George J. Stigler Center for the Study of the Economy and the State

2016–17 Annual Report
Over the past 40 years, the Stigler Center has been dedicated to understanding the interaction between politics and the economy through research on regulatory capture, subversion of competition by special interests, and the role of private markets and competition in promoting human welfare. Nobel laureate George J. Stigler founded the Center for the Study of the Economy and the State at the University of Chicago in 1977. From the beginning, it has been a joint enterprise of economists and legal scholars at Chicago Booth, the Department of Economics, the Law School, and other areas of the university. The center was renamed in Stigler’s memory after his death in 1991.

To carry out its mission of promoting competitive markets, the Stigler Center has embarked on a program of outreach, education, and research. The center publishes a working paper series and a case study series, and disseminates its research via conferences and lectures. In addition, the center engages with the wider community through its blog, ProMarket, its Journalists in Residence Program, and through outreach with students and alumni.

The George J. Stigler Center is a significant contributor to the continuity and growth of “Chicago Economics,” which is known worldwide for four attributes:

- A view of economic theory as a powerful tool for understanding the world
- A deep appreciation for the role of private markets in promoting human welfare
- An understanding of the legal infrastructure that facilitates market performance
- Careful empirical testing of the predictions of economic theory

The Stigler Center is appreciative of the philanthropic support* from The Lynde and Harry Bradley Foundation; La Marzocco; Chuck McQuaid, ’76 and Monica McQuaid; Jerry Raymond Wallace, ’85; and Anonymous.

*Gifts made July 2016–June 2017
In the academic year 2016-17, the Stigler Center successfully advanced its mission to promote a true market culture in the United States and abroad. The center also launched two important new initiatives. The first is a fellowship program for PhD students who are writing their dissertations on themes related to the center’s mission. These PhD students, in disciplines spanning from political science to law, from marketing to finance, have presented their work throughout the year at a regular Stigler Center lunch workshop. The cross-fertilization has produced two important papers, which enriched the center’s working paper series.

The second initiative is the Journalists in Residence Program. The program offers the opportunity for eight up-and-coming journalists from all over the world to audit three Chicago Booth classes; participate in Stigler, Booth, and university events; collaborate with peers; and socialize with the university’s greatest scholars. This year fellows included very talented journalists from The Economist, Marketplace, The Hindu, and Brazil’s Epoca.

The center has increased its effort in hosting conferences by organizing three conferences on campus. The first was a continuation of the Theory of the Firm conference co-organized with Harvard Business School in 2015. The second was a conference on whether there is a concentration problem in America. This conference brought together all the major scholars in antitrust and had vast echoes in the media (for example, an article in The Economist was dedicated to this topic). The third conference was on the Political Economy of Finance. Even though this was a new conference, it received more than 100 paper submissions.

In the past year, the center continued and expanded initiatives that were started the prior school year. The ProMarket blog greatly increased its reach and its set of contributors, becoming a standard reference for many journalists and opinion makers. For example, BBC and NPR interviewed Nobel laureate Oliver Hart, and specifically asked him about a ProMarket post that I wrote on him.

The center’s public lecture program has been divided in two. One segment includes book presentations, which this year spanned from Nobel laureate Joseph Stiglitz to accounting professor and Booth alumnus Eugene Soltes. The other segment focuses on our mini-series, consisting of three lectures given by the most qualified scholars on a topic of interest. These lectures are recorded and the videos made available on the Stigler website. Particularly successful was David Yermack’s lecture on blockchain that received more than 4,000 views. In addition, the first two Stigler business case studies have been publicly released. Students and faculty can download them for free from the center’s website.

Last but not least, the center has provided support for a new course I taught to undergraduates called Crony Capitalism, which is designed to explain why competitive markets work and to examine the forces that try to subvert capitalism.

This past academic year has been very rich. As we enter 2017-18 (the 40th anniversary of the Stigler Center), we have an even broader plan of activities lined up. I am excited about the prospects for the Stigler Center and am confident that you will be too. Please join me in working to enhance and extend Stigler’s legacy throughout the world. Do not hesitate to contact me if you have any questions or suggestions.

Sincerely yours,

Luigi Zingales
Director, George J. Stigler Center
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IMPACTING THE WORLD
On September 30, a large crowd of University of Chicago students and faculty attended the Stigler Center’s Welcome Back BBQ, held at the Charles M. Harper Center at Chicago Booth.

The event aimed to introduce the Stigler Center and its initiatives to the faculty and the student body. Posters hung around the room displayed the wide array of center activities—its research efforts, the Case Study program, the ProMarket blog, the Campaign Financing Capture Index, the Political Economy Lecture Series, and classes led by Stigler-affiliated faculty. Members of the center were on hand to answer questions and explain to students how they can get involved.

Despite unfriendly weather conditions, the event drew a sizable crowd of 264 students, both from Chicago Booth and from other University of Chicago departments. While enjoying the complimentary food, participants explored the different stalls and engaged in lively discussions with Stigler Center staff. Stigler Center director Luigi Zingales and codirector Guy Rolnik mingled with the attendant crowd and explained the center’s mission and its goals.

As the inaugural event of the Autumn Quarter, the BBQ marked the beginning of a year of tremendous growth and transformation for the Stigler Center.
Launched in 2015–16, the Stigler Center’s political economy lecture series features thought leaders in academia, business, the legal profession, and the media with experience in the way special interest groups distort markets. In 2016-17, the Stigler Center hosted five of these lectures, on topics as varied as whistleblowers, the future of the euro, and the economics of investigative journalism.
Eric Ben-Artzi, a former risk officer turned whistleblower, caused a global media sensation in late August 2016 when he publicly rejected a multimillion-dollar award from the Securities and Exchange Commission via an op-ed in the Financial Times. The award was Ben-Artzi’s share of a $55 million settlement between the SEC and Deutsche Bank that concluded a five-year investigation into allegations that the bank had overvalued its derivatives portfolio at the height of the financial crisis to hide potential trading losses. Ben-Artzi, a former Deutsche Bank risk officer, was one of three insiders who came forward in 2010-11 to notify regulators of the bank’s improper accounting. As an informant, Ben-Artzi was entitled to 15 percent of the settlement under the Dodd-Frank Act, which he estimates at $3.5 million after payments to lawyers and experts. However, he publicly rejected his share of the award due to the agency’s failure to punish Deutsche Bank’s executives.

