I. Introduction to Behavioral Economics

Behavioral economics combines psychology and economics to understand the decision-making processes of individuals and institutions (Koch Rebecca). It is based on the idea that humans do not always make rational choices. Instead, it investigates and predicts human behavior and irrationality to positively influence behavior through “nudges” (Ey.com). It is connected with normative economics and challenges traditional economic theories by focusing on how humans actually behave instead of how they should behave. Behavioral economics attempts to understand why people make irrational decisions and how their behavior deviates from economic models (Kenton Will).

Behavioral economics is crafted around many principles, including bounded rationality, which involves people making decisions based on incomplete information or limited cognitive resources. Other principles include framing, which refers to how the presentation of information affects decision-making, heuristics, cognitive biases, and herd mentality. Loss aversion, the concept that people are more averse to losses than they are to receiving an equivalent gain, and the sunk-cost fallacy, the idea that people sometimes continue to invest in a project even when it is no longer viable, are also key principles. Companies have taken to using information from behavioral economics to price their goods, craft commercials, and package their products. Starbucks’ limited-time drinks, Amazon’s lightning deals, and “buy one, get one” promotions are all examples of strategies that use the principles of behavioral economics to appeal to customers (Kenton Will).

Behavioral economics is effective and has been proven in market experiments and real environments. Many financial institutions, marketing and commercial teams, talent teams, and governments are already using it to design better ways to reach customers, increase employee wellbeing and motivation, and launch effective civil policies (Ey.com). Financial institutions, in particular, have found that the applications of behavioral economics are extensive, both for internal and external customers. The complexity of financial products poses cognitive barriers that slow down decision-making. Companies can use BE knowledge and methodologies to investigate and eliminate these barriers or frictions and create effective triggers or incentives for customers. This positively influences customers to make better financial decisions, leading to higher satisfaction, loyalty, and financial impact. Nobel Prize winners endorse the theories of behavioral economics, and empirical tests verify its results (Byrne EY Global; Aaron).

In conclusion, behavioral economics analyzes the decisions people make and why irrational choices are chosen (Kenton Will). It investigates and predicts human behavior and irrationality to positively influence behavior through “nudges”. The study of judgment and choice focuses on how humans actually behave instead of how they should behave (Ey.com). It helps to explain why people do things financially that may be irrational (Kenton Will). Its principles and concepts, such as cognitive biases, heuristics, bounded rationalities, and herd mentality, have applications in different fields, including commercial, financial, governmental, and marketing (Kenton Will).

II. Decision Making

Behavioral economics is a growing field of economic psychology that investigates how people make financial decisions and why those choices can deviate from economic sciences' traditional models (Ey.com) (Byrne EY Global; Aaron). Behavioral economics is influenced by cognitive biases, framing effects, heuristics, and bounded rationality and herd mentality (Kenton Will). The key principles of behavioral economics include heuristics, loss aversion, framing, and sunk-cost fallacy. Behavioral economics is extensively used by financial institutions, marketing teams, and governments for designing enhanced ways to reach customers, enhance motivation and employee well-being, and launch effective civil policies (Kenton Will) (Ey.com). Starbucks' limited drinks, Amazon's lightning deals, and "buy one, get one" are examples of how brands harness behavioral economics information for their commodity packaging and pricing (Byrne EY Global; Aaron) (Kenton Will).

Behavioral economics is a powerful tool validated by Nobel Prize winners who support its applicability and usefulness (Ey.com). Behavioral economics challenges traditional economic theories and affirms hypotheses with a comprehensive approach based on observable human behavior . Founding fathers of behavioral economics are Daniel Kahneman and Amos Tversky. Kahneman noticed that humans make decisions based on their cognitive and emotional conditions (Kenton Will). Thaler recognized that many individuals possess limited capacity, social preferences, and lack self-control. Other renowned figures in the field include Gary Becker, Herbert Simon, and Richard Thaler (Kenton Will). Behavioral economics can be useful for financial institutions striving to grasp client behavior and generate suitable financial products. With knowledge and methodologies from behavioral economics, companies can obtain effective triggers and incentives, positively impacting customers to make better financial decisions, which leads to higher satisfaction, loyalty, and financial impact (Ey.com).

