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# The Effect of Ownership Structure on Firm's Financial Performance: An Empirical Study on the Most Active Firms in the Egyptian Stock Exchange

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**Abstract**
This paper seeks to examine the effect of ownership structure on firm financial performance in Egypt. Using a sample of 50 more active Egyptian companies listed on the Egyptian Stock Exchange of the non-financial sector covering the period of three financial years from 2007 to 2009. Ownership Structure is represented by Managerial Ownership, Institutional Ownership, Block holder Ownership and Free Float Ownership. Return on Assets (ROA) and Return on Equity (ROE) are used as a proxy for Firm financial Performance. Using multiple linear regressions as method of estimation, the results provide evidences that there is no significant relationship between ownership structure variables and firm financial performance measures by (ROA and ROE). This study provides many recommendations to the regulatory authorities in Egypt regarding ways to strengthen and reinforce the internal governance structure of companies especially ownership structure.
**Keywords:** Corporate governance, Ownership structure, Firm Financial Performance, Egypt

## 1. Introduction

Ownership structure is one of the main dimensions of corporate governance and is obviously seen by country-level corporate governance characteristics for example the development of the stock market and the nature of country intervention and regulation (La Porta et al.1998). Ownership structure was defined by the distribution of equity with regard to votes and capital but also by the identity of equity owners (Jensen and Meckling, 1976).

Corporate ownership structures around the world are very diverse but there seem to be two distinct groups (La Porta *et al*., 1999). In the Anglo-Saxon countries, majority of the shares are widely held or diffuse, but in the European countries shares are concentrated in the hands of a few large shareholders. When ownership is diffuse, agency problems rise owing to conflicts of interest between managers and shareholders (Jensen and Meckling, 1976; and Roe, 1994).As ownership concentration increases to a level where an owner obtains effective control of the firm, the nature of agency problems shifts away from the manager-shareholder conflicts to conflicts between the controlling owner and minority shareholders (Shleifer and Vishny, 1997).

La Porta *et al* (1997, 1998, 1999 and 2000) have shown that the countries with weak legal environment, the original owners tries to maintain large positions in their corporations which results in concentration of ownership. Equity ownership by insiders can align insider interest with those of shareholders, thereby leading to greater firm value (Klapper and Love, 2002). In underdeveloped markets in addition to weak legal enforcement reasons, due to underdeveloped nature of financial markets that would allow limited access to external financing and result in predominance of family firms (La Porta *et al.,* 1997, 1998).

Ownership structure determines the firm's profitability, enjoyed by different stake-holders. Ownership structure is an effective device for reducing the agency costs associated with the separation of ownership and management, which can be used to protect property rights of the firm (Barbosa and Louri, 2002). With the development of corporate governance, many corporations owned by disperse shareholders and are controlled by hire manager. As a results incorporated firms whose owners are dispersed and each of them owns a small fraction of total outstanding shares, tend to underperform as indicated by Berle and Means (1932).

The purpose of this paper is to examine the effect of Ownership structure on financial performance. The rest of this paper is structured as follows: section 2 reviews the previous literature and empirical hypothesis on the relationship between Ownership structure and financial performance; section 3 provides a discussion of the variables tested, model development and sample; section 4 lays out Analysis and Findings. Finally, section 5 presents research contributions and suggestions for future studies.

## 2. Literature Review and the Hypotheses

The relationship between ownership structure and financial performance has been an important subject and an ongoing debate in corporate finance literature since the work of Berle and Means (1932). They debated about conflict interests between controllers and managers. They assert that in view of growing diffusion of ownership, ability of shareholders to control managements will be less. Therefore, they suggest that correlation between ownership concentration and firm performance should be a negative one.

Their view has been challenged by Demsetz (1983), who argues that the ownership structure of a corporation should be thought of as an endogenous outcome of decisions that reflect the influence of

shareholders and of trading on the market for shares. When owners of a privately held company decide to sell shares, and when shareholders of a publicly held corporation agree to a new secondary distribution, they are, in effect, deciding to alter the ownership structure of their firms and, with high probability, to make that structure more diffuse. Subsequent trading of shares will reflect the desire of potential and existing owners to change their ownership stakes in the firm. In the case of a corporate takeover, those who would be owners have a direct and dominating influence on the firm's ownership structure. In these ways, a firm's ownership structure reflects decisions made by those who own or who would own shares. The ownership structure that emerges, whether concentrated or diffuse, ought to be influenced by the profit-maximizing interests of shareholders, so that, as a result, there should be no systematic relation between variations in ownership structure and variations in firm performance.

There are two streams of thought regarding an effective ownership structure. Firstly, insiders or managers of the firm act also as shareholders if they acquire a considerable portion of the entity's shares, and this is deemed to be useful in reducing agency conflicts and aligning the interests of management and shareholders. Secondly, outsiders who own a significant number of the firm's shares, have more power and more incentive to monitor management activity.

The ownership structure of a company can be of critical importance to the quality and comprehensiveness of the oversight administered in that company (Pergola, 2005; and Song and Windram, 2004). Four variables represent the internal and external. Ownership (namely managerial ownership, institutional ownership, block holder ownership and free float) are used to represent the ownership structure of firms in this study.

