THE ROLE OF BEHAVIORAL ECONOMICS IN CONSUMER DECISION-MAKING

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Abstract: This paper aims to analyze how behavioral economics theories and practices play an importantl role on consumption and consumer choice behavior. Behavioral economics main purpose is to obtain deeper understanding of human behavior and interactions, also to understand how they interact both as individuals and as a group. Moreover, by observing how an individual chose its precious time, income or even assets we can assume how that individual shall make the choices. Among many important theories of behavioral economics, prospect theory and its loss and gains aspects are mostly and widely studied, thus applied aspects on consumption. Prospect theory show that individuals are loss-averse, hence they more dislike losses rather than counterpart gains, therefore they are more willing to take risks to avoid a loss. Consumer behaviors towards losses or gains may also lead towards endowment effect an attachment feeling towards valuing and paying higher price for an item that is already in possession, rather than owning a new one (Thaler, 1980) . In behavioral economics consumer choice is influenced also by mental accounting, where according to Thaler (1985) is used as a cognitive bookkeeping tool that consumers use in order to keep records of financial activities and to control consumption. Application of behavioral economics theories and examples illustrated in this paper aimto show that BE and its principles have been applied in many consumption and consumer choice domains like product choice and product value, consumer spending and behavior.

Key words : Behavioral Economics , Consumer Decision-Making , consumption , prospect theory, and mental accounting.

Introduction

Consumer decision-making is a complex process influenced by numerous factors, ranging from personal preferences to external stimuli. Traditional economic theories assume that consumers are rational actors who make decisions based on maximizing utility. However, real-world observations often contradict this assumption, revealing that consumers frequently make seemingly irrational choices. Behavioral economics emerged as a field to bridge the gap between economic theory and actual consumer behavior by incorporating psychological insights into economic models**.** In the economics, rational choice theory indicates that when individuals are offered numerous choices under the circumstances of scarcity, they would tend to select the alternative that maximizes their satisfaction. Under this theory the assumption is that individuals, given their preferences and limitations, have capabilities to bring rational decisions by efficiently evaluating costs and benefits of each available option provided to them (Ostrom, 1998). The rational individual has self-control, is not influenced from external factors, hence knows what is best for oneself and final decision will be the best choice made. Understanding the role of behavioral economics in consumer decision-making has significant implications for both theory and practice. By elucidating the psychological underpinnings of consumer behavior, this study contributes to the development of more accurate economic models and more effective interventions.

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Literature Review

The consumer decision-making process is a central focus in the study of behavioral economics, as it provides insights into how consumers interact with various market dynamics and make choices. This process is influenced by a range of factors, from psychological and cognitive elements to social and cultural influences. Pirouz (2015) delves into the neuroscience of consumer behavioral decision-making, offering a perspective that bridges the gap between traditional economic theories and psychological insights. This approach is crucial in understanding the underlying neural mechanisms that drive consumer decisions, particularly in cases where these decisions appear irrational or counterintuitive. By examining the neurological basis of decision-making, this research provides a more comprehensive understanding of consumer behavior, which is essential for designing consumer protection policies and marketing strategies that align with actual consumer behavior. Tesic and Bogetić (2022) provide a literature review on various models of consumer behavior, tracing the evolution from early models focused on rational consumer behavior to contemporary models that appreciate the emotional aspect of consumer decisions. This shift in focus highlights the growing recognition of the complexity of consumer behavior, which is not solely driven by rational calculations but also by emotional and psychological factors. The review of models such as the Nicosia model, Engel-Kollat-Blackwell model, and Howard-Sheth model, among others, offers a comprehensive overview of the theoretical underpinnings of consumer decision-making processes. Khanna (2021) conducts an empirical study on the factors affecting consumer-buying motivations from a behavioral economics perspective. This study emphasizes the influence of cultural, social, and personal factors on consumer purchasing behavior and shopping habits. By understanding these factors, brands and businesses can develop more effective strategies and marketing messages that resonate with the targeted consumers' needs and preferences. This research is particularly relevant in understanding how various attributes, such as culture and social class, impact product and service choices.

In summary, the consumer decision-making process is a multifaceted phenomenon influenced by a myriad of factors, including psychological, social, and cultural elements. Understanding these factors is crucial for developing consumer protection policies, marketing strategies, and business models that effectively address the needs and preferences of consumers. As consumer markets continue to evolve, insights from behavioral economics will be invaluable in shaping strategies that align with the complex realities of consumer decision-making.

Methodology

This study employs a qualitative research approach to explore the role of behavioral economics in consumer decision-making. This kind of methods are suitable for investigating complex phenomena such as consumer behavior, allowing for a deep understanding of how individuals perceive various economic and psychological factors and respond to them.

Discussion

In the achievements of cognitive psychology, the psy hological factors that make consumers show irrational decision-making and behavior, such as anchoring effect, cognitive disagreement, frame dependence deviation, etc., are all taken by Daniel Kahneman and Tversky. Theoretical guidance.

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After running the corresponding economic model, consumer decision-making results that are completely different from the assumptions of traditional economics are obtained. Prospect theory is the development of expected utility theory. It is different from the expected utility theory of traditional economics, which believes that the absolute value of people's utility is equal between equal amounts of "gains" and "losses." The "gains" and "losses" with the same absolute number make different subjective value evaluations [4]. Firstly, people tend to hate returns. They always maintain a cautious and humble attitude before the harvest, worrying about the lost harvest. Therefore, the general investor's mentality is to take profit. In this experiment, people choose between buying two lottery tickets[5]. A lottery ticket is 100% worth 200 yuan, the probability of a B lottery ticket being scratched by 600 yuan is 1/3, and the probability of 2/3 is thanks for oner patronage. The expected value of this lottery is the same, but the A lottery is still the choice of most people. In addition, from the perspective of loss preference research, most people will not stop in front of the sacrifices that have already begun, hoping to make up for losses with greater risks. For example, let people choose between two treatment options. Option A can only heal 20% of the body. Option B has a 2/3 probability of being invalid, but a 1/3 probability of healing the body 60%. The results showed that most of the subjects chose option B. Finally, most people are more sensitive to loss than gain[6]. When the same amount of money is gained or lost, the pain caused by the loss will be greater than the happiness gained. Taking the consumer's risk aversion psychology into account, businesses should ensure that the discounts and conditions of promotional activities are clear and clear, and give consumers a full sense of security. There is also to ensure the reliability of marketing strategies. Once certain marketing activities have started, do not change or even cancel them easily. This is because path dependence and consumer psychology, which are more sensitive to losses, will make consumers feel that they have suffered losses after changing their strategies, thereby reducing their trust in businesses. Some negative examples are the hidden thresholds for various discounts in Double Eleven events in recent years[7]. The coupon ratio and discount strength are not directly proportional to the speed of panic buying. Such marketing a vities will arouse consumer disgust and lead to low sales.
22 Consumer behavior characteristics under.

Conclusion

This paper advances how behavioral economics has significantly influenced consumer choice behavior in the last decades. The rational individual has self-control, is not influenced from external factors, hence knows what is best for itself and final decision will be their best choice made. In the modern world, people always tend to make ideal decisions that will provide them with the benefit and satisfaction. However, it is crucial to recognize the contextual variability of behavioral effects across different cultures and socioeconomic backgrounds, which presents challenges for the universal application of behavioral insights. Nowadays, it is a shared knowledge and broadly accepted that consumers are cognitive misers and therefore, small and unintentional changes in the decision circumstance can significantly influence their decisions.

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