

# Rationality, Plasticity and Framing

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**RISK AND CRISIS MANAGEMENT**

## Are People Rational?

### ⊕ Economists' Claims

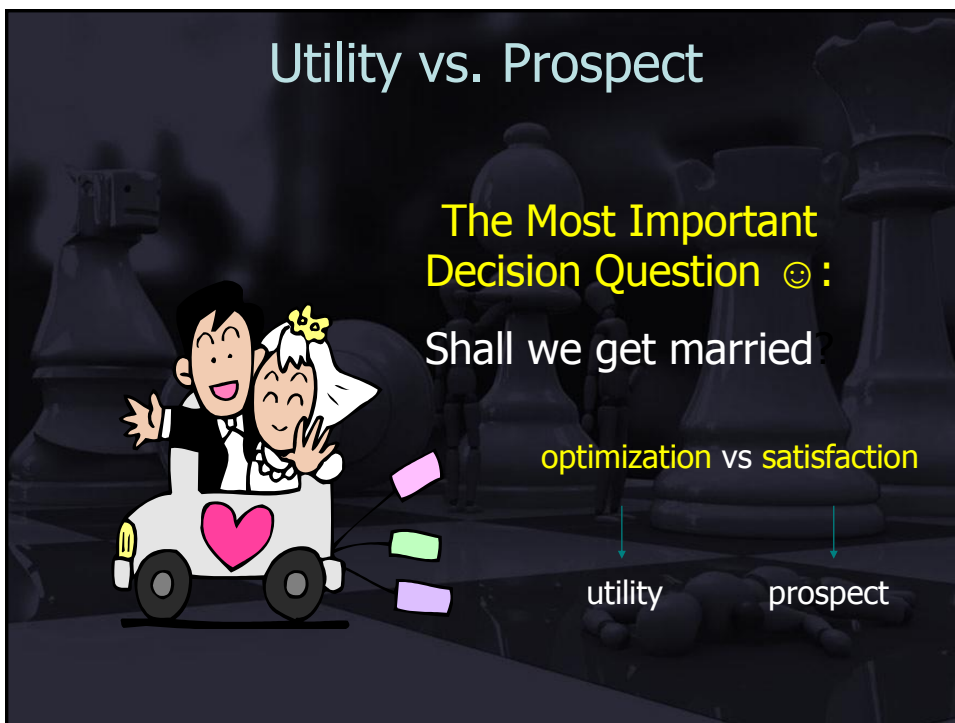
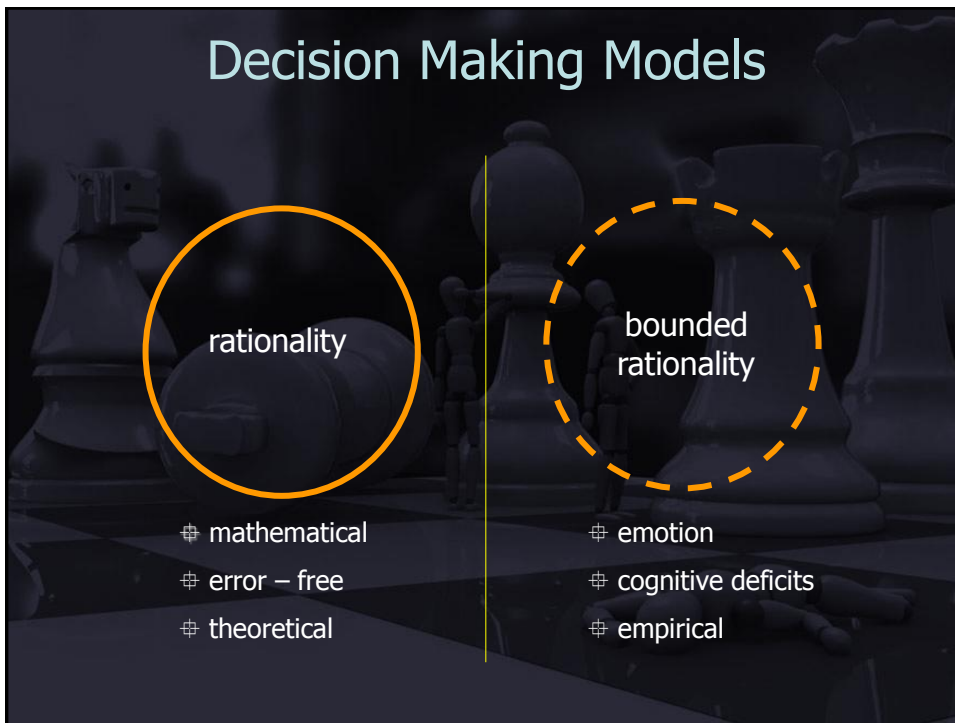
⊕ Humans are fundamentally rational and ultimately efficient in decision making.

