Decision Processes Colloquia

Monday, February 16, 2015

Where: 245 JMHH

When: 12:00 – 1:15 pm

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Putting All of Your Eggs in One Basket: Costly Reluctance to Hedge Emotions

ABSTRACT: By hedging, people routinely minimize the potential losses from their investments by making a contrary investment (e.g., insurance) that pays off under an undesired state of the world. We examined whether people hedge against emotional disappointment. Loss aversion suggests people should minimize the risk of feeling negative emotions by betting against rather than on the occurrence of desired outcomes. In contrast, we found in the context of a US Presidential Elections, an NCAA basketball game, an NCAA hockey game, and NFL football games that a substantial proportion of participants violated loss aversion and were unwilling to hedge the potential loss of their preferred candidate or team. Participants were reluctant to hedge whether hedges were risky or without risk, hypothetical or real, and were for money or other goods. Participants were reluctant to hedge even when controlling for optimistic beliefs about the probability of the desired outcome, and many refused even when hedging dominated its alternative. Forty-six percent of NCAA basketball fans, for example, rejected a free hedge that would pay $5 or a comparably valuable good if their team lost the game they were about to attend. Willingness to hedge did increase for most participants as the value of the hedge increased, and was greater when the payout would be donated to charity than paid to the bettor. The results suggest that reluctance to hedge emotions stems from an interdependence dilemma: commitment (e.g., to a candidate or team) induces a willingness to engage in costly self-sacrifice. Furthermore, it produces two notable anomalies in decision making: risk seeking behavior and a preference for dominated alternatives.

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