Implications of Ownership Identity and Insider's Supermacy on the Economic Performance of the Liste Companies

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IMPLICATIONS OF OWNERSHIP IDENTITY AND INSIDER'S SUPREMACY ON THE ECONOMIC PERFORMANCE OF THE LISTED COMPANIES

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Abstract

We adopt a multi-theoretic approach to investigate a previously unexplored phenomenon in extant literature, namely the differential impact of ownership identity and director dominate shareholding on the performance of emerging market firms. The main research question addressed is, whether the impact of this relationship is conditional on the identity of the block investor. First, the relationship between overall block ownership and firm performance is tested by employing multiple regressions on 500 firm-year observations for the period from 2007 to 2011. Then, the block ownership is classified as the state, individuals, insiders, financial institutions, corporate and foreign investors and the influence of these identities on firm performance is examined. It was found that only the ownership categories such as the government, institutions and foreign ownership have positive influence on the firm performance. The results also indicate that high level of insider ownership also negatively associated with the firm performance. The main contribution of this paper is the examination of the relationship between block ownership and firm performance from the perspective of the identity of investors.

Keywords: Ownership Structure, Firm Performance, Director Domination

JEL Classification: G32, G34

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1. Introduction

The corporate governance literature classifies ownership identity as an influential internal governance mechanism (Shleifer & Vishny, 1997). Agency theory highlights that principals and agents often have conflicting goals and capacities to influence corporate behaviour and outcomes (Milgrom & Roberts, 1992). An important contribution of agency theory is that it facilitates a structured approach to the analysis of economic motivations and the incentives of managers and shareholders (Eisenhardt, 1989). However, agency theory has been criticized in the sociology literature for its failure to pay sufficient attention to the context in which exchange and principal-agent relations are embedded (Hamilton & Biggart, 1988).

Studies that investigated ownership structure and performance relationship focused only on the conventional separation of ownership and control concept, in reality there are many different types of ownership in existence, for example, institutional investors, corporate investors, government investors, individual investors, insider ownership (Boone et al., 2011). These ownership types have different behavioral characteristics which provide them with different levels of involvement in companies.

The increased volatility of corporate ownership portfolios observed in recent years has led to renewed interest in ownership structures, especially with respect to multinational enterprises. As the economies of the world become more and more globally integrated, such issues will become more prominent and will affect our understanding of the interweaving systems of corporate relations, through which formal and informal networks of power are established (Heubischl, 2006 and Pfeffer, 1972). They can be understood as a potential source for inter-corporate power and coordination leading to corporate control.

We investigate this issue by analyzing a sample of KSE-100 indexed Pakistani companies where outside block ownership is common but does not necessarily reside with one category of investors. The argument advanced in this study is that the blockholders represent different segments of investors in the market (corporate, individuals, institutions, state, foreign and director ownership) and therefore, their incentives to monitor managers can vary from one group to another. In a non-homogenous block ownership environment, it is important to account for

these differential influences in order to arrive at a conclusion about the relationship between ownership identity and firm performance.

The remainder of the paper proceeds as follows: Section II reviews the relevant literature on ownership identity and performance relationship. Section III provides Hypotheses development and IV description about Pakistani environment while Section V describes the data collection procedure and analytical methodology employed. This is followed by the discussion of empirical findings in Section VI. The last section offers some conclusions on the topic.

2. Literature Review

a) Ownership Identity

According to Zeitun & Gary (2007), ownership structure depends on a country's social, political, economic and cultural norms. In an emerging market like Pakistan, these factors are likely to be entirely different from those of developed countries, which may limit the application of empirical models tested in mature markets.

There is substantial empirical literature on the impact of ownership structure on the financial efficiency of firms (Morck et al., 2000; Anderson & Reeb, 2003; Burkart et al, 2003; Caselli & Gennaioli, 2003; Bartholomeusz & Tanewski, 2006; Villalonga & Amit, 2006; Balsmeyer & Czarnitzki, 2010; and Bozec et al, 2010). The findings, however, are not conclusive and the spectrum of results is quite wide. Thus, for US firms the analysis by Demsetz and Villalonga (2001) and Holderness (2003) revealed no relationship between ownership structure and performance. Studies conducted by Claessens & Djankov, (1999); Gorton & Schmid, (2000); Sarkar & Sarkar (2000); Sun & Tong, (2003) and Lee, (2008) report that the financial performance of a firm is positively influenced by the level of ownership structure. While Franks & Mayer (2001) find a higher turnover of directors in closely held firms in comparison to their widely held counterparts, investigations conducted by Kaplan & Minton (1994) and Kang & Shivdasani (1995) reveal that firms with block shareholdings are more likely to replace managers or to restructure their firms following a period of underperformance. Additionally, the presence of large shareholders increases the susceptibility of a firm to and probability of a takeover thereby proving managers with incentives to generate attractive returns to shareholders (Shleifer & Vishny, 1986 and Shivdasani, 1993).

