

MBA 603 Detailed Course Outline and Reading Assignments:

Monday, August 14: 8:00 a.m.-12:00 noon/1:00 p.m.-5:00 p.m.

Topics: basics of market systems, demand and supply analysis.

Reading assignments:

Text:

BSZ, ch. 3, "Markets, Organizations, and the Role of Knowledge."

Goal of economic systems

Property rights and exchange in a market economy

Basics of supply and demand

 The price mechanism

 Prices as social coordinators

 Government intervention

Markets versus central planning

 Specific knowledge and the economic system

 Incentives in markets

Contracting costs and existence of firms

 Contracting costs within firms

Outside readings:

"China's Winter of Discontent," *WSJ*, 3/14/06.

"Lawmakers struggle to define gasoline price 'gouging,'" *WSJ*, 11/9/05.

"Tenants in Mumbai will endure a lot for an \$8.50 flat," *WSJ*, 6/5/06.

Team assignment #1: Due at the beginning of class on 8/16.

Read "Un-Natural Situation," (*WSJ* 6/15/06) and evaluate short and long term effects of recent sharp changes in natural gas prices on related markets. Imagine that you and your teammates work for an energy consulting firm. You have several clients in related markets (i.e. upstream, downstream, substitutes, complements) whom you advise on a regular basis. Recent wide swings in gas prices have led them to seek your analytical input. Choose two or three related markets to focus on, and submit a two page (outline format with bullet points, 12 pt. font, 1-inch margins) report. Evaluate short-run and long-run adjustments that can be expected to occur in these markets.

Wednesday, August 16: 8:00 a.m.-12:00 noon/1:00 p.m.-5:00 p.m.

Topics: determinants of demand, estimating demand, elasticity.

Reading assignments:

Text:

BSZ, ch. 4: "Demand."

Demand functions

Demand curves

Law of demand

Elasticity of demand

Other factors that influence demand

Prices of related products

Income

Other variables

Industry vs. firm demand

Product attributes

Product life cycles

Demand estimation

Interviews

Price experimentation

Statistical analysis

Outside readings:

"Thrill parks try to boost attendance: Some lower their fees to attract crowds,"

Lexington Herald-Leader, 5/27/06.

Team assignment #2: Due at the beginning of class on 8/18.

Read "When it comes to plates, Virginians are vain bunch," (*The Roanoke Times* 6/4/06) and put together a proposal for how you would conduct a demand study for vanity plates for the Kentucky Division of Motor Vehicles.

Suppose that Kentucky offers only one basic auto license plate at a price that just covers all of the costs involved in producing and distributing license plates. The Kentucky DMV puts out a request for proposals to study the possibility of increasing license plate revenues without raising the ire of drivers/voters. Since your firm specializes in quantitative marketing research, you decide to respond. You know that many other states have extensive vanity license plate programs. The KY DMV knows all about the costs of producing license plates, but it needs specific information about demand so that it will know how to price different types of specialized plates. Write a two-page proposal that outlines how you would conduct such a study, what data you would collect, and what economic relationships you would attempt to identify.

Friday, August 18: 8:00 a.m.-10:00 a.m./1:00 p.m.-3:00 p.m.

Topics: production, economic costs, economic profit.

Reading assignments:

Text:

BSZ, ch. 5: "Production and cost."

Production functions

 Returns to scale

 Returns to a factor

Choice of inputs (skim)

Costs

 Cost curves

 Short run vs. long run

 Minimum efficient scale

 Learning curves

 Economies of scope

Outside readings:

"Frito-Lay Aims to Cut Gas Bill's Bite," *WSJ*, 6/5/06.

"Small Talk," *WSJ* 5/30/06.

Individual assignment: take virtual plant tours of Toyota's Georgetown manufacturing facility (<http://www.toyotageorgetown.com/vtour/vtour.asp>) and Purity Dairy's dairy processing facility (<http://www.puritydairies.com/tour/index.html>).

