Do prisons provide a microcosm of society?
And if so, what economic lessons can we learn?

In this two-part feature, **VICKY PRYCE** and **DAVID SKARBEK** examine the social and economic consequences of crime and punishment

What **ECONOMICS** can **TEACH US** about **PRISONS**

Economics teaches us that prisons do not work. Crime costs the UK economy hundreds of millions of pounds every year and prisons have a minimal impact on crime.

Prisons do not act as a deterrent to crime: people who commit crimes either act from impulse or do not think they will get caught.

Indeed, the vast majority do not get caught. In 2014, police were unable to find a suspect in half the crimes reported to them.

Value for money is particularly poor. UK government departments are routinely brought in front of Parliament's Public Accounts Committee to explain themselves if money is wasted. The Ministry of Justice, with an annual budget of some £7bn, should receive greater scrutiny.

The average cost of keeping someone in prison is £30,000 to £40,000 a year – more than most expensive private boarding schools.

Yet re-offending rates are nearly 60 per cent for those in jail for less than 12 months, and the cost to the economy from re-offending alone is estimated at some £9.5bn to £13bn a year.

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Economics gives us the tools to evaluate policies to test correlations and prove causality. But we ignore the fact that most known forms of crime have been falling consistently. This is true both for crimes reported to the police and those that are outlined in the annual crime surveys.

Why is this? It is not because we have doubled the prison population in the last 20 years.

The decline is due to other factors. Getting richer helps: there is more to lose if caught. So is getting older as a nation: peak crime age is around 24. Better security technology also contributes: automated cash tills make it more difficult to commit retail crime and increased use of sophisticated locks and alarms acts as a deterrent. And so on...

In truth, people in prison are there in greater numbers because there are more offences now classified as meriting a custodial sentence and tighter sentencing policy has resulted in longer sentences.

And yet there is no evidence that raising a sentence from say two to four months or from three to five years makes any difference to the likelihood that someone will commit the relevant crime.

What the evidence does suggest is that the only thing that might affect the willingness to commit a crime is the absolute certainty of being caught. This implies much more money spent on detection. This will not be easy as resources are being cut back aggressively.

Alternative solutions, such as community sentencing are less costly and have a much lower re-offending rate.

Even more important is understanding what does reduce crime. Offenders tend, on average, to be under-educated and much more likely to be unemployed than the rest of the population.

Women prisoners are known to have already been vulnerable before committing crimes with 50 per cent of them victims of domestic abuse and one in three victims of sexual abuse. Many are drug and alcohol dependent.

Furthermore, whereas only 1 per cent of children are in care in the UK, about a quarter of adult prisoners have been in care at some point in their lives.

And then, on leaving prison, life chances decrease. It is harder to get a house, to obtain credit or insurance, and to get a job. Only 25 per cent of prisoners enter employment on release – and their children who had been separated from them are more likely to offend too at some stage.

Keeping people in the community, tackling mental health issues and better education and employment are key to reducing crime. That is what the economic evidence suggests and where the emphasis of policy should be•

