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## Fostering an Independent Media with a Diversity of Views

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I have been interested in the question of how to promote a competitive and pluralistic media for a very long time. In a way, it is a very natural outgrowth of my work on the economics of information. My research analyzed how information is important for the economy to function well and how there are systematic distortions in incentives to provide information that lead to information asymmetries and a whole set of other problems.

My more recent interests have been in information and political processes, that is, how imperfect information affects political processes, just as my earlier work focused on how imperfect information affects economic processes. Here again I have attempted to analyze incentives: why there are often incentives to provide distorted information and how we can make political systems work more effectively, both through the provision of information and by the adoption of certain regulatory and legal frameworks.

This chapter will deal primarily with the impact of information provided by the media on public policy. However, much of what I will discuss also applies to the importance of information in the functioning of markets, for instance, in identifying market failures, including abuses of market power and failings in corporate governance.

The view that good policies require good information is widely accepted. In a democratic society, the views of citizens are critical. Democracy is not meaningful if people do not know what they are voting about. Voters' beliefs are shaped by what they see and read in the media.

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The consequence is that distortion of information can contribute to views that are distanced from reality. We saw a dramatic example of this in the months prior to the commencement of the Iraq war, where there were markedly different perceptions of reality in different countries, each shaped by the distinctive media coverage in the respective countries. The differences in perceptions were, to a large extent, a result of differences in media coverage.<sup>1</sup> The further consequence is that different views of reality lead to support for different positions and policies. Those countries where media coverage was particularly distorted adopted policies that were not only adverse to global interests but arguably were adverse even to national interests.

One way of focusing more narrowly on the role of information in democratic societies is to observe that underlying well-functioning democracies is a system of checks and balances. British historian Lord Acton said that power corrupts and absolute power corrupts absolutely. There is another aphorism, "knowledge is power." The absence of information gives those who are in policy making positions a level of power that would be limited by greater access to information. Corruption provides another example illustrating the role of information—and the media—in political processes. The subject of corruption has recently received considerable attention at the World Bank, and rightly so. Corruption is an "agency" issue, that is to say, individuals with delegated authority advance their own interests in particularly egregious ways at the expense of those whose interests they should be representing. Agency problems arise because of imperfections of information; they would not occur in a world with perfect information. If we could observe what was happening instantaneously all the time, these agency problems would not arise and thus the scope for corruption would be limited. People would realize that they would be caught and would act appropriately. Monitoring provides a check, and it is an important way of dealing with agency problems.

The problem is that monitoring is a public good, and, more broadly, the public good is a public good. Managing society in ways that benefit everyone is a public good. In some ways, it is the most important public good. Ensuring that the government acts in ways consistent with the public good is itself a public good, and monitoring, which is essential to this process, is a public good. It follows, then, that since in general there is an undersupply of public goods, there will be an undersupply of monitoring.

In democratic societies, the media are one of the key monitors. But if the media are to perform their role, two "rights" have to be recognized: the

right to tell—or freedom of the press—and the right to know, highlighting the importance of having access to information, reflected in Freedom of Information Acts. There has been great progress in recent years in the passage of such acts around the world. After leaving the World Bank, I helped create a think tank at Columbia University called "The Initiative for Policy Dialogue," and we have pushed these Freedom of Information Acts. Many countries have adopted these laws; the real challenge now is enforcement. Even in the United States we have trouble with the government understanding the intent and the purpose of this law. Perhaps it would be more accurate to say that those in power do understand not only the purpose of the law but also its effects; it is because they know it limits their power and their opportunities for corruption by making them more accountable that they have worked to limit the scope of the law.

I do not mean to imply that circumscribing corruption and strengthening the system of checks and balances so essential for a functioning democracy are the only reasons that it is important to have good information. Even without corruption, all individuals are fallible, and the consequence of human fallibility is that there has to be shared decision making. A number of years ago my colleague Raaj Sah and I described a framework for thinking about human fallibility and collective decision making.<sup>2</sup> For example, we explored how the structure of decision making could affect the tradeoffs between type one and type two errors. (Type one errors are also known as *false positives*. To use a medical example, if tests for cancer reveal that persons have cancer when in fact they do not, these would be type one errors. Type two errors are known as *false negatives*. Returning to our example, this would describe situations where the tests failed to identify those who actually had cancer.) Our work provides another argument for having widespread participation in decision making by reducing the likelihood of these errors, but effective participation requires information. Again, the media play a key role as an information intermediary, and there is a problem of the undersupply of the public good of information.

