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ABSTRACT. This study examined the relationship between executive stock ownership and the financial performance of firms in the hospitality industry. The study sample included 30 public hospitality companies listed on NASDAQ, all of which had 14 years of complete financial data. The study used the Pearson correlation and linear regression analysis to test the relationship in the hotel segment, the restaurant segment, and the combined hospitality segment. The results show there is no statistically significant positive relationship between executive stock ownership and firm profit in the hotel segment, whereas in the restaurant segment, there is a negative linear relationship. Furthermore, the combined 30 hospitality companies show a slight negative linear relationship. The findings neither support the "Agency Theory," nor reveal a clear correlation between executive stock ownership and the profit performance of firms in the hospitality group.

INTRODUCTION

Since the 1930s, the conflict of interest inherent between managers and shareholders within a public company, also known as the *agency problem*, has been studied extensively by both academic and business researchers (Himmelberg, Hubbard, & Palia, 1999). In recent years, studies have focused on examining whether there is a relationship between executive stock ownership and a firm's financial performance. Most of the studies typically rely on analyzing subsamples of the Fortune 500 companies (Sundaramurthy, Rhoades, & Rechner, 2005). There has been very little research on this subject focused on the hospitality industry, and there is no clear evidence in the wider literature that companies can perform better financially when their executives own stock in the company. One view, the *convergence-of-interest effect*, suggests that the greater the percentage of stock ownership by managers, the better the firm's financial performance will be, because the interests of managers and shareholders will be aligned. The other view, the *entrenchment effect*, suggests that the greater the percentage of ownership by managers, the worse the firm's financial performance, because managers become insulated from market forces and consequently, with their significant voting power, can make decisions that only further their interests.

This study aimed to provide more empirical evidence about the link between *executive stock ownership* and *financial performance* in the hospitality industry. The most recent study on the subject, by Chen, Huo, and Lee (2012), examined quarterly financial performance data for seven publicly traded hotel companies in Taiwan. In this work, a total of 30 U.S. companies were studied with 10 from the hotel sector and 20 from the restaurant sector. The study analyzed 30 public hospitality corporations using the *pretax profit margin*

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(PPM; percentage of pretax income to total revenue) as the financial indicator and the percentage of executive-owned stock value (%OS) as the ownership indicator.

LITERATURE REVIEW

Chen et al. (2012) studied the impact of managerial ownership on the financial performance of Taiwanese tourist hotel companies from 1997–2009. They differentiated between managers and directors and the percentages of their shareholdings in the companies. Given that Taiwanese company managers tend to wield a significantly high power within their firms, sometimes to the detriment of shareholders, their study expected to find strong links between managerial ownership and financial performance. Their study found that hotel financial performance improves with insider stock ownership up to a point, and beyond that, increases in ownership results in deteriorating financial performance. In their study, both the convergence of interest and entrenchment effect were evident. In an earlier study, McConnell and Servaes (1990) similarly found that firm performance first increases with increased managerial stock ownership; however, beyond a certain level of ownership, performance begins to decline. Collett (2006) also concluded from his paper that CEO ownership is positively related to operating performance.

Dahya, Lonie, and Power (1998) studied 2,643 UK firms and concluded that the strategy of aligning shareholder interests with managerial interests through managerial stock ownership might come with inherent dangers. Their study found that poor firm financial performance leading to executive dismissals was more frequent in companies in which the executives held 1% or less of the stock; however, when executives owned more than 1%, then they became entrenched and their dismissals were less frequent.

Sundaramurthy et al. (2005) also conducted a meta–analysis to test the effects of executive and institutional ownership on firm performance, and they found a positive relationship between the two. Mura's study (2007) also concluded that "an increase in director's share ownership is associated with improving performance at low and at very high levels of ownership."

Several recent studies have indicated that there is no relationship between executive ownership and firms' financial performance. The study by Loderer and Martin (1997) showed that there is no evidence that larger stockholding by executives will lead to better financial performance of the firm. The study indicated that management is constrained by competition in the marketplace and further emphasizes the point that it is not always necessary for management to own stocks in order to gain a financial benefit from the company. Demsetz and Villalonga's (2001) study about the ownership structure and firm performance also concluded that there is no statistically significant relation between the two. This is complemented by the Himmelberg et al. (1999) study about the link between managerial ownership and performance that concluded that changes in managerial ownership do not affect firm performance.

