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# Prosociality and Risk Preferences in the Financial Sector

Max Deter

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# Prosociality and Risk Preferences in the Financial Sector

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## Abstract

Using large-scale data from the German Socio-Economic Panel (SOEP), this paper finds that financial professionals have a lower prosociality and riskier behavior than a control group. I interpret these findings using the person-organization fit theory, and thus, the compatibility between the employee's personality and the prevailing culture in their organization. The financial sector attracts riskier individuals, but professionals *become* less prosocial in the sector. These attitudes are associated with behavioral consequences, and are mainly driven by male professionals in lower management.

**Keywords:** prosocial motivation; risk; financial sector; selection; socialization

**JEL Codes:** D64, D81, D53, D90, M5

**Compliance with Ethical Standards:** This article does not contain any studies with human participants or animals performed by any of the authors.

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# 1 Introduction

Throughout history, banking was often perceived as a rent-seeking and unethical activity. The prohibition of interest rates goes back to the Old Testament (Exodus 22:24). Although, the financial sector plays a crucial role for the economy by managing risks (Froot, Scharfstein, & Stein, 1993), providing price signals (Hayek, 1945), and promoting economic opportunities (Levine, 2005), the sector is perceived as highly selfish and even dishonest (Ashraf & Bandiera, 2017). Many financial activities are associated with higher private than (perceived) social returns (Zingales, 2015). Currently, lawsuits against banks are peaking and concern the causes of the global financial crisis 2007-08, the libor manipulation, the enabling of tax evasion and money laundering, and the cum-ex scandal. In the United Kingdom, banks had to pay \$56bn in fines between 2011 and 2014, which equals more than 60 percent of their profits during this time (The Economist, 2014). A large amount of the blame for what goes wrong in the financial sector has been attached to a “failure of professionalism and ethics”, to quote the British Parliamentary Commission on Banking Standards (PCBS) (The Economist, 2016).

However, empirical evidence on a risky and less prosocial financial sector is relatively scarce. Monetary experiments show that economic students behave more selfishly and greedier than the average student (Frey & Meier, 2003; Wang, Malhotra, & Murnighan, 2011). Professional bankers are more dishonest when their professional identity is rendered salient (Cohn, Fehr, & Maréchal, 2014), but *less* risk-loving (Cohn, Fehr, & Maréchal, 2017). This suggests that a problem with the business norm concerning ethics exists, but not concerning risk. Cross-sectional data from the European Social Survey, however, reveal only negligible lower prosocial values of financial employees (Van Hoorn, 2015, 2017).

The present study analyzes prosocial and risk preferences as well as actual behavioral consequences in large-scale panel data, and is therefore able to answer the question whether differences stem from a selection of individuals or a socialization during their employment.

It is based on the person-organization fit theory of O'Reilly, Chatman, & Caldwell (1991), thus, the compatibility between the employee's traits (personality, preferences) and the organizational culture. Although financial companies are not all the same, the industry shares similar norms and faces the same market conditions, regulatory constraints, and stakeholder expectations (Gordon, 1991). The hypothesis here is that recent scandals occurred, because the financial sector has a problem with its business ethic, thus, individual preferences concerning prosociality and risk are different, potentially because competitive risk behavior is enhanced by norms and (monetary) incentive schemes in the banking sector.

Regressions reveal that prosocial attitudes of financial professionals are lower, and financial risk preference increases the probability of working in the financial sector. These results are mainly driven by male professionals in middle management and not managers with many subordinates. While a higher risk preference is already present before the start of financial employment, prosociality decreases with increasing time in finance. Moreover, differences in preferences are associated with actual behavioral consequences, this is, civic involvement and risky investments. The results are important since they indicate a business norm that attracts and socializes professionals who think and behave in a riskier and less prosocial manner. This confirms that a cultural change in the financial industry might be a complementary measure on which governments can focus.

The paper is set up as follows. Section 2 discusses data and measures. Section 3 presents the results. Finally, Section 4 concludes.

