

NBER WORKING PAPER SERIES

IDEOLOGY

Roland Bénabou

Working Paper 13907

<http://www.nber.org/papers/w13907>

NATIONAL BUREAU OF ECONOMIC RESEARCH

1050 Massachusetts Avenue

Cambridge, MA 02138

April 2008

This paper formed the basis for my Joseph Schumpeter lecture, given at the 22d Annual Congress of the European Economic association in Budapest, August 2007. I am particularly grateful to Jean Tirole, as the paper builds on much of our earlier joint work. I am also grateful for helpful comments to Daron Acemoglu, Rafael Di Tella, Xavier Gabaix, Mohammad Yildiz, Jean-Charles Rochet, Tom Romer, Karl Schlag, and Glen Weyl. Rainer Schwabe provided superb research assistance. Support from the Canadian Institute for Advanced Research is gratefully acknowledged. The views expressed herein are those of the author(s) and do not necessarily reflect the views of the National Bureau of Economic Research.

NBER working papers are circulated for discussion and comment purposes. They have not been peer-reviewed or been subject to the review by the NBER Board of Directors that accompanies official NBER publications.

© 2008 by Roland Bénabou. All rights reserved. Short sections of text, not to exceed two paragraphs, may be quoted without explicit permission provided that full credit, including © notice, is given to the source.

Ideology  
Roland Bénabou  
NBER Working Paper No. 13907  
April 2008  
JEL No. D72,D83,H11,P16,Z1

### **ABSTRACT**

I develop a model of ideologies as collectively sustained (yet individually rational) distortions in beliefs concerning the proper scope of governments versus markets. In processing and interpreting signals of the efficacy of public and market provision of education, health insurance, pensions, etc., individuals optimally trade off the value of remaining hopeful about their future prospects (or their children's) versus the costs of misinformed decisions. Because these future outcomes also depend on whether other citizens respond to unpleasant facts with realism or denial, endogenous social cognitions emerge. Thus, an equilibrium in which people acknowledge the limitations of interventionism coexists with one in which they remain obstinately blind to them, embracing a statist ideology and voting for an excessively large government. Conversely, an equilibrium associated with appropriate public responses to market failures coexists with one dominated by a laissez-faire ideology and blind faith in the invisible hand. With public-sector capital, this interplay of beliefs and institutions leads to history-dependent dynamics. The model also explains why societies find it desirable to set up constitutional protections for dissenting views, even when ex-post everyone would prefer to ignore unwelcome news.

Roland Bénabou  
Department of Economics  
and Woodrow Wilson School  
Princeton University  
Princeton, NJ 08544  
and NBER  
rbenabou@princeton.edu

“Social scientists have incorporated the costliness of information in their models, but have not come to grips with the subjective mental constructs by which individuals process information and arrive at conclusions that shape their choices....

“The subjective mental constructs of the 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.

Douglass North, (1990) *Institutions, Institutional Change and Economic Performance*.

## 1 Introduction

Coined on the eve of the 19th century by the Enlightenment philosopher and economist Destutt de Tracy, *ideologie* originally carried a hopeful connotation: it was to be a new “science of ideas” that would unify the social, political and moral sciences, starting from a common foundation in psychology.<sup>1</sup> Over the next two hundred years, the word took on a variety of less positive meanings (starting with Marx and Engels’ writings on the subject) and today it most often designates a system of beliefs that some group collectively upholds and maintains rigidly, even though it involves a substantial degree of reality denial or “false consciousness”. It also implicitly conveys the notion of ideologies as competing and mutually incompatible worldviews.

In this paper I take ideology in both senses of the term. First, as an exercise in the study of ideas, by providing a model and describing recent work that answers the call for incorporating into political economy a more accurate representation of individuals’ “subjective mental constructs”. Second, by showing how these interact across agents and with institutions to generate *social cognitions* that rest on distorted perceptions of reality, yet persist over time.

In doing so, I focus more concretely on one perennial ideological battleground: the relative merits of the market and the state. Figure 1 provides a good illustration of the range and clustering of these beliefs. Among Americans, for instance, about 72% express confidence in the free-market system and free enterprise –predictably above the survey’s average of 65%, but below China’s striking 74%. Among the French, only 36%, or *half as many*, agree –even lower than Russia’s 43%, and considerably below neighboring Germany’s 65%.

These are striking differences, and they have real meaning. In Figure 2, I plot the size of the government’s “footprint” in the economy, measured by the share of taxes in GDP, against the extent of free-market beliefs in the country (from Figure 1). This reveals a negative and significant correlation, consistent with the view that popular beliefs shape policy, not just in

---

<sup>1</sup>Antoine Louis Claude, comte Destutt de Tracy (1754-1836), in his *Eléments d’Idéologie*, published between 1801 to 1815. De Tracy’s own political views favored republicanism, liberalism and free markets. He was an admirer of American democracy and, conversely, Thomas Jefferson was an admirer of his work, translating into English his *Treatise on Political Economy*.

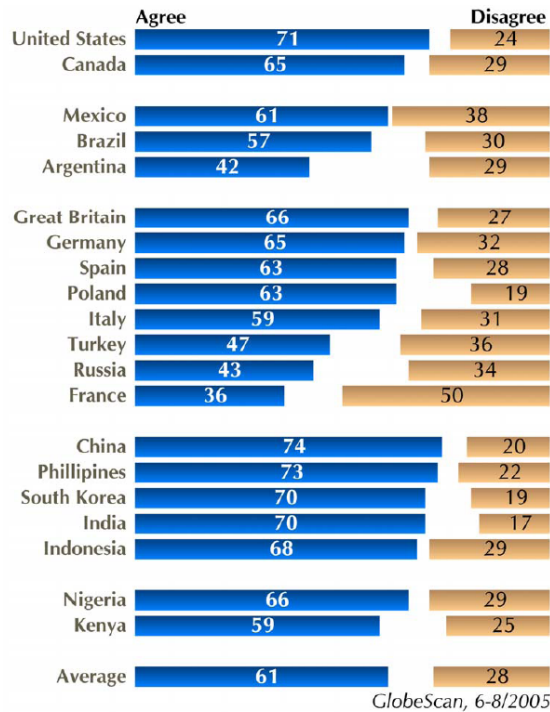


Figure 1: Responses to the statement: “The free enterprise system and free market economy is the best system on which to base the future of the world.” Source: World Public Opinion Survey (2005).

democracies.<sup>2</sup> The question, however, is where these beliefs come from and how they can persistently diverge, especially in an age of widely available and cheap information. Another piece of the puzzle is that within any given country, the dominant beliefs are often demonstrably at odds with the facts.<sup>3</sup> Nonetheless they endure, and the power of collective reality-avoidance and adherence to comforting myths is often seen as a significant obstacle to necessary reforms.

To analyze these issues, I develop in this paper a simple model of ideology as *collectively sustained reality distortions* about the merits of state versus market. Agents vote over the extent to which a good with long-run payoffs such as education, health insurance, or pensions should be publicly provided or left to individual decisions. They also allocate their disposable income in ways that reflect their expectations of what the state or market will ultimately deliver. The relative efficacy of public and private provision is a priori uncertain. Agents observe a common signal about this variable (e.g., performance in the past or in other areas), which they can then

<sup>2</sup>Other measures, such as the restrictiveness of labor laws or overall regulation in the economy lead to similar results, but are available for only a smaller sample of countries (ten to twelve OECD nations).

<sup>3</sup>See, e.g., Kaiser Foundation et al. (1996a) and Caplan (2007) on the public’s distorted views of competition, firms and international trade; Kaiser Foundation et al. (1996b) on their distorted views of government; Gilens (1999), Kuklinski et al. (2000) and Alesina and Glaeser (2004) on misperceptions and stereotypes about welfare programs and the poor.

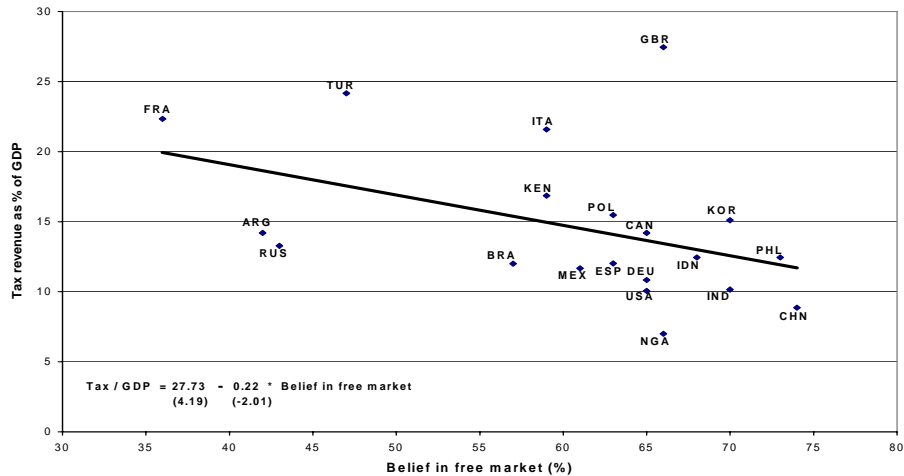


Figure 2: Free-market beliefs and size of the state. Source: author’s calculations, based on data from World Development Survey (2005) and World Development Indicators (2004).

process objectively or subjectively: paying attention to and acknowledging it, or on the contrary dismissing it, rationalizing it away and more generally minimizing their awareness of its content. In doing so, each agent optimally trades off the value of maintaining a reassuring, hopeful view of their future prospects or those of their children (anticipatory utility) versus the costs of delusion, in particular misallocating their own resources.

The key point is that these “subjective mental constructs” are inevitably interdependent (as noted by North), even absent any built-in complementarities: the relative attractiveness of realism and denial depends on other agents’ voting and private decisions, and therefore on the extent to which they themselves embrace reality or avert their eyes from it. “Social cognitions” thus endogenously emerge. I first show how a realistic equilibrium, in which people acknowledge the limitations and burdens of the welfare state, can coexist with one in which they remain blind to them, embracing a *statist ideology* and voting for a large but ineffective government. I then show how the presence of market failures can give rise to the converse scenario, in which a realistic equilibrium associated with appropriate public interventions coexists with one dominated by *laissez-faire ideology* and blind faith in unhindered markets. The role of history –working through inherited public-sector capital and prior beliefs– in determining which ideology prevails is also investigated, with the interplay of beliefs and institutions generating path-dependent dynamics. Finally, the welfare analysis explains why societies find it desirable to set up (*ex-ante*) constitutional protections for the expression of dissenting views –guarantees of free speech, a free press, etc.– even when *ex-post* everyone (not just a majority) would want to ignore bad news or “kill” their messenger.

The model builds on and extends the motivated-beliefs and optimal-awareness (attention, memory) framework of Bénabou and Tirole (2002, 2004, 2006). It relates most closely to Bénabou (2007), in which I develop a general theory of “groupthink” as individually rational but collectively sustained episodes of wishful thinking in groups, organizations, and markets.

## 1.1 Related literature

The perceived merits and flaws of markets and governments are among a number of societal beliefs about “how the world works” that are attracting increasing attention from economists. Other important ones include those bearing on the role of effort versus luck in life outcomes,<sup>4</sup> the extent to which other people (or specific groups) can be trusted,<sup>5</sup> many aspects of culture and of course religion.<sup>6</sup> These beliefs all share with those displayed in Figures 1-2 five key features, which I take as constitutive of ideologies (good or bad):

1) They vary widely across countries (even similarly developed ones) and are correlated with important political and economic outcomes.

2) At the individual level, they are strong predictors of voter preferences (toward redistribution, regulation, criminal justice, etc.) as well as important personal behaviors (savings, entrepreneurship, etc.).

3) There is a tendency for each society or group to think that its vision or “model” is the right one, not just for itself but for others as well.

4) Inevitably since not everyone can be right, these beliefs are often clearly at odds with the relevant facts.<sup>7</sup>

5) Nonetheless they persist, displaying remarkable “immunity to evidence” and powerfully shaping the societies in which they take hold.

The idea that voters’ attitudes often reflects distorted beliefs which they are affectively, culturally or instrumentally attached to is common in political science and political psychology (e.g., Lane (1959), Lerner (1982), Hochschild (1981, 1996), Kuran (1995), Jost and Major (2001)).

