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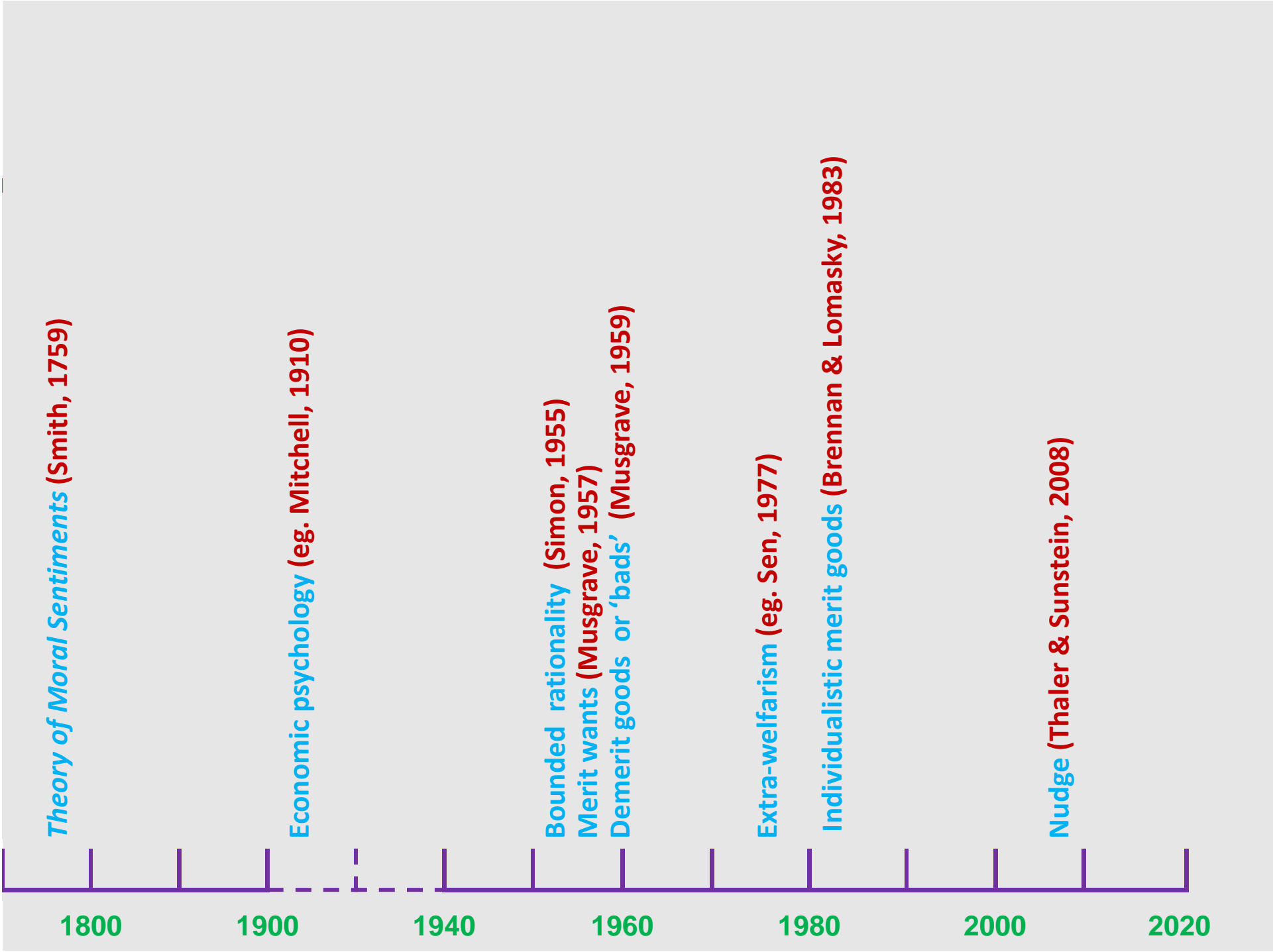
Business and Economics

