



Are You Suffering from the Sunk Cost Fallacy?

Why, during a hazardous snowstorm, would we avoid driving to a concert if our tickets were free, but jeopardize life and limb to attend if we had instead paid for the tickets? The risk in driving remains the same regardless of the ticket cost.

This example illustrates the "sunk cost fallacy." A sunk cost refers to any cost - money, time, emotional, effort - that has already been paid and cannot be recovered.

We are wired to feel losses more strongly than gains. As a result, we make irrational decisions based on negating the feeling of loss instead of recognizing the gains from an option that promises to give us a better future.

The Sunk Cost Fallacy plays out in many business areas.

Hiring and training- Hiring and training involves high monetary and manpower cost. The reluctance to let someone go, even when they are significantly underperforming or otherwise negatively impacting the organization, reflects the sunk cost fallacy. The belief is that the devil you know is better than the devil you don't know.

Marketing- To decide and move forward on a marketing initiative is a significant investment. When expected results don't follow, abandoning the effort is difficult. The hope is that the desired outcomes must be just around the corner.

Systems- Businesses often develop their own data or client management systems. When those systems encounter serious glitches, more time, money, and brain power are poured into improvements. The conviction is that what the business does is so unique that no commercial industry system could provide the right service.

How can the Sunk Cost Fallacy be avoided?

Learn to recognize a sunk cost problem. Do you keep having the same conversation about the same problem? Do you feel exhausted and "spent" about a certain topic? Do you keep hoping for different results without anything changing? If you answered yes, then it's time to assess a sunk cost situation and consider a new course of action.

Focus on the future, not the past. What are your business objectives? What results do you want in the future? If it seems good money is being spent after bad, cut your losses and invest for the future.

Generate alternatives. What other options exist? Assess the costs and benefits, keeping in mind the hours of time and energy spent on a failing solution. Where can these resources be redirected?

Get a second opinion. Speak to a trusted advisor who is not emotionally involved in the situation. This person will be objective and able to evaluate the situation logically.