

School of Economics and Finance

**MMPE520 SPECIAL TOPIC:  
ECONOMICS OF BEHAVIOUR  
AND BEHAVIOURAL ECONOMICS**

Trimester 1, 2015

**COURSE OUTLINE**

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**Names and Contact Details**

Course Coordinator/lecturer:

Professor Morris Altman

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Course Administrator:

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**Trimester Dates**

Teaching Period: Monday 2nd March – Friday 5<sup>th</sup> June

Study Period: Monday 8<sup>th</sup> June – Thursday 11<sup>th</sup> June

Examination Period: Friday 12<sup>th</sup> June – Wednesday 1st July (inclusive)

**Withdrawal from Course**

1. Your fees will be refunded if you withdraw from this course on or by Friday 15<sup>th</sup> March 2015.
2. The standard last date for withdrawal from this course is Friday 15<sup>th</sup> May. After this date, students forced to withdraw by circumstances beyond their control must apply for permission on an 'Application for Associate Dean's Permission to Withdraw Late' including supporting documentation. The application form is available from either of the Faculty's Student Customer Service Desks or [online](#).

**Class Times and Room Numbers**

Monday 08.30-12.20 RWW128

There will be six four hour classes held in weeks 1, 3, 5, 6, 8 and 10. There will be a 2 hour mid-term test in week 6, and a final exam in the exam period.

**Course Delivery**

The class will consist of a research paper & related class presentation (30%), two research reports (10%), mid-term examination (20%), and a final examination (40% of the total grade). All research papers and reports must be typed and available in electronic format.

## **Course Content**

This course details the economics of behaviour and the importance of behavioural assumptions (and assumptions in general) for the analytical predictions of economic theory. This brings us to a discussion of the pioneering work of Milton Friedman on Methodology to an analysis of the utility maximizing framework of George Stigler and Gary Becker as this pertains to an understanding of economic theory and an understanding of the analytics of choice. This provides a lead to the alternative modelling frameworks developed in the works of Herbert Simon, Daniel Kahneman and Amos Tversky, Gerd Gigerenzer, Harvey Leibenstein, George Akerlof, Vernon Smith, Elinor Ostrom, Oliver Williamson, Frederick Hayek, and Douglass North and its implication for economic analysis. Some of this discussion relates to the issue of rationality in the decision making process and its effect on model building and public policy. This relates to the recent literature on nudging, animal spirits, and behavioural finance. One important component of this course relates to the importance of behavioural economics to the theory of the firm. This leads to a focus upon efficiency wage and x-efficiency theory and how this connects to an understanding of firm behaviour, economic predictions, and public policy. Also discussed in this course are issues related to behavioural finance, behavioural macro, culture and development, and the economics of ethics. We will also discuss aspects of experimental economics, which is an important area within the domain of behavioural economics.

*The economics of behaviour has significant implications for public and private economic policy, ethics, and decision making which will be discussed in some detail in this course.*

## **Course Learning Objectives**

By the end of this course the student should be able to

- 1 Demonstrate an understanding of behavioural economics
- 2 Define the main features of experimental economics
- 3 Discuss the implications of behavioural economics for public policy
- 4 Assemble economic research
- 5 Realise the importance of presenting and articulating ones ideas in a public forum

## **Expected Workload**

The MMPE520 programme is a 20-point course and on the basis of Victoria University of Wellington having designated one point = 10 hours work, expected work load would total 200 hours. This would involve attending one 4 hour lecture for six of the 12 teaching weeks, plus readings, completing assignment work with the preparation of research report and class presentation.

## **Prescription**

A discussion of the importance of behavioural and institutional assumptions for the analytical predictions of economic theory and casual analysis, and aspects of experimental economics. The implications of behavioural economics for economic policy and decision-making are also examined.

## **Readings**

### **Readings (required and available purchase at the university bookstore)**

Altman, Morris (2012). *Behavioural Economics for Dummies*. New York: Wiley.

