

AMERICAN UNIVERSITY of CENTRAL ASIA

SYLLABUS

ECONOMICS OF THE FIRM

ECO – 431

Lecturer: *Liudmila Konstants*, Ph.D.,
Associate Professor of the Department of Economics

Contact information:

Office Location: 204/1
Office Phone: 663-501
E-mail: knst@mail.auca.kg
Office Hours: by appointments

Course objectives: because of the strong focus on the economics of the firms, markets, and competitive behavior, this course is eminently suitable for students of MBA and undergraduate business majors. The course objective has been to cover what every business student need to know about microeconomic theory and competitive market economics. While the strong micro-theory content makes the course quite suitable for students of economic majors, the students' attention will be deliberately stressed on concepts and applications especially pertinent to analyzing the behavior of firms and competitive markets.

Course description: The primary unit of analysis is the business firms. Students are exposed again and again to how the conclusions of microeconomic analysis guide firms into one course of action rather than another. The economics of the firm is looked at from the inside as concerns production, cost, profitability, and competitive strategy considerations, and it is examined from the outside as concerns the influences of consumer demand, competition, market structure, and recourse supply.

The result is the course (1) that is strong on theory and analysis, (2) that takes as its focal point the economic of the firm in a competitive market environment, and (3) that uses examples and applications to bridge the gap between theory and practice.

At the end of this class, a student should understand:

- ◆ difference among varying methods of economic analyses (including “scientific testing,” deductive logic, argument by example, diagrammatic models, and the use of mathematical proofs), what a theory is, the role of assumptions and abstraction, and the relevance of theory to explaining real-world economic phenomena;
- ◆ different profit concepts, profit theories, the debate over profit maximization, and non-profit goal of firm;
- ◆ multiple-goal models of business behavior;
- ◆ the five competitive forces, built around Michael Porter’s now classis model for diagnosing how competition works in a given industry;
- ◆ ways of creating and defending competitive advantage;
- ◆ how to deal with a firm’s cost competitiveness vis-à-vis rivals, multiproduct pricing, price signaling through the media, taxing excess profits, the competitive effects of advertizing and product differentiation, first mover advantages, switching costs, driving forces, the mapping of competitive groups, the wage-employment effects of unions, the impact of minimum wage legislation, and the economics of productivity changes.

Prerequisite: Intermediate Microeconomics.

Course Material:

1. Thompson, Arthur A. Jr., John P. Formby. Economics of the Firm: Theory and Practice. Sixth Ed. NJ: Prentice Hall, Upper Saddle River, 1993. [ISBN 0-13-092867-4]
2. Peapall, Lynne, Daniel J. Richards, and George Norman. Industrial Organization: Contemporary Theory and Practice. International: South-Western College Publishing, 1999. [ISBN 0-538-85948-2] (Carlton. W. Dennis)
3. Pindyck, Robert, S., Daniel L. Rubinfeld. Microeconomics. Seventh Ed. NJ: PEARSON, 2009. [ISBN-13; 978-0-13-208023-1; ISBN-10:0-13-208023-0]
4. Carlton. W. Dennis, and Jeffrey M. Perloff. Modern Industrial Organization. Fourth Ed. Boston, etc.: PEARSON, 2005. [ISBN 0-321-18023-2]
5. Waldman, Don E., and Elizabeth J. Jensen. Industrial Organization: Theory and Practice. Third Ed. Boston, etc.: PEARSON, 2007. [ISBN 0-321-37610-2]

## of the Lecture	Lectures outline	Reference
1.	<p>Introduction to Microeconomic Analysis: The Method of Economic Analysis: The “scientific method” approach to developing economic theories and constructing models of economic behavior. Must economic analysis always be “scientific”? Some alternatives to the scientific method. The methods of economic analysis. What is a theory? The realism of assumption.</p>	(1.) Ch.1
2.	<p>Production Technology and Costs. 2.1. MARKET STRUCTURE AND CONCENTRATION 2.1.2. Measurement Problems: What is the Market? 2.1.3. Upstream and Downstream Firms, Vertical restriction 2.2. The Neoclassical or Technological View of the Firm. 2.2.1 The Neoclassical or Technological View of the Firm 2.2.3. Sources of Scale Economies. 2.2.4. Scale Economies – Fixed Costs and Sunk Costs</p>	(2.) Ch.2.2 – 2.4.
3.	<p>2.3 MULTIPRODUCT TECHNOLOGY: ECONOMIES OF SCALE AND SCOPE 2.3.1 Flexible Manufacturing: Scope Economies and Product Differentiation 2.4 NONCOST DETERMINANTS OF INDUSTRY STRUCTURE 2.4.1 The Size of the Market</p>	
4.	<p>The Firm and Its Costs. 2.6 Cost Concepts: Multiproduct Firms. The Theory of the Firm. The Structure of Modern Firms. Constraints on Managers. Economy of Scale and Scope: flexible manufacturing – scope economies and product differentiation. Empirical evidence of multiproduct cost function. Non-cost determinants of industry structure.</p>	(1.) Ch.2 p.p.17 - 31 p.p. 39-46
5.	<p>The Profit Motive and Other Goals of the Firm: The many ways profit can be defined.</p>	(1) Ch.9

