

The Impact of Different Types of Foreign Owners on Firm Performance - Case of Romanian Listed Companies

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The main objective of this paper was to investigate the relation between the different types of foreign owners and firm performance. The study was conducted for the manufacturing companies listed on both segments of Bucharest Stock Exchange. The final sample included 260 manufacturing companies. Return on Assets and Return on Equity were the measures of performance used for this study. For the different types of foreign owners we used dummy variables. Econometric tools like linear regression analysis were used for analysis. The results of the study suggest that there is no significant link between firm performance and the existence of different types of foreign owners.

Keywords: foreign owner, ultimate owner, performance, ownership structure

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1. Introduction

The general perception is that foreign ownership positively influences firm performance and profitability. This view is drawn from the assumption that foreign direct investment is a channel for technology, capital, managerial skills, training techniques and various intangibles that promote efficiency. Another benefit of foreign ownership is considered to be good corporate governance. The main objective of the paper is to explore whether could be established a significant relationship between firm performance and the types of the ultimate owners in a sample of Romanian manufacturing companies listed on Bucharest Stock Exchange. The paper deals with one important issue, namely the distinction between different types of foreign owners and the link between foreign ownership and performance.

2. Literature review

The literature about the relation between ownership structure and corporate performance is extensive. Various studies were run to study the effects of different types of ownership structure on firm performance in both developed and transition economies. Ownership structure can be examined along a number of dimensions: managerial ownership, family ownership, state ownership, foreign ownership and ownership concentration. Although the relation between firm performance and foreign ownership was widely investigated, the effects of different types of foreign owners on firm's performance remain rather unexplored.

The existing literature on identity of the owners emphasizes the different roles that various types of owners can play in setting a firm's strategy and influencing firm performance. For example Thomsen and Pedersen (2000) have found that the companies owned by financial institutions have higher market-to book values than companies in which the largest owner is a family, another company or the government. In the same paper the authors have found that companies whose largest owner is a family or another company have significantly higher sales growth. Also, nationality is found to influence the relationship between ownership structure and market-to-book values. Ownership identities in emerging economies can be even more multifaceted than those in developed economies.

The researches about ownership identity for emerging economy firms have found a similar importance of ownership identity with respect to its implications for firm strategy and performance (Singh et al., 2002). Typical ownership profiles in emerging economies include state ownership, institutional ownership, bank ownership, corporate ownership, family ownership, legal person ownership and employee ownership (Xu and Wang, 1999).

Krivogorsky and Grudnitski (2009) have investigated whether economic performance is consistently affected by the nature of a company's dominant stakeholder. After disaggregating the overall sample by specific ownership type and by country, they find statistical support for the relationship between dominant ownership and performance being strongly positive for firms in which banks and

families/ individuals are dominant owners and being inversely related when corporations are the dominant owners. Further they tested this relationship for more countries and the results suggested that countries are not homogenous in terms of their ownership landscapes, and, hence, their effects on performance.

Delios, Jian Wu and Zhou (2006) introduced a new perspective on the conceptualization and measurement of ownership identities of China's listed companies. They examined issues related to the ownership identity, firm strategy and firm performance for China's listed companies for the period 1991–2002. They identified 16 types of ownership identities.

Liu and Sun (2005) examined Chinese listed companies and find that 84% of the listed companies are controlled by the state, when the principle of ultimate ownership is considered. Therefore, this issue of ultimate control is important in Chinese listed companies, when considering a classification system that characterizes the identities of the various owners of a firm.

When we analyze the impact of ownership on firm performance it is important to consider who the ultimate owner is behind any shareholder. This problem has started to appear in the corporate finance literature, which has extensively analyzed the impact of the direct ownership structure of a firm on its value and the financial decisions made in the firm (Becht et al., 2003).

The ultimate owner is the last shareholder of a control chain (Delios, Jian Wu and Zhou, 2006).

