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CORPORATE OWNERSHIP STRUCTURE AND FIRM VALUE: EMPIRICAL EVIDENCE OF JSE-LISTED FIRMS, SOUTH AFRICA

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Abstract

This paper examines the relationship between corporate ownership structure and firm value of JSE-listed firms in the phase of the Black Economic Empowerment program in South Africa. Since the end of the apartheid era, corporate governance practices have evolved and the enactment of the BBE Act has altered ownership and control in the South African corporate sector. Using data from 187 firms between 2004 and 2016, we observed that ownership concentration measured by five large shareholders and foreign ownership has a negative impact on firm value proxied with Tobin's Q and return on assets, while domestic share ownership has a positive relationship with corporate performance. Contrary to the agency theory notion on the role of large shareholders in minimizing losses that arise from the separation of ownership and control and significant foreign investors corporate governance practices in the host countries, the results obtained in this study suggest that local shareholders in the host capital market are important in strengthening corporate governance practices and improve corporate performance. This study contributes to the ownership-firm value relationship literature by offering new evidence on the impact of ownership concentration, foreign ownership, and domestic ownership in an emerging market undergoing transformation through programs addressing its historical inequalities.

Keywords: Ownership Structure, Corporate Governance, Dynamic Model, Black Economic Empowerment, South Africa

JEL Classifications: G10, G15, G17

1. Introduction

A lot of attention has been drawn to ownership structure and firm value since Berle and Means (1932) uphold the significance of the separation of ownership and control in relation to shareholders' diffusion. As the number of shareholders increase, the goal of corporate wealth creation may be compromised, as corporate resources are often used to amass corporate

benefits and non-value maximizing by managers. To minimize losses that arise from the separation of ownership and control, the principal (the shareholders) needs to supervise and motivate the agents (the managers) (Jensen and Meckling, 1976). In this regard, the outlook of shareholders' value maximization depends on the ownership structure.

The structure of shareholders in countries hovers between large shareholders, foreign investors, domestic investors, among others (Shleifer and Vishny, 1997). Conclusions drawn from various empirical findings on ownership structure and firm value relationship seem contradictory to corporate environments and institutional frameworks (Maher and Andersson, 2002). In this regard, we focus on the corporate ownership structure and firm value of JSE listed in South Africa, an emerging market economy that introduced Black Economic Empowerment (BEE) as a way of addressing historical ownership imbalances created during the apartheid era.

This study contributes to the literature on the ownership-firm value relationship in several ways. First, we offer new evidence on the impact of ownership concentration, foreign ownership, and domestic ownership in an emerging market (South Africa) that is transforming its economy through a program such as BEE. None of the existing studies provide any emerging market evidence, even though emerging markets such as South Africa are transforming ownership structure and improving their corporate governance systems. Second, from a methodological perspective, the current work improves on previous work by using a dynamic panel data model. This study employs the System Generalized Method of Moments (System GMM) estimation technique to take care of the endogeneity problem between firm value and some of the regressors, and also the problem of autocorrelation which is prevalent in dynamic panel estimations. Our results show evidence that domestic ownership has a positive influence on JSE-listed firm values as measured by Tobin's Q and ROA, while ownership concentration and foreign ownership have a negative influence.

The rest of the paper is structured as follows: Section 2 presents an overview of ownership and control on the JSE in the South African corporate context. Section 3 provides an overview of corporate governance in the South African corporate context. In Section 4, we review the empirical literature and develop our hypotheses. The data and methodology are discussed in Section 5. Section 6 presents and discusses the estimation results, robustness checks, and limitations of the analysis. Finally, Section 7 concludes the paper.

2. Ownership and control on the JSE in South Africa

The debate on corporate ownership in South Africa has been ongoing since the demise of the apartheid regime when the economy was controlled by the white minority (Chabane *et al.* 2006). The dawn of democracy in 1994 led to the formulation of new policies and regulations to reform the economy to redistribute the national wealth and redress inequalities among all South Africans (Maloka, 2004). The new government adopted a multi-faceted institutional framework approach that embraced several socio-economic development programs (Esser and Dekker, 2008). These include BEE in 1998, which was promulgated to promote the participation of previously disadvantaged South Africans under the apartheid government in economic activities through ownership and control in different sectors (Tangri and Southall, 2008; Freund, 2007; Esser and Dekker, 2008). The BEE policy was first initiated under the competition law to address the high concentration of ownership and control of the economy and to promote black people's participation in economic activities (BEECom, 2001, Roberts, 2004). The South African government also established the National Empowerment Fund (NEF) Act to acquire shares in private and state-owned enterprises and, thereafter, to be sold to historically disadvantaged individuals (BEECom, 2001). Subsequently, the Broad-Based Black Economic Empowerment (B-BBEE) Act was introduced in 2003 as a result of the failure of NEF to help previously disadvantaged South Africans to acquire such shares and the external shock of the Asian financial crisis in 1998-1999 that caused huge indebtedness among BEE equity vendors (Sartorius and Botha, 2008; Veloso, 2009). The B-BBEE aimed to promote the full participation of previously disadvantaged South Africans under apartheid government for more equitable distribution of wealth through ownership and management, enterprise development, employment equity, skills development, preferential procurement, and corporate social investment (Ponte *et al.* 2007).

Ownership and management control were the topmost important tools of the BEE to deracialize the South African market and create a free market economy (Sartorius and Botha, 2008; Thomas, 2017).

