THE EFFECT OF CEO POLITICAL IDEOLOGY ON MERGERS & ACQUISITIONS

Master Thesis

Financial Management

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ABSTRACT

The central question of this research is to examine to what extent a CEO's political ideology has an influence on mergers and acquisition decisions. This research is based on previous literature and research about behavioral consistency and how personal characteristics and ideologies of CEOs work through to corporate decision making. Empirical results were based on a sample of 138 firms in the Netherlands stock market index from 2017-2021. The results suggest that right-wing CEOs are not less likely to engage in M&A activities, which is contradictory with previous literature and the first proposed hypothesis, as right-wing CEOs were considered to be more conservative in their corporate investment decisions. However, the effect is not found significant. It is found that right-wing CEOs are less likely to use stock as a payment method. The direction is consistent with the hypothesis, but not a significant result is found. Right-wing CEOs are significantly less likely to engage in focus-increasing deals, which is not consistent with earlier argumentation about their preference to remain the status quo and preference for familiar stimuli. This research makes an important contribution to already existing research as it considers the dutch political system for the first time.

1. INTRODUCTION

Mergers and acquisitions have become more common over the years, especially in the healthcare, technology, financial services, and retail sectors. But how does a CEO's political ideology play a role in these kinds of deals?

In the Netherlands, when we discuss political ideologies, we distinguish three main areas. In order to classify the political parties, the terms 'left', 'center' and 'right' are usually used (Ramkema, Hesselink & Parren, 2008). However, because the division is interpreted in different ways by the parties themselves and also by voters, caution is advised. Today, in this classification, the left represents more progressive parties who want a greater role for government in social life, while the right-wing parties are more conservative and want to limit the role of government and hold on to more traditional views. In addition to, or as alternative to, the division into left and right, a division based on 'progressive' and 'conservative' is often made. Where progressive stands for a progressive and change-oriented policy and conservative for a conservative course (Ramkema, Hesselink & Parren, 2008).

The objective of this paper is to examine the relation between dutch CEO's political ideology and mergers and acquisition deals of their firm. It is important to investigate the effect of CEOs' political ideology on M&A decisions, since these decisions are one of the most important decisions CEOs make, as they have a significant effect on the wealth of the company's shareholders (Deng et al., 2013).

Referring to 'the behavioral consistency principle', previous literature suggests that individuals' preferences, attitudes, and personal traits convert to choice problems (Wernimont and Campbell, 1968). For example, Bonaparte et al. (2010), Hong and Kostovetsky (2012), and Jiang et al. (2011) document that investment decisions and forecasts are significantly affected by personal political preferences. More recent research of Hutton et al. (2014) tested if the political ideology of CEOs affects the degree of financial conservatism in their companies. The results of this study show that Republican CEOs exhibit more conservative corporate policies, for example lower leverage ratios, lower capital and R&D expenditures, less risky investment, higher dividend payouts, and greater profitability. The study of Elnahas and Kim (2017) extends this literature by testing the effect of a CEO's political ideology on M&A decisions and finds that Republican CEOs are significantly less inclined to employ those activities. These findings are consistent with previous literature (Jost et al., 2003; Wilson, 1973; Kish et al., 1973) saying that conservative people show a strong tendency to maintain the status quo. These results show that conservatives' behavioral consistency stretches to CEO's corporate investment and mergers and acquisitions decisions.

The research question that will be answered in this paper is to what extent does dutch CEOs' political ideology affect M&A decisions of their firm. Other research has only covered this question related to the US political system and US CEOs and companies. Therefore this research contributes to previous literature about behavioral consistency and how personal characteristics and ideologies of CEOs work through to corporate decision making. Conservative Republican CEOs were found to be less likely to engage in merger and acquisition (Elnahas and Kim, 2017). Accordingly, I propose that dutch CEOs that have a preference for more conservative right-wing parties will also be less willing to proceed with mergers and acquisition deals. However, the findings of this research are somewhat contradictory with the current literature about US CEOs. The main discovery is that dutch right-wing CEOs are not less likely to engage in M&A. Furthermore, the preferences for methods of payment for M&A deals of more conservative CEOs do correspond with the current literature, but the expectation that those CEOs would prefer more focus-increasing deals is rejected.

The structure of the remainder of this paper will be as follows. Section 2 provides a literature review and the hypotheses. Section 3 describes the data that is used and the methodology of the research. Section 4 provides the empirical results. Section 5 discusses the results and the last section covers the conclusion.

2. LITERATURE REVIEW

Ideology

Ideologies can be defined as the implicit or explicit beliefs and thoughts about existence. They also define what an individual person or a group sees as a desirable scheme of beliefs, ideas, view of the world and norms. Hence, ideologies have an important role in the decision making process of humans. Ideologies are developed throughout a person's life. Various factors, such as birth place, language, growing-up environment, special events, education, parents and many others affect the formation of an individual's or group's ideology. These ideologies influence not only decision-making styles, but also affect the decision-making process (Chen & Dahan, 2011). Decision-making is done by identifying and selecting alternatives based on values and preferences of the one making the decision (Harris, 1998). The individual makes a reasonable choice among all of the alternatives a decision offers by engaging in a process of reducing uncertainty and doubt by reasoning from their ideology (Harris, 1998).

