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Global Carriers' Governance and Business Scope*

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ABSTRACT

Recent structural changes to the shipping industry triggered severe liquidity risks for not only small and medium-sized shipping lines but also global lines. Despite a severe downturn in the industry, a few lines have shown stable performance their finances. This study thus raises two research questions. Why do a few shipping lines maintain stable financial performance (FP)? How much does the governance feature (GVF) and the business scope (BSC) influence FP? To answer these questions, this research uses regression analysis (RA) to verify the relationships among the variables, GVF, BSC, and FP. The result of the RA showed a positive relationship between BSC and FP, but slight relationship between BSC and GVF and between knowledge and FP.

1. Introduction

Because of the global financial tsunami in 2008, the Baltic Dry Index (BDI) fell quickly 4,492P to 1,549P within two years. Most shipping lines, such as CMA CGM, APL, COSCON, Hyundai Merchant Marine (HMM), and Hanjin Shipping (HJS), underwent a liquidity crisis. In these circumstances, some carriers merged in order to realize economies of scale. Three alliances occurred worldwide. Securing shipping economies of scale became important, and then the shipping industry was stabilized because of mergers and acquisitions (M&A) and mega alliances between shipping lines.

The shipping industry is also called the cycle industry because several strategic choices cannot be made by individual companies. Comparisons of the sales trends of major liner companies do not show many differences. However, in recent years, this situation has changed dramatically.

Despite the severe downturn in the shipping market, a few liners, such as the Maersk-Line, have continued to make large profits, but most lines have faced severe liquidity risks. In the case of Maersk, Arnold Peter Moller Maersk founded the line. His great-grandson has been taking a course in management. Today Maersk has five unique core values: constant care, humbleness, uprightness, the staff, and the name, which have continuously shown considerable social as well as financial

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performance (FP). In addition, the Maersk-Line has a more flexible and solid decision-making mechanism than other lines have. The mechanism has three stages. The top-priority executive group consists of the only share-holders, who are related to the founding family and possess about 40% of whole group's stocks. The second group is constituted by the board of directors, which consists of 12 directors including two founding family members. The last group is executive board. They directly manage each company and have to submit annual investment plans to the second group.

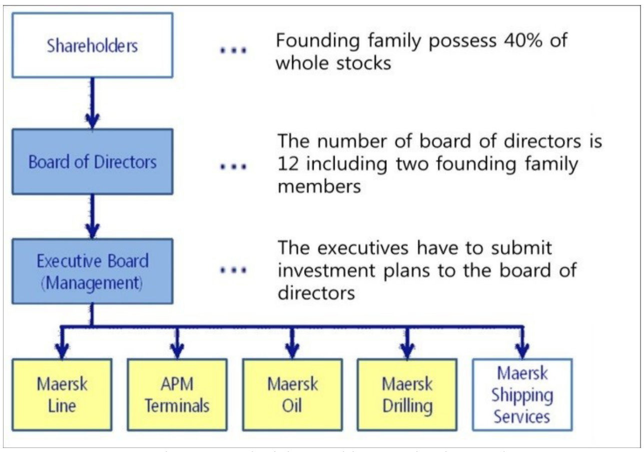

Fig. 1. Maersk group's decision making mechanism and structure

Source: European Global Top carriers' Competitive Strategy published by MIZUHO (2016) in Japanese

In addition, some mega carriers, Mediterranean Shipping Company (MSC), CMA CGM, Evergreen line are family business. Some carriers employ a chief executive officer (CEO), and a few lines are state-owned enterprises.

This study thus raises the following research questions. Why do some shipping lines a make a stable profit? How much dose governance feature (GVF) and the business scope (BSC) influence profit? Which business strategy is more useful: specialization or diversification?

To answer these questions, this research uses regression analysis (RA) to shed light on the relationships among several variables: GVF, BSC, and profit.

Similarly studies have conducted on shipping and another industries (Lee and Moon, 2016; Syriopoulos and Tsatsaronis, 2012; Koufopoulos et al., 2010). Previous studies provided a main idea and substantial knowledge, such as the relationship between the CEO's demographics and FP (Lee and Moon, 2016; Syriopoulos and Tsatsaronis, 2012) and the relationship between the governance and performance of shipping lines (Koufopoulos et al., 2010). To date, the relationships between GVF, BSC, and FP from the perspective of global shipping lines is still an under-researched area in the discipline.

The remainder of this paper is organized in four sections. Section 2 reviews previous studies and states hypotheses. Section 3 presents the data analysis and discusses results. Section 4 concludes the paper with suggestions for future research directions.

2. Literature Review and hypotheses

In the business discipline, there are two compulsory theories of corporate governance. First, the upper echelon theory (UET) supports specialized manager's governance. Second, agency theory (AT) shows the risks in business delegation. In this section, we review the two conflicting theories and then state the hypothesis.

2.1. *Upper echelon theory*

In a strategic business discipline, the UET has a perspective that differs from that in industrial organizations, resource-based views, and population ecology (Hambrick and Mason, 1984). According to the UET, business is a reflection of CEO's features and philosophy. That is why CEO decides business policy using his or her value, belief, cognitive pattern, education, and other demographics (Finkelstein and Hambrick, 1996). UET's core understanding is that the top manager makes decisions under bounded rationality (Lee and Moon, 2016). In other words, the enterprise does not choose an optimal decision maker based on rationality. Instead, the company makes acceptable decisions about business issues under bounded rationality (March and Simon, 1993; Simon, 1997). The concept of UET has been used as core knowledge in several studies (Matta and Beamish, 2008; Yunlu and Murphy, 2012; Colombelli, 2015). Most previous studies bsed on the concept of UET used observable variables, such as age (Colombelli, 2015), tenure (Chen, 2013), and level of education (Damanour and Schneider, 2006).

2.2. *Agency theory*

Agency theory (AT) concerns the business environment. Both the imbalance of information and the incompleteness of observations between principals and agents could affect many problems, such as moral hazard, adverse selection, and so on (Jensen and Meckling, 1976). According to the theory, the principal gives his or her authority to the agent to control the company. The agent then has more information and authority than the principal has (Fama, 1980; Bebchuk and Fried, 2003). In addition, the agent hides information from the principal in order to gain wealth (Jensen, 1986; Braun and Guston, 2003). This case is understood as moral hazard (Laffont and Martimort, 2009). Thus, the principal arranges an excessive monitoring system, which destroys the value of firm (Jacobides and Croson, 2001).

2.3. *Hypotheses*

Lee and Moon (2016) empirically analyzed the relationships of the CEO of several airlines to strategic risk taking (SRT) and their demographics. The results showed that both employment status and education had a positive relationship with the CEO's SRT. Koufopoulos et al. (2010) revealed the traits of Greek shipping companies. The family-owned companies are heavily self-controlled and have strong internal integration and a corporate culture. Because most Greek shipping companies are small and medium-sized, they show a substantial FP. In their empirical study, Syriopoulos and Tsatsaronis (2012) found that the CEO's governance was strongly related to FP. These previous studies showed that governance structure is substantially related to FP. Therefore, the following hypothesis is stated:

H_1. The GVF of global carriers positively affects their FP.

Thomas (2006) identified a u-shaped curve linear in the linear relationship of international business diversification and a firm's FP. In particular, Mexican corporations rarely experienced plentiful FP. The corporation had to overcome a great deal of business risk through paying learning costs. Palich et al.'s (2000) empirical study found that a medium