Although you may consider yourself to be a methodical decision maker, who possesses intelligence and patience, like most people, you are also likely a victim of psychological traps. In fact, very smart people likely make the same decision-making mistakes over and over again. Fortunately – or unfortunately – “bad” decision-making can result in positive outcomes. Similarly “good” decision-making processes can result in negative outcomes (just ask anyone who invested money in the NASDAQ in 2000). However, where we can “cleanse” the biases and psychological traps from our decision making processes and become “good” decision makers, we are almost guaranteed more positive versus negative outcomes over our decision-making lifetime.

Before we can cleanse these biases and traps from the way we make decisions, we must first be aware of their existence. Although there are dozens of psychological traps that have been studied by psychiatrists as well as decision-theorists, there are five that are particularly common. A brief description of these five traps follows.

**TRAP 1: The Anchoring Trap.** How would you answer these two questions:

A. Is the population of Kazakhstan greater than 20 million?
B. What is the population of Kazakhstan?

If you are like most people, the figure of 20 million cited in the first question – a figure chosen arbitrarily – biased your answer. This simple test has been conducted over the years with a consistent result – the people who are shown both questions will almost always generate an answer closer to 20 million than the answer of the people only presented with question B. This is an example of the Anchoring Trap – initial data will almost always “anchor” subsequent thoughts, regardless of their accuracy.

Anchors can take many guises. They can be as simple and seemingly innocuous as a comment offered by your spouse or a statistic from the newspaper. One of the most common types of anchors is a past experience or trend. A manager attempting to forecast the number of projects for the next year, will begin by looking at the number of projects from the previous year. The historical number becomes an anchor, which will then be adjusted based upon other factors. Although this approach may often lead to reasonably good estimates, it tends to give too much weight to the past figure and insufficient weight to other factors. Particularly in situations characterized by rapid change, the historical anchor can lead to poor forecasts and “bad” decision-making.

Whatever their source, anchors often prejudice our thinking in ways that prevent us from making good decisions. Because anchors have the effect of establishing
the terms on which a decision will be made, they are often used by savvy negotiators as a bargaining tactic. For example, let's say you are interested in a piece of art to hang in your office. You visit a local art dealer and see on display a unique and interesting painting by an unknown local artist – a work with no real market value (and no price tag). You estimate its worth to you at $500, but when you begin talking about the painting with the dealer, he suggests a price of $2500. If you respond by bargaining down from $2500, the final cost is then inappropriately influenced by the dealer's initial proposal – the anchor.

**TRAP 2: The Status Quo Trap** You inherit 100 shares of a stock that you would never have bought yourself. You can sell the shares and reinvest the money for a nominal commission and no tax consequences. What will you do?

When faced with this situation, a surprising number of people hang on to the inherited shares. They find the status quo comfortable, and avoid the stress of having to make a decision. “I'll rethink this later”. But later is always later.

In fact, most decision makers display a bias towards alternatives that perpetuate the current situation. On a broad scale, we can see this tendency at work whenever a radically new product is introduced. For example, the first automobiles were called “horseless carriages” and looked like the buggies they replaced.

Experiments have demonstrated that the status quo is stronger when the number of alternatives increases...people are more likely to stay with their current situation when they have five alternatives than if they have one alternative.

**TRAP 3: The Sunk Cost Trap** Three months ago, your eight-year-old car suddenly needed serious engine repairs. Faced with spending $5,000 on the engine work or junking the car and buying a new one, you decide to repair the car. Now however, your transmission is shot and the car needs another $1,500 in work. Alternatively, you could sell the car for $1,000. You know the car will likely continue to need work. What do you do?

If you are like most people, you will decide to fix the transmission, not wanting to “lose” your $5,000 that you spent on the first round of repairs. But that is the wrong decision. Would you make the same decision if the work had been done by a friend for free? Probably not...yet that is how you should think about the problem. What matters NOW is the current condition of the car and the economic pros and cons of the two alternatives. The past has past and is now irrelevant to your current decision-making.

