

The Political Economy of Alternative Realities

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- Over 40% of Republicans hold / do not reject
 - Climate change not human made,
 - 2020 election not free and fair.
- **This paper** models coherent but false alternative reality:
 - Members of intellectual elite conspire
 - Criticize politician about commonly important issue (competence) if disagree about divisive issue (e.g., cultural values).
- Politician chooses whether to supply alternative reality, which partially persuades voter.
- Once voter believes alternative reality, he engages with it strategically in Bayesian fashion.
 - He will distrust elite's criticism of politician and vote accordingly.
- Model explains salient unexplained facts about politics.

- Supply of misinformation in politics: Glaeser (2005), Kamenica and Gentzkow (2011), Guriev and Treisman (2020), Eliaz and Spiegler (2020).
- Misspecified learning: Benabou, Falk, Tirole (2018), Galperti (2019), Eliaz, Galperti and Spiegler (2022), Schwartzstein and Sunderam (2021), Aina (2023).
- Populism and identity politics: Bonomi, Gennaioli and Tabellini (2021), Besley and Persson (2021), Bellodi, Morelli, Nicolo, and Roberti (2023).
- **Our contribution:** Portable model of alternative reality, implications on voter behavior, endogenous conspiracy theories, and bad policies.

Outline from here

- ① Model and main result
- ② Applications
- ③ Conclusion

Key alternative reality: Intellectual elite conspires to attack politician because they disagree about ideology.

- Deep state attacks Trump b/c he protects conservative values.
- Soros network attacks Orban b/c he is anti-immigration.
- Judiciary attacks Netanyahu b/c he is pro-annexation.
- ...

If believed, alternative reality discredits criticism of the elite.

Principal-agent model with alternative reality

- Two principals:
 - Intellectual elite: continuum of identical members report about competence of politician ($s \in \{0, 1\}$).
 - Incumbent politician: may send propaganda ($p \in \{0, 1\}$) to change voter's prior.
- Two agents:
 - Receptive/unreceptive voters form beliefs about the politician's type
- Key modeling idea: principals have "reality" types R or AR
 - AR types have zero objective probability.
 - But: we assume propaganda makes voter's prior of AR positive.
 - AR has real consequences since voter treats them real.
- AR is a conspiracy theory:
 - In R, atomistic elite cannot influence voter and messages truthfully.
 - In AR, elite can act collectively and sends message to influence voter.

Types, beliefs, and preferences

Politician:

- Common: bad or good, $\theta_c \in \{0, 1\}$, elite gets an imperfect signal.
 - Examples: uncorrupt or increases prosperity.
- Reality types: AR politician believes elite is AR.

$$U_p = \bar{\mu}(\theta_c = 1|p, s) - f \cdot p. \quad (1)$$

Elite has reality types $\theta_r \in \{R, AR\}$, objective equivalent to

$$U_e = 1_{\{\theta_r=R\}} \cdot 1_{\{s=\theta_c\}} + 1_{\{\theta_r=AR\}} \cdot \bar{\mu}(\theta_c = 0|p, s). \quad (2)$$

- A coordinated elite would harm the politician

Receptive voter has “mind types”: normal and persuaded.

- Normal has correct beliefs: knows AR does not exist.
- Persuaded (reached by propaganda): puts positive weight on AR.

Unreceptive voter

- Do not recognize propaganda, remain normal

Timing

- 0 Politician's type realized and observed by the politician.
- 1 With $1 - \beta$ prob politician can decide on propaganda. Elite observes the propaganda and receives a signal on the politician's type (correct with π).
- 2 Elite sends its message. All voters observe the elite signal, and receptive voter (α share of electorate) also observes the propaganda. Voters form their beliefs.

- PBE modified to account for manipulated prior
 - Persuaded voter's posterior computed from his (incorrect) prior.
 - Persuaded voter makes Bayesian inference from prop, elite report.
 - But only after experiencing change in prior.
- Restrict attention to "PPO" equilibria:
 - Politician-pure: all politician types use pure strategies.
 - Politician-optimal: best for R politician.

