

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

**Fall 2016**

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<b>Instruction language:</b>	<b>English</b>
<b>Type of Instruction:</b>	<b>interactive lectures, discussion of journal articles</b>
<b>Type of exams:</b>	<b>Assignments, class participation, research proposal</b>
<b>Level:</b>	<b>Research Master Economics, 2<sup>nd</sup> year</b>
<b>Course load:</b>	<b>3 ECTS; 6 x 180 minutes</b>

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

The course delivers an introduction to theories of organizations (about 2/3) and institutions (about 1/3) that rely on economic thinking. The goal is to familiarize students with theoretical approaches, to guide them to the research frontier in selected topics, and to let them explore open and interesting research questions, both theoretical, empirical, and experimental, on their own.

We study relationships within firms (authority, incentives, the role of managers), between firms (formal and informal contracting, vertical and horizontal integration, strategic alliances, firm networks and groups), and beyond firms (organizations and institutions). We review the main economic theories that explain the existence, scale, and scope of firms (transaction costs economics, property rights theory, and agency theory), study contracting options and the impact of an organization's form (for-profit, nonprofit, public, cooperative, or member-owned) on its decisions. In the institutional economics part, we study how different institutions, both by private and public ordering, solve economic governance problems such as collective actions, contract enforcement, and property rights protection.

### **Course format:**

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 to read papers and send 2 questions on each paper before the respective 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.

The literature used consists of research in economics but many papers take an interdisciplinary perspective, e.g. combining economics with law, history, management or political science. Similarly, the class in this course typically consists of students both from economics and from business.

## 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)

### Lecture 1: Foundations of Organizational Economics

#### Transaction Cost Theory

- \* Coase, Ronald. 1937. "The Nature of the Firm." *Economica*, 4: 386-405.
- \* Williamson, Oliver. 1979. "Transaction Cost Economics: The Governance of Contractual Relations." *Journal of Law and Economics*, 22: 233-261.
- \* 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.
- Hennart, Jean-Francois. 1993. "Explaining the swollen middle: why most transactions are a mix of "market" and "hierarchy". *Organizational science*, 4 (4): 529-547
- Williamson, Oliver. 1971. "The Vertical Integration of Production: Market Failure Considerations." *American Economic Review P&P*, 61: 112-123.
- Bigelow, Lyda S., Argyres, Nicholas. 2008. Transaction costs, industry experience and make-or-buy decisions in the population of early U.S. auto firms". *Journal of Economic Behavior & Organization*, 66: 791-807
- Kyle J. Mayer and Robert M. Salomon Capabilities, Contractual Hazards, and Governance: Integrating Resource-Based and Transaction Cost Perspectives. *ACAD MANAGE J* October 1, 2006 vol. 49 no. 5 942-959

#### 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.

### Lecture 2: Incentives, Ownership, and Contracts

#### Incentives:

- 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.
- \* Gibbons, Robert, and John Roberts. 2012. "Economic Theories of Incentives in Organizations." In: Robert Gibbons and John Roberts (eds.), *Handbook of*

*Organizational Economics*. Princeton, NJ: Princeton University Press: 56-99.

#### Optimal Ownership:

- \* Hansmann, Henry. 1996. *The Ownership of Enterprise*. Cambridge, MA: Belknap/Harvard University Press; Part I.
- 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.

#### Methods: Clinical Studies:

- \* Baker, George P., and Ricard Gil. 2012. "Clinical Papers in Organizational Economics." In: Robert Gibbons and John Roberts (eds.), *Handbook of Organizational Economics*. Princeton, NJ: Princeton University Press: 193-212.

#### 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.

#### Lecture 3: Managers and Authority

##### Informal Contracts and the Role of Managers:

- 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.
- \* Gibbons, Robert, and Rebecca Henderson. 2012. "What Do Managers Do?" In: Robert Gibbons and John Roberts (eds.), *Handbook of Organizational Economics*. Princeton, NJ: Princeton University Press: 680-731.
- \* Bloom, Nicholas, Lemos, Renata, Sadun, Raffaella, Scur, Daniela, and John Van Reenen. 2014. "The New Empirical Economics of Management," *Journal of the European Economic Association* 12(4): 835-876.

##### 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.
- Gibbons, Robert. 2005. "Incentives Between Firms (and Within)." *Management Science*, 51, 1: 2-17.
- \* Bolton, Patrick, and Mathias Dewatripont. 2012. "Authority in Organizations." In: Robert Gibbons and John Roberts (eds.), *Handbook of Organizational Economics*. Princeton, NJ: Princeton University Press: 342-372.

## Lecture 4: Alternative Organizational Forms

### 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.
- \* Filistrucchi, Lapo, and Jens Prüfer. 2013. "Faithful Strategies: How Religion Shapes Nonprofit Management." *CentER Discussion Paper*, No. 2013-052.

### 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.

### Member-owned Organizations:

- Cornes, Richard, and Todd Sandler. 1996. *The Theory of Externalities: Public Goods and Club Goods*. Cambridge: Cambridge University Press; ch. 12.
- \* Larrain, Maria, and Jens Prüfer. 2015. "Trade Associations, Lobbying, and Endogenous Institutions." *Journal of Legal Analysis* 7(2): 467-516.

## Lecture 5: Institutions and Economic Governance

### Overviews and Classification:

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

### Solving the Credibility Problem in Historical Perspective

- \* 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.

## Lecture 6: The Credibility Problem and the Clarity Problem

### Private vs. Public Ordering:

- 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.
- Dixit, Avinash. 2003. "Trade Expansion and Contract Enforcement," *Journal of Political Economy*, 111, 6: 1293-1317.
- 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.
- \* Masten, Scott E., and Jens Prüfer. 2014. "On the Evolution of Collective Enforcement Institutions: Communities and Courts", *Journal of Legal Studies*, 43(2): 359-400.
- \* Prüfer, Jens. 2016. "Business Associations and Private Ordering," *Journal of Law, Economics, and Organizations*, 32(2): 306-358.

### A Behavioral Approach to the Credibility Problem: Endogenous Social Norms

- \* Tabellini, Guido. 2008. "The Scope of Cooperation: Values and Incentives," *Quarterly Journal of Economics*, 123(3): 905-950.

### Solving the Clarity Problem:

- \* Hadfield, Gillian K. and Barry R. Weingast. 2012. "What Is Law? A Coordination Model of the Characteristics of Legal Order," *Journal of Legal Analysis*, 4: 471-514.