European Journal of Political Economy 40 (2015) 395–417

Contents lists available at ScienceDirect

European Journal of Political Economy

journal homepage: www.elsevier.com/locate/ejpe

Behavioral political economy: A survey

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ARTICLE INFO

Article history:
Received 7 September 2014
Received in revised form 28 April 2015
Accepted 8 May 2015
Available online 16 May 2015

JEL classification:
D78
D03
A12

Keywords:
Behavioral political economy
Rational irrationality
Cognitive biases
Social norms
Voting
Paternalism

ABSTRACT

In explaining individual behavior in politics, economists should rely on the same motivational assumptions they use to explain behavior in the market: that is what Political Economy, understood as the application of economics to the study of political processes, is all about. In its standard variant, individuals who play the game of politics should also be considered rational and self-interested, unlike the benevolent despot of traditional welfare economics. History repeats itself with the rise of behavioral economics: Assuming cognitive biases to be present in the market, but not in politics, behavioral economists often call for government to intervene in a "benevolent" way. Recently, however, political economists have started to apply behavioral economics insights to the study of political processes, thereby re-establishing a unified methodology. This paper surveys the current state of the emerging field of "behavioral political economy" and considers the scope for further research.

1. Introduction

Explanations of individual behavior in politics should rely on the same motivational assumptions that guide the economic analysis of market behavior. And the systemic processes that generate political outcomes should be understood as reflecting the interplay of supply and demand. That is what Political Economy — to be understood as the application of economic analysis to the study of political processes — is all about. In its standard (neoclassical) variant, aligning the motivational assumptions means, of course, to model agents as maximizing their expected utility not only in the marketplace, but also in the political arena — as voters, politicians, lobbyists or bureaucrats. As Brennan (2008) emphasizes, though, *motivational* symmetry does not necessarily translate into *behavioral* symmetry, given the weak incentives to invest in rational decision-making that prevail in the realm of collective decision-making.[1] This holds in particular for voters, whose perfectly rational individual behavior may lead to catastrophic collective outcomes, because in the political arena, individual feedback and learning mechanisms are much weaker and more indirect than in the marketplace.

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[1] This point seems to be supported by Kirchgässner (2008), referring to Adam Smith's (1759) complex motivational theory.

http://dx.doi.org/10.1016/j.ejpoleco.2015.05.002
0176-2680/

Thus, we can expect cognitive biases to be at least as, and probably more important in politics than in the marketplace. Political Economy is therefore one of the fields particularly likely to benefit from applying behavioral economics insights. Strikingly, though, behavioral approaches in Political Economy are by and large a relatively recent phenomenon.[2] This may be due to the fact that the application of economic tools of analysis to the political sphere had been dominated by the Virginia School of Public Choice, whose members were busy exporting the rational choice approach to non-market areas of research, a project that seemed more urgent at the time than improving the economist's toolbox itself (Wallerstein, 2004). Things are more complex, though, when it comes to the leading figure in Public Choice, James Buchanan: While insisting on using a narrow version of *homo economicus* in constitutional economics, he was open to the use of non-standard behavioral assumptions to guide empirical research in Public Choice, and even believed non-standard assumptions to be more relevant in explaining decisions in politics than decisions in markets (Kirchgässner, 2014).[3] It is also noteworthy that parts of modern experimental economics can in fact be traced back to the Virginia School of Public Choice (Plott, in this issue). For obvious spatial restrictions, we will focus on *behavioral* political economy (which is partly informed by evidence gained in the lab), rather than on *experimental* political economy.[4] In general, behavioral economics and experimental economics are separate and only partly overlapping research fields (see, e.g., Heukelom, 2014 on their historical background).

In applying behavioral approaches to Political Economy, stating that individuals are more prone to biases and other cognitive problems when entering the political arena cannot be the end of the story. Rather, a systematic analysis of deviations from the baseline assumption of *homo economicus* is called for. Accordingly, many authors have encouraged scholars in the field to venture beyond the usual assumptions on rationality and utility-maximization (e.g. Simon, 1995; Ostrom, 1998; Kliemt, 2005).[5]

