

Economics 454
Benefit-Cost Analysis
Spring 2022
Prof. Robert Halvorsen

In ECON 454 we will discuss how benefit-cost analysis *should* be done. In real life, benefit-cost analyses are often done very badly, frequently because the people doing them are trying to provide support for what they have already decided to do, rather than objectively analyzing what they should do. By the end of the Quarter, students should have a firm understanding of the issues, techniques, and practical difficulties involved in benefit-cost analysis and therefore the ability to critique real-life benefit-cost analyses. The prerequisite for this course is ECON 300 and the class discussions will assume that students have a solid understanding of intermediate level microeconomics.

Lectures and exams will occur in person at the regularly scheduled class times. Lectures will not be recorded but lecture notes will be posted on Canvas. There is no textbook or course pack.

Three, non-cumulative, exams will each count for 30% of the course grade. Please refer to the next page for very important information on the rules for taking exams. Note especially the information concerning cell phones. Last Quarter's exams will be posted on Canvas as a preview of the types of questions that will be asked as well as sources of practice questions in studying for this Quarter's exams.

Three problem sets will count for 10% of the course grade and will be graded credit/no credit. Problem sets must be posted to Canvas as PDF's. They do not need to be typed but do need to be easy to read. Detailed answer sheets for the problem sets will be posted on Canvas. Reviewing the answers and comparing them to your own are excellent ways to learn the course material.

My office hour for ECON 454 will be on Zoom from 10:00–11:00 on Friday. An appointment to meet either on Zoom or in person at another mutually convenient time can be made by email at halvor@uw.edu. You can also use email to ask any short-answer questions that may arise as you review your notes or work on the problem sets.

Exam Rules

I Exam Absence Policy

1. If you are unable to make it to an exam due to illness, the grades on the other two exams will be reweighted accordingly.
2. If you know that you are going to be away due to a University-related activity, such as participation in an away sport or debate, let me know well in advance so that arrangements can be made.

II Exam Taking Rules

1. Material allowed during an exam.
 - i. You must bring a large bluebook with nothing written on or in it.
 - ii. All books, papers, notebooks, etc., must be placed inside your backpack or other type of bag, which must be securely and fully closed. If you do not have a bag, you must place all your material out of your reach.
 - iii. Cell phones must be turned off and placed in your closed bag (not in your pocket). **If your cell phone is observed at any point during the exam, your exam will be taken away and assigned a grade of zero.**
 - iv. Baseball caps and any other kinds of headgear that conceal your eyes are not permitted.
2. Attendance and special accommodation
 - i. You are not allowed to leave the room during the exam. This includes restroom use; be sure to use the restroom before the beginning of the exam.
 - ii. If you arrive late to an exam, you will not get extra time after the official end of the exam to make up for the missing time at the beginning.

III Academic Integrity

1. Exams are individual work and cheating will not be tolerated. Looking at notes or your neighbors' answers will result in the immediate termination of your exam time and a grade of zero for the exam.
2. Altering an exam before submitting it for a review of the grading, obtaining an advance copy of an examination, or arranging for a surrogate test-taker are all flagrant violations of University policy.
3. Cheating of any kind may result in expulsion from the University. The Department will follow University policy in case of academic misconduct. I strongly recommend that you review University policy at <http://www.washington.edu/uaa/advising/help/academicintegrity.php>. Students found to have engaged in academic dishonesty will be subject to sanctions, which range from a disciplinary warning to permanent expulsion from the University, depending on the seriousness of the misconduct.

Course Schedule

All dates except for the final exam are subject to revision.

Washington state law requires that UW develop a policy for accommodation of student absences or significant hardship due to reasons of faith or conscience, or for organized religious activities. The UW's policy, including more information about how to request an accommodation, is available at [Religious Accommodations Policy](https://registrar.washington.edu/staffandfaculty/religious-accommodations-policy/)

(<https://registrar.washington.edu/staffandfaculty/religious-accommodations-policy/>).

Accommodations must be requested within the first two weeks of this course.

March 29th Lecture 1

Benefit-cost analysis as four-way aggregation

Standing

Social Welfare Criterion

Pareto Criterion

March 31st Lecture 2

Potential Compensation Criterion

Aggregation over commodities

Valuation principles

April 5th Lecture 3

Valuation in undistorted, perfectly competitive, markets

Valuation when markets are not used or are distorted

April 7th Lecture 4

Aggregation over time

Robinson Crusoe model

Present value of consumption criterion

April 12th Lecture 5

Capital markets and dynamic efficiency

Net present value decision rules

Special cases of discounting formulas

April 14th Exam review. Problem Set 1 due.

April 19th Exam 1

April 21th Lecture 6

Alternative investment decision rules

April 26th Lecture 7

Dynamic inefficiency

Net social benefit criterion

April 28th Lecture 8

Aggregation over States of the World

Certainty equivalent (CE)

Risk aversion

Expected utility

May 3rd Lecture 9

EMV as approximation of CE

May 5th Lecture 10

Aggregation over Individuals

Methods using explicit distributional weights

May 10th Lecture 11

Methods not using explicit distributional weights

May 12th Exam review. Problem Set 2 due.

May 17th Exam 2

May 19th Lecture 12

Valuation of Commodities with Incomplete Market Data

Limited observations on price and quantity

Cost of alternative supply

Use of market data for related commodities

May 24th Lecture 13

Valuation when Commodities Have No Market Data

Use of market data for related commodities

Travel cost technique

May 26th Lecture 14

Valuation of Risks to Life

Cost effectiveness

Implicit vs. Explicit Valuation

May 31st Lecture 15

Value of a Statistical Life

Estimation

Factors affecting the value of a statistical life

Risk-risk analysis

June 2nd Exam review. Problem Set 3 Due.

June 7th Exam 3