

# Groupthink and Ideology

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Princeton University

Schumpeter Lecture – Budapest 2007

## Two main papers

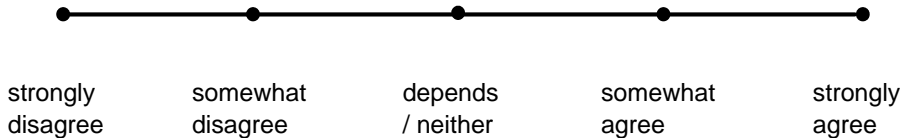
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- “Belief in a Just World and Redistributive Politics”, with Jean Tirole. *Quart. Jour. Econ.* 2006

## Two main papers

- “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

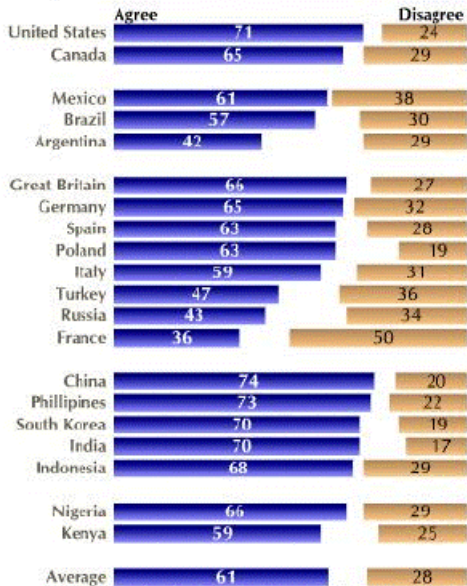
*The free enterprise and free market economy is the best system on which to base the future of the world*

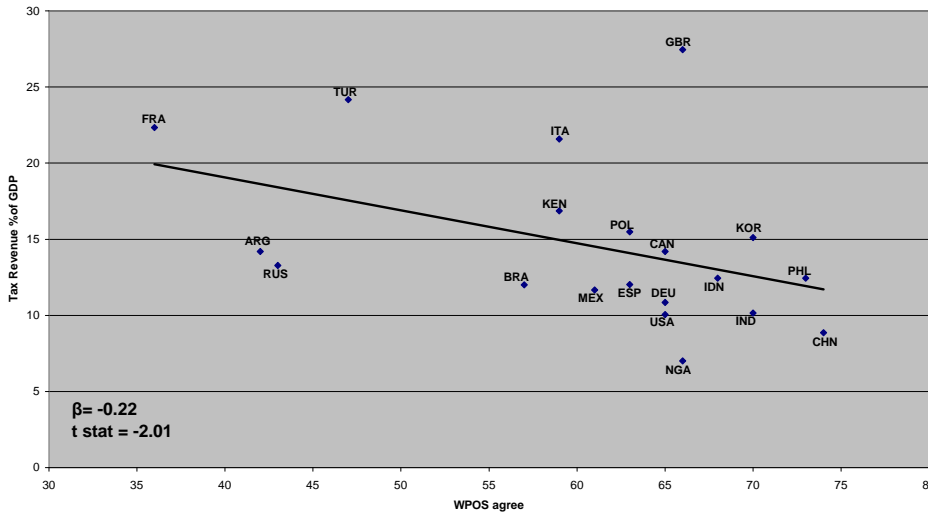
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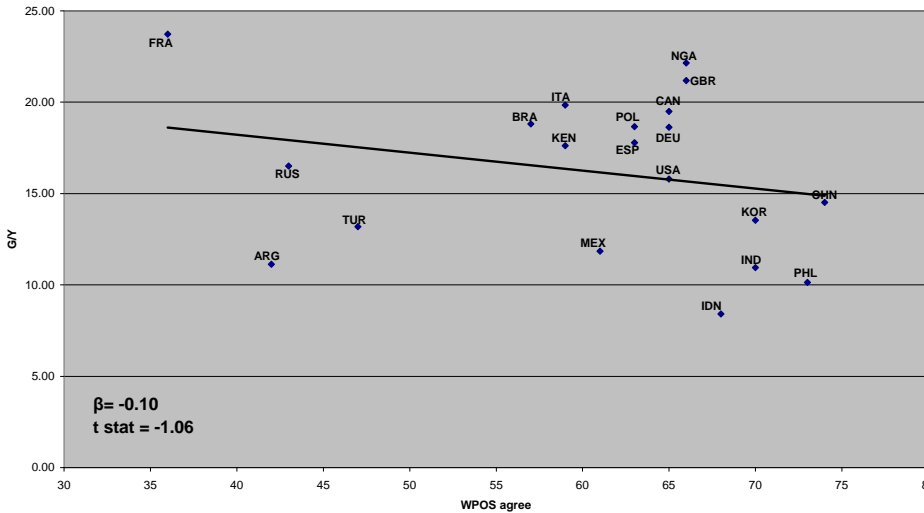


