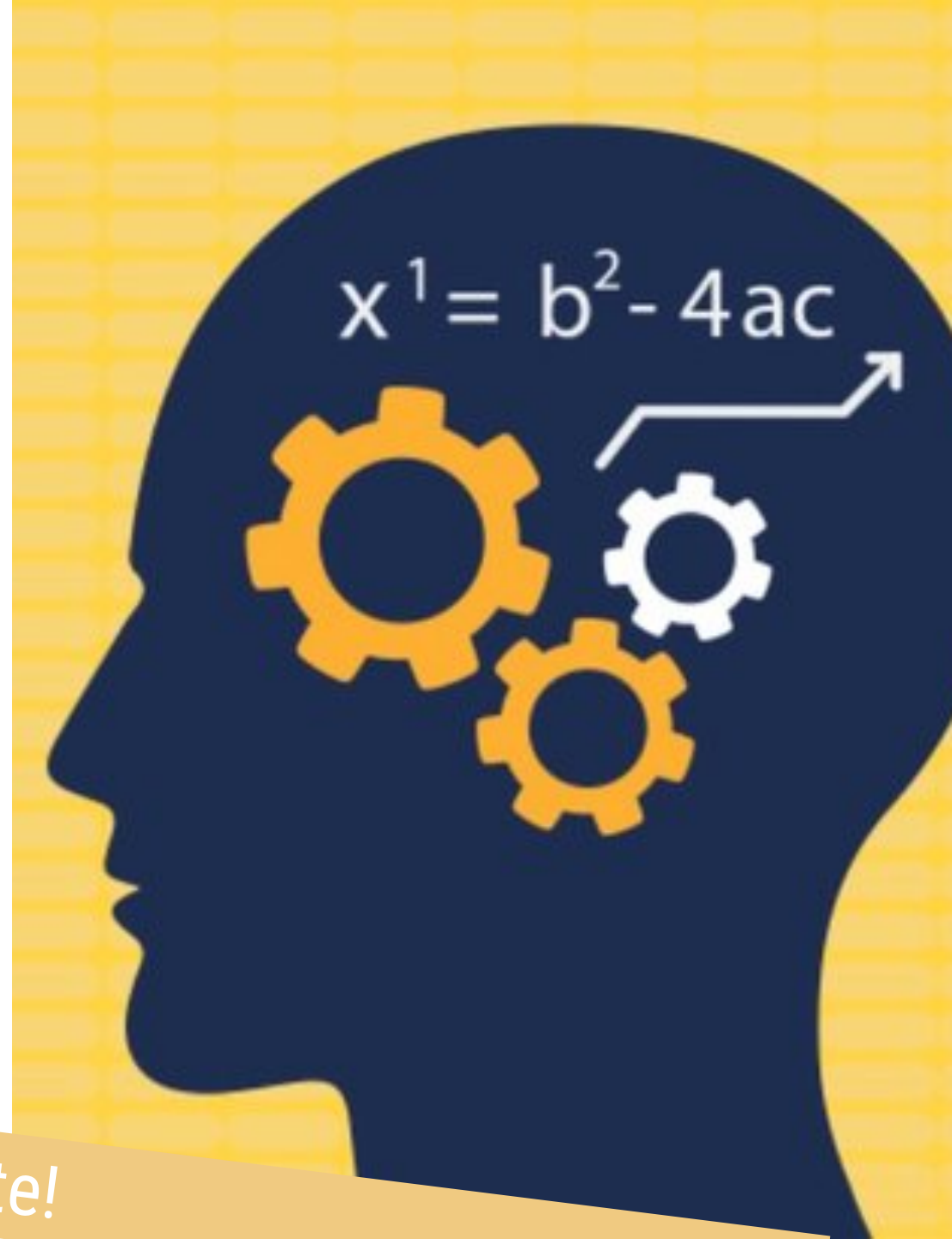


Incentives and human behavior

MPA 612: Public Management Economics

January 31, 2018

Fill out your reading report on Learning Suite!



Current events

People are rational and
always maximize utility

Except when they don't

Fun and games

Go to
andhs.co/quiz1
and take a quiz

Go to
andhs.co/quiz2
and take a quiz

Go to
andhs.co/quiz3
and take a quiz



$$8 \times 7 \times 6 \times 5 \times 4 \times 3 \times 2 \times 1$$

$$1 \times 2 \times 3 \times 4 \times 5 \times 6 \times 7 \times 8$$

Plan for today

Fun and games

Heuristics and shortcuts

Nudges

Incentives

Heuristics and shortcuts

Thinking is hard.

