



B70.2335.20
Judgment and Decision Making
Spring 2007, TR 10:30-11:50
Location: K-MEC 3-65

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Course Overview

This course is intended for future marketing managers, industry analysts and management consultants interested in developing and evaluating marketing and business strategies based on Nobel Prize-winning research on judgment and decision making.

Successful marketing and business strategies depend on a thorough understanding of how people make decisions. However, traditional models of decision making, especially so-called normative or rational models, have serious limitations. Rather than making decisions in the manner postulated by these models, people often use a variety of rules and processes that lead to (sometimes counterintuitive, but often predictable) decision behavior. For instance, people have an exaggerated tendency to select compromise or middle options when making choices. As well, customers are easily seduced by features of a product that seem to differentiate it from other products, even when these features in fact add no value. Seemingly "irrational" decision phenomena such as these abound. The premise of the course is that a series of similar findings from research in decision-making have powerful business implications.

The purpose of this course is to inform future managers and consultants of people's decision rules and their associated biases and to enable these future managers and consultants to incorporate such insights in their business and marketing strategies. The course has two facets. First, it gives students a broad overview of important results from various behavioral sciences (e.g., social and cognitive psychology, behavioral decision research, consumer research) that clarify how people really make decisions. Second, it investigates how these results can be leveraged to design original and more effective marketing and business strategies. Knowledge of these issues can be a significant source of competitive advantage, because they are unknown to most managers and are not taught in most business schools.

Format

Intended to be intellectually stimulating and challenging, I value class participation and application of the ideas and theories we will be discussing. Classroom time will be devoted to a combination of lectures, discussions, exercises, and student presentations illustrating the main concepts. An important feature of the course is that students will be systematically asked to identify and generate original marketing and business applications of the course's concepts.

Evaluation

Participation (30%). In a course like this, the adage “garbage-in-garbage-out” is especially apt. Students will only get out of this course as much as they are willing to put in. It is therefore very important that students take an active role in classroom activities and discussions and come fully prepared. The class participation grade will reflect class attendance and the quality of the student's involvement in the class's activities and discussions. Near-perfect attendance is expected.

Short Writing Assignments (30%). To reinforce the learning process, individual writing assignments will be assigned 7 times throughout the semester. The tentative schedule for these assignments, as well as the assignments themselves, are listed later in this syllabus. *You are required to do at least 6 of these assignments.* Thus, each assignment is worth 5% of your grade. If you do all 7, your lowest assignment grade will be dropped. Late papers will not be accepted except in the case of bona fide emergencies (such as if you've fallen and can't get up) or if you make prior arrangements with the instructor.

The primary reason for the short writing assignments is to get you thinking seriously about the topics for the days ahead so that the class discussion is more informed and sophisticated. These papers have a 600 word limit. Please print the word count on your paper. All papers should be double spaced with wide margins and 12 point font. As well, you should use your student ID instead of your name to enable anonymous grading.

The short papers are graded using a five point system. The grades can be interpreted as follows:

1= Some evidence of reading, but little understanding and minimal application of the course concepts to the actual question that was asked.

2 = An attempt at applying the course material, but with little or no depth of analysis (possibly just repeating ideas from the reading).

3 = A solid application of the course material, with some good points but few creative insights; the majority of papers will receive this grade.

4 = A deeper level of thinking than the obvious answer, clearly written, perhaps with creative examples.

5 = An exceptional paper, with an original insight and clear analysis. Such papers make me say “I wish I had thought of that!” Very few of these grades are given.

For *all* written assignments, there will be another option. If you want to think about one article we have read more deeply, you can write a *Customer Insight Brief* which takes one major finding and asks you to think carefully about it. These, too, have a 600 word limit. A template is part of this syllabus.

Final Project (40%). The final project has two components: a 10-page paper and a 10-minute presentation, with your grade based primarily on the former. The presentations take place during the last two days of class and the paper is due the last day of class (in class). Again, being trapped under a heavy object is the only excuse for late papers unless prior arrangement has been made with the instructor. There are two project options:

Business Proposal: Describe an *original* business idea that capitalizes on one or more of the phenomena discussed in the course (a new type of loyalty program, a new way of presenting product assortments, a new type of mutual fund, etc.). Your paper and presentation should clearly outline the proposal and argue for why it should be effective (with references to the appropriate research).

