Economic Theory of Choice and the Preference Reversal Phenomenon: Reply

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We feel the contribution of Werner Pommerehne, Friedrich Schneider, and Peter Zweifel's (hereafter P-S-Z) comment is somewhat obscured by the wording of the conclusions. The following summary is offered.

1) The preference reversal phenomenon was observed by P-S-Z under substantially different conditions than those studied in our earlier paper (G-P). The subject pools differed. The experiments differed. The language differed, so naturally the questions were "framed" differently. Substantially different motivation conditions were imposed. Nevertheless, the phenomenon was there.

P-S-Z did observe lower rates than G-P, but a claim that this was due to a higher incentive structure seems a bit premature. Since P-S-Z did not conduct a control with the G-P incentives, any of the above variables could account for the differences. Furthermore, the P-S-Z payment scheme is different from G-P but it is not obvious that the incentives were greater.

2) An increase in the potential payoff for a "win" sufficient to give it a higher expected value while leaving other variables the same did not substantially reduce the reversals of those who chose the P bet.

3) Replication of the experience does not reduce the frequency of reversals by those who chose a P bet.

4) Access to records of previous decisions does not change the rate of reversals.

5) Experience and records can change behavior but the reversal rate is substantially unaffected.

In their closing remarks, P-S-Z suggest a move outside the framework of the expected utility theory and reference prospect theory (see their fn. 8) as a candidate. We need to reemphasize that the phenomenon causes problems for preference theory in general, and not for just the expected utility theory. Prospect theory as a special type of preference theory cannot account for the results.

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