EFFECTS OF CULTURE ON INDIVIDUAL FINANCIAL RISK TOLERANCE ACROSS THE LIFE SPAN: DOES CUSHION WEAR OUT OVER TIME?

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ABSTRACT (LONG)

An examination of the effect of culture on individual financial risk tolerance was initiated by Weber and Hsee (1998), with collectivism found to be associated with increased financial risk tolerance relative to individualism. To explain their findings they introduce the cushion hypothesis. Specifically, in financial hardship, members in collectivist society can approach their internal groups (family and social network) for help and support, while this is not the case in the individualism. Weber and Hsee (1998) claim that such readily available financial support act to conceal the risk embedded in financial options. Consequently, collectivist individuals perceive the same financial option as less risky, and hence they are more risk tolerant comparing to their individualist counterparts.

The primary aim of this study is to investigate a potential moderating effect of age in the relationship between culture and financial risk tolerance, along with identifying reasons for such an effect if found to be present. The idea of the mitigated effect of age stems from empirical results obtained by Hallahan et al. (2003) and Fan and Xiao (2006), showing that the marginal reduction in reported risk tolerance increases with age, and is larger with Chinese individuals than with Americans. Furthermore, previous anthropological and psychological literatures report changes in one's personal traits, patterns of thinking, judging, and acting, across the life span. Particularly, as collectivist members grow older, the development of their self-conscious emotions (embarrassment, shame, guilt, and self-esteem)[1] may reduce their willingness to seek financial help[2], especially in societies with

[1] Hofstede (2001), Mandel (2003), Lewis et al. (2001), Benedict (1974), Bedford and Hwang (2003), Hwang (2001), Izard (1997), Bedford (1990), Demo (1992), Bengtson et al. (1985), Shaw et al. (2010), Giarrusso et al. (2001), Orth et al. (2010), Robins et al. (2002), Rosow (1985), Mirowsky and Ross (1992)
[2] Harel et al. (1990), Veroff (1981)

high level of power distance (strong social hierarchy), assuming that the availability of support stays unchanged. Consequently, it is predicted that as age advances, the level of risk tolerance of collectivist members would reduce; as would that of their individualist counterparts (age effect per se). However, the marginal reduction in risk tolerance in the social-collectivism is higher than in the individualism.

Two main contributions are made to the extant literature. Firstly, employing a range of measures capturing culture and risk attitudes, along with alternative statistical analysis, we re-examine the cultural effects on financial risk tolerance and clarify the cushion hypothesis. The second contribution relates to whether age would influence such cultural effects through the cushion hypothesis. We survey responses of 1,889 individuals from five different countries: the US and the UK (individualism); China and Vietnam (collectivism); and Singapore (a multicultural nation, allowing within-country cultural heterogeneity). We find evidence of a significant negative moderating effect of age on cultural differences in financial risk tolerance. More specifically, the cultural effect on risk tolerance is influenced by one’s age such that as age increases, the increased financial risk tolerance of collectivism reduces.

In general, more collectivistic individuals perceive greater financial help to be available from their social networks, causing smaller risk perception and higher risk attitude compared to less collectivistic individuals. As a result, they are more risk tolerant. Nevertheless, such cultural differences in risk tolerance reduce across age. Specifically, as collectivistic individuals get older, their willingness to ask for financial help reduces, despite the availability of such support remaining unchanged. Consequently, their attitudes toward financial risk diminish, causing their risk tolerance to reduce.

KEY WORDS: Age; culture; financial risk tolerance; risk perception; risk attitude.

ABSTRACT (SHORT)

The effect of culture on individual financial risk tolerance has been examined in the cultural finance literature, with collectivism found to be associated with increased financial risk tolerance in relative to individualism. The main purpose of this study is to investigate a potential moderating effect of age in the relationship between culture and financial risk tolerant, along with identifying reasons for such an effect if found to be present. Furthermore, by employing a range of measures capturing culture and risk attitudes, along with alternative statistical analysis, we re-examine the cultural effects on financial risk tolerance and clarify the cushion hypothesis.

We survey responses of 1,889 individuals from five different countries: the US and the UK (individualism); China and Vietnam (collectivism); and Singapore (a multicultural nation, allowing within-country cultural heterogeneity). Study finds that more collectivistic individuals perceive greater financial help to be available from their social networks, causing smaller risk perception and higher risk attitude comparing to less collectivistic individuals. As a result, they are more risk tolerant. Nevertheless, such cultural differences in risk tolerance reduce across age. Specifically, as collectivistic individuals get older, their willingness to ask for financial help reduces, despite the available support remains unchanged. Consequently, their attitudes toward financial risk diminish, causing their risk tolerance to reduce.

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