Ideology in political decision-making

Studies concerning ideology depend on a number of important characteristics. To start, the term 'ideology' can mean several things to humans and therefore voters. It can indicate a preference for either conservatism or liberalism. Or from a more nuanced perspective, ideology can be identified as, among others, libertarianism, environmentalism and populism. Some people see ideology as an identity. Ideological labels are anchored in political and non-political identities. The term 'conservative' can be explained as only a social orientation that is only loosely associated with the philosophical principles related to conservatism, for example limiting the interference of the government. The term 'liberalism' or 'progressivism' indicate a different view, that may be related to for example expanding the social safety net. Ideology is used to understand the complexity of government policy and as cognitive organization. Humans organize policy beliefs around organizational principles.

Given its diversity, it is important to use the term ideology in an accurate way to better understand how humans rely on it in their decision-making. Ideology would act as a kind of lens through which the world is interpreted. Moreover, it often fulfills an individual's unique motivational, psychological and personality traits (Weber, 2019).

Executive Political ideology

Many behavioral scientists have studied personal values. Outstanding research was done by England (1967), granting empirical evidence that personal values directly affect the decision-making and performance behavior of managers, and therefore also influence corporate strategy. More recent studies provide evidence of behavioral consistency in corporate situations (Epstein, 1979; Funder & Colvin, 1992). Their research states that personal beliefs are translated into other states of affairs, as well as corporate policies (Di Giuli & Kostevetsky, 2014). Strategic decision-making is more an interpretative undertaking than an objective one. Executives identify their circumstances and options through lenses that are much personalized. These lenses are formed by their experiences, values and personalities and these outline the courses of action of executives (Hambrick & Mason, 1984; Hambrick, 2007; Chin et al., 2013).

According to evidence provided by political psychology literature, it is safe to suggest that the political orientations of CEOs mirror their values. Therefore, people's actions can be rationalized (Rosenberg, 1956; Layman, 1997; Barnea & Schwartz, 1998; Goren, Federico & Kittilson, 2009). According to Goren et al (2009, p. 805) ''party identification represents the most stable and influential political predisposition in the belief system of ordinary citizens.'' Especially in the US, where politics and law are very contradictory. In the US, most political and societal concerns can be illustrated in liberal vs. conservative terms, with Democrats suiting liberal positions and Republicans largely covering conservative standpoints (Poole & Rosenthal 1984).

This liberal-conservative spectrum is essential in understanding human's core beliefs (Schwartz,1996). This political spectrum involves the range of positions, opinions and ideas that exist from the liberal or progressive left-wing to the conservative right-wing. Where the first is more open to change and the latter prefers to keep things as they are (Jost et al. (2003). Conservatives score in general better on internal control and also prefer the Protestant Work Ethic concept, which emphasizes the fundamental meaning and value of work and the strong link between effort and results, and is positively linked with performance. Unlike liberals, who see outcomes more as a result of factors that are beyond people's personal control, including luck and characteristics of the social system. Another difference is that liberals explain fairness on the basis of equality, meaning equal results regardless of contributions and reach for the government to enforce social justice and for the help of those in need. Conservatives explain fairness on the basis of equity, meaning that results have to be proportional to contributions. They rely on the free market to assign outcomes and prefer individuals and private organizations to take care of those in need. High levels of political conservatism are linked to the preference for stability, conformity, tradition, but also order and structure. They avoid ambiguity and chaos and prefer to categorize. High levels of political liberalism is linked to the preference for creativity, curiosity, novelty-seeking and new experiences. They tolerate ambiguity and chaos and prefer flexibility and tackling cognitive conflicts (Napier, 2008). High conservatism is linked to a sense of threat or a perception of danger. People with more conservative versus liberal views see ambiguous faces more as a threat and react to threatening stimuli with more aggression and physical responses, such as blink startle and skin conduction. Conservatives' preference for stability and their resistance to change could contribute to the cohesion that gives them meaning in their life. The conservative course is characteristic for its fundamental trait of fear of change, a timid distrust of all that is new. The liberal course, on the other hand, is known for courage and confidence, to let change run its course even when it is impossible to predict where it will lead (Napier, 2008).

This discussion can be attached to corporate political activities inside companies. Corporate contributions are essentially made not by firms themselves, but by individuals (Ansolabehere, de Figueiredo and Snyder, 2003). Therefore, they state that any form of monetary contributions or political collaboration can be explained as a personal consumption aimed at promoting a personal ideology, rather than a manifestation of impartial corporate entanglement. Organizational results, both strategies as effectiveness, are seen as a reflection of the values and cognitive ground of mighty and influential people in an organization, such as CEOs. This applies to both observable characteristics of CEOs, such as age, tenure in the organization, functional background, education, socioeconomic roots, and financial position, as non-observable characteristics, such as political preference. (Hambrick & Mason, 1984). CEOs who identify themselves with Republicans are found to uphold more financially conservative corporate policies (Ansolabehere, de Figueiredo & Snyder, 2003). Those companies have lower levels of corporate debt, lower capital, as well as research and development (R&D) expenditures, less risky investments, but higher profitability (Hutton et al., 2014). Those CEOs also have more respect for authority, order and stability (Erikson, Luttbeg & Tedin, 1988; Jost et al., 2003). CEOs who identify themselves with Democrats are more socially responsible. They place more emphasis on issues such as the environment, human rights and social change (Schwartz, 1996). Chin et al. (2013) tested the effect of conservatism versus liberalism of managers on organizational outcomes and came to the conclusion that liberal CEOs showed more concern for corporate social responsibility practices compared to conservative CEOs. Even though the study is largely focused on CSR, the conclusion that can be drawn is of fundamental importance as it shows the relevance of CEOs' values in determining the strategies and payoffs of large corporations.

