Institutional Investors' Impact on the Performance of Listed Companies in China

Jiaxin Guo

College of Economics, Jinan University, Guangzhou 510000, China

Abstract

This paper empirically studies the impact of institutional investors on performance of listed companies from China's Growth Enterprises Market (GEM). The empirical results show that the shareholding of institutional investors has a significant positive effect on the performance of the company, among which the shareholding of fund companies has the most significant effect. On the other hand, previous literature has pointed out that institutional investors have less effect on improving the performance of state-owned enterprises than private enterprises, however, the empirical results show that this difference is not significant in China's GEM.

Keywords

Growth Enterprises Market (GEM), institutional investors, performance.

1. RESEARCH BACKGROUND

Institutional investors have developed for nearly a century in developed countries such as Britain and the United States. With the continuous development of institutional investors, their influence on the companies being held is increasing. In the United States, for example, after nearly a century of development, institutional investors gradually changed from passive shareholders who merely traded stocks to active shareholders who interfered in corporate decision-making. Compared with western developed countries, China's institutional investors started late, but with the government's policy support, China's stock market institutional investors have developed rapidly and their influence on the companies being held is also expanding. for example, in 2003, when the stock market was in a slump, China Merchants Bank proposed to issue a refinancing proposal of no more than 10 billion yuan of convertible bonds. Within 20 trading days after the announcement, its share price fell by more than 13%, seriously harming the interests of shareholders of tradable shares. This caused strong resistance from institutional shareholders. After a long confrontation, China Merchants Bank finally announced the convertible bond plan in 2004, which made a substantial adjustment in favor of the shareholders of tradable shares.

In 2009, the establishment of China's Growth Enterprises Market (GEM) provided a financing channel for small and medium-sized enterprises that did not meet the conditions for listing on the main board and were in the early stage of growth. As GEM listed companies are less mature than main board listed companies, they have more problems in corporate governance, and institutional investors may have greater influence on their operation. In order to verify this influencing mechanism, this paper empirically examines the impact of institutional investors' shareholding on corporate performance based on data from China's GEM.

2. LITERATURE REVIEW

At present, the research literature on the influence of institutional investors on corporate performance can be roughly divided into three categories, namely, institutional investors have a positive impact on corporate performance, negative impact and insignificant impact.

Among the theories that hold that institutional investors have a positive impact on corporate performance, Shleifer and Vishny (1986) believed that the unit cost of institutional investors with high shareholding ratio to intervene in the management of a company was lower than that of investors with low shareholding ratio, so there was a stronger incentive to supervise and intervene in the company, therefore, the shareholding ratio of institutional investors was positively correlated with the performance of the company [1]. pound (1988) proposed the hypothesis of efficiency supervision, which holds that institutional investors have more professional knowledge, experience and technology than retail investors, so they can supervise companies more effectively and enhance corporate value at a lower cost [2]. Chaganti (1991) conducted an empirical study on 40 data of manufacturing companies from 1983 to 1985, and found that companies with a high institutional shareholding ratio had a lower debt-to-capital ratio than those with a small institutional shareholding ratio, and the return on equity (ROE) of the company was significantly positively correlated with the institutional shareholding ratio [3].Hutchinson et al. (2016) examined the Australian stock market data from 2006 to 2008, and found that the involvement of institutional investors could significantly improve the performance of those companies in financial difficulties (ROA and Tobin Q)[4].

Some scholars believe that the involvement of institutional investors is not conducive to corporate performance. Robert (2003) indicates that the stock held by institutional investors is characterized by high liquidity, which makes institutional investors have a "short-sighted image" of pursuing short-term interests in corporate management, and thus the intervention of institutional investors is not conducive to the long-term development of companies. [5].

In addition to the above two situations, there are studies show that institutional investors have no significant influence on corporate performance. Pound (1988) proposed the conflict of interest hypothesis and the strategic alliance hypothesis. According to the conflict of interest hypothesis, institutional investors may also have agency problems and blindly support managers' plans out of consideration of their own interests due to their interest exchanges with listed companies, thus failing to supervise listed companies effectively. On the other hand, the strategic alliance hypothesis holds that institutional investors and listed companies seek common interests and reach a cooperative relationship, and the supervision and restriction of institutional investment on companies are not effective, which makes it difficult to improve corporate performance [2]. David and Kochhar (1996) believed that the shareholding ratio of a single institution to the company being held was small, the phenomenon of the listed company being dominant and the measures taken by the management to limit the intervention of institutional investors in the company made institutional investors play a limited role. On the other hand, it is difficult for institutional investors to obtain timely information about strategic decisions and changes of the company, thus they cannot effectively intervene in the management of the company[6]. Karpoff et al. (1996) examined the data of 269 American listed companies from 1987 to 1990 that had received shareholder proposals on corporate management, and found that there was no significant relationship between corporate governance proposals put forward by shareholders, including institutional investors, and corporate operating performance, and positive shareholder governance was difficult to have an impact on the company's stock price and changes in senior managers [7].

