# Europe Ownership Change on Firm Performance

#### **Why Foreign Investors Experience Productivity Growth**

Mārtiņš Lindemanis, Artūrs Loze, Anete Pajuste, The effect of domestic to foreign ownership change on firm performance in Europe, International Review of Financial Analysis, Volume 81, 2022, 101341, ISSN 1057-5219, <https://doi.org/10.1016/j.irfa.2019.04.004>.

Despite the theoretical rationale for positive foreign direct investment [spillovers](https://www.sciencedirect.com/topics/economics-econometrics-and-finance/spillover-effect) into the host country's economy, empirical studies show inconsistent evidence of the relationship between foreign investment and firm productivity and growth (see the review by [Bruno & Cipollina, 2018](https://www.sciencedirect.com/science/article/pii/S1057521918302217?casa_token=QBTvT7NcnncAAAAA:h5JsR1KdoFs9j-WixNfRN-gQGVwCUWO2b7e6V4CWraXNob-qMUk1HYQTFzidqH-0S7qGoVbh_Q" \l "bb0050)). One reason for this inconclusive evidence is that the results depend on the relative standing of the acquirer and target countries. For example, [Hymer (1970)](https://www.sciencedirect.com/science/article/pii/S1057521918302217?casa_token=QBTvT7NcnncAAAAA:h5JsR1KdoFs9j-WixNfRN-gQGVwCUWO2b7e6V4CWraXNob-qMUk1HYQTFzidqH-0S7qGoVbh_Q" \l "bb0185) suggests that large foreign acquirers may capitalize on targets' lack of capability and exploit their bargaining power vis-à-vis governments and targets in less developed countries. Similarly, foreign production might depend on the specific attractions of a firm's home country relative to those of a foreign market ([Dunning, 1980](https://www.sciencedirect.com/science/article/pii/S1057521918302217?casa_token=QBTvT7NcnncAAAAA:h5JsR1KdoFs9j-WixNfRN-gQGVwCUWO2b7e6V4CWraXNob-qMUk1HYQTFzidqH-0S7qGoVbh_Q" \l "bb0110); [Fayerweather, 1982](https://www.sciencedirect.com/science/article/pii/S1057521918302217?casa_token=QBTvT7NcnncAAAAA:h5JsR1KdoFs9j-WixNfRN-gQGVwCUWO2b7e6V4CWraXNob-qMUk1HYQTFzidqH-0S7qGoVbh_Q" \l "bb0125)), or foreign investment may be part of the company's vertical integration strategy ([Buckley, 1988](https://www.sciencedirect.com/science/article/pii/S1057521918302217?casa_token=QBTvT7NcnncAAAAA:h5JsR1KdoFs9j-WixNfRN-gQGVwCUWO2b7e6V4CWraXNob-qMUk1HYQTFzidqH-0S7qGoVbh_Q" \l "bb0060); [Buckley & Casson, 1976](https://www.sciencedirect.com/science/article/pii/S1057521918302217?casa_token=QBTvT7NcnncAAAAA:h5JsR1KdoFs9j-WixNfRN-gQGVwCUWO2b7e6V4CWraXNob-qMUk1HYQTFzidqH-0S7qGoVbh_Q" \l "bb0065)). Finally, most previous empirical studies differentiate between foreign and domestic acquirers as a group, while more recent literature reveals that foreign acquirers are not homogeneous and their origin does matter for firm performance (e.g., [Bris & Cabolis, 2008](https://www.sciencedirect.com/science/article/pii/S1057521918302217?casa_token=QBTvT7NcnncAAAAA:h5JsR1KdoFs9j-WixNfRN-gQGVwCUWO2b7e6V4CWraXNob-qMUk1HYQTFzidqH-0S7qGoVbh_Q" \l "bb0045); [Chen, 2011](https://www.sciencedirect.com/science/article/pii/S1057521918302217?casa_token=QBTvT7NcnncAAAAA:h5JsR1KdoFs9j-WixNfRN-gQGVwCUWO2b7e6V4CWraXNob-qMUk1HYQTFzidqH-0S7qGoVbh_Q" \l "bb0090)).

#### Higher Level of Governance of the Investor Home Country Increases Firm Productivity

Mārtiņš Lindemanis, Artūrs Loze, Anete Pajuste, The effect of domestic to foreign ownership change on firm performance in Europe, International Review of Financial Analysis, Volume 81, 2022, 101341, ISSN 1057-5219, <https://doi.org/10.1016/j.irfa.2019.04.004>.

