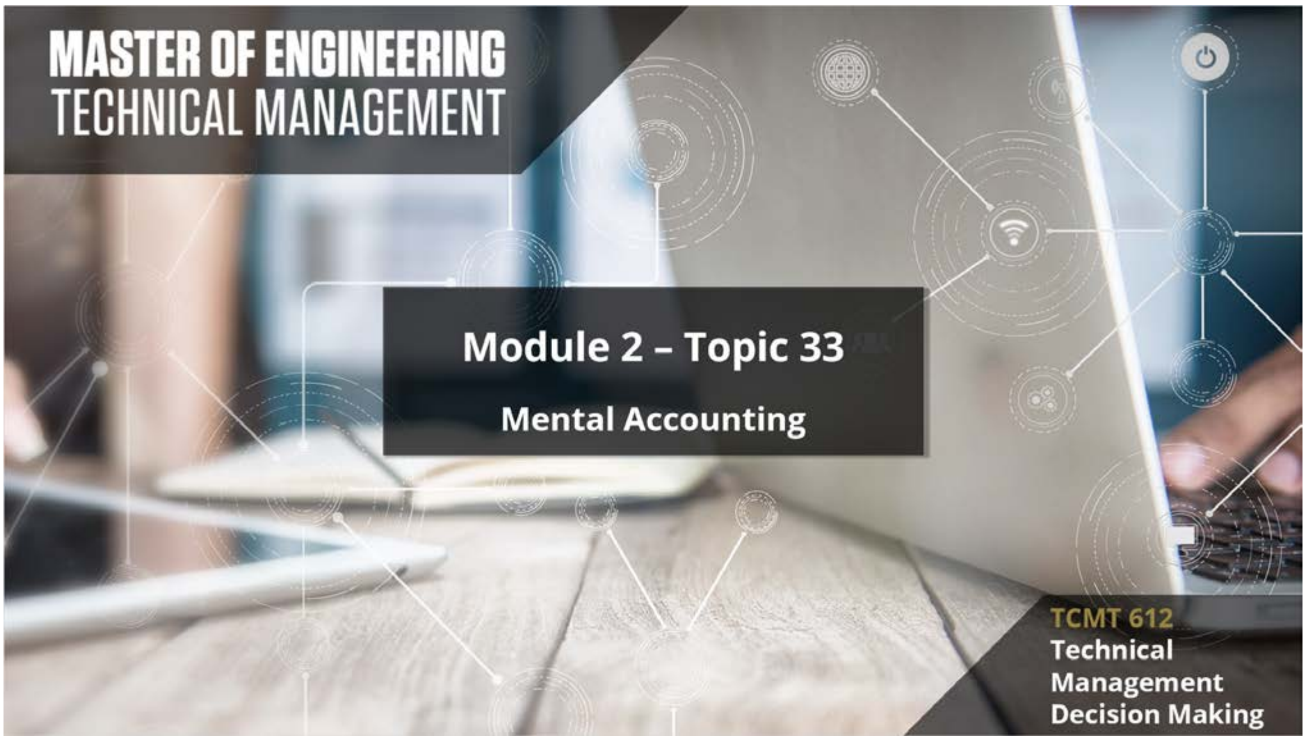
TCMT612_02M_033T_Mental-accounting

1. Main

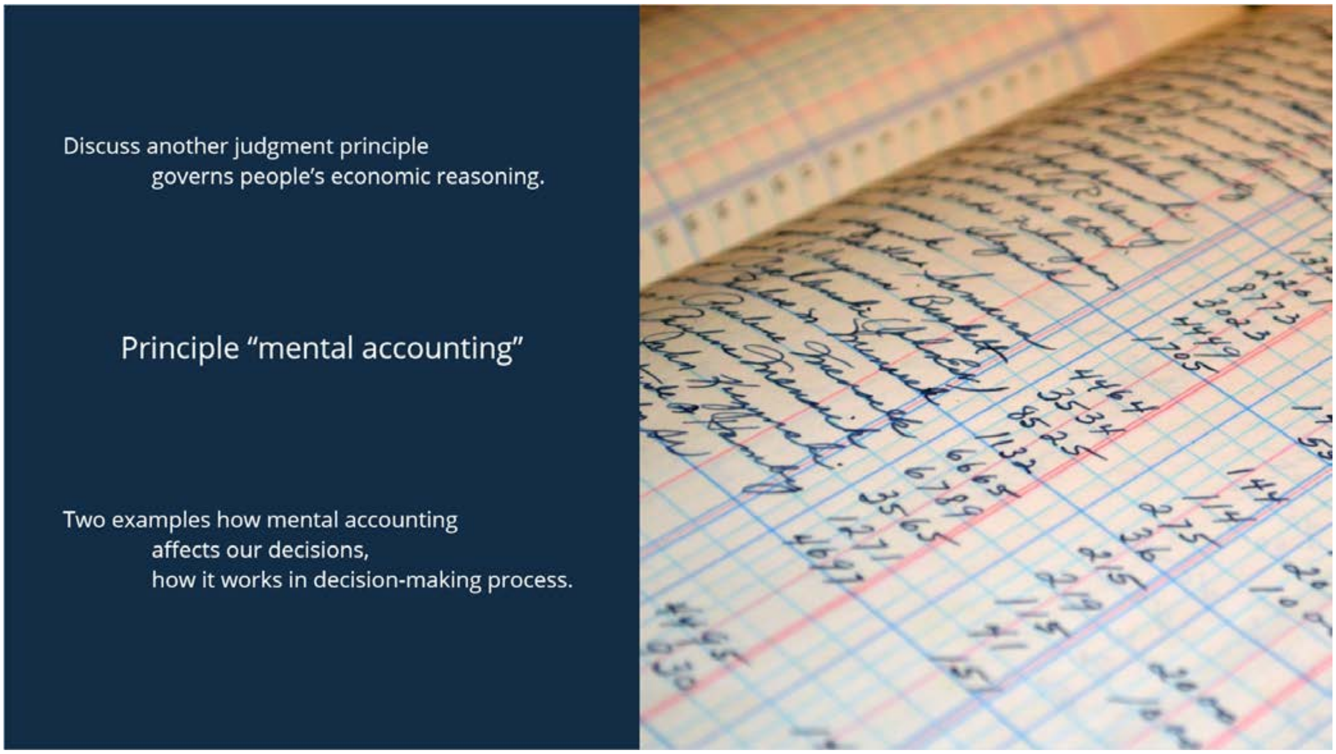
1.2 Topic title



Notes:

In this topic the professor introduces the principle of mental accounting.