3. INFLUENCE PATH AND RESEARCH HYPOTHESIS

3.1. Influence Path

There are two ways for institutional investors to influence corporate governance: direct way and indirect way. Among them, the direct way includes the following several kinds, first, Submit a shareholder proposal. Institutional investors participate in the company's business decisions by presenting their concerns to the general meeting of shareholders for discussion. Because of the one-share, one-vote system, the larger the proportion of shares held by institutional investors, the stronger their voting power in the shareholders' meeting, and the more likely their proposals are to pass. Second, Open call for voting rights. Institutional investors may restrict major shareholders and safeguard the interests of small and medium-sized investors by actively soliciting the voting rights of small and medium-sized shareholders on a certain resolution or a number of resolutions of the general meeting. Take joint agency action as an example, the influence of a single investor is limited, but a collection of all institutional investors holding a company's shares can be a greater constraint.

The indirect influence path means that the institutional investors sell the company's stock by "voting with their feet" and the stock price falls, and the negative news conveyed by the stock price falls affects the compensation of the company's managers, thus forcing the managers to improve the management of the company.

3.2. Research Hypothesis

It has been more than 10 years since the establishment of GEM in China. Through continuous development, institutional investors have taken over half of their total shareholding in GEM and become important participants in the market. GEM listed companies are in the early development stage, its corporate governance level is less mature compared with companies listed on the main board market. With the expansion of the shareholding ratio of institutional investors, the unit cost of intervening in corporate governance will be reduced, which encourage institutional investors to intervene in corporate governance, such as restrain the "tunneling" behavior of major shareholders. Based on the above discussion, research hypothesis 1 is proposed as follow.

H_1: The shareholding of institutional investors has a positive impact on the performance of China's GEM listed companies.

As the income of investment funds mainly comes from management fees, and the level of management fees depends on the scale and performance of the fund. Meanwhile, the fund holds the largest proportion of shares in the Chinese market, so the fund companies are more motivated to intervene in the management of the company. Based on the above discussion, research hypothesis 2 is proposed as follow.

H_2: Compared with other types of institutional investors, the effect of fund company shareholding on corporate performance is more significant.

Since state-owned equity participation enterprises, especially state-owned absolute holding enterprises, are often subject to government intervention, the compensation of soe managers is generally restricted by the government. At this time, the forcing mechanism of institutional investors "voting with their feet" is ineffective, and a large number of major decisions of soes need to be reported to the government for approval, so the direct intervention of institutional investors is limited. Based on this, this paper believes that institutional investors have limited influence on the performance of enterprises with a high degree of state-owned equity participation, and puts forward research hypothesis 3.

H_3: Compared with state-owned enterprises, the participation of institutional investors has a more obvious effect on improving the performance of non-state-owned enterprises.

4. DATA AND EMPIRICAL FRAMEWORK

4.1. The Data Source

In this paper, listed companies on China's GEM from 2012 to 2016 are taken as samples and excluded companies with the following characteristics: 1) companies with incomplete data ; 2) A listed company that is PT or ST during the study period

The listed companies that PT or ST are excluded during the investigation period; Excluding financial listed companies. Finally, 342 listed companies were selected from gutai 'an database and Oriental Wealth Choice database for empirical test.

4.2. Variable Setting

Explained variable. Earnings per share (EPS) and return on total assets (ROA) are used as explained variables (corporate performance).

Explanatory variables. Explanatory variables selected in this paper include total shareholding ratio of institutional investors (IR), fund shareholding Ratio (IRfund), Securities broker's shareholding Ratio (IRsec), QFII shareholding Ratio (IRQFII), Social Security Fund shareholding ratio (IRssf), Trust shareholding ratio (IRtrust), Insurance shareholding ratio (IRinsurance), State-owned shareholding ratio (SOH), and the cross multiplier between institutional Shareholding Ratio and State-owned Shareholding Ratio (IR_SOH).

