The seven traps in decision-making, and how to avoid them

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We get through the day with heuristics. These rules of thumb serve us reasonably well, allowing us to make decisions quickly, so that we can efficiently carry out the tasks that are demanded of us. But heuristics can be highly fallible. For example, we judge distance by how clear objects are - on a hazy day, we judge objects to be further away. Most of us are not flying an airplane, so this error seldom has a fatal result, therefore our misjudgements often do not get the serious attention they deserve (for insights into how pilots gauge distance, see footnote below).

There are seven cognitive traps identified by Hammond, Keeney and Raiffa in their article 'The Hidden Traps in Decision Making'. [1]

(Image: Wikimedia Commons)

1. Anchoring

When considering a decision, we give a disproportionate weight to the first information we receive. If we asked two groups the following questions, those that were asked the second set gave a larger estimate.

Is the population of Turkey greater than 35 million?
What's your estimate of Turkey's population?

Is the population of Turkey greater than 150 million?
What's your estimate of Turkey's population?

This might be a simple and predictable example, but the effect of anchors in decision-making has been shown in numerous experiments to affect not only managers, but accountants, engineers, bankers (believe it or not), lawyers and stock analysts.

To mitigate the effect of anchoring, it would be prudent to view a problem from different perspectives - alternative starting points. Essentially be open-minded.

2. The status quo trap

Choosing the status quo saves energy. Research shows that people are more likely to choose the status quo when two alternatives are presented as opposed to one. The perceived mental energy that needs to be expended becomes high, so we take a shortcut.

To lessen the pull to default to what is, always remind yourself of the objective, and ask yourself whether you would choose the status quo alternative, if in fact it was not the status quo.

3. Sunk cost trap

We tend to make choices that justify our past decisions, even if those past decisions no longer seem valid.

This bias shows up regularly in banking when a borrower's business runs into trouble. In this case, the initial lender will tend to advance funds more readily in the hope of reaffirming that the original decision was the right one. Banks have wised up to this and have introduced a policy that the loan is reassigned to another banker when problems arise - someone for whom the original decision is not worth 'saving'.

As Warrren Buffett says: "When you find yourself in a hole, the best thing you can do is stop digging."

4. Confirming evidence trap

This cognitive bias encourages us to seek out information that supports our existing point of view, while avoiding information that contradicts it. There are two psychological forces that have an impact here. The first is our tendency to decide immediately what we want to do before we have really worked out why we want to do it. The second is that we become more engaged with things we like than things we dislike.

To address this trap, someone who plays the role of the devil's advocate is appropriate to build up counterarguments. But an even better prescription would be for you to be honest about your motives.

5. Framing trap

The way a problem is presented can profoundly affect the choice you make. In a classic experiment by Daniel Kahneman and Amos Tversky, the following was proposed:

Three barges have sunk. Each barge holds $200,000 worth of cargo. These are your salvage options - which would you choose?

Plan A: *Saving the cargo of one of the three barges, worth $200,000*
Plan B: *Have a one-third probability of saving the cargo on all three barges worth $600,000, but with a two-thirds probability of saving nothing.*

Over 70% chose the 'less risky' option of Plan A, even though both have the same potential outcome. The questions were just framed differently.

To counteract the framing trap, don't automatically accept the initial framing - always try to reframe the problem in different ways. This is crucially important for strategy, because the first step is always defining the problem correctly.

6. The estimating and forecasting traps

I have yet to see the headline "Clairvoyant wins lottery". Predicting the future is fiction. Other than weather forecasters and bookmakers we generally don't use a great deal of data which we carefully track over a long period of time. We are, however, good at making accurate estimates about time, distance, weight and volume, because we're constantly making judgements about these and getting immediate feedback, so our minds become finely calibrated.

Forecasting sales is a difficult process at best. One of the Big Three automakers felt this most keenly. The planning department responsible for the final forecast asked each of the other departments for their forecasts using key variables such as dealer demand, competitor actions, and costs. The problem was that each department gave a high forecast in favour of building more cars 'just to be safe'. So, the planners had a collection of estimates - all which played safe. It took six months to sell off the surplus resorting to substantial discounts. Garbage in, garbage out.

7. The recallability trap

When estimating forecasts it should come as no surprise that we base our predictions about future events largely on our memory of past events. The problem is that we are overly influenced by events that are more dramatic. For example, we exaggerate the probability of events such as plane crashes and shark attacks, because they get a disproportionate amount of attention in the media.

To reduce the effects of the recallability trap, the idea is to consider the extremes of the situation - the low and high ends of the possible range of values, and then challenge your estimates of the extremes.

To minimise the distortions due to recallability, it's best not to be guided by impressions, but the actual stats. As I've always said: "In G_d we trust. Everyone else bring data".

Footnote [2]

Pilot strategy to estimate distance:
"I found that initially by plotting my ground track and then noting prominent features that I would be able to see off to either side - hills, roads, railways, grain silos, power-lines etc - and then measuring them off on the map, I pretty soon acquired a knack for estimating distances to objects and features reasonably accurately. I also found that by checking at how quickly I was passing a feature, and knowing my groundspeed, I could also use that to help estimate distance; naturally the faster the passing relative to the groundspeed, the closer it was. I suppose the basic rule is: get used to the sizes of common, stationary objects or features and how they look from measured distances and consciously plant the size in your mind. From there on it becomes relatively easy to judge distances reasonably accurately. Well, accurately enough not to fly into the things. There's also simply stepping off your fingers over your map track for a reasonable estimation."

References

1: John S Hammond, Ralph L Keeney and Howard Raiffa. *The Hidden Traps in Decision Making. On Making Smart Decisions. HBR's 10 Must Reads*. Harvard Business Review Press, 2013.
2. Rod Baker. Former pilot. Personal correspondence, June 2014.

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