Chapter 8
Governance Practices and CEO Hubris:
An Italian Banking Case

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ABSTRACT

This chapter analyzes the connection between CEO hubris and corporate governance contingencies, including a case study of an Italian bank for which the state of financial distress shall be linkable also to bad governance. The main objective is to verify whether, in presence of hubristic CEO, the internal control mechanisms, set to ensure the board vigilance and limit the overconfidence of the leader, are implemented, and if so, whether such mechanisms, even when formally respected, may be not so appropriate to guarantee a good governance. Particularly, the existence of a CEO hubris could neutralize their positive expected balancing effects on the power dynamics between CEO and board, such as to give prevalence to substance over form. Therefore, it may occur that some governance mechanisms (e.g., independence, non-duality), even if formally implemented, are unable to stem the managerial entrenchment of the CEO, who succeeds in enhancing immoderately his substantial power in the decision-making process.

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INTRODUCTION

The many calls for banks' sound internal governance as one of the fundamental drivers for achieving institutions stability underline the relevance of corporate governance issues, which recently receive increased attention from scholars as well as international authorities (e.g., EBA, 2017). In the wake of such scenario of growing interest, and considering the various perspectives of analysis of corporate governance of banks, the authors decided to focus their attention on the CEO psychological pattern attributable to hubris, trying to understand whether such pattern could enable the CEO to strengthen immoderately his power, thereby weakening the effectiveness of board vigilance mechanisms, set to contribute to the protection of the decision process from a CEO hubris, and, ultimately, to a sound and prudent management.

The concept of hubris, defined originally by studies in mythology as the disproportionate, blind and arrogant presumption of man in the face of the unsurpassable limits decreed by the gods (Cantarella, 2002; Cerinotti, 2018; Cipolla, 2011; Graves, 2014), has been progressively extended to other disciplines, such as the economic and financial one (Hayward & Hambrick, 1997; Malmendier & Tate, 2008; Roll, 1986). Within the latter line of research and focusing particularly on the connection with the role of the CEO, the existing literature (Brennan & Conroy, 2013; Petit & Bollaert, 2012) identifies the presuppositions of hubris, on one side, with overconfidence together with narcissism, and on the other side, with CEO substantial power. It becomes therefore crucial to understand the essence of hubris from a strictly managerial perspective, and whether it could negatively affect the managerial procedures, among which the governance practices cover a role of primary importance.

In order to give a contribution to this debate, this study analyzes the complex question of hubris, in terms of definition and conceptualization (e.g., it is almost frequent the overlapping with overconfidence and narcissism), as well as in connection with some corporate governance contingencies (e.g., independence of directors, non-duality, ownership). Then, the authors examine such issues considering a case study of an Italian bank for which the financial distress may be linkable also to its inadequate governance. The focus on the banking sector is explained in the light of the above-mentioned interest for internal governance matters, currently increasing also in response to the global financial crisis. Additionally, the limited number of studies on CEO hubris within the banking sector (Brennan & Conroy, 2013; Lawrence et al., 2011; Wray, 2016) calls for further investigation, in respect of which this study intends give a contribution. Particularly, the case study undertakes to verify the existence of hubristic traits in the CEO of an Italian bank, in order to answer the research question: "Is there evidence of CEO hubris?". Secondly, it attempts to examine the presence of board vigilance mechanisms, that literature suggests as