Syllabus: MGMT 900 Economic Foundations of Management

Fall 2017

Professor Daniel Levinthal
3209 Steinberg-Dietrich Hall

Office Hours: By Appointment
levinthal@wharton.upenn.edu

Overview

This course examines some of the central questions in management with economic approaches as a starting point, but with an eye to links to behavioral perspectives on these same questions. Economics concerns itself with goal directed behavior of individuals interacting in a competitive context. We adopt that general orientation but recognize that goal directed action need not take the form of maximizing behavior, particularly for organizations comprised of individuals with possibly divergent interests and distinct sub-goals. Further, we treat competitive processes as playing out over meaningful periods of calendar time and, in general, not equilibrating instantaneously. A central property of firms, as with any organization, is the interdependent nature of activity within them. Thus, understanding firms as “systems” is quite important, a perspective which has important implications for understanding processes of organizational adaptation.

Among the sorts of questions we explore are the following: What underlies a firm’s capabilities? How does individual knowledge aggregate to form collective capabilities? What do these perspectives on firms say about the scope of a firm’s activities, both horizontally (diversification) and vertically (buy-supply relationships)? We also explore what our understanding of firms says about market dynamics and industry evolution, particularly in the context of technological change.

Assignments

Reaction Papers

For 10 of the 13 class sessions, you are to prepare a brief (roughly three page) reaction paper. This note should convey some provocative reflections on your part on the readings. These reflections may take many forms. They make be organized around some degree of puzzlement at the argument that the author(s) are making. They may reflect on contrasts in the arguments of the various authors. The write-up, might identify gaps in the existing literature and, in turn, research opportunities that these gaps present. Alternatively, the note could focus on application and examine ways in which the conceptual material may provide insight into some important phenomena. Alternatively, it might be useful to consider how important empirical phenomena point to gaps and weaknesses in the theoretical ideas. These notes should not merely, or primarily, restate the arguments of the various authors. In writing these notes, you should assume that your audience (me and your fellow students) have read the articles associated with that class session with some care and would not be interested in regurgitation of these ideas, but would be stimulated by a fresh and provocative take on them. Furthermore, your note may draw from a subset of the readings; however, it should be anchored in at least one of the articles.

Your reaction papers are to be submitted by **8 am the day of class**. Place an electronic copy on the course Canvass web site. **No reaction papers will be accepted subsequent to the associated class session.**

In-Class Discussion

In class, we will discuss the particular papers and explore the broader "conversations" in the field of which these papers are a part. To help seed these discussions **for each class** session, you are to choose an article for which you will serve as an opening discussant. This discussion will highlight what you view as the main contribution of the work, how it fits into the related literature, and particular strengths and limitations that you see in the work. A spreadsheet is posted in Canvass which lists the articles associated with each class session. There are two columns for student names as at most two students can choose the same piece. There is not a written component to this assignment and the article for which you serve as a discussant need not be featured in your reaction paper.

While students are responsible for a focal paper, all students are expected to have read carefully all papers. At various junctures in our discussions, I may select a student **at random** to serve as a catalyst to our conversation.

The course grade will be based on a 50% weight on your reaction papers, 50% class discussion.

Materials

The readings for the course are available on the course Canvas site: https://canvas.upenn.edu/courses/1370991. The readings for each class session have an internal logical flow and are **best read in the sequence suggested in the syllabus**.

1. **Theories of Choice** (9/6)

Kreps, D. (1988). *Notes on the Theory of Choice*. Boulder, CO: Westview publishing. Pp 43-46.

Simon, H. (1955). “A behavioral model of rational choice”. *Quarterly Journal of Economics,* 69: 99-118.

Kahneman, D. and A. Tversky (1979). “An analysis of decision under risk”. *Econometrica*, 47: 263-291.

Cohen, M. (2007). “Reading Dewey: Reflections on the study of routine”. *Organizational Studies*: 28(5): 773-786.

Levinthal, D. (2011). “What is not a behavioral strategy --- What’s the alternative?” *Strategic Management Journal*, 32: 1517-1523.

Parkes, D. and M. Wellman (2015). “Economic reasoning and artificial intelligence”. *Science,* 349: 267-272.
1:1-23.

2. **Problem of Goals** (9/13)

Gibbons, R. (1998). “Incentives in organizations”. *Journal of Economic Perspectives*, 12(4): 115-132.

Baker, G., R. Gibbons, and K. Murphy (1994). “Subjective performance measures in optimal incentive contracts”. *Quarterly Journal of Economics*, 109(4): 1125-1156.

Cyert, R. and J. March (1963). Chapter 3, “Organizational goals”. *A Behavioral Theory of the Firm*. Prentice-Hall, Englewood New Jersey.