Centre for Health Economics



A/PROF DUNCAN MORTIMER

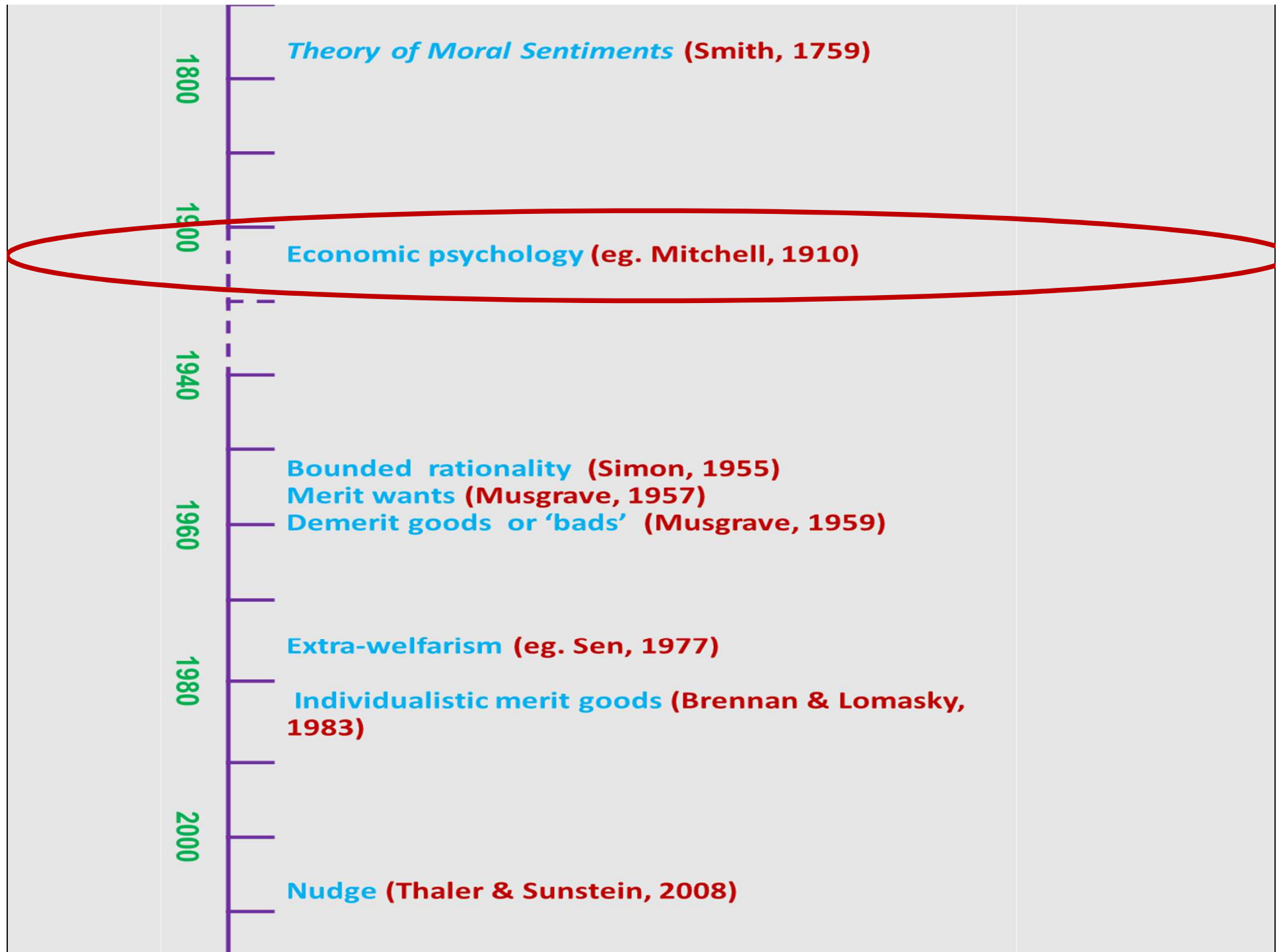
Economics,
behavioural economics
& nudge.



“Adam Smith, behavioural economist” (Ashraf et al, 2005)

“Smith (1759) argued that behaviour was determined by the struggle between ...the ‘passions’ and the ‘impartial spectator’. The passions included drives such as hunger and sex, emotions such as fear and anger.

Smith viewed behaviour as under the direct control of the passions, but believed that people could override passion-driven behaviour by viewing their own behaviour from the perspective of an outsider” (Ashraf et al, 2005 p131).



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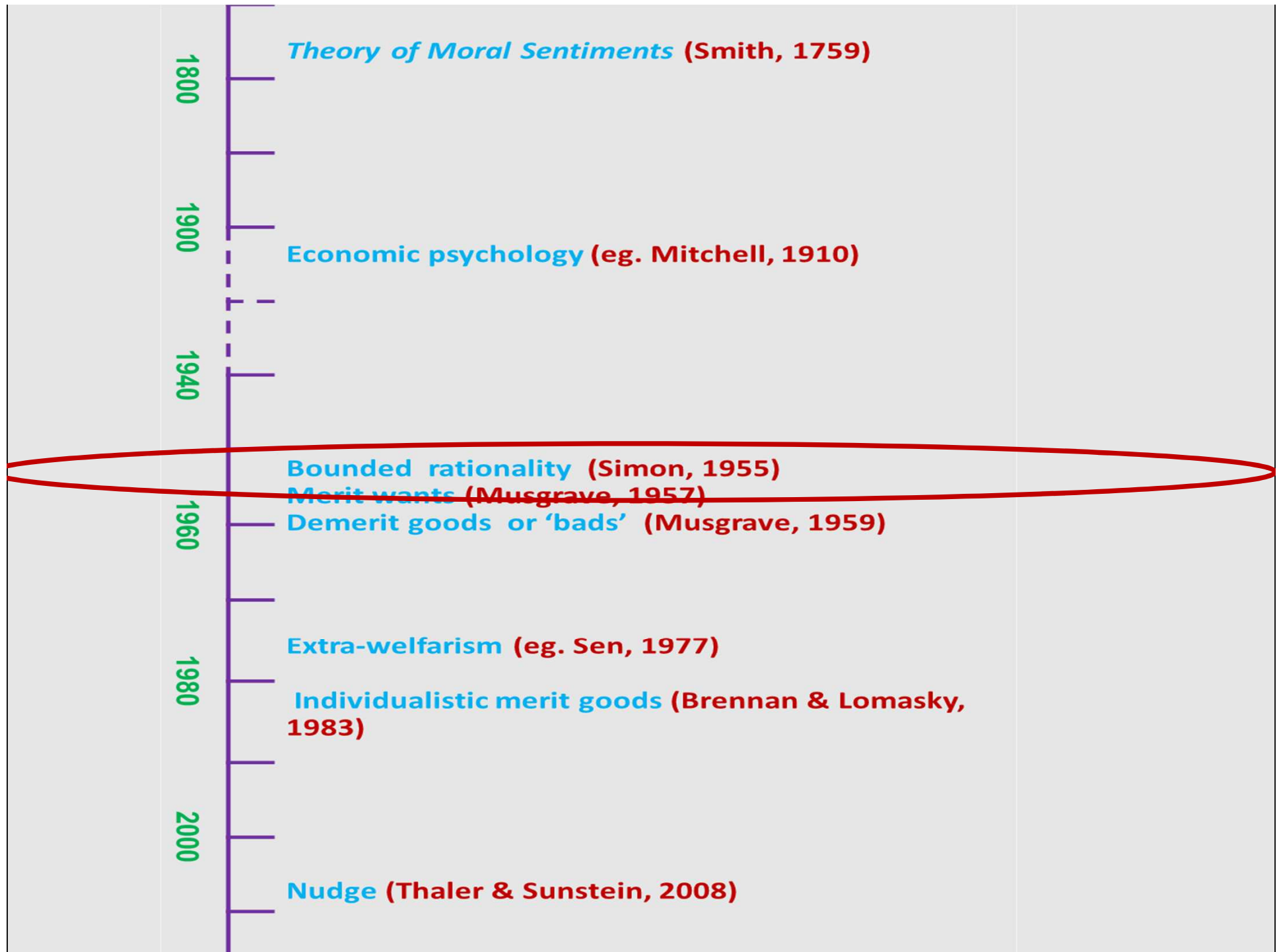
FEBRUARY—1910

