

Does Overconfidence Affect Corporate Investment? CEO Overconfidence Measures Revisited

Ulrike Malmendier, Geoffrey Tate

First published: 08 November 2005

<https://doi.org/10.1111/j.1354-7798.2005.00302.x>

Accessibility issue? [Request accessibility update.](#)



Abstract

This article presents the growing research area of Behavioural Corporate Finance in the context of one specific example: distortions in corporate investment due to CEO overconfidence. We first review the relevant psychology and experimental evidence on overconfidence. We then summarise the results of Malmendier and Tate (2005a) on the impact of overconfidence on corporate investment. We present supplementary evidence on the relationship between CEOs' press portrayals and overconfident investment decisions. This alternative approach to measuring overconfidence, developed in Malmendier and Tate (2005b), relies on the perception of outsiders rather than the CEO's own actions. The robustness of the results across such diverse proxies jointly corroborates previous findings and suggests new avenues to measuring executive overconfidence.

References

Alicke, M. D., 'Global self-evaluation as determined by the desirability and controllability of trait adjectives', *Journal of Personality and Social Psychology*, Vol. 49, 1985, pp. 1621-30.

[Web of Science®](#) | [Google Scholar](#)

This website utilizes technologies such as cookies to enable essential site functionality, as well as for analytics, personalization, and targeted advertising. You may change your settings at any time or accept the default settings. You may close this banner to continue with only essential cookies. [Privacy Policy](#)

Manage Preferences

Accept All

Reject Non-Essential

Baker, M. and Wurgler, J., 'The equity share in new issues and aggregate stock returns', *Journal of Finance*, Vol. 55, 2000, pp. 2219-57.

[Web of Science®](#) | [Google Scholar](#)

Baker, M. and Wurgler, J., 'Market timing and capital structure', *Journal of Finance*, Vol. 57, 2002, pp. 1-32.

[PubMed](#) | [Web of Science®](#) | [Google Scholar](#)

Baker, M., Ruback, R. and Wurgler, J., 'Behavioral corporate finance: a survey', in E. Eckbo (ed.), *The Handbook of Corporate Finance: Empirical Corporate Finance*(New York: Elsevier/North Holland, forthcoming).

[Google Scholar](#)

Bazerman, M. H., *Judgment in Managerial Decision Making*, 5th ed. (Hoboken NJ: John Wiley & Sons, 2002).

[Google Scholar](#)

Becker, G., *The Economics of Discrimination*(Chicago: University of Chicago Press, 1957).

[Google Scholar](#)

Bergman, N. and Jenter, D., 'Employee sentiment and stock option compensation', *Working Paper* (MIT, 2005).

[Google Scholar](#)

Camerer, C. and Lovallo, D., 'Overconfidence and excess entry: an experimental approach', *American Economic Review*, Vol. 89, no. 1, 1999, pp. 306-18.

[Web of Science®](#) | [Google Scholar](#)

Camerer, C. and Malmendier, U., 'Behavioral economics of organizations', in P. Diamond and H. Vartiainen(eds), *Economic Institutions and Behavioral Economics*, (Princeton NJ: Princeton University Press, Yrjö

This website utilizes technologies such as cookies to enable essential site functionality, as well as for analytics, personalization, and targeted advertising. You may change your settings at any time or accept the default settings. You may close this banner to continue with only essential cookies. [Privacy Policy](#)

Manage Preferences

Accept All

Reject Non-Essential

Cooper, A. C., Woo, C. Y. and Dunkelberg, W. C., 'Entrepreneurs' perceived chances for success', *Journal of Business Venturing* Vol. 3, 1988, pp. 97-108.

[Web of Science®](#) | [Google Scholar](#)

DellaVigna, S. and Malmendier, U., 'Contract design and self-control: theory and evidence', *Quarterly Journal of Economics*, Vol. 119, no. 2, 2004, pp. 353-402.

[Web of Science®](#) | [Google Scholar](#)

Feather, N. T. and Simon, J. G., 'Attribution of responsibility and valence of outcome in relation to initial confidence and success and failure of self and other', *Journal of Personality & Social Psychology*, Vol. 18, no. 2, 1971, pp. 173-88.

