

The Advisory Alliance

60-Second Email™ – August 29, 2006

Is Rational Decision-Making an Illusion? The Impact of Framing.

In this month's 60-Second Email™, we finish our brief look at the work of Daniel Kahneman, world renowned psychologist and 2002 Nobel Prize winner in Economic Sciences. Much of Kahneman's work examines how people make decisions and to what extent people decide *rationally*. Kahneman observed that decision-making is influenced by several factors, avoidance of loss being one of them (the focus of last month's 60-Second Email™), and "framing" being another, the focus of this month's Email™.

Here's a very concrete and timely example of framing that Kahneman used in his 2002 Nobel Prize acceptance speech, which was well before public awareness of avian influenza, or bird flu:

The Asian Disease – Version 1

"Imagine that the United States is preparing for the outbreak of an unusual Asian disease, which is expected to kill 600 people. Two alternative programs to combat the disease have been proposed. Assume that the exact scientific estimates of the consequences of the programs are as follows:

- If Program A is adopted, 200 people will be saved.
- If Program B is adopted, there is a one-third probability that 600 people will be saved and a two-thirds probability that no people will be saved.

Which of the two programs would you favor?"

In this version, a substantial majority will favor Program A.

The Asian Disease – Version 2

In the second version, everything remains the same, including the Program outcomes, but the Program outcomes are *described* differently.

- "If Program A is adopted, 400 people will die.
- If Program B is adopted, there is a one-third probability that nobody will die and a two-thirds probability that 600 people will die."

Which of the two programs would you favor?"

In this version, a notable majority will prefer Program B instead.

Why is this so noteworthy? Well, if you compare Program A in both Versions, you will see that the outcome is identical, only worded differently: In both Programs A, 200 people live and 400 people die. If you compare Program B in both Versions, you will see that again the outcome is identical, only worded differently: In both Programs B, the odds of everyone living and everyone dying are the same.

So why are we inconsistent in our decision-making? Why do we tend to choose Program A in Version 1 but avoid Program A in Version 2, especially given that both Programs A contain the same outcome, just worded differently? The answer: "Framing".

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As Kahneman observes, in Version 1 “the certainty of *saving* 200 people is disproportionately *attractive*”, and so people prefer Program A, the sure bet (“200 people will be saved”). In Version 2, “the certainty of deaths is disproportionately *aversive*”, and so people avoid Program A, the sure bet (“400 people will die”) even though the outcome is the same, namely that 200 people will be saved.

If math is not your strong suit, my apologies for what must seem like the solution to Fermat’s Last Theorem. Net, net: people tend to overweight *certain* (as in “known for certain”) outcomes. More specifically, our decisions are affected by framing:

- When choices lead to different *positive* outcomes, people tend to choose the outcome that’s certain.
- When choices lead to different *negative* outcomes, people tend to *avoid* the outcome that’s certain.

So in many ways people do not decide rationally. As we saw last month, often we would rather avoid loss than seek gain. And how we decide is heavily dependent upon the framing of our decisions: specifically, the nature of their outcomes (positive or negative), and the certainty of those outcomes.

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Until next month,

David

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