Bénabou and Tirole (2006) provide a first model of such phenomena for a broad class of beliefs relating to the *long-term rewards for personal effort*: “just-world” beliefs about self-reliance and economic mobility, perceptions of the link between income and happiness, and

---

<sup>4</sup>See, e.g., Piketty (1995), Bénabou and Ok (2001), Fong (2001), Alesina et al. (2001), Alesina and La Ferrara (2005), Bénabou and Tirole (2006) and Di Tella et al. (2007).

<sup>5</sup>See, e.g., Tirole (1996), Tabellini (2006, 2008), Putnam (2007) and Guiso et al. (2007).

<sup>6</sup>On culture, see, e.g. Bisin and Verdier (2000, 2001), Guiso et al. (2006) and Fernandez and Fogli (2006). On religion, see e.g. Barro and McCleary (2003), Noland (2003), Guiso et al. (2003), Scheve and Stasavage (2006), and Levy and Razin (2007).

<sup>7</sup>On the distorted nature of popular beliefs, see the references in footnote 3; for their persistence, see also Ferrie (2005) on misperceptions of American “exceptionalism” in social mobility, and Alesina and Fuchs-Schündeln (2007) on attitudes towards government intervention in West versus former East Germany. Religion provides many other examples (for (3) as well as (5)), such as creationism versus evolution and geology.

religious doctrines offering different “afterlife incentives” for thrift and industriousness. In that model, optimistic beliefs about the fact that everyone will ultimately get their “just deserts” have a *functional* value: they help individuals motivate themselves or their children towards effort, educational investment, perseverance against adversity and away from the temptations of idleness, welfare dependency, etc. This motivation value, moreover, depends on the incentive properties of the institutions which agents face: it is higher in a society that carries out little redistribution than where marginal taxes are high and the safety net generous. Since the political outcome itself depends on what people believe, there can be two stable outcomes. A first, “American” equilibrium is characterized by a dominance of just-world beliefs (and resistance to contrary evidence), low redistribution, high effort and stigma attached to poverty. The second, “European” equilibrium is characterized by more “realistic pessimism” as the majority view, a more extensive welfare state, more blaming of poverty on luck and circumstances, and lower effort.<sup>8</sup>

In this paper I take up a different but equally important set of societal beliefs, namely those concerning the relative virtues of *markets and governments* in delivering goods and services, particularly those that have society-wide benefits such as education, health, or safety. I also emphasize the very different source of motivated beliefs (hedonic anticipatory feelings instead of instrumental self-motivation) that is relevant when uncertainty and the ideological debate bear on the value of public goods and interventions in the market, rather than on how individuals come to be rich or poor.

This research thus brings together two literatures. The first, emanating from the recent field of “economics and psychology,” focusses on cognitive dissonance, wishful thinking and other forms of self-deception or belief distortion.<sup>9</sup> The second, also fast-growing, stems from a wealth of recent survey data on variations in beliefs and values across countries, regions or social groups.<sup>10</sup> Beyond economics, the paper relates to the large literatures in social and political psychology on motivated individual beliefs and on competing “worldviews” at the societal level. It formalizes concepts such as “system justification” (Jost and Major (2001)), “social axioms” (Leung et al. (2002)), or “cultural cognition” (Kahan and Braman (2006)).

The motivated, evidence-averse nature of ideological beliefs makes them quite different from standard self-fulfilling expectations. In recent politico-economic models where different countries

---

<sup>8</sup>Alternative, “non-ideological” explanations are proposed by Piketty (1995), based on costly learning and heterogenous priors about the mobility process; and by Alesina and Angeletos (2005), based on self-fulfilling, accurate beliefs about the extent to which individual incomes result from productive investments.

<sup>9</sup>On cognitive dissonance and belief distortion see, e.g., Akerlof and Dickens (1982), Schelling (1986), Kuran (1993), Carrillo and Mariotti (2000), Bénabou and Tirole (2002, 2004), Battaglini et al. (2005) and Dessi (2005). On anticipatory utility, see e.g. Loewenstein (1987), Caplin and Leahy (2001), Landier (2000), Caplin and Eliaz (2003), Brunnermeier and Parker (2005), Köszegi (2006, 2007), Bernheim and Thomsen (2005) and Bénabou and Tirole (2007).

<sup>10</sup>In addition to the references cited earlier see also Greif (2006), Cervellati et al. (2006), Corneo and Jeanne (2007) and Saint Paul (2007).

are identified with multiple rational-expectations equilibria,<sup>11</sup> voters’ beliefs in each country correspond objectively to the statistical reality they observe. They would also never refuse information ex-ante or process it in a biased way ex-post, but treat good and bad news as equally valuable increments to their information set. For the same reason, ideological thought is quite different from the public misrepresentation of one’s true beliefs due to threat of repression or social sanctions (e.g., Kuran (1995)); and very different as well from the off-the-equilibrium paths beliefs used as threats to sustain certain social outcomes in repeated-game models of culture (e.g., Greif (2006), Anderlini et al. (2007)). Ideology as motivated cognition also differs from a view based on outright indoctrination, though the two are highly complementary. Indeed, while agents are modeled here as distorting their own processing of information, a near-identical model applies to parents who strategically shape the beliefs of their children.<sup>12</sup> Moreover, agents’ endogenous “demand” for beliefs can also be read as a differential *receptivity* to propaganda supplied by competing political parties, interest groups and other political entrepreneurs.<sup>13</sup>

## 2 Ideology: the state or the market

I now turn to the study of a particular set of “ideas”, namely those concerning the proper scope of governments and markets.

Drawing on a large comparative survey of American voters and economists (Kaiser Family Foundation et al. (1996a)), Caplan (2007) presents extensive evidence of “anti-market bias”: distrust of the profit motive, unfairness of price allocations, perception of competition as a rigged, negative-sum game, desire to protect existing jobs against technological change and especially foreign competition, etc. His explanation is that voters derive consumption value from beliefs, and since holding incorrect ones is of little personal consequence because each vote has a negligible chance of mattering, they freely indulge in a number of exogenous “feel-good” biases. The present analysis will share this emphasis on the consumption value of beliefs but also differ in several important ways.

First, why (or when) should anti-market beliefs and blind faith in public bureaucracies make voters “feel better” than anti-state beliefs and blind faith in the invisible hand? The international evidence shown in Figures 1 and 2 reveals substantial variations in these beliefs across countries, which a theory of emotionally-thinking voters should aim to address. Second, there are also common instances of anti-government, pro-market bias. For instance, in spite of massive, textbook-case market failures in the employer-based system of health insurance, a large share of American voters still perceives and fears as inefficient and bureaucratic “socialized

---

<sup>11</sup>See, e.g., Bénabou (2000), Acemoglu and Robinson (2001) and Alesina and Angeletos (2005).

<sup>12</sup>See Bénabou and Tirole (2006) for such an equivalence in the context of anti- and pro-redistributive ideologies.

<sup>13</sup>See, e.g., Hochschild (1996), Gilens (1999), Alesina and Glaeser (2004), Glaeser (2005) and Saint Paul (2007) for work emphasizing this “supply” side of politico-economic beliefs.



medicine” the type of single-payer or centrally regulated system found in most other countries.<sup>14</sup>

To analyze these issues, one needs to explicitly model both the economic and the psychological costs and benefits of different worldviews, and in particular how they depend *endogenously* on the current or anticipated politico-economic environment.

## 2.1 The model

**1. Technology.** A continuum of risk-neutral individuals,  $i \in [0, 1]$ , are endowed with 1 unit each of perfectly divisible labor. Labor can be transformed into a taxable market good at a rate of 1 for 1, or into home production or other non-taxable forms of output at a rate of 1 to  $\bar{\tau} < 1$ . The highest feasible tax rate is thus  $\bar{\tau}$ , and the revenue from any rate  $\tau \leq \bar{\tau}$  is equal to  $\tau$ .

In period 1, agents use some of their disposable resources to accumulate human capital, broadly defined (education, health), retirement assets, or some other good that might have external effects. Such investment can take place both privately and through government provision (e.g., public education or pension system), according to the technology:

$$(1) \quad h^i = \min \{ \gamma e^i + \theta \tau, E \},$$

in which  $E < \gamma$  is some fixed maximal level.<sup>15</sup> The productivity of private expenditure is a known  $\gamma > 1$ , whereas that of public provision is uncertain (it could also be the reverse):  $\theta = \theta_H$  in state  $H$  and  $\theta = \theta_L$  in state  $L$ , with prior probabilities  $q$  and  $1 - q$  respectively, and

$$(2) \quad 0 \leq \theta_L < \gamma < \theta_H < E/\bar{\tau}.$$

The state could thus be less efficient than the market, or more. At the same time, government resources are limited, so some private investment is always needed ( $\bar{\tau}\theta_H < E$ ). Note also that  $\theta\tau$  is net of collection and administrative costs and could thus incorporate a deadweight loss, whether as a fixed proportion or as itself a source of uncertainty. In period 2, each agent, or his offspring, will have income (or some equivalent payoff)

$$(3) \quad y^i \equiv \alpha h^i + (1 - \alpha)\bar{h},$$

where  $\bar{h}$  is the population average and  $1 - \alpha \geq 0$  represents the extent to which  $h^i$  is of a public-good nature, generating a spillover for the rest of society. The presence of such spillovers will strengthen the results, but is not essential. It is also important to note that there is *no assumed*

---

<sup>14</sup>See, e.g., Krugman and Wells (2006) and references therein. Recall that the model developed below can also be interpreted as explaining why agents are likely to be differentially receptive to arguments or propaganda from different sides of a contested issue.

<sup>15</sup>This specification is chosen for simplicity, as it allows for substitutability between public and private investment (making policy a choice between the two) while preserving the linearity of the model.

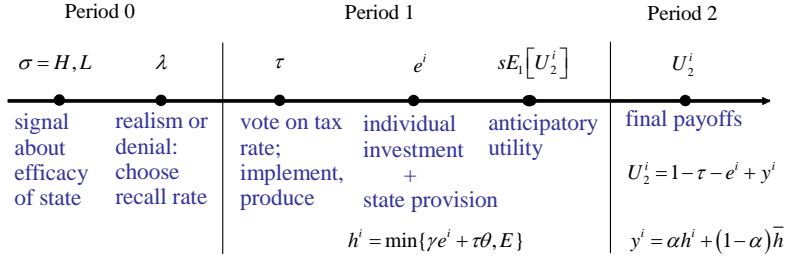


Figure 3: The state and the market: timeline

*complementarity* between agents' choices.

**2. Preferences and decisions.** During period 1, agents first vote on the tax rate  $\tau$ , then make their individual investments,  $e^i$ ; see Figure 3.<sup>16</sup> The remainder of their disposable income is saved until period 2, at which time it is consumed (or split between consumption and a bequest), resulting in final utility<sup>17</sup>

$$(4) \quad U_2^i = 1 - \tau - e^i + y^i.$$

The only payoff received by an agent during period 1 stems from thoughts and feelings about his future prospects. Thus, from the time when  $\tau$  and the  $e^i$ 's are chosen and until all uncertainty is resolved at  $t = 2$ , agent  $i$  experiences a flow of *anticipatory utility*  $sE_1^i[U_2^i]$ , where  $s \geq 0$  parametrizes the importance of hope, anxiety, dread, and similar emotions. This parameter (which stands for “savoring”) also typically increases with the length of period 1.<sup>18</sup> Anticipatory feelings could also occur prior to the determination of public and private investments; I leave this extension to the appendix and will simply mention in the text the one place where it matters.

Given the tax rate, individual investment is chosen so as to maximize the discounted value

<sup>16</sup>Since agents know  $\tau$  when they choose effort, multiple equilibria due to standard “increasing fiscal returns” or “battle of the sexes” mechanisms between the private and public sectors are –intentionally– ruled out. The mechanism is also very different from that in Bénabou and Tirole (2006), as  $\tau$  is here a lump-sum tax and thus has no incentive effect. The psychological motive underlying belief distortions also differs, as explained earlier.

