PPE 110A&B – Economics Seminar and Tutorial
Spring 2016 Syllabus

Professor Cameron Shelton
Email: cshelton@cmc.edu
Bauer North 108 (Basement)
Office Hours: Tuesday/Thursday 3:00-4:30pm

Seminar: Bauer Center 2, Wednesday (and sometimes on Monday) 1:15pm-4:00pm
Tutorial: Bauer North 108, Monday (and once on Wednesday), by appointment

Course Description

Tutorial

Tutorial is loosely modeled on the traditional Oxbridge model. Ten of out twenty-eight meetings will be tutorials. Students will be split into two groups, \( x \) and \( y \). For each tutorial, each student will be paired with a member of the opposite group. One student will write a 1200-1600 word tutorial paper. The other student will receive this paper and write a 400-600 word comment on it. Students will alternate between writing papers and comments. Thus each student will write five papers and five comments over the course of the semester. Student papers and comments will provide the basis of a discussion among the two students and me. These tutorials will be held on Monday, in my office (Bauer North 108), last 40 minutes, and will be scheduled between Noon and 5pm. Papers must be e-mailed to me and to your tutorial partner by 11:59pm on Saturday. Comments must be emailed to me and to your tutorial partner by 9am Monday morning. The five papers will constitute 70% of your grade; the five comments the remaining 30%.

Seminar

On days without a tutorial, we will meet together for class in BC2. These days will consist of a mixture of discussion and lecture. In general, the first and largest part will consist of a discussion of the assigned readings while the second, smaller part will be a brief lecture to prepare you for coming material. In a few cases, the day is scheduled for only discussion or only lecture.

Each discussion section will come with a set of questions. You are expected to write answers to one or more of these questions. Your answers should posted on Sakai the day before the seminar. The answers should be approximately 300-500 words and serve both to test your understanding of the material and (more importantly) to provide a focus for our discussion. It goes without saying, therefore, that you are expected to have done the reading prior to each seminar. These answers will account for 40% of your seminar grade. A further 20% of your seminar grade will be determined by the quality of your participation. Half of that grade will be determined by me, the other half (confidentially) by your peers. The final 40% of your grade will be based upon a 6000-8000 word paper due at the end of the term. This paper will be an extended response to one of the questions or issues raised previously in tutorial or discussion.
**Grading Criteria:**
To reiterate what was explained above, your final grade will be calculated as the weighted average of the individual assignment grades using the following weights:

Tutorial:
- 5 Tutorial papers: 70%
- 5 Tutorial responses: 30%

Seminar:
- 14 Discussion Forum posts: 40%
- Participation grade (professor’s evaluation): 10%
- Participation grade (confidential peer evaluation): 10%
- Final paper: 40%

**Readings**
Many of the readings are articles which I have posted on Sakai.
The book by Trumbull is available as an ebook via Honnold library
In addition, the following books are available via Huntley or online booksellers.

**Policies**
Attendance: Come to seminar and tutorial prepared, come with the readings, and come on time. Given the nature of the tutorial, your tutorial papers must be in on time. I will enforce this by reducing your grade on the paper by one letter grade for each hour the seminar paper is late.

All components of both the tutorial and seminar must be completed to earn a passing grade. Participation obviously requires attendance, so excessive absences from the seminar will result in failing the course. To this end please make me aware of any planned or emergency absences as swiftly as possible. I may request documentation and/or make-up work.

Obviously, all work must be your own. If in doubt, cite! Possible violations of academic integrity will be reported to the Academic Standards Committee.

Finally, please turn your phones off and put them away; it will be good for your soul, not to mention class discussion. You may bring a computer or other electronic gadget, but it is to be used solely for accessing readings and taking notes—that means no Internet browsing or electronic chatting with friends! This is PPE so all of this should go without saying, but it has now been said.
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The Role of Markets

Readings:
1. Hayek “The Use of Knowledge in Society” *AER* 1945
2. Alchian and Demsetz, “Production, Information Costs, and Economic Organization” *AER* 1977

Discussion Questions: choose and respond to at least one
a. What are the classic errors of centralized planning? Of decentralized planning? Use examples.
b. Consider in turn each of a variety of types of organizations such as a for-profit company, non-profit, NGO, student group. Are decisions within this organization made in a centralized or decentralized manner?
c. Where, according to Alchian and Demsetz, does the crucial local knowledge reside in a firm, and how is it created or transmitted?
d. What are the factors that determine the proper organization of team production (form of the corporation)?
e. What are the particular set of challenges addressed by the limited liability corporation and how do the various institutional details fit together to solve these challenges?
f. Do modern information technologies shift the efficient mode of organization in favor of centralization or decentralization? In favor of markets or firms? Be specific in your examples.
g. Compare and contrast Hayek’s local knowledge with Scott’s *metis*. Why do they come to different conclusions regarding the role of markets?

