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Exogenous Shock, Time Preference, and Utility Curvature (*)

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Abstract

This paper analyzes the interaction between change in time preference caused by exogenous shock and utility curvature using a model of behavioral economics. Time preference is an important factor for determining individuals' intertemporal choices in their daily lives. In traditional economics, individuals' time discount rates have been assumed to be constant over their lives. However, behavioral economists point out that some individuals follow a hyperbolic discounting rate. Especially, recent some empirical studies reveal that individual's preferences change through exogenous shocks such as natural disaster. This study considers the case that individuals prefer present consumption to future consumption because their expected utility from consumption falls by exogenous shock and analyzes the effect of their utility curvature.

Keywords: Time preference, Economic shock, Life-cycle model