Available online at www.sciencedirect.com
ScienceDirect
Procedia - Social and Behavioral Sciences 191 (2015) 884 – 889
Procedia
Social and Behavioral Sciences

WCES 2014

Education As Public Good: Behavioral Economics Approach

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Abstract

Nowadays in developed countries education as a system often becomes public, society getting a lot of new information and knowledge based values. Education in its general sense is a form of learning in which the knowledge, skills, and habits of a group of people are transferred from one generation to the next through teaching, training, or research. Education is available for more people than in previous times; even it can be identified as mass education that can be evaluated as a public good. Behavioural economics study the effects of social, cognitive, and emotional factors on the economic decisions of individuals and institutions and the consequences for benefit and the resource allocation. Behavioral economics does not take the characteristics of the decision-maker as fixed, the focus is on the non-equilibrium processes, actions of diverse agents with bounded rationality who may learn from experience and interactions. The education and as result, high cumulative level of knowledge in society, might have an influence on complexity and difficulty on country's economic system, especially regarding behavior economics approach. The research object of this article is identifying correlation between mass education and complexity of rationality in financial economics. The research aims of this article to describe and evaluate different approaches of rationality in financial economics field regarding mass education. The results of research are to provide readers with understanding of behavioral economics approach regarding different level of education and financial literacy.

Selection and peer-review under responsibility of the Organizing Committee of WCES 2014

Keywords: Education, behavioral economics, rationality, financial markets.

1. Education and behavioral economics

Today's relationship between level of economic (more particular, financial) education and efficiency of real economy is one of the main topic in scientific debate in the field of many different approaches. It is practically impossible separate economics science from others disciplines, like psychology, human behavior, philosophy, ethic and etc. A common approach is that financial literacy is determined by knowledge; in various studies the population

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Selection and peer-review under responsibility of the Organizing Committee of WCES 2014
doi:10.1016/j.sbspro.2015.04.401

is categorized into literate or illiterate, according to whether they have saved money for hard times or have set long-term planning goals, or their taking care of the income and funds assigned for retirement. (Borodich, Deplazes, Kardash, and Kovzik, 2010). Also the population's investment in the stock market, awareness of their actions or proper distribution of investment is taken into account. For determining financial literacy, the following issues are taken into account: whether a person knows how to align daily income and expenses, whether he is not hopelessly indebted. With sufficient knowledge it is possible to further develop skills that could be useful for gaining financial benefit. Therefore, it is important to develop knowledge: first in mathematics, then in micro and macroeconomics, so that to realize how finances are managed, how they depend on the environment, also to learn the most essential things about money, interest, inflation, etc. (Evans and Honkapohja, 2001). Overall knowledge should promote rational behavior, proper choice of financial services and help to avoid errors that impair the person's financial situation. Globalization and recovery of financial markets and permanent changes in economics, which are difficult to predict, highlight the need for financial literacy (Barro, and Ursua, 2009; Roubini, Nouriel and Mihm, 2010)These changes and technological innovation is changing the financial behavior of individuals and personal financial management. With the development of economic science, the economists' approach to the consumer's financial behavior has changed (see figure 1 a). Two basic theories are distinguished: the efficient market hypothesis and financial behavior. In recent years, there is much debate on the efficient market hypothesis and the significance of financial behavior in economic theory.

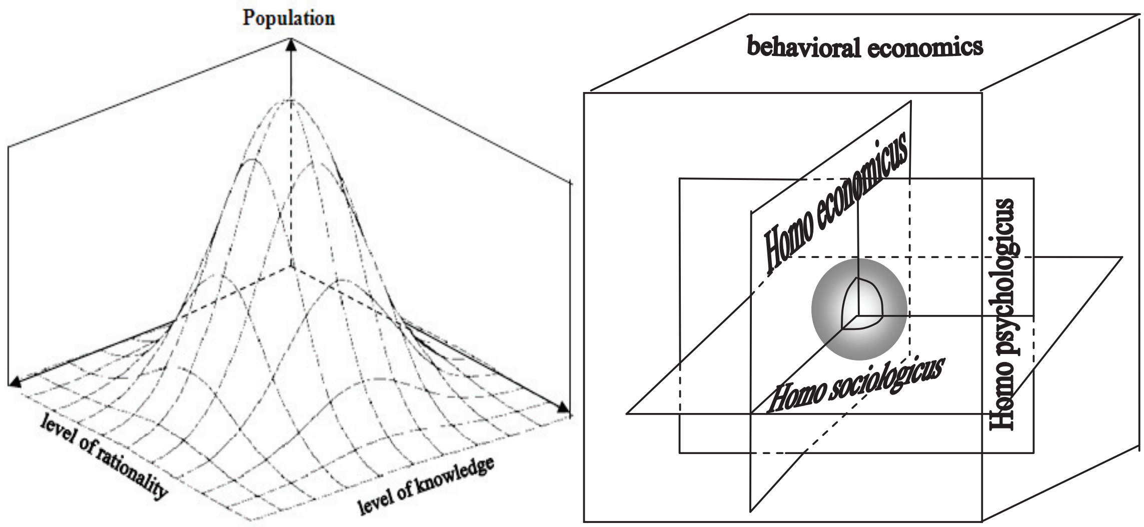

Fig. 1. (a) Gaussian 3D function regarding level of knowledge and rationality ; (b) behavioural economics approach

The emerging discrepancy between the efficient market hypothesis and reality encouraged a deeper insight focused on psychology, as an important factor in financial theory. Behavioral economics was formulated - a new branch of theory, combining the knowledge of psychology, sociology and other social sciences (see figure 1 b Buss,) (Buss, 2009). Due to the integration of various scientific knowledge behavioral economics better explains market anomalies and financial behavior of individuals. An efficient market theory hypothesis maintains that investors, while competing for big profits, establish fair prices. In order to better understand an individual financial behavior, the behavioral theory of psychology, sociology and anthropology is applied. An efficient market is associated with the theory of rational expectations, including the assessment of all information about property. However, if there are many irrational investors and their financial behavior does not correlate, and their transactions invalidate each other and have an impact on prices, the question arises on a far too poor assessment of the irrational investors' impact on the market. If investors are irrational, their financial decisions determine prices, although do not change the value of financial assets. As a result, rational investors can sell overvalued or buy undervalued assets, thus gaining profit, until the asset price converges with its value (Berg and Gigerenzer 2010).