

Media, Development, and Institutional Change

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Chapter 1 – The Big Picture: Media, Development, and Institutional Change

Following the election of President Alberto Fujimori in July 1990, Vladimiro Montesinos was named chief of the *Servicio de Inteligencia Nacional (SIN)*, Peru's national intelligence service. Prior to this appointment, Montesinos had been a captain in the Peruvian army, an aid to the army chief and prime minister of Peru, and a private lawyer. In his position as chief of *SIN*, Montesinos served as Fujimori's chief advisor and had near unlimited power. Indeed, many considered Montesinos to be more powerful than the president in the daily operations of Peru. In addition to repressing political opponents through threats and violence, Montesinos was also involved in embezzlement, bribery and drug trafficking. The extent and magnitude of Montesinos's corruption became evident in 2000.

In September 2000, a video tape surfaced of Montesinos paying a bribe of \$15,000 to opposition political leader, Alberto Kouri, to defect and support President Fujimori. Quickly thereafter, political opponents of Montesinos aired the scandalous footage. At first the only television channel in Peru to repeatedly broadcast the video of Montesinos' corruption was Channel N, the only private television channel in the country not on Montesinos' payroll. However, as word of the video spread, other television stations, including those previously under Montesinos' control, began airing the video as well.

In addition to his meeting with Kouri, Montesinos had videotaped himself in meetings with judges, political leaders and members of the media, bribing them as well. Following the broadcast of the Montesinos-Kouri video, these other videos of Montesinos' corruption surfaced and also aired on Peruvian television. These public broadcasts, which became known as "vladivideos," led to the downfall of the Fujimori regime and the end of Montesinos's reign as

chief of the *SIN*. Fujimori fled to Japan while Montesinos fled to Venezuela. Eventually, authorities arrested Montesinos who returned to Peru where the government convicted him of the “usurpation of authority” and later for dealing illegal arms.

The fall of Alberto Fujimori and Vladimiro Montesinos illustrates the potentially pivotal role of the media in checking the abuses of political agents. The airing of the vladivideos single handedly led to the demise of Fujimori and Montesinos and their far-reaching web of corruption. The importance of media as a check on government corruption and predation appears even more clearly when one compares the magnitude of the bribes Montesinos paid to judges, politicians and members of the media.

Economists John McMillan and Pablo Zoido (2004) analyzed these bribes and found that the typical bribe Montesinos paid to a television channel owner was nearly one hundred times greater than the bribe he paid to a politician, which was slightly greater than what he paid to judges. Further, while the typical bribe paid to newspaper owners was less than that paid to the television channel owners, it was still larger than what Montesinos paid to judges and politicians. If Montesinos’s pattern of bribery tells us anything, it tell us, as McMillan and Zoido conclude, that the strongest threat to government power in Peru was in fact the media.

In addition to highlighting the role of media as a check on government actors, the Montesinos story is significant because it highlights the importance of a free media as a mechanism of social change. As mentioned above, the initial video of the Montesinos-Kouri meeting was aired on Channel N, a small private Peruvian cable station, and the only cable channel Montesinos had not bribed. At the time, Channel N had a relatively small market share – less than 5% – with a subscription base only in the tens of thousands (Bowen and Holligan, 2003: 332-337). This is probably part of the reason Montesinos did not bother bribing its

owners. Despite its small market share, Channel N's decision to repeatedly show the Montesinos bribery video was the catalyst for the Fujimori government's eventual downfall. Political activists overcame Channel N's small market share by setting up televisions in the streets so that passers-by could see the video. Only because Channel N was free from state interference was it able to engage in investigative journalism and expose Montesinos's corruption by airing the video. This suggests that even when the media industry is heavily influenced by the state, it can still be an important mechanism of change.

Channel N's broadcasting of the Montesinos-Kouri tape initiated a public backlash against the rampant corruption of the Fujimori government. In this sense, the media served as a coordination mechanism for the Peruvian population. The repeated public airings of the vladivideos created common knowledge of the government's corruption, leading to a concerted response against such behavior.

