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Female directors and UK company acquisitiveness

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ABSTRACT

We show that the presence, and proportion, of female directors are strongly related to the level of acquisitiveness of a company. This finding is made through a dataset covering significant size acquisitions made by FTSE 100 constituents over a 12-year time period from 2000 to 2011 and includes multiple controls for potential confounding financial and director characteristics. A novel main testing approach of zero-inflated Poisson regressions is utilised, with a variety of alternative tests and specifications further reported to add to the robustness of the study. The finding draws on psychological and decision-making research showing females to be less overconfident in their decision-making.

1. Introduction

> The evidence is that there is a positive link between women in leadership and business performance, so if we fail to unlock the potential of women in the labour market, we're not only failing those individuals, we're failing our whole economy
> [Mr David Cameron, United Kingdom Prime Minister, 7th Feb 2012]

Women account for just 12.5% of directors in the United Kingdom's largest companies (Davies, 2011). There is a self-evident social justice argument for a move towards equal opportunities for females at these higher echelons of the corporate world. Much discourse, however, has instead focused on the business benefits of a gender-diverse Board of Directors. A problem is that there is a paucity of robust research to inform this later argument, and it is into this void that this research is aimed. Specifically, we investigate the relationship between the proportion of female directors in FTSE 100 companies and the likelihood of a company engaging in significant size acquisitions. Our findings strongly support a conclusion that female directors are related to a reduced level of acquisitiveness in a company.

This research is driven by the ample psychological findings showing that males and females differ in their risk propensity. Research suggests that females exhibit less overconfidence compared to males (e.g. Johnson et al., 2006). With overconfidence linked to propensity to take excess risks and make poor financial decisions (Barber & Odean, 2001; Doukas & Petmezas, 2007), a reasonable hypothesis therefore is that reducing overconfidence among a Board of Directors through reducing the excessive historical bias towards male directors, should reduce excessive risk taking. Some prior research supports this contention. For example, increased female director representation has been linked to higher-quality earnings (Srinidhi, Gul, & Tsui, 2011) and better monitoring of firm activities (Adams & Ferreira, 2009).

We extend this area of investigation by examining whether the presence, and proportion, of female directors might reduce the propensity of the firm to engage in the risky activity of making large acquisitions. International research finds acquisitions to generally be value-neutral for large companies, in addition to being a distraction of management focus (Netter, Stegemoller, & Wintoki, 2011). Given the minimal benefits, the cost of management distraction, and the risks particularly associated with large acquisitions (Moeller, Schlingemann, & Stulz, 2005), M&A appears to be an unrewarding activity, or, at least, a risky activity.

Given the poor business case for large acquisitions, motivations for engaging in such acquisitions have increasingly focussed on behavioural characteristics of the key decision makers who decide to acquire. Most studied are the psychological characteristics of CEOs, including displays of overconfidence (Croci, Petmezas, & Vagenas-Nanos, 2010; Malmendier & Tate, 2005, 2008, in a UK context), narcissism (Chatterjee & Hambrick, 2011) and their social status (Lucey, Plaksina, & Dowling, in press; Malmendier & Tate, 2009). It is within this behavioural focus that our research is situated.

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Our study provides a robust investigation of whether the presence of female directors is related to likelihood of engaging in significant size acquisitions (where the transaction value is greater than 5% market capitalisation of acquirer) for UK FTSE 100 constituent companies over a 12 year period from January 2000 to December 2011. The proportion of female directors on a company board is shown to be significantly negatively related to the acquisitiveness of the company. This finding is robust to a number of financial controls (Tobin's Q, leverage, a measure of Operating Cash Flow, and total assets of the firm) and director controls (Board size, average age of directors, and percentage of independent directors). A number of testing approaches are reported with the main model being a zero-inflated Poisson regression.

The most relevant prior research is that of Levi, Li, and Zhang (2012) which finds evidence that higher number of female directors reduces acquisitiveness in a dataset of large US companies. Our paper is the first to test the influence of female directors on acquisitiveness outside of the US and includes a number of advances, particularly in the range of testing approaches and the range of specifications applied. Some specific new empirical contributions are an extension of the studied acquisition targets beyond just listed targets, the finding that female directors appear to also influence the volume of smaller size acquisitions, and a tentative conclusion that the number of female directors appears to be a better measure of influence compared to percentage of female directors.

2. The influence of directors

The board of directors is considered to be the highest-level of control mechanism in an organisation as they possess the ultimate power to compensate the decisions that are made by the top management (e.g. Fama & Jensen, 1983). Evidence suggests that the structural characteristics of the board may influence the effectiveness of its decisions. These characteristics are primarily the following: size of the board, the presence of independent non-executive directors, and board diversity and director characteristics.

