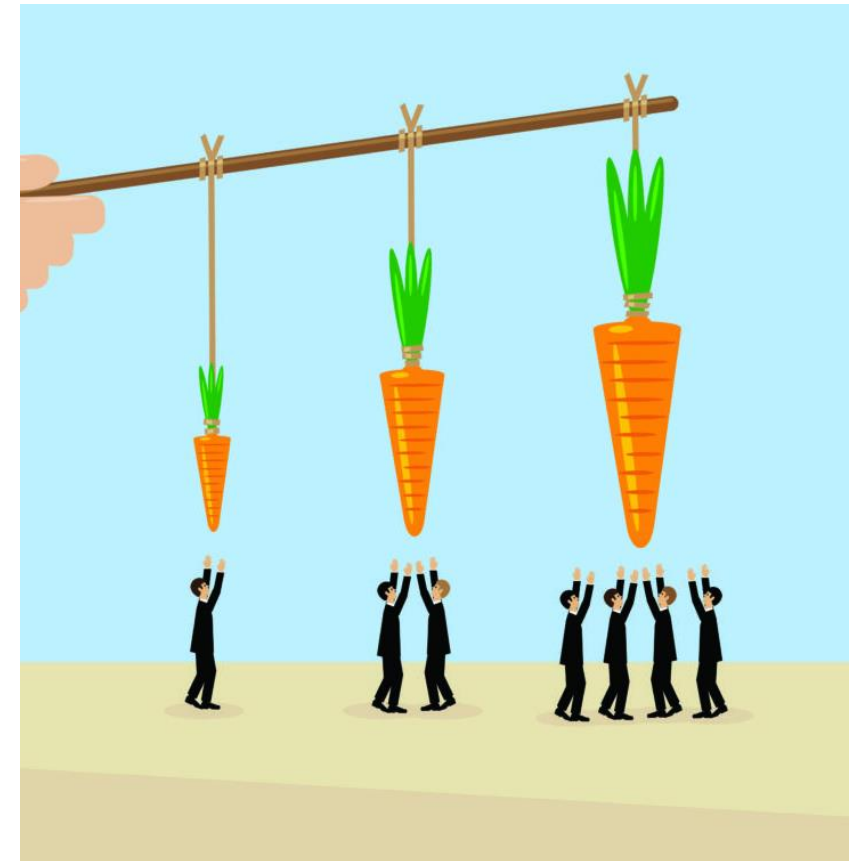# Incentives in Economics

Incentive

Incentive is something that motivates or drives one to do something or behave in a certain way

Applications:

- Behavioral Economics
- Policy making
- Decision making
- Business strategy
- Risk mitigation etc.

Cobra Bounty

- In colonial India, the British saw that there were too many Cobra's slithering around, so they decided to offer a bounty for cobra corpses

Cobra Bounty

- At first this seemed to work, but it just led to people setting up cobra farms, breeding them and turning them in for the bounties.

- Soon the British Officials figured it out

Cobra Bounty

- Britishers cancelled the bounty
- Cobra ranchers released their now worthless cobras
- Now there were even more Cobras in India than there had been before.

It does not matter what was intended, what matters is what happened in the end

Rat bounty in Vietnam

Day Care Centre

- A day care center in Israel was having a problem of parents showing up late to pick up their kids forcing the teacher/workers to have to stay longer than they wanted until all the parents arrived.

- So, they implemented a small late fee of like three dollars for anyone more than a few minutes late?

Day Care Centre

- After that late fee was implemented the number of late parents went up significantly
- This was a strange finding, so some researchers tested this with several daycare centers
- Outcomes were identical for all day care centers.
- What could be the reason?

Day Care Centre

- The contract of what it means to be late is completely changed

- Without the fee it's a game of morality, parent arriving late will only have to deal with feeling bad

- Once the fee is introduced now punishment is tied to money it takes away the guilty feeling for being late because you've paid for that time

- They'll accept the fee as a convenience since you paid for that guilt
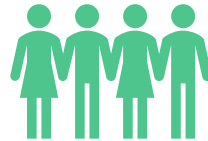