To understand the importance of media as a coordinating-enhancing institution it is important to recognize that the allegations of rampant Peruvian public sector corruption evidenced in the video of the Montesinos-Kouri meeting were nothing new. Previous accusations, however, often lacked hard evidence, allowing Montesinos to discredit them. As a result, before the public airing of the vladivideos Peruvian citizens had little incentive to respond in a concerted effort against the Fujimori government's corruption. Any one citizen who considered reacting against the government could not be sure that other citizens would join him. Citizens suffered from a "coordination failure" because they could not be sure what others would do (Hardin 1999, Weingast 1995, 1997). One, or only a few, citizens reacting against the government would have no effect. Further, if only a handful of citizens agitated for change,

Montesinos could have easily identified them and would likely have violently silenced the dissenters.

The public airing of the vladivideos solved this coordination problem by creating common knowledge of Montesinos's corruption. Because of the repeated media broadcast of the tape, Peruvian citizens could be confident that others knew about the government's corruption, and that these other citizens knew that they knew about the corruption, and so forth. Further, the bribery payment shown on the video provided incontrovertible evidence of Montesinos's political abuse. The common knowledge created by the public broadcasts of the vladivideos enabled Peruvian citizens to coordinate on a common reaction to the Fujimori government's misdeeds (McMillian and Zoido 2004: 20-21).

Despite the clear importance of media freedom in constraining the predatory inclinations of government officials and generating the common knowledge and coordination required for social and institutional change, only a minority of the world's countries have what could be described as a genuinely free media. Media freedom is the degree to which governments control or influence the flow of media-provided information reaching their citizens. Inhabitants in developed countries often take media freedom for granted and focus on perceived ideological biases in media reporting (see for instance Goldberg 2003 and Kuypers 2002). However, in most of the world the central issue is not reporting bias but a more fundamental issue of state control of the media in general.¹ In countries where media is not free, the issue is one of the extent and magnitude of state ownership and government manipulation of the media through threats, bribes and financial pressures.

Freedom House produces an annual *Freedom of the Press* report that measures media freedom in countries across the globe. The Freedom House index measures countries' media

freedom by considering their legal environment, which looks at laws, statutes, constitutional provisions, and regulations that enable or restrict the media's ability to operate freely in a country; political environment, which evaluates the degree of political control over the content of news media in each country (such as editorial independence, official or unofficial censorship, harassment or attacks against journalists, etc.); and economic environment, which includes the structure of media ownership, media-related infrastructure, its concentration, the impact of corruption or bribery on news media content, and the selective withholding or bestowal of subsidies or other sources of financial revenue on some media outlets by the state. The media considered in the index includes TV, radio, newspaper, and the Internet. On the basis of their total scores, Freedom House ranks each country's media as either "Free," "Partly Free" or "Not Free." This ranking provides some means of quantifying the extent to which each country permits the free flow of information and also allows for comparative and trend analysis.

Of course, any attempt to provide an aggregate measure of media freedom will be imperfect and fail to capture all relevant aspects of the topic under study. For instance, the *Freedom of the Press* report does not take into account the quality of the media or ethical standards of journalists. Despite these imperfections, Freedom House's annual report provides a widely accepted means of considering media freedom at the global level. Table 1 provides an overview of media freedom by region for 2007.

| Region | Status | Number of Countries | Percentage of Regional Total |
|---|-----------------------|----------------------------|-------------------------------------|
| Sub-Saharan Africa | | | |
| | Free | 8 | 17% |
| | Partially Free | 19 | 39% |
| | Not Free | 21 | 44% |
| Americas | | | |
| | Free | 17 | 48% |
| | Partially Free | 16 | 46% |
| | Not Free | 2 | 6% |
| Asia-Pacific | | | |
| | Free | 16 | 40% |
| | Partially Free | 10 | 25% |
| | Not Free | 14 | 35% |
| Middle East & North Africa | | | |
| | Free | 1 | 5% |
| | Partially Free | 2 | 11% |
| | Not Free | 16 | 84% |
| Central and Eastern Europe (former Soviet Union) | | | |
| | Free | 8 | 28% |
| | Partially Free | 10 | 36% |
| | Not Free | 10 | 36% |
| Western Europe | | | |
| | Free | 24 | 96% |
| | Partially Free | 1 | 4% |
| | Not Free | 0 | 0% |
| TOTAL – GLOBAL | | | |
| | Free | 74 | 38% |
| | Partially Free | 58 | 30% |
| | Not Free | 63 | 32% |