## **2 Data and Variable Measurement**

### **2.1 Sample Selection**

In the empirical analysis, I use unbalanced data from the 1984-2017 German Socio-Economic Panel (SOEP), an annual panel survey, as representative of the resident German population (Goebel et al., 2019). The financial sector in the analysis includes financial services

Table 1: Descriptive Statistics, Averages

	Financial Sector	Other Sectors
Age of Individual	43.85	44.47
Female	0.27	0.31
Having a Partner	0.83	0.82
German Nationality	0.95	0.96
College Degree	0.60	0.56
Log HH Income	6.38	6.21
Full-Time Empl. Exp.	17.89	18.59
Part-Time Empl. Exp.	1.30	1.59
Observations	1,170	16,822

SOEP 1984-2017; only Employees

and insurance activities, except compulsory social security and the public sector (NACE classification: 65, 66 and 67). Financial employees in the sample only include professionals that are involved in decision-making regarding financial products, such as corporate managers, production and operations managers, and business professionals (ISCO-88 Occupation Code classification: 1-3). In the control group, professionals in the same occupations but who work in non-financial sectors are considered (see Appendix). Thus, personal characteristics between financial and non-financial employees are relatively balanced in terms of education, age, and employment experience (see Table 1). Included, furthermore, are only individuals who were full-time, part-time or self-employed. More information on the ISCO88 classification can be found on the website of the International Labour Organization, <https://www.ilo.org/public/english/bureau/stat/isco/>. This leads to a sample of 5,050 individuals with 17,992 observations.

## 2.2 Measures

The dependent variable *financial sector* captures the probability that an individual is employed in the financial sector (= 1) or not (= 0). The explanatory variables used in the analysis are the following.

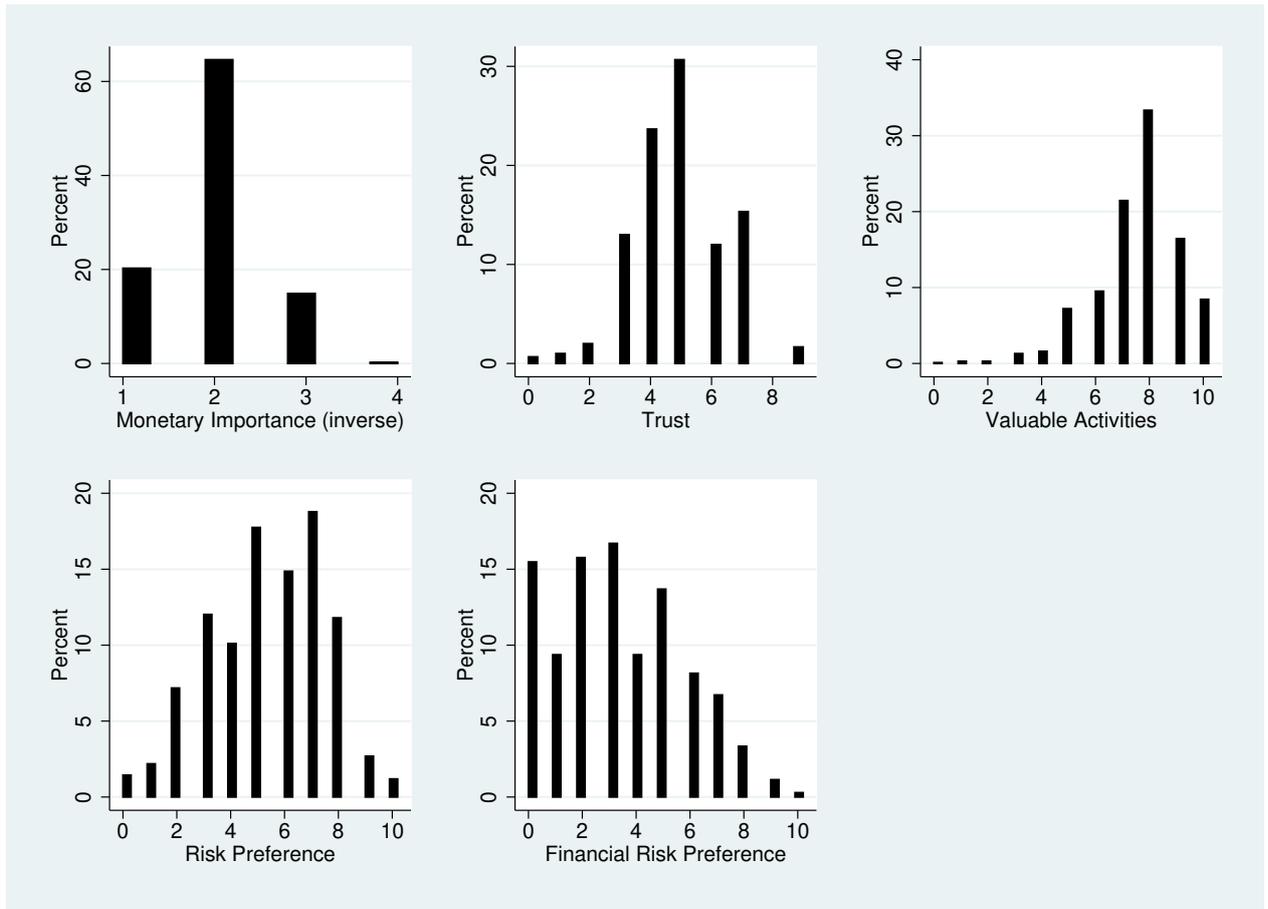
*Prosocial motivation*, as the willingness to support other people’s well-being, is an impor-