Control variable. The control variables selected in this paper are as follows: Equity concentration (HERF): the squares sum of the shareholding ratios of the top five shareholders, namely Herfindahl coefficient. Financial leverage (LEV): asset-liability ratio. Revenue growth rate (Growth). Company size: Take the logarithm of company size (LnSize).

4.3. Descriptive Statistics

Table 1. Descriptive statistics

	Mean	Median	Max	Min	SD
ROA	0.0474	0.0481	0.297	-0.6464	0.0513
EPS	0.3285	0.2818	2.79	-2.8801	0.3628
ROE	0.0629	0.0651	0.4499	-1.8069	0.1006
IR	0.2162	0.1505	0.8823	0	0.1869
SOH	0.0097	0	0.722	0	0.0518
First	0.3148	0.2952	0.689	0.0438	0.1247
IR_First	0.7792	0.5468	5.6541	0	0.771
IRfund	0.0568	0.0331	0.4316	0	0.0659
IRsec	0.0029	0	0.0599	0	0.0068
IRQFII	0.0007	0	0.0989	0	0.0047
IRssf	0.0047	0	0.0759	0	0.0099
IRtrust	0.0013	0	0.1498	0	0.0077
IRinsurance	0.0005	0	0.043	0	0.0035
HERF	0.1392	0.1155	0.4767	0.00357	0.0847
Growth	0.2704	0.2026	5.8017	-0.91064	0.4771
LnSize	21.20637	21.0901	24.1962	19.2895	0.7343
LEV	0.2714	0.2471	0.886	0.01103	0.162

Table 1 shows the statistical properties of each variable, among which the average shareholding ratio of the largest shareholder exceeds 30%.Although the IR average of the total institutional shareholding ratio reaches 20%, the average shareholding ratio of all types of institutional investors is small, among which the fund with the largest average shareholding

ratio is only less than 6%, indicating that there is a great disparity between the strength of certain institutional investors and major shareholders, and the problem of "single dominant share" of gem enterprises is obvious. In addition, the average proportion of state-owned shares is less than 1%, indicating that the state-owned nature of gem enterprises is not obvious, and most of them are private enterprises.

4.4. Empirical Framework

In order to control the possible endogeneity between institutional shareholding and corporate performance, the regression of explanatory variables and control variables was carried out after one period of lag. In order to verify that the shareholding ratio of institutional investors has a positive impact on the performance of companies listed on GEM (hypothesis 1), the following model is constructed:

$$ROA_{i,t}=\alpha_0+\alpha_1 IR_{i,t-1}+\alpha_2 HERF_{i,t-1}+\alpha_3 LEV_{i,t-1}+\alpha_4 Growth_{i,t-1}+\alpha_5 LnSize_{i,t-1}+\varepsilon_{i,t} \qquad (1)$$

$$EPS_{i,t}=\alpha_0+\alpha_1 IR_{i,t-1}+\alpha_2 HERF_{i,t-1}+\alpha_3 LEV_{i,t-1}+\alpha_4 Growth_{i,t-1}+\alpha_5 LnSize_{i,t-1}+\varepsilon_{i,t} \qquad (2)$$

In order to test whether there are differences in the influence of different types of institutional investors on corporate performance, and whether hypothesis 2 is true, the test model is established as follows:

$$ROA_{i,t}=\alpha_0+\alpha_1 IRfund_{i,t-1}+\alpha_2 IRsec_{i,t-1}+\alpha_3 IRQFII_{i,t-1}+\alpha_4 IRtrust_{i,t-1}+\alpha_5 IRssf_{i,t-1}+\alpha_6 IRinsurance_{i,t-1}+$$
$$\alpha_7 HERF_{i,t-1}+\alpha_8 LEV_{i,t-1}+\alpha_9 Growth_{i,t-1}+\alpha_{10} LnSize_{i,t-1}+\varepsilon_{i,t} \qquad (3)$$

$$EPS_{i,t}=\alpha_0+\alpha_1 IRfund_{i,t-1}+\alpha_2 IRsec_{i,t-1}+\alpha_3 IRQFII_{i,t-1}+\alpha_4 IRtrust_{i,t-1}+\alpha_5 IRssf_{i,t-1}+\alpha_6 IRinsurance_{i,t-1}+$$
$$\alpha_7 HERF_{i,t-1}+\alpha_8 LEV_{i,t-1}+\alpha_9 Growth_{i,t-1}+\alpha_{10} LnSize_{i,t-1}+\varepsilon_{i,t} \qquad (4)$$