Table 1: Global Press Freedom by Region - 2007²

As Table 1 indicates, in 32 percent of the world’s countries the media is “Not Free.” In another 30 percent of the globe media is only “Partly Free.” North Africa and the Middle East have the

lowest levels of media freedom; 84 percent of the countries in these regions are rated as “Not Free.” In contrast, countries in Western Europe fair the best in terms of media freedom; 96 percent of the countries in this region have a “Free” media. Further, Western Europe is the only region where a majority of countries have a media rated as “Free.” In all other regions a majority of countries are either “Partially Free” or “Not Free.” In terms of population, the 2007 Freedom House report found that only 18 percent of the world’s inhabitants enjoy a “Free” press. In contrast, 39 percent live under a “Partly Free” press, and 43 percent live under a press that is “Not Free.”

To provide some insight into media freedom over a number of years, Table 2 provides time series data for global media freedom between 1990 and 2007.

| Survey Year | Not Free | Partially Free | Free | Total Countries Surveyed |
|----------------------------|-----------------|-----------------------|-------------|---------------------------------|
| Percentage of Total | | | | |
| 1990 | 46.5 | 18.2 | 35.2 | 159 |
| 1991 | 39.5 | 21.7 | 38.9 | 157 |
| 1992 | 28.4 | 30.2 | 41.4 | 162 |
| 1993 | 28.2 | 33.9 | 37.9 | 177 |
| 1994 | 30.1 | 33.9 | 36 | 186 |
| 1995 | 32.6 | 33.7 | 33.7 | 187 |
| 1996 | 32.1 | 33.7 | 34.2 | 187 |
| 1997 | 33.2 | 32.6 | 34.2 | 187 |
| 1998 | 34.9 | 29 | 36 | 186 |
| 1999 | 35.5 | 28 | 36.6 | 186 |
| 2000 | 35.5 | 27.4 | 37.1 | 186 |
| 2001 | 33.2 | 28.3 | 38.5 | 187 |
| 2002 | 32.8 | 26.9 | 40.3 | 186 |
| 2003 | 35.2 | 24.4 | 40.4 | 193 |
| 2004 | 37.3 | 24.9 | 37.8 | 193 |
| 2005 | 35.6 | 25.8 | 38.7 | 194 |
| 2006 | 34.5 | 27.8 | 37.6 | 194 |
| 2007 | 32 | 30 | 38 | 195 |

Table 2: Global Press Freedom – 1990 – 2007³

The data in Table 2 indicate that media freedom, or the lack thereof, has remained relatively consistent over the globe for the past seventeen years. In general, approximately a third of the world has been characterized by a media that is “Not Free” while another third is characterized by a media that is “Partially Free.” The data in Tables 1 and 2 illustrate that for most countries in the world media freedom cannot be taken for granted.

The absence of medium freedom carries significant costs. This was highlighted in the World Bank’s, *World Development Report 2002: Building Institutions for Markets*, which dedicated a chapter to the importance of media freedom for economic and human development (2002: 181-192). The topics explored in the chapter included how a free media could reduce corruption, assist in public health efforts and improve education. Without a free media, achieving these outcomes is dramatically more difficult.

The importance of media as a mechanism for monitoring government and generating institutional change, coupled with the fact that media in two-thirds of the world are either “Partly Free” or “Not Free,” suggests that it is critical to understand the factors influencing the effectiveness of media. The purpose of this book is to contribute to our understanding of media as it relates to economic development and institutional change. Our goal is to analyze the specific factors that constrain the effectiveness of media as a check on government. Further, we explore the process of institutional change and how media serves as a coordination mechanism in this process. Our study considers the media in the broadest sense including the press, television, and radio, as well as more recent media mediums, such as the Internet.

To pursue this goal, we ask some fundamental questions about how economics can explain the role of media in economic development and institutional change. How is media connected to the fact that some countries adopt policies that promote economic development while others fail to do so? What factors influence the effectiveness of media as a check on government? In what ways does the government manipulate media to constrain its effectiveness as a check on government activities? How does media contribute to the evolution of existing institutions and the adoption of new institutions? Finding answers to these questions is critical to understanding the role of media in economic development and institutional change.

