

University of Wisconsin-La Crosse
Department of Economics
ECO474 Behavioral Economics
Associate Professor Lisa Giddings
Fall 2011

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If, by chance, you cannot come during these specified hours, feel free to call me and set up an appointment. Given advance notice, I can meet you just about anytime, anywhere.

“Broadly stated, the task is to replace the global rationality of economic man with a kind of rational behavior that is compatible with the access to information and the computational capacities that are actually possessed by organisms, including man, in the kinds of environments in which such organisms exist” Herbert Simon (1955).

Course Objectives & Content

I expect that this course will be unlike any course you have taken at UW-L. Behavioral Economics is different than any economics that you’ve probably ever heard about or studied, but it is probably a lot closer to what you experience as a living being on this planet. If you’ve had enough econ courses, you’ve probably gotten a good dose of Neoclassical economics and its description of how people behave: using indifference curves to maximize utility, why we should ignore sunk costs, why we don’t cooperate in a prisoner’s dilemma etc. Much of this theory is based on very specific assumptions about behavior and human biology: most people make choices with the goal of maximizing their utility. But behavioral economics is different: it studies how people actually behave, not how we think people should behave.

Behavioral economics began with a debunking of neoclassical economic theory by psychologists such as Amos Tversky and Daniel Kahneman, and experimental game theorists such as Vernon Smith. However, ideas once considered outside the realm of economics, or descriptive “anomalies” contradicting the neoclassical model, have become accepted into mainstream economics with cross-disciplinary explanations under the new heading of “behavioral economics,” also evidenced by the 2002 Nobel prize in Economics being awarded to Kahneman and Smith. The Nobel Commission noted integrating “insights from psychological research into economic science, ... thereby laying the foundation for a new field of research” by demonstrating “how human decisions may systematically depart from those predicted by standard economic theory.”

Behavioral economists have particularly been concerned with situations in which what people actually do differs from what the rational choice model (or the neoclassical model of economic behavior) predicts what people will do. We know, for example, that people would rather get a lower salary and be the highest earner in their firm than receive a higher salary and be the lowest earner at their firm. Crazy, huh? But by exploring how people really behave and then developing models based on more accurate assumptions about human behavior, behavioral economics hopes to design better institutions and policies.

Many of the insights of behavioral economics originate from evolutionary biology, evolutionary psychology and psychological models of behavior. Because of this we will be reading articles that are cross-disciplinary including a graphic novel of Charles Darwin’s theory of evolution!

Many of the behavioral insights that economists have come to rely on experimental economics. This is a methodology that economists can use to test theories directly rather than using secondary data. Experimental

economists are much more like physical scientists in that they generate hypotheses, run experiments under controlled conditions and gather data that they then use to evaluate their hypotheses.

Course Prerequisite

Economics 110, Principles of Economics, is a necessary prerequisite, it would be great if you have also taken ECO308, but this is not necessary.

Course Materials

The following texts are required. I will add additional readings as the course progresses. Other readings are either available online (at <http://www.uwlax.edu/faculty/giddings>) or will be available on the D2L site.

Books Available At Campus Center

Ariely, Dan. 2010. *The Upside of Irrationality*.

Keller, Michael. 2010. *Charles Darwin's On the Origin of Species: A Graphic Adaptation*.

Books You are Required to Purchase (or find a copy online)

Holt, Charles A. 2007. *Markets, Games and Strategic Behavior: Recipes for Interactive Learning*.

Online at: <http://www.google.com/products/catalog?q=markets+games+and+strategic+behavior&oe=utf-8&rls=org.mozilla:en-US:official&client=firefox-a&um=1&ie=UTF-8&tbm=shop&cid=14853131203502190306&sa=X&ei=fxNRTu-HK8fYgQf6r9nzBg&ved=0CEcQ8wIwBA>

Requirements for the Class

- 1. Class Preparation and Attendance:** This course will consist of lectures, seminars and a science labs. A seminar is a collective endeavor in which all participants learn from each other. This means that much of class time will be spent discussing the readings assigned. The quality of the classroom sessions, then, depends on your preparedness and active participation. This will require you to complete the assigned readings *prior* to class. Because class participation is crucial to this course, it will be considered in your final grade. You will not be able to earn an A in this course without preparing (through reading and writing) carefully and consistently for classroom discussions and then partaking in the class discussions.

