

Risk and Time: An Experimental Investigation of Behavioral Analogies

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Abstract: Choices under risk and over time are very similar in nature. Based upon prospect information the decision maker intrinsically attaches weights to outcome utilities. Weighting functions in both fields have been found to deviate from classic economic assumptions, and depend on the distance from reference points. This paper empirically examines the relationship between weight distortions in risky and intertemporal choices by employing data from a laboratory experiment with real monetary incentives. Using two separate procedures, individual certainty equivalents and individual discount rates were elicited. The findings emphasize that there exists a link between individual behavior in both fields: Subjects who deviate from linear probability weighting are also likely to deviate from exponential discounting. Beside identifying distinct types, people exhibiting distorted weighting functions, and people behaving as classic economic theories suggest, a strong relationship between individual sensitivity to changes in probability and time is uncovered. It is argued that weighting distortions in both fields have common underlying sources. (JEL D01, D81, D91)