### **Other Readings (available purchase at the university bookstore)**

Altman, Morris (ed.) (2006). *Handbook of Contemporary Behavioural Economics: Foundations and Developments*. Armonk, New York: M.E. Sharpe Publishers.

Becker, Gary S. (1998). *Accounting for Tastes*. Cambridge, Mass: Harvard University Press.

Gigerenzer, Gerd (2007). *Gut Feelings: The Intelligence of the Unconscious*. New York: Viking.

Thaler, Richard H. and Cass Sustein (2008). *Nudge: Improving Decisions about Health, Wealth, and Happiness*. New Haven and London: Yale University Press.

### **On-line Reference**

Good reference on-line dictionary: <http://www.sfb504.uni-mannheim.de/glossary/>

### **Books on 3-day loan in the commerce library:**

Altman, Morris (ed.) (2006). *Handbook of Contemporary Behavioral Economics: Foundations and Developments*. Armonk, New York: M.E. Sharpe Publishers.

Becker, Gary S. (1998). *Accounting for Tastes*. Cambridge, Mass: Harvard University Press.

Diamond, Peter and Hannu Vartiainen, eds. (2007). *Behavioral Economics and Its Applications*. Princeton, NJ: Princeton University Press.

Gigerenzer, Gerd (2007). *Gut Feelings: The Intelligence of the Unconscious*. New York: Viking.

### **Supplementary Readings (useful for research papers)**

Selected readings from below will be required (TBA in class and/or blackboard)

Akerlof, G.A. and J.L. Yellen, eds. (1986). *Efficiency Wage Models of the Labor Market*, Cambridge, England and New York: Cambridge University Press.

Akerlof, George A. 2002. Behavioral Macroeconomics and Macroeconomic Behavior. *American Economic Review* 92: 411-433.

Akerlof, G. A. (1982). "Labor Contracts as Partial Gift Exchange," *Quarterly Journal of Economics* 97: 543-596.

Akerlof, G.A. (2002). "Behavioral Macroeconomics and Macroeconomic Behavior," *American Economic Review*, 92: 411-433.

Akerlof, G.A., W. Dickens and G. Perry (2000) "Near-Rational Wage and Price Setting and the Long-Run Phillips Curve," *Brookings Papers on Economic Activity* (1)-60.

Akerlof, G.A and Rachel E. Kranton (2010). *Identity Economics: How Our Identities Shape Our Work, Wages, and Well-Being*. Princeton, New Jersey: Princeton University.

Akerlof, George A. and Robert J. Shiller (2009). *Animal Spirits: How Human Psychology Drives the Economy, and Why it Matters for Global Capitalism*. Princeton: Princeton University Press.

Alchian, Armen A. (1950). "Uncertainty, Evolution, and Economic Theory," *Journal of Political Economy* 58: 211-

Altman, Morris (2012) "Implications of behavioural economics for financial literacy and public policy," *Journal of Socio-Economics* 41: 677-690.

Altman, Morris (2007). "Behavioral Economics," *International Encyclopedia of the Social Sciences*. New York: Macmillan.

Altman, Morris (2005). Reconciling Altruistic, Moralistic, and Ethical Behavior with the Rational Economic Agent and Competitive Markets. *Journal of Economic Psychology* 26: 732-757