We are fully cognizant of the fact that economic development is a vast topic, both theoretically and empirically. We cannot possibly hope to cover all of its nuances or angles. Instead, our goal is to analyze the role that media plays in the successful adoption of policies and institutions that foster economic progress. It is our hope that our analysis of media will contribute to our understanding of one of the many ingredients in the complex recipe for economic development.

Economic Analysis of Media and Development

The study of media has a long and varied history. The broader field of “media studies” has historically drawn on tools and methods from disciplines as diverse as sociology, social theory, communication theory, literary theory, cultural studies and anthropology to study media’s various aspects. Political scientists have studied the role of media in the context of the formation of public opinion and as a means of informing the electorate (see Bartels 1993, Briens and Wattenberg 1996 and Mondak 1995). The subfield of “media economics” is relatively young but has increased in popularity over the past two decades. Media economics applies the tools of

economics to study the industrial organization of the media and explores both theoretical and empirical questions including media regulation, ownership structures and market share, intellectual property rights, innovation, and advertising, among other topics (see for instance Albarran 2002, Alexander et al. 2003 and Doyle 2002).

For the purposes of our study, we are most concerned with the literature that applies the theories and methods of economics to analyze the connection between media and economic development. This area of research is growing but still in its early stages. The existing literature in this area can be broken in to two general categories. The first category focuses on the role of media in negotiating the principal-agent problem that citizens confront vis-à-vis their political rulers. It investigates the media as a mechanism that checks government actors. The second category focuses on the economic implications of different media ownership structures. It examines how the features of the media industry affect economic and human development.

Nobel Laureate Amartya Sen (1984, 1999) was the first economist to discuss the importance of media as a means of checking government. Sen addressed the issue of media in connection to the prevention of famines with a specific focus on India. Along these lines, Sen notes that “a free press and an active political opposition constitute the best early-warning system a country threatened by famines can have” (1999: 181). His basic argument is that a free press, coupled with an open and stable democracy, pressure political actors to prevent the outbreak of famines. The underlying logic is that in a politically competitive environment, political opposition will have the incentive to communicate the threat of famine to the public to weaken support for incumbents. A free media is the main means of communicating this information to the masses. Failure by the party in power to act will lead to a political backlash at the voting booth, leading political agents to faithfully serve their citizens.

For Sen, open political competition *and* a free press are both vital for the prevention of famines. The information provided by the press will not be effective unless there is political competition so that incumbents can be voted out of office. Likewise, without a free press to provide information to voters, political competition will be ineffective because there is no means of publicly disseminating information about incumbents' performance.

Other economists have built on Sen's initial work. Besley and Burgess (2002) provide an empirical test of Sen's hypothesis regarding famine, democracy and media. Relying on data from the sixteen major Indian states, they explore whether governments are more responsive when there is more political competition and a greater number of newspapers. India's sixteen states provide an interesting case because there is variance among their vulnerability to famine, as well as in their newspaper circulation and political competition.

Besley and Burgess find that Sen's thesis does in fact hold. A "1 percent increase in newspaper circulation is associated with a 2.4 percent increase in public food distribution and a 5.5 percent increase in calamity relief expenditures" (2002: 1435). Further, they find that the greater the circulation of a newspaper, the greater is the government's response to a crisis. They also find that greater levels of public food distribution are associated with greater political competition. Consistent with Sen's pioneering hypothesis, Besley and Burgess conclude their analysis by noting that "...representative democracy and the development of free and independent regional presses appear as key factors in ensuring protection for vulnerable citizens" (1446).

In a subsequent paper, Besley and Prat (2006) explore how collusion between the government and the media can undermine the effectiveness of media as a check on the behavior of political actors. They conclude that media capture has two major negative effects on the well-

being of citizens. First, where the media is captured, the grabbing hand of the state will tend to engage in more rent extraction when media capture exists because political actors are less concerned that they will be caught by the public. Second, where government controls the media there will be less political turnover because voters will be unable to punish elected officials due to a lack of information about their ineffectiveness.

