Managerial Bullshitting and Shareholders' Cognitive Processing Abilities: Evidence from M&As

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Abstract

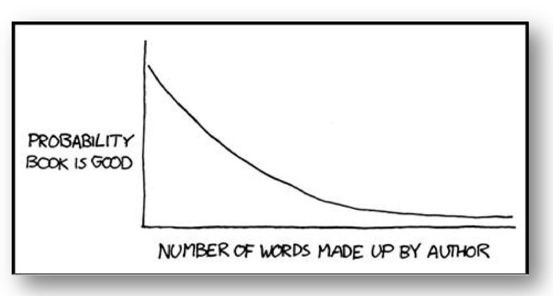
This study examines takeover motives stated by CEOs in press releases and general media. I find that the more motives are claimed by the manager for pursuing M&As, the poorer the transaction. Specifically, managers use special merger rhetoric to whitewash a deal which leads to inferior short- and long-term performance. For example, if a long-short portfolio strategy is applied on single vs. multi-motive bidders, excess returns of approx. 13% can be achieved after five years. Claiming many M&A synergies is linked to a bullshitting behavior and managerial overconfidence to which an average shareholder overreacts. However, institutional investors see the manager's impression management through and correctly incorporate the single vs. multi-M&A information into prices already at deal announcement. If complexities with regard to claimed synergies are reduced, then the average shareholders' behavioral bias of overreaction is decreased. When computational linguistics are applied to objectively quantify M&A synergies, the results are even more significant.

Introduction

Due to practitioners' negative connotations with regard to M&As, the **clear communication** of takeover motives becomes crucial. Not only must managers meet **differing goals** of stakeholders but they must also justify **high premiums** paid for acquisitions.

However, plenty of anecdotal evidence shows that managers do not always clearly convey the intricacies of M&As but:

- *Overblow* the potential of M&As (WSJ, 2005).
- Use specific *merger rhetoric to white-wash* a deal (WSJ, 2005; Sirower & Lipin, 2003).



Literature & RQ

- **"Multiple Objectives = No Objectives"** (Jensen, 2002, 2010)
- **Impression Management: Theory of BS** (Frankfurt, 2005; Merkl-Davies & Brennan, 2007)

This study examines the potential consequences of (over-)stating multiple objectives in the context of M&A. Specifically, it studies the extent to which markets incorporate the information of i) **multi-objective** decisions (quantity of M&A motives) and ii) **"managerial ambiguity"** (quality of M&A motives).

