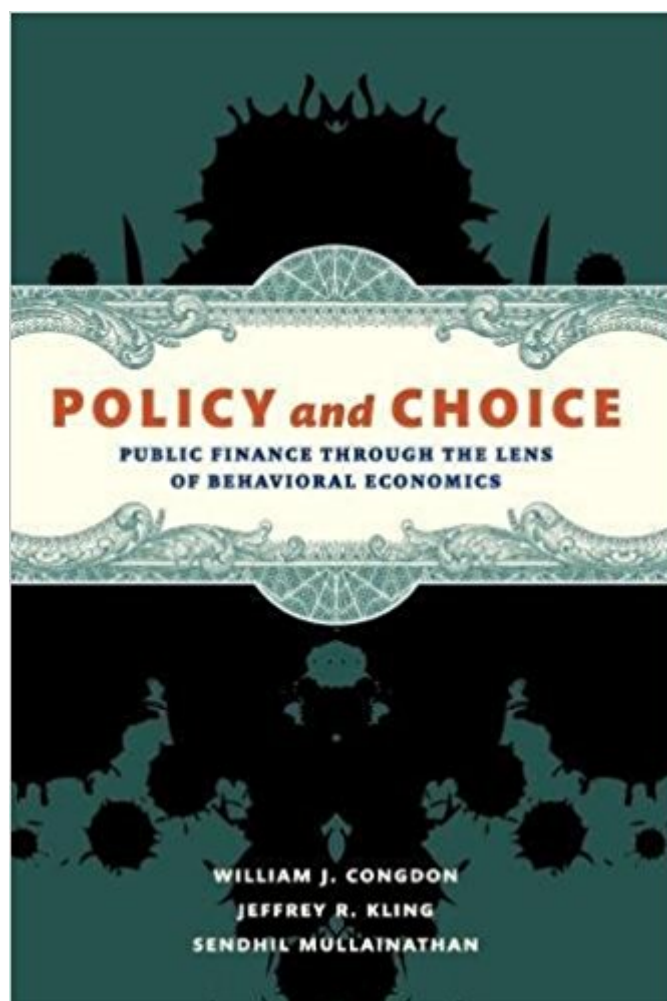


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Policy And Choice: Public Finance Through The Lens Of Behavioral Economics



Synopsis

Traditional public finance provides a powerful framework for policy analysis, but it relies on a model of human behavior that the new science of behavioral economics increasingly calls into question. In *Policy and Choice* economists William Congdon, Jeffrey Kling, and Sendhil Mullainathan argue that public finance not only can incorporate many lessons of behavioral economics but also can serve as a solid foundation from which to apply insights from psychology to questions of economic policy. The authors revisit the core questions of public finance, armed with a richer perspective on human behavior. They do not merely apply findings from psychology to specific economic problems; instead, they explore how psychological factors actually reshape core concepts in public finance such as moral hazard, deadweight loss, and incentives. Part one sets the stage for integrating behavioral economics into public finance by interpreting the evidence from psychology and developing a framework for applying it to questions in public finance. In part two, the authors apply that framework to specific topics in public finance, including social insurance, externalities and public goods, income support and redistribution, and taxation. In doing so, the authors build a unified analytical approach that encompasses both traditional policy levers, such as taxes and subsidies, and more psychologically informed instruments. The net result of this innovative approach is a fully behavioral public finance, an integration of psychology and the economics of the public sector that is explicit, systematic, rigorous, and realistic.

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Customer Reviews

" *Policy and Choice* is a must-read for students of public finance. If you want to learn how the

emerging field of behavioral economics can help lead to better policy, there is nothing better." — N. Gregory Mankiw, Harvard University, former chairman of the President's Council of Economic Advisers, and author of *Principles of Economics* "This fantastic volume will become the standard reference for those interested in understanding the impact of behavioral economics on government tax and spending policies. The authors take a stream of research which had highlighted particular 'nudges' and turn it into a comprehensive framework for thinking about policy in a more realistic world where psychology is incorporated into economic decisionmaking. This excellent book will be widely used and cited." — Jonathan Gruber, Massachusetts Institute of Technology, former Treasury Department official, and author of *Public Finance and Public Policy* "The proper design of public policy has never been more important, and it will be shaped by the emerging insights of behavioral economics. Congdon, Kling, and Mullainathan have produced a clear and accessible road map to the key issues." — Douglas Holtz-Eakin, American Action Forum president and former director of the Congressional Budget Office "For decades, economists have been advising governments with an impoverished toolkit because they based their advice on a fully rational depiction of human behavior. This book shows the world how much more powerful economic science can be when it is enriched with important insights from psychology. If you are a public finance scholar or practitioner you need to read this book right now; don't procrastinate!" — Richard H. Thaler, University of Chicago, coauthor of *Nudge* "Congdon, Kling, and Mullainathan have provided a lucid and crisply written primer on how to apply insights from psychology to important issues that arise in public sector economics. This volume will be of interest not only to students in public finance courses, but also to researchers who want to find out what behavioral economics is all about." — Harvey S. Rosen, Princeton University, former chairman of the President's Council of Economic Advisers, and author of *Public Finance*

William J. Congdon is a research director in the Brookings Institution's Economic Studies program, where he studies how best to apply behavioral economics to public policy. Jeffrey R. Kling is the associate director for economic analysis at the Congressional Budget Office, where he contributes to all aspects of the agency's analytic work. He is a former deputy director of Economic Studies at Brookings. Sendhil Mullainathan is a professor of economics at Harvard University and a director of ideas42, a non-profit that applies behavioral science to social problems. He previously taught at the Massachusetts Institute of Technology, and in 2002 he was awarded a MacArthur fellowship.

There is much to like about this book. It attempts to use the insights of behavioral economics to

improve the field of public finance. Behavioral economics presents people as they really are, with all their flaws. This is in sharp contrast to standard neoclassical economics that assumes that people are rational and self-disciplined. The authors first present the basic findings of behavioral economics: people have limited capacity to calculate, they have biases in their thinking that systematically lead to incorrect decisions, they have bounded self-control, and sometimes they care about others. The authors then explain how these things alter the standard analysis of market failures due to asymmetric information, externalities, and public goods. They also address poverty and conclude with a discussion of taxation. For the most part they provide excellent insights into how to improve policy. If one studies how people actually behave, one has a better chance of achieving one's policy goals. Economists and policy makers should both read this book. So then why only three stars? The answer is that the book is a chore to read, and it did not have to be that way. It is standard academic prose. To cite just one example, rather than say, "People have selective memories," they actually write, "There are systematic deviations between experienced well-being and recalled well-being." Worse yet, they repeat themselves far too much. The authors have important things to say. But if they want to reach a broad audience, they should read McCloskey's little book "Economical Writing." Clear prose will earn them a bigger audience.

Horrible writing...I can't really say how good the textbook was because I could barely make it through the paragraphs. I had to keep going back to. Re read what I just went over. The response in my class was negative towards this book

Oh my god how many commas can you use in one sentence. Very hard to read

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