In this paper, we concur with the view that foreign acquirers differ in their impact on the target firm's performance. In particular, we argue that acquirers from countries with a higher governance level are more likely to improve the target firm's long-term performance. To examine this relationship, we investigate the effect of ownership change from domestic to foreign on company performance in the European Union (EU) during the years 2008–2014. We start with a panel of 129,511 private companies.[1](https://www.sciencedirect.com/science/article/pii/S1057521918302217?casa_token=QBTvT7NcnncAAAAA:h5JsR1KdoFs9j-WixNfRN-gQGVwCUWO2b7e6V4CWraXNob-qMUk1HYQTFzidqH-0S7qGoVbh_Q" \l "fn0005) To isolate the effect of ownership change, using the [propensity score matching](https://www.sciencedirect.com/topics/economics-econometrics-and-finance/propensity-score-matching) method, we match companies that change ownership with those that remain domestic throughout the sample period. At the first stage, we estimate a [probit model](https://www.sciencedirect.com/topics/economics-econometrics-and-finance/probit-model" \o "Learn more about probit model from ScienceDirect's AI-generated Topic Pages) and find the determinants of ownership change. Empirically, the results show that ownership change from domestic to foreign is more likely in larger (by revenues) and less profitable (by return on assets) firms, which is consistent with the managerial discipline hypothesis. In the second step, we compute the propensity score of ownership change for each company and then match firms on this score, separately for each year, country and industry, using the nearest neighbour match without replacement. The matching procedure produces a sample of 850 firms with an ownership change and an equal number of firms that remain domestically owned. Finally, we run cross-sectional regressions on the performance variables of our interest, namely, return on assets, profit margin, sales per employee, and others.

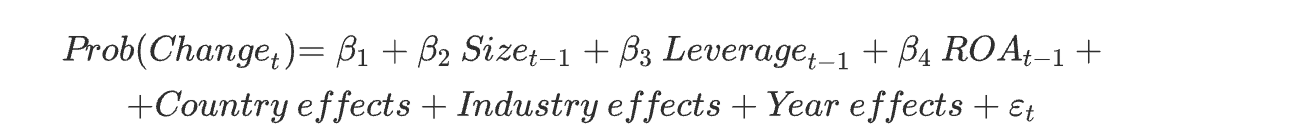
#### Few Papers Looking at Ownership Changes

Mārtiņš Lindemanis, Artūrs Loze, Anete Pajuste, The effect of domestic to foreign ownership change on firm performance in Europe, International Review of Financial Analysis, Volume 81, 2022, 101341, ISSN 1057-5219, <https://doi.org/10.1016/j.irfa.2019.04.004>.