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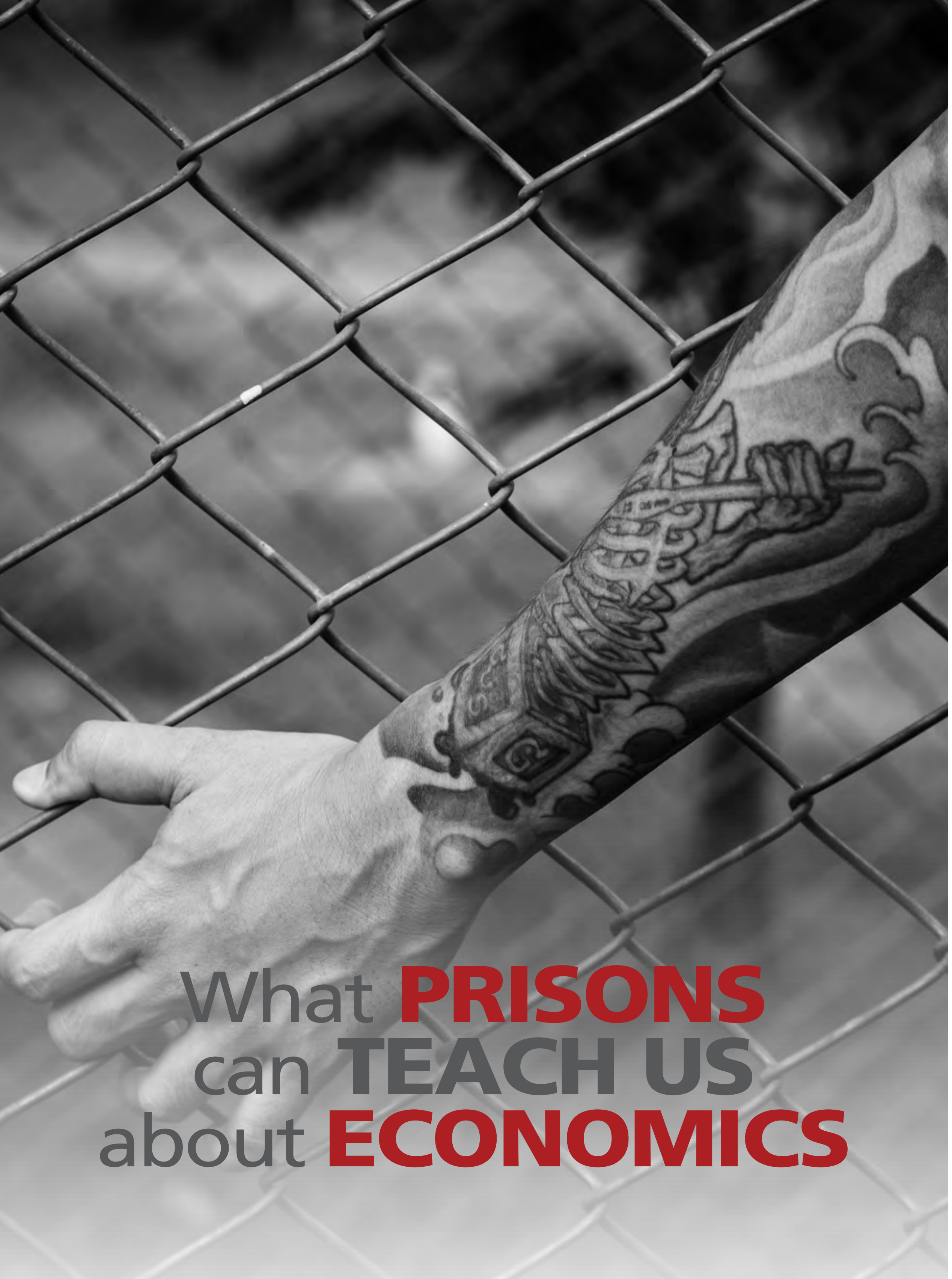

What PRISONS can TEACH US about ECONOMICS

With the exception of Vicky Pryce, few economists will ever step foot in prison. Most will never study crime and punishment in any form. Instead, the vast amount of research on the topic is conducted by sociologists and criminologists. That is a shame, however, because the economist's toolkit is perfectly suited to understanding nearly every aspect of the goings on within a prison.

And life in prison teaches important economic lessons, too. In particular, life behind bars has much to show economists about how people respond to incentives and the general problem of how to sustain social cooperation.

The very nature of prison is rules. Inmates are prohibited in their movements, in what they can own, and with whom they can interact.

There is a long tradition in political economy studying how rules work, what differs between formal and informal rules, where rules come from, and what makes for a good rule.

Indeed, Adam Smith studied such things. A major challenge in this tradition is in determining how to devise rules that lead to good outcomes, even when the people governed by those rules are less than angelic.

Inmates want to feel safe from other inmates; they want their property protected; and they want assurances that dealings with other inmates will be carried out. Sometimes prison guards provide governance, but very often this is not the case.

One problem facing inmates is that they tend to have less self control, less education, come from poorer backgrounds and broken families, and are less trustworthy than the typical person in society.

Despite these limitations, my work on prison life in California shows that they are actually able to sustain a high level of cooperation. Consider two different situations.

Firstly, when prison populations are small, inmates know each other well. Fear of being deemed an outcast amongst a tightly-knit group of convicts encourages people to be nicer to each other.

When inmates want drugs or alcohol, they can only turn to inmate entrepreneurs. Somebody who takes advantage of another inmate in such an exchange will be ostracised or assaulted. Fear of becoming an outlaw among outlaws incentivises good conduct. As a result, the underground economy flourishes.

However, when prison populations get too big, it becomes difficult to keep track of other inmates' social standing. Decentralised rules fail. It is too hard to know who amongst the thieves and killers will be trustworthy and who should be shunned.

As such, ostracism is not a feasible punishment device, and the fear of being an outcast no longer provides a sufficiently strong check on bad behaviour.

In such situations in California a major source of order has emerged from among a group of people that we typically assume are a primary cause of disorder – prison gangs.

Prison gangs wield violence to govern the social and economic affairs of inmate life. They develop written constitutions. They have informal courts to adjudicate disputes between inmates. Their extensive record-keeping allows them to keep track of disruptive inmates far more carefully than in a decentralised system.

When the prison yard is peaceful, gangs make substantial profits selling drugs, so they have an incentive to control chaotic acts of violence. Stability and peace are the key to profits.

There are two lessons here. Even amongst the least trustworthy people in society, prison life shows us that order can emerge in a spontaneous way, and that this process can sometimes achieve very high levels of social and economic cooperation.

Secondly, the larger the grouping, the more important are more formal rules. This is something that we also see, for example, in financial markets. It is amazing how far these observations generalise to other areas of economics•

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