

# Reconsidering Risk Aversion

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Measuring risk preferences is challenging because people's choices over lotteries violate expected-utility axioms and sometimes vary depending on how the lotteries are framed. We develop a two-stage procedure to measure risk preferences, and we demonstrate it via a survey about hypothetical retirement investment choices administered to 601 Cornell students. The first stage is the standard method of eliciting choices over risky lotteries. In the second stage, we confront participants with their inconsistencies—their different responses to choices framed differently that should be the same according to expected-utility axioms—and allow them to update their choices. Our key assumption is that individuals' updated, "reasoned" choices more closely reflect their preferences than their original, "untutored" choices. We find that on average, participants update in the direction of consistency with expected-utility axioms, and their reasoned choices exhibit less risk aversion than their untutored choices. Our results suggest that deviations from the axioms usually reflect decision errors rather than non-expected-utility preferences.

Our two-stage procedure may hold promise as a way to measure risk preferences for the purpose of setting optimal defaults or giving advice about portfolio allocation.