



# Anchoring in Negotiation Strategy

Jinze Guo <sup>1, †</sup>, Wei Li <sup>2, †</sup>, Zuoming Liu <sup>3, \*, †</sup>

<sup>1</sup> Shanghai World Foreign Language Academy, Shanghai, 200233, China

<sup>2</sup> The Village School, Houston, 77077, United State of America

<sup>3</sup> Cardiff Sixth Form College, CF24 0AA, United Kingdom

\*Corresponding author. Email: andy.liu@ccoex.com

<sup>†</sup>These authors contributed equally.

## ABSTRACT

The essay mainly focuses on the Anchoring effect and it discusses how the anchor functions in real life. To begin with, the term Anchoring is defined and many related types of research are cited to show that anchoring has important uses in our lives. Then, four different types of anchors are provided, and each shows a different way for our ways of thinking. Next, the essay points out how it works in the negotiation strategy, mentions the anchoring of the initial offering and the selective accessibility, and provides an example in the real estate market. There is much evidence given that the anchoring affects this market. It is concluded that the anchoring bias is common in our lives and can easily affect people in different aspects without our perception. It influences people's consciousness in our minds to affect our decisions.

**Keywords:** *Anchoring, Negotiation, Price*

## 1. INTRODUCTION

The Anchoring Heuristic, focalism, refers to the human beings' inclination to accept and depend on the initial information obtained before making a judgment or decision. In the 1970s, a series of studies on the field of anchoring and judgmental decision-making was first conducted by psychologists Amos Tversky and Daniel Kahneman in their early articles describing the theory. Daniel Kahneman conducted a series of studies on anchoring and judgemental decision making in their early articles describing the transformation of preferences into theory, and based on these studies discovered a number of biases in the economic field [1] [2]. In 2002, Kahneman was awarded the Nobel Prize in Economics for his work integrating psychology and economics. Anchoring behavior occurs when people make estimates or judgements about something as a result of anchoring psychology and the tendency to link current estimates to those already used in the past, to place too much weight on historical information (or even misperceptions), and then to make inadequate adjustments on the basis of them. When judgements and decisions are influenced by the fact that the outcome or target value is close to the direction of the initial information or initial value, i.e., the 'anchor,' the anchoring effect occurs. Anchoring refers to the practice of using the anchor value as a starting point for adjusting the final answer, despite the fact that the

anchor value may be a partial calculation or an implication of the problem formulation, and the adjustment from the anchor value to the target value is frequently insufficient, resulting in estimation bias. It is critical to emphasize that the information obtained in the first place is the key to the anchoring effect, which is crucial in the negotiation process. People tend to form a position with respect to this initial information, and this position eventually creates a constraint in people's minds that governs their estimation of that event that requires a decision to be made. Most rational people will adjust their estimates to some extent based on their own experience, knowledge, judgment, and speculation, but such adjustments are frequently insufficient, resulting in estimates that are not as good as they could be. Furthermore, the anchor can be conscious, informative, valuable, or irrelevant to the decision at hand. However, it is worth noting that most people are driven by this initial information, even if it has no bearing on the final decision.

The main purpose of this paper is to discover the relationship between the anchoring negotiation and business strategy, which has been a popular topic to chart about in our modern society. This relationship is quite important as good negotiations contribute significantly to business success, which can aid the business in delivering lasting, quality solution. And the the first real reference

point is provided by the anchoring or what one expects out of a potential deal.

## 2. TYPES OF ANCHORS

There are many different types of anchors in the anchoring effect, and each anchor has its different uses to incentivize people to make irrational decisions. One common type of anchor is the anchor from the initiative minds. In the research done by Nicholas Epley and Thomas Gilovich [3], they discovered that anchoring can function to help people quickly respond to the things that are close to the correct answer. However, they are required to adjust and correct to get the closer correct value. Thus, people are easily influenced by the simple things that have appeared in their minds. Take the experiment taken by Kahneman that when calculating the product from 1 to 8, one is the ascending order (1x2x3x4x5x6x7x8) and the other is the descending order (8x7x6x5x4x3x2x1). The researchers ask the experimenters to predict the product in 5 seconds. The result shows that the sequence of numbers with the descending order has a higher number of predictions than the sequence of numbers with ascending order. This is due to the initial mind that they make predictions based on the first few numbers they saw. For the descending order, they start predicting by first calculating 8x7, and further calculating. However, for the ascending order, they start predicting from the calculation of 1x2, thus the value got is smaller than the descending order. It is the 'self-generated anchor' that contrasts the externally-provided anchors in the standard anchoring paradigm [3]. This is the first common type of anchor that is based on intuition.

