

Groupthink and Ideology

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Princeton University

Schumpeter Lecture – Budapest 2007

Two main papers

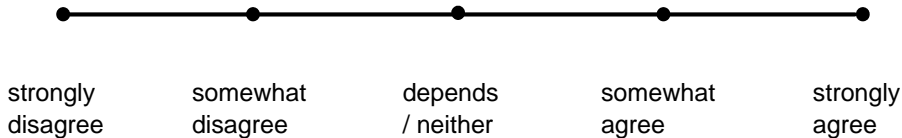
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- “Groupthink and Ideology”. Mimeo, May 2007
- “Belief in a Just World and Redistributive Politics”, with Jean Tirole. *Quart. Jour. Econ.* 2006
- New paper also based on framework developed with **Jean Tirole** in series of papers on belief formation. Psychology-based, information-theoretic approach
- Common building blocks, links. Take / extend here to new economic questions

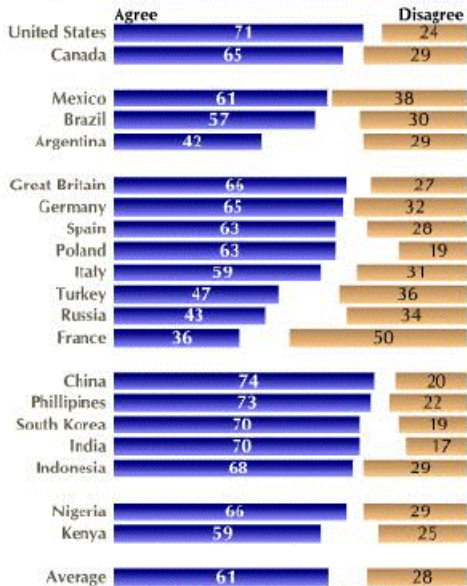
The free enterprise and free market economy is the best system on which to base the future of the world

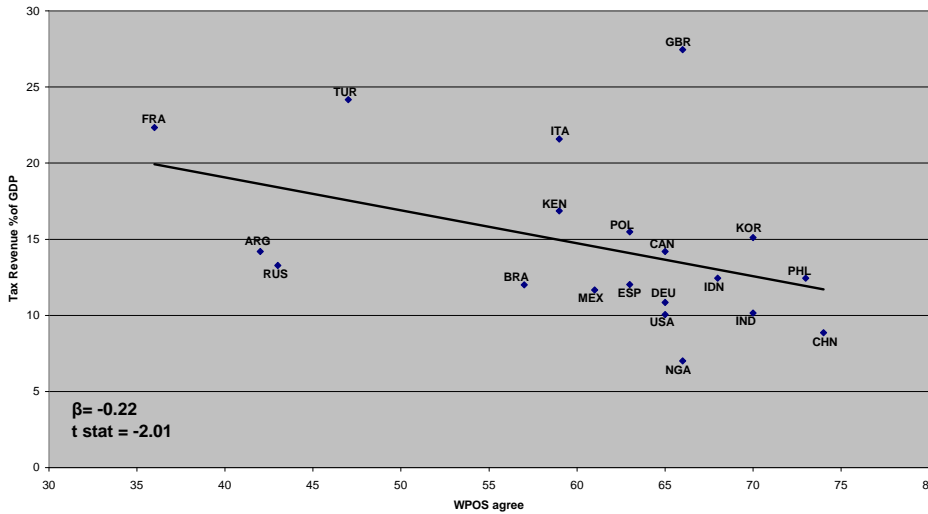
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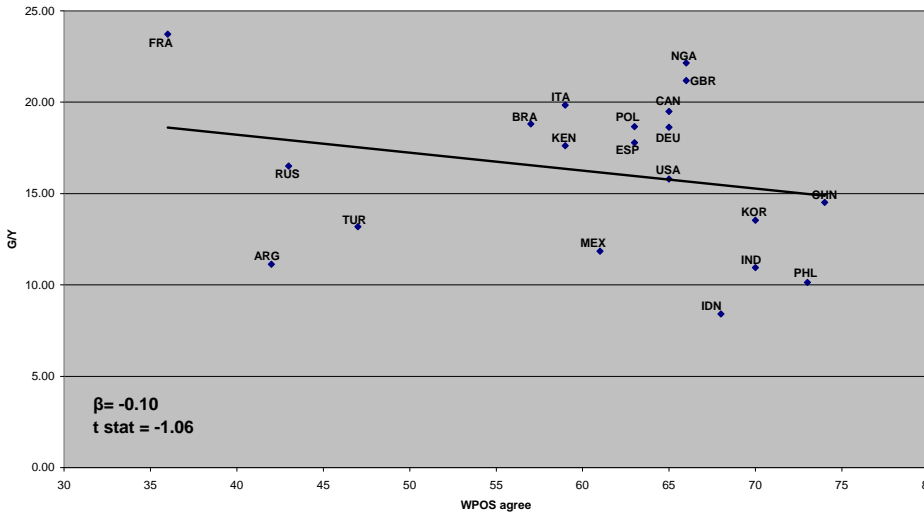


Free Market System

The free enterprise system and free market economy is the best system on which to base the future of the world.







Ideology

Many economically important beliefs about “how the world works”, such as those concerning...

- Role of effort vs. luck of in life outcomes...
- Relative merits of state vs. market, proper scope of government
- Other people: trust, stereotypes
- Religion, culture

Ideology

Many economically important beliefs about “how the world works”, such as those concerning...

- Role of effort vs. luck of in life outcomes...

Piketty 1995), Bénabou-Ok (20001), Fong (2001), Alesina-Glaeser-Sacerdote (2001), Alesina-Angeletos (2005), Alesina-La Ferrara (2005), Bénabou-Tirole (2006), Di Tella-Galiani-Schargrodsky (2007)...

- Relative merits of state vs. market, proper scope of government

Kaiser Foundation (2006), Caplan (2007)...

