https://utilitarianism.net/theories-of-wellbeing/

A core element of utilitarianism is welfarism—the view that only the welfare (also called well-being) of individuals determines how good a particular state of the world is. While consequentialists claim that what is right is to promote the amount of good in the world, welfarists specifically equate the good to be promoted with well-being.

The term well-being is used in philosophy to describe everything that is in itself good for someone—so-called intrinsic or basic welfare goods—as opposed to things that are only instrumentally good. For example, happiness is intrinsically good for you; it directly increases your well-being. In contrast, money can buy many useful things and is thus instrumentally good for you, but does not directly, in itself, contribute to your well-being. (We can similarly speak of things that are intrinsically bad for you, like misery, as "welfare bads".)

The three main theories of well-being are hedonism, desire theories, and objective list theories.

Hedonism

Hedonism is the view that well-being consists in, and only in, the balance of positive over negative conscious experiences.

Hedonism about well-being should not be confused with psychological hedonism, the dubious empirical claim that humans always pursue what will give themselves the greatest happiness.

The hedonistic conception of happiness is broad: It covers not only paradigmatic instances of sensory pleasure—such as the experiences of eating delicious food—but also other positively valenced experiences, such as the experiences of solving a problem, reading a novel, or helping a friend. Hedonists claim that all of these enjoyable experiences are intrinsically valuable. Other goods, such as wealth, health, justice, fairness, and equality, are also valued by hedonists, but they are valued instrumentally. That is, they are only valued to the extent that they increase happiness and reduce suffering.

Desire Theories

Desire theories hold that well-being consists in the satisfaction (minus frustration) of desires or preferences.

According to desire theories, what makes your life go well for you is simply to get whatever it is that you want, desire, or prefer. Combining utilitarianism with a desire theory of well-being yields preference utilitarianism, according to which the right action best promotes (everyone's) preferences overall.

Objective List Theories

Both hedonism and desire theories are monist. They suggest that well-being consists of a single thing—either happiness or desire satisfaction. In contrast, while objective list theorists usually agree that happiness is an important component of well-being, they deny that it is the only such component; consequently, objective list theories are pluralist.30

Objective list theories hold that there are a variety of objectively valuable things that contribute to one's well-being.

In addition to happiness, these lists commonly include loving relationships, achievement, aesthetic appreciation, creativity, knowledge,31 and more. Crucially, these list items are understood as basic or intrinsic goods; they are valuable in themselves, not because of some instrumental benefit they provide. The list is called objective, because its items are purported to be good for you regardless of how you feel about them.

Behavioral Finance

Traditional economic theories assume that people act rationally when making financial decisions. So, what is behavioral finance? It's an economic theory that explains often irrational financial behavior, such as overspending on credit cards or panic selling during a market downturn. People often make financial decisions based on emotions rather than rationality.

Behavioral finance uses financial psychology to analyze investors' actions. According to behavioral finance, investors aren't rational. Instead, they have cognitive biases and limited self-control that cause errors in judgment.[2] Keep reading to explore more about behavioral finance principles.

Daniel Kahneman and Amos Tversky proposed that most investors tend to make decisions based on subjective reference points rather than objectively choosing the best option.

Richard Thaler introduced the notion of "mental accounting," which is the idea that people view their money differently based on its function, such as whether it's for retirement or a college fund. Eventually, their work became the basis for the study of cognitive psychology and behavioral biases in finance, which features prominently in the field of behavioral finance.

Financial Psychology

According to behavioral finance theory, there are several types of cognitive biases that can affect an investor's judgment. Being aware of the most common ones can help you avoid them in order to make more rational decisions.

Overconfidence

Most people tend to overestimate their abilities in many areas. For instance, 65% of Americans think their intelligence is above average, and 73% think they're better-than-average drivers.

When you overestimate how much you know about the market or a specific stock, you'll be tempted to make risky decisions like trying to time the market, which is trying to predict the best time to buy or sell stocks, or overinvesting in high-risk stocks, which are more likely to lose money.

Herd Mentality

Humans are social animals, so going along with the crowd is in our nature. From the hot new fashion trend everyone is wearing to the crowded restaurant that requires you to make reservations months in advance, people tend to make choices based on what others are doing.

In many situations, herd mentality is appropriate and benign—the only lasting harm is old pictures your children will mock (and eventually try to emulate). In financial markets, however, herd mentality can lead to asset bubbles, which is when the price of an asset like a stock rises rapidly but will eventually fall, and market crashes, which occur when a lot of investors sell off their stock.

For example, the recent Silicon Valley Bank collapse was largely driven by social media rumors and ended up being the second-largest bank collapse in U.S. history.

Loss Aversion

People feel the pain of a loss more acutely than the euphoria of a win, even if they win more than they lose. In financial terms, investors will often hold onto stocks they should sell to avoid realizing a loss. Conversely, they may sell too early to avoid further losses, when waiting for a market rebound would be the better option. Often investors with a strong loss aversion bias have portfolios that are too conservative, underperforming market norms.

Confirmation

Confirmation bias explains how two people with opposing viewpoints can hear the same information, and each comes away believing it supports their opinion. When you have a firmly-held belief, you give heavier weight to evidence supporting your belief while minimizing evidence contradicting it.

In finance, confirmation bias can lead you to overlook investment strategies or assets that fall outside of your bubble, causing you to miss significant growth opportunities. You may also invest too heavily in one area because you haven't fully analyzed the risks.

Behavioral Investing

While biases are a critical component in behavioral finance, there are other key elements in the theory, as well.

Heuristics

Heuristics is the process of simplifying a problem when you don't have enough information to make a "perfect" decision. In these instances, you're likely to use a shortcut or rule-of-thumb to make a decision that feels right. Heuristics simplify the decision-making process, which means they simplify the financial decision making process, as well. Without them, you'd have to spend much more time making decisions. However, relying on heuristics without carefully analyzing investment options can lead to irrational or incorrect decisions.

Mental Accounting

In mental accounting, you place different values on money based on how you obtained it. If you buy a winning lottery ticket, for instance, you might blow it all on a spontaneous shopping spree even though you carefully budget your paycheck. This can lead to irrational financial decisions.

Anchoring

Anchoring is a type of heuristics that involves subconsciously using irrelevant information as a reference point. Historical values are common anchors. For example, if you bought a stock for $100 but it starts losing its value, you may be tempted to hold onto it because you don't want to sell it for less.

Salespeople take advantage of anchoring by starting negotiations at far above market value. The inflated price serves as an anchor, so when they come down, it'll seem like a good deal.

Why Behavioral Finance Matters

Understanding behavioral finance can help you better serve your clients. Financial professionals who can use behavioral economics and finance to help their clients identify and overcome financial biases and mistaken heuristics will be in a position to provide more valuable advice. Additionally, experts in behavioral finance are viewed as thought leaders in the financial industry, which can further advance your career.13

Become a Sought-After Financial Expert

While economic theory is rooted in numbers and formulas, people aren't so easily constrained and categorized. Understanding what drives peoples' behavior is essential for fully understanding any human endeavor, and finance is a uniquely human endeavor.