

Rationalization

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Economics and Psychology

Economics: Agents think to relate means and consequences

Choice = Preference

Psychology:

- "[e]veryone feels that as a rational creature he must be able to give a connected, logical and continuous account of himself, his conduct and opinions, and all his mental processes are unconsciously manipulated and revised to that end." Ernest Jones, 1908 "Rationalisation in every-day life."
- "This apparently simple idea is one of most far-reaching significance, both to psychology and to the sciences, such as sociology, that must be founded in psychology. We are beginning to see man not as the smooth self-acting agent he pretends to be, but as he really is, a creature only dimly conscious of the various influences that mould his thought and action, and blindly resisting with all the means at his command the forces that are making for a higher and fuller consciousness"

Model of a Decision-maker

Rationalization as a psychological constraint. If the decision maker (Dee) cannot justify an action to herself than she will not take it (even if she prefers it to all feasible alternatives)

Dee has preferences U and a *set of rationales* $\{R_i, i=1, \dots, n\}$

- B Feasible set ; $\tau(B) \subseteq B$ Psychologically feasible
- x in $\tau(B)$ iff for some rationale R_i
 $x R_i y$ for every y in B

Choice $C(B)$ maximizes U s.t. $\tau(B)$

Literature Review

- Manzini and Mariotti (2007, 2009)
- Ambrus, A., and K. Rozen. (2008)
- Carillo, J. and T. Mariotti (2000)
- Chambers. C. and T. Hayashi (2008)
- Dekel, E., B. Lipman, and A. Rustichini (2001)
- Eliaz, K. and E. Ok (2006)
- Green, J., and D. Hojman. (2007)
- Gul, F. and W. Pesendorfer (2004, 2005)
- Kalai, G., A. Rubinstein, and R. Spiegler (2002)
- Masatlioglu, Y. and D. Nakajima (2007)
- Ok, E., P. Ortoleva, and G. Riella (2008)
- Salant, Y. and A. Rubinstein (2006)
- Spiegler, R. (2002, 2004)
- Masatlioglu, Nakajima and Ozbay (2009)
- Houy and Tadenuma (2009)
- Lehrer and Teper (2008)

Results

1) Empirical Content of Rationalization Theory

Violation of Weak WARP

$$\{\underline{x}, y\} \subseteq \{x, \underline{y}, z, \dots\} \subseteq \{x, y, z, w, \dots\}$$

Th 1: Equivalence of rationalization and Weak WARP

Cor : Anomalies (e.g., cycles) are consistent with basic principle of constrained optimization of preference

Why Law Breeds Cycles (with Leo Katz)

- Constitution/Legislators/Judges/Citizens

Cycles of a Law-Abiding Citizen.

- Duress : Defendant is threatened to help assailant. She greatly cares about her life-work manuscript.

x helps assailant

y endures pain z yields manuscript

{x,y}

{y,z}

{x,z}

Necessity;

Self-defense;

Negligence

Results (cont)

Th 2: Full characterization of revealed preferences
 $\{x, y\} \subseteq \{x, y, z, \dots\}$ iff x is revealed preferred to y
Revealed preferences made (only) through anomalies.

Avoiding the Handicapped. We cannot conclude that Dee wants to see the movie alone unless we also assume

- 1) Dee preference is a complete order
- 2) Dee can rationalize watching the movie with the handicap

Need to rationalize (universal)

Rationales themselves (culture-specific)

Minimal Constraint Principle

To make additional inferences on motivations we need

More data (speech) leading to assumptions like y in $\tau(x,y)$

Minimal Constraint Principle

Two models (U, τ) and (U', τ') underlie C

$\tau'(B) \subseteq \tau(B)$, with some strict inclusion, eliminate (U', τ')

Th 3: U survives the minimal constraint principle iff
some data (speech) can reveal U as Dee's preferences.

Th 4: In absence of cycles, Dee's preferences are revealed by her binary choices (even if choices are anomalous)

Economics and Psychology

—[T]here is one and **only one** social responsibility of business –to use its resources and engage in activities designed to increase its profits so long as it stays within the rules of the game, which is to say, engages in open and free competition without deception or fraud|| (Milton Friedman, 1970)