The enactment of the B-BBEE Act also led to the reformation of the listing requirements on the JSE, as did the King II Report on corporate governance in 2002 (Esser and Dekker, 2008). The 2016 King IV Report on corporate governance published in 2016 also prompted the amendment of listing requirements for JSE-listed companies to promote racial diversity at board level and annualized disclosure of B-BBEE performance in compliance with the amended B-BBEE Act of 2013 (Africa Business Communities, 2017). The Act requires that directors promote the interests of stakeholders rather than shareholders by giving effect to the triple context corporate governance approach set out in the King Report (Esser and Dekker, 2008). Should they not comply with these requirements, they could be found to be in breach of their fiduciary duties (Sartorius and Botha, 2008).

Prior to the democratic dispensation in South Africa, ownership and control of JSE-listed firms were concentrated among certain groups and family-owned conglomerates (Kantor, 1998). In compliance with the Code of Good Practice issued in 2007, the B-BBEE program aimed to achieve 50.1% ownership and control of corporate activities by previously disadvantaged South Africans (Dongwana, 2016; Department of Trade and Industry South Africa, 2003). This resulted in a significant increase in transactions in the equity market and ongoing change in share ownership patterns. Such ownership diffusion is contrary to Berle and Means's (1932) suggestion that shareholder concentration should be promoted to ensure adequate monitoring of corporate assets, minimize corporate risk, and enhance management.

Based on the aforementioned, we investigated the interaction of corporates ownership structure which includes ownership concentration, foreign and domestic ownership on firm value of JSE-listed companies since the adoption of corporate governance practices in the phase of the BEE program in South Africa.

3. Corporate governance concern on corporate ownership in South Africa

The agency theory deals with the conflicting interests between the principal (owners) and agents (managers) (La Porta *et al.* 2000; Walsh and Seward, 1990; Ward and Filatotchev, 2010). The principal-principal conflict of interests occurs when dominant owners with excessive power gain influence over the firms at the disadvantage of minority shareholders. Expropriation by the majority owners who have controlling interest over the corporate assets will result in principal-principal agency problems that are detrimental to firm value (La Porta *et al.* 2000; Walsh and Seward, 1990). In this regard, the nature of the firm has heightened the importance of corporate governance practices concerning ownership structure and firm value in numerous studies.

Special attention is drawn to developed economies such as the United Kingdom (UK) and the United States of America (USA), among others, where the traits of shareholders' diffuseness and well-established corporate governance quality are more pronounced (Nguyen *et al.* 2014). Like many other countries, the corporate governance structure in South Africa resembles that in the UK. The South African Companies Act was adopted in 1973, and the English common law plays a significant role in corporate governance guidelines in South Africa (West, 2009). The guidelines on corporate governance reports are given via the King's code issued by the South Africa Institute of Directors (Steyn and Stainbank, 2013). The King Committee in South Africa was set up after the release of the Cadbury reports in the UK in 1992. The idea of the corporate governance committee is to provide firms with enabling policies and principles that govern the corporation effectively and assist the board of directors to monitor and make decisions that maximize the shareholder's wealth and reduce the expropriation risk (Ntim, 2013). The assumption of King's corporate governance is the triple contest of the economy, society, and the environment to improve firm value (King ME, 2016). The King's corporate governance reports are concerned with solving the deviation of interest that could occur among stakeholders by attributing a triple contest approach to protect the interest of the firm (Abdo and Fisher, 2007). Following this, this study considers the interaction of corporate governance mechanisms on the relationship between ownership structure and firm value in South Africa.

4. Literature review and hypothesis development

4.1. Ownership concentration and firm value

The relationship between ownership concentration and firm value has been the focal point of corporate governance literature (Shleifer and Vishny, 1997; De Miguel *et al.* 2004; Jensen and Meckling, 1976). Berle and Means (1932) posit that shareholders' ownership concentration addresses problems arising from the separation of ownership and control and thus improves firm value. Jensen and Meckling's (1976) agency theory states that separation of ownership and control enables managers to pursue personal gain. Large shareholders can prevent this by monitoring decisions and using their votes to remove managers whose interests conflict with those of the shareholders (Shleifer and Vishny, 1997; Berle and Means, 1932; Demsetz and Lehn, 1985). In this regard, an increase in ownership concentration is expected to drive the reduction in agency costs and increase corporate performance.

Large shareholders provide more desirable corporate confidence to corporate investors and assure them of protecting their interests (Shleifer and Vishny, 1986). The earliest study of Berle and Means (1932) explained that ownership concentration has a positive interaction with corporate profitability. They pinpointed that the wide-spreading shareholders reduce owners' residual claims on corporate decision and control, thereby reducing firm value. Similarly, Hill and Snell (1989) observed that ownership concentration influences firm profitability. Using the data of Fortune 500 companies in the US, they contended that large shareholders offset unnecessary investment diversification strategies of managers and minimize conflicts between managers and shareholders. Large shareholders manage managers' investment diversification strategy with adequate monitoring and benefit/incentivize to motivate them to maximize the value of shareholders (Jensen and Meckling, 1976; Thomsen and Pedersen, 2000). Effective monitoring facilitates investment growth and risk-bearing that enhances firm value (Singal and Singal, 2011). Thomsen and Pedersen (2000) found that large shareholders put pressure on managers to prevent ill-conceived diversification and enhance corporate performance in a study of ownership concentration and shareholder value relationships among large European companies. A study by Singal and Singal (2011) on Indian corporate sectors concluded that large shareholders outperformed diffuse owners in terms of attracting investment and increasing firm value, irrespective of the type of owner. Claessens *et al.* (2000) used cross-sectional data on the Czech Republic listed firms and found a positive relationship between ownership concentration and firm value, as well as labor profitability. Kapopoulos and Lazaretou (2007) found a positive relationship between ownership concentration and firm profitability using dynamic panel data on 175 Greek-listed firms. They argued that higher profitability reduces debt and interest on debt that increases firms' operating costs. Ownership concentration is thus positively related to firm value.

