No Guts, No Glory: Excessive Risk-Taking in Tournaments
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We study risk-taking behavior in a tournament in which the optimal strategy is to take no risk. In a laboratory experiment subjects were randomly matched into groups of four and could choose how much experimental currency units (ECU) to invest in the following lottery: With probability 4/5 subjects lost the amount ECU invested. With probability 1/5 subjects won x times the amount invested (with x=4 and x=10, respectively). The one with the highest amount of ECU after the lottery draw received a monetary prize while the others received nothing. With more than one subject on top, the winner was chosen by drawing lots. The game was played 15 rounds. Since four subjects were competing, and there was only 1/5 chance of winning in the lottery, the optimal strategy was to invest zero each round. However, less than 10% of the subjects invested zero in the first rounds. This increased to almost 30% in the last rounds. The majority playing dominated strategies increased their risk-taking during the 15 rounds. We also find strong peer group effects. In particular, the group winner’s decision in round t-1 had a strong and significant effect on the other group-members’ risk-taking in round t.