

РАЗДЕЛ 2
СТРУКТУРА СОБСТВЕННОСТИ

SECTION 2
OWNERSHIP STRUCTURE



MARKET BASED PERFORMANCE: DO OWNERSHIP
STRUCTURES, OR FIRM POLICY CHOICE MATTER?

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Abstract

This study examines whether the structure of share ownership or firm's dividend and debt policies provide explanation for firm performances in Malaysia. Firm performance, measured as Tobin's Q is modelled in a dynamic panel framework to estimate effects of director ownership, family ownership, foreign ownership, and firm's dividend and debt policy. The generalised methods of moments (GMM) method is used to estimate the models for 80 CI components companies listed on Main Board of Malaysia observed from 1999 to 2002. The findings reveal strong evidence of positive impact of firm's dividend and debt policy on firm performance. However, ownership structure seems to be less important for market based performance of Malaysian firms. These results are expected to provide guidelines to the investors regarding the significance of firm dividend policy, leverage policy and market to book value ratio as some of the key sources of value creation for Malaysian listed firms.

Keywords: ownership concentration, dividend and debt policies, dynamic panel

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1. Introduction

There seems to be an ongoing puzzle as to whether ownership structure (directors, family and foreign ownership concentration) or firm policy choice (dividends and debt level) play an important role in determining firm performances. Firm's dividend policy and choice of leverage as a source of funding of firm's business activities are some of the most widely researched topics in empirical finance. Yet researchers have different views about whether the ownership structure or firm's policy choices primarily contribute towards firm performance. The earlier

studies on these issues attempted to link firm performance or profitability with three important aspects namely: corporate governance (Gugler et al., 2002), corporate ownership, and corporate debt and dividend policy. However, none of the previous studies in Malaysia attempted to develop and test hypothesis as to whether ownership or policy choice is an important determinant of market based firm performance using dynamic panel data. The present study builds on this line of research and examines firstly, the dynamic relationship between ownership structure presented by (family ownership concentration, foreign ownership and director's

ownership) and firm value measured by Tobin's Q (TQ), and secondly, the relationship between firm's choice of policy on level of dividend and leverage in proportion to asset and firm performance. The Malaysian capital market is a fast growing sector with improved regulatory standards and diverse equity ownership observed among listed firm particularly after the Asian financial crisis.

The rest of the paper is organized as follows: Section Two discusses the theoretical and empirical literature that provides a framework that explains how ownership structure and firm policy on dividend and debt provide useful explanation for firm performance. Section Three briefly describes data and methodology highlighting the dynamic panel approach to estimation. Section Four presents the findings of the study and section Five concludes.

2. Empirical Overview

The theoretical and empirical work of Berle and Means (1932) and (Jensen and Meckling, 1976) highlight the importance of corporate governance at the presence of the conflict of interest between shareholders and managers. Ownership concentration (ensuring better monitoring), and managerial equity holdings (increasing managerial effort and decreasing perquisite consumption), were supposed to lead to better firm performance.

There has been a good body of literature on the effects of ownership on firm performance (Morck et al. 1988; McConnell and Servaes 1990; Hermalin and Weisbach 1991; Himmelberg et al., 1999). Important empirical literature examining this prediction mainly focused on the relationship between managerial ownership and firm value. Stulz (1988) predicted a concave relationship between managerial ownership and firm performance. Morck et al. (1988), McConnell and Servaes (1990), Hermalin and Weisbach (1991) and Holderness et al. (1999) found that at lower levels of managerial ownership, firm value tends to increase, while at higher levels of managerial ownership firm value tends to decline. These results were interpreted as the evidence of managerial entrenchment. Other studies showed that dispersed shareholdings are much less frequent than expected and a high degree of ownership concentration is observed instead (La Porta et al., 1999; Becht and Roell, 1999). This trend raises concerns among investors about the possible expropriation of the minority investors by the controlling owners (Johnson et al., 2000, Faccio and Lang, 2002; Lehman and Weigand, 2000).

Several papers also explored empirically the impact of ownership structure on firm performance taking into account endogeneity of ownership. Demsetz and Lehn (1985), Loderer and Martin (1997) and Cho (1998) estimated an equation system and found no significant relationship between ownership

structure and performance. Using firm fixed effects to control for unobserved heterogeneity, Himmelberg et al. (1999) also found no significant relationship and concluded that shareholders choose ownership structure optimally.

