Advertising Content when Consumers are Loss Averse*

Heiko Karle†
Université Libre de Bruxelles

Version: September 21, 2011 (first version: June 2011)

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Abstract

In this paper, we examine the product match and price advertising strategies of a single–product monopolist when consumers are expectation–based loss averse à la Koszegi and Rabin (2006) and Heidhues and Koszegi (2010). Consumers are initially uncertain about their individual match values and the price set by the monopolist but receive the monopolist's advertising signal before forming their reference point distribution in the match value and the price dimension. The advertising signal contains match value and/or price information or no information at all. Before undertaking their purchase decision, consumers become fully informed (independently of the content of the advertising signal). So, with standard consumers, the advertising signal is fully redundant, whereas, with loss–averse consumers, it is not since consumers' purchase decision depends on their expectations at the stage when their reference point is formed. We show that the monopolist can increase loss–averse consumers' willingness to pay ex post above their true valuation (attachment effect) by either engaging in low–price advertising or partial match value disclosure. For

*I am grateful to Botond Koszegi, Paul Heidhues, Martin Peitz, Michael Grubb, Jidong Zhou, Fabian Herweg, Patrick Legros, Georg Kirchsteiger, Estelle Cantillon, Johannes Spinnewijn, Claudio Karl, Malin Arve, Luca Merlino and the participants of the Mainz Workshop in Behavioral Economics in August 2011 for their valuable comments and suggestions. I gratefully acknowledge financial support from the National Bank of Belgium (Research Grant, "The Impact of Consumer Loss Aversion on the Price Elasticity of Demand").

†ECARES, SBSEM, Université Libre de Bruxelles (ULB), B-1050 Brussels, Belgium. E-mail: hkarle@ulb.ac.be.

varying levels of product complexity, we characterize the monopolist's optimal advertising strategies in this paper.

Keywords: Advertising, Loss Aversion, Reference-Dependent Utility, Information Disclosure, Behavioral Industrial Organization

JEL Classification: D83, L41, M37.