However, there is also a third viewpoint of this theme. Bertrand and Mullainathan's (2001) research suggested that CEOs would not perform better when they have higher rewards. Kyereboah-Coleman and Biekpe (2006) concluded in a separate study using Ghanaian companies that when the CEO also doubles as Chairman of the Board of the company this impacts negatively on the firm's performance. By examining a sample of 105 London Stock Exchange firms, Young (1998) pointed out that higher level of managerial ownership impacts companies in two ways: on one hand, higher managerial ownership can impact the company performance in a positive way because of the alignment of the interests of the shareholders with those of the management; on the other hand, it can also "serve to entrench managers, making their removal more difficult when their performance falls below some predetermined level" (p. 1121). McConnell, Servaes, and Lins (2008) studied the relationship between insider ownership and its impact on firm value. They concluded that insider ownership can increase firm value to

a point after which additional ownership actually reduces firm value, confirming a curvilinear relationship between insider ownership and firm value. Similarly, Weber and Dudney (2003) also concluded that there is dual causality between CEO ownership and firm value.

METHODOLOGY

The sample consisted of 10 public hotel companies and 20 public restaurant companies. Annual data from the fiscal years beginning 2000 and ending 2013 of each company was obtained from Factset and analyzed using Statistical Package for the Social Sciences (SPSS) software. The dependent variable was the PPM, calculated by dividing pretax income by annual total sales. The independent variable was executive ownership percentage (%OS) from each of the 14 years, which is the aggregated individual ownership for each year without insider/stock ownership value and excluding the portions of trustee, private investor firms, subsidiaries, and so forth.

The analysis was conducted using the Pearson correlation to summarize the association between the %OS and the PPM. It is reported in several related researches that differences in firm size and scale could affect the results (Himmelberg et al., 1999; Kole, 1995), thus, using %OS along with PPM, instead of the absolute values of both indicators, avoids the scale and size problems.

The analysis was conducted along three dimensions:

1. Data was separated into three categories: hotel companies segment, restaurant companies segment, and combined hospitality companies segment, which included both hotel and restaurant segments. Each segment had two groups of variables: %OS and PPM.
2. Pearson correlation and linear regression were conducted to analyze the two groups of variables of each segment, respectively, and determine whether a relationship exists between the two variables within each segment.
3. The results were compared among the three industry segments.

RESULTS

1. Demographics of the sample:
   a. The majority of %OS of the hotel companies fell between 0% and 10%, whereas the majority of PPM fell between −10% and 10% (see Appendix 1).
   b. The majority of %OS of the restaurant companies was between 0% and 10%, whereas the majority of PPM was between 0% and 15% (see Appendix 2).
   c. In the combined subsample of hotel and restaurant companies, the majority of %OS fell between 0% and 10%, whereas the majority of PPM was between 0% and 10% (see Appendix 3).
   d. To make these three segments comparable to one another, each segment is subcategorized into five groups based on percentage of the ownership from highest to lowest, as is shown in Table 1.
2. Pearson Correlation & Linear Regression results:
   Table 2 shows the Pearson correlation and linear regression results for the three segments.

TABLE 1. Each Segment Category Based on Percentage of Executive Ownership

Group	Group 1	Group 2	Group 3	Group 4	Group 5
%OS	>40%	31%–40%	21%–30%	11%–20%	≤10%

TABLE 2. Pearson Correlation and Linear Regression Results

	Pearson Correlation	Linear Regression		
		F	*t*	Sig.
Seg-1	.062	.533	.730	.467
Seg-2	−.212	14.465	−3.803	.000
Seg-3	−.086	3.332	−1.825	.069

a. The hotel companies segment (Seg-1):
As shown in Table 2, for the hotels group, the Pearson correlation figure is 0.062, suggesting that the relationship between the two variables is very weak. The linear regression result shows a *t*-value of 0.730 and a significance of 0.467, showing no linear association between executive ownership and firms' performance on profit.

