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Anomalies: The Endowment Effect, Loss Aversion, and Status Quo Bias

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Abstract

A wine-loving economist we know purchased some nice Bordeaux wines years ago at low prices. The wines have greatly appreciated in value, so that a bottle that cost only $10 when purchased would now fetch $200 at auction. This economist now drinks some of this wine occasionally, but would neither be willing to sell the wine at the auction price nor buy an additional bottle at that price. Thaler (1980) called this pattern—the fact that people often demand much more to give up an object than they would be willing to pay to acquire it—the endowment effect. The example also illustrates what Samuelson and Zeckhauser (1988) call a status quo bias, a preference for the current state that biases the economist against both buying and selling his wine. These anomalies are a manifestation of an asymmetry of value that Kahneman and Tversky (1984) call loss aversion—the disutility of giving up an object is greater that the utility associated with acquiring it. This column documents the evidence supporting endowment effects and status quo biases, and discusses their relation to loss aversion.

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