One of the deciding factors in behavioral economics is cognitive bias, which refers to decision-making biases due to heuristics like the availability heuristic, which makes relevant events more prevalent in people's minds, which causes irrational interpretation of data (Kenton Will). Behavioral economists also recognize that people justify their actions using an architecture of choices, including the sunk-cost fallacy, loss aversion, and framing (Byrne EY Global; Aaron). Overall, behavioral economics is a useful and effective psychology that has real-life, observable benefits. As companies use behavioral economics beyond just selling goods, it's clear that its findings have a close relationship with people's everyday lives (Kenton Will). Behavioral economics is a prominent research field that aims to predict and positively influence human behavior thought "nudges", recognizing that heuristics and biases have a significant impact on our decision-making processes (Kenton Will). Behavioral economics is designed to understand how people make economic choices and aims to validate hypotheses through empirical tests and offer solutions based on them (Kenton Will) (Ey.com).

III. Applications of Behavioral Economics

Behavioral economics is the study of the psychology behind decision-making and the reasons irrational choices are chosen (Kenton Will) (Tagliabue et al.). Influenced by bounded rationality, architecture of choices, cognitive biases, and herd mentality, it is designed around many principles, such as framing, heuristics, loss aversion, and the sunk-cost fallacy (Kenton Will) (Tagliabue et al.) (Ey.com). Some notable people in the field are Gary Becker, Herbert Simon, Daniel Kahneman, George Akerlof, and Richard H. Thaler (Kenton Will). Daniel Kahneman and Amos Tversky are considered the founding fathers of behavioral economics . Behavioral economics challenges traditional economic theories and seeks to validate hypotheses through exhaustive methodology and its real-world applications (Kenton Will) (Ey.com). Researchers aim to positively impact behavior by identifying cognitive errors in decision-making caused by heuristics and cognitive biases (Ey.com).

The financial sector has applied behavioral economics extensively, using it to build better ways to interact with their customers and increase their employees' wellbeing and motivation (Ey.com) (Kenton Will). Behavioral economics is particularly useful in comprehending clients' behaviors and decision-making in finance, an industry with complex and unattractive products that slow down decision-making and poses cognitive barriers (Kenton Will). BE knowledge and methodologies can identify and relieve these cognitive barriers to decision-making, while also creating effective triggers and incentives that positively influence customer behavior, resulting in higher satisfaction, loyalty, and financial impact (Kenton Will).

Behavioral economics is not confined to financial institutions. Several companies, marketing teams, talent teams, and governments use the principles of behavioral economics, applying them to price their goods, craft their commercials, and package their products. Behavioral economics can promote creative initiatives to drive sales by creating special deals that encourage customers to purchase more, such as Starbucks' limited season drinks, Amazon's Lightning Deals, or "buy one, get one" promotions (Kenton Will) (Tagliabue et al.). BE can also craft effective promotional deals by anticipating and addressing consumer biases (Ey.com). Behavioral economics also investigates and predicts human behavior and irrationality to positively influence behavior through "nudges" (Kenton Will) (Ey.com).

In conclusion, behavioral economics has a significant impact on policy and strategy due to its effectiveness and reach (Ey.com). It has proved to be effective in market experiments and real environments, providing a comprehensive understanding of decision-making, and predicting human behavior and irrationality to create effective triggers (Kenton Will) (Ey.com). Applying BE methodologies can reveal the cognitive barriers to decision-making and create effective incentives, promoting customer satisfaction, loyalty, and better decision-making while improving business effectiveness for clients (Kenton Will). By examining the psychology behind decision-making and understanding the reasons irrational choices are made, BE drives creative initiatives that positively impact bottom lines across industries, leading to significant advancements and success (Kenton Will) (Ey.com) (Tagliabue et al.).

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