Political Activism and the Provision of Dynamic Incentives: Growing the Pie in the Battle for Redistribution

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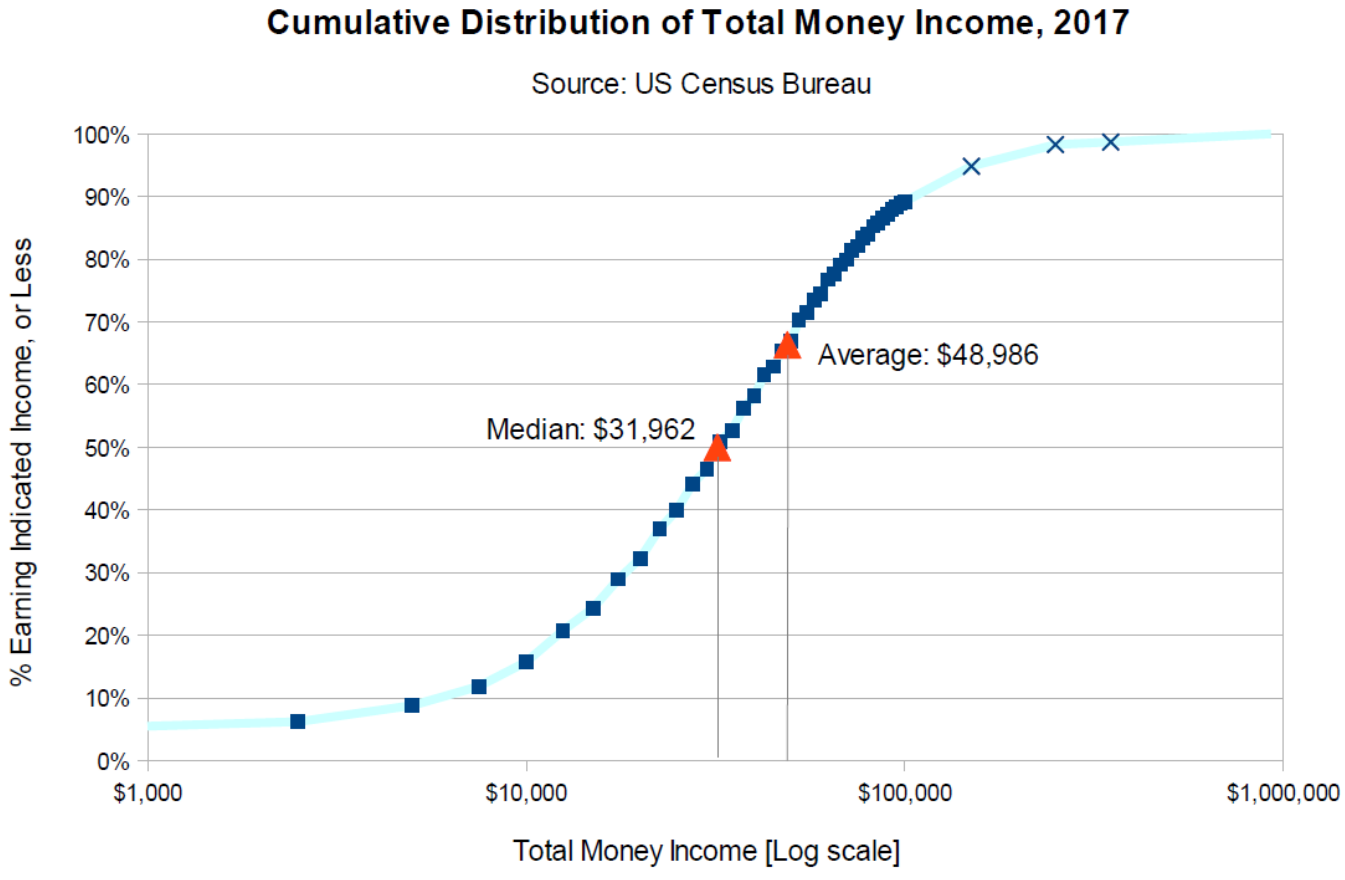
Motivation



⇒ **Why don't we observe full redistribution?**

more

One answer: POUM hypothesis

> *... [the] idea that the poor do not support high levels of redistribution because of the hope that they, or their offspring, may make it up the income ladder....* Benabou and Ok (2000)

Necessary conditions ... a bit excessive

i. **income mobility:** at the yacht club in the future

   ↪ current median income richer than average tmr !