I have talked about the role of information in monitoring and in enabling shared decision making. I have suggested that there will be an undersupply of information in either case. However, the issue is not only the level of information supplied but also the nature of the information supplied, or in other words, distortions in the information supplied. The problem is that those who supply information often have an incentive to supply distorted information, and this is true both in the public and the private sectors.

The problems in the public sector are obvious—politicians do not want citizens to know of the corruption in which they are engaged, to have their power circumscribed or their mistakes to be exposed—but let me emphasize that these are just as important in the private sector. The point is that decisionmakers in both the public and private sectors do not like checks and balances. People like to have their way and operate without someone looking over their shoulders. People particularly do not like to be monitored when they are making mistakes, even if the mistakes are honest and not corrupt. The problem is that we often have a difficult time distinguishing between honest mistakes and corrupt mistakes. If there were any question about that difficulty, we can look at Iraq and Hurricane Katrina, where massive mistakes have occurred and massive amounts of money have been spent with outcomes that are disappointing, to say the least. The question is to what extent these outcomes are due to corruption or to incompetence. The general answer is that there were some of both, but the difficulty lies in trying to parse out what fraction of the failures is due to corruption and what fraction is due to incompetence. In the end, it may not be that important to distinguish between the two, as long as we arrive at the correct decision of what to do about the situation.

Government officials want to increase support for their positions by enhancing the belief of likely success, and so they have a strong incentive for supplying distorted information. Unfortunately, we have seen ample evidence of this in recent years.

But this is only part of the problem. There are also opportunities for more pervasive corruption in the supply of information. This is another agency problem that is widespread throughout the government: the marginal cost of providing information should be zero, but an artificial scarcity can be created through secrecy, thereby reducing the flow of information and creating something of value. Free information has no value because everybody has it. Restricting the supply of information, however, gives it value, and those who have that information then can trade it.

Now, for the most part in the United States, we do not have outright corruption in the sense that it exists in some other countries, where officials actually take bribes. We do have an American form of corruption that is possibly more corrosive of our society, and it is larger in magnitude in terms of absolute dollars (largely because the economy is larger). It is traded in what is sometimes called "gift exchange": I create something of scarcity, which somebody then wants, meaning there is room for a deal. I give him what he wants, and he gives me what I want. What the government official

wants from the typical business person is a campaign contribution. What the government official wants from the media are stories written in the way that the official wants. This may include giving more weight to the slant of the government or putting the government official in a more pivotal role than is the case. It may include, as part of the package, a couple of puff pieces about how great the government official is. (When we see a puff piece in the newspaper, we can be fairly sure that it was part of a gift exchange, a return for getting some piece of information.)

When I was in the White House, first as a member of the Council of Economic Advisers (1993–95) and then as its chairman (1995–97), it was obvious who "owned" which reporters and what they were getting in exchange for their stories. Often there are well-established relationships, with each reporter owned by a particular member of the administration and providing "services" in return for which he gets access to so-called "inside information." I understood the market in information that was at work; but most of us do not see it as clearly. This makes it more difficult to evaluate the information that has been provided and to understand the ways in which it may have been distorted. In other cases, access to information is an exchange for campaign contributions, although this is probably not the major source of corruption in campaign contributions; far more important, sources are pieces of legislation, like our prescription drug benefits that cost Americans amounts probably in the hundreds of billions of dollars. These are good investments, high returns for relatively small campaign contributions.

On the supply side of the market, are the government officials who create an artificial scarcity of information; but there are lots of people on the demand side, both businesses and journalists. Knowledge is power, and access to information can be converted into profits. More specifically, having information before anyone else can make a great deal of money. However, this does not necessarily have any social return. Let me make it clear: a lot of this information has very little social return, but knowing something before somebody else could give a high private return. Obviously, there is also demand from the media, with kudos and sales for those who break news. In both cases, there are high private returns to having information just slightly before others, and there is a large disparity between social and private returns.

