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LIVING FOREVER: ENTREPRENEURIAL OVERCONFIDENCE AND SUBJECTIVE LIFE EXPECTANCY (SUMMARY)

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≈ SUMMARY ≈

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Principal Topic

The high failure rates of business start-ups and low average returns of self-employment suggest that too many people become entrepreneurs. Part of this excess market entry is thought to result from overconfidence in future entrepreneurial success: it is argued that entrepreneurs are more prone to overconfidence than wage-workers. Establishing overconfidence as a driver of entrepreneurial activity using field data is challenging because statements about the relative level of overconfidence among entrepreneurs versus non-entrepreneurs ideally require representative population samples, and the direction of causality between occupational choice and self-perception is difficult to determine.

Method

We present a method for tackling the identification problems by using a population-based panel dataset that allows for the construction of an objective overconfidence measure by comparing subjective expectations of life duration and observed life spans. Beliefs about life expectancy are not likely to be a consequence of entrepreneurial behavior because learning-by-doing, self-justification of occupational choices and job-related information are domain-specific and unlikely to have a direct influence on life expectancy. Specifically, we test whether entrepreneurs are more prone to exhibit overconfidence in relation to life expectancy than non-entrepreneurs. Furthermore, we use the panel structure of our data to directly test for potential reverse causality, exploiting the fact that the time spent in entrepreneurial activities would be positively correlated with overconfidence if overconfidence were the result of occupational choice.

Results and Implications

Our results show that both entrepreneurs and non-entrepreneurs exhibit overconfidence in terms of life expectancy. However, controlling for real life spans, we find that entrepreneurs are significantly more overconfident than non-entrepreneurs. We provide evidence that entrepreneurial status rather than the time spent in entrepreneurial activities explains the observed difference in overconfidence. This result provides evidence for a self-selection effect of overconfident individuals into entrepreneurship. Our study design represents a novel approach to overcoming the methodological shortcomings that are typical among field studies on entrepreneurial overconfidence. The observation that overconfidence in a non-economic domain relates to entrepreneurial behavior implies that overconfidence is, to some extent, a personality-specific phenomenon rather than being purely situation- or domain-specific. This contributes towards our understanding of the origins of overconfidence.

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