*2.1 Managerial Ownership and Firm Financial Performance*

Managerial ownership is the way to align the objective functions of the owners and the managers (Holmstrom, 1979). Managerial ownership became important in the 1980s, although the debate on relationship between managerial ownership and firm performance dates back to Berle and Means‟ thesis (1932). The agency theory suggests that a higher percentage management ownership implies higher firm value, since the goals of management and other shareholders are greatly aligned (Jensen and Meckling, 1976). Jensen and Meckling (1976) also use the agency theory to argue that managers with a high ownership are less likely to alter earnings for short-term private gains at the expense of other shareholders. Shareholders are likely to perceive that managers‟ interests are aligned with their interests when managers become shareholders by acquiring equity shares. Managerial ownership is variable which is influenced by differences in industry and business environment as much as by characteristics of a firm and its managers (Himmelberg et al., 1999).

A series of researches examines the relationship between managerial ownership and firm performance. The extensive investigation, however, has only generated mixed results:

On one hand, some researcher found positive relationship between managerial ownership and firm performance. According to Li *et al*., (2007) the results indicated that managerial ownership has a positive effect on firm performance. Although return on assets and return on sales decline post privatization, firms with high managerial ownership and, especially, high CEO ownership, show a smaller performance decline. They also find that the influence on firm performance becomes less significant at higher levels of CEO ownership. In contrast, performance continues to increase with managerial ownership. This finding suggests that, beyond a certain point, the distribution of shares would be more effective if extended to the whole management team instead of being limited to the chief executive. Similar evidence of the significant relationship was detected by Mehran (1995) found a positive relation between managerial ownership and firm performance.

Also, Wei et al., (2014) examined the relation between ownership structure and firm performance in Malaysia in trading and services sector. The sample consists of 70 companies from trading and services Sector Company listed in Bursa Malaysia during 2008-2012. They used firm age, firm size, leverage, return on assets (ROA), return on equity (ROE) as dependent variables and managerial ownership structure and Non-managerial ownership structure as independent variables .They found that the firm size, leverage and Tobin's Q have significant relationship with ownership structure of the company.

Mork *et al*. (1988) found that firm performance rises as managerial ownership increases up to 5%, falls up to the 25% level and then slightly rises again. Similar evidence of the positive relationship was detected by Mueller and Spitz (2006) they show that performance of companies with managerial ownership percentage above 40%, is being improved.

On the other hand, some researcher found no significant relationship between managerial ownership and firm performance. According to Bayrakdaroglu (2010) He found ownership concentration and free float rate variables have an effect on financial performance, foreign ownership and managerial ownership variables which measures ownership structure are not found to be statistically significant affect on financial performance. Also, Faccio and Lasfer (1999), Hubbard and Palia (1999) , Demsetz and Lehn (1985) , Agrawal and Knoeber (1996) found no relation between managerial ownership and firm performance.

Based upon the pervious discussion, the following hypothesis can be generated:
**H1:** *There is a relationship between managerial ownership and firm financial performance.*

*2.2 Institutional Ownership and Firm Financial Performance*

A considerable body of research has focused on the role of institutional investors as corporate monitors and a major governance mechanism that improves firm performance. The rationale is that due to the high cost of monitoring, only large shareholders such as institutional investors can achieve sufficient benefits to have an incentive to monitor (Grossman and Hart, 1980). Indeed, Shleifer and Vishny (1986) note that large shareholders may have a greater incentive to monitor managers than members of the board of directors, who may have little or no wealth invested in the firm. Moreover, large institutional investors have the opportunity, resources, and ability to monitor, discipline, and influence managers. McConnell and Servaes (1990), Nesbitt (1994), Smith (1996), and Del Guercio and Hawkins (1999) have found evidence consistent with the hypothesis that corporate monitoring by institutional investors can force managers to focus more on corporate performance and less on opportunistic or self-serving behavior.

Many studies have examined the effects of institutional investors on firm performance and found mixed results: Namazi and Kermani (2008) analyzed the impact of ownership structure on corporate performance of listed companies in Tehran stock Exchange. They found a significant and negative relationship between institutional ownership and firm performance and a significant and negative relationship between management ownership and firm performance. In general, there is a significant relationship between the ownership structure and performance of the companies.On the contrary, Bargezar and Babu (2008) found a positive relationship between institutional ownership and firm performance in the case of Iran. In addition, it is found that ownership structure is highly concentrated and firms with diffused ownership have performed better than those with concentrated ownership. Additionally, Loderer and Martin (1997) , Craswell *et al*., (1997), Agrawal and Knoeber(1996) observed no significant relationship between institutional ownership and firm performance.
Based upon the pervious discussion, the following hypothesis can be generated:
**H2:** *There is a relationship between Institutional ownership and firm financial performance.*

*2.3 Block holders' Ownership and Firm Financial Performance*

The role of large owners in the economy is one of the most important topics in corporate governance. Theoretically, large owners (block holders) may play a valuable role by reducing the familiar agency problems between shareholder and managers. Research has shown that the presence of a large shareholder or block holder can benefit minority shareholders (Jensen and Meckling, 1976; Schleifer and Vishny, 1986) by undertaking the monitoring role of management, but recent research has emphasized that large block holdings give rise to a second agency problem between block holders and minority investors (Shleifer and Vishny, 1997, Becht, Bolton and Röell, 2002). There is a risk that one or a group of block holders might exploit this position and expropriate and enjoy private benefits at the expense of minority shareholders (Fama and Jensen, 1983; La Porta et al., 2002). Additionally, a position close to management and the board of the company might make it possible for a block holder to influence the strategic direction of the company in ways that are not favorable to minority shareholders. This conflict between block holders and minority investors is considered being at least as relevant as the owner-manager conflict (Schleifer and Vishny, 1997; La Porta et al., 1999 and Maury and Pajuste, 2005).