## Free Market System

*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

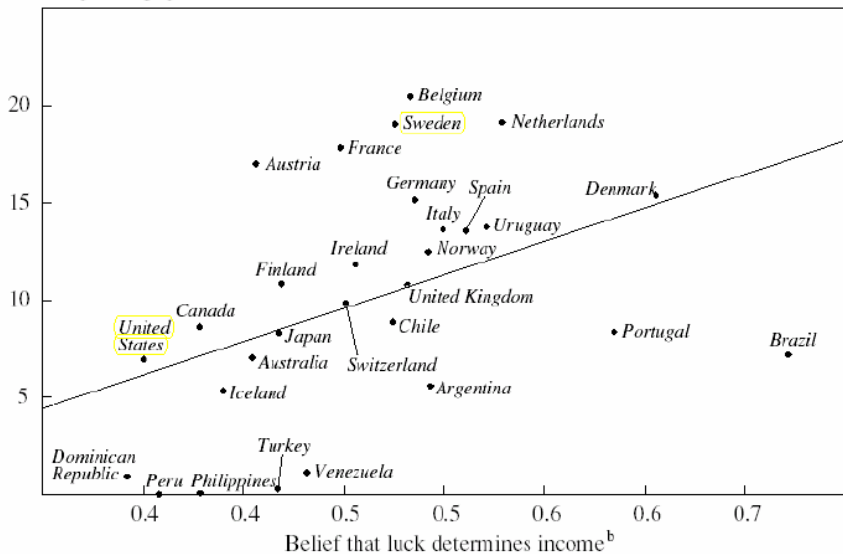
Putnam (2000), Guiso-Sapienza-Zingales (2005), Tabellini (2005, 2007)...

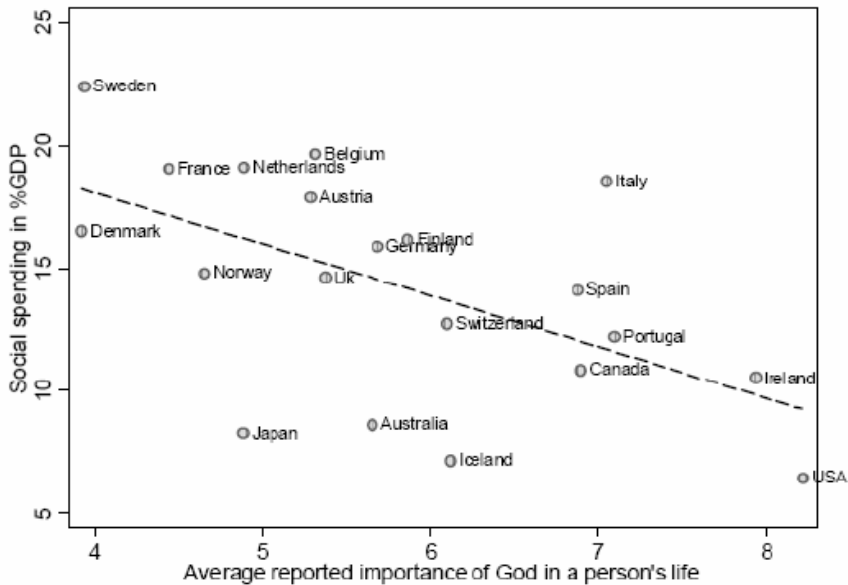
- Religion, culture

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)<sup>a</sup>



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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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...

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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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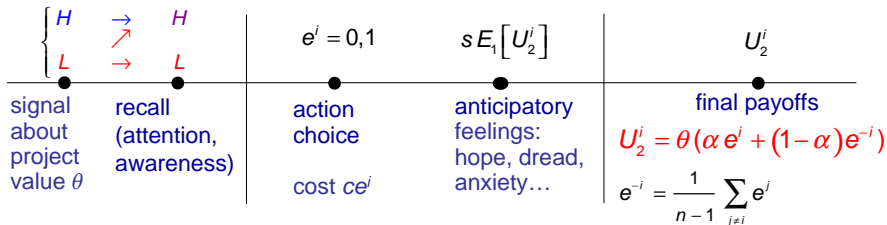
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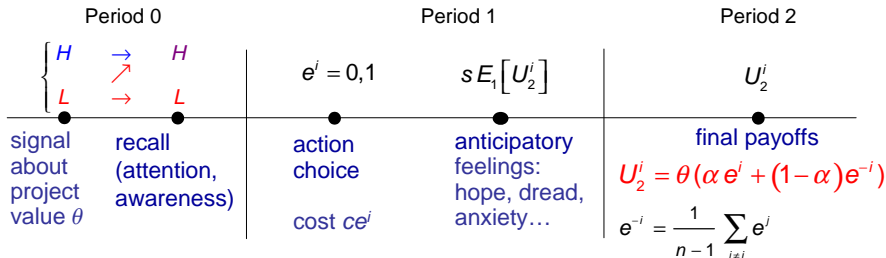
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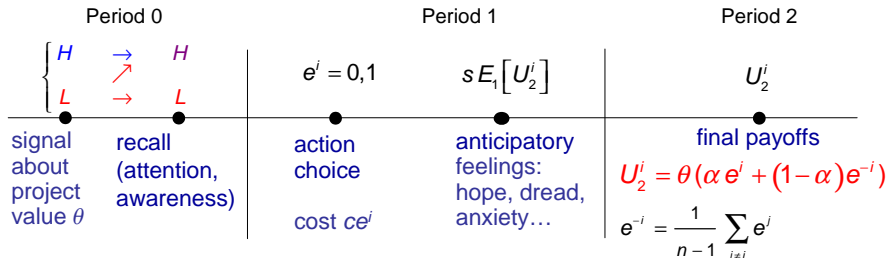




