

BIOPHARMACEUTICALS HIT THE SWEET SPOT

States and localities are all angling for a piece of the action in what has come to be known as biopharmaceuticals. And no wonder: According to new estimates from the Milken Institute, the industry will add some 129,000 jobs and nearly \$60 billion in real output annually to the U.S. economy over the next decade. The report, *Biopharmaceutical Industry Contributions to State and U.S. Economies*, is available online at www.milkeninstitute.org.

ARKANSAS GOES FOR THE GOLD

In its latest state assessment, the Institute's Regional Economics group focused on Arkansas – and, in particular, what it would take to make the Mockingbird State a winner in the fiercely competitive global economy. The group's conclusion: First and foremost, Arkansas must sharply improve the skill level of its workforce.

The study, prepared in conjunction with the University of Arkansas's Center for Business and Economic Research, was commissioned by Accelerate Arkansas, a non-profit business development group. Arkansas' Position in the Knowledge-based Economy: Prospects and Policy Options is available online at www.milkeninstitute.org.

LET'S GO TO THE TAPE

Attendees of the Milken Institute's 7th annual Global Conference last April got to

choose among nearly four dozen panels. And there lay the rub: it wasn't possible to experience more than a handful of the total.

But now even those who were foolish enough to skip the event altogether can watch every single session, as often as they like. The complete recordings on DVD are now available for \$595; recordings of individual panels can be had for \$25. Order online at www.milkeninstitute.org.

What's more, thanks to the generosity of our sponsor, BNP Paribas, qualifying non-profit organizations can purchase a complete set for \$195.

Contact Skip Rimer, director of communications (srimer@milkeninstitute.org) to see if you are eligible for the big discount.

EVERYTHING YOU ALWAYS WANTED TO KNOW ABOUT LEVERAGED LOANS

Leveraged loans constitute one of the fastest growing and most innovative sectors of the U.S. capital market. Care to learn more? You've come to the right place. *The U.S. Leveraged Loan Market: A Primer*, written by the Institute's Capital Studies group, is available online at www.milkeninstitute.org.

HATS OFF TO GLENN YAGO

Yago, the Institute's director of capital studies, has been named a senior fellow by the Koret Foundation, a San Francisco-based charitable trust. He will supervise seven Koret fellows doing research on market-linked reforms for the Israeli economy.

The economist on the spine of the last four issues is Ronald Coase, a stunningly original thinker whose two big ideas are as simple as they are profound. Actually, the British-born Coase who has long taught at the University of Chicago, was trained as a lawyer, not as an economist. But don't remind the Bank of Sweden, which awarded him a Nobel Prize in 1991.

Back to those big ideas. In 1937, Coase wrote "The Nature of the Firm," which likened the corporation to a centrally planned economy, with all the attendant problems of distorted incentives. Why, then, do firms exist if all the people's republics have col-

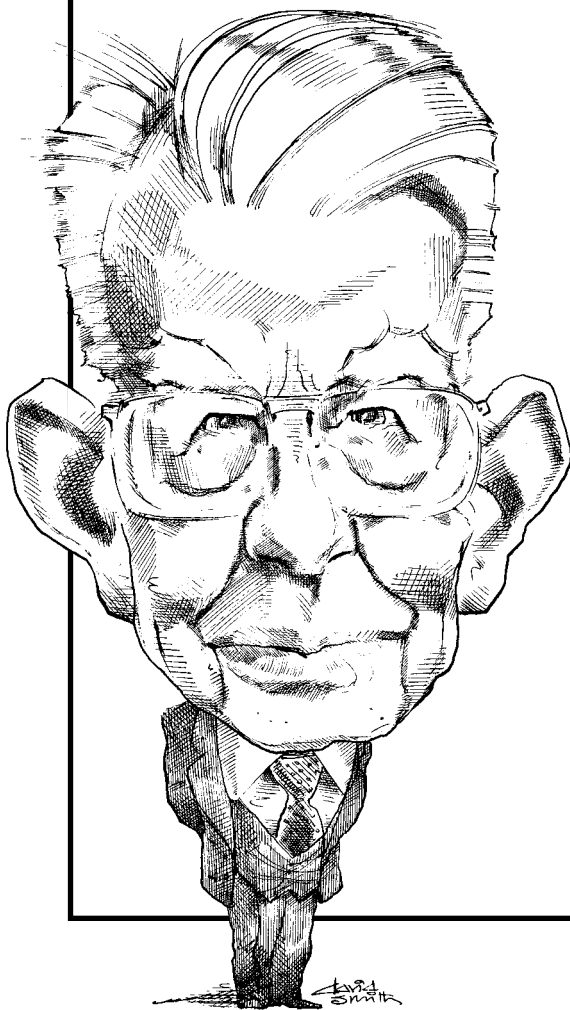
lapsed under their own weight? Because creating value through markets can generate enormous transaction costs.

Example: Pizzerias must labor under the burden of indolent employees, ineffective advertising media, etc. But they thrive because the other way of obtaining pizza – buying the ingredients at the supermarket, learning to make crust, and the like – is even less efficient. Thus, the tension between the inefficiencies of central planning and the high transaction costs of creating value through disaggregated markets defines the natural boundaries of the firm.

Coase's second big idea is found in "The Problem of Social Cost" (1960). Here, he argued that one classic source of market failure – the existence of external costs and benefits to an activity – does not necessarily imply the need for government intervention.

Example: A farmer's cows pollute a brook, making the water unfit for drinking downstream. If the value of pure water downstream exceeds the cost of keeping the farmer's cows away from the brook, it would pay for the other users to bribe the farmer to keep the brook clean. On the other hand, if the value isn't sufficient to justify the bribe, thirsty downstream consumers may feel aggrieved, but the market hasn't failed to allocate resources to their best use.

The market failure associated with externalities, Coase argued, is the high cost of the negotiation that prevents efficient allocation. It still may make sense to make it illegal to pollute the brook because folks downstream can't effectively organize to bribe the farmer. M



DAVID SMITH