

**MANAGERIAL ECONOMICS:
ORGANIZATIONS, MARKETS AND MANAGEMENT
MBA 6240
COURSE SYLLABUS**

**Masters of Business Administration Program
Max M. Fisher College of Business
The Ohio State University**

Professor Jay Dial

COURSE OBJECTIVES

To develop an economics-oriented framework that facilitates the identification and analysis of business problems, and the development and implementation of solutions to those problems. The tools of the course apply to economy-wide problems, industry-wide problems, firm and organization specific problems and individual decision-making. You should expect to leave the course, not with a set of "cookbook" solutions to problems, but with a set of new, powerful ways of thinking about business problems and their solutions.

APPROACH TO PROBLEMS AND SOLUTIONS

The course material stresses the importance of theory in solving problems, and combines theory development with both examples and case analyses that illuminate and challenge the theory. While the material is theoretical and analytical, it is not mathematically technical. At times the material may be extraordinarily frustrating, at others deceptively easy. As is so often the case in business, what appears obvious and simple is often, in fact, subtle and complex. Frustration often results from material that adopts a position radically different from students' current views. At such times the material can seem one-sided, and this is exacerbated by the fact that the analysis can lead to an unambiguous point-of-view that is controversial.

CLASSROOM ENVIRONMENT

With the objective of establishing as dynamic and effective a learning environment as possible, the course requires a commitment on your part not only to attend all classes, but to prepare fully and to participate. We will work together to create an environment in which open, rigorous discourse is the standard. Thus, each of you must be willing not only to share your ideas and analysis with your colleagues, but be open to well-intentioned challenges of those ideas.

COURSE MATERIALS

The course material is cumulative, making it important to keep up with the readings, to pay close attention to class discussions, and to keep good notes. Failure to do so can leave students lost and confused when it comes time to apply the material. I recommend that you review the course materials and your course notes regularly. Readings, cases, journal articles, discussion questions and study questions will form the basis of class discussions. The text is a custom text provided by Irwin/McGraw-Hill. It uses selected chapters from two separate texts:

Principles of Micro-Economics, Robert H. Frank and Ben S. Bernanke, Irwin/McGraw-Hill, 2007

Managerial Economics and Organizational Architecture, James A. Brickley, Clifford W. Smith, Jr. and Jerold L. Zimmerman, 2006, 4th Edition.

Typically, students comprehend much of the textbook material without substantial lecturing by the instructor. Thus, while there will be some lectures on the more important and/or difficult material, most of our class time will be spent applying the theory and concepts to problems through open, interactive classroom discussion.

Each session's assignment contains a set of questions. You might find it helpful to read the discussion questions both before and after reading the assigned materials. Past students have found this to be a useful way to focus their reading efforts and prepare for class discussions.

SEATING ARRANGEMENTS

I would like to request that you sit in the same seat each day. This helps me keep track of class contribution and makes it easier for you to interact with each other during class discussions. Please select your preferred seat at the beginning of our second session and try to sit in this seat in each session during the remainder of the quarter.

COURSE REQUIREMENTS AND GRADING

The following are the general principles of grading in this course:

- The requirements of the course are identical for everyone. This means it is not possible to make up for poor performance through extra credit work.
- No late assignments will be accepted for any reason.
- Exams cannot be retaken or taken at other than the scheduled time except under extreme circumstances.

There are 250 possible points to be earned through assignments for this course. The points are allocated as follows:

- *Contribution to class discussions*: 30 points
- *Individual problem sets (3)*: 60 points total
- *Group Projects (2)*: 60 points total
- *Final Exam*: 100 points

Grade Appeal Policy: Grades on exams and assignments are intended to reflect the overall quality of performance of the student(s). If you think your grade on an exam or assignment does not reflect the quality of your performance, submit a clear written explanation of your reasoning within one week after the return of your assignment or exam. The written document need not be long, but must clearly identify the problem or issue of concern. I will carefully consider all such appeals. There will be no grading appeals after the one week deadline has passed.

OFFICE APPOINTMENTS (virtual and otherwise)

I am happy to discuss any issues of concern to you on an individual basis either after class, in my office, via phone or via email. My office is in Fisher Hall 860, my office phone is 614-292-5438, my email is dial.12@osu.edu. Email is best.

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Class Format - The Case Method: Why We Rely on Discussion Learning

Most of our class time will be spent discussing business cases. Why do we rely on the case method so extensively and how do these discussions enhance our learning? The case-study method brings a “real world” approach to business education in at least three important ways. First, case discussions generate a dynamic process of vigorous questioning and responding, examination and debate among students and discussion leader. Because strategy issues are often characterized by ambiguity, complexity or uncertainty, this course is more about *asking the right questions* than it is about knowing the right answers. Rather than simply lecture about the current state of “best practices,” we recognize that theories change over time but reasoning skills survive. So the case method helps students to refine their skills as insightful questioners, rather than just good answer-finders. In this model of learning, it is the *journey* more than the *destination* that matters. In addition, discussion learning requires all students to participate *actively* in the learning experience. The MBA degree is about more than just acquiring a tool box of analytical skills. It is also about developing the ability to contribute to the group so that we expand the boundaries of everyone’s learning. Just as in management, there is no formula that you can follow for every case. Nevertheless, over the course of the academic quarter, students gradually build on a combination of theory and analysis as well as judgment and experience to acquire important skills that the general manager needs. The case method requires a high level of student commitment where students personally engage the problem and “own” the solution. Consequently, the case method is inherently a student-oriented process. Walter Wriston has said, “Good judgment comes from experience. Experience comes from bad judgment.” As in the “real world,” the case method replicates the trial-and-error experience of seasoned managers, thereby deepening judgment. It also does so in the low risk environment of the classroom where career casualties are not at stake.