Cited academic work concludes that while a company engages in corporate political activities (CPA), essentially for business-like reasons, CEOs as individuals may engage in political activities as expression of their own values and beliefs. Therefore, corporate political activities can potentially become a CEO's personal instruments. An executive's ideology can be viewed as a determinant of activities in an attempt to advocate favorable political and regulatory outcomes, gains, and all embracing, to implement a cohesive strategy that matches a firm's resources and objectives inside a certain political environment (Hart, 2010; Hillman & Hitt, 1999).

CEO political ideology & corporate decision making

The basic proposition of the research of Elnahas and Kim (2017) is that an executive's political ideology extends to the financial and investment decisions of their firms. Left and right differences are real and are strongly interconnected to the relative openness to change versus safeguarding traditions. Political right is, in general, linked to conservatism and political left to progressivism (Carney et al. (2008). As discussed before, conservatives want to preserve a certain status quo compared to liberals who are open to changes and explore innovation (Jost et al. (2003). Particularly, conservatives are not that open to unconventional perspectives (Jost and Thompson, 2000), chase less external stimulants (Wilson, 1973a) and are more careful about making changes in their lives (Feather, 1979).

CEO's cover the decisions about internal investment, also known as capital expenditures, and external investment, such as mergers and acquisitions. Analyses of industry patterns in capital expenditures and mergers and acquisitions find that both are comparable as they are both instruments to improve a firm's capital base as a reply to growth opportunities (Andrade and Stafford 2004). On the other hand, Harford and Li (2007) state that executives handle capital expenditures and mergers and acquisitions differently and argue that the motivations differ, mainly due to the information asymmetry and uncertainty that is linked to mergers and acquisitions. Aspects of merger agreements provide a direct channel for uncertainty to influence M&A actions, which is known to vary significantly over time. Economic, regulatory and technological shocks as well as macroeconomic conditions are explanations for M&A activity. Another explanation is mispricing in the stock market and market conditions. The general conclusion from the current literature is that there are many factors that contribute to M&A activity, but economic shocks and macroeconomic conditions dominate in determining uncertainty linked to M&A (Bhagwat et al., (2016). Higher uncertainty will decrease deal activity (Bhagwat et al., (2016).

Elnahas and Kim (2017) expected and found in their research that politically conservative CEOs, who are identified as Republicans, undertake more conservative financial decisions for their firms. They are significantly less inclined to engage in merger and acquisition deals and favor internal investment over external investment. These results are consistent with the arguments in existing literature that conservatives have more proneness to maintain the current state of affairs (Elnahas and Kim, 2017) and are more uncertainty averse (Fishman, 1989).

There is a large literature file that states that many acquisitions destroy value for the acquirer of a M&A deal (Harford and Li, 2007; Loughran and Vijh, 1997; Moeller et al., 2004). The acquisitions of public firms are more likely to be value decreasing. All value destruction involves overpayment. This can be due to the selection of low synergy targets or just paying too much for normal or high synergy targets. The post-merger operating performance is worse, proposing that poor target selection, as opposed to simply overpaying for valuable targets, clarifies the value extermination. In addition, most mergers and acquisitions fail to generate the anticipated synergies. Since conservative CEOs are more concerned with better operating performance and greater profitability, they will be less eager to engage in M&A deals (Hutton et al., 2014).

Dutch political system

Dutch political parties can be classified in different ways. The political parties are often divided into left-wing, right-wing and center parties (Ramkema, Hesselink & Parren, 2008). This classification is a bit controversial and can be unclear at times. The extent to which a party strives for more income equality, knowledge and power in society determines its position. In addition, the extent to which it is prepared to deploy government policy for their goals also plays a role. This is mainly a question of socio-economic policies, employment, taxes, income and benefits, although it also concerns education policy and the democratization of industry and institutions. Parties that favor state intervention to achieve more equality and change of the current state are called "left" or progressive. Parties that do accept existing inequalities and want to remain the current state of affairs are called 'right-wing' or conservative (Ramkema, Hesselink & Parren, 2008). However, it is becoming more troublesome to use these categories, since parties sometimes deviate from their normal course nowadays. Views of normally left-wing parties may now overlap with those of right-wing parties on some issues and vice versa (Ramkema, Hesselink & Parren, 2008).

Hypotheses

The reviewed research suggests that ideologies and values influence political decision-making and that political ideologies characteristics play a role in CEO's corporate decisions. Conservative CEOs undertake more conservative financial decisions. Republicans are linked to conservatism and research has shown that Republican CEOs are less willing to undertake M&A compared to Democratic CEOs. They are significantly less inclined to engage in merger and acquisition deals and favor internal investment over external investment. These results are consistent with the arguments in existing literature that conservatives have more proneness to maintain the current state of affairs. I suggest that this will hold true also for the dutch political system and dutch CEOs, since views of right-wing parties in the dutch political system correspond more with conservatism and those of left-wing parties are more aligned with progressive ideas (Ramkema, Hesselink & Parren, 2008). This leads to the following hypothesis:

H1: Right-wing CEOs are less likely to engage in mergers and acquisitions than left-wing CEOs.

