



Economics Undergraduate Board  
UNIVERSITY OF WASHINGTON

# THE ECONOMIZER

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DEPARTMENT OF ECONOMICS

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## Illegal Music Downloading: Is the RIAA Justified?

By Alex Feng

According to a recent study by the Institute for Policy Innovation, the U.S. economy loses 12.5 billion in total output annually; 71,060 in lost jobs, and 2.7 billion in lost earnings from the music industry. These are astounding numbers, but it is difficult to know what forces actually affect the loss of revenue. The general concept is that a consumer can obtain a song or an album illegally and therefore would substitute the downloaded copies for legal ones, displacing sales. In other words, a person would be less likely to buy a song if they could download it for free. However, other arguments state that the increased distribution of music as a result of illegal downloading actually expands its influence by making more people aware of the music, therefore increasing general welfare and possibly influencing more sales. In today's world, when students on university campuses around the nation are sent letters from the Recording Industry Association of America (RIAA) and fines for their downloading activities, it is necessary to determine the actual extent of the loss of revenue from downloading so as to better design a method of mitigating the problem.

The technology of illegal downloading has expanded in recent years and the reality is not as it was in the early 2000s. Although the compact disc is still the most popular way of selling music, online legal ways of downloading are becoming increasingly available. With the expansion of the use of iTunes and other methods of legal downloading, consumers can choose between using the legal or illegal methods, an option they did not have in the past. Variables such as the loss of quality in the music after copying and high costs of duplication do not exist today; now, a copy of a copy of a song retained the same quality of sound as the original, and also costs very little to duplicate. With today's technology, the cost to download a song is almost zero, thanks to the widespread use of broadband internet.

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## Is It Better to Give Than to Receive?

By ZiLai Li

From THINKING STRATEGICALLY by Avinash K. Dixit and Barry J. Nalebuff

Question: A hotel's management and labor are negotiating over how to divide the season's profits. Suppose that only management gets to make offers, and labor can only accept or reject.

The season lasts 101 days. Each day the hotel operates, it makes a profit of \$1,000 and negotiations start at the beginning of the season. Each day, the management presents its offer, which is either accepted or rejected by labor. If accepted, the hotel opens and begins making money. If rejected, the negotiations continue until either an offer is accepted or the season ends and the entire profits are lost. If both labor and management's only concern is to maximize its own payoff, what do you expect will happen (and when)?

Answer: In this case we expect the outcome to differ radically from 50:50. Because management has the sole power to propose, it is in the much stronger bargaining position. Management should be able to get close to the entire amount and reach agreement on the first day.

Let's use backward induction. On the last day there is no value in continuing, so labor should be willing to accept any positive amount, say \$1.00. On the penultimate day, labor recognizes that rejecting today's offer will bring only \$1.00 tomorrow; hence they prefer to accept \$2.00 today. The argument continues right up to the first day. Management proposes to give labor \$101, and labor, seeing no better alternative in the future, accepts.

This story clearly exaggerates management's true bargaining power. The above example's radically unequal divi-

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# Key Findings from Annual Undergraduate Survey

By Mary LaBissoniere

The Economics Undergraduate Board was created in 1989 by a group of economics majors who, with full support from the Department, committed themselves to acting as an intermediary between students, faculty/staff and alumni with the simple aim of improving the educational experience of undergraduates studying economics. Over the years, the EUB has assumed more responsibilities and has grown in strength. Some of these responsibilities include producing this quarterly newsletter, maintaining the EUB Web Site, and hosting educational seminars on a diverse set of topics. We also tutor on a regular basis and act as the voice for students in the economics field. We emphasize teamwork and we aim to bridge any gaps between the economic department and the undergraduate economics population.

In our endeavors to improve the academic experience for undergraduate students, the EUB conducts a survey every year from our current students. Some useful and entertaining facts from this survey are summarized below.

