**Econ 4390 The Economic Theory of Advertising**  Simon P. Anderson TENTATIVE COURSE OUTLINE, FALL 2015

**Lectures:** T, R, 1100-1215, New Cabell 332

**Office Hours:** W 1030-1130 or by appointment.

**Office:** Monroe, 239, tel. 4-3861; sa9w@

**Dates**:

first class T, 8-25; last class T, 12-8;

no classes 10-6, 11-26; final exam R 12-17, 0900-1200.

**Grading:** 10-15 quizzes (25%); presentation (20%); final (50%); discretionary/participation (5%). All parts of the course are compulsory.

Failure to complete any part will result in failing the course.

I will drop the 3 lowest quiz scores. All quizzes before the Drop Date are compulsory.

Because I will be out of town after the end of classes it will not be possible to take the final at any other time.  If you cannot take the final at the scheduled time you should drop this class.

**Requirements:** 301 / 311 (Grade B or better suggested), active calculus.

401 and 419 are useful, though not necessary.

**No laptops, ‘phones, Ipads, newspapers PLEASE**

**Preliminary reading:**

The Media and Advertising: a tale of two-sided markets: S. P. Anderson and J. J. Gabszewicz: http://economics.virginia.edu/sites/economics.virginia.edu/files/anderson/fullfinaltale.pdf

You can check out other ad related papers on this page too.

**Course Objectives:**

The course will consider the economic functions of advertising and the explanations that economists have proffered as to its mechanisms.

The first part of the course will look at advertising and the media, especially the economic performance of markets in which finance through advertising is important (commercial television, radio, magazines). It then considers information congestion.

The second part of the course will consider advertising at the industry level. We shall consider informative and signaling models of advertising, as well as persuasive ads.

The main emphasis of the course will be theoretical. The course uses simple (multi-variate) calculus. If you are not at ease with this, you are advised to take the course at a later date. Remember though that the Math is a tool to better convey the economics.

**Outline:**

This course covers an area that is not treated in dedicated Economics texts (although you will find some treatment in IO texts.) The course therefore relies on Notes and papers available on the Collab web-page. Further references will be given as needed. Some sub-topics are not covered by readings, and are covered only in the class itself.

On the back is a tentative course outline of topics that may be covered. The actual order may differ. It is strongly recommended that you read the text assignment BEFORE the lecture (plus any additional readings assigned in class).

KEY: Papers – my online downloadable papers page; Collab – the 439 site

1) Introduction (math diagnostic test)

2) Review of Surplus analysis, competition, and market power.

Readings: my CS and PS articles with Engers, Papers; your 301/311 text/ notes.

3) billboard competition. Reading: Billboards, Toolkit

4) Advertising and the media. Duplication and the Lowest Common Denominator.

Reading: Steiner, Beebe articles and Norway notes on Collab;

5) Spatial competition model, fixed prices.

Reading: Eaton and Lipsey, RES 1975, especially sections 1, 2 (“Eaton” on Collab)

6) Price and locations, application to advertising (“Hotelling” notes on Collab)

7) TV as a 2-sided market. Reading: Anderson-Gabszewicz article on Papers.

8) junk mail, spam, and telemarketing. Reading: Information Congestion on Papers

9) persuasive advertising. reading: Dixit and Norman (on Collab)

10) Informative advertising; the monopoly case. Class Notes.

11) informative advertising and oligopoly. (Butters and Grossman-Shapiro models). Reading: Tirole excerpt (Collab)

12) complementary goods: (Stigler-Becker and Murphy / Spence models). Reading: “SigComp” and Tirole excerpt on Collab

13) Advertising: the persuasion game reading: (Milgrom) Reading: “Unravel” on Collab

14) signaling models. Reading: Nelson, “SigComp”, Tirole excerpt on Collab

15) content analysis

16) Advertising Content. Reading: Anderson and Renault, “Advertising Content” on Papers

17) Comparative advertising: see Papers

18) student presentations

19) Further topics (Media Bias, Media Mergers, Search and Advertising, Gatekeepers …)

20) conclusions

**Selected References on Advertising:** most are online; others from JStor etc. (http://www.lib.virginia.edu/economics/) Some of these paper are not easily accessible to undergraduates. For such, notes are available online. Apologies in advance that notation is not always consistent across sources. In class, we’ll keep to the same notation throughout. Actual Assigned Readings on previous page.

