**Judgement in Managerial Decision Making Max Bazerman**

**Chapter 1 Introduction to managerial decision making**

* Without an understanding of our though and behaviours, we cannot anticipate when the cognitive processes that usually serve us so well are likely to lead us astray.
* 6 steps when applying a “rational” decision making process
  + Define the problem – don’t solve the wrong problem. Error by defining the problem in terms of a proposed solution, missing a bigger problem or diagnosing the problem in terms of its symptoms. Goal to solve problem not eliminate its temporary symptoms.
  + Identify the criteria – usually more than one objective.
  + Weight the criteria – varying importance.
  + Generate alternatives – possible courses of action. An optimal search continues only until the cost of the search outweighs the value of the added information.
  + Rate each alternative on each criterion – most difficult stage.
  + Compute the optimal decision – by multiplying rating in step 5 by weight of each criterion, adding up the weighted ration across all criteria and choosing the solution with the highest sum of weighted rations.

**System 1 and system 2 thinking**

* S1 refers to our intuitive system, typically fast, automatic, effortless, implicit and emotional, we make most decision in life using s1 thinking. S2 refers to reasoning that is slower, conscious, effortful, explicit and logical.
* S2 should influence our most important decisions. Key goal is to identify situations where s2 is needed.
* Most people have great deal of trust in intuitions – s1 thinking – the drawing of two rotated tables example

**The bound of human rationality**

* The rational model based on a set of assumptions that prescribe how a decision SHOULD be made rather than describing how a decision is made.
* Two schools of thought – prescriptive – develop methods for making optimal decision. Descriptive – consider how decision are actually made.
* Decision makers will forgo the best solution in favour of one that is acceptable or reasonable, that is we satisfice, simply search until we find a satisfactory solution that will suffice.
* Humans usually rely on rule of thumb or heuristics.
* Bounded rationality – willpower is bounded, our temporary motivations are often in consistent with our long term interest. Our self-interest is bounded.

**Introduction to judgemental heuristics**

* Heuristics provide time pressured managers a simple way of dealing with a complex world. Usually produce correct or partially correct judgments.
* Reliance may create problem, people typically unaware they rely on them. May lead people astray

**The availability heuristic**

* People assess the frequency, probability of an event by the degree to which instances or occurrences of that event are readily “available” in memory. An event that evokes emotions and is vivid, easily imagined and specific will be more available than an event that is unemotional in nature, bland, difficult to imagine or vague.
* E.g. a subordinate who works closer to manager’s office is likely to receive a more critical perf evaluation at year end as manger is more aware of nearby person’s errors.
* Product manager base assessment of probability of new products success on recollection of the successes and failure of similar products in the recent past.
* Fallible because the availability of info is also affected by factors unrelated to the object frequency of the judged event. (vividness) can inappropriately influence
* “the more available the stock is, the more overvalued it will be”

**The representativeness heuristic**

* Tend to look for traits an individual may have that correspond with previously formed stereotypes.
* “the plant is categorised as belonging to the species that its principle features most nearly resemble”
* Offers a good first cut approximation, drawing our attention to the best options.

**Positive Hypothesis Testing**

* Four separate situations to consider when assessing the association between 2 events, assuming that each one has 2 possible outcomes. Over everyday decision making commonly neglects this fact.
* Use selective data when testing hypotheses in which the variable of interest is present. Called the positive hypothesis testing or congruence heuristic.
* Can trigger the confirmation bias, anchoring, overconfidence of the hind sight bias.

**The Affect Heuristic**

* Our judgements are evoked by an effective or emotional evaluation that occurs even before higher level reasoning takes place. Could be how a candidate compares to the previous application or the mood of the manger.
* Has been shown that stock prices go up on sunny days, presumably due to the good mood and optimism induced by the weather. Can be a good guide but can prevent making optimal choices.
* Outrage heuristic – the fact that legal awards are highly predicted by the jury’s affective outrage at the defendants behaviour, rather than simply by logical reasoning about the harm created by the defendant.
* Lewin says for change to be successful, necessary to get the individual to unfreeze existing decision making processes, provide the content necessary for change, and create the conditions that refreeze new processes, thus making the change part of the individual’s standard repertoire.

**CHAPTER 2 COMMON BIASES**

* List of American and non-American companies example.
* American company names are more familiar, more recognisable and more memorable to Americans that the foreign company names – illustrates the availability heuristic.
* Heuristics provide good decisions in a signification proportion of the time, can lead managers to make systematically biased judgments.