While this research focuses on the role of media as a mechanism for monitoring the actions of political actors, a second strand of literature explores the economic implications of various forms of media ownership. Djankov et al. (2003) carried out the main research in this area, which asks: who owns the media? In order to explore this question, the authors develop a dataset on media ownership patterns in 97 countries. The data display two dominant forms of media ownership in the world – state ownership and private ownership in the form of controlling families. The authors use this data to analyze two competing hypothesis regarding media ownership.

The first hypothesis is the public interest, or Pigouvian, theory which argues that state ownership of the media is desirable because information is a public good that exhibits increasing returns. On the one hand, once information is produced it is costly to exclude people from consuming it. On the other hand, although there are high fixed costs to gathering and distributing information, once these initial costs are covered, the marginal cost of distributing information is extremely low.

The second hypothesis of media ownership is rooted in a public choice theory. In contrast to the public interest theory of the media, the public choice view contends that state owned media will tend to manipulate information to benefit those currently in power. This manipulation will skew reported information reported in favor of incumbents, which prevents

voters from making informed decisions. For this reason, the public choice view concludes that private ownership is preferable to state ownership.

Djankov et al.'s analysis supports the public choice view. Specifically, they find that higher levels of state ownership are associated with lower levels of primary school enrollment, lower levels of political rights and lower levels of civil liberties. Further, countries with higher levels of state ownership of media tend to be poorer and more autocratic, and have higher levels of corruption. These results hold even after controlling for differences in economic development, education, political competition, state intervention in the economy, ethno-linguistic heterogeneity and latitude.

Our goal in this book is to contribute to the existing literature exploring the connection between media and economic development. While the existing literature provides important insights into this connection, it is far from complete. For instance, while it is clear from existing research that media can serve as a check on government, we still lack a complete understanding of how media can provide the incentive for elected officials to adopt policies that are conducive to economic development. Further, while the existing literature discusses the perverse effects of media capture and state ownership of the media, there has been little discussion of how the state actually manipulates media-provided information. Finally, the connection between the media and institutional change has yet to be explored. How does media serve as a mechanism that facilitates the process of economic and social change? More specifically, what is the precise channel connecting media, institutional change, and development? Our analysis seeks to fill these gaps.

Is There Consensus for a Free and Privately Owned Media?

While the existing literature certainly points to the desirability of privately-owned media, it would be a mistake to conclude that there is a general consensus on this issue. The appearance of consensus that a private and free media is preferable to state ownership overlooks the fact that several arguments exist for government intervention and ownership of the media. These arguments are very much part of the ongoing debate about the desirability of privately owned media.

For instance, consider the growing media economics literature discussed at the beginning of the previous section. In exploring the economic aspects of information and the structure of the media industry, some of this literature notes how the unregulated market may fail to provide the “optimal” amount of information (Doyle 2002). The market failures associated with information and media include the public good and externality characteristics of information and the alleged natural monopoly aspects of the media industry. As with market failure stories for other goods and services, the application of this logic to the media market at least in principle leaves room for government intervention to overcome these market failures.

There is an important tension that emerges from these market failure arguments for government intervention in media. To the extent that the market for media does suffer from the various market failures there is, at least in theory, some scope for government intervention to serve as a corrective. At the same time, as the literature on media and economic development discussed above indicates, state ownership or regulation of media can lead to many perverse economic outcomes. Of course the extent of government intervention in the media industry, if any at all, is still an open issue. Nonetheless, this should highlight the fact that the “freeness” of the media industry is still very much open for debate. We will address some of these market failure arguments for government intervention in the media in the concluding chapter.

Traditional political economy, which emphasizes power relations in the economic, political and social spheres, has also produced a large literature analyzing the media (see for instance, Bagdikian 1990, Herman and Chomsky 1988 and Golding and Murdock 1997). This literature tends to be skeptical of media that emerges on the free market. This pessimism stems from the view that two main groups of capitalists – media owners and advertisers – will utilize media as a tool of manipulation of the masses. Those writing in this tradition argue that the media that emerges in a capitalistic system will fail to provide a diversity of information, perspectives and cultural resources to the public.

