Economics 310—Introduction to Behavioral Economics
Winter 2019

Lectures: Tuesday and Thursday 4:05-5:25pm. Burnside 1B36.

Instructor: Jian Li. Office: 426 Leacock. Telephone: 514-398-3030 extension 00830. Email: jian.li7@mcgill.ca (please include “Econ 310” in subject for filtering.)

Office hours: Tuesday and Thursday 1:45-2:30 pm.

Teaching Assistant: Audrey Azerot. Email: audrey.azerot@mail.mcgill.ca. The TA will hold regular office hours and give conferences before problem set due dates and exams. The exact time and location will be announced later.

Goals of the Course

This course introduces you to a relatively new field—behavioral economics. The goal is to learn how to think about economic decisionmaking in a psychologically richer way while maintaining the rigor of economic analysis. You will learn (i) what are the basic psychological phenomena that are most important for economics; (ii) how to identify these phenomena from simple decisions and capture them in economic terms; and (iii) how they should change our understanding of basic economic questions.

Course Materials

There is no textbook for this course. The required reading for the course is a set of relatively detailed lecture slides, together with a few academic papers in the required readings. I will post them after each lecture on MyCourses (www.mcgill.ca/lms). You should also take notes in class in order to supplement the lecture slides. The lecture slides are drawn from a rich source of research papers in economics, psychology, and sociology. These papers written for an academic audience and harder than most textbooks you have encountered. You are strongly encouraged to selectively read some of the papers in additional readings to explore things more deeply. In addition, if you need more perspectives on the material, you can consult the background readings suggested below.

1I thank Botond Kószegi for generously sharing a lot of materials.
Background Readings

I encourage all of you to read Thaler’s *The Winner’s Curse: Paradoxes and Anomalies of Economic Life*. It is a collection of great and easy-to-read articles. Gilboa’s *Making Better Decisions: Decision Theory in Practice* offers a more rigorous (and somewhat philosophical) discussion on the topics. Ariely’s *Predictably Irrational* offers more of a psychologist’s perspective on the topics. Thaler and Sunstein’s *Nudge: Improving Decisions about Health, Wealth, and Happiness* draws out a view on some of the policy implications. Other background readings you might want to look at:

- Kahneman, *Thinking, Fast and Slow*
- Camerer, *Behavioral Game Theory: Experiments in Strategic Interaction*
- Loewenstein and Elster, *Choice over Time*
- Rabin, *Psychology and Economics*
- Thaler, *Advances in Behavioral Finance*

Requirements

Prerequisite: Econ 208 and Econ 209. Some knowledge of probability and statistics. (For example, part of the materials will be easier if you know the Bayes’ rule and how to calculate conditional probabilities.) Basic knowledge of game theory is helpful.

Problem Sets: There will be about 4 problem sets during the semester. They will be posted as the course progresses. This includes mathematical problems for which you have to calculate solutions and give interpretations, as well as essay-type questions that ask you to apply the new concepts learned in class to discuss economic “puzzles”. Working hard on the problem sets is the best way to learn the materials and prepare for exams. You are welcome (even encouraged) to work in groups, but you must write up the solutions on your own, using your own words and understandings. Problem sets will be graded by four cases: fail to submit (0), incomplete (1), complete but with major error (2), complete and no major error (3).

Exams: There are one midterm and one *cumulative* final exam. The midterm is in-class and will take place on February 21 (tentative date). If you miss the midterm due to a medical emergency (with doctor’s note), then the weight for the midterm will be transferred to the final exam. No makeup midterm will be given. The final exam will be in April and
it is a three-hour comprehensive exam that covers everything taught in the semester. The exact time and location of the final exam will be announced towards the end of the semester.

You will be evaluated by a combination of (i) problem sets (10%), (ii) midterm (30%), (iii) final exam (60%).

McGill Policy Statements

McGill University values academic integrity. Therefore, all students must understand the meaning and consequences of cheating, plagiarism and other academic offences under the Code of Student Conduct and Disciplinary Procedures (see www.mcgill.ca/students/srr/honest/ for more information).

According to Senate regulations, instructors are not permitted to make special arrangements for final exams. Please consult the calendar, section 4.7.2.1, General University Information and Regulations, at www.mcgill.ca.

In accord with McGill University’s Charter of Students’ Rights, students in this course have the right to submit in English or in French any written work that is to be graded.

Tentative Outline

Below is a tentative outline of topics that will be covered. Actual lectures might be subjected to changes so please check often for updates.

INTRODUCTION

What is behavioural economics.

Overview of major themes in a few examples.

PART I: DECISION UNDER RISK AND UNCERTAINTY

Review of classic expected utility theory.

Kahneman and Tversky’s Prospect Theory

Evidence and features of the prospect theory.

Economic applications of the prospect theory.
Determination of the reference point.

**OTHER non-EU utility theories**


**PART II: Choice Over Time**

Samuelson’s exponential-discounting model.

Self-control problems and hyperbolic discounting.

Anxiety, optimism and other anticipatory emotions.

Misperception of future utility.

Experimental methods.

Behavioral public policy.

**PART III: Heuristics and Biases in Probabilistic Judgment**

Bayesian learning model.

Intuitive decision making.

Representativeness and other heuristics.

Law of small number and other biases.

**PART IV: Behavioral Game Theory**

**Social Preferences**

“Distributional” social preferences.

“Face-saving Concerns”.

“Intention-based” social preferences.

Social preferences and institutional design.

**Behavioral Game Theory**

A brief review of game theory.

Game theory versus behavioral game theory.

Irrational players and equilibrium.

Models of boundedly rational strategic play.

Winner’s curse.

Learning in games.