Many empirical studies that have investigated the relationship between block ownership and firm performance have analyzed either the overall level of block ownership (Demsetz and Lehn, 1985; Demsetz, and Villalonga, 2001) or just inside block ownership (Morck et al., 1988; McConnell and Servaes, 1990; Craswell et al., 1997; Himmelberg et al., 1999; Short and Keasey, 1999) or block ownership samples gathered in unique microstructure settings such as bank block ownership in the bank centered economies of Japan and Germany (Morck, et al. 2000; Gorton and Schmid 2000), state non-tradable block ownership in China (Qi et al., 2000; Sun & Tong, 2003; Wei et al., 2005; Gunasekarage et al., 2007) and, institutional and foreign block ownership in privatized firms (Claessens & Djankov, 1999). The findings reported in these studies are inconclusive.

b) Director Domination Ownership

Agency theory argued that dominating director ownership implies better incentives to monitor, greater incentive alignment, undeviating partaking and therefore higher expected profits and share prices (Larner, 1971; McEachern, 1975; Herman, 1981 and Sorenson, 1996). But higher insider ownership may also imply greater managerial entrenchment, diversion of funds and thereby leads to lower efficiency (Jensen and Meckling 1976; Morck et al, 1988; Gugler, 1999; and Dyck & Zingales, 2004).

A large number of empirical researches scrutinize the relationship between insider dominating shareholding and firm performance in developed countries which based on "single equation models" generally found a positive or perhaps insignificant relationship between insider ownership and performance (Short 1994), While non-linear relationships between managerial ownership and market valuation (e.g. Morck et al. 1988, McConnell and Servaes, 1990, Thomsen and Pedersen 2000). But, as mentioned, more recent simultaneous estimations of the "causes and consequences" of insider ownership have found insignificant performance effects (Loderer & Martin 1997; and Himmelberg et al, 1999).

Gugler, Mueller & Yurtoglu (2008) stated that in the US, firm performance initially rose with an increase in the insider ownership but fell when the insider ownership exceeded 60 percent of the companies. Loderer & Martin (1997) used the sample of 867 US companies found a weak bowl-shaped effect of director ownership on both measures estimated by simple regression. Therefore, research interpret these results as evidence that managers have inside knowledge and increase their shareholdings prior to good acquisitions whereas high share prices and Q-values induce them to sell out.

Cho (1998) examines investment as an intermediate variable between director ownership and performance measured by Q-values of 326 Fortune 500 firms in 1991. He found that Q-values have a positive impact on dominating director ownership and that director ownership has a significant non-monotonous effect on investment, which again has a positive impact on Q-values. When taking this into account in a 3-equation model simultaneously determining director ownership, Q-values and

investment, the non-monotonous effect of ownership structure on Q-values becomes insignificant.

However, previous research found a positive association between low levels of insider ownership and performance (Kim, Lee, & Francis, 1988; Mehran, 1995; Hossain, Prevost, & Rao, 2001; Elayan, Lau, & Meyer, 2003; Welch, 2003). On the other side, researchers report the relationship between dominating director ownership and firm performance is non-monotonic (Chen et al., 1993; Griffith, 1999; McConnell & Servaes, 1990; Morck, Shleifer, & Vishny, 1988; Short & Keasey, 1999), supporting convergence-of-interest hypothesis at some low levels of insider ownership and an entrenchment hypothesis at higher levels of director ownership which indicate non-linear relationship between ownership and performance. However, stewardship theorist claims that there is no relationship between insider ownership and performance (Demsetz, 1983; Demsetz & Lehn, 1985; Demsetz & Villalonga, 2001).

3. Hypotheses Development

The standard assumption is that each of the ownership categories has different objective with implications for corporate strategy and performance (Edwards & Nibler, 2000; Morck et al., 2000 and Thomsen & Pedersen, 2000). Thomsen & Pedersen (2002) argue that the identity of large owners e.g. family, bank, institutional investors, government, and other companies has important implications for corporate strategy and performance. Evidence suggests that blockholder identity may matter because shareholders can have heterogeneous incentives and capacities to monitor managers (Gedajlovic, 1993 and Thomsen & Pederson, 2000).

a) Associate Company Shareholding

In corporate shareholding or associated company shareholding is that where the shares are held by one company in another. Business groups are also one of the major ownership categories that also called associated company ownership or family ownership.

Business groups consist of a collection of firms, which are linked together by common ownership, and director interlocks. Group affiliation has both benefits and costs. Among the beneficial effects, Chang and Hong (2000) find that group companies serve as an organizational structure for appropriating quasi rents, which accrue from access to scarce and imperfectly marketed inputs such as capital and information. Khanna and Rivkin (2001) defined Business group as a set of firms which, though legally independent are bound together by a group of formal and informal ties and are accustomed to taking coordinated action. However, groups are also associated with the larger possibility of (i) inefficient transfer of resources from more profitable firms to financially constrained firms (Shin and Park, 1999) and (ii) exploitation of minority shareholders by means of tunneling of resources through pyramids and extensive crossholdings by the controlling family (Johnson et al., 2000, and Bertrand et al., 2002).

Alchain (1969) argued that group business create the internal capital market facility. Scharfstein & Stein (1994) extended the Alchain argument by comparing the financing arrangement with-in the group and financing through bank (in case bank is not a group member). They argued that group headquarter is better able to monitor and access to information regarding member company than bank. Where capital market is underdeveloped, business groups facilitate capital allocation among group members (Perotti & Gelfer, 2001). Hoshi (1991), and Kim & Limpaphayom, (1998), in their studies found that Japanese keiretsu structure of companies had close relationship with their main bank and this relationship played a significant role in reducing the costs of financial distress. Kester (1986); Berglof & Perotti (1994) argued that keiretsu structure also reduces the informational asymmetries between creditors and shareholders.

