

# The Power of Incentives

Scottsburg New Tech High School

# Starting Off...Yesterday's Activity

- Normally, we eat candy as soon as we get it, right?
  - How did I get some of you to
    - Bring your candy back?
- OR
- Give your candy away?



# I Provided Incentives...

- Incentives - things that cause a person to act, such as the prospect of a reward or penalty.
- Bring Your Candy Back, Get a Reward
- Give Your Candy Away, or Get a Penalty



# Incentives are important



- Incentives are one of the most important concepts in Economics.
- “Most of Economics can be summarized in four words: ‘People respond to incentives.’” – Steven Landsburg

# Why are incentives important?

- Knowledge of incentives allows us to understand and predict the behavior of people and organizations
  - Assume our school went to a “no grading policy,” meaning teachers would no longer assign grades. How would students react?

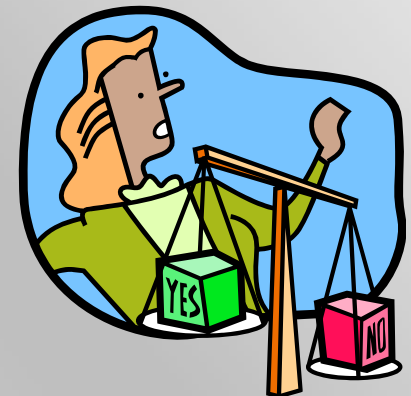


# Why are incentives important?

- We all respond (predictably) to incentives
  - We make choices based on costs and benefits, seeking alternatives that provide us with the most satisfaction.
  - Choices we make reflect our own rational self-interest

Does NOT mean we are selfish...just reality

Even when we act charitably we are acting with self-interest



## Responding predictably...

- If the price of Polar Pops went up to \$5 each, what would that do to the amount we buy?
- If the price of Polar Pops went down to \$.05 each, what would that do to the amount we buy?



# Incentives in Action

- Businesses use incentives to...
  - Get us to buy their products
    - BOGO
    - SALES
  - Guide employee behavior



# Incentives in Action

- Governments use incentives to

- Encourage certain types of behavior

- What are some things the Government wants us to do?

- What are some things the Government wants us to buy?

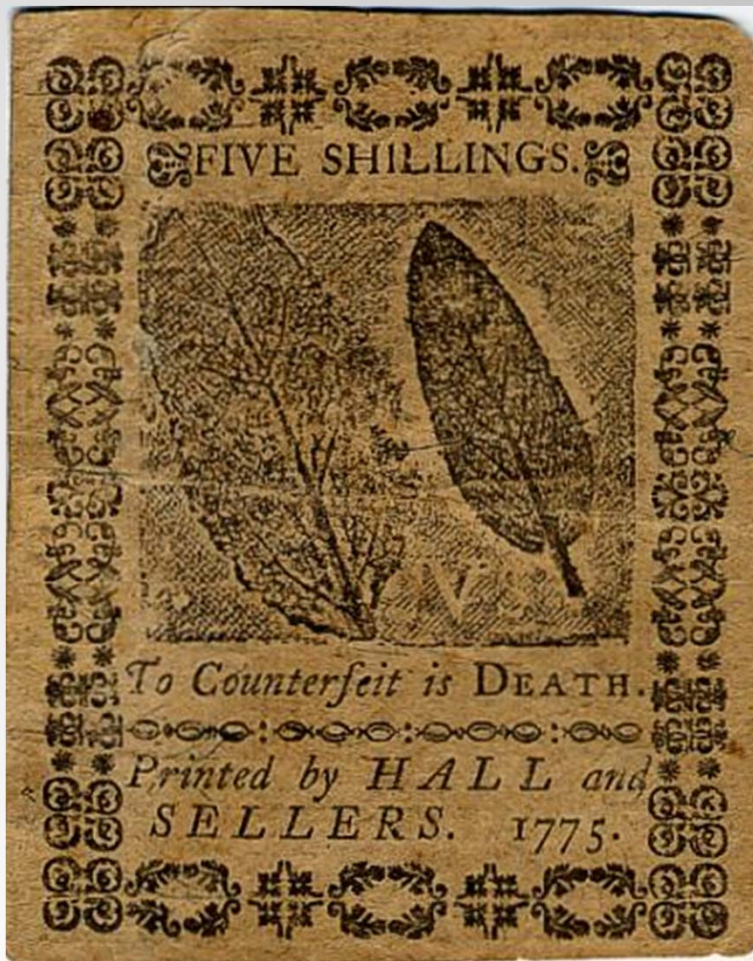
- Discourage certain types of behavior

- What are some things the Government does not want us doing?

