

Superstar firms

In the early 1980s, Sherwin Rosen, an economist at the University of Chicago, published a famous article entitled «The Economics of Superstars». In it, he explored the reasons why, increasingly, a handful of people in the world of art or sport, for instance, were able to earn astronomical sums and command a significant portion of all the income in their profession. Why was the income of Pavarotti – an exceptional tenor – hundreds of times higher than that of a good opera singer?

Part of the response was relatively intuitive: great talents offer something unique, a differentiated product that has no perfect substitutes and that we are willing to pay a substantial premium for. However, in addition, there is an even more important reason associated with technology: in the superstar economy, production costs barely grow with the size of the market – for Pavarotti, the effort involved in singing in front of 1,000 or 100,000 people was the same, while the cost to play his music on a hi-fi, and therefore to reach an audience of millions, was close to zero. Rosen ended his article with a foreboding question: «What changes in the future will be wrought by cable, video cassettes, and home computers?» As we have seen, the changes have been profound.

At present, in addition to continuing to have superstar talents at the individual level, globalisation and digitisation have facilitated the formation of superstar firms. These are global corporations that have taken advantage of the fall of trade barriers between countries, the liberalisation of sectors and the dismantling of old public monopolies, or that are leading the era of digital transformation with new business models. Digital platforms like Amazon and Google are prime examples of such companies.

Digital platforms create value by facilitating direct interaction between two or more groups. Amazon, for instance, does so between merchants and shoppers. These platforms are characterised by economies of scale (because adding a user entails hardly any cost at all) and, especially, by what are known as cross-side network effects: the value to clients of one side of the platform increases with the number of clients who participate in the other side. Both economies of scale and network effects can create high barriers to entry and, with them, a market in which the winner takes it all.

Superstar firms can sometimes acquire a dominant position in their respective markets. Logically, this can create suspicion and even rejection among some parts of society (particularly among competitors). But we should not forget that the possibility to come to dominate a market as a result of a company's success is a powerful incentive for innovation and one of the drivers of productivity growth in our economies. What should not be allowed is the abuse of a dominant position, which is precisely what the competition authorities should seek to prevent.

Unfortunately, identifying and proving abuse of a dominant position is not easy, since practices that *a priori* could be considered anti-competitive may be legitimate in certain circumstances (setting a price below cost, for example, to gain sufficient critical mass in a platform). In practice, a balance must be found that avoids excessive *laissez faire* (giving superstars free rein of the market), but that also avoids providing disproportionate protection to competitors that may be less efficient than the superstar firm. In any case, this balance must, of course, be struck within a framework of legal certainty.

Finally, a level playing field also requires companies, regardless of their size, to meet their tax obligations. In this regard, the growing importance of companies that can shift profits between different jurisdictions with relative ease requires greater international coordination efforts in defining taxable profit bases. A good start, at least, would be to coordinate these efforts at the European level.

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