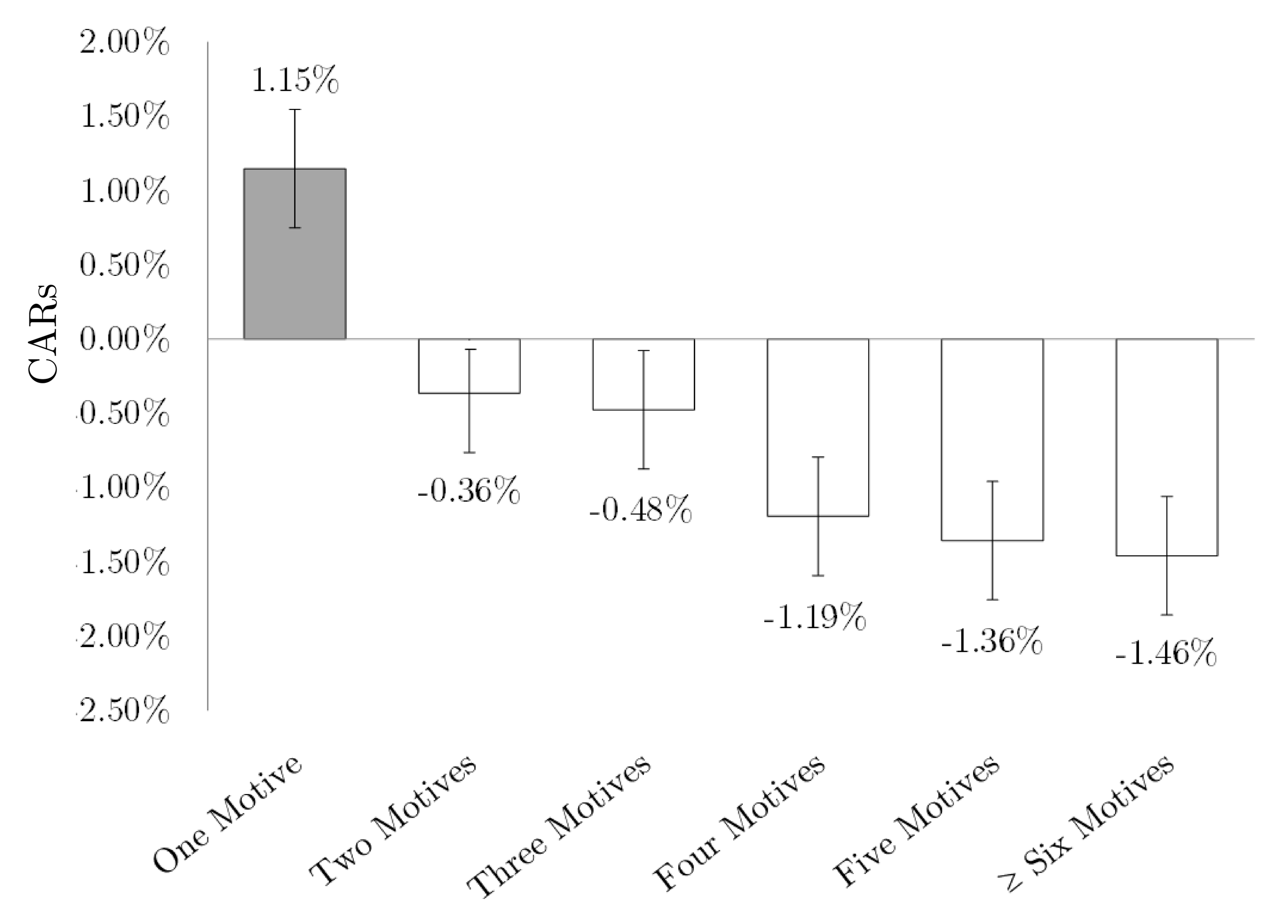
Data & Sample

Sample: 2,118 M&As by 658 S&P 500 firms, from 1983 to 2017.

Data: i) M&A motives, i.e., **qualitative approach**, are derived inductively and deductively; ii) deal-related bullshitting proxies, i.e., **quantitative approach**, using computational linguistics.

Multiple M&A motives are positively correlated to variables that are linked to M&A underperformance: **diversifying** deals, **stock** deals, **crossborder** deals or deals involving **publicly listed** targets, as well as managerial **overconfidence** and **bullshitting** (e.g., Arikan & Stulz, 2016; Bruner, 2004; Kaplan & Weisbach, 1992; Malmendier & Tate, 2015; Shleifer & Vishny, 2003).

Behavioral Manager – Bullshitting Behavior



CARs	(1)	(2)	(3)	(4)	(5)	(6)
Multiple M&A Motives	-0.023***	-0.023***	-0.023***	-0.023***	-0.023***	-0.023***
	(0.003)	(0.003)	(0.003)	(0.003)	(0.003)	(0.003)
Soft Content	0.032					-0.125
	(0.105)					(0.117)
Weak Modal		-0.865**				-0.641
		(0.438)				(0.434)
Modest Modal			-1.047**			-0.969**
			(0.409)			(0.410)
Semantic Ambiguity				-0.000**		-0.000**
				(0.000)		(0.000)
Positive Tone					0.524**	0.607**
					(0.216)	(0.236)
Constant	0.014	0.016	0.022**	0.019*	0.009	0.023**
	(0.010)	(0.010)	(0.010)	(0.010)	(0.010)	(0.011)
No. of obs.	1,799	1,799	1,799	1,799	1,799	1,799
Industry & Year FE & Controls	Yes	Yes	Yes	Yes	Yes	Yes