In a related study, Kuznetsov and Muravyev (2001) argue that concentrated ownership has its costs when large shareholders, capable to influence corporate decision directly, maximize value for themselves and deprive small owners of their part of residual income. Other negative consequences of ownership include raised cost of capital due to lower market liquidity or reduced diversification opportunities on the part of the investors (Fama and Jensen, 1983a, 1983b) and prevention of additional monitoring of managers by the stock market available under diffused ownership with high liquidity of shares (Holmstrom and Tirole, 1993). La Porta et al. (1999), Claessens et al. (2000) and Faccio and Lang (2002) found that publicly traded companies in most countries possess a higher level of ownership concentration. Dzierzowski and Tamowicz (2004) for Poland and Cheema et al. (2003) for Pakistan found that the companies' shares are commonly concentrated in the hands of the largest shareholders.

The literature on dividend policy has been dominated by Miller and Modigliani's (1961) classic dividend irrelevance proposition which was later endorsed by Black and Scholes (1974) and Miller and Scholes (1978). However, a number of other researchers did not lend a support to the proposition (Long, 1978). In addition, survey research by Farrelly et al. (1986) showed that corporate managers typically believe that dividend policy affects a firm's value and that an optimal level of dividend payout exists. In reality, most firms pay cash dividends to signal about future prospect of the firm profitability, although paying dividends is costly in many ways. Thus, empirical evidence on whether dividend policy affects a firm's value offers contradictory guideline to corporate managers. Hence there is no conclusive evidence as to the existence of a particular choice of dividend payment pattern.

The literature on firm leverage affecting firm performance has been voluminous.⁴⁹ Agency theory suggests that the choice of capital structure may help mitigate the agency costs. It also predicts that leverage reduces the agency costs of outside equity holders and increases firm value by constraining or encouraging managers to act more in the interests of the shareholders. But the issue remains unresolved particularly in developing economies. A number of other studies on the choice of leverage provide extended explanation for firm performance particularly through assessing firm's TQ (Harris and Raviv, 1991 and Myers, 2001). Greater financial

⁴⁹ See the survey papers by Harris and Raviv (1991) and Myers (2001).

leverage may affect managerial use of discretion in undertaking risky investment activities, thereby reducing agency costs through the threat of liquidation. The choice of higher level of leverage also exerts continuous pressure on management to maintain greater level of liquidity by generating sufficient cash flow to pay interest expenses (e.g., Jensen 1986).

3. Methodology and Data

Theoretical Model

Many relationships involving economic and financial variables are dynamic in nature. For a newly industrialised country such as Malaysia with firms registering significant structural change and growth in terms of scale, scope, ownership and policies; we expect a dynamic model to accurately portray the relationships among the variables in a longitudinal perspective. Hence, we adopt a dynamic panel data model for this study. One of the advantages of the panel data is that they allow the researchers to better understand the dynamics of adjustment (Baltagi, 2005). Balestra and Nerlove (1966) developed a model for dynamic panel data, which has been widely used in empirical econometrics.⁵⁰ These dynamic relationships are characterized by the inclusion of a lagged dependent variable among the regressors. In other words, the model is developed with a first order autoregressive component, i.e., with a one-period lag of the dependent variable. For the i -th firm in the t -th period. The general form of the model is,

$$Y_{it} = \delta Y_{i,t-1} + X'_{it}\beta + v_{it} \quad (1)$$

Where δ is a scalar, X'_{it} is a $1 \times k$ matrix of regressors and β is a $k \times 1$ vector of parameters.⁵¹

Note that the dynamic panel data model is characterised by two sources of persistence over time. The first is autocorrelation due to the lagged dependent variables among the regressors. The second source is the variants of the individual effects characterizing the heterogeneity among the individuals or firms, in this case.

⁵⁰ Also see Holtz-Eakin (1988), Blundell et al. (1992) and Islam (1995).

⁵¹ We assume that v_{it} follow a one-way error correction

model such that, $v_{it} = \mu_i + u_{it}$ where $\mu_i \sim iid(0, \sigma_\mu^2)$ and $u_{it} \sim iid(0, \sigma_u^2)$.

Dynamic Panel Data Model for Tobin's Q

We develop a dynamic model for panel data to examine effects of ownership structure and policies on firm's performances. TQ, which shows a firm's value relative to its replacement costs, has been widely used for assessing firm performances. The empirical appeal of the Q model stems from a simple relationship between the ratio of shadow value to price (marginal Q), and the observable ratio of market valuation to replacement cost value of capital (average Q).⁵² Assigning TQ as the measure of firm performance, we specify the following dynamic panel data model for estimations:

$$TQ_{it} = \beta_0 + \delta_1 TQ_{i,t-1} + \beta_1 MULTI_{it} + \beta_2 INSID_{it} + \beta_3 FAM_{it} + \beta_4 DTA_{it} + \beta_5 DIVTA_{it} + \beta_6 MB_{it} + v_{it} \quad (2)$$

Where,

INSID = the level of director ownership concentration proxied by percentage of director ownership on the firm.

