FEB13061: Behavioral Economics (B.Sc.)

Víctor González-Jiménez

Spring Semester-2024 (Block 3)

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Course Outline

In this course we will cover several topics in behavioral economics. Lectures will take place on Mondays and Tuesdays (mostly) from 11:00-12:45, from January 8 to February 20. The exam will take place on Thursday 27 February, from 18:30 to 20:30.

Week	Date	Day	Lecture Nr.	Topic	To do
1	08/01/2024	Mon	-	Introduction	
	09/01/2024	Tue	1	Reference Dependence	
2	15/01/2024	Mon	2	Probability Weighting Functions	**Quiz 1: Readings Week 1**
	16/01/2024	Tue	3	Ambiguity	
3	22/01/2024	Mon	4	Beliefs	**Quiz 2: Readings Week 2**
	23/01/2024	Tue	5	Time Inconsistent Preferences	
4	29/01/2024	Mon	6	Game Theory: Review and Anomalities	
	30/01/2024	Tue	-	Tutorial 1	**Hand in Assignment 1**
5	05/02/2024	Mon	7	Social Preferences	**Quiz 3: Readings Week 3 and 4**
	06/02/2024	Tue	8	Behavioral Game Theory	
6	13/02/2024	Tue	9	Application: Poverty Under the Lens of Behavioral Economics	**Quiz 4: Readings Week 5**
7	19/02/2024	Mon	-	Tutorial 2	**Hand in Assignment 2**
	20/02/2024	Tue	10	Question Time (Q&A)	

Course Description

This course will make you familiar with the most relevant concepts and theories in behavioral economics. After following it, you will be able to answer the following questions:

- Why most people buy insurance and also lottery tickets?

- How can individuals exhibit risk aversion for lotteries with small takes while not being absurdly risk averse for lotteries with large stakes?
- Why people exhibit a preference for local stocks over foreign stocks regardless of market trends?
- Why individuals make consumption plans they cannot fulfill?
- Why people donate to charities?
- Why don't we observe more tragedy of the commons?
- Why do people fail to play the Nash Equilibrium of a game?

The questions above describe behaviors that are incompatible with standard economics. For example, according to expected utility theory an individual should buy insurance, i.e. be risk averse, or lottery tickets, i.e. be risk seeking, but not buy these two goods at the same time.

To explain these seemingly anomalous behaviors, you will become acquainted with economic theories that have more realistic psychological underpinnings. Namely, Prospect Theory (Kahneman and Tversky 1992), Max-Min Expected-Utility (Schmeidler, 1986), Quasi-Hyperbolic Discounting (Laibson 1987), Inequality Aversion (Fehr and Schmidt, 1999), Quantal Response Equlibrium (McKelvey and Palfrey, 1995). Throughout the course it will be shown that these theories are better for explaining economic behavior.

Readings

Compulsory readings are indicated with (*), the other readings contain material that is used in the lecture and are included in this list for self-study.

- Week 1:
  - (*) Pope, Devin G., and Maurice E. Schweitzer. "Is Tiger Woods loss averse? Persistent bias in the face of experience, competition, and high stakes." American Economic Review 101, no. 1 (2011): 129-157.
  - Rabin, Matthew Richard H. Thaler (2001) "Anomalies: Risk Aversion," Journal of Economic Perspectives 15, 219–232.
- Week 2:
  - (*) Dimmock, Stephen G., Roy Kouwenberg, Olivia S. Mitchell, & Kim Peijnenburg. "Household portfolio underdiversification and probability weighting: Evidence from the field." The Review of Financial Studies 34, no. 9 (2021): 4524-4563.
  - Wakker, Peter P. (2008), "Uncertainty." In Lawrence Blume & Steven N. Durlauf (Eds.), The New Palgrave: A Dictionary of Economics. The MacMillan Press, London, 6780–6791.
- Week 3:

  - (*) Della Vigna, Stefano, & Ulrike Malmendier. "Paying not to go to the gym." American Economic Review 96, no. 3 (2006): 694-719.
  - Tversky, Amos, & Daniel Kahneman. "Judgment under Uncertainty: Heuristics and Biases: Biases in judgments reveal some heuristics of thinking under uncertainty." Science 185, no. 4157 (1974): 1124-1131.
  - O'Donoghue, Ted, and Matthew Rabin (2000), "The Economics of Immediate Gratification," Journal of Behavioral Decision Making, 13, 233-250.

