Emotions, Mood and Decision Making

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ABSTRACT

Decisions are made according to a complex cognitive and emotional evaluation of the situation. The aim of the paper is to examine the effect of mood on risky investment decision making by using a mood induction procedure. The paper investigates how happy and sad mood affects risky investment decision making and whether there is a difference between the perception of fixed investments and monetary investments. The analysis has been conducted focusing on individual investment decisions. Data for the research comes from a laboratory experiment, where 166 participants in happy, sad and neutral mood, filled out a questionnaire of investment decisions. The results indicate that mood does affect investment decision making, and positive and negative mood might have similar effect on the investment decision.

Keywords: Behavioural Economics, Emotions, Experiment, Decision Making, Experimental Economics, Investment, Mood

INTRODUCTION

Human beings do not behave in a perfectly rational cognitive way, mostly because our behaviour is influenced by psychological and emotional factors. This is also why behavioural economics researches these topics, which are relevant in the decision making process.

The contemporary economics has more and more subfields which connects economics with other social or even biological sciences. Accordingly, decision making is researched as a field connected to psychology, sociology, neuroscience etc. Neuroscience and economics has produced a new subfield of research, known as neuroeconomics, which inves-
tigates through neuroscientific methods phenomena in the brain triggered by economics related cognitive processes.

The paper investigates how emotions and mood influence decision making. The paper describes the role and importance of emotions in the decision making process by presenting research findings from behavioural economics and neuroeconomics based on literature review. The selected literature explains how decision making related cognitive processes involve emotions, which in turn will influence decision making itself.

Until recently the role of psychological factors in decision making have not been seriously studied by economists. Even after the appearance of the first well aimed psychology deliberations, which suggested that psychological factors may be more important in economic decision making than it has been acknowledged, economists were reluctant to incorporate into their research the role of psychological factors. It is only now, after the emergence and publications of hard neuroscientific data, that the role of emotions is being more and more acknowledged in the economic decision making process.

In the last few decades an important and continuously developing subfield of economics started to have a large research support. This subfield of economics is the experimental economics. Traditionally the only source of empirical data was the field data, coming from naturally occurring economic processes, which had major limitations. Experimental economics is able to produce new sources of data, which cannot be found on the field, and which makes it possible to test theory under controlled conditions in an artificial environment. Experimental economics has the necessary methods and tools to make it possible to test the effect of different emotions and mood on people’s decisions and risk perception.

Current research in behavioural economics is able to explain better and better the effects and influences of specific and particular emotions on economic and investment decision making. There is still much to study, especially how mixed emotions, and how different moods can change investment decisions. This paper provides research findings on the matter how different moods influence decision making, and people’s willingness to invest. A laboratory experiment was run to test the effect of mood on investment decision making.

The aim of the paper is to present how positive (happy), negative (sad) mood, compared to a neutral mood, affects investment decision making, by using a mood induction procedure.

The finding of the paper is that investment decisions made under happy or sad mood differ from decisions made under a neutral mood.

LITERATURE REVIEW

According to Rabin (1998), “because psychology systematically explores human judgment, behavior, and well-being, it can teach us important facts about how humans differ from the way they are traditionally described by economists.” (p. 11) According to Kahneman (2003),
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