FAM = a dummy variable representing the family ownership, which takes a value of 1, if firm ownership is concentrated by family (both the managing director and chairman are from same family), and 0 otherwise.

DIVTA = the level of dividend payment to total asset.

DTA = the level of debt to total asset

MB = market to book value ratio, proxied for investment opportunities.

MULTI = a dummy variable that takes a value of 1, if there is a 20% or more shareholding by foreign ownership, and 0 otherwise.

Hypothesis development

We developed two distinct hypotheses to examine the relative contribution of ownership structure and firm's policies on firm performances. The first of these hypotheses entails that firm performance does not depend on ownership structure while the second hypothesis is developed to test whether firm's financing policies determine firm performances in Malaysia.

Hypothesis 1: There is no effect of ownership structure on firm performance

It is hypothesized that firm performance measured by TQ is not related to structure of ownership in general, family and insider ownership. Alternatively, market based firm performance would depend on firm ownership structure for a number of reasons. Firstly, as the level of managerial ownership increases in the firm, inside director may be induced to perform tasks that are beneficial to the firm value, since any impact on firm value might also directly impact on their holdings. Firm's control dominated by

⁵² See Blundell et al (1992)

family ownership serves as an internal control mechanism that aligns the interest of the manager with that of outside shareholders. Hence, any activity undertaken at the firm level by the manager would suit the best interest of shareholders. Therefore a positive association is expected between the family ownership concentration and firm performance. Moreover, sizeable foreign ownership induces fresh ideas and expertise into firm. Therefore, investors may take this as positive monitoring substitute for management activities thereby leading to better firm performance.

Hypothesis 2: Firm policy choices on dividend and leverage structure have no dynamic effect on firm performance.

The proposition of Modigliani and Miller (1961) that both dividend and leverage policies are irrelevant for firm value has been subject to controversy and debate among the academics. Nonetheless, given the complexity of organizational structure, firm may use dividend policy choice as a form of signalling device to reduce information asymmetry between prospective investors and firms. On the other hand choice of leverage can also be used as an instrument to restrict managerial discretion on taking investment projects that may be detrimental to shareholders' value. For example, debt covenants may not allow management to undertake risky investments that have uncertain

future cash flows. Hence, it is likely that firm's choice of policy on dividend and leverage will have important impact on firm performance.

The Data

This study uses data collected from Annual Hand Book of Kuala Lumpur Stock Exchange (KLSE) Library. A sample of 80 firms was collected for the period 1999-2002. The final data included a balanced panel of 320 observations. Most of these firms are drawn from Composite Index (CI) component firms which serve as market barometer.

4. Results and Discussion

For estimation of the dynamic panel data model (2), we use the Generalised Methods of Moments (GMM) (Hansen, 1982). One major merit of the GMM method is that it goes beyond the nonlinear two-stage least squares (2SLS) method of Amemiya (1974). The GMM incorporates nonlinear moment conditions beyond those generated by orthogonality of exogenous regressors with disturbances in a model. Further, the key advantage of the use of GMM as compared to Maximum Likelihood Estimator (MLE) is that it is less stringent on statistical parameter in hypothesis tests.

Table 1. Estimates from Dynamic Panel Analysis (Dependent Variable: TQ)

Explanatory Variables	Estimated Coefficients	Standard Errors	p-value
TQ(-1)	0.0396***	0.0134	0.0036
FAM	0.0456	0.2357	0.8466
MULTI	-0.1070	0.1340	0.4255
INSID	-0.0054	0.0046	0.2388
DTA	1.5923***	0.0206	0.0000
DIVTA	0.5108***	0.0764	0.0000
MB	0.1548***	0.0198	0.0000
C	0.4994***	0.0979	0.0000
Weighted Statistics			
R-squared	0.964036	Mean depend. Var	1.896817
Adjusted R-squared	0.962951	S.D. depend. Var	4.938525
S.E. of regression	0.950579	Sum sq. resid	209.6353
Durbin-Watson stat	1.995886	J-statistic	5.75E-28
Instrument rank	8.000000		

*** Significant at 1% level.

Table 1 provides the GMM estimates of the full dynamic model given by (2) for market based firm performance represented by TQ and ownership structure proxied by family ownership concentration, directors' ownership and foreign ownership concentration. We include market to book value ratio

(MB) as a control variable for market performance. The GMM estimates reported in Table 1 suggest that the estimated coefficients of *FAM*, *MULTI* and *INSID* are all insignificant. Hence, it is evident that ownership structures do not exert any significant effect on market based firm performance in Malaysia.