- Week 4:

  - (*) Goeree, Jacob K.,& Charles A. Holt (2001), "Ten Little Treasures of Game Theory and Ten Intuitive Contradictions," The American Economic Review, 91 (5), 1402-1422.
    - Skip pages 1412-1415, i.e. paragraphs III & IV

- Week 5:

  - (*) Rao, Gautham. (2019). Familiarity does not breed contempt: Generosity, discrimination, and diversity in Delhi schools. American Economic Review, 109(3), 774-809.
    - Skip the heading "Model and Structural Estimation" in pages 798-800.
  - (*)Li, Chen, Uyanga Turmunkh, and Peter P. Wakker. "Trust as a decision under ambiguity." Experimental Economics 22 (2019): 51-75.
  - Fehr, Ernst, and Klaus M. Schmidt (1999), "A Theory of Fairness, Competition, and Cooperation", The Quarterly Journal of Economics 114(3), 817-868.
  - Goeree, Jacob. K., Charles A. Holt & Thomas R. Palfrey (2010). Quantal response equilibria. In Behavioural and experimental economics (pp. 234-242). London: Palgrave Macmillan UK.

- Week 6:

  - (*) Duflo, Esther, Michael Kremer, & Jonathan Robinson. "Nudging farmers to use fertilizer: Theory and experimental evidence from Kenya." American economic review 101, no. 6 (2011): 2350-2390.
  - Dalton, P. S., Ghosal, S., Mani, A. (2016). Poverty and aspirations failure. The Economic Journal, 126(590), 165-188.

Course Structure

Lectures and Tutorials

There will be 9 lectures in total in which the main topics of the course will be presented and some applications will be discussed. There will also be 2 tutorials in which assignments will be discussed and solved. Finally, there will be a "question time (Q&A)" Session.

Assignments

There will be two assignments that are designed to enhance the knowledge of the topics discussed in the lectures. To work in the assignments you should form groups of at most 3 students. Please upload your assignments on Canvas before the respective deadlines. Contact David Gonzalez-Jimenez for information about the assignments.

Quizzes

There will be four in-class quizzes. Each quiz consists of multiple choice or True or False questions and covers knowledge of the required readings of the previous week.

Exam

There will be a written exam. The exam consists of open questions and covers the material discussed in the lectures. You should bring a non-programmable calculator to the exam.

Grading and Grading Policy

The Erasmus University grading scale will be used. I reserve the right to curve the scale dependent on overall class scores at the end of the block. Any curve will only ever make it easier to obtain a certain grade. The grade will count the assessments using the following proportions:

- **50%** of your grade will be determined by a final exam.
- **25%** of your grade will be determined by two assignments (each weighting 12.5% of the total grade).
- **25%** of your grade will be determined by four in-class quizzes.

In each of these criteria students can attain a maximum total of 100 points. This means that to pass the course the student needs to attain at least 55% of all points.

Exercises

Depending on the topic, exam-like exercises will be given during the lectures and discussed in class. Our advice is that you first try to answer the questions before we provide the solutions.

A mock exam will be provided to help you study for the exam. The questions contained in the mock exam are of similar difficulty those that will be included in the exam but are not representative of the topics that might be covered.

Course Policies

During Class

I understand that the electronic recording of notes will be important for class. Please refrain from using computers for anything but activities related to the class. Eating and drinking are allowed in class but please refrain from it affecting the course.

Attendance Policy

Attendance is expected in all lectures and exams. Valid excuses for absence will be accepted before class. In extenuating circumstances, valid excuses with proof will be accepted after class.

Policies on Incomplete Grades and Late Assignments

If an extended deadline is not authorized by the instructor or department, an unfinished incomplete grade will automatically change to a 0.

Late assignments will be accepted for no penalty if a valid excuse is communicated to the instructor before the deadline. After the deadline, assignments will be accepted for a 50% deduction to the score up to 2 days after the deadline. After this any assignments handed in will be given 0.

Academic Integrity and Honesty

Students are required to comply with the university policy on academic integrity found in the Code of Student Conduct.