Arguments in favor of ownership concentration underplay conflicts of interest between majority and minority shareholders that lead to expropriation and poor corporate performance (Shleifer and Vishny, 1997; Porta *et al.* 1999; Walsh and Seward, 1990; Ward and Filatotchev, 2010). The risk of expropriation (value diversion) increases when large shareholders with controlling interests monitor corporate management for their own benefit using unethical means (Shleifer and Vishny, 1997). Earle *et al.* (2005) used panel data on firms listed in the Budapest Stock Exchange in Hungary and found that while a single owner is positively related to firm performance, the marginal costs of large shareholders may outweigh the benefits when they increase beyond a certain level. Demsetz and Lehn (1985) also concluded that diffuse shareholders are inversely related to firm value.

Another school of thought argues that large shareholders have both positive and negative impacts on firm value. Shleifer and Vishny (1997) contended that adequate monitoring can improve corporate performance and prevent opportunistic value diversion. Hence, corporate governance is required for efficient and effective performance. However, the corporate governance literature has identified ownership concentration as an influential mechanism that alleviates the free-riding problem and mitigates conflicts of interest, thus enhancing firm value (Shleifer and Vishny, 1997; Claessens *et al.* 2000). Nonetheless, it should be borne in mind that large shareholders represent an incomplete solution as they can experience conflicts of interest with minority shareholders. Claessens *et al.* (2000) and Porta *et al.* (1999) observed that weak

legal and institutional frameworks of the countries where the firm operates and the failed contractual agreements between the principal and agents make ownership concentration to influence firm value. Therefore, this calls for the importance of ownership concentration on efficient corporate governance mechanisms to improve firm value (Gugler, 1998; Thomsen and Pedersen, 2000). Considering the literature reviewed, we hypothesize that there is a positive relationship between ownership concentration and firm value of JSE-listed companies.

4.2. Foreign ownership and firm value

The growing consensus on foreign ownership to improve firm value in host countries has attracted the substantial interest of policymakers and scholars. In recent years, capital markets in developed and developing economies are more globalized through mergers and acquisitions and cross-listing of firms across national boundaries. Globalized capital markets allow foreign investors to easily invest in firms based in different locations across the globe.

The JSE has grown to become one of the world's largest stock exchanges and one of the major investible global stock markets, and it continues to magnet investors to South Africa. It is, therefore, reasonable to present evidence relevant to issues of foreign ownership and firm value in South Africa. Many studies have documented the reasons why foreign-controlled firms have advantages over domestic firms (Gugler, 1998; Ongore, 2011; Phung and Mishra, 2016). The benefits of foreign ownership in host economies include capital opportunities, modern technology, managerial techniques, access to the international market, increase in productivity, increase in industry competitiveness in the host countries, labor productivity, better investment returns, improvement in corporate governance practices, among others, and thus enhance firm value.

A study by Weche Gelübcke (2013) on foreign ownership and firm performance in Germany's services sectors established that foreign-controlled affiliates perform better than domestic affiliated firms. The study found that foreign ownership provides better employee wages, higher productivity, and superior export intensity that tends to increase the country's gross domestic products. Khanna and Palepu (1999) studied Indian-listed firms and found that foreign institutional ownership provided adequate monitoring skills better than domestic institutional ownership. They highlighted that companies with foreign-affiliated operations in the host countries' emerging markets like India reduce the risk of corporate investment and improve firm performance and thus, attract more foreign investors to the firm. Ongore (2011) found that Kenyan firms with more presence of foreign ownership tend to perform better than their local counterparts and noted that foreign-owned firms enjoy massive resources that can be raised when the need arises. Ongore (2011) further observed that the replication of the corporate management system of affiliates abroad improves firm performances.

Koo and Maeng (2006) studied the foreign ownership and investment relationship in Korea and found that cash-flow sensitivity to investment decreases with the high level of foreign ownership. They inferred that foreign ownership may ease a firm's financial constraints and improve accessibility to external finance, and thus, motivate more investment for higher firm value. Using dynamic panel data, Wellalage and Locke (2012) studied Sri Lankan-listed firms and found a positive relationship between foreign ownership and firm performance.

Barbosa and Louri (2005) studied the relationship between corporate ownership and corporate performance in Portugal and Greece. They observed that multinational-owned corporations outperform the domestic firms in Portugal and Greece. They argue that corporate governance mechanisms of a local firm with capital advantage and managerial skill through a foreign-controlled firm influence the firm's performance. Phung and Hoang (2013) pinpointed that a higher level of foreign equity ownership and adequate monitoring improves firm values. They suggested that corporate governance mechanisms can improve with an increase in foreign equity ownership to an appropriate level. Pervan *et al.* (2012) found that the role of foreign ownership in the firm has positively impacted the strategic decision-making of firm performance in Croatia. They argued that it is the investment preference of foreign investors, which generates a superior return that increases corporate performance in Croatia. Using a panel data analysis in China, Greenaway *et al.* (2014) found that foreign ownership contributed to firm modern technology, capital-intensive, better governance mechanisms, quality managerial skill, and international

network that promote firm productivity. Based on the literature reviewed, we hypothesize that there is a positive relationship between foreign ownership and firm value of JSE-listed companies.

4.3. Domestic ownership and firm value

The state, private equity firms, and individuals may hold shares in local firms (Gugler, 1998). Given that, like foreign owners, domestic owners are responsible for management decisions and monitoring, local shareholders are expected to improve the firm value and mitigate the conflicts of interest to ensure a positive impact on firm value.

