Book Review: Misbehaving: The Making of Behavioural Economics

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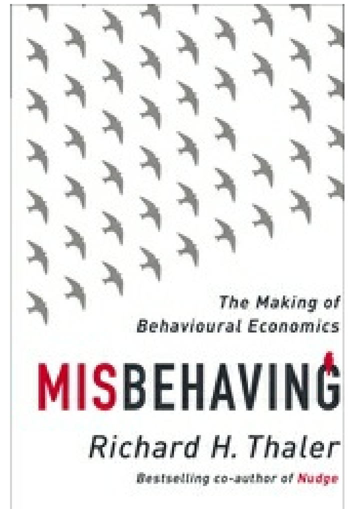
*Reviewer **Adam Oliver** finds that Richard Thaler's new book, **Misbehaving: The Making of Behavioural Economics**, covers the core concepts of behavioural economics, but finds that this book is more a 'personal intellectual history, supplemented by stories, anecdotes and occasional reposts to past combatants' that misses two important issues 'relating to suggestions for the future development of behavioural economics'.*



Misbehaving: The Making of Behavioural Economics. Richard H. Thaler. Penguin Random House, 2015.

I begin this review of Richard Thaler's new book with a gripe, or rather a double gripe, about its title. Thaler, arguably the world's leading behavioural economist and one of its early pioneers, perhaps feels as though his career has been a 40-year odyssey of misbehaving in relation to the mainstream economics community, but given that he has devoted himself to the study of how people actually make, rather than ought to make, decisions, one could make a case for deleting 'Mis' from the front of the title. And I would question whether this is a book that outlines the making of behavioural economics. Rather, it is a personal intellectual history, supplemented by stories, anecdotes and occasional reposts to past combatants. It is an American (and American-based Israeli) centric book. There is no mention of Maurice Allais, for instance, who arguably designed the first empirical experiments in behavioural economics. The important work produced by Robert Sugden and Graham Loomes and their followers from the 1980s onwards is not noted, and there is very little mention of Ernst Fehr and others from continental Europe. A telling remark is given when Thaler writes that, "In the late 1980s, there were really just three people beside me who thought of themselves as behavioural economists. One was George Loewenstein … Another was Robert Shiller … and the third was Colin Camerer", a sentence that might cause many British behavioural economists to choke into their teacups.

But perhaps I am being churlish since the title was no doubt chosen with an eye on marketing, and the material covered is substantive. As noted above, from the mid-1970s onwards, Thaler has been at the forefront of these developments, but, in common with most behavioural economists, retains expected utility maximisation as the normative ideal; he states, for instance, that, "Expected utility theory is the right way to make decisions". I wonder. It may after all often be the case that people deliberately prefer to trade off expected utility to satisfy other values. I committed myself to writing this review, for instance, and thus I feel honour bound. I want to do it, even though today is unusually warm (for England), and at this point in time I expect I would gain more utility by going to Greenwich Park to eat an ice-cream.

The bulk of *Misbehaving* covers many aspects of behavioural economics that Thaler was personally involved in uncovering, including endowment effects (i.e. people value something substantially more when they own it than before they own it), mental accounting (i.e. people treat money as non-fungible – for example, they pay only the smallest required payment off their credit card bill while having sufficient savings to pay off the whole bill, and are thus paying interest on debt that is many multiples higher than the interest earned on their savings), and issues of self-control, which include the very heavy emphasis that people place on the immediate moment (i.e. present bias). Thaler also discusses the concept of transaction utility; that is, the utility that someone enjoys when they experience a good deal and the pain that they suffer when they are ripped off, which goes beyond the standard economic assumption that only acquisition utility matters.

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To my mind, there are two important issues relating to suggestions for the future development of behavioural economics that are missing from the book. The first is that a theory of meaning for the behavioural economic phenomena unearthed over the last several decades has not been developed sufficiently. The phenomena, some of which have been observed in other species, no doubt have evolutionary explanations. If survival in the moment rather than maximisation over a lifetime is the objective, then present bias and loss aversion are not so difficult to comprehend. Thaler agrees that evolution was probably the cause behind the phenomena, but sees little import for these explanations in economic analyses: "…there was no doubt that many of the aspects of human behavior…had evolutionary roots. But…accepting the theory of evolution as true does not mean that it needs to feature prominently in an economic analysis. We know people are loss averse; we don't need to know whether it has an evolutionary explanation." Perhaps Thaler's ambivalence to a discourse on explanation is grounded in his faith in the normative weight of expected utility theory, but an analysis of the possible causes of the behavioural economic findings might lead us to conclude not only that people often fail to behave according to the axioms of economic rationality, but that in certain circumstances they ought not necessarily comply with these axioms either.

Second, the ethics of using behavioural economics in policy formation warrants further and closer scrutiny. Thaler, clearly stung by charges of manipulation, states at several points in his book that most nudges are visible, but this defence misses the point. They may be physically visible, but the reasons why nudges are being used are not always, or indeed often, transparent, and thus the charge that they are somewhat circumnavigating deliberative scrutiny is not one that ought to be ignored. Following sufficient ethical scrutiny many of us may decide that nudges (to name but one form of behavioural economic-informed policy) are generally, on balance, acceptable, but that debate has yet to be had.

Popular science books implicitly use a behavioural economic phenomenon – present bias – to introduce areas that might otherwise be too arduous for most people to study. That is, they aim to make ideas and concepts fun to read. A downside is that they sometimes trivialise and misrepresent important scholarly fields. Richard Thaler's *Misbehaving* is guilty of neither of these latter charges, although, like most of us and certainly, as he points out, like most economists, he might be a little guilty of being resistant to challenges to his own ideas. This is perhaps unavoidable. It is human nature, an endowment effect of sorts.

Nonetheless, Richard Thaler has done more to popularise behavioural economics in the policy discourse than perhaps anyone else. For anyone who wishes not just to be entertained frivolously, but is serious about learning about the core concepts in the behavioural economic field, then *Misbehaving*, read together with Daniel Kahneman's *Thinking Fast and Slow*, is a good place to start.

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Author Richard Thaler gave a public lecture about his book at the LSE; you can listen here.