NUMBER 2

THE RATIONALITY OF ECONOMIC ACTIVITY. I

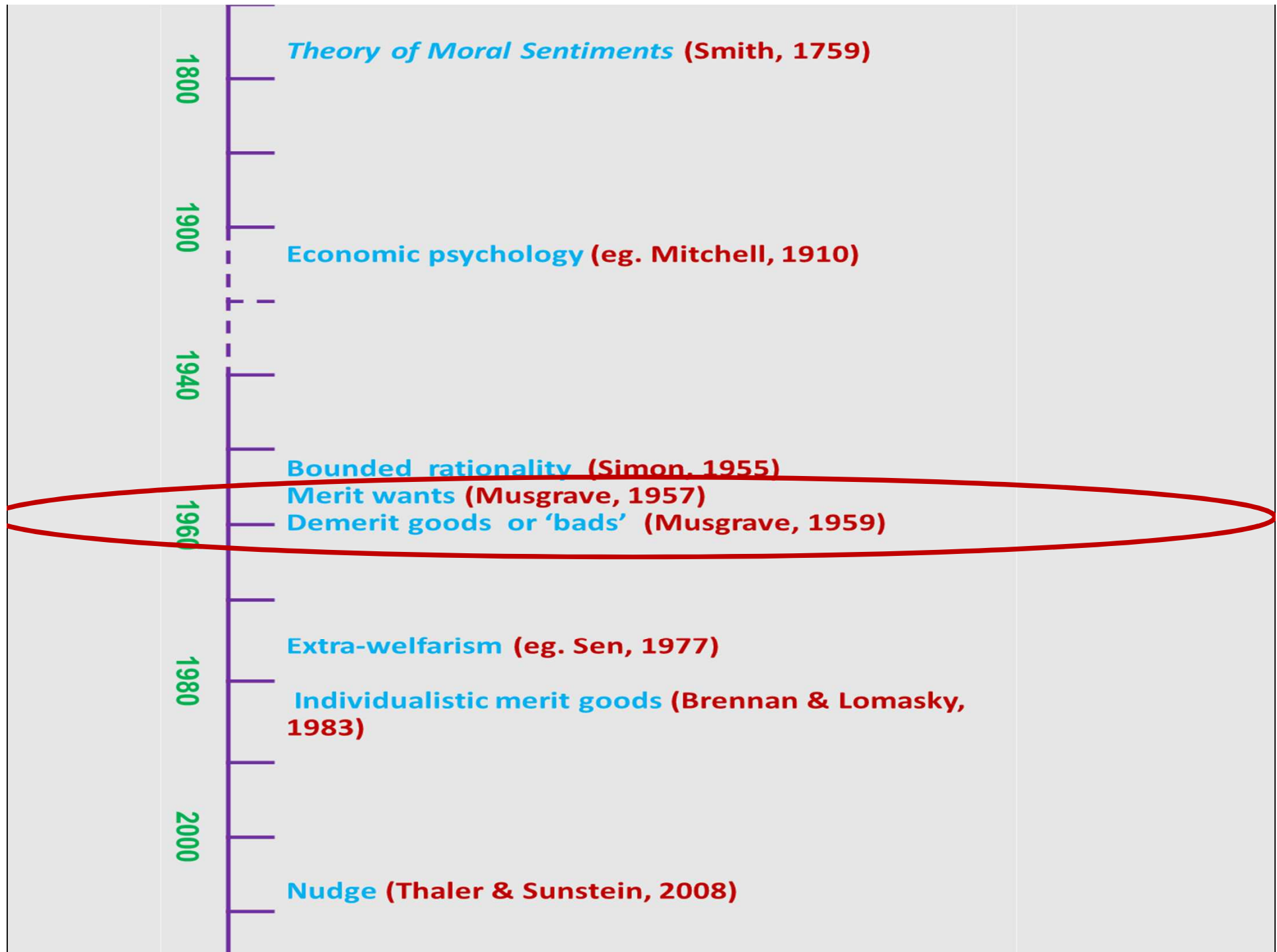
Few economists have regarded the study of psychology as a necessary part of the equipment for their work. Certain psychological notions, it is true, have always figured among the assumptions of the science; for serious discussion of any phase of human activity involves some concept of human nature. But during the formulative stage of economic theory all such concepts lay hidden among the tacit preconceptions upon which inquiry proceeded uncritically. When economists did become definitely conscious of what they had been assuming concerning human nature, it might have been expected that they would apply to psychologists to gain a knowledge of the mind and its modes of operation. On the contrary, they adopted the practice of formulating for themselves "a few principles of human nature," proven by past experience to be serviceable for the ends of economic inquiry. Rather disingenuously, they spoke of these principles as "borrowed from psychology," and for proofs referred their readers to the latter subject at large.

