

An Anchor For Your Thoughts?

The psychological factors that influence strategic decision making in business can be quite interesting. If you want to do some reading, a couple of great books in this area are *Decision Traps* by Edward Russo and Paul Shoemaker and *Influence—The Psychology of Persuasion* by Robert Cialdini.

Both touch on the concept of anchoring—how an initial number or concept powerfully affects our final analysis. For example, ask ten people for a gas price forecast by saying, “Experts believe gas prices will continue to rise past \$4.00/gallon. What is your forecast for gas prices next year?” Next say to ten others, “Experts believe gas prices will stabilize at less than \$3.00/gallon. What is your forecast?” Variations of this experiment time and again show that the second group of people will estimate a lower average price than the first group. Why? The original number acted as an anchor from which they adjusted their estimate. The anchor doesn't even have to be relevant to the question. If you asked people to write down the last two digits of their social security number before they guessed the percentage of cars that were silver, those with higher numbers would write down a higher percentage as their guess. So, what does this mean for business?

1 » PRICING

Conventional wisdom says that you can always lower your original price, but it's tough to go up! Your original price acts as an anchor.

2 » NEGOTIATIONS

Anchors can serve as the reference point for the negotiation from which concessions are granted and can dramatically affect the final outcome.

3 » BUDGETING

When forecasting, we often choose a natural anchor, like last year's number, and adjust from there. To make better decisions, don't let the original anchor exert too strong a hold. Instead, use other scenarios and benchmarks as well.

4 » COMPETITIVE STRATEGY

Anchoring is not involved with numbers. Often when a firm surprises the industry with a new product, the competition starts thinking of ways they can respond with something incrementally better. A better approach is to focus on the real need that this new product is solving rather than anchoring all thoughts on the product itself.

There are many other scenarios as well, and if you look for it, you'll see this mental bias at work everywhere. Usually, you would have to pay \$5,000 for a business course to get this kind of information. So wasn't this article valuable?

An initial number
or image powerfully
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