Schleifer and Vishny (1997) list a number of papers that have found that block holders or large shareholders benefit minority shareholders in different ways. Japanese companies with large shareholders are more prone to replace managers in companies with poor performance than companies with dispersed ownership (Kaplan and Minton, 1994; Kang and Shivdasani, 1995 in Schleifer and Vishny, 1997). It is also found that a takeover is more likely if there are large outside shareholders (Shivdasani, 1993 in Schleifer and Vishny, 1997). Also, if a takeover is defeated, management is more likely to be reorganized in poor performing companies with block holders (Denis and Serrano, 1996 in Schleifer and Vishny, 1997). These results all suggest that block holders have the power and incentive to monitor and if necessary replace management.

The definition of a block holder in this studt is a shareholder holding at least 5% of outstanding shares. This definition agreed with the definitions made in the papers (Shleifer and Vishny, 1986; McConnell and Servaes, 1990; Short and Keasey, 1999; Agrawal and Mandelke, 1990; Weir et al., 2002; Marchica and Mura, 2005; Thomsen et al., 2006; and Hillier and McColgan, 2006). A number of studies have examined whether block holders affect the firm performance.

Many studies have examined the effects of block holders on firm performance and found mixed results: On one hand, some researcher found significant relationship between block holder ownership and firm performance. According to Guedri and Hollandts (2008) examined the impact of employee ownership (proxies by largest shareholder and shareholders who owned at least 5% of a firm's stock) on firm performance for 230 French firms over the period 2000–2005. They found a positive relationship between the largest shareholder and firm performance, whilst a negative relationship between the shareholders who owned at least 5% of a firm's

stock and firm performance. Kapopoulos and Lazaretou (2007) found that higher firm profitability requires less diffused ownership structure. He also provides evidence that large non management block holders can mitigate the valuation discounts associated with the expected agency problem. Similar evidence of the significant relationship was detected by Lins (2000) he found that non management block shareholding is positively related with firm performance.

Also, Thomsen et al., (2006) examined the causal relationship by using the Granger causality test between block holder ownership and firm value of the largest continental Europe, UK and US firms, they used Ordinary Least Squares (OLS) regression to estimate the relationship between block holder ownership and firm value. They found that causality runs from block holder ownership to firm value in continental Europe but not in the UK or the US. Further, this causality runs in a negative direction thus, they suggest, the high percentage of continental Europe block holder ownership creates conflicts of interest between block holders and firm minority shareholders.

On the other hand, some researcher found no significant relationship between block holder ownership and firm performance. According to Mehran (1995) ; McConnell and Servaes (1990) and Loderer and Martin (1997) they found no significant association between firm value and shares held by block holders.

Based upon the pervious discussion, the following hypothesis can be generated:

***H3****: There is a relationship between a block holding of 5% or more in a firm and firm financial performance.*

*2.4 Free float and Firm Financial Performance*

Diverse shareholders (free float) definitely have incentives to monitor and control managerial action and decisions. Nevertheless, the problem of collective action of those shareholders and maybe free-rider problems (single shareholders do not monitor and control but also do participate from such action and lower agency costs above average) are limiting to monitoring and controlling management (Grossman and Hart, 1988).Consequently, management may use this gap self-serving and opportunistically. Thus, a high proportion of free-float is connected with lower firm performance (McGuinness and Ferguson, 2005). Accordingly, countries like the U.S. with traditionally low ownership concentration and relying heavily on stock markets to channel the flow of capital are linked with a higher extent of investor protection (Ruiz-Mallorqui and Santana-Martin, 2009).

Hence, a higher extent of (minority) shareholder protection generally increases costs to hold bigger share proportions in those countries, as they require higher effort to achieve their goals (Becht *et al*., 2003). Despite negative effects of free-float due to losses in monitoring efficiency, high free-float ratios are a positive indicator for high liquidity of shares, too (Rojahn and Elschen, 2009). Illiquid shares cause higher cost of equity and, thus, induce cautious investment and dividend policy due to refinancing risks. On the contrary, increasing opportunity costs of a single shareholder lead to a higher risk-adjusted required rate of return (Chan and Faff, 2005). Thus, companies demand an optimum shareholder structure (Rojahn and Elschen, 2009). A major shareholder (block holder) is expected to have enough power to force management to improve corporate governance structures.

Talebnia *et al*. (2011) examined the relation between free float stock rate and stock yield rate of the listed companies in Tehran Stock Exchange. The sample consists of 320 companies during 2005 - 2009. They found there is no relation between free float stock and stock yield rate of the companies. Ongore (2011) examined the relationship between shareholder types and financial performance as measured by ROA, ROE and Dividend Yield (DY) in Listed Companies in Kenya .The sample consists of 54 listed companies in Nairobi Stock Exchange during 2006 -2008. They found a significant positive relationship between diverse ownership and firm performance.

