

Referee Report on
“Youth and Inexperience: Dynamic Inconsistency Among Emerging Adults,”
by Gibbons and Paxton
June 2015

An important behavioral economics problem is to analyze the sources and explanations for time inconsistent decision making, particularly in regard to financial decisionmaking taken over an individual's life cycle. Gibbons and Paxton contribute to this with a largely empirical and descriptive statistical study on the decision making by young adults. They base their results on a survey of more than 1000 students at Ohio University. There is no attempt to argue this sample is in any way representative. Indeed, their results — that the sample is stratified into two groups, one relatively young and the other taken as relatively more mature, indicate the former group makes saving-investment decisions in a manner that is time inconsistent. A variety of interesting hypotheses are put on the table to explain this observation. The authors note that a proper panel study is really required to make inferences about changing decisions that could be construed as time inconsistent decisions.

The author seem to believe the time inconsistency problem begins to be noticed in 1968. This is false. Strotz defined the problem in the mid 1950s. It is instructive to examine his paper as it makes clear that the issue is one that arises when planning horizons are infinite. Nonexponential discounting in that context simply means that a forward shift in calendar time alone, all other things equal, means that a rational optimizing agent would adopt a different decision rule than the one found by solving the infinite horizon programming problem one period earlier. Hyperbolic and quasi-hyperbolic utility functions are merely important examples where this problem would be expected in the infinite horizon setting.

However, the agents in the survey data are not infinite horizon planning agents. They are finitely-lived and there is nothing in the dataset to confirm or deny they are also taking their descendants welfare into account when they save today. IF these agents are optimizing over a finite horizon, and they apply standard backward induction logic from dynamic programming, their decision rules will be time dependent. Why is this NOT an alternative explanation for the behavior seen in the data set? Put differently, is it the case that time inconsistency due to the structure of discounting future payoffs in a finite horizon setting must necessarily be the only explanation for the apparant time inconsistency?

The paper is provocative in so far as it is a nice take on behavioral ideas, some taken from broader social science research. And, it has the unfortunate feature that no model is actually formally stated so that the readers have no idea what the decision problem IS that agents are taken to act on. Hence, it is difficult to assess the paper's contribution as no formal model is actually attacked by the authors.

The paper's contribution is to propose a problem for proper future analysis. There is a theoretical issue (the finite horizon matter), and the data problem of asking the questions about panel data. I do not believe that papers that propose problems are appropriate for publication where it is not clear what that problem is absent a model to frame the question. It is insufficient to point at a particular discounting function and blame it absent a fully articulated decision problem with constraints and payoffs spelled-out. As the matter stands, it is an interesting empirical story without a substantive explanation. I do not recommend publication at this time.