Fine for homework

Plastic Bag
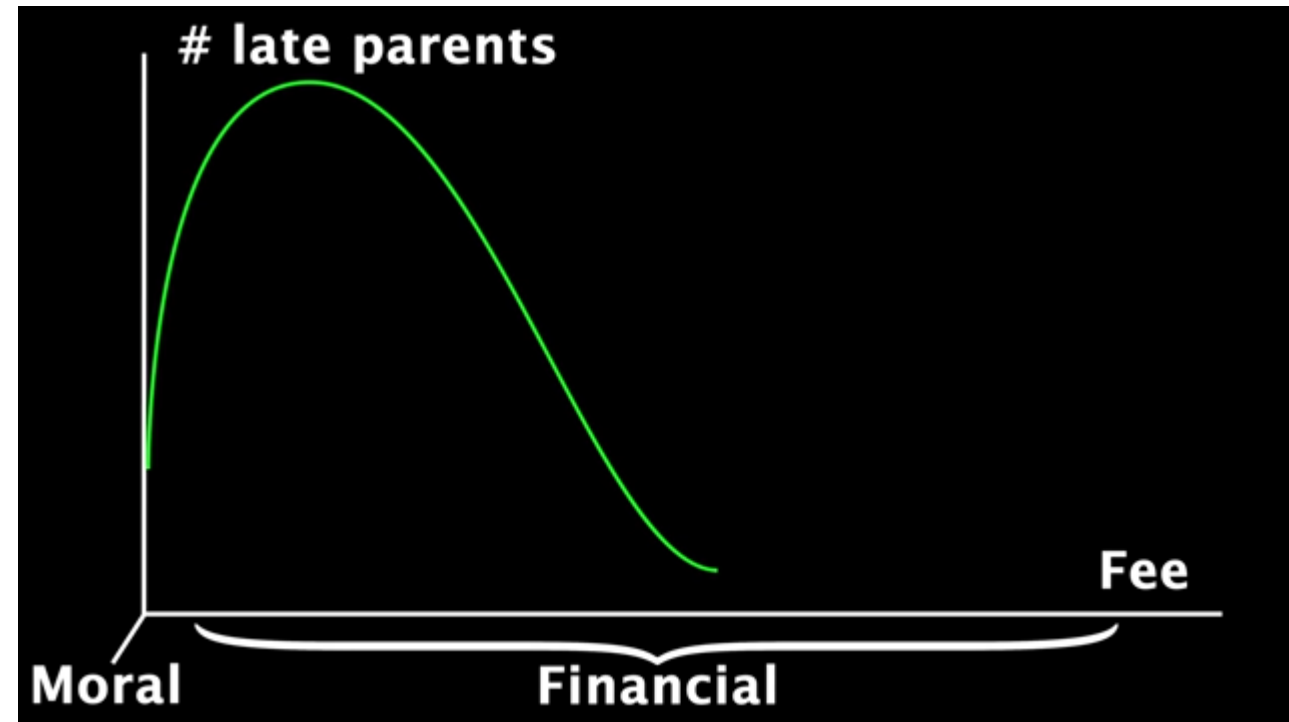
Types of Incentives
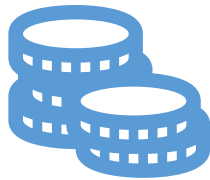
Economic

Money or Rewards

Social

Perception

Moral

Felt by oneself

Behavioral economists suggests that people are expected to act smartly but they rather act on emotions and ego
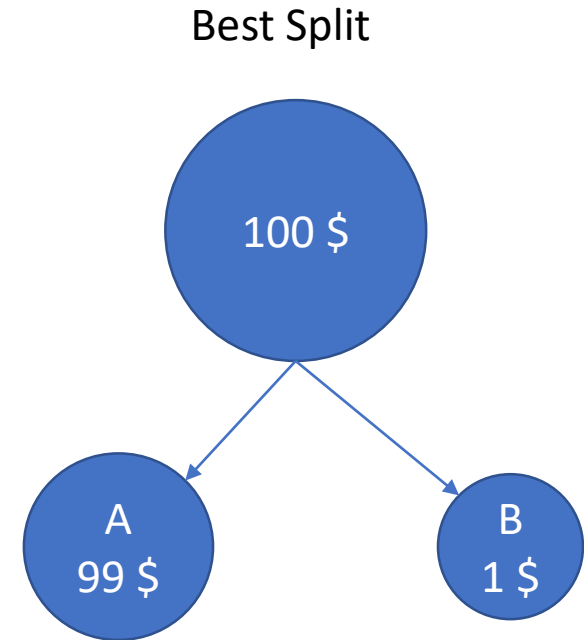
Game of Ultimatum

- 100$ to split

- Person A suggests the split
  - If person B agrees, they get the suggested amount
  - If person B rejects, both get nothing

Game of Ultimatum

Best Split

- Most logical scenario for B would be accept whatever A offers
- But in reality, people decline the offer unless it isn't somewhat fair to them.