- Other people: trust, stereotypes

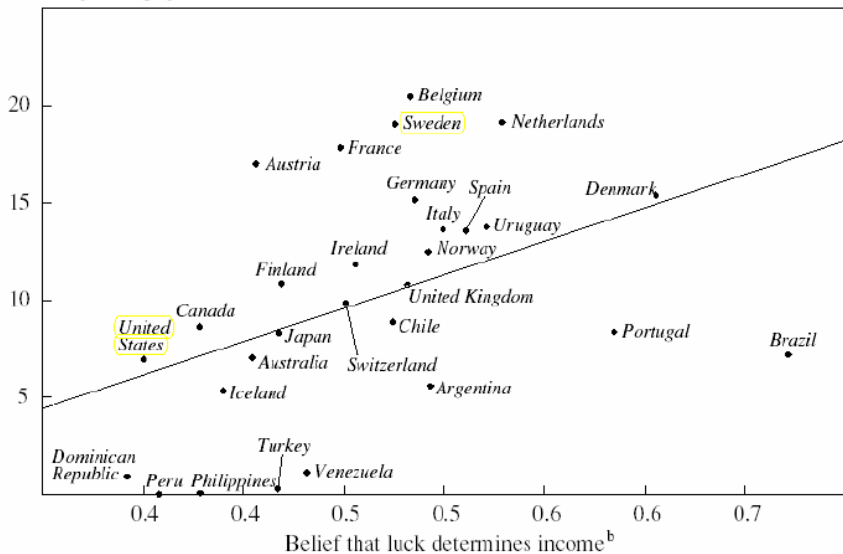
Putnam (2000), Guiso-Sapienza-Zingales (2005), Tabellini (2005, 2007)...

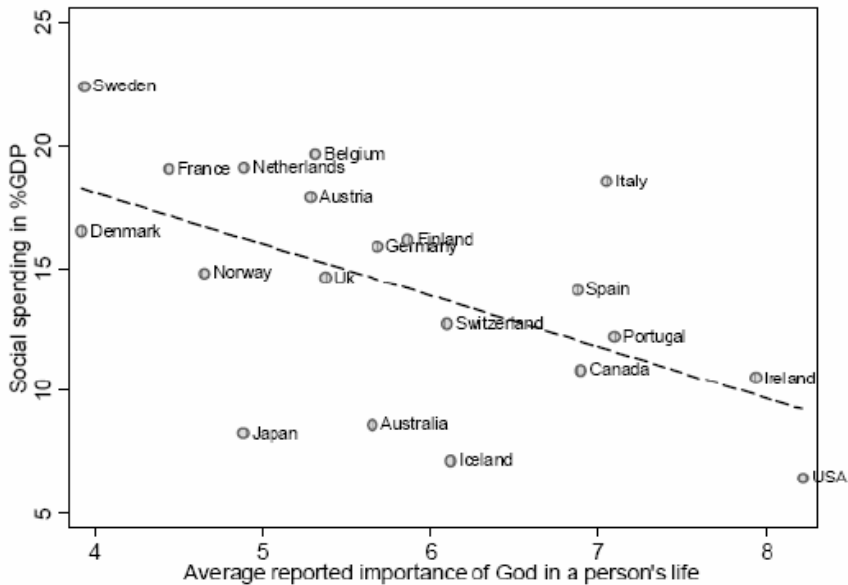
- Religion, culture

Guiso-Sapienza-Zingales (2003), Scheve-Stasavage, 2005, Levy-Razin 2006...

... share the following features

- 1 Vary widely across countries, correlated with policy
- 2 At individual level, powerful predictors of political attitudes and certain economic behaviors
- 3 Each group or country tends to think its own “model” is right one, not just for itself but for others
- 4 Not surprisingly (can't all be right), these beliefs are often quite misaligned with reality
- 5 Yet they persist over time, and are often considered important impediments to necessary reforms. Sometimes, beneficial.

Social spending (percent of GDP)^a



Scheve and Stasavage (2005)

Questions

- 1 Formation and persistence of societal beliefs, particularly involving reality distortion: ideology
- 2 Collective delusions more generally: groupthink

Groupthink: a pattern of thought characterized by self-deception, forced manufacture of consent, and conformity to group values and ethics (Merriam-Webster)

Coined by Janis (1972) to designate set of symptoms of flawed decision-making in organizations. Case studies of foreign policy fiascoes and successes.

- Bureaucracies, govt. Challenger (1986) and Columbia (2003) space shuttle investigations
More recent departures from “reality community”
- Corporate, financial meltdowns: many red flags which people ignored / rationalized away, evidence which refused to see.
Culture of hubris: this time it is different / new economy, we are smarter and have better tools, old ways of thinking no longer apply...
- Latest episode: subprime mortgage crisis.
Previous: Enron, etc., internet bubble. Before...

Some elements from psychology...

- Overoptimism, “illusion of control”
- Self-serving recall, selective attention, self-deception, rationalizations
- People “invest” in and protect their beliefs:
 - ▶ Affective, emotional value: need to feel that the world is predictable, fair, not hopeless, etc.
 - ▶ Functional, instrumental value: helps to motivate oneself, or one's children, to work, persist, cooperate.

... in economic models

- Cognitive dissonance / self deception

Akerlof-Dickens (1982), Rabin (1994), Carrillo-Mariotti (2000), Bénabou-Tirole (2002, 2004)

Köszegi (2005), Battaglini-Bénabou-Tirole (2005), Dessi (2005)

- Attention (but selective)

Sims (2006), Reis, (2006), Karlsson-Loewenstein- Seppi (2005)...

- Anticipatory utility

Loewenstein (1987), Caplin-Leahy (2001, 2003), Landier (2000), Caplin Elias (2005)

Brunnermeier-Parker (2005), Bernheim-Thomadsen (2005), Bénabou-Tirole (2006)...

- Overoptimism in firms

Fang-Moscarini (2005), Gervais-Goldtsein (2005), Van den Steen (2005)...

Outline

- **Part I.** Realism and denial in relatively “small” groups: firms, teams, governments, public-goods providers, cults, etc.

Main intuitions and results.

- **Part II.** Societal beliefs: statist and laissez-faire ideologies

Combine groupthink with political economy

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- **Part I.** Realism and denial in relatively “small” groups: firms, teams, governments, public-goods providers, cults, etc.
Main intuitions and results.
- **Part II.** Societal beliefs: statist and laissez-faire ideologies
Combine groupthink with political economy
- Single model for corporate culture & national culture

Richard Feynman, *Challenger Commission Report* (1986)

It appears that there are enormous differences of opinion as to the probability of a failure with loss of vehicle and of human life. The estimates range from roughly 1 in 100 to 1 in 100,000. The higher figures come from the working engineers, and the very low figures from management. What are the causes and consequences of this lack of agreement?

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Part I

Groupthink in Organizations

□ Period 1: actions...

