

Abstract

This research studies how a CEO's risk preference is able to moderate the peer firm effect on a firm's capital structure decision. The sample of analysis covers from the US firms from 1992 to 2018 that are listed within S&P 500, S&P 400, and S&P 600. However, the analysis restricts the sample from financial, utility, and governmental companies to avoid regulatory bias, which results to 1094 firms. Using fixed-effect regression, the relationship moderates the peer firm leverage with the CEOs' option Vega in estimating the firm-specific leverage. Past evidence suggests that, higher Vega leads to higher/riskier policies. Hence, the hypothesis of this study is, as given the peer firm effect, risk-seeking CEOs have the higher leverage ratio compared to risk-averse CEOs, and risk-averse CEOs have the lower leverage ratio compared to risk-seeking CEOs. However, the result shows that risk-averse CEOs have the higher magnitude of leverage in comparison to risk-seeking CEOs, and vice versa even after with the robustness check. This suggests that risk-averse CEOs sensitively mimic more to the peer firms or to the industry standards, while risk-seeking CEOs mimic less, be less affected by peer firms, go against the industrial herding behaviour, and prefer delving more into their internal self-capabilities. Eventually, the relationship shown can implicate to the importance of corporate governance and network profiling for strategic endeavour.

Keywords: Vega, CEO, Risk Preference, Peer Firm Effect, Risk-seeking, Risk-averse, Leverage, Capital Structure