

## ANDREI SHLEIFER

### JOHN BATES CLARK MEDALIST

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Andrei Shleifer is a superb economist, working in the old Chicago tradition of building simple models, emphasizing basic economic mechanisms, and carefully looking at the evidence. He has made major contributions to corporate finance (corporate governance), the economics of financial markets (deviations from efficient markets), and the economics of transition. In each case, his contributions have shaped the basic paradigm and triggered considerable follow-up research.

*Corporate Governance.*—Andrei’s research on corporate finance has been organized around the following question: Once managers have received funds from shareholders, debt-holders, or others, what prevents them from misbehaving?

His contribution has come from the steady accumulation of theoretical and empirical papers that look at the role of large shareholders, boards of directors, takeovers, and so on. His main findings, and the general lessons to be drawn are presented in “Corporate Governance” (*Journal of Finance*, 1997), written with Robert Vishny—a coauthor of many of Andrei’s papers, and whose work is also recognized by this award.

Recently, Andrei has turned to the role of laws in shaping the structure of corporate finance and governance. By constructing measures of investor protection for a large number of countries, he has shown how differences in protection lead to different financial structures. He has demonstrated, for example, how poorer shareholder protection leads to higher concentration of shares, and how better investor protection leads to larger and broader debt and equity markets.

*Financial Markets.*—In his work on financial markets, Andrei has challenged the efficient-markets hypothesis. His contributions, which are summarized in his Clarendon Lectures (Oxford University Press, 1999), can be divided into two groups.

The first group is the documentation of apparent “anomalies” in financial markets. Andrei has argued that most can be put into one of two categories. The first is “underreaction” to news at high frequency. Bond and stock markets appear not to respond to publicly available news instantaneously, but rather take some time to adjust. The second is “overreaction” to sequences of news of the same sign. A sequence of positive news about a company tends to lead to overvaluation for some time.

The second group is the interpretation of these facts through models based on the presence of both noise traders and limited arbitrage. In 1996, for example, he argued that, because of principal-agent problems faced by fund managers, they would be unable to arbitrage precisely at those times when prices were furthest away from fundamentals. In those times, arbitrage would be destabilizing. This paper turned out to be prescient, anticipating the Long Term Capital Management crisis by a full two years.

*Transition.*—Andrei has been a major contributor to the economics of transition. He is one of the architects of privatization in Russia. Not only did he help design the program, but he was directly involved in its implementation.

In most transition countries, initial privatization schemes were not implemented. The reason was that the firms were not for the state to dispose of as it wanted. There were many stakeholders, from managers and workers to local authorities and ministries. Any of them could block privatization and, in most cases, indeed did.

With this in mind, Andrei’s approach was to identify initial stakeholders and constraints, and then to find the best feasible privatization scheme. The result was Russian privatization, where firms were effectively sold at a large discount to insiders, on the assumption that they would have the proper incentive to resell later if this was value-maximizing. The logic of the design is described in *Privatizing Russia* (MIT Press, 1995, with Maxim Boycko and Robert Vishny). Whether privatization is one of the successes or failures of transition in Russia remains controversial. But the general approach, based on a clear identification of the various stakeholders to generate a politically feasible solution, is an important contribution.

Be it on governance, finance, or transition, Andrei Shleifer’s work has been important, controversial, and influential. He very much deserves the John Bates Clark Medal.