**Biases emanating from the availability heuristic**

**Bias 1: Ease of Recall (based on vividness and recency)**

* Example of ranking the deaths in the usa
* The availability of vivid stories in the media biases our perception of the frequency of events toward the more extreme deaths. Overestimate cars guns and drugs
* AIDS story, people ignored it until a woman said she was deliberately spreading it.
* The availability heuristic describes the inferences were make about event commonness based on the ease with which we can remember instances of that event.
* Two group study of list of male and female names, and important people. The important people gender seen as having the most names on the list
* Manager’s performance appraisals- fall victim, working from memory, vivid instances of an employee’s behaviour will be most easily recalled.
* Receny of events also a factor. More weight placed on more recent times.
* People buying insurance after a natural disaster

**Bias 2 : Retrievabilty (based on memory structures)**

* Example, estimating words in dictionary with a, and words with a as third letter
* We are better at retrieving words from memory using the words initial letter than the words third letter
* Retail store location is influenced by the way in which consumers search their minds when seeking a particular commodity.
* Why are multiple gas stations at the same junction or the same upscale retailers in the same mall – consumers learn the location of a particular type of product or store and organise their minds accordingly.

**Biases emanation from the representativeness heuristic**

**Bias 3: insensitivity to base rates**

* Down syndrome example, probability.
* Tend to ignore the base rate – the overall prevalence of DS
* Causes people to ignore background info relevant to the problem
* Tendency is even strong when the specific info is vivid and compelling
* Example of layer and engineer group, 70, 30 and 30 70, all people said engineer no matter the group size
* Participants do use base rate data correctly when no other info is provided. People understand the relevance of base rate info but tend to disregard such data when individuating data are also available.

**Bias 4: Insensitivity to sample size**

* Example of hospital and male birth rates
* People have basic idea of how unusual it is to have 60 percent of a random event occurring in a specific direction
* Sample size rarely part of our intuition
* When responding to problems dealing with sampling, people often use the representativeness heuristic

**Bias 5: Misconceptions of Chance**

* Example of family of children, will next be a boy or girl
* Triggers our inappropriate tendency to assume that random and non-random events will balance out.
* The gamblers fallacy
* “Chance is commonly viewed as a self-correcting process in which a deviation in one direction induces a deviation In the opposite direction to restore equilibrium. In fact, deviations are not corrected as a chance process unfolds, they are merely diluted”
* Streaks are part of our conception of chance in athletic competition.
* We don’t think of a string of four in a row shots as a situation where he missed his fifth shot. As a result we have a misconception of connectedness, when in fact chance is actually in effect
* Leads people to see patterns where there are none.

**Bias 6: Regression to the mean**

* Example of batting averages
* Basic principles of statistics tell us that any extreme performance is likely to regress to the mean over time.
* Gifted children frequently have less successful sibling. Short parents tend to have taller children
* Individuals typically assume that future outcomes will be directly predictable from past outcomes. Thus we tend to naively develop predictions based on the assumption of perfect correlation with past data.

**Bias 7: The conjunction fallacy**

* Lisa teacher example, the and rule
* People make judgments according to the degree to which a specific description corresponds to a broader category within their minds.
* Probability – the subset cannot be more likely than a larger set that completely includes the subset.
* Predicts that a conjunction will be judged more probably than a single component descriptor when the conjunction appears more representative than the component descriptor.

**Biases emanating from the confirmation heuristic**

**Bias 8: The confirmation trap**

* Example 2,4,6 rule
* Rule is broader “any three ascending numbers” solution requires participants to accumulate disconfirming, rather than confirming evidence
* When we encounter info that is consistnet with our beliefs, we usually accept it with an open mind and a glad heart.
* We accept info uncritically unless there is an unavoidable reason to doubt it
* Death penalty example – both groups left the experiment even more solidly assured of their opening opinions
* Management consulting- yes person versus the devils advocate

**Bias 9: Anchoring**

* Phone number and guessing taj mahal build date.
* People influenced by irrelevant information
* We often develop estimates by starting with an initial anchor that is based on whatever info is provided and adjust from the anchor to yield a final answer
* Existence of an anchor leads people to think of info that is consistent with that anchor rather than accessing info that is inconsistent with the anchor.
* We place much emphasis on initial impression anchors and fail to adjust our opinion appropriately at a later date when we have the chance to do so

**Bias 10: Conjunctive and disjunctive events bias**

* Which event appears most likely example
* Bias to over estimate the probability of conjunctive events, and to underestimate disjunctive events or events that occur independently

**Bias 11: Overconfidence**

* The ten questions example, name upper and lower bound
* Most of us are overconfident in the precision of our beliefs and do not acknowledge our true uncertainty.
* Can be a barrier to effective professional decision making
* Too sure that we know the right answer, we become impervious to new evidence or alternative perspectives
* Confirmation heuristic leads to over confidence