tant aspect of human personality and affects economic outcomes (for an overview, see Kosse et al. (2020)). It is captured by three variables: self-perceived prosociality is measured by the question “Do you have the feeling that what you are doing in life is useful and meaningful”, where 0 represents “not at all valuable and useful” and 10 “completely valuable and useful”. It can be argued that employees scoring lower on this variable perceive what they are doing at work (among other things) as less useful, and contributing less to society or the world as a whole. The second variable is the inverse of prosociality, monetary motivation, thus “the importance of being able to afford things”. The measure ranges from 1 (“very important”) to 4 (“not at all important”) so that higher values correspond to lower monetary importance. It can be argued that monetary motivation is the opposite of prosocial motivation (holding income constant) and reflects a rather selfish motivation. The third prosocial variable is trust that is measured with three items, “general trust in people”, “nowadays can’t trust anyone” and “caution with strangers” on a scale of 0-3, respectively, where 0 means “totally agree” and 3 “totally disagree”. For the second and the third trust question, the inverse is taken so that higher values correspond to higher trust. In order to be proportional, the three variables are z-standardized (mean = 0, SE = 1) and added for every person-year observation (where available) into one variable.

*Risk Preference*, as a second explanatory variable, is an important predictor for many labor market decisions such as educational choice (Fossen & Glocker, 2017), occupational choice (Bonin et al., 2007), and migration (Jaeger et al., 2010); self-reported risk attitudes in the SOEP data are found to correlate with risky choices in incentivized lottery experiments (Dohmen et al., 2011). General risk preference is measured by asking individuals about their readiness to take risk on a scale of 0-10: “Are you generally a person who is willing to take risks or do you try to avoid taking risks?”, where 0 means “not at all willing to take risks” and 10 means “very willing to take risks”. The preference for risk regarding financial investments is measured the same way.

The distribution of prosociality and risk answers are shown in Figure 1. Following

Figure 1: Distribution of Prosociality and Risk Answers



Note: The inverse of monetary importance is considered, so that higher values correspond to lower monetary importance (4: not important at all); trust is the measure of three items (scale: 0-2), 8 is therefore non-existent

Caliendo, Fossen, & Kritikos (2014), if preferences are missing for one year, the value of an individual before (or after, if values before are missing as well) is inserted if the individual has not changed their status away from either being a financial employee or being in the control group. This is reasonable as personality traits and preferences are shown to be relatively stable over time (Cobb-Clark & Schurer, 2012).