ii. **persistent tax rates:** else redistribute now, undo it later

   ↪ taxes today apply to next generation, i.e. commitment

iii. **low risk aversion:** accept the gamble

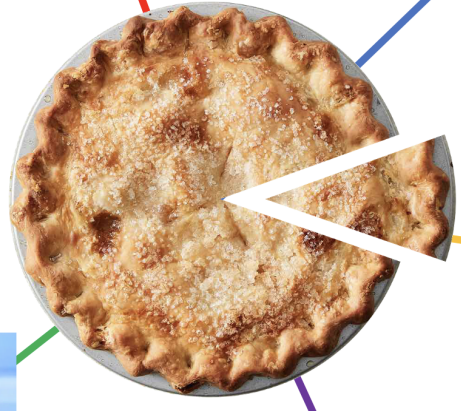
⇒ **This project:** endogenous income mobility and no commitment

Our answer: Political Activism

Redistribution

vs.

Growth



Bryan Thomas
@bdthom03

Replying to @trish_regan and @RepScottPerry
Remember when America was great . We did tax the wealthy

Jennifer Krog
@JenniferKrog1

Replying to @trish_regan @RepMarkMeadows and @RepScottPerry
Democrats don't know how to generate wealth, they only know how to tax it.

Our answer: Political Activism

Conflict growth vs. redistribution

Activism $\Rightarrow$ Political Persuasion $\Rightarrow$ **(efficient) incomplete** redistribution

Outline

1. **Description of the economy**
2. **Politics and activism**

1. Environment

Environment

Agent θ dynamic choice

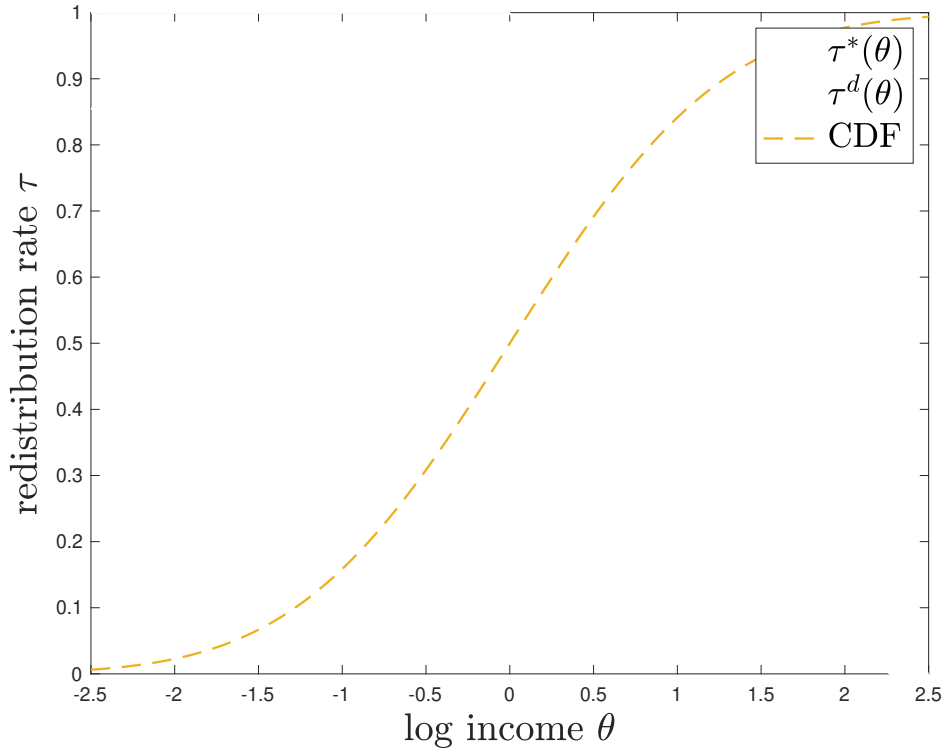
$$\max_{e} \ \log(c) + \beta E\big(\log(c')\big)$$

$c = \theta - e$	$t = 1$
$\theta' = z\theta^{\alpha} e^{\delta}$	gross income $t = 2$
$c' = \hat{\theta}' = \theta'^{1-\tau} \bar{\theta}'^{\tau}$	net income $t = 2$