In summary, all this research states that the influence of the political ideology of CEO expands to the decision-making about M&A. Saying that conservative Republican CEOs are less likely to engage in M&A than liberal Democratic CEOs. This confirms the hypothesis stated in this paper, where this situation from the current literature is translated to the dutch political system, namely: dutch CEOs who have a preference for right-wing parties, which are considered more conservative, will be less willing to engage in mergers and acquisition deals, compared to CEOs who have a preference for left-wing parties, who are considered more open to change.

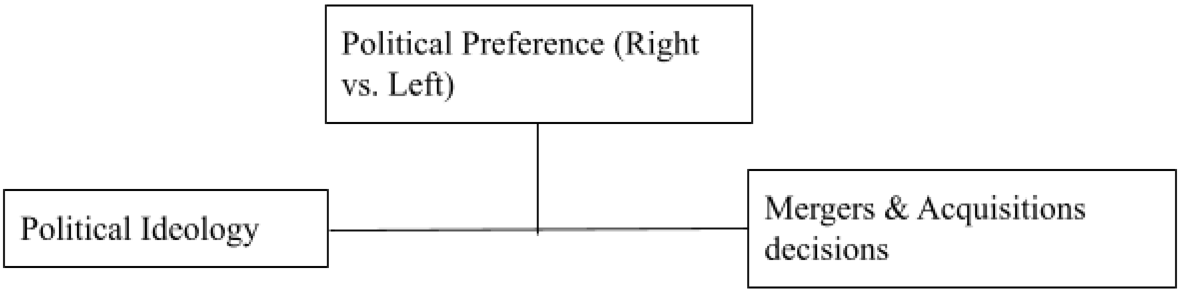

Figure 1: Effect of political ideology on mergers and acquisition decisions.

Literature about mergers & acquisitions has indicated negative announcement returns concerning the acquirer's stocks in mergers sponsored with stock as the method of payment (Servaes, 1991; Travlos, 1987). The lower stock performance of the acquirer goes on even after the announcement term. Post-acquisitions stock returns are lower for stock-financed acquisitions compared to cash-financed (Agrawal et al. 1992b). Stock-financed acquisitions result in significantly lower operating performance for a maximum of five years after acquisition. Hence, if more conservative CEOs are more concerned with higher profitability, it is reasonable to assume that right-wing CEOs would be more loss averse and more sensitive to potentially poor stock performance (Wilson, 1973a). Therefore, right-wing CEOs would be less likely to pay with stock for acquisitions. In addition, conservatives have a preference for low complexity and uncertainty. Cash payments enable a faster completion of deals and therefore reduce the risk of bids of competitors and lower the chance of bid rejection since acquisition price is held constant.

Cash offers are more common when the targets involve low uncertainty (Fishman, 1989); Martin, 1996). In case of a deal financed with cash, the roles of the parties involved are clear, and shares and money are exchanged to reach a simple transfer of the ownership. But in case of share exchange it is more complex who the seller and who the buyer is. Sometimes the acquired firm's shareholders end up possessing most of the firm that actually bought their shares. In deals financed with stock, the value and the risks are shared with the acquired company. In cash deals, the acquiring firm takes on all the risk and all the value in the end. When an acquirer is really confident, he or she is expected to pay with cash for the acquisition. When a M&A deal is financed with stock, this will send two signals to the market. The first being that the company is overvalued and the second being that the management has little confidence in the acquisition. Hence, if a company is confident about a successful integration, and is convinced that its own shares are undervalued or fair valued, it should always go for cash as the method of payment for a M&A deal. In addition, the consideration between stock or cash says something about the expectations of the acquirer of the risks of failing to attain the forecasted synergies from the M&A deal. An acquirer with a lot of confidence in the deal would be expected to pay cash, in order to manage that its shareholders would not have to share any of the expected merger gains with the shareholders of the acquired company. But if the management thinks there exists a substantial risk of not achieving the required level of synergy, they can hedge their bets by offering stock. Losses before and/or after the deal are limited by blurring their company's ownership interest. After all, empirical research shows that the market significantly reacts more opportunely to cash deal announcements compared to stock deal announcements (Rappaport & Sirower, 1999).

To conclude, cash deals involve less uncertainty, complexity and are more beneficial for stock-performance. Hence, conservative loss-averse CEOs will have a preference for cash-financed M&A deals. According to this information, the following hypothesis is formed:

H2: Right-wing CEOs are less likely to use stock as a method of payment than left-wing CEOs.

Conservatives have a preference for familiar stimuli compared to unfamiliar stimuli (Glasgow et al., 1985). Hutton et al. (2014) showed that conservative Republican CEOs display more conservative corporate policies, for example lower leverage ratios, lower capital and R&D expenditures, less risky investment, higher dividend payouts, and greater profitability. When we consider M&A, CEOs can choose to acquire targets that are in the same industry, hence focus-increasing, or they can choose to acquire targets in a different industry, then we talk about diversifying deals. Diversification is the process of accessing new business markets by acquiring already existing companies or by broadening their own businesses into new markets and new areas of production or service (Byrd et al., 1997). Diversifying requires significant expenditures of time and resources of a firm. This makes it a process that can make or actually break a firm. The success of making diversification efforts differs considerably. The probability of success decreases rapidly as the company strays further from existing competencies (Byrd et al., 1997). Morck et al. (1990) has shown that diversifying mergers and acquisition deals come with negative announcement returns, hence they are value destroying. Others have also documented diversification mark downs (Berger