Although using risk and prosocial attitudes as a proxy for behavior is justified, as they are proven to correlate with it (Booth & Nolen, 2012; Kosse et al., 2020), they are not perfectly behaviorally meaningful. Self-serving biases, i.e. attributing positive events to one's own character, or inattention can bias the results (Camerer & Hogarth, 1999). This is why actual behavioral measures are additionally taken into consideration.

*Prosocial Behavior* is measured by four different variables: blood donation, volunteer work, an individual's participation in a citizen's group, political party or local government, and his or her civic participation (previous variable) in future retirement. These groups or clubs contribute significantly to society; therefore, a participation in one of them is a reasonable proxy for prosocial behavior. If prosocial behavior is missing for one year, the value of four years after or before is considered, if an individual has not changed from the treatment to the control group.

*Risk Behavior* is measured by the question of whether the household of the surveyed individual holds risky investments such as stocks, funds, bonds or equity options. It may be logical that financial employees undertake riskier investments because they have a higher knowledge about investments. However, it could also be the case that they are more risk-averse regarding financial investments since they know that risky options can lead to high losses, for example in 2008, and financial professionals are therefore more careful in holding risky shares in the financial markets.

Even if a lower prosocial and a higher risk motivation is associated with actual behavioral consequences, the measures could still be problematic. It could be the case, that risky attitudes and risky individual behavior is only present in the private and not the professional

context; thus, individuals buy risky stocks, but not in their professional position as it is other people’s money. This possibility cannot be ruled out here. Second, *clients* could drive the risky and less prosocial decisions of bankers, and professionals’ attitudes and behavior are less meaningful, because the professionals follow instructions and profit expectations of their clients. However, it can be argued that preferences of banking professionals, such as consultants and traders, play still a crucial part in financial decision-making.

Personal controls are used to hold factors constant that bias the findings if they are correlated with the explanatory and the dependent variable. These include age, sex, having a partner, German nationality, college degree, logarithmized monthly household income, and both full-time and part-time work experience. Year and regional (federal states of Germany) fixed effects are applied as well.

## 3 Results

### 3.1 Is the Financial Sector different?

To examine whether different attitudes are related to differences in the probability to be employed in the financial sector, a probit regression is applied. The probit results are reported in Table 2. Marginal effects are estimated to show how the probability of financial employment increases if an explanatory variable increases by one unit. The explanatory variables are prosocial attitudes, risk preference, and risk preference regarding finances. Since the explanatory variables are z-standardized, the interpretation is the same as in the linear ordinary least squares model (Ayaita, Güllal, & Yang, 2018). Robust standard errors are applied to control for heteroskedasticity.

An increase in prosociality by one standard deviation, lowers the probability of working in the financial industry significantly by 0.082, which is 8.2 percent (Model 1, Table 2). Since the overall probability of working in finance is 6.5% for this sample, the decrease by 8.2 percent relates to  $(8.2/0.65) = 12.61\%$  when all controls are applied. It is important to

Table 2: Probit Model - Who sorts into the Financial Sector?