Furthermore, the most common type of anchor for real-life applications which is related to the magnitude of the anchor is often called the magnitude priming. It is generally meant for the large or the small magnitude which can be shown in a specific circumstance. Thus, people's feelings and estimations can be affected a lot [4]. It usually refers to the situation where the size or length of the anchor will influence people's decision-making a lot. The anchor can be not related so much to the main topic, like the example presented in the essay that people who make the longer lines will be more likely to make a great prediction of the average temperature in Honolulu in July and to generate the synonymous words that take the place of the original words [2]. Therefore, the magnitude of the anchor will influence people's decisions a lot. This can be discovered in the psychology part that a person's internal mind of something else can reflect their behaviors, whether they are bold or conservative.

What's more, there is another common variety of anchors that show the circumstance for the best time or the worst time. Therefore, people will tend to make more rational decisions so that they are influenced a lot by the

anchor. People may sometimes tend to underestimate the time taken for them to finish one thing so that they are not arranging the time so well to do other important things [6]. Similar to that, it is mentioned that when predictions are made by people, the outcome that can be easily obtained is usually not the likely event, but it is regarded as the most emotional event, or the event that is the most relevant to the personal objectives [7]. Therefore, the anchor itself often has some relationships with you so that you have emotions on it to become the anchor that influences your decisions. In some of the experiments, researchers can determine the extent of optimism by just looking at the anchor of the movement of the head and the body. Thus, the best and worst scenario shows the prediction as the initial anchor is decided here and if different predictions of behaviors are made, the accuracy and outcomes are different.

Last but not the least, another form of anchor is the incidental anchor, which can be regarded as the anchor that is attached without doing specialized research on it. This kind of anchor often does not have so much obvious effect, but it will influence people's behavior slightly to a small extent. As mentioned, the influence on judgment - that is, their impact as anchors - is likely to be relatively small [2]. But their effect is not always zero. In this case, people will be imperceptibly influenced by the things which are shown to them but are not regarded as the anchor. For example, another experiment that is often told in the anchoring effect is the problem of the percentage of African countries in the United Nations. Two groups of people are shown with two different numbers which are 10 and 65. Then they are going to predict the percentage of African countries in the United Nations. For the group that shows 10, the average percentage is 25%, but for the other group, the average percentage is 45%. This presents that the two numbers that seem to be useless act as the anchor that affects people's decisions. This can be regarded as the incidental anchor.

These are the common types of anchors that people often use in real life and if we notice these different types of anchors a lot, some of the irrational behaviors can be eliminated.

## 3. ANCHORING IN NEGOTIATION

The effect of incidental anchoring is ubiquitous in negotiation as any small piece of information may influence our decision-making, which explains a common tendency of giving too much weight to the first number presented in the negotiation and then making appropriate adjustments from that starting point or "anchor", proven by an experiment done by Amos Tversky and Daniel Kahneman (mentioned in the types of anchors). Negotiation, a strategic discussion, settles an issue or problem in a way that both parties find adequate. In one negotiation, the agreement on a certain point of

view is the thing that each party is trying to achieve, and all involved partakers attempt to sidestep arguing but agree to reach a form of compromise.

### ***3.1 Initial offering***

The first offer can be considered as the anchor in the context of negotiation, which demonstrates the influences of the first offer as well as the final outcome: an initial offer may function as an anchor to incorporate final judgment toward the negotiation process [8]. For instance, a person owns a house and he wants to sell it; he, then, asks an agent to inspect and evaluate the house, and the agent gives the price that it will list for the house and the price of purchasing. Low and high anchors can be provided by the manipulated price; the listing price can influence each of the estimations. The price that the agent would list for the house can be considered the first potential offering in the negotiations. The expert of real estate, however, will rather deny the listing price but re-evaluate the house based on the features of the property to justify the estimation of the agent [9]. This judgment is consistent with Mussweiler and Strack selective accessibility model, derived from confirmatory hypothesis testing theory, in which the judge (the expert in the context) will evaluate whether the anchor is a suitable answer or not by looking for ways in which it is similar to the anchor, resulting in the anchoring effect [10]. Nevertheless, this initial offering effect could be altered or eliminated according to Galinsky and Mussweiler [11]. They found that considering the opponent's BATNA (best alternative to the negotiated agreement), rejecting the lower value of the agreement, and the reservation price could eliminate the initial offer, which is only advantageous if the negotiator is conscious of the value of the anchor. However, the anchor value will influence the negotiators subconsciously and internalize their judgment to the preliminary reference. The reference price, anchor value, is presented to the negotiators or consumers to consider the offer [11].

