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Institutional distance and institutional complexity in international business

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CHAPTER 5

MANAGERIAL OWNERSHIP AND FIRM PERFORMANCE: THE CULTURAL BOUNDARIES OF AGENCY THEORY

5.1 INTRODUCTION

In their seminal work, Berle & Means (1932) called attention to the question: who actually controls the modern corporation, shareholders or managers? They posit that, when operational control is concentrated in the hands of managers and capital ownership is dispersed among many small shareholders, managers are effectively unaccountable to shareholders. This is problematic, because “the separation of ownership from control produces a condition where the interests of owner and of ultimate manager may, and often do, diverge, and where many of the checks which formerly operated to limit the use of power disappear” (Berle & Means, 1932: 7). To date, this misalignment argument is the foundational assumption of agency theory as used in the fields of corporate governance and corporate finance (Baumol, 1959; Grossman & Hart, 1980; Jensen & Meckling, 1976; Marris, 1964; Penrose, 1959; Williamson, 1964).

Agency theory suggests aligning the interests of the agent with those of the principal by making managers co-owners of the firm (Eisenhardt, 1989; Jensen & Meckling, 1976). A key prediction of agency theory is that managerial ownership is the “lynchpin for resolution of agency problems” (Boyd & Solarino, 2016: 1288) and therefore will have a positive effect on firm performance (Dalton, Hitt, Certo, & Dalton, 2007). However, empirical evidence on the key prediction currently fails to support the offered solutions to this agency problem (Lan & Heracleous, 2010). This leads Ghoshal to conclude “What is interesting is that agency theory [...] has little explanatory or predictive power. [...] The facts are that none of [the solutions described by agency theory] have the predicted effects on corporate performance” (2005: 80). Ghoshal’s observation echoes one of the early critiques on management research in general, claiming that it is a post-World War II, American-based profession; additionally, it is questionable whether the U.S.-developed management theories are transferable to other settings or whether they are country/region specific (Boyd & Solarino, 2016; Boyacigiller & Adler, 1991; Hofstede, 1983; Ng, 2005; Sekaran, 1981). This concern also plagues agency theory (Peng & Jiang, 2010; Wiseman, Cuevas-Rodriguez, & Gomez-Mejia, 2012). To increase the predictive power of agency theory and extend the theory beyond the U.S. context in which it was originally developed (Davis, Diekmann, & Tinsley, 1994; Davis, Lukomnik, & Pitt-Watson, 2009; Dobbin & Zorn, 2005; Powell, 2001), comparative corporate

governance scholars emphasize the institutional context in which firms operate, addressing the degree and nature of agency conflicts as well as the effectiveness of the described governance mechanisms (Aguilera & Jackson, 2003; Tihanyi, Graffin, & George, 2014). A key question in this literature concerns the extent to which the assumptions and mechanisms subscribed by agency theory are relevant in each country's context (Aguilera & Jackson, 2010; Aguilera, Florackis, & Kim, 2016).

In this chapter, I explore whether the key prediction of agency theory on the positive relation between managerial ownership and firm performance is universal or if this prediction is bound by the national cultural context in which firms operate. Drawing on a worldwide sample of firms in 123 countries, I relate managerial ownership to firm performance in a sample of 27,852 listed firms over a period of eight years (2009-2016). My findings show that cultural context moderates the relationship between managerial ownership and performance such that only firms embedded in the Anglo-Saxon culture experience positive performance effects from managerial ownership.

Despite the vast literature on the institutional embeddedness of corporate governance practices (e.g., Aguilera & Jackson, 2003, 2010; Fainshmidt, Judge, Aguilera, & Smith, 2016; Haxhi & Aguilera, 2017; Wiseman et al., 2012), to the best of my knowledge, I am the first to demonstrate that the key prediction of agency theory is culture-specific. This important finding contributes to the literature in two ways. First and foremost, I show that agency theory is contingent on the cultural setting in which the firm is embedded (Aggarwal & Goodell, 2014). I argue that the parts of agency theory that rely on current human behavior assumptions should be considered "regiocentric" instead of universally applicable (Boyacigiller & Adler, 1991). Therefore, I contribute to the discussion on how to control the corporation outside the Anglo-Saxon context by emphasizing the need to develop alternative theoretical frameworks, such as stewardship theory (Davis, Schoorman, & Donaldson, 1997; Donaldson & Davis, 1991). Second, I extend the comparative corporate governance literature by showing why the relation between managerial ownership and firm performance differs across the world (Aguilera & Jackson, 2010; Boyd & Solarino, 2016).

