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# Extraversion, individualism and M&A activities

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ABSTRACT

Previous studies have documented that variations in economic and business environments can explain the patterns of mergers and acquisitions (M&A) across different countries. We investigated these patterns from a psychological perspective and found that the personality trait of extraversion and the cultural dimension of individualism (IDV) also affected the patterns of M&A activities across countries. Our results suggest that the psychological characteristics of corporate decision makers play a very important role in the M&A decision-making process, even after controlling for external economic and business factors. Furthermore, IDV significantly mediates the relationship between extraversion and M&A activities. This result provides support for the reverse causation hypothesis.



## 1. Introduction

Mergers and acquisitions (M&A) are important business activities that significantly affect economic development. According to the M&A report released by Wilmerhale (2011), the total deal value of global M&A activities reached US$2.03 trillion in 2010 (based on data taken from the MergerStat database). Detailed surveys of different M&A theories have been provided by Trautwein (1990), Cartwright and Schoenberg (2006), McCarthy and Dolfsma (2012) and Gomes, Angwin, Weber, and Tarba (2013). Different M&A theories have been developed along different disciplinary lines, such as economics, finance, strategic management and psychology.

M&A theories from the economics and finance disciplines, such as efficiency theory (Jensen, 1986; Manne, 1965; Porter, 1985), monopoly theory (Steiner, 1975; Stigler, 1950) and empire-building theory (Rhoades, 1983), emphasize the benefits that accrue to the shareholders and managers of acquiring firms. Recent strategic management studies (Bauer, Matzler, & Wolf, 2014; Colombo & Rabbiosi, 2014; Grimpe & Hussinger, 2014; Makri, Hitt, & Lane, 2010) have considered value creation in relation to the acquisition of technology and innovative capabilities as a major motive of M&A.

However, empirical studies have suggested that M&A activities may not generate any efficiency improvements or economic benefits for the shareholders of acquiring firms. In fact, they can result in significant economic losses (Agrawal, Jaffe, & Mandelker, 1992; Eger, 1983; Firth, 1980; Malatesta, 1983; Moeller, Schlingemann, & Stulz, 2005). The poor post-acquisition performance of acquiring firms indicates that the economic benefits of shareholders are not the key concern for the corporate managers involved in M&A decision making. These results are more consistent with M&A theories that emphasize the self-interest of corporate managers, such as transaction cost economics (Williamson, 1975, 1985, 1996) and agency theory (Jensen & Meckling, 1976). These theories predict that the divergence between the interests of managers and shareholders may lead corporate managers to make M&A decisions that follow their interests, but only at the expense of the acquiring firms' shareholders.

For example, a manager may negotiate with the board of directors for a better remuneration package for managing a bigger firm formed by M&A. Fong, Misangyi, and Tosi (2010) summarized the theories and empirical evidence provided by the literature and found that increasing firm size was a way for CEOs to increase their monetary and nonmonetary rewards. However, as mentioned

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previously, many empirical studies have documented the likelihood of negative returns for the shareholders of acquiring firms in the post-acquisition period. The poor outcomes for shareholders in acquiring firms are the consequences of rational choices made by corporate managers with the primary objective of maximizing their personal benefits (Angwin, Stern, & Bradley, 2004; Beatty & Zajac, 1994; Fung, Jo, & Tsai, 2009; Lang, Stulz, & Walkling, 1991; Morck, Shleifer, & Vishny, 1990; Parvinen & Tikkanen, 2007).

Rossi and Volpin (2004) investigated how the external business regulatory environment, which protects shareholders' interests from mismanagement or malpractice by corporate managers, affects the intensity of a country's M&A activities. Their results indicated that a country's accounting and shareholder protection standards could explain the intensity of its M&A activities. They also showed that the variables describing the macroeconomic environment, including the logarithm of gross national product (GNP) per capita and the growth rate of gross domestic product (GDP), could explain the intensity of M&A activities.

The economic benefits to shareholders and managers are not the only drivers of M&A decisions. These decisions may also be driven by managers' psychological and behavioral biases, which cannot be explained by the expected utility theory in the standard economic framework that analyzes the economic benefits involved. Roll (1986) developed the hubris hypothesis to explain corporate takeover activities from a psychological perspective. Furthermore, recent studies have documented evidence of a psychological bias toward overconfidence in the decision-making processes of corporate executives (Ben-David, Graham, & Harvey, 2007; Doukas & Petmezas, 2007; Malmendier & Tate, 2005, 2008). Goel and Thakor (2008) developed a theoretical economic model to provide a rational explanation for the psychologically biased behavior of CEOs. Given that this well-documented psychological bias of managerial overconfidence is a personality trait of extraverts (Costa & McCrae, 1992; Schaefer, Williams, Goodie, & Campbell, 2004) and that personality traits and cultural dimensions are interrelated (Allik & McCrae, 2002; Hofstede & McCrae, 2004; McCrae, 2001), personality traits and cultural dimensions are expected to play an important role in M&A activities.

