

BEHAVIORAL ECONOMICS

3 module, 2023/2024 academic year

Anton Suvorov & Evgeny Yakovlev

Course information

Course Website: My.Nes

Instructor's Office Hours: by appointment

Class Time: TBA

Room Number: 401

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Course description

The dominant approach in mainstream economics is based on the neoclassical paradigm, dealing with rational economic agents who have an adequate worldview, stable preferences and always make optimal decisions. However, well documented systematic deviations from rationality call into question universality of this method. "Behavioral Economics" is a relatively new field that suggests an alternative to the fully rational economics. A unifying feature of the different research programs associated with it is an attempt to bring psychological realism to economic analysis. Some contributions, mostly the earlier ones, focus on documenting the systematic departures of the actual human behavior from the one predicted by mainstream economic models. Others incorporate more realistic, psychologically grounded assumptions into economic models to investigate their implications. Yet others are interested in explaining seemingly irrational behavior using tools of economics and game theory with some minor departures from conventional assumptions.

This course covers main topics - both theoretical and empirical- of behavioral economics. The primary focus will be on the use of behavioral economics models to explain real life phenomena. It consists from 14 lectures and 6 seminars.

Taking the course would allow the students to broaden their overview in economics, show new venues for research and, optimistically, help to avoid some behavioral traps in life.

Course requirements, grading, and attendance policies

Prerequisites: Micro 1-5, Econometrics 1-2.

Final grade is based on two problem sets, a project (essay based on academic paper with some personal value added, presentation of the essay) and a written final exam. Make up will be held in written form too.

Grading: written essay (20%), presentation of the essay (20%), evaluation of peers' presentations (10%), two problem sets (10% each), final exam (30%). The format of retake is the same as that of the final test.

To pass the course, one should score at least 30 points (out of 100) for the exam and at least 40 (out of 100) points for the essay and 40 (out of 100) points for the presentation.

Essay is to be based on a paper chosen by the student from a suggested list of papers (that will be distributed, as well as detailed guidelines). Essay is to be written by a team of 2-3 students. The essay should briefly communicate the main ideas and results (with intuition) of the paper it is based on, report a constructive critique of the paper and, eventually, contain a brief original extension done by the student(s). Normally the essay should be 5-15 pages long.

Presentation is to be prepared in the same teams.

Each student will be required to take part in evaluating two peers' presentations, which includes asking the presenters at least one question and submitting a very short summary of key take-aways from the presentation along with the list of questions. At least one of the evaluated presentations should take place in the date different from when one's own presentation is delivered.

Course contents

The course will cover several key topics in behavioral economics, such as reference dependent utilities, different types of reference points, time inconsistency, projection bias, incorrect beliefs etc.

Part 1. Evgeny Yakovlev

Lectures 1-2 . Short Introduction. Time inconsistency

Introduction to mispredicting preferences
Misprediction of future utility: principles and evidence
Misprediction of future utility: modeling and applications

Lectures 3-4: Time inconsistency

Principles of present-biased preferences and procrastination
Introduction to biases in judgment and quasi-Bayesian models
Empirical papers on present-biased preferences

Lecture 5-6. Social Preferences

Introduction to social inference and non-inference
Reciprocal preferences, self-image, social image

Lecture 7. Focusing and bracketing effects

Focusing and bracketing effects
Context effects and choice-set-dependent distortions

Part 2. Anton Suvorov

Lectures 8-9. Reference dependent preferences, endowment effect

Introduction to reference dependence and prospect theory

Endowment effect

Reference dependence under rational expectations; personal equilibrium

Lectures 10-11. Belief-based preferences, biased worldviews

Cognitive dissonance and its economic consequences

Anticipatory utility and ego utility, overconfidence

Overconfidence and self-control

Lecture 12. Image concerns

Image concerns and prosocial attitudes

Effectiveness of incentives in the presence of image concerns

Lecture 13-14. Intrinsic motivation. Incentives in the presence of intrinsic motivation

Image concerns and prosocial attitudes

Sample tasks for course evaluation

TASK 1

Братья Петя, Ваня и Андрей ходят в кино по субботам. У них есть деньги только на 4 фильма из пяти которые показывают в этом месяце (так уж получилось что в этом месяце пять суббот). У них одинаковые полезности от фильмов которые представлены в таблице. Все имеют полезности $U_t = u_t + \beta \sum_{i=1}^4 (0.9999)^i u_{t+i}$.