<sup>17</sup>The assumption that agents only want to consume in period 2 is inessential, as is the zero interest rate. It just simplifies the exposition by making standard, material consumption (derived from the resources  $1 - \tau - e^i + y^i$ ) and “belief consumption” take place in separate periods, rather than having some of both occur in period 1. For the intergenerational interpretation, let a parent have utility  $v(c, b, y) \equiv c^\beta (b + y)^{1-\beta} / \beta^\beta (1 - \beta)^{1-\beta}$  over old-age consumption  $c$ , her financial bequest to her child  $b$ , and the latter’s effective human capital endowment  $y$ , given by (3). Given any initial inherited wealth  $b'$ , parent  $i$ ’s lifetime budget constraint is  $c^i + b^i + y^i = b' + 1 - \tau - e^i + y^i$ . This is also her maximized date-2 utility  $v^i$ , which thus differs from  $U_2^i$  only by a constant.

<sup>18</sup>See, e.g., Caplin and Leahy (2001), Köszegi (2006, 2007), Brunnermeier and Parker (2005) or Bénabou and Tirole (2007). The linear specification,  $sE_1^i[U_2^i]$ , avoids exogenously building into the model either information aversion or information-loving.

of payoffs

$$(5) \quad U_1^i = sE_1^i [U_2^i] + \delta E_1^i [U_2^i],$$

which means maximizing  $E_1^i [U_2^i]$ . At  $t = 1$ , an agent with belief  $\mu^i$  that the state is  $H$  thus solves

$$(6) \quad \max_e \left\{ 1 - \tau - e + \alpha \left[ \mu^i \min \{ \gamma e + \theta_H \tau, E \} + (1 - \mu^i) \min \{ \gamma e + \theta_L \tau, E \} \right] \right\}.$$

Naturally, someone who is more optimistic about the public provision of education or retirement income (say) will rely less on the market. In particular, as long as

$$(7) \quad \alpha \gamma > 1 \geq (1 - q) \alpha \gamma,$$

an agent who has no credible information beyond his prior ( $\mu^i = q$ ) will only invest  $e^i = (E - \tau \theta_H) / \gamma$ , whereas one who knows that the state is  $L$  ( $\mu^i = 0$ ) will invest  $e^i = (E - \tau \theta_L) / \gamma$ .

An agent's beliefs at  $t = 1$  depend on the news received at  $t = 0$  and how he processed them – accepting reality or averting his eyes from it, as specified below. In doing so, he acts so as to maximize the discounted utility of all payoffs

$$(8) \quad U_0^i = -M + \delta E_0^i [sE_1^i [U_2^i]] + \delta^2 E_0^i [U_2^i],$$

where  $M$  represents the date-0 costs, if any, of his information-processing strategy and  $E_t^i$  reflects his beliefs at date  $t = 0, 1$ . Equation (8) embodies the key tradeoff between having accurate beliefs at  $t = 1$ , which leads to decisions that maximize  $E_0^i [U_2^i]$ , and having hopeful ones, which raises  $E_1^i [U_2^i]$ .

**3. Information and beliefs.** To represent agents' optimal processing of information I use a variant of the recall or awareness “technology” from Bénabou and Tirole (2002, 2006). At  $t = 0$ , agents observe a common signal about the efficacy of state intervention:  $\sigma = H, L$ , with probabilities  $q$  and  $1 - q$  respectively.<sup>19</sup> This could be a measure of past performance, the policies and outcomes of other countries, an expert study, or media reports. Each agent then has some flexibility in how much attention to pay to this data, how to interpret it, whether to “keep it in mind” or “not think about it”, etc. Formally, he can :

(a) Accept the news realistically, thus truthfully encoding  $\hat{\sigma}^i = \sigma$  into memory or awareness (his date-1 information set).

---

<sup>19</sup>The fact that  $\sigma$  is fully informative about  $\theta$  is only a simplifying assumption; nothing changes if the signal is noisy. The perfect correlation of signals across individuals is chosen for the same reason (it just needs to be high enough) and to make clear that the mechanism at work here has nothing to do with herding or informational cascades, in which agents with private signals make inferences from each other's behavior.

(b) Engage in denial or censoring, thus encoding  $\hat{\sigma}^i = H$  instead of  $\sigma = L$ , or  $\hat{\sigma}^i = H$  instead of  $\sigma = L$ . In addition to distorting later decisions, this may entail an immediate cost  $m \geq 0$ .

(c) Deal in partial truths, by using a mixed strategy. The relevant (stable) equilibria of the model, however, will turn out to be in pure strategies.

Instead of “tuning out” unwelcome news (denial), selective awareness can also be pursued by investing more resources in retaining good ones (rehearsal, preserving evidence), when accurate information retention is naturally imperfect but can be raised at some cost (this is like setting  $m < 0$  in the above specification). Both mechanisms lead to broadly similar results and can be combined: what matters is that there be a possibility (and a motive) for differential awareness of  $H$  and  $L$ , not how this is achieved. As mentioned earlier, ideological thought typically involves willful inattention, distorted interpretations and repression of inconvenient facts, ex-post rationalizations, etc. The model therefore emphasizes “optimal forgetting” or obfuscation rather than than “optimal remembering”.

Given (1) and (8), it is easy to see that it is only in state  $L$  that agents may want to censor their signal: someone with anticipatory utility would not want to substitute bad news for good ones. I therefore focus here on cognitive decisions in state  $L$ , denoted simply

$$(9) \quad \lambda \equiv \Pr[\hat{\sigma} = L | \sigma = L].$$

Later on I consider more general payoffs structures than (1), under which either state may (endogenously) be censored.

While agents can process information selectively (or subjectively), their beliefs remain constrained by Bayesian rationality: at  $t = 1$ , agent  $i$  may no longer have direct access to the original signal, but if he (as others) has a systematic tendency toward selective attention or interpretation, he will take that into account, using Bayes’ rule to form posteriors. Thus, when  $\hat{\sigma}^i = L$  the agent knows that the state is  $L$ , but when  $\hat{\sigma}^i = H$  his posterior belief is only

$$(10) \quad \Pr[\sigma = H | \hat{\sigma}^i = H, \lambda^i] = \frac{q}{q + (1 - q)(1 - \lambda^i)} \equiv r(\lambda^i),$$

where  $\lambda^i$  is his *equilibrium* rate of realism.<sup>20</sup> In particular, for an agent who systematically censors bad signals, being aware of only good signals is uninformative,  $r(0) = q$ .

**4. Voting.** To keep the model as transparent as possible, I abstract from heterogeneity in preferences or productivities. The unanimity of votes that will result is clearly unrealistic, but could be eliminated by introducing “partisan” agents with fixed preferences for either zero

---

<sup>20</sup>It is straightforward to allow for agent naiveté, parametrized for instance by a coefficient  $\chi \leq 1$  multiplying  $(1 - q)(1 - \lambda^i)$  in (10). This leaves all the positive results unchanged but can affect the welfare conclusions. See Bénabou and Tirole (2002, 2006) for such a treatment, as well as extensive discussions of the experimental and field evidence on motivated beliefs and selective recall.

or maximal provision of government services.<sup>21</sup> Different social cognitions would then tip the majority rather than the whole electorate, but the basic message would remain unchanged (see Bénabou and Tirole (2006) for a similar effect in a redistributive-policy context). Finally, given the continuum of agents, there is no state of the world in which a single voter can be pivotal, hence no incentive for anyone to strategically alter his vote or his cognitive choices so as to upset the equilibrium. Agents are assumed to vote sincerely based on the information they have at the time ( $t = 1$ ) and, when making their initial information-processing decisions ( $t = 0$ ), to take the expected majority outcome as beyond their control.<sup>22</sup>

### 3 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.” (French President Jacques Chirac, July 14, 2005).

I now study the possibility of different societal beliefs, each associated to different public policies and private decisions. In doing so, I focus on symmetric pure-strategy equilibria:  $\lambda^j \equiv 1$  (Realism) and  $\lambda^j \equiv 0$  (Statist Ideology).

#### 3.1 Sustaining realism

When  $\lambda^j \equiv 1$ , everyone acknowledges what public policy can or cannot deliver and responds appropriately, investing  $e^j = (E - \tau\theta_L) / \gamma$  in state  $L$  and  $e^j = (E - \tau\theta_H) / \gamma$  in state  $H$ , achieving  $h^j = E$  in either case. A representative voter’s date-1 expected utility from implementing a policy  $\tau$  is thus  $s + \delta$  times

$$(11) \quad 1 - \tau - (E - \tau\theta_L) / \gamma + E$$

in the first case, and the same expression with  $\theta_L$  replaced by  $\theta_H$  in the second. Therefore, by (2), voters unanimously choose  $\tau_L = 0$  in state  $L$  and the maximum feasible rate  $\tau_H = \bar{\tau}$  in state  $H$ .

Since the policy outcome is *different in each state*, any agent who had censored at  $t = 0$  the fact that  $\sigma = L$  will be inescapably confronted again with that reality at  $t = 1$ , thus depriving him of the benefits of wishful thinking (and leaving his investment undistorted). Anticipating

---

<sup>21</sup>For instance, some agents for whom  $\theta^i \equiv 0$  in both states and  $\alpha^i = 0$ , and others for whom  $\theta^i \equiv \theta_H$  in both states and  $\alpha^i = 1$ .

<sup>22</sup>This simplifies the analysis and is realistic. At the same time, it is not essential to the results -what matters is that there be *some* aspect of the equilibrium environment that lies beyond their control (e.g., capital stocks inherited from past generations’ political choices as in Section 5 below, or other agents’ private behavior as in Bénabou (2007)).

this, no one will invest in denial, which would only waste the cost  $m$ . Consequently,  $\lambda = 1$  is always an equilibrium.

This result reflects a first general idea: interacting with realists makes it more difficult to sustain delusions; conversely, the more others avoid the truth, the easier it is for one to avoid it –if so desired.<sup>23</sup> While this is straightforward, note how information aversion reverses a key property of standard models in which agents value accurate signals. In such models, their decisions are naturally substitutes: the more others invest in obtaining private signals, the more informative is the market price (or other aggregate variable), and thus the lower each individual’s incentive to pay for information (Grossman and Stiglitz (1980)). When people seek instead to avoid, dismiss or distort unwelcome information, their actions are complements: the more others ignore or distort their signals, the more effectively each one can do so.

In the present context, this general mechanism has the stark implication that  $\lambda = 1$  is sustainable as a social equilibrium for all values of  $s$ . This, however, is due to the assumption that when agents experience anticipatory feelings, they are no longer in doubt over which policy has prevailed – only over what its long-run effects will be. More generally, when anticipation also occurs *prior* to the determination of  $\tau$ , with importance  $s\phi$ ,  $\lambda = 1$  is an equilibrium when<sup>24</sup>

$$(12) \quad s \leq \frac{m/\delta\phi}{(\theta_H/\gamma - 1)\bar{\tau}} \equiv \hat{s}.$$

The numerator reflects the absence of choice distortion (the only private cost of denial is  $m$ ), while the denominator represents the financial savings agents can hope to realize by implementing an effective public policy in the good state.

### 3.2 Sustaining ideology

When  $\lambda^j \equiv 0$ , agents avert their eyes from the limitations and burdens of the welfare state and “read” both signals as  $H$ , resulting in a constant posterior  $r(0) = q$  on the state truly being  $H$ . From (7), they respond to  $\tau$  by investing  $e^i = (E - \tau\theta_H)/\gamma$ , which is the optimal amount in state  $H$  but falls short by  $\tau\Delta\theta/\gamma$  in state  $L$ . A representative voter at date 1 is one citizen *inter alia* with posterior belief  $q$ , so his expected utility from implementing a tax rate  $\tau$  is now  $s + \delta$  times

$$(13) \quad 1 - \tau - (E - \tau\theta_H)/\gamma + qE + (1 - q)(E - \tau\Delta\theta).$$

---

<sup>23</sup>On a related point, Kuran (1993) contains an interesting (albeit informal) discussion of potential mechanisms by which ideas which are not explicitly expressed in society may eventually come to disappear from it.

<sup>24</sup>For instance, anticipatory payoffs may be proportional to the duration of the relevant period of uncertainty:  $s' = \phi s$  and  $s'' = (1 - \phi)s$ , where  $s$  is some baseline intensity and voting takes place at date  $1 + \phi$ . I focus the exposition on the case  $\phi = 0$ , so that  $\hat{s} = +\infty$ , and treat the more general case in the appendix.

