Macro-Economic Forces, Managerial Behaviour and Board Networks as Drivers of M&A Activity

Submitted by Felix Haller to the University of Exeter

as a thesis for the degree of

Doctor of Philosophy in Finance

In May 2013

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Abstract

Mergers and acquisitions play an important role in international financial markets, which explains why this research area attracts a lot of attention from academics, bankers, and investors. Generally, in takeovers, two firms merge in order to achieve specific strategic and business objectives. The ultimate goal is often, but not always, the creation of shareholder value.

In many cases, the creation of shareholder value is not the primary objective of the managers, however, which is one of the reasons why takeovers have been associated with the destruction of value in several existing studies. Instead, many M&A decisions are a function of managerial behaviour. In this thesis, I investigate the drivers of M&A activity, and consider both purely rational (neo-classical) and behavioural reasons as managers’ motivations for getting involved in M&A transactions. The thesis’s main body consists of three empirical studies that investigate how M&A activity is driven by macro-economic forces, managerial behaviour and board networks.

Chapter 3 investigates whether merger waves are driven by macro-economic determinants and financial markets; Chapter 4 tests whether envy among CEOs has any explanatory power over the appearance of merger waves; Chapter 5 looks at whether board networks affect the relative merits of acquisitions and the probability of acquiring firms in “linked” industries.

More specifically, Chapter 3 tests the extent to which US and UK merger waves are driven by macro-economic and financial market factors. Besides the analysis of domestic M&A activity, I also study the drivers of cross-border acquisitions between the UK and the US. I disentangle M&A activities according to how they are financed, and test whether managers follow market timing strategies when engaging in M&A transactions. I find evidence that domestic takeovers in the US and in the UK are highly correlated with the credit cycle and moderately correlated with the business cycle. I also test wave patterns in US and UK merger waves, and find that the merger waves in the two countries are significantly related to each other.

Chapter 4 considers the view that irrational managerial behaviour could trigger UK merger waves. In particular, I assume that CEOs assess their own situation relative to those of their peers. If a CEO earns less than his peers, he becomes envious. Since it is established in the
literature that firm size and executive compensation are positively correlated, CEOs have an incentive to engage in size-increasing mergers in order to decrease any compensation differential. Cross-sectional envy should therefore be considered as a potential explanation for merger waves. In an interdisciplinary approach, I develop a new measure for envy that is based on theories borrowed from the sociology area. My results from comprehensive tests with this new measure show that envy is unlikely to be an explanation for UK merger waves.

Chapter 5 uses social networking theory to examine possible benefits for the acquirer from being well-connected. I assume that strong board networks are associated with better and faster access to information. Building on this rationale, I hypothesize that well-connected acquirers make better acquisitions due to reduced information asymmetries between them and the target. This chapter examines whether board interlocks between the acquirer and the target, existing prior to the acquisition, are associated with superior cumulative abnormal returns for the acquirer. Using centrality measures from social networking theory, I test whether firms that are well-connected make better acquisitions, as measured by the announcement returns of the acquirer. I find acquirer-target board interlocks to be significantly and positively associated with the acquirer’s cumulative abnormal returns. Centrality measures, however, turn out not to have any significant impact on the acquirer’s stock price reaction. Lastly, I show that acquirers are significantly more likely to acquire firms from industries with which they are “linked” via board members that have multiple directorships.
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