We can't process all
information, but we can
filter and privilege
information

Common heuristics and mistakes

Representativeness

Availability

Adjustment and anchoring

Time issues

Representativeness

We make judgments based on how well information represents the norm

Ignore base rates, think backwards, start with exceptions and stereotypes

Representativeness

Insensitivity to prior probability of outcomes

Insensitivity to sample size

Misconceptions of chance

Misconceptions of regression

Availability

We make judgments based on how quickly other examples come to mind

Availability

Biases due to the retrievability of instances

Biases of imaginability

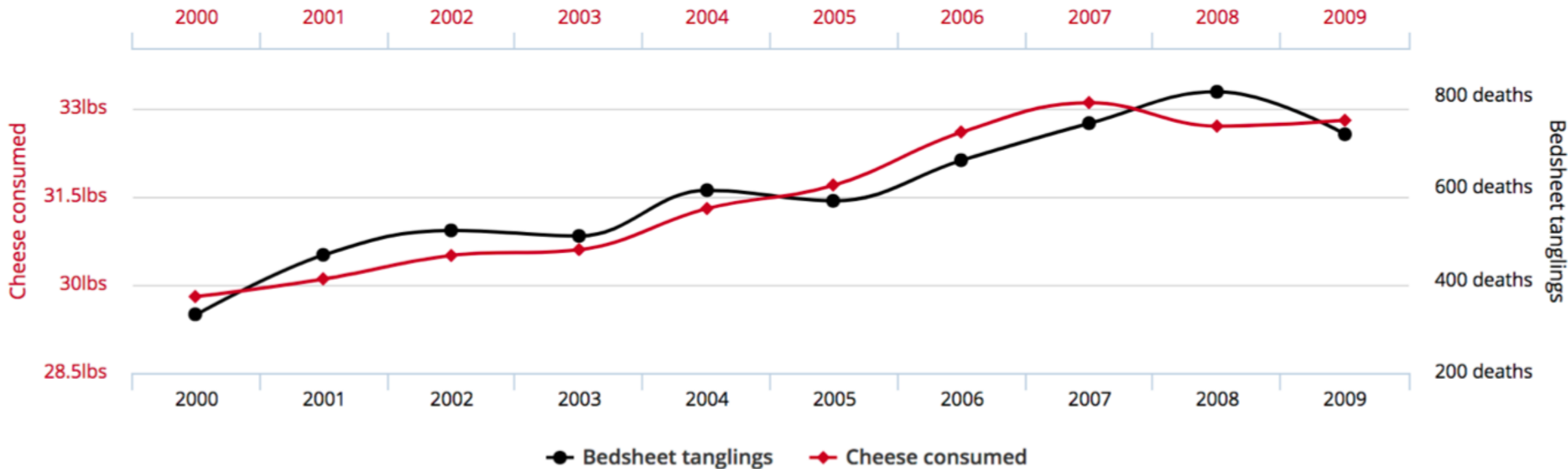
Illusory correlation



Per capita cheese consumption correlates with

Number of people who died by becoming tangled in their bedsheets

Correlation: 94.71% (r=0.947091)



tylervigen.com

Data sources: U.S. Department of Agriculture and Centers for Disease Control & Prevention

Adjustment and anchoring

Different starting points yield estimates that are biased toward the initial values