Robust standard errors in parentheses, *** p<0.01, ** p<0.05, * p<0.1

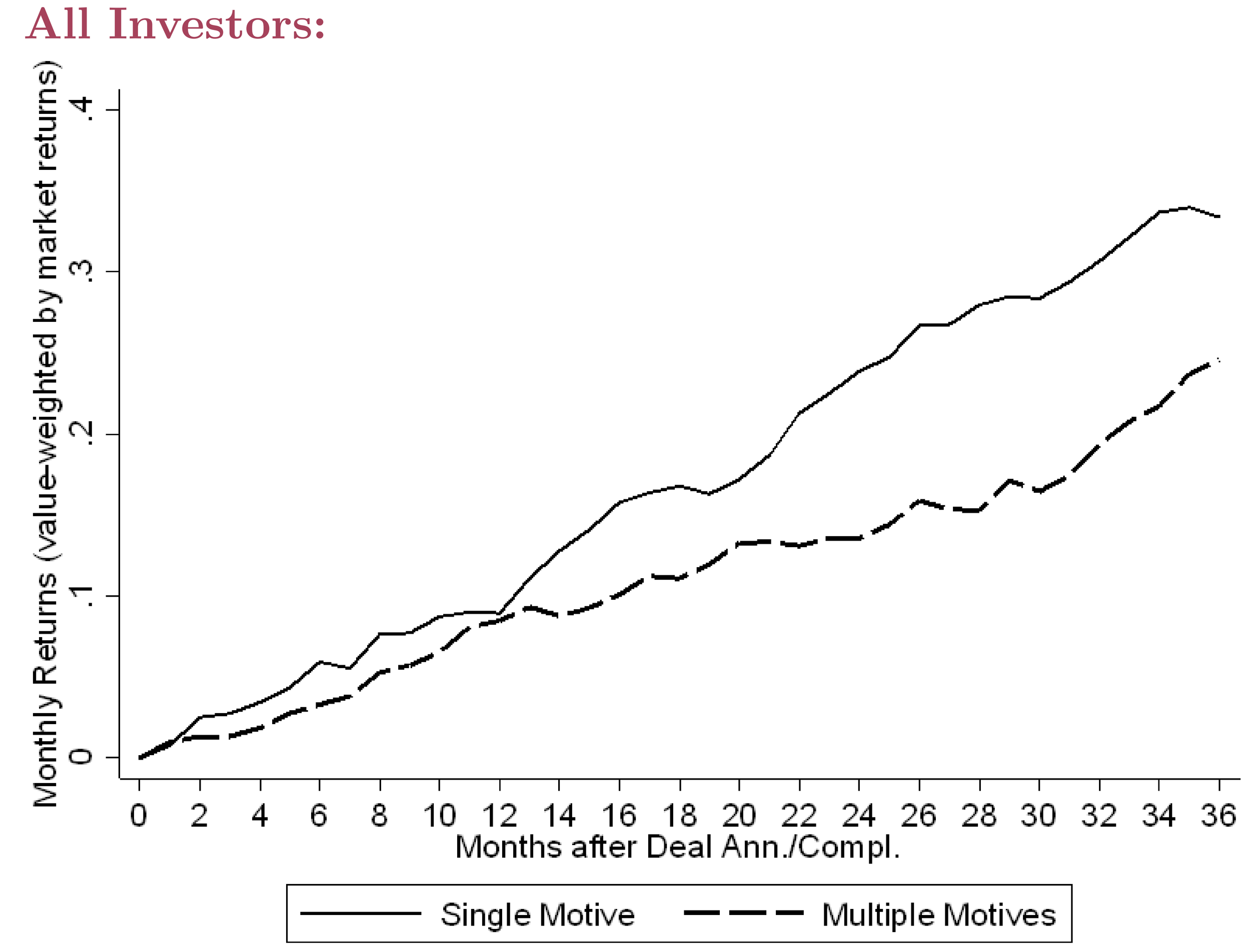
Proxies are computed to capture bullshitting content on approx. 40,000 texts covering the sample deals. **Bullshitting rhetoric** is positively **correlated** with claiming **multiple M&A motives**. Despite severe bullshitting rhetoric accompanying a deal, **multiple** M&A motives **underperform single** motive acquisitions.

Results

Single motive deals exhibit **significantly higher** acquirer announcement returns than acquisitions with **multiple** motives. Also, the more synergies are stated, the lower the respective CARs at M&A announcement. The results remain similar if I include **fixed** effects (time, industry) and control for **deal**, **acquirer**, and **target characteristics** as well as if different **estimation**, **event windows** or if **combined CARs** are applied.