	(1)	(2)	(3)
	Finance	Finance	Finance
<b>Prosociality</b>	<b>-0.082***</b>		
	<b>(0.01)</b>		
<b>Risk Preference</b>		<b>0.018</b>	
		<b>(0.02)</b>	
<b>Financial Risk Preference</b>			<b>0.223***</b>
			<b>(0.02)</b>
Age	0.002	-0.001	0.001
	(0.00)	(0.00)	(0.00)
Female	-0.087*	-0.041	0.052
	(0.04)	(0.04)	(0.05)
Having a Partner	0.126*	0.156**	0.157*
	(0.05)	(0.05)	(0.06)
German Nationality	-0.044	-0.046	0.021
	(0.09)	(0.08)	(0.10)
College Degree	0.038	-0.002	-0.005
	(0.04)	(0.04)	(0.05)
Log HH Income	0.081***	0.115***	0.090***
	(0.02)	(0.02)	(0.02)
Full-Time Experience	-0.005	-0.004	-0.003
	(0.00)	(0.00)	(0.00)
Part-Time Experience	-0.023**	-0.022**	-0.033***
	(0.01)	(0.01)	(0.01)
Constant	-2.244***	-2.369***	-2.550***
	(0.29)	(0.29)	(0.32)
Year and Regional FE	Yes	Yes	Yes
Observations	15,785	14,301	12,715
Pseudo R <sup>2</sup>	0.047	0.035	0.066

robust SE in (); \*\*\*p<0.001, \*\*p<0.01, \*p<0.05

Table 3: Financial Sorting based on Behavior

	(1)	(2)	(3)	(4)	(5)
	Finance	Finance	Finance	Finance	Finance
<b>Blood Donations</b>	<b>0.027</b> (0.19)				
<b>Volunteering</b>		<b>-0.056</b> (0.03)			
<b>Civic Participation</b>			<b>-0.205***</b> (0.06)		
<b>Civic Participation Retirement</b>				<b>-0.363**</b> (0.13)	
<b>Holding Stocks</b>					<b>0.352***</b> (0.04)
Med. Reasons for not Donating	-0.187** (0.07)				
Working Hours	0.001 (0.00)	0.000 (0.00)	0.000 (0.00)	-0.007 (0.01)	
Holding Savings Account					-0.058 (0.04)
Adults in HH					0.032 (0.03)
Year and Regional FE	Yes	Yes	Yes	Yes	Yes
Controls	Yes	Yes	Yes	Yes	Yes
Observations	6,693	15,851	12,069	1,241	13,755
Pseudo R <sup>2</sup>	0.054	0.042	0.037	0.218	0.039

robust SE in (); \*\*\*p&lt;0.001, \*\*p&lt;0.01, \*p&lt;0.05

not here that the three prosocial variables (useful activities, monetary importance, trust) are also separately significant (not shown here), but the overall measure “Prosociality” is used for simplicity. Interestingly, a higher risk preference does not significantly increase the probability of financial sector employment (column 2), only the risk preference concerning financial investments does (column 3). Thus, financial professionals have only a higher preference for risk when financial investments are involved, but not in general. The findings of this table support the idea that prosociality is less and risk preference more common in the financial sector.

Furthermore, prosociality is significantly higher for women, but only in the financial sector (see Appendix). Financial risk preference is lower for women in both sectors. Thus, prosocial and risk differences are mainly driven by male professionals, which aligns with previous studies (Booth & Nolen, 2012). Barber & Odean (2001) showed that male financial professionals lose more money through excessive trades over the year than women. Hiring more heterogeneously could lower risk and increase prosociality as measured here.

Table 3 shows that attitude differences relate to differences in actual behavior of financial professionals. No significant differences between financial and non-financial professionals can be observed concerning blood donation (conditional on medical reasons for not donating) and volunteering (conditional on working hours). However, the probability of financial employment is lower when an individual is involved in civic activities either at the time of the survey (conditional on working hours) or sometime in future retirement. Moreover, financial employment is more likely if an individual hold stocks (risky financial investments) conditional on having a savings account and number of adults in the household.