- Invest or not in common project: firm, team, policy

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□ Period 2: final payoffs

- Depends (linearly) on own and others' actions
- Affected by overall project value: uncertain

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- Common signal about expected value of the project

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- Common signal about expected value of the project
- Process information: acknowledge/retain, or look away/misread/forget

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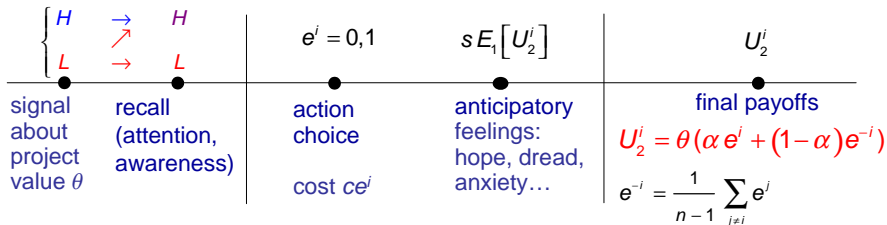
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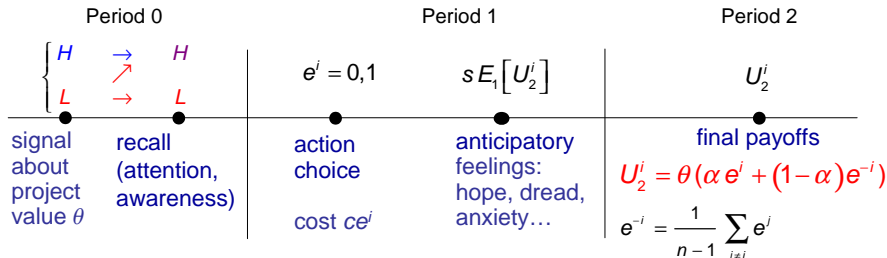
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Period 1

Period 2

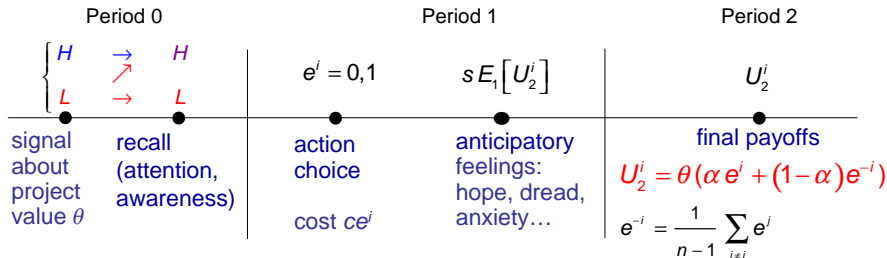




- Period 1: chooses action to maximize

$$U_1^i = -ce^i + sE_1[U_2^i] + \delta E_1[U_2^i]$$

- ▶ acts if confident enough, $(s + \delta)\alpha E_1[\theta] > c$



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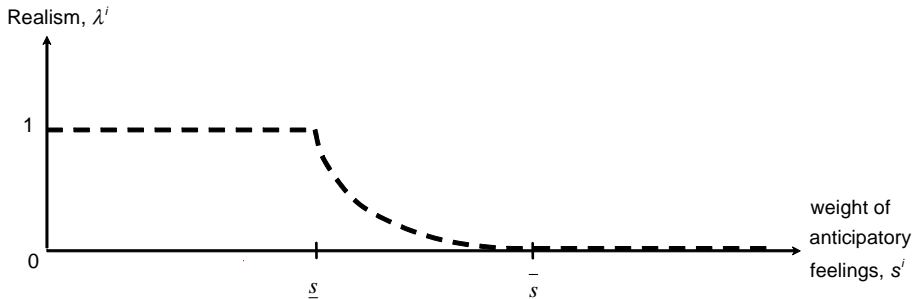
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- Period 0: cognitive decisions, aiming to maximize

$$U_0^i = - \text{info costs} + \delta E_0[-ce^i + sE_1[U_2^i]] + \delta^2 E_0[U_2^i]$$

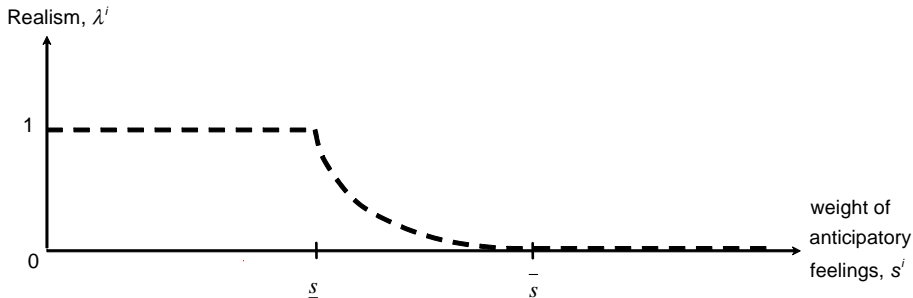
- ▶ tradeoff: more pleasant feelings vs. costs, mistakes

◆ Optimal awareness



- Individual trades off costs vs. benefits of censoring, disregarding bad news. Fully rational at every stage

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- Key question: how does this tradeoff depend on other's degree of realism or denial?

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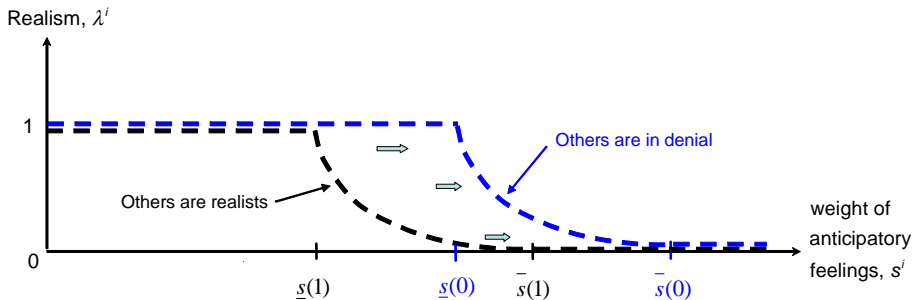
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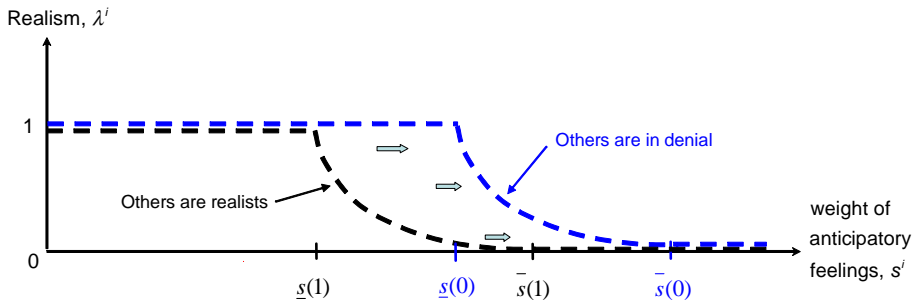
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- **Ugly:** low state θ_L , with $\theta_L < 0$