Second, the case method trains students to think as administrators (rather than as scholars), so that they: (1) see a problem looking for solutions rather than a concept looking for applications, (2) focus on defining and prioritizing a maize of tangled problems and determining which one(s) to attack with the limited time and resources available, (3) appreciate differing agendas and points of view, and (4) *take action*, not just report findings.

Third, by linking analysis with individual action, the case method encourages moral awareness by requiring students to *take a stand*. The give-and-take of case discussion often brings to the surface subtle ethical dilemmas that might otherwise be missed. The case method helps students learn to assess and embrace the tradeoffs among different stakeholders’ interests. The case method requires students to use all of their knowledge, skills and experience to respond in real time to the questions raised in class and to effectively communicate their ideas to classmates to create a greater shared understanding of the problem at hand. Thus, students also become the teachers as well as learners.

In sum, we teach with case studies because the method embodies important values of professional education. The case method is not simply a technique; it is a rich philosophy about judgment, analysis, action and learning. (*The preceding was adapted from an article by Robert F. Bruner*)

While our applications will emphasize exercise of judgment, by no means is this course “theory free.” We will learn to break down complex problems into manageable analytical issues where we can then apply a rigorous set of theoretical tools. The analytical approaches in our “strategy tool kit” will be covered in the required readings prior to each case. These readings have been carefully selected to convey often complex topics in a concise, understandable manner. In general, I have assigned managerially-oriented readings and spared you the pain of reading pointy-headed, scholarly-type articles. Since these readings articulate much of the theoretical content of the course, they will be crucial to your comprehension of our course concepts. It is extremely important that you read, study and discuss the articles with each other when assigned so that you will be able to apply the concepts to our case discussions.

The key requirement of this course is that you THINK. This course requires that you synthesize material that you have learned in prior classes in your business education in conjunction with new concepts we will introduce. I will ask that you add a dose of common sense and filter these ideas through your own experiences and “world view.” We will reach consensus on *some* issues, yet many among you will have differing interpretations as we proceed through the course. This is the nature of strategy and policy issues. You may find yourself occasionally frustrated by the ambiguity and the difficulty of assimilating conflicting points of view. Welcome to real life.

Our readings and case discussions are designed to help you understand how firms formulate and implement strategies under the impetus of competition, technology, government action, and other important contextual forces. This, in turn, requires a deep understanding of the functional strategies associated with economics, marketing, operations, finance and human resources. Our challenge in this course will be to integrate your learning from other courses in a synthesis with new material introduced here to see how general managers develop functional strategies into overall business and corporate strategies and to see how their chosen strategies are implemented. While this may not happen overnight, over the course of the quarter, you can expect to begin to see how the “pieces fit together.” You will be better prepared to enhance your careers with a more comprehensive vision of the firm as a whole and your role in it.

Class Contribution

Most of your learning will occur in preparation for and participating in the case discussions. To enhance your preparation and learning, **I strongly encourage you to use study groups to discuss the cases prior to class.** To guide you in your preparation, this syllabus includes preparation questions for each case.

As noted earlier, the complexity of the course material relies heavily on discussion learning. This process allows the cumulative insights of your colleagues to contribute to the evolution of the class’s learning. Thus, the entire class learning experience relies on each of you taking responsibility for contributing to the discussion. **In order to do so, it is imperative that each of you is present and fully prepared each day.**

In order to emphasize the necessity to be prepared for and to contribute to each class, class contribution will comprise a significant portion of your grade. As is the case with real world work environments, you are judged not by what you know but by what you **contribute**. Note that this is distinct from merely participating in the discussions. Even if you feel that you know the material, unless you share your insights with the class, I cannot adequately evaluate your preparedness and contribution. Students are never penalized for making comments which don’t appear to be the “right answer.” It is only through consideration of many diverse opinions and viewpoints that we will move toward a greater shared understanding of the multi-dimensional material which this course entails.

Each day, I will ask one or more individuals to “open” the case with a summary of the key issues along with his or her analysis of those issues. It is important that each of you be prepared to respond to the invitation to open the discussion. In the unlikely event that you are not prepared for class, then please let me know beforehand so that I might spare both of us the embarrassment of my calling on you. You should be able to identify the key issues, problems and opportunities facing the central case protagonists, to articulate and evaluate alternative approaches to problems, and to describe the course of action that you recommend and the reasons for yours recommendations. I may begin the discussion with one of the questions in the syllabus or with another question.

