

## Accepted Manuscript

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PII: S0929-1199(17)30003-2  
DOI: doi: [10.1016/j.jcorpfin.2017.01.002](https://doi.org/10.1016/j.jcorpfin.2017.01.002)  
Reference: CORFIN 1142

To appear in: *Journal of Corporate Finance*

Received date: 12 January 2016  
Revised date: 18 December 2016  
Accepted date: 3 January 2017



Please cite this article as: Pikulina, Elena, Renneboog, Luc, Tobler, Philippe N., Overconfidence and investment: An experimental approach, *Journal of Corporate Finance* (2017), doi: [10.1016/j.jcorpfin.2017.01.002](https://doi.org/10.1016/j.jcorpfin.2017.01.002)

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## Overconfidence and Investment: An Experimental Approach\*

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A positive relation between overconfidence and investment provision has been theoretically justified and practically assumed in the literature, but has not been thoroughly investigated. We test and confirm this positive relation between direct measures of overconfidence in one's financial knowledge and choice of investment. More precisely, strong overconfidence results in excess investment, underconfidence induces underinvestment, whereas moderate overconfidence leads to accurate investments. Our experimental results are based on different subject pools, financial professionals and students, and different media: computer-, paper-, and web-based. The degree of one's overestimation of one's individual financial knowledge relative to one's actual knowledge as well as relative to the knowledge of peers explains investment decisions better than one's actual knowledge. The relation between overconfidence and investment is robust to the degree of individual risk aversion, the riskiness of the investment projects, and to the changes in incentives structure.

*JEL Classification* G11, J22

*Keywords:* Overconfidence, Better-That-Average, Bias, Investment, Risk Aversion, Professionals

\* *Acknowledgments:* We are grateful to Elena Asparouhova, Peter Bossaerts, Fabio Braggion, Evy Bruyland, Colin Camerer, Eddy Cardinaels, Peter Cziraki, Frank de Jong, Marc Deloof, Joost Driessen, Rik Frehen, Peter de Goeij, Holger Herz, Jooa Julia Lee, Hao Liang, Alberto Manconi, Charles Noussair, Charles Plott, Kirill Pogorelsky, Jan Potters, Anne-Francoise Rutkowski, Oliver Spalt, and Stefan Trautmann for useful comments and suggestions. We also acknowledge the contribution of the participants in TIBER XI at Tilburg University (2012), Florence Workshop on Behavioral and Experimental Economics (2013), Experimental Finance Conference (Tilburg 2013) and seminar presentations at Caltech and Tilburg University. All remaining errors are our own. We gratefully acknowledge financial support from the CentER Fund for Experimental Research, the AXA foundation (Elena Pikulina), Inquire Europe (Luc Renneboog), and the Swiss National Science Foundation (Philippe Tobler).

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