Hypothesis H_{1a}: There is a positive relationship between the higher proportion of corporate ownership and profitability among Pakistani firms.

b) Directors' Shareholding

The classical publication of Adam Smith (1776: 700) have suggested that "negligence and profusion, therefore, must have prevail" in management controlled companies because it cannot be expected that those who mange others' money will watch over it with the same "anxious vigilance" as they would watch over their own. Meanwhile, Jensen & Meckling (1976) and Fama & Jensen (1983) argue that insider ownership can cause two types of fully differentiated behaviour: convergence of interests with shareholders and the entrenchment effect.

McKnight & Weir (2009) found that higher managerial ownership reduces company agency costs, supporting the earlier findings of Coles, Lemmon and Mescke (2005). This may be because higher personal shareholding by directors bonds them to the company and acts as a method for mitigating agency costs in listed companies. Studies by Ang, Cole & Lin, (2000) and Singh & Davidson (2003) validate that higher director ownership reduces the misalignment between shareholders and managers and lowers agency costs. However, an optimal level of insider ownership is determined by firm size, industry, investor protection level, and performance of the firm (Hu & Izumida, 2008).

Previous studies find mixed results for director ownership and its effects on the firm value and performance. Demsetz (1983) and Demsetz & Lehn (1985) argue that insider ownership and company financial value have endogenous effects and that there should be no systematic relationship. However,

controlling the endogenous effect of insider ownership and company financial performance, Bohren and Odegaard (2001) find a positive relationship between insider ownership and company value in the Norwegian context.

In a review of a number of these studies;

Hypothesis H_{1b}: There is a positive relationship between the higher proportion of insider's ownership and profitability among Pakistani firms.

c) Individual Public Shareholding

In many emerging countries, public ownership is among the largest group of blockholders (Claessens et al., 2000). Sun & Tong (2003) reported that public ownership has positive impact on firm performance after share issue privatization, using listed firms' data during the period 1994-2000. Delios & Wu (2005) reported a U-pattern relationship between individual public ownership and Tobin's Q using the data of public firms listed on China's two stock exchanges during 1991-2001. In a review of a number of these studies:

Hypothesis H_{1c}: There is a positive relationship between the higher public shareholding and profitability among Pakistani firms.

d) Foreign Shareholders

It is important to disentangle the effects of foreign ownership in a firm belonging to foreign industrial corporations and foreign financial institutions. Agency theory suggests that since foreign corporate ownership stakes are larger and less fragmented than stakes held by foreign institutional shareholders, the incentives of these larger shareholders are more aligned to perform an effective monitoring role. Gorg & Greenaway (2004) argue that the main challenging question in the international business strategy is the outcome gained from foreign ownership of firms. It is mainly accepted that foreign ownership plays a crucial role in firm performance, particularly in developing and transitional economies. There are important governance implications for firms with and without foreign holdings which ultimately have a bearing on the performance of firms. These performance differences arise from the possession of certain firm specific advantages that accrue to the firm with foreign ownership. These firm specific advantages stem from advanced technological know-how, marketing and managing skills, export contacts, coordinated relationships with suppliers and customers and reputation (Aitken & Harrison, 1999).

Empirical studies found evidence supporting such a conjecture. For instance, Boardman, Shapiro & Vining (1997) find significant performance differences among multinational enterprises or their subsidiaries and domestic firms in Canada. Harris & Robinson (2003) report that presence of foreign owners in companies in the UK manufacturing industry leads to an improvement in the productivity. Chibber & Majumdar, (1999) find that the extent of a foreign firm's control over a domestic firm is positively associated with the degree of resource commitment to technology transfer. Djankov & Hoekman (2000) find foreign investment is directly associated with the provision of generic knowledge and specific knowledge. Goethals & Ooghe (1997) in their study of Belgium (held on 50 foreign and 25 local companies) concluded that foreign companies have a better financial performance compared to domestic companies. Among emerging economies, Willmore (1986) analyzing a matched sample of foreign and domestic firms in Brazil and finds foreign firms to have higher ratios of value-added to output, higher labor productivity and greater capital intensity among others. However, from Thailand Wiwattanakantang (2001) found that foreign controlled firms exhibit superior performance.

As a consequence, we expect to find a positive relationship between the foreign ownership and firm performance of Pakistani corporations:

Hypothesis H_{1d}: There is a positive relationship between the higher proportion of foreign ownership and profitability among Pakistani firms.

e) State Shareholding

The government shares are held by the federal and provincial State. State ownership is an involvement ownership type because governments have power not only from the corporate legal property right point of view, but from state policy setting, implementation and reputation.

De Alessi (1980 & 1982) defines state-owned enterprises as 'political' firms with general public as a collective owner. A specific characteristic of these firms is that individual citizens have no direct claim on their residual income and are not able to transfer their ownership rights. Boycko, Shleifer & Vishny (1996) argue that in most cases the agency problem in government owned companies arises from political issues rather than managerial issues.

However, Boycko, Shleifer & Vishny (1996) argue that in most cases the agency problem in government owned companies arises from political issues rather than managerial issues. The conflict of interest between government and other owners often arises because the State is more interested in political outcomes compared to the other owners who are more interested in the financial returns. Gursoy & Aydogan (2002) found that when compared to the family-owned companies, government-owned companies have lower accounting-based returns but higher market-based returns in Turkish listed companies. Sun, Tong & Tong (2002) report that the relationship between government owners and Chinese companies' performance follow an inverted U-shape pattern.

