

Coalition formation and bargaining

one of the strongest objections to those who believe that Coase-style bargaining will reach efficient outcomes is that with imperfect information, such bargaining often results in suboptimal outcomes (Furell 1987).

To convey information about bargaining resolve, fallback position, and so on, there is often recourse to inefficient signals. Bargaining in life is also not a one-shot episode. Each round affects the fallback position for the next. Although the two sides in, say, a labor dispute may not fully realize it, each is solving a complicated dynamic program problem with uncertainty and imperfect information.

strikes are a manifestation of "bargaining" inefficiency in the private sector, the failure to enact Pareto improvements is a manifestation in the public.

The awareness of the dynamic nature of the bargaining game has further repercussions. Legislation can help crystallize some groups, and attenuate the strength of other. It affects the coalitions which are formed, and thereby the outcome of political processes. Participants in the political game today realize this, and hence actions which in the short run might look like a Pareto improvement can look far riskier from a LT, dynamic perspective.

Destructive competition

In market economies, we are used to extolling the virtues of competition. Yet we recognize that in the absence of perfect competition, sometimes destruction can be destructive. In imperfectly competitive markets, firms can get ahead not just by producing a better product at lower costs, but also by raising the costs of their rivals. Destructive competition is most prevalent in zero-sum games where the gains of one are at the expense of another. Political games are particularly prone to this kind of behaviour. Competition in political markets is far from perfect, and the scope for destructive competition is therefore all the greater.

Uncertainty about the consequences of change

Imperfect information can create an impediment to mutually productive bargains. In some models of the stock markets, no trading takes place because of information asymmetries.

These information asymmetries limit trade even when differences in risk preferences and circumstances might, with symmetric information, lead to mutually

⇒ the buyer is never sure whether the seller is willing to sell because of inside info. which lets the seller know that the buyer is overpaying, or whether there are grounds for a mutually beneficial exchange.

This skepticism derives not just from the standard asymmetric info. in eco. models, but also from the fact that many people lack the training or patience to understand the consequences of policies.

the uncertainty about the consequences of policies has an important implication: complicated policies and arguments have little place in political discourse.

The public has neither the background or the patience to digest a complicated message, so this "simplicity constraint" makes it more difficult to put together politically appealing reforms which are Pareto improvements.

Now, the author will discuss steps we can take to build a climate of openness and transparency that allows good policies to be recognized and promoted

① Secrecy vs openness in decision-making

Secrecy aggravates the government failures identified above. First, it makes it harder to establish credible commitments. Second, secrecy aggravates the problem of positional goods and destructive competition. Third, by making information scarce, it contributes both to both the perception and reality of asymmetrical information, and puts into play a dynamic which is more likely to lead to biased and unrealistic information.

The one argument that may have some merit is that hiding information may sometimes provide a tactical advantage in the political bargaining game.

⇒ "Sunshine is the most powerful antiseptic"

↳ There are some discussions which can happen only if secrecy (uranium...).

But the secrecy mind-set plays out even when there appears no rational reasoning for secrecy.

Adversarial vs consensus systems

The political process involves a similar mixture of adversarial and consensus-based systems.

Stiglitz believe that a shift to greater reliance on consensus processes is more likely to lead to Pareto improvements. To see why, let me describe some of the contrasts between both systems.

- Dialogue/debate: consensus requires open dialogue. You need to get people to understand your position and persuade them it is the right one. Adversarial system needs debate. The objective is to win a victory in the political process.

- Nation/private interests: The success of a consensus-based system requires some shared conception of the national interests. The adversarial system only requires that each group express its own interests and these interests be aggregated by voting or some other procedure.

- The third contrast refers to when issues are believed to be settled. In a consensus-based system, an issue is over when everyone has come to a mutually acceptable agreement.

⇒ A consensus-based system is thus able to mitigate some of the problems I discussed earlier.

Michael Bruno (predecessor of Stiglitz) emphasized the importance of consensus building in ending inflation (Bruno, 1993).

Isham et al (1995) found the success rate for rural water projects that involved participation was substantially higher than the success rate for those that did not.

Participation and consensus formation should be valued in their own right and may lead to better outcomes, but this is not necessarily the case, especially where expertise plays a large role.

⇒ Education processes can expand and enhance participation by helping people better understanding the issues.

Incentives for secrecy

Other forces besides special interests and the fear of exposing policy mistakes help maintain the climate of secrecy. Secrecy creates rents, because the hidden information is potentially valuable. Whenever a valuable commodity exists, markets are created.

Less secrecy would not only increase the flow of information; it would reduce the rent-creating and rent-seeking activities which lead to a distorted flow of information.

[...] If instead they had increased the number of stories they would have found that the press and public would come to a better understanding of the deliberative process or, more likely, simply become too bored to raise much of a problem.

Expertise and democratic values

For a large number of issues, expertise is required.

That is why, we have established independent agencies in many areas to move critical parts of decision-making at least slightly further from the political scene. Ultimately, there is political responsibility for the performance. Therefore, there is a consensus that statistics should be collected at some distance from the political process. But what about some central issues of macro policy?

As for monetary policy, its representativeness can be questioned, since not all of its members are even appointed by the president or ratified by the Senate. In either case, how much secrecy should surround the deliberations?

Making financial markets into tyrants

If members of the Federal open market committee discussed their views about monetary policy more openly and more often, the most likely effect would be a clamping of financial market volatility. In a sense, the market for information would be thicker and possibly more stable as each individual's particular pronouncements would matter less.

↳ World Development Report (1997), catalogs the costs of the extreme lack of transparency that is so frequently found in countries with corrupt governments.