Nudge: Improving Decisions about Health, Wealth, and Happiness

Richard H. Thaler and Cass R. Sunstein
New Haven: Yale University Press, 2008, 304 pp.

When it comes to social policy, inertia can be a bitch. While the sentiment may not seem all that profound, its gradual realization by economists and policymakers is beginning to have an impact on public policy. It has already wreaked havoc within the economics discipline.

The idea of individual rationality—that people respond to incentives, or, more generally, that they tend to make the right choices when it comes to maximizing their economic well-being—has been a crucial tenet of economics almost since its inception. It can be both a strength and a limitation. Ultimately, this idea makes economics a real discipline and not just a bunch of people telling stories to explain how the world works, unlike a few other disciplines I could name. However, some of the implications of rational behavior (namely, that laissez-faire policies often result in the best outcomes for society) often conflict with a politician's desire to fix something. We also observe all kinds of behavior that cannot be neatly slotted into the category of "rational" without some twisting—the cretins who paid $40 to stand next to me at a recent concert and shout to each other over the music about a lazy co-worker come to mind. As a result, the notion that people behave in a rational way is constantly under attack both from within and outside of the profession.

Some economists merely discard the yoke of rationality entirely, leaving themselves free to address crucial policy problems by merely positing that people are myopic (and hence save too little), stupid (thus getting themselves into mortgages that are too costly), or gluttonous (contributing to our ever-expanding waistline). While these judgments may very well aptly describe a portion of the people caught in a pricey mortgage or carrying a spare tire around their midsection, these aren't exactly testable hypotheses. Nevertheless, the policy conclusions are at once obvious and preordained: the government needs to save the people from themselves.

Richard Thaler and his ilk approach apparently dubious behavior from another perspective, asking what is it about the process of deciding how much to save, eat, or spend on a house that have led to so many people ending up in a spot they would rather not be in. Do people make predictable mistakes when they make decisions, and if so, can we make their decisions a bit less complicated or the outcomes closer to where people profess they want to end up?

Economists and psychologists have been studying the limits to individual decisionmaking for some time and a subdiscipline has developed around this pursuit that has come to be called behavioral economics. Thaler's 1993 book *The Winner's Curse* marked the creation of a bona fide movement within the profession and introduced behavioral economics to a generation of economists. Steven Levitt's boffo *Freakonomics* is a direct descendant of this work, and its astounding success doubtless partly motivated *Nudge*.

The knock against the behavioral economists has been that their work is little more than a set of curiosities in search of a theory. They have shown us that people have an innate sense of fairness that goes beyond rational self-interest, that the mere act of possessing a good increases the value we assign to it, and that context matters when we make a decision—all of which have been greeted with a collective shrug by a good chunk of the profession. That may be true, they acknowledge, but is there a broader implication that is relevant for policy?

Thaler and Sunstein argue that there is indeed an overarching message to this inchoate set of observations, and *Nudge* is their attempt to synthesize it. Their message is simple: people do not like change and are not particularly fond of making decisions in the first place (especially financial ones), so let's fix it so that the people who would rather not be bothered to make a decision end up in a good spot. And let's make it as simple as possible to understand the implications of these decisions as well.

To cite their most prominent example, when people begin a new job they suggest that we automatically enroll them in the company's 401(k) program unless they say otherwise, since we know that nearly all employees want to do so if they can just get around to filling out the forms. If they don't specify an investment preference let's come up with a default investment that chooses the level of risk appropriate for someone their age, and dial down the risk as they get older. The recently passed Pension Protection Act made it much easier for companies to participate in such plans, and Thaler's research was the driving force for that provision.

They also opine on the new Medicare Part D program, suggesting that if we require all seniors to enroll in a drug benefit program, it makes sense to give them a limited number of options, make it easy to understand each option, and create a sensible default plan for those that decline to make a selection. Sometimes, less choice is better, they reason.

And when it comes to the convoluted mortgage market, they would radically simplify the paperwork that comes with most mortgages to make the actual cost (and commitment) of a mortgage much more transparent. With the burgeoning number of choices now available to a home buyer, they would also set a default mortgage (a 30-year fixed with no points) for those who don't want to wrack their brain to figure out what might be the best deal for them.

Their preferred label for these policy prescriptions, "paternalistic libertarianism," has encountered skepticism from libertarians, who resent the imposition of any choice upon an unwary populace. Thaler and Sunstein are quite sensitive to this critique and take great pains to refute it by arguing, in the words of the renowned philosopher Geddy Lee of the rock band Rush, that if you choose not to decide you still have made the choice. There is always *some* default, they reason. For instance, we know that how food is presented in school cafeterias affects what children eat, and there's no way for the cafeteria manager to escape making some decision about what food students see first and what they see last. The debate is about what ought to be in the front of the line and not whether anything at all should be placed in front. The urban anthropologist Paco Underhill discussed the same set of issues in his tract on retail shopping, *Why We Buy*.

(The other side has registered their complaints as well: an earnest staffer for Public Interest, an entity founded by Ralph Nader to press for more regulations, asked Thaler and Sunstein at a book event at the American Enterprise Institute why they seemed much more worried about what libertarians thought than the paternalists like themselves.)

Is this book another *Freakonomics*, the standard to which it begs to be compared? It lacks its sizzle, for want of a better term: there are no sumo wrestlers or bookies or cheating teachers in its pages, but *Nudge* also lacks the pointless verbiage that enveloped each chapter in what was an obvious attempt to pad what originally began as an article into the minimum necessary length to be called a book.

Nudge is all bacon. It carpetbombs the reader with interesting anecdotes, and while none quite match the best of the ones in *Freakonomics*, the sheer number and variety create an informative and readable book. The timeliness of their work is also a point in their favor—for instance, the discussion of how to implement peak-load pricing, whereby utilities change the cost of energy to the user on an hourly basis, is being discussed in Congress right now. The vignette is a great example of the strength of the book: the typical reader can quickly grasp that it would be a great benefit to create a pricing system that deters energy usage during the peak demand times of the day, since the surge in demand necessitates older and invariably less efficient and dirtier plants to operate for that short period. However, it is not at all obvious that the way the utility conveys this information to the customer is important, and to read how power companies devised a simple yet powerful way to do so feels like actual learning is taking place, which can be fun and quite satisfying in small doses.

It takes a while for new ideas in economics to become digested by the profession and become relevant for policy, and *Nudge* is in many respects the official coming-out party for behavioral economics. It may take a while to get to the next step, where politicians misinterpret, distort, and exaggerate the authors' ideas for their own narrow political gains, but it is only a matter of time before we get there.

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Forgotten Continent: The Battle for Latin America's Soul
Michael Reid
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For most of this decade, Latin America has been neglected by the developed world. At least that is a recurring grievance from leaders and specialists in the region. The attention of rich countries has switched to terrorism in the Middle East and poverty in Africa, while pressing needs and conflicts remain unattended in Latin America.

Judging by the title of his book, Michael Reid, editor of the Americas section of *The Economist*, would seem to follow this argu-