Jean Tirole: «The Nobel Prize Was a Tipping Point»
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Economics Nobel Prize winner Jean Tirole reveals in an exclusive interview with finews.first how the prize changed his life, monopolies can be tamed and how regulation should strike a balance between inefficient laissez-faire and intrusive measures.

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Jean Tirole, when did you realize that you could possibly win the «Economics Nobel Prize» in 2014?

When I received the call from the Swedish Royal Academy 45 minutes before the official announcement. There are lots of rumors in the profession, but none stemming from the Academy itself and so those rumors are highly unreliable.

What has changed for you since then?

It has brought me a sense of responsibility for communicating about my field. Before the «Nobel», I spoke to economists and experts in ministries, regulatory authorities, companies. The «Nobel» was a tipping point.

Why?

I met quite a number of people, sometimes just unknown people in the street, who simultaneously demonstrated a real interest in and many questions about what economists do, whether they are useful, whether economics is a science, whether the key challenges we face can be solved. They made me aware of my responsibility to step out of my laboratory to explain my job, and share more of my knowledge; without being a news commentator. But by simply talking about what economic research has to say about our world.

I otherwise have tried to keep the same life as before, and I spend as much time as I can on research and teaching.
The research cited by the Nobel Committee is about taming monopolies. What, roughly speaking, is your core thesis?

Firms with substantial market power – the ability to raise price substantially over cost and to offer poor quality without losing too many customers – are a big challenge for the economy. For one thing, people have less purchasing power and consume less.

«Promoting competition is not plain sailing»

But competition is not only reflected in lower prices. It encourages businesses to produce more efficiently and to innovate. It promotes a diversity of approaches and experiments, giving rise to new technologies and business models, as we now see online.
Finally, monopolies usually generate little innovation. By innovating they would cannibalize their existing activities. What they gain on new products they lose in part through lower sales of existing products. And they really don’t need to innovate anyway because their executives face no criticism for being less dynamic than a competitor.

**What is your conclusion?**

For all that, promoting competition is not plain sailing. Incumbents want to block new competitors or claim financial compensation from the government if they lose their exclusive access to a particular market. And the state may give in to their demands: it may want to grant favors to the lobbies seeking protection against competition, or it may resent competition as a restraint on its political action and power.

«The role of economics is to help make this world a better place»

The victims of this lack of competition are the consumers who have less purchasing power as a result. They are poorly organized and ignorant of the impact of the public decisions that they either do not follow or do not understand. This is why competition authorities – in charge of preventing illicit monopolization and abuse of dominant positions – and sectoral regulators (telecoms, electricity, railroads) are in general independant rather than subservient to the political powers.

**Do you believe that your research has a real benefit for the consumers?**

Bad economics and bad regulations can make economies completely dysfunctional, as is illustrated by the widespread failure of planned economies in terms of living standards (which triggered other failures in terms of the environment, civil liberties, culture etc). In a modern economy both market failures and state failures are common, and social scientists must design regulations that account for both. The role of economics is to help make this world a better place.

**What influence does the Internet and the online trade have on your research and on pricing?**

This is a topic that has attracted the interest of researchers at the Toulouse School of
Economics and elsewhere for a long time. We recently had our 10th international conference on the economics of the internet and software industry. Not only because the five largest companies (Amazon, Alphabet, Apple, Facebook, Microsoft) in the world in market capitalization are two-sided internet and software platforms, but also because many competition policy and societal challenges emerge, that economists and more generally social scientists must address.

_Your research is very mathematical. Is this not detrimental if one takes into account that the financial crisis ten years ago might have just broken out due to an all too mathematical orientation in developing financial products?_

I would answer this in two parts: first, the issue with financial products that were designed by mathematically-oriented financial experts is that they were put to the wrong use, and that there was a state failure: the necessary regulation was not put into place. This is a general problem: any innovation, if wrongly used, can have detrimental effects. One can single out the inventor, but one should perhaps look at who allowed the invention to be put to the wrong use!