On their side, psychologists have shown a similar lack of interest in what economists were doing. They have had their own technical interests, their own new methods to apply, their own new view-points to develop. Until the recent rise of functional psychology their problems and theories have had little in common with the problems and theories of men engaged in studying phases of social activity. Their work offered little incentive



Bounded rationality & satisficing

“...if all alternatives are not be examined, some criterion must be used to determine that an adequate solution has been found. The Scottish word ‘satisficing’ has been revived to denote decision making that sets an aspiration level, searches (only) until an alternative is found that is satisfactory, and selects that alternative” (Simon, 1972).



(de)Merit goods

“....the concept of merit wants is put forward to epitomize a further range of cases where individual preferences expressed in a market setting may nevertheless require correction.

...distinction between social wants ‘where corrective policy is required in order to secure an allocation that is in line with consumer preferences’ and merit wants ‘where the reason for budgetary action is to correct individual choices’ (Musgrave, 1959 p. 9)” (Head, 1991 p. 229).

Individual welfare \neq individual preference

Head (1991): divergence between choice and welfare might arise due to ignorance and uncertainty, problems of impulsiveness and weakness of will, or due to “myopia or a failure to recognize the multi-period character and future implications of certain choices” (p. 237).

Ng (1983): “revealed preferences might differ from true welfare due to ignorance and imperfect foresight, rigid adherence to some habit or principle inconsistent with welfare maximisation, or due to paralysing fear or overwhelming temptation” (p10).

Consumers might make errors when they weigh the costs and benefits of some consumption bundles.

Consumer sovereignty

“...individuals are themselves the best – some might say ‘the only’ – judges of what contributes most to their utility and how much that contribution is” (Brouwer et al, 2008 p327).

“Every buyer determines to some degree the direction of industry. The market is a democracy where every penny gives a right of vote.” (Persky, 1993 p185 citing Fetter, 1903).

Consumer sovereignty & WARP

Weak Axiom of Revealed Preference (WARP): If A, B feasible and A chosen, then at any prices and income where A, B are feasible, the consumer will choose A over B.

WARP says two things:

1. **People choose what they prefer and so should never willingly choose a (divisible) consumption bundle that includes a 'bad'.**
2. Preferences are consistent. Therefore, a single observed choice reveals a stable preference.

Normative authority of WTP?

“....amongst the decisions to be taken is one about whose values are to be used to underpin utility and other preference- or value-based estimates of benefit and costs...

...in extra-welfarist economics any number of stakeholders might be regarded as appropriate sources of different values for different entities and how they ought to be traded off against one another and compared interpersonally...

...under extra-welfarism, policy makers become one important potential source of values” (Brouwer et al, 2008)

1800

Theory of Moral Sentiments (Smith, 1759)

1900

Economic psychology (eg. Mitchell, 1910)

1940

1960

Bounded rationality (Simon, 1955)

Merit wants (Musgrave, 1957)

Demerit goods or 'bads' (Musgrave, 1959)

1980

Extra-welfarism (eg. Sen, 1977)

Individualistic merit goods (Brennan & Lomasky, 1983)

2000

Nudge (Thaler & Sunstein, 2008)



Table 1

Summary of four main and related differences between the welfarist and extra-welfarist approaches