Accordingly, we propose the following hypotheses:

Hypothesis H_{1e}: There is a positive relationship between the higher proportion of state ownership and profitability among Pakistani firms.

f) Institutional Shareholding

The role of financial institutions on the theoretical literature of ownership identity has been crucial pragmatic as anti-takeover barriers (Sheard, 1991). Meanwhile, Gedajlovic & Shapiro (2002) argue that these financial institutions are well positioned to monitor the executives of the firms within their network. Heaw-Wellalage & Locke (2011) stated from Sri Lanka that institutional ownership is predominant and approximately 95% of multinational subsidiaries are owned and operated by institutional investors and performed betters as compare to domestic companies. Hayashi (2003) found that institutional ownership was responsible for 60% of all outstanding equity in US, compared to 8% in 1950. As a result of the growing volume of equity controlled by institutional owners, the role of institutional investors has changed from passive investors to active monitors. Meanwhile, Chirinko et al. (1999) explain that financial institutions might be important mainly because of their role as supplier of debt but also as equity holder and their representation on supervisory board. Jensen (1989) argues that joint ownership of debt and equity by large informed investors results in stringent managerial monitoring and create strong incentive for managers to make value maximizing decisions. Cornett et al. (2007) explain institutional shareholders have more opportunity, resources and ability to monitor and influence managers.

Institutional shares are held by investment bank, insurance companies, mutual fund companies and/or other investment institutions. Nickel, Nicolitsas & Dryden (1997) did not found the effect of dominant external shareholders on company performance, except when the dominant external shareholder is a financial institution. Chaganti & Damanpour (1991) investigated the effect of institutional investors that presence of higher proportion of institutional investor leads to relatively higher performance. Xu and Wang (1997) found positive and significant correlation between profitability and large institutional shareholders in China.

Navissi & Naiker (2006) find institutional owners have greater incentive to monitor management in New Zealand context, and it positively affects firms' financial performance. This may be due to fact that unlike boards of directors, institutional investors have increasingly used their power to pressure managers to come into line with the shareholders' interests (Cornett et al., 2007). Moreover, higher institutional ownership is always associated with higher board remuneration and incentive-related executive compensation, and it reduces the likelihood of CEO duality on the board (Henry, 2010). Gürbüz, Aybars & Kutlu (2010) analyze 164 firms from Turkey and demonstrate a positive relationship between corporate governance and institutional ownership on firm financial performance. Clay (2001) finds a significant positive relationship between company performance and institutional ownership percentage in US, where a 1% increase in institutional ownership leads to 0.75% increase in company financial performance. Similar results were found by Lin (2010) who posits that when the institutional ownership is higher than 81.2% in Taiwanese companies, firm values start to increase.

Hartzell & Starks (2003) find that institutional ownership mitigates agency costs between shareholders and managers, because it increases the monitoring. In line with the above findings, using firms from the North American casino industry, Tasi & Gu (2007) posit a negative agency costs relationship between institutional ownership and agency costs. However, Henry (2010) employed Australian listed companies' data and found negative results. In a review of a number of these studies:

Hypothesis H_{1f}: There is a positive relationship between the higher proportion of Institutional ownership and profitability among Pakistani firms.

g) Others' Categories of Shareholding

Other categories of the shareholding consist of public companies, charitable and other trusts, NGOs, Cooperative societies, etc. Literature is considerably thin about this class of ownership and need to research on it seriously. These blockholders usually have a long investment horizon. Allen and Philips (2000) present evidence that supports the argument that corporate ownership provides significant benefits to firms involved in certain business agreements by reducing the costs of monitoring the alliances or ventures between firms.

Hypothesis H_{1g}: There is a positive relationship between the higher proportion of 'others categories' of ownership and profitability among Pakistani firms.

4. Corporate Landscape in Pakistan

The ownership structure of companies in Pakistan together with other governance mechanisms makes an investigation of block ownership in this country interesting. First, being an emerging economy with a relatively inactive market for corporate control, Pakistan investors can be expected to rely on internal governance mechanisms such as block ownership to minimize agency conflict and to generate a return for their investment. Second, and in relation to the first point, corporate ownership in Pakistan is characterized by a strikingly high level of concentrated ownership; this has remained unchanged for a long period of time.

There are considerable differences in corporate governance frameworks and practices between Pakistan and most developing economies. Pakistan is

a common law country having one tier board structure and the majority of large public companies display concentrated ownership structures with strong family ownership or associate companies. As a result, the Pakistani corporate environment is characterized by power asymmetries among controlling shareholders, minority shareholders and management, in favor of the first. In order to improve the corporate governance environment in Pakistan, an array of institutional and government initiatives have been implemented from last decade. Institutional investors, National Investment Trust (NIT), Investment Corporation of Pakistan (ICP), have increased their participation as minority shareholders of large public companies and currently play an important role in developing local corporate governance practices.

Securities and Exchange Commission of Pakistan (SECP) is the principal regulator of securities market and non-bank companies, including non-listed companies. State Bank of Pakistan (SBP) regulates Commercial Banks & Non-Banking Financial Institutions with prudential regulations. Since its establishment, it has initiated a number of reforms aimed at improving corporate governance policies, structures and frameworks in Pakistan. The most important reform was the implementation of the code of Corporate Governance in March, 2002 and revised in May, 2012.

Pakistan Institute of Corporate Governance (PICG) playing a pivotal role in conjoining SBP and seventeen other associations that were all concerned with corporate governance. PICG is today a hybrid Institute of Governance and Institute of Directors. As the Institute of Governance, it increases awareness and champion the cause of good governance practices and, as the Institute of Directors, it develops professionalism and encourages engagement of corporate bodies and individuals in the role of effective oversight. PICG providing knowledge about best practices in corporate governance to all key stakeholders affected by corporate governance by improving the quality of corporate governance in Pakistan.

