PACIFIC-BASIN FINANCE JOURNAL

ELSEVIER Pacific-Basin Finance Journal 10 (2002) 163–181

www.elsevier.com/locate/econbase

Ownership structure pre- and post-IPOs and the operating performance of JASDAQ companies

Kenji Kutsuna [a,*], Hideo Okamura [b], Marc Cowling [c]

[a] *Institute for Economic Research, Osaka City University, Sumiyoshi, Osaka 558-8585, Japan*
[b] *School of Business Administration, Kwansei Gakuin University, Nishinomiya, Hyogo 662-8501, Japan*
[c] *Research Centre for Industrial Strategy, Department of Commerce, University of Birmingham, Birmingham B15 2TT, UK*

Received 21 April 2000; accepted 14 November 2001

Abstract

This paper considers how the operating performance of JASDAQ companies is affected by the ownership structure pre- and post-IPOs. We document that operating performance varies according to managerial ownership in addition to the age and size of the firm. Our results on JASDAQ contrast with evidence from Cai and Wei [Pacific-Basin Finance Journal 5 (1997) 389], who analyze the operating performance of companies newly listed on the Tokyo Stock Exchange (TSE). They indicate the post-IPO deterioration in operating performance cannot be attributed to the reduced managerial ownership. © 2002 Elsevier Science B.V. All rights reserved.

JEL classification: G15; G32; G38; F21

Keywords: Initial public offerings; Bank monitoring; Venture capital investment; Manager's incentive; Operating performance; Ownership structure

1. Introduction

There is a long tradition of research concerning the relationship between ownership structure and company performance. First, the conflict of interest between managers and shareholders has been discussed in various studies (McConnell and Servaes, 1990; Craswell et al., 1997; Short and Keasey, 1999; Palia and Lichtenberg, 1999). Jensen

* Corresponding author. Tel.: +81-6-6605-2471; fax: +81-6-6605-2475.
E-mail address: kutsuna@eri.osaka-cu.ac.jp (K. Kutsuna).

PII: S0927-538X(01)00041-5

and Meckling (1976) point out that the interest of managers and shareholders diverge as managers' stakes decrease and ownership is dispersed. This implies that the firm's operating performance will decline after an initial public offering (IPO). Regarding the relationship between changes in ownership structure and operating performance of companies that go public, Jain and Kini (1994) report a significant decline in operating performance post-IPO and argue that this is partly explained by a decrease in the managers' incentives. In a similar vein, Cai and Wei (1997) and Cai and Laughran (1998) analyze the subsequent performance of seasoned and unseasoned equity offerings on the Tokyo Stock Exchange, but argue that the post-issue deterioration in operating performance cannot be attributed to reduced managerial ownership. Yet, the evidence is not conclusive. For example, Mikkelson et al. (1997) find no relationship between operating performance and ownership of officers and directors in IPO companies. This result is confirmed by Hirota (1996). By contrast, Yonezawa and Miyazaki (1996) find that the performance of Japanese firms rises as the ownership structure becomes concentrated and the managers' stake increases.

Second, in relation to monitoring, venture capital firms (VCs) are expected to play an important role in adding value to investee companies, thus producing high growth companies (Gorman and Sahlman, 1989; Sapienza, 1992; Lerner, 1994; Sapienza et al., 1996). Jain and Kini (1995) considered the relationship between venture capitalist participation and the post-issue operating performance of IPO firms, and found that VC-backed IPO firms showed superior post-issue operating performance compared to non-VC-backed IPO firms. Concerning stock price performance, Brav and Gompers (1997) investigated the long-run underperformance of IPOs documented by Ritter (1991) and Loughran and Ritter (1995). They found that VC-backed IPOs out-performed non-VC-backed IPOs and that the overall underperformance of IPOs is driven by small, non-VC-backed IPOs. Empirical results from Barry et al. (1990) and Megginson and Weiss (1991) also show that venture capital backing results in significantly lower initial returns.

In contrast to prior research in the US, investment from venture capital firms in Japanese firms did not favorably influence short-run stock price performance after flotation. For example, Kutsuna et al. (2000) find that companies in which venture capital firms were involved before flotation have lower stock prices than those with no VC involvement. Furthermore, companies in which venture capital firms sold their equity stakes shortly after flotation underperform compared to companies in which VCs did not invest or maintain their equity stakes after flotation.

Third, bank–firm relationships, in particular the Japanese banking system, have been a focal point for research (see example, Prowse, 1992; Aoki and Patrick, 1994; Kang and Shivdasani, 1995, 1999). Here, the focus is on the effectiveness of bank monitoring via shareholding, lending, and the appointment of directors. Yonezawa and Miyazaki (1996) report a significant and positive relationship between bank shareholding and firms' productivity. Moreover, Packer (1995) investigates whether bank shareholding affects the degree of underpricing of initial public offerings in Japan, and finds that either direct bank shareholding or through venture capital subsidiaries reduces underpricing. In addition, Packer (1995) concludes that bank shareholding reduces agency costs associated with asymmetric information. In contrast, Hirota (1996) reports that bank shareholding is