& Ofek, 1995; Lang & Stulz, 1994; Rajan et al., 2000). Diversification would destroy value, because for example it could create incompetent capital markets during overinvestment in underperforming companies or through internal power efforts that generate influence costs. In addition, Divisions' managers who have a future prospect within the company are inspired to persuade a company's top management to assign resources to them (Galvan et al., 2007). Jensen (1996) states that multi-segment firm managers are susceptible to investing any free cash flow to enhance organizational inefficiencies. Other costs of diversifications in literature are also listed, such as losses due to control and effort, coordination costs, and more disadvantages related to an organization with distinctions between companies. Indisputable is that managers of multi-segment companies have more possibilities to carry out projects, and thus more resources as long as diversification eases the constraints demanded by imperfect external capital markets. This can result in them overinvesting their resources. Costs of multi-segment operations also generate costs because it is difficult to design an optimal incentive fee for managers of firms with diversification and because of information asymmetry between central and division managers. Although diversification results in lower financial risk, it increases the business risk because of the different nature and characteristics of the business that has to be driven. Managers might have narrow expertise and are not qualified to manage diverse businesses in a good and efficient way. In addition, unconnected segments could have different operational styles or corporate cultures that are conflicting (Galvan et al., 2007). To summarize, all these factors state that the marginal cost increases fast as diversification grows. Hence, diversification and performance and value are negatively correlated (Galvan et al., 2007). In addition, Elnahas & Kim state in their research of 2017 that more conservative Republican CEOs, which are compared in this paper with dutch right-wing CEOs, have a preference for focus-increasing deals.

If CEOs who are more conservative have indeed a preference for familiar stimuli and are more concerned with good performance, it is expected that they are less likely to engage in risky diversifying acquisitions. Hence, they will choose targets within their own operating industry, leading to the following hypothesis:

H3a: Right-wing CEOs are more likely to acquire targets that are in the same industry.

However, there are also some contradictory theoretical arguments suggesting that diversification can also have value-increasing effects. In the past, much research has been done based on the assumption that diversification and value are positively and linearly related to each other (Gort, 1962). This assumption is mainly driven by the market power theory and arguments about market efficiency (Scherer, 1980). The diversification literature was established on the argument that diversified companies could exploit market power advantages that are unavailable to more focused opponents. Moreover, more diversified companies can benefit from easy access to external funds to capitalize growth of their firm and are also able to transfer funds between businesses within the portfolio. Different efficiencies can be achieved by diversification that are difficult to realize by a single business company (Galvan et al., 2007). Above arguments state that diversification is positively correlated with value and performance. There are more reasons why a firm would diversify. The diversification strategy could result in gains from economies of scale and from increased debt capacity. For example, when risk diversification reduces the risk of a firm, this may be a good sign in context of debt capacity and cost of capital as it allows the company to profit more from tax advantages from increased borrowing (Galvan et al., 2007). One of the most important positive benefits of diversification is the reduction of a company's risk by being involved in multiple businesses in its portfolio. In addition, the increase in market power is established by predatory pricing, future higher prices, and losses that are fixed by cross-subsidization, meaning that the company uses additional revenues from one of their products to support another (Galvan et al., 2007). Managers of diversified companies also have monitoring and information advantages over external capital markets (Weston, 1970; Williamson, 1975). There is more flexibility in the formation of capital as diversified companies can access external sources and also sources that are generated internally. The created internal capital markets allow for a more efficient allocation of resources across firms, which results in considerable financial interests (Galvan et al., 2007).

To conclude, all these arguments state that diversification works as a strategy that creates value. Hence, if conservative CEOs are indeed concerned with better performance, it is also possible they would prefer M&A deals that diversify the company's portfolio to enhance firm value, which leads to the following hypothesis:

H3b: Right-wing CEOs are more likely to acquire targets that are in a different industry.

In the following sections the methodology of the conducted research will be explained and the hypotheses will be tested.

3. DATA & METHODOLOGY

The sample of CEOs is drawn from the COMPUSTAT Executive Compensation (ExecuCOMP) database. The sample captures 138 firms in the Netherlands stock market index between the years 2017 till 2021.

The database gives the full name, title, position, age, gender and CEO tenure for each fiscal year. The political contribution data of the CEOs is obtained manually from news articles and other media sources. Sometimes an assumption had to be made based on expressed interests, goals and values of the CEO and/or the associated company.

The personal and political information of the dutch CEOs is then matched with M&A database. Bloomberg is consulted to obtain data on M&A financing information for finished deals by the companies in the sample. The requirements made for this research are that the acquiring firm obtains at least 51% of the target's shares, and therefore has control. In addition, the deal value needs to exceed 1 million euros. This is necessary, since the acquisitions of smaller targets may not need the interference of the CEO of the acquirer firm in an active manner. Accounting variables on firm level are obtained from the annual reports of the firms in the sample.

To measure the effect of the political preference of the acquirer firm CEOs, a dummy variable is created. The dummy variable takes the value of 1 if the CEO's political preference goes out to right-wing parties, and of zero otherwise, meaning the preference goes out to parties that can be categorized as more politically left or center. This measure does not change during the indicated sample period, because this supports the belief that political identification is formed in the early years of adulthood and will persist afterwards (Green et al., 2002).