$\Rightarrow$ individual education $e(\theta, \tau)$ decreasing in τ

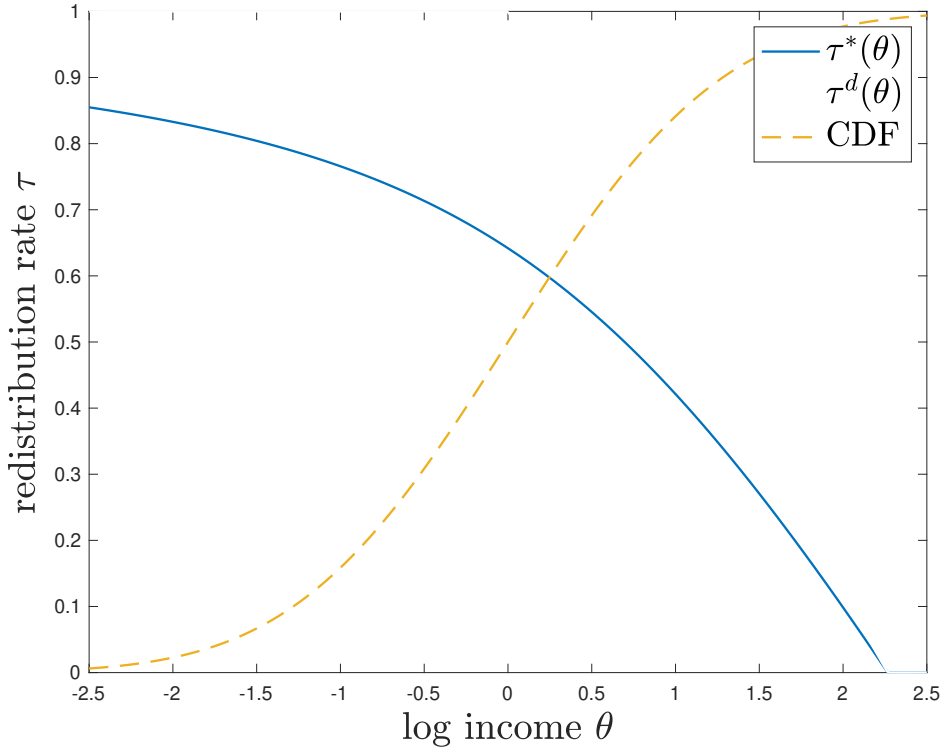
$\Rightarrow$ **which redistribution rate $\tau \in [0, 1]$?**

What is agent θ favorite τ?



What is agent θ favorite τ?

At $t = 1$, **before** education choice



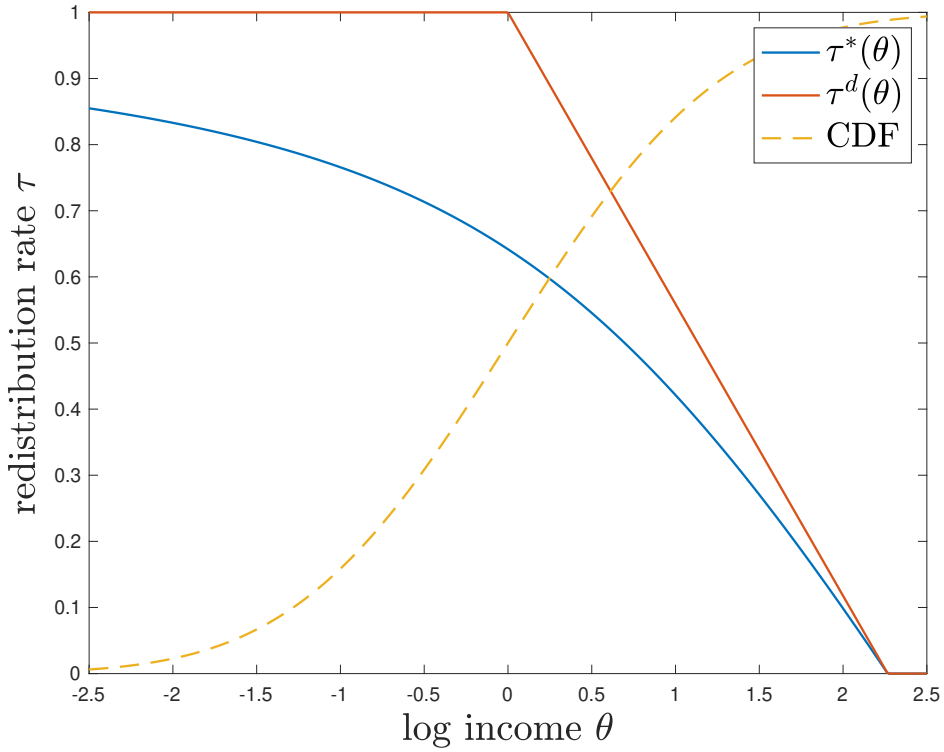
→ <u>redistribution</u>
across population θ

→ <u>insurance</u>
against idio. shock z

→ <u>incentives</u>
with private return δ

What is agent θ favorite τ?

