



BEHAVIORAL ECONOMICS

2021/22

Course code	GRAE022
Compulsory in the programmes	<i>Behavioural Economics</i>
Level of studies	<i>Graduate</i>
Number of credits	6 ECTS (36 contact hours + 2 consultation hours, 124 individual work hours)
Course coordinator (title and name)	Prof. Dr. Slavisa Tasic slatas@faculty.ism.lt
Prerequisites	None
Language of instruction	English

THE AIM OF THE COURSE

In this course we examine the role of rationality in economic theory and practice. We will study what rationality means in various branches of economics, how realistic the assumption of rationality is, and how deviations from the assumed standards of rationality impact economic policy and financial behavior. Using textbook readings, journal articles, classroom experiments, and exercises we will review some important results of behavioral economics and discuss the implications of these results for economic theory and public policy. The course will also introduce some influential critiques, challenges, and recent debates in the field of behavioral economics.

MAPPING OF COURSE LEVEL LEARNING OUTCOMES (OBJECTIVES) WITH DEGREE LEVEL LEARNING OBJECTIVES (See Annex), ASSESMENT AND TEACHING METHODS

Course level learning outcomes (objectives)	Degree level learning objectives (Number of LO)	Assessment methods	Teaching methods
CLO1. Understand and apply the main concepts, research tools and methodologies of behavioral economics that help to reveal biases, heuristics, etc. in the decision making process on individual, corporate, policy, and financial market level.	LO1.1.	Final exam, Research project, Presentation	Lectures
CLO2. Present the main results in the field of behavioral economics focusing on financial market processes including market anomalies.	LO1.1, LO3.1	Final exam, Research project, Presentation	Lectures, seminars
CLO3. Explore behavioral economics considering financial, investment and dividend policy decisions and contrasting traditional and behavioral approaches.	LO1.1, LO3.1 LO3.2	Final exam, Class participation, Research project, Presentation	Lectures, seminars
CLO4. Research, prepare and present behavioral economics problems	LO1.1, LO1.2 LO3.1, LO3.2	Research project, Presentation	Seminars

ACADEMIC HONESTY AND INTEGRITY

The ISM University of Management and Economics Code of Ethics, including cheating and plagiarism are fully applicable and will be strictly enforced in the course. Academic dishonesty, and cheating can and will lead to a report to the ISM Committee of Ethics. With regard to remote learning, ISM remind students that they are expected to adhere and maintain the same academic honesty and integrity that they would in a classroom setting.

COURSE OUTLINE

Session	Topics	In-class hours	Readings
Oct 4	Introduction Rationality in microeconomics: preferences, choice under certainty, consumer theory	4	Varian, 2009: Chapters 2-7
Oct 6	Rationality in microeconomics: choice under uncertainty Prospect theory	4	Varian, 2009: Chapter 12 Kahneman & Tversky, 1979 Barberis, 2013
Oct 8	Rationality in macroeconomics (behavioral macroeconomics) Rationality in game theory Methodological issues of economics	4	Akerlof, 2001 Diamond, Shafir, Tversky, 1997 Cowen, 2001 Optional: Friedman, 1966
Oct 11	Perception biases: anchoring, saliency, framing, sunk-cost bias Inertial effects: endowment, status-quo, disposition	4	Kahneman & Tversky, 1974 Kahneman, Knetsch & Thaler, 1991 Optional: Finklestein, 2009; Chetty et al, 2009; Odean, 1998
Oct 13	Causality and statistics: representativeness, conjunction fallacy, reading into randomness, small sample bias, probability neglect Illusions: talent, skill, superiority, validity	4	Thaler, 1999, Malmendier & Tate, 2015
Oct 15	Rationality in finance Stock market behavior and anomalies: serial correlation, calendar effects, predictability of stock prices, momentum, equity-premium puzzle	4	Shiller, 2003 DeLong & Magin, 2009
Oct 18	Rational choice in political economy Behavioral public policy	4	Sunstein, 2014 Caplan, 2007 Optional: Tasic 2009, Tasic 2011, Lucas & Tasic 2015
Oct 20	Behavioral economics critiques Two systems vs. ecological rationality	4	Kahneman, 2011: Chapters 1-2 Gigerenzer, 2015 Buturovic & Tasic, 2015 Taleb, 2017 Optional: List, 2004