**Bias 12: Hindsight and the curse of knowledge**

* “I knew that was a bad play”
* We are not very good at recalling or reconstructing the way an uncertain situation appeared to us before finding out the results of the decision.
* Tend to overestimate what we knew beforehand based upon what we later learned.
* Example of participants and war story, they believe that even if thye had not been told the outcome, they would have judged the outcome that they were later told had happened as being most likely.
* Knowledge of an outcome increases an individuals belief about the degree to which he or she would have predicted that outcome without the benefit of that knowledge.
* Knowledge of an events outcome works as an anchor by which individuals interpret their prior judgements of the events likelihood
* Hindsight knowledge biases our perceptions of what we remember knowing in foresight
* Reduces our ability to learn from the past and to evaluate decisions objectively, individuals should be judged by the process and logic of their decisions, not just on their results.
* Curse of knowledge – designing tech, to technical for ordinary people – half of high tech devices that consumers return as malfunctioning are in fact in perfect working order, the consumer just cant figure out how to use it

**Integration and commentary**

* Heuristics – any loss in decision quality will be out weighted by time saved

**CHAPTER 3: BOUNDED AWARENESS**

* Rely on heuristics because they provide an efficient way to simplify complex decisions
* People lack the attention and brain power to pay attention to every potentially relevant fact or piece of info
* Example 6 v 26 jam choices, people less likely to buy when there is a bigger selection
* Bounded awareness, prevents them from noticing or focusing on useful, observable and relevant data
* Often leads people to ignore accessible, perceivable and important info, while paying attention to other equally accessible but irrelevant info
* People naturally create a boundary that frames the problem and constrains them from finding a solution, example does not tell you to keep your pencil within the bounds imposed by the nine dots
* The most critical barriers to creative decisions are out assumptions or the info we allow into the defined problem space.
* Tendency to place false perceived bounds is a very common aspect of decision making

**In attentional blindness**

* Example of two groups playing basket ball and money
* By focusing on one task people miss very obvious info in their visual world
* Have a tendency not to see what they are not looking for, even when they are looking directly at it

**Change Blindness**

* People fail to notice visual changes in their physical environments
* Person holding basketball and asking for directions example. Someone else comes in and takes the ball, no one notice
* Example – change of character clothes during a set
* People are even more prone to missing changes that occur gradually
* Auditing example – slowly voilateing the laws
* Much more likely to notice and refuse to sign the statemetns if the ethical lapse occurs abruptly from one year to the next – based on the notion of “slippery slope” of unethical behaviour
* Slippery slope theory – one tiny step away from high ethical standards puts a corporation on a slippery slope downward into larger ethical lapses. More likely to occur through tiny slips than in one fell swoop
* Boiling frog – if you throw a frog in boiling water it will jump out. But if you put a frog in nice warm water and slowly raise the temperature, by the time the frog realiases the water ahs become too hot, it will already be cooked

**Focalism and the focusing illusion**

* Focalsim – tendency to focus too much on a particular event and too little on other events that are likely to occur concurrently
* Tend to overestimate the impact of positive and negative events, such as the wins and losses of our preferred team or candidate, on our overall happiness.
* Focusing illusion- tendency of people to make judgements based on their attention to only a subset of available info, to overweight that info, and to underweight unattended info
* Example the probabilities of each of the 8 teams winning, totalled more than 100%
* Challenger example – not looking at the o-ring that had survived

**Bounded awareness in groups**

* Info discussed by a group has a key influence on any final decision
* The awareness of groups is bounded by the information that becomes part of the discussion
* Has advantage of collectively possess more info than does any individual member
* Sharing unique info is a critical source of group potential
* Tendency of groups to focus more on shared info (info previously known to all group member) than on unique or unshared info (info previously known by only one member of the group)
* Example of sharing info about a candidate v not sharing it, with both groups collectively having the same data

**Bounded awareness in strategic settings**

* Minor changes in the decisions of others and the ruls of the game can create huge differences in the optimal strategy for a negotiator – bounded awareness, most people miss this info

**Multiparty ultimatum games**

* Zero sum games
* Bounded awareness keeps negotiators from failing to differentiate the problems

**The monty hall game**

* Door opens, probabilities change

**Acquiring a company example**

* Example when you are buying a gem stone and make an offer that you think is on the low side and the mercent accepts straight away, how do you feel – known as the winners curse. But if you were comfortable with your voluntary offer, why would you suddently wish it had not been accepted?
* In the bargaining context, key feature of the winners curse is that one side often has much btter info than the other side

**What do people actually do?**

* an overly narrow focus on their own thoughts and actions causes negotiators to ignore the rules of the game and the decisions of the opposing party
* individuals systematically exclude info from their decision making processes that they have the ability to include
* social interaction creates a mechanism to overcome the inefficient outcoems predicted by game theory and behavioural decision theory
* people have beter info about the home team than they do about the competition, and they don’t bother collecting more balanced info before placing their bets

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