

UNLIMITED POTENTIAL

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Newsletter

The 8 Traps of Decision Making

Before making an important decision, prudent managers evaluate the situations confronting them – and often fall into one of the eight traps of faulty thinking.

Some managers are too optimistic and overconfident: They overestimate success and underestimate the range of potential outcomes. On the flipside, other managers are cautious to a fault: They take costly steps to defend against unlikely outcomes.

These are just two of the well-documented psychological traps that ensnare most managers at some point in their careers. Other pitfalls that distort our reasoning abilities and cater to our biases are identified in the classic 1998 *Harvard Business Review* article “The Hidden Traps in Decision Making,” by John S. Hammond, Ralph L. Keeney and Howard Raiffa:

- We have a tendency to stick with the status quo.
- We only look for evidence that confirms our preferences.
- We are likely to throw good money after bad to defend our position and avoid admitting a mistake.

The way a problem is framed can influence how you develop solutions. To avoid this trap, you need to reframe the question in various ways to see how your thinking may change based on each version.

We can't always avoid the distortions ingrained in the way our minds work, but we can build in tests to make our decision-making processes more reliable, thus improving the quality of the choices we make.

The Brain Science of Decisions

The human brain's inherent functions can sabotage our decisions. It takes enormous energy to consciously work through possibilities and risks, so the brain looks for shortcuts. We use unconscious routines, known as heuristics, to cope with complexity – and they normally serve us well. But because they operate largely out of our awareness, they also present traps.



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Researchers have identified a series of flaws in the way we think when making decisions. They are hardwired into our thinking process, so we often fail to recognize them. This means they can undermine everything from new product development to acquisitions and divestiture strategy to succession planning.

While we cannot entirely rid ourselves of these ingrained flaws, we can learn to understand the traps and compensate for them. The best defense is awareness.

1. The Anchoring Trap

When considering a decision, the mind gives disproportionate weight to the first information it receives. Initial impressions, estimates or data anchor subsequent thoughts and judgments. In business, a common anchor is a past event or trend. While relying on such may lead to a reasonably accurate estimate of future numbers, it also tends to give too much weight to past events and not enough to other factors. Especially in markets with rapid changes, historical anchors can lead to poor forecasts and misguided choices.

Because anchors can establish the terms on which a decision is made, they are often used as a bargaining tactic by savvy negotiators.

The Antidote

Anchors affect how managers, accountants, engineers, bankers, lawyers, consultants, stock analysts and virtually all professionals make decisions. No one can avoid their influence. But managers who are aware of their dangers can reduce their impact by using the following techniques:

- Always view a problem from different perspectives. Try using alternative starting points and approaches rather than sticking with your first line of thought.
- Think about the problem on your own before consulting others to avoid becoming anchored to their ideas.
- Be open-minded. Seek information and opinions from a variety of people to widen your frame of reference.
- Avoid anchoring your advisers, consultants and others from whom you solicit information. Tell them as little as possible about your ideas and estimates. If you reveal too much, your preconceptions may simply come back to you.

2. The Status-Quo Trap

We all carry biases that influence the choices we make. For example, each of us is predisposed to perpetuating the status quo; it's an inherent part of our thinking. Deep within our psyches, we are self-protective and risk-averse.

In business, where sins of commission tend to be punished more severely than sins of omission, the status quo holds a particularly magnetic position.

The Antidote

You don't want to maintain the status quo just because it's comfortable. Do so only when it turns out to be the genuinely best choice. By becoming aware of the status-quo trap, you can lessen its pull by:

- Always reminding yourself of your objectives and examining how they would be served by the status quo.
- Never thinking of the status quo as your only alternative. Identify other options and use them as counterbalances.
- Asking yourself whether you would choose the status quo if it weren't so.
- Remembering the desirability of the status quo will change over time.

3. The Sunk-Cost Trap

Another deep seated bias is our tendency to make choices in ways that justify past decisions, even when the latter no longer seem valid. We know rationally that sunk costs are irrelevant to present decisions, but they nevertheless prey on our minds and lead to inappropriate choices.

This frequently occurs when we're unwilling, consciously or not, to admit a mistake. Acknowledging a poor business decision is a very public matter, inviting criticism from colleagues and bosses. It's psychologically safer to justify past decisions, make allowances and continue a tenuous course, even when we know the outcome is risky.

The Antidote

You'll need to make a conscious effort to set aside any sunk costs – psychological or financial—that muddy your thinking. Try these techniques:

- Seek out, and listen carefully to, the views of people who were uninvolved in the earlier decision.
- Examine why admitting a past mistake distresses you. Even the best and most experienced managers are not immune to errors in judgment. Remember the wise words of Warren Buffett: "When you find yourself in a hole, the best thing you can do is stop digging."
- Be on the lookout for the influence of sunk-cost biases in subordinates' decisions and recommendations.
- Don't cultivate a failure-fearing culture that leads employees to perpetuate and cover up mistakes.