	Under welfarist economics	Under extra-welfarism
Relevant outcomes	Only individual utility, normally taken to represent preference orderings. Social welfare is a function of individual welfares	May include individual utility as well as extra measures and indicators of well-being. In health policy, common outcomes will include health or health gain and the distribution of health or health gain, but may include other measures like patient satisfaction or caregiver burden. The selection of relevant outcomes is an important element in extra-welfarist evaluation and is context dependent and seems not for economists to decide (rather for decision-makers with authority). Some outcome measures may be based on preference measurement, when this is deemed a useful way to measure characteristics of interest
Source of valuation of relevant outcomes	As a rule the affected individual	Might be the affected individual, but could also be an expert or a representative sample of the general public or an authoritative decision-maker
Weighting of relevant outcomes	Sometimes permitted in a social welfare function, where the weights normally pertain to the distribution of individual utilities. Unclear whether such weights still classify as utility information	Allowed and often considered important as means of incorporating equity and other considerations. Weights may be based upon a variety of ethical considerations including wealth, need and desert and can relate to the variety of relevant outcomes considered important (e.g. capabilities)
Interpersonal comparability of relevant outcomes	Although some theoretical approaches allow it (e.g. in a social welfare function), especially in applied work, normally considered impossible in the relevant evaluative space, i.e. individual utilities	Explicitly allowed in the relevant outcomes, though normally not in terms of individual utility, but rather in terms of capabilities and characteristics like health, handicap, ability to cope, schooling, ability to exercise discretion

Govt Intervention?

“It is one thing to argue that individuals are not perfect judges of their own interests, and another entirely to argue that they are not the best judges.

...even if in certain cases there exists some person who better knows what is good for the individual than he does himself, there is an additional step in arguing that a ‘superior’ choice will emerge from political processes” (Brennan & Lomasky, 1983 p. 184).

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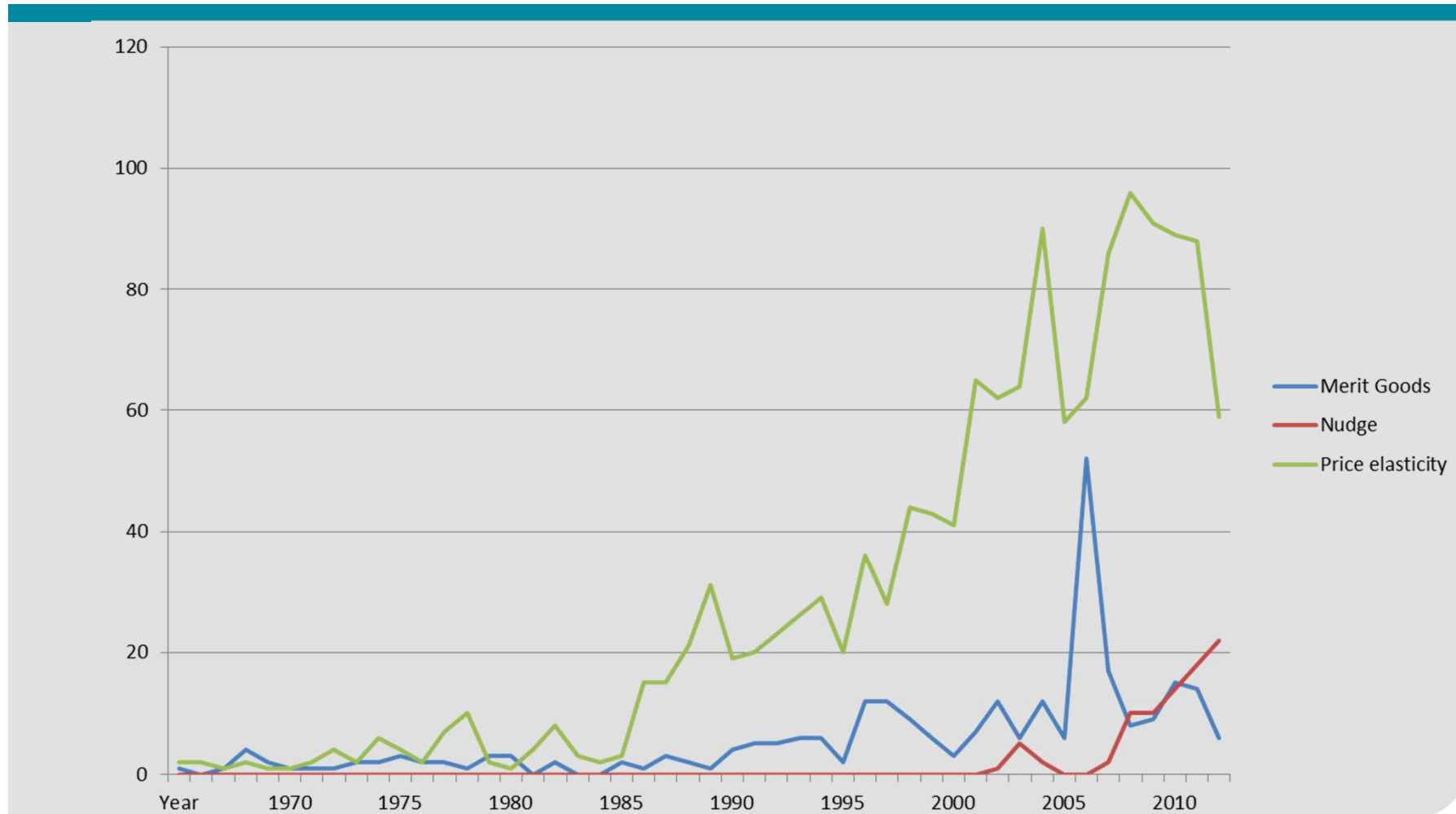
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Traction & progress



Traction & progress


“Those against the use of the divergence between preference and welfare as a justification for illiberal policies argue:

- that the undesirable side-effects of such policies overbalance their benefits; or
- that the divergence is insignificant in practice” (Ng, 1983 p12).