Negative expected value, social and private

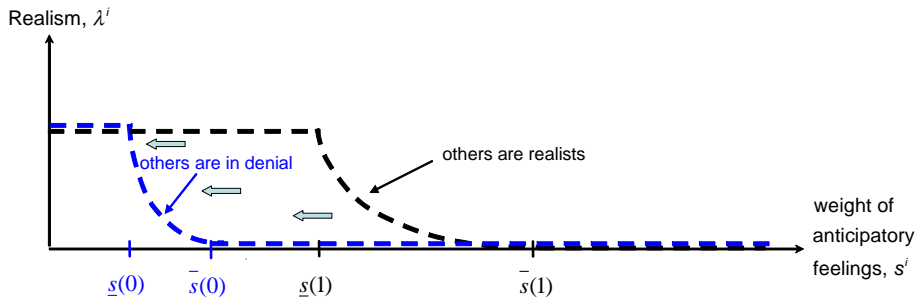


- When others' disregard of bad news leads them to act in a way that is *better* for an agent than if they were realists, it makes those news less bad



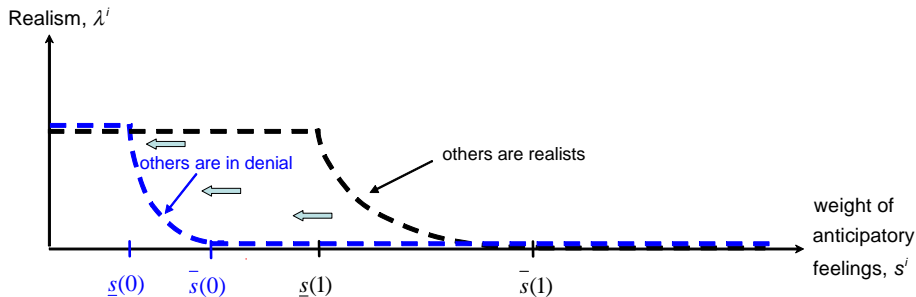
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 \Rightarrow *reduces* incentive to engage in denial

High-risk corporate or military strategy, cults... $\theta_L < 0$



- When others' reality denial leads them to make things *worse* for an agent than if they were realists, his future prospects are even worse

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 \Rightarrow *increases* incentive to look the other way

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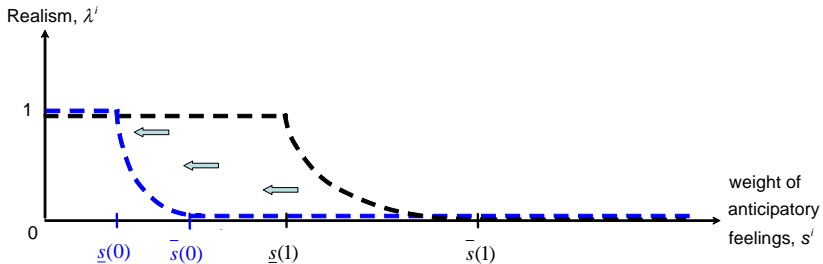
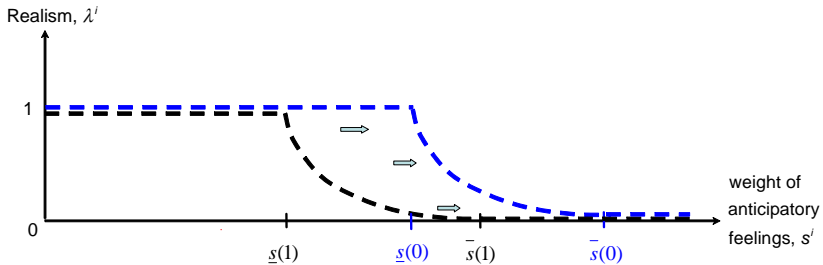
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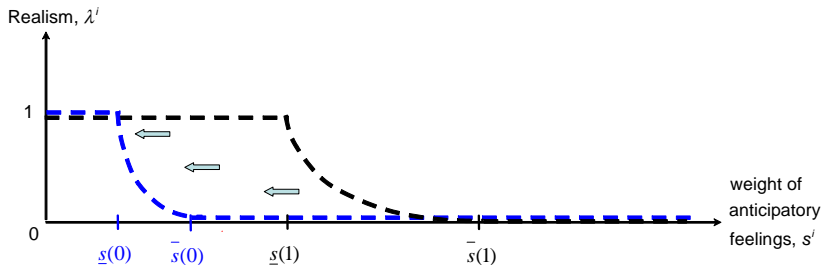
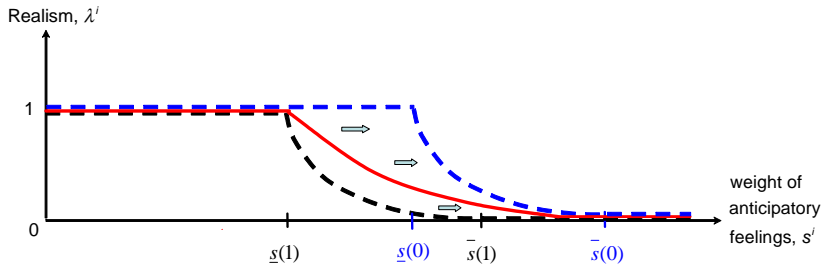
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- Next, look for equilibrium: corporate culture, social cognition

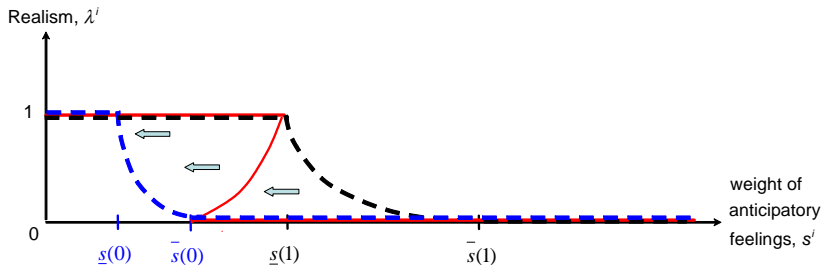
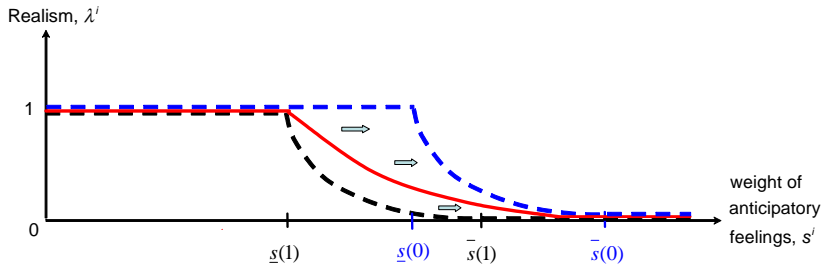
The two cases



Group Morale...