We need to understand who is the ultimate owner of a firm when identifying ownership identities, as there is a potential conflict that can arise between the ultimate controller and the other stakeholders in a firm, if these owners and controllers are of a different nature. The ultimate owner of the company could exercise control while retaining only a small fraction of the equity claims on the company's cash flows. This is the key distinctive feature of the ultimate ownership structure which alters the typical agency conflicts inside a firm (Bebchuk et al., 2000). According to the law and finance literature, a legal system oriented towards minority investor protection is thought to prevent the controlling shareholders from expropriating minority stakeholders through complex ownership structures, such as pyramids (Bebchuk et al., 2000). However, Romania is considered a country with relatively low minority investor protection. As a consequence, the phenomenon of ultimate control in Romania can be pronounced.

According to OECD (2001) there are five categories of shareholders that control companies listed on Bucharest Stock Exchange: strategic investors, the employees associations, institutional investors, the state and natural persons. Strategic investors, institutional investors and natural persons can be both Romanian investors and foreign investors, while the origin of employees associations and state is Romanian.

3. Data

Our main data source for ownership data used in this paper is from AMADEUS, which is a fully integrated public company database and analytical information solution produced by Bureau van Dijk Electronic Publishing, SA (BvD). AMADEUS provides financials, ownership, news, ratings, earnings and stock data for the companies from all over European countries.

Information used for the empirical analysis concerned only manufacturing companies listed on both segments of BSE. In 2010 there were 395 manufacturing companies listed on both segments of BSE. Because our analysis concern foreign ultimate owner of the companies we disregarded listed independent companies. So, from 395 manufacturing companies we have eliminated 131 independent companies. Therefore, the remaining sample was of 264 companies which have as ultimate owner both foreign and domestic owners.

Identification of ultimate control and ownership rights distribution in Romania is not an easy mission. Romanian corporations have very distinctive ownership structures that have changed as a result of multi-stage mass privatization process followed by severe battles for corporate control. In general, ownership structures in Romania are distinguished by extremely low transparency, by dominance of holding structures with complex control chains, and by direct or indirect involvement of governments.

The ownership structures of Romanian listed companies are very concentrated. It is very hard to observe the ownership structure as the owners intentionally split their blocks and hide their identities through the use of nominees and foreign offshore holding companies. All these features require special treatment and can be captured only by making adjustments to the traditional methodology of identifying ultimate owners through the tracing of control chains introduced by La Porta, Silanes, and Shleifer (1998). Regarding the identification of ultimate owner of Romanian manufacturing companies we used the database provided by AMADEUS. This data base offers ownership information related to direct shareholders, ultimate ownership and controlling owners.

4. Variables used and specifications

In order to estimate the relationship between typology of owners and business performance, first it was necessary to establish the most appropriate performance indicators. The performance measures used in most of the literature to compare the performance of foreign capital with the performance of domestic capital are mostly indicators calculated on the basis of financial statement, such as return on equity, return on assets and return on sales. Another measure frequently used in some literature is Tobin's q. This is a ratio between company's market value (capitalization) and its book value. The indicator was developed by James Tobin and the company's capitalization is calculated by dividing the replacement value of its assets. In general, the literature considers that the assessment of performance based on accounting information does not take into account the company's future prospects as the case of indicators based on market values determined. However, the high volatility of the market gives us sufficient reason to doubt the effectiveness of the Romanian capital market.

Among the financial ratios, the most commonly used candidates for performance measures are return on assets (ROA), return on sales (ROS), and return on equity (ROE). Return on assets as the ratio of net profit to firm's assets gives an idea as to how efficient management is at using its assets to generate earnings. Return on sales is the ratio of yearly sales to assets and captures company's operational efficiency and growth opportunities. Return on equity (ROE), the ratio of net profit to equity, captures firm's efficiency at generating profits from shareholders' equity.