- Altman, Morris (2004). "The Nobel Prize in Behavioral and Experimental Economics: A Contextual and Critical Appraisal of the Contributions of Daniel Kahneman and Vernon Smith," *Review of Political Economy* 16: 3-41.
- Altman, Morris (2001). *Worker Satisfaction and Economic Performance: The Microfoundations of Economic Success and Failure*. Armonk, New York: M.E. Sharpe.
- Altman, Morris (2001). "Behavioural Economics." Jonathan Michie, ed., *Reader's Guide to the Social Sciences*. London: Fitzroy Dearborn Publishers.
- Altman, Morris (1999). "A Theory of Population Growth When Women Really Count," *Kyklos* 52: 27-44.
- Altman, Morris (1998). "High Path to Economic Growth and Development," *Challenge: the Magazine of Economic Affairs* 41: 91-104.
- Blaug, Mark (1998). "Disturbing Currents in Modern Economics," *Challenge: the Magazine of Economic Affairs* 41: 11-34.
- Caldwell, Bruce J. (1980). "A Critique of Friedman's Methodological Instrumentalism," *Southern Economic Journal* 47: 366-374.
- Camerer, Colin, George Loewenstein, and Drazen Prelec (2005). "Neuroeconomics: How Neuroscience Can Inform Economics," *Journal of Economic Literature* 43: 9-64.
- Camerer, Colin F., George Loewenstein, and Matthew Rabin (eds.) (2003). *Advances in Behavioral Economics*. Princeton: Princeton University Press.
- Chaudhuri, Ananish (2009). *Experiments in Economics: Playing Fair With Money*. New York: Routledge.
- Coase, R.H. (1994). "How Should Economists Choose?" in R. H. Coase, *Essays on Economics and Economists*, Chicago and London: University of Chicago Press: 15-33.
- Diamond, Peter and Hannu Vartiainen, eds. (2007). *Behavioral Economics and Its Applications*. Princeton, N.J.: Princeton University Press.
- Eckel, C.C. and P.J. Grossman (1966). "Altruism in Anonymous Dictator Games." *Games and Economic Behavior*, 16: 181-91.
- Farmer, Roger E. A. (2010). *How the Economy Works: Confidence, Crashes and Self-Fulfilling Prophecies*. New York: Oxford University Press.
- Fehr, Ernst and Klaus M. Schmidt (1999). "A Theory Of Fairness, Competition, And Cooperation," *Quarterly Journal of Economics*, 114: 817-868.
- Fehr, Ernst and Urs Fischbacher (2003). "The Nature of Human Altruism," *Nature* 425: 785-791.
- Fehr, Ernst, Herbert Gintis, Samuel Bowles, and Robert Boyd, "Explaining Altruistic Behavior in Human," *Evolution and Human Behavior* 24: 153-172.
- Freidman, Daniel and Shyam Sunder (1994). *Experimental Economics: A Primer for Economists*. New York: Cambridge University Press.
- Friedman, Milton (1953). "The Methodology of Positive Economics." In Milton Friedman, *Essays in Positive Economics*, Chicago: University of Chicago Press: 3-43.
- Gigerenzer, Gerd (2007). *Gut Feelings: The Intelligence of the Unconscious*. New York: Viking.
- Gigerenzer, Gerd, and Reinhard Selten, eds. (2001). *Bounded Rationality: The Adaptive Toolbox*. Cambridge, MA: MIT Press.
- Gigerenzer, Gerd and Peter M. Todd (1999). "Fast and Frugal Heuristics: The Adaptive Toolbox." In: Gerd Gigerenzer, Peter M. Todd, and the ABC Research Group, eds., *Simple Heuristics that Make Us Smart*. New York: Oxford University Press.
- Gintis, Herbert & Samuel Bowles & Robert T. Boyd & Ernst Fehr, eds., (2006). *Moral Sentiments and Material Interests: The Foundations of Cooperation in Economic Life*. Cambridge, Mass.: MIT Press.
- Güth, Werner. 1995. "On Ultimatum Bargaining Experiments — A Personal Review." *Journal of Economic Behavior & Organization* 27: 329-344.
- Kahneman, Daniel and Amos Tversky (1979). "Prospect Theory: An Analysis of Decisions under Risk," *Econometrica* 47: 363-391.
- Leibenstein, H. (1966). "Allocative Efficiency vs. 'X-Efficiency,'" *American Economic Review* 56: 392-415.

