Innovative Interaction in Mixed Market

Shinjiro Miyazawa
Graduate School of Economics, The University of Tokyo
e-mail: ee47029@mail.ecc.u-tokyo.ac.jp

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We investigate the effects of agency problem (hidden action problem) in public firm in mixed duopoly market. It has an effect to reduce the investment level of the public firm and to increase that of the private firm competing with the public firm (substitution effect). It, as a result, improves the expected social welfare when the distortion derived from it is positive but less than certain degree. The reservation-utility level of the public firm’s manager affects the degree of distortion. There exists certain range of reservation-utility level for which the agency problem improves the expected social welfare. We apply the model to investigate optimal bureaucrat system. Setting guaranteed utility level or minimum wage level plays a role of commitment device. The optimal level of both the guaranteed utility and the minimum wage is positive in some cases.

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