5. Methodology

In line with prior studies that examine the relationship between ownership and firm performance (Gedajlovic and Shapiro, 1998; Thomsen and Pedersen, 2000; Khanna and Palepu, 2000), this research uses the following regression specification:

Performance = f (ownership variables, control variables)

a) Data Collection

Our sample comprised KSE – 100 index companies for five years 2007 to 2011. Companies were excluded in case of non availability of data and/or missing data. According to the Karachi Stock Exchange official brochure (Published in 2012) "The KSE-100 Index was introduced in November 1991 with base value of 1,000 points. The KSE - 100 Index comprises of 100 companies selected on the basis of sector representation and highest market capitalization, which captures over 90% of the total market capitalization of the companies listed on the Exchange. Out of the following 33 Sectors, 32 companies are selected i.e. one company from each sector (excluding Open-End Mutual Fund Sector) on the basis of the largest market capitalization and the remaining 66 companies are selected on the basis of largest market capitalization in descending order. This is a total return index i.e. dividend, bonus and rights are adjusted." (p. 7)

Data on required variables is collected through secondary sources. Data on Corporate Governance internal mechanism are collected through company information page, compliance with the code of corporate governance report, directors' profiles and directors' report to the shareholders. Data related to financial part of the study is collected from financial statement part of Annual Reports.

b) Reliability Analysis

Reliability analysis was used to assess internal consistency (degree of homogeneity among the items). Cronbach's Alpha coefficients were computed and the overall assessment was 0.87. According to Nunnally (1978), a data collection instrument with a good internal consistency should have Cronbach's Alpha coefficients that are higher than 0.7. The items were therefore, found to be highly homogeneous.

Variables

The variables employed in our equations are described in Table 1.

a) Performance Variable

The concept of enterprise performance allows many interpretations. In applied studies it is common to associate improvements in firm performance with increased profitability, higher efficiency, and increased output (Bevan et al., 1999).

Demsetz & Villalonga (2001) divided the measures according to the time perspectives and the measuring identity: the accounting profit is backward-looking and are calculated by accountants under the constraints of standards; Tobin's q, on the other hand, is forward-looking and are caught by the community of investors under the constraints of markets.

The variables employed in this study for firm profitability were ROE (return on equity), ROA (return on assets), Tobin's Q (Q) and EVA (Economic Value Added).

Table 1. Description of variables

Corporate Ownership (O_COR)	Percentage of associated company ownership in a company to the total equity.
Individual Ownership (O_IND)	Percentage of Individual Public ownership in a company to the total equity.
Director Ownership (O_DIR)	Percentage of Company Directors ownership in a company to the total equity.
Institutional Ownership (O_INS)	Percentage of Institutional investor's ownership in a company to the total equity.
Foreign Ownership (O_FOR)	Percentage of foreign investor's ownership in a company to the total equity.
State Ownership (O_STA)	Percentage of Government ownership in a company to the total equity.
Other's Ownership (O_OTH)	Percentage of ownership other than above said types in a company to the total equity.
Director Domination (D_DOM)	Companies having more than 51% executive director's domination.
Return on Equity (ROE)	Net Profit divided by Total Equity (Demsetz & Villalonga, 2001; Gugler & Yurtoglu, 2003 and Bjuggren & Wiberg, 2008)
Return on Assets (ROA)	Net Profit divided by Total Assets (Barber & Lyon, 1996; Core, Guay & Rusticus, 2006 and Bhagat & Bolton, 2010)
Tobin Q (Q)	The ratio between the market value and replacement value of the same physical asset (Demsetz & Villalonga, 2001; Gugler & Yurtoglu, 2003; Bjuggren & Wiberg, 2008)
Economic Value Added (EVA)	Net Operating Profit After Taxation (NOPAT) Weighted average cost of capital (WACC) Invested Capital (IC) EVA = NOPAT – (WACC x IC)
Financial Leverage (FL)	Total Debt/Total Equity (Jensen, 1986 and Kim & Sorensen, 1986)
Firm Size (F_SIZE)	Natural Logarithm of Total Assets (Pedersen & Thomsen, 1999)
Firm Age (F_AGE)	Number of years from the incorporation (Anderson & Reeb, 2003; Han & Suk, 1998)

b) Control Variable

Financial Leverage, measured as the ratio of debt to capital employed, is included as a control variable in the regression models because a firm's capital structure may influence its investment decisions and the discretion afforded managers (Harris & Raviv, 1991).

Firm value will be included in the equation for ownership concentration to deal with the potential problem of reverse causality: it has been argued that although ownership may affect performance, ownership structure may also be affected by the firm leverage. In line with Chen and Jaggi (2000), debt-to-equity ratio (FLV) was used to measure firm leverage.

A company increases its leverage with the intention of increasing its return on stockholder equity. A 1.5 ratio indicates that the company is using Rs. 1 in equity financing for each Rs. 1.50 in assets. The ratio provides a direct relationship: the higher the ratio, the higher the debt, or the lower the ratio, the lower the debt. A ratio of one indicates that the company has no debt.

In the existing empirical studies ownership concentration tends to be negatively affected by firm size (Demsetz and Lehn, 1985, Himmelberg et al. 1999). This result reflects probably wealth limitations (it is simply more costly to acquire large portion of equity in larger firms) and the concern with risk diversification. But size is also sometimes considered as a proxy for managerial discretion (Himmelberg et al., 1999); in that case we expect size will positively affect ownership concentration. Size may also be viewed by potential shareholders as a proxy for reputation. I measure size as the natural logarithm of the firm's assets.