In October, Ben-Artzi was interviewed via video conference by Guy Rolnik, codirector of the Stigler Center. During the interview, he explained at length what it takes to disclose fraud. He outlined his reasons for becoming a whistleblower, what he has learned about the American judicial system, and the role of the revolving door at the SEC. “The problem is not that you have misbehavior on Wall Street. It’s that you have misbehavior by the people who are supposed to enforce the law, by the prosecutors, by the regulators,” he said.

Eugene Soltes, Jakurski Family Associate Professor of Business Administration at Harvard Business School, spent the past seven years speaking to and corresponding with nearly 50 prominent executives convicted of financial crimes. Many of his interview subjects were people of great wealth and influence who commanded respect within their industries. To understand why they had risked it all by breaking the law, he visited some of them in prison (among them convicted Ponzi fraudsters Bernie Madoff and Allen Stanford), often even meeting them and their families in an attempt to identify what separates honest, hardworking executives from those who choose to commit fraud or other white-collar crimes.

In October, Soltes visited the Stigler Center for a discussion with Nick Epley, a professor at Chicago Booth. Soltes discussed his book Why They Do It: Inside the Mind of the White-Collar Criminal (Public Affairs, 2016) and explained what led him to peek into the minds of some of the most infamous financial criminals of our generation and described what he learned about the motivations behind white-collar crimes. “Oftentimes, the people that are perpetrating these acts have little to no emotion at the time that what they are doing is actually sinister or that they’re doing anything harmful,” said Soltes. He hypothesized that many of the most well-known cases of executive failure might better be described as failures of managerial intuition rather than failures of reasoning.
Is the euro doomed? Or is it an irreversible step toward a closer political union that has brought peace and stability to Europe? In November, the Stigler Center hosted a panel, moderated by director Luigi Zingales, between Nobel laureate and Columbia University Professor Joseph Stiglitz and Princeton University Professor Markus Brunnermeier, both authors of recent books on the euro crisis. The panel, which pitted skepticism versus optimism, dealt with issues such as the structure of the European single currency, the opposing economic philosophies of Germany and France, and the rise of political populism.

Stiglitz, author of *The Euro: How a Common Currency Threatens the Future of Europe*, offered a more pessimistic take. He argued that the financial crisis of 2008 compounded the conditions that led to the euro crisis by allowing flaws in the euro’s design to manifest. Stiglitz suggested that Europe may be unable to build the institutions necessary to save the single currency and may have to abandon the euro altogether. “It may be necessary to abandon the euro to save the European project,” said Stiglitz.

Brunnermeier, author of *The Euro and the Battle of Ideas*, offered a far more optimistic view of the crisis. Many required reforms have already been made, he said, despite the “Rhine divide” between France and Germany regarding the euro. “We are at a critical phase, but shooting down [the euro] would be a huge step backwards,” said Brunnermeier. The measures taken so far by European leaders have made him confident in the survival of the single currency: “My confidence comes from the fact that so many steps were taken.”
Is American Democracy in Trouble?
March 6, 2017

Fears about extreme political conflict and polarization have been at the center of American political discourse in recent years. Is American democracy in trouble or is conflict an essential feature of American democracy? David Moss, the Paul Whiton Cherington Professor of Business Administration at Harvard Business School, took up this question from a historical perspective, exploring the strengths and weaknesses of the nation’s political system as it evolved over the past 230-plus years.

In his recent book, *Democracy: A Case Study*, Moss applies the case-study method made famous by the Harvard Business School to American history. In it, he examines the health of American democracy from a historical perspective by focusing on moments of intense political conflict, such as the Civil War. Moss went on to discuss the shifting nature of political conflict over time and whether partisan divisions and other political fault lines have become especially dangerous today—or whether American democracy is likely to bounce back, as it has so many times before.

The “diminishment of America’s democratic culture,” argued Moss, preceded the 2016 election as increasing polarization led Americans to lose confidence in their fellow countrymen and weakened American’s commitment to democracy. Nevertheless, said Moss, “Fierce debate is not the exception in American history—it is the rule.” A combination of conflict and commitment to democratic ideals, he added, is key to sustaining a healthy democracy. Even conflicts and tension can be “good, even crucial, in fighting the tyranny of the majority and capture by special interests.”
Investigative journalism that exposes wrongdoing and holds the powerful to account plays a crucial role in the proper function of democracy and competitive markets. Yet with the disintegration of journalism’s business model, media outlets are left with fewer resources to fund costly and time-consuming investigations. In a global media landscape that’s characterized by shrinking ad revenues, conventional wisdom has it that investigative journalism is financially unviable.

Is investigative journalism, currently under-provided in the marketplace, really a public good? In April, the Stigler Center hosted a special event to discuss this very question. The event, which marked the publication of the center’s inaugural case study on the French news start-up Mediapart, featured its editor-in-chief, Edwy Plenel, and cofounder, Marie-Hélène Smiejan-Wanneroy, as well as James T. Hamilton, Hearst Professor of Communication at Stanford University, and author of the recent book *Democracy’s Detectives*.

The panel revolved around the success of Mediapart, which has been profitable since 2011, and the economic challenges facing investigative journalism. “The digital age is a golden age of journalism but also a battlefield,” said Plenel. Discussing Mediapart’s unique business model, which shuns advertising and relies solely on subscription revenues, Smiejan-Wanneroy said, “Our goal is not to maximize profits, but prove a newspaper can be independent.” Professor Hamilton, whose book examines the economics of investigative journalism, detailed the findings of his research, which found that for every $1 invested in investigative journalism, society gains $100 in public benefits.
In 2016-17, the Stigler Center launched its mini-course series targeted to MBA and PhD students. The new program invites leading scholars from other universities to teach a series of stand-alone, interrelated seminars on cutting-edge ideas not incorporated into the standard curriculum. Videos of the four mini-courses held this year can be found on the Stigler Center website.
Political Economy in China: Capital Markets, Governance, and Growth
December 5, 6, and 8, 2016

Bernard Yeung, the dean and Stephen Riady Distinguished Professor in Finance and Strategic Management at the National University of Singapore Business School, visited the Stigler Center in December and taught a mini-course of three stand-alone lunch seminars on the topic of corruption and growth in China.

