
ACQUISITION PROPENSITY IN FAMILY FIRMS: THE MULTIFACETED ROLE OF FAMILY INVOLVEMENT

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Abstract

Building on behavioral agency theory, we explore the role played by corporate governance characteristics of family firms in affecting their acquisition propensity. Specifically, we investigate family members' ownership stake and their appointment to the board of directors as predictors of the likelihood to execute acquisitions. Furthermore, we explore the effect of having a family chief executive officer (CEO) and the generational step. Using a sample of 207 acquisitions executed by 93 Italian listed family firms in the 2014–2020 period, we find evidence that the extent of family ownership does not affect acquisitions propensity. Additionally, while family members on the board are negatively associated with acquisitions, the opposite emerges in case of a family CEO. Finally, the propensity to acquire does not appear to be driven by whether the firm is still in its founding generation or later generations.

1. INTRODUCTION

The relationship between corporate governance and risk preferences shows particular characteristics in the context of family firms, as decision-making is guided by long-term, often non-financial, objectives and the preservation of the firm's socio-emotional endowment

(Gómez-Mejía, Haynes, Núñez-Nickel, Jacobson, & Moyano-Fuentes, 2007). In this sense, the acquisition decision is especially important and risky for family firms as it carries substantial implications in terms of potential gains and losses in socioemotional wealth (Hussinger & Issah, 2019). Given these controversial pressures, the role played by family ownership and family involvement in guiding acquisition decisions has provided mixed findings and thus offers room for further exploration. This study, therefore, focuses on how family firms' characteristics drive their propensity to acquire.

2. LITERATURE REVIEW AND HYPOTHESES DEVELOPMENT

The involvement of family members in the business directly affects decision-making at multiple levels (Zahra, 2005). The corporate risk profile in family firms may actually be the result of corporate governance characteristics in the executive bodies rather than the mere ownership. Indeed, while family ownership may play an important role in a family vs non-family context, it may be less significant within a family context: family firms, although differing in terms of percentage of family ownership, share to some extent the common condition of being owned by a family and thus are all guided by socioemotional considerations, which thus makes family ownership a less significant driver of family firms' heterogeneity in decision-making. Building on this, we posit the following hypothesis:

H1: Family ownership stake is a non-significant predictor of the likelihood that a family firm will execute an acquisition.

Building on the prior logic, we believe that the board characteristics in terms of family involvement on the board and the presence of a family CEO may be more significant drivers of a family firm's propensity to embark on risky projects such as corporate acquisitions in view of their peculiar roles in terms of active involvement in decision-making. Several studies have suggested that the board characteristics play an important role in shaping family firms' risk profiles. Insiders' risk-taking is driven by several, different factors, such as their total wealth portfolios, pecuniary and non-pecuniary benefits and the potential for entrenchment (Wright, Ferris, Sarin, & Awasthi, 1996). Thus, the appointment of family owners to the board of directors affects the risk faced by firms, driving managers towards risk levels aligned with owners' preferences (Sullivan & Spong, 1998).

Although extant literature suggests that the family component among board members is a characterizing feature relative to other non-family board members (Wilson, Wright, & Scholes, 2013), the current investigation of family members' involvement in the board of directors still offers extensive room for further exploitation (Nordqvist, Marzano, Brenes, Jiménez, & Fonseca-Parades, 2011).

Because family directors mainly focus on maintaining a trade-off between business and family objectives, we hypothesize that greater involvement of family members sitting on the board will be associated with a greater risk aversion in order to preserve the firm socio-emotional endowment. In turn, this implies that a greater presence of family executives will reduce the likelihood that the firm will execute risky investment projects such as corporate acquisitions. We thus posit that:

H2: An increasing family involvement in the board is negatively associated with the likelihood that a family firm will execute an acquisition.

According to the behavioral agency model, family CEOs are willing to take greater risks in order to prevent possible wealth losses and rather avoid risk-taking whenever they need to minimize wealth losses (Larraza-Kintana, Wiseman, Gómez-Mejía, & Welbourne, 2007; Wiseman & Gómez-Mejía, 1998). Thus, the literature seems to suggest that CEOs actually have heterogeneous risk preferences based on their perception of wealth increase vs decrease (Wiseman & Gómez-Mejía, 1998; Martin, Gómez-Mejía, & Wiseman, 2013).

The CEO's propensity to commit resources, exploit opportunities, and engage in corporate investments with uncertain outcomes is, therefore, a particularly important dimension shaping the overall risk profile of the firm. Because of the substantial benefits that CEOs may derive from corporate acquisitions in terms of company empire building, power, and compensation, their propensity to execute acquisitions may be particularly strong in the context of family firms.

