Silver lining effect study, 'I have some good news and some bad news'

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Communicating "I have some good news and some bad news" is better than combining messages into a single, bleak result when small gains and large losses occur together, according to a study in the current issue of *Management Science*, the flagship journal of the Institute for Operations Research and the Management Sciences (INFORMS).

"The Silver Lining Effect: Formal Analysis and Experiments" is by Peter Jarnebrant of the European School of Management and Technology and Olivier Toubia and Eric Johnson of Columbia University.

The authors ask how people's choices change when they are presented with information in either of two ways: as an integrated whole or as two segregated pieces. For example, they ask, does an investor prefer a statement showing only an aggregate loss of $95 - or one showing a loss of $100 and a gain of $5?

The authors follow upon work first done by RH Thaler in 1985.

"Thaler's intuition was that decision makers would prefer to mentally separate a small gain from a big loss, thus providing a silver lining to the loss," explains Prof. Olivier Toubia, one of the authors. This study provides new tests to the original assumptions.

The authors also tested to determine the threshold balance - for example, if subjects also prefer the information divided when there is a more even, 50/50 split in gain and loss.

The authors determined that the smaller the positive amount ($5 in the above example) and the larger the negative one ($95), the more people prefer that the information be presented in separate sections rather than summed together.

"When the loss gets larger, you're more likely to want to separate a small gain from that loss," explains Toubia.

This perception plays better with customers who are less loss averse, they determined.

The observation, the authors write, is important for decision makers in finance, retailing, and other organizations.

In finance, for example, a mutual fund posting a quarterly loss would be better perceived by investors if the accompanying information pointed out the portions of the portfolio that posted a gain.

In a retailing example, automobile manufacturers and dealers will be better appreciated by potential customers if they price a car at $20,000 with a $500 rebate than if they price the same car at $19,500.

They reached their conclusion through two experiments with online respondents. In the first, involving an online panel, respondents were asked to imagine losing their jobs and having to choose between two new job possibilities offering different mixes of lost winter and summer vacation time. In the second experiment, with a group who signed on via the Amazon.com company Mechanical Turk, respondents rated four sets of gambles involving a one in three chance of winning. In one set of gambles, the gain and loss were presented separately; in another, the total amount was combined.

Source: Institute for Operations Research and the Management Sciences

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