey of some of the theoretical models used to analyze the strategic interaction between firms in an industry. The other is to survey recent advances in the literature by studying recently published papers.

Grading: The course grade is based on:

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| (i) Problem sets | 50% |
| (ii) Option of Paper or Presentation or Final | 50% |

On problem sets, I encourage you to work together. In fact, if you like, any combination of you can form a “team” and turn in one problem set with several names on it (in which case each participant receives the same grade on that problem set). I have found that students are very good at minimizing the free rider problem.

The other half will be your option:

- Take a final exam.
- Present to the class an article on an IO topic of interest to you published with the last 5 years.
- Write a paper that develops a model and outlines how to analyze it to derive some results of interest in industrial organization. This would probably need to be about 10 to 15 pages (double-spaced). If you decide to do this, you will need to get the topic approved by me. Generally I would expect you to take this option only if you were thinking of a second-year paper or dissertation in this area.

Course Outline

0. Game Theory Topics and References

A. Games in Strategic Form (Nash Equilibria)

1. Tirole (11.1, 11.2)

2. IHIO (5.2.1, 5.2.2, 5.2.3)

3. Supplemental Readings:

“Non-Cooperative Games,” John Nash, Annals of Mathematics (1951)

Game Theory, Roger B. Myerson (excellent, but demanding)

Game Theory, Drew Fudenberg and Jean Tirole (ditto)

Game Theory, James W. Friedman

Games and Information, Eric Rasmusen

Thinking Strategically, by Avinash Dixit and Barry Nalebuff (entertaining to read)

B. Games in Extensive Form (Subgame Perfect Equilibria)

1. Tirole (11.3)

2. IHIO (5.3.1, 5.3.2)

3. Supplemental Readings:

“Reexamination of the Perfectness Concept for Equilibrium Points in Extensive Form Games,” Reinhard Selten, International Journal of Game Theory (1975)

Texts by Myerson, Fudenberg and Tirole, Friedman, and Rasmusen

C. Games with Incomplete Information (Bayesian and Perfect Bayesian Equilibria)

1. Tirole (11.4, 11.5)

2. IHIO (5.4.1, 5.4.2, 5.5.1, 5.5.2)

3. Supplemental Readings:

“Games with Incomplete Information Played by Bayesian Players, I-III,” John Harsanyi, Management Science (1967-8)

Texts by Myerson, Friedman, Fudenberg and Tirole, and Rasmusen

I. Product Differentiation: Price Competition and Non-Price Competition

A. Monopolistic Competition

1. Tirole (7.2)

2. IHIO (4.3, 12.2)

B. Advertising and Informational Product Differentiation

1. Tirole (7.3)

2. Supplemental Readings:

The Economics of Advertising, Schmalensee

“A Model of Advertising and Product Quality,” Schmalensee, Journal of Political Economy (1978)

“Notes on Advertising, Economies of Scale, and Entry Barriers,” A. M. Spence, Quarterly Journal of Economics (1980)

C. Vertical Product Differentiation

1. Tirole (7.5)

2. IHIO (12.6)

3. Supplemental Reading:

“Relaxing Price Competition Through Product Differentiation,” Review of Economic Studies, J. Shaked and J. Sutton (1982)

II. Asymmetric Information, Reputation, and Strategic Behavior

A. Sharing Cost Information

1. Tirole (9.1)

2. Supplemental Readings:

“Information Transmission-Cournot and Bertrand Equilibria,” Gal-Or, Review of Economic Studies (1986)

“Exchange of Cost Information in Oligopoly,” Shapiro, Review of Economic Studies (1986)

“Sharing Cost Information: A Counterexample,” Jensen, Economic Theory (1993)

III. Mergers

A. Mergers Laws, Enforcement, and Effects

“Antitrust Policy Toward Horizontal Mergers” (IHIO Ch. 36)

B. Endogenous Mergers

“The Limits of Monopolization Through Acquisition,” Quarterly Journal of Economics, M.I. Kamien and I. Zang (1990)

IV. Research and Development, Innovation, Patents, and Adoption of New Technology

A. Innovation and R&D

1. Tirole (10.1, 10.3, 10.4)

2. IHIO (14)

3. Supplemental Readings:

“Economic Welfare and the Allocation of Resources for Invention,” Arrow, in The Rate and Direction of Inventive Activity, ed. by R. Nelson (1962)

“Real Effects of Academic Research,” Jaffe, American Economic Review (1989)

“Geographic Localization of Knowledge Spillovers as Evidenced by Patent Citations,” Jaffe, Trajtenberg and Henderson, Quarterly Journal of Economics (1993)

“The Management of Innovation,” Aghion and Tirole, Quarterly Journal of Economics (1994)

“Intellectual Capital and the Firm: The Technology of Geographically Localized Knowledge Spillovers,” Zucker, Darby and Armstrong, NBER Working Paper #4946 (1994).

“Universities as a Source of Commercial Technology: A Detailed Analysis of University Patenting, 1965-1988,” Henderson, Jaffe and Trajtenberg, NBER Working Paper #5068 (1995).

“Star Scientists and Institutional Transformation: Patterns of Invention and Innovation in the Formation of the Biotechnology Industry,” Zucker and Darby, Proceedings of the National Academy of Sciences (1996)

“Intellectual Capital and the Birth of U.S. Biotechnology Enterprises,” Zucker, Darby and Brewer, American Economic Review (1998)

B. Patent Races.

1. Tirole (10.2)
 2. IHIO (14.2)
 3. Supplemental Reading:
 - “Patent Races, Product Standards, and International Competition,” Jensen and Thursby, International Economic Review (1996)
- C. Adoption and Diffusion of New Technology
1. Tirole (10.5)
 2. IHIO (14.5)
 3. Supplemental Readings:
 - “Adoption and Diffusion of an Innovation of Uncertain Profitability,” Jensen, Journal of Economic Theory (1982)
 - “Innovation Adoption and Diffusion When There Are Competing Innovations,” Jensen, Journal of Economic Theory (1983)
 - “Entry, Exit, and Diffusion with Learning by Doing,” Jovanovic and Lach, American Economic Review (1989)
 - “Innovation Adoption and Welfare Under Uncertainty,” Jensen, Journal of Industrial Economics (1992)
 - “Strategic Timing of Adoption of New Technologies Under Uncertainty,” Stenbacka and Tombak, International Journal of Industrial Organization (1994)
 - “Demand and Supply in New Markets: Diffusion with Bilateral Learning,” Vettas, RAND Journal of Economics (1998)
- D. Patent Licensing, Research Joint Ventures
1. Tirole (10.8)
 2. IHIO (14.4)
 3. Supplementary Readings:
 - “Technology Transfer under Asymmetric Information,” Gallini and Wright, RAND Journal of Economics (1990)
 - “Patent Licensing,” M. I. Kamien, in The Handbook of Game Theory, ed. by Aumann and Hart (1992)
 - “Dynamic Patent Licensing,” Jensen, International Journal of Industrial Organization (1992)
 - “Reputational Spillovers, Innovation, Licensing, and Entry,” Jensen, International Journal of Industrial Organization (1992)
 - “The Licensing of Patents under Asymmetric Information,” Beggs, International Journal of Industrial Organization (1992)
 - “RJV and R&D Cartels,” Kamien, Muller, and Zang, American Economic Review (1992)
 - “Proofs and Prototypes for Sale: The Tale of University Licensing,” Jensen and Thursby, American Economic Review (2001)