Design a Case: Pick a *novel* managerial decision from the wild that turned out badly (e.g., a specific dot.com going public too early (or too late), AT&T's acquisition of cable companies) and analyze it in retrospect applying the principles from this course. Your paper and presentation should clearly document the mistake and explain it with reference to the appropriate judgment or decision making phenomenon (or phenomena), citing the appropriate research.

You have the option of completing this project solo or in groups of up to 4. If you elect to do the project with a group, the group will turn in a single paper and make a single presentation, with each member of the group receiving the same grade.

Note: I recommend meeting with me to discuss your individual or group project well before it is due, on the off chance I might actually have something valuable to contribute.

Readings / Slides

Readings are available online (via Blackboard). Please note that the readings are copyrighted works provided for your educational purposes only and, in accordance with copyright laws, are not to be copied, distributed, or insulted. Portions of the slides will be posted on blackboard the night before each class.

Cheating

No.

Tentative Syllabus*

| | | Readings Required | Optional | Written Assignment |
|-----------------------------------------------------|--------------------------------------------------|----------------------|---------------------|-----------------------|
| 1/23 | Topic Introduction..... | — | — | — |
| Part 1: Judgment under uncertainty | | | | |
| 1/25 | <i>No Class</i> | R1, R2 | — | — |
| 1/30 | Heuristics..... | R3, R4 | <i>R5, R6</i> | — |
| 2/1 | Self-serving biases Part 1..... | R7, R8 | <i>R9, R10, R11</i> | W1 |
| 2/6 | Self-serving biases Part 2..... | — | <i>R49</i> | — |
| 2/8 | Innumeracy..... | R12, R13 | <i>R14, R15</i> | — |
| 2/13 | Expectancies..... | R16 | <i>R17</i> | W2 |
| 2/15 | Memory..... | R18, R19 | <i>R20</i> | — |
| 2/20 | Introspection..... | R21 | <i>R22</i> | — |
| Part 2: Decision making and choice | | | | |
| 2/22 | Prospect theory Part 1..... | R23, R24 | <i>R25</i> | W3 |
| 2/27 | Prospect theory Part 2..... | R26 | — | — |
| 3/1 | Mental accounting..... | R27 | <i>R28, R29</i> | — |
| 3/6 | Choosing among options..... | R30 | <i>R31</i> | W4 |
| 3/8 | The paradox of choice..... | R32 | <i>R33</i> | — |
| 3/13 | <i>No class (Spring Break)</i> | — | — | — |
| 3/15 | <i>No class (Spring Break)</i> | — | — | — |
| 3/20 | Satisfaction with choice..... | R34 | <i>R35</i> | — |
| 3/22 | Intertemporal choice..... | R36, R37 | <i>R38</i> | W5 |
| 3/27 | Group decision making part 1..... | R39 | <i>R40</i> | — |
| 3/29 | Group decision making part 2..... | R41 | <i>R42</i> | W6 |
| 4/3 | Competitive thinking..... | R43 | <i>R44</i> | — |
| 4/5 | Fairness & cooperation..... | R45, R46 | — | — |
| Part 3: Persuasion, affect, and satisfaction | | | | |
| 4/10 | Persuasion..... | R50 | <i>R51, R52</i> | W7 |
| 4/12 | Affect & decision making..... | R53 | <i>R54, R55</i> | — |
| 4/17 | Guest Lecture: Gary Klein, Klein Associates..... | — | — | — |
| 4/19 | Satisfaction..... | R56, R57 | — | — |
| Part 4: The home stretch | | | | |
| 4/24 | Student presentations part 1..... | — | — | — |
| 4/26 | Student presentations part 2..... | — | — | — |

*Dates are rough approximations only; we may speed up or slow down as needed.

Reading list (Readings with an * are highly recommended, but optional)