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$$U_1^i = -ce^i + sE_1[U_2^i] + \delta E_1[U_2^i]$$

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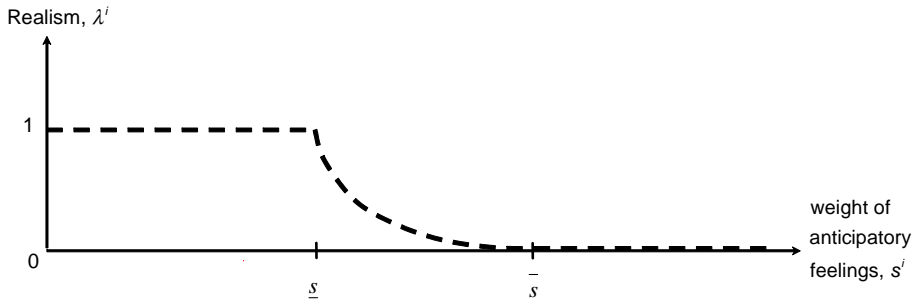
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- Period 0: cognitive decisions, aiming to maximize

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

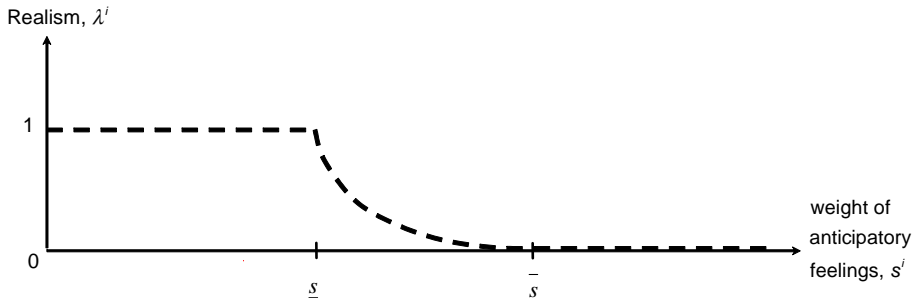
- ▶ tradeoff: more pleasant feelings vs. costs, mistakes

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

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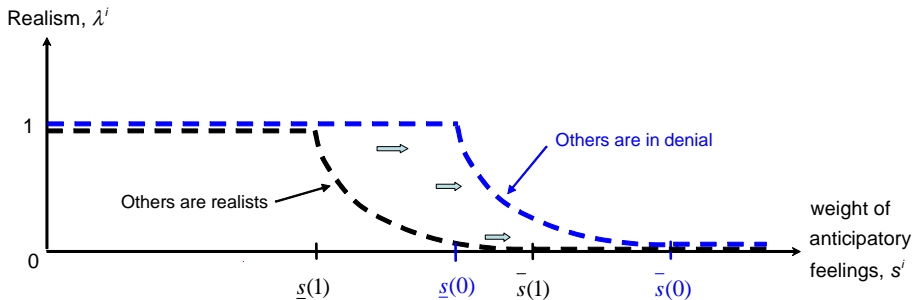
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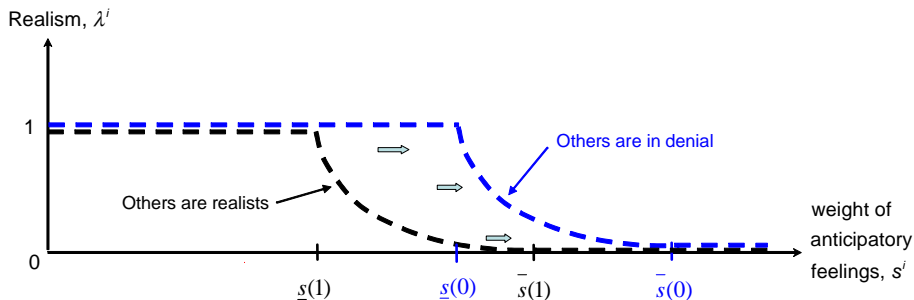
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- **Ugly:** low state  $\theta_L$ , with  $\theta_L < 0$