The net marginal value of  $\tau$  is positive, provided

$$(14) \quad \theta_H/\gamma > 1 + (1 - q) \Delta\theta,$$

and voters ignorant or in denial about the true state will then choose  $\tau_H = \tau_L = \bar{\tau}$ .

As the prevailing policy no longer reveals the state of the world, it is now *feasible* for an agent to maintain ignorance of a signal he initially censored. To determine whether it is *optimal* for him to remain blind to “government failures”, consider his cognitive problem at  $t = 0$ , in state  $L$ .

If he retains the bad news, he will correctly invest  $e^i = (E - \bar{\tau}\theta_L)/\gamma$  but have to live with the knowledge that the taxes levied are unproductive and that everyone else is underinvesting due to their excessive faith in the state, with adverse implications for his or his offspring’s future prospects. His expected intertemporal utility will thus be ( $R$  stands for “realism”):

$$(15) \quad U_{0,R}^i \equiv \delta (s + \delta) [1 - \bar{\tau} - (E - \bar{\tau}\theta_L)/\gamma + \alpha E + (1 - \alpha) (E - \bar{\tau}\Delta\theta)].$$

If the agent goes along with the prevailing ideology, he too will underinvest, but be able to maintain, in proportion to  $r(\lambda^i)$ , the comforting hope of a better future in which public expenditure will prove effective and there will be no shortfall of the public good. Hence ( $D$  stands for “denial”):

$$(16) \quad \begin{aligned} U_{0,D}^i &= -m + \delta (s + \delta) [1 - \bar{\tau} - (E - \bar{\tau}\theta_H)/\gamma] \\ &\quad + \delta s [r(\lambda^i)E + (1 - r(\lambda^i)) (E - \bar{\tau}\Delta\theta)] + \delta^2 [E - \bar{\tau}\Delta\theta]. \end{aligned}$$

Agent  $i$ ’s ex-post incentive to repress negative news, given that others are doing so ( $\lambda^j = 0$ ) and that his own habitual (or conjectured) degree of truthfulness is  $\lambda^i$ , is thus:

$$(17) \quad (U_{0,D}^i - U_{0,R}^i) / \delta = -m/\delta - (s + \delta) (\alpha - 1/\gamma) \bar{\tau}\Delta\theta + sr(\lambda^i)\bar{\tau}\Delta\theta.$$

The first two terms are the costs of denial –direct cost plus underinvestment. The last term is the gain in anticipatory utility: by maintaining hope that  $\theta = \theta_H$  the agent avoids facing the fact that, due to others’ ideological blindness, society is on the wrong track, wasting resources and ending up with a suboptimal level of (say) education or health  $\bar{h}$ .

This reflects a second (and more novel) general insight, which in Bénabou (2007) I termed the *Mutually Assured Delusion* (MAD) principle: when others’ denial of an unpleasant reality leads them to act in ways that further worsen an agent’s prospects, this increases his own incentive to engage in wishful thinking, making cognitive strategies *complements*. Conversely, when others’ ignorance of bad news is beneficial, that news become less hard to face and cognitive strategies

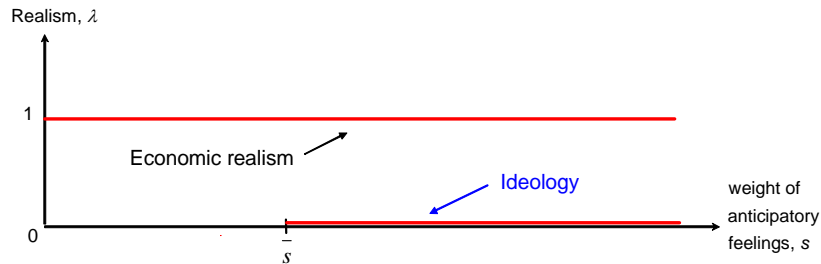


Figure 4: Societal beliefs on state versus market

are substitutes. The political and economic interactions considered here clearly belong to the first case. Indeed, when an ideological electorate votes for the wrong policy, each citizen suffers an expected loss (fiscal channel).<sup>25</sup> Moreover, if people's distorted view of what the state or market will deliver leads them to underinvest in their children's education, undersave for their retirement, etc., there will be further collective losses to bear (interactions channel). Hence the following results, illustrated in Figure 4.

**Proposition 1 (*Statist ideology*)** 1) Assume (2), (7) and (14). For

$$(18) \quad s \geq \frac{m/\delta + \delta(\alpha - 1/\gamma)\bar{\tau}\Delta\theta}{(q - \alpha + 1/\gamma)\bar{\tau}\Delta\theta} \equiv \bar{s},$$

both realism ( $\lambda = 1$ ) and collective denial ( $\lambda = 0$ ) are equilibrium social cognitions. In the latter, agents believe in and vote for a large government, in spite of good evidence that it is inefficient.<sup>26</sup> 2) The more important the spillovers from a good, and the worse the efficiency of the state in providing it, the more likely is statist ideology:  $\bar{s}$  falls with  $1 - \alpha$  and (for  $m > 0$ ) with  $\theta_L$ .

Observers of continental Europe frequently note and puzzle at the persistent power of collective reality-avoidance and adherence to comforting myths in preventing necessary reforms of welfare states and statist economies.<sup>27</sup> Proposition 1 sheds light on this phenomenon and on the conditions that make it more likely. The first one, unsurprisingly, is a more favorable prior (a higher  $q$ ), perhaps inherited from a previous period of war reconstruction during which extensive state intervention was indeed effective, even indispensable. Second, the more important is the public-good nature of the activity under consideration (e.g., education versus pensions),

<sup>25</sup>In a symmetric context. Looking at tax and spending policies with unequal incidence is a natural direction for further research.

<sup>26</sup>When agents derive anticipatory utility both prior to and after the setting of  $\tau$ , with importance  $s' = \phi s$  and  $s'' = (1 - \phi)s$  as in footnote 24, (18) is unchanged but (12) is now required for the  $\lambda = 1$  equilibrium to exist. For  $\bar{s} < \hat{s}$ , these two conditions define an interval for  $s$  leading to multiplicity.

<sup>27</sup>See, e.g., on the case of France, Krugman (1997), Landier and Thesmar (2007), De Menil (2007) and Saint-Paul (2007). The latter two authors also point to France's extreme position in the World Public Opinion Survey (2005) reported in Figure 1.



the easier it is to sustain collective illusions concerning it. At the same time, the public-finance link *alone* can suffice to give rise to ideological thinking: the proposition holds for  $\alpha = 1$ .

The third result is somewhat striking: *the worse* the failings of a statist system, the greater is the likelihood that agents will fall prey to ideological blindness –for which they pay personal costs, including suboptimal investments in human or retirement capital.<sup>28</sup> While this stark form of the result is somewhat specification-dependent, it points to more general message: a worsening of state performance need not speed up reform, but can instead trigger ideological “defenses” that will block or delay it further, until reality finally hits in a way that can no longer be ignored or rationalized away.

### 3.3 Social welfare

This leads naturally to the question of whether social beliefs bearing on governments and markets are ultimately useful or harmful to society. To answer it, I compare social welfare under realism and denial –whether achieved as equilibria, or through some collective commitment mechanism (such as considered later on).

Consider first state  $\sigma = L$ , which occurs with probability  $1 - q$ . When agents are realists (setting  $\lambda^j = 1$  in (15)), equilibrium welfare is  $U_{L,R}^* = \delta(s + \delta) [1 - E/\gamma + E]$ . When they are deniers (setting  $\lambda^j = 0$  in (16)), it is:

$$(19) \quad U_{L,D}^* = -m + \delta(s + \delta) [1 - E/\gamma + E + \bar{\tau}(\theta_H/\gamma - 1) - \bar{\tau}\Delta\theta] + \delta sq\bar{\tau}\Delta\theta,$$

where the last term reflect the value of maintaining hope in the efficacy of the state.

**Proposition 2** *1) Following bad news (state L), there is a threshold  $s^* \geq \bar{s}$  such that realism leads to higher welfare than statist ideology if and only if  $s < s^*$ . When  $s^* > \bar{s}$  either equilibrium can lead to higher ex-post welfare, depending on  $s$ .*

*2) When  $s^* < \bar{s}$ , where statist ideology is an equilibrium it dominates realism, and for  $s \in (s^*, \bar{s})$  agents would be better off in state L if everyone could commit to ignoring bad news.*

Consider now welfare in state  $H$ , which occurs with probability  $q$ . Given (14), in both equilibria the tax rate is  $\bar{\tau}$  and agents invest  $e^j = (E - \bar{\tau}\theta_H)/\gamma$ . When  $\lambda = 0$ , however, they cannot be sure of whether the signal was truly  $H$ , or it was really  $L$  and they censored the bad news, in which case everyone will underinvest. Due to this “rational doubt”, welfare in state  $H$

---

<sup>28</sup>By contrast, a downward shift in the entire probability distribution of what public intervention is capable of achieving relative to the market, even in the best state (an increase in  $\gamma$ , which lowers  $\theta - \gamma$  uniformly across states) reduces the scope for statist ideology. Note also that if the pure cost of information censoring  $m$  increases in proportion to the “size” of the news  $\Delta\theta$ , a change in  $\theta_L$  or  $\theta_H$  leaves the equilibrium set unchanged.

is now lower in an ideological society:<sup>29</sup>

$$(20) \quad U_{H,R}^* = \delta(s + \delta) [1 - E/\gamma + E + \bar{\tau}(\theta_H/\gamma - 1)],$$

$$(21) \quad U_{H,D}^* = U_{H,R}^* - s(1 - q)\bar{\tau}\Delta\theta.$$

Averaging over the two states, finally, the gain from raising expectations in state  $L$  and the loss from lowering them in state  $H$  (last terms in (19) and (21) respectively) just cancel, reflecting Bayes' rule. The net welfare impact of denial is thus an unambiguous loss

$$(22) \quad U_{0,D}^* - U_{0,R}^* = -(1 - q)[m + \delta(s + \delta)\bar{\tau}(1 - \theta_L/\gamma + \Delta\theta(1 - 1/\gamma))],$$

incurred in state  $L$ .

**Proposition 3** 1) *Following good news (state  $H$ ), welfare is always higher, the more realistic agents are when faced with bad news (state  $L$ ).*

2) *Ideology always lowers ex ante welfare.*

Thus, even when ideological thought generates social welfare gains in state  $L$ , those are always dominated by the losses it induces in state  $H$ . This normative result has important positive implications for how societies deal with “unwelcome news” and those bearing them.

### 3.4 Ideology, dissent, and freedom of speech

Suppose now that, in state  $L$ , an individual or group with a lower  $s$  or a different payoff structure attempts to bring (back) to everyone's attention evidence of the public sector's low efficiency. If this occurs after policy has already been set and agents have made their private investments, all it does is to reduce everyone's utility in (5), so they will refuse to pay attention or may even try to silence the dissenter (pay a new cost to eliminate the signal). Anticipating that others will behave in this way, in turn, allows everyone to more confidently engage in ideological denial. More strikingly, even bad news that comes in time to correct course can be unwelcome: when  $s > s^*$ , the citizens would rather keep their pleasant illusions and “stay the course” than admit to a bleak future. Bringing back evidence about the state really being  $L$  (and society's opportunity set thus disappointingly limited) will again make everyone worse off, leading to a universal unwillingness to listen and rejection of dissenters. And yet, ideological cognition *always* remains socially harmful *ex ante*. This tension provides a new rationale for why societies find it desirable to set up commitment mechanisms such as constitutional rights to free speech,

---

<sup>29</sup>This “shadow of doubt” cast over the good state by the censoring of the bad state could also distort some decisions in state  $H$ , although in this instance it does not. Conversely, departing from Bayesian updating, for instance by introducing a “naivete” coefficient  $\chi \leq 1$  multiplying  $1 - \lambda$  in (10), would attenuate the losses in state  $H$  and thus allow ex-ante gains. See Bénabou and Tirole (2002) for examples of both effects.

independence of the press, etc. If effective, these will ensure that bad news will most likely “resurface” *ex-post* in a way that is hard to ignore, thus lowering the *ex ante* return (or raising the cost) of investing in denial.