100 $

A
99 $

B
1 $

Cancer Donations

Kids collecting donations split into three groups

- No Compensation was given(All Charitable)
- Kids received 1% of their total collections (not taken from the donations)
- Kids received 10% of their total donations(not taken from the donations)

Which group would raise the most money?

No Compensation

1% Compensation

10% Compensation

Cancer Donations

No Compensation

1% Compensation

10% Compensation

Cancer Donations

- Once anything at all is paid, the game changes from Morality and Altruism to Sales Gig
- Group 1 was driven by Morality and Altruism (Moral Incentive)
- 1% enough to feel like sales gig, but not enough to drive the cause.
- To change the game from morality or altruism to a financial one, better introduce significant financial incentive otherwise just don't introduce it at all (Social Incentive)

Charitable cause No Compensation

Sales Gig 1% Compensation

Sales Gig 10% Compensation

Blood Donation
TLH

ABS System

- ABS System didn't reduce number of road crashes significantly.
- People tend to drive more dangerously because of safety features **(Risk Compensation)**
- Safety system aren't ineffective. People response is wrong

Theft Insurance and Leniency
Helmet Wearers and Careless driving
Seatbelt

Cash for Grades

Students with good disciplinary record (Good Attendance, No Suspensions, No detentions etc.) but scoring C and D were chosen for the study

Students were divided into 3 categories
- Group 1- Given 40$ for scoring above C
- Group 2- Given 80$ for scoring above C
- Group 3- Given 20$ in advanced and if they score below C, they'll have to return amount

40$ for scoring > C

80$ for scoring > C

-20$ for soring < C

Cash for Grades

- Fear of Losing > Motivation to Win (Loss Aversion)
- Higher incentives made students push themselves harder in general

40$ for scoring > C

80$ for scoring > C

-20$ for soring < C

Employee Bonus
Plastic Bag

Cash for Grades

- Even after the rewards were stopped, the students kept performing better
- Academics is a long-term investment, and they were given rewards in short run
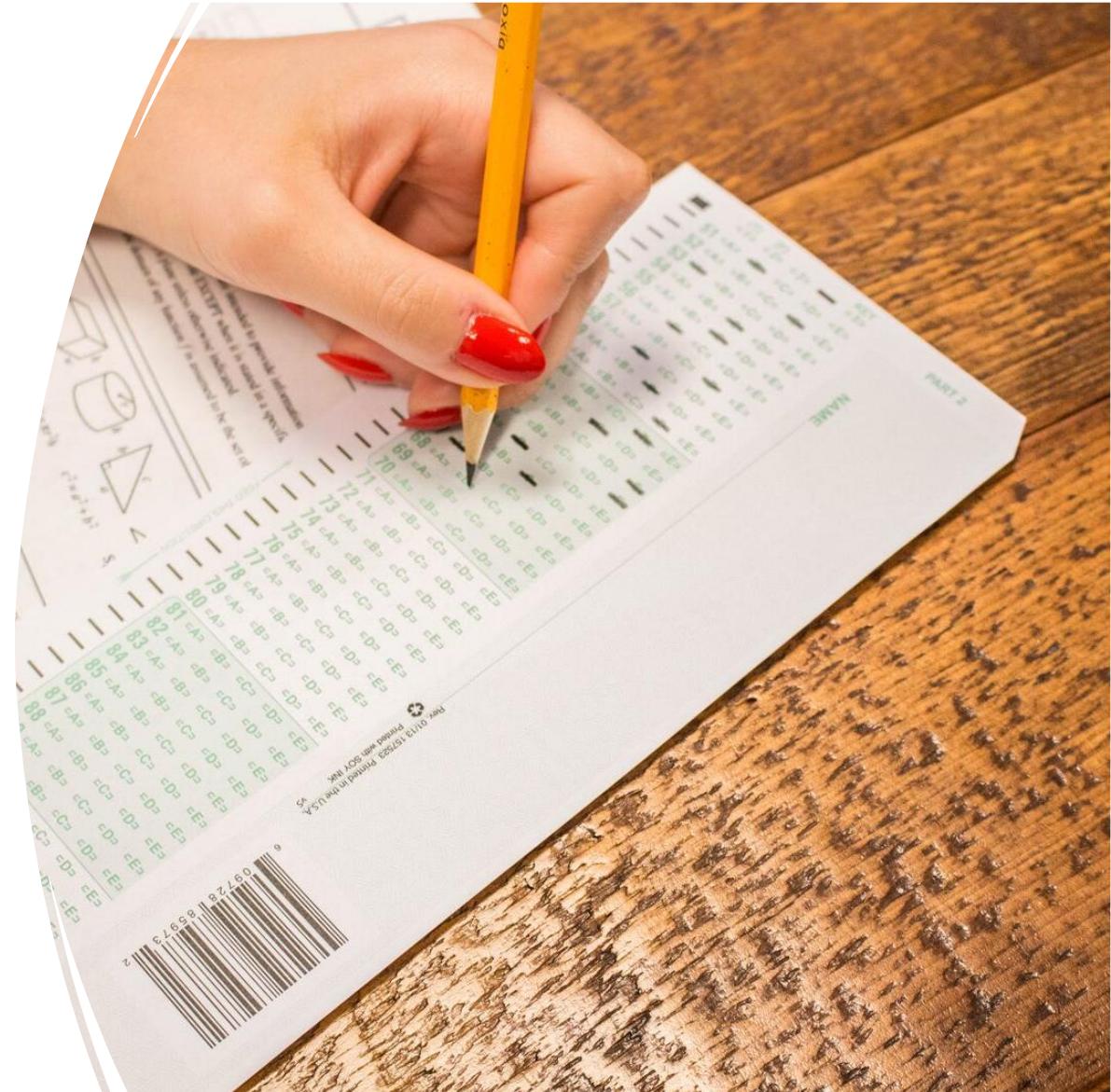
40$ for scoring > C