There is limited empirical research on the impact of domestic ownership on firm value. Douma *et al.* (2006) used multiple theories to examine the Indian capital market and found that local shareholders comprised the majority of owners of the Indian firms. The study established a positive relationship between domestic ownership and firm performance. They argued that superior returns are achieved when local investors hold a large proportion of shares; this enables incentives to be offered to managers and ensures adequate monitoring to improve firm value.

In contrast, a study by Pervan *et al.* (2012) on listed Croatian firms found a negative relationship between domestic ownership and firm profitability. They concluded that locally controlled firms' returns are no better than those that are owned by foreign shareholders. Khanna and Palepu (1999) explored the relationship between ownership by domestic financial institutions and firm performance and concluded that domestic ownership is negatively related to firm value. They argued that local investors do not ensure adequate management monitoring and support to promote effective governance.

Against this background, this study investigated the effect of domestic ownership on the firm value of JSE-listed companies in South Africa's equity market in light of policies that aim to promote diversification and expansion of local shareholders, including affirmative action programs and changes in the JSE's listing requirements. We hypothesize that there is a positive relationship between domestic ownership and the firm value of JSE-listed companies.

5. Research design

5.1. Data nature and sources

Data on JSE-listed firms in South Africa, which includes ownership variable, control variables, and firm value variables, were sourced from the IRESS and Bloomberg online databases. The study period (2004 to 2016) was influenced by data availability and covers both the adoption and amendment period of King Code II, III, and IV report on corporate governance and enactment of the B-BBEE Act in South Africa. The JSE-listed firms adopted corporate governance in 2002, and B-BBEE was enacted in 2003 by the South African government. Following previous studies (Douma *et al.* 2006; Phung and Mishra, 2016; De Miguel *et al.* 2004), financial services firms were eliminated. Firms delisted by the JSE due to the violation of listing requirements and firms with inadequate information were also excluded from the study. As a result of this data cleaning exercise, 187 firms were selected for analysis.

5.2. Description of variables

The firm value was proxied by Tobin's Q and return on assets (ROA) which represent dependent variables. The explanatory variables are ownership concentration, foreign ownership, domestic ownership. Other control variables include leverage, profitability, liquidity, board size, board remuneration, BEE firm, and firm size.

5.2.1. Dependent variable

Firm value is described as a benefit derived from the effective and efficient utilization of the firm resources over time (Al-Matari *et al.* 2014). Firm value symbolizes the circumstances that surround the management of the firm to generate a reward for the principal. Firm value is measured by using accounting-based and market-based indicators (Al-Matari *et al.* 2014). An

accounting-based indicator measures the performance based on accounting standards established by the professionals, and it explains the inward-looking aspects of the firm operation (Demsetz and Villalonga, 2001; Kapopoulos and Lazaretou, 2007). The accounting-based measure includes return on assets (ROA), return on equity (ROE), and earnings per share (EPS), profit margin (PM), among others. The market-based performance measures are characterized by forward-looking aspects of the firm's operation that reflect market future expectations about the firm's performance to shareholders (Al-Matari *et al.* 2014). The market-based measures include Tobin's Q, dividend yield (DY), market value added (MVA), the price-earnings ratio (PE), among others. This study uses Tobin's Q and return on assets (ROA) as a proxy of firm value to minimize potential weakness in the valuation of corporate performance.

Tobin's Q or Q ratio is described as the market value of the enterprise's equity plus the book value of interest-bearing debt to the replacement cost of its fixed assets. Further, Tobin's Q is used to capture firm market performance that explains the sum of the market value of equity and book value of debt over the book value of total assets (Morck, 2000; Demsetz and Villalonga, 2001; Douma *et al.* 2006). ROA is calculated as the operating profit after tax divided by the total assets. ROA evaluates how efficient managements are in utilizing available resources to generate returns to all the providers of funds (Demsetz and Villalonga, 2001).

5.2.2. Explanatory variables

Following previous studies (Demsetz and Lehn, 1985; Demsetz and Villalonga, 2001), ownership concentration is measured as the percentage of ordinary share equity held by large five shareholders in the firm. In this study, foreign ownership is described as the percentage of a firm's shares (votes) held by foreign or international investors. Managerial ownership is measured as the sum of ordinary shares owned by insiders such as the board of directors, the CEO, and the managers that run the firm (De Miguel *et al.* 2004; McConnell and Servaes, 1990; Morck *et al.* 1988; Short and Keasey, 1999; Himmelberg *et al.* 1999; Zondi and Sibanda, 2015; Mugobo *et al.* 2016; Ntim, 2013; Al-Matari *et al.* 2013; Meyer and de Wet, 2013).

5.2.3. Control variables

To ease the potential estimation biases caused by omitted variables, we include control variables that include leverage, profitability, liquidity, board sizes, board remuneration, firm sizes, firm BEE rating to uphold accurate effect of ownership concentration, and managerial ownership influence on firm value.

Leverage measures the amount of funding provided by outsiders. Debt is an alternative source of finance for firm operations, and it is expected to have a positive and negative effect on firm value. Jensen and Meckling (1976) observed that leverage serves as one of the main internal governance mechanisms to mitigate agency costs when there is a cash-flow shortage, and this need arises to enhance firm value. Agrawal and Knoeber (1996) added that when debt is used to finance a firm, lenders motivate managers to monitor its operations, thereby improving firm performance.