What would you choose from the following options?

Information	An oral conventional medicine available without prescription	An oral complementary medicine available without prescription
This product was recommended by:	A pharmacist	Staff from the local pharmacy
The person who recommended it:	Didn't mention or know anything about side-effects	Didn't mention or know anything about side-effects
I know I can buy this product:	At a pharmacy	At a pharmacy

Product labels:

RHEUMAZIDE	CAMFlower Joint Relief Formula 						
Provides temporary effective relief of joint pain.	Provides temporary effective relief of joint pain.						
Dosage: Take 2 tablets in the morning with food.	Dosage: Take 2 tablets in the morning with food.						
CAUTION: This product may interact with certain medications, such as medicines for high blood pressure, heart problems or depression.	CAUTION: This product may interact with certain medications, such as medicines for high blood pressure, heart problems or depression.						
	WARNING: Do not use if pregnant or breastfeeding. If pain persists, see your doctor.						
	<i>This product HAS been evaluated by Australian Health Authorities for efficacy.</i>						
Government Authority Rating:	Government Authority Rating:						
Likely effective for joint pain	Likely effective for joint pain						
May cause side-effects*	May cause side-effects*						
May interact with other medicines*	May interact with other medicines*						
<table border="1"> <tr> <td>HIGH CAUTION</td> <td>MODERATE CAUTION</td> <td>LOW CAUTION</td> </tr> </table>	HIGH CAUTION	MODERATE CAUTION	LOW CAUTION	<table border="1"> <tr> <td>HIGH CAUTION</td> <td>MODERATE CAUTION</td> <td>LOW CAUTION</td> </tr> </table>	HIGH CAUTION	MODERATE CAUTION	LOW CAUTION
HIGH CAUTION	MODERATE CAUTION	LOW CAUTION					
HIGH CAUTION	MODERATE CAUTION	LOW CAUTION					
*For more information visit www.medicinescentre.gov.au or call 1900 123 123	*For more information visit www.medicinescentre.gov.au or call 1900 123 123						

\$34.35
One month supply

\$33.20
One month supply

I would choose:
(please tick)