1.3 Introduction

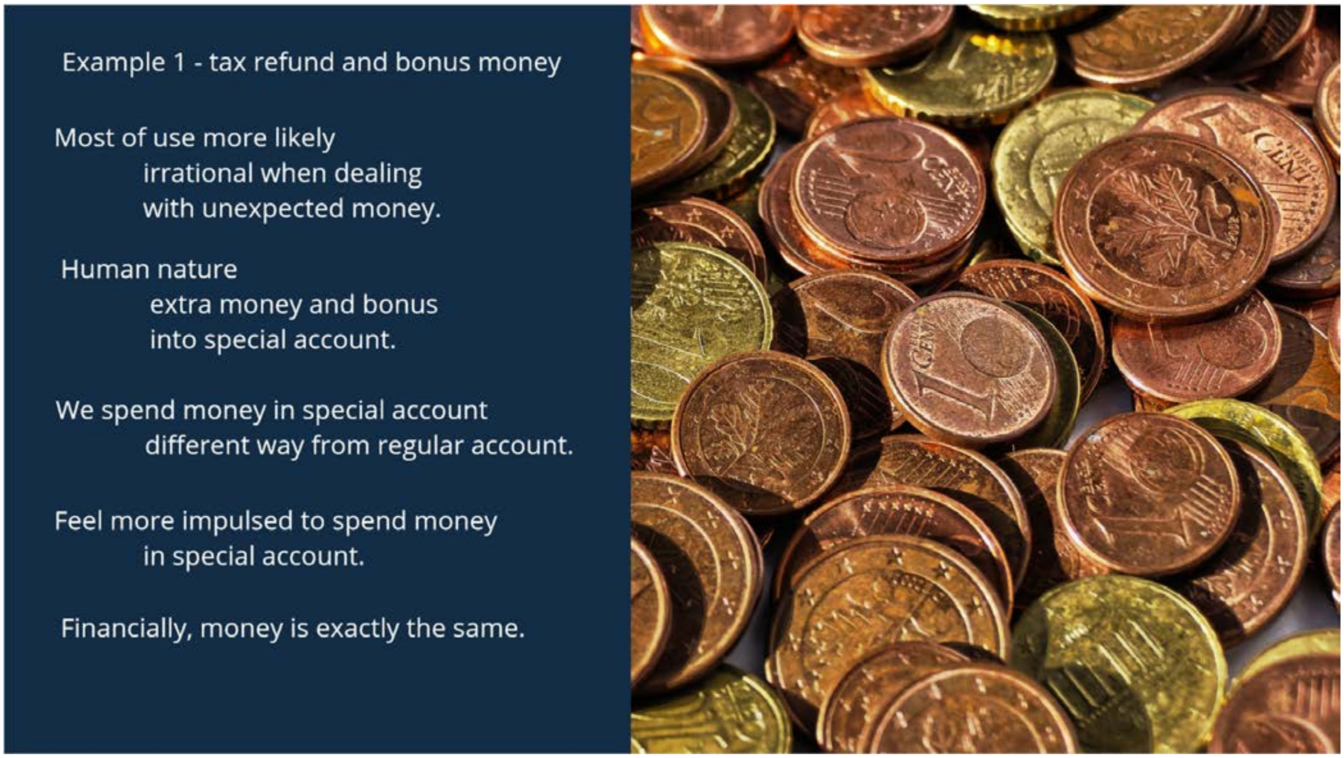


Notes:

Let us change gears a little bit and discuss another judgment principle that governs people's economic reasoning.