With reference to recent studies (Colombo & Rabbiosi, 2014; Grimpe & Hussinger, 2014; Makri et al., 2010) regarding the acquisition of technology and innovative capabilities as a major motive of M&A, Bauer et al. (2014) further found that a national culture is an important factor in the integration of innovativeness into M&A. The influence of cultural factors and personality has become a new direction for studies of M&A activities (Coisne, 2012; Petkova & McCarthy, 2012).

In this study, we adopt a psychological perspective in examining how the personality trait of extraversion and the cultural dimension of individualism (IDV) are associated with the intensity of M&A activities across countries. We define the intensity of M&A activities in each country for each year as the number of announced successful domestic M&A transactions in a country during the year over the total number of publicly traded firms in the country at the end of the year. Our aim is to demonstrate the additional explanatory power of extraversion and IDV on the intensity of M&A activities and thus expand the economic explanations given by Rossi and Volpin (2004) while showing that IDV significantly mediates the interaction between extraversion and M&A activities. The following two paragraphs provide a brief explanation of the IDV and extraversion variables.

To define national culture, Hofstede (1983) developed the following dimensions: (a) IDV versus collectivism, (b) large or small power distance, (c) strong or weak uncertainty avoidance, (d) masculinity versus femininity and (e) long-term orientation. The dimension of "IDV versus collectivism" represents two ways of understanding the relationships between individuals in a group (Hofstede, 1983). People in an individualistic society view "persons as separate entities, clearly distinguishable from their social milieus" (Bochner, 1994, p. 274). They believe that they are supposed to take care of themselves because they consider themselves to be more independent, autonomous and self-contained. These individuals see themselves as more special and thus different from others. One of the characteristics of people in an IDV society is an "I" consciousness that emphasizes their right to privacy and personal opinions (Hofstede, 2011). IDV individuals are more calculative and success oriented and strive to attain as many benefits as possible. Studies have investigated the effectiveness of IDV on different aspects of individuals' lives. For example, van Hoorn (2014) showed that employers in an individualistic society engage in more sophisticated management practices that improve firm performance. Rinne, Steel, and Fairweather (2013) found that IDV and people's creativity were positively related, indicating that the characteristics demonstrated by individualists (such as autonomy and independence) were important to creativity. Although the dimension of "IDV versus collectivism" was developed by Hofstede decades ago, it remains widely applied in current research.

Extraversion is a Big Five personality trait (Wiggins & Trapnell, 1997). According to Komarraju, Karau, Schmeck, and Avdic (2011), some of the characteristics of extraverts include high degrees of sociability, assertiveness and talkativeness. Nyhus and Pons (2012) mentioned that extraverts have a high tendency to seek novelty and stimulation. They are also assertive and gregarious. Individuals who exhibit high levels of extraversion have certain advantages. For example, Petrides et al. (2010) found that extraversion was positively related to emotional intelligence and well-being. In a study of 818 urban employees from 5 cities in China, Zhai, Willis, O'Shea, Zhai, and Yang (2013) found extraversion to be strongly and positively related to job satisfaction and subjective well-being. Kiany (1998) investigated the relationship between extraversion and academic achievement and described extraverts as more impulsive, outgoing and possibly more easily disturbed mentally by other people or things, which may lead to decreased concentration. Kiany also found extraversion and academic achievement to be negatively related. Therefore, the personality trait of extraversion carries both positive and negative aspects.

In this paper, we establish hypotheses for the relationships between extraversion, IDV and the intensity of domestic M&A activities. We also provide empirical evidence supporting our hypotheses. The remainder of this paper is organized as follows. We present the literature review and hypotheses development in the next section, followed by a section describing the data and methodology used in the study. In the subsequent section, the statistical results are presented and discussed. The final section presents the implications and limitations of the study and offers suggestions for future research.

## 2. Literature review and hypotheses development

Most M&A theories consider the benefits that accrue to the shareholders and managers of acquiring firms to be the primary motivation for M&A activities. For example, efficiency theory (Jensen, 1986; Manne, 1965; Porter, 1985) and monopoly theory (Steiner, 1975; Stigler, 1950) hypothesize that the economic benefits gained by shareholders from the synergy effect and from increased monopolistic power are the major motives for initiating M&A activities. In contrast, empire-building theory (Rhoades, 1983) emphasizes the personal benefits gained by the managers of acquiring firms. Recent strategic management studies (Bauer et al., 2014; Colombo & Rabbiosi, 2014; Grimpe & Hussinger, 2014; Makri et al., 2010) have focused on the benefits of value creation