September 7, 2018

Econ 243 Class Notes

Walked through schedule as overview topics: producers over consumers, and in general strategy unimportant unless there's a tradeoff between p and Q, some version of monopoly / market power.

Strategic interactions (soon defined via example), tacit collusion (examples from auto parts, local barbers of illegal non-tacit collusion), advertising, price discrimination, and lots on innovation. There's flexibility in the schedule, pending a potential date to visit Devils Backbone.

Beer (via the Ogle book) will provide a common set of industry examples. Approach me if you want to work on a different industry [I've already talked to one student.]

Initial example Hotelling model (see book index) using Anheuser-Busch entry into the light beer market launched by Miller's "Lite" in 1975. A clear equilibrium strategy: if consumers are located uniformly along a line segment, the original firm and any new entrant chose the same spot in product space. In other words, mimic your rival's product. And in fact the various "low-cal" beers ["Lite" may be trademarked!] are effectively indistinguishable in blindfold taste-tests.

But … the mathematical model is not robust, no solution if 3 firms, but always a solution with an even number! Does that make sense?

Three lessons: one (i) is that our models are very sensitive to assumptions, sometimes in ways that don't ring true. They help organize thinking, but (ii) real-world strategies do seem to be very specific to the circumstances. That (iii) makes the subject challenging: there are a many models, even if we limit ourselves to "major" examples and ignore variations. To be honest, that isn't disturbing, because strategy in the real world isn't easy. It does mean that our bottom line is a mindset rather than a recipe book.

A second example: cell phones. I made the claim that Apple is in decline. Underlying it is a model where a dominant firm doesn't swat at gnats, as will be detailed later in the term. And if we look at Africa, India and China there are lots of (generally still-small) competitors. Now there's the opposite evidence of Apple's market valuation. What does my simple analysis ignore? do minor variations in the model match the Apple case better, and give a different bottom line? We can return to this later in the term. I pose it as an interesting intellectual challenge that revolves around just a bit of real-world money.