



# Multiple reference points in investor regret

Chien-Huang Lin <sup>a</sup>, Wen-Hsien Huang <sup>b,\*</sup>, Marcel Zeelenberg <sup>c</sup>

<sup>a</sup> *Department of Business Administration, National Central University, Taiwan*

<sup>b</sup> *Department of Business Administration, Soochow University, Taiwan*

<sup>c</sup> *Department of Economic and Social Psychology, Tilburg University, The Netherlands*

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## Abstract

Regret is the result of a comparison between “what is” and “what might have been”. Although regret is a relevant emotion in the life of investors, research studying the regrets of real investors and how these are influenced by multiple reference points is lacking. We present a field survey that investigated the regrets of real stock investors in relation to multiple “what might have been’s.” We found that their regrets are most influenced by what their outcomes might have been had they not invested, by their expected outcomes and by the best-performing unchosen stocks. In addition, we also found that the feeling of regret was influenced by losses or gains relative to each reference point rather than by the size of the loss or gain.

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## 1. Introduction

George is planning to invest \$50,000 in the stock market. After narrowing the search, he considers three stocks (Yahoo, eBay, and Amazon). He decides to invest in eBay, mainly

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\* Corresponding author. Address: 6F, No. 74, Zhongshan Road, Sanchong City, Taipei County 241, Taiwan. Tel./fax: +886 2 29874084.

E-mail address: [huang.wenh sien@seed.net.tw](mailto:huang.wenh sien@seed.net.tw) (W.-H. Huang).

due to his expectation that it will provide higher returns than the alternative investments (eBay is expected to increase by 20% within the next year). A year later eBay's stock price increased 10%, while the price of Yahoo increased by 35% and that of Amazon decreased by 5%. How does George now feel about his decision to invest in eBay? Does he feel regret, because he compares his actual outcome (a 10% gain) to the counterfactual outcome that would have been obtained when he had invested in Yahoo's (a 35% gain). Or does he feel rejoicing (the opposite of regret), stemming from a comparison with the outcome that would have been had he invested in Amazon (a 5% loss)? George's post-decisional feelings may, in addition, be influenced by his expected profit (a 20% gain) and what his outcome would have been had he remained inactive (i.e., the non-investment outcome which would be no gain and no loss). How do these four possible reference points influence regret? This is the question that is central in the present manuscript.<sup>1</sup> Additional questions are: Which of these reference points has the largest impact on regret? Do the losses (the unfavorable comparisons between the obtained outcome and each reference point) have larger influence than the gains (the favorable comparisons between the obtained outcome and each reference point)? Put differently, are there asymmetric effects of these reference points on regret? Is investment regret mainly driven by the sign of the outcome (is the outcome a loss or a gain in comparison to the reference point) or more by the magnitude of that loss and gain? We have investigated these questions in large survey with over two hundred real investors, reflecting on their personal investment decisions.

Regret is the most relevant emotion in domain of decision making (Zeelenberg & Pieters, 2006). It stems from the comparison between "what is" and "what might have been" (e.g., Loomes & Sugden, 1982; Van Dijk & Zeelenberg, 2005). Although it has often been argued that regret is a relevant emotion in the life of investors (e.g., Kahneman & Riepe, 1998; Shefrin & Statman, 1986), we do not know of any study actually investigating investors regret. The study we report here is a first attempt to obtain insight in such regrets. We think these regrets are of particular interest because of the different reference points that are naturally associated with investment decisions. At present, we know little about the simultaneous impact of multiple reference points on regret. In most regret studies, subjects are simply asked to indicate their regret over a decision concerning two alternatives (e.g., gamble A vs. gamble B or brand A vs. brand B) with the unchosen alternative being the only reference point. Although some scholars have recognized that decision makers may use multiple reference points in decision making and in judgments of post-decisional regret (Bell, 1982; Boles & Messick, 1995; Inman, Dyer, & Jia, 1997; Oliver, 1996), Frederick and Loewenstein (1999) recently pointed out that the information of multiple reference points and their relative weighting has not been investigated empirically.

To our best knowledge, Tsiros (1998) presented the first regret study in which the choice set was extended to three-alternatives. In his first study, undergraduate students read a scenario describing a business decision. They read that there were three options and that the selected option neither the best, nor the worst. In the second study students chose between three different gambles. The participants indicated the amount of regret they felt. Tsiros found that when the obtained outcome exceeded expectations regret was influenced by

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<sup>1</sup> Of course we should note that it is possible that investors may use still other, additional, reference points, such as a stock that investors had not even considered previously, but that has become famous after they purchased the target stock. However, these more incidental reference points are not the focus of our current research.

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