It is important to appreciate that every student is an important cog in the class discussion, and that it is equally important that each of us listen carefully to one another and attempt to build on or constructively critique prior comments. Please resist the temptation to jump to topics that are not specifically open for discussion. Some of the specific things on which you will be evaluated include:

- Is there a willingness to take *intellectual risks* and test new ideas or are all comments “safe”? (For example, repetition of case facts without analysis or conclusions or repeating comments already been made by someone else do not represent intellectual risk-taking nor do they earn credit towards your class contribution evaluation.)
- Is the contributor a good listener?
- Are the points made relevant to the discussion? Are they linked to the comments of others and to the themes that the class is exploring together?
- Do the comments add to our understanding of the situation? Are they incisive? Do they cut to the core of the problem?
- Is there a willingness to challenge the ideas that are being expressed by discussants or the professor?
- Does the contributor integrate material from past classes or the readings where appropriate? Do the comments reflect cumulative learning over the strategy course and the MBA curriculum or does the contributor merely consider each case in isolation?

Finally, I understand that participating in class can be an intimidating experience initially, and I will try to help you in any way that I can. I will evaluate each person’s contribution for each and every class and keep a running score on class contribution. In addition, I will request volunteers to be *peer evaluators* for each class period. Those students will offer a confidential interpretation of the *quality* of class contribution that I will use to supplement to my own evaluation. It is through the combined effort of the class that we develop an open environment for discourse and examination of ideas and experience tells us that this is where a substantial amount of your learning will occur in this class. With that in mind, your commitment to contributing to this environment not only determines the success of the class, but also helps to define your grade in the course. Consequently, your attendance is vital and will affect your contribution score. While it is your business whether you want to attend class and contribute, your classmates also bear the cost when you fail to do so. Thus, in an effort to internalize the externality arising from absences from class, you will bear the cost to your contribution score when you choose to miss a class. Interviews are not excused absences.

As required by school policy, grading will be based on relative rather than absolute standards.

Classroom Policies

Attendance: A major part of your learning in this course will take place in the classroom. Because the course is designed to help you develop a personal synthesis and perspective, it is not possible to make up for an absence, nor can you offer a contribution to classmates when you are not present. The Professor will excuse absences only in the case of documented serious illness, family emergency, religious observance, or civic obligation. If you will miss class for religious observance or civic obligation, please inform him no later than the first week of class.

Technology:

The use of laptops, smartphones, & other electronic devices are not allowed in class. While I see benefits to their use, they have considerable negative externalities and I have found that their disadvantages ultimately outweigh their advantages. The inappropriate use of technology is an indicator of poor class contribution.

Academic Integrity (Academic Misconduct)

Academic integrity is essential to maintaining an environment that fosters excellence in teaching, research, and other educational and scholarly activities. Thus, The Ohio State University and the Committee on Academic Misconduct (COAM) expect that all students have read and understand the University's Code of Student Conduct [can be found at http://studentaffairs.osu.edu/pdfs/csc_12-31-07.pdf], and that all students will complete all academic and scholarly assignments with fairness and honesty. Ignorance of the Code is not an excuse for violation. Students must recognize that failure to follow the rules and guidelines established in the University's Code of Student Conduct and this syllabus may constitute "Academic Misconduct." Additional guidance for maintaining academic integrity can be found at Ten Suggestions for Preserving Academic Integrity [can be found at <http://oaa.osu.edu/coamtensuggestions.html>].

The Ohio State University's Code of Student Conduct (Section 3335-23-04) defines academic misconduct as: "Any activity that tends to compromise the academic integrity of the University, or subvert the educational process." Examples of academic misconduct include (but are not limited to) plagiarism, collusion (unauthorized collaboration), copying the work of another student, and possession of unauthorized materials during an examination. Ignorance of the University's Code of Student Conduct is never considered an "excuse" for academic misconduct, so I recommend that you review the Code of Student Conduct and, specifically, the sections dealing with academic misconduct.

If I suspect that a student has committed academic misconduct in this course, I am obligated by University Rules to report my suspicions to the Committee on Academic Misconduct. If COAM determines that you have violated the University's Code of Student Conduct (i.e., committed academic misconduct), the sanctions for the misconduct could include a failing grade in this course and suspension or dismissal from the University.

While most students have high standards and behave honorably, like every academic institution, we encounter cases of academic misconduct. It is the obligation of students and faculty to report suspected cases of academic and student misconduct. Students can report suspected violations of academic integrity or student misconduct to faculty or to a program's leadership. All reported cases of academic misconduct are actively pursued and confidentiality is maintained.

JAY DIAL BIO

Dr. Jay Dial is Clinical Professor of Management & Human Resources at The Ohio State University's Fisher College of Business. Professor Dial teaches strategy, microeconomics and leadership courses in Fisher's MBA and undergraduate programs. He has been honored with the Alumni Association Award for Distinguished Teaching, Ohio State's highest honor granted for teaching and has been admitted to the University Academy of Teaching. He has been recognized as the Outstanding Professor in the Full-time, Working Professional and Executive MBA Programs eighteen times and has also received the College's highest teaching award, the Daniel Westerbeck Pace Setters Award for Graduate Teaching.