Aoki, Masahiko (1983). “Managerialism revisited in the light of bargaining-game theory”. *International Journal of Industrial Organization*, 1: 1-21.

Sutton, R. and A. Barto (1999). Chapter 3 “The reinforcement learning problem”. *Reinforcement Learning*. MIT Press, Cambridge: MA.

3. **Views of Production** (9/20)

Syverson, C. (2011). “What determines productivity?” *Journal of Economic Literature*, 49(2): 326-365.

Nelson, R. and S. Winter (1982). "Organizational capabilities and behavior". *An Evolutionary Theory of Economic Change*. Cambridge, MA: Harvard University Press.

Diericks, I. and K. Cool (1989). "Asset stock accumulation and sustainability of competitive advantage". *Management Science,* 35: 1504-1511.

Helfat, C. and S. Winter (2011). "Untangling dynamic and operational capabilities: Strategy for the (n)ever changing world". *Strategic Management Journal,* 32: 1243-1250.

Gibbons, R. and R. Henderson (2012). "Relational contracts and organizational capabilities". *Organization Science*: 1350-1364.

4. **Resources and Rent** (9/27)

Barney, J. (1991). "Firm resources and sustained competitive advantage". *Journal of Management*, 17: 99-120.

Peteraf, M. (1993). "The cornerstones of competitive advantage: A resource-based view". *Strategic Management Journal*, 14: 179-191.

Jacobides, M., S. Winter, and S. Kassberger (2012). "The dynamics of wealth, profit, and sustainable advantage". *Strategic Management Journal,* 33(12): 1384-1410.

Adner, R. and P. Zemsky (2006). "A demand-based perspective on sustainable competitive advantage". *Strategic Management Journal*, 27: 215-239.

Gans, J. and M. Ryall (2017). "Value capture theory: A strategic management review". *Strategic Management Journal*, 38(1): 17-41.

5. **Aggregation of Knowledge** (10/4)

Hayek, F. (1945). "The use of knowledge in society". *American Economic Review,* 35: 519-530.

Stiglitz, J. (2000). "Contribution of the economics of information to Twentieth Century economics". *Quarterly Journal of Economics,* 115(4): 1444-1478.

Cohen, W. and D. Levinthal (1990). "Absorptive capacity: A new perspective on learning and innovation". *Administrative Science Quarterly,* 35: 128-152.

Grant, R. (1996). "Toward a knowledge-based theory of the firm". *Strategic Management Journal*, 17: 109-122.

Garicano, L. and Y. Wu (2012). "Knowledge, communication, and organizational capabilities". *Organization Science,* 23: 1382-1397.

6. **Firms as Interdependent Systems** (10/11)

Simon, H. (1962). "The architecture of complexity". *Proceedings of the American Philosophical Society,* 106: 467-482.

Levinthal, D. (1997). "Adaptation on rugged landscapes". *Management Science,* 43: 934-950.

Milgrom, P. and J. Roberts (1995). "Complementarities and fit: Strategy, structure, and organizational change". *Journal of Accounting and Economics,* 19: 179-208.

Porter, M. (1996). "What is strategy?" *Harvard Business Review,* Nov.-Dec. 3-20.

Henderson, R. and K. Clark (1990). "Architectural innovation: The reconfiguration of existing product technologies and the failure of established firms". *Administrative Science Quarterly,* 35: 9-30.

7. **Organizational Form** (10/18)

Harris, M. and A. Raviv (2002). "Organization design". *Management Science,* 48(7): 852-865

Aghion, P. and J. Tirole (1997). "Formal and real authority in organizations". *Journal of Political Economy*, 105(1): 1-29.

Csaszar, F. (2013). "An efficient frontier in organizational design: Organizational structure as a determinant of exploration and exploitation". *Organization Science,* 24(4): 1083-1101.

Puranam, P., O. Alexy, and M. Reitzig (2014). "What's 'new' about new forms of organizing?" *Academy of Management Review*, 39(2): 162-180.

Foss, N (2003). "Selective intervention and internal hybrids: Interpreting and learning from the rise and decline of the Oticon Spaghetti Organization". *Organization Science*, 14(3): 331-349.

8. **Exploration and Exploitation** (10/25)

March, J. (1991). “Exploration and exploitation in organizational learning”. *Organization Science*, 2: 71-87.

Posen, H. and D. Levinthal (2012). “Chasing a moving target: Exploration and exploitation in a dynamic environment. *Management Science*, 58: 587-601.

Manso, G. (2011). “Motivating innovation”. *Journal of Finance*, 66(5): 1823-1860.

Levinthal, D. and J. March (1993). “The myopia of learning”. *Strategic Management Journal*, 14: 95-112.