b. The restaurant companies segment (Seg-2):
This segment's Pearson correlation value is −0.212, suggesting that the relationship between the two variables is negative. It shows that for the restaurant group, the higher the % OS, the lower the firm's financial performance. Linear regression shows a *t*-value of −3.803 and a significance of 0.000, indicating a strong and significant negative linear relationship between executive ownership and firm performance on profit. It shows clearly that, for the restaurant companies, the increase of the %OS leads to a decrease of the firms' PPMs.

c. The combined hospitality companies segment (Seg-3):
The Pearson correlation value for this segment is −0.086, showing a negative but very weak relationship between executive ownership and firm performance for all the 30 companies as a whole. Although the hotel company segment shows a slightly positive linear relation between the two variables, the restaurant segment has a stronger negative linear relationship in comparison, so the combined segment shows a negative direction. The linear regression results are similar to the correlation results; the *t*-value is

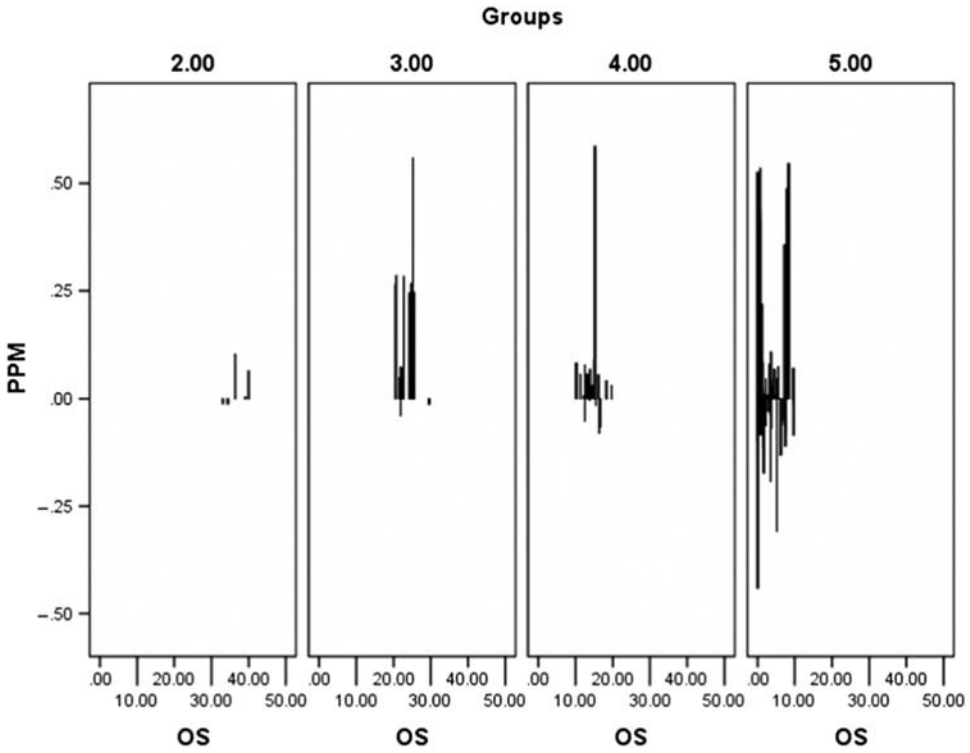

FIGURE 1. The pretax profit margin (PPM) performance of each group within hotel segment. *Note*. OS = ownership.

−1.825 with a significance of 0.069, suggesting a negative relationship between the variables that is not significant.

3. The PPM Performance:
   a. The hotel companies segment (Seg-1):

      There were 10 hotel companies representing the hotel segment and they were sorted into 5 groups based on their %OS (see Table 1). In all 10 companies, there was no hotel with 40% or more in %OS, so Group 1 had no hotels. Group 2, with %OS between 31% and 40%, the average PPM for these companies was barely above 0%. In Groups 3 (21%–30%) and 4 (11%–20%), the PPM were positive and strong (see Figure 1).

      Among all five groups, Group 3 (% OS between 21% and 30%) shows a comparably stable and positive performance in PPM, which demonstrates that when the executives hold between 21% and 30% stocks in their companies, they are more likely to make positive decisions that benefit the companies.

