Research Paper
Impact Factor: 5.442
Peer Reviewed Monthly Journal
www.ijmdrr.com

IJMDRR
E- ISSN –2395-1885
ISSN -2395-1877

CONSUMER BEHAVIOUR AND GAME OF STATUS A CONCEPTUAL NOTE ON STATE INTERVENTION UNDER BEHAVIOURAL ECONOMICS

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Abstract
The policy making in an economy draws heavily from the standard economic wisdom. The conventional economic theory fuels into setting up of the policy framework. This is true of all walks of decision making, consumer theory being no exception. However, apart from theory, the choices that we make are guided by our behaviour to a great extent. Besides what the theoretical wisdom says, our behaviour and instincts are more elementary in helping us take certain decisions. Hence, when consumer behaviour is directed by both- theory as well as heuristics, building up policies merely on the basis of the former is destined to give erroneous results. This in turn can have serious repercussions for the economy. Thus, in order for the economic policy making to be more realistic in achieving its objectives, it is important that it takes into consideration a whole set of factors impacting consumer behaviour. This will help bridge the gap between the actual and expected policy outcomes. This paper is a conceptual note that uses consumer behaviour under conditions of income inequality to explain the implications of state intervention, without considering behavioural heuristics. It shows that in absence of behavioural approach, state policy to reduce income inequalities tend to guide consumption pattern in favour of wasteful outlays on positional goods vis-à-vis more developmental expenditure on required heads, including human capital.

Keywords: Behavioural Economics, Income Inequality, Consumer Behaviour, Positional Goods, Role of State.

Introduction

Economic status and affluence of an individual determines a lot about his social life. Poverty line not only acts as a threshold dividing two sections of economically assorted sets but also creates two different worlds- poles apart in nature and too diverse to be gelled up.The section falling short of income to touch up the poverty line gives rise to a socially unacceptable lot of individuals. With not having enough income to buy food and afford adequate housing, with living hand-to-mouth even for basics of human survival like water, food, shelter and clothes and with all this economic inadequacy turning out into inadequacy of opportunities as well, poverty imposes on them traits of seclusion. Poverty is, thus, the most visible characteristic of underdevelopment of any nation, dividing its population not only in terms of their socio-economic profile but even in opportunity, aspirations and achievements. Nevertheless, what creates and sustains the creation of these two worlds is yet another significant, however hidden, phenomenon, called inequality. It is the paucity of income and a resource that is the root cause, but accentuates the problem is rather a relative paucity than the actual extent.

Development of every economy is based on simultaneous growth of all the sections of the society and not only on that of relatively well off. Thus, the prosperity of the middle income group and more importantly the economically weaker sections is equally important. The growth of a country is not measured by looking merely at the growth trends, rather the welfare effects of the same. This growth can however be seen from two distinct perspectives. Firstly, it is the data and numbers pertaining to Gross Domestic Product- both absolute as well as per capita, that are important. This is so because income is the cake which when gets divided amongst the population, provides them utility. Secondly, it is the distribution of GDP, not per capita, rather actual. Calculation of per capita income assumes that GDP is divided amongst each and every individual in the economy, and that too equally. However, this is far from reality. Given the population of an economy, there is always one set of people who do not get any share in the growth of the economy i.e. inspite of an increase in the national income, this set of people witness no change in their incomes. There is another group of individuals who do witness a rise in their personal incomes, but this rise is proportionately way too little in comparison to the actual increase in income in the economy. And then there is yet another group who corners most of the income gain and thus shares disproportionately an extensive share of the income growth. Hence income inequality comes into play.

The rest of the story develops on the fundamentals of behavioral economics. The two perspectives, discussed above, taken together, impose huge complexes on those lying on the lower rungs of income distribution. People cannot change the level of incomes that they earn, neither can they control their placement in the income hierarchy in the economy. Thus, in order to overcome these complexes, people try and manipulate their consumption basket. They do it in a way so as to make others perceive that they belong to a higher income category. For this they resort to a consumption behavior that cannot be explained using conventional economic theories. The explanation is more psychological, than calculative. This paper is an attempt to study these manipulations, understand their implications and list the possible challenges that the state may face in order to deal with the same. The paper hence posts the conflict that arises when policy gets divorced from the ground reality as the former is set on micro economic foundations whereas the latter rests on behavioral heuristics.

Literature Survey

Marx (1847) wrote that"…a house may be large or small; as long as the neighbouring houses are likewise small, it satisfies all social requirements for a residence. But let there arise next to the little house a palace, and the little house shrinks to a hut…".The standard economic theory is based on the idea that utility of individuals is independent of the social framework. This is to say that an individual's utility is a function of level of his own consumption. Recent studies and experiments under behavioural economics (Kahneman and Tversky, 1974), however, show that the income and associated status of peers has a systematic impact on observed degrees of utility of an individual. Thus an individual's utility function also accommodates the level and pattern of consumption of peers. Many economists and researchers have attempted to gauge into this issue with a view to answer the 'how(s)' and 'why(s)' of this pattern.