Proposition

For $\alpha < 0.5$ and π large, the PPO equilibrium:

- ① *In the reality (R):*
 - *Elite reports common type truthfully.*
 - *Bad politician sends propaganda.*
- ② *In the alternative reality (AR):*
 - *Elite reports politician bad,*
 - *All politician sends propaganda.*

▶ α large

▶ Demand

- We think about a narrative as an equilibrium.
- Equilibrium beliefs are supported by behavior of AR principals:
 - AR elite conspires, always criticizes the politician
 - AR politician believes elite is AR → sends propaganda
 - Voter cannot infer from propaganda that politician is bad: in AR even good politician sends propaganda

- Propaganda increases voters' belief about the bad politician
 - Similar implication to Guriev and Treisman (2020), but different mechanism and in a democratic environment.
 - In line with empirical evidence by Di Tella, Galiani, and Schargrodsky (2018); and Guriev and Treisman (2022).

- Once voter believes in the AR, elite criticism benefits politician
 - Elite always criticizes in AR, not always in R.
 - Hence observing criticism increases posterior of AR, and with it posterior that politician is good.

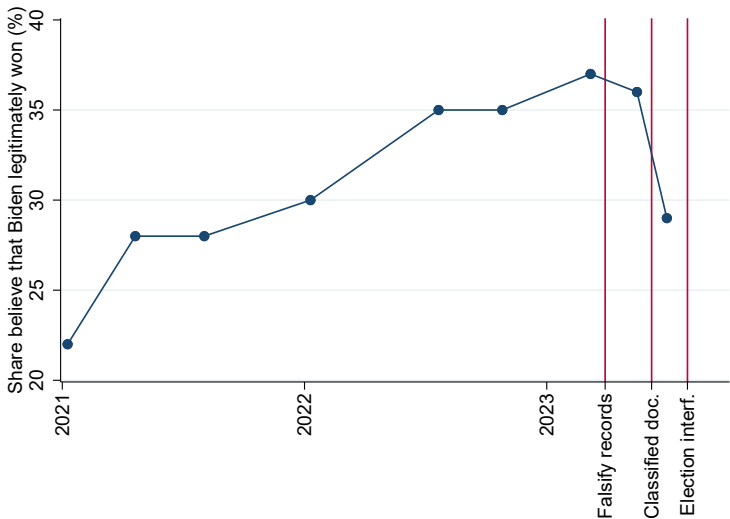
Evidence on inverted effect: Trump

- CBS News Poll – June 7 - 10, 2023
- If Donald Trump is indicted in the matter of his handling of classified documents, would that make you...

	Moderate	Conservative
More likely to vote for him	24%	44%
Less likely to vote for him	13%	3%
Not affect whether you vote for him	63%	53%
Observations	80	408

- Once voter believes in the AR, elite criticism benefits politician
 - Elite always criticizes in AR, not always in R.
 - Hence observing criticism increases **posterior of AR**, and with it posterior that politician is good.

Inverted effect: Belief in AR



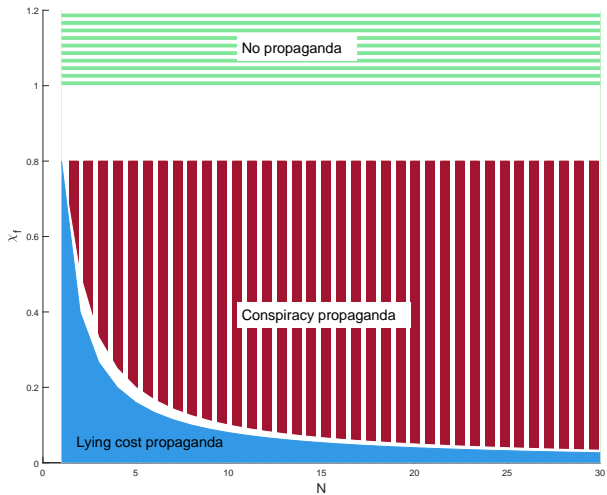
- 9 CNN polls on the legitimacy of 2020 Elections

- ① Model and main result
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- ③ Conclusion

Application 1: Endogenous alternative reality

- Why is alternative reality a conspiracy theory?
- Simpler version: elite members have low reputation/lying cost.
- Advantage of conspiracy: explains away more credible evidence.
 - Elite has a “public good” problem: members do not internalize that their lies benefit each other.
 - Low benefit from lying.
 - Conspiracy solves public good problem.
 - High benefit from lying.
- Implication: The more hard evidence presented in media, the more the politician prefers conspiracy to lying cost propaganda.