To earn an "A" for the day, students must contribute to the conversation by, for example, contributing a good insight during the discussions. Failure to attend class, tardiness, or inattention will result in a D. Good discussions can also occur on D2L.

The course timeline contains each reading and activity that will be covered during each day. Readings marked with [L] will be explicitly covered in the lecture. Readings marked with a [D] are required for students to read and be prepared to discuss in class. I expect that students will: (1) read articles carefully, (2) listen carefully when others speak, (3) ask good questions and (4) disagree constructively and respectfully. Each student is required to present one paper from the reading list. Suitable papers are denoted by "S". Papers will be allocated on a first-come-first-serve basis and students may work in groups of two. Sign up in my office during the first two weeks of the course.

- 2. Computer Lab Days:** We will spend several class periods in the computer lab running in-class experiments using Veconlab created by Charles Holt. This is a Website for experimental economics that is free-of-charge to students and faculty members. To participate, students log on at: <http://veconlab.econ.virginia.edu/login.htm>
All students must contribute \$10 to a pool used to reward performance in the experiments. I, too, will be contributing \$10. This pool will be used as an incentive schema to get students to take the experiments seriously, thereby maximizing the educational impact.
- 3. Term Paper and Term Paper Presentation:** All students are required to complete an experiment-based research project, summarize their findings in a term paper, and present the paper during the final weeks of the course. Students may work in groups of two. Students in this course will be asked to generate their own data

from laboratory or field experiments. One option is to investigate some aspect of economic behavior by varying the environment in which subjects operate (for example, sellers may compete in one environment and then be allowed to collude in another). Alternatively, you might examine differences in behavior across populations (for example, are women more altruistic than men?). In all cases, students must a) formulate an interesting and testable hypothesis; b) develop an experimental protocol; c) recruit subjects; d) conduct the experiment; e) analyze the results; f) relate the results to the existing literature; and g) submit a final paper/make a presentation. This paper is due **during finals week**.

Paper Grading Criteria

a) statement of question with three citations (due week 5)	5%	
b) two-page proposal (due week 7)		10%
c) novelty and importance of the question	15%	
d) writing		20%
e) literature survey		20%
f) experimental design	10%	
g) quality of data gathered		5%
h) analysis of results		10%
i) presentation	5%	

Potential research Areas:

1. Endowment Effects (decisions)
2. Risk Aversion (decisions)
3. Overconfidence (decisions)
4. Self-control (decisions in time)
5. Ultimatum, Trust and Public Goods Games (regard for others)
6. Learning and Reputation (repeated games)
7. Fairness and Reciprocity (labor market)
8. Incentive Schemes (labor markets)
9. Bubbles and Herding (asset markets)
10. The Winner's Curse (auctions)

4. Review Questions/Lab Questions

For each week's set of readings and/or each lab I will provide questions for review and discussion. You can turn these in to the dropbox on the D2L Website on the day after the topic has been discussed. These will not be graded per se, but will be attached to your participation grade.

5. Exams

There will be one in-class exam during the semester, **October 27th** and a final exam. Each exam will be cumulative.