... and Groupthink

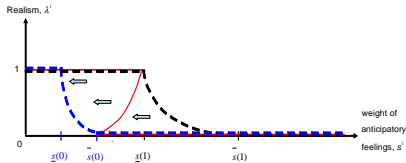
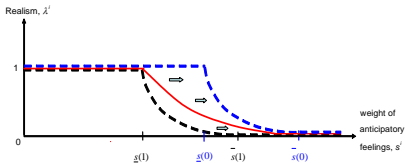


◆ Groupthink

- ① *When losses from others' delusions are large enough,*

$$\text{Prob}(\text{state } L) \times (\theta_H - \theta_L) < (1 - \alpha) (0 - \theta_L),$$

both collective realism and collective denial are equilibria, for s in some range

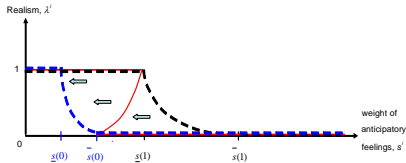
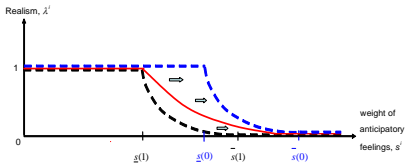


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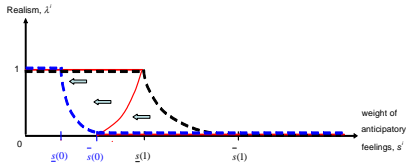
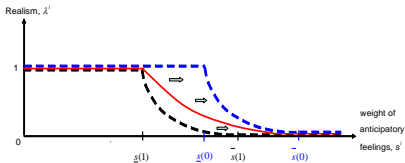
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- ② Culture of denial: all persist in wrong course of action, ignoring the red flags –because others do
- ③ Groupthink more likely when more “common fate”, few exit options; more risky project, worse bad news

Asymmetric groups and hierarchies

- General payoff structure: in state $\sigma = H$ or L ,

$$U_2^i \equiv \sum_{j=1}^n (a_{\sigma}^{ji} e^j + b_{\sigma}^{ji} (1 - e^j))$$

- Agents may also differ in costs, preferences, priors.
Could add standard strategic interactions
- Compare incentive to ignore signal L when everyone else is doing so vs. when they are realists

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Psychological multiplier > 1 when others' blindness (persist in state L) is, *on net*, harmful to agent

◆ Generalized MAD-ness

① Multiple equilibria when

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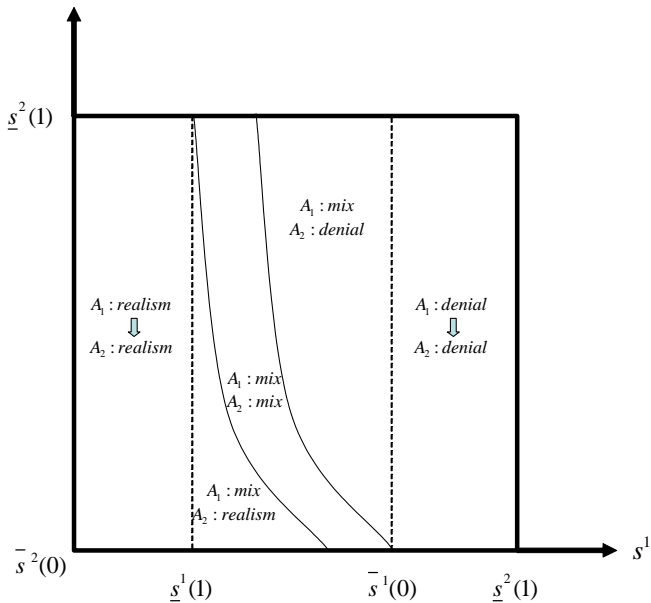
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- 3 Simple hierarchy: agent 1 = manager, 2 = worker(s)
Manager delusions hurt workers >> reverse
 $b_L^{12} - a_L^{12}$, large, $b_L^{21} - a_L^{21}$ small \Rightarrow

◆ Follow the leader



“Trickle down” of beliefs in a hierarchy

Welfare, dissent and free speech

- Are agents under collective illusion worse or better off than facing the truth?

Group morale vs. groupthink

- Alternative equilibria, or achieved through collective commitment mechanism
- Role and treatment of the bearers of bad news

Similar issues for small groups / firms and later on for societies / polities

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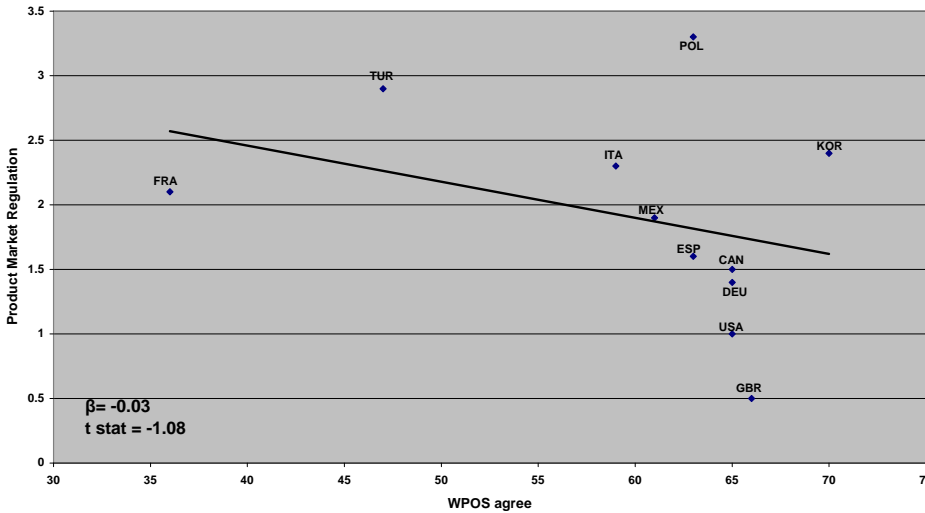
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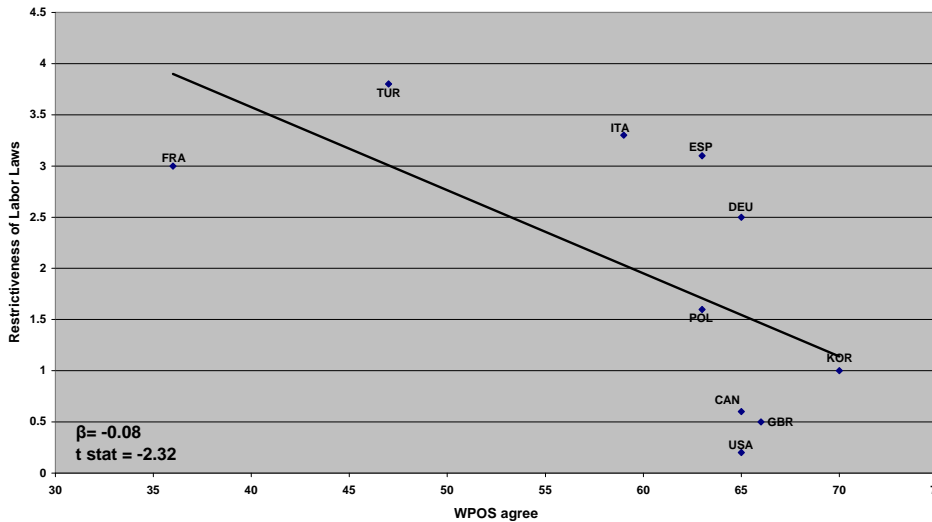
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- Tension between *ex-ante* and *ex-post* incentives to tolerate dissent. Curse of Cassandra
 - ▶ Explains need for institutions to foster and protect speech