Anti-Corruption Reforms and Shareholder Valuations: Evidence from China

In his first Stigler talk, Yeung examined the success of China’s anticorruption efforts. In 2012, he said, China experienced a political shock, in the form of Xi Jinping’s ascension and the political power struggles that preceded it, that shook the equilibrium of the political economy and led to the current anticorruption efforts. Some, however, questioned whether the anticorruption drive is motivated by political agendas or a true desire to reform. Stock market returns, Yeung said, show that shareholders react positively to the reforms, and see them not just as the result of an internal power struggle but as a way for meaningful economic change.

China’s Growth Model, Governance and Development

In his second Stigler talk, Yeung examined Chinese growth since the 1978 reforms. Dividing growth in China into three main phases of consecutive reforms, Yeung found that while business groups created a big push across multiple sectors, the government (particularly the state-owned firms and banks) led growth in China, with many local officials incentivized to pursue growth in order to further their careers (“growth for promotion”). The government’s concentrated control of the economy and the finance sector, Yeung said, has been a major factor in China’s economic success.

The Chinese Economy: Moving Forward

In his third and final Stigler talk, Yeung reviewed the conclusions of his previous lectures and discussed the various challenges facing the Chinese economy, including corporate debts, rising cost of living, income disparities, high healthcare costs, and an aging population. China is unlikely to suffer systemic problems, he said, due to the government’s control of the economy, but localized problems could occur.
Blockchains and the Future of Finance
January 9, 10, and 11, 2017

David Yermack, Albert Fingerhut Professor of Finance and Business Transformation at New York University Stern School of Business, touched on the potential implications of blockchain technology for the future of finance, as well as for managers, institutional investors, small shareholders, auditors, central banks, and other groups in the financial world.

What Problems Do Blockchains Solve?
In his first talk, Yermack surveyed the research that led to the creation of digital currencies relying on blockchain technologies and the different initiatives by the financial services industry to adopt, or “co-opt,” the new technology. The blockchain, he said, could remake and disrupt the financial industry from the top down in a similar manner to what Napster and other peer-to-peer file-sharing services did to the music business two decades ago.

Blockchains and Corporate Finance
In his second talk, Yermack examined the implications of blockchain technology on corporate finance, shareholders, and shareholder activists. The move toward blockchains, he said, will significantly impact what it means for a company to go public and issue shares.

Blockchains, he added, would have dramatic implications for shareholder voting and electoral democracy. NGO groups around the world are currently pushing for voting through blockchains as a potential reform against corrupt governments. Applying the blockchain to US corporate elections, he said, would limit the ability of corporate managements to manipulate elections.

Blockchains and Central Bank Digital Currency
Are digital currencies serious competitors with sovereign currencies issued by central banks? And should central banks retire notes and coins and move to electronic currency on a national blockchain? Yermack’s third and final Stigler lecture largely focused on questions regarding the future of central banking.

Digital currencies, he posited, could one day be seen as competing with central bank fiat money. At the same time, central banks could one day use the blockchain themselves, and dozens of central banks around the world are already looking into this, examining if a “national blockchain” would give them more precise control over monetary policy. Should central banks get into the business of a national blockchain? Yes, said Yermack.

If one day sovereign currencies would be issued on blockchains, he added, the result could be that the system of fractional reserve banking “would be gone.”
Trump and Trade
April 24 and 25, 2017

Douglas Irwin, John Sloan Dickey Third Century Professor in the Social Sciences in the Department of Economics at Dartmouth College, visited the Stigler Center in April and held two stand-alone, interrelated lunch seminars in which he examined President Trump’s trade policies and the threat that the wave of rising nationalism around the world presents to global competition.

Are We Losing? Trade Deficits and Global Competition

In his first Stigler talk, Irwin examined President Trump’s repeated claims that America is “losing” when it comes to free trade and criticized notions that trade agreements have had a significant impact on job losses or the decline of the American middle class. The US was already headed on a path toward fewer manufacturing jobs before NAFTA was signed, he said. Even though car production has risen since the financial crisis, employment in the car sector continues to be down. “We shed more jobs but produce more cars,” said Irwin, who argued that much of the dislocation and job losses have more to do with technological change. “Trade is not killing the US, and protectionism is not a cure for the trade deficit,” he said, adding that trade agreements have brought “small but positive gains” to the US economy.

Irwin criticized the president’s aggressive line on trade, his withdrawal from TPP, and his promises to pursue an aggressive line when it comes to trade by arguing that Trump’s planned economic policies, particularly his tax cuts, will in fact increase the trade deficit, since they will increase spending.

Bad Deals? Those Disastrous Trade Agreements

In his second talk, Irwin continued to criticize the anti-trade line held by Trump and his aides and supporters. TPP, he said, was “generally a very good agreement.” Irwin went on to predict that Trump’s trade policies will likely spark an international backlash similar to the one that followed the Smoot-Hawley Tariff Act of 1930. The continued attacks on NAFTA by the president and his staff, he said, were already affecting global politics, leading to an anti-American backlash in Mexico and increasing chances of anti-American populists being elected. The more autarkic and isolated the US becomes, he added, the less power and influence it will have in the world economy and world politics. “Trump’s withdrawal from TPP means China will have a major say on 21st century trade instead of the US,” he said.
Can direct democracy be used to fix the crisis of representative democracy and can it be used as the answer to rising populism? John Matsusaka, Charles F. Sexton Chair in American Enterprise in the Marshall School of Business, Gould School of Law, and Department of Political Science at the University of Southern California, visited the Stigler Center in May for a series of three stand-alone, interrelated lunch seminars that focused on these very questions.

Are the People Losing Control Over the Institutions They Elect?
In his first talk, Matsusaka examined the rise of public anger in the United States and the subsequent rise of populist politicians. “People are feeling that they don’t have a say in the government, and it’s [been] going on for a long time,” he said. Matsusaka went on to discuss the role of the 2008 financial crisis and courts actively reversing Congress in building populist anger. He also detailed the finding of his research into public policy, which shows that public policy is often not congruent with the opinion of a majority of the electorate. Voters, he said, sense a “loss of control.” Matsusaka then discussed the increasing role of referendums and initiatives in American policymaking and the potential for this role to expand even further.