the **conventional** medicine

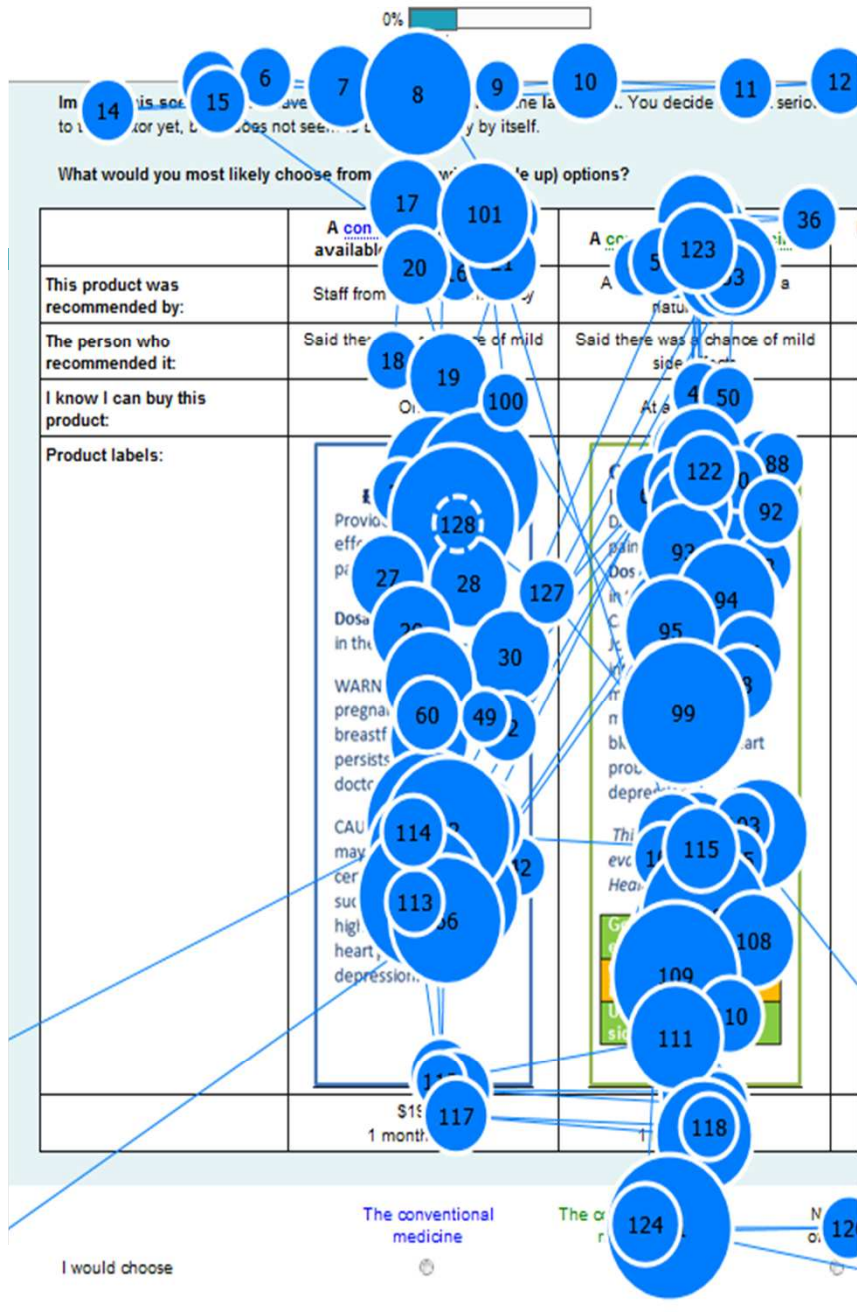
the **complementary** medicine

something else

Just add information

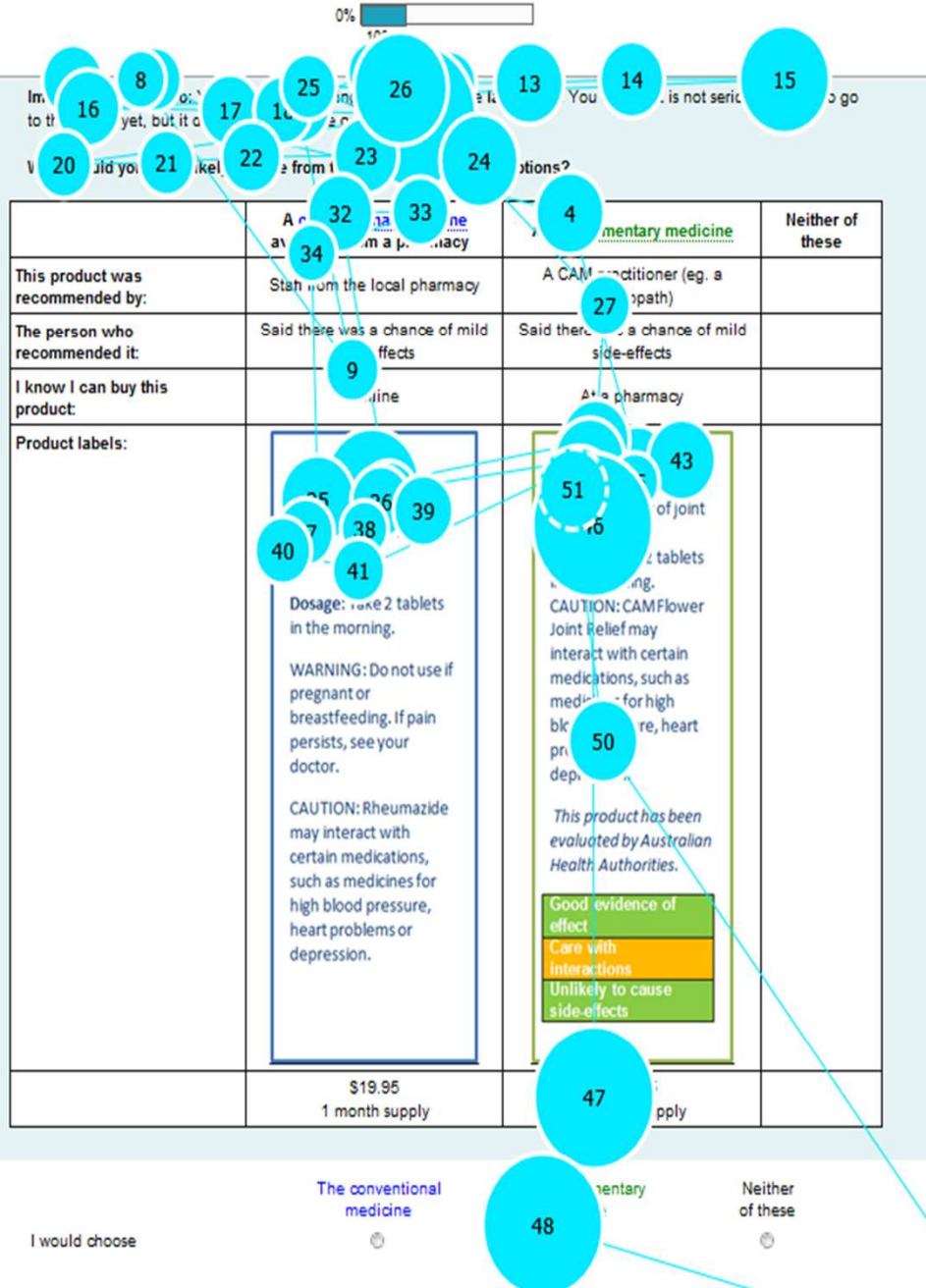
Question	Number of attributes presented	Health condition	<u>Conventional choice</u> # participants (%)	<u>CAM choice</u> # participants (%)
1	3	joint	28 (88)	29 (91)
2	3	insomnia	24 (75)	20 (63)
3	4	joint	26 (81)	24 (75)
4	4	insomnia	24 (75)	18 (56)
5	5	joint	13 (41)	14 (44)
6	6	insomnia	13 (41)	12 (38)
7	8	joint	13 (41)	12 (38)
8	8	insomnia	15 (47)	14 (44)

Table 1: Number of participants who attended to every attribute within a choice (N=32)



Resume later

by



Resume later

Govt Intervention?