Based upon the pervious discussion, the following hypothesis can be generated:

**H4***: There is a relationship between diffuse ownership (free float) and firm financial performance.*

Table 1. Empirical Analysis on the Effect of Ownership Structure on Firm Financial Performance

| Paper | Sample | Period | Performance Measure | Methodology | Relationship |
|---|---|---|---|---|---|
| Zhang and Kyaw (2017) | 1178 | 2004 - 2008 | -ROA<br>-ROE<br>- Tobin's Q | fixed-effect panel model | institutional ownership has a positive relationship and Tradable shares have a negative relationship with firm performance |
| Gugong et al., (2014) | 17 firms | 2001 – 2010 | ROA & ROE | the simple linear regression | A positive relationship |
| Manawaduge, A. and De Zoysa, A. (2013) | 157 | 2000–2008 | -ROA<br>-ROE<br>-market-to-book-value ratio (MBR)<br>- Tobin's Q | Regression Analysis | A positive relationship with ROA & ROE and no significant relationship with MBR & TQ |
| Pathirawasam, C. (2013). | 102 | 2008 - 2009 | ROA | Ordinary Least Square (OLS) | No significant relationship |
| Tanrioven and Aksoy (2010) | 113 | 1996-2009 | ROA , ROE and Net Profit Margin | Regression analysis | A positive relationship |
| Li *et al*., (2007) | 155 Chinese | 1992–2000 | ROA & ROS | OLS | A positive relationship |
| Mork *et al*. (1988) | 500 | 1980 | Tobin's Q | piecewise linear regressions | Nonlinear association between managerial ownership and firm value |
| Bayrakdaroglu (2010) | 30 | 2005- 2009 | ROA & ROE | panel regressions | No significant relationship |
| Mehran (1995) | 170 | 1979-1980 | ROA & Tobin's Q | OLS | A positive relationship |
| Hubbard and Palia (1999) | 600 | 1982 - 1992 | Tobin's Q | OLS | No significant relationship |
| Agrawal and Knoeber (1996) | 400 | 1987 | Tobin's Q | OLS | No significant relationship |
| Bargezar and Babu (2008) | 50 | 2001-2003 | ROA & ROE | OLS | A positive relationship |
| Ongore (2011) | 54 | 2006-2008 | ROA & ROE | OLS | A positive relationship |

## 3. Research Methodology

*3.1 Data collection and sample selection*

The sample consists of 50 most active companies on Egyptian stock exchange, which are 50 firms belong to 12 sectors, which are Basic Resources, Chemicals, Construction and Materials, Food and Beverage, Media and Telecommunications, etc. In this study the researcher excludes the banking and insurance sectors because the characteristics of these firms are different from the firms in other industrial sectors in terms of specialized in nature and were subject to different regulations, tax and accounting rules (Zeitun and Tian 2007). The final sample consists of 48 firms.

This paper uses secondary data only which is collected from the most recent available financial statements of the firms. This study employed annual data from 2007 to 2009. The researcher depends on the Egypt exchange disclosure book and official Egypt stock exchange web page to collect data.

*3.2 Variables and Measurement*

The variables used in this study can be categorized into two main types which are; the dependent and independent variables.

*3.2.1 Dependent Variable*

The dependent variable for this study is the financial performance of firms in the Egyptian market. The performance will be measured by the Return on Assets (ROA) and Return on Equity (ROE). Return on equity (ROE) and Return on assets (ROA) are the most commonly used measures in the former ownership literatures (Brown and Caylor, 2009; Soliman , 2013 ).

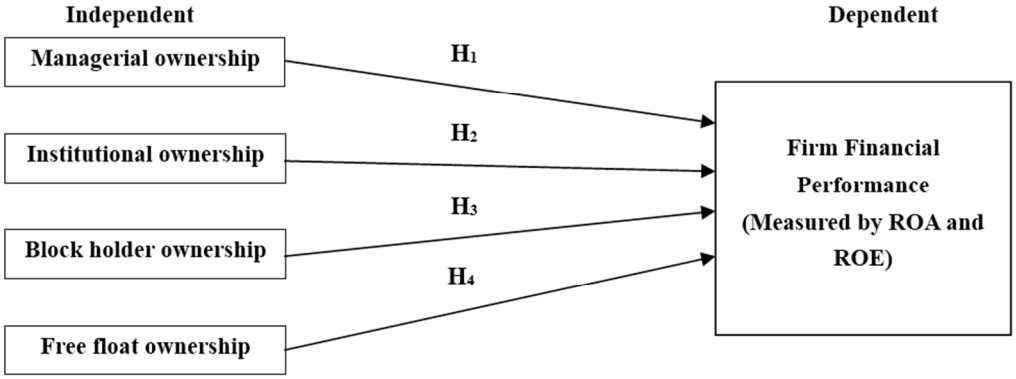
*3.2.2 Independent variables*

The independent variables employed in this study are factors identified in prior research as influences performance, either positively or negatively. There are four independent variables that will be measured. These

are managerial ownership, institutional ownership, block holder ownership and free float ownership.
This research tried to look at the possibility of the relationship between dependent variable and independent variables .The relationship between dependent variable and independent variables is explained in figure (1).

Figure 1
Relationship Diagram between independent variables and dependent variable




*3.2.3 Control variables*
The control variables were selected in accordance to similar studies made on this topic (e.g. Gutiérrez and Tribó, 2004; Maury and Pajuste, 2005; and Leung and Horwitz, 2009). The selected variables are firm size and financial leverage. These variables are selected because they have been shown to have simultaneous effect on both ownership structure and performance (Gutiérrez and Tribó, 2004).
Table (2) presents a summary for all the variables including the dependent, independent and control variables of the study.

