The Cultural Origin of Preferences: CEO Cultural Heritage and Corporate Investment

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Abstract

Does culture shape risk preferences? While economic models of the origins of preferences point to an important role of culture, supporting empirical evidence is largely missing for risk and time preferences. In this study, we exploit variation in cultural heritage across CEOs of public U.S. companies and demonstrate an important effect of CEOs' culturally transmitted risk preferences on corporate physical investment. CEOs' tolerance for uncertainty negatively affects corporate investment, and the effect is larger for acquisitions than for capital expenditures (Capx). Our finding is robust to controlling for economic and institutional differences as well as genetic differences across countries of origin, and it does not depend on first-generation immigrant CEOs. CEOs' risk preferences seem to have a causal influence on riskier and more discretionary corporate decisions such as acquisitions. But the association between CEO risk preferences and more routine investment decisions such as Capx is largely explained by firm-CEO matching. Our results provide novel evidence of important social transmission of risk preferences, their effect on corporate investment policies, and the interplay of the culturally transmitted preferences of CEOs, corporate boards, and other top executives.

JEL classification:
Key words: Culture, corporate culture, risk preferences, corporate investment, CEOs

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