80$ for scoring > C

-20$ for soring < C

Atlanta School Scandal

- Criterion-Referenced Competency Tests (CRCT) is competency exam for 4th 6th and 8th grades
- MCQ Format
- Schools get various incentives including funding, infra etc.

Atlanta School Scandal

- Statistically unlikely test scores, including extraordinary gains or losses in a single year
- An investigation by the Georgia Bureau of Investigation (GBI) released in July 2011 indicated that 44 out of 56 schools cheated on the 2009 CRCT.

Marks in Indian Education
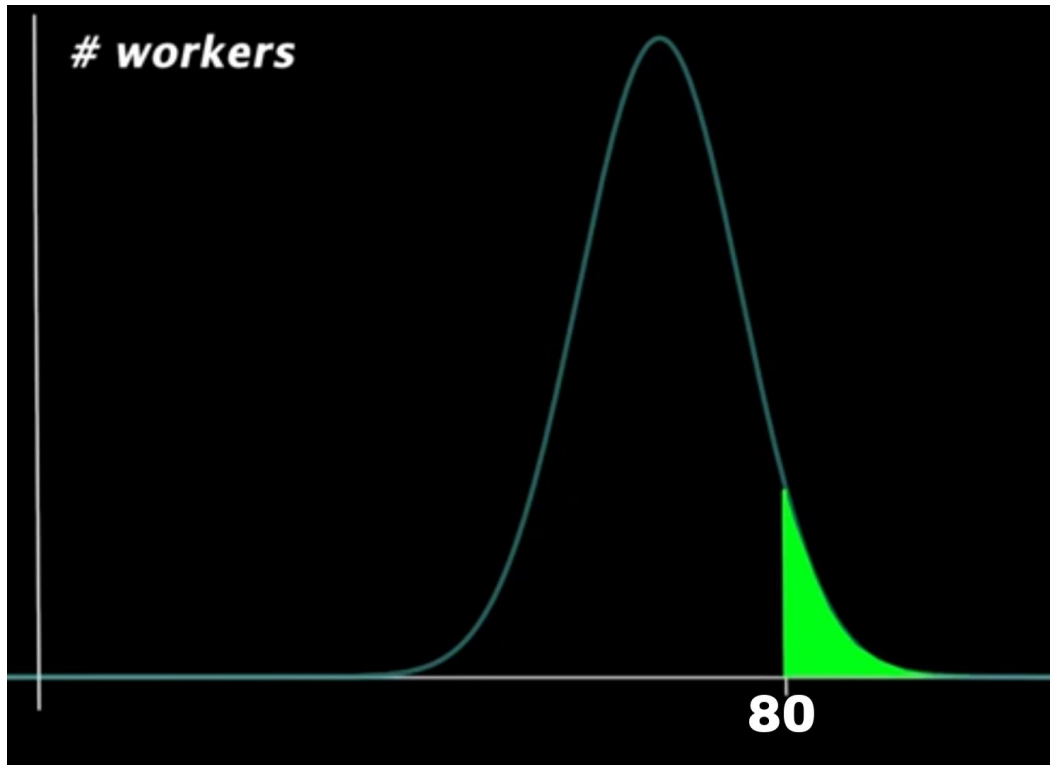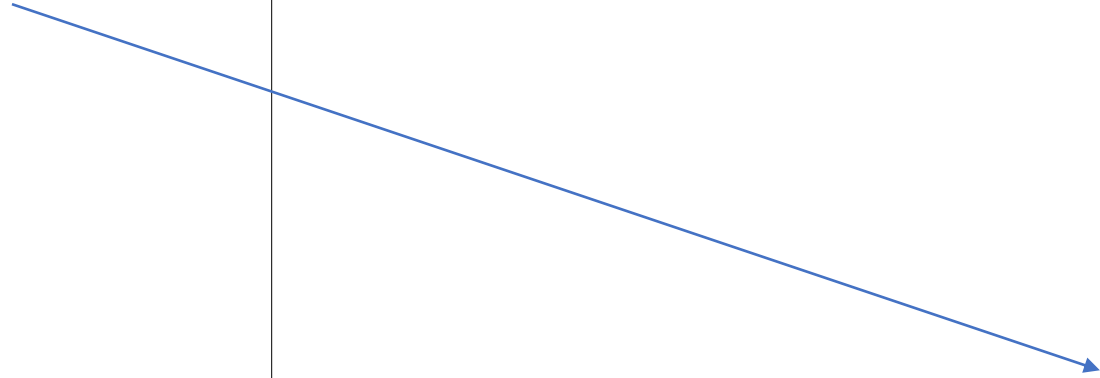
Bonus Motivation