6. Findings and Discussions

a) Descriptive Statistics

Table 2 reports the descriptive statistics for the sample data. The highest mean value is for corporate ownership that is 41.6%, the highest percentage of corporate ownership is 98.9%, and the lowest ownership representation is 0%. This is consistent with the view that group ownership/corporate ownership of listed companies in Pakistan is relatively high. The highest director ownership in the sample data is 90%, while 8% firms of the KSE-100 are

directors dominating. Nevertheless, Bhabra (2007) reports an average director ownership for her sample of larger New Zealand firms was 9.34%, and Short and Keasey (1999) report an average insider ownership of 13% in their UK sample. Overall, companies listed on the KSE-100 indexed companies having higher director's ownership compared to companies in developed markets.

The mean of domestic public ownership is 17% while institutional shareholding is 11%. This indicates that a very high percentage of shares on the Karachi stock market are owned by institutional investors and general public. Foreign ownership highest is 84% while the mean value is 9.9% that is 5th largest form of ownership in Pakistani companies. The market based financial performance measure, Tobin's Q, has a mean of 1.034 that is comparable to developed markets. However, the return on equity (ROE) and return on assets (ROA) mean values are 0.13 and 0.069 respectively; which indicates that KSE listed companies are not performing well. The control variables, firm age, leverage and log of firm size are also listed.

Table 2. Descriptive Statistics (N = 475)

	Min	Max	Mean	SD
Individual Ownership (O_IND)	0.00	1.00	0.169	0.176
State Ownership (O_STA)	0.00	0.90	0.069	0.194
Institutional Ownership (O_INS)	0.00	0.586	0.109	0.107
Corporate Ownership (O_COR)	0.00	0.989	0.416	0.315
Director Ownership (O_DIR)	0.00	0.90	0.108	0.205
Foreign Ownership (O_FOR)	0.00	0.84	0.099	0.150
Other Type Ownership (O_OTH)	0.00	0.46	0.030	0.080
Director Dominate Firms (DOM_D)	0.00	1.0	0.080	0.272
Firm Age (F_Age)	5	152	37.19	26.68
Firm Size (F_Size)	5.112	9.061	7.397	0.703
Financial Leverage (FL)	0.00	3.607	0.148	0.268
Economic Value Added (EVA)	0	1	0.37	0.484
Return on Equity (ROE)	-14.743	1.772	0.130	0.792
Return on Assets (ROA)	-0.876	0.531	0.069	0.135
Tobin's Q	0.047	9.160	1.034	1.095

b) Correlation Test

The influence of overall ownership structure on firm performance has been studied in many markets. In order to provide evidence on this aspect for Pakistan, we first analyze the relationship between ownership structure and firm performance. The correlation matrix among ownership structure, firm performance measures and other control variables is tabulated in Table 3. It is worth notification that the four firm performance variables are highly correlated each other. This proves that the selection of these four performance measures is reasonable since they test the firm performance in same perspectives. The results stated that high level of individual ownership is negatively correlated with ROA, Tobin's Q and EVA. While, high level of state ownership in sample companies is positively correlated with ROA, Tobin's Q and EVA. Both results are consistent with the all three types of performance measurement.

The higher level of institutional ownership has positive relationships with EVA and negative correlation with Tobin's Q.

The relationship between director's dominating organization and market based performance measure (Tobin's Q) is negative, which indicates that the market performance of director dominating companies is poor.

Results of Table 3 also reveals that firms with higher level of director's ownership has negative impact on the economic performance of the company.

c) Regression Analysis

The R^2 value was 9.1%, 20.6% & 18.8%, this was adjusted to 8.0%, 14% & 13.5% (R^2 adjusted) respectively.

To conclude, the results from Table 4 shows that a significant negative relationship exists between ROE, Tobin's Q and director dominated companies and higher level of domestic public ownership variables ($p = 0.000, < 0.05$). The higher level of institutional ownership variable is significant for ROA and Tobin's Q with the F-statistics reported at 0.560, 2.942 and 2.455, Since prob.(F)<0.05, and significant relationship exists between the variables.

Table 3. Correlation Coefficient Analaysis (N = 475)

Variables	O_IND	O_STA	O_COR	O_ISN	O_DIR	O_FOR	O_OTH	DOM_D	ROE	ROA	Tobin's Q
DIS_O	.756 (.000)										
O_STA	-.216 (.000)	.									
O_COR	-.461 (.000)	-.322 (.000)									
O_ISN	.119 (.009)	-.145 (.002)	-.163 (.000)								
O_DIR	.029 (.525)	-.109 (.017)	-.474 (.000)	-.176 (.000)							
O_FOR	-.121 (.432)	-.200 (.322)	.011 (.000)	.211 (.061)	-.112 (.090)						
DOM_D	-.023 (.614)	-.038 (.404)	-.388 (.000)	-.165 (.000)	.844 (.000)	.111 (.019)					
O_OTH	-.197 (.555)	.059 (.873)	-.056 (.076)	.098 (.074)	.033 (.100)	-.186 (.111)	.121 (.099)				
ROE	-.002 (.971)	.045 (.326)	-.047 (.310)	.063 (.174)	-.043 (.353)	.129 (.247)	-.900 (.070)	-.039 (.401)			
ROA	-.201 (.000)	.102 (.026)	.071 (.125)	.060 (.191)	-.083 (.073)	.011 (.195)	.089 (.120)	-.052 (.262)	.323 (.000)		
Tobin Q	-.170 (.000)	.150 (.001)	.054 (.241)	-.111 (.016)	-.077 (.094)	.011 (.025)	.344 (.200)	-.096 (.037)	.120 (.009)	.299 (.000)	
EVA	-.096 (.037)	.088 (.050)	.000 (.993)	.169 (.000)	-.102 (.027)	.199 (.312)	.132 (.333)	-.039 (.402)	.156 (.001)	.348 (.000)	.195 (.000)