      The Group 5 companies (%OS less than 10%) in the graph show both extreme high and low PPM figures; no distinct pattern of PPM exists. This suggests that when executives have very small stock ownership the company's PPM is unpredictable. For example, Intercontinental Hotel Group's executives have no stock ownership in the company, however the company's PPM is quite high.

   b. The restaurant companies segment (Seg-2):

      Figure 2 shows the PPM performance for each group in the restaurant segment.

      From Figure 2, Group 1 (%OS higher than 40%) shows a fair and stable positive performance pattern in PPM. There are fewer companies in

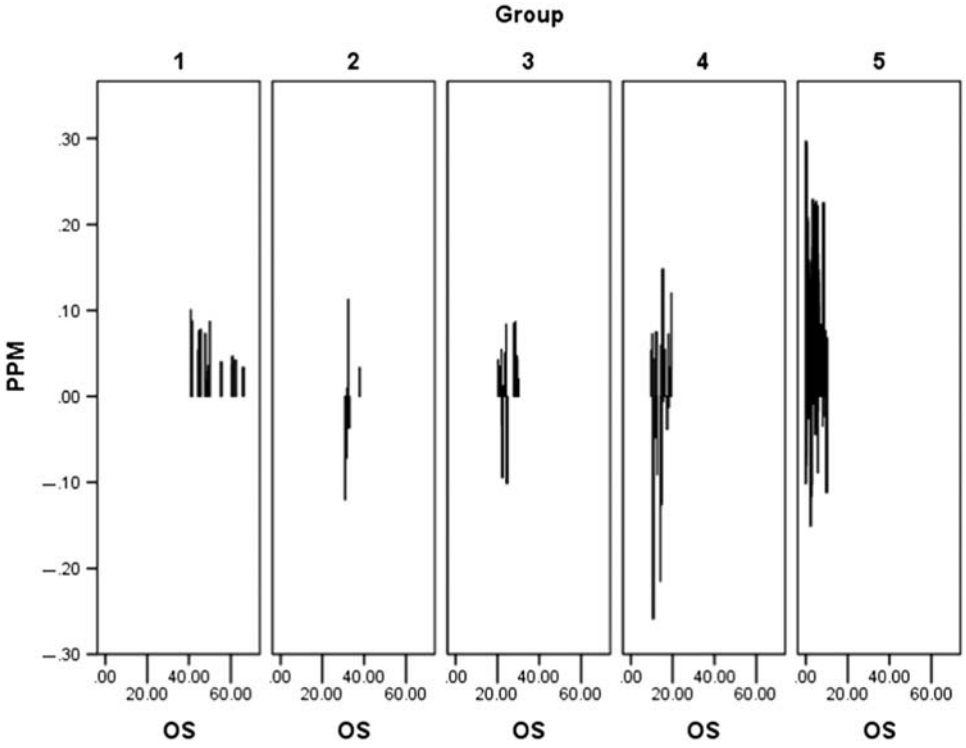

FIGURE 2. The pretax profit margin (PPM) performance of each group within the restaurant segment. *Note*. OS = ownership.