5.2 THEORY AND HYPOTHESES

5.2.1 Agency Theory

Agency theory is a cornerstone of corporate governance in both theory and practice (Lan & Heracleous, 2010). It conceives the corporation as a nexus of contracts between principals (risk-bearing shareholders) and agents (managers with specialized expertise) (Aguilera & Jackson, 2010). Agency theory deals with the issue of how to align the diverging interests of the agent and the principal (Eisenhardt, 1989). Or, as Shleifer and Vishny posit, the problem addressed in agency theory is “how investors get the managers to give them back their money” (1997: 738). Agency theory assumes that people are opportunistic and motivated by self-interest (Davis et al., 1997). Under this assumption, agency problems arise when both the desires and/or goals of the agent and principal differ, as well as when it is difficult for the principal to monitor the behavior of the agent (Eisenhardt, 1989). In such a case, the agent has both the opportunity and the motive to take advantage of his/her position at the cost of the principal.

To align the interests of the agent with those of the principal, agency theory offers two solutions. First, it suggests strengthening the information system, therefore increasing the ease of monitoring the agent’s behavior (Eisenhardt, 1989; Fama & Jensen, 1983). Second, agency theory suggests aligning the interests of the agent with the interests of the principal by moving toward outcome-based contracts because agents are more likely to behave in the interest of the principal when awarded through such contracts (Eisenhardt, 1989). One way for a principal to create an outcome-based contract is by awarding the manager with ownership. Managers are made more accountable using measures such as executive compensation schemes, performance-based bonuses, and stock options. Managerial ownership aligns the interests of the principal and the agent because the agent financially suffers in the form of decreasing value of ownership shares when they squander corporate wealth (Jensen & Meckling, 1976). In that case, the agency costs should decrease, as reflected in lower monitoring expenditures of the principal, lower bonding expenditures of the agent, and reduced residual welfare loss by the principal (Jensen & Meckling, 1976). As a result, managerial ownership

leads to increased market value of the firm. The baseline hypothesis of agency theory is that managerial ownership has a positive effect on firm performance.

5.2.2 Boundary Conditions of Agency Theory

Our understanding of the relation between managerial ownership and firm performance has been refined and developed in both theoretical (e.g., Donaldson & Davis, 1991; Donaldson & Preston, 1995; Lan & Heracleous, 2010; Sundaram & Inkpen, 2004) and empirical directions (e.g., Morck, Shleifer, & Vishny, 1988; Ng, 2005). Nonetheless, agency theory is not uncriticized (Daily, Dalton, & Cannella, 2003; Dalton et al., 2007; Ghoshal, 2005; Hirsch, Michaels, & Friedman, 1987; Jensen, 1983; Perrow, 1986; Wiseman et al., 2012). Theoretically, most criticism focuses on the assumption of human behavior underlying agency theory. A particularly forceful critique on the key assumption of agency theory was put forward by Ghoshal (2005). Rather than considering managers as rational self-interested maximizers, Ghoshal refers to key findings in experimental and behavioral sciences (e.g., Camerer & Thaler, 1995) to argue that people possess preferences that can be considered self-regarding, other-regarding, and process-regarding (Ghoshal, 2005).

Ghoshal's (2005) critique resonates with earlier work on the applicability of U.S.-developed managerial theories in other cultural environments. As the scope and primary orientation of most theories is North American in origin, the question arises as to whether these theories are universally applicable or not (Boyacigiller & Adler, 1991). Rather than assuming that human behavior is homogenous across the world, human behavior is culture-specific (Hofstede, 2001). As a result, the importance of the assumptions underlying agency theory regarding humans as self-interested opportunists as well as the offered solution of co-ownership must be understood.

For an agency problem to occur in the first place, (1) there must be misalignment between the goals and desires of the agent and the principal, (2) the agent's behavior must be difficult and/or costly to monitor, and (3) the agent must be willing to behave opportunistically. In addition, to solve this issue by awarding the agent with co-ownership, both the principal's and agent's goals and desires must include maximizing financial gains, and the offered reward must outweigh the agent's potential benefits of maximizing its own financial gains. All the above conditions are required for an agency

problem to occur and rewarding the agent with co-ownership to be the appropriate solution. However, when removing the assumption of self-interest maximizing human behavior—or, more specifically, profit maximizing behavior (Jensen & Meckling, 1976; Shleifer & Vishny, 1997)—several conditions, such as the willingness of the agent to behave opportunistically and the goal of both agent and principal being profit maximization, are not necessarily met and consequently influence the frequency and severity of agency problems as well as the appropriateness of offered solutions.