[3] Wednesday January 27th: In-class Discussion

Externalities and the Coase Theorem

Readings:
4. *Free Parking*, NPR Planet Money Episode 630

Discussion Questions: choose and respond to at least one
a. What would be the difficulty with a centralized solution to the problem Coase describes in the first full paragraph of page 2?
b. Why is it that legal injunctions have no effect on economic usage and efficiency in sections 3-5? Does it follow that legal injunctions have no effects at all?
c. At the end of p13, Coase describes the “beauties of a smoothly operating pricing system.” What are the components of such a system, according to this article?
d. In a world with costly bargaining, Coase suggests several imperfect systems of assigning property rights. What are they and what are the factors that are most likely to be relevant when deciding which delivers the most efficient outcome?
e. What are the implications of Coase for distributional equity?
f. In section VII, Coase mentions it is important for “the results of legal actions [be] easy to forecast.” Why is this relevant to economic efficiency? Relatedly, what is the purpose of case law defining what is and is not a nuisance?
g. In section VII, Coase discusses several examples by which courts seem to weigh costs and benefits when assigning rights. Why should the court do this rather than simply assign the property right and tell the *already assembled parties* to decide on a side payment? Are the courts actually affecting the economic outcome or merely assigning disputed property rights?
h. What factors does Cheung believe explain institutional variation? What is the implied view of institutional change should these factors shift? How is this related to Coase?
Monday February 1st: Tutorial
Prediction Markets
Readings:

Prompt: Design a prediction market. It may pertain to daily life on campus, a job you have held, or public policy. Explain why there is a need for a prediction market (rather than some other arrangement). Specify the contracts to be traded explicitly. Discuss the likely strengths and shortcomings of your particular case, referencing the articles. You should cover who will trade, why they will, the distribution of information, etc.

Wednesday February 3rd: In-class Discussion
Principal-Agent Theory
Readings:

Discussion Questions: choose and respond to at least one
a. Bebchuck and Fried argue that “since Jensen and Meckling (1976) the problem of managerial power and discretion has been analyzed in modern finance as an ‘agency problem.’” In light of Sappington and Eisenhardt what does that mean?

b. What are the limits on optimal contracting in the context of hiring managers? Why do Bebchuck and Fried reject optimal contracting in favor of managerial power?

Monday Feb 8th: Tutorial
Decentralized Bargaining in Practice
Readings:

Prompt: Explain why Farrell views the Coase Theorem as tautological or wrong. Would Coase disagree?
Wednesday February 10th: In-Class Discussion

**Theories of the Firm**

Readings:

Discussion Questions: choose and respond to at least one

a. What is the fundamental puzzle that all of these “theories of the firm” are trying to answer? In other words, why would a classical economist operating in a Walrasian world not expect the firm to exist?
b. According to Coase, why would the owners of a production process want to replace exchange coordinated spontaneously by relative prices (a market) for coordination by central design or direction? Is Alchian and Demsetz answer “Coasian”?
c. What is asset specificity? How does it relate to the hold-up problem? What is quasi-rent and how does it differ from rents (economic profit)?
d. Is Hart’s theory merely a specific case of Coase? If so, what does he add? If not, why not?
e. Are these three theories mutually exclusive?

Monday February 15th: Tutorial

**Corporate Culture**

Readings

Prompt: Coase, Simon, and Kreps have fundamentally different explanations of the necessity of the organizational structure known as the firm. Contrast these visions. Are they mutually incompatible? What are the strengths and weaknesses of each?

Wednesday February 17th: Lecture

Optional Reading: Dixit and Skeath “Games of Strategy”, 2nd edition chapters 1, 3, 4, 9

Monday February 22nd: Lecture

Optional Reading: Dixit and Skeath “Games of Strategy”, 2nd edition chapters 11, 13
[11] Wednesday February 27th: In-class Discussion
Collective Action

1. Olson, Mancur (1965) *The Logic of Collective Action*, chapters 1-3, 5 & 6
2. Trumbull, Gunnar (2012) *Strength in Numbers: The Political Power of Weak Interests*, chapters 1, 3, 4, 5, 7, 8 (this is available via the library as an online ebook.)