## 4 Laissez-faire ideology

“Capitalism is based on self-interest and self-esteem; it holds integrity and trustworthiness as cardinal virtues and makes them pay off in the marketplace, thus demanding that men survive by means of virtues, not of vices. It is this superlatively moral system that the welfare statisticians propose to improve upon by means of preventative law, snooping bureaucrats, and the chronic goad of fear” (Alan Greenspan, 1963).

The model so far helps explain the puzzle of countries that persist in an overoptimistic view of the effectiveness of the state –or of their own national brand of government intervention– relative to the market. The Mutually Assured Delusion principle cuts both ways, however, and can also take the form of anti-government ideology and blindness to market failures.<sup>30</sup> The example of health insurance in the United States was mentioned earlier, but other widespread anti-interventionist beliefs are also at odds with the facts. One is the public’s vast overestimation of the “excessive” shares of public spending going to domestic welfare, fraction of people on welfare, and level of welfare benefits, or the even larger perceptual biases found concerning foreign aid.<sup>31</sup> Another example concerns estate taxation, which many middle and working class voters implausibly perceive as likely to affect them or their children, and consequently oppose.<sup>32</sup>

To demonstrate the workings of laissez-faire ideology, I simply extend (1) to:

$$(23) \quad h^i = \min \{ \gamma e^i + \theta (\tau - \kappa), E \}$$

and distinguish two cases.<sup>33</sup>

---

<sup>30</sup>It is interesting, in that respect (and in light of the latest crisis in financial markets) to relate this section’s opening quotation to a later one: “An infectious greed seemed to grip much of our business community”... The trouble, unfortunately, is that the shock of what has happened will keep malfeasance down for a while. But *human nature being what it is –and memories fade–* it will be back. And it is important that at that time appropriate legislation be in place to inhibit activities that we would perceive to be inappropriate” (Alan Greenspan, 2002a,b; emphasis added).

<sup>31</sup>Thus, in Kuklinski et al. (2000), survey respondents’ average estimate of welfare’s share in the federal budget was around 9%, versus the actual 1%. All six measures of bias in factual beliefs about welfare were highly correlated across individuals, and powerful predictors of respondents’ attitudes towards the desirability of welfare cuts. On opposition to welfare, see also Gilens (1999) and Alesina and Glaeser (2004). On mistrust of government, see Kaiser et al. (1996b), and on foreign aid see that same source as well as the discussions and references in Caplan (2007).

<sup>32</sup>See, e.g., Bartels (2005), who analyses data from the 2002 National Election Survey. For instance, 49% of respondents believed that “most families have to pay” the tax, and among the 57% in favor of its repeal, 69% cited as a reason the fact that “it might affect YOU someday” The tax actually affects only affects 0.5% of estates.

<sup>33</sup>I focus here, as in the core part of Proposition 1, on the benchmark case in which agents already know the policy when they experience anticipatory feelings –e.g., the vote on  $\tau$  occurs at the start of period 1 ( $\phi = 0$ ).

a) When  $\kappa < \bar{\tau}$ , state  $H$  remains (conditionally on  $\tau = \bar{\tau}$ ) a more favorable state than state  $L$ . One can then show that the results of the case  $\kappa = 0$  carry through: for  $s$  large enough, a statist-ideology equilibrium coexists with the realistic one.<sup>34</sup>

b) Assume instead that  $\kappa > \bar{\tau}$ . One can then think of state  $H$  as a “market failure” state in which there is a need for government intervention but, even when carried out to its fullest, it will not suffice to restore the first best. The MAD intuition can then be simply expressed as follows: whereas agents “could live with” and realistically accept such a *second-best* situation, an uncorrected market failure (*third best*) is much harder to face, resulting in a greater incentive to maintain faith in the invisible hand (*first best*). Thus, alongside with the realistic equilibrium in which citizens have recourse to government intervention when necessary, there exists for  $s$  high enough an ideological one in which they systematically censor the signal  $\sigma = H$  and vote against public provision.

The parallelism between the two cases can be seen by recasting the second one in terms of the effectiveness of *market* provision relative to the government alternative:  $\tilde{\theta}_{\tilde{H}} \equiv -\theta_L$  in state  $\tilde{H} \equiv L$  and  $\tilde{\theta}_{\tilde{L}} \equiv -\theta_H$  in state  $\tilde{L} \equiv H$ , with respective probabilities  $\tilde{q} \equiv 1 - q$  and  $1 - \tilde{q}$  and voters choosing the *degree of laissez-faire* in policy,  $\tilde{\tau} \equiv \kappa - \tau \in [\kappa - \bar{\tau}, \kappa]$ . Apart from these substitutions, the only condition that differs is the one ensuring that agents acting on their priors now choose  $\tau = 0$ , which corresponds to the maximal value of  $\tilde{\tau}$ . As shown in the appendix, (14) is replaced by

$$(24) \quad \theta_L/\gamma < 1 - q\Delta\theta.$$

**Proposition 4 (*Laissez-faire ideology*).** *Assume (24) and let  $1 - q$  and  $\kappa$  respectively replace  $q$  and  $\bar{\tau}$  in each of the conditions stated for Proposition 1.*

1) *For*

$$(25) \quad s \geq \frac{m/\delta + \delta(\alpha - 1/\gamma)\kappa\Delta\theta}{(1 - q - \alpha + 1/\gamma)\kappa\Delta\theta} \equiv \bar{s},$$

*both realism ( $\lambda = 1$ ) and collective denial of market failures ( $\lambda = 0$ ) are equilibrium social cognitions. In the latter, agents distrust and vote against government provision in spite of good evidence that it is necessary and effective.*

2) *The more important the spillovers from a good, and the worse the market failure, the more likely is laissez-faire ideology:  $\bar{s}$  is decreasing in  $1 - \alpha$  and (for  $m > 0$ ) decreasing in  $\theta_H$ .*

---

<sup>34</sup>It is also the unique ideological equilibrium if either  $\kappa \leq 0$  (which is allowed in (23) as long as  $\theta_H(\bar{\tau} - \kappa)$  remains less than  $E$ ), or if  $q$  is large enough that the conditions of Proposition 4 are not satisfied. See Lemma 1 in the appendix.

The welfare analysis is the same as with statist ideology, and so are its implications concerning the necessity of constitutional (ex ante) protections for dissenting speech.

## 5 The role of history and public capital

Multiple equilibria are most interestingly thought of as the steady-states of a cumulative dynamic process, with initial conditions and historical accidents determining which one the economy converges to.

The relevant state variable here is public-sector capital: physical infrastructure, institutions, civil-service human capital, etc. The larger the stock inherited from previous generations, the greater is citizens' incentive to *believe that this is a productive asset* that will deliver valuable benefits. If such is the prevailing ideology, in turn, voters will opt for high taxes and continued investment in public capital, much of which will remain for the next generation. Conversely, where there is little preexisting public capital, so that a meaningful stock would have to be built up at considerable tax expense, cognitive incentives go in the direction of *thinking that it is not really needed*. Hence voters will not support public investment and a small public sector will persist.

The following dynamic extension of the model formalizes this idea. The timeline in Figure 3 now represents the life-cycle of a representative generation, with no altruism links between successive ones. Public services now flow from a *stock* of public capital  $K_t$ ,

$$(26) \quad h_t^i = \min \{ \gamma e_t^i + \theta (K_t - \kappa), E \},$$

which accumulates across generations according to

$$(27) \quad K_t = (1 - d)K_{t-1} + \tau_t.$$

Thus,  $\tau_t$  is tax-financed investment in generation  $t$  and  $d < 1$  the depreciation rate (previously equal to 1). Everything else in the model is unchanged, and in particular each generation receives a signal  $\sigma \in \{H, L\}$  about the productivity of public capital,  $\theta$ . The latter is, for simplicity, i.i.d. across periods.<sup>35</sup> Note that (26) is the same as (23), but with a state-dependent  $\kappa_t \equiv \kappa - (1 - d)K_{t-1}$ . Therefore, the model leads to the following results.

First, starting from any  $K_0$  there exists a realistic equilibrium, in which public investment occurs only in state  $H$  and capital evolves according to the difference equation (27), where  $\tau_t$

---

<sup>35</sup>It could also be persistent, e.g. constant, as long as each generation is either: i) unable to observe, or observes only with sufficient noise, the output and consumption outcomes of previous generations (their previous policy choice, on the other hand, contain no information along a denial equilibrium); or: ii) able to treat such observations as any other initial signal about the state that can be denied, forgotten, rationalized away, etc.

is i.i.d., equal to  $\bar{\tau}$  with probability  $q$  and to 0 with probability  $1 - q$ . The average (stochastic steady-state) capital stock is  $K_R^* \equiv q\bar{\tau}/d$ .

Second, if preceding generations invested enough that  $(1-d)K_{t-1} > \kappa - \bar{\tau}$ , generation  $t$  faces the same problem as analyzed in Section 3: since  $\kappa_t < 0$ ,  $H$  is both the state in which  $\theta$  is high and a “better” state to be in than  $L$ . Thus, if  $s$  is high enough, it is an equilibrium for agents to ignore any negative signal about public-sector efficiency and invest the maximum  $\tau_t = \bar{\tau}$  in both states.

Conversely, if previous generations did not invest, or invested little enough that  $(1-d)K_{t-1} < \kappa - \bar{\tau}$ , generation  $t$  faces the same problem as analyzed in Section 4:  $\kappa_t > \bar{\tau}$ , so even when using policy to maximal effect,  $H$  is now a worse state to be in than  $L$ . Thus, if  $s$  is high enough, it is an equilibrium for agents to ignore any positive signal about public-sector efficiency (or negative signal about market efficiency) and invest nothing in both states,  $\tau_t = 0$ .

Putting the last two cases together, let

$$(28) \quad \left( \frac{d}{1-d} \right) \kappa < \bar{\tau} < \kappa$$

and denote

$$(29) \quad K_{LF}^* \equiv 0 < \underline{K} \equiv \frac{\kappa - \bar{\tau}}{1-d} < \bar{K} \equiv \frac{\kappa}{1-d} < K_{ST}^* \equiv \frac{\bar{\tau}}{d}.$$

**Proposition 5** *Let (28) hold and let  $q$  satisfy the conditions listed in both Proposition 1 and Proposition 4. For  $s$  above some finite threshold:*

- 1) *For  $K_0 > \bar{K}$ , there is a unique ideological equilibrium, which is statist: agents in each generation censor  $L$  signals and invest  $\bar{\tau}$  in public capital. The capital stock  $K_t$  converges monotonically to the steady-state  $K_{ST}^* = \bar{\tau}/d$ .*
- 2) *For  $K_0 < \underline{K}$ , there is a unique ideological equilibrium, which is laissez-faire: agents in each generation censor  $H$  signals and invest nothing in public capital. The capital stock  $K_t$  converges monotonically to the steady-state  $K_{LF}^* = 0$ .*
- 3) *For  $K_0 \in [\underline{K}, \bar{K}]$ , there is a multiplicity of ideological equilibrium paths.*

Both ideology and policy thus exhibit history-dependence, mediated by the stock of public-sector assets. When it is high enough or low enough, there is a unique “adapted” ideology that can take hold and become self-sustaining. For intermediate values, which ideology emerges as dominant is indeterminate and depends (as usual) on how agents’ expectations are coordinated.

## 6 Conclusion

While I have focussed here on ideologies concerning the state versus the market, the model illustrates three more general points that are applicable to most collective beliefs such as those concerning trust in others, poverty and redistribution, culture, identity and religion.

First, individuals' cognitive approaches to information, and thus their resulting perceptions of reality, are highly interdependent. In particular, subjective beliefs both shape social institutions and optimally adapt to them. Second, this leads to the development of history-dependent, mutually incompatible visions of how the world works, some of them embodying evidence-resistant delusions that severely impede necessary reforms. Third, while concepts such as wishful thinking, collective denial or ideology used to lie outside the realm of economics, today we increasingly have the tools to model and analyze them rigorously. In particular, an explicitly information-based approach can capture the key phenomenon of "not wanting to know" that is central to most ideologies. It also leads, as we saw, to new results concerning the desirability of constitutional protections for free speech, even though ex-post society will often unanimously prefer to ignore or silence the bearers of bad news.

While De Tracy's vision of a unified "science of ideas" is still some years away, the recent *rapprochements* between political science, economics and psychology are moving us closer. In particular, a rich and exciting research agenda lies ahead in the bringing together of political economy with social and political psychology.