Dial is a regular contributor to Fisher's custom executive programs working with various clients, such as Nationwide, Textron, The Limited, Cardinal Health, OSU Medical Center/Ross Heart Hospital and the Abbott Nutrition among others. Dial has also worked in executive programs at Cornell University and Tulane University working with senior executives from Fortune 100 companies, such as IBM, Citibank, Chase Manhattan, Intel and Hewlett-Packard. He has also consulted to a broad variety of clients on strategy issues, including Aeropostale, Cardinal Health, Greif, Timken, Netjets, Roadway, Lubrizol, Baker-Hughes, Amerisource Bergen, Keybank, Tosoh America and Sterling Commerce.

Professor Jay Dial's interests include competitive strategy, leadership and governance issues. He has published scholarly articles in various journals, including the *Academy of Management Review*, *Journal of Financial Economics* and *Journal of Management*. Professor Dial is the author of numerous Harvard Business School teaching cases and also conducts seminars throughout the world for business school faculty on teaching with the case method.

Professor Dial joined the Ohio State faculty in 2002 after previously serving on the faculties at Case Western Reserve University and Texas A&M University. He also worked as a management consultant with Deloitte & Touche (now Deloitte Consulting) in Boston, focusing on corporate finance and corporate strategy issues. Prior to that, he worked in brand management at Kraft at their Glenview, IL world headquarters.

Dial holds a Doctor of Business Administration degree in General Management from Harvard University and has an MBA from the University of Chicago with concentrations in Business Policy, Finance and Marketing. He is a summa cum laude graduate of Old Dominion University in Norfolk, VA where he majored in Marketing and, upon graduation, was named the University Outstanding Scholar.

Jay lives in Upper Arlington, OH with his wife Aparna and son Bennett, 8, and daughter Annika, 4. He enjoys woodworking, movies, jazz and acoustic music and rooting for the Cincinnati Reds, Dallas Cowboys and Buckeyes.

Course Topics by Meeting and Session

Course Content and Structure

Meeting 1: Thursday, January 12, 2017, Morning

- Supply, Demand and Equilibrium
- Comparative Statics

Meeting 2: Thursday, January 12, 2017, Afternoon

- Firm Cost Structures and Industry Structure
- Economics of Regulation

Meeting 3: Friday, January 13, 2017, Morning

- Case discussion
DeBeers Consolidated Mines, Ltd. (A)
- Introduction to Property Rights and the Coase Theorem

Meeting 4: Saturday, January 14, 2017, Afternoon

- What Makes Markets Work:
Hernando DeSoto, Property Rights and Global Economic Development
- When Markets Fail:
Property Rights and Externalities

Meeting 5: Thursday, February 9, 2017, Afternoon

- Case discussion
**Aluminum Industry in 1994 and Aluminum Smelting in South Africa:
Alusaf's Hillside Project**
- Case discussion
**Life, Death and Property Rights:
The Pharmaceutical Industry Faces AIDS in Africa**

Meeting 6: Friday, February 10, 2017, Morning

- **Agency Costs, Incentives and Contracts**
Organizational Architecture
Information Asymmetry, Adverse Selection and Moral Hazard
- Case discussion
Lincoln Electric

Meeting 7: Thursday, March 9, 2017, Morning

- **Introduction to Vertical Integration**
- Case discussion
The Walt Disney Company and Pixar, Inc: To Acquire or Not to Acquire

8 Saturday, March 11, 2017, Morning

- **Assessing Divisional Performance: Transfer Pricing and Theory of Bureaucracy**
 - case discussion
Transfer Pricing at Timken
 - case discussion
General Dynamics: Compensation and Strategy (A)
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Thursday, January 12, 2017, Morning

SESSION 1
SUPPLY, DEMAND AND EQUILIBRIUM
COMPARATIVE STATICS

Readings

“The Outlook: US Farmers Are Hurt by Asian Crises, Too,” Bernard Wysocki Jr., *The Wall Street Journal*, 7/20/98.

“How Uncle Sam Could Ease the Shortage,” Gary S. Becker, *Business Week*, 1/20/97.

“Lessons from a Hurricane: It Pays Not To Gouge,” Steve Lohr *The New York Times*, Sept. 22, 1992, p. D1, column 3.

Textbook reading: : Chapter 2, “Comparative Advantage: The Basis for Exchange,” *Principles of Micro-Economics*, Robert H. Frank and Ben S. Bernanke, Irwin/McGraw-Hill, 2007.

Chapter 3, “Supply and Demand: An Introduction,” *Principles of Micro-Economics*, Robert H. Frank and Ben S. Bernanke, Irwin/McGraw-Hill, 2007.

Chapter 4 “Elasticity,” *Principles of Micro-Economics*, Robert H. Frank and Ben S. Bernanke, Irwin/McGraw-Hill, 2007.

Chapter 5, “Demand: The Benefit Side of the Market,” *Principles of Micro-Economics*, Robert H. Frank and Ben S. Bernanke, Irwin/McGraw-Hill, 2007.

Discussion Questions

Based on the information contained in each of the press articles and the theory presented in the textbook chapters answer the following questions.

