Doctoral dissertation at Göteborg University, Sweden, 2003

Abstract

Juliusson, E. A. (2003). *Studies in Escalation of Investment Decisions*. Department of Psychology, Göteborg University, Sweden.

The tendency to continue to invest following a negative outcome (sunk cost) is referred to as the sunk cost effect or escalation. To take sunk cost into account in making decisions is not rational when there is another more beneficial alternative. In the present thesis, explanations are proposed and tested. Two studies investigated the hypothesis that a loss-minimizing decision goal will lead to stronger sunk cost effects than a gain-maximizing decision goal. In Study I consisting of three experiments where participants made fictitious investment choices, the results only supported the hypothesis when the decisions were personal investments, not when they were business investments. Furthermore, it was found that both prior losses and gains affected the decisions. It was also shown that future net returns and sunk outcomes jointly affect investment decisions. A principle of contingent weighing of past and future outcomes was proposed in Study II. Experiment 1 tested the prediction that participants who were instructed to minimize losses would place more weight on prior outcomes but less on future outcomes, whereas the reverse was predicted of participants instructed to maximize gains. In Experiment 2 the instructions were augmented by a bonus, either for (personal investment) decision scenarios or decontextualized gambles. The results yielded main effects of instructions and bonuses but no evidence of contingent weighing. Yet, replicating the results of Study I, both future and past outcomes affected the decisions and participants both escalated and de-escalated. By introducing a gain-loss frame manipulation in Study III, the results indicated that a gain frame (gain-maximizing goal) led to a stronger preference for continuing investment when the sunk cost was high than when it was low. No such effect was found for a loss frame (loss-minimizing goal) or a control condition. The inconsistent results were hypothesized to be due to an overreaction for a loss-minimizing goal so that participants discontinued without considering the sunk cost. However, for a gain-maximizing goal participants considered both prior and future gains and losses. Study IV addressed the generalizability of escalation research. It was hypothesized that the task dimensions monetary vs. non-monetary decision goal, transparent vs. non-transparent sunk cost, and accountability would distinguish real-life business, political, and personal decisions. In support of the hypothesis, ratings of typicality of rel-life showed that a monetary decision goal, a transparent sunk cost, and accountability characterize business decisions, and that a non-monetary decision goal, a non-transparent sunk cost, and no accountability characterize personal decisions. Inconsistent with the hypothesis, monetary decision goal and no accountability and, consistent with the hypothesis, a non-transparent sunk cost characterized political decisions. Escalation was found for all the types of decisions but was not related to the task dimensions.

Key words: Decision making, sunk cost, escalation.