5.2.3. Agency in the Anglo-Saxon Culture

Corporate governance institutions do not develop in a societal vacuum, but are embedded in norms and values (Beugelsdijk & Maseland, 2011; North, 1991; Williamson, 2000). Formal institutional structures are fundamentally related to cognitive and normative collective norms of conduct (Scott, 1995). A key feature of this comparative corporate governance literature is the focus on institutional diversity and how it shapes firms' organizational behavior (Aguilera & Jackson, 2003; Haxhi & Aguilera, 2017). Institutional sociologists argue that legal structures and collective norms of behavior only become institutionalized when they are internalized (Jackson & Deeg, 2008), implying that cultural values play a key role in the effectiveness of particular formal institutions (Aguilera, Desender, Bednar, & Lee, 2015). Using a variety of national culture frameworks (mainly Hofstede, 1980, 2001), researchers have indicated that national culture supports particular kinds of corporate governance institutions (e.g., Griffin, Guedhami, Kwok, & Shao, 2017; Haxhi & van Ees, 2009; Kirkman, Lowe, & Gibson, 2006).

Cultural similarities between countries often coincide with institutional similarities (Beugelsdijk, Kostova, & Roth, 2017). Cultural values and institutional norms often “hang together” as a system (Fainschmidt et al., 2016), as predicted by institutional logic (Thornton, Ocasio, & Lounsbury, 2012). The complementarities of culture-based values and institution-based norms make it very difficult to draw causal arrows between cultural and institutional variables (Aguilera & Jackson, 2010). One reason is that countries with a shared history of close ties due to proximity, trade, conquest, or religion demonstrate more similar cultural values due to institutional transmission than do countries lacking such ties (Peterson & Barreto, 2015: xxvi). As a result, and irrespective of the

cultural framework used (Hofstede, Schwartz, or GLOBE), national cultures tend to cluster together in supra-national cultural zones, including the Anglo-Saxon cluster (Beugelsdijk, Kostova, & Roth, 2017; Hofstede, 1980, 2001; House et al., 2004; Ronen & Shenkar, 2013; Schwartz, 1994, 1999).

The comparative corporate governance literature and varieties of capitalism literature distinguish between Anglo-Saxon, or liberal market economies, and Continental European, or coordinated market economies. Although the latter was criticized for being too broad and consequently separated into sub-categories (Hall & Gingerich, 2009; Jackson & Deeg, 2006; Nolke & Vliegenthart, 2009; Witt, Kabbach de Castro, Amaeshi, Mahroum, Bohle, & Saez, 2017), the Anglo-Saxon category has remained remarkably stable over time. Whether explained through corporate governance literature (e.g., La Porta, Lopez-De-Silane, Shleifer, & Vishny, 1998 [the Anglo-Saxon model of corporate governance]), *Varieties of Capitalism* (Hall & Soskice, 2001 [liberal market economies]), national business systems (Whitley, 1992 [the regulatory state]), cultural theory (Ronen & Shenkar, 1985, 2013 [the Anglo-Saxon cluster]), or alternative institutional approaches (e.g., Haxhi & Aguilera, 2017 [the classic shareholder-oriented model]), all agree on the uniqueness of the Anglo-Saxon context, the behaviors it stimulates and constrains, and the resulting dominant corporate governance practices.

The consensus is that the Anglo-Saxon context distinguishes itself from other contexts by strong protection of property rights through common law (La Porta, Lopez-De-Silane, & Shleifer, 1999a), a laissez-faire or “arm’s length” approach toward government (Hall & Soskice, 2001; La Porta, Lopez-De-Silane, & Shleifer, 2008; Whitley, 1992), a strong capital domain (Haxhi & Aguilera, 2017), and a strong individualistic and risk-taking culture (Ronen & Shenkar, 1985, 2013) with values highlighting individual responsibility over group responsibility (Hofstede, 2004).

Considering the unique cultural and institutional nature of the Anglo-Saxon context, we contend that the conditions for agency problems to occur and be solved through co-ownership are more frequently met in the Anglo-Saxon cultural context compared to other contexts. Consequently, the practice of awarding a manager with co-ownership is a more effective tool in the Anglo-Saxon context. We identify two reasons why managerial ownership is more effective in the Anglo-Saxon context than in other contexts. First, Anglo-Saxon cultures are highly individualistic (Hofstede, 1980;

House et al., 2004; Ronen & Shenkar, 1985, 2013; Schwartz, 1999), and the characteristics of such individualistic cultures fit agency theory more closely than do the characteristics of collectivistic cultures. Second, due to the institutional configuration of the Anglo-Saxon context, ownership is fairly dispersed, resulting in (a) more difficulty in monitoring the agent's behavior and (b) a nearly exclusive focus on maximizing financial gains by the principal (shareholder value).

