## Non-Integration, Integration, and the Decentralized Firm: Management of "Externalities vs. Private Benefits" \*

Yutaka Suzuki

Faculty of Economics, Hosei University 4342 Aihara, Machida-City, Tokyo 194-0298 Japan

E-mail: yutaka@mt.tama.hosei.ac.jp

## First Version: January 2003 Revised: June 20, 2006

## Abstract

We present a comparative theory of "Non-Integrated", "Integrated", and "Decentralized" firms, and study the optimal scope of a firm and the assignment of different types of managers to different types of firms, in an IO setting with R&D and production activities. "Non-integrated firms" fail to take into account the externalities that managers' decisions have on other firms. While an "integrated firm" internalizes these externalities, it does not take into consideration the "private benefits" of managers. The "Decentralized Firm" works as a hybrid of these two structures. We also interpret our model from the viewpoint of the allocation of formal authority, and uncover some interesting economic implications.

*Key words* Non-Integration, Integration, Decentralized Firm, Private Benefit, Internalization of Externalities.

JEL classification D23, L22

Running heads Decentralized Firm

<sup>•</sup> This paper was begun when the author was a visiting scholar at Harvard University from April 2002 to March 2003. He is grateful to the university for its stimulating environment and the hospitality. He also thanks the seminar participants at Hosei University, Kyoto University, and *Econometric society* Far Eastern Meeting, Beijing, 2006 for their valuable comments. Financial support for this research was provided through Grant-in-Aid for Scientific Research by Japan Society for the Promotion of Science (No. 17530192).