Syllabus

Features of this course

This course is the continuation of the 219A class in *Psychology and Economics – Theory*, taught by Dmitry Taubinsky. As in 219A, we will keep emphasizing the psychological evidence as the basis for sound economic analysis. We will also insist on the importance of neoclassical theory as a successful benchmark that you are required to know. Finally, several topics of this course are designed to be the empirical counterpart of the theory covered in 219A.

There are two main differences between 219A and 219B. First, this class has largely an empirical orientation, as opposed to the mostly theoretical orientation of 219B. I will present empirical papers drawn from a variety of fields: asset pricing, corporate finance, consumption, development economics, environmental economics, health economics, industrial organization, labor economics, political economy, and public economics. As such, the class is also meant for applied students that do not intend to make Psychology and Economics one of their main fields, but want to apply some of the behavioral ideas to their field of interest.

The second main feature of the course will be its emphasis on dissertation writing. Throughout the course I will do my best to point out what seem to me like good directions for empirical research. In addition, as an incentive to get you started, one of the requirements of the course is a paper on an applied topic using field data.

The 219B course also covers a set of Methodological Topics, including some of the how-to-do list for empirical behavioral research. This year in particular we are going to emphasize the theme of Structural Behavioral Economics, or model-based empirical research in behavioral economics. The methodological topics are integrated with the other research topics.

Rules of the game

As a general rule, you should have taken the 219A course before you take this course. If you have not, but are interested in taking this course, please come and talk to me. The prerequisites of the 219A course, that is, an understanding of the economics of uncertainty and game theory at the level of 201B, apply to this course as well. In addition, it is important that you have had exposure to econometrics and empirical research. You should be familiar with key econometrics topics, like panel data models, discrete choice models, and the basics of maximum likelihood and minimum distance estimation. Although it is not a requirement for this course, I recommend taking at least one labor economics, public economics, or applied econometrics course to anyone contemplating doing empirical research.
Throughout the course, I will assign two to four required readings each week. The required readings are starred in the reading list below. The non-starred readings are optional, but I suggest that you at least read the introduction. So much of a paper is in the introduction (if the introduction is well-written).

There are four requirements for the course: problem sets, a final exam, an empirical problem set, and an empirical paper. The last two requirements are either/or, that is, you can do either the empirical problem set or the paper.

**Problem Sets.** The problem sets will test your knowledge of modeling and of empirical specifications. The problem sets will be on Present-Biased Preferences, Reference Dependence, on Structural Behavioral Economics, and on Behavioral Finance. This year’s problem sets are updated relative to previous years to include some instances of structural estimation.

**Exam.** The in-class exam will cover the material of the whole class and will be modeled on the type of questions that I ask in the problem sets. You will have some previous exams to practice.

**Empirical Paper.** I encourage everyone to try to write an empirical paper on a Psychology and Economics topic. This will help you to get started on your research, which of course is the ultimate purpose of taking a PhD. The paper can be written with up to two other students in the class. A two-page written proposal is due after Spring Break. The final 10-15 page paper is due on May 13.

The *ideal* paper contains a novel idea, the empirical strategy, and preliminary empirical results. Realistically, you can do significantly less as long as you show significant effort. Two things are key: (i) that you do at least some preliminary analysis with data, since one purpose of the requirement is to make sure that you learn to use Stata or another statistical package; (ii) that you use field data, as opposed to experimental data. (This is by no means meant as a negative on doing lab experiments. Laboratory experiments are great. However, this class focuses on field data) Replication of existing studies is perfectly fine, and encouraged. Replication, in fact, is a good way to start original research, and more and more replication data sets are available on the AER, JPE, and now QJE websites. Some of the papers prepared for this class in past years have turned into publishable papers and, in one case, even into a job market paper. I encourage you therefore to think of presenting the paper that comes out of this class in the Psychology and Economics Friday Lunch.

In any case, you are strongly encouraged to attend the Psychology and Economics Friday lunch (meeting on most Fridays 12-1 at Haas) if you are interested in making Psychology and Economics one of your fields. In addition, you should attend the Psychology and Economics Seminar (Tu 2-3.30) as much as you can. Spots to go for lunch with outside speakers are available for sign-up.

