**FORBES: 5 Behavioral Economics Principles Marketers Can't Afford to Ignore**

Understanding the consumer psyche and the irrationality of the human decision-making process is key to developing winning value propositions or product features to test in the market. Here is a discussion of 5 Key Behavioral [Economics](http://www.forbes.com/economics/) (BE) principles (among dozens) that all marketers should not only understand but internalize. BTW, if you are looking to leverage analytics to drive better marketing decision, we recommend [assessing your analytics aptitude](http://aryng.com/aryngs-analytical-aptitude-assessment/) to see how well you would be able to apply what you learn here to your day-to-day projects. And if driving impact with data is your thing, check out the book '[Behind Every Good Decision](http://www.aryng.com/business-analytics-book.html?utm_source=Forbes&utm_medium=Partner&utm_campaign=Art)', a step-by-step guide on how 'anyone' can use Business Analytics to turn data into profitable insights.

**Power Of Free**: Can reducing the price of two commodities by the exact same amount, completely reverse consumer preference of one over the other? Traditional economics says NO. But indeed it is possible.

A group of researchers offered participants of a study a choice between purchasing a [Hershey](file:////companies/hershey/) [**HSY +0.77%**](file:////companies/hershey/)’s Kisses chocolate for 1-cent ($0.01) or Lindt Lindor chocolate truffle for 15 cents ($0.15). The participants, recognizing this as a good deal since the price differential in a supermarket would be larger than 14 cents between the two options, overwhelmingly chose the latter. However, when the price of both was reduced by 1 cent, thus making Kisses free and the Lindt Lindor for $0.14, the preference completely reversed with an overwhelming majority choosing Kisses!

What happened here? Nothing had changed–consumers would still get the same amount of incremental joy (consuming an exotic truffle vs. a regular candy) to the same amount of incremental pain (spending $0.14 more). The preference should not have changed.

[](http://creativanalytics.files.wordpress.com/2012/03/power-of-free1.png)

So why did it? Well, our response to price reduction becomes very non-linear when the price reaches “free”. We just love the word “FREE”. It evokes unreasonably positive feelings in the brain. Just the sight of the word “free” releases large quantities of dopamine in our brain to make us feel happy, and we end up responding irrationally.

So how does this play out in the real world. We get inundated with “free” offers every day and may believe that this does not affect us. But consider two economically identical deals– one messaged as ‘buy 1 get 1 free’; the other messaged as a volume discount deal as ‘get 50% off if you buy two’. Which one are you more likely to respond to?

**Dominated Alternatives:**Can introducing a third decoy option make you more likely to choose the option, I secretly want you to choose?

Consider this scenario at the Economist. Potential customers were given two subscription offers shown below– essentially an ‘online only’ subscription for $56, and and ‘online + print’ subscription for $125.

A large majority of people chose the first option ($56), although the second option ($125) was preferable to the publishers. They then introduced a third decoy option, that they knew nobody would prefer–**$125 for print only**.

As expected no one chose the third option, but something magical happened! An overwhelming majority now chose the second option ($125 for online + print)! The mere introduction of this third option, made option #2 look very attractive–you were getting online version for free now!

[](http://creativanalytics.files.wordpress.com/2012/03/economist.png)

What happened here? Well, this goes back to the idea that consumers have a very poor understanding of what a commodity is truly worth. They had no idea what a print or online subscription of the Economist is truly worth in $ terms. The first scenario with two options they had nothing to compare either option to. But with the introduction of the third option, option #2 and #3 are comparable and #2 wins hands down (you are getting online version for free after all!) . Option #1 has no comparable so it gets left out.

This principle has been demonstrated successfully in many different scenarios. The most bizarre according to me, is one of dating. Participants of this study were shown pictures of 3 individuals of the opposite sex and asked which one would they prefer to go out on a date with. Only, there were only two individuals in the pictures, the third was a digitally altered slightly inferior version of one of the two. So think of it as A, B, and inferior B (say B’). An overwhelming majority chose B in this scenario! The idea is the same–no comparable for A, so A gets left out; B and B’ look similar, B being more attractive. Hence B wins in a large majority of cases.

[Next](file:////companies/next/) [**NXGPY +0%**](file:////companies/next/) time you are evaluating vacation packages, or buying a home, pay attention to how different options are being positioned. These professionals have figured this stuff out through experience, even if they do not articulate it this way.

**Irrational Value Assessment:**Are you more likely to admire a $5 bottle of wine, if I lied to you and told you that it costs $45? Research says you are. Members of the Stanford Wine Club were invited to taste 5 bottles of wine and rate them based on their liking. Only, there were actually only 3 different wines in those bottles– two wines had two bottles each. Each bottle was marked only with the price tag and nothing else. Some of the same wines were marked at significantly different prices. For example, the $5 wine and the $45 wine were actually the same, the true cost being $5. There was a clear correlation between the rating of the wine and the price tag — more expensive wines got systematically higher ratings. So the $45 bottle of wine got a significantly higher rating than the $5 bottle, although they were the exact same wine!

[](http://creativanalytics.files.wordpress.com/2012/03/wines.jpg)

In another experiment, the same group was asked to rate the same wines again. Only this time even the price tags were absent. The cheapest wine was ranked the highest in this case!

Now, before we start calling these wine-experts snobs, consider this. Prozac was tested against a placebo. Only, the placebo was sold at a higher price ($2.50 per pill) than Prozac ($2.00 per pill). Placebo outperformed Prozac!

Consider another experiment, where students were given a caffeine +  sugar rich drink that was supposed to improve their alertness and focus in the short term. Their task was to solve as many puzzles as they can. Half of the group was asked to pay the full price of the drink, and the other half was given a significant discount on the price. The group that got the discounted drink, solved 30% fewer puzzles! This result has been consistent in multiple such studies over time.

<https://www.forbes.com/>