Why Direct Democracy Can Work
In his second talk, Matsusaka discussed his research into the effects of referendums and ballot initiatives on public policy, including two recent Stigler Center working papers. Contrary to persistent notions that direct democracy leads to excessive spending and chaos, Matsusaka finds the opposite is the case: referendum voters tend to make reasonable, even conservative choices, especially when it comes to fiscal issues. The United States “has had direct democracy at all levels for over 150 years, and that hasn’t led to chaos or anarchy,” said Matsusaka. He went on to argue that direct democracy better represents the will of the majority and therefore might also be better able to counteract the power of special interests over policymaking.

Can We Use Direct Democracy to Fix Democracy?
In his third and final talk, Matsusaka once again examined the rise of populist anger, arguing that the present day populist challenge is similar to the populist/progressive movements from 1890-1920. The solution to that previous populist challenge, explained Matsusaka, was measures that increased democracy, such as universal suffrage. A similar recipe, he argued, can be applied to the current crisis of democracy. Direct democracy, he said, makes policy more responsive to public opinion, introduces competition into the policy process, and “breaks the monopoly of incumbents over what is considered.”
How Incomplete Is the Theory of the Firm?
March 3-4, 2017, Chicago

The standard (economic) theory of the firm is silent on the role firms can play in shaping the rules of the game under which they operate. In reality, many firms lobby politicians and try to capture regulators in order to modify the rules of the game in their favor. Some scholars have argued that the resources devoted to these activities are relatively so small that they are likely to have insignificant effects, and/or that regardless of how much firms invest in political activities, in a well-functioning democracy there are countervailing forces that effectively level the playing field. Other scholars have noted that the resources firms devote to shaping the rules of the game to their own advantage are sufficiently large and their effects sufficiently important enough to warrant a rethinking of the standard economic theory of the firm. Which of these two views has more empirical support? If the latter, should the economic theory of the firm be modified? If so, how, and is the potential fix better or worse than the existing problem?

In March, the Stigler Center at Chicago Booth, along with Harvard Business School and Oxford University, hosted a conference in Chicago to answer the following questions: Should the economic theory of the firm be modified? And if so, how? The conference was a follow-up to the Stigler Center’s 2015 conference on the crisis in the theory of the firm at Harvard Business School, which brought together top economists, legal scholars, political scientists, sociologists, and historians.

For two days, conference participants discussed various papers that dealt with political engagement by corporations, including three Stigler Center case studies on the Walt Disney Company, Piraeus, and DuPont. Other topics that were discussed during the conference included lobbying, regulatory capture, globalization and technological change, and the question of whether business schools have a responsibility to instill ethical norms in their students.
Is There a Concentration Problem in America?
March 27–29, 2017, Chicago

The Stigler Center hosted a first-of-its-kind, three-day conference in Chicago that focused on the question of whether the US economy has a concentration problem. The conference, which garnered widespread media attention, brought together dozens of top academics from law, economics, history, and political science, as well as policymakers, journalists, and public intellectuals.

In the past two years, the debate over concentration, market power, and bigness—and their potential effects on the US economy—has increased significantly, along with a growing body of research that showed competition has diminished across multiple American industries. At the same time, antitrust has returned to the forefront of American political discourse, particularly during the 2016 presidential election, in which both Democrats and Republicans promised to be more active on antitrust enforcement.

During the conference, participants discussed the validity of empirical evidence that suggests concentration in America is rising, as well as the possible connection between rising concentration and inequality, which has been understudied for many years. Participants also discussed the vast history of American antitrust and political engagement by corporations, particularly powerful digital platforms, and the changing nature of competition and markets in the age of Big Data. After four decades in which the predominant approach to antitrust was that enforcement should only be guided by economic considerations such as efficiency and consumer welfare, several participants also raised the political dimensions of antitrust and questioned whether political power should be taken into account as well.

Among the conference highlights was a remarkable keynote interview between Professor Zingales and Judge Richard A. Posner of the United States Court of Appeals for the Seventh Circuit in Chicago, one of America’s foremost legal minds and among the most influential antitrust scholars of the past 50 years. Another highlight was a video address by Margrethe Vestager, the European Commissioner for Competition, in which she extolled the benefits of competition.
In the past 20 years, political considerations have played an increasingly important role in financial economics—from the design of the rules that make financial markets viable to politically motivated changes in bankruptcy law, and from political connections in firms to the effects of political uncertainty on investments. Yet despite its growing importance, this area of economic research has remained relatively understudied until fairly recently.

On June 1-2, the Stigler Center hosted a first-of-its-kind conference focusing on the growing role of politics in financial research. The conference brought together top researchers and academics and featured a number of innovative papers that explored various themes related to the connection between finance and politics. The papers presented during the conference featured a wide array of topics, from political determinants of competition in the US wireless industry to the nexus of finance and politics in China, and from the way access to the Obama White House benefited companies whose CEOs met with White House officials to the impact of political influence over bank bailouts in Germany. The presenters, discussants, and participants debated the impact that political engagement by corporations has on changing the rules of the game, as well as the importance of taking political influence into account in studying financial markets.

The conference also included a riveting keynote address by Raghuram Rajan, Chicago Booth professor and former governor of the Reserve Bank of India, who explored the current wave of public discontent, the subsequent rise of populist nationalism, and its roots in the impact of technology and trade on blue-collar communities.
The Stigler Center launched ProMarket on March 12, 2016, with the aim of promoting discussion on issues that receive little attention in the media and academia: the subversion of competition by special interests, barriers to entry, and regulation that protects incumbents and discourages competition. The blog’s goal is to gather information on the nature and cost of subversion of competition in order to educate the public about the importance of competitive markets. While other publications and economic blogs devote little attention to these issues (and when they do so they do it from a partisan standpoint) ProMarket’s loyalty doesn’t lie with one political faction but with the economic principle that competition enhances welfare.

At the beginning of its second year of operation, ProMarket covered original research done at the Stigler Center (such as “Declining Labor and Capital Shares” by Simcha Barkai (Chicago Booth), “When Harry Fired Sally: The Double Standard in Punishing Misconduct” by Mark Egan (University of Minnesota), Gregor Matvos (Chicago Booth), and Amit Seru (Stanford), and “Public Policy and the Initiative and Referendum: A Survey with Some New Evidence” by John G. Matsusaka (University of Southern California) and by Chicago Booth faculty. It also kept its coverage of cutting-edge academic research on markets and regulatory capture, as well as interviews with influential scholars, including Nobel laureates Oliver Hart and Bengt Holmstrom.