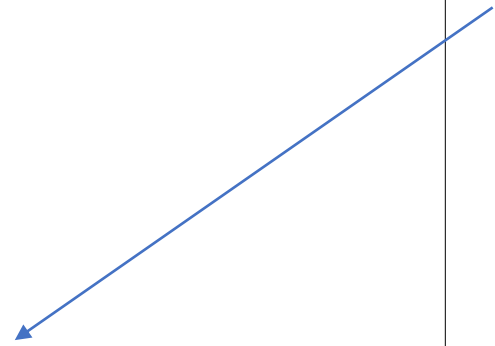**Conditions:** Employees reaching a target Performance score of 80 would receive 2L bonus
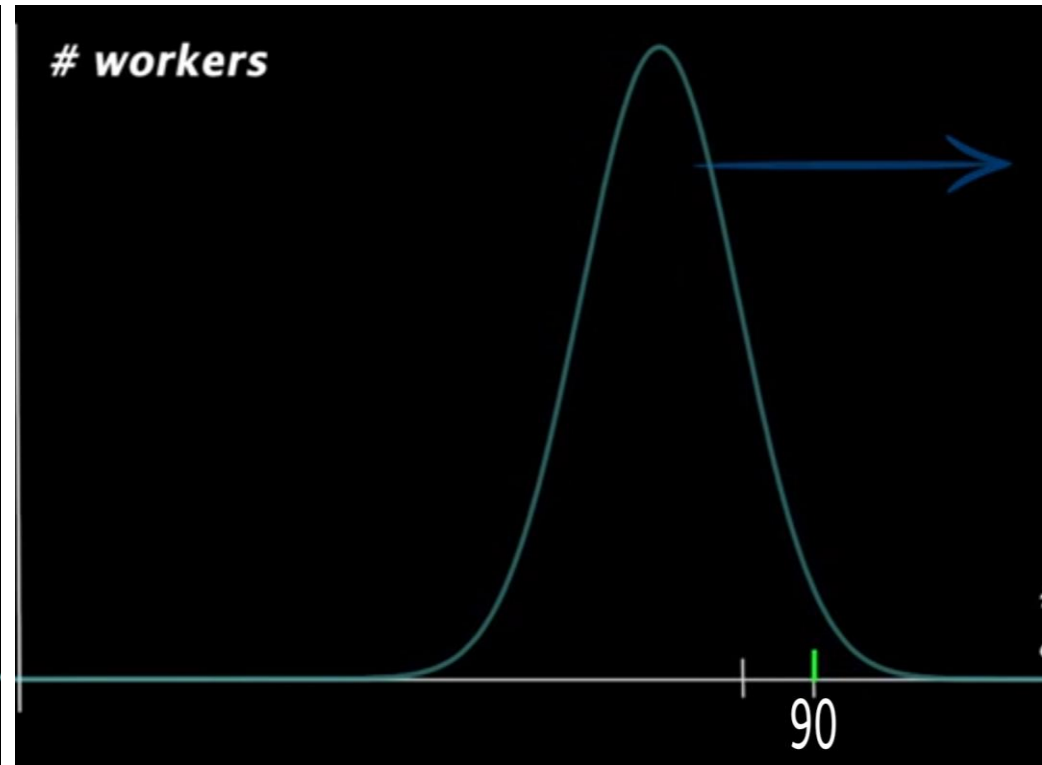
Modification: Employees reaching a target Performance score of 90 would receive 2L bonus