Our paper relates to several strands of literature. First, although there are numerous empirical studies on performance comparison of foreign-owned and domestic-owned companies ([Gelübcke Wecke, 2013a](https://www.sciencedirect.com/science/article/pii/S1057521918302217?casa_token=QBTvT7NcnncAAAAA:h5JsR1KdoFs9j-WixNfRN-gQGVwCUWO2b7e6V4CWraXNob-qMUk1HYQTFzidqH-0S7qGoVbh_Q" \l "bb0140)), research on the impact of ownership change from domestic to foreign on company performance is scarce (see [Jurajda and Stancik (2012)](https://www.sciencedirect.com/science/article/pii/S1057521918302217?casa_token=QBTvT7NcnncAAAAA:h5JsR1KdoFs9j-WixNfRN-gQGVwCUWO2b7e6V4CWraXNob-qMUk1HYQTFzidqH-0S7qGoVbh_Q" \l "bb0205) for the Czech Republic and [Fukao, Ito, Kwon, and Takizawa (2008)](https://www.sciencedirect.com/science/article/pii/S1057521918302217?casa_token=QBTvT7NcnncAAAAA:h5JsR1KdoFs9j-WixNfRN-gQGVwCUWO2b7e6V4CWraXNob-qMUk1HYQTFzidqH-0S7qGoVbh_Q" \l "bb0135) for Japan). We fill this gap by presenting the first cross-country evidence, using a comprehensive secondary dataset on ownership changes instead of self-reported company surveys. Second, by examining the characteristics of acquired firms, we extend the literature on the “cherry picking” ([Bandick & Karpaty, 2011](https://www.sciencedirect.com/science/article/pii/S1057521918302217?casa_token=QBTvT7NcnncAAAAA:h5JsR1KdoFs9j-WixNfRN-gQGVwCUWO2b7e6V4CWraXNob-qMUk1HYQTFzidqH-0S7qGoVbh_Q" \l "bb0030); [Guadalupe, Kuzmina, & Thomas, 2012](https://www.sciencedirect.com/science/article/pii/S1057521918302217?casa_token=QBTvT7NcnncAAAAA:h5JsR1KdoFs9j-WixNfRN-gQGVwCUWO2b7e6V4CWraXNob-qMUk1HYQTFzidqH-0S7qGoVbh_Q" \l "bb0155); [Paprzycki & Fukao, 2008](https://www.sciencedirect.com/science/article/pii/S1057521918302217?casa_token=QBTvT7NcnncAAAAA:h5JsR1KdoFs9j-WixNfRN-gQGVwCUWO2b7e6V4CWraXNob-qMUk1HYQTFzidqH-0S7qGoVbh_Q" \l "bb0270)) and “managerial discipline” theories ([Lichtenberg & Siegel, 1987](https://www.sciencedirect.com/science/article/pii/S1057521918302217?casa_token=QBTvT7NcnncAAAAA:h5JsR1KdoFs9j-WixNfRN-gQGVwCUWO2b7e6V4CWraXNob-qMUk1HYQTFzidqH-0S7qGoVbh_Q" \l "bb0235)). Although the basic idea of managerial discipline dates back to [Berle and Means (1968)](https://www.sciencedirect.com/science/article/pii/S1057521918302217?casa_token=QBTvT7NcnncAAAAA:h5JsR1KdoFs9j-WixNfRN-gQGVwCUWO2b7e6V4CWraXNob-qMUk1HYQTFzidqH-0S7qGoVbh_Q" \l "bb0035) and seems to apply only to publicly traded targets, we contribute by providing evidence from private (unlisted) firms. Third, our paper contributes to the literature by documenting that the origin of the acquirer matters for firm performance ([Bris & Cabolis, 2008](https://www.sciencedirect.com/science/article/pii/S1057521918302217?casa_token=QBTvT7NcnncAAAAA:h5JsR1KdoFs9j-WixNfRN-gQGVwCUWO2b7e6V4CWraXNob-qMUk1HYQTFzidqH-0S7qGoVbh_Q#bb0045); [Chen, 2011](https://www.sciencedirect.com/science/article/pii/S1057521918302217?casa_token=QBTvT7NcnncAAAAA:h5JsR1KdoFs9j-WixNfRN-gQGVwCUWO2b7e6V4CWraXNob-qMUk1HYQTFzidqH-0S7qGoVbh_Q#bb0090); [Girma & Görg, 2007](https://www.sciencedirect.com/science/article/pii/S1057521918302217?casa_token=QBTvT7NcnncAAAAA:h5JsR1KdoFs9j-WixNfRN-gQGVwCUWO2b7e6V4CWraXNob-qMUk1HYQTFzidqH-0S7qGoVbh_Q" \l "bb0150); [Javorcik & Spatareanu, 2011](https://www.sciencedirect.com/science/article/pii/S1057521918302217?casa_token=QBTvT7NcnncAAAAA:h5JsR1KdoFs9j-WixNfRN-gQGVwCUWO2b7e6V4CWraXNob-qMUk1HYQTFzidqH-0S7qGoVbh_Q" \l "bb0195)). Finally, by examining the corporate risk-taking of acquired firms, we add to the literature that suggests risk choices are affected by the identity of the firm's shareholders ([Boubakri, Cosset, & Saffar, 2013](https://www.sciencedirect.com/science/article/pii/S1057521918302217?casa_token=QBTvT7NcnncAAAAA:h5JsR1KdoFs9j-WixNfRN-gQGVwCUWO2b7e6V4CWraXNob-qMUk1HYQTFzidqH-0S7qGoVbh_Q" \l "bb0040); [Faccio, Marchica, & Mura, 2011](https://www.sciencedirect.com/science/article/pii/S1057521918302217?casa_token=QBTvT7NcnncAAAAA:h5JsR1KdoFs9j-WixNfRN-gQGVwCUWO2b7e6V4CWraXNob-qMUk1HYQTFzidqH-0S7qGoVbh_Q" \l "bb0120); [Wang & Wang, 2015](https://www.sciencedirect.com/science/article/pii/S1057521918302217?casa_token=QBTvT7NcnncAAAAA:h5JsR1KdoFs9j-WixNfRN-gQGVwCUWO2b7e6V4CWraXNob-qMUk1HYQTFzidqH-0S7qGoVbh_Q" \l "bb0295)).