- What are some things the Government does not want us to buy?



# Criminals respond to incentives, too



In 1775, the punishment for Counterfeiting money was death

How much counterfeiting do you think occurred?

Let's fast forward 230 years later...

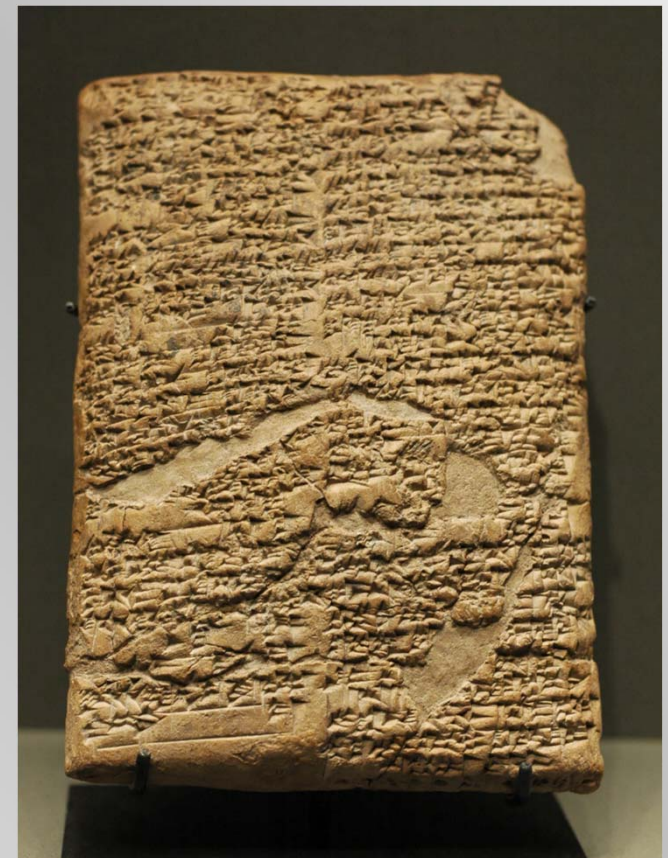


# Criminals respond to incentives, too

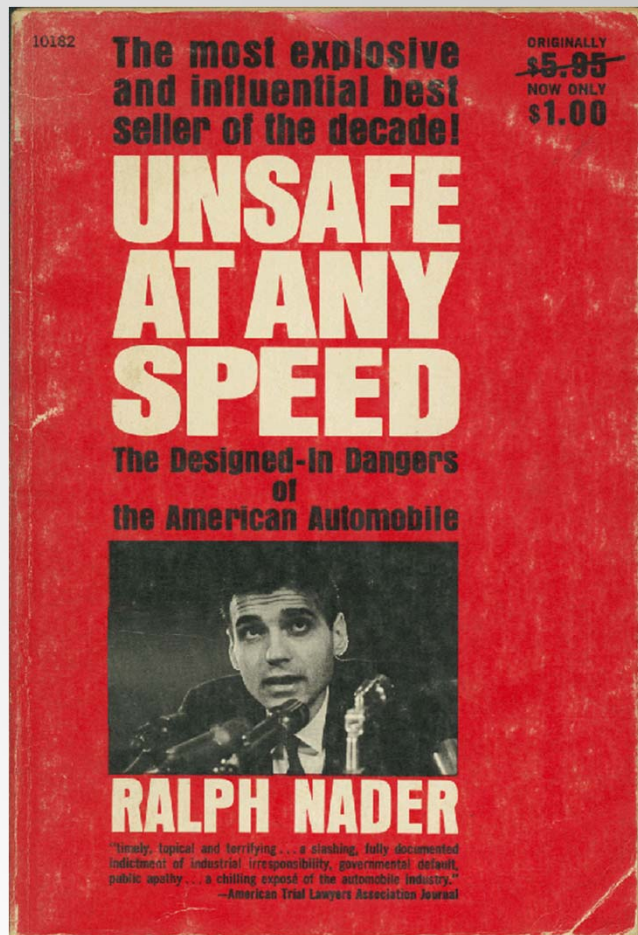
- the U.S. Treasury Department was no match for Art Williams, one of the most inventive and prolific counterfeiters of recent decades. After learning the craft at 16 from his mother's boyfriend, Williams, the product of a tough neighborhood on Chicago's South Side, **went on to print an estimated \$10 million in fake money** by outmaneuvering the government's ever-tightening security measures. Color-changing ink was replicated by automotive paint; watermarks were painstakingly sketched by hand; a close copy of the secret paper came from leftover newsprint rolls made at local mills. Williams had a successful 10-year run before **he was finally caught by the U.S. Secret Service and sentenced in 2002 to three years in prison.**
- Read more:  
<http://www.time.com/time/nation/article/0,8599,1904595,00.html#ixzz1TkBtWxCo>

