

## Chapter 15

# Behavioral Economics: New Dimension in Understanding the Real Economic Behavior

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### ABSTRACT

*The idea of the significance of the psychological dimension of human behavior is not new and has existed in the social sciences since ancient times. Accordingly, there is an endeavor to place economic analysis on the foundations of psychological research, which takes its form of expression in economic theory through the affirmation of behavioral economics. The aim of this chapter is to critically analyze various normative research programs in behavioral economics and to consider the importance of alternative concepts, models, and theories from the point of view of improving understanding of real economic and social behavior. The particular value of this chapter lies in affirming the importance of a program of behavioral economics known as new paternalism, which is based on challenging the concept of maximizing rationality and opens a new dimension of understanding the justification of state interference in the sphere of economy and society.*

### INTRODUCTION

Economic theory has traditionally analyzed the world inhabited by calculated, insensitive maximizers called *homo economicus*. In a sense, economic theory defines itself as explicitly “anti-behavioral” Virtually, all behaviors studied by cognitive and social psychologists are either ignored or excluded in a rational model. *Homo economicus* or non-behavioral actor is defended on many grounds (Askari, & Eshaghi Gordji, 2018). Some have argued that the rational model is “correct”; most others have simply argued that this model is easier to formalize and is practically relevant (Thaler, 1980). Behavioral eco-

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conomic theory considers that the claims mentioned above are not true. Behavioral economics explores the constraints of human rationality. The findings of this area of economic theory are not related only to market decisions, but to, almost, all areas of human decision-making: politics, medicine, the tax system, and daily life. It is a combination of economics and psychology that explains in very understandable and attractive way why humans are not rational beings and why they often do own harm? Further work about behavioral economics has clearly demonstrated that psychological ideas could be formalized into an alternative model and used to form predictions that could be applied in real economic environment (Krstić & Đekić, 2018).

The aim of this chapter is to critically analyze different normative research programs in behavioral economics and to consider the importance of alternative concepts, models and theories from the point of view of improving understanding of real economic and social behavior. The chapter itself consists of five interconnected parts. In the introduction, the authors present basic information about behavioral decision theory (or behavioral economics) as an alternative to classical or orthodox economic theory. Then the authors give a detailed overview of some significant theorists whose work has left an indelible mark in this field. In the third, fourth and fifth parts of the paper, the authors describe the normative research programs that emerged within behavioral decision theory. The particular value of the chapter lies in affirming the importance of the normative program of behavioral economics known as “new paternalism”, that, on the basis of refuting the concept of “maximizing rationality”, “opens” a “new dimension” to understanding the justification of state intervention in the sphere of economy and society. In this regard, in this chapter, the authors will discuss on the need to apply new paternalism measures in order to moderate (reduce) the degree of the irrationality of citizens and economic entities in the Republic of Serbia and stimulate their action towards making better decisions on the use of restricted resources.

## **BACKGROUND**

In the theoretical literature, the emergence of new analytical direction, by which the name behavioral economics has become “domesticated” and “consolidated”, has the status of one of the most interesting and significant events in economic science in recent decades. The ideas and approaches developed within behavioral economics quickly gained “academic recognition”. This allowed behavioral theory to partly penetrate into the economic mainstream, which, among other things, led to certain changes and transformations of some of its segments and parts. In the continuation of this chapter, the authors present behavioral ideas of Adam Smith, Robert Maltus, John Stuart Mill, and other “giants” of economic science who, through their theoretical considerations, determined the “path” of developing the behavioral economics as we know it today.

In *The Theory of Moral Sentiments*, Adam Smith, before writing *The Wealth of Nations*, dealt in detail, with what would today be considered psychological problems (feelings, pleasure, human nature). Although skilled in that kind of analysis, he did not see reason for explicit exposure of his view of human nature in *The Wealth of Nations*. Indeed, the impression is that Adam Smith considers people as they are. He had, mainly, acquired knowledge of human nature in Scotland and assumed that there was one “Scot” in each individual. It is quite natural that he believes that the constant and consistent driving of a man to make his position better is understandable in itself. This premise about human nature is a key feature Smith’s “system of natural freedom” (Smith, 1998).

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