Divers

Thrivers

Bonus Motivation

- Group given a bonus at the beginning, and it would be taken back if performance is below certain score
- This group performed significantly better than the ones given bonus at the end

Free Bagels

- Corporate Office started keeping Bagels and Cash Deposit box on desk
- Employees were expected to pay the price on Honor Systems

Free Bagels

- More than 90% of amount was received

Finding:
  - Crime is very low. Infinite Opportunities
  - People commit behavior what they expect from others

Free Bagels

- When price was increased unreasonably, collections reduced drastically
- When working conditions went bad, collections reduced

If there is mistrust or if employer is greedy honor system wouldn't work

Sumo Fixing

- Sumo wrestling is Japan's national sport and had religious significance

- Rikishi must win at least 8 match from a set of 15 to be promoted

- People always felt that something is wrong with the sport, but nobody said it openly

Sumo Fixing

7–7

8–6

- 7–7 "rikishi" was highly motivated to win his last match to gain promotion, rather than demotion, while the 8–6 rikishi had already guaranteed his promotion, so was not as motivated

- Next tournament in which the two wrestlers met, there was a significant advantage to the 8–6 wrestler over the 7–7, regardless of the performance of either wrestler

- After Media Backlash, the winning rate dropped to 50%
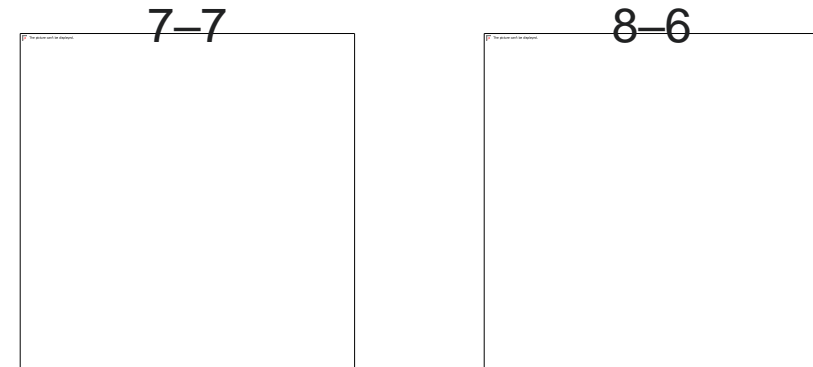
Expected- 48.7% probability of A(7-7) winning
Reality- 80% times A won

Carrot and Stick

A Sequence of rewards and penalties is administered to maximize output

- Cab drivers given huge incentives earlier to join the platforms
- Drivers took loans to buy the vehicles and they could comfortably pay EMIs
- The company reduced the drivers share later and drivers must work harder to earn equal amount of money

Payment Systems

Best Incentive System
- UPI Apps- Gives Financial Incentive(Cashbacks), Social Incentive(Gamification), Moral Incentive(Donations) to increase userbase
- Users might feel like they are in profit but, they are the actual profits

- More than 40% people in Debt Trap
- People spend 70%-100% more when shopping with Credit Card

PBM

Tax the Rich

- Increasing Corporate and Luxury Taxes would never affect the people buying it
- People working get affected the most

Govt offering Huge incentives in form of tax exemptions to setup offices in the States
- Corporate Tax, Property, Business, Income

The picture can't be displayed.