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Ownership Structure and Publicness of Firms: A Literature Review

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ABSTRACT

There has been an extensive body of literature studying the link between ownership structure and firm performance. Some of them focus on the performance difference across ownership types (i.e. state vs foreign vs private domestic). On the other hand, some studies stress ownership structure on the fraction of ownership based on agency theory (i.e. majority versus minority) and its derivatives (e.g. ultimate ownership, cross listing). However, an important element has not been explored while discussing ownership structure of firms which is the concept of publicness of firms. Publicness is important to explain to which extent an organization is related with governmental institutions. In fact, there are many engagements of firms with governmental bodies (e.g. deposit and lending from and to public organization). In this present paper, I provide a comprehensive literature review on the intersection between publicness level of firms and ownership structure. Going deeper, I also provide a literature review on the measurement of publicness and postulate a model to link between these two and firm performance as a venue for future studies.

Kata Kunci:
Teori Agensi; Kinerja Perusahaan; Struktur Kepemilikan; Hubungan Politik; Kepublikan

ABSTRAK

Banyak literatur yang mempelajari hubungan antara struktur kepemilikan dan kinerja perusahaan. Beberapa di antaranya fokus pada kinerja perusahaan dengan tipe kepemilikan yang berbeda (yaitu pemerintah vs asing vs swasta domestik). Di sisi lain, beberapa studi menekankan struktur kepemilikan pada pemecahan kepemilikan berdasarkan teori agensi (yaitu mayoritas versus minoritas) dan derivatifnya (misalnya ultimate ownership, cross listing). Namun, elemen penting tentang struktur kepemilikan perusahaan dalam konsep publicness perusahaan belum banyak dieksplorasi. Publicness penting untuk menjelaskan sejauh mana sebuah organisasi berhubungan dengan lembaga pemerintah. Pada kenyataannya, ada banyak keterlibatan perusahaan dengan lembaga pemerintah (misalnya simpanan dan pinjaman dari dan ke organisasi publik). Tulisan ini, memberikan tinjauan literatur secara komprehensif tentang hubungan antara tingkat publicness perusahaan dan struktur kepemilikan. Lebih jauh, saya juga memberikan tinjauan literatur tentang pengukuran publicness dan mendalilkan model untuk menghubungkan antara kedua hal tersebut dengan kinerja perusahaan, sebagai wahana bagi penelitian selanjutnya.

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The concept of publicness has been extensively studied in management and organization areas pioneered by Bozeman (1987), Nutt & Backoff (1993), and Bozeman & Bretschneider (1994). Basically, it could be considered as to which extent an organization is related with governmental institutions (Untoro & Angriawan, 2016). More formally, Anderson (2012) defines that publicness is a characteristic of an organization reflecting the extent to which the organization is influenced by political power. The publicness level of an organization becomes important due to it has been a tool to differentiate between private and public organizations (Boyne, 2002). Goldstein & Naor (2005) mention that there are 4 dimensions of publicness which are ownership, goal setting, funding, and control.

It is, however, slightly different with the concept of government-controlled firms or state-owned enterprises that have been explored by economics, finance, and accounting scholars (e.g. Dewenter & Malatesta, 2001; La Porta, Lopez-de-Silanes, & Shleifer, 2002; Goldeng, Grünfeld, & Benito, 2008; Prabowo et al., 2014). Aulich (2010) also point out that publicness is different with ownership, it is more on control and connectedness rather than on ownership. Most of studies on the government-controlled firms argue that disentangling between public and private is a dichotomous and there is no grey area in between. The publicness concept takes the different perspective in which the difference between public and private firms is continuous not discrete (Goldstein & Naor, 2005). Therefore, rather than using a dummy variable to measure the publicness, scholars in management build some indicators to measure the degree (level) of publicness. However, the measurements (constructs) are mostly taken using self-reporting questionnaire which is criticized due to more likely to be bias.

Most papers studying publicness in empirical way take the context in the public service organization such as universities (Bozeman & Bretschneider, 1994; Feeney & Welch, 2012), hospitals (Goldstein & Naor, 2005), public transport (Paget-Seekins & Tironi, 2016), and local government (Untoro & Angriawan, 2016). Little is found on the publicness level of profit organization (firms). In this present paper, I provide a comprehensive literature review on the intersection between publicness level of firms, ownership and political relatedness. Here, I focus on the publicness level of firms or corporate as in fact, there are many engagements of firms with governmental bodies even though those firms are privately-owned firms. For instance, in the banking industry, both public and private banks are related to the government through for example deposit and lending from and to public organization. Going deeper, I also provide a literature review on the measurement of publicness and postulate a model to link between these two and firm performance as a venue for future studies.

