

Advanced Micro II: 32410

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Winter 2019

Overview of the Class

This class builds on some of the concepts you've learned in Micro I and II to study at a deeper level a variety of topics relevant to students of public policy. We will build foundations for understanding risk, uncertainty, problems of asymmetric information, public goods, and externalities. Throughout the course we will also discuss how policy makers grapple with the theoretical issues we've been discussing in class.

Text

The text is Nicholson and Snyder *Microeconomic Theory: Basic Principles and Extensions* 11th edition. However, your primary resource for studying/understanding the material should be my notes, which I will post online.

Logistics

Section I of this class meets on Mondays and Wednesdays from 9:30-10:50AM in room Keller 1022. Section 2 of this class meets on Mondays and Wednesdays from 11:00-12:20PM in room Keller 1022. There will be a TA section on Tues, 02:00 PM-03:20 PM, Thursdays, 11:00 AM-12:20 PM, and Fridays, 09:30 AM-10:50 AM. Please stick with the section you were enrolled in. I will hold office hours on Fridays from 3-4PM in Keller 2045. TA's OH are TBA. A Canvas website for the class has been set up. I will post readings and handouts there, make announcements, etc.

Formal Requirements

Formal requirements for this class are 5 problem sets, a midterm, a final exam, and class participation. The problem sets will be given out at least a week in advance and will be due at the beginning of class. You can work together on problem sets (in groups of up to 4) but everyone has to turn in their own problem set. Please write the names of anyone you worked with on your problem set. The preliminary date for the midterm is February 11th in class. The Final will be for both sections 1 and 2 on Monday, March 18, 2019, 1:00 -3:50pm in Keller 1022 (section 1) and Keller 1002 (section 2). Your final grade will be given by the following weights:

- 20% homeworks
- 35% midterm
- 40% final
- 5%: participation

Academic Integrity

Please read and understand the University of Chicago's statement on Academic Honesty and Plagiarism:

It is contrary to justice, academic integrity, and to the spirit of intellectual inquiry to submit another's statements or ideas of work as one's own. To do so is plagiarism or cheating, offenses punishable under the University's disciplinary system. Because these offenses undercut the distinctive moral and intellectual character of the University, we take them very seriously.

Proper acknowledgment of another's ideas, whether by direct quotation or paraphrase, is expected. In particular, if any written or electronic source is consulted and material is used from that source, directly or indirectly, the source should be identified by author, title, and page number, or by website and date accessed. Any doubts about what constitutes "use" should be addressed to the instructor.

Cheating, copying, and all forms of plagiarism and academic dishonesty are considered a serious offense in the Harris School of Public Policy. All work you submit must be your own. You may never pass off as your own the work of another student or materials you found online.

I will notify the Dean of Students of any violations of this policy, no matter how minor. A first offense will be punished with a zero for the assignment or test on which the violation occurred, and with being placed on academic probation. All instructors will be made aware of the first incident and a second offense is very likely to result in termination from the program.

Tentative Outline

- Monday 1/7: Introduction + Firm's decisions
 - review the nature of the firm's input choice problem and various types of cost
 - **NS Chapter 10.**
- Wednesday 1/9: Firm's decisions (continued)
 - **NS Chapter 10, Chapter 11.**
 - Costs, profit, and monopolists
- Monday 1/14: Partial equilibrium and taxation in a competitive market
 - Discuss deadweight loss of taxation, incidence of taxation, price floors, etc.
 - **NS pp. 439-447, 501-522**
- Wednesday 1/16: Christopher Gallen: Market Power and the Profit Incentive
- Monday 1/21: Martin Luther King Day (no class)
- Wednesday 1/23: Externalities, Coase theorem, Pigouvian taxes
 - Define externalities, discuss market failure, when can taxation restore efficiency? Property rights and externalities.
 - **NS pp. 685-694**
- Monday 1/28: General Equilibrium
 - Define an Edgeworth box, discuss partial vs. general equilibrium (examples of when it matters—taxation), discuss welfare theorems.
 - **NS pp. 457-489**
- Wednesday 1/30: Public Goods
 - Define Lindahl equilibrium: how to define equilibrium when everyone is paying different prices but consuming the same good at the same time, but each might want different quantities of the good.
 - **NS pp. 694-702**
- Monday 2/04: Public Goods
 - Discuss the problem of true preference elicitation, mechanisms to support true preference elicitation
 - **NS pp. 708-709**
 - Homework 2 due
- Wednesday 2/06: Review and catch up
- Monday 2/11: Midterm
- Wednesday 2/13: Risk and uncertainty
 - formalize the concept of risk, define expected values, lotteries. Define axioms of expected utility theory and vN-M expected utility functions. Begin discussing risk aversion.
- Monday 2/18: Risk and uncertainty (cont.)

- Discuss various equivalent definitions of risk aversion, certainty equivalents, risk premia, CARA, DRRA, etc.
- What is the alternative to insurance and why does insurance/income smoothing increase welfare?
- **NS pp. 209-222**; notes closely follow **MWG ch. 6 (pp. 167-194)** which is posted on blackboard.
- Wednesday 2/20: An introduction to insurance
 - Define insurance and show that a risk averse person chooses perfect insurance under “fair” prices. Formalize the notion of insurance: who can offer it, to whom, and at what price?
 - **NS pp. 233-238**
 - Homework 3 due
- Monday 2/25: Adverse selection and moral hazard
 - Why are insurance markets in real life so incomplete (deductibles, caps in coverage, tons of rules, denial of coverage)? Discuss practical barriers which arise when one agent’s behavior/characteristics aren’t perfectly observable to another: adverse selection and moral hazard. Define first-best vs. second-best equilibrium.
 - **NS pp. 641-653, 670-674**
- Wednesday 2/27: Adverse selection and moral hazard (cont.)
 - **NS pp. 641-653, 670-674**
 - Homework 4 due
- Monday 3/04: Economics of discrimination
 - What do economists have to say about discrimination? We will define two theories of discrimination: statistical discrimination (in which individuals are assigned the average attributes of their group when being evaluated) and taste-based discrimination (in which employers/customers/coworkers dislike interactions with members of minority groups). How does statistical discrimination affect wages and employment of minority workers? How might statistical discrimination affect firm tenure, lifecycle wages, and promotion?
 - ban the box and the unintended consequences of policy intervention
- Wednesday 3/06: Economics of discrimination
 - We will discuss taste-based discrimination and how discrimination can survive in competitive markets. We will discuss empirical evidence to support various models of discrimination.
 - **Charles, K. K. and Guryan, J. (2008). Prejudice and wages: An empirical assessment of becker’s the economics of discrimination. *Journal of Political Economy*, 116(5):773–809
 - Homework 5 due
- Monday 3/11: NO CLASS
- Wednesday 3/13: Guest Lecture
- Friday 3/15: Make-up class 5PM-6:20PM