«Modeling forces researchers to verify the logic of their reasoning»

Second, one must understand why economists use mathematics. Modeling forces researchers to state their assumptions clearly, and to verify the logic of their reasoning, as Harvard economist Dani Rodrik once said: «we use math not because we’re smart, but because we aren’t smart enough. We are just smart enough to recognize that we are not smart enough».

_Could there have been an «ideal regulation» that could have prevented the financial crisis ten years ago?_
As long as the current reforms are implemented and not derailed, the financial system will in my opinion prove to be less risky than it was before: the Basel III reforms, for example, seem to be headed in the right direction. An increased requirement of equity capital, the introduction of a minimum liquidity ratio, the inception of macroprudential measures in the form of countercyclical equity capital buffers, a greater use of centralized exchanges instead of over-the-counter markets, institutional reforms all are genuine improvements.

That said, one cannot predict that there will be no future crisis. First, there are still major risk concerns. Second, and as I explain in the book, economists will always be more comfortable identifying the factors likely to lead to a crisis than predicting whether it will occur, or on what date. Just as a physician will be more comfortable identifying factors that might cause an illness or a heart attack than in saying exactly when they will occur.

Does the financial sector have a special weight in your research?

Yes I have always believed that the financial sector is key to a number of economic issues.
Accordingly I have been working in this area for a long time: I worked on asset bubbles in my PhD thesis and shortly thereafter. Mathias Dewatripont and I published a book on banking regulation in 1994, when few economists were interested in this arcane topic.

Bengt Holmström and I also showed in the 90s how shortages of liquidity naturally arise in an economy and analyzed the role of the state in supplementing liquidity. Jean-Charles Rochet and I studied contagion effects and thought about the centralization of transactions in exchanges. The financial sector has become more mainstream in the 2000s and especially since the 2008 crisis. Like many colleagues, I keep working on banking and Sovereign crises.

*Doesn’t your conviction policy stance run the risk of affecting the functioning of the free market economy by too many state regulations?*

Economic regulation must strike a balance between inefficient laissez-faire and intrusive regulation that would hamper incentives, competitiveness and innovation. This is why I emphasize the need for taking into account the informational handicap faced by the state in many areas of economic regulation.

«Many of our key regulations have a microeconomic flavor»

As I show in my research, asymmetries of information have deep consequences for how one should design environmental regulation, labor market policies, innovation policies and many other regulations. Government hubris is dangerous as it may lead to the wrong policies.

*What gave you the impetus to devote yourself to the topic of «industrial economics»?*

Many of our key regulations have a microeconomic flavor. Industrial organization focuses on competition policy and the regulation of network industries (telecoms, electricity, railroads, postal services), but, to cite some other areas in which I have been working, banking, labor market and environment regulations are primarily microeconomic, even though they also have macroeconomic dimensions.

*What are your research activities today?*

With co-authors, as research is so often teamwork, I am working on a range of topics. Industrial
organizational course; banking, including how shadow banking poses new challenges and alters our regulatory and macroeconomic environment.

- Jean Tirole is the Keynote Speaker at the 12th Annual Meeting of the Swiss Finance Institute on the 4th of October 2017 in Zurich.

Jean Tirole is laureate of numerous international distinctions, including the 2014 Sveriges Riksbank prize in economic sciences in memory of Alfred Nobel and the 2007 CNRS gold medal. He is chairman of the Jean-Jacques Laffont - Toulouse School of Economics Foundation and scientific director of the Institute for Industrial Economics. He is also affiliated with MIT, where he holds a visiting position, the Ecole des Hautes Etudes en Sciences Sociales, the Institut de France and the Institute for Advanced Study in Toulouse, which he co-founded in 2011. He has published over two hundred articles in international reviews, as well as twelve scientific books. Published in French in 2016, his latest book entitled «Economics for the Common Good», accessible to a wide audience is under translation into a number of other languages.