6.	<p>Theories of profit: compensatory and functional theories profit; friction and monopoly theories of profit; technology and innovation theories of profit; profit theories in perspective.</p> <p>The Social Benefit of Profit</p> <p>The profit record of Business Enterprises</p> <p>Do Business Firms Seek to Maximize Profits?</p> <p>Why Firms Behave as if They Seek to Maximize Profit?</p> <p>Why Firms do not or Cannot Maximize Profit?</p> <p>How Business Executives Define What is a “Reasonable” Profit?</p> <p>The Alternatives to Strict Profit Maximization: Satisfying Behavior, Revenue Maximization, Market Share Goals, Long-Run Survival Goals; The Goal of Social Responsibility, Growth and Diversification Goals.</p> <p>Multiple Goals: Conflict and Tradeoffs.</p> <p>Personal Goals of Corporate Managers.</p> <p>Principal-Agent Problems and the Goal of the Firm</p>	
7.	<p>Markets with Asymmetric Information</p> <p>Quality Uncertainty and the Markets for “Lemons”.</p> <p>Implications of Asymmetric Information: Insurance; the Market for Credits; The Importance of Reputation and Standardization.</p> <p>Market Signaling: Guarantees and Warranties.</p> <p>Moral Hazard.</p>	Ch. 17 of R.Pindyck
8.	<p>The Principal-Agent Problem: (1) in Private Enterprises; (2) in Public Enterprises; Incentives in the Principal-Agent Framework.</p> <p>Managerial Incentives in an Integrated Firm.</p> <p>Asymmetric information in Labor Market: Efficiency Wage Theory.</p>	
MIDTERM TEST March, 22 @ 14:00-17:00 Aud. # 403		
9.	<p>The Economics of Firms With Multiple Prices, Plants, Products, or Objectives. The model of price discrimination.</p> <p>Price strategies where strict profit-maximization is not the dominant consideration. Multi-plant production and the conditions for maximizing profit. Multiproduct pricing models.</p>	(1.) Ch. 14
10.	<p>ADVERTISING</p> <p>10.1 Consumer Fraud and Truth in Advertising</p> <p>10.2 ADVERTISING: SOME BASIC ANALYSIS</p> <p>10.2.1 The Extent of Advertising in the United States</p> <p>10.2.2 Early Views on the Effect of Advertising Expenditures</p> <p>10.3 ADVERTISING AND SIGNALING</p>	(2.) Ch.10
11.	<p>10.4 A COMPLEMENTARY VIEW OF ADVERTISING AND MONOPOLY POWER</p> <p>10.4.1 Advertising and Crowd Appeal</p> <p>10.4.2 Advertising, Brand Recognition, and Information</p> <p>10.4.3 The Monopolist's Profit-Maximizing Choice of Advertising</p> <p>10.4.4. Monopoly Power: Too Much or Too Little Advertising</p> <p>10.4.5 Competition and the Extent of Advertising</p>	
12.	<p>10.5 ADVERTISING AND BRAND COMPETITION</p> <p>Optimal Advertising and Optimal Pricing in the Spatial Model</p> <p>10.6 COOPERATIVE ADVERTISING</p>	

	AND THE ROBINSON-PATMAN ACT How Much Is That Window with the Novel?	
13.	<i>The Five Competitive Forces.</i> The Five-Forces Model of Competition: a Key Analytical Tools. Factors Affecting the Strength of Inter-firm Rivalry: The Competitive Force of Substitute Products; ... of Potential Entry. The Market Power of Suppliers. The Market Power of Buyers.	Ch. 15
14.	<i>Why Market and Competitive Conditions Change – the Concept of Driving Forces.</i>	
15.	<i>Technically-Economic Analysis of a Firm Activity.</i>	Lecture and Case-Studies.
MAY,3	10:00 – 13:00 @ aud. # 403: TEST # 2. For those students who take Industrial Organization course: you'll have exam on Economics of the Firm @ 14:00–17:00	

I reserve the right to modify any or all the portions of this syllabus at any time during the period of the course. I'll let you know this on e-course – keep your attention on this Syllabus.

Assessment and Grading

Overall course grades will be founded on two written tests. There's no any strong condition that each of them should be of 50%. I will summarize all the points you'll "earn" within these two tests and will divide the sum over all possible points you were able to "earn" within two tests (this amount of points will mean 100% of the possibility) – that will be your "earned" percentage.

In case of your active and constructive participation in the classes within the entire semester and under the condition that you are always completely prepared with your homework you will be able to get additional ten points as a premium. This additional 'premium' is my personal award – you may not ask me about it.

Moreover, you can be provided with a possibility to "earn" additional points for exceptionally good presentations of a "fresh" (of this or last year) relevant to the studied theory case study (no info and text from the textbook!). This option will be left to your discretion. You'll be able to get 100% grade without these bonus points.

Grading Scale: Your final letter grade for the course will be based on the following scale - expressed as a percentage.