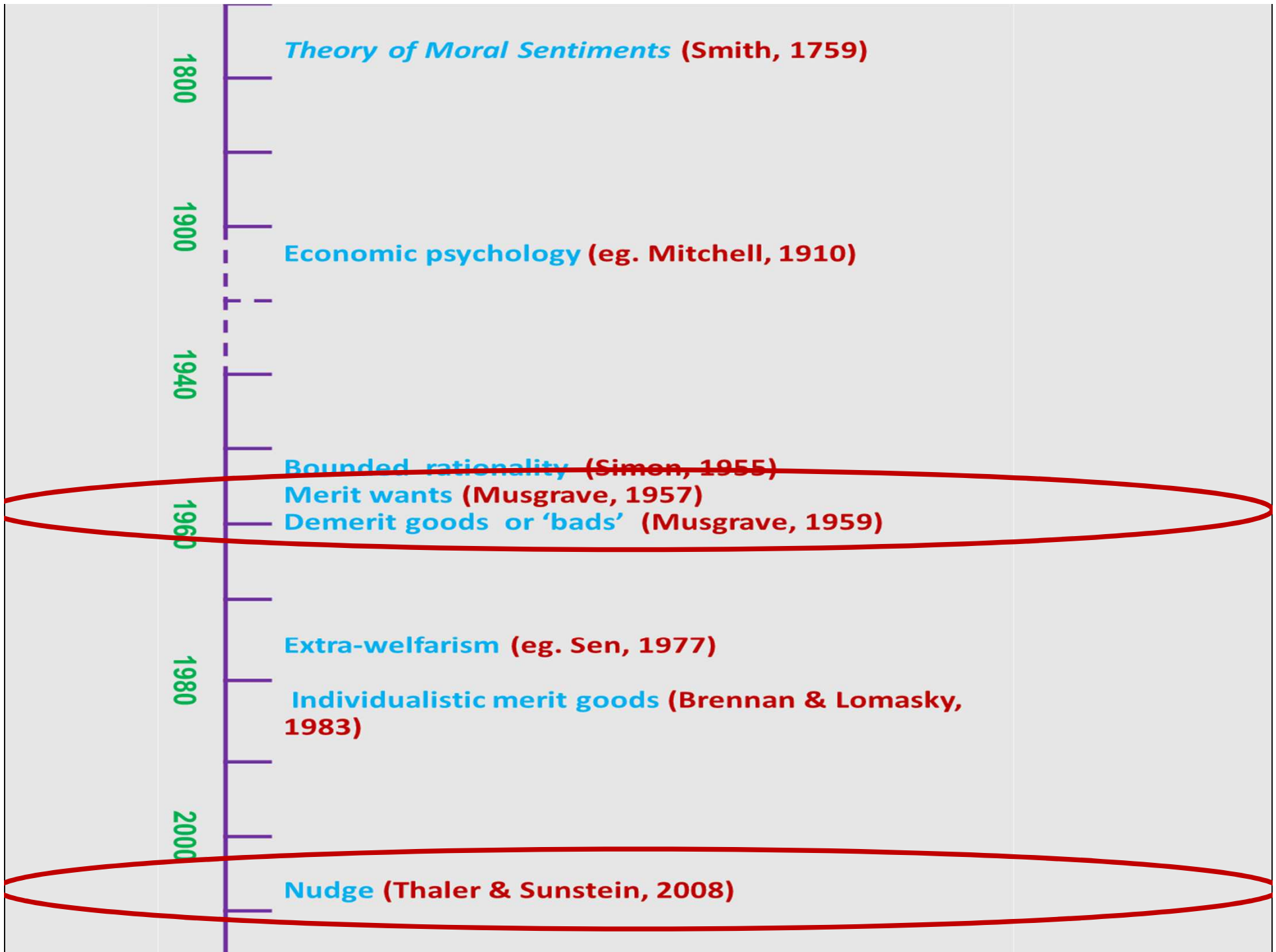
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By Chao Zhou and Yuting Zhang

The Vast Majority Of Medicare Part D Beneficiaries Still Don't Choose The Cheapest Plans That Meet Their Medication Needs

ABSTRACT When the Medicare Part D prescription drug benefit began in 2006, a primary concern for some policy makers was whether seniors would be able to make smart choices from among the dozens of competing plans. Using 2009 Part D data, we found that only 5.2 percent of beneficiaries chose the cheapest plan. Nationwide, beneficiaries on average spent \$368 more annually than they would have spent had they purchased the cheapest plan available in their region, given their medication needs. More than a fifth of beneficiaries spent at least \$500 a year more than they needed to. Beneficiaries often overprotected themselves by paying higher premiums for plan features that they did not need, such as generic drug coverage in the coverage gap. Our findings suggest that beneficiaries need more targeted assistance from the government to help them choose plans, such as customized communications about the most cost-effective plans that would cover their medication needs.

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Foundation, Inc.

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Yuting Zhang is an assistant professor of health economics and director of the Pharmaceutical Economics Research Group, University of Pittsburgh.

12 September 2013, 2.39pm AEST

Pre-committing to a grocery list may help in the battle of the bulge

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