

Chapter 13

Effect of Ownership Structure on Firm Performance Evidence From Non- Financial Listed Firms: Ownership Structure and Performance

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ABSTRACT

In modern organizations, there is a separation between ownership and control of the firm. On the lenses of agency theory, this study statistically examines the relationship between ownership structure (i.e., ownership concentration and owner identity) and firm performance of non-financial listed firms of Pakistan by taking firm-level control variables of size, age, liquidity, financial leverage, and growth of the firm. Secondary data is collected from annual reports of 65 non-financial listed firms for the year 2008 to 2012. The least-square dummy variable model followed by the random effect model has been employed to statistically determining the impact of ownership structure on firm performance. The results of the least square dummy variable model reveal that the ownership concentration has a significant positive impact on firm performance. The owner identity (such as dispersed, family, institutional, and government ownership) has a significant causal effect on firm performance as indicated from t and p values.

INTRODUCTION

Among many others, poor corporate governance (CG) is also quoted as one of the main reasons that led to the global financial crisis. The nature of the relation between the ownership structure and corporate governance structure has been the core issue in the existing CG literature. Agency theory is the main fundamental concept in CG studies that focuses on the conflicts among principals (owners) and agents

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(managers). Adam Smith (1776) contended that managers will not work with as much dedication as the owner. Since then, multiple dimensions of agency problems have been tinted in the existing literature. Existing literature suggests that ownership structure is one of the core corporate governance mechanisms influencing the scale and growth of a firm's agency costs (Alabdullah, 2018). Therefore, the effect of ownership structure and firm performance has been measured extensively both in empirical and theoretical literature (Alabdullah, 2018, Phung and Mishra, 2016, Ozili and Uadiale, 2017). However, prior studies have mainly focused on developed countries such as USA, UK, and other Western countries (Wintoki et al., 2012, Bhagat and Bolton, 2019) while few studies have focused on emerging economies especially in Asia (Arora and Sharma, 2016, Alabdullah, 2018, Shah et al., 2020). This provides us the opportunity to fill the gap in existing literature. Arslan and Alqatan (2020) argued that Asian firms operate in a distinctive legal and institutional framework and socioeconomic factors are quite different as compared to other developed countries that may have a material effect on ownership structure and firm performance relationship. In similar vein, Arslan et al. (2019) also found that developing countries have weak institutions and therefore, the CG practices are compromised. Researchers argued that ownership concentration positively affects the firm performance because it lessens the conflicts among the managers and owners of the firms (Jensen and Meckling, 1976, Ozili and Uadiale, 2017, Al-Matari et al., 2019). Recently, several studies have shifted the focus towards internal benefits that shareholders can experience inside a firm. Researchers (e.g. (Arslan and Abidin, 2019b, Arslan et al., 2019, La Porta et al., 2000, Arslan and Alqatan, 2020, Attiya et al., 2012) found the expropriation of minority shareholders by controlling shareholders. Expropriation exists in different forms such as the sale of assets and products to related parties at an unfair price, paying excessively to an executive, outright theft and giving lucrative positions to relatives. Expropriation can create inefficiency in the financial system in a sense that fund providers will be hesitant to surrender their wealth in the face of probable expropriation by the insider. The legal way to control expropriation is to develop laws and implement them effectively (La Porta et al., 1999, La Porta et al., 1998, Arslan and Abidin, 2019a, Arslan and Alqatan, 2020). In modern organizations, there is a separation between ownership and control of the firm. There is a lack of widely held corporations in Pakistan (Khan, 2017, Salman and Siddiqui, 2013, Samza, 2016). This ownership concentration is common in Pakistan and provides plenty of incentives to larger shareholders (Arslan and Abidin, 2019b, Arslan et al., 2019).

Pakistan is one such country where insiders block holdings are ubiquitous in the corporate sector but sufficient protection to minority shareholders is not available (Samza, 2016, Khan, 2014, Arslan and Abidin, 2019a). One evidence of low judicial efficiency in Pakistan comes from a report by the World Bank (Bank, 2010). According to this report of the World Bank, Pakistan ranks 158th among 183 countries on the overall contract agreement. Furthermore, this report shows that average costs are 23.8% of the claim and the average time taken in disposing of a judicial case is 978 days. From these statistics, it can be interpreted that the judicial process in Pakistan is costly and lengthy as compared to other countries. Several studies have been conducted in Pakistan to examine the relationship between ownership structure and firm performance while findings of these studies are inconclusive (Khan and Nouman, 2017, Anwar and Tabassum, 2011, Yasser and Al Mamun, 2015, Ullah et al., 2017). Hence, this provides us opportunity to examine the relationship between ownership structure and firm performance. In addition, there is a divergence between the interests of the owners and managers. To explore the link between ownership concentration and ownership identity concerning the performance of the firm seems more interested according to the context of Pakistan. The findings of some studies showed that the ownership identity has more impact on firm performance as compared to ownership concentration

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