Nobel for 'economic shock' study

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London: The Nobel Memorial Prize in Economic Sciences was awarded on Monday to Robert E. Hall and Michael Woodford, two American professors, for research that has helped guide policies aimed at reducing economic volatility.

Who are the winners?

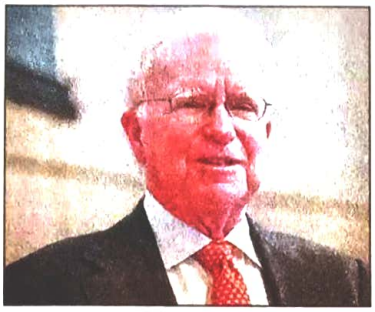
Hall is a professor at Stanford University and Woodford is a professor of political economy at Columbia University. They were awarded the prize "for microeconomic foundations of macroeconomic stabilisation", the awarding committee said.

Hall studied consumer demand and spending to develop his models, while Woodford studied the supply side of the economy, looking at the price-setting behaviour of companies. Their research has helped shape a framework for politicians, central banks and others to implement timely economic policies during upturns and downturns.

They will receive 12 million Swedish kronor, about $1.2 million, split equally between them.

Why did the committee say they received the prize?

The Royal Swedish Academy of Sciences said their work helped to inform fiscal and monetary policy measures, by governments and central banks, that reduced volatility in economies, so that there were milder peaks and troughs.



Robert E Hall. (Reuters)



Michael Woodford. (Reuters)

Because of their research, "we are better equipped to deal with shocks in the economy, such as energy crises or sudden changes in how much households consume", said John Hassler, chair of the Committee for the Prize in Economic Sciences.

Hall and Woodford have revitalised so-called stabilisation policy, which was pioneered by John Maynard Keynes, the early 20th-century British economist. This year's prize winners developed models using microeconomic foundations, a bottom-up approach that considers how the decisions of individual households and businesses affect the economy as a whole.

By doing this, they showed the importance of how real-world behaviour impacts policy and why it must be taken into account alongside broad economic variables like inflation and production. A critical aspect of their models rests on the idea that households and businesses make decisions based on what they believe will happen in the future. So when governments and policymakers communicate their economic plans, they can influence people's expectations. That in itself can help steer the economy.

What did the laureates say about winning the prize?

Woodford said on the phone at the news conference announcing the award that he was elated. "It's a tremendous honour," he said. "It's a surprise but I feel very good about it."

He said his work was intended to "improve the foundations for discussion of economic policy", contributing to the management of the economy as well as the public's understanding of the economy. He added that one of the main themes of his work was helping policymakers to appreciate that it was important to understand the behaviour of individuals in the market: How they make decisions about spending and what they understand about future economic policy.

"One of the key goals of trying to develop an analytical framework was not simply to use it on people," he said. "But to also talk to people about why the things that are being done are being done."

Consider the immediate aftermath of the 2008 financial crisis, when central banks were scrambling to deal with an economic downturn. Policymakers quickly lowered interest rates but it was not enough. Additional tools were developed, such as so-called forward guidance, in which central bankers made explicit statements about the likely future path of interest rates, Woodford said. "That was an important part of the policy response in the years in the years from 2009 onward, and I think it did contribute to better stabilization," he added.

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