- March, James G. (1978). "Bounded Rationality, Ambiguity, and the Engineering of Choice," *Bell Journal of Economics* 9: 587-608.
- McCloskey, D. N. (1992). "The American Question: If You're So Smart Why Ain't You Rich." In: D.N. McCloskey, *If You're So Smart: The Narrative of Economic Expertise*. University of Chicago: Chicago: 111-122.
- Miller, G.J., (1992). *Managerial Dilemmas: The Political Economy of Hierarchy*, New York: Cambridge University Press.
- Musgrave, Alan (1981). "'Unreal Assumptions' in Economic Theory: The F-Twist Untwisted," *Kyklos* 34: 377-387.
- Nagel, Rosemarie (1995). "Unraveling in Guessing Games: An Experimental Study". *American Economic Review* 85 (5): 1313–1326.
- Ostrom, Elinor (1999). "Coping with Tragedies of the Commons," *Annual Review of Political Science* 2: 493–535.
- Ostrom, Elinor (2010). "Beyond Markets and States: Polycentric Governance of Complex Economic Systems," *American Economic Review*, 100: [641-672](#).
- Rabin, Mathew (1998). "Psychology and Economics," *Journal of Economic Literature*, 36: 11-46
- Reder, Melvin W. (1982). "Chicago Economics: Permanence and Change," *Journal of Economic Literature* 20: 1-38.
- Roth, Alvin and J.H. Kagel eds. (1995). *Handbook of Experimental Economics*. Princeton N.J.: Princeton University Press.
- Simon, Herbert (1978). "Rationality as a Process and as a Product of Thought," *American Economic Review* 70, 1-16.
- Smith, Vernon L. (1962). "An Experimental Study of Competitive Market Behavior," *Journal of Political Economy*, 70(2), pp. 111-137.
- Smith, Vernon L. (2003). "Constructivist and Ecological Rationality in Economics," *American Economic Review* 93: 465-508.
- Smith, Vernon L. (2005). Behavioral Economics Research and the Foundations of Economics. *Journal of Socio-Economics* 34: 135–50.
- Stigler, G. J. (1976). "The X-istence of X-Efficiency," *American Economic Review* 66: 213-216.
- Stigler, G.J. (1961) "The Economics of Information," *Journal of Political Economy* 69: 213-225.
- Stiglitz, J.E. (1987). "The Causes and Consequences of the Dependence of Quality on Price," *Journal of Economic Literature* 25: 1-48.
- Thaler, Richard H. and Cass Sustein (2003). "Behavioral Economics, Public Policy, and Paternalism: Libertarian Paternalism," *American Economic Review, Papers and Proceedings* 93: 175-179.
- Thaler, Richard H. (1992). *The Winner's Curse: Paradox's and Anamolies of Economic Life*, New York: Free Press.
- Todd, Peter M., and Gerd Gigerenzer. 2003. Bounding Rationality to the World. *Journal of Economic Psychology* 24: 143–65.
- Tversky, Amos and Kahneman, Daniel (1981). "The Framing of Decisions and the Psychology of Choice," *Science* 211: 453-458.
- Williamson, Oliver E. (1981). "The Modern Corporation: Origins, Evolutions, Attributes," *Journal of Economic Literature* 19: 1537-1568.

### **Materials and Equipment**

Any additional notes will be posted on Blackboard.

### **Assessment Requirements**

Your final grade will be composed of

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|---|-----|
| 1. One 15 page or 4,500 word (maximum) research paper | 30% |
| <b>LAST WEEK OF CLASS</b>                             |     |
| 2. Two research reports (up to 3 pages each)          | 10% |
| Due dates: March 27 (paper #1); April 24 (paper #2)   |     |
| 3. A mid-term exam. April 20.                         | 20% |
| 4. A two hour final exam                              | 40% |

The Assessment Handbook will apply to all VUW courses: see

<http://www.victoria.ac.nz/documents/policy/staff-policy/assessment-handbook.pdf>.

### **Link to general information**

For general information about course-related matters, go to

<http://www.victoria.ac.nz/vbs/studenthelp/general-course-information>

### **Note to Students**

Your assessed work may also be used for quality assurance purposes, such as to assess the level of achievement of learning objectives as required for accreditation and academic audit. The findings may be used to inform changes aimed at improving the quality of VBS programmes. All material used for such processes will be treated as confidential, and the outcome will not affect your grade for the course.

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