



# Do progressive social norms affect economic outcomes? Evidence from corporate takeovers<sup>☆</sup>



Yangyang Chen<sup>a,\*</sup>, Edward J. Podolski<sup>b</sup>, S. Ghon Rhee<sup>c,e</sup>, Madhu Veeraraghavan<sup>d</sup>

<sup>a</sup> The Hong Kong Polytechnic University, Hong Kong

<sup>b</sup> Deakin University, Australia

<sup>c</sup> University of Hawaii, United States

<sup>d</sup> T.A. Pai Management Institute, India

<sup>e</sup> Monash University, Australia

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## ABSTRACT

This paper investigates how religion-induced attitudes toward change and diversity affect corporate acquisition decisions. By studying the variation in religious adherence across U.S. counties, we find that acquirer announcement returns and total synergy are larger in counties in which progressive religious denominations are popular. In contrast, conservative religious denominations affect neither acquirer announcement returns nor total synergies. Our evidence indicates that religion-induced social norms are an important driver of large corporate transactions, while various religious denominations affect corporate outcomes differently.

## 1. Introduction

The United States is diverse in terms of its religious composition and the geographic distribution of religious groups. This religious diversity can have tangible consequences for the way corporate decisions are made. Ultimately, corporations are not detached from their local environment, but rather interact with their surroundings through their employees, local customers, and local suppliers (Gao et al., 2011). Consistent with this intuition, prior research has demonstrated that religious diversity has significant implications for local firms. For example, Hilary and Hui (2009) find that the level of religiosity surrounding the firm's headquarters influences corporate policies by reducing executives' appetite for risk, while Callen and Fang (2015) show that firms headquartered in counties with high levels of religiosity exhibit lower managerial bad-news-hoarding activities, which results in lower stock price crash risk.

Motivated by prior literature on the importance of geographic religious heterogeneity across the U.S. in economic outcomes, we examine how religion-induced attitudes affect corporate merger and acquisition outcomes. Our study differs from prior literature

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\* Correspondence to: M743, Li Ka Shing Tower, The Hong Kong Polytechnic University, Kowloon, Hong Kong.

E-mail addresses: [yangyang.chen@polyu.edu.hk](mailto:yangyang.chen@polyu.edu.hk) (Y. Chen), [edward.podolski@deakin.edu.au](mailto:edward.podolski@deakin.edu.au) (E.J. Podolski), [rheesg@hawaii.edu](mailto:rheesg@hawaii.edu) (S.G. Rhee), [madhuveeraraghavan@tapmi.edu.in](mailto:madhuveeraraghavan@tapmi.edu.in) (M. Veeraraghavan).

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(e.g., Hilary and Hui, 2009; Callen and Fang, 2015) in that we focus on a specific religious denomination – Mainline Protestants – instead of regarding all religious denominations as a homogeneous group. Mainline Protestants differ from other religious denominations in terms of attitudes towards change and diversity (i.e., progressive attitudes). Since acquirers' attitudes towards change and diversity are essential to the takeover process, we examine whether acquirers located in areas with a high proportion of Mainline Protestants are better able to integrate with the target and realize synergies. Our empirical findings show that acquirer announcement returns and total synergy gains are higher for acquirers located in areas with a high proportion of Mainline Protestants, and there is no such effect for other religious denominations. The findings provide supporting evidence of our argument and highlight the unique impact of the religious social norms associated with Mainline Protestants on economic outcomes.

Religion plays an important role in shaping the behavioral preferences of individuals and societies.<sup>1</sup> Indeed, the existing literature identifies attitudes towards change and diversity as one of the most important distinguishing factors between various religious groups (Jelen and Wilcox, 1990; Tamney and Johnson, 1997; Reimer and Park, 2001; Tuntiya, 2005). Among the three major Christian denominations (i.e., Catholics, Mainline Protestants, and Evangelical Protestants), Mainline Protestants hold considerably more liberal views of the world (e.g., interpretation of the Bible and ways to salvation), which makes them less conservative and more tolerant of different views (Beatty and Walter, 1984; Hunter, 1984; Jelen and Wilcox, 1990). Since local attitudes toward change and diversity are closely related to religious norms in the local area, we argue that people in areas with a greater proportion of Mainline Protestants tend to be more progressive, tolerant and open to new ways of doing business.

