

MICROECONOMIC POLICY ANALYSIS

I. OBJECTIVES

This course continues from PP210A and shares the same general objectives, which are repeated here. It is designed to teach you how economic analysis can be brought to bear on public policy issues. The vantage point from which you will bring it to bear is up to you, but the training helps you to form your vision as an analyst, public manager or civic leader. It helps you to understand what is possible, what is practical, and what is desirable. Each of you, in diverse ways, will work to further the public interest. Each of you will work with and around many special interests when you try to effect change. You will rely upon your economics training to help keep your public-interest vision clear and to achieve it.

Specifically, you will learn: (1) *to identify the relevant economic questions* to consider about policy issues that you must confront; (2) *to evaluate analyses* that you will encounter in the policy world for their economic strengths and weaknesses; (3) *to comprehend* and evaluate what professional economists write in the *economic journals* that may bear on issues of concern to you; (4) *to design policy alternatives* with cognizance of their economic consequences; and (5) *to communicate* economic analysis effectively in the policy-making process.

We continue with the same textbooks this semester. I will emphasize the material from the second half of my book **The Microeconomics of Public Policy Analysis (MPPA)**, Princeton Univ. Press, 2002). The readings from Walter Nicholson & Christopher Snyder (**Microeconomic Theory**, 10th ed.) are optional, intended both to supplement the theory in **MPPA** as well as to provide a second way of explaining many concepts. In addition, there are a small number of required articles that supplement the text materials (most available online through the UC MELVYL system, any others by distribution). You are expected to achieve command over the principles contained in the textbooks as they may bear on issues of public policy. *It is not sufficient simply to learn the principles; you must learn how and when they may be applied to issues of policy. You must learn how to think and analyze using them. You must learn to use them as a way to create improvements.*

To achieve this, many principles are developed in the context of particular policy issues that I hope are of interest to you for their own sake. The issues we will discuss are identified on the reading list. The issues are sequenced to allow systematic development of the relationships between principles and to allow repetition of principles in different applications.

II. CLASS MEETINGS

Classes meet three (3) times per week for 1-1/2 hours each. The Monday and Wednesday classes will be used to introduce new material that is required of all students. On Friday, generally the class will review the principles of theory introduced in earlier classes, as well as questions about the application of these principles and problem sets.

III. ASSIGNMENTS

A. Reading

Assignments are to be read before coming to class. Don't let yourself fall behind. If you feel there is too much reading, yell.

B. Problem Sets

Problem sets will be assigned approximately every 2-3 weeks. Students are not expected to spend more than three hours on any problem set; do what you can within that time frame. While you may discuss the problems before you attempt to do them, please turn in your assignment before actually finding out how others did it. I want to know what each person can do on his/her own and to be able to judge progress over time.

C. Written Exercises

During the semester, one short memo assignment (given February 25th, due March 4) will be given in connection with a case assignment. The assignment requires you to apply economic principles, given limited data, to a policy problem. It also requires you to communicate the results of your work appropriately.

A second memo assignment will be given on April 8 and due on April 22. This assignment will require you to read one or more journal articles or other documents and use them, along with your general economic skills, in a new policy context.

IV. GRADING

To receive at least a passing grade, all problem sets must be turned in on time and they must show a satisfactory level of work. Other than this, they are not counted in grading. They will be corrected and scored for your benefit.

The short memo assignment due March 4 will count for 20% of the semester grade. A mid-term examination will be given on March 18 and count for 25% of the semester grade. The third graded assignment will be the memo due on April 22 and will count for 30% of the grade.

There will be a final exam on May 14, 9AM-12 in Room 250 GSPP, and it will count for 25% of the semester grade.

Lectures Mon. & Wed. Sect. 1 8:30-10:00 Rm 250 GSPP; Sect. 2 10:00-11:30 Rm 250 GSPP

Review Fri. S101 9-10:30 Rm 250 GSPP; S102 10:30-12 Rm 250 GSPP

READING ASSIGNMENTS

- I. Efficiency** January 21, 26
- MPPA**, Chapter 12, pp. 461-471 (through "Efficiency in an Economy with Production")
Nicholson, Chapter 13, 442-449 (Edgeworth Box Diagram-Example 13.1), Chapter 13, 466-471, 476-481.
- II. Achieving Efficiency Through Pricing in Perfectly Competitive, Trouble—Free Markets**
- A. Price Formation in Competitive Product Markets January 28, Feb. 2
- MPPA**, review Chapter 10, esp. pp. 373-381, 397-414.
MPPA, Chapter 12, pp. 471-478 ("Competitive Equilibrium in One Industry")
Nicholson, Part IV Intro, Chapter 13, pp. 441-442, Chapter 12
- B. Pricing in Competitive Factor Markets February 4
- Nicholson**, review Chapter 11 on input demand, pp. 374-380.
- C. Capital Markets February 9
- MPPA**, review Chapter 8, pp. 278-296.
MPPA, Chapter 19, pp. 696-700 ("Perfectly Competitive...Capital Markets")
Nicholson, Chapter 17, pp. 595-608.
- D. The Pareto Optimality of Competitive Markets (discuss: roles of prediction markets) February 11
- MPPA**, Chapter 12, pp. 478-481 ("The Twin Theorems...")
Nicholson, Chapter 13, 471-475.
Andrew Leigh and Justin Wolfers, "Prediction Markets for Business and Public Policy," **The Melbourne Review**, 3, No. 1, May 2007, pp. 7-15, available online with Calnet at
<http://bpp.wharton.upenn.edu/jwolfers/Press/PredictionMarketsforBPP.pdf>

- E. General Competitive Analysis:
Tax Efficiency and Incidence Feb. 18, 23

MPPA, Chapter 12, pp. 481-506 ("General Competitive Analysis..." to end)
Nicholson, Chapter 13, 449-465, 487-488.

