Cognitive bias

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.

**Social**
- Failure to estimate

**Financial**
- Short-termism

**Origin**
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. Kahneman was awarded a Nobel Prize in 2002 after further developing the ideas and applying them to economics.

**Confirmation Bias**
Supporting an argument even when we lack evidence.

**Anchoring Effect**
Relying too much on the initial piece of information offered when making decisions.

**Availability Heuristic**
Overestimating the importance and likelihood of events given the greater availability of information.

**Bandwagon Effect**
Believing things more based on the number of people who share that belief.

**Blind Spot Bias**
Excluding, or underestimating the importance of small clusters or patterns in large data.

**Clustering Illusion**
Excluding, or underestimating the importance of small clusters or patterns in large data.

**Endowment Effect**
Irrationally overvaluing something you own regardless of its objective market value.

**Gambler’s Fallacy**
Believing that future probabilities are altered by past events, when in fact they are unchanged.

**Status Quo Bias**
Preferring the current state of affairs over change.

**Ostrich Effect**
Avoiding negative financial information by pretending it doesn’t exist.

**Post-Purchase Rationalization**
Persuading yourself that a purchase was the right decision.

**Illusory Validity**
Overestimating the importance and likelihood of events given the greater availability of information.

**Risk Compensation**
Taking bigger risks when perceived safety increases; being more careful when perceived risks increase.

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