Regarding the cultural orientation of the context, agency theory requires natural misalignment, opportunistic behavior, and maximization of financial gains as a goal of both the agent and the principal. These requirements are largely dependent upon the culture in which the firm operates. More specifically, we contend that the effectiveness of agency theory depends on the degree of individualism in the operational context. Individualism (versus collectivism) denotes the extent to which people see themselves primarily as autonomous personalities (individualism) or primarily as members of tightly-knit communities (collectivism). Individualistic and collectivistic cultures differ in the form of affiliations that people pursue. In individualistic cultures, people choose their affiliations voluntarily, while in collectivistic cultures, affiliations are imposed upon them (Hofstede, 2001). Individualistic cultures fit well with the requirements of agency theory, where individualists are generally more self-reliant, and are therefore aimed toward maximizing their own self-interest. As a result, the underlying assumptions of human behavior of agency theory match up with highly individualistic contexts. In collectivistic cultures, people value the need of the in-group over the need of the individual. Considering a firm as an in-group, the collectivistic culture fits poorly with the agency theory requirements. When both the agent and principal value the needs of the firm over their own needs for maximizing financial gains, the chance of natural misalignment occurring between the goals of principal and agent diminishes radically. In such cases, both principal and agent share the same in-group goals, rendering their goals and desires naturally aligned rather than naturally misaligned. Furthermore, in cases where the goals are misaligned within collectivistic contexts, the chance that the agent behaves opportunistically toward maximizing self-interest is reduced since maximizing self-interest over group interest would violate the cultural norm.

To exemplify situations in which the agent does not aim to maximize its financial gains due to collectivistic norms, consider that, in Japan (a collectivist country), large paychecks are considered a

taboo and a sign of greed. Consequently, eight of the ten highest-paid CEOs in Japan are foreign (Melin & Suzuki, 2016). Reversely, Anglo-Saxon countries tend to be at the top of both the Bloomberg CEO average pay index and the Bloomberg CEO pay-to-average ratio (Lu & Melin, 2016). The conjecture that individualistic cultures value maximizing self-interest more than collectivistic cultures is reflected in the significant relation between the individualism scores of Hofstede (1980) and the CEO pay data by Bloomberg (Lu & Melin, 2016). There is a strong and significant positive relation ($p < 0.01$), where Hofstede's individualism explains 37% of the variation in CEO pay⁹. Similarly, Witt & Redding (2009) conducted multiple interviews with senior executives in Germany, Japan, and the US. They found that only the U.S. executives strongly subscribe to shareholder value maximization as the locus of the firm's existence, while both German and Japanese executives did not favor a strong focus on the shareholder, therefore indicating that agents' desires, goals, and motivations naturally differ across contexts.

5.2.4. Institutional Context

One key institutional characteristic of the Anglo-Saxon context is that corporate ownership tends to be relatively dispersed (Roe, 2002). To exemplify this, the average percentage of common shares owned by the top three shareholders in the ten largest non-financial, privately-owned domestic firms in the Anglo-Saxon context is 31%, while this percentage rises to 49% in the non-Anglo-Saxon context (La Porta et al., 1999a). Several reasons are identified for ownership dispersion versus the presence of blockholders. First, ownership dispersion is stimulated by strong property rights, where common law traditions value outside investor protection and, in turn, stimulate ownership dispersion (La Porta et al., 1998, 2008). Second, ownership dispersion is encouraged through political action, where bank ownership is historically curtailed in the Anglo-Saxon context (Roe, 1994). Third, both individualism and a lack of uncertainty avoidance lead to larger ownership dispersion (Griffin et al., 2017; Hofstede, 2004). Individualism values accountability, transparency, and equal rights, resulting

⁹ When regressing (through simple OLS) Individualism on the CEO pay index, while controlling for both GDP and GDP per capita, the R^2 rises to 48.03% and individualism has a significant and positive effect ($\beta = 1.119$ & $p = 0.019$; $n = 25$). Complete results available in Appendix D.

in the protection of both inside investors, outside investors, and consequently to dispersion of ownership. Reversely, controlling shareholders in a high uncertainty avoidance context would be less willing to issue equity to outside shareholders due to the associated risk of the loss of control with dispersed ownership (Griffin et al., 2017). The Anglo-Saxon context uniquely combines all these features (Fainshmidt et al., 2016; Haxhi & Aguilera, 2017), making ownership dispersion a key characteristic of its institutional configuration.