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Today

\$100

December 25

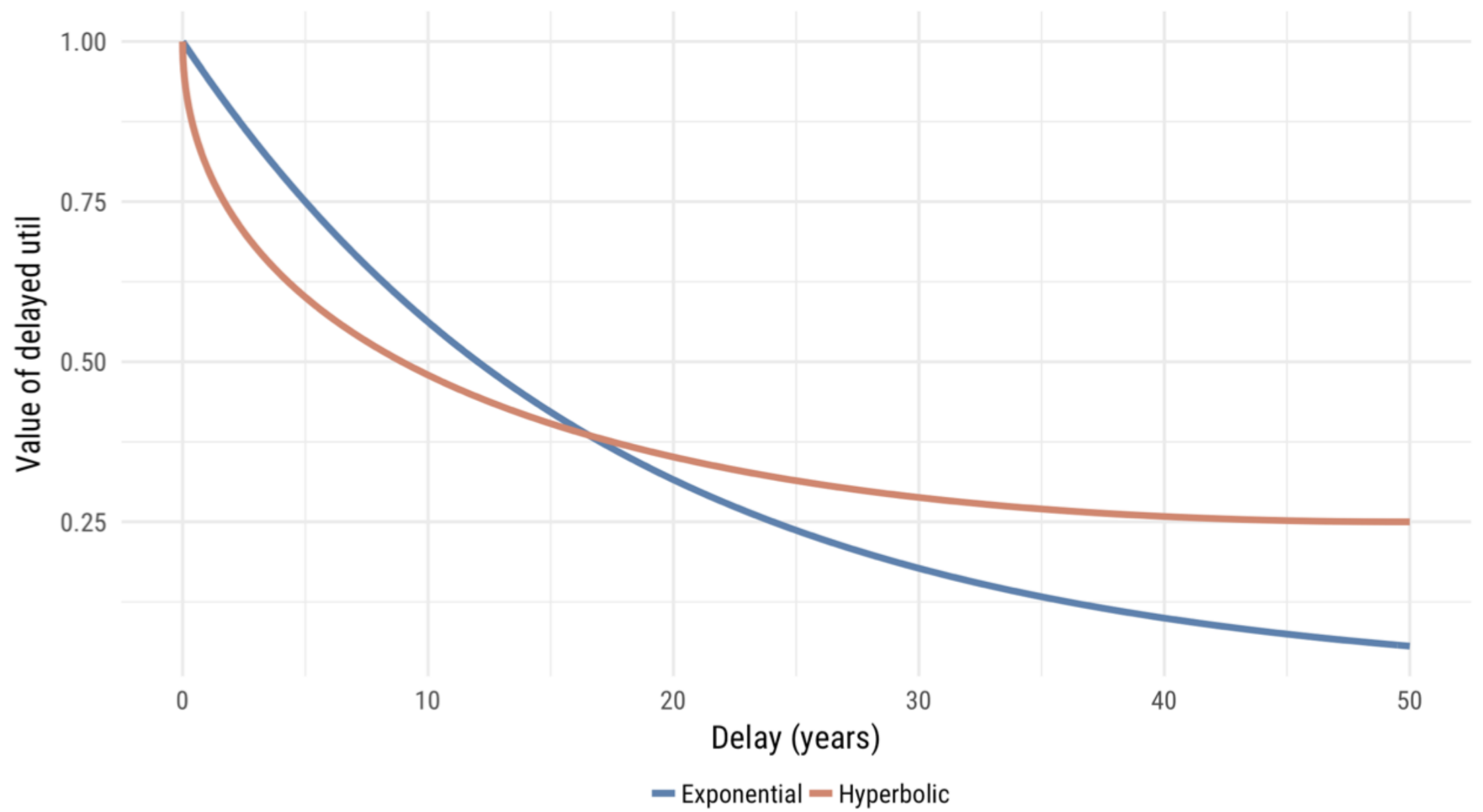
Next week

\$110

December 31

Hyperbolic discounting

We prefer immediate payoffs more than
future payoffs



The battle within us

Intrapersonal strategic conflict

Our present selves force their preferences on our future selves

Chips and salsa

Saving for retirement



Commitment devices

Deadlines and coauthors

Exercise pacts

Save More Tomorrow

Nudges

Helping people overcome mental biases with public policy

What is a nudge?

Adjusting choice architecture in a way that helps people make better choices

Libertarian paternalism

Why nudge?

Why not nudge?

Best conditions for nudges

Disconnect between costs and benefits

Costs now, benefits later

Benefits now, costs later

Choices are complex

Mortgages

Choices are rare

Buying a car

Getting married

Low feedback

High cholesterol diet

Poor knowledge

Health plans

Examples of nudges?

Incentives

We respond to incentives. That can backfire.

Why do people do what they do?

People get utility from doing stuff

Extrinsic rewards

Intrinsic rewards

These can get distorted and crowded out, though!

Good policy uses incentives to channel behavior toward some desired outcome. Bad policy either ignores incentives or fails to anticipate how rational individuals might change their behavior to avoid being penalized.

Naked Economics, p. 39

Perverse incentives



People respond to what
you signal

You get what you measure

Daycares and late pickups

Blood donors

Taxes

Design work

Thanksgiving

Playgroups and daycares

MLMs

Extrinsic rewards can crowd out intrinsic motivations

Don't violate important social relationships by reducing services to a market transaction

Pay enough or don't pay at all