Nonetheless, the initial offering or reference price still has a significant impact on the negotiation process [12]. Researching the mechanics of online auctions, they discovered that the consumers' bid and purchase intentions will be impacted by reference price, which illustrates the mighty effect of anchoring in practical decision-making situations, impacting the interest and rights of individuals [12].

### ***3.2 Selective accessibility***

Priming, areas of the brain related to a concept that remains activated at some level, is relied on by this theory, which is ubiquitous. Making the concept more easily accessible, priming makes it more able to affect the behavior of people without realization of themselves. According to this theory, given that people are offered the

anchoring piece of information, they will mentally appraise whether this is the plausible value for whatever they are thinking of by building a mental representation of the situations or objects. While people are building their model, they will consider or activate other pieces of information that are consistent with the anchor, simultaneously. Thus, this information becomes primed and possibly affects the decision-making process [13].

In 1997, Strack and Mussweiler made an experiment to test the idea mentioned above by using a form of a questionnaire in which they were asked to reckon whether the value of an object is more elevated or more subordinate than the anchor given. In the experiment, the participants would be given a specific object (Target) and asked to evaluate whether the range given (Anchor) is higher or lower than the actual value merely by using their minds. Furthermore, they would be asked another question similar to the previous one. The results demonstrated that the anchoring effect is considerably stronger if the object dimension was identical for both questions, which supports the theory of selective accessibility. The anchor-and-adjust hypothesis seems incorrect, however. Rather, it suggests that anchoring bias depends on numerous, various mechanisms; depending on the different circumstances, it occurs for diverse reasons [13].

## **4. APPLICATION**

In the real estate market, the limited rationality of traders has also resulted in some puzzling "anomalies" in different economic states. During a boom, properties sell quickly and for close to or above the asking price. Properties take longer to sell during a property slump because sellers ask for more than they expect to sell for, and some sellers are even forced out of the market. The anchoring effect in negotiation can explain these "anomalies" in the real estate market. When house prices rise, traders form their own expectations of future price rises and anchor their offers to the trend of that expectation, i.e. buyers adjust their offers and sellers adjust their asking prices, and trading occurs only when buyers offer more than or equal to sellers' asking prices. So, at this point, the volume of transactions will change before the price of transactions, i.e. the increase in volume precedes the increase in price; in the circumstance of falling price, the reserve price of sellers in the real estate market traders is more sticky than the reserve price of buyers. Due to loss aversion (as sellers are more sensitive to the same losses than gains), sellers have an incentive to anchor to the previous higher historical price (i.e. the higher historical price is used previously as a reference price) to adjust their asking price, and buyers adjust their offer accordingly. Similarly, a transaction will only occur if the buyer's offer is greater than or equal to the seller's asking price, at which point the property market will eventually take longer to reach

a higher mutually acceptable price, resulting in a change in transaction volumes ahead of transaction prices, i.e. a drop in transaction volumes ahead of a drop in house prices. Hence, anchoring in negotiation significantly influences the transactional volumes and housing prices.

Numerous economists have discovered strong evidence of anchoring effects in the global real estate market [15][16][17][18]. According to Zeng, he alternatively, believed that the effect may be due to characteristics of the housing market [14]. Real estate as a market that is not purely an asset (an owned property), the combination of the dual attributes of investment and consumption leads to a certain degree of specificity in the use of the real estate for residential consumption, and it is this specificity that leads to the fact that real estate is no longer just a consumer good but also an investment good, at which point the nature of the asset is distorted to varying degrees. From the standpoint of the real estate market as a pure asset (investment property), investors' judgments, expectations, emotions, and other psychological factors formed during the transaction process are not only reactions to the market, but also the emotional foundation of the entire market, and these psychological factors can influence investor behavior, leading to significant oscillations in the entire market away from the fundamentals of the real economy. As a result, investor behavior in the real estate market is irrational. By using the well-known "Humans and Econs" theory in Behavioral Economics, those investors are Humans (ibid) [18].

## 5. CONCLUSION

Anchoring bias does influence humans' daily lives, which is unquestionable. With numerous research from around the world and different time periods, many studies have demonstrated the robust effect of anchoring in human decision-making processes. As we are living in the current situation, in the absence of other information, people have to realize and recognize the impact of anchoring, which may be imperceivable. Especially in the negotiation, of any kind, people are frequently affected by it without perception, relying heavily on the piece of information given by the opponents or others in order to shape the decisions to negotiate: they always tend to believe their cognitive consciousness rather than thinking it logically. It limits people's ability to think logically and consider other aspects that ought to be considered. Adequate anchoring helps people to set their expectations of what is standard or premium, reduces the cognitive cost of decisions, and can even increase the perceived value of a product, such as the real estate market mentioned in the essay. Moreover, experts, and real estate agents, can be strongly impacted by anchors in negotiation. High anchors entice our awareness of the positive qualities of the item or individual, and low

anchors lure awareness to flaws, when conditions are uncertain [11].