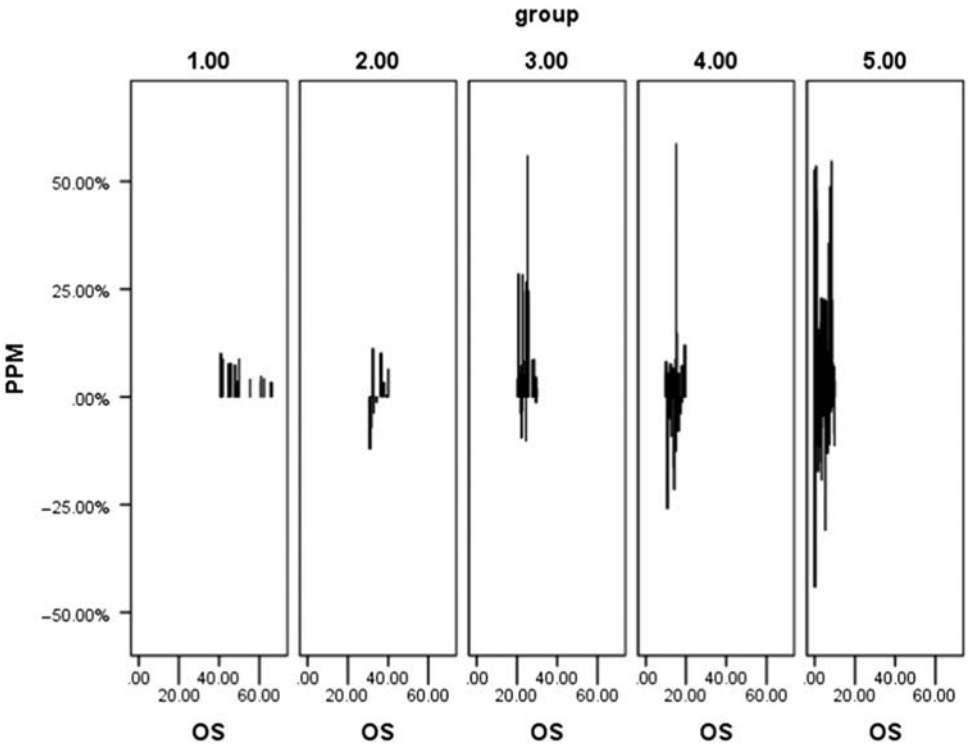

FIGURE 3. The pretax profit margin (PPM) performance of each group within the combined hospitality segment. Note. OS = ownership.

the second group (%OS between 31% and 40%), and it shows both positive and negative PPMs.

In Group 3 (%OS between 21% and 30%), more companies have a positive profit figure than a negative one. Companies in Group 4 (%OS of 11% to 20%) have a significantly negative PPM. In Group 5, where companies' executives have less than 10% of the company's stock, the PPM is significantly negative and positive.

c. The combined hospitality companies segment (Seg-3):

Figure 3 shows the PPM performance for each group in the combined hospitality segment.

From Figure 3, the majority of executive ownership in Group 5 (0%–10%) ranges from 0% to 10% with a strong positive as well as negative PPM. For the most part, Group 4 hospitality companies show more of a negative PPM compared to the rest of the groups. Group 3 has a higher %OS and also exhibits positive PPM. The figure clearly shows that only very few of these companies show a slight negative profit performance. Group 2 displays both a slight positive and negative profit performance. Finally, Group 1 is the only segment in which the hospitality companies show no negative PPM with a minor positive profit figure.

DISCUSSION

The results for both Pearson correlation and linear regression analysis of the relationship between executive stock ownership and corporate financial performance in hotels indicates no significant association; however, for the restaurant companies the relationship is linear, negative, and significant. When the hotel and restaurant companies are combined, the relationship between the variables is negative but not significant.

For all three segments, the results indicate that the higher the ownership (shown in Group 1 with the %OS higher than 40%), the less drastic the decisions are that the executives make. When executives own more corporate stock, they tend to stabilize their personal equity rather than make risky decisions that might lead to negative financial performance. Nevertheless, the hotel segment has no companies in this group, which means that compared to restaurant companies, executives of hotel corporations usually hold no more than 40% of a company's total stock. Companies that are in Group 5, with executive ownership less than 10%, show both extreme high and low PPMs, which means their pretax profit is very unpredictable. This result indicates that issuing a small number of stocks to executives could encourage them to be either fearless about making risky decisions or insufficiently motivated to improve their company's financial performance.

For the hotel segment, companies with 21%–30% of executive stock ownership have the most stable financial performance, whereas for the restaurant segment, companies with executive ownership above 40% of corporate stocks in total have a fairly positive PPM. However, in general, hotel companies show a more stable performance than restaurants, and this can be seen in Figure 1 where there is hardly any contrast in the PPM of the groups, with the exception of Group 5.

For restaurant companies in the sample, the highest %OS for a company reached 65%, and the group with higher than 40% executive ownership is also large.

CONCLUSION

In the sample of hospitality companies in this study, the relationship between executive stock ownership and pretax profit margin of hotel companies is different from that of restaurant companies. Hotel companies show a very weak relationship, whereas the restaurant companies show a strong negative relationship, that is, the higher the executive ownership percentage, the lower the pretax profit performance of the company. In total, all 30 companies appear to have a slightly negative relationship between the two variables.

These results reflect the two viewpoints from previous studies, which show no relationship or a negative relationship between the two. This also suggests that eliminating the agency problem by issuing company executives more stock might not yield the desired result in the hospitality industry.