GRADING SCALE (in %)

You get: if you earn:

You get: if you earn:

"F" - < 40.0 %

"D-" - (40.0 – 44.5)

"D" - (45.0 - 49.5)

"C -" - (50.0 - 54.5)

"C" - (55.0 - 59.5)

"C+" - (60.0 - 66.5)

"B-" - (67.0 - 70.0)

"B" - (70.5 - 75.0)

"B+" - (75.5 - 80.0)

"A-" - (80.5 - 85.0)

"A" - (85.5 and above)

Grading Guidelines for Presentations

‘A’ = 5 points: Students presented important points with good collection of “fresh” scientific literature and data in a thorough manner;

made extensive eye contact with the audience;

did not read the presentation;

kept to the 6-9 minute time limit.

The speech is natural and continuous with few or no unnatural pauses.

‘B’ = 4 points: Students presented some important points with good collection of “fresh” scientific literature and data but could have been more thorough;

made limited eye contact with the audience;

did not read the presentation;

kept within one minute of the 6-9 minute time limit;

Slight stumbling [спотыкание; запинка; задержка] but manages to rephrase or continue.

‘C’ = 3 points: Lacking in important points and/or details;

Limited collection of literature or/and data (or they not pretty “fresh”);

made little eye contact with the audience;

read the presentation often;

diverged from the 6-9 minute time limit by 2-3 minutes.

The speech frequently hesitant, sentences may be left uncompleted.

‘D’ = 2 points: Severely lacking in important points and/or details;

Limited collection of literature and data (or they not pretty “fresh”);

failed to make eye contact;

read the presentation;

diverged from the time limit by more than three minutes;

The speech is very slow and uneven, except for short or routine sentences.

‘F’ = 0 points: Assignments where none of the above apply.

Attendance and Participation

By registering for this course, students have made a commitment to participate in the course classes as well as other course related activities. To receive credits for class participation a student should be prepared and should actively participate in all class meetings. Participation includes much more than being able to answer questions: students are expected to be engaged in and support class discussions about other students’ topics and papers. To utilize the class environment your timely presents and participation are necessary.

Keep in mind: late arrivals are disruptive and inconsiderable to the rest of the class.

After three unexcused absences your grade will be dropped one letter grade.

Three late arrivals (10-15 minutes) will be count as one absence.

Please, NOTE: (1) Students who are not paying attention in a class will be counted as absent.

MISSING THE TEST MEANS “0” POINTS. NO MAKE-UP WILL BE PROVIDED – IN NO WAY

In case of a serious illness the University provides a grade “I”.

[A student is allowed a maximum of one unexcused absence. A student who misses 25% of the course meeting (3 – 3.5 weeks – without proved sound documentation) will get a grade “F”. For missing such amount of classes due to serious reason with proved official documentation (sufficiency of that documentation will be determined by the instructor(s)) a student *can be* dropped with grade “I”.]

Professional Conduct and Attitude

As a critical part of your education, we encourage you to continue strengthening the community that you’ve build with your classmates and teacher, which is based on relationships of mutual trust and respect. The way that you choose to conduct yourself will be considered an integral part of your professional development and will therefore affect the feedback and grades you receive. Please, approach me if you have ANY concerns, problems or questions connected to the course issues. The minutes immediately after regular class hours are often the best opportunities to see me for any special help you may need. You may also contact me for a meeting outside of scheduled class hours. I don’t mind putting in the extra time, and I expect that you won’t either, as long as it doesn’t conflict with anyone’s other scheduled courses or meetings. Keep-in-mind: before the consultation, please, read the Chapter carefully and try to find a solution for issues under the questions. Firstly you will be asked, “What is written in a chapter about the issue?” and asked to show the ways you used for solutions.

I look forward to working with you this semester!

APPEAL: any student is encouraged to have a look at his/her written test after the grading. You are encouraged to see your strong parts of explanations or your mistakes; you can calculate whether all the points are counted by the professor. Nevertheless, if you find “mistakes(s)” from the professor’s side you should prepare your written appeal: you should re-write the task, to explore the best answer from the studied source(s), to refer on it (title, chapter, and page); and to point-out that your answer was exactly the same. After getting your Appeal I will re-check the entire test (not just that point). It could be that you’ll get a new score which could be higher or lower of the initial.

A calculating test is counted as “Done” if you get a right result (showing all the essential steps of a calculus).

CHEATING. If within the test time I see that you use a not-authorized source (paper, cell-phone, etc.) I’ll write on your test blank, “Cheating”. You’ll leave a test auditorium right immediately without any arguing. You’ll get “0” and I leave the right to issue an Appeal case against you.

Course Requirements

- Students are expected to read the assigned materials before they are covered in classes. This practice will increase the learning process so significantly that you will be surprised.
- Assignments and papers must be turned in by the due date unless prior arrangements are made with the instructor(s). No late assignments will be accepted!
- It is recommended that students collaborated and work together. However, cheating or academic dishonesty at any form will not be tolerated.
- All students are expected to adhere to the AUCA Honor Code and other general rules of the university etiquette.

Your cell-phone MUST BE TURNED-OFF within classes and TESTS: you won’t be allowed to use it instead of a calculator on tests.