Part II

Ideology





- Statist ideology

“The French Social Model is neither inefficient nor outdated. It has a great ambition which can be expressed simply: permanently to level up. We must keep it. In a way it's our national genius. It is a necessity.” (President J. Chirac, 2005)

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- **Institutions \Rightarrow Beliefs.** Anticipatory feelings create incentive to like what you have, not miss what you don't have. Decisions of ideological majority further worsens unpleasant reality:
 - ▶ high taxes, little return in terms of public effectiveness
 - ▶ underinvest privately: education, health, etc..; spillovers

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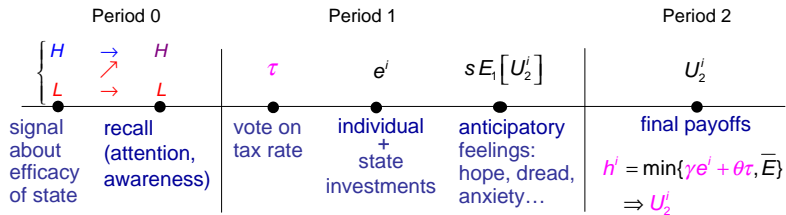
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- **Institutions \Rightarrow Beliefs.** Anticipatory feelings create incentive to like what you have, not miss what you don't have. Decisions of ideological majority further worsens unpleasant reality:
 - ▶ high taxes, little return in terms of public effectiveness
 - ▶ underinvest privately: education, health, etc..; spillovers \Rightarrow increases incentive to convince oneself that we are not in such a world. Join ideological majority

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- D. North (1990):

“The subjective mental constructs of the society’s participants will evolve an ideology that not only rationalizes the society’s structure but accounts for its poor performance. As a result, the economy will evolve policies that reinforce the existing incentives and organizations.”

The state or the market



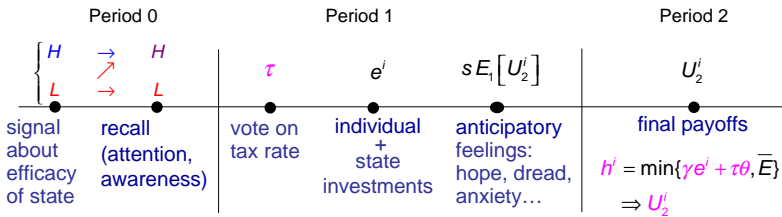
- Period 1: investment in education, health, retirement assets, ... Private, or / and government provision

$$h^i = \gamma e^i + \theta \tau, \quad \text{up to some maximum } \bar{E}$$

- Period 2: agent or offspring will have income

$$y^i \equiv \alpha h^i + (1 - \alpha) \bar{h},$$

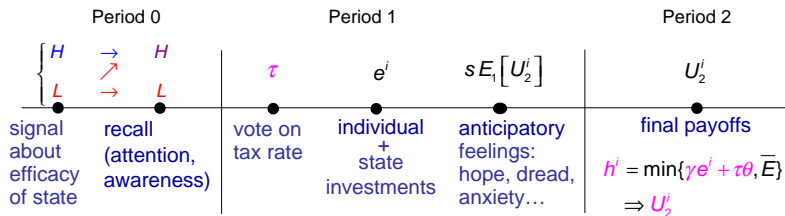
\bar{h} : population average



- Uncertainty: the state could be less efficient than the market, or more, at providing the good:

$$\theta_L < \gamma < \theta_H$$

- Period 0 : observe common signal L or H about efficacy of state intervention \Rightarrow accept or censor
- Or: differential receptivity to L vs H propaganda



- Finally payoffs:

$$U_2^i = 1 - \tau - e^i + \alpha h^i + (1 - \alpha)\bar{h}$$

- Intertemporal preferences unchanged

$$U_1^i = sE_1^i[U_2^i] + \delta E_1^i[U_2^i] \rightarrow e^i, \tau$$

$$U_0^i = - \text{info costs} + \delta E_0^i [sE_1^i[U_2^i]] + \delta^2 E_0^i[U_2^i] \rightarrow \lambda^i$$

Realism

- People acknowledge what gvt. can / cannot deliver, respond appropriately to policy: $\gamma e^j = E - \tau\theta_H$ in state H and $\gamma e^j = E - \tau\theta_L$ in state L
- Representative voter knows this + also aware of true state, so chooses correct tax rate:

$\tau_L = 0$ when L , revenue-maximizing $\tau_H = \bar{\tau}$ when H

- Public policy different in each state \Rightarrow one is unavoidably confronted again with reality at $t = 1$
No point in censoring at $t = 0$.

\Rightarrow *Realism is always an equilibrium*

Statist Ideology

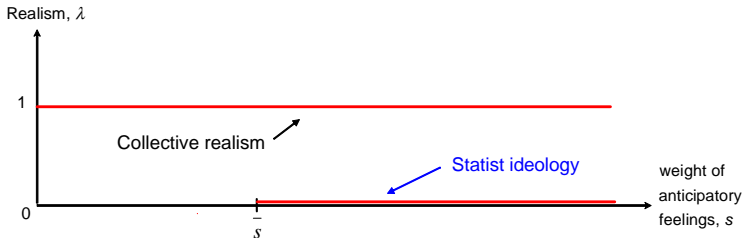
- People avert their eyes from inefficiency of gvt. provision: “read” both signals as H
(\Rightarrow same posterior = prior)
- Respond to policy τ with $\gamma e^j = E - \tau\theta_H$: right amount in state H , but falls short in L .
- Representative voter is one *inter alia*, censoring bad news like everyone else. If prior high enough, sets $\tau_H = \tau_L = \bar{\tau}$.
- Policy no longer reveals the state of the world

