Press Release **Nice, London, Singapore, January 11, 2012**

EDHEC-Risk Institute Draws the French Government's Attention to the Inadvisability of Imposing a Tobin Tax in France

In an open letter dated January 10, 2012 addressed to the French Prime Minister, which itself referred to a previous letter addressed to the European Internal Market and Services Commissioner, Michel Barnier, EDHEC-Risk Institute has underlined the difficulties and risks associated with implementing a tax on financial transactions in France.

On the basis of a position paper* by Raman Uppal, Professor of Finance at EDHEC Business School, EDHEC-Risk Institute's recommendations are structured around theoretical evidence on financial transaction taxation, empirical evidence on its effects, as well as the implementation challenges of such a tax. The key findings from this study are as follows:

- The findings of theoretical models are mixed about the effectiveness of the "Tobin tax" to reduce volatility and improve welfare. The Tobin tax will obviously lead to a reduction in the trading of securities on which the tax is imposed. But, a reduction in the trading of financial securities also means that it is now more difficult to use the financial markets to smooth consumption over time and in different economic conditions. The Tobin tax reduces speculative activity in financial markets; but, this tax also drives away investors who provide liquidity and stabilise prices. Thus, introducing a Tobin tax has both advantages and disadvantages, and the net effect on volatility is likely to be small.
- There is a substantial body of empirical work studying the effect of a transactions tax on volatility of the price of financial securities. Most of these studies find that a transaction tax either fails to reduce return volatility, or leads to an increase in volatility. Moreover, the imposition of a transaction tax leads to a reduction in the demand for that financial security, and thus, a drop in its price. This drawback could go against the wishes of eurozone leaders to facilitate the distribution of their debt in stable conditions and to decrease the cost of the debt for the zone's most fragile economies.
- Finally, imposing a tax on financial transactions presents its own challenges. For example, can regulators really distinguish between transactions related to fundamental business and those that are purely speculative? Can regulators determine the appropriate rate for the Tobin tax that would reduce the activities of investors who are not fully rational, but not drive away trade by rational investors? And, from the point of view of speculators, unless all major financial centres introduced it, the Tobin tax would appear easy to circumvent by routing transactions through countries where the tax is not imposed.

A copy of the open letter to Prime Minister Fillon can be found here (translated from the French):

EDHEC-Risk Institute Letter to the French Prime Minister, January 10, 2012

* A copy of the EDHEC-Risk Institute position paper can be found here:

EDHEC-Risk Institute Position Paper A Short Note on the Tobin Tax: The Costs and Benefits of a Tax on Financial Transactions

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