Anderson, Simon P. and de Palma, Andre, “Product Diversity in Asymmetric Oligopoly: Is the Quality of Consumer Goods too Low?”, *The Journal of Industrial Economics*, Vol 49, No. 2. (June., 2001), pp 113-135.

Becker, Gary S. and Murphy, Kevin S., “A simple theory of advertising as good or bad”, *The Quarterly Journal of Economics*, Vol. 108, No. 4. (Nov., 1993), pp. 941-964.

Beebe, Jack, ”Institutional Structure and Program Choices in Television Markets”, *The Quarterly Journal of Economics*, Vol. 91, No. 1. (Feb., 1977), pp. 15-37.

Dixit, Avinash and Norman, Victor, “Advertising and welfare”, *The Bell Journal of Economics*, Vol. 9, No. 1. (Spring, 1978), pp. 1-17.

Dixit, Avinash and Norman, Victor. “Reply”, *The Bell Journal of Economics*, Vol. 10, No. 2. (Autumn, 1979), pp. 728-729.

Dixit, Avinash and Norman, Victor, “Another Reply”, *The Bell Journal of Economics*, Vol. 11, No. 2. (Autumn, 1980), pp. 753-754.

Eaton, B.C. and Lipsey, R., “The Principle of Minimum Differentiation Reconsidered”, *Review of Economic Studies*, Vol. 42, No. 1. (Jan., 1975), pp. 27-49.

Fisher, Franklin and McGowan, John, “Advertising and Welfare: Comment”, *The Bell Journal of Economics*, Vol. 10, No. 2. (Autumn, 1979), pp. 726-727.

Kihlstrom, Richard E. and Riordan, Michael H., ”Advertising as signal”, *The Journal of Political Economy*, Vol. 92, No. 3. (Jun., 1984), pp. 427-450.

Martin, Stephen, “Advertising, Concentration, and Profitability: the Simultaneity Problem”, *The Bell Journal of Economics*, Vol. 10, No. 2. (Autumn, 1979), pp. 639-647.

Milgrom, Paul and Roberts, John, “Price and advertising signals of product quality”, *The Journal of Political Economy*, Vol. 94, No. 4. (Aug., 1986), pp. 796-821.

Shapiro, Carl. “Advertising and Welfare: Comment”, *The Bell Journal of Economics*, Vol. 11, No. 2. (Autumn, 1980), pp. 749-752.

Steiner, Peter, “Program Patterns and Preferences and the Workability of Competition in Radio Broadcasting”, *The Quarterly Journal of Economics*, 66(2) (May, 1952), pp. 194-223.

### Class Honor Policy Statement

I trust every student in this course to fully comply with all of the provisions of the UVA honor system. That institution is one of the glories of Mr. Jefferson's University, and provides important benefits to the whole community. Each of us has an obligation to help maintain it.

On every exam, please write "Pledged", and sign your name. On every homework assignment you hand in, please write "Pledged". If you work with a Study Group, each member of your Study Group should sign beneath it.

In addition to pledging that you (or your Study Group) have neither received nor given aid while taking your exam or doing your homework, your signature also affirms that you have not accessed anyone else’s notes, study outlines, problem sets, old exams, answer keys, or the textbook while taking an exam, and that you have not obtained any answers from another student's exam.

Plagiarism is an Honor offense. The Honor Committee provides a very straightforward discussion, "Fraud and the Honor System", at: www.virginia.edu/honor/proc/fraud.html

If, in my judgment, it is beyond a reasonable doubt that a student has committed an honor violation with regard to a given exam, that student will receive an immediate grade of 'F' for that exam, regardless of any subsequent action taken by the Honor Committee.

Simon Anderson