Regarding limitations, this study was conducted by analyzing a sample of only 30 public hospitality companies in total over a 14-year period (2000–2013). The study could be improved by expanding the sample and the annual data to extend the period of time or use quarterly profit data to increase the number of observations.

The executive stock ownership that is analyzed with respect to the pretax profit margin does not take into account the number of executives among whom the stock is distributed. For example, in the fiscal year of 2013, approximately 22.7% of Marriott International Inc.'s stock was owned by 36 executives, whereas in Red Lion Hotels Group, 30 executive stockholders own only about 7.42% of the whole company's stock. This variance in stock ownership can lead to significant differences in the type of decisions executives make on behalf of their companies to achieve profitability. The theory by Hambrick and Mason (1984) states that"organizational outcomes—strategic choices and performance levels—are partially predicted by managerial background characteristics" (p. 193).

In this study, the financial performance of a firm is examined using only the PPM, which overlooks the impact of other important variables that capture the financial success of a company and its stockholders. Other financial indicators could be used in additional studies to validate the results of this research.

AUTHOR NOTES

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APPENDIX 1

Demographic of the Sample

Segment 1: The hotel companies segment (10 companies).

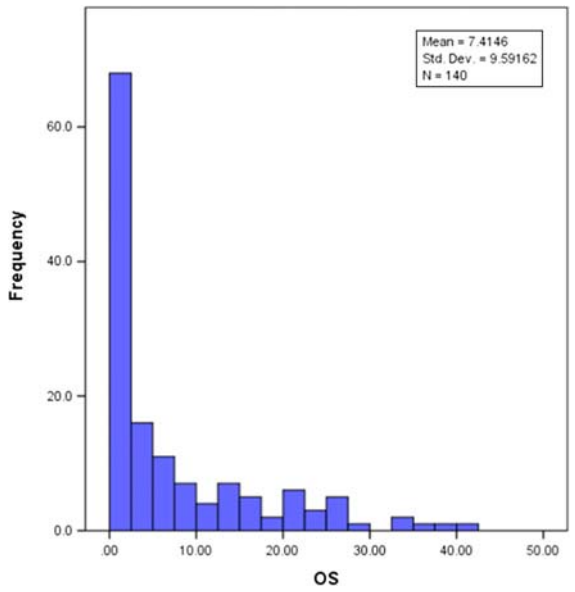

FIGURE A1. The frequency of the ownership (OS) percentage of hotel companies segment.

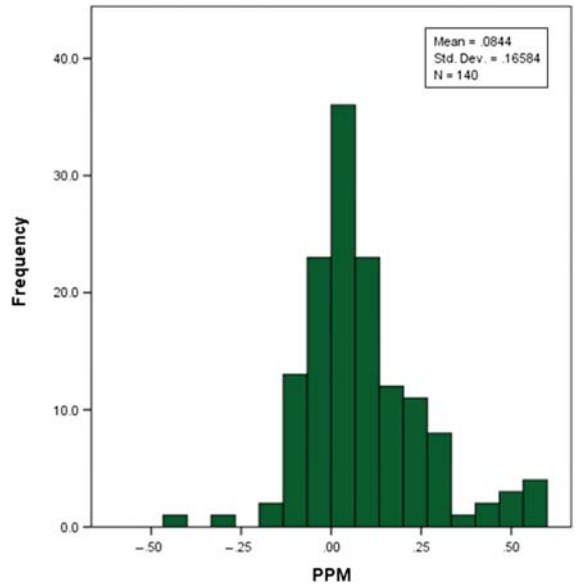

FIGURE A2. The frequency of the pretax profit margin (PPM) of hotel companies segment.

Segment 2: The restaurant companies segment (20 companies).