ProMarket also launched two new interview series. One, titled “How Incomplete is the Theory of the Firm?” discussed the gap between the standard theory of the firm and the growing engagement of firms with the world of politics. The other, titled “Is There a Concentration Problem in America?” discussed the interplay between competition, bigness, and market power. Both series featured influential scholars from economics, law, history, and political science who discussed these issues in their work.
The 2016 election cycle was an unusual one in many respects. In financial terms, what was widely expected to be the most expensive election cycle in US history turned out to be slightly less costly than the previous election cycle, thanks to Donald Trump’s free media coverage that kept costs down somewhat. Congressional races, on the other hand, were pricier than ever. The 2016 election was also characterized by a growing concentration of donors, with fewer donors providing a larger share of the funding.

The Campaign Financing Capture Index was launched in 2016 with the aim of tracking the attempts of large political contributors to affect public policy. It did so by focusing on the fraction of total funds raised from large donors, based on the premise that campaign donations can be a mere expression of political preference, but contributions that exceed $5,000 are more likely aimed at altering policy in favor of the donor’s interest rather than promoting the public interest. Published monthly, the index analyzed the distribution of political contributions to presidential candidates and took into account individual contributions and contributions to the campaign committees, as well as contributions to PACs, super PACs, and joint fundraising committees that supported each candidate. Based on data collected from the Federal Election Commission website, the index aimed to provide a measure of candidates’ potential dependence on special interest groups.
EDUCATION
As part of its focus on regulatory capture and distortions created by special interest groups, the Stigler Center develops courses for MBA and undergraduate students. The center also continues to develop business case studies to enhance teaching on issues related to regulatory capture, lobbying, and the subversion of competition by special interest groups.

In 2016–17, Stigler Center Director Luigi Zingales created a new undergraduate course on crony capitalism.

Crony Capitalism

The economic system prevailing in most of the world today differs greatly from the idealist version of free markets generally taught in economic classes. In his course, Zingales analyzed the biggest problems facing the global economy—slow growth, inequality, pollution, and the eurozone crisis—and examined the role that corporate governance, wealth inequality, regulation, the media, and the political process in general play in producing these deviations from the free market ideal.

Zingales explained why all of these problems can be traced back to some form of crony capitalism, such as excessive lobbying and rent-seeking, insufficient competition, the political power of producers or nepotism, and why the crony capitalism that prevails in much of the world today is becoming more entrenched in the US. This multidisciplinary course, which combined elements of history, politics, and sociology, was taught to both undergraduate and graduate students.
In the Autumn Quarter, Stigler Center’s Codirector, Guy Rolnick, taught two sections of his course Reputation, Regulation and Communications—How Media Influences Business that was launched in 2015–16.

Reputation, Regulation and Communications—
How Media Influences Business

All businesses face multiple stakeholders, including shareholders, customers, employees, activists, NGOs, politicians, and regulators. Businesses interact with all these stakeholders mainly through the media. The media shape their reputation vis-à-vis their stakeholders, the way they are regulated, their costs, and their opportunities. This course explains how media influences companies and industries and how companies can affect this interaction. We start by analyzing the economics of media companies and how they work on the commercial and editorial sides. We delve deeper into the interplay between media, regulators, and companies, and focus in depth on media and the financial markets, crisis communication management, and the role of the internet and social networks. Students will participate in a simulation on the influence of the media on company stakeholders, including shareholders and potential investors, customers, employees, activists, NGOs, politicians, and regulators. The simulation gives the opportunity to put into practice some of the skills and strategies that the students learn during the course.
In the past year, the Stigler Center launched its first two business cases and continued work on three more.

### COMPLETED CASES

**Cumplo**

How regulation is used to prevent entry, especially in developing countries

Cumplo is a peer-to-peer lender that broke into the oligopolistic world of consumer financing in Chile. The incumbents pressured the regulator to criminally indict Cumplo for violation of the banking law. The founders were able to fend off this attack by promoting their image in the local and international press. Cumplo is now poised to become the main peer-to-peer lending platform in Latin America.

**Suitable courses:** entrepreneurship, strategy, media, political economy.

**Bigger picture:** This case illustrates how new business models, which challenge powerful incumbent industries, need to adopt a media strategy parallel to their business strategy.

**Mediapart**

Bucking the trend in the media industry

Started by former *Le Monde* editor Edwy Plenel, Mediapart seemingly runs against all the conventional wisdoms about how media should work in 2016. Most notably, it manages to break even and profit solely on subscribers’ revenues, it gets the French people to pay for online content, and it produces long-form investigative journalism and not just clickbait. What are the drivers of this apparent success story? Are they sustainable? What are the challenges they still have to face?

**Suitable courses:** entrepreneurship, strategy, media.

**Bigger picture:** This case is both an example of successful entrepreneurship in a very difficult industry and an alternative business model for investigative journalism.
CASE STUDIES

CASES IN PROGRESS

Walt Disney Company
How much of the Disney Company’s business model is riding on its ability to change US copyright laws?

When MBA students discuss the Walt Disney Company, it is usually within contexts such as vertical integration, creativity, and the like. But a large part of Disney’s revenues depends on constantly extending the copyright protections it enjoys. This is why every time that the copyright over Mickey Mouse is about to expire, Disney lobbies heavily—and successfully—to change federal laws and extend (retroactively!) the protection it enjoys. The Mickey Mouse example illustrates how policies meant to incentivize innovation can be co-opted to stifle it.

Suitable Courses: The case appeals to courses on business strategy, entertainment industry, and intellectual property, as well as regulation and political economy.

Bigger picture: It raises issues of intellectual property protection, such as how much is too much from a societal perspective? And who gets to dictate the answers?

The Marker
Can a newspaper be a tribune of the people? Should it?

The Israel-based business magazine–turned-newspaper, The Marker, adopted an agenda of fighting against economic and political concentration. The paper’s active, constant campaign led to unprecedented socioeconomic protests, which were later translated into unprecedented legislation meant to reduce economic concentration. But at what cost to the media company? And at what benefit to society? The Marker and its “parent” publication, Haaretz, suffered from an advertising boycott as a result of their activism. And the real impact of the concentration reform remains to be seen: the reform may die slowly in its implementation stage without actually improving the economy. The change may be short-lived and simply a congruence of events rather than a seismic shift.

Suitable courses: primarily media-related courses, but also macroeconomics, antitrust, political economy, regulation.