Table 2. Summary of dependent, independent and control variables

| Variables | Measures |
|---|---|
| **Performance measures:** Return on Assets (ROA) | Return on Assets (ROA) $= \frac{\text{Net Profit After Tax}}{\text{Total Assets}}$ |
| Return on Equity (ROE) | Return on Equity (ROE) $= \frac{\text{Net Profit After Tax}}{\text{Shareholders Equity}}$ |
| **Ownership variables:** Managerial ownership (MOWN) | The percentage of total shares held by all members of the board of directors divided by total ordinary shares outstanding. |
| Institutional ownership ( IOWN) | The percentage of shares held by institutional investors to total outstanding shares. |
| Block holder ownership (BOWN) | The percentage of equity owned by persons and institutions holding 5% or more of the company's equity. |
| Free float ownership (FF) | The portion of a company's equity that is available for trading on the stock market. |
| **Control variables:** Firm size (Size) | The natural logarithm of total assets |
| Financial Leverage (LEV) | Financial Leverage (LEV) $= \frac{\text{Total Liabilities}}{\text{stockholders' equity}}$ |

*3.3 Research Model*
The model used in the study was adapted from Ongore (2011). This model of analysis was done to examine the simultaneous effects of several independent variables on a dependent variable. The Predictive Analytics Software (PASW) version 18 program will be to generate the result from the data. To examine the effect of ownership on firm financial performance, this study estimate using the following model:

$$p_{i,t=}\beta_0 + \beta_1\ MOWN_{i,t} + \beta_2\ INSTOWN_{i,t} + \beta_3\ BOWN_{i,t} + \beta_4\ FFOWN_{i,t} + \beta_5\ SIZE_{i,t} + \beta_6\ LEVE_{i,t} + \varepsilon_{i,t} \quad (1)$$

where $p_{i,t}$ is the financial performance of firm i in period t represented by both $ROA$ and $ROE$; $MOWN$, Managerial ownership; $INSTOWN$, Institutional shareholding; $BOWN$, Block holding ; $FFOWN$ , Free float; $SIZE$, Firm size; $LEVE$, Financial Leverage ; $\beta_0$ is the intercept, $\beta$ is the regression coefficient and $\varepsilon$ is the composite error terms.

## 4. Findings and Analysis

*4.1 Descriptive Analysis*
Table (3) summarizes the Minimum, Maximum, Mean and Standard Deviations for the research variables.

Table 3. Descriptive statistics

| Research Variables | Minimum | Maximum | Mean | Std. Deviation |
|---|---|---|---|---|
| ROA | -49.00- | 40.80 | 6.7132 | 10.97182 |
| ROE | -29.00- | 104.00 | 17.1243 | 19.60025 |
| Managerial Ownership | .0000 | .6627 | .089586 | .1602698 |
| Institutional Ownership | .0000 | .9730 | .382857 | .2827408 |
| Block holder Ownership | .0000 | .9390 | .445419 | .2317676 |
| Free float Ownership | .0240 | .9900 | .470849 | .2268400 |
| Firm size | 4.28 | 7.98 | 6.0046 | .79579 |
| Financial Leverage | -1.599- | 11.732 | 1.52832 | 2.186397 |

*Sample size (n) = 48 firm year observations during the years 2007 – 2009, Based on the availability of data

The mean of return on asset ROA of 48 companies is 6.7132, with a minimum of -49.00 to a maximum of 40.80. While the mean of return on equity ROE is 17.1243, with a minimum of -29.00 to a maximum of 104.00 .The results from table (3) show that the Managerial Ownership has a mean of 8.95%, with a minimum of 0% to a maximum of 66.27%. Also it explains that, there are companies that do not have the Managerial Ownership and thus the ownership structure is distribution between the remaining ownership. The average manager's ownership in Egyptian companies is 8.958 %, while the average institutional investor ownership is 38.28%, block holder ownership is 44.5% and free float is 47.08%. This indicates that managerial ownership compared to the rest variables has the lowest influence on firm financial performance. Results also show that the distribution of manager's ownership is wide with a Min. of 0.00% and a Max. of 66.27%.Also, the institutional ownership range is wide with a Min. of 0.00% and a Max of 97.30%. The mean of the ownership blocks is 44.54%, there are companies with a truly diffused ownership structure, in which no shareholder owns more than 5% of the shares; therefore the minimum block is 0.00%. Results also show that the mean of free float is 47.08%, with a distribution range of Min. of 2.40 % and a Max. of 99 %. Results show that the mean of Firm size is 6.0046, with a minimum of 4.28 to a maximum of 7.98. The mean of Financial Leverage is 1.52832, with a minimum of -1.599 to a maximum of 11.732.

*4.2 Pearson Correlation coefficients*

Correlation is a single number that describes the degree of relationship between two variables. The coefficient has a range of possible value from -1.00 to +1.00. The value indicates the strength of the relationship, while the sign (+ or -) indicates the direction.

Table 4, Table 5 presents Pearson's correlation analysis which express the degree or strength of the linear relationship between independent and dependent variables, covering the three year period 2007- 2009 at level 5% of significance. The correlation coefficients among variables in the study are presented as follows.