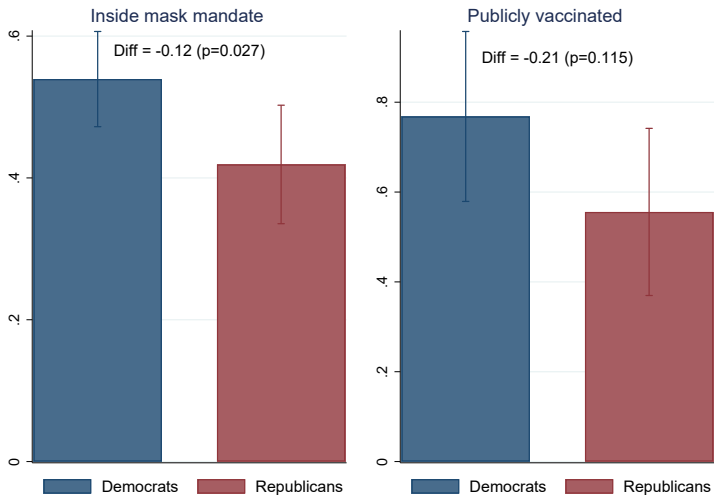
Endogenous AR: result



Application 2: Government policy

- **Main idea:** Politician will follow policies that contradict elite consensus even if doing so is universally harmful.
 - To avoid praise from the discredited elite.
 - Logic of the model:
 - Politician can take harmful action to influence precision of elite signal.
 - Politician overweighes receptive (core) voters.
 - Propaganda inverts criticism for the receptive voter.
- ⇓
- Politician prefers precise signal: acts against elite concensus.

Evidence on government policy



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Conclusion

Prediction	New result	New mechanism	Evidence
Basic model			
1. Propaganda lowers accountability in democracies	yes	yes	consistent
2. Elite's effect inverted with propaganda	yes	yes	causal
3. AR beliefs amplified by subsequent events	yes	no	consistent
Endogenous alternative reality			
5. Alternative realities feature conspiracy theories	yes	yes	consistent
6. Credible evidence makes AR conspiratorial	yes	yes	none
7. Propaganda creates distrust and non-adoption	yes	yes	consistent
Government policy			
8. Propaganda causes harmful policies	yes	yes	consistent

Table: New predictions

Overview

- Paper looks at the impact of regime changes on FDI
- Authors exploit 4 regime changes in 2 countries:
 - Poland: $A \xrightarrow{\text{Fall of Berlin Wall}} D \xrightarrow{\text{PiS in power}} A \xrightarrow{\text{PiS out of power}} D$
 - Israel: $D \xrightarrow{\text{Judicial overhaul}} A$
- Authoritarian backsliding is bad for FDI

My impressions

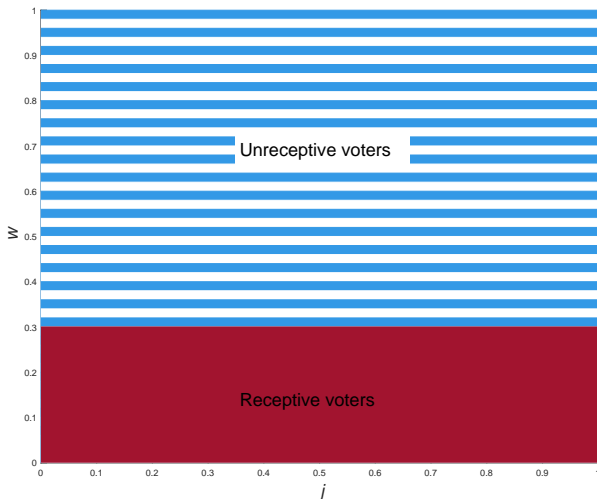
- Question is of primary importance
 - Identifies an important mechanism of the democracy-growth relationship for open economies
- Documents two (or four) interesting case studies
- External validity: Poland and Israel are rare examples (developed countries with recent shifts)
 - Do we expect similar effects for developing countries?
- Evidence is so far anecdotal
 - Extend analysis to more regime changes (Acemoglu et al. 2019)
 - Extend analysis to heterogeneity across industries/firms
 - export vs domestic market
 - large multinationals vs startups

