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## Narcissism and stock market investing: Correlates and consequences of cocksure investing

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### ABSTRACT

Two studies tested whether narcissists are prone to making risky stock market investments. In Study 1, narcissistic participants reported being more inclined to invest in stocks that exhibited high volatility (i.e., large price fluctuations). In study 2, participants created hypothetical investment portfolios using a selection of real stocks whose values were tracked for a five-week period. Narcissists selected more highly volatile stocks for their portfolios and this tendency was explained by narcissists' heightened approach motivation. Narcissists also lost significantly more money during the tracking period—the stock market as a whole declined by approximately 30% during the tracking period—and this was fully explained by the heightened volatility of their investments. Cumulatively, these results suggest that narcissistic personality is linked to risky stock market investing, which is especially maladaptive during periods of economic decline.

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### 1. Introduction

The global economy is in the midst of its worst decline since the Great Depression. The causes of this financial calamity are varied and complex, although many commentators speculate that cocksure investors and corporate leaders played a significant role by making risky and often foolhardy financial decisions (e.g., Cohan, 2009; Gladwell, 2009). What fueled this cocksureness? During the 1990s and early 2000s, the economy experienced one of the most prominent bull markets in history. Investors were positive about the future and confident that their investments would pay off. For instance, when surveyed in October 2007, more than three-quarters of individual and institutional investors predicted that the US stock market would rise during the next year (Shiller, 2000, 2009). These investors were clearly overconfident because the stock market ultimately plunged by nearly 40%.

Economic climate played an important role in investor exuberance and overconfidence. However, the level of risk that investors bore is probably not fully explained by situational factors alone. Consider that during even the historic bull markets of the 1990s and early 2000s, most investors did not utilize risky financial instruments, such as derivatives. Most families purchased homes within their means. Most corporations' investments were not

leveraged to the point that even a small fraction of losses would be ruinous. The economic situation was not so powerful that everyone simply got swept up by a tsunami of financial risk-taking. Flagrant financial risk-taking was prevalent during this time period, but it was limited to a proportion of investors. The purpose of the present research was to examine one characteristic, narcissistic personality, that we think might distinguish these risky investors from the general investor population.

Narcissism is particularly relevant to the current economic crisis. Narcissists<sup>1</sup> are more likely than others to rise to leadership positions (Brunell et al., 2008). Thus, the financial decisions that narcissists make affect greater numbers of individuals (e.g., employees, investors, tax-payers). Although we cannot say for certain how many corporate leadership positions were/are occupied by narcissists, anecdotal evidence suggests that narcissists are overrepresented in this population. To the extent that corporate leaders of the recent past were more narcissistic than the general population, and if narcissism is indeed linked to financial risk-taking, then narcissism might have played a role in the economic meltdown.

<sup>1</sup> We use the term "narcissist" as a matter of convenience to refer to individuals who score above the mean on measures of narcissistic personality. In actuality, most narcissism measures, such as the *Narcissistic Personality Inventory* (NPI), do not capture a specific group of "narcissists" (Foster & Campbell, 2007). Furthermore, the NPI—the measure used in the present studies—is not a measure of clinical narcissism and thus "narcissists" in this context should not be confused with individuals with Narcissistic Personality Disorder.

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Why would narcissists be expected to make risky financial decisions? Financial decisions are often preceded by an assessment of risk (i.e., potential financial losses) and reward (i.e., potential financial gains). Individuals who are more strongly motivated by reward (i.e., highly approach motivated) than punishment (i.e., weakly avoidance motivated) tend to make riskier financial decisions (e.g., Hamilton & Biehal, 2005; Zhou, Pham, Mick, Iacobucci, & Huber, 2004). Recent research suggests that narcissism is characterized by strong approach motivation and weak avoidance motivation (Foster, Misra, & Reidy, 2010; Foster, Shenese, & Goff, 2010; Foster & Trimm, 2008). That is, narcissists are more strongly motivated by reward acquisition than punishment avoidance. Thus, narcissists should be expected to make riskier financial decisions. Evidence supporting this hypothesis comes from studies showing that narcissists engage more frequently in risky financial activities, such as gambling (Lakey, Rose, Campbell, & Goodie, 2008). More directly, Foster, Misra et al. (2010) showed that narcissists are more likely to endorse financial investment strategies that couple high risk with high reward potential (e.g., investing in stocks rather than bonds).

The purpose of the present study was to test whether narcissism predicts financial risk-taking within the specific context of stock market investing. We hypothesized that narcissism would predict a tendency to invest in riskier stocks, with “risky” being defined in terms of a stock’s volatility. Stock volatility—i.e., how much a stock’s value (i.e., price per share) fluctuates relative to other stocks—is a useful metric of stock riskiness for a couple of reasons. Practically speaking, there exist well-established measures of stock volatility. One of these measures is the economic indicator  $\beta$  (used in Study 2), which indicates how much a single stock’s value fluctuates relative to a market indicator, such as the S&P 500 or FTSE. In terms of validity, highly volatile stocks are indeed risky investments. Put simply, highly volatile stocks are riskier than average stocks because their price valleys are deeper. However, they are also more potentially rewarding because their price peaks are higher.