As perextensivewisdom, social status is a concept associated with social relativity in positioning. It is a positioning of individuals in a specific social hierarchy based on what they own and what can they do with it all (De Botton 2004; Weiss and Fershtman 1998). There exists a direct relationship between social status and one's positionality with respect to other people. These further acts as a reflection of superiority or inferiority that an individual enjoys with respect to his social standing (Goldthorpe 2010).On a similar note, Wilkinson and Pickett (2010: 40) state, "higher status almost always carries connotations of being better, superior, more successful and more able". Social status is significant as an individual who is placed higher in the social heirarchy is by virtue of his position expected to be treated favourably by others with whom (s)he might engage in social and economic interactions (Berger and Zelditch 1998; Stewart 2005) as against those who fail to rise up the social status ladder. In addition, such social status is also indicative of ownership of power and privileged access to scarce resources. And consequently, the economic rewards and social benefitsassociated with status make people strive for it.

Consequently, the literature advocates that it is obvious for people to be eager to attain higher and higher status, giving rise to what may be called a‘status competition’ (Marmot 2004). Wilkinson and Pickett 2010 discuss another related phenomenon called the status anxiety. Status anxiety develops as an outcome of status differences, and evolves as these variations become starker and more visible. Wade (2009) rather suggested that the economic financial crisis of 2008 was partially driven by status anxiety. It was the dire wish of the low-status-people- specifically those belonging to the poor and the middle-income groups, to catch up with the living standards of the rest- i.e. the rich, that drove the former deeper into debt. The popular idiom of ‘Keeping up with the Joneses’ also denotesan individual’sinclination to compare himself with their peers as a benchmark. Failing to keep up to the status of those around is perceived to be a sign of social inferiority, and hence results in anxiety and discontent (Luttmer 2005).

One manifestation of anxiety, is the presentation of the self as superior through self-enhancement. Hierarchy in the social context and thus societal status of an individual (or a household), plays an important role in fabricating the consumption pattern. This pattern, however, may not necessarily be in line with the consumption requirements and income levels that this individual enjoys. Consequently, his utility does depend upon his own status vis-à- vis others, based on his ranking in the income distribution. This brings about a great deal of spending on what are called ‘positional goods’ (or status goods) as compared to the non-positional ones. Unfortunately, this shift is a result of a status-led race. So, in particular, each attempts to bring about a balance with those above in the sense that he is willing even to take higher risks if this gives him the chance to break even with his peers. Therefore, caring about their own status, defined as their rank in the distribution of income and accompanying consumption, the consumer’s problem becomes ‘strategic’ as his utility now depends on the status, income and thus consumption choices available to others too. In an unequal society, thus, the hoard to get ahead of one’s own group and a need to be a part of those ahead make individuals spend more on conspicuous consumption than what is warranted by their respective incomes. And with falling incomes, affordability and opportunities as one goes down the income deciles, this is ensured by a risk-taking behaviour-getting stronger and stronger.of late, apprehension about the negativities arising out of rising income inequalities have massively picked up. And thus, the possibilities of a resultant append of status anxiety has also got further reinforced (OECD 2009, 2011). Inequalities in income distribution are found to be strongly and positively associated with creation, maintenance and sustenance of social hierarchies. This is seen to be giving further impetus to social anxiety, causing detrimental penalties in the form of strengthened criminal behaviour and violence, lack of trustworthiness and many such unfavourable consequences (Wilkinson and Pickett 2010). Disrespect and status in securities are what drive such aggressive behavior (Faris and Felmlee 2011). Many more negative consequences and implications of status anxiety, ranging from obesity and drug use to educational performance and social mobility, are discussed by Wilkinson (2004). This too is a major manifestation of the game of status.

However, the idea that inequality fosters status anxiety has a sea of empirical evidences also. Or to put it correctly, not only has it been massively assumed in literature, the empirical evidences for its validation are massive too. Loughnan et al. (2011) and Layte and Whelan (2013) presents such relationship. They found a positive relationship between income inequality and status anxiety.

However, once this relationship is well accepted, it is time to make it a significant part of policy framework also. Ignoring it can have serious challenges for the success of the policies so framed and executed. A detailed understanding of this statement is presented in the section that follows.