“The Outlook: US Farmers Are Hurt by Asian Crises, Too”

1. Why have prices for pork and beef plummeted recently? What does the author list as some of the factors contributing to the recent situation?
2. What are the determinants of supply and demand that have changed? Use a supply and demand diagram to illustrate how they affected the market equilibrium.

“How Uncle Sam Could Ease the Shortage”

1. What does the author believe about the scope of the supply curve for organs?
2. What do you see as the adverse consequences of being able to sell your organs for transplant after you die? Could the fact that more lives would be saved because of these sales ever overcome these objections?
3. More generally, do you think that the state is entitled to stand in the way of a mutually advantageous exchange? Under what circumstances

“Lessons from a Hurricane”

1. What effect does the hurricane have on the market-clearing price and quantity of plywood? Draw a picture to illustrate your answer.
2. Will the Florida Attorney General's attempt to curtail price gouging \ be successful? Who gains and who loses as the result of such a policy?
3. Is this an example of a situation in which markets don't work, and thus intervention is appropriate? Why or why not?

Thursday, January 12, 2017, Afternoon

SESSION 2
FIRM COST STRUCTURES & INDUSTRY STRUCTURE
INTRODUCTION TO ECONOMICS OF REGULATION

Readings

“Discussion problem: ‘Relaxing’ Bayer’s Patent on Cipro,” Karen H. Wruck.

“Discussion problem: Pharmaceutical Pricing in the U.S. and Canada,” Karen H. Wruck

Textbook reading: Chapter 6, “Perfectly Competitive Supply: The Cost Side of the Market,” *Principles of Micro-Economics*, Robert H. Frank and Ben S. Bernanke, Irwin/McGraw-Hill, 2007.

Chapter 8, “The Quest for Profit and the Invisible Hand,” *Principles of Micro-Economics*, Robert H. Frank and Ben S. Bernanke, Irwin/McGraw-Hill, 2007.

Chapter 10 “Monopoly and Other Forms of Imperfect Competition,” *Principles of Micro-Economics*, Robert H. Frank and Ben S. Bernanke, Irwin/McGraw-Hill, 2007.

Discussion Questions

“ ‘Relaxing’ Bayer AG’s patent on Cipro”

1. Explain briefly how the fact that Bayer AG holds a patent on the drug Cipro is likely to affect its pricing and production (quantity) decisions. Support your answer with a diagram that depicts this type of pricing policy and illustrates whether or not it is optimal from society’s point of view. (For convenience, you may assume that marginal cost is constant across all quantities.) Be sure to clearly label all elements of your graph.
2. Explain how recent increased concern regarding the threat of bio-terrorism would affect Bayer’s pricing and production (quantity) decisions if the company chooses to maximize profits in the short-run.
3. On October 17, 2001, Bayer announced that it would hold prices of Cipro at their pre-September 11, 2001 levels. The company also announced that it would run its Cipro production facilities 24 hours a day, 7 days a week and bring a closed facility back on-line to produce 200 million Cipro tablets over the next three months. Is this decision profit maximizing in the short-run for Bayer? In the long-run? Why or why not? What factors likely entered into the company’s decision to undertake this approach to its Cipro pricing and production?
4. If the U.S. government persuades Bayer to “relax” its patent, what are the short-run implications for that company, manufacturers of the generic form of Cipro (ciproflaxin), the U.S. government and potential consumers of Cipro?

“ Pharmaceutical Pricing in the U.S. and Canada”

1. What are the most important factors in assessing whether the Canadian or the U.S. approach to pharmaceutical pricing is better for society? How do these factors differ if you take a short-run versus a long-run perspective?
2. Lawyers representing U.S. pharmaceuticals companies argue that what SPC is doing clearly violates FDA regulations. But SPC managers aren't concerned that the FDA will enforce these regulations. Nor are they concerned that politicians, even those with pro-business views, will pressure the FDA to undertake such enforcement. One of SPC's principal shareholders commented that “it would take an extremely courageous politician” to challenge our program. Why would politicians be reluctant to challenge SPC's Canadian Prescription Drug plan, despite the legal, regulatory and potential safety issues?
3. Suppose that SPC's Canadian Prescription Drug program grows and other firms begin offering similar programs. What are the implications for the market structure of the prescription drug industry in the U.S. and worldwide? What are the implications for U.S. consumers in the short run and long run? For international consumers in the short run and long run?

Textbook reading: Chapter 6, “Supply, Demand and Government Policies,” Principles of Microeconomics, N. Greg Mankiw, Harcourt, 2001, pp. 117-137. (In your course package.)

“Discussion Problem: The California Electricity Market: A Simplified but True Story,” Karen H. Wruck.

Friday, January 13, 2017, Morning
SESSION 3

INDUSTRY STRUCTURE CASE DISCUSSION

INTRODUCTION TO PROPERTY RIGHTS AND THE COASE THEOREM

Readings

“De Beers Consolidated MinesLtd. (A),” Pankaj Ghemawat and Toby Lenk, Harvard Business School Case 9-391-076.

1. What functions does the CSO perform as a global intermediary? How do these functions help expand the economic pie in the diamond industry?
2. How does that expanded economic pie end up getting divided among the various players in the diamond industry? Why?
3. Should De Beers pull the plug on the CSO's stockpiling strategy? Depending on your answer, what specific actions would you recommend?