[Web of Science®](#) | [Google Scholar](#)

Fischhoff, B., Slovic, P. and Lichtenstein, S., 'Knowing with certainty', *Journal of Experimental Psychology: Human Perception and Performance*, Vol. 3, 1977, pp. 552-64.

[Web of Science®](#) | [Google Scholar](#)

Gabaix, X. and Laibson, D., 'Shrouded attributes, consumer myopia, and information suppression in competitive markets', *Working Paper* (MIT, 2005).

[Google Scholar](#)

Gervais, S., Heaton, J. B. and Odean, T., 'Overconfidence, investment policy and stock options', *Working Paper* (Duke University, 2003).

[Google Scholar](#)

Goel, A. M. and Thakor, A., 'Rationality, overconfidence and leadership', *Working Paper* No. 00-022 (University of Michigan Business School Faculty, 2000).

[Google Scholar](#)

This website utilizes technologies such as cookies to enable essential site functionality, as well as for analytics, personalization, and targeted advertising. You may change your settings at any time or accept the default settings. You may close this banner to continue with only essential cookies. [Privacy Policy](#)

Manage Preferences

Accept All

Reject Non-Essential

Hall, B. and Murphy, K. J., 'Stock options for undiversified executives', *Journal of Accounting and Economics*, Vol. 33, 2002, pp. 3-42.

[Web of Science®](#) | [Google Scholar](#)

Heaton, J. B., 'Managerial optimism and corporate finance', *Financial Management*, Vol. 31, 2002, pp. 33-45.

[Web of Science®](#) | [Google Scholar](#)

Hey, J. D., 'The economics of optimism and pessimism', *Kyklos*, Vol. 37, no. 2, 1984, pp. 181-205.

[Web of Science®](#) | [Google Scholar](#)

Kruger, J., 'Lake Wobegon be gone! The 'below-average effect' and the egocentric nature of comparative ability judgments', *Journal of Personality and Social Psychology*, Vol. 77, no. 2, 1999, pp. 221-32.

[CAS](#) | [PubMed](#) | [Web of Science®](#) | [Google Scholar](#)

Kunda, Z., 'Motivated inference: self-serving generation and evaluation of causal theories', *Journal of Personality and Social Psychology*, Vol. 53, 1987, pp. 636-47.

[Web of Science®](#) | [Google Scholar](#)

Landier, A. and Thesmar, D., 'Entrepreneurial optimism and financial contracting', *Working Paper* (NYU, 2004).

[Google Scholar](#)

Langer, E. J., 'The illusion of control', *Journal of Personality and Social Psychology*, Vol. 32, 1975, pp. 311-28.

[CAS](#) | [Web of Science®](#) | [Google Scholar](#)

Larwood, L. and Whittaker, W., 'Managerial myopia: self-serving biases in organizational planning', *Journal of Applied Psychology*, Vol. 62, 1977, pp. 194-98.

This website utilizes technologies such as cookies to enable essential site functionality, as well as for analytics, personalization, and targeted advertising. You may change your settings at any time or accept the default settings. You may close this banner to continue with only essential cookies. [Privacy Policy](#)

Manage Preferences

Accept All

Reject Non-Essential

Malmendier, U. and Tate, G., 'Who makes acquisitions? CEO overconfidence and the market's reaction', *Working Paper* (Stanford University, 2005b).

[Google Scholar](#) 

Malmendier, U., Tate, G. and Yan, J., 'Corporate financial policies with overconfident CEOs', *Working Paper*, (Stanford University, 2005).

[Google Scholar](#) 

March, J. and Shapira, Z., 'Managerial perspectives on risk and risk taking', *Management Science*, Vol. **33**, no. 11, 1987, pp. 1404-19.

[Web of Science®](#)  | [Google Scholar](#) 

Milburn, M. A., 'Sources of bias in the prediction of future events', *Organizational Behavior and Human Performance*, Vol. **21**, 1978, pp. 17-26.

