

Economic Brief

Behavioural economics and experimental economics

Interventions in the economy can be strengthened by the use of ex-ante road-testing. Further, interventions may need to be tweaked after implementation in order to improve policy performance. Behavioural economics, and the use of experimental economics, can provide invaluable information on the expected outcomes of policy interventions prior to rollout, and, after the intervention is applied, to improve desired outcomes and to correct unexpected policy outcomes.

The method explicitly factors in the range of competing interests that parties have and the sometimes unpredictable nature of human behaviour. It couples intense theoretical research with actual testing or 'experiments' and as a result provides meaningful insights into policy design. Participants in the experiments receive actual financial payments and incur real losses which mimic the payoffs that parties would face under different policy scenarios in the field. By the use of financial incentives, the method mitigates the problem of people saying they will behave in certain way but when faced with a real-life trade-offs behave differently.

Economic experiments take place under controlled 'laboratory' conditions which has benefits in terms of,

- Being able to vary some conditions while holding others constant in order to isolate the specific influence of particular features of an intervention
- Comparing across alternative interventions
- Provision of quantitative data for analysis and decision making akin to the physical sciences
- Facilitate evidence based decision making by repeating experiments and checking the robustness of results



These features are important as traditionally, as economics is a social science, it has not been possible to conduct tests of outcomes ahead of time, and it is infeasible, given cost, to undertake policy actions across the economy simply to better understand the outcomes.

London Economics brings a unique approach to the use of behavioural and experimental economics as our economists have successfully applied these methods to policy design internationally. Such examples include:

- evaluation of consumer policy interventions and remedies currently for the Office of Fair Trading in the UK
- pollution policy for both air and water for the Australian National Government
- habitat offset schemes and biodiversity and landscape maintenance incentives for the Victorian Government, Australia
- urban development impacts on the environment and local amenities for water and sewerage firms in Australia

We have strong relationships with leading researchers in the field. These specialists act as an international advisory panel, and work with our economists to deliver innovative solutions across the economy. Our specialists include, Professor Steffen Huck, Head of Economics Department at University College London, Professor Charles Plott of the Californian Institute of Technology USA, and Associate Professor Lata Gangadharan at the University of Melbourne Australia.

For further information on behavioural and experimental economics please contact Dr Charlotte Duke cduke@londecon.co.uk