****MEMO ASSIGNMENT (GIVEN FEBRUARY 25) DUE****

March 4

III. Achieving Equity in Competitive Markets

- A. The Distribution of Income February 25

Piketty, Thomas and Emmanuel Saez, "How Progressive is the U.S. Federal Tax System? A Historical and International Perspective," **The Journal of Economic Perspectives**, 21, No. 1, Winter 2007, pp. 3-24 (available online through UC MELVYL)

Smeeding, Timothy, "Public Policy, Economic Inequality, and Poverty: The United States in Comparative Perspective," **Social Science Quarterly**, 86, s1, December 2005, pp. 955-983 (available online through Blackwell-Synergy)

- B. Specific Equity: Housing, Military Service and Gasoline

1. Apartment Rent Control March 2, 4

MPPA, Chapter 13

2. Military Service and Gasoline Rationing March 9, 11

MPPA, Chapter 14

IV. Efficiency Problems and Alternative Institutional Responses

- A. Market and Government Allocative Difficulties March 16

MPPA, Chapter 15

MPPA, Chapter 11, pp. 429-432 ("Public Bureaus and Enterprises")

John McMillan, "Market Design: The Policy Uses of Theory," **The American Economic Review**, 93, No. 2, May 2003, pp. 139-144 (available online through MELVYL).

Nicholson, Chapter 13, pp. 475-476, Chapter 19, pp. 687-689.

****MID-TERM EXAMINATION****

March 18

B. Public Goods and Public Television

March 30, April 1

MPPA, Chapter 16

David Brookshire and Don Coursey, "Measuring the Value of a Public Good: An Empirical Comparison of Elicitation Procedures," **The American Economic Review**, 77, No. 4, Sept. 1987, pp. 554—566 (available online through JSTOR).
Nicholson, Chapter 19, pp. 679-687, 690-693.

C. Externalities, with Application to Air Pollution

April 6, 8

MPPA, Chapter 17

Stern Review, The Economics of Climate Change, October 2006, Executive Summary (long), available on the website of HM Treasury, United Kingdom (http://www.hm-treasury.gov.uk/d/Executive_Summary.pdf)

William Nordhaus, The Stern Review on the Economics of Climate Change, May 2007, available at http://nordhaus.econ.yale.edu/stern_050307.pdf

Partha Dasgupta, Comments on the Stern Review's Economics of Climate Change, Nov. 2006, available at <http://www.econ.cam.ac.uk/faculty/dasgupta/STERN.pdf>

Nicholson, Chapter 19, pp. 670-679, 694.

D. Market Structure Problems

1. Oligopoly

April 13

MPPA, Chapter 18, pp. 660-671 (through "Oligopoly...")

Nicholson, Chapter 15

Lawrence Kahn, "Markets: Cartel Behavior and Amateurism in College Sports," Journal of Economic Perspectives, 21, No. 1, Winter 2007, pp. 209-226 (available online through UC MELVYL)

2. Natural Monopoly, with Application to Public Transit and CATV

April 15, 20

MPPA, Chapter 11, pp. 432-457 ("Empirical Predictions..." to end)

MPPA, Chapter 18, pp. 671-695 ("Rate-of Return..." to end)

Nicholson, Chapter 14

3. Imperfect Factor Markets, Labor and Higher Education Finance

April 22

MPPA, Chapter 19, pp. 700-707 ("The Social Rate..." and "Education...")

MPPA, Chapter 20, pp. 724-734 ("Asymmetric Information")

Nicholson, Chapter 16

****MEMO ASSIGNMENT (GIVEN APRIL 8) DUE****

April 22

4. Imperfect Factor Markets and Capital Investments (Exhaustible Resources)

April 27, 29

MPPA, Chapter 19, pp. 707-723 ("The Allocation..." to end)
 Nicholson, Chapter 17, pp. 608-614.

E. Imperfect Information and Decision-Making

1. Savings, Learning, and Economic Development—the Asian Miracle May 4

Richard R. Nelson and Howard Pack, "The Asian Miracle and Modern Growth Theory," **The Economic Journal**, 109, No. 457, July 1999, pp. 416-436 (available online through MELVYL, Blackwell).

2. Trust and Non-Profit Day Care May 6

MPPA, Chapter 11, pp. 417-429 ("Nonprofit Organizations...")
MPPA, Chapter 20, pp. 734-751 ("Nonprofit Organizations..." to end)
 David M. Blau, "Do Child Care Regulations Affect the Child Care and Labor Markets?" **Journal of Policy Analysis and Management**, 22, No. 3, Summer 2003, pp. 443-465 (skim, read carefully "Predictions from Economic Theory; available online through MELVYL).

SUMMARY & REVIEW May 11

****FINAL EXAM**** **9AM-12 Room 250 GSPP** **May 14**

Friday Schedule

Jan.	23	Open
Jan.	30	Review
Feb.	6	Review
Feb.	13	Review & PS#1
Feb.	20	Review
Feb.	27	Review
March	6	Review
March	13	Review & PS#2
March	20	Review & PS#3
March	27	Spring Break
April	3	Review
April	10	Review & PS#4
April	17	Review
April	24	Review
May	1	Review & PS#5
May	8	Review