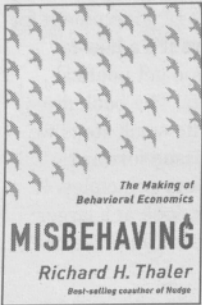


# The human puzzle

*Professor tells us why economics can't be separated from human behavior*



**"Misbehaving: The Making of Behavioral Economics,"** by Richard H. Thaler

**BY MEGAN WILHOOD**  
CONTRIBUTING COLUMNIST

**"T**he book is not the sort you might expect an economics professor to write. It is neither a treatise nor a polemic," Richard Thaler said of his narrative-meets-argument, "Misbehaving."

It is the story of the birth of the field of behavioral economics, which is so common now as to sound redundant. How would one even study economics without studying the behavior of the entities who participate in economics? These entities are "humans," as opposed to "Econs," creatures Thaler argues most of economic theory was based on until the creation of the behavioral branch.

"Economics is distinguished from other social sciences," Thaler writes, "by the belief that most behavior can be explained by assuming that agents have stable, well-defined preferences and make rational choices consistent with these preferences in markets that (eventually) clear. An empirical result is anomalous if it is difficult to 'rationalize,' or if implausible assumptions are necessary to explain it within the paradigm."

In a world of Econs, gifts are foreign concepts; prices are always naturally set at the right level by the "invisible hand" of supply and demand; and buying, saving and investing choices are all easily predictable.

But Thaler started to notice some outliers, people not making the predicted choice, people who were "misbehaving." The core principle of economic theory is that people make unbiased choices to optimize gain. But Thaler points out that it takes a lot of training to be economically knowledgeable enough to make truly optimal choices. And what kind of training would suffice to eliminate all biases? Economics is in the business of

constructing models to predict and explain behavior and, as Thaler writes, "economists are really good at inventing rational explanations for behavior, no matter how dumb that behavior appears to be." Economists run into trouble when "they make a highly specific prediction that depends explicitly on everyone being economically sophisticated."

Thaler reassures us that we don't have to stop this kind of modeling — the kind that describes "Econs" — but it's not helping very much to assume that these are accurate predictions of behavior and, more importantly, basing major public policies on them.

The problem is that, "As (John Maynard) Keynes notes, following the conventional wisdom keeps you from getting fired." So, interspersed with detailed but not overly complex descriptions of experiments he ran in his classes, Thaler also describes how much of a misguided apostate he was assumed to be in his own field. His conversational, amusingly self-deprecating tone and light-hearted anecdotes help keep the lay reader engaged; it would likely help to have a basic understanding of economics, at least to get through some of Thaler's material with more enthusiasm.

But even the reader with only a cursory understanding of economics will find Thaler's anomalies fascinating: "Roughly speaking, losses hurt twice as much as gains make you feel good" (could this be why we generally remember insults more than compliments?). "Those who start out with some object will tend to keep it, while those who don't have such an object won't be that keen to buy one" (could this be why we struggle to muster up the political and social will to alleviate poverty?). "Self-control is, centrally, about conflict. And, like tango, it takes (at least) two to have a conflict" (could this be part of what's

behind the expression "part of me feels X but part of me feels Y?"). "There is clear evidence that people dislike unfair offers and are willing to take a financial hit to punish those who make them. It is less clear that people feel morally obliged to make fair offers" (whatever happened to the Golden Rule?).

Thaler, not surprisingly, takes a strictly economic view on poverty, it seems. Even

with a behavioral-economics view, though, one can misrepresent the factors and causes of poverty, on the global or micro level. But what behavioral economics does have to say on the topic is more useful than current public policy suggests. For instance, Thaler writes, "The idea is that a certain amount of money can seem small or large depending on context." Applying this concept to poverty alleviation results in localizing policies and solutions to poverty rather than one-size-fits-all legislation or action.

Thaler's main argument is, "Humans do not have the brains of Einstein, nor do they have the self-control of an ascetic Buddhist monk. Rather, they have passions, faulty telescopes (pleasure is hard to defer), treat various pots of wealth quite differently and can be influenced by short-run returns in the stock market. We need a model of these kinds of Humans." This is why, even if you're not interested in economics, Thaler has a lot to say to those who are interested in humans.

*Reprinted from Street Roots' sister paper Real Change News in Seattle.*

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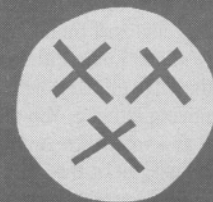
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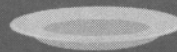
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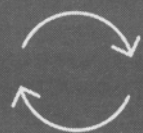
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