

Common Principles of Behavioral Economics

Takeaways from *"Incorporating Behavioral Insights in Financial Product Design"*
9/17/2014

Friction

Overconfidence	Everyone believes they are right and everyone believes they are above average
Availability bias	People tend to focus on what comes easily to mind
Default bias	People tend to make the easiest choice – which often means no choice at all
Planning fallacy	People consistently under-estimate how long things will take
Decision paralysis	When given too many choices, people often don't choose at all
Limited attention	People often miss important details because they can only process a limited amount of information at a time

The Psychology of Money

Loss aversion	People feel losses more than gains, and they try to prevent losses more than they try to make gains
Reciprocity	People often respond to a positive action or gift by providing something of equal or greater value in return
Sunk cost effect	People are unable to forget the money they've already spent
Mental accounting	People categorize and treat money differently depending on where it came from and where it is going
Opportunity cost neglect	People tend to ignore what they give up when they make a choice
Anchoring	People are tied to their first impression and the first number they hear, placing less emphasis on subsequent information

Herding People tend to confuse the actions of others as the right action

Endowment effect People overvalue what they have

Now versus Later

Present bias People overvalue rewards in the present and undervalue future costs and benefits

Lack of self control People have a hard time deciding between doing what's good for us in the long term versus what feels good right now

Ego depletion People's ability to make good decisions is a limited resource that can be drained by decision overload and external fatigue

Further Resources

Websites
 Innovations for Poverty Action - www.poverty-action.org
 Center for Advanced Hindsight - advanced-hindsight.com
 Ideas42 – www.Ideas42.org
 Behavioural Design Lab - www.behaviouraldesignlab.org

Blogs
 Dan Ariely – danariely.com
 Ethics of Nudge - ethicsofnudge.com
 Nudge Blog (Richard Thaler and Cass Sunstein) – nudges.org

Books
Nudge: Improving Decisions About Health, Wealth, and Happiness by Richard Thaler and Cass Sunstein
Thinking, Fast and Slow by Daniel Kahneman
Predictably Irrational: The Hidden Forces That Shape Our Decisions by Dan Ariely
Scarcity: Why Having Too Little Means So Much by Sendhil Mullainathan and Eldar Shafir
Behavioural Economics for Kids by Neil Bendle (available as a free eBook at neilbendle.com)