- But is it indeed optimal to remain blind to “government failure”?
 - ▷ Acknowledge \Rightarrow correctly invest $\gamma e^j = E - \bar{\tau}\theta_L$, but live with knowledge that:
 - high taxes levied, but unproductive
 - others underinvest, due to excessive faith in gvt.
 - ▷ Go along with prevailing ideology \Rightarrow underinvest, but enjoy comforting hope / beliefs that public institutions will deliver + no negative externalities

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- MAD: majority's delusions make a bad reality worse

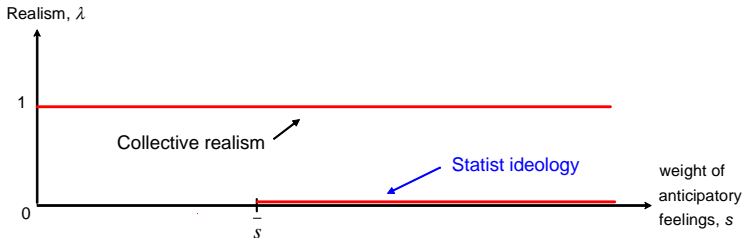
◆ Statist ideology

- 1 Realism always an equilibrium, appropriate policy



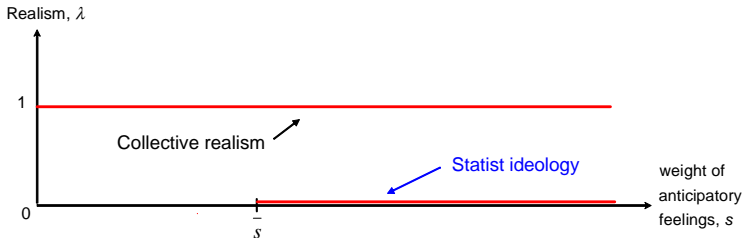
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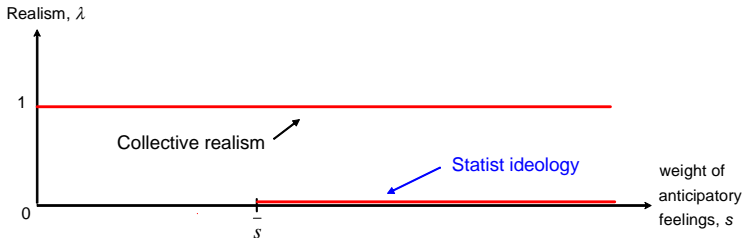
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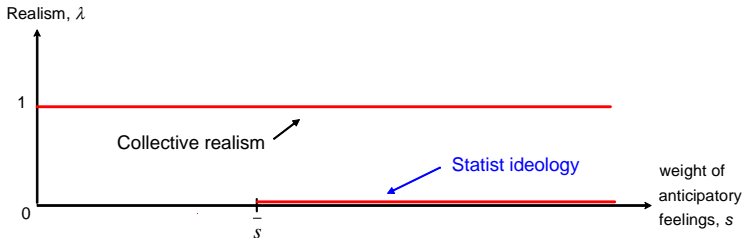
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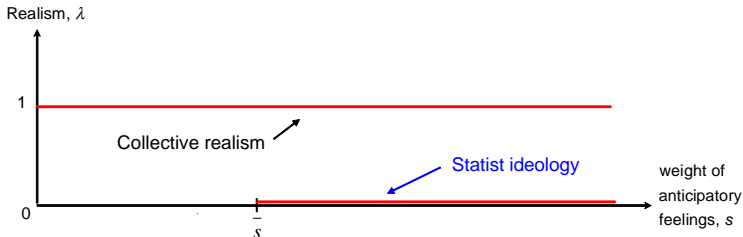
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 - ▶ the worse the actual efficiency of the state (θ_L)



Laissez-faire ideology

- Wishful thinking cuts both ways:
 - Ample evidence of excessive faith in gvt., national “social model,” anti-market bias (Caplan 2000)
 - Can also take form of anti-government bias, blindness to market failures
- Anti-interventionist beliefs at odds with facts:
 - ▶ Health insurance: major market failures in employer based system, yet persisting fear / myth of single-payer as “socialized medicine”
 - ▶ Transfers, foreign aid: vast overestimation of budget share, number or recipients, ethnicity...
 - ▶ “Laziness” of the poor (e.g., Alesina-Glaeser 2004)
 - ▶ Estate taxes: vast overestimation of incidence

- Dealing with market failures

$$h^i = \min \{ \gamma e^i + \theta (\tau - \kappa), E \}$$

- $\kappa < \bar{\tau}$: state H remains more favorable than $L \Rightarrow$ similar: realism or statist ideology
- $\kappa > \bar{\tau}$: H is a “market failure” state: public intervention is highly needed but will not suffice to restore first-best. Agents still worse off than in “no-market-failure” state L .

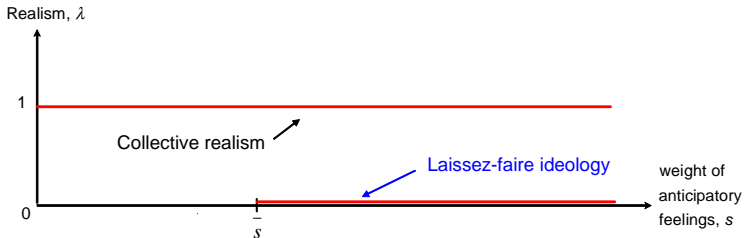
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- MAD: could “live with” second-best situation, but uncorrected market failure (third best) harder to face. Greater incentive to embrace faith in the invisible hand (first best).