In order to test hypothesis 3, IR_SOH, a cross multiplier of institutional shareholding ratio and state-owned shareholding ratio is introduced, and the corresponding model is as follows:

$$ROA_{i,t}=\alpha_0+\alpha_1 IR_{i,t-1}+\alpha_3 SOH_{i,t-1}+\alpha_3 IR\_SOH_{i,t-1}+\alpha_4 HERF_{i,t-1}+\alpha_5 LEV_{i,t-1}+\alpha_6 Growth_{i,t-1}+\alpha_7 LnSize_{i,t-1}+\varepsilon_{i,t} \qquad (5)$$

$$EPS_{i,t}=\alpha_0+\alpha_1 IR_{i,t-1}+\alpha_3 SOH_{i,t-1}+\alpha_3 IR\_SOH_{i,t-1}+\alpha_4 HERF_{i,t-1}+\alpha_5 LEV_{i,t-1}+\alpha_6 Growth_{i,t-1}+\alpha_7 LnSize_{i,t-1}+\varepsilon_{i,t} \qquad (6)$$

5. EMPIRICAL RESULTS AND ANALYSIS

The test results of hypothesis 1 are shown in Table 2. Whether ROA or EPS is adopted as the measurement indicators of corporate performance, institutional shareholding ratio has a positive impact on the performance of listed companies, and it passes the test at the significance level of 1%, indicating that hypothesis 1 has been verified by data. Control variable operating income growth rate and the company's total assets of value through the 1% level of significance test, the revenue growth rate has a positive effect on corporate performance, while the size of the company has a negative impact on corporate performance. From the significance test (F test) of the overall linearity of the two equations, the P values corresponding to the F test of the regression of the two equations are all less than 1%, indicating that the linear relationship between the two equations is valid at the significance level of 1%, indicating that the regression effect is well.

Table 2. Institutional investors' impact on the performance of listed companies

	ROA	EPS
IR	0.042***	0.2636***
	(2.72)	(2.60)
HERF	-0.0247	0.2036
	(-0.60)	(0.62)
Growth	0.0149***	0.0797*
	(2.88)	(1.66)
LnSize	-0.0182***	-0.1233***
	(-3.86)	(-3.15)
LEV	0.021	0.0828
	(0.06)	(0.44)
constant	0.0988***	2.7668***
	(4.25)	(3.40)
F-statistic	5.64	5.38
Prob(F-statistic)	0.0001	0.0001

Note: The value of t is reported in parentheses. *, **, ***denote statistical significance at the 10%, 5% and 1% levels, respectively.

Table 3 results show that in all institutional investors, only fund companies have an significant positive influence on the performance of listed companies, hypothesis 2 is verified.

As Chinese securities companies often act as agents for securities underwriting and financial consulting services of listed companies, securities companies are often unwilling to destroy the interest relationship with the invested companies, so they do not want to interfere too much in the management of the company and have conflicts with the management. In addition, the income of Chinese securities companies is mainly derived from commission income from securities trading, net income from securities underwriting and sponsorship, and financial advisory business, while the income from stock trading on their own account is relatively small. On the contrary, the income of fund companies mainly comes from management fees, which are related to the performance of the fund. Moreover, fund companies do not have the same interest relationship between securities companies and listed companies, so fund companies should have more enthusiasm to supervise and intervene the invested companies. On the other hand, in China's stock market, fund companies are the institutional investors with the largest shareholding scale. A high shareholding scale reduces the unit cost of fund intervention in corporate governance, so funds have a stronger incentive to intervene in corporate governance and protect their own interests compared with other institutional investors with low shareholding ratio.

From the perspective of shareholding nature, insurance shareholding is more about the pursuit of stable dividend and bonus income and less about the interference in corporate governance. As for the shareholding ratio of QFII, social security fund and trust, the influence on corporate performance also fails to pass the significance test. The reason may be that the shareholding ratio is too dispersed and the shareholding ratio of specific companies is small, thus the unit intervention cost is too high.