Burgelman, R. (1991). “Intraorganizational ecology of strategy making and organizational adaptation: Theory and field research”. *Organization Science*, 2: 239-262

Adner, R. and D. Levinthal (2008). “Doing versus seeing: Acts of exploitation and perceptions of exploration”. *Strategic Entrepreneurship Journal*, 2: 43-52.

9. Capital Allocation within the Firm (11/1)

Stein, J. (1997). Internal capital markets and the competition for corporate resources. *Journal of Finance*, 52(1): 111-133.

Dewatripont, M. and E. Maskin (1995). “Credit and efficiency in centralized and decentralized economies”. *Review of Economic Studies*, 62: 541-555.

Rajan, R. Servaes, H. and L. Zingales (2000). “The cost of diversity: The diversification discount and inefficient investment”. *Journal of Finance*, 55(1): 35-80.

Adner, R. and D. Levinthal (2004). “What is *not* a real option: Considering boundaries for the application of real options to business strategy”. *Academy of Management Review*, 29: 74-85.

Ewens, M., R. Nanda, and M. Rhodes-Kropf (2015). “Costs of experimentation and the evolution of venture capital”. Harvard Business School Working Paper.

10. **Economics of the Diversified Firm** (11/8)

Montgomery, C. (1994). “Corporate diversification”. *Journal of Economic Perspectives*, 8 (3): 163-78.

Penrose, E. (1959). Chapter VII "The economics of diversification" in *The Theory of the Growth of the Firm.* White Plains, NY: M. E. Sharpe.

Levinthal, D. and B. Wu (2010). "Opportunity costs and non-scale free capabilities: Profit maximization, corporate scope, and profit margins". *Strategic Management Journal,* 31: 780-801.

Helfat, C. and K. Eisenhardt (2004). "Inter-temporal economies of scope, organizational modularity, and the dynamics of diversification". *Strategic Management Journal,* 25: 1217-1232.

Rawley, E. (2010). "Diversification, coordination costs, and organizational rigidity: Evidence from microdata". *Strategic Management Journal,* 31(8): 873-891.

11. **Questions of Markets and Hierarchies** (11/15)

Coase, R. (1937). "The nature of the firm". *Economica,* 4(16): 386-405.

Williamson, O. (1988). "The logic of economic organization". *Journal of Law, Economics, and Organization.* 4(1): 65-93.

Grossman, S. and O. Hart (1986). "The costs and benefits of ownership: A theory of vertical and lateral integration". *Journal of Political Economy*, 94: 691-719.

Bradach, J. and R. Eccles (1989). "Price, authority, and trust: From ideal types to practical forms". *Annual Review of Sociology*, 15: 97-118.

Bidwell, M. (2012). "Politics and firm boundaries: How organizational structure, group interest, and resources affect outsourcing". *Organization Science,* 23(6): 1622-1642.

12. **Linking Firm and Industry Dynamics** (11/29)

Porter, M. (1981). "The contributions of industrial organization to strategic management". *Academy of Management Review*, 6(4): 609-620.

Klepper, S. and E. Graddy (1990). "The evolution of new industries and the determinants of market structure". *Rand Journal of Economics,* 21(1): 27-45.

Moeen, M. and R. Agarwal (2017). "Incubation of an industry: Heterogeneous knowledge bases and modes of value capture". *Strategic Management Journal,* 38: 566-587.

Adner, R., F. Ruiz-Aliseda, and P. Zemksy (2016). "Specialist versus generalist positioning: Demand heterogeneity, technology scalability and endogenous market segmentation". *Strategy Science,* 1(3): 184-206.

Hannan, M. (2010). "Partiality of membership in categories and audiences". *Annual Review of Sociology,* 36: 159-181.

Zuckerman, E. (2016). "Optimal distinctiveness revisited: An integrative framework for understanding the balance between differentiation and conformity in individual and organizational identities". *Handbook of Organizational Identities* Edited by M. Pratt, M. Schultz, B. Ashforth, and D. Ravasi. Oxford Press, Oxford England.

13. **Technological Change** (12/6)

Adner, R. (2002). "When are technologies disruptive? A demand-based view of the emergence of competition". *Strategic Management Journal,* 23: 667-688.

Gans, J., S. Stern (2003). "The product market and the market for 'ideas': Commercialization strategies for technology entrepreneurs". *Research Policy,* 32: 333-350.

David, P. (1990). "The dynamo and the computer: An historical perspective on the modern productivity paradox". *American Economic Review,* 80(2): 355-361.

Levinthal, D. (1998). "The slow pace of rapid technological change: Gradualism and punctuation in technological change". *Industrial and Corporate Change,* 7(2): 217-247.