Solutions to these perceived problems vary widely. Some argue that despite its problems, private media is still preferable given the alternatives. Others call on the state to play an active role in the media industry. There is again no consensus about the desirable extent of government intervention in the media market, with proposals ranging from government regulation of private media, to subsidies to certain media outlets, to outright state ownership of at least part of the media.

Similar to the media economics literature that emphasizes market failure, the traditional political economy literature also highlights the fact that agreement about the desirability of a free media characterized by private ownership is far from reached. As such, sharpening our understanding of the way media influences economic development, as well as how different ownership structures influence the effectiveness of media in this regard, is of the utmost importance.

The Importance of Institutions for Economic Development

Our main focus in this book is on the role of media in economic development. A critical element of economic development is institutions and institutional change. Given this, it is important to clarify the connection between institutions and economic development. Institutions can be understood as the formal and informal rules governing human behavior, and the enforcement of these rules (North 1990). Formal institutions include codified institutions that are intentionally designed. Examples would include state-made constitutions, rules and legislation. In contrast, informal institutions evolve over time and are not the result of intentional design. They include, for example, norms, conventions, mores and what is generally referred to as culture.

The enforcement of both formal and informal institutions can occur through the internalization of certain norms of behavior, the social pressure exerted on the individual by the group, or the power of third party enforcers who threaten to use force against individuals who violate rules. Institutions reduce uncertainty by providing a predictable structure in which people can act. In providing the rules of the game, institutions facilitate economic, social and political interactions. As such, differences in economic outcomes across societies and countries can be attributed to different institutional structures. Moreover, changes in institutions, for better or worse, directly influence changes in economic well being.

Nobel Laureate economist Douglass North (1990) is best known for developing a theory of institutions, as well as analyzing the evolution of institutions and the consequences of those institutions on economic performance. Building on North's initial work in this area there is a growing number of empirical studies that analyze the importance of institutions for economic outcomes. These studies analyze institutional explanations for economic development and compare them with other potential explanations, such as geography, fractionalization and trade integration.

The most well-known empirical work that examines the impact of institutions on economic performance is a series of articles by Acemoglu, Johnson and Robinson (2001, 2002). These authors explore the effect of institutions on income in the ex-colonies. Some of these countries, such as the United States, New Zealand, and Australia, exhibit high levels of economic development. Others, such as the majority of countries in Sub-Saharan Africa, display the reverse.

The authors argue that this distribution of income across the ex-colonies can be explained by the property rights institutions they developed as a result of the different kinds of disease environments that colonizers faced when they colonized them. According to their analysis, the property rights institutions we observe across these countries today were determined by the property rights institutions they inherited from their colonizers. In places like the United States, New Zealand, and Australia, the prevalence of diseases, such as malaria, at the time of colonization was relatively low. Thus, colonizers could settle in these places for long periods of time. Since as inhabitants of these countries colonizers would be subject to the long-run effects of the property rights institutions they created, where they settled more permanently it was in their interest to establish institutions of long-run economic growth, namely well-protected private property rights.

In contrast, in other countries, such as those in Sub-Saharan Africa, diseases like malaria were rampant and posed a serious threat to the lives of colonizers. In these places, colonizers could not settle permanently. This shaped their colonizing strategy in that it created a very short-run time horizon for the colonizers. They sought to get in, extract as many resources as possible, and get out. This led colonizers in these places to establish extractive institutions that poorly protected citizens' private property rights.

The key finding of Acemoglu, Johnson and Robinson's study is that private property rights are the primary determinant of nations' levels of economic development. This is true even after controlling for other potential determinants of income, such as colonizer identity (e.g., British or French), and a slew of geographic variables like latitude, distance from a coast, and climate, which some have argued is responsible for the wealth and poverty of nations (see for instance, Gallup, Sachs and Mellinger 1999; Sachs 2001, 2003).

Building on this work, Acemoglu and Johnson (2005) have gone further in clarifying the type of property institutions that are important for economic development. They point to the fact that there are multiple types of property institutions that may matter for economic development. On the one hand there are what they call "contracting institutions," such as government courts that enforce private agreements between citizens. These institutions are important because they aim to protect the property rights of citizens vis-à-vis one another. On the other hand there are "property rights institutions," such as constraints on the government's ability to seize citizens' property arbitrarily. These institutions are important because they aim to protect the private property rights of citizens against government predation.