Table 4. Regression Analysis Results

Variables	**ROE**	**ROA**	**Tobin's Q**	**EVA**
	t-Value (Prob.)	**t-Value (Prob.)**	**t-Value (Prob.)**	**t-Value (Prob.)**
O_IND	-.551 (.582)	-1.706 (.089)	-2.044 (.042)	-1.788 (.074)
O_STA	-.746 (.456)	-.982 (.326)	-1.619 (.106)	-1.175 (.241)
O_INS	.392 (.695)	.688 (.009)	2.966 (.003)	2.525 (.012)
O_COR	-1.392 (.165)	-.840 (.401)	-1.182 (.238)	-1.093 (.275)
O_DIR	-.857 (.392)	-1.299 (.195)	-.249 (.804)	-2.294 (.022)
O_FOR	0.982 (0.327)	1.733 (0.084)	2.424 (0.016)	1.121 (0.263)
O_OTH	.944 (.211)	-.721 (.544)	.329 (.100)	1.100 (.201)
DOM_D	-.018 (.006)	.605 (.545)	0.857 (.392)	-2.056 (.040)
R^2	0.091	0.206	0.188	0.209
Adjusted R^2	0.080	0.140	0.135	0.144
F-statistics	0.560	2.942	2.455	3.045
Prob. (F.stat)	0.788	0.005	0.018	0.004
Durbin-Watson	1.987	1.972	1.715	1.429

d) Hypotheses Justification

Hypothesis H_{1a}: Associated company ownership has a positive effect on firm performance.

The Linear Regression results: ROE (r=0.165, p<0.05), ROA (r=0.401, p<0.05), Tobin's Q (r=0.238, p<0.05) and EVA (r=0.275, p<0.05). Correlation results: ROE (β= 0.310, p<0.05), ROA (β=0.125, p<0.05), Tobin's Q (β= 0.241, p<0.05) and EVA (β = 0.993, p<0.05). The relationship was not significant, and hypothesis H_{1a} was rejected.

Hypothesis H_{1b}: Director's ownership (insider ownership) has a positive effect on firm performance.

The Linear Regression results: ROE (r=0.392, p<0.05), ROA (r=0.195, p<0.05), Tobin's Q (r=0.804, p<0.05) and EVA (**r=-0.022**, p<0.05). Correlation results: ROE (β= 0.353, p<0.05), ROA (β=0.173, p<0.05), Tobin's Q (β= 0.094, p<0.05) and EVA (**β =**

-0.027, p<0.05). The relationship was not significant, and hypothesis H_{1b} was rejected.

Hypothesis H_{1c}: Public Ownership has a positive Effect on firm Performance.

The Linear Regression results: ROE (r=0.582, p<0.05), ROA (r=0.089, p<0.05), Tobin's Q (**r=-0.042**, p<0.05) and EVA (r=-0.074, p<0.05). Correlation results: ROE (β= 0.971, p<0.05), ROA (**β=-0.000,** p<0.05), Tobin's Q **(β= -0.000**, p<0.05) and EVA (**β = -0.037**, p<0.05). The relationship was not significant, and hypothesis H_{1c} was rejected.

Hypothesis H_{1d}: Foreign Shareholding has a positive effect on firm performance

The Linear Regression results: ROE (r=0.327, p<0.05), ROA (r=0.084, p<0.05), Tobin's Q (**r=0.016**, p<0.05) and EVA (r=-0.263, p<0.05). Correlation results: ROE (β= 0.247, p<0.05), ROA (β=0.195, p<0.05), Tobin's Q (**β= 0.025**, p<0.05) and EVA (β = 0.312, p<0.05). The relationship was significant, and hypothesis H_{1d} was accepted.

Hypothesis H_{1e}: Government/State Shareholding has a positive effect on firm performance

The Linear Regression results: ROE (r=0.456, p<0.05), ROA (r=0.326, p<0.05), Tobin's Q (r=0.106, p<0.05) and EVA (r=0.241, p<0.05). Correlation results: ROE (β= 0.326, p<0.05), ROA (**β=0.026**, p<0.05), Tobin's Q (**β= 0.001**, p<0.05) and EVA (**β = 0.050**, p<0.05). The relationship was significant, and hypothesis H_{1e} was accepted.

Hypothesis H_{1f}: Institutional Shareholding has a positive effect on firm performance

The Linear Regression results: ROE (r=0.174, p<0.05), ROA (r=0.191, p<0.05), Tobin's Q (**r=-0.016,** p<0.05) and EVA (**r=0.000**, p<0.05). Correlation results: ROE (β= 0.695, p<0.05), ROA **(β=0.009,** p<0.05), Tobin's Q (**β= 0.003**, p<0.05) and EVA (**β = 0.012**, p<0.05). The relationship was significant, and hypothesis H_{1f} was accepted.

