

## **Answer on Question #44213 – Economics – Microeconomics**

### **Task**

What is sunk cost? Why don't we take into account sunk cost in economic decision making? Explain it in your words.

### **Solution**

In economics and business decision-making, a sunk cost is a retrospective (past) cost that has already been incurred and cannot be recovered. Sunk costs are sometimes contrasted with prospective costs, which are future costs that may be incurred or changed if an action is taken.

The economic approach that sunk costs should not be considered when decisions are being made can lead to a situation where the sum of a number of good decisions can lead to one big disaster. This dilemma situation can be described using a game theory approach for one-player games.

The sunk cost dilemma with its sequence of good decisions should not be confused with the sunk cost fallacy, where a misconception of sunk costs can lead to bad decisions. Sunk-cost fallacy occurs when people make decisions about a current situation based on what they have previously invested in the situation. For example, spending \$100 on a concert and on the day you find that it's cold and rainy. You feel that if you don't go you would've wasted the money and the time you spent in line to get that ticket and feel obligated to follow through even if you don't want to.