

Predictably Irrational – Dan Ariely

Notes and Takeaways via Duncan Kelm

The decoy effect; when comparing two options, if there is another like comparable it makes it much easier to gauge

- o For example if there is just an A and B options that are not very similar it would be hard to judge, if there was an A and A-, it becomes much easier to value
- o Think about this when working with clients, need to paint the comparison our service is “better” than
- o Once you see the decoy effect in action, it becomes much more apparent that it is a secret agent of decision making

Relativity; when comparing things, we always think in a relative way aka A and A- options above

- o For example if you are in the Safeway shopping center and you can go to the dollar store for a greeting card or Safeway, and the price is \$5 difference, you will make the effort, but if the dollar store was across town, it is not a relative comparison and you may just purchase the greeting card at Safeway

The more you have, the more you want, the only cure is to break the cycle of relativity

To make a man covet a thing or object you must only make the thing difficult to obtain

Anchors; something that ties our thoughts of something to a specific price or view

- o For example, housing comps, if you have something to anchor your analysis you are more likely to arrive at a number that is close to that price
- o In Ariely’s studies when an anchor was used it was always proven to impact the decision making and pricing
- o Anchors can adjust over time, e.g. price of gas, what is the expected anchor today \$4.50 in CA

Herd yourself; deciding something is good based on another’s interest in it

- o For example if you walk by a restaurant and there are three people in line waiting you would think “this must be a popular restaurant” and you join the line, thus adding to the herd
 - When you do this, you set an anchor, and reinforce the anchor after by “enjoying” the meal
- o You can build herd support for yourself
 - For example; if you have gone to Starbucks and had an experience where the caffeine woke you up and you had a positive experience that sensation will send you into Starbucks a second time, ignoring that there may be cheaper or better coffee closer. This will build on itself like a chain reaction until Starbucks is ingrained in people’s minds with the emotion of caffeine bump

Because of these different biases, you should constantly question your repeated behaviors

Price of supply has impact as well as demand

- o The sensitivity we show to price changes might in fact be largely a result of our memory for the prices we have paid in the past and our decision for coherence with our past decisions

The cost of zero; zero is an emotional hot button – a source of irrational excitement

- o Free impacts a lot of decision making; will often take a buy one get one free deal which could be worse than just buying two other like items
- o Making something “free” can actually drive serious demand for that item
- o When we pay for something, there is something called the “pain of paying” that is associated with giving up hard earned cash. When you get something for free it eliminates this pain and thus replaces it with pleasure

Pain of paying goes down as price goes up

- o If you are buying a car, an extra \$300 does not seem like a lot, however if you are buying a coffee table, an extra \$300 will seem astronomical, yet it is still \$300 dollars
- o Analogously if you add one pound to a backpack it will seem like a substantial increase of weight
- o Because purchasing something is more or less painful (giving up cash), zero or free is an important and emotional concept for people

Social norms vs market norms; when social norms and market norms collide, trouble sets in

- o Social norms tend to motivate and drive individuals more
- o Ariely’s study proved that social norms drove greater effort than a dollar incentive
- o No one is offended by a small gift because that is a social norm rather than a market norm, as soon as you label a gift with a price tag, e.g. 50 cent Snickers, it crosses into market norms
- o It is important to keep social relationships and market relationships separate
 - They can cohabitate, but it must be a clear line, e.g. financial advisor and friends, when we are talking finance it is all business
- o If you want to be accepted or demonstrate affection, then the best way to do this is to give a gift
- o Offering someone a small amount of money for their help breaches the social norms and makes it seem more like work. E.g Will you help me move, I’ll pay you \$20. They now associate it with work
- o Anytime you involve money it takes a relationship or interaction from the social norms to the market norms
- o When price is not part of an exchange people become less selfish. E.g. when Ariely offered Starbursts to students for free or for \$.01. When it was free students took far fewer thinking of the others to come. When they were \$.01 each student loaded up. The penny charge made the situation a market scenario from a gift scenario

- o Procrastination and self-control
- o Openly committing to something, drastically increase the likelihood of successfully achieving a goal
- o The same goes for writing a goal down
- o If a particular desired behavior results in an immediate negative outcome (punishment), this behavior will be very difficult to promote, even if the ultimate outcome is highly desirable
- o Important to tie rewards to achieving small goals throughout the process. A reward is far more likely to motivate
- o Useful to look for tricks that match immediate, powerful, and positive reinforcements with the not-so-pleasant steps to take towards long term objectives
- o One man's ceiling is another man's floor

The high price of ownership

- o We are predisposed to be instantly attached to what we already have
- o In our industry, people become very tied to individual stocks
- o In the crypto industry people are openly committed to the idea of crypto so they cannot be seen to back off
- o It is very hard to upgrade a possession and then after its use go back down. You set the bar and then likely only continue to raise it
- o A great idea; view all transactions, especially large ones, as if you are a non-owner, putting some distance between yourself and the item of interest
- o We all have a propensity to overvalue what we own, it is a basic human bias and it reflects a tendency to fall in love with, and be overly optimistic about, anything that has to do with ourselves

Keeping doors open

- o All people have the tendency to try to keep as many doors open as possible even when this causes great expense
- o Ambience and expectation add a great deal to enjoyment. If you are going into an event and have great expectations for why it will be fun, most times you will find reasons to say that it was fun
- o Ariely proved expectation was an important part of the way we experience music
- o Blessed is he who expects nothing, for he will never be disappointed
- o Ariely proved that positive expectations allow us to enjoy things more and improve our perception of the world around us
- o Beliefs and expectations affect how we perceive and interpret, sights, tastes, and other sensory phenomena, but also that our expectations can affect us by altering our subjective and even objective experiences

The cycle of distrust

- o One you begin to cheat a little, it will slowly become a habit overtime

- o Trust once eroded, is very hard to restore
- o Trust is an important, tangible public resource to be protected and cared for
- o All people innately have a desire to please