# Reciprocity and cooperation in strategic contexts



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# Valorization Addendum

To a large extent, public policy choices strongly rely on traditional economic assumptions of behavior, such as perfect rationality and narrow self-interest. For example, reforms aiming at increasing competition (as in the railway, airline, electricity and gas industries) are often based on the conventional wisdom that competition increases (consumer) welfare. This argument assumes that contracts are complete, and that individuals' preferences are exogenous to, and therefore unaffected by, the institutional environment in which individuals make their decisions. Yet, empirical studies have yielded mixed results on the impact of pro-competition reforms on economic performance, and recent experiments have reported on the deteriorating effects of competition on social orientation and subjective well-being. This indicates that preferences and behavior are, at least in part, shaped by the institutional arrangements in place, and casts doubts on the solely positive effects of more competition. Given the importance of reciprocity as a driver of incomplete-contracts labor market outcomes, shown both in the lab and (to some extent) in the field, potential consequences of increased competition on workers' (other-regarding) preferences should not be ignored when designing competition policy reforms.

Chapters 3 and 4 provide controlled evidence on whether more competition leads to higher welfare, while acknowledging the interaction effects between product market, labor market and individuals' (reciprocal) preferences. They are intended to be an informative first step in the assessment of the effects of output market competition for incomplete labor markets. We brought the laboratory environment closer to real life contexts by abandoning the unnatural features of complete contracts, common in the industrial organization literature, and of monopolistic product markets, common in the gift-exchange literature. However, there are other rather relevant aspects we left out. For instance, in our experiments, we limit each employer to hire at most one worker. Clearly, most labor relationships involve more workers per employer. It remains to be seen whether our findings can be generalized to this more realistic context, where also horizontal fairness considerations might play a role. Would reciprocity survive if competition leads to an unequal increase or decrease in wages across workers? Or if some workers are laid off? In this sense, our studies pave the way for more research on the interaction of labor market gift-exchange and output market competition. Adding complexity in a systematic way will allow for a clearer identification of patterns of behavior, which in turn will permit to accurately inform public policy and help designing effective reforms.

Human cooperation has been praised as beneficial in numerous settings. For instance, cooperation in teams boosts team performance; international cooperation helps curb environmental degradation, or further scientific research. In many cases, cooperation requires some prior (coordination on) investments. Working efficiently on an interdisciplinary project, for instance, might require researchers to get familiar with each others' methods or literature. Long-term employment relationships are often facilitated by investments, such as retirement programs. Chapter 5 captures this aspect, and shows that those individuals who invest, and manage to coordinate on relatively high investments, are those who cooperate more. It also shows, however, that most individuals do not invest or choose low investments. This suggests that investments can be an important tool to enforce cooperation, but one cannot solely rely on voluntary investments.

This result has important policy implications. For instance, discussions on how to reduce greenhouse gas emissions have recently moved their focus from emission limits to investments in green technologies. Setting investment levels is argued to be more effective at inducing compliance to environmental agreements, since investments reduce the incentive to deviate and make cooperation credible. Our results provide support for the introduction of this kind of policies. The "2020 Climate and Energy package" adopted by the European Union seems to go in this direction: the agreement requires countries to set emission targets, and, at the same time, to develop renewable energy sources. Our results might be also informative to competition policy. While mergers and acquisitions are thoroughly scrutinized, governments usually encourage firms cooperative investments, especially in R&D, because of the potential benefits resulting, for instance, from spillover effects or cost reduction. However, our results suggest that investments might facilitate collusion in the product market. Therefore, authorities should evaluate firms' co-investments with attention, and investigate the possibility of price collusion in presence of relatively high investments.