### **3.2 Selection vs. Socialization**

Do differences stem from the selection of different individuals or from a socialization of individuals during their career? For this, individuals are sampled, who work in the next year for the first time in the financial sector or in the control group (and have not worked in the

Table 4: Probit Regression - Selection into the Financial Sector

	(1)	(2)
	$Finance_{t+1}$	$Finance_{t+1}$
<b>Prosociality</b>	<b>-0.025</b> <b>(0.04)</b>	
<b>Fin. Risk Preference</b>		<b>0.142*</b> <b>(0.06)</b>
Personal Controls	Yes	Yes
Year and Regional FE	Yes	Yes
Observations	2,007	1,545
Pseudo $R^2$	0.100	0.127

robust SE in (); \*\*\*p<0.001, \*\*p<0.01, \*p<0.05

Table 5: Fixed Effects Regression - Socialization in the Financial Sector

	(1)	(2)
	Prosociality	Fin. Risk
<b>Financial Experience (Years)</b>	<b>-0.066***</b> <b>(0.01)</b>	<b>0.002</b> <b>(0.01)</b>
Non-Financial Experience (Years)	-0.007 (0.01)	0.015*** (0.00)
Personal Controls	No	No
Year FE	Yes	Yes
Personal FE	Yes	Yes
Observations	16,912	13,707
(Within) $R^2$	0.012	0.048

robust SE in (); \*\*\*p<0.001, \*\*p<0.01, \*p<0.05

financial sector before). If professionals show differences already before starting to work in the (non-)financial sector, an attraction of individuals with different attitudes/preferences is present. The probit regressions (Table 4) show that financial risk preference, but not prosociality is already pronounced one year before. This indicates that financially riskier individuals seem to be attracted by the business norm and working conditions in the financial sector.

A further step follows Ayaita, Güral, & Yang (2018) and analyzes in an ordinal least squares regression whether an additional socialization effect of attitudes *during* the time in the financial sector occurs:

$$Prosociality_{it} = \beta_0 + \beta_1 * FinancialExperience_{it} + \beta_2 * NonFinancialExperience_{it} \quad (1)$$

where  $Prosociality_{it}$  is replaced by financial risk preference in additional regressions and  $(Non-)FinancialExperience_{it}$  is the number of years an individual has already worked at the time of the interview in the (non-)financial sector. If  $\beta_1$  is significant and the magnitude larger than  $\beta_2$ , a socialization effect is present in the financial sector. Personal fixed effects are included in this regression to control for unobserved individual heterogeneity, thus, the within-changes of individuals are analyzed.

Results in Table 5 show that financial experience (but not non-financial experience) has a negative effect on prosociality. Thus, financial professionals become less prosocial the longer they work in the sector. A negative effect of a financial business norm on prosociality might be present here and could be problematic. No significant positive effect can be observed concerning financial risk preference. These results confirm the previous table that low prosociality is rather caused by an indoctrination effect, while high risk preferences for financial investments seem to stem from a selection effect.

### 3.3 Incentives in the Financial Sector

Do prosocial and risk-averse individuals find it more difficult to succeed in the financial sector? Thus, does the incentive structure in the financial sector reward risk preference and low prosociality? This is tested by looking into the impact of preferences on the number of subordinates as a proxy for career success (Van Hoorn, 2017) in two separate regressions for the financial and the non-financial sector (see Appendix). Results reveal that prosociality actually *increases* career success in the financial sector, but not in the non-financial sector. Financial risk preference promotes career success only in the non-financial sector. In short, a lower prosociality and a higher preference for financial risk are rather driven by middle

management than by higher management. This aligns with newspapers reporting that, although the board of banks are willing to change the business culture in their companies, they find it difficult to implement it at lower levels (The Economist, 2016).

## 4 Conclusion

This paper analyzed whether financial professionals are less prosocial and more risky than the non-financial professionals. Results showed that differences in preferences are indeed present, have behavioral consequences, and are driven by middle-management professionals and a selection as well as a socialization effect. This confirms that a cultural change in the banking industry might be a complementary measure on which governments can focus. Next to hiring more women, changing the business culture could be carried out by ethical trainings towards more prosocial and risk-averse behavior, and the introduction of an equivalent to the Hippocratic Oath for medical doctors. Implementing a cultural change properly could not only benefit society as a whole, but could also help banks to avoid paying large shares of their profits for fines in the future.

