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Ownership concentration, firm performance, and dividend policy in Hong Kong

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Abstract

We analyze a sample of 412 publicly listed Hong Kong firms during 1995–1998 in order to answer three questions. Does concentrated family ownership affect firm operating performance and value? Does it affect dividend policy? What is the impact of corporate governance on performance, value, and dividend payouts? Our results do not show a positive relationship between family ownership and return on assets, return on equity or the market-to-book ratio. In addition, we find a negative relationship between CEO duality and performance (where CEO duality is much more likely in family-controlled firms). We also find little relationship between family ownership and dividend policy. Only for small firms there is a significant negative relationship between dividend payouts and family ownership up to 10% of the company's stock and a positive relationship for family ownership between 10 and 35%. Dividend payouts in small firms also show little sensitivity to performance. Finally, the composition of the board of directors (proportion of independent non-executive directors, outsider-dominated board, presence of audit committees) has little impact on firm performance and dividend policy, particularly for small market capitalization firms. Our results for Hong Kong are in line with both Demsetz and Lehn (1985) [Demsetz, H., Lehn, K., 1985. The structure of corporate ownership: causes and consequences. Journal of Political Economy 93, 1155–1177] and Himmelberg et al. (1999) [Himmelberg, C.P., Hubbard, R.G., Palia, D., 1999. Understanding the determinants of managerial ownership and the link between ownership and performance. Journal of Financial

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Economics 53. 353–384], who show that concentrated ownership is not associated with better operating performance or higher firm valuation.

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1. Introduction

Does ownership concentration affect firm performance and value? The finance literature has been trying to answer this question since Demsetz and Lehn (1985) found no significant relationship between ownership concentration and the firm's return on equity. Other early studies in the U.S. highlighted a positive relationship between ownership concentration and firm value (Tobin's Q) for low levels of ownership, which can be attributed to the alignment of managerial incentives with shareholder interests. They also found a negative relationship at higher levels of ownership, which can be attributed to managerial entrenchment, since managerial shareholdings confer to management, among other benefits, protection against hostile takeovers (Morck et al., 1988; McConnell and Servaes, 1990; Hermalin and Weisbach, 1991).

On the other hand, in Japan, where firms are subject to monitoring from banks and takeovers are rare, the positive relationship between managerial ownership and firm value has been shown to be monotonic and holding for all levels of ownership (Morck et al., 2000). Similar evidence have been obtained by Hiraki et al. (2003), who found that managerial ownership is monotonically and positively related to the value of Japanese manufacturing companies, and by Chen et al. (2003), who showed that as ownership increases, there is greater alignment of managerial interests with those of stockholders for a sample of large Japanese firms.

However, there is little evidence on the relationship between ownership concentration and performance in South East Asian countries, despite the fact that many economies in the region are characterized by considerable family ownership of listed corporations (Claessens et al., 2000). Standards of corporate governance and investor protection are also lower in the region compared to the U.S. or Japan (La Porta et al., 1998), which adds a potentially interesting dimension to the relationship between ownership concentration and firm value or performance. In countries with poor investor protection, controlling shareholders may have the opportunity to expropriate minority shareholders.

Furthermore, Himmelberg et al. (1999) have cast doubt on previous findings by suggesting that the observed empirical relationships between ownership and performance may be the result of unobservable firm heterogeneity, which may affect both ownership concentration and firm value. They show that regressions of Tobin's Q on ownership concentration may be misspecified, because some unobserved determinants of Tobin's Q are also determinants of ownership concentration. These unobserved exogenous firm characteristics may induce a spurious relationship between Tobin's Q and ownership. Consequently, they find no relationship between ownership concentration and firm value after estimating firm fixed effects.