4. The Confirming-Evidence Trap

Leaders sometimes seek out information that supports their existing instinct or point of view, while avoiding information that contradicts it. This trap affects where we go to collect evidence, as well as how we interpret it. Consequently, we give too much weight to supporting information and too little to conflicting information.

The Antidote

Don't necessarily disregard the choice to which you're subconsciously drawn, but make sure it's the smart one. Here's how to put it to the test:

- Check whether you're examining all evidence with equal rigor.
- Ask someone you respect to play devil's advocate and argue against the decisions you're contemplating.
- Be honest with yourself about your motives. Are you really gathering information to help you make a smart choice – or are you looking for evidence that confirms what you already think and want to do?
- When seeking others' advice, don't ask leading questions that invite confirming evidence – and don't surround yourself with “yes” people.

5. The Framing Trap

The first step in making a decision is to frame the question. It's also one of the most dangerous steps, as how you frame a problem can profoundly influence your choices.

The Antidote

A poorly framed problem can undermine even the best-considered decision. You can limit adverse effects by employing the following guidelines:

- Don't automatically accept the initial frame, whether it was formulated by you or someone else. Always try to reframe the problem in various ways. Look for distortions caused by the way it's framed.
- Try posing problems in neutral, redundant ways that combine gains and losses or embrace different reference points.
- Think hard throughout your decision-making process about how your problem is framed.
- When others recommend decisions, examine the way they framed the problem. Challenge them with different frames.

The Estimating & Forecasting Traps

Meteorologists and bookies have opportunities and incentives to maintain records of their forecasting abilities. The rest of us seldom have enough carefully tracked data to adequately calibrate our minds to make reasonable estimates in the face of uncertainty. This sets us up for three more traps.

6. The Overconfidence Trap

Most of us are overconfident about our judgment abilities and prediction accuracy, as we remember our successes and quickly forget our errors. Our hubris tricks us into considering only a narrow range of possibilities.

Major initiatives and investments often hinge on estimate ranges. Managers who underestimate the high end (or overestimate the low end) of a crucial variable may miss attractive opportunities or expose themselves to far greater risk than ever imagined.

7. The Prudence Trap

When faced with high stakes, we tend to adjust our estimates or forecasts with prudence, “just to be on the safe side.” One common example is the “worst-case” analysis, which can add enormous costs and no practical benefits. Too much prudence can be as dangerous as too little.

8. The “Recallability” Trap

Even when we're neither overly confident nor unduly prudent, we can still fall into the trap of basing predictions on memories of past events. Recollections of dramatic events leave strong impressions on our minds and can skew future decision-making efforts.

Anything that hampers your ability to recall events objectively will distort pending probability assessments.

The Antidote

You must take a very disciplined approach to making forecasts and judging probabilities:

- To reduce the effects of overconfidence when making estimates, always start by considering the extremes: the low and high ends of possible value ranges. This will help you avoid being anchored by an initial estimate. Then, challenge your estimates of the extremes, as well as those of your subordinates and advisers.
- To avoid the prudence trap, always state your estimates honestly, and explain to anyone who will be using them that they have not been adjusted. Emphasize the need for frank input to anyone who will be supplying you with estimates. Test estimates over a reasonable range to assess their impact.
- To minimize the distortion caused by variations in “recallability,” carefully examine all of your assumptions to ensure they're not unduly influenced by your memory. Get actual statistics whenever possible, and avoid being guided by impressions.

There Are No “No-Brainers”

When it comes to business decisions, there are no “no-brainers.” Our brains are always at work, sometimes without our conscious awareness, and sometimes in ways that hinder rather than help us.

At every stage of the decision-making process, misperceptions, faulty assumptions and other mind tricks can influence the choices we make.

Highly complex and important decisions are the most likely to be distorted because they involve the most assumptions, depend on estimates and receive more input from myriad people.

The higher the stakes, the greater the risk of being caught in a psychological trap. These traps can work in isolation or in tandem.

A dramatic first impression may anchor our thinking, causing us to selectively seek out confirming evidence to justify our initial inclination. We then make a hasty decision, which establishes a new status quo.

And as the sunk costs accumulate, we become trapped, unable to find a propitious time to seek out a new, possibly better course.

The best protection is awareness. Forewarned is forearmed. If you cannot eradicate the distortions ingrained in the way your mind works, you can at least build tests and disciplines into your decision-making process that can uncover errors in thinking before they become errors in judgment.

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