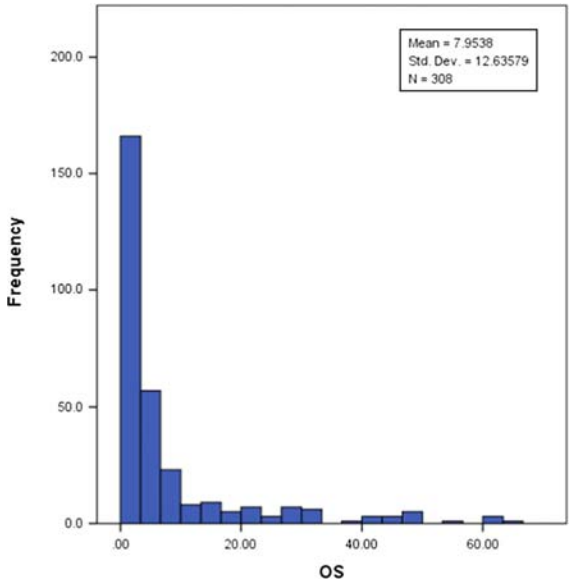

FIGURE A3. The frequency of the ownership (OS) percentage of restaurant companies segment.

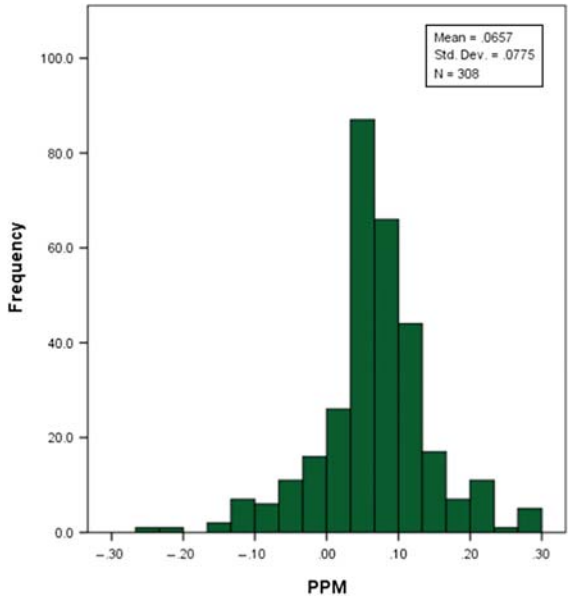

FIGURE A4. The frequency of the pretax profit margin (PPM) of restaurant companies segment.

Segment 3: The combined hospitality companies segment (30 companies).

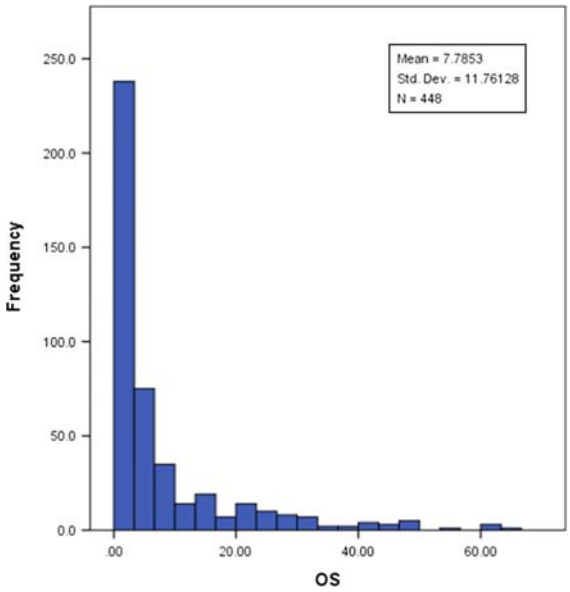

FIGURE A5. The frequency of the ownership (OS) percentage of all hospitality companies segment.

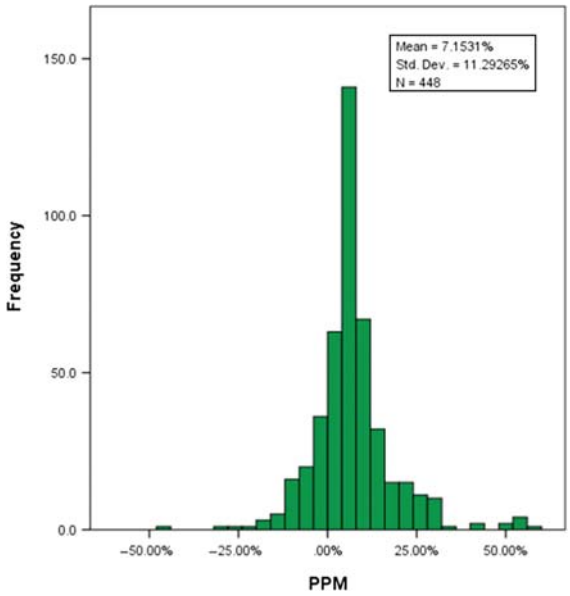

FIGURE A6. The frequency of the pretax profit margin (PPM) of total hospitality companies segment.

