Behavioural Economics: Understanding Choices

Behavioural Economics · Practice Test · 8 Questions

1. What is the 'endowment effect' in behavioural economics, and which experiment best illustrates it?

A) The tendency to overvalue something you own compared to something you don't, demonstrated by Kahneman, Knetsch, and Thaler's mug experiment.
B) The bias towards choosing the default option, shown in experiments with organ donation rates.
C) The inclination to be influenced by the way information is presented, as seen in framing effect studies on medical treatments.
D) The preference for immediate rewards over future rewards, observed in intertemporal choice experiments.

2. Which concept describes the tendency for people to rely on the first piece of information offered (the 'anchor') when making decisions, even if it's irrelevant?

A) Anchoring Bias
B) Confirmation Bias
C) Availability Heuristic
D) Loss Aversion

3. Behavioural economists argue that humans are not always 'rational actors' in the way traditional economics assumes. What term do they use to describe people with limited cognitive abilities and self-control?

A) Bounded Rationality
B) Perfect Rationality
C) Economic Man (Homo Economicus)
D) Systematic Deviator

4. The 'framing effect' demonstrates that people's choices can be influenced by how options are presented. Which classic study highlights this by showing different preferences for medical treatments based on survival versus mortality rates?

A) Tversky and Kahneman's work on prospect theory
B) Dan Ariely's 'Predictably Irrational' experiments
C) Richard Thaler's 'Nudge' principles
D) George Akerlof's market for lemons theory

5. What is 'prospect theory', and what key insight did it offer about decision-making under risk?

A) It describes how people make decisions by evaluating potential gains and losses relative to a reference point, and that people are loss-averse.
B) It posits that individuals make choices to maximize their expected utility, regardless of framing.
C) It explains that past experiences heavily influence future decision-making through learned associations.
D) It suggests that individuals always choose the option with the highest probability of success.

6. Which cognitive bias describes the tendency to search for, interpret, favour, and recall information in a way that confirms one's pre-existing beliefs or hypotheses?

A) Confirmation Bias
B) Hindsight Bias
C) Fundamental Attribution Error
D) Self-Serving Bias

7. The 'default effect' or 'status quo bias' suggests people tend to stick with the pre-selected option. In which real-world policy area has this been effectively utilised to increase participation?

A) Organ donation registration, by making opt-out the default.
B) Retirement savings contributions, by making opt-in the default.
C) Tax filing, by making manual filing the default.
D) Voter registration, by making opt-in the default.

8. Loss aversion, a core concept in prospect theory, states that people feel the pain of a loss more strongly than the pleasure of an equivalent gain. What is the approximate ratio often cited for this effect?

A) Approximately twice as much pain from a loss as pleasure from an equal gain.
B) An equal amount of pain and pleasure from equivalent losses and gains.
C) Slightly more pleasure from a gain than pain from an equal loss.
D) The effect is negligible and not consistently measurable.