## Appendix

**Proof of Proposition 1** I first treat the benchmark case discussed in the text and Proposition, in which agents experience anticipatory feelings only after  $\tau$  is chosen. Since the ex-post incentive for denial, given by (17), is increasing in  $r(\lambda^i)$ , there is a unique (Bayesian Perfect) equilibrium of agent  $i$ 's intrapersonal game of information transmission between  $t = 0$  and  $t = 1$ . This unique “best response” to  $\lambda^{-i} = 0$  involves denial with probability 1 if and only if (17) is positive for  $r^i = r(0) = q$ , which corresponds to  $s$  satisfying (18); note that (7) implies  $q > \alpha - 1/\gamma$ . For  $s$  above this threshold (and in that case only),  $\lambda = 0$  is a social equilibrium. Together with the results in the text on the existence of the  $\lambda = 1$  equilibrium, this establishes the Proposition.

I now extend the results to the more general case with anticipatory feelings both before and after voting. Period 1 is now divided into two subperiods, of durations  $\phi$  and  $1 - \phi$  respectively. At  $t = 1 + \phi$ , agents first vote on a tax rate  $\tau$ , then choose their levels of private investment. As before: (i) the remaining disposable income is consumed only in period 2; (ii) during the remainder of period 1, agents experience anticipatory utility, parametrized by  $s''$ , over their period-2 prospects. Thus, at  $t = 1 + \phi$ , the intertemporal welfare which they seek to maximize is

$$(A.1) \quad U_{1+\phi}^i = (s'' + \delta) E_{1+\phi}^i [1 - \tau - e + y_2^i],$$

leading –in each state– to *the very same* decisions over  $e^i$  and  $\tau$  as before (case  $\phi = 0$ ), under the same parameter assumptions and with  $s$  simply replaced by  $s''$ .

During the first part of period 1, however, prior to the setting of  $\tau$  (which may reveal the state) and the  $e^j$ 's, agents now experience a flow payoff  $s' E_1^i [1 - \tau - e + y_2^i]$ . Finally, intertemporal preferences at  $t = 0$  are again the expected present value of all future payoffs, which now takes the form (reducing to the basic model when  $s' = 0$ ) :

$$(A.2) \quad U_0^i = -m(1 - \lambda) + \delta E_0^i [s' E_1^i [1 - \tau - e + y_2^i] + s'' E_{1+\phi}^i [1 - \tau - e + y_2^i]] \\ + \delta^2 E_0^i [1 - \tau - e + y_2^i].$$

In an *ideological equilibrium*, ( $\lambda^j \equiv 0$ ), the tax rate must be the same in both states and thus can reveal no information (nor does any other aggregate variable). Thus  $E_{1+\phi}^i [\cdot] = E_1^i [\cdot]$  and  $U_0^i$  is the same as before, except that  $s$  is now replaced by  $s' + s'' \equiv s$ . Consequently, this equilibrium exists under the same conditions as stated in the text of Proposition 1.

In a *realism equilibrium* ( $\lambda^j \equiv 1$ ), voters are informed and choose  $\tau = \bar{\tau}$  in state  $H$  and  $\tau = 0$  in state  $L$  (recall from what precedes that equilibrium tax rates and effort levels are unchanged by the presence of a prior subperiod of savoring, since the latter is “sunk” by the time decisions



are made). Therefore, looking forward, an agent learning that  $\sigma = L$  at  $t = 0$  knows that no matter whether he censors the signal or not, he will be fully informed by  $t = 1 + \phi$ . His expected intertemporal utility from realism given  $\sigma = L$  is thus

$$(A.3) \quad U_{0,R}^i = \delta (1 + s' + s'' + \delta) [1 - E/\gamma + E].$$

Under denial, it differs only by the fact that, between  $t = 1$  and  $t = 1 + \phi$  the agent will expect (with probability  $r(\lambda^i)$ ) the state  $\theta = \theta_H$ , with associated policy  $\tau = \bar{\tau}$ , and he will consequently invest only  $(E - \bar{\tau}\theta_H)/\gamma$ . Thus:

$$(A.4) \quad U_{0,D}^i - U_{0,R}^i = -m + \delta s' r(\lambda^i) (\theta_H/\gamma - 1) \bar{\tau}.$$

Since the ex-post incentive for denial is increasing in  $\lambda^i$ , there is again a unique equilibrium for agent  $i$ . It involves realism, and is thus consistent with  $\lambda = 1$  being a social equilibrium, if and only if  $U_{0,D}^i - U_{0,R}^i \leq 0$  for  $\lambda^i = 1$ , which translates into (12).

Finally, for  $s' = \phi s$  and  $s'' = (1 - \phi) s$ , the two conditions for multiplicity become

$$(A.5) \quad \left( \frac{1}{1 - \phi} \right) \left( \frac{m/\delta + \delta (\alpha - 1/\gamma) \bar{\tau} \Delta\theta}{(q - \alpha + 1/\gamma) \Delta\theta} \right) \leq s \leq \left( \frac{1}{\phi} \right) \left( \frac{m/\delta}{(\theta_H/\gamma - 1) \bar{\tau}} \right),$$

defining a nonempty interval for  $s$  provided  $\phi/(1 - \phi)$  is below some simple threshold. ■

**Proof of Proposition 2** From (19), we can compute

$$(A.6) \quad (U_{0,D}^i - U_{0,R}^*) / \delta = -m/\delta + (s + \delta) (\theta_H/\gamma - 1) \bar{\tau} - [s(1 - q) + \delta] \bar{\tau} \Delta\theta.$$

This expression is increasing in  $s$ , since  $\theta_H/\gamma - 1 > (1 - q) \Delta\theta$  by (14). It is positive if

$$(A.7) \quad s > \frac{m/\delta + \delta [\Delta\theta - (\theta_H/\gamma - 1)] \bar{\tau}}{[\theta_H/\gamma - 1 - (1 - q) \Delta\theta] \bar{\tau}} \equiv s^*.$$

To show that  $s^*$  can be above or below  $\bar{s}$ , I focus on the case where  $m = 0$ . From (18) and (A.7),  $\bar{s} < s^*$  then takes the form

$$\frac{\alpha - 1/\gamma}{q - \alpha + 1/\gamma} < \frac{\Delta\theta - (\theta_H/\gamma - 1)}{\theta_H/\gamma - 1 - (1 - q) \Delta\theta} \iff \frac{q}{\alpha - 1/\gamma} > \frac{q\Delta\theta}{\Delta\theta - (\theta_H/\gamma - 1)},$$

or  $\Delta\theta(1 - \alpha + 1/\gamma) > \theta_H/\gamma - 1$ . So, given (14), if

$$(A.8) \quad 1 + (1 - q) \Delta\theta < \theta_H/\gamma < 1 + (1 - \alpha + 1/\gamma) \Delta\theta,$$

then  $\bar{s} < s^*$ . In this case, the denial equilibrium leads to lower (interim) welfare in state  $L$  than the realism equilibrium for  $s \in (\bar{s}, s^*)$ , and to higher welfare for  $s > s^*$ . The opposite ranking

applies when  $\theta_H/\gamma > 1 + (1 - \alpha + 1/\gamma) \Delta\theta$ . ■

The following lemma extends Proposition 1 to the more general technology given by (23), and it will be also used in proving Proposition 4.

**Lemma 1** *For all  $\kappa$  with  $0 \leq \kappa < \bar{\tau}$  in (23), Proposition 1 applies unchanged, with  $\bar{\tau}$  simply replaced by  $\bar{\tau} - \kappa$  in (2) and (18). Furthermore, if  $\kappa \leq 0$  the statist equilibrium in which agents censor  $L$  signals and  $\tau = \bar{\tau}$  is the only (pure-strategy) ideological one. In particular, there can be no equilibrium in which they censor  $H$  signals.*

**Proof.** The proof proceeds in two steps, focusing respectively on statist equilibria, in which state  $L$  is miscoded or misremembered as  $H$  (these will be abbreviated as  $L \rightarrow H$  equilibria) and on laissez-faire ones, in which state  $H$  is miscoded or misremembered as  $L$  (these will be abbreviated as  $H \rightarrow L$  equilibria).<sup>36</sup>

*Step 1. Existence of  $L \rightarrow H$  equilibrium.*

a) Consider first such an equilibrium in which  $\tau - \kappa > 0$ . The arguments used in the text to establish (13) apply unchanged with  $\tau - \kappa$  substituted for  $\tau$ . Condition (14) then implies that  $\tau$  must equal  $\bar{\tau}$ , and the rest of the proof of Proposition 1 applies unchanged with  $\bar{\tau} - \kappa$  substituted for  $\bar{\tau}$ , as long  $\theta_H(\bar{\tau} - \kappa) < E$ , which amounts to the same substitution in condition (2).

b) Consider an  $L \rightarrow H$  equilibrium in which  $\tau - \kappa \leq 0$ . Since  $\mu^i = q$  in such an equilibrium, an agent's investment problem is now

$$(A.9) \quad \max_e \{1 - \tau - e + \alpha [q \min \{\gamma e + \theta_H(\tau - \kappa), E\} + (1 - q) \min \{\gamma e + \theta_L(\tau - \kappa), E\}]\}.$$

Given that  $\alpha\gamma > 1$ , the solution is

$$(A.10) \quad \gamma e^i = \begin{cases} E + \theta_H(\kappa - \tau) & \text{if } q\alpha\gamma \geq 1 \\ E + \theta_L(\kappa - \tau) & \text{if } q\alpha\gamma < 1 \end{cases}.$$

In the first case, the voter's problem is again defined by (13) and, given (14), this leads to  $\tau = \bar{\tau} > \kappa$ , a contradiction. In the second case, the voter's problem becomes

$$(A.11) \quad \max_{\tau} \{1 - \tau - (E + \theta_L(\kappa - \tau))/\gamma + E - q\Delta\theta(\kappa - \tau)\}.$$

If  $\theta_L/\gamma > 1 - q\Delta\theta$  the derivative in  $\tau$  is positive, leading again to a contradiction. If  $\theta_L/\gamma < 1 - q\Delta\theta$  (this is condition (24) in the text; I abstract from the measure-zero case where there is equality), then  $\tau = 0$  is chosen. Moving back to  $t = 0$ , consider now the agent's cognitive

---

<sup>36</sup>It is easy to show (as in Bénabou (2007)) that for all  $m > 0$  there can be no equilibrium in which both states are miscoded (even with mixed strategies). With  $m = 0$  there could be such "babbling" equilibria but they are of no interest and can be eliminated as such, or by assuming an arbitrarily small positive lower bound for  $m$ .

problem (or incentive constraint) in state  $L$ , knowing that the equilibrium tax rate will be  $\tau = 0$  :

$$(A.12) \quad U_{0,R}^i/\delta = (s + \delta) [1 - (E + \theta_L \kappa)/\gamma + E]$$

$$(A.13) \quad \begin{aligned} U_{0,D}^i/\delta &= -m/\delta + \delta [1 - (E + \theta_L \kappa)/\gamma + E] + s [1 - (E + \theta_L \kappa)/\gamma + E - q\kappa\Delta\theta] \\ &= U_{0,R}^i/\delta - m/\delta - sq\kappa\Delta\theta. \end{aligned}$$

For  $\kappa < 0$  this could be an equilibrium, but for  $\kappa \geq 0$  it cannot, so the only  $L \rightarrow H$  equilibrium in this case has  $\tau = \bar{\tau}$ .

