

# **Social Order and the Role of Groups**

75 minutes , 20 slides

## ***Economic Sociology***

but I won't talk much about networks, although clearly relevant

- breakdown of social order can occur for internal or external reasons, or more likely a combination of the two
- poor institutions create vulnerability to external as well as internal disruptions
- in standard economic analysis pretty much ignore the fact that - for example - a severe recession can lead to a breakdown of social order (Leijonhufvud)
- in political economy more effort to contemplate the consequences of policies that might lead to the breakdown of social order
- but difference between efficiency (accounting for costs of breakdown properly) and survivability (minimizing the probability of breakdown) - the latter determining what we see as opposed to what we might want
- should we be studying Switzerland?

## ***Social Breakdown***

- costs are highly uncertain and it is unlikely that there is much agreement
- the one thing we can be fairly confident of is that some people have more to lose, so presumably will care more about breakdown

## ***Role of Groups in Social Breakdown***

- internally the breakdown of social order we think of as being primarily due to conflict between groups
- Olson theory: groups attempt to gain monopoly power, gradual accretion of monopoly power by more and more groups leads to economic breakdown
- Levine/Modica: breakdown due to combination of unlucky circumstances, a smaller number of which a robust system can recover from
- the importance of randomness in determining long-run outcomes

## ***Social Solidarity***

- social solidarity of groups isn't something “mainstream” economics has traditionally dealt with
- historically (see Marx) when economics has dealt with groups it hasn't done an especially good job
- want to emphasize the difference between the strategic and non-strategic aspects of group behavior
- focus primarily on groups that exist for exogenous reasons: trade unions, farm lobbies, banking lobbies, and so forth
- social interaction within the groups occur because of the nature of economic activity in these groups, because of commonality of knowledge and interest, exchange of ideas and learning, and so forth

## ***Economic Psychology: does it help us understand groups?***

- behavioral forces are weak, but this is relevant where individual incentives are weak – for example, voting
- probability assessments, use of information (members of a large group have little incentive to acquire information) - manipulation of information, propaganda
- learning (are incentive constraints satisfied?) - lack of learning especially relevant during unusual times (social breakdown)
- self control - relevant for what happens in crowds?
- reference points, habit formation - in relation to fairness?
- social preferences and fairness - committed voters
- (ambiguity aversion – no idea)

## ***Are Groups Concerned with Fairness?***

- groups are concerned with "fairness" (empirically - mostly "fairness for us" - but people do vote to spend their taxes on transfers to others)
- where are we on theories of fairness?
- altruism and spite versus fairness
- strategic versus non-strategic retaliation
- conflict and consistency of objectives - makes compromise hard (we both fight unless we get 2/3rds the pie); but we don't always see conflict
- what is fair? not yet a good answer in the behavioral literature, in fact serious problems with existing theories (concerning lotteries)
- maybe the what groups perceive as fair is strategic?

## *Groups and Approval*

group members seek approval from other group members

approval isn't so different from other economic commodities - people like to talk, share ideas, be approved of, tell stories, hang-out etc.

- can be traded in markets or through barter
- we have measurements: value of cell phone bandwidth and television bandwidth
- obviously some people are more valuable to you than others (extreme example: people who don't speak a language you know are pretty useless to you)
- relevance of networks should be apparent



## *The Strategic Element*

usually political economy models use a pretty mechanical model of approval

but:

- it isn't just that you “are a member” or “are not a member” you either “adhere to group norms” or you “don't adhere to group norms” and those norms are endogenous
- if you fail to adhere you get punished, many ways, including exclusion/ostracism

we have a very good model of this: the Kandori repeated game model of social norms

## ***The Peer Punishment Model***

strategic and collusive groups that can punish members

- an important form of punishment is exclusion from benefits of being in the group, withdrawal of approval and so forth

special Levine/Mattozzi edition of Levine/Modica peer punishment mechanism for the Palfrey/Rosenthal voter participation model

- *ex ante* identical members of a collusive group privately draw type  $y$  from uniform on  $[0, 1]$
- type determines cost of voting  $c(y)$ , possibly negative
- group can impose punishments  $0 \leq P \leq \bar{P}$  on members
- social norm of group a threshold  $\hat{y}$  together rule prescribing voting if  $y \leq \hat{y}$
- rule enforced through peer auditing and punishment

## ***Monitoring and Punishment***

- each member of the group audited by another group member
- primitive network – a circle, everyone sees the person to their left
- auditor observes whether or not the auditee voted
- auditee did not vote and the group member did not violate the policy (that is,  $y > \hat{y}$ ) probability  $\pi$  that the auditor will learn this
- $\pi$  is signal quality:  $\pi = 0$  auditor learns nothing;  $\pi = 1$  auditor perfectly observes whether  $y$  is above or below the threshold  $\hat{y}$
- if the auditee voted or discovered not to have violated the policy, the auditee is not punished
- auditee did not vote and the auditor cannot determine whether or not the auditee violated the policy: auditee punished with a loss of utility  $P$

## ***Incentive Compatible Social Norms***

social norm is incentive compatible if and only if  $P = c(\hat{y})$

- any member with  $y \leq \hat{y}$  would be willing to pay cost  $c(y)$  of voting rather than face the punishment  $P$
- any member with  $y > \hat{y}$  prefers to pay the expected cost of punishment  $(1 - \pi)P$  over the cost of voting  $c(y)$

overall cost of the punishment to the group is  $\psi P$  where  $\psi \geq 1$

(costs of carrying out punishment along with the cost of the punishment itself)

if auditors not indifferent – need further rounds of punishment, see Levine/Modica

## Group Cost of Participation

$\phi$  the participation rate of the group

$\underline{y}$  is the (unique) value with  $c(\underline{y}) = 0$

cost of participation above  $\underline{y}$  denoted  $D(\phi)$ , has two parts

participation cost  $C(\phi) = \int_{\underline{y}}^{\phi} c(y)dy$  this is increasing and convex

monitoring cost  $M(\phi) = \int_{\underline{y}}^1 \psi(1 - \pi)Pdy$

using the incentive constraint  $M(\phi) = \psi(1 - \pi)(1 - \phi)C'(\phi)$

$\theta \equiv \psi(1 - \pi)$  as the monitoring inefficiency; any non-negative number

- signal quality is high monitoring very efficient
- costs of issuing punishments is high monitoring very inefficient

## *The All-Pay Auction*

### **collusion and the importance of randomization**

convexity:

- $C(\phi)$  is necessarily convex
- $M(\phi)$  cannot be convex
- non-negative and equals zero at both  $\phi = \underline{y}, 1$
- hence  $D(\phi) = C(\phi) + M(\phi)$  need not be convex

why it all matters: in an all-pay auction one group is advantaged and gets all the surplus

- if  $D(\phi)$  is convex the larger group is always advantaged
- need not be so when  $D(\phi)$  fails to be convex
- advantage of being small with respect to monitoring

## ***Conflict or conflict?***

- strikes as creating incentive compatibility
- sustain a particular outcome, force revelation of private information

## *The logic of crowds and protests*

- things can get out of hand

this



may lead to

this





## ***Groups and Polarization***

- tipping point of polarization - people forced to choose sides (Iraq)
- leads to conflict and chaos; prevents economic progress by keeping people from forming economic alliances
- strong central authority keeps this in check (looks what happens when the strong central authority collapses - India, Africa, Yugoslavia, etc.)
- yet if there is too little polarization it is a threat to the central authority (dictators in particular often encourage a moderate amount of polarization) - play both ends against the middle, divide and conquer
- some benefit from polarization
- so: how do we prevent monopolization and prevent conflict?