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The Societal Costs of CEO Overconfidence

The higher a CEO's self-opinion, the less he or she can see the long-term value of corporate social responsibility.

Corporate Social Responsibility (CSR) often loses out when it comes to resource allocation, since it's far from guaranteed to generate high quarterly returns for shareholders. Yet many top firms apparently sense that CSR holds some value for them over the long term—why else would Fortune 500 companies in the U.S. and UK alone **spend more than $15 billion on it** annually? Altruism doesn't wholly explain numbers like these.

Among other tangible benefits, CSR initiatives when done properly can help companies solidify relationships with key stakeholders, creating moral and emotional capital that can be cashed in later. For example, a company that has helped build a school in an impoverished community may meet less resistance if it attempts to place a potentially noisy factory in that community later on.

Consequently, the depth of a firm's commitment to CSR largely depends on management's ability to foresee situations down the line where stakeholder cooperation might be necessary, regardless of the firm's short-term prospects. This particular competency has more to do with personality than with core business skills. Research shows that this is one of the blind spots common to hubristic or overconfident personalities. As a result, firms led by overconfident CEOs tend to shortchange CSR participation.

Measuring CEO hubris

My paper "**How CEO Hubris Affects Corporate Social (Ir)responsibility**" (co-authored by Yi Tang of Hong Kong Polytechnic University, Cuili Qian of City University of Hong Kong, and Rui Shen of Nanyang Technological University), recently published in *Strategic Management Journal*, compares CEOs' level of hubris with their companies' history of CSR activity, or inactivity as the case may be. (For the purposes of this paper, we use "hubris" to mean an overly positive self-image that leads a CEO to underestimate his or her dependence on factors outside the self.)

Specifically, we looked at media coverage of 464 unique CEOs and noted how often words such as "confident", "overconfident", "optimistic" or "optimism" were used to describe them, as opposed to words suggesting the opposite, e.g. "reliable", "cautious", "conservative", and "practical". Based on this, we were able to calculate a "hubris score" for each CEO, which we compared to CSR ratings information for his or her company, as provided by leading agency Kinder, Lydenberg, Domini and Co. (KLD). The results showed that all things being equal, CEO hubris leads to a lower level of company participation in socially responsible activities and a higher level of participation in socially *ir*responsible ones.

Mitigating factors

The link between CEO hubris and CSR activity isn't impervious to context, however. When we accounted for firm size, cash flow, market competitiveness, and market uncertainty, we saw that the link became more or less important depending on whether the firm's situation was stable enough in the short term to support the CEO's sense of invulnerability. If a hubristic CEO is steering a mighty ship through relatively calm waters, chances are he or she will be complacent and engage less in CSR activities. In a more challenging business climate, hubris matters less in influencing CSR activities.

The perils of CEO hubris

We hypothesised that hubristic CEOs are more likely to attribute their firm's success entirely to their own abilities rather than to a combination of forces that are possibly subject to change. In other words, they think they're the reason the seas are calm. (You can see why in Greek tragedy, hubris provokes the wrath of the gods.) Hubristic CEOs think that as long as they're at the helm, things can't help but continue as they are, so why bother sinking resources into CSR? This optimism can be dangerous because it ignores all the other key stakeholders on whom the ultimate fate of the business depends.

When the going gets tough—e.g. a market sector becomes more competitive—and there are immediate difficulties to handle, delusions of grandeur are harder to sustain. Even the most prideful leaders remember they're dependent on others for their success, and that they can't see what's beyond the horizon. It is at this point that they swallow their pride and try to shore up their stakeholder relationships by launching CSR initiatives.

Narcissism vs. hubris

Here, we ought to make a distinction between *CEO hubris* and *CEO narcissism*. They are related concepts with very different implications for CSR participation. While hubristic CEOs, as we've seen, regard others' opinions and feelings as unimportant, narcissistic CEOs crave external validation. For that reason, narcissistic leaders are more likely to embrace CSR so they can receive the positive publicity that comes with it. Of course, this isn't necessarily an improvement, as CSR initiatives undertaken for self-glorification don't always end up benefiting the firm.

It should not surprise anyone that many CEOs are overconfident. Making it to the very top of the corporate ladder requires excessive self-belief at times. Plus, a charismatic leader's hubris can be contagious, so that others come to see him or her as a corporate saviour who can do no wrong. Our paper contributes to a **growing body of research** that cautions against this phenomenon by pointing out the negative effects of unchecked CEO hubris for companies. If investors and company directors fail to provide an effective counterweight to CEO hubris, firms are likely to be ill-prepared should a reversal of fortune be lurking in their future.

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