



INTRO TO THIRD PART

BEHAVIORAL ECONOMICS AND ITS APPLICATIONS

DEFINITION

Conventional vs Behavioral

Conventional economics denies the existence of many problems

- Assumption: rational individuals who engage in maximizing behavior
- Regulatory interventions:
 - Such as targeted taxes and subsidies
 - Only in situations in which an individual's actions imposes costs on others
 - For example, second hand cigarette smoke (externalities)

The potential reach of behavioral economics is much greater.

- Assumption: The prevalence of less than perfectly rational behavior
- Policy interventions:
 - Points to a large category of situations
 - Characterized by costs which people impose on themselves (internalities)
 - Such as the long term health consequences of smoking on smokers.

BEHAVIORAL SOLUTIONS

- BE is a rapidly-emerging discipline with wide-ranging ramifications for any areas such as
 - Consumer policy
 - Finance
 - Undersaving
 - Health policy and practice
 - Health spending and costs and community well-being
 - Overeating
 - Excessive energy consumption, etc.
- Solutions
 - Often combined with new technologies
 - Potential to offer low cost
 - Unobtrusive
 - Conceptually appealing

BEHAVIORAL SOLUTIONS

- BE targets some of the most serious problems of our society
 - Healthcare spending has grown in all countries at a rate that nearly all economists regard as unsustainable
- Government and Behavioral Economics
 - Introduction of the ideas from behavioral economics into policies.
 - In the US, behavioral economists have taken key positions in the Obama administration.
 - In the UK the government has established the Behavioral Insights Team (or “nudge unit”) to advise cabinet ministries
- It will have significant impacts on many problems.

NEW CONCEPTS

“Libertarian paternalism” and “Regulation for conservatives”

- These concepts were deliberately crafted to appeal to groups traditionally hostile toward government intervention.
- They propose “light” paternalistic policies that were intended to nudge decision makers in self beneficial directions using minimally invasive interventions.

REWARD OF PENALTY

One of the most basic questions in designing incentives is whether it is better to use rewards or penalties.

Although many programme designers and social scientists prefer rewards because they seem friendlier to employees, other considerations tend to favour penalties.

It is generally far more efficient to penalize than to reward.

Most rewards will typically be wasted on people who would have behaved in the desired fashion in the absence of rewards.

Fairness can also favour sticks over carrots.

LEVERAGING THE PROBLEM

Errors (biases) can also be used to help people

- Decision makers tend to put too much weight on costs and benefits that are immediate and too little on those that are delayed—a phenomenon known as present bias.
- Present bias can be used to advantage through programs that offer small, frequent (immediate) payments for beneficial behaviours.
- Programs those incorporate social motivators such as competition and peer support can lead to greater behaviour change than programs that implement incentives in an individualistic fashion.
- Many other examples
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POSSIBLE SOLUTIONS

1. Provide small and frequent incentives close to the completion of a healthy activity to encourage adoption of healthy behaviours, while incorporating frequent feedback through the program
2. The use of a lottery-draw to distribute incentives
3. Create an incentives structure that has attainable thresholds and with tiers of rewards so that a larger number of people are engaged.
4. Encourage high frequency of participation in the healthy behaviour during the period when incentives are provided, to improve the potential that the behaviour will be sustained when the incentives are removed.

POSSIBLE SOLUTIONS

5. Consider the importance of testing different types of messaging, as the same information conveyed in different ways can have extremely different effects.
6. Consider the use of ‘contracts’ and commitment devices to pledge to a certain behaviour or goal.
7. Make the healthier option the default or “path of least resistance” option, making it easier for the individual to choose, adopt and sustain that healthier behaviour rather than the unhealthy option.

POSSIBLE SOLUTIONS

8. Leverage social altruism through programs such as offering people who have excelled in mastering a particular disease the opportunity to provide peer support to others who might benefit from such assistance.
9. Incorporate social recognition aspects into program design.