- R1 Tversky, A., & Kahneman, D. (1974). Judgment under uncertainty: Heuristics and biases. *Science*, 185, 1124-1131.
- R2 Sunstein, C. (March 10, 2003). Truth is, sunbathing is probably more dangerous than terrorism. *Los Angeles Times*.
- R3 Gilovich, T., & Savitsky, K. (1996). Like goes with like. *Skeptical Inquirer*, 20, 34-40.
- R4 Slovic, P., Finucane, M., Peters, E., & MacGregor, D. G. (2002). The affect heuristic. In T. Gilovich, D. Griffin, & D. Kahneman (Eds.), *The psychology of intuitive judgment: Heuristics and biases* (pp. 397-420). Cambridge, England: Cambridge University Press.
- *R5: Gladwell, M. (January 12, 2004). Big and bad. *The New Yorker*, 28-33.
- *R6 Thaler, R. H., & Sunstein, C. R. (September 1, 2003). Who's on first. *The New Republic*, 27-30.
- R7 Bazerman, M. H. (2006). *Judgment in managerial decision making (6th edition)* (pp. 68-76). Hoboken, NJ: John Wiley & Sons.
- R8 Lovallo, D., & Kahneman, D. (July, 2003). How optimism undermines executives' decisions. *Harvard Business Review*, 57-63.
- *R9 Clements, J. (September 22, 1998). In the field of investing, self-confidence can sometimes come back to haunt you. *Wall Street Journal*, C. 1.
- *R10 Dreazen, Y. J. (Sept 26, 2002). Behind the fiber glut. *The Wall Street Journal*, B.1.
- *R11 Kruger, J., & Evans, M. (2004). If you don't want to be late, enumerate: Unpacking reduces the planning fallacy. *Journal of Experimental Social Psychology*, 40, 586-594.
- R12 Belsky, G., & Gilovich, T. (1999). *Why smart people make big money mistakes and how to correct them* (pp. 105-128). New York, NY: Simon & Schuster.
- R13 Kruger, J., Savitsky, K., & Gilovich, T. (1999). Superstition and the regression effect. *Skeptical Inquirer*, 23, 24-29.
- *R14 Belkin, L. (August 11, 2002). The odds of that. *New York Times*.
- *R15 Thaler, R. H. (1992). *The Winner's Curse: Paradoxes and anomalies of economic life* (pp. 151-167). Princeton, NJ: Princeton University Press.
- R16 Gilovich, T. (1991). *How we know what isn't so: The fallibility of human reasoning in everyday life* (pp. 49-74). New York, NY: Free Press.
- *R17 Bazerman, M. H., Loewenstein, G., & Moore, D. A. (November, 2002). Why good accountants do bad audits. *Harvard Business Review*, 97-102.
- R18 Chase, R. B. & Dasu, S. (June, 2001). Want to perfect your company's service? Use behavioral science. *Harvard Business Review*, 79-84.
- R19 Wirtz, D., Kruger, J., Scollon, C. N., & Diener, E. (2003). The role of predicted, online, and remembered experience on future choice. *Psychological Science*, 14, 520-524.
- *R20 Kahneman, Fredrickson, Schreiber, & Redelmeier (1993). When more pain is preferred to less: Adding a better end. *Psychological Science*, 4, 401-405.
- R21 Wilson, T. (2002). *Strangers to ourselves: Discovering the adaptive unconscious* (pp. 93-116). Cambridge, MA: Harvard University Press.