In general, the existing literature documents the appropriateness of these financial ratios as performance measures in transition context. However, there are potential problems with the usage of the above-mentioned ratios. ROE is subject to the most serious accounting distortions. The problem is that the positive ROE does not always witnesses that a company is profitable. If the corporation incurs losses during several accounting periods, accumulated losses appear in the equity section and may result in negative value of equity. Therefore, positive values of ROE may occur as the ratio of two negative entries, loss to equity. It may turn out that loss-maker has a positive return on equity. As to the remaining ratios, ROA and ROS, they may also suffer from the accounting errors (both random and intended), missing values in financial reports that cause the bias in estimation. However, they can be mitigated by applying screening procedures, as many researchers do. The magnitude of possible distortions in measuring ROA and ROS is therefore much smaller than in case of ROE and these profitability ratios are considered to be appropriate performance measures. In general, it is reasonable to refer to several performance measures rather than to the single indicator in order to compensate for individual shortcomings. The main dependent variables used in this study are the return on equity (ROE) and Return on Assets (ROA). These returns were calculated based on financial statements of 2010.

As independent variable we used for the types of ultimate owners, a qualitative variable with 5 categories. For this we defined 4 dummy variables (tip1, tip2, tip3 and tip4). The value taken by these variables are presented in table no. 1

Table no. 1 – value of dummy variables

Categories of shareholder	Tip 1	Tip 2	Tip 3	Tip 4
Employees associations	1	0	0	0
Institutional investors	0	1	0	0
One or more named individuals or families	0	0	1	0
State	0	0	0	1
Industrial company	0	0	0	0

Institutional investors are organizations which pool large sums of money and invest those sums in securities, real property and other investment assets. Examples of typical institutional investors include banks, insurance companies, retirement or pension funds, hedge funds, investment advisors and mutual funds. For the purpose of this study we aggregated ultimate owners from these categories in a single category, which is "institutional investors". In our sample we had 29 manufacturing companies which have as ultimate owner an institutional investor (1 – bank, 22 – financial companies and 6 - Mutual and Pension Fund).

Industrial company is a generic term. This category includes all companies that are not banks or financial companies nor insurance companies. They can be involved in manufacturing activities but also in trading activities (wholesalers, retailers, brokers, etc.). They include also companies active in B2B or B2C non-financial services.

The category "one or more named individuals or families" include single private individuals or families, shareholders designated by more than one named individual or families are in this category. The idea behind this is that they would probably exert their voting power together.

We considered a dummy variable to capture the origin of owners, foreign or domestic (FOR). This variable takes the value 1 – if we have a foreign owner and value 0 – otherwise.

The control variables are other factors besides the types of foreign owners that can affect the performance of a company and whose effect we want to control. To take into account the influence of these factors in the analysis we introduced a set of control variables. Thus it can be checked the certainty of the relationship between the dependent variable and independent variable. The most important control variables found in the literature and used in this study are: company size (measured as logarithm of total sales), leverage (the fraction between debt and equity), capital intensity (measured as fraction between total assets and number of employees).

5. Results and interpretation

Table 2 is the descriptive statistics of main variables for the considered samples. It shows that the general level of performance in 2010 for Romanian listed manufacturing firms is negative (average ROA of -1,9%, average ROE -8,20% of, average Profit margin -4,01% and average ROCE of -5,57%. For 24 companies in the sample calculation of ROE is non-significant, because these companies have negative results and also negative equity. Also we can observe that 27,67% of Romanian listed manufacturing companies have foreign ultimate owners.

Regarding the types of owners: 3,97% from the sample companies have as ultimate owner employee associations, 11,46% of companies have as ultimate owners an institutional investor, 43,87% from companies have as ultimate owner individuals or families, 3,95% are state companies. The rest, which means 36,77% of companies are companies which have as ultimate owner an industrial company.