This problem of artificially creating scarcity is one of the most important reasons why it is necessary to have a Freedom of Information Act, as well as to have an independent enforcement agency, because the government has strong incentives not to comply or to comply in a minimal way.

Even without corruption, there can be honest differences of opinion about what is in the national interest; even without corruption, governments still want to distort the flow of information, especially when government policies do not seem to be working in the way advertised.

This is a problem in the private sector as well. The cigarette industry provides one of the obvious cases. It tried to distort the public's beliefs about the amount of carcinogens in light cigarettes and the effects of smoking on cancer and on health more broadly. The members of the cigarette industry had the information; they knew what the effects of smoking were; and they were in a position to engage in research to get still more information. They knew that light cigarettes delivered just as many carcinogens as regular cigarettes, but they also knew that it was not in their interest to have this information disseminated. Instead, they created information saying that there was uncertainty about the science leading to these conclusions, even though there was, in fact, no uncertainty that cigarettes were bad for health.

More recently, Exxon paid money to so-called "think tanks" to disseminate the same kind of uncertainty about climate change. There are some uncertainties, for example, about the pace of change. There are even uncertainties about how serious it is—whether it will be equivalent to the loss of 5 percent or 7 percent of gross domestic product. However, there is no doubt that global warming is real, that it will have a devastating effect on many developing countries, that there have been significant effects from our use of fossil fuels, and that it is an issue we ought to do something about.

These two cases illustrate the worst in corporate practices; but the problems are more pervasive (Stiglitz 2003). Each firm wants potential investors to believe that its expected returns are high. This problem is exacerbated by stock options where the compensation of the chief executive officer (CEO) increases with the stock price; this gives CEOs an incentive to provide distorted information to shareholders and the media. (There was a more pervasive web of distorted incentives: analysts, the investment banks, and the accountants all had incentives to provide distorted information.) Thus, the underlying problem, to which the media have at last caught on, is that those who have control of information often have incentives to provide distorted information.

There is no perfect solution to these problems. The problem is what can be done to mitigate these risks, for instance, by changing incentives or creating various systems of checks and balances in the provision of information. In the private sector, the Sarbanes-Oxley Act<sup>3</sup> has changed incentives for accounting firms. Before the law was enacted, accounting firms were

hired by the CEO of the company rather than by the audit committee, and thus the accounting firms' incentives were to please the CEO. This meant that they were not as concerned about getting accurate information as they were about getting information that the CEO liked. The CEO wanted positive news that would lead to an increase in the stock prices—and thus in the value of options. Before the Sarbanes-Oxley Act, most accounting firms also got most of their money from consulting, which distorted these incentives even more. At the root of the problem is the way CEOs are compensated; stock options provide a strong incentive for distorted information.

The media play a critical role in monitoring and in providing information relative to public decision making. The problem is that, while the media in principle can play this role, they too have incentives that may not be well-aligned with the interests of society. For instance, the reporter or newspaper that gets the news first gains more attention and more advertising dollars, which in turn contributes to the patterns of distorted information described earlier.

This is where diversity comes in. Multiple media can provide an important set of checks and balances. In other words, each reporter or newspaper has an incentive to uncover the mistakes or distortions of others. I want to emphasize that what is relevant is not just the total number of media outlets; one has to look closely at the structure of the industry. Anyone who has been engaged in ascertaining the degree of competition in markets for purposes of antitrust is familiar with this kind of problem. For instance, in banking, one does not look at the total number of banks. There are a lot of banks in the United States, but that does not necessarily mean that the market is highly competitive. Instead, one must look at each market by region and sector, for instance, competition in the supply of loans for small businesses in rural areas within the state of Washington. Despite the large number of banks, few banks serve this particular market, and competition is very limited.

The same thing is true in the context of the media. What is important is how many sources of news or information any one viewer has, or how many sources of coverage any one company has. How many checks are there, how many people are providing independent information to any one person, and how many people are looking at the behavior of a company or a particular politician?