These results are not in direct accord with the findings by Huson and Wadud (2009) who observed a significant and positive impact of managerial ownership on accounting based performance measure namely returns on assets (ROA). It is apparent that much of these differences in results stem from the different measures used for firm performance. However, while Huson and Wadud's (2009) results indicated the role of managerial ownership on firm's

profitability, our results reveal the insignificant effect of a range of ownership types (family, directors and foreign) on firm's growth prospects, which is better measured by TQ. Hence, our results do not necessarily contradict with those in Huson and Wadud (2009) and rather shed further lights on the trivial effects of diverse ownership structures on firm's expansions of operative scale and scope.

Table 2. Estimates from Dynamic Panel Analysis for Ownership Variables (Dependent Variable: TQ)

Explanatory Variables	Estimated Coefficients	Standard Errors	p-value
Q(-1)	0.0574	0.064374	0.3732
FAM	-0.6722	1.212399	0.5798
MULTI	-0.7187	0.686408	0.2962
INSID	-0.0048	0.023377	0.8365
MB	0.2475**	0.102009	0.0160
C	1.7226***	0.497140	0.0006
Weighted Statistics			
R-squared	0.036963	Mean depend. Var	1.896817
Adjusted R-squared	0.016385	S.D. depend. Var	4.938525
S.E. of regression	4.897900	Sum sq. resid	5613.524
Durbin-Watson stat	2.938960	J-statistic	5.42E-30
Instrument rank	6.000000		

*** Significant at 1% level; ** Significant at 2% level.

Table 1 provides strong evidence on the effects of firm's policy choice on firm performances. A significant positive relationship is observed between TQ and respective proxy for policy choice variables namely ratio of dividend to asset (DIVTA) and debt to asset ratio (DTA). Note that higher DIVTA and DTA significantly boost firm performance. In particular, it is interesting to observe that higher dividend payment play a very crucial role in enhancing firm

performance (Table 1). There seems to be dynamic effect in the model as indicated by the significant lagged dependent variable TQ. This shows that the Malaysian firms tend to grow faster due to growth in the preceding periods. Market to book value (MB) ratio is also found to be statistically significant suggesting that alongside the policy variables investors also take MB as an important indicator for firm's valuation.

Table 3. Estimates from Dynamic Panel Analysis for Firm's Policy Variables (Dependent Variable: TQ)

Explanatory Variables	Estimated Coefficients	Standard Errors	p-value
Q(-1)	0.0411***	0.013390	0.0024
DTA	1.5937***	0.020596	0.0000
DIVTA	0.4973***	0.074699	0.0000
MB	0.1579***	0.019699	0.0000
C	0.4170***	0.074058	0.0000
Weighted Statistics			
R-squared	0.963627	Mean depend. Var	1.896817
Adjusted R-squared	0.963008	S.D. depend. Var	4.938525
S.E. of regression	0.949842	Sum sq. resid	212.0171
Durbin-Watson stat	1.958779	J-statistic	1.04E-28
Instrument rank	5.000000		

*** Significant at 1% level.

As a robustness check, upon controlling for MB, we also estimated dynamic panel model separately for ownership and policy variables. However, the results remain largely unchanged, which are reported in Table 2 and Table 3. Estimates reported in Table 2 clearly show that none of the ownership variables are statistically significant. Table 3 reports the GMM estimates of a dynamic panel model involving the policy variables only. The table shows that both policy variables (DIVTA and DTA) are highly statistically significant, further reinforcing the evidence presented in Table 1. Hence we can conclude that traditional policy variables such as dividend and debt level to total asset are important determinants of firm performance measured by firm's TQ in Malaysia for the designated sample period (1999-2002). Therefore, one can argue that investors in the Malaysian capital market are more concerned about wealth maximization through adoption of appropriate dividend and debt policy and are less concerned about how the firm ownership is constituted.

5 Conclusions

This study examines whether ownership structure (director ownership, family ownership and foreign ownership concentration) or policy choice provide explanation for market based firm performances in Malaysia. The study uses dynamic panel data model to capture the interrelationships involving a number of ownership and policy variables over a period from 1999 to 2002 with a sample of 80 CI components companies listed on Main Board of Malaysia. The findings provide no evidence of director ownership, foreign ownership and family ownership concentration impact on TQ based firm performance. However, we find strong evidence of growth prospect proxied by market-to-book value ratio, dividend policy choice and leverage effects on firm performance. These results help to justify our hypotheses as to whether firm ownership structure or policy variables matter for market based performance of Malaysian firms. The findings suggest that in Malaysia, traditional policy choices compared to ownership structure are still important for assessing firm performance. Hence investors are required to look into firm's dividend policy, leverage policy and market to book value ratio as sources of future prospects of the firms.

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