*Step 2. Ruling out  $H \rightarrow L$  equilibria.*

a) Consider first such an equilibrium in which  $\tau - \kappa < 0$ . Posteriors are again equal to  $q$  in both states so, as in part (b) of Step 1, if  $q\alpha\gamma \geq 1$  then  $\gamma e^i = E - \theta_H(\tau - \kappa)$  and the same derivation of the equilibrium tax rate leads again to  $\tau = \bar{\tau}$ , a contradiction. If, on the contrary,  $q\alpha\gamma < 1$ , then as before we also need  $\theta_L/\gamma < 1 - q\Delta\theta$  to have voters choose  $\tau = 0$  rather than  $\tau = \bar{\tau}$ . Under these conditions, the agent's cognitive problem at  $t = 0$  is now, in the relevant state  $H$ ,

$$(A.14) \quad U_{0,R}^i/\delta = (s + \delta) [1 - (E + \theta_H \kappa)/\gamma + E - (1 - \alpha)\kappa\Delta\theta],$$

$$(A.15) \quad \begin{aligned} U_{0,D}^i/\delta &= -m/\delta + \delta [1 - (E + \theta_L \kappa)/\gamma + E - \kappa\Delta\theta] \\ &\quad + s [1 - (E + \theta_L \kappa)/\gamma + (1 - q)E + q(E - \kappa\Delta\theta)] \\ &= -m/\delta + (s + \delta) [1 - (E + \theta_L \kappa)/\gamma + E - \kappa\Delta\theta] + (1 - q)s\kappa\Delta\theta. \end{aligned}$$

Finally,

$$(U_{0,D}^i - U_{0,R}^i)/\delta = -m/\delta + (1 - q)s\kappa\Delta\theta - (s + \delta)(\alpha - 1/\gamma)\kappa\Delta\theta.$$

Therefore, if  $\kappa \leq 0$  there is no  $H \rightarrow L$  equilibrium. For further use, note that for  $\kappa > 0$  there is one if provided'

$$(A.16) \quad s \geq \frac{m/\delta + \delta(\alpha - 1/\gamma)\kappa\Delta\theta}{(1 - q - \alpha + 1/\gamma)\kappa\Delta\theta},$$

which is the right-hand-side of (25).

b) Consider now an  $H \rightarrow L$  equilibrium in which  $\tau - \kappa > 0$ . Recall that under (7), (14) and with posterior belief  $q$ , this leads to  $\gamma e^i = E + \theta_H(\kappa - \tau)$  and  $\tau = \bar{\tau}$ . The agent's cognitive problem at  $t = 0$  in state  $H$  is now

$$(A.17) \quad U_{0,R}^i/\delta = (s + \delta) [1 - \bar{\tau} - (E + \theta_H(\bar{\tau} - \kappa))/\gamma + E],$$

$$\begin{aligned}
\text{(A.18)} \quad U_{0,D}^i/\delta &= -m/\delta + \delta [1 - \bar{\tau} - (E + \theta_H(\bar{\tau} - \kappa))/\gamma + E] \\
&\quad + s [1 - \bar{\tau} - (E + \theta_H(\bar{\tau} - \kappa))/\gamma + E - (1 - q)(\bar{\tau} - \kappa)\Delta\theta] \\
&= -m/\delta + (s + \delta) [1 - \bar{\tau} - (E + \theta_H(\bar{\tau} - \kappa))/\gamma + E] - sq(\bar{\tau} - \kappa)\Delta\theta,
\end{aligned}$$

so that

$$\text{(A.19)} \quad (U_{0,D}^i - U_{0,R}^i) / \delta = -m/\delta - sq(\bar{\tau} - \kappa)\Delta\theta < 0.$$

Thus, there cannot be an  $H \rightarrow L$  equilibrium with  $\tau - \kappa > 0$ , and a fortiori with  $\kappa \leq 0$ . ■

**Proof of Proposition 4** I will in fact show a stronger result, which corresponds to the “mirror image” of Lemma 1.

**Lemma 2** *Proposition 4 holds for all  $0 < \kappa \leq \bar{\tau}$ . Furthermore, if  $\kappa \geq \bar{\tau}$  the laissez faire equilibrium in which agents censor  $H$  signals and  $\tau = 0$  is the only (pure-strategy) ideological one. In particular, there can be no equilibrium in which they censor  $L$  signals.*

**Proof.** With the notation defined in the text, (23) becomes

$$\text{(A.20)} \quad h^i = \min \left\{ \gamma e^i + \tilde{\theta} \tilde{\tau}, E \right\}$$

and the investment choice of an agent with posterior belief  $\tilde{\mu}^i \equiv 1 - \mu^i$  on the state being  $\tilde{H}$  and faced with policy  $\tilde{\tau}$  can be written as:

$$\text{(A.21)} \quad \max_e \left\{ 1 + \tilde{\tau} - \kappa - e + \alpha \left[ \tilde{\mu}^i \min \left\{ \gamma e + \tilde{\theta}_{\tilde{H}} \tilde{\tau}, E \right\} + (1 - \tilde{\mu}^i) \min \left\{ \gamma e + \tilde{\theta}_{\tilde{L}} \tilde{\tau}, E \right\} \right] \right\},$$

which is identical to (6) except for the tildes and the change of  $-\tau$  into  $\tilde{\tau} - \kappa$  in the first term. The proof that an equilibrium with  $\lambda = 1$  always exists, with  $\tilde{\tau}$  taking its maximal value  $\kappa$  in state  $\tilde{H}$  and its minimum value  $\kappa - \bar{\tau}$  in state  $\tilde{L}$ , is then identical to the earlier one. The proof concerning ideological equilibria again proceeds in two steps.

*Step 1. Existence of an  $H \rightarrow L$  (i.e.,  $\tilde{L} \rightarrow \tilde{H}$ ) equilibrium.*

a) Consider first such an equilibrium in which  $\kappa - \tau > 0$ . The relevant analogue of (7) is

$$\text{(A.22)} \quad \alpha\gamma > 1 \geq (1 - \tilde{q}) \alpha\gamma = q\alpha\gamma.$$

These conditions, together with the fact that  $\tilde{\theta}_{\tilde{L}} \tilde{\tau} = -\theta_H(\kappa - \tau) < -\theta_L(\kappa - \tau) \equiv \tilde{\theta}_{\tilde{H}} \tilde{\tau}$ , imply that when agents know the state is  $\tilde{L}$  ( $\tilde{\mu}^i = 0$ ) they invest  $e^i = (E - \tilde{\tau} \tilde{\theta}_{\tilde{L}}) / \gamma = E/\gamma + (\kappa - \tau) \theta_H / \gamma$ , but under ignorance ( $\tilde{\mu}^i = \tilde{q}$ ), they invest only  $e^i = (E - \tilde{\tau} \tilde{\theta}_{\tilde{H}}) / \gamma = E/\gamma + (\kappa - \tau) \theta_L / \gamma$ .

In an ideological equilibrium ( $\lambda = 0$ ) both states are coded as  $\tilde{H}$ , resulting in a posterior  $\tilde{q}$  on the state being truly  $\tilde{H}$ . Agents then always invest  $(E - \tilde{\tau} \tilde{\theta}_{\tilde{H}}) / \gamma$ , which is the optimal amount

(conditional on  $\tilde{\tau}$ ) in state  $\tilde{H}$ , but will fall short by  $\tilde{\tau}\Delta\theta/\gamma$  in state  $\tilde{L}$ . A representative voter's date-1 expected utility from implementing a policy  $\tilde{\tau}$  is then  $s + \delta$  times:

$$(A.23) \quad 1 + \tilde{\tau} - \kappa - (E - \tilde{\tau}\tilde{\theta}_{\tilde{H}})/\gamma + \tilde{q}E + (1 - \tilde{q})(E - \tilde{\tau}\Delta\theta),$$

which is identical to (11) except for the tildes and the change of  $-\tau$  into  $\tilde{\tau} - \kappa$  in the first expression. He will thus choose the maximum value,  $\tilde{\tau}_{\tilde{H}} = \tilde{\tau}_{\tilde{L}} = \kappa$ , provided

$$(A.24) \quad \tilde{\theta}_{\tilde{H}}/\gamma > -1 + (1 - \tilde{q})\Delta\theta,$$

or, equivalently,  $\theta_L/\gamma < 1 - q\Delta\theta$ , which is the relevant analogue to (14) and corresponds to (24).

Consider now agent  $i$ 's decision problem at  $t = 0$ , in state  $\tilde{L}$ . If he remains aware of the news, he will invest  $e^i = (E - \kappa\tilde{\theta}_{\tilde{L}})/\gamma = E/\gamma + \kappa\theta_H/\gamma$  but know that everyone else is investing only  $e^j = (E - \kappa\tilde{\theta}_{\tilde{H}})/\gamma = E/\gamma + \kappa\theta_L/\gamma$ . His expected intertemporal utility will then be:

$$U_{0,R}^i = \delta(s + \delta) \left[ 1 - \kappa - (E - \kappa\tilde{\theta}_{\tilde{L}})/\gamma + \alpha E + (1 - \alpha)(E - \kappa\Delta\theta) \right] + \delta(s + \delta)\kappa.$$

If, on the other hand, he goes along with society's denial, he will also underinvest, but will savor the thought of a more pleasant future in which government intervention is not really needed:

$$(A.25) \quad U_{0,D}^i = -m + \delta \left[ 1 - \kappa - (E - \kappa\tilde{\theta}_{\tilde{H}})/\gamma \right] + \delta(s + \delta)\kappa \\ + \delta s [\tilde{q}E + (1 - \tilde{q})(E - \kappa\Delta\theta)] + \delta^2 [E - \kappa\Delta\theta].$$

Thus  $U_{0,R}^i$  and  $U_{0,D}^i$  have the same expressions as before, except for the tildes and the fact that  $\bar{\tau}$  (the maximal value of  $\tau$ ) is replaced by  $\kappa$  (the maximal value of  $\tilde{\tau}$ ); hence the existence result.

b) Ruling out  $H \rightarrow L$  (i.e.,  $\tilde{L} \rightarrow \tilde{H}$ ) equilibria with  $\kappa - \tau \leq 0$ . The reasoning parallels that in Step 1b of Lemma 1, with the same transformed variables as above. It is not explicated here to minimize repetition.

*Step 2. Ruling out  $L \rightarrow H$  (i.e.,  $\tilde{H} \rightarrow \tilde{L}$ ) equilibria.* The reasoning parallels that in Step 2 of Lemma 1. It is again not explicated here to avoid repetition. ■

**Proof of Proposition 5** For  $q$  in the the intermediate range where it satisfies the conditions of both Propositions 1 and 4, the results follow from the fact, noted in the text, that each generation faces a problem identical to the static one with  $\kappa_t \equiv \kappa - (1 - d)K_{t-1}$ .

Thus, for  $K_{t-1} < \underline{K}$ , i.e.  $(1 - d)K_{t-1} < \kappa - \bar{\tau}$ , we have  $\kappa_t > \bar{\tau}$ , so by Lemma 2 a unique ideological equilibrium exists (for  $s$  above a large enough but fixed threshold, since  $\kappa_t$  remains bounded) and it is laissez-faire, with  $\tau_t = 0$ . As a result,  $K_t = (1 - d)K_{t-1}$  so the same conditions holds in all subsequent periods, implying that ideology remains laissez faire and  $K_{t+n}$  converges to zero.

Conversely, for  $K_{t-1} > \bar{K}$ , i.e.  $(1-d)K_{t-1} > \kappa$ , we have  $\kappa_t < 0$ , so by Lemma 1 a unique ideological equilibrium exists (for  $s$  above a large enough but fixed threshold) and it is statist, with  $\tau_t = \bar{\tau}$ . As a result,

$$(A.26) \quad K_t = (1-d)K_{t-1} + \bar{\tau} > (1-d)\bar{K} + \bar{\tau} = \kappa + \bar{\tau} > \kappa/(1-d),$$

by (29). So the same conditions hold in all subsequent periods, implying that ideology remains statist and  $K_{t+n}$  converges to  $\bar{\tau}/d$ .