Challenging the Conventional Wisdom

The literature so far has shown that the consumer decision making, fostering consumer behaviour, has a lot to do with issues lying outside the purview of microeconomics. Hence, results based on micro-economic modelling alone do not confirm to realty and thus state policing based on the same, and neglecting behavioural aspects altogether, might not be apt. Rather they might end up throwing contradictory implications for the economy. This section puts forth two such fallouts that conformist understating of consumer behaviour fails to project, as they do not base these results on heuristics and behaviours.

Manipulation of Consumption Basket

What is clear from the literature is that 'status' too defines utility. Consumption of any good/service is then guided by the characterization of that good/ service as per the source of utility that it generates. It might generate a pure direct utility, based on the amount of good consumed. It might in addition contribute to utility via a status-enhancing trait or both. Thus, the choice of consumption basket provides certain utility- that is well documented as per the conventional micro economics. But there lies an additional component to this direct utility that takes the form of externality. This form of utility is an upshot of relativity. It is based on one's consumption vis-à-vis others, especially his peer group- and comes under the purview of behavioural economics.

An important behavioral aspect of consumption is thus to signal high status to others. Consumption choices can only do this to the extent they are both visible to others and associated with high status. Part of the motivation for wearing a fine suit or driving a luxury car, both of which are visible to others, is to convey the message to others that one has a status high enough to afford them. Such goods are called visible or positional goods as they signal one's position in the society. With an idea of overcoming the isolation that being a member of lower income category imposes upon them, the poor have no choice but to enter into a forced relook at the utility functions and playing around with the choice of positional and non-positional goods. A strong urge to be a part of those above them [economically] makes each individual devote an extra piece of his income for consumption of the positional goods, leaving behind little that can be spent on necessary, non-positional goods. With not enough income for such non necessary consumption, this still might not (rather in most cases does not), have any negative impact on their utility functions. This is so because these individuals get blinded by a game of status, attaching their utility functions highly with conspicuous consumption, and consequently making the utilities go higher and higher. This being a psychological phenomenon happens with almost everybody, but a small handful of wealthy lot at the top of the income hierarchy.
However, the impact that this status game has on individuals is based on the position they hold in the ladder of income. Thus, heterogeneity in income holdings and thus inequality in income distribution brings out varied impacts ranging from dilution of savings by those above the poverty line to feed into this [un]necessary purchasing to engaging in various speculative and risky ventures by those who don't even have enough to satisfy their basic minimum requirements. Acknowledging the heterogeneity in income distribution even below the poverty line with many hovering near it and still plenty deep below, the situation becomes even graver. The economic impact of setting aside a part of the already meager income and the associated psychological impact can really be highly hampering,

not only for these individuals at the micro level, but even for their households and the nation at the macro level. It means and holds a lot for the growth as well as development of the economy.

To begin with, let us assume that the consumption of an individual is constrained by the income earned by him. Hence, he is neither going to neither dilute his savings, nor will he take up debt to finance his consumption needs. Now since household spending must satisfy an inter-temporal budget constraint, spending devoted to positional consumption must be diverted from some alternative uses. This alternative use has to be the non-positional consumption. Thus, a trade-off between consumption of positional and non-positional goods becomes the first most case. Relaxing our assumption here takes us to another possibility of eating up into savings to finance positional consumption. Thus, when one resumes to swapping positional and non-positional spending, he reduces his direct consumption impact. And in case he dilutes savings, what gets impacted is future consumption. The positionality of status implies that status seeking diverts resources away from welfare-enhancing uses, wasting them- from the point of view of society as a whole- on efforts to win a zero-sum game. Whereas, as one approaches the bottom income segment, this impact weakens because of lack of choices brought about by low income levels. So, the pull of status leaves them with no other option than to be risk-prone. Further, in developing economies like India, the utility functions of those who lay deep below the poverty line suffers the most. This is so as they cannot even afford a risk-taking behaviour, in presence of paucity of resources at their disposal. Going by the model then, the utility function of these people suffers adversely as status and consumption of others- the relatively less poor, middle income group as well as rich- improve vis-à- vis stagnation of the same at their end.

The State Intervention

Asserting the developmental role that the state is expected to play in a developing country like India, the main objective shall be to give a long-time due form and direction to state intervention. In case of a non-behavioral approach, the following strategy would be adopted. With huge inequalities in income distribution, and many lying below the poverty line, state shall take up the responsibility of catering to the needy and the vulnerable. Thus, in an economy where a few share in the growth process, inclusive growth becomes the state's obligation. The convention suggests that the state shall do this via a deliberate trickle-down policy, through a re-income distribution strategy. The idea is to reduce income inequalities, painting a more egalitarian society. However, the behavioral perspective to this problem turns this approach topsy-turvy. This is so because in case of a compressed income distribution, any increase in consumption of positional goods leads to huge rank improvement as the 'jump-over' in status is more. The resultant enhancement of status under positionality is relatively higher when the incomes are clustered as against a situation where incomes are too scattered. Thus, the idea of reducing income inequalities as a deliberate attempt by the state comes under question as it furthers increases the returns on positional spending and thus incentivizes people to hike up their conspicuous consumption without there being any associated increase in income levels.