At $t = 2$, **after** education choice



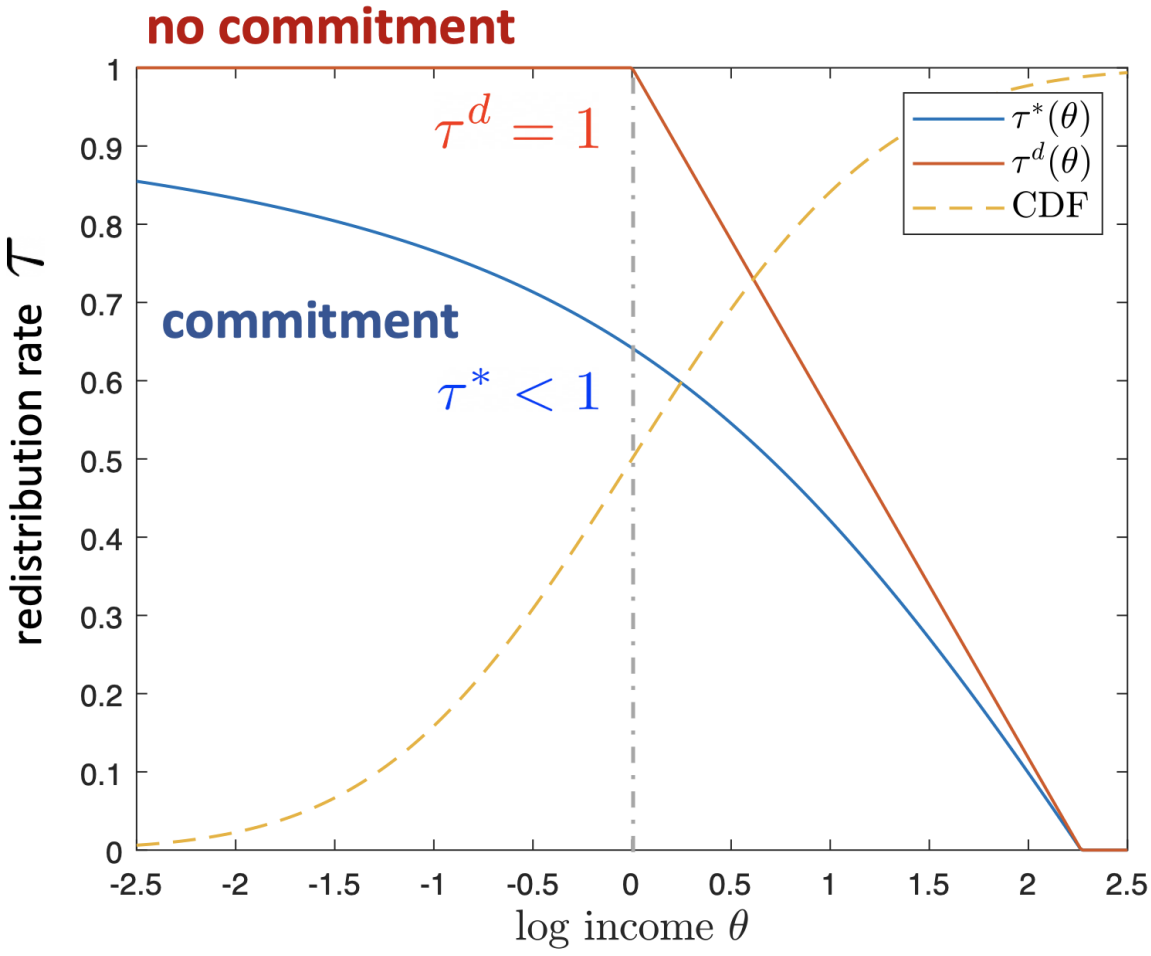
→ redistribution
across population θ

→ insurance
against idio. shock z

→ ~~incentives~~
~~with private return δ~~

$\Rightarrow$ **Higher rates of redistribution**

Benevolent planner?