Introductory lecture on Property Rights and the Coase Theorem

Saturday, January 14, 2017, Afternoon

SESSION 4
WHAT MAKES MARKETS WORK: PROPERTY RIGHTS AND ECONOMIC DEVELOPMENT

WHEN MARKETS FAIL:
PROPERTY RIGHTS, EXTERNALITIES AND GOVERNMENT REGULATION

“Dead Capital and the Poor,” Hernando DeSoto

“The Mystery of Capital,” short summary of DeSoto’s book .

“Slumdogs and Millionaires,” an interview with Hernando DeSoto.

“It’s tough being a tiddler: Credit where credit is due,” *The Economist*, March 20, 1999, p. 9.

“The Missing Ingredient,” Hernando de Soto, *The Economist*, August 23, 1993, pp. 8-10.

Discussion Questions

1. De Soto makes a passionate argument about the importance of property rights in the functioning of a capitalist economy and cites remarkable evidence regarding the wealth held by individuals in “poor” countries. Is the key to wealth creation among the first world countries the presence of property rights or the *right* to property rights? Is this an important distinction?
2. What feature of a capitalist system is critical to the effective functioning of decentralized decision-making in an economy? Is it the presence of a market on which financial claims or vouchers can be traded? Why or why not?
3. De Soto, estimates that in Egypt there exists \$240 billion in “dead capital”—an amount over three times that country’s Gross Domestic Product. He has estimated similarly large figures for other developing countries. Of what importance is this figure? Why does he refer to this capital as “dead”? What would be required to convert it into “living” capital?
4. Assar Lindbeck, a Swedish economist and former chair of the Nobel Prize committee for Economics stated, “next to bombing, rent control seems to be...the most efficient technique so far know for destroying cities...” What evidence likely leads him to come to this conclusion?
5. Economic development policies emphasizing fiscal discipline (such as controlling inflation and the repayment of loans) and employment through major public works projects are more common and more popular than policies emphasizing the formalization of property rights. Why do you think that is the case?

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Readings

“Discussion Problem: Buckeye Egg Farms,” Karen H. Wruck.

“Money to Burn?” *The Economist*, 12/6/97.

“It’s Immoral to Buy the Right to Pollute,” Michael J. Sandel, *The Boston Globe*, 12/15/97.

“Schools Brief: State and Market,” *The Economist*, February 17, 1996.

Textbook reading: Chapter 10, “Externalities,” *Principles of Microeconomics*, N. Greg Mankiw, Harcourt, 2001, pp. 205-224. (In your course package.)

“Money to Burn?” and “It’s Immoral to Buy the Right to Pollute”

1. What are the costs and benefits of using government regulation as a way to reduce pollution?
2. Are tradeable rights a better answer to the pollution problem and “global warming”? Are “green taxes” a better answer?
3. Is there something immoral about allowing individuals, businesses or countries to buy the right to pollute? If so, what is it? If not, why not?

“State and Market”

1. Is it possible for government regulation to lead to a worse outcome than simply letting an imperfect market continue to operate? How?
2. How would you go about assessing the effectiveness of a government regulatory policy?

Thursday, February 9, 2017, Afternoon

SESSION 5 INDUSTRY STRUCTURE AND INVESTMENT DECISIONS

LIFE, DEATH AND PROPERTY RIGHTS

Readings

“The Aluminum Industry in 1994,” Kenneth S. Corts, Harvard Business School Case 9-799-129.

“Aluminum Smelting in South Africa: Alusaf’s Hillside Project,” Kenneth S. Corts, Harvard Business School Case 9-799-130.

GROUP WRITTEN ASSIGNMENT #1

Think carefully about the type of market structure that typifies the aluminum smelting industry in preparing the following assignment.

Following the instructions on the next page and utilizing data from the case as well as the data included in the Excel spreadsheet distributed to you, construct the industry supply curve for primary aluminum.

Then answer the following questions in 3-5 pages total (double-spaced, eleven point type or larger):

1. **Is primary aluminum production an attractive industry? Why or why not?**
2. **At what rate do you expect primary aluminum demand to grow over the coming years? (Be sure not to confuse total aluminum demand with primary aluminum demand; primary aluminum demand is total demand less scrap production.) What do you expect the price of aluminum to be in 5 years? Explain your rationale.**
3. **Assuming that Alusaf desires a 15% annual pre-tax ROI (based on their initial investment of construction costs), should they build the proposed Hillside smelter? What are the key assumptions you have made in your analysis? Is your recommendation particularly sensitive to any assumptions you have made. Explain your rationale. (Discounted cash flow analysis is not necessary. A simple 15% annual return calculation is adequate.)**
4. **Hand in your supply curve picture with the analysis.**

The Aluminum Industry in 1994 Aluminum Smelting in South Africa

Instructions for building the aluminum industry supply curve:

This assignment lets you utilize some of the conceptual tools from the Managerial Economics course to assist you in making strategic decisions. An industry supply curve, which relates industry output to market prices, can be constructed from plant-level cost data. If firms are price-takers, each firm should produce at every plant for which the market price exceeds variable costs. Any margin of price over variable cost makes a contribution toward covering the plant's fixed costs (which is called contribution margin). To construct an industry supply curve, then, you need information on plant capacities and plant variable costs. From this data, you can calculate how much capacity has operating costs less than any particular market price. This is the amount of output one expects from price-taking firms since this would yield positive contribution margins for all those plants. Plotting this information on a graph yields an industry supply curve.