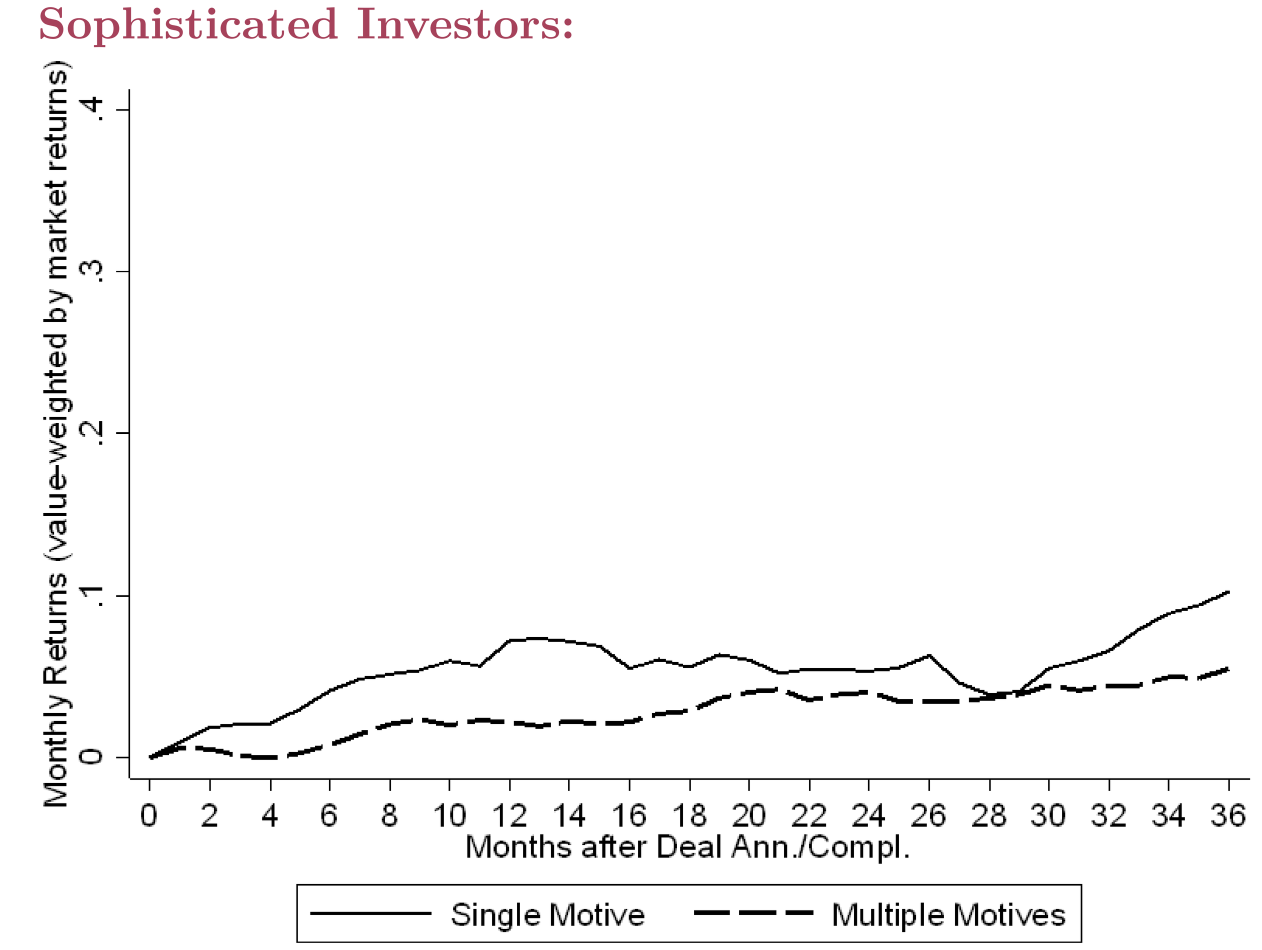
Behavioral Shareholder – Limited Processing Capability

All Investors:



Single motive M&As outperform multiple motive deals, with the **outperformance** increasing over time. Investors initially **underreact** to M&As, however, more so for single motive acquisitions. The results support a behavioral hypothesis, where investors exhibit **bounded rationality** and fail to incorporate the public information at deal announcement.

Sophisticated Investors:



No significant difference is observed between single vs. multi-motive M&As over time, implying that information with regard to deals is already **fully incorporated** in the price at acquisition announcement by **sophisticated investors**. Returns **do not increase** with time, hence, for deals with high **institutional ownership**, investors do not constantly adjust their expectations.

Results

The results stemming from claiming single vs. multiple motives is driven by boundedly rational **"noise traders"**, who are not able to process information revealed by firms at acquisition. In contrast, **sophisticated investors** do not largely overestimate or underestimate single vs. multi-motive deals but at the same time cannot arbitrage away the mispricing. Results remain similar if BHARs are calculated after **deal completion.**

Robustness

A **behavioral shareholder explanation** is further supported by studying subsamples for which arbitrage is easier: large transactions and deals in which complexities are reduced through, e.g., clearer goals as well as autonomous integration of targets.

Further, **alternative rational explanations** are considered by implementing an event-time long-short portfolio strategy controlling for **systematic risk**. Sorting **value-weighted** avg. monthly returns on multiple motives, excess returns of 17.64% can be achieved. Hence, risk-based considerations cannot explain the difference, which provides support for a **behavioral view**.

Results are **not driven** by the **synergy type** as the coefficient of multiple M&A motives remains **negative** for revenue, cost, size, and financial synergies.

To address **simultaneous causality**, a placebo test is performed: todays' CARs are regressed on tomorrows' words and vice versa. Results imply that it is the **firm** that **influences** stock **prices**.

Conclusion

Shareholders respond **negatively** to **multi-motive** deals in the short and long-term. For example, M&As that are accompanied with many synergy claims are associated with a significant decrease in announcement CARs. At the same time, multi-motive acquirers are more likely to be taken over themselves. Further, **underperformance of M&As** is **fortified** when bullshitting rhetoric, e.g., vague language, is used by managers, which is linked to **overconfidence**.

The average shareholder **underreacts** to **multi-motive** deals and more so to **single** synergy M&As. More **sophisticated investors** incorporate the **expected value** of the claimed synergies already at deal announcement, implying that they see the firm's **bullshitting** behavior through. However, they are not able to fully **arbitrage** away the **mispricing**.

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