Journal of Comparative Economics 41 (2013) 265–278

Contents lists available at SciVerse ScienceDirect

Journal of Comparative Economics

journal homepage: www.elsevier.com/locate/jce

Investment behavior and ownership structures in Ukraine: Soft budget constraints, government ownership and private benefits of control

Dariya Mykhayliv [a,1], Klaus G. Zauner [b,*]

[a] Leeds University Business School, Maurice Keyworth Building, University of Leeds, Leeds LS2 9JT, United Kingdom
[b] Social Sciences Building D312, City University London, Northampton Square, London EC1V 0HB, United Kingdom

A R T I C L E   I N F O

Article history:
Received 1 March 2011
Revised 28 February 2012
Available online 21 March 2012

JEL codes:
D92
G31
L 33
P31

Keywords:
Corporate governance
Financial constraints
Investment
Private benefits of control
Ownership

A B S T R A C T

Mykhayliv, Dariya, and Zauner, Klaus G.—Investment behavior and ownership structures in Ukraine: Soft budget constraints, government ownership and private benefits of control

This paper analyzes the relationship between investment behavior of firms and ownership and corporate governance variables for a sample of large Ukrainian firms 2003–2007. The paper sheds light on the role of the ownership structures of firms and its effect on investment behavior via the presence of private benefits of control, financial and soft budget constraints. We find a negative impact of government ownership on investment and evidence for soft budget constraints. Foreign ownership is associated with financial constraints. Firms with management ownership do not appear to suffer from financial constraints. These and other findings demonstrate a significant role for private benefits of control consistent with the presented investment model that allows for private benefits of control and financial and soft budget constraints. *Journal of Comparative Economics* **41** (1) (2013) 265–278. Leeds University Business School, Maurice Keyworth Building, University of Leeds, Leeds LS2 9JT, United Kingdom; Social Sciences Building D312, City University London, Northampton Square, London EC1V 0HB, United Kingdom.
© 2012 Association for Comparative Economic Studies Published by Elsevier Inc. All rights reserved.

1. Introduction

Recent theoretical and empirical research indicates that corporate governance and ownership variables have an important influence on the performance and investment behavior of firms (Shleifer and Vishny, 1997; Gugler, 2003), and, in particular, in transition countries (Brown et al., 2006; Grygorenko and Lutz, 2007; Estrin and Rosevear, 1999a,b). In this paper, we study the impact of ownership and corporate governance variables on investment behavior of large firms in a transitional economy, Ukraine. The question is asked to what extent ownership and corporate governance variables influence investment behavior and firm financing in a sample of large Ukrainian firms over the period 2003–2007. Special consideration is given to indications of the exploitation of ownership, including private benefits and asset stripping, by state or private owners and to questions of financial or soft budget constraints relative to the ownership mix. The ownership and corporate governance variables include government, management, foreign, financial, holding company and financial and industrial group ownership. The governance variables include the presence of a controlling majority and the presence of a blocking minority.

The presented theoretical model (adapted from Mykhayliv and Zauner (2010)) explains investment by marginal Q, financial and soft budget constraints and shares of ownership categories potentially enjoying private benefits of control

* Corresponding author. Fax: +44 (0) 20 7040 8580.
E-mail addresses: bus1d2m@leeds.ac.uk (D. Mykhayliv), klaus.zauner@city.ac.uk (K.G. Zauner).
[1] Fax: +44 (0) 113 343 4465.

0147-5967/$ - see front matter © 2012 Association for Comparative Economic Studies Published by Elsevier Inc. All rights reserved.
http://dx.doi.org/10.1016/j.jce.2012.03.001

(Grossman and Hart, 1988). The empirical specification uses the ratio of investment to fixed assets as the dependent variable and includes the change in Tobin's *Q*, the ratio of market capitalization to the book value of equity, as a proxy for marginal *Q*; cash flow or operating profit as a proxy for the extent of financial or soft budget constraints; and ownership shares of different categories of firms as a proxy for ownership shares of controllers enjoying private benefits as independent variables. The sensitivity of investment with respect to cash flow of the different ownership categories is used as a proxy for financial and soft budget constraints (Fazzari et al., 1988; Lizal and Svejnar, 2002) of that ownership category. Since private benefits of control have to be financed by the firm, the cash flow sensitivities reflect, in addition to the usual financial constraints, the constraints arising from financing of private benefits. Therefore, the ownership variables, as percentages or dummies, measure the impact of private benefits of control, not already captured by the cash flow sensitivity, and present a conservative estimate for the impact of private benefits of control on investment.