Negative expected value, social and private

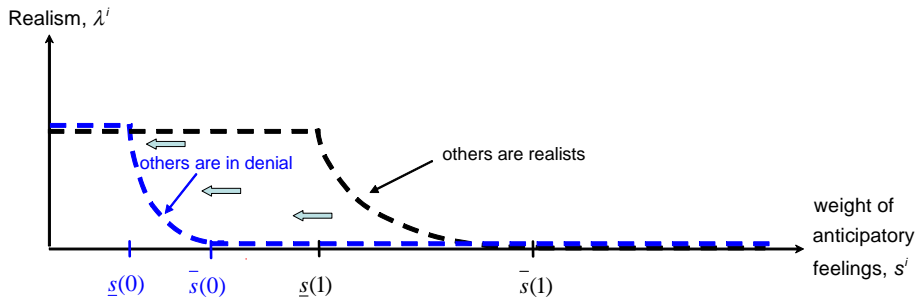


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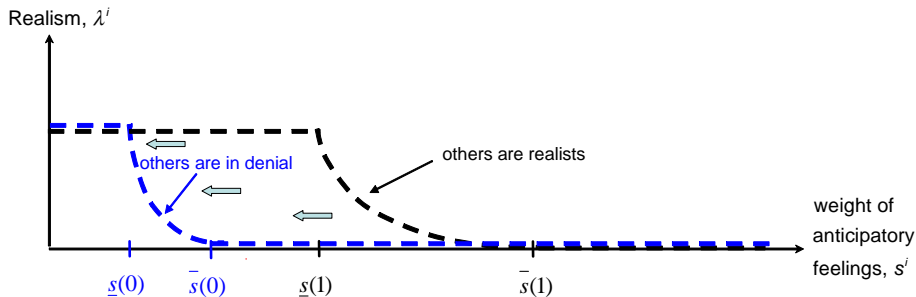
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 $\Rightarrow$  *reduces* incentive to engage in denial

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 $\Rightarrow$  *increases* incentive to look the other way

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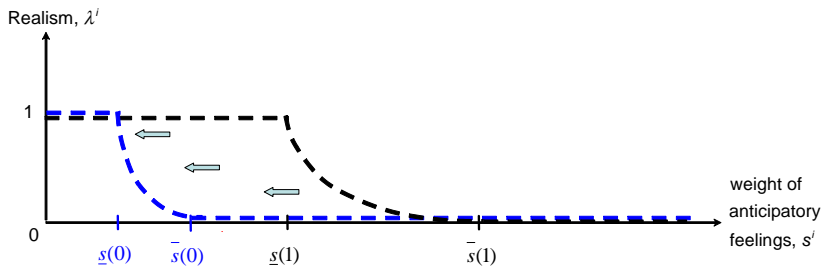
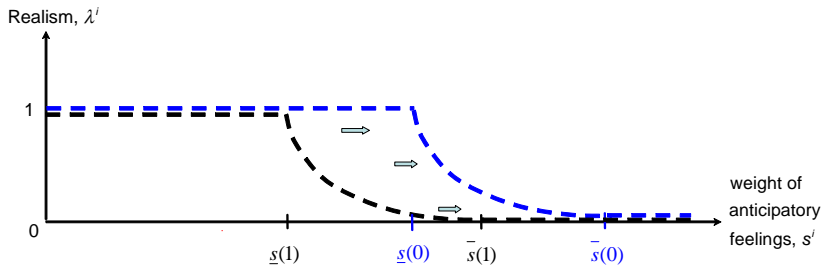
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  - ⇒ interdependent beliefs and actions, although separable linear payoffs, no private information

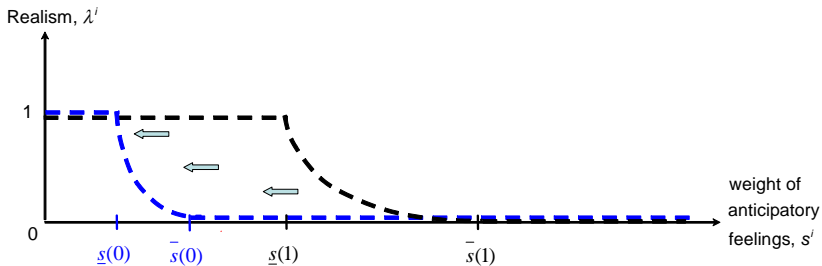
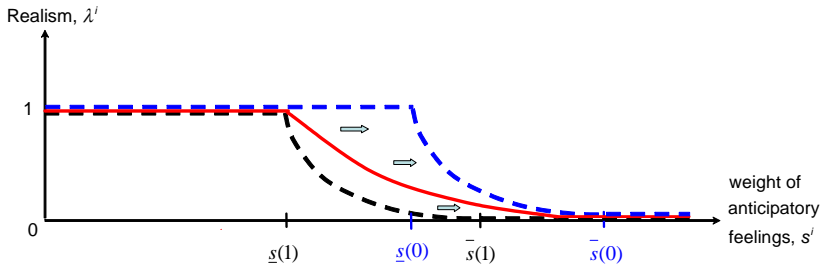
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- Next, look for equilibrium: corporate culture, social cognition

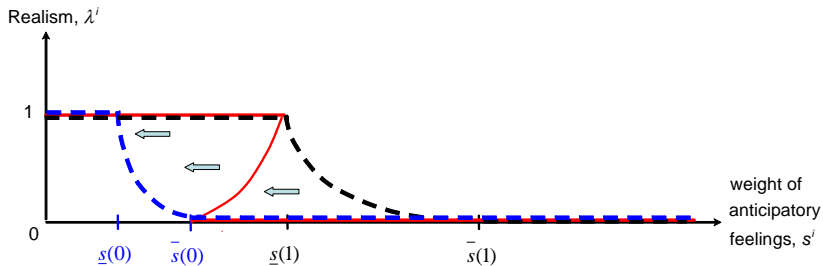
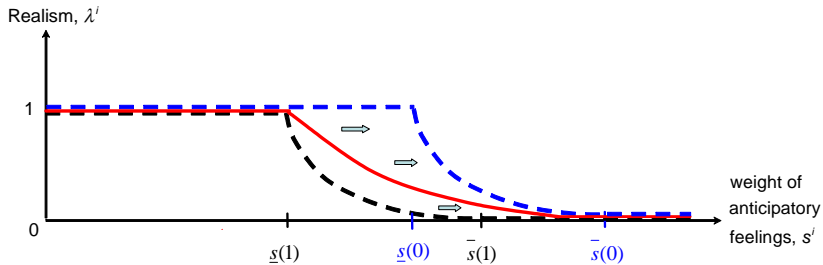
# The two cases