Acemoglu and Johnson's (2005) work aims to "unbundle" these two private property-related institutions to see which is more important for economic development. Alternatively, their analysis can be thought of as asking which type of predation—public or private—poses the greater threat to economic development. The conclusion of this study is that what the authors call "property rights institutions"—institutions that restrain government expropriation—are substantially more important than what they call "contracting institutions"—state-provided institutions to prevent private predation—for nearly all aspects of economic development. State expropriation, not predation by private individuals, is more harmful to economic progress, and

thus far more important to prevent. Conversely, institutional restraints that prevent government from violating the private property rights of their citizens are the dominant determinant of economic development.

Other empirical research supports the importance of property rights institutions for economic development as well. For instance, Rodrik, Subramanian and Trebbi (2004) analyze three possible explanations – geography, trade integration and institutions – for differences in income across countries. They conclude that the quality of institutions is the most important factor in explaining differences in income. After controlling for institutions, the authors of this study find that geography has a weak direct effect on income while trade integration has no direct positive effect on income. The findings of this work further support the original empirical research by Acemoglu, Johnson and Robinson (2001, 2002) in this area concerning the primacy of institutions for economic development. Given the importance of institutions in contributing to economic performance, our analysis focuses on the role the media plays in supporting or undermining an institutional structure conducive to development. Of particular interest is how a free versus an unfree media differentially impacts the broader organization of institutions in developing countries.

The Process of Institutional Change

While the existing empirical literature emphasizes the importance of institutions for economic development, much less is known about the process of institutional change. Given the importance of institutions for economic performance, how do quality institutions emerge where they do not already exist? How do countries currently characterized by poor quality institutions turn the corner toward economic progress and development?

Institutions that exist in the current period are the result of past choices and experiences (Boettke, Coyne, Leeson 2008). Along these lines, there is a growing economics literature focusing on institutional “path dependency,” which emphasizes that the way institutions and beliefs developed in past periods constrains set of feasible choices in the current period (North 1990: 93-8, 2005: 51-2). North (2005) places informal institutions, and especially “belief systems,” at the core of the process of institutional change. He notes that “the process works as follows: the beliefs that humans hold determine the choices they make that, in turn, structure the changes in the human landscape” (2005: 23). This indicates that if we wish to understand institutional differences and institutional change, we must start with the “mental models” or belief systems guiding individual actions.

Within this context, institutional change entails shifts in fundamental belief systems. As North (2005) makes clear, individuals rely on an incomplete mental model since they cannot know the full range of possible opportunities that currently exist or will exist in the future. As individuals become aware of alternative courses of actions, they incorporate those possibilities into their mental model. When new alternatives are introduced, or the relative prices of existing alternatives change, mental models are updated and institutions evolve.

Understanding the process of institutional change thus entails identifying mechanisms that change the fundamental belief systems of the members of a society. It is our contention that media is one such mechanism. Given its potential to reach a large number of consumers, the media has the ability to change fundamental belief systems by making them aware of alternative courses of action. The story of the role of media in the downfall of Vladimiro Montesinos that opened this chapter is one example of this logic. The media can provide information that allows individuals to update their belief systems. Media can also produce common knowledge so that

each individual can be confident that others are updating their mental models as well. This allows for widespread coordination around institutional change.

It is important to note that the evolution of belief systems is endogenous and takes place within an existing structure of formal and informal institutions. This existing structure will influence and constrain the evolution of institutions. In order for formal institutions to operate effectively, they must be supported by informal institutions. However, formal institutions – whether supported by informal institutions or not – will influence the evolution of informal institutions.

When there is a disjuncture between formal and informal institutions, the formal institutions will fail to operate in the desired manner. Perhaps the best example of this is the work of Hernando de Soto (1989). In his analysis of the Peruvian economy, De Soto found that there was a large informal economy characterized by well-defined property rights and cooperation. The formal institutions were characterized by extensive corruption and inefficiencies and failed to recognize existing informal institutions. According to de Soto, this disjoint between the formal and informal stifled the Peruvian economy. The purpose of formal institutions, such as courts, is to reduce the costs of interaction and exchange. In the case of Peru, and many other undeveloped countries, the disjoint between the formal and informal has the opposite effect and actually increases the costs of interaction and exchange. Instead of facilitating trade, individuals have to actively avoid the predation of those abusing formal institutions.

