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Of mice and economics. (discussion of unrecoverable economic costs)(Brief Article)(Column) *Dan Seligman*.

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In both their business decisions and their personal lives, people keep resisting a major precept of **economics**.

STUNNING NEWS: **Mice** do better than people at grasping an important principle of **economics**.

No proposition in **economics** is more firmly established than the supreme irrelevance of sunk costs. A sunk cost is money spent and now unrecoverable. In business, in sports, in everyday life, your next move should be driven by future costs and benefits. Viewing this rule as almost too obvious to mention, the famous Paul Samuelson-William Nordhaus textbook, **Economics**, gives sunk costs only a couple of paragraphs, advising: "Let bygones be bygones."

This advice would seem at first blush to be liberating. In the corporate world, it often means that you can just write off the blunderolas and start over again. The rule also implies that you need not risk heartburn finishing the large pizza you ordered. Or sit through a long, boring play just because the theater tickets cost \$60 each. Or read the New York Times editorial page just because you paid for the subscription.

The rule should be especially liberating in the world of sports, which seems to have a special difficulty in letting bygones be bygones. It appears that the Yankees started pitcher Kenny Rogers in the fourth game of the 1996 World Series mainly because George Steinbrenner had earlier paid \$20 million for Kenny, who was consistently getting clobbered in the weeks leading up to the Series. (As things turned out, he got bombed again, in a game the Yankees miraculously won anyway.)

A huge sunk-cost effect is also discernible in the National Basketball Association. A major cost for NBA teams is the salaries paid for their top draft picks. So what happens when the guy you pick turns out to be a lemon? Do you play him anyway? It seems you do. Evidence for this folly is elaborated in an article in the September 1995 *Administrative Science Quarterly*. Authors Barry M. Staw and Ha Hoang of the University of California, Berkeley reported: "The higher a player was taken in the college draft, the more time he was given on the court, even after controlling for other logical predictors of playing time, such as performance, injury and trade status."

As is implied in the poignant examples above, many people do not feel liberated by the news that sunk costs are irrelevant. Quite the contrary -- they wish to resist the news. Why would they do this?

Different scholars have answered this question in different ways. Sometimes, it appears, the decision makers have a confused notion that the sunk costs will be "wasted" if they are ignored. Sometimes they have a clear and nonconfused reason for believing that their own interests collide with those of the organization. This process is on display in the

chief executive who sees his own personal prospects as definitely rosier if the failing strategy he's been supporting can be propped up until he reaches retirement age. So the company flings good money after bad until it gets a new chief executive, who writes off everything in sight, thus guaranteeing himself a couple of great years.

But the most broad-based, compelling answer to the question is: ego. Higher primates do not like to admit, even to themselves, that they have screwed up. It's not as though somebody was going to fire Steinbrenner if Kenny Rogers had stayed on the bench during the World Series. What seems to have driven George's decision was the standard, deep-seated, egoistic human need -- evidenced in numerous psychological experiments -- to justify the sunk costs in one's life. Research supported by the National Science Foundation and published by the Journal of Abnormal and Social Psychology shows that membership in groups is cherished more deeply when the initiation process has been painful and embarrassing.

Mice are far more rational. Lacking any need for self-justification, and genetically programmed to focus narrowly on getting through the day in one piece, they appear oblivious to unrecoverable past costs. So are ducks, blackbirds, wasps and numerous other "cognitively humble" beings. That phrase appears in a recent (May 23) issue of the British publication *New Scientist*, in an article by Peter Ayton and Hal Arkes. Ayton and Arkes tell us the mouse mother's litter is defended far more vigorously when it's large than when it's small -- which means, clearly, that the mother's cost/benefit calculations are focused on the future. Earlier losses to the litter are forgotten. Those losses are simply written off.

Whether you are an investor holding on to a stinker in the hope of getting your money back, or a telephone company burdened with copper wires in the fiber-optic age, learn from the cognitively humble mouse.

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