Bigger picture: The case spotlights two types of big-picture insights. One set of insights deals with what shapes regulation (public opinion and perception). The second deals with reputational concerns at the media level: can a media outlet create, maintain, and profit from having a reputation for representing the dispersed public?

Piraeus
How banking regulators benefit banks

In the middle of the Cyprus solvency crisis, the Greek bank Piraeus received a large windfall in the form of Greek branches of a Cypriot bank. A tour behind the scenes reveals just how much thought and resources were invested in assuring that the public would finance this gift to Piraeus: advertising, charitable contributions, and personal connections.

Suitable courses: finance/banking, macroeconomics, media.

Bigger picture: This case study fleshes out EU politics and general “soft capture” dynamics: advertising as lobbying, corporate philanthropy as co-optation, and so forth.
JOURNALISTS IN RESIDENCE PROGRAM

One of the missions of the Stigler Center is to enrich the public debate on matters related to the interaction between politics and the economy. The media, by gathering and disseminating information on the behavior of different players in the market, plays a crucial part in the effort to create a better competitive market system.

In order to help shape the next generation of business reporters and enable them to be better able to recognize instances where special interests subvert competition, the Stigler Center launched the Journalists in Residence Program in spring 2017. The one-quarter program offers a transformative learning experience for up-and-coming journalists from around the world who wish to deepen their understanding of political economy. The program will be held again in spring 2018.

The eight journalists who participated in the inaugural cohort of the Journalists in Residence Program were Alexandra Fattal (The Economist), Brooke Fox (Financial Times), Jana Kasperkevic (Marketplace), Chunxiao “Amy” Li (Tradingmen), Francine McKenna (MarketWatch), Alana Rizzo (Epoca), Asaf Shalev (former Columbia University Reporting Fellow), and Sharad Vyas (The Hindu).

The program is organized around four main components:

1. **Auditing classes**: Program participants individually selected three Booth courses to audit. They attend all classes and complete all coursework except for the final exam.

2. **Stigler Center lectures**: “The Intersection of Economics, Media, and Markets,” taught by Stigler Center Faculty Director Zingales and Stigler Center CoDirector Rolnik, introduced journalists to key concepts in the media market.

3. **Seminars**: As part of the program, the journalists attended weekly seminars with University of Chicago faculty and research centers to learn more about the research and activities being done on campus.

4. **Collaboration**: The journalists were given the opportunity to collaborate on group projects with each other and to write for the Stigler Center blog, ProMarket.

Provided with workspace in Chicago Booth’s Harper Center, the journalists were encouraged to meet with faculty and students and socialize within the group in order to strengthen their networks.
INNOVATIVE RESEARCH
Declining Labor and Capital Shares

In this much-cited paper, Simcha Barkai (a Stigler Center PhD Award winner who will join the faculty of London Business School in fall 2017) examines one of the most hotly debated topics in economics these days—the decline in the labor share. In it, he shows that the decline in the labor share over the past 30 years was not offset by an increase in the capital share. Barkai calculates payments to capital as the product of the required rate of return on capital and the value of the capital stock. He documents a large decline in the capital share and a large increase in the profit share in the US non-financial corporate sector over the past 30 years and shows that the decline in the capital share is robust to many calculations of the required rate of return and unlikely to be driven by unobserved capital. Interpreting these results through the lens of a standard general equilibrium model, Barkai shows that only an increase in markups can generate a simultaneous decline in the shares of both labor and capital and provides reduced-form empirical evidence that an increase in markups plays a significant role in the decline in the labor share. These results suggest that the decline in the shares of labor and capital are due to an increase in markups and call into question the conclusion that the decline in the labor share is an efficient outcome.
The Job Rating Game: The Effects of Revolving Doors on Analyst Incentives

Investment banks often hire credit analysts from rating agencies. A widely held view is that this “revolving door” undermines analysts’ incentives to issue accurate ratings, but if this practice is so corrupt, why do credit rating agencies allow it? In her paper, Elisabeth Kempf (Chicago Booth) provides a possible answer to this puzzle: when it comes to credit rating analysts, the revolving door might not distort but strengthen incentives. Using a hand-collected dataset of the performance and career paths of 245 credit rating analysts at Moody’s between 2000–09, Kempf identifies those who joined an investment bank after working for Moody’s and those who did not leave or went to work for another employer (this she does using their LinkedIn profiles). She then links their career trajectories to the performance of 24,406 ratings issued for securitized finance securities by revolving and non-revolving analysts from 2000-09, prior to the enactment of Dodd-Frank. She shows that the ratings by analysts who eventually move to investment banks are on average more accurate than the ratings by other analysts who rate similar securities at the same point in time. A notable exception is the small fraction of securities underwritten by their future employers, where revolving analysts do not outperform. Overall, Kempf’s findings suggest that the revolving door may, on average, strengthen rather than distort analysts’ incentives to issue accurate ratings.
When Harry Fired Sally: The Double Standard in Punishing Misconduct