APPENDIX 2

Pearson Correlation Results

Segment 1: The hotel companies segment (10 companies).

TABLE A1. Pearson Correlation Result for Hotel Companies Segment

		Correlations	
		OS	PPM
OS	Pearson Correlation	1	.062
	Sig. (2-tailed)		.467
	N	140	140
PPM	Pearson Correlation	.062	1
	Sig. (2-tailed)	.467	
	N	140	140

Note. OS = ownership; PPM = pretax profit margin.

Segment 2: The restaurant companies segment (20 companies).

TABLE A2. Pearson Correlation Result for Restaurant Companies Segment

		Correlations	
		OS	PPM
OS	Pearson Correlation	1	−.212**
	Sig. (2-tailed)		.000
	N	308	308
PPM	Pearson Correlation	−.212**	1
	Sig. (2-tailed)	.000	
	N	308	308

Note. OS = ownership; PPM = pretax profit margin.
**Correlation is significant at the 0.01 level (2-tailed).

Segment 3: The hospitality companies segment (30 companies).

TABLE A3. Pearson Correlation Result for Hospitality Companies Segment

		Correlations	
		OS	PPM
OS	Pearson Correlation	1	−.086
	Sig. (2-tailed)		.069
	N	448	448
PPM	Pearson Correlation	−.086	1
	Sig. (2-tailed)	.069	
	N	448	448

Note. OS = ownership; PPM = pretax profit margin.

APPENDIX 3

Linear Regression Results

Segment 1: The hotel companies segment (10 companies).

TABLE A4. Linear Regression Result for Hotel Companies Segment

		ANOVA[a]				
Model		Sum of Squares	df	Mean Square	*F*	Sig.
1	Regression	.015	1	.015	.533	.467[b]
	Residual	3.808	138	.028		
	Total	3.823	139			

		Coefficients[c]				
		Unstandardized Coefficients		Standardized Coefficients		
Model		B	Std. Error	Beta	*t*	Sig.
1	(Constant)	.076	.018		4.301	.000
	OS	.001	.001	.062	.730	.467

Note. ANOVA = analysis of variance, OS = ownership.
[a] Dependent Variable: Pretax Profit Margin.
[b] Predictors: (Constant), OS
[c] Dependent Variable: Pretax Profit Margin.

Segment 2: The restaurant companies segment (20 companies).

TABLE A5. Linear Regression Result for Restaurant Companies Segment

		ANOVA[a]				
Model		Sum of Squares	df	Mean Square	*F*	Sig.
1	Regression	.083	1	.083	14.465	.000[b]
	Residual	1.761	306	.006		
	Total	1.844	307			

		Coefficients[c]				
		Unstandardized Coefficients		Standardized Coefficients		
Model		B	Std. Error	Beta	*t*	Sig.
1	(Constant)	.076	.005		14.886	.000
	OS	− .001	.000	− .212	− 3.803	.000

Note. ANOVA = analysis of variance, OS = ownership.
[a] Dependent Variable: Pretax Profit Margin.
[b] Predictors: (Constant), OS.
[c] Dependent Variable: Pretax Profit Margin.

Segment 3: The combined hospitality companies segment (30 companies).

TABLE A6. Linear Regression Result for Combined Hospitality Companies Segment

		ANOVA[a]				
Model		Sum of Squares	df	Mean Square	*F*	Sig.
1	Regression	422.709	1	422.709	3.332	.069[b]
	Residual	56580.454	446	126.862		
	Total	57003.162	447			
		Coefficients[c]				
		Unstandardized Coefficients		Standardized Coefficients		
Model		B	Std. Error	Beta	*t*	Sig.
1	(Constant)	7.797	.638		12.213	.000
	OS	−.083	.045	−.086	−1.825	.069

Note ANOVA = analysis of variance, OS = ownership.
[a] Dependent Variable: Pretax Profit Margin.
[b] Predictors: (Constant), OS
[c] Dependent Variable: Pretax Profit Margin.