

Prospect Theory - complement

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Prospect versus Utility Theory

- Marketers are implicitly interested in **how** and **why** people make decision
- Having in mind the fact, that we are rational beings :
 - we have to weigh up the odds
 - apply laws of probability
 - make decision
- That is a easy world and marketing would be a simple science

BUT

- We have to know **how** and **why** our behaviour deviates from rational decision models

Prospect versus Utility Theory

- **Utility Theory :**
 - Two prospects with the same expected utility will be given the same preference by rational decision makers
- **Prospect Theory :**
 - Outcome of decision-making under condition of gains and loses is not symmetrical
 - Decision appears to be irrational
 - When we are in positive domain – **risk averse**
 - When we are in negative domain – **risk seekers**

Prospect theory and marketing implication

- How and advertising message is framed
- How a new product is positioned
- How a new product is priced relative to the competitors and consumers expectations
- How a product is priced and the premium a consumer is willing to pay
- What markets will respond to what types of offer

Reference point (area of acceptance)

Gains and losses are valued from subjective reference point

Displeasure associated with loss is **greater** than the pleasure associated with the same amount of gains

Pleasure = value (in our case)

