



北京大學
汇丰商学院

Peking University HSBC Business School

EE&FE Industrial Organization 4th Module, 2017

Course Information

1.1. Instructor: David Ong

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Office Hour: Tues-Thursday 4:00pm-5:00pm by appointment.

1.2. Teaching Assistant:

Phone: TBA

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1.3. Classes:

Lectures: Tues-Fri 3:30pm-5:20pm

Venue: PHBS Building, rm 319

2. Course Description

1.1. Course overview:

Since Cournot and Bertrand, IO has been focused upon the economic analysis of imperfect competition among manufacturers; Manufacturers, until recently, have been at the heart of most developed economies. In the last 30 years, there has been a dramatic shift in developed economies from the manufacturing to the service sector. In the last 15 years, there has been a further shift in the service sector to the information service sector. In particular, more and more of the economy is now influenced by or controlled by experts. In light of this trend and in anticipation that you will be entering this economy, the focus of my course will be on the imperfect competition among experts and their firms. Some examples of what I mean by experts are doctors, lawyers, accountants, investment bankers, credit raters, and management consultants. What characterizes this area of the "knowledge economy" are gross asymmetric information between experts and the consumers of their services. As products get more

Page 1 of 4

technical, the issue of expert sellers dealing with less well informed consumers becomes more important for all parts of IO. When the consumer cannot assess the quality of a product even after consumption, the “expert problem” or the “credence good problem” arises. Such problems are particularly acute in China due to the lack of the development or corruption of the regulatory and certifications institutions for the health and safety of products. Some examples of recent scandals are: lead in toys, antifreeze in toothpaste, toxic chemicals in dry wall, poisoned milk and baby foods, poor construction quality which caused buildings to collapse in recent earthquakes and of course, and most recently, counterfeit vaccines. In this course, we will consider attempted solutions in the West which may open the way for solutions in China.

1.2. Objectives of the Course

This is a research orientated course. It will be run largely like a workshop, where I will first lecture about the basics, then help you find some topic to work on for your presentations. The 1st presentation will be a literature review. The 2nd will be a research proposal. There is not methodological restriction for possible presentation topics: it can be empirical, theoretical, or experimental. However, the topic must be in the area of credence goods/professional services. I will offer you a menu of papers, help you find an interesting topic, related literature and structure the proposal.

1.3. Prerequisites:

The course has no formal prerequisites.

1.4. 1.2 Textbooks and Reading Materials

The course will be based on my lecture notes which I will distribute before classes.

3. Learning Outcomes, Assessment/Grading Details

Research is risky, and the quality of an idea can be hard to judge at the beginning. Furthermore, it’s hard to come up with something interesting if it’s not fun. Thus, to encourage you to choose a fun topic and to hedge you against risk, a lot of your grade will depend on things that require only diligence, e.g., attendance and class participation.

About 80% of the course grade will be based on two presentations: 5% for the topic, 35% for the literature review and 40% for a research proposal. The literature review will be judged on your ability to present one or two papers and to answer related questions from me and the rest of the class. The research proposal will be judged on the originality, feasibility (i.e., low cost), availability of the data, and interestingness of the research idea. Both must be submitted to me the day before your presentation. They will then be distributed to the class. The presentation of the literature review is a chance for you to check and complete your understanding. The presentation of your ideas is a chance to get feedback.

Since this is a research orientated course, and the beginning of research is questioning and independent thinking, your participation in questioning is important for your learning. To encourage you to speak up, I will record your questions and comments in class. Students will then be ranked based on this record and be allotted the 5% accordingly. A further 15% of the grade is based on a quiz to check for basic understanding of the material, which requires minimal preparation to do well, given steady participation. Thus, the total percentage of credit for the course is as follows:

- Class attendance and participation 5%
- Midterm Quiz 15%
- Presentation 1 40%
- Presentation 2 40%

Actual implementation of the research design in Presentation 2 to a pilot study using actually data, though not required, is eligible for a 10% bonus points. I have funding for promising designs.

4. Topics of lectures

- 1) Search, experience and credence goods
- 2) Examples of credence goods
- 3) "Credence good problem" with professional services
- 4) Credence aspect, expertise, reviews
- 5) Bounded rationality
- 6) Economics of credence goods (CG)
- 7) Asymmetric information: reputation mechanism
- 8) Effect of competition
- 9) Market solutions
- 10) 2nd Order market solutions
- 11) Drivers of the increasing importance of the credence aspect of expert industries
- 12) Consumer beliefs about events that didn't occur
- 13) Warranties
- 14) Contingency fees and commissions in CG Market
- 15) Liability
- 16) On Doctors, Mechanics and Computer Specialists: The Economics of Credence Goods
- 17) Verifiability in Markets for Credence Goods
- 18) The Economics of Credence Goods: On the Role of Liability, Verifiability, Reputation and Competition
- 19) Guilt from Promise-Breaking and Trust in Markets for Expert Services Theory and Experiment

- 20) Price as a signal of quality
- 21) Surrogates of quality
- 22) Sweet lemons
- 23) Overconfidence in consumers
- 24) Sweet lemons in education
- 25) Word of mouth
- 26) Heterogeneously informed consumers
- 27) Statistical credence goods
- 28) Surrogates of quality and consumer learning
- 29) Statistical certification by other consumers
- 30) Certifiers as aggregators
- 31) Precision in reviews and trust
- 32) Quantifying likelihood of honesty of certifier
- 33) Adverse selection into certification
- 34) Group liability and trust
- 35) Externalities of specific products on brands and brand portfolios
- 36) Brand extension as signal of quality
- 37) Group report cards and risk sorting
- 38) Creating trust by sunk costs
- 39) Merits of occupational licensing and certification
- 40) Alternatives to licensing
- 41) Licensing and occupational sorting
- 42) Minimum quality standards and free entry
- 43) Effect on entry and exit
- 44) Franchising
- 45) Collective reputations and franchises
- 46) Joint liability among experts
- 47) Self-regulating organizations (SROs)
- 48) Quality standards and market power of SROs
- 49) Experiments in group reputation

5. Rules for Course

Lecture notes will be provided, so laptops must be closed and cell phones turned off. Past experience suggests that if a student misses classes, the quality of their class participation will be poor, and their presentations will be a waste of time for everyone. Therefore, attendance is mandatory, with exceptions for student's documented medical emergency and job interviews. There will be plenty of office hours. However, students are required to send me an email of their notes so we have a permanent record.