Discussion Questions: choose and respond to at least one
a. Olson suggests that the potential for unravelling is a rationale for binding rules of membership and contribution. Do such rules raise the utility of all members?

b. Prior to Olson, political scientists argued that interest group politics is fair and functional provided everyone has access. Toward which groups and what sorts of policies is interest group politics biased?

c. How far do Trumbull’s examples of diffuse interest coordination circumscribe the Olson paradigm? What is the role of government in his examples?

d. Let us import Trumbull’s arguments to the decision of the contributor. Why, according to Trumbull, is Olson’s analysis of this decision incomplete? What, according to Trumbull’s various examples, do we need to add to Olson’s analysis of the agent’s decision so as to explain successful cooperation among diffuse interests?

e. What are the dynamic implications of Olson’s theory? What happens over time to interests that organize as the costs and benefits of policies change? As new technologies and possibilities arise? What happens over time to policy as a result?

Social Norms
Readings

Prompt: Choose and respond to one of the following
a. Compare and contrast Binmore’s and Ostrom’s visions of the development of cooperation.

b. How do the design principles that Ostrom reports relate to Binmore’s theory of social norms?

c. Contrast Binmore’s view of the social contract with that of Rawls. What insights can game theory bring to the idea of a social contract?


[14] Monday March 7th: In-Class Discussion
Institutions of Preference Aggregation
Reading

Discussion Questions: choose and respond to at least one
a. What voting mechanism is preferred? More generally, how ought we to judge voting mechanisms?

b. Which of the stability-institutions discussed in Shepsle and Weingast are democratic and/or fair? By what general principles ought we to judge such structures?

c. By what process does a society form and change its legislative institutions?

d. What are the transactions costs that might induce evolutionary stability of these institutions?
**[15] Wednesday March 9**th**: Tutorial  
Democratic Legitimacy**

Reading  

Optional additional reading  

Prompt: Arrow suggests that democracy cannot be a perfect summary of individual citizens’ preferences. Both Shepsle and Knight/Johnson seem to retreat from that goal. Summarize, compare, and judge their concessions.

**[---] Monday March 14**th**: No class, spring break  
[---] Wednesday March 16**th**: No class, spring break

**[16] Monday March 21**th**: In-class Discussion  
The Role of Political, Economic, and Social Institutions in Development  

Discussion Questions: choose and respond to at least one  

- Why does evidence of correlation between social capital and economic outcomes (e.g. Putnam et al cited p 402 of AJR) not constitute evidence of a causal relationship whereby low social capital delivers poor economic outcomes. What other causal structure is consistent with this correlation? Reason similarly about religious beliefs (e.g. re: Weber). Why is correlation evidence regarding the geography hypothesis less vulnerable to this critique? Indeed, is it altogether immune?  
- In what ways is “open access” in North, Wallace and Weingast a superior institution? In what ways is open access threatened by the problems identified in Olson and Ostrom?  
- AJR argue that political and economic institutions are designed by the conscious choice of those with de facto political power. Does this not ignore the coordination problem discussed by Olson and Ostrom?  
- How does the evidence in Henry and Miller square with AJR and NWW? Are the theories consistent?  
- According to AJR, how do institutional reforms occur? Why are they rare? How is it that reforming the constitution solves the problem of transitory de facto political power?
[17] Wednesday March 23rd: In-class Discussion
Culture, Natural Selection, and the Industrial Revolution
Readings:
2. *What Two Pasta Factories Tell Us About the Italian Economy*, NPR Planet Money Episode 400

Discussion Questions: choose and respond to at least one

a. What is the Malthusian trap? Why are vices and virtues seemingly flipped when in the trap? How does modernity make those still stuck in this trap even worse off, according to Clark?
b. What are the various norms that limit fertility (chapter 4)? What are the broader implications about the genesis and evolution of cultural norms? How does a society “decide” on such things given the decentralized nature of cultural practice? (Don’t miss footnote 6 on p72.)
c. What is Clark’s counter-argument to Acemoglu and Robinson? Is it convincing?
d. What is Clark’s answer to the question: why did the Industrial Revolution happen when and where it did?
e. Why do different countries have different labor productivity rates in essentially identical tasks?

Poverty Traps
Reading:
1. Collier, *The Bottom Billion*

Prompt: Is this new, policy-oriented reading consistent or at odds with our prior, more deeply theoretical readings? How would Acemoglu/Johnson/Robinson, Weingast/Wallis/North, and Clark respond to Collier’s policy prescriptions for countries in the bottom billion? What would Collier suggest they are missing?