In the future, we hope to get deeper through the relationship between it in the real world experience, which can help the researchers to materialize the theory into real life. And further studies and research need to be conducted to investigate in the anchoring in negotiation strategy in which we may not have the opportunity to cover in this paper.

## REFERENCES

- [1] A, Tversky & D, Kahneman (1973). Judgment under Uncertainty: Heuristics and Biases: Biases in judgments reveal some heuristics of thinking under uncertainty. *Science*, 185(4157), pp. 1124-1131.
- [2] D, Kahneman (1992). Reference points, anchors, norms, and mixed feelings. *Organizational Behavior and Human Decision Processes*, 51(2), pp. 296-312.
- [3] N, Epley & T, Gilovich (2001). Putting adjustment back in the anchoring and adjustment heuristic: differential processing of self-generated and experimenter-provided anchors. *Psychological Science*, 12, 391-396.
- [4] D, Oppenheimer, R, Leboeuf & T, Brewer (2008). Anchors aweigh: a demonstration of cross-modality anchoring and magnitude priming. *Cognition*, 106, 13-26.
- [5] N, Epley & T, Gilovich (2010). Anchoring unbound. *Journal of Consumer Psychology*, 20(1), 20-24.
- [6] R, Buehler, D, Griffin & M, Ross (1994). Exploring the "planning fallacy": why people underestimate their task completion times. *Journal of Personality and Social Psychology*, 67, 366-381.
- [7] C, Morewedge, D, Gilbert & T, Wilson (2005). The least likely of times: how remembering the past biases forecasts of the future. *Psychological Science*, 7 (8), 626-630
- [8] A, Galinsky & T, Mussweiler (2001). First offers as anchors: The role of perspective-taking and negotiator focus. *Journal of Personality and Social Psychology*, 81(4), 657-669.
- [9] G, Northcraft & M, Neale (1987). Experts, amateurs, and real estate: An anchoring-and-adjustment perspective on property pricing decisions. *Organizational behavior and human decision processes*, 39(1), pp.84-97.
- [10] T, Mussweiler & F, Strack (1999). Hypothesis-consistent testing and semantic priming in the anchoring paradigm: A selective accessibility model.

- Journal of Experimental Social Psychology*, 35(2), pp.136-164.
- [11] A, Galinsky & T, Mussweiler (2001). First offers as anchors: the role of perspective-taking and negotiator focus. *Journal of personality and social psychology*, 81(4), p.657
- [12] A, Wolk & M, Spann (2008). The effects of reference prices on bidding behavior in interactive pricing mechanisms. *Journal of Interactive Marketing*, 22(4), 2–18.
- [13] F, Strack & T, Mussweiler (1997). Explaining the enigmatic anchoring effect: Mechanisms of selective accessibility. *Journal of Personality and Social Psychology*, 73(3), 437-446.
- [14] J, Zeng (2010). A Study of Anchoring Effect (Doctoral thesis, Fudan University)
- [15] T, Qiu & G, Liu. (2013). ‘Housing anchoring in China, from 1998’, *Contemporary Economy of China* 1(199), pp. 75-85
- [16] W, Zeng & J, Liu (2016). ‘Anchoring and Judging Bias’ (Doctoral thesis, Shandong Caijing University)
- [17] L, Qiu & Z, Deng (2009). ‘Research on the anchoring effect of China’s real estate market’
- [18] R, Thaler & C, Sunstein (2008). *Nudge: Improving decisions about health, wealth, and happiness*. Yale University Press.

**Open Access** This chapter is licensed under the terms of the Creative Commons Attribution-NonCommercial 4.0 International License (<http://creativecommons.org/licenses/by-nc/4.0/>), which permits any noncommercial use, sharing, adaptation, distribution and reproduction in any medium or format, as long as you give appropriate credit to the original author(s) and the source, provide a link to the Creative Commons license and indicate if changes were made.

The images or other third party material in this chapter are included in the chapter’s Creative Commons license, unless indicated otherwise in a credit line to the material. If material is not included in the chapter’s Creative Commons license and your intended use is not permitted by statutory regulation or exceeds the permitted use, you will need to obtain permission directly from the copyright holder.