While informal institutions constrain the effectiveness of formal institutions, existing formal institutions simultaneously influence and constrain the evolution of informal institutions. They do so by establishing and enforcing the formal rules through which individuals are exposed

to alternative beliefs and possibilities. To understand this point, consider that dictators expend a great deal of resources controlling the media and dissemination of information in their countries. Their aim is to restrict the awareness of the citizens to alternative institutional possibilities. If a dictator prevents those living under him from being exposed to alternative forms of economic, political and social organization, citizens are unable to incorporate those alternatives into their belief systems. Because of this, the evolution of informal institutions, and hence formal institutions, is curtailed.

In both the theoretical and applied analysis of media that follows, we emphasize the importance of media as a mechanism of institutional change. In doing so, we consider the various factors that influence the effectiveness of media in influencing peoples' belief systems and the implications for economic development.

The Outline of This Book

In this book we examine the role of media in economic development. Our treatment is broad and consists of theoretical, qualitative and quantitative analysis. Combining these various approaches and methods provides different perspectives on the problem at hand and hence a more complete understanding of our topic of study.

In the next chapter we develop "The Reformers' Dilemma," a theoretical model of the process of institutional change and economic development. Drawing on some basic concepts from game theory, we clarify the fundamental dilemma facing policymakers in developing countries. We also model the process of citizen coordination around new conjectures and belief systems. We posit that the media is a coordination-enhancing mechanism around institutional change.

Chapter 3 explores several key factors influencing the effectiveness of media. The first factor is the government intervention in the media. As discussed above, much of the existing literature on media and economic development has focused either on media as a check on government or on various media ownership patterns. This literature highlights some of the costs and perverse economic outcomes associated with government ownership of the media. We contribute to this discussion by identifying the specific ways that government manipulates the media and weakens its effectiveness as both a check on government and as a mechanism of change.

We then turn to an analysis of how the legal environment impacts media freedom. Our focus here is on information transparency and the protection of journalists and media employees from direct and indirect coercion. The quality of the media is the next factor that we consider. Specific focus is placed on the importance of journalist standards and ethics for delivering accurate and timely information to consumers. Finally, we consider the economic factors that influence the media. Particular focus is placed on consumer demand and the importance of a private advertising sector for sustainable media independence. Our core argument is that a free media is a critical ingredient in the broader process of economic development. However, while a free media is necessary for economic development, it is not, by itself, sufficient. Relevant information must be available to media outlets and that information must be reported accurately and ethically. Finally, consumers must demand certain types of information in order for media to be effective in contributing to economic development.

The next two chapters provide both empirical and quantitative analysis. Utilizing data regarding Eastern and Central Europeans' political knowledge, Chapter 4, statistically analyzes the relationship between media freedom and citizens' political knowledge. Specifically, this

analysis explores the connection between state ownership of the media, political knowledge and voter turnout. The main finding is that in countries where government has greater control over the media, citizens are more politically ignorant and apathetic. Chapter 5 complements this empirical analysis by presenting three case studies focusing on the role of media in economic development. While the statistical evidence in Chapter 4 establishes general patterns, these case studies allow us to trace the causal mechanisms in more detail, while paying particular attention to the specific context in which media outlets operate and evolve. These two chapters will illuminate the analysis provided in previous chapters.

In the final chapter we conclude by discussing the implications of our analysis. In addition to discussing the implications of a free media for economic development, we provide some clear policy steps regarding the media in developing countries. We also address some of the concerns regarding “market failures” in media and information markets in developing countries.

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¹ This is not to dismiss the issue of bias but rather to highlight that in many countries the central media issue is one of the extent and magnitude of state involvement in the media. For an economic analysis of media driven biases, see Sutter (2004), Mullainathan and Shleifer (2005), and Gentzkow and Shapiro (2006) examine market-driven news biases.

² Source: Freedom House (2007).

³ Source of data: <http://www.freedomhouse.org/uploads/fop/historical/CBGlobal.pdf> and Freedom House (2007).