Oct 22	Neuroeconomics		
	Concluding discussion	4	
	Research project presentations		
	Final Project due: Papers and presentation files.		
	Consultations	2	
	Final Exam	2	

FINAL GRADE COMPOSITION

Quizzes (20%)

We will have 8 short quizzes – one every class day, starting from the second day. The quizzes are a way to keep everyone in the class involved and engaged. They will be related to the class material of the previous day. Quizzes will have multiple choice questions, as well as essay questions – typically, you will be asked for your thoughts on a given topic or a problem. Quizzes will be open book.

The total quiz score is the simple sum of your best 7 scores (out of 8 quizzes). Missed quizzes are scored with zero – and there are no exceptions to this rule.

Reports (8%)

Class 7 and class 8 will include assigned videos of lectures, talks, or interviews with an expert related to the session's topic. Your task is to carefully watch the videos and to write a short summary of the most interesting points that caught your attention.

You are not supposed to describe what exactly the videos include, or to retell their contents. Instead, you need to describe what you learned from them. Choose what you think are the few most relevant or most interesting points from the videos and discuss them. A good report will include relevant highlights from the videos, show understanding of the topic, and be no less than 400 words long.

The video and report writing is considered class work reserved for the last hour of our sessions. To add some flexibility, the deadline for reports will be the beginning of the next session. You should e-mail your reports to the instructor.

Participation (2%)

The nature of this course demands active participation and meaningful engagement. Participation is graded with 2%; but credit may be increased to up to 5% for exceptional participation in class.

Final Exam (35%)

The final exam will include a set of open-ended and multiple-choice questions. The exam will be closed book – the use of printed material or electronic equipment will not be allowed.

Research Project (35%)

The Research Project includes a project presentation, and a research paper. The project paper can take one of the following forms:

Option 1: A case study of a particular behavioral phenomenon. Choose a decision-making problem, phenomenon, bias or heuristic that you want to explore. Explain the phenomenon, discuss its applications, survey the academic literature on it, and present the empirical evidence found in the literature. The paper should be 8-12 pages long (at 1.5 spacing, including literature using the APA requirements).

Option 2: An experiment designed to test a particular behavioral phenomenon. State a research question related to the course and come up with your own experimental design or a

survey in order to test it. You can use a behavioral concept existing in the literature or propose an entirely new one. You can perform your experiment or run a survey in the current classroom or online. The accompanying paper should explain your experiment and findings in the usual academic journal form, and there are no specific length requirements for the paper in this case.

In both cases the Research Project includes a paper and a presentation of the proposal. The paper (including the contents of the paper and the quality of the experiment if you choose Option 2) counts for 80% of the project grade. The quality of the proposal presentation itself counts for 20% of the Research Project grade.

The project can be realized individually, or in groups of up to 3 members. Grading requirements are adjusted by the number of group members. Along with the final paper, group members will send a consensus estimate of their relative contributions adding to 100%. (For example, 55:45, or 60:40 for a 2-member group; or 40:40:20, or 33:33:34 for a 3-member group).

READINGS

Books:

Varian, Hal. 2009. *Intermediate Microeconomics*. 8th edition. New York: W. W. Northon & Co.

Kahneman, Daniel. 2011. *Thinking Fast and Slow*. New York: Farrar, Straus and Giroux.

Journal Articles:

Barberis, Nicholas. 2013. Thirty Years of Prospect Theory in Economics: A Review and Assessment. *Journal of Economic Perspectives* 27(1): 173–196.

Buturovic, Zeljka and Slavisa Tasic. 2015. Kahneman's Failed Revolution Against Economic Orthodoxy. *Critical Review* 27(2): 127:145.