Table 4 Pearson correlation between tested variables and ROA (2007-2009)

| | | ROA | Managerial ownership | Institutional ownership | Block Holder ownership | Free float ownership | Firm size | Financial Leverage |
|---|---|---|---|---|---|---|---|---|
| **ROA** | **Pearson correlation** | 1 | | | | | | |
| | **Sig. (2- tailed)** | | | | | | | |
| **Managerial ownership** | **Pearson correlation** | .070 | 1 | | | | | |
| | **Sig. (2- tailed)** | .406 | | | | | | |
| **Institutional ownership** | **Pearson correlation** | .067 | -.521-** | 1 | | | | |
| | **Sig. (2- tailed)** | .426 | .000 | | | | | |
| **Free float ownership** | **Pearson correlation** | -.189-* | -.080- | -.669- | 1 | | | |
| | **Sig. (2- tailed)** | .023 | .339 | .000 | | | | |
| **Block Holder ownership** | **Pearson correlation** | .141 | .203* | .464** | -.866-** | 1 | | |
| | **Sig. (2- tailed)** | .092 | .014 | .000 | .000 | | | |
| **Firm size** | **Pearson correlation** | .240** | .078 | .174* | -.350-** | .401** | 1 | |
| | **Sig. (2- tailed)** | .004 | .353 | .038 | .000 | .000 | | |
| **Financial Leverage** | **Pearson correlation** | .031 | .128 | -.094- | .121 | -.005- | .049 | 1 |
| | **Sig. (2- tailed)** | .711 | .127 | .264 | .150 | .952 | .561 | |

Table 4, indicates that ROA is positively correlated with Managerial ownership and Institutional ownership but insignificant at 5% levels. The results also show that a negative and significant (0.023) relationship exists between ROA and Free float ownership. The results also show that a positive but insignificant (0.092) relationship exists between ROA and Block Holder ownership. Also the relation between ROA and Firm size is positive relation and significant relation (0.004). Financial Leverage also has a positive but insignificant (0.711) relationship with ROA.

Table 5 Pearson correlation between tested variables and ROE (2007-2009)

| | | ROE | Managerial ownership | Institutional ownership | Free float | Block Holder ownership | Firm size | Financial Leverage |
|---|---|---|---|---|---|---|---|---|
| **ROE** | **Pearson correlation** | 1 | | | | | | |
| | **Sig. (2- tailed)** | | | | | | | |
| **Managerial ownership** | **Pearson correlation** | .111 | 1 | | | | | |
| | **Sig. (2- tailed)** | .185 | | | | | | |
| **Institutional ownership** | **Pearson correlation** | .180* | -.521-** | 1 | | | | |
| | **Sig. (2- tailed)** | .031 | .000 | | | | | |
| **Free float** | **Pearson correlation** | -.283-** | -.080- | -.669-** | 1 | | | |
| | **Sig. (2- tailed)** | .001 | .339 | .000 | | | | |
| **Block Holder ownership** | **Pearson correlation** | .339** | .203* | .464** | -.866-** | 1 | | |
| | **Sig. (2- tailed)** | .000 | .014 | .000 | .000 | | | |
| **Firm size** | **Pearson correlation** | .097 | .078 | .174* | -.350-** | .401** | 1 | |
| | **Sig. (2- tailed)** | .248 | .353 | .038 | .000 | .000 | | |
| **Financial Leverage** | **Pearson correlation** | .278** | .128 | -.094- | .121 | -.005- | .049 | 1 |
| | **Sig. (2- tailed)** | .001 | .127 | .264 | .150 | .952 | .561 | |

The results are shown in Table 5, ROE is positively correlated with Managerial ownership but insignificant because sig (0.185) greater than 0.05. ROE also has a positive and significant (0.031) relationship with Institutional ownership. The results also show that a negative and significant (0.001) relationship exists between ROE and Free float. The results also show that a positive and significant (0.000) relationship exists between ROE and Block Holder ownership. The relation between ROE and Firm size is positive relation but insignificant (0.248). Financial Leverage has a positive and significant (0.001) relationship with ROE.

*4.3 Multiple regression analysis*

*4.3.1 Regression results for firm performance (ROA)*

In table (6) the regression model shows the association between ROA and Managerial ownership, Institutional ownership, Block holder, Free Float ownership, Firm size and financial leverage during the period from 2007 to 2009.

Table 6. Regression Coefficients [a]

| Model | | Unstandardized Coefficients | | Standardized Coefficients | t | Sig. |
|---|---|---|---|---|---|---|
| | | B | Std. Error | Beta | | |
| 1 | (Constant) | 4.397 | 12.618 | | .348 | .728 |
| | Managerial Ownership | -.064- | 8.923 | -.001- | -.007- | .994 |
| | Institutional Ownership | -4.581- | 6.849 | -.118- | -.669- | .505 |
| | Block holder | -12.065- | 8.406 | -.252- | -1.435- | .154 |
| | Free float | -19.792- | 11.136 | -.402- | -1.777- | .078 |
| | Firm size | 3.042 | 1.255 | .220 | 2.424 | .017 |
| | Leverage | .356 | .442 | .068 | .806 | .422 |

a. Dependent Variable: ROA

$$\boldsymbol{ROA} = 4.397 - 0.064\ MOWN - 4.581\ INSTOWN - 12.065\ BOWN - 19.792\ FFOWN + 3.042\ SIZE + 0.356\ LEVE$$

From regression result, It is found that Managerial Ownership has a negative and insignificant (P-value = 0.994, p > 0.05) relationship on firm financial performance (ROA). This result does not support for the argument that managerial ownership has a positive significant relationship on firm financial performance. Therefore, hypothesis $H_1$ is rejected. Institutional Ownership has a negative and insignificant (P-value = 0.505,

p > 0.05) relationship on firm financial performance (ROA) .Therefore, hypothesis $H_2$ is rejected. The results also show that a negative and insignificant (P-value = .154, p > 0.05) relationship exists between ROA and Block holder. Therefore, hypothesis $H_3$ is rejected. Also The relation between ROA and Free float negative relation and insignificant (P-value = .078, p > 0.05). Therefore, hypothesis $H_4$ is rejected.

