

## Introduction to the Psychology of Misjudgment

“Man is a rational animal. So at least we have been told. Throughout a long life I have searched diligently for evidence in favor of this statement. So far, I have not had the good fortune to come across it.” –Bertrand Russell <sup>[4]</sup>

*This introduction is part of a [multi-part series](#) on human misjudgment by Phil Ordway, managing principal of [Anabatic Investment Partners](#).*

Danny Kahneman’s book [Thinking, Fast & Slow](#) has filled in a lot of holes in my knowledge, and it is the best collection of thinking on the subject that I’ve found. I had previously listened to a [recording](#) of Munger’s “The Psychology of Human Misjudgment” and read the [transcript](#) in [Poor Charlie’s Almanack](#) and elsewhere. That probably spurred some of my initial interest in the subject, and the combination of Munger’s talk with Kahneman’s research and writing is especially powerful. I think those two books tell you almost everything you need to know about the psychology of investing, and a lot about life in general too.

A special focus here will be business and investing. That is partly because those fields are such a fertile ground for misjudgment, but these lessons apply to almost all areas of life. I didn’t revisit my old college textbook in psychology, either – most or all of these examples were taken from own experiences or from the popular accounts I found online, in the newspaper, etc. over the past few months.

I’m assuming that most people are familiar with the original masterpiece, so I plan to just briefly allude to the “standard causes of human misjudgment” and the original examples so we can spend time on more recent findings and examples. As usual, Munger figured out the important ideas and left very few holes for us to patch, so I’ve tried to take the original material and add one or two new or supplemental topics and a few new examples. As always, the biggest bang for our buck – the lollapaloozas – will be found when the various factors *combine* and act in concert. “*Cherchez la femme*” and the combination. We need a working understanding of multiple models and their interaction, and it must be derived individually – it will be different for each circumstance and each person.

A short list of topics that would likely get more attention in “The Psychology of Human Misjudgment 3.0”:

- **Baseline information or base rates**
- **Prospect Theory and loss aversion**
- **Overconfidence**
- **Munger’s “two-track analysis”** – first, what are the fundamentals of the situation, rationally judged, and second, what are the subconscious or other psychological factors at play?
- **Self-awareness and self-honesty**

<sup>[4]</sup> The Basic Writings of Bertrand Russell (2009), p. 45