As you tour these two plants, try to understand how various different inputs are used in each production process to produce different outputs. You should attempt to connect each theoretical concept in the textbook reading with something you observe in the plant tour. If you were plant manager, how would you go about increasing output over a short time horizon? A longer time horizon? How difficult would it be to change the amounts of different inputs? Are any of the human or physical capital inputs specialized to this particular production process? How much of the investment in plant and equipment is fixed and irreversible?

Monday, August 21: 8:00 a.m.-12:00 noon/1:00 p.m.-5:00 p.m.

Topics: horizontal boundaries of the firm.

Reading assignments:

Text:

BDSS, ch. 2: “The Horizontal Boundaries of the Firm: Economies of Scale and Scope.”

Where do economies of scale come from?

Definition of economies of scale

Definition of economies of scope

Where do scale economies come from?

Indivisibilities and the spreading of fixed costs

Inventories

The cube-square rule and the physical properties of production

Sources of diseconomies of scale

The learning curve

Outside readings:

“A Tale of Two Auto Plants,” *WSJ*, 5/24/06.

“Power Pork: Corporations Begin to Turn Hog Business into an Assembly Line,”
WSJ, 3/28/94.

Wednesday, August 23: 8:00 a.m.-12:00 noon/1:00 p.m.-5:00 p.m.

Topics: vertical boundaries of the firm.

Reading assignments:

Text:

BDSS, ch. 3: “The Vertical Boundaries of the Firm.”

Make vs. buy

Upstream, downstream

Some make-or-buy fallacies

Reasons to “buy”

Tangible benefits of using the market: exploiting scale and learning

Economies

Coordination of production flows through the vertical chain

Relationship-specific assets

Rents and quasi-rents

The holdup problem

The holdup problem and transactions costs

Recap: from relationship-specific assets to transactions costs

Summarizing make-or-buy decisions: the make-or-buy decision tree

Outside readings:

“Made to Measure: Invisible Supplier Has Penney’s Shirts All Buttoned Up,”

WSJ, 9/11/03.

“Bike Maker Faces a Tactical Shift,” WSJ, 10/28/98.

Team Assignment #3: Due at the beginning of class on 8/25.

The University uses many inputs in its production of teaching, research, and service. It in-sources (makes) many of these inputs, and out-sources (buys) many others. The Executive Vice President for Finance and Administration commissions your group to evaluate various activities/inputs in UK’s educational production process for in-sourcing or out-sourcing. Your report should explain the economic rationale for each recommendation that you make.

An example of the type of activity you might consider is the University’s recent decision to outsource duplicating. The Duplicating Center in the basement of the White Classroom Building was closed, and the University has contracted with Kinko’s to provide duplicating services. Choose a couple of activities that might save the University money if they were outsourced. Choose a couple of activities that are more efficiently done in-house. Explain the economic logic in each of your recommendations. Provide a two-page report of your group’s brainstorming.

Friday, August 24: 8:00 a.m.-10:00 a.m./1:00 p.m.-3:00 p.m.

Topics: principal-agent relationships.

Reading assignments:

Text:

BDSS, ch. 14: "Agency and Performance Measurement."

The principal/agent framework

Using contracts to provide incentives

How employees respond to performance measures in incentive contracts

Costs of tying pay to performance

Risk aversion and risk sharing

Outside readings:

"Big Mac's Makeover," *The Economist*, 10/16/04.

"Levi's Factory Are Assigned to Teams, and Morale Takes a Hit," *WSJ*, 5/20/98.

Individual assignment: visit several different fast-food restaurants, purchase a meal, and then observe while you consume your meal. The owner of the brand name (e.g. Wendy's) has a strong incentive to maintain system-wide quality, while each franchisee has an incentive to chisel on quality at its own location and free-ride on the company's reputation. Imagine that you have been employed by corporate headquarters to improve the ways that the franchisor monitors each individual outlet. Remember that you want to come up with cheap and easy, yet effective, monitoring mechanisms. If you want to make the shift manager nervous, bring along a pad of paper and take notes while you look around. Discuss your thoughts with your classmates.