For the control variables, the results also show that firm size has a positive and statistically significant relationship with firm financial performance (ROA) (P-value = .017, p < 0.05). And the relationship with leverage is positive but insignificant (P-value = .422, p > 0.05).

- *Model Summary*

R square gives the amount of variance in ROA explained by the predictor variables together. Table (7), shows the model summary. The $R^2$ is .089. This means that 8.9% of the variation in ROA is explained by the variation in the independent variables.

Table 7. Model Summary

| Model | R | R Square | Adjusted R Square | Std. Error of the Estimate |
|---|---|---|---|---|
| 1 | .298[a] | .089 | .049 | 10.72798 |

a. Predictors: (Constant), Financial Leverage, Firm size, Managerial Ownership, Free float , Block holder Ownership, Institutional Ownership

Table 8. ANOVA[(b)]

| Model | Sum of Squares | df | Mean Square | F | Sig. |
|---|---|---|---|---|---|
| Regression | 1528.262 | 6 | 254.710 | 2.213 | .045[a] |
| Residual | 15652.173 | 136 | 115.090 | | |
| Total | 17180.435 | 142 | | | |

a. Predictors: (Constant), Financial Leverage, Firm size, Managerial Ownership, Free float , Block holder Ownership, Institutional Ownership

b. Dependent Variable: ROA

From ANOVA, it can be seen that the regression model is significant as a whole because sig = 0.045 less than 0.05.

*4.3.2 Regression results for firm performance (ROE)*

In table (9) the regression model shows the association between ROE and Managerial Ownership, Institutional Ownership, Block holder Ownership, Free float, Firm size and financial leverage during the period from 2007 to 2009.

Table 9. Regression Coefficients (a)

| Model | | Unstandardized Coefficients | | Standardized Coefficients | t | Sig. |
|---|---|---|---|---|---|---|
| | | B | Std. Error | Beta | | |
| 1 | (Constant) | .846 | 21.044 | | .040 | .968 |
| | Managerial Ownership | 13.247 | 14.882 | .108 | .890 | .375 |
| | Institutional Ownership | 12.091 | 11.422 | .174 | 1.059 | .292 |
| | Block holder | 25.230 | 14.019 | .295 | 1.800 | .074 |
| | Free float | 5.117 | 18.571 | .058 | .276 | .783 |
| | Firm size | -1.186- | 2.093 | -.048- | -.566- | .572 |
| | Leverage | 2.649 | .737 | .285 | 3.594 | .000 |

a. Dependent Variable: ROE

$$\boldsymbol{ROE} = 0.846 + 13.247\,MOWN + 12.091\,INSTOWN + 25.230\,BOWN + 5.117\,FFOWN - 1.186\,SIZE + 2.649\,LEVE$$

From regression result, It is found that Managerial Ownership has positive relationship on firm financial performance (ROE) but insignificant (P-value = .375, p > 0.05). Therefore, hypothesis $H_1$ is rejected. Also The relation between ROE and Institutional Ownership positive relation but insignificant (P-value = .292, p > 0.05). Hence, hypothesis $H_2$ is rejected. The results also show that a positive but insignificant (P-value = .074, p < 0.05) relationship exists between ROE and Block holder. Therefore, hypothesis $H_3$ is rejected. Also The relation between ROE and Free float positive and insignificant (P-value = .783, p > 0.05). Therefore, hypothesis $H_4$ is rejected.

For the control variables, the results show that Firm size has a negative and insignificant relationship with firm financial performance (ROE) (P-value = .572, p < 0.05). The results also show that leverage has a positive and statistically significant relationship with firm financial performance (ROE) (P-value = .000, p < 0.05).

- **Model Summary**

Table (10), shows the model summary. The R2 is 0.207. This means that 20.7% of the variation in ROE is

explained by the variation in the independent variables.

Table 10. Model Summary

| Model | R | R Square | Adjusted R Square | Std. Error of the Estimate |
|---|---|---|---|---|
| 1 | .455[a] | .207 | .172 | 17.89158 |

a. Predictors: (Constant), Financial Leverage, Firm size, Managerial Ownership, Free float , Block holder, Institutional Ownership

Table 11. ANOVA(b)

| Model | Sum of Squares | df | Mean Square | F | Sig. |
|---|---|---|---|---|---|
| Regression | 11335.037 | 6 | 1889.173 | 5.902 | .000[a] |
| Residual | 43534.762 | 136 | 320.109 | | |
| Total | 54869.799 | 142 | | | |

a. Predictors: (Constant), Financial Leverage, Firm size, Managerial Ownership, Free float , Block holder, Institutional Ownership

b. Dependent Variable: ROE

From ANOVA, it can be seen that the regression model is significant as a whole because sig = 0.000 less than 0.05.