We also have to examine closely what the differences are within media, that is, whether there are significant differences in incentives and perspectives. Both the amount and the kind of information are of concern, and one of the problems with privately funded or privately owned media is that

their business is to make money. This leads to a whole set of issues: they worry about offending advertisers or a large number of readers, and they worry about offending government officials and thereby losing access.

Let me be clear: these are real worries. I saw what happened when journalists do not pay sufficient attention to these concerns. A reporter for a prestigious U.S. newspaper who covered the Federal Reserve (Fed), with very good access, thought he was supposed to write about what was going on at the Fed, and he thought that meant occasionally writing critically about what was happening. However, the Fed did not view that as the job of reporters covering the Fed, especially those who were given "access"; rather, the Fed viewed the job of the reporter as being more of a public relations outlet. This young reporter, who was getting front-page news stories in one of the major newspapers, made a mistake: he wrote a critical article. It was not long before he was reporting about automobiles in Detroit.<sup>4</sup> He had lost access, and without access, he had lost his value covering the Fed. His loss of access revealed the dangers of offending government officials.

Another set of problems arises when the owners of media outlets have economic interests that might be affected by how they cover a story. For instance, Americans are debating why the Iraq war coverage was so bad—and so distorted—in the United States before the war. There are a number of explanations, but one is that several of the newspapers were trying to get television licenses at the time and did not want to offend the regulatory authorities, where presidential appointees predominated. Whether this is true or not, it at least alerts one to the possibility that politics can color news coverage, even apart from outright censorship and even in a democratic society. It should make us particularly sensitive to the media being subjected to economic pressures from politically controlled regulatory authorities, particularly when discretionary decisions are being made by regulators. Imposing restrictions (such as that newspapers cannot own television and radio stations) reduces the scope for such self-censorship and may increase media diversity.

The problem is exacerbated by the fact that many people, including rich business people, want to shape the world. There is nothing wrong with this, and they should be commended for their public spiritedness. But they are able and willing to spend a great deal of money to do so. Some owners of media outlets clearly view their control as a mechanism for advancing particular political positions. That this is a concern is evident in the ownership restrictions on media that many countries have. The United States has ownership restrictions on television, and one of the reasons is the

worry that foreign owners might promulgate a view that is un-American. These concerns highlight the fact that ownership matters. But if the rich disproportionately control the media, and if the rich disproportionately share common views (for example, on the desirability of low taxes, the elimination of the estate tax, and fears of big government), the media may not be able to do their job: the media may supply distorted news coverage and/or may be perceived as doing so. At the very least, there will not be a diverse set of perspectives that should underlie active democratic processes.

There have been real concerns about media ownership in the Russian Federation. In the Russian election of 1996, the oligarchs clearly used their positions and wealth to advance the reelection of Boris Yeltsin, in return for which they received large ownership shares in what was called the "Sale of the Century" (Freeland 2000). Some estimates put the value of state assets that were transferred to the oligarchs at bargain-basement prices at between US\$1 trillion and US\$1.5 trillion, and this has had a long-term effect on Russian society. People in Russia say they went from a state-controlled media that gave them very little diversity to an oligarch-controlled media that gave them very little diversity. Now they are returning to a more mixed system, where censorship may be more subtle, or at least less formal, but no less repressive.

If the media are to perform their critical role in democratic societies, it is important to have a diversity of views. This means that competition is more important in the media than in other sectors. The usual standards for competition in other sectors, such as monopoly power (evidenced by the ability to charge prices above marginal costs), are not the appropriate ones for this sector. What is at stake here is more fundamental: the effective functioning of our democratic society. Thus, the criteria for assessing excessive concentrations of media power need to be markedly different and markedly tighter. Also, because different media reach different audiences, the definition of "market concentration" needs to be very attentive to the issues of both coverage and audience. We need diversity not only within each media but also diversity across media. We should accordingly worry about ownership of television and radio by newspapers because it reduces the overall scope for diversity. This may be a problem of increasing concern, as economies of scope act as a natural force leading to increased media concentration.

