Christoph Meyer

The Effect of Founder-CEO Overconfidence on Merger Premium

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The Effect of Founder-CEO Overconfidence on Merger
Premium – Evidence of the High-Tech Industry

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ABSTRACT

Purpose – Theoretical and empirical research has indicated that overconfidence affects merger decision-making and merger premium. However, founder-CEOs have not been subject of such a study, yet. This lack is particular surprising when considering the differences between founder and manager-CEOs as well as the media attention of founder-CEOs. The present dissertation aims to fill the research gap through investigating the effect of founder-CEO overconfidence on merger premium in the high-tech industry. Moreover, this dissertation aims to extend the literature by including target CEO overconfidence and studying the impact on merger premium when both, acquirer and target CEO are overconfident. By studying founder-CEOs this dissertation also aims to establish the effectiveness of founders as CEOs. The resource-based perspective argues that while founders help in the early years of the company, they become less effective as the firm evolves, since they lack the necessary management skills.

Design/methodology/approach – Using ordinary least square (OLS) technique, this study investigates the effects of implemented factors in determining the merger premium paid in high-tech acquisitions. A sample consisting of 245 acquisitions in the high-tech industry of 124 CEOs during a 19-year period (1995 to 2013) has been observed. In order to test the founder-CEO effects, this dissertation develops a matched sample approach of 62 founder-CEOs and 62 manager-CEOs.

Findings – This study shows a strong relationship between CEO overconfidence and acquisitions premium paid. The results suggest that the CEO overconfidence may provide an explanation for the well-rehearsed overpayment problem. An additional analysis indicates that the highest premium is paid when combined acquiring and target firm CEO overconfidence exist. The dissertation also shows that founder-CEOs pay higher premia than manager-CEOs in the high-tech industry. It has been proven that founder-CEOs’ decisions are more independent from interventions of the board of directors and that founder-CEO overpayment is not dependent on the company’s size.
or relatedness of mergers. The findings are reliable as the results remain constant for applied robustness tests.

Originality/value – To the best of the author’s knowledge, this is the first study which incorporates founder-CEOs overconfidence and merger premia within the same study. The findings about founder-CEO and premium paid contribute to the on-going research on strategic leadership. Moreover, a new measure for overconfidence – based on seven components which describe national, religious, cultural and gender CEO characteristics – is built. In this aspect, the dissertation contributes to the literature by providing a new and more flexible measure of overconfidence.

Conclusion – From the analysis in this study it can be concluded that while founders provide many benefits compared to manager-CEOs, such as a higher commitment or comprehensive firm and market knowledge, they are more liable to the problem of overpayment. Hence, another conclusion is that cognitive biases may be beneficial under some circumstances, such as implementing a business, whereas in other situations they might cause major problems. Moreover, this overpayment problem is consistent and cannot be ameliorated with corporate governance. Thus, shareholder’s investment in a company with its founder as CEO is more risky with regards to M&A overpayment. Target firms on the other hand, are more likely to obtain an overpaid premium when selling to an overconfident founder-CEO. That could have significant consequences on the sales and negotiation strategy of future mergers and acquisitions.
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