Table no. 2- Descriptive Statistics

	N	Minimum	Maximum	Mean	Std. Deviation
ROA	251	- 97,58	37,16	- 1,9065	13,04737
Profit margin	232	- 92,59	44,84	- 4,0148	20,27105
ROE	229	- 518,70	217,01	- 8,1993	53,06840
ROCE	185	- 505,47	36,07	-5,5679	48,90152
FOR	253	0,00	1,00	0,2767	0,44824
tip1	253	0,00	1,00	0,0395	0,19523
tip2	253	0,00	1,00	0,1146	0,31920
tip3	253	0,00	1,00	0,4387	0,49722
tip4	253	0,00	1,00	0,0395	0,19523
CONC	253	0,00	1,00	0,7887	0,24520
HERF	253	0,00	1,00	0,5667	0,25720
Capital intensity 1	252	-0,58	3,69	1,4563	0,69590
Growth rate of sales	251	-1,00	12,11	0,1501	1,27374
Size S	250	-0,01	5,63	3,3690	0,94961
LEVERAGE	253	0,01	4,56	0,5419	0,51248
Valid N (listwise)	170				

For capturing the interaction effect between the two qualitative variables, the existence of foreign ownership (FOR) and the typology of investors (TYPE) we define a variable called "interaction dummy" (FOR_TYPE). This variable gives the joint or simultaneous effect of the two dummy variables (existence of foreign ownership and the different types of owners) and is calculated as product of dummy variables. The variable FOR_TYPE 2 capture the effect of foreign institutional investors and variable FOR_TYPE 3 capture the effect of one or more foreign named individuals or families. Given the fact that employee

ownership and state ownership are both categories of domestic ownership, the variables FOR_TYPE 1 and FOR_TYPE 4 will not be included in the analysis.

Table no. 3 – Coefficients of regression

	Model 1 – ROE dependent variable		Model 2 – ROA dependent variables	
	Coefficients B	Sig.	Coefficients B	Sig.
(Constant)	-12,934	(0,549)	1,964	(0,679)
FOR	-12,449	(0,296)	1,543	(0,571)
tip1	-11,521	(0,521)	2,200	(0,610)
tip2	-3,154	(0,828)	4,629	(0,183)
tip3	1,938	(0,842)	2,995	(0,184)
tip4	-70,149	(0,001)	5,277	(0,265)
for_tip2	22,211	(0,351)	-2,406	(0,661)
for_tip3	-5,977	(0,767)	-4,412	(0,356)
size_S	7,662	(0,065)	0,602	(0,509)
LEV_2	-56,127	(0,000)	-10,811	(0,000)
capital_intensity_2	4,159	(0,526)	-1,306	(0,389)
R Square	0,140		0,159	
Adjusted R Square	0,101		0,123	
F	3,514		4,471	
Sig.	0,000		0,000	

We can observe that the firm performance, expressed by ROA and ROE is significant influenced by the simultaneously variation of independent variables: foreign capital, type of ownership and size of the company, leverage and capital intensity. The coefficients of dummy variables represent the difference of performance between companies with domestic ownership and having as ultimate owner an industrial company and companies with foreign ownership and different types of ultimate owners.

6. Concluding remarks

We analyzed the impact of different types of foreign owners on the financial and economic performance of Romanian manufacturing companies listed on both segments of Bucharest Stock Exchange. The proposed models of the study show no significant results for the relationship between different types of foreign owners and firm performance.

The validity of the results is drawn primarily depends on the nature of the sample. Our sample included only manufacturing companies listed on BSE. For future research we will try to extend the sample to others industry. There are many factors that influence firm performance and not all of them have been controlled for and to test the impact of different types of foreign investors, it may be necessary to collect data for a longer time horizon.

The findings of this study should be analyzed in the context of ownership structure and cultural background in Romania. Cultural features of the Romanian society are also an important factor that should be taken in to account for the sound analysis of the findings. As discussed above, Romanian companies have very distinguishing features. Romanian firms are mostly owned by families. Families are not only the controlling shareholders, but they also are very involved with the management of the family firms.

For further research, we would like to study the channels through which different types of foreign owners can affect firm performance. We hope to separate this problem and carry out further studies to investigate the effects of foreign owners on specific financial activities (investment, earning management, corporate transparency, dividend policy, capital structure, etc).

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