Firm profitability is a significant factor when measuring corporate value. Many previous studies on ownership structure found a positive association between profitability and firm value (Phung and Mishra, 2016). Higher profitability indicates efficient use of the firm's resources and is, thus, expected to influence firm value. Firm profitability is significant when considering the dividend policy, retained profit, investment opportunities, reduction in debt finance, and access to long-term finance and lease finance that affect firms' operations (Himmelberg *et al.* 1999; Phung and Mishra, 2016).

Highly liquid firms are expected to have better investment prospects and improved access to debt finance, and superior performance (Cho, 1998; Uno and Kamiyama, 2010). Liquidity improves the firm's credit rating and access to lease finance and other credit finance in times of financial distress. However, studies on ownership structure have produced mixed findings on the relationship between liquidity and firm value. Using data obtained from Tokyo Stock Exchange, Uno and Kamiyama (2010) found that a low level of liquidity increases long-term investment and

thus increases firm value. They explained that ownership concentration and managerial ownership can lead to poor firm liquidity and future firm value. Cho (1998) noted that higher liquidity opens investment opportunities and access to finance to improve firm performance.

While board sizes have been found to influence firm value, there is no optimal board size (Fauzi and Locke, 2012). A larger board is preferable as it promotes diversity and brings in more professional managers to oversee the operations of the firm and maximize firm value (Marashdeh, 2014). Since boards are the apex of the internal control mechanisms that monitor operations and provide management support, larger boards have a propensity to provide more skills and knowledge and offer diverse perspectives that are likely to enhance corporate performance. Jensen (1993) proposes that, while larger boards mean higher monitoring costs, they offer better opportunities and superior decisions that increase firm value.

Board remuneration also plays a significant role in monitoring management and is expected to influence firm value. Jensen and Meckling (1976) propose that incentive alignment (board compensation) will mitigate conflicts of interest and improve firm value. Miyianda *et al.* (2012) investigated the relationship between directors' remuneration and company performance among firms listed on the Nairobi Securities Exchange in Kenya using ROE, earnings after tax (EAT), and Tobin's Q as measures of performance and found that board remuneration is positively related to firm value. They contended that efficiency and effective utilization of firm resources to improve firm value can be a gauge of board remuneration. Yatim (2013) conducted a cross-sectional analysis of Malaysia's listed firms and concluded that directors' remuneration is positively and significantly related to firm value. The author noted that board remuneration not only encourages sound firm performance but also the ways in which firms' results are achieved.

We control for the BEE affirmation program introduced by the South African government as part of the framework to diffuse share ownership structure in the country after the end of the apartheid government. The BEE program aims to transform the economy through ownership, management, and control of companies by incorporating previously disadvantaged black people, addressing inequality among both private and state-owned enterprises, and creating a free market economy (Dongwana, 2016). The BEE rating is measured using a balanced scorecard introduced by the South Africa government as a benchmark to assess the BEE program in the firms operating in the country since the enactment of the B-BBEE Act of 2003. The balanced scorecard is used to check the adherence of firms in South Africa to the BEE plan by the government.

We also controlled for firm size in this study. Short and Keasey (1999) note that large firms can draw on substantial resources, both internal and external, that reduce financial constraints and have a beneficial effect on firm value. Jensen and Murphy (1990) propose that firm size may be employed as a control proxy when analyzing the principal-agent problem. However, they add that when a firm is large, this could boost managers' confidence to exert more control and thus lead to conflicts of interest between managers and shareholders. Himmelberg *et al.* (1999) argue that in large-sized firms, insider shareowners have higher expectations, and this leads to an increase in monitoring costs. Jensen and Meckling (1976) argue that an increase in firm size leads to increased management costs and gives management more discretion to increase firm value.

5.3. Empirical models

The empirical models employed to test the study hypotheses are given in Equation 1, 2, and 3.

$$FV_{it} = \beta_0 + \gamma FV_{i,t-1} + \phi_2 OC_{it} + \varphi Z_{it} + w_i + v_t + \varepsilon_{it} \quad (1)$$

$$FV_{it} = \beta_0 + \gamma FV_{i,t-1} + \phi_2 FO_{it} + \varphi Z_{it} + w_i + v_t + \varepsilon_{it} \quad (2)$$

$$FV_{it} = \beta_0 + \gamma FV_{i,t-1} + \phi_2 DO_{it} + \varphi Z_{it} + w_i + v_t + \varepsilon_{it} \quad (3)$$

where; FV_{it} denotes the value of firm i at time t , $FV_{i,t-1}$ is lagged value of firm value, OC_{it} is ownership concentration of firm i at time t , FO_{it} is the foreign ownership of firm i at time t , DO_{it} is the domestic ownership of firm i at time t , and Z_{it} is the matrix of the control variables which include leverage, profitability, liquidity, board sizes, board remuneration, BEE firm, and firm sizes.

5.4. Endogeneity of ownership structure variables

Analyzing the relationship between ownership structure and firm value is fraught with endogeneity challenges. Endogeneity was acknowledged in previous studies on ownership structure relationships (Demsetz and Lehn, 1985; Himmelberg *et al.* 1999; De Miguel *et al.* 2004). Endogeneity in the statistical model arises when an independent variable correlates with the error term. Precisely, this is when ownership variables, as well as other control variables, are influenced by unobserved variables. Endogeneity leads to inefficient and inconsistent parameter estimation in the experimental model. According to Demsetz and Lehn (1985), firm owners are aware of the consequences when specific decisions and right processes have been transferred to the professional manager who controls the firm and the cost associated with the benefit. Therefore, whether shareholders choose a concentrated and dispersed ownership structure, the rational assumption is the benefit they will acquire to offset the costs and ensure goal congruency of value maximization. A study by Demsetz and Lehn (1985) on the relationship between ownership concentration and firm performance found that ownership structure is endogenously determined. Thus, the firm character should be observed when studying the relationship between ownership structures.