Lack of commitment $\Rightarrow$ full redistribution (No POUM)

2. Politics and activism

Game and Timing

i. Choice of platforms: 2 office seeking candidates choose τ_l vs. τ_h

ii. Group activism choice

iii. Individual education choice at $t = 1$

iv. Political preference shocks: individuals and aggregate

v. Vote: majority voting over τ_l vs. τ_h

vi. End game individual uncertainty z, tax and transfer and consumption

Game and Timing

i. Choice of platforms: 2 office seeking candidates choose τ_l vs. τ_h

ii. Group activism choice **continuous and persistent**

iii. Individual education choice at $t = 1$

iv. Political preference shocks: individuals and aggregate

v. Vote: majority voting over τ_l vs. τ_h **no commitment**

vi. End game individual uncertainty z, tax and transfer and consumption

Which equilibrium platforms $\tau_l \leq \tau_h$?

Backward solution

3. Vote over policy platforms $\rightarrow$ probability p_h
2. Activism decisions $\rightarrow$ A^l vs. A^h
1. Candidate choice of platforms $\rightarrow$ $\tau_l \leq \tau_h$

3. Vote

- Given aggregate activism $\{A^l, A^h\}$ ...
- ... education ϵ and political shocks (χ, ψ) for τ_l,
- an agent with income θ votes for τ_h iff

$$V_2(\theta, \tau_h|\epsilon) > V_2(\theta, \tau_l|\epsilon) + \chi + \psi + \gamma\left(A^l - A^h\right)$$

where $\gamma \geq 0$ is *activism technology*

$\Rightarrow$ τ_h **wins with probability**

$$p_h = \frac{1}{2} + \Psi\beta(\tau_h - \tau_l)\frac{\sigma_2^2}{2}(2 - \tau_h - \tau_l) + \Psi\gamma\left(A^h - A^l\right)$$

2. Activism

Group θ choice (before education !)

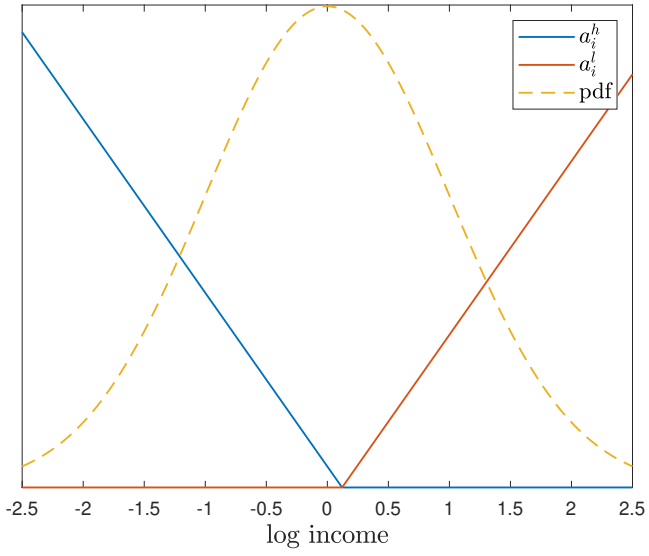
Given (τ_l, τ_h) and $\{A^l_{-\theta}, A^h_{-\theta}\}$,

$$\max_{A^l_\theta, A^h_\theta \geq 0} \quad f(\theta) V_1(\theta, \tau) - \frac{1}{2}\Big((A^l_\theta)^2 + (A^h_\theta)^2\Big)$$

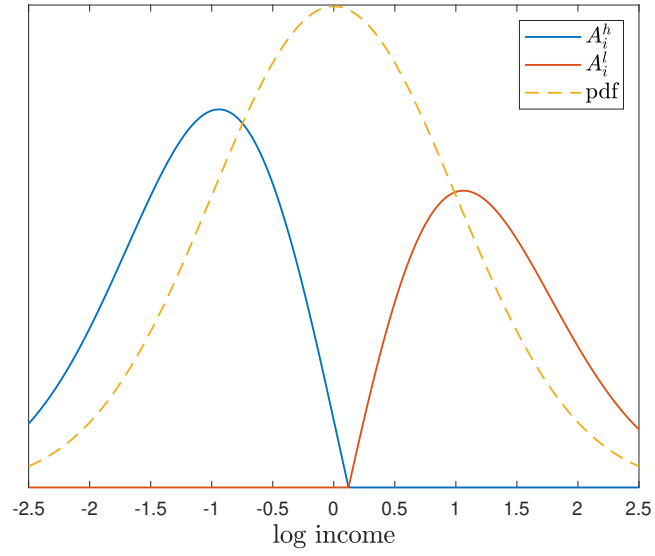
s.t. $A^x = \int_i A^x_i di$ and the outcome of the vote

$$p_h = \frac{1}{2} + \Psi\beta(\tau_h - \tau_l)\frac{\sigma_2^2}{2}(2 - \tau_h - \tau_l) + \Psi\gamma\big(A^h - A^l\big)$$

Activism across income groups...