The fact that ownership is relatively more dispersed in the Anglo-Saxon context than in the non-Anglo-Saxon context affects the predictive power of agency theory for two reasons. First, the presence of blockholders increases the likelihood that monitoring becomes easier and/or less costly for the principal, where blockholders can exercise tight control over a firm and therefore exert their influence over management (Aguilera & Jackson, 2010). Therefore, blockholder ownership has the potential to decrease the monitoring difficulty and costs, thus reducing the agency problem. Second, with large blockholders, the principal may exert a significant amount of pressure over the goals set by the firm, therefore allowing the principal to pursue different, non-profit maximizing goals. Reversely, with high levels of ownership dispersion, it becomes difficult to establish goals other than profit maximization.

There is plenty of evidence describing the tendency of blockholders to aim for alternative goals as reflected in, for example, the presence of state ownership (e.g., Boubakri, Guedhami, Kwok, & Saffar, 2016) and business groups (Colli & Colpan, 2016; Douthett & Jung, 2001) outside the Anglo-Saxon context (*vis-a-vis* their absence in the Anglo-Saxon context), as well as the role of family firms (Anderson & Reeb, 2003; Ng, 2005; Peng & Jiang, 2010) and banks as blockholders (Crossland & Hambrick, 2007; Jürgens & Rupp, 2002). What unites these forms of governance is that they have a goal orientation that is not solely driven by shareholder value, as assumed by agency theory and typically found in the Anglo-Saxon context, but also includes goals other than profit maximization, such as stakeholder value and long-term performance. State-owned firms tend to value societal goals, and business groups value both survival and within-group cooperation over profit maximization (Colli & Colpan, 2016; Douthett & Jung, 2001). Similarly, banks tend to favor low-risk and long-term strategies (Crossland & Hambrick, 2007). The consequence of a principal pursuing

alternative goals for the solution offered by agency theory is that, in these cases, rewarding the manager with co-ownership does not decrease the misalignment between principal and agent; rather, it would potentially increase the misalignment, where the manager is stimulated to pursue a goal for which the shareholder does not necessarily aim.

Overall, we conjecture that the assumptions and causal mechanisms as described by agency theory apply inside the Anglo-Saxon context, but fail to work outside the Anglo-Saxon context. This leads to the following hypothesis:

Hypothesis 1. The relation between managerial ownership and firm performance is positively moderated by the Anglo-Saxon context.

5.3 DATA AND METHOD

5.3.1. Sample and Data Collection

To identify whether supra-national context moderates the relation between managerial ownership and firm performance, I collected firm-level data on publicly listed firms from the financial database Orbis for the 2009-2016 period. Following La Porta, Lopez-de-Silanes, Shleifer, & Vishny (1999b), I exclude financial firms because valuation ratios for such firms are not comparable to non-financial firms. The final sample consists of 157,375 observations of 27,852 firms in 123 countries.

TABLE 5.1
Descriptives and Bivariate Correlations

Variable	Mean	Std. dev.	1	2	3	4	5	6	7	8	9	10
1. Anglo-Saxon ^a	0.11	0.31	1.000									
2. Man. Owner ^a	0.39	0.49	-0.010	1.000								
3. Man. is GUO ^a	0.15	0.36	0.035	-0.514	1.000							
4. Firm Age ^b	3.19	0.86	0.154	0.022	0.017	1.000						
5. Firm Size ^b	12.13	2.14	0.122	0.186	0.052	-0.098	1.000					
6. Current Ratio ^b	0.52	0.82	0.029	-0.021	-0.012	-0.006	0.089	1.000				
7. Sales Growth	2.17	23.95	-0.005	-0.030	-0.014	0.084	-0.108	-0.009	1.000			
8. GDP	2867.21	3757.727	-0.249	-0.038	-0.001	0.052	-0.243	-0.080	-0.026	1.000		
9. GDP per Capita	24.31	22.11	-0.404	-0.047	0.045	-0.134	-0.191	-0.040	0.044	0.012	1.000	
10. Solv. Ratio	50.79	24.77	0.001	-0.001	0.014	0.042	0.053	-0.628	-0.007	0.031	-0.003	1.000

Note: N=157,375; ^adummy variable; ^blog transformed

Dependent variable. I operationalize *firm performance* using Tobin's Q, one of the most commonly used indices of firm performance incorporating both past performance and future outlook

(La Porta et al., 1999b; Moreck et al., 1988). In order to normalize the data and remove outliers, I have taken the log of Tobin's Q and used the outlier detection labeling rule (Tukey, 1977).