The success of corporate mergers and acquisitions relies on synergies realized in integrating the assets between the acquirer and the target. Numerous studies show that organizational flexibility, collaboration with the target, and learning from the target are key elements of realizing synergies (Malekzadeh and Nahavandi, 1990; Zollo and Singh, 2004; Datta, 2006; Thach and Nyman, 2001). Firms located in areas in which progressive and tolerant views are more pronounced have internal cultures that are more open to change. Since openness to change helps the acquirer to nourish and integrate the strengths of the target to realize synergies, it is regarded as an essential element of successful mergers and acquisitions (Malekzadeh and Nahavandi, 1990; Thach and Nyman, 2001; Zollo and Singh, 2004; Datta, 2006). Further, progressive culture is able to reduce conflicts and the associated transaction costs in merger and acquisition deals such as excess employee turnover and lower-level agency problems, which leads to more synergies. Therefore, we argue that firms located in areas with proportionally higher Mainline Protestant adherences are better acquirers in that they have higher announcement returns of takeover deals and realize greater synergy gains in the takeover process.

Our core argument is that social norms pertaining to tolerance and change are relevant for takeover outcomes because these social norms will systematically influence the attitudes of employees at all levels of the organization. Since the willingness with which employees below the executive levels embrace change and diversity is vital to takeover success, we expect the positive influence of Mainline Protestant adherence on takeover returns to be stronger amongst labor-intensive firms. At the same time, we expect that powerful CEOs, who are in a better position to instill their individual attitudes on their employees, to reduce the effect that Mainline Protestant adherence has on takeover outcomes.

We collect a large sample of publicly listed acquirers. We calculate the ratio of Mainline Protestant adherents to the total population of the county in which each acquirer is headquartered. Since stock prices are expected to reflect the market perception of the synergies that the acquirer will successfully realize, we relate the acquirer's Mainline Protestant ratio with the announcement returns over a five-day period. Consistent with our *ex ante* expectation, we find a strong positive relation between the Mainline Protestant ratio and announcement returns. The results are robust to alternate measures of announcement returns, the inclusion of a large set of control variables, and correcting for data truncation issues using Heckman's (1979) methodology. More significantly, we find that our results remain unchanged when we control for the religion-induced norms surrounding the target firm's headquarters. This result suggests that the acquiring firm employees' attitudes towards change and diversity influence takeover outcomes, independent of the attitudes of the target firm.

In further analysis, we examine how labor intensity and CEO characteristics influence the relation between Mainline Protestant adherence and takeover outcomes. We find that religion-induced social norms have a greater effect on announcement returns amongst labor-intensive firms. This result is consistent with the idea that religion-induced local norms are important for takeover outcomes because employees below the executive level are important for generating synergy gains. However, we find no evidence that CEO characteristics, such as CEO ability and overconfidence (Demerjian et al., 2012; Malmendier and Tate, 2008), influence the effect that religion-induced progressive social norms have on takeover outcomes. However, we find that social norms have a weaker effect on announcement returns amongst CEO-centric firms (i.e., firms with powerful CEOs), suggesting that powerful CEOs have a stronger influence on the internal culture within firms, thus making such firms less susceptible to local social norms. Although the presence of these powerful CEOs can mitigate the benefits associated with progressive social norms, their presence can also overcome the disadvantage associated with conservative social norms.

In the final set of tests, we directly examine whether the positive association between Mainline Protestant populations and acquirer announcement returns is due to improved synergy creation or whether higher acquirer returns are due to the ability of acquirers located in high Mainline Protestant areas to expropriate a greater portion of synergy gains for their own shareholders. Our results strongly support the notion that more positive attitudes towards change and diversity facilitate greater synergy creation. Mainline Protestant populations are positively associated with premiums paid to the target and overall synergy creation. In contrast, we find no evidence that Mainline Protestant populations are related with greater synergy extraction by the acquirer. In sum, our results suggest that progressive religion-induced social norms are economically beneficial in the takeover process.

<sup>1</sup> See Iannaccone (1998) for a review.

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