Proposition

For $\alpha > 0.5$ and π large the PPO equilibrium:

- *In the reality (R):*
 - *Bad politician sends propaganda.*
 - *Elite reports common type truthfully.*
- *In the alternative reality (AR):*
 - *Politician always sends propaganda.*
 - *Elite randomizes when the politician is pro-voter and good, otherwise does the same as for small α .*

Voter types



Audience of media $j = \{(z, w) \in [0, 1]^2 : z = j\}$

Placebo: competition effect

	Trump share (1)	Trump donors (2)	Other donors (3)
Δ pred Dem vote margin	0.001 (0.001)	-1.07 (1.60)	1.43 (3.57)
Old pred Dem vote margin	0.001 (0.0006)	0.402 (0.454)	5.36*** (1.05)
Constant	0.109*** (0.017)	49.7*** (14.1)	346.4*** (38.2)
Observations	266	296	296

▶ Back

Timing

- 0 Politician's type realized and observed by the politician.
- 1 With $1 - \beta$ prob politician can decide on propaganda. Elite observes the propaganda and receives a signal on the politician's type (correct with π). The receptive voter observes the propaganda and chooses her $q_{ar} \geq 0$ prior about the AR.
- 2 Elite sends its message. All voters observe the elite signal. Voters update their beliefs.
- 3 The voter can reelect or replace the incumbent.

Demand for alternative reality

- Voter utility

$$V_{rec,i} = \underbrace{\tilde{E}_{q_{ar}}[c \cdot \tilde{\theta}_c + (\eta_i + \epsilon) \cdot 1_{\{\text{incumbent}\}}]}_{\text{utility from politics}} - \underbrace{E\{C[\mu(AR|p, s, q_{ar})]\}}_{\text{utility from private decisions}}$$

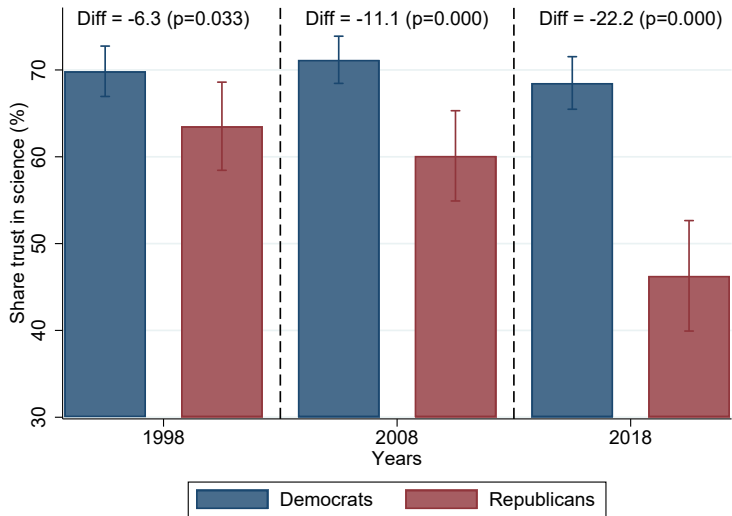
- $\tilde{\theta}_c$ is type of elected politician
- ϵ and η_i are common and individual preference shocks
- $\tilde{E}_{q_{ar}}(\cdot)$ is subjective expectation using new prior q_{ar}
- $E(\cdot)$ is the objective expectation
- $C[\mu(AR|p, s, q_{ar})]$ cost of misspecified beliefs about the reality