PUBLICNESS OF FIRMS, OWNERSHIP, AND POLITICAL RELATEDNESS

Ownership structure has been extensively studied in finance, management, economics, accounting, and public administration. Agency theory (Jensen & Meckling, 1976) is most used perspective to explain the role of ownership structure on the organization outcomes. This theory basically explains that the separation of ownership and control could lead to agency problem where there is self-interested behaviour of managers (agent) which is not in line with the primary objective of the stockholders (principal). It then could also lead to the conflict between majority (agent) and minority shareholders/ principal (see paper of Bhaumik & Gregoriou (2010) for more comprehensive review on this particular issue).

Many empirical papers look at the outcome (performance) differences between public and private firms (e.g. Dewenter & Malatesta, 2001). In a seminal paper, Shleifer & Vishny (1994) argue that public (state-owned) firms could be less efficient due to the self-interest of politicians. Some other empirical papers find the same results which is the lower performance and less efficient government-controlled firms compared to private firms due to political and social aspects misallocation of lending (e.g. Dinc, 2005), excess employees (Wu, Wu, & Rui, 2010), and others. Few papers find differently either insignificant different or higher performance of state-owned enterprises than private firms (see Untoro (2016) for detailed literature review in this particular field). For instance, Prabowo et al. (2014) argue that due to their higher market power, state-owned enterprises are still more profitable even though they may be less efficient than private firms.

Some papers focus on the difference performance between domestic and foreign-controlled firms (e.g. Claessens, Kunt, & Huizinga, 2001; Detragiache, Tressel, & Gupta, 2008). A number of papers find positive effect of foreign entry especially in developing countries due to technological advancement and better in human resources and human capital making foreign firms more efficient compared to domestic firms. The other strand of literature regarding ownership structure, standing on the agency theory as explained earlier, is on the fraction of ownership (i.e. majority versus minority) and its derivatives (e.g. ultimate ownership, cross listing, …) on some aspects such as performance and firm value, see for example the paper of Lepetit, Saghi-Zedek, & Tarazi (2015).

On the other hand, those from management and public administration have also introduced the concept of publicness which is to which extent an organization is related with governmental institutions (Untoro & Angriawan, 2016). Similarly, Anderson (2012) also defines that the extent to which firms influenced and benefitted by political authority can define the publicness level of firms. By using this definition, the correlation between government ownership (public) and publicness level may not be so high due to some private institutions may have strong relations with governmental institutions. It has been proved in some finance and economics papers that firm political connections of firms are not only embedded in the state-owned enterprises but some private firms also have links with the political power. For example the paper of Nys, Tarazi, & Trinugroho (2015), they provide empirical evidence that some private banks are also politically connected in some ways such as ownership by politicians or hiring politicians or former top bureaucrats in their board. Therefore, the definition of publicness level of firms is apparently opaque. I, therefore, argue here that the concept of publicness of firms is closer to the concept of political relatedness rather than the concept of government ownership of firms. There is a strong intersection between these two which could be combined for future studies as mostly people disentangle between publicness and political relatedness.

MEASURING PUBLICNESS LEVEL OF FIRMS

As I argue that the publicness level of firm is the extent to which a firm has relation with governmental organization, it is therefore, I could suggest some new venues of research in the future especially with regards to the measurement of publicness level of firms. It is previously explained that most studies on publicness mostly conducted by those from management and public administration fields have built the measures of publiness level of organizations mainly using self-reporting survey employing questionnaire. For example, our previous study (Untoro & Angriawan, 2016) adopt the widely-used 14 questions introduced by Frederickson et al. (1976) to measure the publicness level of organization. An exception is the paper of Goldstein & Naor (2005) in which they measure publicness level of firms by combining objective measures for the 3 dimensions of publicness which are ownership (profit or non-profit), goal setting, as well as funding, and self-reporting survey for capturing one dimension of publicness which is control. Bozeman (1987) also explains the various sources to differentiate between public and private organizations which are ownership, funding, and political control. However, most of them lack of objectives tools (measures) to precisely derive the three dimensions into measurable proxies.

In this present paper, I introduce the new measures of publicness level of organization, more particular profit organization or firm. I therefore argue that firms have more engagements with political power could have a higher level of publicness although they are "formally" categorized as private firms. Engagements with political authority could be, for example banking firms, in the form of deposits banks receive from governmental agencies and lending to governmental organizations including state-owned enterprises. Nys, Tarazi, & Trinugroho (2015) explain that banks having connections with political authority have easier access to get deposit funding from governmental organizations. Similarly, in the non-financial firms, the relations could be measured through the sales to the governmental institutions or the number of projects of governmental institutions runs by the firms to total outstanding projects. Agrawal & Knoeber (2001) argue that the need of political connections is more prevalent for companies with larger sales to government, exports, and lobbying.