Because narcissists are more strongly motivated by reward than punishment, they should make investment decisions that maximize reward potential even at the cost of heightened risk exposure. In other words, highly volatile stocks should be particularly attractive to narcissists. If our hypothesis is correct, then narcissism should be an adaptive personality trait during economic bull markets and a maladaptive trait during economic bear markets. This is because volatility correlates positively with price during bull markets (i.e., when most stocks’ values are rising) and negatively with price during bear markets (i.e., when most stocks’ values are falling). Therefore, investing in more volatile stocks will generally result in greater profits during bull markets and greater losses during bear markets.

In this article, we present findings from two studies that test the link between narcissism and risky stock market investing. In Study 1, participants were asked to select which stock they would rather invest money into from amongst four hypothetical stocks depicted by plots showing varying degrees of volatility. In Study 2, participants created hypothetical investment portfolios using actual stocks and performance indicators, including  $\beta$ . In both studies, narcissistic participants were expected to be attracted to highly volatile stocks. Specifically, narcissistic participants were expected to select stocks depicted in plots showing high volatility (Study 1) and create investment portfolios more heavily populated with highly volatile stocks (Study 2). Finally, the investment portfolios created in Study 2 were tracked for five weeks to determine whether narcissism predicts investment performance. By chance, the US stock market experienced a historic collapse during this tracking period, which allowed us to examine how investments by narcissists perform during strong economic declines (i.e., a bear market).

## 2. Study 1

In this study, we conducted an initial test of the link between narcissism and risky stock market investing. We hypothesized that narcissists would be prone to making hypothetical investments into stocks that displayed higher levels of volatility (i.e., stocks with more severe price fluctuations).

### 2.1. Method

#### 2.1.1. Participants and procedure

A sample of 237 University of South Alabama undergraduates ( $M$  age = 20.93; 56% female) completed measures of narcissism and stock volatility preference.

**2.1.1.1. Narcissism.** Narcissism was measured with the 40-item *Narcissistic Personality Inventory* (NPI; Raskin & Terry, 1988). NPI scores for the present sample ranged from one to 39 ( $M = 17.74$ ,  $SD = 7.54$ ,  $\alpha = .87$ ) with higher scores indicating higher levels of narcissistic personality.

**2.1.1.2. Stock volatility preference.** Participants were presented with four hypothetical stocks that differed in terms of volatility and asked to select the one that they would most want to invest their money. Volatility was depicted graphically as the amount each stock’s price fluctuated during the previous 1000 stock market closings (see Appendix A for actual plots used in study). To create these plots, times series data for 1000 time points were simulated such that the value for each successive time point differed from that of the previous time point by a random integer between  $-3$  and  $+3$ . Time point #1 was designated as the present time and was set at 100 (i.e., the price of the stock at the most recent close of the stock market was set at \$100). Therefore the price for time point #2 could range from 97 to 103, the price for time point #3 could range from 94 to 106 (the actual price depended, of course, on what the price for time point #2 was), and so forth all of the way to time point #1000. These prices were then plotted with the Y-axis designated as the stock’s closing price and the X-axis designated as time. Time points were reversed before plotting so that time point #1 appeared at the far right end of the X-axis. This ensured that the most recent closing price of the stock was fixed at \$100. This simulation was repeated until a plot with adequate visual appeal (e.g., appeared to show relatively consistent price fluctuations across the time series) emerged. We term this plot and data set the *standard time series*.

Next, to create the four plots used in the study, a plot representing very low volatility was created by multiplying by 0.5 the range with which the prices for each time point in the standard time series were allowed to differ (i.e., the range was changed from  $\pm 3$  to  $\pm 1.5$ ). In other words, we created a new time series plot that displayed one-half the daily fluctuation displayed in the standard time series plot. To create the second, third, and fourth plots, we used multipliers of 2.0, 3.5, and 5.0, respectively. In sum, we created four time series plots that displayed between one-half and five times the volatility displayed in the standard time series plot. For quantitative purposes, we use the numbers 1–4 to represent these plots with higher numbers representing plots reflecting higher volatility. Participants were asked to select from amongst these four plots ( $M = 2.39$ ,  $SD = .99$ ).

## 3. Results and discussion

As hypothesized, narcissism positively predicted the selection of stocks represented by plots depicting greater price volatility,  $r = .13$ ,  $p < .05$ ,  $R^2 = .02$ . Put differently, participants who selected

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