For  $K_{t-1} \in [\underline{K}, \bar{K}]$ ,  $\kappa_t \in [0, \bar{\tau}]$  so the conjunction of Lemmas 1 and 2 implies that (again, for  $s$  large enough) both  $L \rightarrow H$  and  $H \rightarrow L$  ideological equilibria exist. ■

## REFERENCES

- Acemoglu, Daron and James Robinson (2001) “A Theory of Political Transitions,” *The American Economic Review*, 91(4), 938-963.
- Akerlof, George, and William Dickens (1982) “The Economic Consequences of Cognitive Dissonance,” *American Economic Review*, 72 , 307-319.
- Alesina, Alberto, and George-Marios Angeletos (2005) “Fairness and Redistribution: US versus Europe,” *American Economic Review*, 95, 960-980.
- Alesina, Alberto, and Nicola Fuchs-Schuendeln (2006) “Good Bye Lenin (or not?) – The Effect of Communism on People’s Preferences,” *American Economic Review*, 97, 1507-1528,
- Alesina, Alberto, and Eliana La Ferrara (2005) “Redistribution in the Land of Opportunities,” *Journal of Public Economics*, 89, 897–931.
- Alesina, Alberto, and Edward Glaeser (2004) *Fighting Poverty in the US and Europe: A World of Difference*. Oxford, England: Oxford University Press.
- Alesina, Alberto, Glaeser, Edward, and Bruce Sacerdote (2001) “Why Doesn’t the US Have a European-Type Welfare State?” *Brookings Papers on Economic Activity*, 2, 187–277.
- Anderlini, Luca, Gerardi, Dino, and Roger Lagunoff (2007) “Social Memory and Evidence from the Past,” Georgetown University mimeo, January.
- Barro, Robert and McCleary R. (2003) “Religion and Economic Growth,” NBER Working Paper 9682, May.
- Bartels, Lawrence (2005) “Homer Gets a Tax Cut: Inequality and Public Policy in the American Mind,” *Perspectives on Politics*, 3(1), 15-31.
- Battaglini, Marco, Bénabou, Roland and Jean Tirole (2005) “Self-Control in Peer Groups,” *Journal of Economic Theory*, 123, 105–134.
- Bénabou, Roland (2000) “Unequal Societies: Income Distribution and the Social Contract,” *American Economic Review*, 90, 96–129.
- Bénabou, Roland (2007) “Groupthink: Collective Delusions in Organizations and Markets,” Princeton University mimeo.
- Bénabou, Roland, and Efe Ok (2001) “Social Mobility and the Demand for Redistribution: the POUM Hypothesis,” *Quarterly Journal of Economics*, 116(2), 447–487.
- Bénabou, Roland, and Jean Tirole (2002) “Self-Confidence and Personal Motivation,” *Quarterly Journal of Economics*, 117 , 871–915.
- Bénabou, Roland, and Jean Tirole (2004) “Willpower and Personal Rules,” *Journal of Political Economy*, 112, 848–887.
- Bénabou, Roland, and Jean Tirole (2006) “Belief in a Just World and Redistributive Politics,” *Quarterly Journal of Economics*, 121(2), 699-746.

- Bénabou, Roland, and Jean Tirole (2007) "Identity, Dignity and Taboos: Beliefs as Assets," CEPR Discussion Paper 6123, February.
- Bisin, Alberto, and Thierry Verdier (2000) "A Model of Cultural Transmission, Voting and Political Ideology," *European Journal of Political Economy*, 16, 5–29.
- Bisin, Alberto, and Thierry Verdier (2001) "The Economics of Cultural Transmission and the Evolution of Preferences," *Journal of Economic Theory*, 97(2), 298–319.
- Brunnermeier, Markus, and Jonathan Parker (2005) "Optimal Expectations," *American Economic Review*, 95, 1092–1118.
- Caplan, Bryan (2007) *The Myth of the Rational Voter: Why Democracies Choose Bad Policies*. Princeton, NJ: Princeton University Press.
- Caplin, Andrew and John Leahy (2001) "Psychological Expected Utility Theory and Anticipatory Feelings," *Quarterly Journal of Economics*, 116, 55–79.
- Caplin, Andrew and Kfir Eliaz (2003) "AIDS Policy and Psychology: A Mechanism-Design Approach," *RAND Journal of Economics*, 34(4), 631–46.
- Carrillo, Juan, and Thomas Mariotti (2000) "Strategic Ignorance as a Self-Disciplining Device," *Review of Economic Studies*, 66, 529–544.
- Cervellati, Matteo, Esteban, Joan, and Laurence Kranich (2006) "The Social Contract with Endogenous Sentiments," Institute for the Study of Labor Discussion Paper No. 2312, September.
- Corneo, Giacomo, and Olivier Jeanne (2007) "Symbolic Values, Occupational Choice, and Economic Development," Institute for the Study of Labor Discussion Paper No. 2763, April.
- De Menil, Georges (2007) *Common Sense: Pour Débloquent la Société Française*. Paris, France: Odile Jacob.
- Dessi, Roberta (2005) "Collective Memory, Identity, and Cultural Investments," IDEI mimeo, November.
- Di Tella, Rafael, Galiani, S. and E. Schargrotsky (2007) "The Formation of Beliefs: Evidence from the Allocation of Land Titles to Squatters," *Quarterly Journal of Economics*, 122(1), 209–241.
- Fernandez, Raquel and Alessandra Fogli (2006) "Fertility: The Role of Culture and Family Experience," *Journal of the European Economic Association*, 4(2-3), 552–561.
- Ferrie, Joseph (2005) "History Lessons: The End of American Exceptionalism? Mobility in the United States Since 1850," *Journal of Economic Perspectives*, 19(3), 199–215
- Fong, Christina (2001) "Social Preferences, Self-Interest, and the Demand for Redistribution," *Journal of Public Economics*, 82, 225–246.
- Glaeser, Edward (2005) "The Political Economy of Hatred," *Quarterly Journal of Economics*, 120(1), 45–86.
- Gilens, Martin (1999) *Why Americans Hate Welfare: Race, Media, and the Politics of Antipoverty Policy*. Chicago: University of Chicago Press.



- Greenspan, Alan (1963) "The Assault on Integrity," *The Objectivist Newsletter*, August, 2(8).
- Greenspan, Alan (2002a) *Report to Congress before the Committee on Banking, Housing and Urban Affairs*, United States Senate, July 16. Available at [www.federalreserve.gov/boarddocs/hh/2002/july/testimony.htm](http://www.federalreserve.gov/boarddocs/hh/2002/july/testimony.htm).
- Greenspan, Alan (2002b) *Testimony to the United States House Financial Services Committee*, July 17. Excerpt reported at [www.washingtonpost.com/wp-srv/business/articles/greenspan\\_comments.html](http://www.washingtonpost.com/wp-srv/business/articles/greenspan_comments.html).
- Greif, A. (2006) *Institutions and the Path to the Modern Economy: Lessons from Medieval Trade*. Cambridge, UK: Cambridge University Press.
- Grossman, Sanford and Stiglitz, Joseph (1980) "On the Impossibility of Informationally Efficient Markets," *American Economic Review*, 70(3), 393-408.
- Guiso, Luigi, Sapienza, Paola and Luigi Zingales (2007) "Social Capital as Culture," *Journal of the European Economic Association*, this volume.
- Guiso, Luigi, Sapienza, Paola and Luigi Zingales (2003) "People's Opium? Religion and Economic Attitudes," *Journal of Monetary Economics*, 50, 225–282.
- Guiso, Luigi, Sapienza, Paola and Luigi Zingales (2006) "Does Culture Affect Economic Outcomes?," *Journal of Economic Perspectives*, 20(2), 23-48.
- Hochschild, Jennifer (1981) *What's Fair? American Beliefs about Distributive Justice*. Cambridge, MA: Harvard University Press.
- Hochschild, Jennifer (1996) *Facing Up to the American Dream* (Princeton, NJ: Princeton University Press).
- Jost, John and Brenda Major (Eds.) (2001). *The Psychology of Legitimacy: Emerging Perspectives on Ideology, Justice, and Intergroup Relations*. New York: Cambridge University Press.
- Kahan, Dan and Donald Braman (2006) "Cultural Cognition and Public Policy," *Yale Law and Policy Review*, 24, 147-170.
- Kaiser Family Foundation, Harvard University Survey Project and Washington Post (1996a) *Survey of Americans and Economists on the Economy*, <http://www.kff.org/kaiserpolls/1199-econgen.cfm>.
- Kaiser Family Foundation, Harvard University Survey Project and Washington Post (1996b) *Why Don't Americans Trust The Government?*, <http://www.kff.org/kaiserpolls/1110-governs.cfm>.
- Köszegi, Botond (2006) "Emotional Agency," *Quarterly Journal of Economics*, 21(1), 121-156.
- Köszegi, Botond (2007) "Utility from Anticipation and Personal Equilibrium," UC Berkeley mimeo, August.
- Kuklinski, James, Quirk, Paul, Jerit, Jennifer, Schwieder, David and Robert Rich (2000) "Misinformation and the Currency of Democratic Citizenship," *The Journal of Politics*, 62(3), 790-816.
- Krugman, Paul (1997) "Unmitigated Gauls: Pardon My French About French Economics." *Slate*, June 6, at [www.slate.com/id/1921](http://www.slate.com/id/1921).

- Krugman, Paul, and Robin Wells. (2006) “The Health Care Crisis and What To Do About It.” *The New York Review of Books*, 53(5), March 23, at [www.nybooks.com/articles/18802](http://www.nybooks.com/articles/18802).
- Kuran, Timur (1993) “The Unthinkable and the Unthought,” *Rationality and Society*, 5, 73-505.
- Kuran, Timur (1995) *Private Truths, Public Lies: The Social Consequences of Preference Falsification*. Cambridge, Mass.: Harvard University Press.
- Landier, Augustin (2000) “Wishful Thinking: A Model of Optimal Reality Denial,” Massachusetts Institute of Technology mimeo.
- Landier, Augustin and David Thesmar (2007) *Le Grand Méchant Marché: Décryptage d'un Fantôme Français*. Paris, France: Flammarion.
- Lane, Robert (1959), “Fear of Equality,” *American Political Science Review*, 59, 35–51.
- Lerner, Melvin (1982), *The Belief in a Just World: A Fundamental Delusion*. New York, NY: Plenum Press.
- Leung, Kwok, Bond, Michael, de Carrasquel, S., Muñoz, Carlos, Hernández, Marisela, Murakami, Fumio, Yamaguchi, Susumu, Bierbrauer, Günter and Theodore Singelis (2002) “Social Axioms: The Search for Universal Dimensions of General Beliefs about How the World Functions,” *Journal of Cross-Cultural Psychology*, 33(3), 286-302.
- Levy, Gilat and Ronny Razin (2007) “A Theory of Religious Organizations,” London School of Economics mimeo, November.
- Loewenstein, George (1987) “Anticipation and the Valuation of Delayed Consumption,” *Economic Journal*, 97, 666-684.
- Noland, Marcus (2003) “Religion, Culture, and Economic Performance,” KDI School of Public Policy and Management Working Paper No. 03-13.
- North, Douglass (1990) *Institutions, Institutional Change and Economic Performance*. Cambridge, UK: Cambridge University Press.
- Piketty, Thomas (1995) “Social Mobility and Redistributive Politics,” *Quarterly Journal of Economics*, 110, 551–583.
- Putnam, Robert (2007) “E Pluribus Unum: Diversity and Community in the Twenty-first Century”, *Scandinavian Political Studies* 30 (2), 137-174.
- Schelling, Thomas (1986) “The Mind as a Consuming Organ,” in David E. Bell, Howard Raiffa, and Amos Tversky, eds., *Decision Making : Descriptive, Normative, and Prescriptive Interactions*. Cambridge, MA: Cambridge University Press.
- Scheve, Kenneth and David Stasavage (2005) “Religion and Preferences for Social Insurance,” London School of Economics mimeo.
- Saint-Paul, Gilles (2007) “Le Rôle des Croyances et des Idéologies dans l’Economie Politique des Réformes,” Université de Toulouse mimeo, October.
- Scheve, Kenneth and David Stasavage (2006) “Religion and Preferences for Social Insurance,” *Quarterly Journal of Political Science*, 1(3), 255-286.

Tabellini, Guido, (2005) “Culture and Institutions: Economic Development in the Regions of Europe,” CESifo Working Paper No. 1492.

Tabellini, Guido, (2007) “The Scope of Cooperation: Norms and Incentives,” Università Bocconi mimeo, February.

Tabellini, Guido (2008) “Institutions and Culture,” *Journal of the European Economic Association*, this volume.

Tirole, Jean (1996) “A Theory of Collective Reputations (with Applications to the Persistence of Corruption and to Firm Quality),” *Review of Economic Studies*, 63(1), 1-22.

World Bank (2004) *World Development Indicators*. Washington, D.C.: The World Bank.

World Public Opinion (2005) “20 Nation Poll Finds Strong Global Consensus: Support for Free Market System, But also More Regulation of Large Companies. Published by the *Program on International Policy Attitudes*, at <http://www.worldpublicopinion.org>.