In this highly cited paper, Amit Seru (Stanford University) and coauthors Mark Egan (University of Minnesota) and Gregor Matvos (Chicago Booth) examine gender discrimination in the financial advisory industry. They study firm discipline following missteps (a less salient mechanism for discrimination) and find substantial differences in the punishment of misconduct across genders. Their research shows that male advisers are more than three times as likely to engage in misconduct: on average, one in 11 male financial advisers have records of past misconduct, compared to only one in 33 female advisers. Relative to women, men are three times as likely to engage in misconduct, are twice as likely to be repeat offenders, and engage in misconduct that is 20 percent costlier. Yet, female advisers face much more severe punishments at both the firm level and the industry level following an incidence of misconduct. Despite engaging in less costly misconduct and despite a lower propensity towards repeat offenses, female advisers are also punished more severely. Following an incidence of misconduct, female advisers are 20 percent more likely to lose their job and 30 percent less likely to find new jobs relative to male advisers. Their evidence suggests that the observed behavior is not driven by productivity differences across advisers. Rather, they find supporting evidence for taste-based discrimination. They also find that female advisers are more likely to be punished if their boss is a man. Firms with greater percentages of male executives/owners at a given branch tend to punish female advisers more severely following misconduct and also tend to hire fewer female advisers with past records of misconduct.
In a paper that provides a unique view into Russia’s news market, Andrey Simonov and Justin Rao explore the following questions: Does the fact that Russian readers consume news produced by government-controlled (GC) entities, even though they have access to independent sources, imply a demand for pro-government bias in news? Or is it that perhaps consumers enjoy other aspects of GC news outlets, such as quality and coverage of issues, that are non-contentious? To answer these questions, Simonov (a Stigler Center Bradley Fellow who joined the faculty at Columbia Business School in fall 2017) and Justin Rao (Microsoft Research) examine consumers’ demand in the Russian online news market. They use publication records of the top 48 online news outlets to characterize the methods of government control in the news and identify the news that is sensitive for the government. Simonov and Rao then use temporal variation in the amount of sensitive news and click-level browsing panel data to estimate the demand for news. They find the average consumer prefers news with less pro-government bias, but substantial heterogeneity exists across consumers. In particular, preferences of frequent news consumers differ from the rest of consumers. In a counterfactual simulation, they show that GC news outlets would have higher market shares in the absence of control. At the same time, GC news outlets maintain the majority of their readers when control is imposed, suggesting that control is effective.
When managers actively oppose shareholder proposals, are they acting in the best interest of shareholders at large or their own private interests? Managers often argue that shareholder proposals are harmful to firm value because they are uninformed or opportunistic, while activists tend to argue that managerial opposition is self-interested and proposals increase firm value by counteracting managerial agency problems. In their paper, John Matsusaka (University of Southern California) and coauthors Oguzhan Ozbas (University of Southern California) and Irene Yi (University of Southern California) try to answer the question by examining stock price movements following SEC no-action letter decisions to provide evidence on managerial motives. Relative to previous studies that are limited by an inability to identify precisely when investors become aware of a proposal, their new approach is to study a well-defined event date at which the SEC makes an uncertain and expressly value-neutral decision to block or allow a proposal to go forward, allowing causal estimates of the value consequences. After finding that the market embraces the shutting down of proposals opposed by managers, their conclusion is that managers are typically acting responsibly, as opposed to acting in their self-interest. They find that over the time period from 2007–16, the market reacts positively when the SEC permits a proposal to be omitted from the proxy, suggesting that investors agree with managers that these proposals are value-destroying attempts.
Public Policy and the Initiative and Referendum: A Survey with Some New Evidence

This paper, written by John G. Matsusaka of the University of Southern California, surveys the extensive literature regarding the effects of referendums and public initiatives on public policy and draws two main conclusions. First, contrary to the persistent notion that referendums and other forms of direct democracy lead to chaos, voters actually tend to make reasonable, even conservative choices, especially when it comes to issues like government spending or borrowing. And secondly, direct democracy better represents the will of the majority and therefore might also be better able to counteract the power of special interests over policymaking. When voting on specific policies, particularly fiscal policies, referendum voters tend to be more conservative than their elected representatives. While initiative American states and Swiss cantons have supported lower spending in the past 50 years, ballot initiatives have also driven up spending in cities. This, Matsusaka suggests, indicates that officials at the state (and canton) level tend to spend more than voters would like, whereas on the local level, politicians tend to spend less than voters would like. Ballot initiatives are consistently associated with more conservative social policies as well. Matsusaka also finds that US states with initiative process policies are more likely to be congruent with the majority opinion of the electorate compared to states without the initiative, which suggests that direct democracy allows the majority to counteract the power of special interests.

When Do Legislators Follow Constituent Opinion? Evidence from Matched Roll Call and Referendum Votes

This paper investigates how often and under what conditions legislators vote in accordance with constituent opinion. How often do politicians stray from the opinion of the majority and what motivates them to do so? Matsusaka (University of Southern California) aims to answer the question by offering a new empirical approach to measuring congruence between public policy and public opinion. The main innovation measures constituent opinion by using referendum election returns. For this paper, he analyzed a sample of 28 referendums held between 2000-16 in nine states that allow citizens to challenge newly approved state laws through referendums. Matsusaka then examines 3,555 roll call votes associated with these referendums in state legislatures. The referendums covered fiscal, political, and social issues, from high-profile issues of national importance like minimum wage and same-sex marriage to more localized issues like the mascot of the University of North Dakota. Matsusaka finds that legislator roll call votes were congruent with the opinion of a majority of their constituents 65 percent of the time. However, when legislator preferences differed from district opinion on an issue, legislators voted congruent with district opinion only 29 percent of the time. The data do not show a reliable connection between congruence and competitive elections, term limits, campaign contributions, or media attention, suggesting that legislators vote their own preferences, which is most in line with the citizen-candidate model.
Will the Market Fix the Market? A Theory of Stock Exchange Competition and Innovation

Can the market adopt new market designs, such as frequent batch auctions (FBA), that address the negative aspects of high-frequency trading? In the paper “Will the Market Fix the Market? A Theory of Stock Exchange Competition and Innovation,” coauthored with Robin Lee (Harvard University) and John Shim (Chicago Booth), Chicago Booth Professor Eric Budish attempts to address this question by constructing a new model of stock exchange competition. The paper is a follow-up to a 2015 paper coauthored with Shim and Peter Cramton (University of Maryland), in which Budish focused on the arms race in high-frequency trading (HFT), arguing that many of the negative aspects of HFT are in fact symptoms of flawed market design.

Budish outlined the paper’s main conclusions during an AEA/AFA joint luncheon address. Budish et al.’s model shows that under the current market design, competition among the 12 stock exchanges that operate in the US (as of early 2017) is fierce, but also that exchanges have market power in the sale of exchange-specific speed technology from which they earn economic rents. The authors use the model to study the private and social incentives for market design innovation, finding that if a new exchange enters with a market design that eliminates latency arbitrage, it would win market share and tip other exchanges toward adopting the new design. The private returns to introducing the new design, they find, are zero for a de novo entrant and negative for an incumbent, in contrast with social returns that are large. The authors propose a circumscribed public policy response that would tip the balance of incentives and encourage the “market to fix the market.”
Banks’ Voluntary Disclosures in Response to Shocks

The 2007-09 financial crisis demonstrated that bank stakeholders (regulators, market participants, and funding providers) need high-quality information about banks’ investments, capital and funding structure, and risk-taking activities. Banks’ voluntary disclosures—such as the management discussion and analysis (MD&A) in SEC filings and analyst conference calls—are rich primary sources of such information. However, to date, we have little understanding of the role that these information sources played in the financial crisis. Over the past year, John Gallemore, Anya Kleymenova, and Yao Lu (all at Chicago Booth) have used textual analysis techniques to construct a rich and novel dataset of bank disclosures from SEC filings and analyst conference calls covering the period from 1994 to 2016. As a first step, they provide descriptive evidence of the nature of voluntary disclosures by studying the actual information disclosed. Furthermore, they are currently exploring how these disclosures vary across banks and over time by investigating disclosure changes when financial institutions experience shocks to their information environment and disclosure regime such as deregulation, regulatory changes, M&A activities, and changes in management.