We, therefore, formulate the following hypothesis:

H3: A family CEO is positively associated with the likelihood that a family firm will execute an acquisition.

Another element that may shape the willingness of a family firm to commit substantial resources to risky projects such as acquisitions is the transgenerational outlook that uniquely characterizes family-controlled firms. The ability to create value across generations in terms of both financial results and strategic continuity is a primary concern in family firms (Habbershon, Nordqvist, & Zellweger, 2010).

We argue that the generation of the family firm may also have substantial implications in terms of risk-taking vs risk aversion in corporate decisions. In particular, because of their willingness to preserve the firm's longevity and the family control, we suggest that the founding generation may be more risk-averse relative to later generations. Later generations, indeed, may be less cautious when deciding upon the firm's socioemotional capital. We thus hypothesize the following:

H4: The founding generation is negatively associated with the likelihood that a family firm will execute an acquisition.

3. METHODOLOGY AND SAMPLE

Our hypotheses are tested on a sample of 207 acquisitions executed by 93 Italian family listed companies from 2014 to 2020. Data on the deals were collected from Zephyr, a comprehensive database on M&A produced by Bureau Van Dijk.

Our observations include both acquisitions for capital increase, i.e., where the acquirer already owned prior stakes in the target company, and pure acquisitions, where, on the contrary, the acquirer does not own any prior stake in the target firm.

4. RESULTS

Results are shown in Table 1. In line with our *H1*, the percentage of family ownership does not seem to influence the acquisition behavior, confirming prior literature (Miller, Le Breton-Miller, & Lester, 2010). The findings also indicate a negative impact of family governance on the propensity to acquire; in particular, the presence of family members sitting on the board of directors has a negative effect on acquisition propensity ($\beta = -0.32$, p-value < 0.05). Thus, *H2* is supported and confirms that the higher the family involvement in the decision-making body, the greater the firm's risk aversion. *H3* on the positive effect of a family CEO on the propensity to acquire is also supported ($\beta = 0.08$, p-value < 0.01). Our *H3* on the positive effect of the family on acquisition propensity is also supported ($\beta = 0.08$, p-value < 0.001). Finally, our results do not provide support for our *H4* exploring the role played by the family generation: the variable capturing the generational step is not significant; however, it is worth noting that the sign of the coefficient mirrors the expected direction.

Table 1. Regression results

<i>Independent variables</i>	<i>Model 1: Only controls</i>	<i>Model 2: Full model</i>
<i>Family ownership</i>		0.18 (0.22)
<i>Family involvement in the board</i>		-0.32(0.40)**
<i>Family CEO</i>		0.08 (0.04)***
<i>First generation family</i>		-0.01(0.78)
<i>Leverage</i>	0.26 (0.06)**	0.25 (0.11)**
<i>Firm size</i>	0.13 (0.01)**	0.01 (0.47)**
<i>Diversification</i>	1.38 (0.05)**	1.15(0.00)**
<i>Domestic deals</i>	-0.63 (0.07)**	-0.83(0.04)**
<i>Manufacturing</i>	0.01(0.04)	-0.01(0.75)
Year dummies	Included	Included
Number of obs.	207	207
R ²	0.59	0.60

Note: Dependent variable: acquisition propensity. Standard errors are reported in brackets. Significance codes: * p-value < 0.1, ** p-value < 0.05, *** p-value < 0.01, **** p-value < 0.001.

5. DISCUSSION AND CONCLUSION

The conceptual framework of this study suggests that while family ownership may be an important predictor of corporate decisions in a family vs. non-family research context when focusing on family firms, the extent of family ownership may actually be a less valuable driver of the firm's corporate risk-taking. Rather, since decision-making takes place in executive bodies, the family involvement in the board and the family CEO may be stronger predictors of the family firm's propensity to embark on risky projects such as a corporate acquisition. This study provides intriguing findings on the contrasting effects of such variables. Indeed, while the family involvement in the board intensifies the firm's risk aversion, which confirms the socio-emotional wealth paradigm, the presence of a family CEO points in the opposite direction. This may actually be consistent with a behavioral agency model, as the potential gains prospects in terms of reputation and compensation implied in a corporate acquisition may substantially encourage the family CEO to embark on such a project.

Although our results do not show statistical significance for the variable capturing the firm's generational step, we believe that the willingness to take on risks and to commit resources to investment projects may be substantially affected by whether the firm is controlled by the founding vs later generations. To the best of our knowledge, this is the first study to incorporate the role played by generational control in affecting corporate risk-taking in family firms. Thus, future research might explore whether the transgenerational dimension may drive corporate-level decisions.

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