Course title	Behavioural Economics: Regulation and Competition Implications
Level	Advanced Undergraduate / Postgraduate
Duration	4 hours
Dates	14 July 2014
Instructor	Xeni Dassiou, City University London

Course objectives

Examine behavioral economics as an instrument used by regulatory and competition authorities to influence consumer behaviour and analyze firm behaviour & strategies and their anti-competitive implications. The course will explain how this allows the policy maker to design appropriate responses in order to prevent undesirable outcomes for the consumer through the promotion of competition where feasible.

Course Description

behavioural economics introduction – the framing effect - anchoring effects; endowment effects - information overload - theory of regret - mental accounting & loss aversion - hyperbolic discounting - sunk cost fallacy - endowment effects - over optimism - satisfying vs. optimizing – herding - drip pricing

Course Outline

Behavioural economics is not a new approach: John Maynard Keynes employs the term “animal spirits”, a term which he used to indicate the emotional component of economics represented in consumer behaviour (see, “Animal Spirits; How human psychology drives the economy and why it matters for global capitalism”, Akerlof & Shiller). Simon (1957) distinguishes between the methodology of neoclassical economics which is based on the extreme rationality of economic agents and the maximisation of an objective function, and behavioural economics which modifies and adjusts rationality to take account of the actual behaviour of economic agents He suggests that “behavioural economics” can be seen as a commitment to test and modify a model on the basis of actual behaviour. Hence he indicates a need for case studies a, survey research and laboratory experiments (e.g. experimental economics). In the economic literature there are plenty of different puzzles and anomalies; for example the Allais paradox (1953) shows the inconsistency between actual behaviour and theoretical predictions, while in the Ellsberg paradox (1961) people violate the prediction of expected utility and once again we see a failure to predict actual behaviour.

Behavioural economics in its most recent form retains this interface between economics and psychology. Its usefulness stems from its use as a way to explain and alter consumer behaviour (Kahneman & Tversky, 1979, 1986; Thaler, 1980, 1985), and more recently as a means to guide competition policy (OFT, March 2010) and explain the behaviour not only of consumers, but also that of firms (Armstrong & Huck, 2010) and even, ultimately, regulators and policy makers themselves.

Should behavioural economics as an instrument to describe, explain and influence consumers' and firms' behaviour be considered as a complement to the regulators' toolkit, or as a substitute for regulatory intervention itself? We provide an overview of the literature and discuss how even in simple problems people violate the rules of rational choice assumed in economics. We provide an analysis of new insights and concepts, such as endowment effects, loss aversion and the theory of regret, framing choices, and libertarian paternalism (Sunstein & Thaler, 2003), etc. We then analyse how these insights can both explain and provide solutions into problems faced by policy makers and regulators.

Educational Outcomes

Understanding of behavoural economics as an interface between economics and psychology and appreciate its usefulness for acting as a complement to standard regulatory and antocompetitive practises by affecting consumer behaviour and understanding the stratigic choises by firm in an alternative framework from that of the neoclassical framework of utility and profit maximisation by rational agents.

Basic Bibliography

- Akerlof, G. and Shiller, R. 'Animal Spirits; How Human Psychology Drives the Economy, and Why it Matters for Global Capitalism', Princeton University Press, 2009.
- Armstrong, M. and Huck, S. 'Behavioral Economics as Applied to Firms: A Primer', MPRA Paper No. 20356, January 2010.
- Frank, R. Microeconomics and Behaviour, Eighth edition, McGraw-Hill 2010.
- Kahneman, D. and Tversky, A. 'Rational Choice and the Framing of Decisions', The Journal of Business, 59(4-2): S251-S278, 1986.
- Kahneman, D. and Tversky A., 'Prospect Theory: An Analysis of Decisions under Risk', Econometrica, 47(2): 263-291, 1979.
- 'What does Behavioural Economics Mean for Competition Policy? , OFT 1224, Office of Fair Trading, March 2010.
- Simon, H. 'A Behavioral Model of Rational Choice', in Models of Man, Social and Rational: Mathematical Essays on Rational Human Behavior in a Social Setting. New York: Wiley, 1957.
- Sunstein, C. & Thaler, R. 'Libertarian Paternalism is not an Oxymoron', AEI-Brookings Joint Center for Regulatory Studies, Working Paper 03-2, The Law School, The University of Chicago, May 2003.
- Thaler, R. 'Mental Accounting and Consumer Choice', Marketing Science, 4(3): 199-214, 1985.
- Thaler, R. 'Toward a Positive Theory of Consumer Choice',

	Journal of Economic Behavior and Organization, 1, 39-60: 1980.
Teaching Methodology	Lectures 2 = 4 h Total = 4 h
Language	English
Location	EPLO Headquarters, Sounion
General note	