In a follow-up project, they will examine the economic effects of these voluntary disclosures during the 2007-09 financial crisis. For example, they plan to study whether banks with better quality disclosures cut lending less, contribute less to the systemic risk during funding shocks, or are less likely to require recapitalization through TARP or liquidity support through the discount window during the financial crisis. Overall, they are interested in understanding whether banks with higher quality, more informative disclosures experience better or worse economic outcomes during the financial crisis. These findings would have key policy implications for financial and banking regulators. On the one hand, if more informative disclosures lead to better economic outcomes (for example, lower funding costs or lower risk of failure), implementing further disclosure requirements might be beneficial. On the other hand, finding that higher quality disclosures lead to greater problems, such as runs by corporate credit line borrowers or wholesale funding providers, would suggest that policymakers might need to consider decreasing bank transparency to outsiders during crisis periods.
As part of its mission to support and promote innovative research, the Stigler Center launched the PhD Dissertation Awards in 2016-17. The award is open to PhD students in their third, fourth, or fifth year who are in the process of writing a dissertation about the political, economic, and cultural obstacles to better working markets.

Three PhD students were selected for the inaugural Stigler PhD Award and four were designated as Bradley Fellows. The students were selected for their academic excellence and rigorous research.

**STIGLER PHD AWARD WINNERS**
- **Simcha Barkai**, Joint Program in Financial Economics, University of Chicago Economics and Chicago Booth
- **Krisztina Orban**, Economics, University of Chicago
- **Natasha Piano**, Political Science, University of Chicago

**BRADLEY FELLOWS**
- **Silvia Beltrametti**, Law, University of Chicago Law School
- **Matthias Breuer**, Accounting, Chicago Booth
- **Simone Lenzu**, Economics, University of Chicago
- **Andrey Simonov**, Quantitative Marketing, University of Chicago
John G. Matsusaka is Charles F. Sexton Chair in American Enterprise in the Marshall School of Business, Gould School of Law, and Department of Political Science at the University of Southern California, and Executive Director of the Initiative and Referendum Institute at USC. He received his PhD in economics from the University of Chicago, and has held visiting appointments at the Hoover Institution at Stanford University, UCLA, Caltech, and the University of Chicago. His research focuses on the financing, governance, and organization of corporations and governments. He has published numerous scholarly articles, served as a consultant for the White House Council of Economic Advisers, and is the author of *For the Many or the Few: The Initiative, Public Policy, and American Democracy* (University of Chicago Press, 2004). From 2007-13, he served as vice dean for faculty and academic affairs in the USC Marshall School of Business.

During his time at the Stigler Center, Matsusaka published three working papers: “Why Do Managers Fight Shareholder Proposals? Evidence from SEC No-Action Letter Decisions,” (cowritten with Oguzhan Ozbas and Irene Yi) about managers who resist shareholder proposals; “Public Policy and the Initiative and Referendum: A Survey with Some New Evidence,” in which he surveyed the extensive literature regarding the effects of referendums and public initiatives on public policy; and “When Do Legislators Follow Constituent Opinion? Evidence from Matched Roll Call and Referendum Votes,” in which he investigated how often and under what conditions politicians stray from their constituents’ opinions. Matsusaka also held three stand-alone, interrelated lunch seminars on direct democracy as a solution to political populism.
Mara Faccio is Hanna Chair in Entrepreneurship and professor of finance at Purdue University’s Krannert School of Management. Her research focuses primarily on international corporate finance, family firms, mergers and acquisitions, and corporate political connections. Her work has been published in *American Economic Review*, *Review of Financial Studies*, *Financial Management*, *Journal of Business*, *Journal of Corporate Finance*, and the *Journal of Financial and Quantitative Analysis*, among others.

Alongside the projects Faccio worked on during her time at the Stigler Center was a working paper (coauthored by Zingales) that examined the political factors that shape competition in the wireless sector in the United States and around the world. In the paper, titled “Political Determinants of Competition in the Mobile Telecommunication Industry,” the authors compare the wireless industries in Germany, Denmark, and the United States. They find that pro-competition policies, such as number portability, have a significant effect in reducing concentration and prices. Comparing price levels, they find that the monthly revenue per unique subscriber in the United States is considerably higher than in Germany and Denmark. Each year, US mobile consumers pay $280 more than German customers and $189 more than Danish customers.

Viktar Fedaseyeu is an assistant professor at Bocconi University’s Department of Finance. His research interests are in the areas of corporate finance, political economy, and household finance. His recent work focuses on corporate governance and political economy, with an emphasis on how economic interests affect political preferences. In addition to his appointment at Bocconi, Fedaseyeu is also a visiting scholar at the Payment Cards Center at the Federal Reserve Bank of Philadelphia. During his time at the Stigler Center, Fedaseyeu participated as a discussant in the Stigler Center Political Economy of Finance Conference and also presented research at the Stigler Center PhD lunch workshop titled “Fracking, Earthquakes, and Media Capture.”

MARA FACCIO
Hanna Chair in Entrepreneurship & Professor of Finance, Krannert School of Management at Purdue University

VIKTAR FEDASEYEU
Assistant Professor, Department of Finance, Bocconi University
George J. Stigler joined the faculty of the University of Chicago Booth School of Business and the Department of Economics at the University of Chicago in 1958. This event, and the arrival two years later of Merton Miller, is widely recognized in establishing Chicago Booth as a world leader in academic research, as well as making it a full partner in an extraordinarily fruitful cooperative research enterprise with the university’s Department of Economics and Law School.

Stigler was one of the great economists of the 20th century. He made seminal contributions to the economic theory of information and oligopoly, as well as to the economic analysis of government regulation and the public sector. Stigler received the profession’s highest honors, including the presidency of the American Economic Association and a Nobel Memorial Prize in Economic Sciences. His 1982 Nobel Prize was the first awarded to an economist whose primary appointment was in a business school.
40 Years of Cutting-Edge Research on the Political Economy of Markets