We tend to make choices in a way that allows us to justify our past choices. Our past decisions create what economists call “sunk costs” – investments of time and money that are irrecoverable. We know, rationally, that sunk costs are irrelevant to our decision-making, but nevertheless they prey on our psyche and
lead us to make poor decisions. Acknowledging a decision that has gone wrong is difficult and involves one’s own self-esteem. It may make you open to criticisms from friends, colleagues or family. If you fire your poorly performing recent hire, you are making a public admission of poor decision-making. It may seem psychologically safer to let him or her stay on, even though you are just compounding the error.

**TRAP 4: The Confirming Evidence Trap** For a while you have been concerned that the stock market has gone too high and you have all but decided to sell most of your portfolio and invest the cash in a money market mutual fund. But before you call your broker, you decide to do one more thing to check the wisdom of selling. You call a friend, who you know sold out her portfolio last week, to find out her reasoning. She presents you with a strong case for an imminent market decline. What do you do?

If you are like most people, you will justify your decision to sell based upon your friend’s actions and rationales. This is an example of the Confirming Evidence Trap. This trap leads us to seek out information that support our instinct while avoiding information that contradicts our intuition. Would you have expected your friend to have provided you with a balanced or even alternative position to selling out, when that is exactly what she just did?

The Confirming Evidence Trap not only effects WHERE we go to collect evidence, but also HOW we interpret what we received, leading us to give too much weight to supporting information and insufficient weight to conflicting information.

In one psychological study of this trap, two groups were asked to read two articles on capital punishment. One group was in favor of capital punishment and one group was not. Similarly, one of the articles concluded that the death penalty was effective in reducing the crime rate while the other concluded that it was not. In spite of each article having the same amount of scientific evidence supporting the respective disparate positions, the members of BOTH groups were even more convinced that their position was correct after reading both articles. They accepted the supporting information as factual and dismissed the conflicting information.

There are two psychological forces at work here. The first is our tendency to subconsciously decide what we want to do before we figure out why we want to do it. The second is our tendency to be more engaged in things we like than in things we dislike. Naturally then, we are drawn to information that confirms our subconscious leanings.

**TRAP 5: The Framing Trap** In one experiment, the impact of framing was explored by posing the following problem to a group of insurance professionals:
You are a marine property adjuster charged with minimizing the loss of cargo on three insured barges that sank yesterday off the coast of Alaska. Each barge holds $200,000 worth of cargo, which will be completely lost if not salvaged within the next 72 hours. The owner of a local marine salvage company gives you two options, both of which will cost the same –

A. Save the complete cargo of only one of the barges.
B. Engage in an operation that has a one third probability of saving the cargo on all three barges, but a two thirds probability of saving nothing.

If you are like 71% of the respondents in the study, you will choose the “less risky” plan A, which will save one barge for sure. Another group in the same study were presented with options C and D –

C. Engage in an operation that will result in the certain loss of two of the three barges.
D. Engage in an operation that has a two-thirds probability of resulting in the loss of all three barges and the entire $600,000, but has a one third probability of losing no cargo.

Faced with this choice, 80% of the respondents preferred plan D.

The pairs of alternatives are, of course, equivalent – they have simply been framed in different ways. The strikingly different responses reveal that people are risk-adverse when a problem is posed in terms of gains (barges saved) but risk-seeking when a problem is posed in terms of avoiding losses (barges lost). Furthermore, they tend to adopt the frame as it is presented to them rather than restating the problem in their own way.

The same problem can also elicit very different responses when frames use different reference points. Let’s say you have $2,000 in your checking account, and you are asked the following question –

Would you accept a 50-50 chance of losing $300 or winning $500?

Now, what if you were asked a different question –

Would you prefer keeping your current checking account balance or accepting a 50-50 chance that would result in having $1700 or $2500 in your account?

Once again, the two questions pose the same problem. Although your answers to both questions should, in theory, be the same, studies have shown that many people would refuse the first chance but accept the second chance. Their different reactions result from the different reference points of the two frames. The first frame, with its reference point of 0, emphasizes incremental gains and losses, and the thought of losing triggers a conservative response in most
people’s minds. The second frame, with its reference point of $2,000, puts things into perspective by emphasizing the broader financial impact of the decision.