Петя time consistent, Ваня sophisticated time inconsistent ($\beta = \beta^* = 1/2$) и Андрей naive time inconsistent ($\beta = 1/2, \beta^* = 1$).

В решении можете заменять $\delta = 0.9999$ на $\delta = 1$ когда это не принципиально.

Полезности от походов в кино следующие

1я суббота 3

2я суббота 3

3я суббота 5

4я суббота 8

5я суббота 13

a) В какой день Петя не пойдет в кино?

b) В какой день Ваня не пойдет в кино?

c) В какой день Андрей не пойдет в кино?

TASK 2

Оля идет покупать на рынок туфли. Она ожидает что на рынке возможны две цены ($p_l=4$, $p_h=10$), вероятность $\Pr(p=p_h)=0.5$. Олиная полезность $u(c_1, c_2; r_1, r_2) = v c_1 + n(v(c_1 - r_1)) - c_2 + n(r_2 - c_2)$. Здесь c_1 туфли (1 если купила, 0 если нет), c_2 деньги. Gain-loss полезность $n(x) = x$ for $x > 0$ and $n(x) = \lambda x$ for $x < 0$. Ценность туфель v равна 12.

Reference Points- ее ожидания относительно количества денег которые она потратит и туфель которые она купит.

а) Пусть loss aversion $\lambda = 1$. Как себя будет вести Оля когда придет на рынок?

Далее пусть $\lambda = 2$.

б) Опишите самоподдерживающиеся (равновесные) стратегии Оли.

Course materials

Lecture Slides

Lecture notes (when available)

Selected papers

Kahneman and Tversky, eds., Choices, Values, and Frames, 2000

Rabin, Matthew, "Psychology and Economics" JEL 1998

Camerer, Loewenstein, and Rabin, eds. 2003, "Advances in Behavioral Economics" "

Stefano DellaVigna: "Psychology and Economics: Evidence from the Field", JEL 2009

Plus

Rabin, Matthew. (2013): "An Approach to Incorporating Psychology into Economics." *American Economic Review Papers and Proceedings*, 103(3): 617-622.

Rabin, Matthew. (2013): "Incorporating Limited Rationality into Economics," *Journal of Economic Literature*, 51(2): 528-543

Chetty, Raj (2015), "Behavioral Economics and Public Policy: A Pragmatic Perspective," Richard T. Ely Lecture, *American Economic Review: Papers & Proceedings 2015*, 105(5): 1-33.

Koszegi, B. (2006): "Emotional Agency," *Quarterly Journal of Economics*, 121(1): 121-155.

Koszegi, B. and M. Rabin. (2006): "A Model of Reference-Dependent Preferences," *Quarterly Journal of Economics*, 121(4), 1133-1166.

Koszegi, B. and M. Rabin. (2007): "Reference-Dependent Risk Preferences," *American Economic Review*, 97(4), 1047-1073.

Charness, G. and Rabin, M. (2002): "Understanding Social Preferences with Simple Tests," *Quarterly Journal of Economics*, 117 (3): 817-869.

Dana, J., R. Weber, and J. Kuang. (2007): "Exploiting moral wriggle room: experiments demonstrating an illusory preference for fairness." *Economic Theory*, 33, 67-80.

Gul, F. and W. Pesendorfer (2001): "Temptation and Self-Control," *Econometrica*

Rabin, Matthew and Georg Weizsäcker. (2009): "Narrow Bracketing and Dominated Choices," *American Economic Review*, 99 (4): 1508-1543.

Frederick, S., Loewenstein, G. and O'Donoghue, T. (2002), "Time discounting and time preference: A critical review," *Journal of Economic Literature*, 40 (2): 351-401.

O'Donoghue, Ted and M. Rabin. (1999): "Doing it now or later." *American Economic Review*, 89(1), 103-124.

O'Donoghue, T. and M. Rabin. (2001): "Choice and Procrastination," *Quarterly Journal of Economics*, 116(1), 121-160.

Academic integrity policy

Cheating, plagiarism, and any other violations of academic ethics at NES are not tolerated.