In this paper, we look at the essential contributions that have been made so far, and discuss promising avenues for future research. As to labels, we chose to follow Della Vigna (2009) and Berggren (2012) in speaking of "behavioral political economy" (henceforth BPE). We define BPE as the psychologically informed, economic analysis of behavior and its effects in the political arena.[6] We distinguish between a "weak" variant and a "strong" variant of BPE. The former merely alters specific auxiliary assumptions on either agents' cognitive capacities or willpower or the content of their utility functions, by arguing, for example, that voters not only care about political outcomes, but also about their "citizen duty" when going to the polls, or that they care about other aspects that seem irrelevant from a strictly instrumental standpoint, like a candidate's looks or considerations related to 'identity' (e.g. Berggren et al., 2010; Hillman et al., 2015–in this issue). In other words, weak BPE examines the implications of non-standard preferences, or cognitive biases — formerly known as "anomalies" — , as well as limits of attention and self-control, on the behavior of those active in the political arena.[7] Useful as they may be, we therefore exclude from BPE models that merely incorporate information asymmetries or uncertainty into an otherwise standard setting. The "strong" variant of BPE goes beyond this and attempts to actually *explain* (rather than just postulate) motivational and other psychologically informed extensions to the standard model. For instance, it may try to examine the mental processes causing differences in agents' susceptibility to certain biases. In the parlance of Simon (1978), while weak BPE joins orthodox economics in focusing on rational choice as a "product of thought", strong BPE takes account of the processes underlying and preceding choice itself. We will discuss contributions from both types of BPE in this paper. We have decided to refrain from recapitulating the most important insights of behavioral economics in a separate section, referring the reader instead to the excellent surveys by Rabin (1998), Camerer et al. (2004), and of course to Kahneman (2011).[8]

There are a number of intellectual ancestors to BPE. Not surprisingly, Adam Smith already ventured into this territory when speculating, first, that a key rationale for government to exist is to protect private property from the transgressions of those who depart from "reasonable" behavior (which, for Smith, implied acting morally). Second, he argued that rational individuals will underinvest in the quality of political decisions: As George Stigler observed, Smith was a pessimist in this respect in the sense that he "gave a larger role to emotion, prejudice, and ignorance in political life than he ever allowed in ordinary economic affairs" (Stigler, 1982: 140).[9] After Smith, the belief that individuals lose some of their capacity for well-informed, thorough reasoning upon entering the political sphere can be found, e.g., in Mill (1848), who in defense of laissez-faire warns of herd behavior in politics (Ch. XI,Section 3), incompetence

[2] This is not true for political science itself, where a "behavioral" strand developed in the 1960s, with a focus on the question whether poor voter competence affects the performance of democracies (e.g. Delli Carpini and Keeter, 1996; Lupia and McCubbins, 1998; Ashworth and Bueno de Mesquita, 2014). See also Wilson (2011).

[3] This ambivalence points to an interesting question that we will only sketch in passing: A *normative* case can be made for sticking to the *homo economicus* fiction when suggesting constitutional design, in order to make constitutional rules incentive-compatible (David Hume's well-known "knaves" argument). See, however, Frey (1997a) for the potential side-effects of such a strategy.

[4] On which see, e.g., Fiorina and Plott (1978); Plott (in this issue); Palfrey (forthcoming) and the surveys on political behavior in Plott and Smith (2008).

[5] From a methodological viewpoint, one may object, for instance, that the rationality assumption is essentially irrefutable: Under suitably redefined constraints, everyone can be described as acting rationally (e.g. Boland, 1981). As Pelikan (2010) shows, however, this perspective breaks down as soon as we leave the one-person setting and examine interactions with heterogeneous agents that differ in their degree of rationality. Thus, in the area of Public Choice we can safely treat rational choice as a refutable (and often refuted) empirical hypothesis. See, however, the caveat expressed in footnote 2, above.

[6] See Wallerstein (2004). The definition suggested by Della Vigna (2009: 361) seems too narrow: According to him, BPE is about how "politicians change their behavior to respond to voter biases" such as limited attention (Della Vigna, 2009: 364); he contrasts it from "behavioral institutional design", which is about the use of behavioral economics insights in designing policies (Della Vigna, 2009: 361, 364–365) and would then be closely related to "Behavioral Public Finance" (e.g. Mullainathan et al., 2012). "Behavioral Politics", suggested by Brennan (2008) seems to connote a normative bias. Berggren (2012: 199) defines BPE, also rather narrowly, as the application of the analytical tools of behavioral economics to "political decision-makers".

[7] Strictly speaking, merely introducing non-standard and non-procedural contents into the utility function should not qualify as BPE at all, since the orthodox approach is agnostic as to what an agent chooses, as long as its outcomes. We suggest that future discussions of the field should take this into account.

[8] See also Kamenica (2012).

[9] On Smith in this context see also Buchanan (1976). Smith's argument, however, is not a harbinger of the modern concept of rational ignorance. It is rather an institutionalist argument: Individuals, from landowners to monarchs, are simply not trained for making good political decisions, or their habits constrain them from making them. Smith sees ignorance and inaptitude as unfortunate realities in political affairs, but they are not explained themselves as the outcomes of a rational choice between alternatives.