

# What next for Identity Economics?

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Identity economics offers a radical new way for economists to explain decision anomalies. By incorporating identity and norms into the classic utility function Akerlof and Kranton have, virtually for the first time, introduced social context as a key factor in understanding economic decision making. They introduce an identity term into the utility function to explain anomalous decision behaviour, and to reveal a new way to change preferences. We argue that the identity term in their utility function, is too general. It combines distinct elements of the social identification process, as defined by social psychologists, into one term, pointing research toward non-specific associations between a too-broad concept of identity and specific economic decisions.

In addition, to accommodate the fact that identity is malleable, influenced by situation and context, Akerlof and Kranton argue their utility function is non-standard and preferences vary according to the norms of the group that the individual identifies with. That is, norms change over time and therefore preferences change over time in response to social, societal and contextual factors. It appears that social identity changes preferences through the gradual change in the norms for a subject's salient group and not due to specific contextual factors within the setting of the current decision maker and current problem.

Yet to date, the research in identity economics has been designed to test the situational contextual factors on the decision maker, not the evolution of the norms of the group with which they identify. As Akerlof and Kranton also note, norms of groups evolve slowly over time. If so, then norms are not significant in understanding how preferences change. They provide a source for understanding what a decision maker may choose once they have ascribed to the set of norms of the social group they have identified with, but little more.

A more fundamental and situational driver of a change in preferences is whether an individual chooses to identify with a specific group or not. It is therefore more relevant to understand what makes a specific social identity salient to understand changing preferences, rather than knowing the norms of that group. It is this logic that leads us to argue that the identity term in Akerlof and Kranton's utility conflates distinct motivations by which identity can change preferences. One goal for identity economics is to show how identifiable social factors can directly and reliably influence economic decisions, in much the same way that behavioural economists have shown links between the framing of problems and predictable decision biases.

We reinterpret identity economics to incorporate a more specific definition of social identity and the social identification and categorisation processes that underpin it. We draw on social categorisation theory (SCT) and bounded generalised reciprocity theory (BGR) from social psychology for these additional elements.

We then add perspectives from Bacharach and Sugden's team reasoning approach, to offer a more robust definition of social identity and the social identification process. We argue that preferences change because the agency of motivation switches from 'me' to 'us'. The utility function then no longer describes motivation in individual terms but in social group terms. That is, the individual is motivated to choose outcomes that are in the group's or team's interest not the individual's self-interest alone.

We present two sets of recommendations for our research. We aim to link one social factor - common knowledge of group affiliation - as key to the development of a salient social identity by an economic agent. We then propose that, in adopting a social identity, an agency transformation occurs so the individual engages in team reasoning such that social group utility becomes the agent's goal.

We propose to use subjects' football team allegiance for an English Premier League team as the salient social identity. This avoids the challenge of manipulating subjects in the lab to create an artificial social identity.

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### **Key Words**

Identity Economics, salience, social identity, decision making