## Departmental Statistics

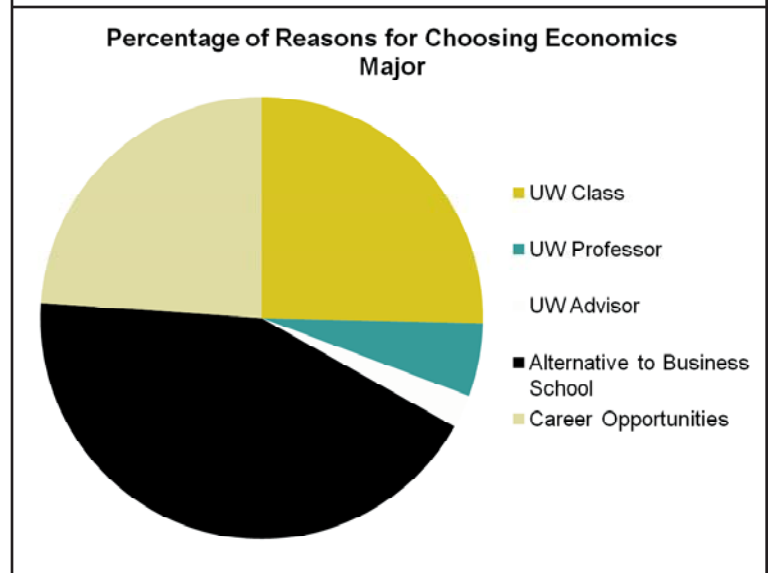
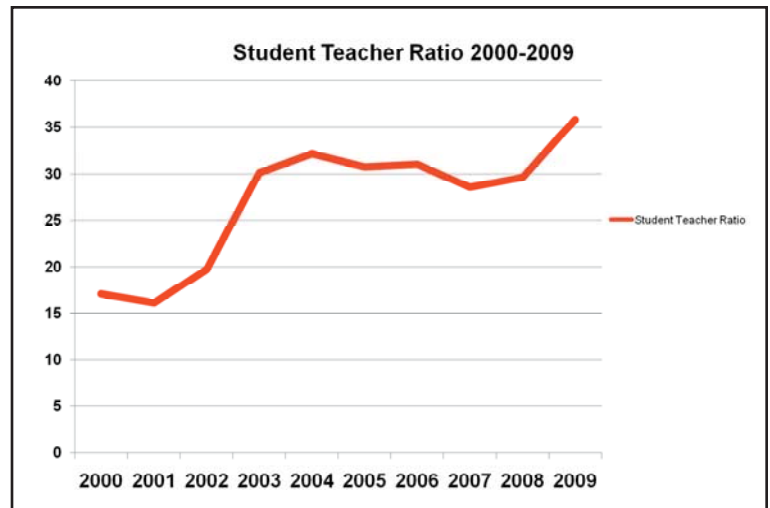
- 967 Undergraduate Majors
- Increase in more than 20% majors per quarter over the last three quarters
- 60% of students work

## Department Growth

- 27 Faculty Members
- Most recommended courses were Econ 471 and Econ 472
- 43% of students will earn a certificate with their undergraduate degree
- A majority of students plan to pursue further education after graduation from the econ department

## Academic Interests

- Most influential professor was Greg Ellis, followed by Theo Eicher
- 33% of students interested in finance and international economics courses



## Congratulations to our New EUB Members!

The application process this quarter was especially competitive and we are welcoming eight new members to our board for Fall 2009:

- Cheng-Yu Chan
- Colin Fendrick
- Xinue Kang
- Karina Kats
- Kurt Ladwig
- James McQueen
- Icing Song
- Jeremy Supinski
- Jason Yu

## Illegal Downloading...

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According to a recent econometric study on downloading and buying patterns as well as related characteristics that might affect people's decisions, there is a negative relationship between downloading illegally and buying music: for every three songs a person downloads, they purchase one less song that they would have otherwise obtained legally. In particular, males seem to purchase fewer songs than females. The sample was based upon university students that seem to have overwhelming access to high speed internet and mp3 players. Although there are numerous methods of curtailing losses, there will always exist ways to circumvent protection.

## Give or Receive...

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sion is not possible. But that doesn't mean we must return to an even split. Management still has all the bargaining power. Its goal should be to find the minimally acceptable amount to give to labor so that labor prefers getting that amount over nothing, even though management may get more.

Splitting the difference or even division is a common but not universal solution to such a bargaining problem. Looking forward and reasoning backwards provides an explanation for why we might expect to find unequal division. In particular, it suggests that in the case of making offers, "It is better to give than to receive."

## Thinking About Writing a Senior Thesis? Go For It!

*By Maggie Haight*

Writing a senior thesis was long, hard, and frustrating; most of the time I wanted to give up and die. However, I finally turned it in last Monday and despite all the whining and complaining, it was easily the most valuable experience of my college career. The process allowed me to synthesize something that drew from everything I had learned during my four years. I worked closely with a professor (shout out to Charles Nelson, a GREAT advisor), gained insight on time management (leaving things to the last minute is not a good idea), and got to explore a topic that I am passionate about (investing in art). Here is a summary of my thesis "The Damien Hirst Business Plan: The rate of return to outsourcing labor and creating a brand in the art market."

Damien Hirst, prominent British modern artist, does not actually make a significant body of his own work. Commenting on his famous series of spot paintings (Figure 1), Hirst describes his personal efforts as "shite." He only painted five of these before outsourcing the work to assistants because "[he] couldn't be f\*\*\*ing arsed to do it." In addition to outsourcing, according to my research, approximately half of Hirst's total body of work for sale at auction is created in three series of nearly identical works. The three repeated series of works are: "Spots," "Spins," and "Butterflies." The pieces within the series vary slightly by size and color, but are distinctly recognizable and artistically unoriginal. In contrast, the rest of Hirst's work follows some over-arching themes, but the individual pieces are for the most part unique, and Hirst seems to play a large part in their creation.