**Empirical Problem Set.** The alternative assignment is a one-time, significant empirical problem set that is meant to familiarize you with empirical research in Psychology and Economics. You can work on the assignment in groups of up to three people, but each one should hand in a solution.

The course webpage is an important instrument for this course (you can find the link from my webpage). On the website you will find updated lists of readings, the assignments, and the revised lecture notes in pdf format.
Grading. The final grade will be an average with weight 30% on the problem sets, 40% on the final (in-class) exam, and the remaining 30% on either the paper or empirical problem set.

Meeting. The best way to meet is to send me an email to schedule – in fact, you are supposed to email me so we can talk about your paper project.

Tentative schedule of classes

The schedule will vary somewhat as the class unfolds. The syllabus will be updated periodically on the course webpage.

Part I -- Non-Standard Preferences
January 17 – Lecture 1
  Introduction
  Psychology and Economics: The Methodologies
  Psychology and Economics: The Fields
  Present-Biased Preferences, Part 1
    Status-Quo in Financial Decisions
  Methodological Topic: Reading the Psychology Journals
  Problem Set 1 on Present-Biased Preferences assigned

January 24 – Lecture 2
  Present-Biased Preferences, Part 2
    Present-Bias and Status Quo
    Consumption Choices: Investment Goods
      Homework Completion
      Exercise
  Problem Set 1 on Present-Biased Preferences due

January 31 – Lecture 3
  Present-Biased Preferences, Part 3
    Consumption Choices: Investment Goods
      Job Search
      Work Effort
      Delay with Deadline
    Consumption Choices: Leisure Goods
      Credit Card Borrowing
      Consumption-Savings
      Drinking
    Methodological Topic: Commitment Field Experiment Designs
  Problem Set 2 on Reference Dependence assigned

February 7 – Lecture 4
  Present-Biased Preferences, Part 4
  Laboratory Evidence
  Methodological Topic: Common Errors in Applying Present-Biased Preferences
  Reference Dependence, Part 1
    Housing Market
    Bunching-Based Evidence:
February 14 – Lecture 5
Reference Dependence, Part 2
Bunching-Based Evidence:
Taxes
Running
Mergers
Job Search
Daily Labor Supply
Employment and Effort
Domestic Violence

Problem Set 2 on Reference Dependence due

February 21 – Lecture 6
Reference Dependence, Part 3
Golf
Job Search
Applications with Full Prospect Theory
Insurance Choices
Equity Premium
Reference Points: Forward vs. Backward
Endowment Effect
Effort

February 28 – Lecture 7
Social Preferences, Part 1
Wave I: Altruism
   Altruism within Workplace
   Shaping Social Preferences
Wave II: Warm Glow and Charitable Giving
Wave III: Inequity Aversion and Reciprocity
   Workplace Effort
Methodological Topic: Running a Field Experiment

March 7 – Lecture 8
Social Preferences, Part 2
Wave III: Inequity Aversion and Reciprocity
   Gift Exchange in the Lab and Field
Wave IV: Social Pressure, Signaling, and Social Norms
   Social Pressure, Various
   Social Pressure and Charitable Giving

Week of March 15 – Meet Stefano to discuss paper topic

Part II -- Non-Standard Beliefs
March 14 – Lecture 9
Social Preferences, Part 3
Wave IV: Social Pressure, Signaling, and Social Norms
   Social Signaling
   Social Norms
Non-Standard Beliefs
Overconfidence
Law of Small Numbers
Projection Bias

Problem Set 3 on Structural Behavioral assigned

Part III -- Non-Standard Decision-Making
March 21 – Lecture 10
Limited Attention
  Introduction/Model
  Shipping Costs
  Taxes
  Left-Digit Inattention
  Financial Market Evidence

Methodological Topic: Portfolio Methodology
Framing
Menu Effects
  Choice Avoidance
  Preference for Familiar

March 28– Spring Break – No Lecture

April 4 – Lecture 11
Menu Effects
  Preference for Salient
  Confusion
Choice of Dominated Options
Mental Accounting
Persuasion
Emotions: Mood
Emotions: Arousal

Two-page proposal due

Part IV – Market Response to Biases
April 11 – Lecture 12
Happiness
Market Reaction to Biases, Part 1
  Behavioral IO
  Behavioral Firms