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Table A: Operationalization of Main Variables

Variable	Item	Years
<b>Dependent Variable</b> Financial Sector	In which economic sector/branch of industry/service area is the company or institution that you work for? 1: Finance (NACE: 65-67), 0: Other Sectors	all
<b>Prosociality</b> Valuable Activities	“Do you have the feeling that what you are doing in life is valuable and useful?” (0-10)	2015-2017
Financial Motivation	Different things are important to different people, How important are the following things to you? Very important, important, less important or quite unimportant? - Being able to afford things for myself (1-4)	1990, 92, 95, 2004, 08, 10, 12, 16
Trust	What is your opinion on the following three statements? - People can generally be trusted (1-4) - Nowadays you can't rely on anyone (1-4) - If you are dealing with strangers, it is better to be careful before trusting them (1-4)	2003, 08, 13
<b>Risk Preference</b> General Risk	“Would you describe yourself as someone who tries to avoid risks (risk-averse) or as someone who is willing to take risks (risk-prone)?” (0-10)	2004, 06, 08 2010-17
Financial Risk	“People can behave differently in different situations. How would you rate your willingness to take risks in the following areas?” - in financial matters?	2004, 09, 14
<b>Prosocial Behavior</b> Blood Donation	Blood Donation (last 5 years)	2010, 2015
Volunteering	Volunteer work in clubs or social services	2005,07,08,09 2011,13,15,17
Civic Involvement	Involvement in a citizens' group, political party, local government	2005,07,08,09 2011,13,15,17
<b>Risk Behavior</b> Holding Stocks	Did you or another member of the household own any of the following savings or investment securities last year - Other securities (e.g., stocks, funds, bonds, equity options)	2001-17

Table B: Occupations

Current Occupation(ISCO-88 COM, 4 digits)	Finance Sector	Non-Finance
1200 Corporate Managers	25	1,248
1210 Directors and Chief Executives	53	2,718
1227 Production and Operations Managers	526	2,996
1231 Financial, Administration Dept. Manager	19	333
1233 Sales, Marketing Department Manager	49	2,521
1300 Managers of Small Enterprises	29	1,427
2121 Mathematicians, Statisticians, Rel. Professionals	22	34
2122 Statisticians	5	39
2411 Accountants	44	791
2419 Business Professionals Not Elsewhere Classified	228	3,564
2421 Lawyer	19	1,360
2429 Legal Professionals Not Elsewhere Classified	121	727
2441 Economists	36	594
3411 Securities and Finance Dealers and Brokers	100	10
3421 Trade Brokers	10	18

Table C: OLS regressions - Female Differences in the Financial Sector

	(1)	(2)
	Prosoc.	Fin. Risk
Female	0.001	-0.524***
	(0.02)	(0.02)
Financial Sector	-0.302***	0.500***
	(0.05)	(0.04)
<b>Female*Financial Sector</b>	<b>0.222*</b>	<b>-0.251**</b>
	<b>(0.09)</b>	<b>(0.09)</b>
Personal Controls	Yes	Yes
Year and Reg. FE	Yes	Yes
Observations	15,785	12,785
R <sup>2</sup>	0.038	0.094

robust SE in (); \*\*\*p<0.001, \*\*p<0.01, \*p<0.05

Table D: OLS Regression - Incentives in the Financial Sector

	(1)	(2)	(3)	(4)
	Subordinates	Subordinates	Subordinates	Subordinates
	Finance	Non-Finance	Finance	Non-Finance
<b>Prosociality</b>	<b>1.914*</b>	0.746		
	<b>(0.96)</b>	(0.65)		
<b>Financial Risk Preference</b>			<b>-1.383</b>	3.347***
			<b>(1.34)</b>	(0.99)
Personal Controls	Yes	Yes	Yes	Yes
Year and Reg. FE	Yes	Yes	Yes	Yes
Observations	934	15,846	721	12,906
(Adjusted) $R^2$	0.080	0.014	0.091	0.015

robust SE in (); \*\*\*p<0.001, \*\*p<0.01, \*p<0.05