#### Run Regression to Find Likelihood of Ownership Change then Propensity Score Matching

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The total number of firms with an ownership change is 1409, and the matching procedure produces a sample of 850 firms with an ownership change (treatment group) and an equal number of firms that remained domestically owned (control group). [Table 1](https://www.sciencedirect.com/science/article/pii/S1057521918302217?casa_token=QBTvT7NcnncAAAAA:h5JsR1KdoFs9j-WixNfRN-gQGVwCUWO2b7e6V4CWraXNob-qMUk1HYQTFzidqH-0S7qGoVbh_Q" \l "t0005) shows the description of firm sample by country and year. The sample shrinks considerably after matching because of the strict one-to-one matching requirement at the country, year and industry group level. The [descriptive statistics](https://www.sciencedirect.com/topics/economics-econometrics-and-finance/descriptive-statistics) and correlations of the financial variables in the matched sample are shown in [Table 2](https://www.sciencedirect.com/science/article/pii/S1057521918302217?casa_token=QBTvT7NcnncAAAAA:h5JsR1KdoFs9j-WixNfRN-gQGVwCUWO2b7e6V4CWraXNob-qMUk1HYQTFzidqH-0S7qGoVbh_Q" \l "t0010).

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# Endogeneity

#### Is Ownership endogenous to firm performace

Harold Demsetz, Belén Villalonga, Ownership structure and corporate performance, Journal of Corporate Finance, Volume 7, Issue 3, 2001, Pages 209-233,

As argued by [Demsetz (1983)](https://www.sciencedirect.com/science/article/pii/S0929119901000207" \l "BIB4) and shown by [Demsetz and Lehn (1985)](https://www.sciencedirect.com/science/article/pii/S0929119901000207" \l "BIB6) and some of the subsequent studies, ownership structure is endogenous. Persistent diffuseness of a firm's ownership structure plausibly serves the firm's shareholders better than would a concentrated ownership structure, even if more diffuseness of ownership does allow professional management to divert more of the firm's resources to serve its own narrow interests. We have no doubt that management is self-serving to the degree that imperfect monitoring allows it to be, but this is largely irrelevant. Owners of a corporation would like all inputs to come without problems and, if possible, without cost. The central issue is whether professional management and diffuse ownership structure bring special advantages to firms that are sufficient to offset the special disadvantages they may also bring. If there are compensating advantages, there should be no systematic relation between managerial shareholdings and firm performance. If the advantages are not fully compensating, there should be a systematic relation, but then there arises a question: Why do diffuse ownership structures survive? There are costs to changing a non-optimal ownership structure, but these are not likely to insulate a clearly improper structure over periods as long as many diffuse ownership structures persist.

The finding that ownership structure is endogenous and plausibly determined, among other factors, by firm performance itself, implies that this endogeneity must be taken into account when seeking to ascertain the relation between ownership and performance. Failing to do so is bound to yield biased regression estimates. The Demsetz and Lehn study, which takes as its primary task the investigation of how ownership structure responds to aspects of the firm and of its environment, necessarily treats ownership structure as endogenous to determine whether it affects firm performance. Their two-stage least squares regression shows that ownership fails to explain variations in firm performance.[5](https://www.sciencedirect.com/science/article/pii/S0929119901000207" \l "FN5) Those of the follow-on studies referred to in [Appendix A](https://www.sciencedirect.com/science/article/pii/S0929119901000207" \l "APP1) that treat ownership as endogenous in one way or another arrive at a similar conclusion [Hermalin and Weisbach, 1988](https://www.sciencedirect.com/science/article/pii/S0929119901000207" \l "BIB7), [Loderer and Martin, 1997](https://www.sciencedirect.com/science/article/pii/S0929119901000207" \l "BIB10), [Cho, 1998](https://www.sciencedirect.com/science/article/pii/S0929119901000207" \l "BIB2). On the other hand, [Morck et al. (1988)](https://www.sciencedirect.com/science/article/pii/S0929119901000207" \l "BIB12) and other studies fail to account for the endogeneity of ownership structure. These are the studies that have yielded “evidence” of a statistically significant effect of ownership structure on performance.