Demsetz and Villalonga (2001) state that most prior studies on ownership structures have not solved the endogeneity problem in ownership variables. They argue that the sources of endogenous ownership structure can be viewed in the simultaneity approach. This implies that the *ceteris paribus* of firm value depends on the ownership structure. While ownership structure is influenced by firm value, the firm value can also influence ownership structure. Wintoki *et al.* (2012) posited that the past performance of the firm has a direct influence on the corporate information environment, profit potential, opportunity cost, and all the other factors that affect ownership structure. They argued that corporate governance mechanism interacts with firm performance. Thus, suggested that any estimation that does not observe for dynamic nature when dealing with ownership variable and firm value relationship will yield inconsistent estimation.

Considering these arguments, the OLS, fixed effect, and random effect will yield biased estimations. Thus, this research study employs the dynamic model stated in the empirical model specification using the generalized method of moment (GMM) estimation to deal with all endogeneity issues of ownership structure on firm value, specifically in South Africa's dynamic institutional framework.

6. Empirical findings

6.1. Descriptive statistics

Table 1 presents the descriptive statistics of the variables used in this study. Tobin's Q, the market base of measuring firm values, is 1.71 on average with a minimum and maximum value of 0.00 and 52.11, respectively. The Tobin's Q is higher than previous South Africa-centered studies of Ntim (2013) and Meyer and de Wet (2013) with 1.52 and 1.46, respectively. This suggests that a consistent or a longer stay of firm operation on the JSE market will improve corporate performance. ROA, the accounting base of measuring firm value, is 10.04 on average with a minimum and maximum value of -8.45 to 105, respectively, during the study period from 2004 to 2016. It is lower than that observed by Mugobo *et al.* (2016) with 16.0 and Zondi and Sibanda (2015) with 14.73.

Table 1. Descriptive statistics summary

Variables	Observation	Mean	Std. Dev.	Min.	Max.
TOQ	2,035	1.715	2.795	0.000	52.110
ROA	1,949	10.045	38.886	-845.200	105.26
Ownership Structure					
OC	1,938	40.103	22.172	0.030	98.400
FO	2,040	2.017	5.627	0.000	80.350
DO	2,041	97.984	5.626	19.650	100.000
Control Variables					
LV	1,951	0.487	0.258	0.000	2.910
PR	1,905	-145.480	2588	-95400	59670
LQ	1,948	1.536	2.311	0.050	38.380
BS	1,907	10.561	3.938	2.000	36.000
BR	1,921	16.673	333.500	-695.26	14465
BF	2,046	0.206	0.404	0.000	1.000
FS	1,795	14892.760	38530	13.395	41138

Note: Tobin's Q (TOQ) and return on asset (ROA) are used to measure the firm value. OC, LV, PR, LQ, BS, BR, BF, and FS stand for ownership concentration, leverage, profitability, liquidity, board size, board remuneration, and firm size, respectively.

Source: Authors' computation based on the secondary data collected

The average value of ownership concentration (OC) measured by the number of percentage share with a vote held by large five shareholders on the JSE equity market is 40.10%, and this is higher than the 32.36% reported by Steyn and Stainbank (2013) on the same stock exchange in South Africa. These figures suggest that shareholders on the JSE are more concentrated, and hence the need for shareholders' diffuseness to spread the ownership and management control of the JSE. Domestic ownership ranges from 0% to 100%, with an average value of 97.98%. It shows that local investors possess high percentages of firm shares on the JSE equity market. Foreign investors possess a very low percentage of firm shares on the JSE equity market, with the average value being 2.02% and with a minimum and maximum value of 0% and 80.35%, respectively. This could indicate that the inward listing rule permitted by the JSE to raise capital on the bourse by listing foreign firms on the capital market is to improve domestic shareholders in South Africa.

Leverage (LV) on the average value on the JSE equity market is 0.487. This implies that South African listed firm is more equity finance than debt finance. Profitability (PR) on average indicates a negative of -145.47 and a maximum of 5967 and, a minimum net profit margin. Liquidity averages the value of 1.54, with the minimum and maximum values of 0.05 and 38.38, respectively. The board size (BS) average value is 10.58, with a minimum of 2 and a maximum of 38 directors that oversee affairs of corporate resources of the JSE-listed companies, whereas the board remuneration on average is at 16.67%. The firm size on average is 14,893, with the minimum and maximum values of 13,395 and 41,138, respectively.

6.2. Correlation coefficient analysis

Table 2 shows the degree of correlation for all variables that are used in the regression analysis. The correlation coefficient shows the interaction between the dependent variables and the explanatory variable. There is a low correlation among the variables, which shows that there is no problem with multicollinearity. Tobin's Q is positively correlated with ROA, firm size, board size, BEE firm, liquidity, and leverage. Managerial ownership, ownership concentration, profitability, and board remuneration have a negative correlation with Tobin's Q. Further, ROA has a negative correlation with ownership concentration, leverage, board remuneration, BEE firm

rating, and managerial ownership, and it has a positive correlation with liquidity, board size, and firm size.