Hypothesis H_{1g}: Other Categories of Shareholding has a positive effect on firm performance

The Linear Regression results: ROE (r=0.211, p<0.05), ROA (r=0.544, p<0.05), Tobin's Q (r=0.100, p<0.05) and EVA (r=0.201, p<0.05). Correlation results: ROE (β= 0.070, p<0.05), ROA (β=0.120, p<0.05), Tobin's Q (β= 0.200, p<0.05) and EVA (β = -0.333, p<0.05). The relationship was not significant, and hypothesis H_{1g} was rejected.

7. Implications of the Findings

a) There is not any significant relationship between Associate company/Corporate ownership and firm performance. The monitoring and control school of thought argues that the free-rider problems associated with diffuse ownership, since the majority shareholder captures most of the benefits associated with this monitoring. Associated company ownership or corporate ownership is the one of the largest shareholding recipe of Pakistani listed companies but this found out that this type of ownership does not having any impact on the firm performance in Pakistan. The results of the study have therefore, shown there is dire need to reasonably diversify shareholding as a way of attracting more skills and competencies among the shareholders that can be tapped to improve firm performance.

b) There is a negative relationship between higher insider ownership and directors dominating ownership on firm performance. It has been argued that agency theory views managerial discretion as an opportunity for managers to serve their own objectives rather than the objectives of their controlling shareholders. The controlling shareholders may develop various strategies to prevent managers from using their decision making discretion to pursue self-serving objectives at the expense of firm performance. In fact, the study reaffirmed this position among listed companies in Pakistan. According to Chang and Wong (2003), strategic management of managerial discretion is dependent, to a large extent, on a comparison of the objectives of controlling shareholders and those of managers. Although it is now a well established fact that managers may have self-serving objectives, there is no priori that restricting managerial discretion will better serve the goal of maximizing firm performance.

c) There is a negative relationship between high public ownership and firm performance. The global trend toward diffuse ownership has confounded many researchers, since it undermines the popular belief that executives are inherently self-seeking and can easily wreck the organization if left without close monitoring. The findings have brought a new dimension that emphasizes block shareholding for creativity and innovation, and less monitoring by shareholders. Thus, diffuse ownership of firms does not provide environment for excellent policies to be developed and implemented by managers due to the Pakistani market structure with compare to the developed economies. The managers are therefore best informed regarding alternative uses for the investors' funds. As a result, the managers end up with substantial residual control rights and discretion to allocate funds as they choose which creates agency issues. The downside of this argument is that it presumes that managers are honest, and always prepared to work in the objective interest of the shareholders, a position that is often not true. The fact that managers have most of the control rights can lead to problems of management entrenchment and rent–seeking behavior.

d) The positive and significant relationship between foreign ownership and firm performance appears to have gained universal acceptance across the globe due to a number of factors. First, mostly these foreign owned companies are from developed countries and have access to management systems whose efficacy has been tested in many contexts. The massive resource base and bail-out plans for fledgling

affiliates are other factors that enhance performance of foreign owned firms. However, the ability of these companies to re-organize their global operations to be able to assign more costs to harsh tax regimes and profits to tax havens in a bid to reduce their overall tax liability, is the most damning feature of foreign ownership.

e) There is a significant positive relationship between government ownership and firm performance. Government ownership has been roundly criticized for contributing to generally poor performance of firms, due to excessive bureaucracy, tribalism, nepotism, poor human resource policies, political expediency in appointments and lack of respect for laws and regulations of the country. But the current study has confirmed this long-held position wrong. Most of the companies having strong state/government ownership are having monopolistic competition and enjoy the ultimate resources and discretionary powers.

f) There is a positive relationship between Institutional ownership and firm performance. Most of previous studies have found positive significant relationship between institutional ownership and firm performance, due mainly to the differences in investment preferences, professional management and shareholders' goals. Institutional investors manage savings collectively on behalf of other investors toward a specific objective in term of acceptable risk, return maximization, and mature of claims (Davis, 2001). Institutional investors prefer to simply "vote with their feet's" and sell of poorly performing firms.

g) There is no significant relationship between other ownership categories and firm performance. The findings have brought that these types of investment having live long relationships with the company and there is not any practical participation with the decision making process. Thus, this diffuse ownership of firms purchase shares like their saving and just care about the sustainability instead of any other specific corporate goal related to the performance of the company and they have sufficient latitude for innovation and creativity, that is, less monitoring by principals.

Conclusion

Using a panel of Pakistani listed firms during the period 2007 to 2011, this study examines the affects of ownership identity and director domination on firm financial performance by using market based performance measure, accounting based performance measure and as well economic profit of the firms. The results indicate a negative relationship of director ownership and financial performance. Furthermore, these findings suggest negative impact of associated company ownership and performance, indicating higher director ownership adverse effects on ROE and EVA and misalignment of the interests of management and owners. This study validate the agency issue are placed in Pakistani listed companies where the ownership structure and the firm's performance echo this.

The results of this study have important implications for the ownership structure, insider's dominance and firm performance in Pakistan. It confirms that the effect of director ownership on firm performance is more negative where legal protection for investors is weak. It suggests that although new legislative reforms have been enacted, Pakistani companies are highly dependent on internal governance mechanisms. Due to high director/insider ownership, managerial expropriation is very likely to exist. There is potential merit in promulgating new rules and regulations to control the expropriation of minority shareholders.

The findings provide direction for further research as to (i) what mechanisms are used by block investors such as the government, financial institutions and foreign investors in monitoring managers and (ii) why some categories of investors such as individuals, directors and corporate do not contribute to the internal governance of firms even though they invest a large amount of their wealth in these companies.

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