[Web of Science®](#)  | [Google Scholar](#) 

Miller, D. T. and Ross, M., 'Self-serving biases in the attribution of causality: fact or fiction?' *Psychological Bulletin*, Vol. **82**, no. 2, 1975, pp. 213-25.

[Web of Science®](#)  | [Google Scholar](#) 

Moore, P. G., 'The manager's struggle with uncertainty', *Journal of The Royal Statistical Society Series A*, Vol. **149**, 1977, pp. 129-65.

[Web of Science®](#)  | [Google Scholar](#) 

Moore, D. A. and Kim, T. G., 'Myopic social prediction and the solo comparison effect', *Journal of Personality and Social Psychology*, Vol. **85**, no. 6, 2003, pp. 1121-35.

[PubMed](#)  | [Web of Science®](#)  | [Google Scholar](#) 

This website utilizes technologies such as cookies to enable essential site functionality, as well as for analytics, personalization, and targeted advertising. You may change your settings at any time or accept the default settings. You may close this banner to continue with only essential cookies. [Privacy Policy](#)

Manage Preferences

Accept All

Reject Non-Essential

Roll, R., 'The hubris hypothesis of corporate takeovers', *Journal of Business*, Vol. 59, no. 2, 1986, pp. 197-217.

[Web of Science®](#) [Google Scholar](#)

Shyam-Sunder, L. and Myers, S. C., 'Testing static tradeoff against pecking order models of capital structure', *Journal of Financial Economics*, Vol. 51, 1999, pp. 219-44.

[Web of Science®](#) [Google Scholar](#)

Stigler, G. J., 'The economies of scale', *Journal of Law and Economics*, Vol. 1, 1958, pp. 54-71.

[Web of Science®](#) [Google Scholar](#)

Svenson, O., 'Are we all less risky and more skillful than our fellow drivers?' *Acta Psychologica*, Vol. 47, 1981, pp. 143-48.

[Web of Science®](#) [Google Scholar](#)

Van den Steen, E., 'Organizational beliefs and managerial vision', *Journal of Law, Economics, and Organization*, Vol. 21, no. 1, Spring 2005, pp. 256-83.

[Web of Science®](#) [Google Scholar](#)

Weinstein, N. D., 'Unrealistic optimism about future life events', *Journal of Personality and Social Psychology*, Vol. 39, 1980, pp. 806-20.

[Web of Science®](#) [Google Scholar](#)

Weinstein, N. D. and Klein, W. M., 'Resistance of personal risk perceptions to debiasing interventions', in T. Gilovich, D. Griffin and D. Kahneman (eds), *Heuristics and Biases: the Psychology of Intuitive Judgment*(Cambridge: Cambridge University Press, 2002, pp. 313-23.

[Google Scholar](#)

This website utilizes technologies such as cookies to enable essential site functionality, as well as for analytics, personalization, and targeted advertising. You may change your settings at any time or accept the default settings. You may close this banner to continue with only essential cookies. [Privacy Policy](#)

Manage Preferences

Accept All

Reject Non-Essential

ABOUT WILEY ONLINE LIBRARY

[Privacy Policy](#)

[Terms of Use](#)

[About Cookies](#)

[Manage Cookies](#)

[Accessibility](#)

[Wiley Research DE&I Statement and Publishing Policies](#)

HELP & SUPPORT

[Contact Us](#)

[Training and Support](#)

[DMCA & Reporting Piracy](#)

[Sitemap](#)

OPPORTUNITIES

[Subscription Agents](#)

[Advertisers & Corporate Partners](#)

CONNECT WITH WILEY

[The Wiley Network](#)

[Wiley Press Room](#)

Copyright © 1999-2026 John Wiley & Sons, Inc or related companies. All rights reserved, including rights for text and data mining and training of artificial intelligence technologies or similar technologies.

WILEY

This website utilizes technologies such as cookies to enable essential site functionality, as well as for analytics, personalization, and targeted advertising. You may change your settings at any time or accept the default settings. You may close this banner to continue with only essential cookies. [Privacy Policy](#)



[Manage Preferences](#)

[Accept All](#)

[Reject Non-Essential](#)