To test the first hypothesis, the following probit regression is used:

$$Pr(Y=1 \mid P_{i,t}, X_{i,t}) = G(B0 + B1P_{i,t} + B2age_{i,t} + B3CEOtenure_{i,t} + B4female_{i} + B5TQ_{i,t} + B6size_{i,t} + B7fcf_{i,t} + B8leverage_{i,t} + B9r\&d_{i,t} + B10capex_{i,t} + U_{i,t})$$

Where Y is a dummy variable which takes the value of 1 when the firm interacts in M&A in a given year. P is the measure of political ideology, which takes a value of 1 when the CEO of the firm has a preference for right-wing parties, and zero otherwise. Hence, the dummy takes a value of zero when the CEO of the firm has a preference for parties that can be categorized as politically left or center. X stands for the control variables, which include age, CEO tenure and a gender dummy. In addition some firm-specific variables are taken into account: Tobin's Q as a measure for investment opportunities (Servaes, 1991 and Lang and Stulz, 1994), size (Moeller et al., 2004), free cash flow as a measure of internal resources (Jensen, 1986 and Lang et al., 1991), leverage (Lang et al., 1996 and Lewellen, 1971), R&D (Phillips and Zhdanov, 2013) and capital expenditures (Lang et al., 1996). And lastly, an error term. Definitions of the variables can be found in the attached appendix.

Table 1 presents the summary statistics of the sample. It exhibits the difference between firm- and CEO-specific variables between firms with right-wing CEOs versus firms with left-wing CEOs. Right-wing CEOs (taking a value of 1) versus left-wing CEOs (taking a value of 0).

Summary statistics

N	All (690)	1 (309)	0 (381)
M&A dummy	0.19	0.20	0.18
Firm size	9.19	14.57	5.07
Tobin's Q	3.37	5.70	0.99
Free cash flow	0.05	0.06	0.04
Leverage	2.31	-0.42	4.39
R&D	0.02	0.04	0.01
Capital expenditure	0.03	0.02	0.04
CEO age	53.51	56.68	51.07
CEO Tenure	6.14	7.34	5.21
Gender	0.04	0.03	0.05

To test the second and third hypothesis the following model is used:

$$Pr(Y=1 \mid P_{i,t}, X_{i,t}) = G(B_0 + B_1P_{i,t} + B_2age_{i,t} + B_3CEOtenure_{i,t} + B_4female_i + B_5TQ_{i,t} + B_6size_{i,t} + B_7fcf_{i,t} + B_8leverage_{i,t} + B_9industrycompetition_{i,t} + B_{10}dealvalue_{i,t} + U_{i,t})$$

Where Y is again a dummy variable where 1 signifies, for the second hypothesis, when the CEO uses stock as a payment. For the third hypothesis, Y is a binary variable where 1 implies that the acquirer and target operate in the same industry. Looking at the control variables, different from the first model is that industry competition and deal value are now independent variables of interest. Industry competition is measured using the Herfindahl-index. R&D and capital expenditures are removed as control variables.

4. RESULTS

A regression analysis was conducted to test the proposed hypotheses. To discover whether individual traits of CEOs affect their investment choices, the main empirical analysis investigates the relationship between CEO's political ideology and their firm's investment choices. The CEO's likelihood to engage in M&A was investigated. Furthermore, in case of acquisition, their choices of payment method and deal characteristics (in the same industry vs. diversification) were inspected.

Table 2 reports the results of the probit regressions. Z-values are given in parentheses based on standard errors that are robust to heteroscedasticity and clustered by company and year. The models are predicted with the year and industry fixed effects.
$***$, $**$, and $*$ indicate statistical significance at 1%, 5% and 10% level, respectively. Multicollinearity, meaning that several independent variables in the model are correlated, could be expected since the last two models have a somewhat high pseudo R-squared, but few significant coefficients. To see if there is indeed multicollinearity present, the pairwise correlations are analyzed and the table is included in the appendix. From the pairwise correlations can be concluded that there is no multicollinearity present, since the pairwise correlations are all below 0.8, and there is no need to correct for it.

Variable	(1) M&A	(2) Method of Payment	(3) Focus-increasing
Right-wing CEO dummy	0.0278663	-0.2240358	-0.7186575**
	(0.12)	(-1.08)	(-2.33)
CEO age	0.0109171	-0.0515049	-0.0103893
	(0.93)	(-1.48)	(-0.96)
CEO tenure	0.0264919	0.1056073	0.0465818
	(1.01)	(1.16)	(1.4)
Female dummy	0.000	0.000	0.000
	(0.10)	(0.12)	(0.15)
Size	2.9600061	0.0000239*	-0.0001462***
	(0.57)	(1.94)	(-3.08)
Tobin's Q	0.000	-0.0757007*	0.0014095
	(-0.21)	(-1.72)	(1.62)
Free cash flow	0.000	-0.0006885**	0.0001739**
	(0.17)	(-2.22)	(2.06)
Leverage	0.0014331	-0.0065650	-0.0007087
	(0.42)	(-1.54)	(-0.19)
Capital expenditures	-0.0001313	-	-
	(-0.61)		
R&D expenditures	-0.000038***	-	-
	(-4.43)		
Industry competition	-	0.5871567	0.3016397**
		(1.32)	(2.23)
Deal value	-	0.00032***	0.0146881***
		(5.03)	(3.21)
Constant	-1.605699**	-3.479024*	-2.331283***
	(-2.55)	(-1.80)	(-3.14)
Ind./year fixed effects	Yes	Yes	Yes
Observations	690	690	690
Pseudo R-squared	0.0457	0.3214	0.5016

Referring to the first model, the likelihood of right-wing CEOs engagement in M&A was tested, controlling for the earlier mentioned variables. The effect of right-wing CEOs on M&A frequency appears to be slightly positive. The estimate of the right-wing CEO dummy is 0.028, but is not found to be significant at any confidence level. This finding is not consistent with the first hypothesis. The effect is found positive instead of negative, which was the primary expectation based on the current literature and the proposed hypothesis, saying that more conservative right-wing CEOs are less inclined to engage in M&A deals (Elnahas and Kim, 2017). The result found, according to the positive value of the coefficient, states the opposite, namely that right-wing CEOs are more inclined to engage in M&A deals.

