

**Universidad de Los Andes**  
**Facultad de Economía**  
**Escuela Internacional de Verano 2005**  
**Curso: Behavioral economics: a review of evidence, methods,**  
**and policy implications**

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**Fecha:** 13 de junio al 1° de julio de 2005

**Área de énfasis:** Economía Social, Políticas Públicas y Medio Ambiente

Nota: La fecha límite para retirarse del curso será el viernes 1° de julio. Si el examen final se programa para ese día, el retiro deberá hacerse a más tardar el 30 de junio.

### **Introduction**

The rapidly developing field of behavioral economics offers economic analysts substantial potential to provide better explanations of economic choices and to make better predictions -- to (in Thaler's terms) do economics with a higher R-squared. In this course, we will discuss how behavioral economics is done, review findings in several illustrative and important areas, examine a number of economic anomalies in which observed behavioral is at variance with predictions of standard theory, and discuss the implications for economics, for policy, and for applied analyses.

### **Objectives**

The course is intended to provide an introduction and review of methods, findings and implications of work in the area of behavioural economics (or, economic psychology). Further, participants will gain a basic understanding of the purpose and experience with the logistics of behavioral economic experiments through classroom demonstrations, participation in experiments, and by carrying out extensions of experiments reported in published articles to be reviewed in the course.

### **Contents**

The range of topics discussed will cover behavioral economic research findings and their application to real policy issues, though other topics will be included depending on availability of time and on the interests of participants. Most of the topics will be the focus of lectures/discussions, some of these and others will be discussed in the context of the reports made to the group by individual class participants. The emphasis in the discussion of each topic will be on the methods used in the studies and the implications of the findings, as well as on the results themselves.

### **Credit and Evaluation**

Course evaluations will be based on:

- 1) Presence and active participation;
- 2) Completion of the assignments and results of a short exam.
- 3) Conducting and reporting on the design and results of an experiment.

### **Teaching methods**

Course participants are assumed to have familiarity with basic economics, but no particular background in the area is required. The course material will be presented in lecture/discussions, classroom experiments, individual presentations and discussions of assigned material, and a small empirical research study including a brief report.

### **Program**

Topics to be discussed in the course will include the following:

*Overview of behavioural economics* – history, methods, relationship to other fields of economics, growing prominence.

*Heuristics and biases* – assumptions and behavioural evidence, mistake vs. real preferences.

*The endowment, or reference, effect* – evidence disparity between valuations of gains and losses: methods, findings.

*Implications of endowment effect* – individual choices (e.g. preference axioms, gains from trade, conflict resolution) policy implications.

*The choice of appropriate measure* – different measures and different values, criteria and why it matters.

*Time preferences* – standard assumption of invariant rates and evidence of variability.

*Mental accounting* – frame for evaluation, examples and consequences.

*Context dependence of preferences* – evidence at variance with stability of preferences assumptions, and observed patterns to context dependencies.

*Research in behavioural economics* – getting started, interesting questions.

*Risk perceptions and preferences* – standard views and evidence, determinants of seriousness of risks.

*Behavioural finance* – evidence of behaviour of individual financial dealings and financial market outcomes.

*Other regarding choices* – fairness, ultimatum, dictator, and trust games.

*Money illusion* – nominal a common response.

*Well-being* – so-called happiness studies, comparisons, determinants of responses of levels of well-being.

*Individuals and firms and organizations* – most conclusions based on individual choice.

*Stated preference techniques* – use (environmental, transportation, etc.), history, shortcomings.

*Schedules of sanctions* – relative weights from community preferences, environmental and legal examples.

*Incentives and under employment of behavioural findings* – still little use, absence in texts.

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### **Literature**

Several advance readings will be expected to have been read before or at the beginning of the course. These will include:

Rabin, M. (1998) Psychology and Economics, *Journal of Economic Literature* 36: 11-46.

McFadden, D. (1999) Rationality for Economists, *Journal of Risk and Uncertainty* 19: 73-105.

Thaler, R. (2000) From Homo Economicus to Homo Sapiens, *Journal of Economic Perspectives* 14: 133-141.

Additional readings will be assigned from:

Kahneman, D. and A. Tversky (2000) Choices, Values and Frames. Cambridge: Cambridge University Press.