Thus, we have follow-on studies that do not treat managerial holdings as endogenous, and studies that do treat it as such but take no note of shareholdings by investors who are not part of the firm's management. To our knowledge, no study has both treated the endogeneity issue with the fullness that it deserves and, at the same time, examined the roles played by different types of shareholders. The restudy of the ownership and control problem described in the following sections does both.

# Agency Theory

#### Mangers are Agents of Owners

Ujunwa, A., Okoyeuzu, C., & Nwakoby, I. (2012). Corporate board diversity and firm performance: Evidence from Nigeria. Revista de Management Comparat International, 13(4), 605.

Corporate governance research has been influenced mainly by agency theory. Agency theory is based on the fact that many corporate managers are not owners but agents of owners, contracted to manage the company on their behalf. Since they are not direct owners but managers, and thus have less personal wealth at stake, their natural pursuit of self-interest could result in their taking riskier or even dishonest actions, which could bring harm to the firm or its owners (Jensen and Meckling, 1976). Agency problem arises whenever managers have incentives to pursue their own interest (self-serving behaviour) at the expense of shareholders. Most studies on corporate governance focus on how to effectively monitor the agents (resolving the conflict) against narcissistic behaviour in order to protect shareholders‘ interest.

#### Averse Selection and Moral Hazard

Ujunwa, A., Okoyeuzu, C., & Nwakoby, I. (2012). Corporate board diversity and firm performance: Evidence from Nigeria. Revista de Management Comparat International, 13(4), 605.

Agency theory argues that where there is separation of management and ownership, the manager seeks to act in self interest which is not always in the best interests of the owner and departs from those required to maximise the shareholder‘s returns. This agency problem can take two different forms such as adverse selection and moral hazard (Eisenhardt, 1989). Adverse selection can occur if the agent misrepresents his ability to perform the functions assigned and gets chosen as an agent. Moral hazard occurs if the chosen agent shirks the responsibilities or underperforms due to lack of sufficient dedication to the assigned duties. Such under-performance by an agent, even if acting in the best interest of the principal, will lead to a residual cost to the principal (Jensen and Meckling, 1976). These costs, resulting from sub-optimal performance by agents, are termed agency costs.

# Enthnicity, Sex, Minority, or …

#### Differentiation Between Firms owned by Different Sexes

Coleman, S. (2005). The impact of human capital measures on firm performance: A comparison by gender, race and ethnicity. The Journal of Entrepreneurial Finance, 10(2), 38-56.

An important consideration relating to small firms is their ability to generate jobs that would benefit the economy. These findings reveal there were almost no significant differences between firms owned by white men and those owned by women and minorities in terms of their willingness and ability to generate jobs when we control for industry sector, human capital, and firm size. The only firms that had a significantly smaller number of total employees were those owned by Asian men. These results also indicate that women- and minority-owned firms were no less profitable than firms owned by white men. In fact, firms owned by white women and black women were significantly more profitable than firms owned by white men. Similarly, there were no significant differences in the year to year growth rate in sales aside from the fact that firms owned by white women had a significantly higher growth rate than firms owned by white men, while firms owned by Asian men were significantly less likely to grow at all. In summary, these findings indicate that, when we control for industry sector and human capital, most of the supposed performance differences between women- and minority owned firms disappear. It does seem that firms owned by white women and black men and women are still somewhat smaller than firms owned by white men, but aside from that, women- and minority-owned firms are no less profitable nor less likely to grow. Overall, these findings seem to suggest that firm performance is heavily influenced by industry selection (and with it firm size) and by the firm owner’s level of human capital. These results are significant, because they highlight the importance of preparation and planning well in advance of business ownership. They suggest the desirability of having potential entrepreneurs weigh the relative attractiveness of various industries and businesses in order to select a business that will provide opportunities for profitability and growth. Further, these results highlight the importance of the entrepreneur’s personal qualifications, or the human capital attributes that help to prepare him for success in that business. Finally, these findings suggest that if we can find ways to help women- and minority entrepreneurs make good choices about the businesses they start, and if we can help them to acquire human capital in the form of education and relevant experience, we can increase their chances for success.