- ⊕ People are self-interested
- ⊕ People are consistent
- ⊕ People are rational

⊕ *So, people are making self-interested, consistent, and rational calculations when they are making (financial) decisions.*

**Social Psychologists and Behavioral Economists ask:**

*Why do we tip?*



## Which alternative would you choose?

⊕ Alternative A

A 100 percent chance of losing \$50

⊕ Alternative B

A 25 percent chance of losing \$200, and a 75 percent chance of losing nothing.

⊕ Alternative A

A 100 percent chance to gain \$50

⊕ Alternative B

A 25 percent chance to gain \$200, and a 75 percent chance of to gain nothing.

## What if ?... Changing the story

⊕ Alternative A

A 100 percent chance of giving \$50 for insurance.

⊕ Alternative B

A 25 percent chance of losing \$200 for non-insured item, and a 75 percent chance of losing nothing.

risk averse vs risk seeking individuals

## Order Effects

- ⊕ Should divorce in this country be
  - ⊕ easier to obtain (23%)
  - ⊕ more difficult to obtain (36%)
  - ⊕ stay as it is now (41%)

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- ⊕ Should divorce in this country be
  - ⊕ easier to obtain (26%)
  - ⊕ stay as it is now (29%)
  - ⊕ more difficult to obtain (46%)

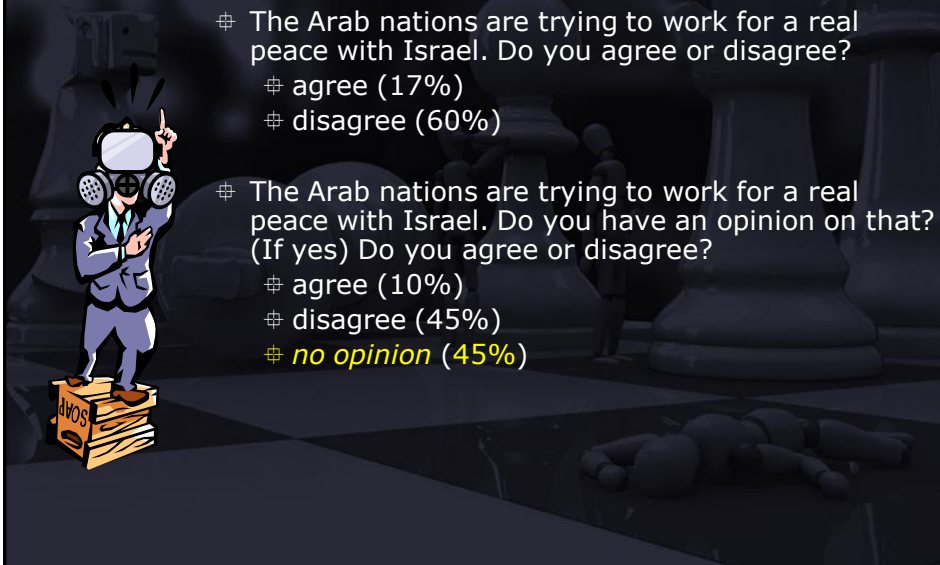
## Pseudo - Opinions

- ⊕ Are you in favor of or opposed to incest?
  - ⊕ opposed (66%)
  - ⊕ in favor of (34%)



! ... if respondents who know very little about an issue are added to those who have never heard of it, the percentage of pseudo opinions frequently constitutes an absolute majority ... (p.55)

## Filtering Out Pseudo - Opinions



- ⊕ The Arab nations are trying to work for a real peace with Israel. Do you agree or disagree?
  - ⊕ agree (17%)
  - ⊕ disagree (60%)
- ⊕ The Arab nations are trying to work for a real peace with Israel. Do you have an opinion on that? (If yes) Do you agree or disagree?
  - ⊕ agree (10%)
  - ⊕ disagree (45%)
  - ⊕ *no opinion* (45%)

## The effects of wording

What is the difference between safe and safer?

**r** ≈ 10%

## Framing Effect I

Imagine that the U.S. 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 estimate of the consequences of the programs are as follows:

- If program A is adopted, 200 people saved.
- If program B is adopted, there is  $\frac{1}{3}$  probability that 600 people will be saved, and  $\frac{2}{3}$  probability that no people will be saved.

Which of the two programs would you favor?

## Framing Effect - II

Imagine that the U.S. 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 estimate of the consequences of the programs are as follows:

- If program A is adopted, 400 people will die.
- If program B is adopted, there is  $\frac{1}{3}$  probability that nobody will die, and  $\frac{2}{3}$  probability that 600 people will die.

Which of the two programs would you favor?

## Psychological Accounting

Imagine that you are about to purchase a jacket for \$125, and a calculator for \$15. The calculator salesman informs you that the calculator you wish to buy is on sale for \$10 at the other branch of the store, located 20 minutes drive away. Would you make the trip to the other store?



Imagine that you are about to purchase a jacket for \$15, and a calculator for \$125. The calculator salesman informs you that the calculator you wish to buy is on sale for \$120 at the other branch of the store, located 20 minutes drive away. Would you make the trip to the other store?

ratio – difference principle

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