The empirical results are as follows. In contrast to other transitional studies, Tobin's *Q* includes information about the profitability of investment since the change in Tobin's *Q*, a proxy for marginal *Q*, is positive and highly significant. Due to private benefits of control, government ownership has a negative impact on investment in contrast to some recent investment studies. Government owned firms also appear to suffer from soft budget constraint. Management owned firms do not face financial constraints but soft budget constraints. There appears to be some evidence for private benefits of managers consistent with the free cash flow theory of Jensen (1986). Ownership by foreigners involves significant financial constraints and private benefits of control and impacts investment negatively. Ownership by financial firms, holding companies and financial and industrial groups (Kostyuk et al., 2004), the presence of a blocking minority or of a controlling majority does not significantly influence investment.

An important reason why the ownership structure of firms matters for firms' investment and, in general, for firms' performance is the presence of private benefits of controllers, tunneling and asset stripping. Private benefits of control (Grossman and Hart, 1988) relate to the benefits of the manager at the expense of the shareholders or to the benefits of the controlling shareholder at the expense of the non-controlling shareholder (Young et al., 2008). Tunneling, "the transfer of assets and profits out of firms for the benefit of those who control them" (Johnson et al., 2000, p. 22), and asset stripping, obtaining firms' assets significantly below market prices (for example, Campos and Giovannoni, 2006) include activities such as self-dealing, theft, fraud, asset sales, transfer pricing, excessive executive compensation, loan guarantees, expropriation, dilutive share issues, minority freeze-outs, insider trading, hidden acquisition of shares, and others can be interpreted as an extreme form of private benefits of control. As emphasized by Jensen (1986), Wu and Wang (2005), Myers and Majluf (1984) and Stulz (1990), private benefits of controllers from undertaking investment projects may have a significant impact on the behavior of firms. In this context it is important to emphasize that asset stripping, related party transactions or share dilutions are not explicitly prohibited by law in Ukraine (Mycyk et al., 2007).

An important question is to what extent soft budget constraints (Kornai et al., 2003) play a role in firms' investment behavior. A firm facing a soft budget constraint lacks financial discipline because of financial injections from the outside. Such financial injections include explicit and implicit financing from the government, tax authorities, suppliers or other entities (Kornai, 1979, 1980; Kornai et al., 2003). We also aim to investigate the impact of government ownership on investment behavior of firms. To understand the role of government ownership in firm's investment behavior it is helpful to take a look at the privatization and restructuring programs (see, for example, Roland, 2000; Roland and Sekkat, 2000) in the Eastern European transitional economies that have been largely motivated by moving ownership structures away from government and towards private ownership: "Rapid privatization early in the transition aimed to get the state out of enterprise management" (World-Bank, 2002, p. 71). In their survey on empirical research on the effects of privatization and private ownership, Megginson and Netter (2001, p. 381), summarize the current state of the literature "We know that privatization "works," in the sense that divested firms almost always become more efficient, more profitable, and financially healthier, and increase their capital investment spending." In their meta-analysis of empirical studies on transitional economies, Djankov and Murrell (2002, p. 751), find positive effects of privatization and private ownership, however, for the Commonwealth of Independent States (CIS) countries, in particular, Ukraine (excluding the Baltic states) the effects of privatization and private ownership are insignificant. The World-Bank (2002, p. 71), relates this partial ineffectiveness of privatization and private ownership in the Commonwealth of Independent States (CIS) countries to "insider ownership and the lack of an appropriate institutional framework like strong mechanisms of corporate governance, including rules to protect minority shareholders; rules against insider deals and conflicts of interest; and adequate accounting, auditing, and disclosure standards; takeover, insolvency, and collateral legislation, as well as strong creditor surveillance by well-run private banks."

The question then arises whether government ownership is detrimental to firms' performance and investment. In the case of Ukraine, studies of the impact of private ownership on firms' performance are inconclusive. Estrin and Rosevear (1999b) and Estrin and Rosevear (1999a) find no significant effect of private ownership on enterprise performance. Grygorenko and Lutz (2007) find that majority government ownership in Ukraine is associated with worse enterprise performance, but an increase in the government ownership stake seems to have beneficial effects on enterprise performance. In two very carefully executed studies, Brown et al. (2006) and Brown and Earle (2007) find substantial effects of privatization on multi-factor productivity that widens with calendar years and years after privatization in transitional countries, in particular, in Ukraine.

Regarding investment and government ownership in the Eastern European transitional context (Lizal and Svejnar, 2002 (Czech Republic); Perotti and Vesnaver, 2004 (Hungary)), there is little empirical evidence that government ownership positively or negatively influences investment.

Download English Version:

https://daneshyari.com/en/article/5092272

Download Persian Version:

https://daneshyari.com/article/5092272

Daneshyari.com