# Group Morale...



## ... and Groupthink

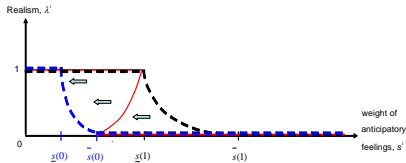
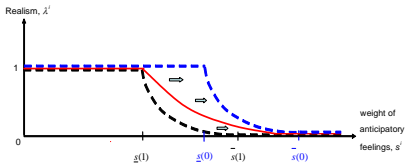


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- ① *When losses from others' delusions are large enough,*

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

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

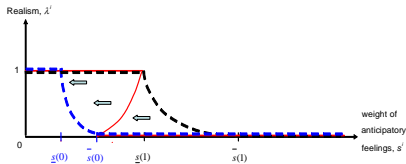
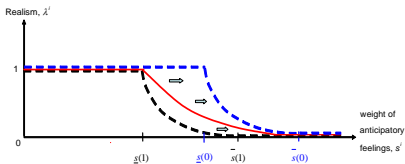


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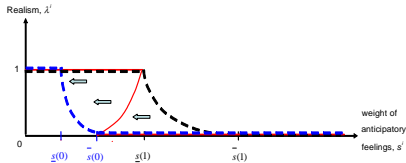
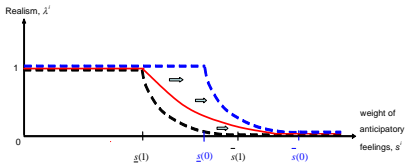
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- ② Culture of denial: all persist in wrong course of action, ignoring the red flags –because others do
- ③ Groupthink more likely when more “common fate”, few exit options; more risky project, worse bad news

## 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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- Compare incentive to ignore signal  $L$  when everyone else is doing so vs. when they are realists  $\Rightarrow$   
Psychological multiplier  $> 1$  when others' blindness (persist in state  $L$ ) is, *on net*, harmful to agent

## ◆ Generalized MAD-ness

① Multiple equilibria when

$$\text{Prob}(\text{state } L) \times \left( \begin{array}{l} \text{gains to } i \text{ from} \\ \text{being in state } H \text{ vs. } L, \\ \text{keeping } e^j = 1 \text{ for all} \end{array} \right) < \left( \begin{array}{l} \text{losses to } i \text{ from others'} \\ \text{delusions } \rightarrow \text{choose} \\ e^j = 1 \text{ in state } L \end{array} \right)$$
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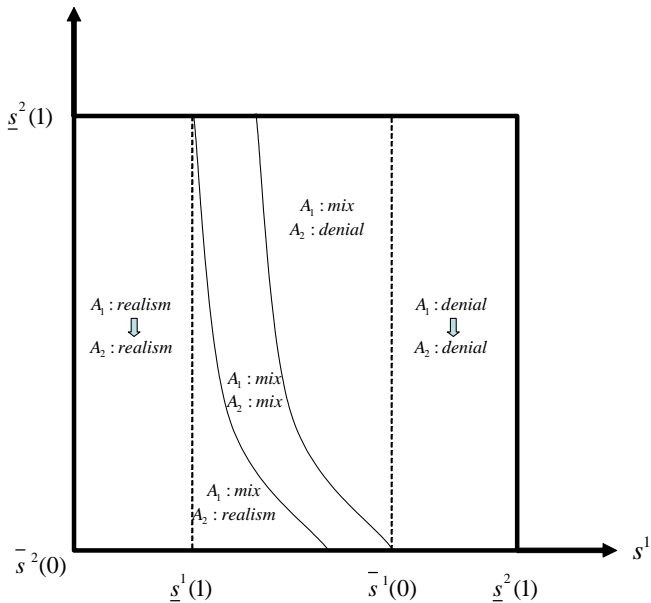
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- 2 Individual's cognitive strategy depends most on how key contributors to his welfare deal with  $L$
- 3 Simple hierarchy: agent 1 = manager, 2 = worker(s)  
Manager delusions hurt workers >> reverse  
 $b_L^{12} - a_L^{12}$ , large,  $b_L^{21} - a_L^{21}$  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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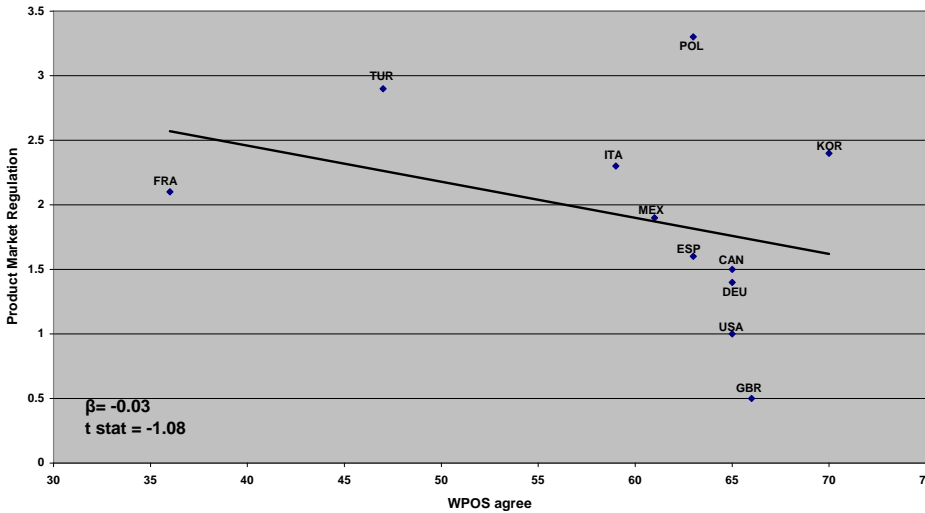
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- *Groupthink*:  $\Delta W < 0$ . Novel case: even when illusions raise social welfare in state  $L$ , gains always dominated by the losses induced in state  $H$

