A Neurological Explanation of Strategic Mortgage Default

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Notes

1. The inability to pay one's mortgage due to such factors as job loss, income curtailment, or prolonged illness is known as an "economic default."

2. The negative monthly cash flow refers to the ability to rent a comparable home for less than what it costs to own the same home.

3. Even in recourse states (there are 41 of them), legal maneuvers can make it

7. At the time of Staw (1976), the more common term was "escalation of commitment." It has subsequently been referred to more often in a business environment as "sunk cost fallacy." In game theory, consideration of sunk costs are often referred to the "Concorde Effect," named after the observed behavior of the British and French governments' continued investment in the Concorde airplane long after it was evident the economics clearly did not support further production efforts.

8. While a bit of a hard sell, authors such as Baliga and Ely (2011) argue that due to an array of possible alternative mental constraints, considering sunk costs can be partially justified. In this study, we adopt a more traditional approach of viewing the incorporation of sunk costs as a fallacy.

13. Because being underwater is a necessary condition for strategic mortgage default, all of our scenarios are associated with negative equity. As such, the behavioral theories we test are all taking place in the loss domain as defined in Kahneman and Tversky (1979).

14. Note that by pairing the scenarios the way we did allows us to conduct a ceteris paribus analysis so that we can attribute and difference in results to the sole variable that differs in the analysis.

15. This interval was deemed appropriate through pre-testing in that it allows sufficient time for blood to flow to the specific area (s) of the brain while contemplating the decision, but not so much time that the respondent's mind begins to drift. It should be noted that if a sub-optimal interval is selected, it

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