

# PREFACE

Why yet another text on industrial organization (IO)? IO texts are not in short supply, and so the question is only fair and natural. Accordingly, this preface provides a convincing answer to this opening question.

Industrial organization has changed a great deal over the past two decades. Most importantly, it has evolved from a niche area in economics to an independent discipline that is studied by most economists and by students and scholars in areas such as finance, marketing, and strategy. This shift has resulted from two factors: (1) IO is the first economics discipline to incorporate the developments in game theory that took place during the late 1960s and 1970s, and (2) the analysis of imperfectly competitive markets (a possible definition of IO) is an inherently interesting and important task.

The evolution of the status of IO has not been reflected in the supply of new IO texts. Although the latter have increased in number, one cannot avoid the feeling that most texts have been written primarily for an audience of advanced undergraduate economics students; and in some cases for students who intend to pursue an academic career in economics. Why do I say this? First, because the *level* at which they are written is somewhat advanced for a student who does not have economics as a primary field of study. Second, many of these texts are *methodology* driven rather than *issue* driven: They introduce readers to a collection of models and econometric regressions as if to initiate them in the activity of research in IO—which is a natural bias, given that most authors are well-known IO researchers.

This text fills the perceived gap: Here, then, is a text that will appeal to a wide audience of readers, including economics students as well as students from other areas who are interested in economics as part of their education. Accordingly, the two main objectives of this book are the following:

1. The book is an *introduction*. This is naturally reflected by its length, between one third and one half of the size of most other texts. However, brevity is achieved not so much through superficiality in the treatment of each issue, but rather through greater selectivity in the list of topics addressed.<sup>a</sup>
2. The book is *issue* driven rather than *methodology* driven or *literature* driven. Although I make extensive use of models (because I think they are a useful way of understanding reality), I introduce a new model only when this is justified in terms of the marginal benefit in understanding an issue.<sup>b</sup>

Studying this book will not make the reader an expert in industrial organization; nor will it provide a complete or even representative view of two decades of research in the field. However, it *will* give an idea of the main issues involved in the analysis

<sup>a</sup> G. K. Chesterton once wrote a long letter to the editor of a newspaper. Asked why he wrote such a long letter, he allegedly answered, “Because I didn’t have the time to write a short one.” I consider its relatively short length as one of the accomplishments of this text.

<sup>b</sup> In particular, I should emphasize that the list of references in the book does *not* reflect a balanced survey of the IO literature. To stress this point, I have chosen not to make direct reference to sources in the text, leaving bibliographic references to notes at the end of the text. (These are the notes marked with numbers, as opposed to footnotes such as this one, which are marked with letters.)

of market competition, and in applying these ideas to the understanding of relevant problems reported in the *Wall Street Journal*, *Financial Times*, *Economist*, and related publications:<sup>c</sup> How should Nintendo react to Sony's cutting the price of its PlayStation? Was the Department of Justice right in suing Microsoft for bundling Windows with Internet Explorer? How will the proposed merger between British Airways and American Airlines impact on transatlantic airfares? Should the European Union allow the merger? And so forth.

This text is as up-to-date as possible. Although most of the developments in IO occurred during the 1980s, it is surprising how many are still not included in textbooks. Although their original treatment is rather technical, the basic ideas are sufficiently important to warrant a simplified textbook treatment. Examples include the analysis of price competition with capacity constraints, dynamic models of collusive behavior, competitive selection, endogenous entry costs, and vertical restraints.

The text strikes a balance in terms of the relative weight of ideas and examples and of the relative weight of U.S. and non-U.S. examples (the latter mostly European). Some of the examples are presented in separate boxes, of which there are more than thirty in the book; most are introduced in the main text.

Readers should be familiar with basic economics, at the level of Economics 1. Those less familiar with the background concepts necessary for IO can start with chapter 2, a primer in microeconomics that covers the necessary concepts for the purpose of this book. The basic text consists mostly of graphical analysis. This is complemented by a series of supplemental materials (posted on the web) that make more extensive use of algebra and calculus. In this way, the book is sufficiently flexible to accommodate readers of different technical backgrounds. Although the basic text is self-contained without the mathematical sections, readers familiar with algebra and differential calculus will find the supplemental sections helpful.

The exercises at the end of each chapter are divided into "Revision and Practice" exercises and "Extension" exercises. The titles are self-explanatory. Extension exercises typically consider generalizations of results presented in the main text. Exercises are classified from (no asterisk) to \*\*\*, according to level of difficulty.

The book's website may be accessed at the following address:

<http://luiscabral.org>

<sup>c</sup>The number of citations to newspaper articles in this book is approximately equal to the number of citations to scholarly articles.

At this site, readers will find advanced mathematical sections, additional examples and case studies, solutions to exercises, and other materials of interest. The site also includes sections especially designed to help instructors.