The principle is called "mental accounting."
I am going to give two examples to explain how mental accounting affects our decision and how it works in our decision-making process.

1.4 Example 1



Notes:

Example one is how we treat tax refund and bonus money.

Most of us are more likely to be irrational when dealing with unexpected money.

It is our human nature to put extra money and the bonus into a special account, and we spend the money in the special account in a different way from money in a regular account.

We feel more impulse to spend the money in the special account, even though financially the money in two different accounts is exactly the same.

1.5 Example 2

Notes:

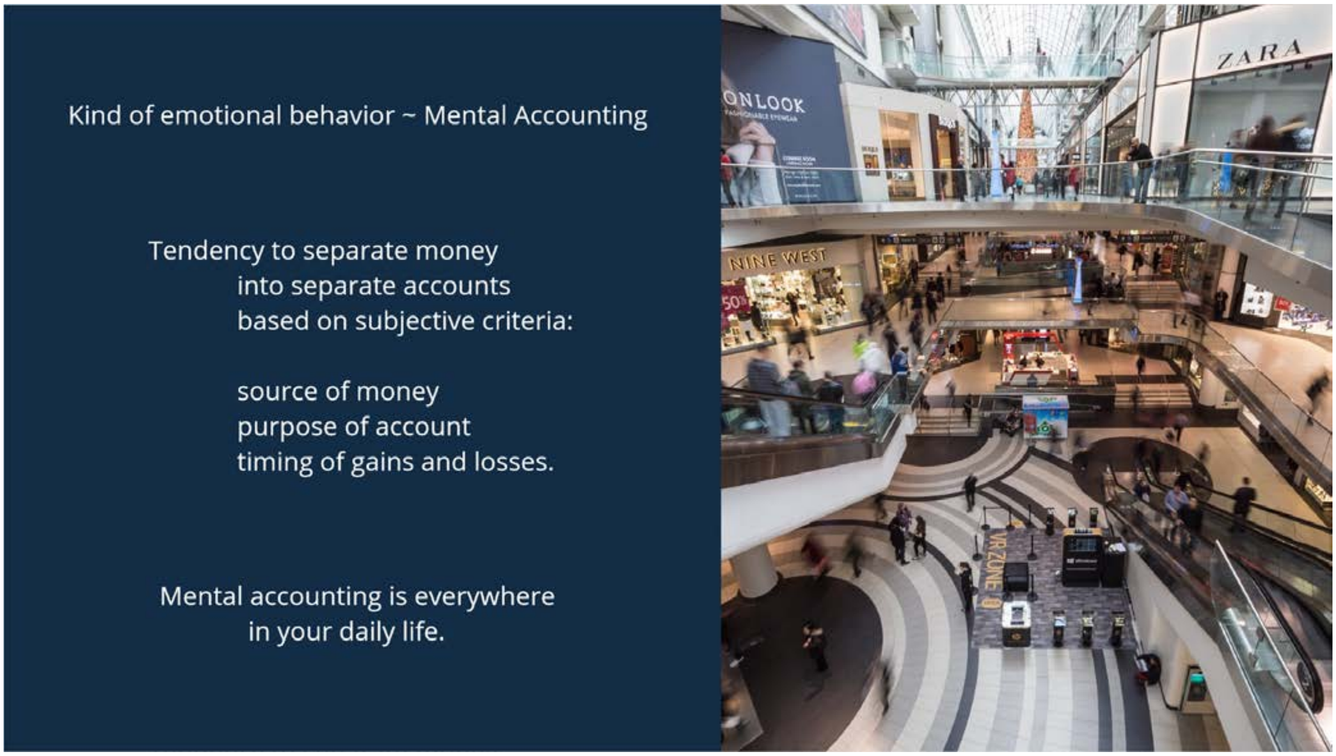
The other great example of mental accounting is our reaction to coupon certificate that grocery stores offer.

Most of the customers spend more money in grocery stores once they receive a small amount coupon.

The excessive spending associated with a coupon is focused on groceries that customers do not typically buy, which means that when we receive the special discount we are more irrational to spend money on other things that we don't expect.

The small amount of extra money drove us to be more irrational and reckless when making a purchasing decision.

1.6 Daily life



Notes:

This kind of emotional behavior is called mental accounting, which refers to the tendency for people to separate their money into separate accounts based on a variety of subjective criteria, like the source of the money, the purpose for each account, and timing of gains and losses.

Mental accounting is everywhere in your daily life.

1.7 Different purposes

Notes:

In addition to different sources, different purpose also create a strong mental accounting bias, and this is very common in the investment fields.

For instance, many investors put some amount of their investment capital in a special account in addition to their normal account.

The special category is high-risk fund or the money they can afford to lose.
Thus, investors are more comfortable investing the money in the special account in high-risk projects that they normally do not invest in.

Those investors make very different decisions with their money in the special account that was created for specific purpose.

1.8 YouTube

Notes:

The YouTube video explains mental accounting with some animation and more details.

Enjoy it. https://www.youtube.com/watch?v=4TuQ7YI-soQ