There are other important aspects of a program for designing a more effective and diverse media, in addition to strong competition and diversity laws. For instance, we should encourage the entry of foreign media, for this broadens the set of perspectives that confront citizens. Moreover,

foreign media may be less subject to some of the political pressures to which I alluded earlier. Also, as we have noted, some countries have strong restrictions on foreign ownership of media. Worry about foreign domination of media is understandable, but foreign views can be an important check. In the United States, in the months preceding the war in Iraq many Americans found that the only accurate sources of information, judged both *ex ante* and *ex post*, were provided by the BBC and the *Financial Times*. The American media did not do their job; but, even if the information provided by the foreign media turns out to be wrong, having a diversity of views on a global issue like war is important. At the very least, it is important for citizens to see the information that is being provided to those in other countries, unfiltered through domestic media.<sup>5</sup>

There is another reason that it is important to have this foreign perspective: foreign media often have a different set of incentives and a different kind of accountability. The kinds of "biases" that exist in one country may also be different from those of another. They may have their own biases, but at least they are different, which is what leads to a diversity of perspectives.

Another example that illustrates this is the New York Stock Exchange scandal involving then-chairman of the Exchange, Dick Grasso, who received an extraordinarily large pay package approved by the Exchange's Board of Directors. The New York Stock Exchange provides "self-regulation" of its members; there is an obvious conflict of interest in the "regulated" setting the compensation for the "regulator." Perceived inadequacies in certain aspects of this self-regulation have heightened concerns about these potential conflicts of interest.<sup>6</sup> When news of the magnitude of Grasso's compensation broke, it became a scandal, and he was forced to resign.

The interesting thing about the episode was that the story was evidently broken by the *Wall Street Journal* about six months before the *Financial Times* began its series. However, in the eyes of the *Wall Street Journal* the compensation was perfectly normal, or at least not scandalous. Perhaps the editors did not want to offend their "customers," many of whom are people receiving similarly generous compensation packages, and some of whom may have engaged in practices that might, in appearances at least, look similarly scandalous. It took an outsider to point out that it was not acceptable to have the compensation of a self-regulator be decided by people who are engaging in practices that clearly ought to be circumscribed. The *Financial Times* began an attack on what was going on at the New York Stock Exchange; as is so often the case in such scandals, every day new aspects were reported.

Grasso and the Board of the New York Stock Exchange may have hoped that the story would go away, but it did not. Eventually, it is safe to say that the *Financial Times* brought about Grasso's resignation.

A third example where foreign media played an important role in covering an American story is the scandal involving Harvard University and Andre Shleifer. The Harvard Institute for International Development was given a large contract by the United States Agency for International Development to give advice to Russia about privatization. The principals in the contract were Shleifer and a colleague. Whatever can be said about the quality of their advice, what is clear is that they used the opportunity to advance their own financial interests. Harvard eventually had to pay US\$28 million, and Shleifer and his colleague had to pay the U.S. government between US\$2 million and US\$3 million. The story is described at great length in the *Institutional Investor* (McClintock 2006).<sup>7</sup> However, what was reported in the *Institutional Investor* is not the full story; it is much worse than that. This is another model case of corruption, with enormous ramifications within Russia, but my point here is to call attention to the nature of the media coverage. The coverage in the *Financial Times* was again much stronger than in American newspapers, perhaps because the incentive structures are different. Perhaps the American newspapers felt uneasy about rattling an establishment institution in this way.<sup>8</sup> Perhaps it was because the *Financial Times* was more sensitive to the global consequences of this instance of American corruption and how it affected perceptions of the nature of Russia's transition from communism to a market economy.

It is important not only that there be a diversity of media but also that media have an incentive to provide information that is relevant for public decision making. The private incentives in gathering and providing content may not be in accord with social returns. We may get more advertising revenues by having Mickey Mouse on the air 24 hours a day than by having any news programming, and the private media will therefore have 24 hours of Mickey Mouse programming.

This is an example where there is a large deviation between private and social returns; one way of dealing with this would be to require all television and radio stations to provide programming about matters of public concern, such as political debates. This is a legitimate restriction; after all, the spectrum is owned by the public and so the public has the right to allocate it in ways that advance the public good. People will disagree about the best way of doing so, but because the spectrum is a public resource, there is an obligation to ensure that this resource is used in ways that are consonant with the public interest.<sup>9</sup>

There is also a role for public media; the obsession with privately owned media is misplaced. Public media can have different incentives and, therefore, different perspectives. There are many examples that demonstrate that one can have high quality, publicly controlled media that are relatively politically independent in well-functioning democracies. Obviously, the institutional design is important. Not every country has succeeded in having this, but some have; the BBC is an excellent example.