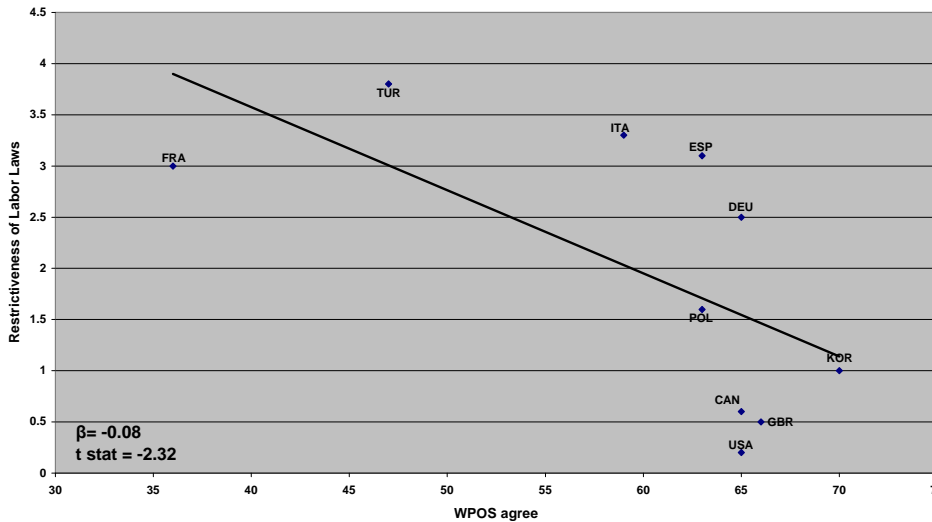
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- Tension between *ex-ante* and *ex-post* incentives to tolerate dissent. Curse of Cassandra
  - ▶ Explains need for institutions to foster and protect speech

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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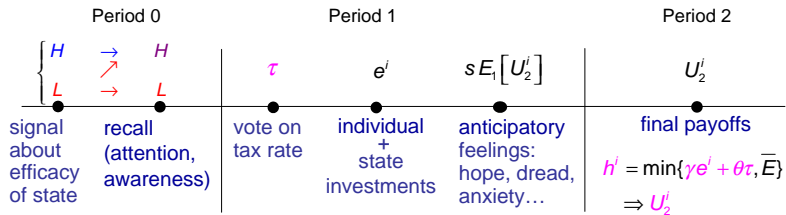
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  - ▶ high taxes, little return in terms of public effectiveness
  - ▶ underinvest privately: education, health, etc..; spillovers $\Rightarrow$  increases incentive to convince oneself that we are not in such a world. Join ideological majority

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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



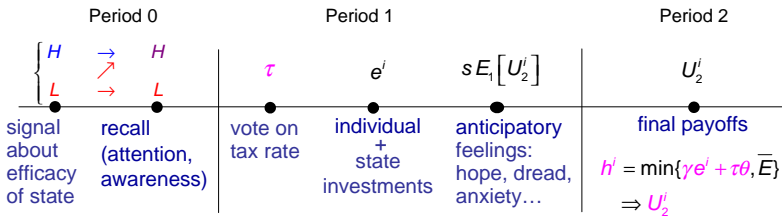
- Period 1: investment in education, health, retirement assets, ... Private, or / and government provision