## 5. Conclusion

This study examined the effect of Ownership Structure on firm financial performance on practices of listed companies in Egypt, from 2007 to 2009. The empirical results of the event study were presented. The results of managerial ownership, institutional ownership, block holder ownership and free float have a negative and insignificant relationship with ROA measure. The results also show that a positive but insignificant relationship exists between Ownership structure variables and ROE measure. Therefore, a general conclusion can be determined that all hypotheses are rejected.

Firstly, the relationship between managerial ownership and firm financial performance under ROA and ROE performance measures, it was found no significant relationship between them. The positive relationship between managerial ownership and ROE its prediction as per the Companies Law No.159 of 1981 which is declaring that board of directors deserve to take 10% of the profit and consequently board of directors prefer to increase the company profit in order to achieve the 10% of the profit, regardless of the increase of the company actual value. In another words, it's found that the actual value of the stock owned by the shareholders does not increase. Accordingly, the Egyptian companies should locate a maximum limit for the reward of the board of directors like in Saudi Arabia maximum limit for the board of director's reward is specified.

Secondly, the relationship between the proportion of institutional share ownership and firm financial performance under ROA and ROE performance measures, the result was found no significant relationship between them. On the one hand, some studies have suggested that Institutional investors will help increase the influence of the external shareholders to put pressure on listed companies to improve firm performance (McConnell and Servaes, 1990; Nesbitt, 1994; Smith, 1996; Del Guercio and Hawkins, 1999; Cornett *et al*., 2007). However, on the other hand, Maug (1998) notes that whether institutions use their ability to influence corporate decisions are partially a function of the size of their shareholdings. If institutional investor shareholdings are high, shares are less marketable and are thus held for longer periods. In this case, there is greater incentive to monitor a firm's management. However, when institutional investors hold relatively few shares in a firm, they can easily liquidate their investments if the firm performs poorly, and therefore have less incentive to monitor. They focus mainly on current earnings rather than long-term earnings in determining stock prices (Bushee, 2001). They engage less in the management monitoring process and, if they are unhappy with the firm's results, they prefer to sell their stakes rather than to monitor or remove inefficient managers (Coffee, 1991).Thus, in general, Institutional ownership does not affect firm financial performance of Egyptian listed companies although the proportion of institutional share in listed companies is not small this mean that they don't attend The Corporate General Assembly Meetings (GAM) and therefore, they don't contribute in making decisions that benefit the company.

Thirdly, the empirical results report that the relationship between block holder ownership and firm financial performance under ROA and ROE performance measures, it was found no significant relationship between them. On the one hand, large owners (block holders) will reduce the conflict of interest between shareholders and managers in Egyptian listed companies, since Egyptian investors are unable to monitor executives effectively. On the other hand, block holders will exacerbate the conflict of interest between shareholders, thereby decreasing firm financial performance (Dahya *et al*., 2008). These opposing effects of block holder ownership on firm financial performance lead to the insignificant effect of block holder ownership on firm financial performance in Egyptian listed companies.

Fourthly, the empirical results indicate that there was insignificant relationship between the proportion

of tradable shares and firm financial performance in Egyptian listed companies. It implies that although it was found the higher proportion of tradable shares in Egyptian listed companies, it was noted that these shareholders are less concerned about the quality of corporate governance of Egyptian listed companies. As a result, these new investors lack the ability to monitor the companies and drive the managerial team to align managerial activities with the interest of the company. Resulting of insignificant relationship between the proportion of tradable shares and firm financial performance (ROA and ROE) it's necessary for the company to motivate these shareholders to attend the company meetings and to know the firm work progress in order to cooperate in improving the company performance.

At the same time, the ownership structure variables: insider ownership, institutional investors, block holder and free float have an insignificant impact on Egyptian firm performance. This result may be interpreted by the absence of a real application for the appropriate principles and standards of corporate governance to the listed firms in the Egypt.

This study suggests some recommendations to the Capital Markets Authority (CMA) to make mandatory the implementation corporate governance code for the listed companies.

Firstly, The positive relationship between managerial ownership and ROE its prediction as per the Companies Law No.159 of 1981 which is declaring that board of directors deserve to take 10% of the profit and consequently board of directors prefer to increase the company profit in order to achieve the 10% of the profit, regardless of the increase of the company actual value. In another words, it's found that the actual value of the stock owned by the shareholders does not increase. Accordingly, the Egyptian companies should locate a maximum limit for the reward of the board of directors like in Saudi Arabia maximum limit for the board of director's reward is specified. Secondly, the investors which represent free float ownership should attend The Corporate General Assembly Meetings (GAM) to contribute in making decisions that benefit the company. Thirdly, Ownership structure should include a higher percentage of insider shareholders from top managers and employees. Finally, the government should help in building a cadre of qualified, experienced, and professional directors and owners that understand the business case and have the tools to effectively implement good corporate governance.

For future research, this study is using a small sample of 48 companies. This sample may be small in size and, by construction, composed of the most active Egyptian listed companies and thus may not be representative of the population of Egyptian firms, consequently, caution should be considered in evaluating the results. Thus, it might have been better to look at companies from a wider range. Also, this study focuses on the four major variables that were used by prior researchers. Thus, it would be beneficial if further research would be able to include more factors that affect the relationship between ownership structure and financial performance of firms such as government ownership, family ownership and dividends and other financial ratios to reach a significant relationship between dependent and independent variables.

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