

*Course syllabus*

# **Ekonomiskt och finansiellt beslutsfattande**

## **Economic and Financial Decision- making**

**EXTN80, 7,5 credits, A (Second Cycle)**

**Valid for:** 2023/24

**Faculty:** Faculty of Engineering, LTH

**Decided by:** PLED I

**Date of Decision:** 2023-04-14

### **General Information**

**Elective for:** I5, Pi4

**Language of instruction:** The course will be given in English

### **Aim**

The goal for education at this level is to instil a deeper understanding of economic theory and the application of scientific methods of analysis. The objective is also to instil an ability to handle empirical material in an independent and critical manner. The more specific aims of this course are to enhance students' understanding of situations where individuals, firms and organizations operate in environments characterized by risk, uncertainty and imperfect information.

### **Learning outcomes**

*Knowledge and understanding*

For a passing grade the student must

Students shall have a knowledge and understanding of:

- axiomatic theories of individual choice under risk and uncertainty,
- reference dependent utility theories,
- theories of inter-temporal decision making,
- how these theories contribute to the analysis of a wide range of fundamental problems in economics and finance

- psychological phenomena important for economic and financial decision making.

#### *Competences and skills*

For a passing grade the student must

Students shall have the ability to independently:

- apply models of decision making to problems in a wide range of economic and financial contexts,
- present verbal, graphical and mathematical representations of the theoretical models and communicate to a layman how the models can explain various economic phenomena, for example the demand for insurance and investor behaviour.

#### *Judgement and approach*

For a passing grade the student must

Students shall have the ability to interpret empirical results through the lens of the classical decision theories as well as the psychologically grounded alternative theories proposed by behavioural economics, and to apply these theories to design interventions to improve behavioural outcomes.

## **Contents**

A fundamental component in most economic analysis is a description of how individuals make decisions. The objective of the course is to introduce students to the study of economic and financial decision making. This will be done in two steps. First, we will review classical theories of rational economic and financial decision making and confront these theories with empirical evidence. Second, we will discuss alternative, more psychologically grounded, theories from behavioral economics that can better accommodate the empirical evidence.

The first part of this course will discuss how rational people should make simple decisions and form empirical judgments. This part also discusses the systematic ways in which real human beings deviate from these models in practice. A notable part of this discussion will focus on heuristics (simple decision rules) and the biases that result from relying on them. We will also cover mental accounting and more recent behavioral economic theories, as well as relevant empirical evidence.

The second part of this course will instead focus on decisions under risk and uncertainty. How should rational economic agents behave when facing risk or uncertain environments? How do they behave in practice? And what alternative models have behavioral economists developed to better explain the existing evidence? Large sections of this part will be about the rational benchmark of expected utility theory and the behavioral alternative of prospect theory, though we will discuss some other alternative models as well.

The last part of the course is devoted to the study of inter-temporal decision making. The course will cover the standard economic model based on exponential discounting, which assumes that behavior is time-consistent. However, there is empirical evidence that people sometimes behave in a time-inconsistent manner, postponing activities with immediate costs and being too eager on performing actions with immediate rewards. The course will review this evidence and discuss extensions of the standard model that can account for these phenomena.

Throughout the course, the theoretical discussions of decision making will be complemented with numerous economic and financial applications illustrating the underlying ideas and showing how they can be used in economic analysis.

## Examination details

**Grading scale:** TH - (U,3,4,5) - (Fail, Three, Four, Five)

**Assessment:** Examination consists of compulsory and voluntary assignments, compulsory participation in seminars, and a final written exam which takes place at the end of the course. There will be further opportunities for examination close to this date. Other forms of examination may be used to a limited extent. Points earned on the different parts of the examination are valid in the current term.

The examiner, in consultation with Disability Support Services, may deviate from the regular form of examination in order to provide a permanently disabled student with a form of examination equivalent to that of a student without a disability.

## Admission

**Admission requirements:**

- EXTA40 Introduction to Microeconomic Theory

**The number of participants is limited to:** No

**The course overlaps following course/s:** NEKM61, NEKN22, TEK090

## Reading list

- Angner, Erik: A Course in Behavioral Economics, second or third edition. Palgrave MacMillan, 2020.
- Supplementary material.

## Contact and other information

**Course coordinator:** Roel van Veldhuizen, [roel.van\\_veldhuizen@nek.lu.se](mailto:roel.van_veldhuizen@nek.lu.se)

**Course homepage:** <http://www.nek.lu.se>

**Further information:** For more information, please contact the Department of Economics.