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

- Period 2: agent or offspring will have income

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

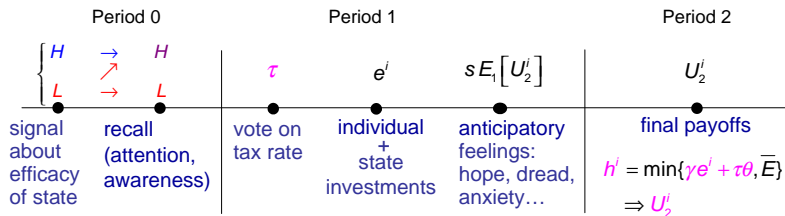
$\bar{h}$  : population average



- 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

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

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

# 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

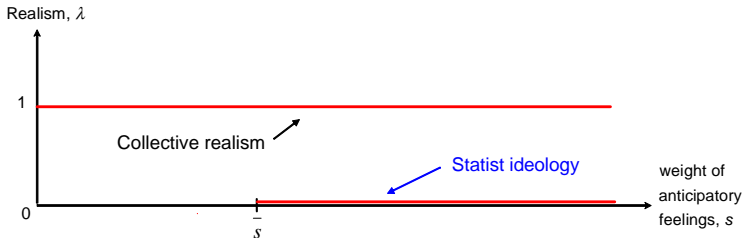
- People avert their eyes from inefficiency of gvt. provision: “read” both signals as  $H$   
( $\Rightarrow$  same posterior = prior)
- Respond to policy  $\tau$  with  $\gamma e^j = E - \tau\theta_H$ : right amount in state  $H$ , but falls short in  $L$ .
- Representative voter is one *inter alia*, 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

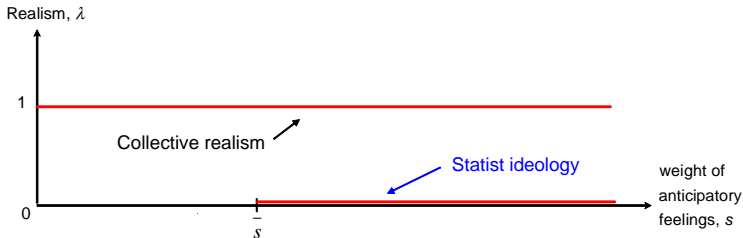
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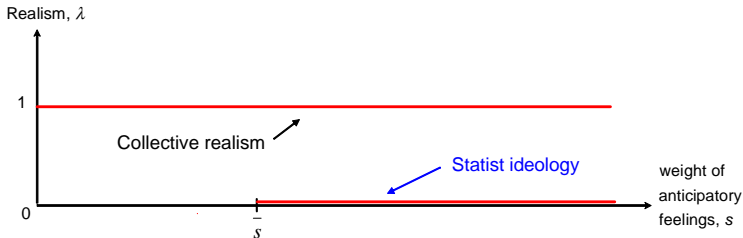
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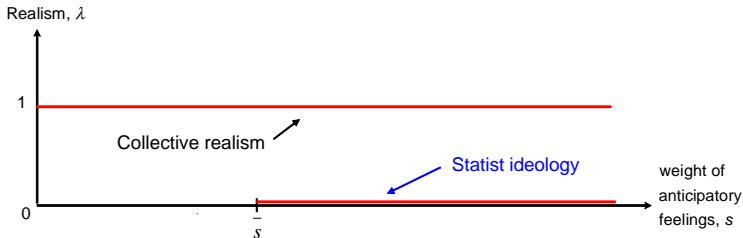
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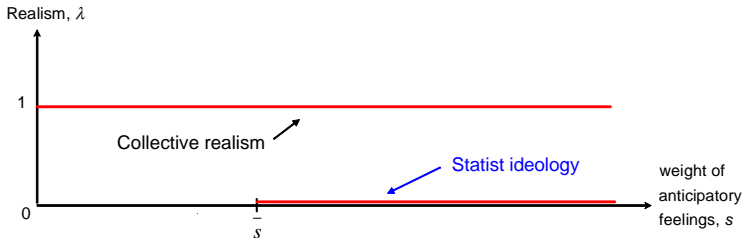
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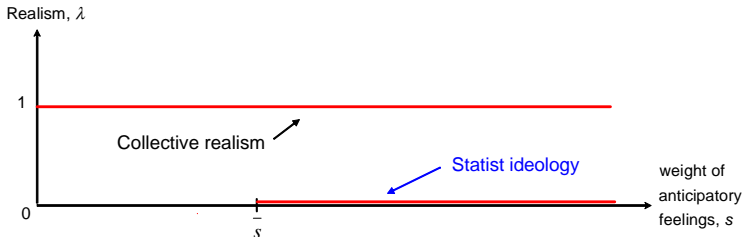
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  - ▶ the worse the actual efficiency of the state ( $\theta_L$ )



## 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  $L$ .

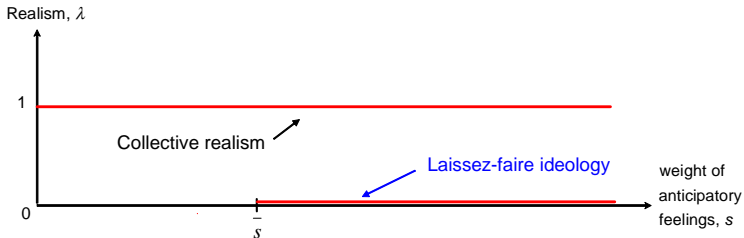
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- MAD: could “live with” second-best situation, but uncorrected market failure (third best) harder to face. Greater incentive to embrace faith in the invisible hand (first best).