Caplan, Bryan. 2007. "The Myth of the Rational Voter". *Cato Policy Analysis* 594.

Chetty, Raj, Adam Looney and Kory Kroft. 2009. Salience and Taxation: Theory and Evidence. *The American Economic Review* 99(4): 1145-1177.

Cowen, Tyler. 2001. "How Do Economists Think about Rationality?" In *Satisficing and Maximizing: Moral Theorists on Practical Reason*, ed. Michael Byron. Cambridge: Cambridge University Press.

DeLong, Brad and Konstantin Magin. 2009. The U.S. Equity Return Premium: Past, Present, and Future. *The Journal of Economic Perspectives* 23(1): 193-208.

Diamond, Peter, Eldar Shafir and Amos Tversky. 1997. Money Illusion. *Quarterly Journal of Economics* 112(2): 341-374.

Finklestein, Amy. 2009. E-Z Tax. Tax Salience and Tax Rates. 2009. *Quarterly Journal of Economics* 124(3): 969-1010.

Friedman, Milton. 1966. "The Methodology of Positive Economics". In *Essays In Positive Economics*. Chicago: Univ. of Chicago Press.

Gigerenzer, Gerd. 2015. Towards a Rational Theory of Heuristics. Mimeo.

Kahneman, Daniel and Amos Tversky. 1974. Judgement under Uncertainty: Heuristics and Biases. *Science* 185(4157):1124-1131.

Kahneman, Daniel and Amos Tversky. 1979. Prospect Theory: An Analysis of Decisions under Risk. *Econometrica* 47(2):263-292.

Kahneman, Daniel, Jack Knetsch and Richard Thaler. 1991. Anomalies: The Endowment Effect, Loss Aversion, and Status Quo Bias. *The Journal of Economic Perspectives* 5(1): 193:206.

List, John. 2004. Neoclassical Theory versus Prospect Theory: Evidence from the Marketplace. *Econometrica* 72(2): 615-625.

- Lucas, Gary & Slavisa Tasic. 2015. Behavioral Public Choice and the Law. *West Virginia Law Review* 118(1), 199-266.
- Malmendier, Urilike and Geoffrey Tate. 2015. Behavioral CEOs: The Role of Managerial Overconfidence. *Journal of Economic Perspectives* 29(4): 37–60.
- Odean, Terrance. 1998. Are investors reluctant to realize their losses? *Journal of Finance* 53(5): 1775–1798.
- Shiller, Robert. 2003. From Efficient Markets Theory to Behavioral Finance. *Journal of Economic Perspectives* 17(1): 83–104.
- Sunstein, Cass. 2014: Nudging: A Very Short Guide. *Journal of Consumer Policy* 583.
- Taleb, Nassim. 2017. “How to be Rational about Rationality”, in *Skin in the Game*.
- Tasic, Slavisa. 2009. The Illusion of Regulatory Competence. *Critical Review* 21(4): 423-436.
- Tasic, Slavisa. 2011. Are Regulators Rational? *Journal des Economistes et des Etudes Humaines* 17(1).
- Thaler, Richard. 1999. Mental Accounting Matters. *Journal of Behavioral Decision Making* 12:183-206.

DEGREE LEVEL LEARNING OBJECTIVES

Learning objectives for Master of Social Science*Programme:**Financial Economics*

Learning Goals	Learning Objectives
Students will be critical thinkers	LO1.1. Students will be able to identify underlying assumptions, limitations of previous research; evaluate managerial solution alternatives.
	LO1.2. Students will become independent learners and develop their own comprehension of scientific theories, models, and concepts.
Students will be socially responsible leaders	LO2.1. Students will be able to evaluate past and current practices in their discipline from an ethical perspective .
Students will be effective communicators	LO3.1. Students will develop and deliver a coherent oral presentation .
	LO3.2. Students will develop and deliver a coherent written research paper .