# Code of Hammurabi

- ~ 1700 BC Babylon
- 282 Laws
- “If anyone brings an accusation of any crime before the elders, and does not prove what he has charged, he shall, if a capital offense is charged, be put to death.”
- “If anyone commits a robbery and is caught, he shall be put to death.”
- “If a son strikes his father, his hands shall be hewn off.”



# Incentives Gone Wild



# Government Reaction

- Passed laws requiring automobile manufacturers to add:
  - Penetration-resistant windshields
  - Collapsible steering columns
  - Dual braking systems
  - Seatbelts
  - Padded dashboards



(c) Travis R. Martin, 2011

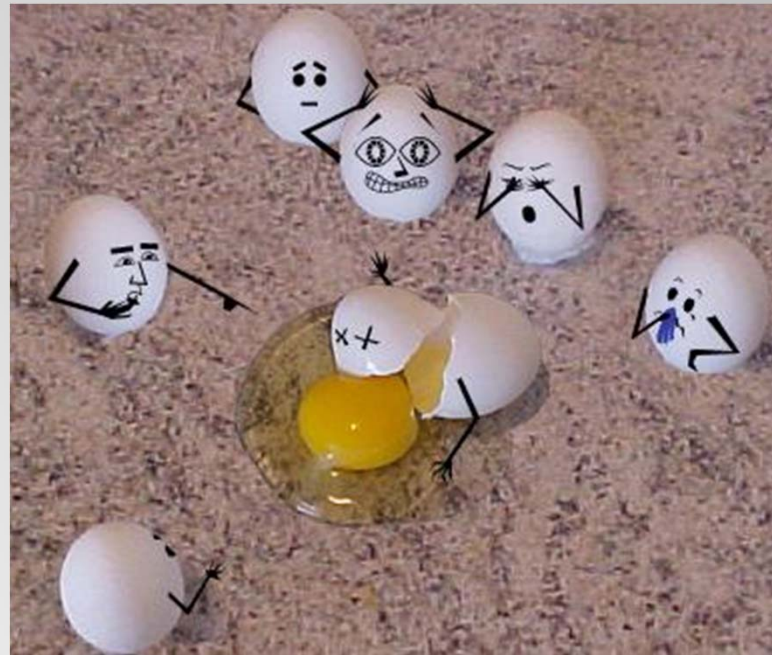


# What do you think the results were?

- Think about how driver incentives changed with the new safety regulations
- In your group, DISCUSS AND GUESS the law's short-term effect on the:
  - # of traffic fatalities
  - # of traffic accidents
  - # of pedestrian deaths

# Incentives Gone Wild

- Before we look at the results of automobile safety regulations in the 1960's, let's try to simulate what happened – from an incentives standpoint!





# The Eggy Interstate

## LANE 1 – UNSAFE EGGMAN

- Using spoons, transport your UNSAFE RAW EGGMAN from point A – B – C.
- Try to make it through as quickly as possible.
- If your EGGMAN falls from the spoon and hits the floor, he dies. Your group must stop the activity and clean him up.
- Quickest time through course wins.

## LANE 2 – SAFE EGGMAN

- Using spoons, transport your SAFE BOILED EGGMAN from point A-B-C.
- Try to make it through as quickly as possible.
- If your EGGMAN falls from the spoon, you may pick him back up and continue (Reattach limbs if necessary).
- Quickest time through course wins.



# The Peltzman Effect

- The threat of being killed (or cracked on the floor) in an automobile accident (or spoon race) is a powerful incentive to drive carefully.
- Drivers with seat belts, air bags, and padded dashboards face less of a threat to their personal safety.
- Because people respond to incentives...drivers are less careful.
- Resulting in:
  - More Accidents
  - Steady number of traffic fatalities
  - More Pedestrian deaths (Pedestrians don't benefit from seat belts or air bags)

# A little reading

- “Incentives Matter” *Common Sense Economics*