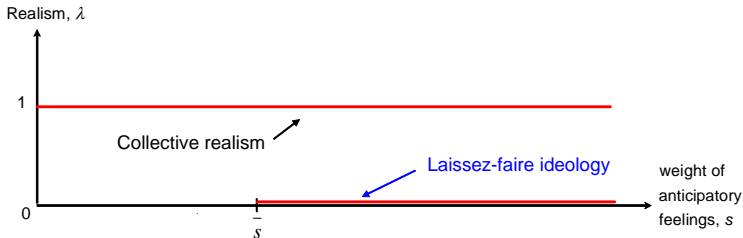
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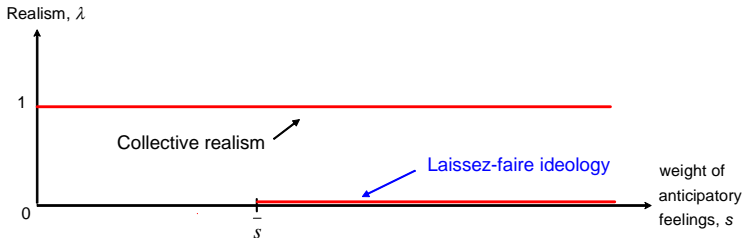
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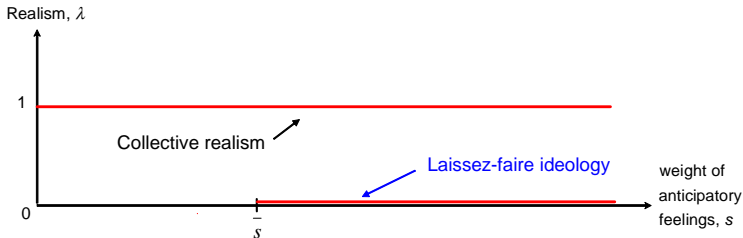
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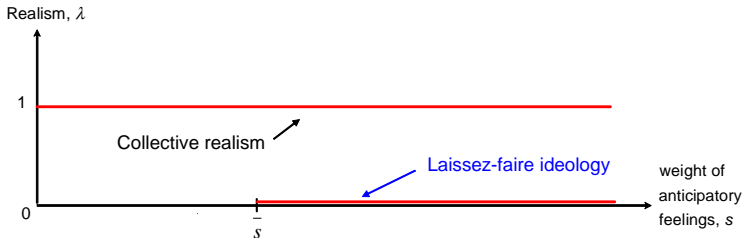
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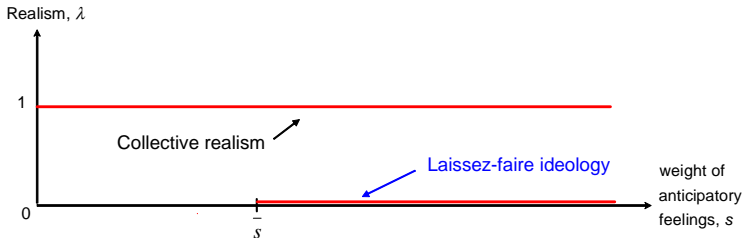
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## ◆ Five key points

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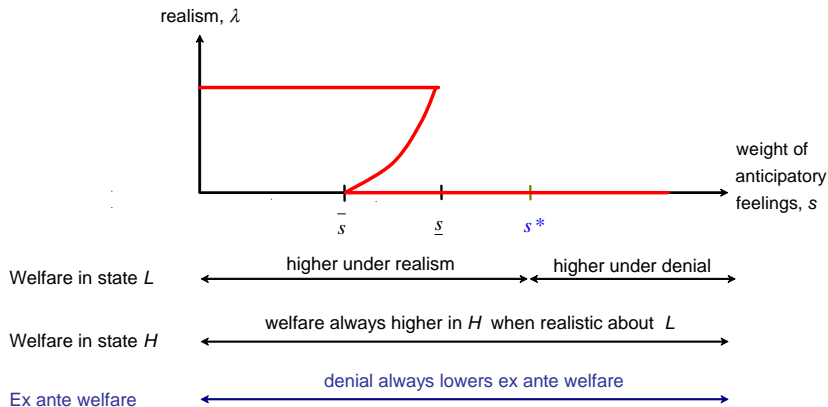
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- 5 Statist and laissez-faire ideologies: collectively sustained wishful thinking and immunity to evidence about efficacy of governments or markets





## ◆ Additional results

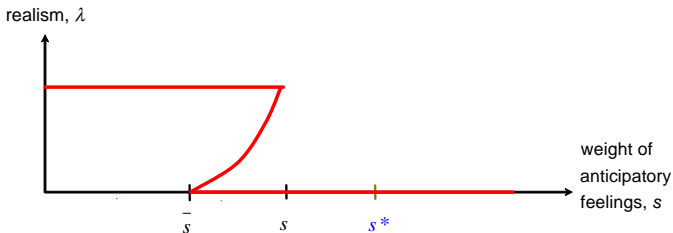
- ① Welfare analysis provides rationale for ex ante, “constitutional” protections for dissenting speech, which ex post no one wants to listen to
- ② Groupthink can also take form of apathy, fatalism. “Tuning out” humanitarian disasters, poverty. Each looks the other way—because others do. Explain puzzles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



Welfare in state  $L$       higher under realism      higher under denial

Welfare in state  $H$       welfare always higher in  $H$  when realistic about  $L$

Ex ante welfare      denial always lowers ex ante welfare

Dissenter in state  $L$       welcome before investment stage, unwelcome after      unwelcome

Free-speech protections, devil's advocates      may be needed      always needed

## ◆ 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
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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