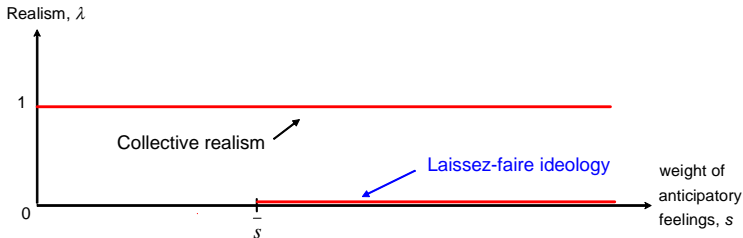
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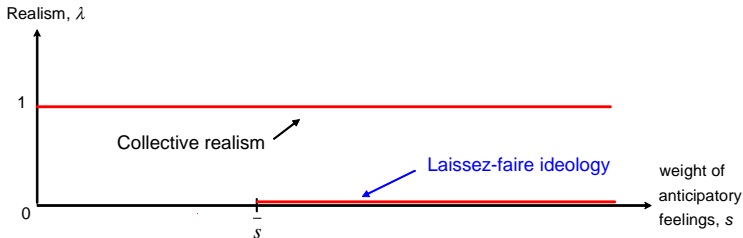
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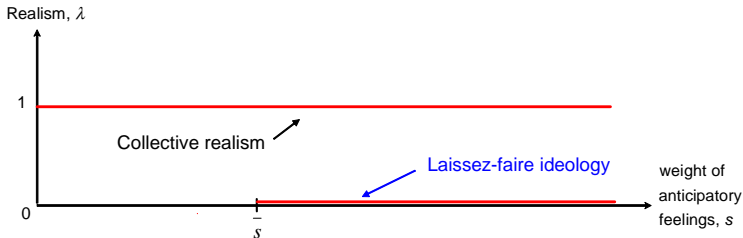
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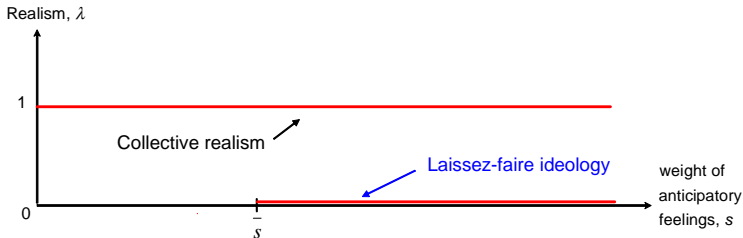
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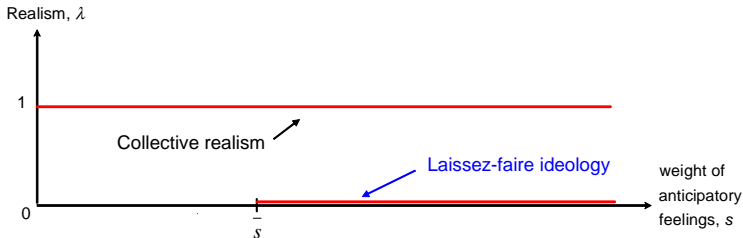
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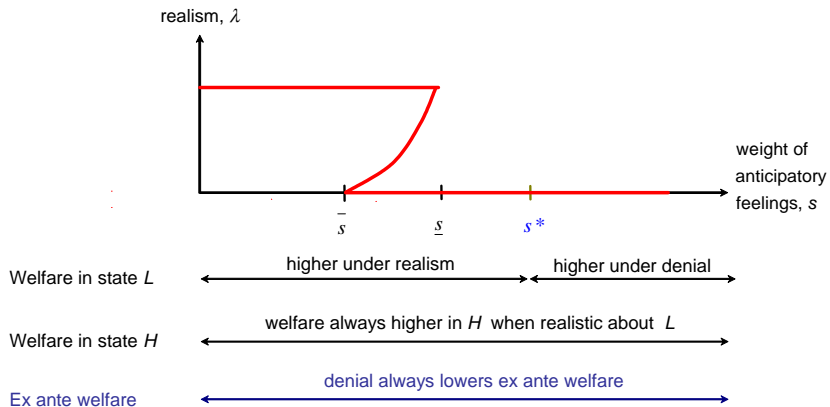
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- ③ Beliefs trickle down the hierarchy
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- ⑤ Statist and laissez-faire ideologies: collectively sustained wishful thinking and immunity to evidence about efficacy of governments or markets

◆ Additional results

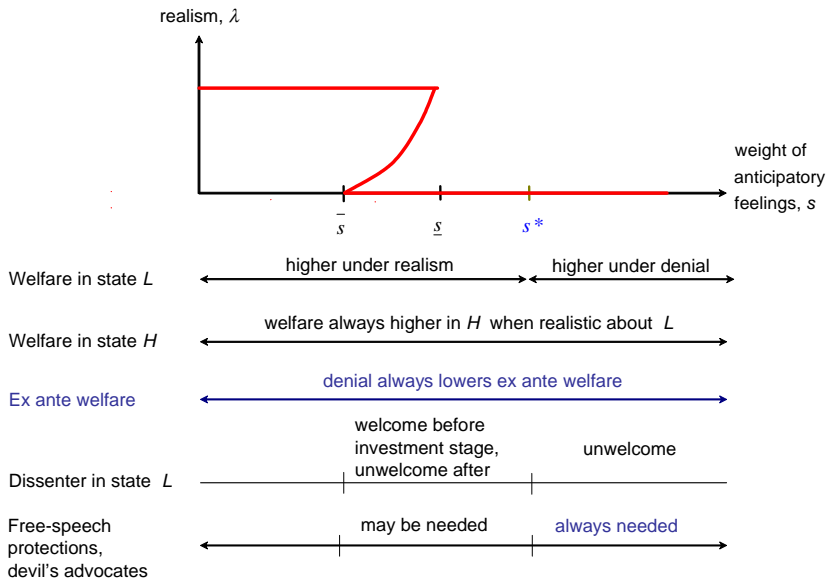
- ① Welfare analysis provides rationale for ex ante, “constitutional” protections for dissenting speech, which ex post no one wants to listen to
- ② Groupthink can also take form of apathy, fatalism. “Tuning out” humanitarian disasters, poverty. Each looks the other way—because others do. Explain puzzles in charitable giving.



- Denial may help in state L but “spoils” value of H
- Bayes: mean belief = prior \Rightarrow ex ante welfare impact of denial just $(\delta + s) \theta_L - c - m/\delta$, lost in state L

Social welfare and free speech

(groupthink case)



◆ Collective apathy and fatalism

- Groupthink so far: collective “illusion of control” . Enron-like scenarios, some wars, cults...
- Opposite case: rather than face up to a crisis, everyone prefers to pretend that things “could be worse” and /or “nothing can be done”
 - ▶ Oppressed or threatened ethnic group “acquiescing” , out-group favoritism (Cialdini 1984, Hochschild 1996)
 - ▶ Looking away from humanitarian disasters, poverty; “psychic numbing” (Slovic 2007)
 - people “feel” less and give less as number of perceived victims increases
 - people give more when think that others are giving more

- Extend model

$$U_2^i = \theta [\alpha e^i + (1 - \alpha)e^{-i} - \kappa]$$

- ▶ $\kappa < 1$: state H remains more favorable than $L \Rightarrow$ similar
- ▶ $\kappa > 1$: H is a “crisis” state: action is called for, but will not suffice to offset the shock. Better off in $L \Rightarrow$

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- ◆ *Group apathy*: “mirror” results , with denial now in high-productivity, crisis state H , and leading to inaction. Multiple equilibria when

$$q\kappa (\theta_H - \theta_L) < (1 - \alpha) \theta_H.$$

- Charitable giving: can account for “tuning off,” social imitation, intensity vs. numbers effects