Behavioral Economics: Insights & Tools for Practice

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3 Big Questions – 3 Big Answers

• What is behavioral economics?

• Why do we need experiments?

• How can SPI insights be applied?

But what does it mean??
BEHAVIORAL ECONOMICS
Economics is a Science

• Decisions are **not random**!
• In fact, people behave in predictable ways, as defined by:
  – Constraints (what the individual *can* do)
  – Preferences (what the individual *wants* to do)

• People make decisions to maximize their satisfaction/utility (based on preferences) while remaining within the constraints.
“George Gets a Letter”

- George carefully reads the letter.
- He thinks about whether the charity deserves a donation.
- He thinks about how much money he has.
- If he has enough money, and the charity looks good, he writes a check.
“George Gets a Letter”

- George glances at the letter
- He thinks about his satisfaction from a donation
- He thinks about what his friends are doing
- He thinks about feeling guilty if he doesn’t donate
- He thinks about what the charity will do with the money
“George Gets a Letter” – Econ Jargon

<table>
<thead>
<tr>
<th>George glances at the letter</th>
<th>Transaction Cost</th>
</tr>
</thead>
<tbody>
<tr>
<td>He thinks about his satisfaction from a donation</td>
<td>Self-interest: Warm glow, “cold prickle”</td>
</tr>
<tr>
<td>He thinks about feeling guilty if he doesn’t donate</td>
<td>Framing</td>
</tr>
<tr>
<td>The letter tells him something about how he ‘should’ act</td>
<td>Social norms</td>
</tr>
<tr>
<td>He thinks about what his friends are doing</td>
<td></td>
</tr>
<tr>
<td>He thinks about what the charity will do with the money</td>
<td></td>
</tr>
</tbody>
</table>
What is Behavioral Economics?

• Learning about underpinnings of human behavior
• Predicting how individuals will behave in different environments
• Providing insights into which environments to apply to obtain desired results
EXPERIMENTS:
IN THE LAB, IN THE FIELD
Why do we Need Experiments?

• We can collect *big data*
  – Data tells us what people actually do in different environments
  – We can learn about human behavior
• But *big data* doesn’t tell the whole story
  – We need to know what **causes** certain behaviors so we can generate insights about how solicitations work
  – Experiments can do that
Causation? 2 Practical Examples

• A CEO of a firm makes the point – our ads work, because *the more ads we used, the more clients we had*!

• We make the point – ice cream is dangerous, because *the more ice cream we eat, the more drownings occur*!

• But does ice cream cause drownings?
Experiments can do that.

CAUSE

NO APPLE?...... NO EFFECT!

EFFECT
Field Experiments

- **Randomize** potential donor pool to different environments (“treatments”)
Expertise from Research Side

• Designing the study
  – Solicitation message
  – Match rate
  – Seed money
  – Recognition

• Randomizing: how to make sure there is ‘balance’

• Drawing conclusions
  – Compare rate of giving and average gift by treatment
  – Infer causation, gain insights!
Expertise from the Practitioners

• Knowledge about the donor base

• Expertise into the ‘art’ of asking: many years of experience

• Ability to bring research into practice
Benefits of a Field Experiments

• Not everyone gets the ‘new’ solicitation
• But that’s ok:
  – We learn about the return to the ‘new’ solicitation
  – If something doesn’t work, we didn’t send it out to the entire pool of donors
• We have more knowledge to move forward
  – Causal knowledge, so we can make scientifically informed decisions
Laboratory Experiments

- Undergraduate student ‘subjects’
- Typically computerized
- Different types of ‘games’ have been developed
  - Can be ‘one shot’ or many ‘periods’
  - Can be in a group or individual
- Remove context
- Very controlled environment
Inferring Causation

• Treatments
  – Many different ‘treatments’ in an experiment
  – Each treatment just changes one aspect of the environment

• Randomization
  – As people sign up online, they do not know into which treatment
  – So we expect, on average, the same types of people in each treatment
  – That means that if we observe a difference in behavior, it is caused by the treatment!
Lab: Public Goods Game

80 tokens: How much to give?

80 tokens: No one will know if I keep it for myself...
## Treatments

<table>
<thead>
<tr>
<th>(N) Control (none shown)</th>
<th>(T) Only top 2 recognized</th>
<th>(B) Only bottom 2 recognized</th>
<th>(A) All recognized</th>
</tr>
</thead>
<tbody>
<tr>
<td>40 (2 sessions)</td>
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</tr>
</tbody>
</table>

**Your Group Members**

You are a group of 5 participants each decision period.

<table>
<thead>
<tr>
<th>#1</th>
<th>#2</th>
<th>#3</th>
<th>#4</th>
<th>#5</th>
</tr>
</thead>
<tbody>
<tr>
<td>Allocated 00 tokens</td>
<td>Allocated 23 tokens</td>
<td>Allocated 12 tokens</td>
<td>Allocated 2 tokens</td>
<td>Allocated 2 tokens</td>
</tr>
</tbody>
</table>

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<th>#5</th>
</tr>
</thead>
<tbody>
<tr>
<td>Allocated 08 tokens</td>
<td>Allocated 21 tokens</td>
<td>Allocated 10 tokens</td>
<td>Allocated 5 tokens</td>
<td>Allocated 2 tokens</td>
</tr>
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Results: Public goods game

Contribution

Period

None-Free
All-Free
Results: Public goods game

Contribution

Period

Contribution:
- Public goods game

Types:
- None-Free
- All-Free
- Top-Free
Results: Public goods game

Contribution

- None-Free
- All-Free
- Top-Free
- Bottom-Free

Period

10% 20% 30% 40% 50% 60% 70% 80%
Lab Experiment Conclusions

- Recognition by peers very effective for increasing giving
- Shame is very relevant for this environment
- Prestige less relevant
- But this environment is special: no entry/exit
- Need to explore additional environments
HOW CAN SPI INSIGHTS BE APPLIED?
Apply what you’ve learned... to change a “No” to a “Yes”!

Please ask questions. We want to talk with you.

Clipart: Thanks, Ron Leishman!