- *R22 Gladwell, M. (2005). *Blink: The power of thinking without thinking* (pp. 147-188). New York, NY: Time Warner.
- R23 Tversky, A., & Kahneman, D. (1981). The framing of decisions and the psychology of choice. *Science*, *211*, 453-458.
- R24 Johnson, E. J., & Goldstein, D. (2003). Do defaults save lives? *Science*, *302*, 1338-1339.
- *R25 Camerer, C. F. (2004). Prospect theory in the wild: Evidence from the field. In C. F. Camerer, G. Loewenstein, & M. Rabin (Eds.), *Advances in Behavioral Economics* (pp. 148-161). Princeton, NJ: Princeton University Press.
- R26 Bell, D. E. (1994). *The Toro Company S'no Risk Program*, HBS Case 9-185017.
- R27 Thaler, R. (2004). Mental accounting matters. In C. F. Camerer, G. Loewenstein, & M. Rabin (Eds.), *Advances in Behavioral Economics* (pp. 75-103). Princeton, NJ: Princeton University Press.
- *R28 Loewenstein, R. (2001, February 11). Exuberance is Rational. *The New York Times Magazine*.
- *R29 Thaler, R. H. (2000). Toward a positive theory of consumer choice. In D. Kahneman & A. Tversky (Eds.), *Choices, Values, and Frames* (pp 269-287). Cambridge, MA: Cambridge University Press.
- R30 Simonson, I. (1993). Get closer to your customers by understanding how they make choices. *California Management Review*, *35*, 68-84.
- *R31 Shafir, E., Simonson, I., & Tversky, A. (2002). Reason-based choice. In D. Kahneman & A. Tversky (Eds.), *Choices, Values, and Frames* (pp 597-619). Cambridge, MA: Cambridge University Press.
- R32 Schwarz, B. (2005). *The paradox of choice: Why more is less* (pp. 9-22). New York, NY: Harper Collins.
- *R33 Iyengar, S. S., & Lepper, M. R. (2000). When choice is demotivating: Can one desire too much of a good thing? *Journal of Personality and Social Psychology*, *79*, 995-1006.
- R34 Schwarz, B. (2005). *The paradox of choice: Why more is less* (pp. 147-179). New York, NY: Harper Collins.
- *R35 Miller, D. T. & Taylor, B. R. (2002). Counterfactual thought, regret, and superstition: How to avoid kicking yourself. In T. Gilovich, D. Griffin, & D. Kahneman (Eds.), *The psychology of intuitive judgment: Heuristics and biases* (pp. 367-378). Cambridge, England: Cambridge University Press.
- R36 Thaler, R. H. (1992). *The Winner's Curse: Paradoxes and anomalies of economic life* (pp. 92-106). Princeton, NJ: Princeton University Press.
- R37 Benson, E. (2002). Gambling on the future you. *Monitor on Psychology*, *33*, 48.
- *R38 Hafner, K. (October 15, 2003). Electronic gadgets, endlessly seductive but soon discarded. *New York Times*, p. A1, C2.
- R39 Myers, D. G. (1994). *Exploring social psychology* (pp 172-205). New York, NY: McGraw Hill.
- *R40 Useem, J. (February 1, 1998). All dressed up and no IPO. *Inc Magazine*.
- R41 Krakauer, J. (September, 1996). Into thin air. *Outside magazine*. Note: For those of you who can find the time, I recommend reading the book instead.

- *R42 Kahneman, D., & Lovallo, D. (2000). Timid choices and bold forecasts: A cognitive perspective on risk taking. In D. Kahneman & A. Tversky (Eds.), *Choices, Values, and Frames* (pp 597-619). Cambridge, MA: Cambridge University Press.
- R43 Ross, L. & Ward, A. (1996). Naïve realism in everyday life: Implications of social conflict and misunderstanding. In E. Reed, E. Turiel, & T. Brown (Eds.), *Social cognition: The Ontario Symposium* (pp. 305-321). Hillsdale, NJ: Erlbaum.
- *R44 Windschitl, P., Kruger, J., & Simms, E. (2003). The influence of egocentrism and focalism on people's confidence in competitions: When what affects us equally affects me more. *Journal of Personality and Social Psychology*, 85, 389-408.
- R45 Thaler, R. H. (1992). *The Winner's Curse: Paradoxes and anomalies of economic life* (pp. 6-20). Princeton, NJ: Princeton University Press.
- R46 Kahneman, D., Knetsch, J. L., & Thaler, R. H. (2004). Fairness as a constraint on profit seeking: Entitlements in the market. In C. F. Camerer, G. Loewenstein, & M. Rabin (Eds.), *Advances in Behavioral Economics* (pp. 148-161). Princeton, NJ: Princeton University Press.
- Note: Assignments R47 & R48 have been deleted, and R49 is an optional reading for 2/6/2006.**
- *R49 Menand, L. (October 5, 2005). Everybody's an expert. *The New Yorker*, p. 98.
- R50 Cialdini, R. (2001). *Influence: Science and Practice*. Needham Heights, MA: Allyn & Bacon. *Note: May substitute with the much shorter "Harnessing the Science of Persuasion" Harvard Business Review, but I advise against it if you can find the time to read the entire book.*
- R51 Epley, N., Savitsky, K., Kacheliski, R. A. (1999). *What every skeptic should know about subliminal persuasion*, 23, 40-45.
- *R52 Gilbert, D. T. (1991). How mental systems believe. *American Psychologist*, 46, 107-119.
- R53 Isen, A. M. (1997). Positive affect and decision making. In W. M. Goldstein & R. M. Hogarth (Eds.), *Research on judgment and decision making* (pp 509-534). Cambridge, UK: Cambridge University Press.
- *R54 Lerner, J., Small, D. A., & Loewenstein, G. (2004). Heart strings and purse strings. *Psychological Science*, 15, 337-341.
- *R55 Loewenstein, G. (2004). Out of control: Visceral influences on behavior. In C. F. Camerer, G. Loewenstein, & M. Rabin (Eds.), *Advances in Behavioral Economics* (pp. 689-723). Princeton, NJ: Princeton University Press.
- R56 Frank, R. H. (1999). *Luxury fever: Why money fails to satisfy in an era of excess* (pp. 64-93). New York, NY: Free Press.
- R57 Gertner, J. (2003, September 7). The futile pursuit of happiness. *New York Times*.

