"In high-stakes decisions, sometimes you've just got to go with your gut."

Managers and entrepreneurs face high-stakes decisions throughout their careers. Should they pursue a new market? Start a business? Enter into a joint venture? Make a high-profile hire? When so much is unknown and unknowable, conventional wisdom says to go with your gut. Harvard Business School professor Max H. Bazerman strongly disagrees. Here, the author of *Judgment in Managerial Decision Making* (6th ed., Wiley & Sons, 2005) explains why the worst time to rely on your intuition is when you're making high-stakes decisions.

—Christina Bielaszka-DuVernay, Editor

CBD: Many managers and executives, especially entrepreneurial types, put a lot of credence on their gut. Stories abound about the entrepreneur who decided to start a business that everyone around him said would never fly, and fly it did.

MB: Yes, people do hear those stories, because they make the news. But the vast majority of new businesses fail, and most of them shouldn't have been started in the first place. Our gut makes us more vulnerable to cognitive biases such as overconfidence.

You see this all the time in the realm of investments. An individual investor is convinced that he has the instincts to sniff out the right stock or fund and buy it at the right time. But very few people can do this with any consistency. He should get his asset allocation right and buy index funds, and spend his time more productively—he'd be better off.

CBD: Can you ever entirely free yourself from cognitive biases?

MB: No, not entirely, but you can do a lot to mitigate their effects. Every scientific test of intuition shows that it's profoundly affected by cognitive biases. When you decide to rely on your gut, you're deciding to let those biases run amok. And that's the last thing you want to do when the decision really matters.

CBD: Say an executive is contemplating having his company enter into a joint venture. There's lots of data on the table, but of course the outcome of the deal simply can't be known. Wouldn't this be a time that the business instincts the executive has developed over the years could be helpful in deciding whether to go forward and under what conditions?

MB: No, absolutely not. His so-called business instincts are likely to be swayed by another cognitive bias, the anchoring bias. Anchoring describes the mind's tendency to "anchor" judgments irrationally against a piece of data or information that may or may not be relevant. Say the last JV the company entered turned out well. That fact will anchor the executive's decision, even if that JV was entirely different than the one currently on the table.

A lot of research demonstrates how anchoring affects judgment without the decision maker's conscious knowledge. For instance, researchers Margaret Neale and Gregory B. Northcraft gave a group of realtors nine pages of information about a house. Half the realtors were given information packets containing a lower price, half were given packets containing a higher price. After all the realtors toured the house, Neale and Northcraft asked them what they'd list it at. The average price suggested by realtors whose information packet contained the higher price was 10% higher than the average price suggested by realtors who'd received information containing a lower list price.

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Neale and Northcraft also asked the realtors if the price listed in the documentation affected their decision. Nearly every one of them said it hadn't.

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CBD: What other cognitive biases lead to flawed decisions?

MB: Another common one is the vivid data bias, which describes our tendency to overweight information that we recently received or that stands out for some reason. Managers fall prey to the vivid data bias when assessing potential hires. Say a manager wants to hire a real superstar for a new high-profile position in her department. One of the candidates she's assessing has one amazing success to his credit, but except for that his résumé is pretty ho-hum. The manager deciding whether to hire him is likely to be overinfluenced by the success and to underweight the rest of the evidence on the résumé.

CBD: So when the stakes are high and so much is unknown, what should managers do to make the best possible decision?

MB: The work that researchers Keith Stanovich and Richard F. West have done is very helpful here. They make a distinction between what they call System 1 and System 2 thinking. System 1 thinking is quick, automatic, and intuitive; System 2 thinking is more deliberate and logical, and offers a structured approach to problem solving.

In high-stakes situations, managers should consciously engage in System 2 thinking. This means stepping back from the situation and assessing it as if you were an outsider. You might want to ask someone whose wisdom and judgment you respect to look at it and share their observations and recommendations with you. Another helpful tactic is to map out pros and cons, assign them weights, and use a decision matrix to guide your thinking.

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If you're considering whether you should spend $40 on a flea-market purchase, let your intuition run wild. But when you're making important decisions, you need to check your intuition with very careful analysis. ◆