Using the smelter cost data provided, you can construct an industry supply curve in Excel in the following five easy steps:

1. Download the smelter cost data by opening the Excel file included in the accompanying email (aluminumworksheet.xls)
2. Calculate the variable cost for each smelter. To do this, create a new row at the bottom of the spreadsheet (labeled "Total Variable Costs") and enter a formula that sums the relevant cost categories. For example, if you believe that the correct definition of variable costs is total raw materials costs, you would click on cell C30 and enter `"=+C12+C16+C18"`. Then, copy this formula into all columns C through FC, which will give you a variable cost number for each of the 157 plants. I am not telling you that the above cells are all those that comprise variable costs. A part of the assignment is using your judgment to assess which categories should be included as variable costs. Think hard about which costs are really variable costs.
3. Sort the smelters according to their variable costs. Highlight the entire data region, excluding the labels in columns A and B. Don't forget to include your new row added in step 2. This area should be the area C5 through FC30. Click on the "Data" menu in Excel and choose "Sort." To sort data that is in columns, not rows, you must choose "Options" and then click next to "Sort left to right." Then click "OK." Now choose to sort "Ascending" by the row you just created—row 30 if you followed the above directions exactly. Then click "OK."
4. Create a measure of total cumulative capacity (which you might choose to label "Total Cumulative Capacity") in each column. This rank ordering will tell you how much capacity is more efficient than any particular plant. For subsequent graphing, it is best to put this in the row just above the row you created in step 2. Enter `"=sum($C8:C8)"` in cell C29. Then copy this formula into cells D29 through FC29. Note: The information in rows 29 and 30 is the supply curve. To see this, find the "marginal plant" at 1994 prices—that is, the plant whose variable costs are just lower than the market price of \$1,110. We expect that plant and all the more efficient plants to its left to produce at that market price. Their total capacity is given in row 29. This calculation can be done for any market price.
5. Create a graph of the supply curve. To do this, highlight cells C29 through FC 30. Click on the "Insert" menu, and then click on the "Chart" item on that menu. Choose the "XY (Scatter) chart" chart-type and choose the lower-right "chart sub-type" before clicking "Next." Click "Next" twice more and then "Finish." Voila. The resulting chart is the industry supply curve. Print and then show it around to amaze your friends and astound your enemies.

Readings

“Life, Death and Property Rights: The Pharmaceutical Industry Faces AIDS in Africa,” Deborah Spar and Nicholas Bartlett, Harvard Business School Case 2-702-049.

Discussion Questions

Life, Death and Property Rights: The Pharmaceutical Industry Faces AIDS in Africa

1. How should the pharmaceutical companies respond to the plague of AIDS in Africa?
2. What strategy should they follow to protect their intellectual property rights?
3. How far should they be willing to go? What are the costs and benefits?

Friday, February 10, 2017, Morning

SESSION 6

ORGANIZATIONAL ARCHITECTURE: AGENCY COSTS AND THE USE OF INFORMATION

LESSONS IN ORGANIZATIONAL ARCHITECTURE

Chapter 11, “Organizational Architecture,” Brickley, Smith and Zimmerman.

Chapter 10, “Incentive Conflicts and Contracts,” Brickley, Smith and Zimmerman.

Asymmetric Information, Moral Hazard and Adverse Selection

“Discussion Problem: Agency Problems and Corporate Jets,” George P. Baker.

Goldman Sachs and Abacus 2007

Discussion Questions

1. What are agency costs?
 2. How are agency costs relevant to resolving conflicts of interest between individuals within an organization?
 3. What is the source of agency problems between stockholders and managers?
 4. Are agency problems unique to corporations? Where, in general, can we expect to find them?
 5. Will it ever be in the self-interest of a manager with a substantial equity ownership stake to take a risky project that she knows will reduce the value of the firm? If so give a specific example, if not why?
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“Lincoln Electric Co.,” Norman A. Berg and Norman E. Fast, Harvard Business School Case 9-376-028.

Textbook reading: Chapter 15, “Incentive Compensation,” Brickley, Smith and Zimmerman., pp. 388-411 (skip the appendix).

Discussion Questions

1. How would you describe Lincoln Electric’s approach to the organization and motivation of their employees?
2. What role do you think this approach has played in Lincoln’s performance over the last 25 years? How do their systems deal with the agency problems that afflict many firms? Have any other factors been more important?
3. What factors will be critical to Lincoln’s continued success? What recommendations would you make to Mr. Willis?
4. What is the applicability of Lincoln’s approach to motivation to other companies and situations? Why don’t more companies operate like Lincoln?

