Framework 1: “Market” “Failures”

Besides Markets: Governance of Value Creation

Organize the Right Problems

Different transactions require different safeguards.

Organize the Right Problems

Different transactions require different safeguards — under different governance structures.
Organize the Right Problems

If contracts were perfect, why would we need bosses? (~Coase, 1937)
Sometimes fiat is more efficient than haggling. (~Williamson, 1971)

Raising central Q
Not giving answer (for “salt” or “idea”)
Not yet building tools for answering

Lessons
1. If a contract will handle your problem well, why use a boss?
2. If a contract would do poorly, you face a hard problem, so a boss might do better but still not be perfect.
3. If the organizations you observe seem less efficient than the markets you observe, consider that they may be handling different problems

Organize the Right Problems

If contracts were perfect, why would we need bosses? (~Coase, 1937)
Sometimes fiat is more efficient than haggling. (~Williamson, 1971)

Bones not immune to problems that wreck contracts.
Visible Hands:

*Governance of Value Creation*

in Firms and Beyond


Invisible Hand?

As every individual, therefore, endeavours as much as he can both to employ his capital in the support of domestic industry, and so to direct that industry that its produce may be of the greatest value, every individual necessarily labours to render the annual revenue of the society as great as he can. He generally, indeed, neither intends to promote the public interest, nor knows how much he is promoting it. By preferring the support of domestic to that of foreign industry, he intends only his own gain, and he is in this sense, as in many other cases, led by an invisible hand to promote an end which was no part of his intention. Nor is it always the worse for the society that it is not part of it. By pursuing his own interest he frequently promotes that of the society more effectually than when he really intends to promote it.

*The Wealth of Nations, Book IV, Chapter II, paragraph 1798*

- Prisoners’ Dilemma?
- Boundary conditions?

Which Interactions Are “Governed”?**

Economics inside firms?
Visible hands outside firms?

Gibbons AER P&A 2020

Effectiveness 100%

Integrated (ILLUSTRATION)

Non-Integrated

Collaboration difficulty

Collaboration

Integrated

Transactions via bosses

Transactions within firms

Transactions are priced

Market (neoclassical)

R. Gibbons, Feb. 2021
Which Interactions Are “Governed”?

“substantially the same factors that are ultimately responsible for ‘market’ ‘failures’ also explain failures of internal organization.” (Williamson, 1975)

R. Gibbons, Feb. 2021