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Machiavellian experimentation☆

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ABSTRACT

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This paper proposes the following mechanism whereby polarization of beliefs could eliminate political gridlock instead of intensifying disagreement: the expectation of political payoffs from being proven correct by a policy failure could drive decision makers who do not believe in the new policy to agree to policy experimentation, because they are confident that the experiment will fail, thus increasing their political power. We formalize this mechanism in a collective decision making model in the presence of heterogeneous beliefs in which any decision other than the default option requires unanimity. We show that this consideration of political payoffs can eliminate the inefficiency caused by a unanimous consent requirement when beliefs are polarized, but could also create under-experimentation when two actors hold beliefs that differ only slightly from one another. We further show that this under-experimentation can be reduced when the political payoffs become endogenous. We illustrate the empirical relevance of the mechanism in two examples with historical narratives: we focus on the decision making process of the Chinese leadership during the country's transition starting in the late 1970s, and we further apply the model to the disagreement within the leadership of the Allied Forces on the Western Front of World War II in the autumn of 1944. *Journal of Comparative Economics* **000** (2017) 1–27. Department of Economics, Columbia University, 420 West 118th Street, 1022 International Affairs Building, New York, NY 10027, USA; Department of Economics, University of California, Riverside, 900 University Avenue, 4128 Sproul Hall, Riverside, CA 92521, USA.

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1. Introduction

In real-world policymaking, policy changes that implement a new idea often require collective decision making by actors who have different beliefs about the effectiveness of the idea. In this situation, we might expect polarization of beliefs to intensify disagreement and result in political gridlock, since the decision maker who holds an extremely pessimistic view about the new idea would oppose its implementation. This paper, however, proposes a mechanism by which polarization of beliefs could do the opposite – it could motivate decision makers to agree upon policy experimentation, but by a Machiavellian consideration: the opponents of the policy are confident that they will gain political power relative to their colleagues after the experiment, because they believe that the experiment will prove them correct and their colleagues wrong.

This mechanism is primarily motivated by investigating an important question in political and development economics and economic history. The question is why China adopted a gradual, piecemeal, and experimental approach in its transition from the planned economy, starting in the late 1970s, instead of pursuing more of a full-scale, "Big Bang" approach, as the all-at-once approach is called in the literature (e.g., the surveys by Roland, 2000, 2002). Conventional wisdom assumes that the Chinese leaders were not certain about the outcome of pursuing the market reform, so they decided not to risk a more overarching reform. A more nuanced reading of the situation emerges, however, when we recognize the two prominent characteristics of Chinese politics of the time. First, from the late 1970s through the 1980s, there were opposing beliefs about market reform among the Communist Party leadership, with the conservative faction extremely conservative. Second, any radical policy change required consensus among the Party leadership. These observations transform the question into why the extremely conservative faction did not veto the experimental reform.

The key to the question is to recognize the political impact of learning through an experimental approach when heterogeneous beliefs exist. Not only can an experiment provide information about a particular reform; it can also indicate which faction was correct, and which incorrect. The correct side can expect to be rewarded in the form of stronger political power, while the incorrect side should be punished. If the two factions hold diametrically opposite beliefs, then *both* of them would be very confident in being proven correct by the experiment's result, and thus in being rewarded. Therefore, if the expected reward is sufficiently large, *both* of them would agree to the experimental approach.[1]

We formalize this mechanism of Machiavellian experimentation by use of a model in which two players within the same organization decide together whether and how to adopt a new policy. There are three options – a Big Bang approach with full-scale adoption; a pilot approach in which adoption will begin on a small scale and then be either generalized or stopped based on the experiment's result; and a default option in which no change occurs. The model has three key assumptions, which are tailored to the context of the Chinese transition but can be generalized beyond it.

Different priors. The two players have different priors about whether the policy will be effective in achieving the desired results, this disagreement is common knowledge, and the players do not infer anything from this disagreement. We label the player who holds the more optimistic belief about the policy *the reformer*, and the other player *the conservative*. Different priors commonly exist in politics, business, and other public or private policymaking (e.g., Sabatier, 1988; Bendor and Hammond, 1992; Mutz, 2008; Minozzi, 2013; Millner et al., 2014; Hirsch, 2016). This is the case because people can be endowed with different priors, just as they can be endowed with different preferences, and people can interpret public information in different ways under different psychological, cultural, or historical backgrounds. Different priors are especially prominent in intra-organizational debates if the organizations, e.g., technology-based companies, compete in a fast-changing environment (Eisenhardt et al., 1997). As seen in a significant and growing literature in economics, management, and political science (e.g., Van den Steen, 2002, 2010a, 2010b, 2010c; Che and Kartik, 2009; Millner et al., 2014; Hirsch, 2016), this assumption is useful in studying the implications of open belief disagreement.[2]

Consensus requirement. Any adoption of the policy requires consensus; otherwise, nothing will happen. In other words, both players can veto any adoption. It is common to see a consensus requirement in real world decision-making. For example, in the United States, the jury in a federal court must reach a unanimous verdict. In the Council of the European Union, decision-making about certain policy questions requires unanimity in voting. In the German two-tier board system of corporate governance, only decisions that garner consensus within the *Vorstand* (management board) will be referred to the *Aufsichtsrat* (supervisory board) for approval (Charkham, 1994). Consensus is usually required to protect decision makers from repercussions of unpopular decisions or to demonstrate unity to those outside the decision making process (e.g., Visser and Swank, 2007). Even if a consensus requirement is not explicitly written into decision-making rules, it can also apply *de facto* when decision makers are equally powerful, as we see in the example of the Chinese transition.

[1] A two-sentence explanation of our title, *Machiavellian Experimentation,* is needed here. First, as the reader might have already seen, we use the word, Machiavellian, in the general sense that the mechanism we propose is political, strategic, calculating, and somehow cynical. Second, one episode in Niccolò Machiavelli's *The Prince* (1947) contains a similar idea: just before the Second Italian War, in 1498, Pope Alexander VI did not oppose the Venetians' plan to invite Louis XII of France back to Italy, but "facilitated it by the annulment of the first marriage of King Louis," expecting that the coming of the French would eventually weaken the Venetians by creating disorder among the Italian states and helping the Pope and his son, Cesare Borgia, acquire Romagna, a strategic area in Italy.

[2] Theoretical works with heterogeneous priors can be traced back to Arrow (1964). Another tradition following Harsanyi (1967, 1968a, 1968b) and Aumann (1976) rules out "agreeing to disagree." For extensive discussions about preserving or breaking the common prior assumption, see Morris (1995), Gul (1998), Che and Kartik (2009), and Hirsch (2016).

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