Next, the CEO's choice of payment and preference for diversification vs. focus-increasing are examined. These aspects of acquisition are among the most important determinants of the acquirer's returns (Elnahas & Kim, 2017). The regression shows that right-wing CEOs are less likely to use stock as the method of payment. The estimate of the dummy variable is -0.224. This estimate is not found to be significant. However, the negative direction of the effect is consistent with the hypothesis, supporting the literature saying that choosing cash as the method of payment is consistent with more uncertainty aversion which is displayed by conservative CEOs (Fishman, 1989). In addition, firms with right-wing CEOs tend to have more cash at hand due to better operating performance (Hutton et al., 2014).

Lastly, CEOs' preference for focus-increasing or diversification is tested. The analysis shows that right-wing CEOs are less likely to engage in focus-increasing deals compared to left-wing CEOs. The estimate of the right-wing CEO dummy is -0.719 and is significant at a 5% confidence level, meaning that right-wing CEOs are not deterred by diversification according to the regression. This is not consistent with hypothesis 3a and current literature about possible losses of diversification and more conservative CEOs being more drawn to familiar stimuli. However, this result is consistent with hypothesis 3b and literature about the value-creating properties of diversification and conservative right-wing CEOs being more concerned with better performance.

5. DISCUSSION

The research that was conducted did not provide support for all the proposed hypotheses. Right-wing CEOs were found to be more likely to engage in mergers and acquisition deals compared to left-wing CEOs, although not significant. This result contradicts the first proposed hypothesis. In addition, this result challenges already existing views and literature stating that CEOs who are supporters of parties that have more conservative ideas are less likely to engage in mergers and acquisitions.

This result gives new insight to an existing discovery of Elnahas and Kim in 2017, reporting that conservative Republican CEOs are less likely to engage in mergers and acquisitions than non-Republican CEOs. The conclusion that might be drawn from the conducted research and based on the contradicting founded results is that the American political system and the dutch political system cannot be compared in this area. The American political system is very different compared to the dutch system. In the Netherlands, there are more political parties compared to the United States, where they only focus on Democratic and Republican parties. In addition, the dutch parties are considerably less divided in terms of views, beliefs, values and ideas. Their opinions sometimes overlap considering certain topics. In addition to being progressive and conservative, the political left and the political right can also entail many other characteristic features. All this might explain why the results of the research done do not match the previous literature, since that literature is based on the American system. The role of CEOs' political ideology in M&A activity seems to differ per country and associated political system. Furthermore, this would also explain the low pseudo R-squared of the first model, indicating that the model does not predict the outcome very accurately.

The results show that right-wing CEOs are less likely to use stock as a method of payment than left-wing CEOs. This is consistent with the current literature, however this effect was not found to be significant. Furthermore, right-wing dutch CEOs were found to be significantly more likely to engage in diversifying M&A deals, which is consistent with hypothesis 3b and contradictory with proposed hypothesis 3a and examined linked literature and research of Elnahas & kim in 2017, saying that more conservative Republican CEOs prefer focus-increasing M&A deals. Again this could be the result of the suggestion that the political systems of the two countries are not comparable. Another explanation would be that experiences with M&A deals involving diversification concerning firm value differ per country due to different economic environments. Supporting the belief that diversification can actually be value enhancing and conservative CEOs that are more concerned with better performance are more drawn to this kind of deals.

This research has several limitations. First, political ideology or orientation, as a belief system, has never been an easy target for empirical analysis or quantification. CEOs were assigned to one or the other political ideology based on verbatim expressions, media statements about their ideas and values, and/or the company's core values. However, this method sometimes leads to assumptions and guesses and can also lead to 'black and white' thinking. It does not take into account different spectra of conservatism versus progressivism. For example, someone may identify with a left-wing party, but still adhere to conservative values. Or another scenario, some political values can translate into one domain, while not affecting others. Therefore, a right-wing CEO may identify as more conservative, but his or her ideology may not be strong enough to actually translate into direct activity in the corporate environment.

A second limitation is the sample size. It is very plausible that the number of examined firms could have influenced the results that were realized. Further data collection with the emphasis on distinct political ideologies would be required to further determine how CEOs' political ideology affects corporate activities. To overcome this limitation, firms in the Netherlands stock market index should be investigated beyond the range of the years 2017-2021. This will enhance the validity and reliability of the study executed.