Thursday, March 9, 2017, Morning

SESSION 7 THE “MAKE OR BUY” DECISION: VERTICAL INTEGRATION AND OUTSOURCING EXPANDING SCOPE THROUGH HORIZONTAL DIVERSIFICATION

Readings

“When and When Not to Vertically Integrate,” “John Stuckey & David White, *Sloan Management Review*, Spring 1993.

“Note on Corporate Strategy,” Mikolaj Jan Piskorski, Harvard Business School Press, #705-449.

“The Walt Disney Company and Pixar, Inc: To Acquire or Not to Acquire?” Juan Alcacer, David J. Collis and Mary Furey, Harvard Business School Case #709462.

Discussion Questions

1. Which is greater: the value of Pixar and Disney in an exclusive relationship, or the sum of the value that each could create if they operated independently of one another or were allowed to form relationships with other companies? Why? In other words, does the combination pass the “Better-Off” test?
2. If it is likely that Pixar and Disney are more valuable in an exclusive relationship, can that value be realized through a new contract? Or is common ownership required? (Does it pass the “Ownership Test” which suggests that Disney must acquire Pixar?)
3. If Disney does acquire Pixar, how should Bob Iger and his team organize and manage the combined entity? What challenges do you foresee, and how would you meet them? Or alternatively, do these challenges outweigh the benefits of buying Pixar?

Written Group Assignment

Respond to Discussion Questions 1, 2 and 3 above. Demonstrate your understanding of the concepts (as articulated in the articles included in the course readings) in shaping your arguments.

Each write-up should be no more than three to five double-spaced pages (in a readable font, 11 points or larger is nice). It is helpful to organize your paper according to the questions asked. Be sure to respond to all parts of the questions.

Saturday, March 11, 2017, Morning

SESSION 8
ASSESSING DIVISIONAL PERFORMANCE:
TRANSFER PRICING AND THE THEORY OF BUREAUCRACY
COMPENSATION, STRATEGY, AND EMPLOYMENT

Readings

Textbook reading: Chapter 17, “Divisional Performance Evaluation,” Managerial Economics and Organizational Architecture, James A. Brickley, Clifford W. Smith, Jr. and Jerold L. Zimmerman, Irwin/McGraw-Hill, 2004, pp. 450-477.

“Transfer Pricing at Timken,” Nicole Bastin and Stefan Reichelstein, Stanford Graduate School of Business Case, A-190.

Transfer Pricing at Timken

Answer the questions at the end of the Timken Case.

1. Is divisional performance measurement an important issue for firms and their managers? Why or why not?
2. What kinds of alternatives are available to firms that want to assess divisional performance? What are the strengths and weaknesses of each alternative?
3. What alternatives are available to firms that want to relate divisional performance measures to rewards? What are the strengths and weaknesses of each alternative?

Readings

“The Eclipse of the Public Corporation,” Michael C. Jensen, Harvard Business Review, Sept/Oct, 1989.

“General Dynamics: Compensation and Strategy (A),” Kevin J. Murphy and Jay Dial, Harvard Business School Case 9-494-048.

Review textbook readings:

Chapter 11, “Organizational Architecture,” Brickley, Smith and Zimmerman.

Chapter 10, “Incentive Conflicts and Contracts,” Brickley, Smith and Zimmerman.

Chapter 15, “Incentive Compensation,” Brickley, Smith and Zimmerman.

Discussion Questions

Evaluate Anders’ strategy for reshaping General Dynamics (GD). Is it value-creating? If so, for whom? If not, why not? In structuring your analysis, also consider the following questions:

1. What is General Dynamics’ position in its industry? How should the company position itself for the future?
2. What are the major components of GD’s management compensation system. How do they affect the level of Anders’ pay? What is the relation between his pay and performance? What are the relevant performance benchmarks embedded in his compensation package?
3. Should GD eliminate its Gain/Sharing Program? Why or why not? What should it replace Gain/Sharing with, if anything?

4. Should top managers, such as Bill Anders, be rewarded 1. for selling assets and reducing employment? Under what circumstances and to what extent? What are the viable alternatives?
5. Jensen espouses the private equity model of ownership and governance (particularly for firms in declining industries), and the General Dynamics case demonstrates the use high-powered incentives to motivate managers. What is your critique of these models for corporations? Where they appropriate or not appropriate? Demonstrate your understanding of the concepts (as articulated in the course readings, including articles and/or book chapters) in shaping your argument.

Deliverables by Interim and Session

For February Meeting

Interim 2

Two Individual assignments—due by midnight, Sunday, February 5, 2017

Turn in Problem Sets 1 & 2

Follow the guidelines set forth in the problem set description

Team assignment—due by midnight, Sunday, February 5, 2017

- **All teams: Write-up an analysis of the case: Aluminum Industry in 1994 and Alusaf's Hillside Project**

The write-up should follow the instructions given along with the assignment in this syllabus.

For March Meeting

Interim 3

Individual assignment—due by midnight, Sunday, March 5, 2017

Turn in Problem Set 3

Follow the guidelines set forth in the problem set description

Team assignment—due by midnight, Sunday, Sunday, March 5, 2017

- **Write-up an analysis of the case: Disney and Pixar (answering the three discussion questions given in the syllabus)**

The write-up should follow the instructions given along with the assignment in this syllabus.