Grading Policy

Students will be graded on the basis of the two exams (a midterm and a final), your term paper and the presentation of that term paper, and class participation (both in class and on D2L). The breakdown of grading is as follows:

- Examination 1: 25%
- Final Examination : 30%
- Term Paper: 25%
- Term Paper Presentation: 5%
- Class Participation, review and lab questions & Seminar Presentation: 15%

Late Work, Absentee, and Honor Policies

If a student is unable to take the midterm exam at the regularly scheduled time, arrangements may be made by the student for a make-up exam provided that s/he contacts the instructor one week prior to the scheduled exam. Make-up exams are mutually inconvenient and, as a result, tend to be more difficult. Please check the class itinerary now for any conflicting religious holidays. The only other excuse for a missed exam is a verifiable medical emergency. In the event of an excused missed exam due to unforeseen medical emergency, the average of the other exam grades will serve as the grade of the missed exam. Students should only take make-up exams in the case of a serious conflict. The final exam may be taken only at the scheduled time.

Late problem sets will not be accepted. Please do not ask for "extra credit" assignments to raise your grade or make up for a low grade. Concentrate instead on doing your best on the existing assignments.

Regarding class attendance, I consider you to be, and will treat you as an adult. In the spirit of the economic discipline, I recognize that time is scarce and I trust that you will make rational decisions concerning the way in which you spend your time. Please be aware, however, that all of our choices embody trade-offs that can be very costly. The topics of this course will be presented sequentially. Therefore, it is in your best interest to attend class and keep up with the course work. Class participation counts for your grade. I expect you to attend, be awake, ask questions, and generally participate in class discussions. Exams will be drawn from class material, and not all class material can be found in the textbook. I will at times communicate with the class via email. Please check your email every day.

Academic Honesty

According to the UW-L Undergraduate catalogue, "[w]e, the students of UW-La Crosse, believe that academic honesty and integrity are fundamental to the mission of higher education. We, as students, are responsible for the honest completion and representation of our work and respect for others' academic endeavors. We, as students and responsible citizens of the city of La Crosse, will aim to uphold the integrity of the University throughout the La Crosse community. It is our individual responsibility as students to uphold these ethical standards and to respect the character of the individuals and the university." If you have any doubts or questions about what constitutes academic dishonesty, see me and I will clarify the university's policies regarding academic honesty for you.

The University's position:

Academic misconduct is a violation of the UW-L student honor code <http://www.uwlax.edu/records/UCGat/Regulations/Disciplinary.htm>. Academic misconduct is unacceptable. All work handed in for this class must be the students' own individual work. Plagiarism or cheating in any form may result in failure of the assignment or exam, failure of the course, and may include harsher sanctions. Refer to the Eagle Eye at http://www.uwlax.edu/StudentLife/academic_misconduct.htm#14.03 for a detailed definition of academic misconduct. For helpful information on how to avoid plagiarism, go to <http://www.uwlax.edu/murphylibrary/research/plagiarism.html>. You may also visit the Office of Student Life if you have questions about plagiarism or cheating incidents. We encourage you to discuss any concerns regarding plagiarism or cheating with any of us directly and well before any assignments are handed in. Failure to understand what constitutes plagiarism or cheating is not a valid excuse for engaging in academic misconduct.

Students with Disabilities

Any student with a documented disability (e.g., physical, learning, psychiatric, vision, or hearing, etc.) who needs to arrange reasonable accommodations must contact the instructor and the Disability Resource Services office (165 Murphy Library) at the beginning of the semester. Students who are currently using the Disability Resource Services will have a copy of a contract that verifies they are qualified students with disabilities who have documentation on file in the Disability Resource Service office.

A Word (or two) of Advice

Economics, while intuitive, is not simple. You will be learning a new language, and a new application of some old math that you probably already know. You should expect this and study accordingly. The class will be immeasurably easier for you if you stay ahead of the game. If, for example, you read the chapter before class, then skim over it after class and keep up with the problem sets, you will a) get a better grade and b) spend less time studying for the final. If, instead, you postpone reading the chapters and fail to participate in the problem set preparations, you will a) spend many hours frantically studying for the final exam and b) most likely not do well in

the class anyway. Again, how you allocate your scarce resource of time is your choice, but be aware of the costs involved.
