

Introduction to EC0381

Class 1 – June 30, 2009

Prerequisites: open mind (and heart), curiosity,



Goal of This Class

Help you decide whether this is the right course for you

Outline

1. About this course (Looking at the forest)
2. 60 seconds bio
3. Syllabus:
 - a. Meetings, office hours, e-mail policies
 - b. Evaluation
 - c. How to succeed in this course
4. About this course (Looking at the trees)

1. About this course (looking at the forest)

- Two main questions:
 1. How people get paid?
 2. What difference does it make?

1. About this course - Forest

People get paid in many different ways

- Piece Rates (P4P)
 - Fee-for-service physicians
 - Taxi drivers
 - Sales Associates
- Team Compensation
 - West Jet profit-sharing plan
 - School funding and standardized tests
- Tournaments
 - CEOs
 - Professional Sports
 - Gangs

1. About this course - Forest

It makes difference how people are paid

Three examples from “Freakonomics”:

- Standardized tests in Chicago
- Sumo wrestling
- Bagel business

1. About this course - Forest

Main Learning Objective

- **How to provide right incentives so that people voluntarily do what is in the society's best interest**
- Examples:
 - Business: CEO compensation, innovative workforce
 - Environment: recycle, use public transport
 - Education: long-term, deep, critical learning
 - Health: adequate and timely medical services

1. About this course - Forest

How to think about this course?

- You have an incentive problem you want to solve
- I am here to provide you with tools:
 - E.g. What incentive contracts are out there?
 - E.g. When is each contract likely to work?

2. 60 seconds bio

- Jasmin Kantarevic
- Education: Ph.D., University of Toronto, 2005
- Teaching: ECO381, ECO239, ECO365
- Work Experience: Ontario Medical Association
- More at www.jasminkantarevic.com

3. Syllabus

Meetings, Office Hours, etc.

- Meetings Tuesdays and Thursdays, 5-8pm, Room WO 35.
 - Office Hours Tuesdays, 7-8pm, and by appointment
 - E-mail jasmin.kantarevic@oma.org

 - Course Website www.jasminkantarevic.com/eco381

 - Material:
 - Lectures
 - Textbook readings
 - Articles
 - Homeworks
- } All posted on the course website.
Textbooks also on reserve.

3. Syllabus

Evaluation

1. Two Midterms (40)
 - The better counts as 30, the worse counts as 10.
 - Mandatory.
 - Tools: Homework, Past Midterms and Exams
2. Research Paper (20)
 - Groups of 2 to 4
 - Incentive solution to a real-world problem
 - Tools: Workshops every Thursday
 - Details to follow
3. Final Exam (40)
 - Tools: Homework, Past Midterms and Exams

3. Syllabus

Pre-requisites

- ECO200Y/206Y, ECO220Y/227Y
- Two main issues:
 1. Calculus: optimization of a single variable
 - E.g. Find the value of x that maximizes $y=x^2+4x$.
 2. Statistics: interpretation of regression model
 - E.g. Interpret the following regression model:
Grade = 100.4 + 5.1×Attendance
(48.2) (1.4)

3. Syllabus

How to succeed in this course?

1. Prior to the class
 - Print and read lecture slides, appendices, articles, and textbook pages relevant to the class
2. After Class
 - Try homework problems
 - Contact me early if you have problems
3. Attend all classes and workshops
4. Allocate 6 to 8 hours per week for the course

4. About this course (looking at the trees)

- People are paid in many different ways and it matters how people are paid.
- How people are paid matters because incentives matter.

- A main role of compensation is to provide right incentives:
 - Reward desirable actions
 - Punish undesirable actions

Example: Evaluation of Students

- Learning is desirable behaviour.
 - The best of two midterms counts
 - Bonus points for class participation
 - Deduct points for missing classes
- Sleeping in the class is undesirable behaviour.
 - Deduct points for sleeping
 - Bonus points for staying awake
 - Free coffee

The Incentive Problem

- Why do we need to provide incentives?
- Two main elements:
 1. Asymmetric Information
 - Workers know more about their actions than firms do.
 2. Conflict of Interest
 - What workers and firms want is usually not the same.

4. About this course - Trees

Incentive Problem: Examples

- Car Owner and Car Mechanic
- Home Buyer and Real Estate Agent
- Patient and Dentist
- Landlord and Tenant
- Investor and Stockbroker

4. About this course - Trees

Plan Ahead

- Study six methods that tie reward for performance:
 1. Piece Rates
 2. Team Compensation
 3. Tournaments
 4. Subjective Evaluation
 5. Dynamic Compensation
 6. Non-monetary Incentives
- These methods are differentiated based on:
 - Individual/Group Performance
 - Static/Dynamic Contract
 - Monetary/Non-Monetary Reward
 - Objective/Subjective Performance Measure

4. About this course - Trees

Plan Ahead

- For each method, answer three main questions:
 1. Can it solve the incentive problem?
 2. When is it likely to work?
 3. Does it work in practice?