Proposition

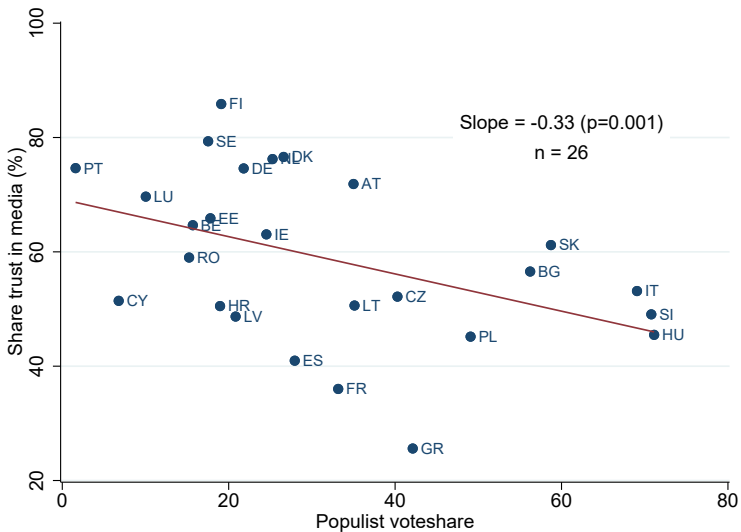
For $\alpha < 0.5$ and π large, then

- ① *Our original equilibrium is an equilibrium of the new game,*
- ② *q_{ar}^* is increasing in the prior probability of a good incumbent q_C .*

Republicans' trust in science declined



Populism and distrust in the intellectual elite



Types and probabilities

Type	Values (probabilities)	Interpretation
A. Politician Common (θ_c)	1 (q_c), 0 ($1 - q_c$)	1=Good
B. Elite Signal ($\hat{\theta}_c$)	θ_c (π), $1 - \theta_c$ ($1 - \pi$)	1=Probably good
C. Politician and Elite Reality (θ_r)	R (q_r), AR (q_{ar})	AR=Altern. reality
D. Receptive voter Mind (θ_m)	N (if $p = 0$), P (if $p = 1$)	P=Persuaded

$$\begin{aligned}\hat{q}_c &= \lim_{\pi \rightarrow 1} \mu_{rec,i}(\theta_c = 1 | p = 1, s = 0, \theta_m = P) \\ &= \frac{q_{ar} q_c}{q_{ar} q_c + (1 - q_c)} > 0.\end{aligned}$$

- Voter's posterior after propaganda:
 - If elite criticizes, assigns $\hat{q}_c > 0$ probability to good politician
 - If elite praises, assigns zero probability b/c in AR elite never praises
- Inverted effect of elite in the presence of propaganda

Equilibrium concept

- PBE modified to account for manipulated prior
 - Persuaded voter's posterior computed from his (incorrect) prior.
 - Persuaded voter makes Bayesian inference from propaganda, elite report
 - But only after experiencing change in prior.
- Restrict attention to "PPO" equilibria:
 - Politician-pure: all politician types use pure strategies.
 - Politician-optimal: best for R politician.

Definitions

Definition

A strategy profile has the *no propaganda form* if no politician type sends propaganda and all elite types report truthfully.

Definition

A strategy profile has the *simple propaganda form* if

① In the reality (R):

- The elite reports the common type truthfully,
- The politician sends propaganda if she can and she is bad.

② In the alternative reality (AR):

- The elite always reports that the politician is bad,
- The politician sends propaganda if she can.

Definition

A strategy profile has *complex propaganda form* if AR elite randomizes when politician is pro-voter and the signal is good, while otherwise profile has simple propaganda form.

Assumption

When elite is fully informative ($\pi = 1$), benefit to the bad pro-voter politician from partially hiding common type exceeds cost of propaganda:

$$\alpha \hat{q}_c > f.$$

Inverted effect: impact of scandals on donations

- We ask if scandals benefit Republican reps among Trump supporters
 - Federal scandals from Wikipedia,
 - Campaign contributions among Trump and other Rep donors.

Inverted effect: Donation levels

	Trump donors Share	Trump donors Amount (1000 dollars)	Other donors
Scandal effect	0.075*** (0.009)	20.33** (9.88)	-9.80 (16.59)
Rep and quarter FE	yes	yes	yes
Control mean	0.065	16.12	119.0
Observations	3,397	4,387	4,387

▶ Placebo

Implications III: Amplification

- Even though signals come from R, expected posterior relative to (post propaganda) prior moves towards the AR.
 - Bayesian update from propaganda and criticism strengthens AR.
 - Propaganda and criticism happens more often in AR than in R.
- Consistent with the structure of successful narratives
 - Events are framed inevitable in the AR
 - Narratives are strategically supplied to match realization of signals, e.g. great replacement theory during 2015 migrant crisis