Let us now turn towards heterogeneity. When income levels are fixed, especially referring to those living below poverty line, any increase in consumption of positional goods can thus most likely be financed through a reduction in consumption of non-positional goods. However, since all are participants to this status game, an increased spending by one will create a strong pull effect on all others and consequently all will follow suit, bringing about a similarity in each one's consumption function. Thus, making it a zero-sum game. This puts a question mark on the nature of role of state and the inequality reducing policies used by them.

Further, since game of status is and will remain an inseparable part of the consumption pattern of people, irrespective of which income class they belong to, the question of affordability turns out as an important aspect. Of many other goods that serve as non-positional goods, human capital in the form of health and education too work as those goods that are traded away in order to increase the spending on positional goods. It goes without saying that a choice of spending between human capital and positional goods shall be made definitely in favor of the former, both from the point of view of the economy as well as personal development. This is so as spending on human capital positively aids in increasing the income earning capacity of an individual and creates possibilities of driving him up the income ladder. Any state policy that provokes people to spend higher on positional goods, thus, either reduces savings and/or brings down the outlay on non-positional heads- including human capital. Such a consumption pattern is undoubtedly against the growth and development norms of any economy, especially the developing ones.

The Road-Map

Understanding the impact of behavioral science on consumer behavior and acknowledging its implication for growth and development of the economy, the challenge is how shall this transition from non-positional to positional and thus, the current low level of human capital spending be curbed. The need here is to understand that consumer will spend on those goods that are status-led and are visible. Human capital has neither of these characters. The need is thus to convert the traits of human capital from being non-positional to being positional. This can be done by imparting ‘visibility’ to consumption of human capital. If an individual’s hunger for possessing visible goods gets satisfied through a better health and education, this would definitely reduce his dependence on other wasteful forms of visible goods. Hence the economy needs to aim at achieving higher level of state provisioning of human capital- both in quantity and in quality.

Even though state intervention is assumed and accepted to be the answer for enhancing the level of human capital formation in the country, the paucity of resource availability in a country like India is equally accepted. Under such circumstances, state cannot solely be held responsible for all the human capital formation. Contribution of private decision making is important too. This, thus is the time to gauge into the behavioural aspect of consumption decision making and use heuristics to supplement the process of pacing up human capital formation and simultaneously bringing down positional spending- via what can be called ‘nudging the choice architecture’.

It’s time to use behavioural economics to understand decision making at micro level, and alter it in a favourable way. This calls for constructing a choice architecture for micro level consumption basket, based on ingredients of economic growth, development and sustainability and then policing accordingly to ensure that the so-developed basket is chosen from all other available alternatives. This will require using ‘paternalist liberalism’ to fusrtly be sure that people choose what is right for them, both in the short as well in the long run. This is synonymous with using guided instincts, and not letting him chooses anything but the best. Secondly ‘liberalism’ remains the superlative as even though the associated selection process is vastly guided, but it is more of ‘guidance in disguise’. The idea is to use behavioural economics and consumer heuristics to nudge for what is targeted, and presenting consumers with such a choice architecture that their personal choice conforms to the socially optimal one.

Possible Complexities and Challenges

There exist certain complexities in such a discussion. These complexities do pose challenges in devising models to understand the related behavioural phenomenon. These are as follows. First, visibility is only one of many properties possessed by any given good that contribute to the observed demand for it. It is difficult to disentangle demand for visibility from demand for these other properties.It simply talks of the fact that while we may conjecture that a person buys a mobile phone, it would anyways satisfy many other properties of being just a phone other than its power for social signaling. Thus, the mobile phone might not here be a visible good in totality but its brand would be.
Second, it is difficult to disentangle conspicuous consumption from social learning as a good deemed as positional at one income class might become non-positional for someone belonging to a higher income category(Grinblatt et al., 2008). Hence, a mobile phone might be visible for somebody belonging to a lower income class whereas it might not be for somebody relatively well-off. Similarly, for this latter individual, buying jewelry might be visible, which again might not be the case for somebody relatively higher on the income ladder.

These complexities definitely do pose great challenges to any study based on behavioral economics but acknowledging them, this study is a worthy start to recognize the impact of behavior in economic decision making. Inspite of all its challenges, such proposed study, to the best of my knowledge, shall be the first systemic analysis of income distribution, intensity of poverty and risk taking.

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IJMDRR
E- ISSN –2395-1885
ISSN -2395-1877

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