In thinking about how to get more media diversity, one ought to think not only about public ownership but also about a variety of ways of subsidizing nongovernmental organizations to run community-based media and other kinds of media. For instance, the costs associated with radio may be very low, which suggests that one could provide support for a large array of perspectives at relatively low costs. This is why a lot of countries are now expressing interest in public radio. Some governments, concerned about the control of the media by a small group of people, are supporting community radio stations, and this is a positive development.

The rationale for the role of government in media is clear. Information is a public good, and as a public good it ought to be publicly supported. The public good is also a public good, as are democratic participation and citizenship. Without public support, there would be an undersupply of these public goods.

Monitoring and maintaining competition and pluralism will be difficult, but a variety of instruments are available through which we can attain these objectives, including antitrust laws, government subsidies, spectrum subsidies, state-owned radio and television, and requirements for public interest programming. It is important, although difficult, to monitor diversity; examples of ways to do so include measuring the diversity of coverage of key issues, constructing a diversity index, and comparing media across locales and over time.

In conclusion, good information is essential to the effective functioning of a market economy and economic processes. Without good information, prices will not provide appropriate information to guide resource allocations. My own work has explained why there are incentives to provide distorted information.

By the same token, good information is essential for the functioning of democratic political processes. Without good information, citizens cannot participate meaningfully. Their votes would not guide resource allocations and other decisions in appropriate ways, and there will be an ineffective system of checks and balances.

The implication is that we need a diverse and competitive media presenting a variety of viewpoints. We need effective and strong laws and regulations ensuring the right to know and the right to tell. But we need more than that: we need a diverse media as a complement. Developing and maintaining pluralism in the media will not be easy because there are strong political and economic forces pushing the media in the other direction. There are people who do not want the kind of open and democratic society that a diverse media helps support; but through a variety of mechanisms that I have outlined in this chapter, I believe we can achieve more competition and more pluralism. Doing so will create more efficient economies. Even more importantly, doing so will strengthen democracy around the world.

## Notes

1. Evidence that television can influence beliefs has been around since Iyengar and Kinder's *News That Matters: Television and American Opinion*. While it is difficult to prove that public opinion, as mediated by television, drove countries' decisions to either participate in or oppose the war in Iraq, it is certainly the case that such differences of opinions existed. The most obvious example pertains to the question of whether Saddam Hussein possessed weapons of mass destruction or aided Al Qaeda prior to the invasion. Even as late as the 2004 presidential elections in America, 75 percent of Bush supporters believed that at least one of these was true (Wills 2004).
2. See, in particular, Sah and Stiglitz (1985, 1986, 1988a, 1988b, 1991).
3. The full text of the act is available: [http://www.sarbanes-oxley.com/section.php?level=1&pub\\_id=Sarbanes-Oxley](http://www.sarbanes-oxley.com/section.php?level=1&pub_id=Sarbanes-Oxley).
4. The transfer could, of course, have just been a coincidence. The worries about loss of access are, however, real.
5. The Internet, for the first time, has increased access to a diversity of viewpoints enormously. However, it is not a substitute for access to television, radio, and print.
6. In addition, some members of the board may have thought the extraordinary compensation was "normal," because compensation was perhaps not totally out of line with (admittedly widely criticized) practices of executive compensation in their own and other companies.
7. In addition, in litigating the case Harvard faced huge legal bills, estimated in the millions of dollars. Harvard's defense—that they were under no obligation not to have had a conflict of interest—hardly set the moral tone for what one would have expected of one of America's leading institutions.
8. This is especially so because of the strong links between Shleifer and Harvard's president, who in turn had close links with other "establishment" figures.
9. By the same token, most cable stations make use, in laying their cables, of public rights of way; and it is a perfectly legitimate demand of the state to request, in return, public interest programming.

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