This study makes a theoretical contribution to the corporate activity literature, and is following the phenomen behavioral consistency. This research incorporates the topic of CEOs' political values into the upper echelons theory, which states that demographics and values of top management affect the decisions and practices of companies (Hambrick & Mason, 1984). Among the many studies of upper echelons theory (described in Finkelstein, Canella & Hambrick, 2009), few studies have considered the impact of CEOs' personality (e.g. Peterson et al., 2003) and even less have explored the role of CEOs' values (Simsek et al., 2005). Even within these studies, upper echelons research has only emphasized the characteristics of a top management team of a company as a whole (Lee & Park, 2006; CameloOrdaz, Hernandez-Lara, & Valle-Cabrera, 2005; Bantel & Jackson, 1989; Dwyer, Richard, & Chadwick, 2003). Therefore, this paper's study aims to extend and supplement the existing theory by not treating companies as a single coalition acting collectively. In addition, the dutch political system has not been considered before.

Top management of firms should consider these findings and take them into account when they make investment decisions for the benefit of their firm. It is important to consider the effect of CEOs' political ideology on M&A decisions, since these decisions are one of the most important decisions CEOs make, as they have a significant effect on the wealth of the company’s shareholders. The more complete picture of the decision-making process can drive better corporate choices. Hence, There is much importance in understanding CEOs’ incentives in corporate takeovers since their weight on the wealth of shareholders and on the organization of assets in the economy is enormous.

This research can serve as a base for future studies on executive political ideologies and attitudes and their influence on firm-level investment decisions. The results of this particular study should be validated by a larger sample size. Extensions of this research to other time periods or countries where the importance of politics differs are also valuable topics for forthcoming investigation.

6. CONCLUSION

This research investigates the influence of CEO political ideology on mergers and acquisitions decisions. In particular, following the literature on behavioral consistency, which explains that CEOs’ personal attributes could influence their decisions in the corporate environment (Wernimont and Campbell, 1968). The effect of CEO political ideology, capturing the level of conservatism, on a firm's M&A decisions is examined.

The results of the empirical model suggest that right-wing CEOs are not less likely to engage in M&A activities. However, the effect is not found significant. The analysis also tests the likelihood that right-wing CEOs would choose stock instead of cash as a method of payment. Consistent with the idea of being conservative, it is found that right-wing CEOs are indeed less likely to use stock as a settlement. Again, not a significant result. It is also found that right-wing CEOs are significantly less likely to engage in focus-increasing deals, which is not consistent with earlier argumentation about their preference to remain the status quo and their aversion against the possible losses of diversification. However, it is consistent with the literature suggesting that a diversification strategy is value enhancing and conservative right-wing CEOs being more concerned with better performance. Results are based on a sample of CEOs of dutch firms, considering the dutch political system. One of the most important take-aways from this research is that the political system of the United States probably cannot be compared with the political system of the Netherlands and its effect on the decisions of CEOs considering M&A deals. Based on the current knowledge, the role of CEOs' political ideology in M&A activity seems to differ per country and associated political system.

APPENDIX

1.1 Definitions of variables

Variable	Definition*
Right-wing CEO dummy	Binary variable where 1 signifies that the CEO prefers right-wing political parties
M&A	Binary variable where 1 signifies that a M&A deal has occurred in given year
Stock payment	Binary variable where 1 signifies that he payment is made in stock
Focus-increasing	Binary variable where 1 signifies that the acquirer and the target are operating in the same industry
CEO age	Log of the age of the CEO in the given year
CEO tenure	Log of the number of years the CEO had held current position in a given year within a given firm
Female dummy	Binary variable where 1 signifies that the CEO is female
Size	Log of book value of total assets
Tobin's Q	Market value of assets divided by book value of assets
Free cash flow	Operating income before depreciation – interest expenses – income taxes – capital expenditures, divided by book value of total assets
Leverage	Book value of debts over market value of the total assets
Capital expenditures	Capital expenditures divided by total assets
R&D expenditures	R&D expenditures divided by total assets
Industry competition	Variable is measured by the Herfindahl index
Deal value	Deal value over bidder market value of equity

* Definitions of the variables are based on the paper of Elnahas & Kim of 2017 and used for this research extension.

1.2 Pairwise correlations

	P	*Year*	*TQ*	*Size*	*FCF*	*Leverage*	*RD*	*CAPEX*	*Age*	*Female*	*CEO tenure*	*Industry competition*	*Deal value*
P	1.0000												
Year	-0.0163	1.0000											
TQ	0.1739	-0.0001	1.0000										
Size	0.1696	0.1080	-0.0585	1.0000									
FCF	0.0357	0.1050	-0.0713	-0.0506	1.0000								
Leverage	-0.1102	-0.0297	0.0451	-0.0046	0.0348	1.0000							
RD	0.2028	-0.0006	-0.0358	-0.0080	-0.0204	-0.0236	1.0000						
CAPEX	-0.1276	-0.0026	-0.0463	0.2318	0.3389	-0.0017	-0.0730	1.0000					
Age	0.1871	0.0698	0.0179	0.0949	0.0811	-0.0159	0.1361	-0.0055	1.0000				
Female	-0.0612	0.1443	-0.0240	-0.0351	-0.2493	0.0401	-0.0366	0.3250	-0.0540	1.0000			
CEO tenure	0.1894	0.1660	0.0037	0.0007	-0.0523	-0.0901	0.5179	-0.1963	0.4410	-0.1881	1.0000		
Industry competition	0.2436	0.0000	-0.1727	0.1708	0.1977	0.0288	-0.0595	0.3210	0.2197	0.0581	-0.1657	1.0000	
Deal value	0.1239	0.0601	-0.0314	0.0892	0.0997	0.0387	-0.0192	0.1020	0.0094	-0.0303	0.0518	0.0784	1.0000

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