As it is argued before that the degree of publicness of firms are related to the political relatedness they have, the other measure or proxy that could be considered to reflect the publicness level of firms is the composition of the members of board of directors. For firms hiring more politicians and former bureaucrats on the board, it could be considered that those firms are more connected with the political power. Therefore, it could be argued that they have a higher level of publicness.

However, it should also be pointed out that publicness level of firms which is measured by its degree of political relatedness could have an endogeneity issue. According to Agrawal & Knoeber (2001), the level of political relatedness is strongly affected by the specific characteristics of firms. Therefore, when doing an empirical study, the issue of endogeneity should be tackled by for example using instrumental variables.

PUBLICNESS, OWNERSHIP, AND FIRM PERFORMANCE

In this section, I provide some venues for future studies to empirically examine the link between publicness of firms and ownership as well as their impact on firm performance. It has been extensively done that ownership, both with regards to the type of ownership and the fraction of ownership, has an impact on firm performance. On the other hand, some papers have also discussed the impact of publicness level on some organization outcomes. Then, related to the previous explanation, I am questioning whether there is an intersection between publicness and ownership in affecting firm performance. More specifically, is the effect of publicness level of firms which is reflected by political relatedness is different across type of ownership and the fraction of ownership?

By taking this new perspective that I argue earlier in which for profit organization, the level of its publicness could be related to the political relatedness, first I argue that the higher publicness level of firms would lead to better or lower performance. In some papers discussing the political relatedness of firms, there are some channels to argue that political relatedness has a positive impact on firm performance through access to financing, access to government project, access in the legal aspect and others (see paper of Nys, Tarazi, & Trinugroho (2015) for the details). However, some also contend that the positive impact is only in the short period, in the long-term political relatedness will decrease performance. Even, some others reveal that the effect in the short term is negative which may be caused by the fact that dependency on political relatedness is susceptible. Therefore, in this particular causality, the impact of publicness level of firms on their performance could be positive or negative.

Second, going deeper, I argue that there is an interaction between publicness and ownership structure in affecting the firm performance. It could be hypothesized that the effect of publiness on firm performance is different across ownership structure. In here, ownership structure which is disentangled into 2 categories. The first one is ownership structure based on type of ownership which could be state-owned firms, foreign-controlled firms and private-domestic firms. The second one is ownership structure based on the fraction of ownership which could be measured by the difference between control right and cash flow right for each firm according to those working on the agency conflict between majority and minority shareholders (e.g. Bae, Kang, & Kim, 2002; Baek, Kang, & Lee, 2006). It could be argued that the expected signs of the moderating effect different across the type and structure. For example, the effect of publicness on firm performance may not be significant for state-owned firms. However, the effect may be significant for foreign firms. It is in line with the previous study of Sutopo, Trinugroho, & Damayanti (2017) in which the effect of political connections on bank performance is more pronounced for foreign-controlled banks.

While to test the proposed model on the contingency effect of ownership structure in the relation between publicness level of firm and firm performance, the empirical model to be estimated is as follows:

Firm Performance = f (Publicness, ownership, publicness*ownership, control variables)

CONCLUSION

In this present paper, I discuss deeply on the publicness of firms. I start with the definition that publicness is the extent to which the organization is influenced by political power. Further, I combine the concept of publicness in the management perspective, agency theory of ownership structure, and the political relatedness that has been widely discussed in finance and economics.

Moreover, I introduce some potential measures of publicness level of firms which closes to the measure of political relatedness. Following the introduction of the new publicness measures, I propose some 2 hypotheses in the impact of publicness level of firms on their performance. There are 2 competing hypotheses in this particular relationship. On the one hand, it could be argued that the higher the publicness level of firms, it could help them to improve performance. On the other hand, however, some argue that dependency on the help of political authority could create poor performance due to the expropriation of politicians and susceptible to political turnover. I also propose an empirical model when ownership structure is included as a moderating factor. Arguably, the moderating effect of ownership is different across type and structure.

Discussing the publicness and political relatedness of firms is practically important especially in emerging countries more particular with regard to 2 aspects especially when the new measures of publicness is considered. First, the limitation on politicians having ownership in firms may be considered to be regulated to minimize the grabbing hand behaviors in which they exploit state-owned firms for the benefits of their own firms. Second, as it is argued that the proportion of deposits of governmental institutions in a bank could be a proxy of publicness level of a bank, imposing government budget, and funds of state-owned enterprises to be placed in the state-owned banks may discourage banking competition. However, there may be an internal regulation among governmental agencies to limit their deposits in private banks.

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