Cognitive bias

Social

Financial

Failure to estimate

Short-termism

When it comes to assessing risk, humans often fail to make rational decisions because our brains take mental shortcuts that prevent us making the correct choice. Since the 1960s behavioural scientists and psychologists have been researching these failings, and have identified and labelled dozens of them. Here are some that can cause havoc when it comes to assessing risks in business

The notion of cognitive biases was first introduced by psychologists Amos Tversky and Daniel Kahneman in the early-1970s. Their research paper, Judgment Under Uncertainty: Heuristics and Biases', in the Science journal has provided the basis of almost all current theories of decision-making and heuristics. Professor Kahneman was awarded a Nobel Prize in 2002 after further developing the ideas and applying them to economics.

ANCHORING EFFECT

Relying too much on the initial piece of information offered when making decisions

"The first test seemed OK. Do we need to look any more?"

AVAILABILITY HEURISTIC

Overestimating the importance and likelihood of events given the greater availability of information

"I saw something very similar to this on LinkedIn. We need to take it seriously'

BANDWAGON EFFECT

Uptake of beliefs and ideas increases the more that they have already been adopted by others

"The whole department knows there's no problem here"

Basing the strength of an argument on the believability or plausibility of the conclusion

"I didn't quite follow your argument but the conclusion seems about right"

BLIND SPOT BIAS

Viewing oneself as less biased

"Let's ignore Sarah's views on this one. She's biased'

CLUSTERING ILLUSION

Erroneously overestimating the importance of small clusters or patterns in large data

"This is the second week in a row that this has happened. There must be a problem"

CONFIRMATION BIAS

Focusing on information that only confirms existing preconceptions

"We did loads of simulations. Most of them showed there's no problem"

COURTESY BIAS

"The last time we discussed this the meeting lasted for hours. Let's move on'

ENDOWMENT EFFECT

The tendency for people to ascribe more value to things merely because they already own/have them

"I know it will cost a fortune to fix but it cost us £15,000. We can't just throw it away."

GAMBLER'S FALLACY "The conveyor belt broke three

Believing that future probabilities are times last month. It's pretty altered by past events, when in fact unlikely it'll happen again." they are unchanged

> "Let's just get the deal done ASAP

HYPERBOLIC DISCOUNTING

Preferring a smaller, sooner payoff over a larger, later reward

"This worked fine in the factory in the Korea, it should work fine here"

ILLUSION OF VALIDITY

doesn't exist

Overestimating our ability to make accurate predictions, especially when data appears to tell a coherent "story"

OSTRICH EFFECT

Avoiding negative financial

information by pretending it

"Looks like we've run out of time to discuss this"

> POST-PURCHASE "We made a good RATIONALISATION call on that one"

"Our competitors are only doing well because their products are cheap"

"Now we've got the new equipment we can cut the time spent on maintenance'

REACTIVE DEVALUATION

Devaluing an idea because it originated from an adversary or opponent

Tendency to retroactively ascribe positive

attributes to an option one has selected

RISK COMPENSATION

Taking bigger risks when perceived safety increases; being more carefu when perceived risks increases

STATUS OUO BIAS

Preferring the current state of affairs

"Dave from tech is worried

- but frankly the tech team are always pessimists"

"If it ain't broke - don't fix it"

STEREOTYPING

because they are a member of a group

RACONTFUR