Short Writing Assignments

W1 Answer ONE of the following:

1. Suggest at least two ways in which the representativeness heuristic might play a role in the behavior of managers engaged in mergers and acquisitions.
2. Does Madison Avenue understand the representativeness heuristic? How? Find an ad that (implicitly) makes use of the concept and explain how it works. (If the ad is print just clip it out or make a copy. For a commercial, try to get a copy of the ad on tape or electronic media (CD, DVD, USB card) so I can play it in class. If not, describe it briefly. This will not count against your word limit.)
3. Imagine you are hiring a new employee; how is the representativeness heuristic likely to influence your evaluation? What steps should you take to avoid biases?

W2 Announce a new decision making heuristic, bias, or other empirical regularity. Give examples of how it happens, explain why, and make suggestions for how to make use of this new insight.

W3 One of the lessons of this course is that framing "matters". Some people have learned that lesson better than others. Find an example of inept framing in the news and fix it. That is, find a quote or argument by anyone being quoted in any news source that you think could be improved had they known how to "frame" and rewrite it in a way that you think will be superior. Explain why you think your approach is better.

W4 Answer ONE of the following:

1. Mental accounting, to the extent that it violates fungibility, is (according to economic theory) irrational. Do you think there are any circumstances where mental accounting makes people better off nonetheless? How?
2. Use mental accounting to develop a new pricing strategy for some product or service.
3. Make a copy of a regular statement (or web interface) you or someone you know receives from a financial services company such as Fidelity or Vanguard. Do whatever is necessary to make the statement confidential (black out names and/or amounts) and then attach the relevant parts to this paper. Now, based on the today's readings, make some suggestions for how this statement could be improved. Be sure to say explicitly what you are trying to improve.

W5 Answer ONE of the following:

1. To deal with self-control problems, many people use the equivalent of sunk costs to commit themselves to an activity. Examples include paying a large annual health club fee rather than paying per visit, or buying season tickets for the theater. Can you suggest other products that might benefit from using prepayment as a self-control device? Devise a marketing strategy to implement this plan.

2. Although people usually procrastinate by postponing the completing of unpleasant tasks, there are also situations in which people procrastinate the enjoyment of something enjoyable, such as drinking a special bottle of wine. For some reason, no occasion ever seems special enough to finish it off, and the activity is continuously postponed. Suppose that you are a seller of luxury goods that have this problem (such as fine wines). How do you get your customers to quit delaying consumption?

W6 Read *Into Thin Air* and answer ALL of the following:

1. Why are the climbers up there? Consider the motivation and incentives facing each participant. What are the implications for potential decisions biases and corrective measures?
2. What are the defining characteristics of the decision-making environment on Mt. Everest? Setting aside the extreme physiological conditions, what are the biggest challenges for good decision making?
3. Describe the decision process used by Hall and Fischer. What mistakes did the guides or members of the climbing teams make during the climb to the summit? Why were these mistakes made? How do these mistakes relate to concepts we have discussed in the course?
4. If you were advising a friend interested in organizing an expedition to the top of Everest (or some other large but potentially dangerous mountain), what advice would you give him or her based on the concepts of this course

W7 Do a consumer insight brief focusing on ONE of Cialdini's 6 major principles.

Customer Insight Brief Template

1. What interesting decision-making phenomenon (phenomena) does this research show?
2. Why does it happen? In other words, what's going on in the customer's mind that makes them behave that way?
3. When do you expect this phenomenon to be most likely to happen (in what situations, in what contexts, for what type of customers, etc.)? When do you expect this phenomenon NOT to happen? Explain why.
4. Can you think of existing business applications or practices—other than the ones mentioned by the author(s)—that capitalize on this phenomenon?
6. Can you think of examples in which businesses are hurting themselves because they are seemingly unaware of this phenomenon? (That is, they would do their business differently if they knew about this phenomenon.)
7. Can you think of a novel way of capitalizing on this phenomenon from a business standpoint?