Inequality Aversion: the Self-Other Perspective

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In this paper we examine how inequality-aversion varies as a function of self vs. other-relevant decisions. We find that people are more inequality averse when decisions are about others versus about themselves. We attribute this difference to invocation of a relationship norm, which values equality, when deciding for others.

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EXTENDED ABSTRACT

In this paper we examine how distributive justice norms vary as a function of self vs. other relevant decisions. We find that people are more inequality averse when decisions are about others versus about themselves. However this is only true when payoffs are to be randomly distributed. When payoffs are related to a meaningful skill, decision-makers become less concerned with inequality in both self- and other-relevant decisions. This “skill shift” is more pronounced for other-relevant decisions than self-relevant decisions.

The trade-off between equality and efficiency has been a critical stress point in theories of distributive justice (Okun 1975, Rawls 1971/2009, Harsanyi 1975). Previous literature has suggested that people are inequality averse. They often sacrifice efficiency in favor of parity (Fehr & Schmidt 1999; Bolton & Ockenfels 2000). This inequality aversion persists even in situations when the person is not informed, ex ante, if the unequal distribution will favor her or the other parties. For instance, imagine that a person has to choose between two state-of-the-worlds. State A will result in equal payoff of $100 to all participants, including the decision-maker. State B will have a higher average payoff (say $120), but it will vary randomly amongst the participants, with a real chance of some people getting less than $100. The decision-maker will know her payoff only after she chooses one of these states. Even in such situations, participants typically favor the equalizing option – State A (Rawls 1971/2009, Binmore 1989). However much of the cited previous work examining this equality-efficiency tradeoff has dealt with self-relevant decisions. That is, the decision maker usually has skin in the game. It is not entirely clear if inequality aversion is similarly influential for other-relevant decisions.

The purpose of our investigation are multifold: Firstly, we want to establish whether people display inequality-aversion in other-relevant decisions. The previous literature cited above suggests that the answer to this question will be in the affirmative. But what is not entirely clear is whether this inequality aversion for other-relevant decisions is equal, more, or less, intense than for self-relevant decisions. A systematic difference in the self- versus other preference for equality can be socially inefficient. Imagine a well-intentioned leader misreading the preferences of others, and imposing a resource allocation regime on a population which is more equal, but less efficient, than what that population prefers.

We contend that the framing of a decision as a “distributional decision” for others evokes a socio-communal relationship norm, instead of a more transactional-utilitarian norm. This invocation of a socio-communal norm will in turn enhance preference for the “equality” value, at the expense of the “efficiency” value. This will result in a higher regard for inequality-aversion in other-relevant distribution decisions. In contrast, this socio-communal norm will be less impactful, and somewhat counterbalanced, by one’s self-serving preferences when making a self-relevant distribution decision. Therefore we expect a systematic self-other disparity, where distribution decisions will be more equal (and less efficient) for others than for self.

Hypothesis 1: There will be greater efficiency- (vs. equality) preference for other- (vs. self-) relevant decisions.

Literature on perspective-taking and self-other decisions has also consistently demonstrated a strong social projection bias. This is a result of egocentric decision-makers falsely projecting their own preferences onto others (Ross, Green & House 1977, Dawes 1990). Therefore we expect a positive relationship between self- and other-distribution decisions.

Hypothesis 2: Self-relevant and Other-relevant distribution decisions will be positively correlated.

In our empirical investigation, we first begin by measuring equality vs. efficiency tradeoff choices for self-relevant and other-relevant outcomes using hypothetical scenario based experiments. We elicit both outcomes from all participants and measure the within-subject self-other gap. In subsequent studies, we also measure individual risk preferences and relate these to equality-efficiency tradeoff choices. It has been previously suggested that inequality-aversion in self-relevant settings may be a manifestation of risk preferences (Christiansen & Jansen 1978). Greater risk aversion translates into a more concave utility function which, in turn, would imply greater willingness to tradeoff expected-value in order to achieve a more egalitarian wealth distribution. We reexamine this link and investigate if this extends to other-relevant decisions as well. In our initial set of experiments, unequal rewards are to be allocated randomly. In the later studies we scrutinize contexts where allocation of rewards is not random, but skill based. In particular, we investigate if skill-based situations enhance preference for efficiency (vs. equality) in both self- and other-relevant decisions, and whether this “skill shift” is similar for both types of decisions.

While preference for equality continues to be the prevailing norm of distributive justice in a variety of socio-communal settings, a preference for differentiation based on individual contributions is normative within the economic domain (Bazerman, White, & Loewenstein, 1995). We argue that in environments where “skill heterogeneity” is prevalent, distribution decisions will acquire a less relational and more transactional motivation. This will in turn lead to greater consideration for efficiency over equity, even for other-relevant decisions.

As far as self-relevant decisions are concerned, we conjecture that this shift from a relational to a transactional norm will be relatively muted. Therefore decision-makers will continue to display even higher consideration for efficiency, but this enhanced consideration will be lower for self-relevant than for other-relevant decisions.

Hypothesis 3: A skill-based context will lead to a higher consideration for efficiency. This enhancement in consideration will be higher for other- (vs. self-) relevant decisions. Therefore we expect an interaction effect of self-other decisions X random-skill based allocation.

REFERENCES