Large board sizes have been argued to improve monitoring ability due to greater overall available time and combined effort (John & Senbet, 1998). Thus, Ghosh, Marra, and Moon (2010), using a US dataset, find a decrease in earnings management, as measured by discretionary accrual levels, as board size increases. However, Jensen (1993) argues that as board size increases, boards can become less effective due to the potential for poorer communication and coordination between members. Coles, Daniel, and Naveen (2008) propose that small boards with a majority of independent directors are effective at monitoring, while large boards provide a valuable advisory function to top management. Guest (2009), in a UK study, finds that large Boards are negatively related to performance and argues that UK Boards tend to play a weaker monitoring role than US Boards. Cheng (2008) finds a reduced level of acquisitions, amongst a range of other reduced risky activities, for large board sizes and posits the explanation that this is due to the increased difficulty of reaching consensus with large numbers of directors.

Independent directors are linked to the responsibility for monitoring managers and thereby reducing agency costs that arise from the separation of ownership and control (Brennan & Mcdermott, 2004). Osma (2008) finds that independent directors are capable of identifying and restraining earnings management that result from R&D cuts. Jaggi, Leung, and Gul (2009) found that independent boards provide effective monitoring of earnings management. With regard to acquisitiveness, Kolasinski and Li (in press) find reduced acquisitiveness related to the increased presence of independent directors.

The diversity of a Board and the characteristics of directors are areas of growing interest amongst researchers and directly related to this research. An example is Kroll, Walters, and Wright (2008) who find that director prior experience in an industry and with engaging in acquisitions is linked to positive acquisition outcomes, while Güner et al. (2008) find that directors from a corporate banking background are associated with poor acquisition outcomes. Carter, Simkins, and Simpson (2003) find that ethnic and gender diversity among a Board of Directors is associated with higher firm value for a sample of large US firms. A recent paper by Berger, Kick, and Schaeck (2012) uses a comprehensive dataset of German bank directors to find that director age, gender, and educational qualifications influence organisational risky decision making.

3. Gender and corporate decision-making

Fondas and Sassalos (2000) assert that gender diversity in the Board of Directors is an effective driver of company performance and may lead to a wider knowledge base. This appears to be the basic argument supporting the contention that female directors may improve decision-making by bringing different perspectives and opinions into decision making process.

This argument is supported by the findings of Erhardt, Werbel, and Shrader (2003) using a sample of US companies to examine the relationship between board gender diversity and financial performance. They found that gender diversity is associated with strong financial performance. Krishnan and Parsons (2008) compared the earnings quality in companies with higher percentages of female directors to those with fewer female directors on their boards. They find that companies with more female senior managers are more profitable and have higher stock returns after initial public offerings than those with fewer females in the management ranks. Female directors appear to be more active compared to male directors; attending more board meetings and being more likely to sit on monitoring committees (Adams & Ferreira, 2009).

One of the main relevant drivers of difference in behaviour between male and female executives appears to be risk attitudes and levels of overconfidence. These gender differences in attitude towards risk and risk behaviour are well-documented in the psychology and decision-making literatures. Eckel and Grossman (2008), in a comprehensive review, summarise the findings in the area as showing women to be more risk averse across a wide variety of field studies. Explanations for the heightened risk aversion amongst females include sociobiological: primarily that risk aversion is beneficial during child rearing (Laborde Witt, 1994); and neurobiological; females have a lower level of testosterone which is linked with risk-taking through reduced fear levels (Sapienza, Zingales, & Maestripieri, 2009).

Influenced by, but distinct from, risk aversion, is overconfidence. Overconfidence can be described as an excessive belief in one's abilities (Kruger, 1999). While this is partially related to risk attitudes, it is also related to self-attribution bias; the tendency to attribute successful outcomes from decisions to one's own actions, and bad outcomes to external factors (see Dowling & Lucey, 2010, for a review of the literature).

Males are particularly prone to overconfidence due to high levels of biased self-attribution (e.g. Lundeberg, Fox, & Punćcohaŕ, 1994). As Lundeberg et al. put it "the problem may not be that women necessarily lack confidence but that, in some cases, men have too much confidence" (p. 120). Croson and Gneezy (2009) provide a recent review of the research in this area. Gender differences in overconfidence provide a strong rationale for this current investigation, given the research by, for example, Malmendier and Tate (2005, 2008) showing the relationship between overconfidence and the acquisitiveness of a company.

This research on gender differences in risk and confidence has been investigated to some extent in finance research. In personal investment research, Sunden and Surette (1998) examined gender differences in the allocation of defined contribution plan assets and found that women are less likely to hold their assets in stocks than men. In the same vein, Dwyer, Gilkeson, and List (2002) show that women hold more conservative mutual fund investments, while