Table 2. Correlation coefficient of all variables on the ownership structure and firm value

	TOQ	ROA	OC	FO	DO	LV	PR	LQ	BS	BR	BF	BS
TOQ	1.000											
ROA	0.539	1.000										
OC	-0.072	-0.884	1.000									
FO	0.219	0.027	-0.171	1.000								
DO	-0.218	-0.027	0.171	-1.000	1.000							
LV	0.029	-0.025	-0.113	0.060	-0.060	1.000						
PR	-0.074	0.120	-0.032	0.014	-0.014	0.043	1.000					
LQ	0.049	0.079	0.054	-0.046	0.046	-0.495	-0.440	1.000				
BS	0.100	0.016	-0.194	0.239	-0.239	0.004	0.014	-0.172	1.000			
BR	-0.030	-0.030	0.024	-0.021	0.021	-0.030	0.006	0.014	-0.021	1.000		
BF	0.095	-0.040	-0.169	0.452	-0.452	0.029	0.016	-0.091	0.246	-0.021	1.000	
FS	0.216	0.161	-0.048	0.281	-0.282	-0.063	0.012	-0.046	0.342	-0.019	0.258	1.000

Source: Authors' computations based on the secondary data collected

6.3. Regression analysis for the empirical hypothesis

Table 3 presents the regression results of this study. The significance of lagged firm value (FV_{t-1}) measures with Tobin's Q and ROA value in the regression results of ownership structure variables (ownership concentration, foreign ownership, and domestic ownership) shows the importance of dynamic nature when considering the relationship between ownership structure and firm value (Wintoki *et al.* 2012).

The presence of the nth-order serial correlation in the instruments was tested using the $m(n)$ test, in which the test statistic is asymptotically distributed as a standard normal variable under the null hypothesis of no second-order serial correlation of the differenced residuals. The results in Table 3 show that the null hypothesis should not be rejected as there is no serial correlation of order 2. The legitimacy of the instruments was verified using the Hansen test, which tests for over-identifying restrictions. The results in Table 3 show that the null hypothesis that the population moment conditions are correct (as shown by the Hansen test) is not rejected.

6.4. Ownership concentration and firm value

Consistent with previous studies of Cameron (2012), Mugobo *et al.* (2016) in South Africa, this study found that the coefficient of the ownership concentration is negative and statistically significantly related to firm value measures of Tobin's Q and ROA. This finding is contrary to Berle and Means (1932), who proposed the importance of large shareholders to reduce corporate risk and increase corporate performance. This finding is also contrary to the agency theory by Jensen and Meckling (1976), who argued that large shareholders can play an important role in minimizing losses that arise from the separation of ownership and control. We denote that the large shareholders' ownership of the JSE market in South Africa is insignificant to minimize conflicts of interest among shareholders and thus could lead to expropriation of the wealth of shareholders (Shleifer and Vishny, 1997; Porta *et al.* 1999; Walsh and Seward, 1990; Ward and Filatotchev, 2010). The economic impact¹ of ownership concentration reveals that one standard deviation increase in large shareholders will reduce the firm value by 16% using Tobin's Q and 33% using ROA as measures of the firm value of JSE-listed companies. This suggests that an adequate corporate governance mechanism will be required to improve corporate performance in South

¹Economic Impact = (the standard deviation of explanatory variable * regression coefficient of the explanatory variable) / standard deviation of the dependent variable

Africa. It would lead to the diffuseness of shareholders and further improve the performance of listed firms in South Africa when shareholders are contracted.

Table 3. Regression results of ownership concentration, foreign and domestic ownership, and firm value

	Ownership concentration		Foreign ownership		Domestic ownership	
	Model 1	Model 1	Model 2	Model 2	Model 3	Model 3
FV	Tobin's Q	ROA	Tobin's Q	ROA	Tobin's Q	ROA
FV _{t-1}	0.4225*** (1.63)	0.1102* (0.76)	0.4160** (2.54)	0.2251** (2.18)	0.4230** (2.54)	0.2206** (2.24)
OC	-0.0201** (-3.77)	-0.5803** (-1.95)				
FO			-0.0218* (0.41)	-0.4990** (-2.25)		
DO					0.0260* (1.90)	0.6944** (2.50)
LV	-0.1058 (-2.04)	-2.2368 (-0.47)	0.0993 (0.48)	3.8303 (1.37)	0.1108 (0.51)	3.9003 (1.33)
PR	0.0012*** (-0.35)	0.0007** (2.43)	-0.0000*** (-2.28)	0.0007*** (2.79)	-0.0000** (-2.00)	0.0007*** (2.61)
LQ	0.4360 (-2.81)	1.7423 (1.39)	0.0336 (0.56)	1.7695* (1.77)	0.0461 (0.73)	1.8236 (1.63)
BS	-0.0119 (0.82)	-0.1666 (-0.51)	-0.0033 (-0.26)	0.0431 (0.24)	-0.0082 (-0.59)	0.0313 (0.17)
BR	-0.0000 (-1.18)	-0.0009*** (-5.29)	-0.0000* (1.84)	-0.0009*** (2.48)	-0.0000* (-1.66)	-0.0009** (-2.31)
BF	0.2188 (-0.71)	-27.787 (-2.55)	-0.7873* (1.89)	-4.3732 (-0.46)	0.9951** (0.028)	-0.4859 (-0.05)
FS	0.0001*** (0.39)	0.0001*** (2.66)	0.0002 (1.11)	0.0001** (2.07)	0.0000 (2.19)	0.0001* (1.74)
Constant	1.5959*** (2.54)	41.647*** (2.58)	0.5226 (2.28)	7.1681** (2.42)	-2.0948 (0.156)	-62.843** (-2.18)
Obs.	1518	1525	1548	1541	1548	1542
AR (1)	0.001	0.009	0.005	0.001	0.004	0.001
AR (2)	0.938	0.820	0.610	0.688	0.565	0.665
Hansen test	0.252	0.580	0.161	0.329	0.190	0.263

Note: Standard errors are shown in parentheses. ***, **, and * represent significance levels at 1%, 5%, and 10%, respectively.