Independent variables. I operationalize managerial ownership through a dummy variable that looks at whether or not current managers are listed as shareholders. Following Ronen & Shenkar (2013) and Hall & Soskice (2001), I consider the U.S., the U.K., New Zealand, Australia, Ireland and Canada part of the Anglo-Saxon cluster.

Control variables. I control for the possibility that the manager is the Global Ultimate Owner (GUO) of the firm; when this occurs, no agency problem should arise since the principal and the agent would be the same person. Following La Porta et al. (1999), I use a cut-off value of 20% to determine if the manager is also the owner of the firm. I use *sales growth*, *solvency ratio*, and *current ratio* to control for the financial health of the company. Furthermore, I control for *firm size* proxied by (log) total assets, and *firm age* measured in the (log) years since incorporation. Additionally, I control for *industry fixed effects* using the two-digit NACE code dummies, and both *GDP* and *GDP per capita* to control for level of economic development. I give an overview of all the variables considered in the main analyses as well as in the robustness checks in Appendix E.

I estimate a random effects model. A random effects model is preferred over a simple OLS, as demonstrated by the Breusch-Pagan Lagrange multiplier ($p < 0.001$). Furthermore, a random effects model is more appropriate than a fixed effects model because our moderating variable only contains variance between firms (firms are nested in countries, countries are nested in supra-national clusters). I use robust standard errors through clustering the errors on the firm level. Furthermore, I have no indication of multicollinearity. Although the correlation between “manager is GUO” and “managerial ownership” is high, the VIF values of both variables are below 2.

5.4 RESULTS

TABLE 5.2
Results: Anglo-Saxon Culture, Managerial Ownership, and firm Performance

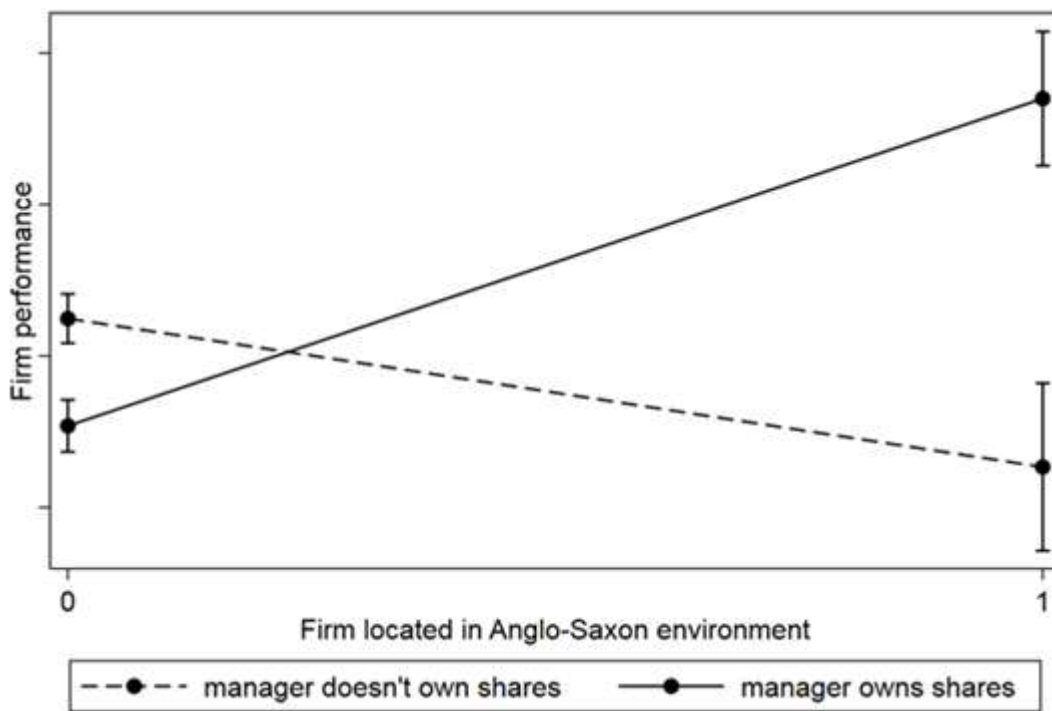
Dependent variable	Firm performance (Tobin's Q)		
	Model 1	Model 2	Model 3
Managerial ownership		-0.025** (0.039)	-0.097*** (0.000)
Anglo-Saxon firm			-0.098*** (0.001)
Man. owner. * Anglo Saxon firm (H1)			0.314*** (0.000)
Manager is GUO	-0.156*** (0.000)	-0.141*** (0.000)	-0.124*** (0.000)
Firm age	-0.144*** (0.000)	-0.145*** (0.000)	-0.143*** (0.000)
Firm size	-0.112*** (0.000)	-0.112*** (0.000)	-0.111*** (0.000)
Current ratio	0.079*** (0.000)	0.079*** (0.000)	0.079*** (0.000)
Sales growth	0.003*** (0.000)	0.003*** (0.000)	0.003*** (0.000)
GDP	0.000*** (0.000)	0.000*** (0.000)	0.000*** (0.000)
GDP per capita	0.002*** (0.000)	0.002*** (0.000)	0.002*** (0.026)
Solvency ratio	0.009*** (0.000)	0.009*** (0.000)	0.009*** (0.000)
Constant	0.390*** (0.000)	0.403*** (0.000)	0.404*** (0.000)
Number of observations	157,375	157,375	157,375
Number of firms	27,852	27,852	27,852
R-squared	22.16	22.18	22.47
Partial F-test	N/A	0.039	0.000