[--] Wednesday March 30th: No class, professor out of town

[19] Monday April 4th: In-class Discussion
Asset Price Bubbles
In-class Discussion 1
2. *The Economist* “Sorry to Burst Your Bubble”
3. Cassidy “Are Speculative Bubbles Good?” *The New Yorker*

Discussion Questions: choose and respond to at least one

a. What factors are responsible for financial bubbles? Which are common and which seem to change across time?
b. What are the real economic costs and/or benefits of bubbles?
c. Is the existence of bubbles at odds with the Welfare Theorems?
[20] Wednesday April 6th: In-class Discussion
Financial Regulation
Readings:
1. Barth, Caprio, and Levine, *Guardians of Finance* (chapters 2, 3, 4, 8 plus first sections of 5, 6, 7)

Discussion Questions: choose and respond to at least one

a. According to BCL, what factors are responsible for financial crises and why are regulators incapable of stopping them?
b. Why would a disclosure system work? How will this ultimately change the incentives of firm managers and investors and prevent an asset price bubble and crash?
c. Why is the Sentinel necessary in a country with a free press?

Regulatory Independence
Readings:

Prompt: choose and respond to one

a. Why is an independent central bank incapable of functioning as a proper financial regulator? Is it possible for BCL’s Sentinel to be simultaneously relevant, accountable, and politically independent?
b. Why is monetary policy given special consideration? Should the IRS be reorganized into an independent tax agency? What about other government agencies such as the Pentagon, the ATF Bureau, etc?

[22] Wednesday April 13th: In-class Discussion
Income Inequality
Readings:
2. Mind the Gap, *The Economist*

Discussion questions: choose and respond to one

a. Choose one of Atkinson’s policy recommendations for reducing income inequality. What are the costs of your chosen policy recommendation? Contrast this with Piketty’s recommendation for a global tax on capital.
b. Explain the significance of human capital versus signaling explanations of wages for the income inequality debate.
[23] Monday April 18th: Tutorial
Redistribution
Readings:
  3. Krueger, Alan (2002), “Inequality, too much of a good thing” *unpublished manuscript*

Prompt: All sides of the inequality debate argue for “better” educational opportunities. In practice what does this mean? How do the educational reforms discussed in Krueger impact income or wealth inequality? Is it necessarily obvious they will decrease inequality? How would Sen or Jencks respond to programs that increased income equality by increasing access to better education for the poor?

[24] Wednesday April 20th: In-class Discussion
The Future of Work
Readings:
  4. The Machine Comes to Town, NPR Planet Money Podcast #623

Discussion questions: choose and respond to at least one

  a. What is the process by which technological unemployment is temporary rather than permanent? What are potential threats to that process? Why might this time be different?
  b. What sorts of human skills are complimentary to technology today? What sorts of human skills are likely to exhibit such complementarities in the future?
  c. Would technological unemployment be evenly distributed? What are the distributional consequences? What are the likely price responses? What are the likely political responses?
  d. How should a society of extensive automation and technological unemployment handle the problem of distribution? Would the problem of scarcity remain?

Cost Disease
Readings:

Prompt: Which is the proper response to cost disease: privatization, higher tax rates, or … something else? Does the answer depend on which stagnant sector is under discussion? Does it intersect with the shifts in the labor market noted by Autor, Brynjolffson, and McAfee? Are other policies needed in conjunction with the one you advocate? You may reference philosophical arguments to justify the moral choice but I am more interested in a clear economic analysis of the results of either choice prior to its moral justification.
[26] **Wednesday April 27th: In-class Discussion**

**Libertarian Paternalism**


Discussion questions: choose and respond to at least one

a. Does the Sunstein-Thaler proposal of two cafeteria lines solve Rizzo and Whitman’s objections? What about the idea of choosing a level of savings increase to trigger automatically when you receive a raise?

b. Do the paradoxical effects of choice noted by Schwartz and Ward mitigate the critiques of libertarian paternalism levied by Rizzo and Whitman?

[27] **Monday May 2nd: Tutorial**

**Asymmetric Paternalism**

Readings


Prompt: Choose and respond to one of the following.

a. Do the restrictions of “asymmetric” paternalism satisfactorily address the critiques of Rizzo and Whitman?

b. How does the deviation of human behavior from the rational *homo economicus* affect Coase’s theorem? Hayek’s view of markets? The proper balance between market and government allocation?

[28] **Wednesday May 4th: In-class Wrap Up**

Readings: TBD

Discussion questions: TBD

**Term Paper due 5pm Tuesday May 10th.**