

## **230991 : Organizational Economics (CentER)**

**Fall 2012**

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**Instruction language:** English  
**Type of Instruction:** interactive lectures, discussion of journal articles  
**Type of exams:** student participation + weekly assignments + term paper  
**Level:** Research Master Economics, 2<sup>nd</sup> year  
**Course load:** 3 ECTS; 6 x 180 minutes

### **Goal and Scope of the course:**

The course delivers an introduction to theories of organizations and strategic interaction that rely on economic thinking. Our goal is to familiarize students with these theoretical approaches, to guide them to the research frontier in selected topics, and to let them explore open and interesting research questions, both theoretical and empirical, on their own.

We will study relationships within firms (authority, incentives, delegation), between firms (formal and informal contracting, vertical and horizontal integration, strategic alliances, firm networks and groups), and beyond firms (organizations and institutions, economic governance). We will review the main economic theories that explain the existence, scale, and scope of firms (transaction costs economics, property rights theory, agency theory, and adaption theory) and study the impact of an organization's form (for-profit, nonprofit, public, cooperative, or club) on its decisions.

### **Course format:**

Each 180 minute session consists of the presentation of four papers. Some will be presented by the lecturer, some by students; all will be discussed jointly.

Students will have weekly assignments to work on, which are due to be delivered before next week's lecture.

Students write a research proposal (5-10 pages) on a topic related to the course. After a short presentation of the key papers related to the student's research question, major emphasis will be put on the resulting research design and on the description of the potential contributions of follow-up work.

### **Grading:**

Assignments and Class Participation (questions and presentations): 20%

Research proposal: 80%

## Reading list

Readings by category: (\* are core readings and will be discussed in class)

September 21, 12:45-16:30: Lecture 1: Foundations of Organizational Economics (AvW & JP)

Transaction Cost Economics:

- \*Coase, Ronald. 1937. "The Nature of the Firm." *Economica*, 4: 386-405.
- \*Williamson, Oliver. 1971. "The Vertical Integration of Production: Market Failure Considerations." *American Economic Review* P&P, 61: 112-123.
- \*Alchian, Armen, and Harold Demsetz. 1972. "Production, Information Costs, and Economic Organization." *American Economic Review*, 62: 316-325.
- \*Klein, Benjamin, Robert Crawford, and Armen Alchian. 1978. "Vertical Integration, Appropriable Rents, and the Competitive Contracting Process." *Journal of Law and Economics*, 21: 297-326.
- Williamson, Oliver. 1979. "Transaction Cost Economics: The Governance of Contractual Relations." *Journal of Law and Economics*, 22: 233-261.

Property Rights Theory:

- \*Grossman, Sanford, and Oliver Hart. 1986. "The Costs and Benefits of Ownership: A Theory of Vertical and Lateral Integration." *Journal of Political Economy* 94, 2: 691-719.
- Hart, Oliver, and John Moore. 1990. "Property Rights and the Nature of the Firm." *Journal of Political Economy*, 98, 6: 1119-1158.
- Hart, Oliver. 1995. *Firms, Contracts, and Financial Structure*. Oxford: Clarendon Press.

September 28, 12:45-16:30: Lecture 2: Agency Theory and Adaptation (JP)

Adaptation:

- \*Simon, Herbert. 1951. "A Formal Theory Model of the Employment Relationship." *Econometrica*, 19: 293-305.
- Hart, Oliver and John Moore. 2008. "Contracts as Reference Points." *Quarterly Journal of Economics*, 123: 1-48.

Incentives:

- Holmstrom, Bengt, and Paul Milgrom. 1991. "Multitask Principal-Agent Analyses: Incentive Contracts, Asset Ownership, and Job Design." *Journal of Law, Economics, and Organization*, 7: 24-52.
- Holmstrom, Bengt, and Paul Milgrom. 1994. "The Firm as an Incentive System." *American Economic Review*, 84, 4: 972-991.
- \*Holmstrom, Bengt. 1999. "The Firm as a Subeconomy." *Journal of Law, Economics, and Organization*, 15: 74-102.

Comparing theories and evidence:

- \*Gibbons, Robert. 2005. "Four formal(izable) theories of the firm?" *Journal of Economic Behavior and Organization*, 58: 200-245.
- Kim, Jongwook. and Joseph T. Mahoney. 2005. "Property Rights Theory, Transaction Costs Theory, and Agency Theory: An Organizational Economics Approach to Strategic Management." *Managerial and Decision Economics*, 26, 4: 223-242.
- \*Lafontaine, Francine, and Margaret Slade. 2007. "Vertical Integration and Firm Boundaries: The Evidence." *Journal of Economic Literature*, 45, 3: 629-685.

October 5, 12:45-16:30: Lecture 3: Contracting and Authority (JP)

Formal Contracts between Firms:

- \*Bajari, Patrick, and Steven Tadelis. 2001. "Incentives Versus Transaction Costs: A Theory of Procurement Contracts." *RAND Journal of Economics*, 32: 387-407.

Informal/relational Contracts:

- Macaulay, Stewart. 1963. "Non Contractual Relations in Business: A Preliminary Study." *American Sociological Review*, 28: 55-67.
- \*Baker, George P., Robert Gibbons, and Kevin J. Murphy. 2002. "Relational Contracts and the Theory of the Firm." *Quarterly Journal of Economics*, 117, 1: 39-84.
- Corts, Kenneth, and Jasjit Singh. 2004. "The Effect of Repeated Interaction on Contract Choice: Evidence from Offshore Drilling." *Journal of Law, Economics, and Organization*, 20: 230-260.

Authority and Decision Making Within Firms:

- \*Aghion, Philippe, and Jean Tirole. 1997. "Formal and Real Authority in Organizations." *Journal of Political Economy*, 105: 1-29.
- Hart, Oliver and John Moore. 2005. "On the Design of Hierarchies: Coordination Versus Specialization." *Journal of Political Economy*, 113: 675-702.