Note: ***p < 0.01; **p < 0.05; *p < 0.10. All models control for industry fixed effects and year fixed effects. Absolute p-values are shown in parentheses.

I estimate three different models, the results of which are shown in Table 5.2. Model 1 shows only the control variables, model 2 includes the direct effect of managerial ownership, and model 3 includes the interaction between managerial ownership and the Anglo-Saxon cluster. Model 3 represents a significant improvement over the control model (partial F-test < 0.001). My results show that the interaction of managerial ownership with the Anglo-Saxon cluster has a positive and

significant effect on firm performance ($p < 0.001$), therefore confirming the hypothesis that the relationship between managerial ownership and firm performance is culture-specific. I find that, in general, there is a significantly negative effect (model 2) of managerial ownership on performance ($p < 0.05$), while agency theory would predict the opposite. This negative effect can be explained through plotting the results of the interaction model (see Figure 5.1). Here, the model of managerial ownership has a significantly negative effect in non-Anglo-Saxon contexts, while in the Anglo-Saxon context, managerial ownership has a significant positive effect on firm performance.

FIGURE 5.1
Interaction between the Anglo-Saxon environment and managerial ownership



5.4.1 Robustness Tests

I conduct multiple robustness tests for which the results are recorded in Table 5.3. First, I re-estimate our results using both different cut-off levels (1% and 5%) and a continuous variable (running from 0% to 20%) for managerial ownership. A maximum of 20% is used because 20+% indicates the manager is the global ultimate owner (La Porta et al., 1999a); this variable is controlled for separately. Second, I exchange the dependent variable Tobin's Q for an alternative measure of performance. The alternative variables I use include price-to-book ratio and market capitalization

growth. Third, I exchange the selection of Anglo-Saxon countries to alternative models, specifically: the classic shareholder-oriented model (Haxhi & Aguilera, 2017 [U.S., U.K., and AUS]) and the old Anglo-Saxon cluster (Ronen & Shenkar, 1985 [U.S., U.K., IRL, AUS, NZL, and ZAF]). Finally, I substitute the Anglo-Saxon dummy variable with a direct measurement of individualism (Hofstede, 1980). The robustness results do not show any significant differences after the above changes were implemented.