(a) Per capita $A_\theta^x / f(\theta)$



(b) Group contribution A_θ^x

$$\tau_l = 1/4 < \tau_h = 3/4$$

activism $\gamma > 0$ and growth $\delta > 0$

1. Choice of platforms

Office seeking candidates

- Given τ_l, candidate H chooses τ_h

$$\max_{\tau_h \in [0,1]} \; p_h(\tau_l, \tau_h)$$

  and given τ_h, candidate L chooses τ_l ...

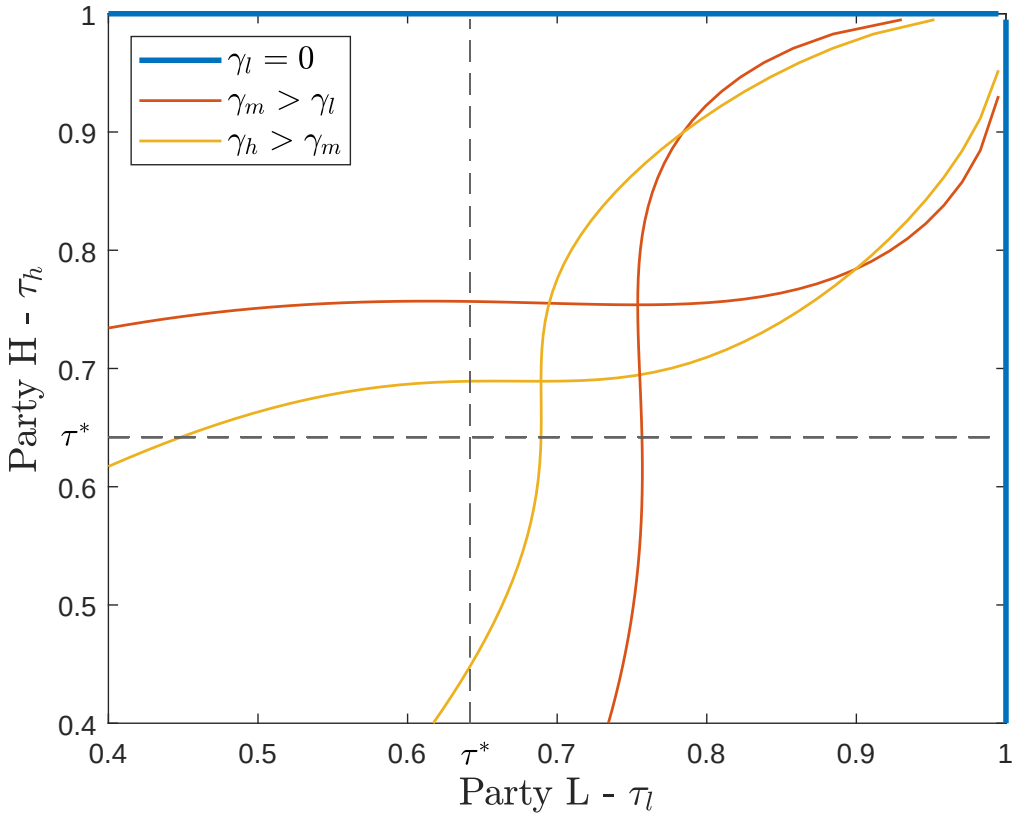
- Both anticipate the response of activism

$\Rightarrow$ **Symmetric Nash equilibrium** τ^p

$\hookrightarrow$ $\tau^p \neq 1$ if and only if **activism** $\gamma > 0$ and **growth** $\delta > 0$

$\hookrightarrow$ $\lim_{\gamma \to +\infty} \tau^{\mathbf{p}} = \tau^*$

Candidates' best response



... activism $\gamma > 0$ discipline candidates away from $\tau = 1$

Conclusions

- Key message: why don't we observe full redistribution?
  - $\rightarrow$ under lack of commitment, interplay
    - *political activism* ...
    - ... tradeoff growth vs. redistribution
  - $\rightarrow$ conflictual activism disciplines politicians

- What explains observed redistribution? more in the paper...
  - Average level of political activism γ
  - Distribution of political activism $\{\alpha_\theta\}$
  - Political preference heterogeneity across groups $\{\phi_\theta\}$
  - Voting participation across groups $\{\lambda_\theta\}$
  - Ideology of candidates μ