Overview:

- \*Gibbons, Robert. 2005. "Incentives Between Firms (and Within)." *Management Science*, 51, 1: 2-17.

October 12, 12:45-16:30: Lecture 4: Alternative Organizational Forms (JP)

Comparing Organizational Forms:

- \*Hansmann, Henry. 1996. *The Ownership of Enterprise*. Cambridge, MA: Belknap/Harvard University Press; Part I.
- Ménard, Claude. 1996. "On Clusters, Hybrids, and Other Strange Forms: The Case of the French Poultry Industry." *Journal of Institutional and Theoretical Economics*, 152: 154-183.
- Herbst, Patrick, and Jens Prüfer. 2007. "Firms, Nonprofits, and Cooperatives: A Theory of Organizational Choice." CentER Discussion Paper, No. 2007-07.

#### Nonprofits:

- Hansmann, Henry. 1980. "The Role of Nonprofit Enterprise." *Yale Law Journal*, 89, 5: 835-901.
- Glaeser, Edward. L., and Andrei Shleifer. 2001. "Not-for-profits entrepreneurs." *Journal of Public Economics*, 81: 99–115.
- \*Prüfer, Jens. 2011. "Competition and Mergers among Nonprofits", *Journal of Competition Law & Economics*, 7, 1: 69-92.

#### Clubs:

- Cornes, Richard, and Todd Sandler. 1996. *The Theory of Externalities: Public Goods and Club Goods*. Cambridge: Cambridge University Press; ch. 12.
- \*Prüfer, Jens, and Uwe Walz. 2012. "Academic faculty governance and recruitment decisions." *Public Choice*: DOI 10.1007/s11127-011-9885-9

#### Network Forms of Organization:

- Powell, Walter. 1990. "Neither Market Nor Hierarchy: Network Forms of Organization." *Research in Organizational Behavior*, 12: 295-336.
- \*Baker, George, Robert Gibbons, and Kevin J. Murphy. "Strategic Alliances: Bridges Between 'Islands of Conscious Power.'" *Journal of the Japanese and International Economies*, 22, no. 2 (June 2008): 146-163.

#### Public organizations:

- \* Hart, Oliver, Andrei Shleifer, and Robert W. Vishny. 1997. "The Proper Scope of Government: Theory and an Application to Prisons." *Quarterly Journal of Economics*, 112: 1127-61.

#### November 30, 12:45-16:30: Lecture 11: Institutions and Organizations (JP)

#### Economic Governance and Alternative Governance Institutions:

- Greif, Avner. 2006. *Institutions and the Path to the Modern Economy: Lessons from Medieval Trade*, New York: Cambridge University Press; ch.1.
- Dixit, Avinash. 2004. *Lawlessness and Economics: Alternative Modes of Governance*, Princeton, NJ: Princeton University Press; ch.1.
- \* Dixit, Avinash. 2009. "Governance Institutions and Economic Activity," *American Economic Review*, 99, 1: 5-24.

#### Private v. Public Enforcement:

- \* Dixit, Avinash. 2003b. "Trade Expansion and Contract Enforcement," *Journal of Political Economy*, 111, 6: 1293-1317.
- \* Masten, Scott E., and Jens Prüfer. 2011. "On the Evolution of Collective Enforcement Institutions: Communities and Courts", CentER Discussion Paper, No. 2011-74; Ross School of Business Paper No 1157.

Enforcement in the Shadow of the Law: Theory:

- Dixit, Avinash. 2003a. "On Modes of Economic Governance," *Econometrica*, 71: 449-81.
- Ellickson, Robert C. 1991. *Order Without Law: How Neighbors Settle Disputes*, Cambridge, MA: Harvard University Press.
- \* Greif, Avner. 1993. "Contract Enforceability and Economic Institutions in Early Trade: The Maghribi Traders' Coalition," *American Economic Review*, 83: 525-48.
- \* Greif, Avner, Paul R. Milgrom, and Barry R. Weingast. 1994. "Coordination, Commitment, and Enforcement: The Case of the Merchant Guild," *Journal of Political Economy*, 102: 745-76.
- Kali, Raja. 1999. "Endogenous business networks," *Journal of Law, Economics & Organization*, 15: 615-636.
- Kandori, Michihiro. 1992. "Social Norms and Community Enforcement," *Review of Economic Studies*, 59,1: 63-80.
- \* Milgrom, Paul R., Douglass C. North, and Barry R. Weingast. 1990. "The Role of Institutions in the Revival of Trade: The Law Merchant, Private Judges, and the Champagne Fairs," *Economics and Politics*, 2: 1-23.
- Ostrom, Elinor. 1990. *Governing the Commons*. Cambridge: Cambridge University Press.
- Tabellini, Guido. 2008. "The Scope of Cooperation: Values and Incentives," *Quarterly Journal of Economics*, 123(3): 905-950.

Enforcement in the Shadow of the Law: Applications:

- Fafchamps, Marcel. 2004. *Market Institutions in Sub-Saharan Africa: Theory and Evidence*. Cambridge, MA: MIT Press.
- \* Leeson, Peter T. 2007., "An-arrgh-chy: The Law and Economics of Pirate Organization", *Journal of Political Economy*, 115, 6: 1049-1094.
- Richardson, Gary, and Michael McBride. 2009. "Religion, Longevity, and Cooperation: The Case of the Craft Guild", *Journal of Economic Behavior & Organization* 71: 172-186.
- Skarbek, David. 2010. "Putting the 'Con' into Constitutions: The Economics of Prison Gangs", *The Journal of Law, Economics, & Organization*, 26, 2: 183-211.