TABLE 5.3
Robustness Checks

	Managerial Ownership			Performance		Anglo-Saxon firm		
	01%	05%	PERC	PBR	MCGR	CSOM	R&S1985	IDV
Managerial ownership	-0.168*** (0.000)	-0.184*** (0.000)	-0.016*** (0.000)	-0.059*** (0.000)	1.026*** (0.000)	-0.062*** (0.000)	-0.076*** (0.000)	-0.148*** (0.000)
Anglo-Saxon firm	0.030 (0.222)	0.051** (0.023)	0.047** (0.033)	-0.161*** (0.000)	-7.041*** (0.000)	-0.156 (0.000)	-0.075*** (0.010)	0.0002 (0.814)
Man. Owner. * Anglo-Saxon Firm (H1)	0.131*** (0.000)	0.091** (0.028)	0.015*** (0.001)	0.351*** (0.000)	3.569*** (0.000)	0.318*** (0.000)	0.315*** (0.000)	0.002** (0.013)
Manager is GUO	-0.043** (0.011)	-0.010 (0.583)	-0.189*** (0.000)	-0.047** (0.014)	1.149*** (0.001)	-0.129*** (0.000)	-0.120*** (0.000)	-0.027 (0.359)
Firm age	-0.141*** (0.000)	-0.142*** (0.000)	-0.142*** (0.000)	-0.137*** (0.000)	0.812*** (0.000)	-0.146*** (0.000)	-0.143*** (0.000)	-0.119*** (0.000)
Firm size	-0.113*** (0.000)	-0.113*** (0.000)	-0.113*** (0.000)	0.001 (0.873)	0.866*** (0.000)	-0.112*** (0.000)	-0.111*** (0.000)	-0.127*** (0.000)
Current ratio	0.079*** (0.000)	0.079*** (0.000)	0.079*** (0.000)	0.007 (0.368)	0.866*** (0.000)	0.079*** (0.000)	0.079*** (0.000)	0.024* (0.066)
Sales growth	0.003*** (0.000)	0.003*** (0.000)	0.003*** (0.000)	0.003*** (0.000)	0.392*** (0.000)	0.003*** (0.000)	0.003*** (0.000)	0.003*** (0.000)
GDP	0.000*** (0.000)	0.000*** (0.000)	0.000*** (0.000)	0.000*** (0.000)	0.001*** (0.000)	0.000*** (0.000)	0.000*** (0.000)	0.000*** (0.000)
GDP per capita	0.002*** (0.000)	0.002*** (0.000)	0.002*** (0.000)	0.001 (0.103)	-0.008 (0.171)	0.002*** (0.000)	0.002*** (0.000)	-0.001* (0.092)
Solvency ratio	0.010*** (0.000)	0.010*** (0.000)	0.009*** (0.000)	0.002*** (0.000)	0.079*** (0.000)	0.009*** (0.000)	0.009*** (0.000)	0.014*** (0.000)
Constant	0.440*** (0.000)	0.422*** (0.000)	0.426*** (0.000)	1.518*** (0.000)	18.023*** (0.000)	0.419*** (0.000)	0.400*** (0.000)	0.573*** (0.001)
N observations	157,375	157,375	157,375	148,452	142,828	157,375	157,375	40,255
N firms	27,852	27,852	27,852	27,027	26,352	27,852	27,852	6,464
R-squared	22.63	22.56	22.58	09.58	12.01	22.33	22.55	30.05
Partial F-test	0.000	0.000	0.033	0.000	0.000	0.000	0.000	0.000

Note: ***p < 0.01; **p < 0.05; *p < 0.10. All models control for industry fixed effects and year effects. Absolute p-values are shown in parentheses.

5.5 DISCUSSION AND CONCLUSION

In this chapter, I have demonstrated that the effect of managerial ownership on performance is positively moderated by the Anglo-Saxon context. My findings indicate that the Anglo-Saxon context is the only context in which managerial ownership has a significant, positive effect on performance, while the effect becomes negative in other contexts. These findings support the argumentation proposed in this chapter as well as previous theoretical work emphasizing the role of the institutional environment in which the firm is embedded (Aguilera & Jackson, 2003; Wiseman et al., 2012). Although critics have argued that agency theory is either invalid or, at the very least, only applicable in the U.S. (Ghoshal, 2005; Hofstede, 2004; Ng, 2005), I argue that my findings do not disqualify the usage of the mechanisms described by agency theory outside the Anglo-Saxon context, but rather show the need for an adjustment of the underlying human assumption based on both cultural and institutional contexts. Conflicts between agent and principal may occur on grounds other than profit maximization, and, in line with my results, incentivizing agents with shares may increase rather than decrease agency problems if the principal does not, first and foremost, aim to maximize profits.

This chapter suggests that we may need to move toward a regiocentric approach regarding principal–agent issues rather than assuming the solutions offered by agency theory are universally applicable. Other theories might fit the human behavior assumptions of other cultural contexts more closely. For instance, stewardship theory assumes humans behave in a collectivist, pro-organizational, and trustworthy manner (Davis et al., 1997), therefore more closely fitting the collectivistic cultural assumptions than does agency theory. Similarly, literature on emerging market family firms describes a set of agency problems that is unique to the context (Morck & Yeung, 2003; Peng & Jiang, 2010). Finally, there are attempts to rephrase agency theory in order to increase its sensibility to institutional differences (e.g., Heracleous & Lan, 2012; Lan & Heracleous, 2010).

Agency theory and its solutions have become a cornerstone of corporate governance both in theory and in practice. Failing to consider the cultural and institutional contexts in which agency theory is applied can lead to the application of practices that do lead to the desired outcome. Even 35 years after

CHAPTER 5: MANAGERIAL OWNERSHIP AND FIRM PERFORMANCE

Hofstede expressed the need for “more cultural sensitivity in management theories” (Hofstede, 1983: 89), a deeper understanding of the nature of agency problems and how they manifest in specific contexts is still require