

Below are a number of mistakes in reasoning that people make in decision making. What name do economists give to these kinds of mistakes? Cognitive biases

Label each of the following with “confirmation bias”, “availability bias”, “anchoring”, “status-quo bias”, “loss aversion”, “bandwagon effect bias” or “inequity aversion”

- Putting money into a safe but low-yielding investment rather than one that is a bit more risky but has the prospect of much higher returns **Loss aversion**
- Choosing to read newspapers because it already presents the points of view that are already held above any other newspaper **Confirmation bias**
- Reading about a burglary in the next town and buying new locks for all of your windows and doors **Availability bias**
- Paying more for something after a period of negotiation because the person selling it started the negotiation with a high price **Anchoring**
- Meaning to become an organ donor but continuously putting off the decision to do so **Status-quo bias**
- Giving a different amount of money to charity when options on a form are: £100, £250, £1,000, £5,000 or ‘other’ as opposed to: £50, £75, £100, £150 or ‘other’ **Anchoring**
- After a period of falling house prices being reluctant to move due to unwillingness to sell a house for less than what was paid for it even though the prices of properties that that could be moved into have also fallen **Loss aversion**
- Ordering a free trial of a magazine subscription and then forgetting to cancel the subscription before the payment period begins **Status-quo bias**
- Gaining weight because your group of friends have also been gaining weight **Bandwagon effect bias**
- Choosing to fill in a tax return in a timely fashion after being told that more than 90 percent of people in the same town had already complied, in full, with their obligations under the tax law **Bandwagon effect bias**
- Continuously putting off enrolling onto a pension scheme and regretting it when reaching retirement age. **Status-quo bias**
- Foregoing a gain in order to prevent another person from receiving a superior reward. **inequity aversion**

**Choices on the margin**

Would you gain more utility from consuming one more glass of water or from owning a diamond?

**Higher marginal utility from a diamond**

How would this be different if you were dying of thirst in a desert?

**Higher marginal utility from a glass of water**

Label each of the following with “bounded rationality” or “bounded self-control”

What aspect of imperfect rationality causes people...

to sign up to a self-imposed gambling ban? **Bounded self-control**

to overeat food and then regret it immediately afterwards? **Bounded self-control**

when purchasing a car with an aim of buying the most fuel efficient, buying a car which is not the most fuel efficient? **Bounded rationality**



Slices of pizza consumed	Marginal Utility	Total utility
-		-
1	11	11
2	9	20
3	7	27
4	5	32
5	3	35
6	1	36
7	-1	35

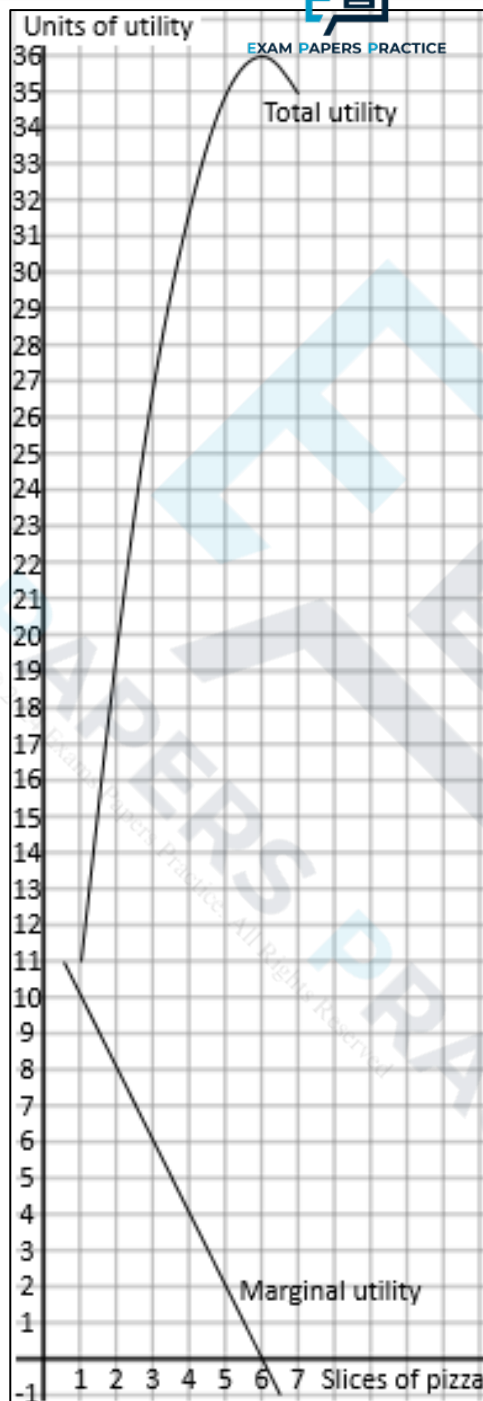
Complete the table above showing the marginal and total utility for consuming slices of pizza.

Graph the total and marginal utility curves in the axes on the right.

Which economic law describes the change in utility gained from consuming additional units of a good?  
The law of diminishing marginal utility

If a consumer attempted to maximise the welfare they gained from consuming slices of pizza, how many should they consume? 6 slices

What term do economists use to describe the maximisation of satisfaction from consuming goods and services? Rational behaviour

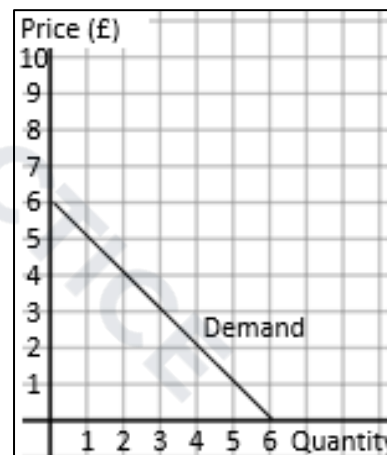


**Word bank:**

- Law of diminishing marginal utility
- The law of demand
- Cognitive biases
- Rational behaviour
- Nudges

If we assume that the consumer makes choices about the quantity and type of goods they buy until the last pound spent on each good generates 2 units of utility, what will this consumer's demand curve for pizza look like? Draw it on the axes below.

Which economic law describes the shape of the curve you have drawn?  
The law of demand



Below are a number of attempts to encourage people to think and act in particular ways. None of them prohibit making a particular choice. What name do economists give to these kinds of methods? Nudges

Label each of the following with "default choice", "framing", "mandated choice" or "restricted choice".

·Making energy companies present a limited set of tariff options to consumers.

·From 2011 all those applying for a UK driving license are required to state whether they wished to donate their organs.

·In an attempt to make more organs available for transplant, changing the organ donation system for those who have not expressed any preference to one of "presumed consent".

·Rephrasing  
"If you use energy saving methods you will save £350 a year" to  
"If don't use energy saving methods you will lose £350 a year"

·By 2018 all employers in the UK must provide a workplace pension scheme with "automatic enrolment".