From the significance test (F test) of the overall linearity of the two equations, the P values corresponding to the F test of the regression of the two equations are all less than 1%, indicating

that the linear relationship between the two equations is valid at the significance level of 1%, indicating that the regression effect is well.

Table 3. The influence of different institutional investors on listed companies' performance

	ROA	EPS
IRfund	0.0607***	0.5245***
	(2.75)	(2.73)
IRsec	0.0593	0.3648
	(0.45)	(0.35)
IRQFII	0.1633	2.0857
	(0.85)	(0.150)
IRssf	0.0483	1.4142
	(0.35)	(0.165)
IRtrust	-0.0421	0.6149
	(-0.33)	(0.53)
IRinsurance	-0.5789	-5.5706*
	(-1.95)	(-1.78)
HERF	-0.0273	0.3521
	(-0.55)	(1.12)
Growth	0.0244***	0.1701***
	(4.43)	(4.06)
LnSize	-0.0136**	-0.0872**
	(-2.19)	(-2.07)
LEV	-0.0403	-0.1806
	(0.06)	(-1.05)
constant	0.3389**	2.0625**
	(2.54)	(2.34)
F-statistic	5.65	5.45
Prob(F-statistic)	0.0000	0.0000

Note: The value of t is reported in parentheses. *, **, ***denote statistical significance at the 10%, 5% and 1% levels, respectively.

The results in Table 4 show that, after the introduction of the proportion of state-owned shares (SOH) and the multiplier of state-owned shares and institutional shares (IR_SOH), institutional shareholding ratio still has a significant positive impact on corporate performance. The coefficient of IR_SOH is. negative, but fail to pass the significance test, which means hypothesis 3 is not supported by the data test results. In China's Growth Enterprise Market, most companies have a low state-owned shareholding ratio, which is difficult to show the effect of state-owned holdings, may be the reason for the insignificant effect of IR_SOH.

Table 4. Institutional investors' impact on the performance of state-owned listed companies

	ROA	EPS
IR	0.0413***	0.2648***
	(2.63)	(2.58)
SOH	0.0337	0.3227*
	(1.22)	(1.86)
IR_SOH	-0.0038	-0.4117
	(-0.08)	(-1.16)
HERF	-0.0282	0.1774
	(-0.68)	(0.54)
Growth	0.0148***	0.0798*
	(2.86)	(1.66)
LnSize	-0.0181***	-0.1231***
	(-3.83)	(-3.14)
LEV	0.0025	0.0881
	(0.12)	(0.47)
constant	0.4181***	2.7629***
	(4.22)	(3.39)
F-statistic	7.32	4.59
Prob (F-statistic)	0.0000	0.0001

Note: The value of t is reported in parentheses. *, **, ***denote statistical significance at the 10%, 5% and 1% levels, respectively.

6. POLICY SUGGESTIONS

To guide institutional investors to play the role of "active shareholders". As can be seen from the above research results, institutional investors can effectively improve the performance of companies, so the development of various types of institutional investors should continue to be steadily promoted and relevant laws should be improved. In addition, institutional investors should be encouraged to learn how to participate in the improvement of corporate governance of listed companies and avoid harmful intervention.

REFERENCES

[1] Shleifer A,Vishny R W (1986). Large Shareholders and Corporate Control. Journal of Politics, vol.94, p.461-488.

[2] John Pound (1988). Proxy contests and the efficiency of shareholder oversight. The Journal of Finance, vol.20, p.203-265.

[3] Chaganti R , Damanpour F (1991). Institutional ownership, capital structure, and firm performance. Strategic Management Journal, vol.12, no.7, p.479-491.

[4] Marion Hutchinson, Michael Seamer, Laerlle Chapple (2016). Institutional investor heterogeneity and firm valuation Evidence from Latin America. Emerging Market Review, vol.26, p.197-221.

[5] Webb R , Beck M , Mckinnon R (2003). Problems and Limitations Of Institutional Investor Participation in Corporate Governance, Institutional Investor Participation.Corporate Governance, 2003, vol.11, p.65-73.

[6] David P, Kochhar R (1996). Barriers to effective corporate governance by institutional investors: Implications for theory and practice[J]. European Management Journal, vol.14,no.5, p.457-466.

[7] Karpoff J M , Malatesta P H , Walkling R A (1996). Corporate governance and shareholder initiatives: Empirical evidence[J]. Journal of Financial Economics, vol.42, no.3, p.365-395.