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The role of emotions in the endowment effect

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Abstract

This paper argues that the endowment effect – the tendency for minimum selling price to exceed maximum buying price for a particular object – might be minimized when a negative emotion is induced. The findings from two experiments on 400 participants support this hypothesis: the endowment effect only occurs when participants are induced to feel happy, and is absent when people are induced to feel sadness. Thus, the importance of emotional states is highlighted.

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1. Introduction

Economists are often concerned about the estimated "value" of various goods or services, and they attempt to derive estimations regarding said value. The assessment of objective values is typically derived from two concepts: "WTA and WTP." "People are required

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to estimate the least price they are willing to accept to sell (WTA), and the ceiling price they are willing to pay (WTP)". Most economists argue that the gap between WTA and WTP should converge for most commodities. However, experimental research shows that the values of WTA and WTP might be remarkably diverse, even for an identical object. Specifically, research on the valuation of objects by laboratory experiments indicated that people set a higher WTA on an owned object than WTP for a not-owned-yet object (Kahneman, Knetsch, & Thaler, 1990; Knetsch & Sinden, 1984; Thaler, 1980).

The gap between the buying price and the selling price of an object is dependant on the status of ownership, and is termed "the endowment effect" (Kahneman et al., 1990; Thaler, 1980). The endowment effect has been highlighted in studies employing diverse methodologies, including laboratory experiments (Kahneman et al., 1990), economics style market experiments (Franciosi, Kujal, Michelitsch, Smith, & Deng, 1996), and field studies (e.g., Johnson, Hershey, Meszaros, & Kunreuther, 1993). Previous research has shown that emotional states are influenced directly by subjective valuation for an object (Forgas & Ciarrochi, 2001). This research also asserts that emotional states may moderate the endowment effect, and two experiments prove the endowment effect only occurs with positive emotions – not with negative emotions.

2. Literature review and building hypotheses

2.1. The endowment effect review

Research on endowment effect (Franciosi et al., 1996; Johnson et al., 1993; Kahneman et al., 1990; Strahilevitz & Loewenstein, 1998) has shown that people tend to demand a higher selling price for a commodity that they own than they would be willing to pay if they were looking to acquire it as a buyer. The endowment effect also appears to be moderated by regulatory focus: participants were reluctant to exchange an endowed object when they focused on preventative measures, but not when they focused on self-promoting goals (Liberman, Idson, Camacho, & Higgins, 1999). Mandel (2002) found that the endowment effect was observed when participants imagined another individual wanting to buy from or sell to them, but not when they imagined wanting to by from or sell to another individual. Recent research has focused on emphasizing the importance of affective response (i.e., positive and negative feeling evaluations).

Loewenstein and Issacharoff (1994) found that the manner in which people obtained particular objects affected their valuation of the objects. Specifically, individuals who received goods based on exemplary performance valued the goods more than if they received the goods by chance or based on poor performance. Loewenstein and Issacharoff suggested that affective roles create positive associations with the items in question. Specifically, much research in decision making has emphasized the importance of affective response in judgment and choice (Damasio, 1994; Loewenstein, 1996; Peter & Slovic, 2000; Slovic, Finucane, Peters, & MacGregor, 2002). Given this data, the following will focus on exploring the relationship between emotional states and the endowment effect.

2.2. Building hypotheses

Reference point dependence and loss aversion are key roles in the endowment effect (Kahneman & Tversky, 1979). In this article, reference point dependence and loss aversion