Methodological Topic: Markets and Non-Standard Behavior
Problem Set 3 on Structural Behavioral due
Problem Set 4 on Behavioral Finance, Assigned

April 18 – Lecture 13
Methodological Topic: Structural Behavioral Economics
Market Reaction to Biases, Part 2
  Behavioral Finance
Behavioral Corporate Finance
Behavioral Political Economy
Behavioral Finance

Problem Set 4 on Behavioral Finance due
Empirical Problem Set Handed Out

April 15 – Lecture 14 and last
Market Reaction to Biases, Part 3
Behavioral Labor
Behavioral Welfare Economics
Additional Topics
Conclusion

In-Class Exam (during RRR period), May 2, 12-3

Sunday May 13 (midnight) – Due date for Paper and Empirical Problem Set
Readings

*designates required readings.

The following paper will cover, in a dense manner, the topics covered in the class:


The following chapter also touches on many of the topics we cover in class:


Comments on this chapter are much appreciated as it is still work in progress, feel free to email me.

The following articles provide partial overviews of the field of Psychology and Economics:

An early classic, emphasizes the psychology and its application to economics

Not comprehensive, but interesting ideas on the field

Classifies most P&E into Bounded Self-Control, Bounded Rationality, and Bounded Self-Interest

For those looking for a background book in social psychology to complement the content of the Psychology and Economics sequence, I highly recommend:

A primer into a number of important social psychology findings, a wonderful classic, just recently was re-printed.

A classic of the cognitive psychology literature.

Part I -- Non-Standard Preferences
Lecture 1
Status-Quo Bias in Financial Decisions


Comparison to Effect of Financial Education


Lecture 2

Status-Quo Bias in Financial Decisions, Explained with Present Bias


Other Default Effects


Present-Biased Preferences: Investment Goods


**Lecture 3**

*Present-Biased Preferences: Investment Goods II*


*Present-Biased Preferences: Leisure Goods*


Schilbach, Frank. 2015. “Alcohol and Self-Control: A Field Experiment in India.” Mimeo, Massachusetts Institute of Technology.

*Methodology: Design of Commitment Field Experiments*


**Lecture 4**

*Present-Biased Preferences: Evidence from the Laboratory*


*Reference Dependence and Housing Markets*

*Methodology: Bunching-Based Evidence of Reference Dependence*


*Reference Dependence and Labor supply*

Lecture 5


*Reference Dependence and Equity Premium*


**Reference Dependence and Job Search**


**Reference Dependence and Endowment Effect**


**Reference Dependence: Forward vs. Backward Looking**


**Lecture 6**

**Reference Dependence and Effort**


**Reference Dependence and Domestic Violence**


**Reference Dependence and Insurance Choices**


**Lecture 7**

**Social Preferences Wave I: Altruism**

**Workplace Effort: Altruism**


**Shaping Social Preferences**

Social Preferences Wave I: Warm Glow and Charitable Giving


Social Preferences Wave II: Inequity Aversion and Reciprocity


Workplace Effort: Inequity Aversion


Methodology: Field Experiments

Lecture 8
Social Preferences in the Workplace: Gift Exchange and Vertical Preferences


* Gift Exchange in Charitable Giving

* Social Preferences Wave III: Moral Wriggle-Room, Social Pressure, and Signaling

* Social Pressure


**Part II -- Non-Standard Beliefs
Lecture 9**

* Overconfidence


**Law of Small Numbers**


**Projection Bias**


**Limited Attention: Introduction**


**Part III -- Non-Standard Decision-Making**
Lecture 10
Limited Attention: Consumption Behavior


Limited Attention: Financial Market Evidence


Lecture 11
Framing


Menu Effects: Choice Avoidance

**Menu Effects: Preference for Familiar**


**Menu Effects: Preference for Salient**


**Menu Effects: Confusion**


**Persuasion**


**Lecture 12**

**Emotions: Mood**


**Emotions: Arousal**


**Methodology: Lab and Field**


**Happiness**


**Part IV -- Market Response to Biases**

**Lecture 13**

* Market Response to Bias: Pricing


**Market Response to Biases: Corporate Decisions**


**Market Response to Biases: Employers**


**Market Response to Biases: Politicians**


**Lecture 14**

**Market Response to Biases: Behavioral Finance**


Market Response to Biases: Welfare Maximization