Source: Authors' computations based on secondary data collected

6.5. Foreign ownership and firm value

Foreign ownership has a negative impact on firm value. This finding suggests that more foreign ownership of JSE-listed firms reduces firm value. The hypothesis that there is a positive relationship between foreign ownership and the firm value of the JSE-listed companies should be rejected. Our findings are contrary to previous studies (Khanna and Palepu, 1999; Oxelheim and Randøy, 2003; Barbosa and Louri, 2005; Koo and Maeng, 2006; Douma *et al.* 2006; Aydin *et al.* 2007; Ghahroudi, 2011; Ongore, 2011; Mi Choi *et al.* 2012; Wellalage and Locke, 2012; Pervan *et al.* 2012; Weche Gelübcke, 2013; Greenaway *et al.* 2014; Phung and Mishra, 2016) which generally concluded that foreign investors improve firm performance in the host country. Our

finding suggests that foreign investors may not be providing adequate corporate monitoring and internal corporate governance mechanisms to improve the value of the JSE equity market (Oxelheim and Randøy, 2003; Mi Choi *et al.* 2012; Phung and Hoang, 2013). The economic impact of foreign ownership results shows that one standard deviation increase in foreign ownership on the JSE market in South Africa leads to a decrease of 4% in Tobin's Q and 7% in ROA as measures of firm value.

The negative impact of foreign ownership on firm value in the South African JSE market suggests that foreign investors' external influences may not be adequate to minimize losses that arise from the separation of ownership and control on the JSE. This finding can be explained by the series of programs implemented in South Africa's transition economy since the end of apartheid. These include the inward listing rule by the JSE to increase the number of domestic shareholders in the equity market, and the government-supported transformation program on the racial diversity of ownership, management, and control of the economy may have had a negative effect on foreign ownership to influence firm value.

6.6. Domestic ownership and firm value

The coefficients of domestic ownership are positive and statistically significant for firm value proxies as initially hypothesized. These findings are consistent with Douma *et al.* (2006), who conducted a similar study on the relationship between domestic ownership and firm value. This finding suggests that local investors can help in improving firm performance and minimize losses that arise from the separation of ownership and control. We infer that domestic ownership with a large proportion of shareholding is important in effectively monitoring JSE-listed firms to improve the firm value and corporate governance practices in South Africa. The economic impact of domestic ownership shows that one standard deviation increase in domestic ownership on the JSE market in South Africa leads to an increase of 5% in Tobin's Q and 10% in ROA as measures of firm value. This obliged significant features of the BEE program in South Africa that prompted racial diversity at the board level, the transformation of ownership, and control of the JSE market (Africa Business Communities, 2017).

6.7. Control variables and firm value

The findings on leverage (LV) reveal a negative effect on firm value when large shareholders are concentrated, consistent with Phung and Mishra (2016). However, leverage has a positive relationship with firm value when foreign and domestic ownership are included in the model. This positive effect is consistent the findings of Agrawal and Knoeber (1996) on firm value. This implies that owners of firms listed on the JSE improve corporate performance when debt finance is employed.

The findings on profitability (PR) exhibit a significant and positive relationship with firm value using ROA, an accounting-based measure, and a negative effect when Tobin's Q is used as a measure of firm value. The findings are consistent with those of Phung and Mishra (2016) that found a negative relationship with firm value. Firm profit rate to sales return is significant when considering the dividend policy, retained profit, investment opportunities, reduction in debt finance, and access to long-term finance and lease finance that affect firms' operations (Himmelberg *et al.* 1999, Phung and Mishra, 2016).

Liquidity (LQ) has a positive relationship with firm value in the model for all ownership structure variables. This is consistent with Uno and Kamiyama's (2010) study that argued highly liquid firms offer better investment prospects and have access to more debt investment finance and can achieve superior corporate performance. Board remuneration (BR) has a negative relationship with firm value in all the models. This is consistent with Fernandes's (2008) finding that board remuneration does not affect firm value using both accounting-based and market-based measures regardless of board composition. This infers that board remuneration (salaries and compensation) among JSE-listed companies does not effect on firm value irrespective of board composition. Firm size (FS) showed a positive relationship with firm value in the models of

all the ownership structure variables. This is consistent with studies by Jensen and Murphy (1990) and Himmelberg *et al.* (1999), who argued that argued firm size boosts managers' morale.

7. Conclusion and recommendation

This study analyzed the impact of ownership concentration, foreign ownership, and domestic ownership on the firm value of JSE-listed companies in the phase of BEE in South Africa. Given the robustness of our empirical evidence using dynamic panel data, we conclude that ownership concentration and foreign ownership are inadequate to minimize the losses that arise from the separation of ownership and control on the JSE market in South Africa.

Further, the conclusion drawn shows that domestic shareholders in the host country strengthen firm monitoring and corporate governance practices in the phase of the diverse institutional framework of the economy. Local shareholders provide adequate monitoring and control of listed firms which improves firm financial performance. Therefore, the BEE program enacted by the South Africa government to promote racial diversity of ownership, management, and control of the firms listed on the JSE market should be encouraged in relation to corporate governance triple context based on economy society, and environments. Given the inverse positive influence of large shareholders and foreign shareholders on the JSE market in South Africa, we recommend further widely spread of shareholders in the host country by policymakers and that more attention should be given to quality corporate governance practices to improve firm financial performance in South Africa. The use of financial statements as the main source of data is the major limitation of this study because financial statements can be manipulated by managers and the researchers have no control over the quality of the financial statements. This study investigated ownership concentration, foreign and domestic ownership, and firm value. Further studies should be conducted on the impact of managerial ownership on firm value.

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