# Institutional Ownership and Firm Performance

#### Institutional Investors Control A Lot of Companies

Charfeddine, L., & Elmarzougui, A. (2010). Institutional ownership and firm performance: Evidence from France. IUP Journal of Behavioral Finance, 7(4), 35.

Institutional investors have become important players in today’s financial markets. Their increasing importance in corporate governance is observed from the growing volume of corporate equity they control. In the US, for example, institutional investors were estimated to control 60% of all outstanding equity in 2003 (Hayashi, 2003), compared to 45% in 1990, 33% in 1980 and 8% in 1950 (Taylor, 1990). The observed increase in Institutional Ownership (IO) in the equity market has been attributed to the growth in pension funds (Graves and Waddock, 1990). Accompanying the growing volume of institutional shareholdings in the equity market, the role of institutional investors has changed dramatically from that of simply passive investors to active monitors.

#### How They Treated Them Indogneitiously

Charfeddine, L., & Elmarzougui, A. (2010). Institutional ownership and firm performance: Evidence from France. IUP Journal of Behavioral Finance, 7(4), 35.

Charfeddine, L., & Elmarzougui, A. (2010). Institutional ownership and firm performance: Evidence from France. IUP Journal of Behavioral Finance, 7(4), 35.

We suspect that the way many previous studies have treated the ownership structure variable in the model testing, the relationship between ownership and performance leads to the mixed results of the empirical literature. Demsetz (1983) first argued that the ownership structure of a firm is an endogenous outcome of competitive selection within the firm leading to the maximization of firm value. Demsetz (1983) suggested that considering the endogeneity of the ownership variable in the model means that the optimal ownership structure in the firm is the consequence of how the firm operates its activities. Demsetz’s (1983) view on ownership endogeneity is partially challenged by Agrawal and Knoeber (1996) who suggested that institutional shareholding decisions are not necessarily dependent on firm value maximization. This implies that a systematic institutional ownership/firm performance relationship may exist. In an endogenous framework and due to some specific factors to the firm, the relationship between IO and firm performance must be studied in the two directions in order to take endogeneity into account and hence obtain consistent empirical results. So, our empirical methodology is based on a simultaneous equations model consisting of Equations (1) and (2):

#### 2SLS Technique—there is no way this is a good way to go about it

Charfeddine, L., & Elmarzougui, A. (2010). Institutional ownership and firm performance: Evidence from France. IUP Journal of Behavioral Finance, 7(4), 35.

where Q is the Tobin’s Q, INST is the percentage of outstanding shares held by institutions, SIZE is the log of total assets, DEBT is the book value of debt as a fraction of the book value of total assets, FIX is the expenditures on fixed plant and equipment as a fraction of sales revenues, ROA is the net income divided by total assets, BETA the systematic risk, DIV the dividend payout ratio, α0 is the constant, α1, α2, α3, α4, α5, α6 are the coefficients, and ε 1 and ε 2 the error terms. The independent variables in Equation (2) not only act as potential determinants of IO, but, more importantly, some of them (ROA, BETA and DEBT) play the role of instrumental variables for INST in the first stage of the 2SLS technique if 2SLS is adopted.

# Paper Meetings With Professor Notes

-Dummy Variable Majority Ownership, Chinese Firms F test with Western Firms to get the effect of , firm country year fe

-Quadratic Firms find the right cutoff value with numeric

-why is there specific endogeneity problems that exist. At investor for firm and other one

Shift share or bar take instrument—global outflows of capital occur when home countries outflow is greater than global means interest rate. May not be enough variation, but this is the basis for SLS

Table 1

Threshold shares in column 5 10 15 20

Separate regression for investor country row

Colonial have long standing not changed much

Describe number of switching thresholds, how firms

how looks like china and who

table 2

counting the number of firms where you are above that threshold ever and number of threshold and have ownership

Indian and Saudi Arabia

Auffray, C., & Fu, X. (2015). Chinese MNEs and managerial knowledge transfer in Africa: the case of the construction sector in Ghana. *Journal of Chinese Economic and Business Studies*, *13*(4), 285-310.

https://www.aicpa.org/news/article/what-is-a-private-company-audit#:~:text=By%20law%2C%20the%20annual%20financial,each%20year%20by%20independent%20auditors.