

# Diminishing marginal utility implies that losses hurt more than gains

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Assume:

$$U : \mathbb{R} \rightarrow \mathbb{R} \tag{1}$$

$$U' > 0 \tag{2}$$

$$U'' < 0 \tag{3}$$

Further assume  $U$  is smooth enough that Taylor's theorem holds.

Let  $\varepsilon > 0$

By Taylor expansion with Lagrange error term,

$$U(W) = U(W_0) + U'(W_0)(W - W_0) + R(W) \tag{4}$$

$$R(W) = \frac{1}{2}U''(c)(W - c)^2, \text{ some } c \tag{5}$$

Want to show:  $U(W_0) - U(W_0 - \varepsilon) > U(W_0 + \varepsilon) - U(W_0)$

$$\iff 2U(W_0) > U(W_0 + \varepsilon) + U(W_0 - \varepsilon)$$

$$\iff 2U(W_0) > [U(W_0) + U'(W_0)(W_0 + \varepsilon - W_0) + R(W_0 + \varepsilon)] + [U(W_0) + U'(W_0)(W_0 - \varepsilon - W_0) + R(W_0 - \varepsilon)] \quad \text{by (4)}$$

$$\iff 0 > R(W_0 + \varepsilon) + R(W_0 - \varepsilon)$$

This is true, by (5), as  $U'' < 0$  by (3)  $\square$