When pieces of art sell for millions of dollars at auction, we assume the buyer is spending the money because: they like the specific image, an illustrious artist created it, and they want to be the sole possessor of an original piece. Do buyers recognize these differences in production and subsequently value the two groups of art differently? This paper examines two groups of Damien Hirst's art work- "repeated" pieces and "unique" pieces- to determine which type of art appreciates more in value over time. Do unique, Hirst-created works appreciate more because they are one-of-a-kind, or does Hirst's established brand support the prices of the pieces in the repeated series?

I find that the laws of supply and demand hold true in the market for Hirst's work. Scarcer, unique works exhibit higher rates of return compared to the repeated series works. However, the fact that Hirst's repeated series works still increase in price despite the increase in supply suggests that there is also value to an artist producing enough similar work that the style of work itself becomes recognized as iconic of the artist; in other words, a brand. In addition, both groups outperform the S&P 500, but have comparable returns to the Case-Schiller Home Price Index during the time period.

# Investing in a College Education

By Mary LaBissoniere

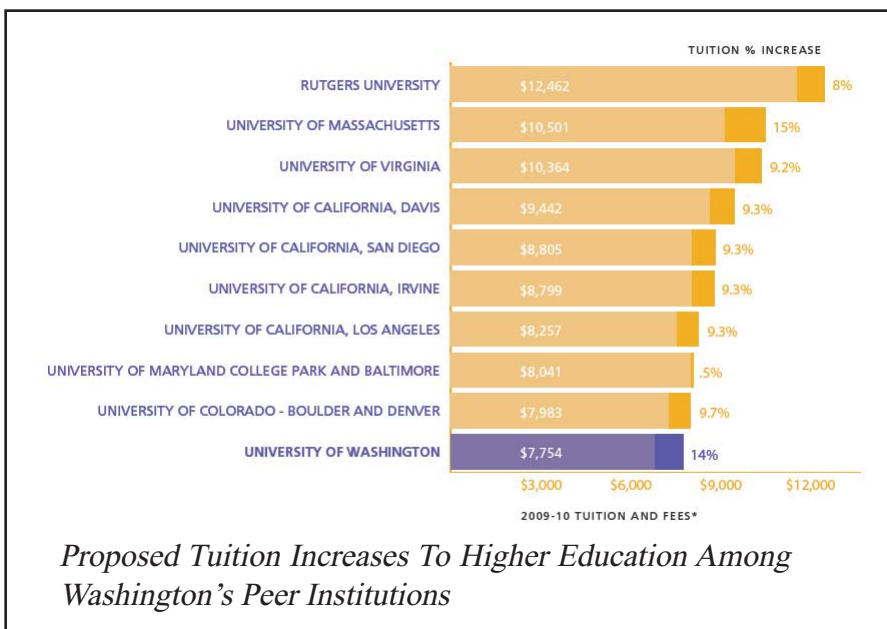
Twittering of birds and sunny day recreations have been overtaken this spring by the drone of students reacting to upcoming tuition increases.

Recent state funding cuts will affect six four-year public universities in the state of Washington, with the highest cuts from the University of Washington. Though the UW will respond to the cuts by decreasing expenditures, a large portion of the cuts will be compensated for by increases in tuition. In response to the budget cuts, the UW Regents will be allowed to raise the cap on tuition increases from 7% per year to 14% annually. This proposed increase mean that tuition for in-state undergraduates alone will rise \$1875 over the next two years.

A comparison to peer universities with tuition increases reveals that the UW will experience near the highest distress. However, at the same time, UW students currently pay on average 16% less than these universities. A similar comparison can be seen across many other peer institutions such as the UCLA, University of Wisconsin, and University of Minnesota, all of which have higher tuition rates than the University of Washington.

Though the tuition increase poses an immediate concern to undergrads, students still see their university degree as an investment with a lofty return. The average university graduate working full time earns an annual salary of \$73,203. At this average, current second year students expecting to graduate in four years would see a 740% return on every dollar invested on their education. While making an average of 168% more on average every year, graduates will earn a present value of \$218,500 more than those without a degree.

Tuition increases are still a concern to students, partyl due to recent the recent financial crisis and subsequent economic downturn, but when considered as an investment from a future economist's point of view, the college



## Congratulations and best of luck to all our graduates!

**2009 Economics Department  
Graduation Celebration  
June 11, 2009  
HUB Ballroom  
4:00pm**

The Economizer is a quarterly newsletter published in the Department of Economics by the EUB. The articles herein do not necessarily reflect the views of the department or its faculty.

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Questions, Comments, Concerns?

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