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The effect of corporate governance, corporate financing decision and ownership structure on firm performance: a panel data approach from Kuwait stock exchange

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The aim of this paper is to examine the effect of corporate governance, corporate financing decision, and ownership structure on firm performance. The study uses panel based regression approach; the analysis is based on a sample of 80 listed Kuwait Stock Exchange Market firms, over a period of 9 years, from 2000 to 2008. Findings suggest that there is no association between ownership structure (identity, types or mix) and firm performance, using both measures of firm performance, ROA and Tobin's Q. This study also finds that government ownership is insignificantly positively related to ROA using pool data; the result for the panel sample documents a hump-shaped curve between government ownership and Tobin's Q. When institutional ownership is used, there is no nonlinearity related to the firm value, using both pool and panel data sample. In this study, we also apply a three-stage least square (3SLS) simultaneous equations model to study the interaction between capital structure, dividend policy, ownership structure and firm performance. We find that, to some extent, the types of shareholders influence firm value significantly. The only two ownership variables that negatively and significantly have an effect on firm value are government shareholding and individual shareholders. We also find evidence of its intermediate function, because both capital structure and dividend policy significantly and positively influence firm value. The results of simultaneous regressions also suggest that ownership structure impacts capital structure and dividend policy, which in turn affects firm value. We also show the endogeneity of capital structure and dividend policy in listed companies in Kuwait. Hence this study provides new lights on corporate governance, corporate financing decision, ownership structure and corporate structure issue on firms' performance.

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Abstract

The aim of this paper is to examine the effect of corporate governance, corporate financing decision, and ownership structure on firm performance. The study uses panel based regression approach; the analysis is based on a sample of 80 listed Kuwait Stock Exchange Market firms, over a period of 9 years, from 2000 to 2008. Findings suggest that there is no association between ownership structure (identity, types or mix) and firm performance, using both measures of firm performance, ROA and Tobin's Q. This study also finds that government ownership is insignificantly positively related to ROA using pool data; the result for the panel sample documents a hump-shaped curve between government ownership and Tobin's Q. When institutional ownership is used, there is no nonlinearity related to the firm value, using both pool and panel data sample. In this study, we also apply a three-stage least square (3SLS) simultaneous equations model to study the interaction between capital structure, dividend policy, ownership structure and firm performance. We find that, to some extent, the types of shareholders influence firm value significantly. The only two ownership variables that negatively and significantly have an effect on firm value are government shareholding and individual shareholders. We also find evidence of its intermediate function, because both capital structure and dividend policy significantly and positively influence firm value. The results of simultaneous regressions also suggest that ownership structure impacts capital structure and dividend policy, which in turn affects firm value. We also show the endogeneity of capital structure and dividend policy in listed companies in Kuwait. Hence this study provides new lights on corporate governance, corporate financing decision, ownership structure and corporate structure issue on firms' performance.

Keywords: Corporate Governance, Ownership Structure Agency Theory, Financial Decisions, Emerging Market

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1. Introduction

The importance of the firm's financial decisions, namely, capital structure and dividend policy impact on the value of the firm, has been at the heart of academic debate. Much research has examined the effect of financial decisions in terms of irrelevancy or relevancy theories. When the imperfections include asymmetric information, taxes and more recently agency costs are introduced to the capital market, conflict of interests among stakeholders is one of the factors mostly affecting the role of debt and dividend policy. Consequently, both capital structure and dividend policy are likely to impact manager's incentives, and therefore, the firm's market value (Harris & Raviv 1991; Barclay & Smith 1999). Whilst most of the literature focuses on developed markets such as the US and UK, there is less attention on the emerging context. Therefore, this makes this research very important to conduct.

Corporate governance is another issue of growing importance, both theoretically and practically. Corporate governance includes all needed mechanisms that discipline organizations and ensure that the resources of the firm are managed efficiently and safeguard the interests of relevant players in the markets. The players of corporate governance include managers, employees, customers, executive management, board of directors, the suppliers of capital, and, mitigating the expropriation of resources by managers (Shleifer & Vishny 1997; Cadbury 1992; Morin & Jarrell 2001). In this study, we focus on the key characteristic of corporate governance, particularly the types of ownership structure, financial decisions and firm performance.

Whilst a substantial body of research in the corporate governance literature links ownership structure with firm performance, most prior research has focused on developed countries, with typically diffuse ownership structures, such as in the US and UK (Morck, Shleifer & Vishny 1988; McConnell & Servaes 1990). However, there is now an increasing awareness that theories originating from developed countries may have limited applicability and may not find their way into the developing countries because there are differences in the nature, direction, magnitude and processes of operation of the relationship between developed and developing financial markets, since there are

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differences in their economic, social, regulatory framework and market behaviour (Heinrich 2002; Ahunwan 2003). Little is known about the roles of corporate governance mechanisms in developing countries. For this reason, there is a substantial need for such theories to be tested in the contexts of emerging markets such as Kuwait that are characterized by different political, economic, cultural, institutional, social and other factors. Corporate governance frameworks originating from developed countries may have limited applicability to developing countries (Bushman & Smith 2001). These differences include a weak market for corporate control, and, more highly concentrated equity ownership structure. Therefore, the main objective of this paper is to contribute to the existing corporate governance literature by empirically analyzing the relationship between ownership structure and firm performance in Kuwait, as in any emerging country in the Middle East. To the best of the authors' knowledge, this is the first study that utilises real figures about ownership structure to investigate its effect on corporate performance for Kuwaiti companies. Furthermore, it could be considered as the first effort to utilise ownership structure variables (mix), as there is a lack of empirical evidence about the effect of ownership structure on corporate performance. However, the firm's ownership structure, capital structure and dividend policy may also be directly related to each other. Therefore, it becomes necessary to investigate the interaction among ownership structure, capital structure and dividend levels in the case of Kuwait.

We choose Kuwait for two reasons. Firstly, Kuwait has witnessed considerable economic progress in recent years, despite the ongoing conflicts in the Middle East region. As Kuwait enters the post-war recovery phase, the on-going reform of the financial market becomes essential to accelerate economic growth. Kuwait has recently started adopting several economic reforms, namely, privatization or the process of deregulation, to pave the way to stimulate the activity of the stock market, improve corporate governance and economic growth and foster international integration. As a result, the institutional ownership level has increased substantially. For this reason it becomes important to investigate the financial performance of listed companies in the Kuwait stock market during the period of privatization. This study contributes to the growing literature on

corporate governance by analysing the recent developments in the ownership structure of publicly traded firms in Kuwait, as one of the most important emerging market cases in the oil-producing region. Specifically, the study measures the impact of outsiders' ownership (government, institutional, family and individual) along with the impact of financial decisions on firm performance.

Secondly, publicly traded companies in Kuwait have a variety of characteristics that make them especially suited to the firm's ownership and firm value investigation. One of the most interesting and salient features of listed firms in Kuwait is the mixed nature of their ownership in all companies, except for the National Bank of Kuwait (NBK), which are almost entirely owned by the private sector (Limam 2001). Although the state intervention in the economy has decreased in the late 90s, there is still considerable state dominance presence in all sectors of the economy, such as the banking sector. As a result, concentrated ownership does exist among large and few business companies. Omet (2004) illustrates that the largest 20 companies are not listed on the stock exchange in Kuwait. Only 3 large companies are listed on the Kuwaiti stock exchange. In other words, the total number of 'large' and listed companies is very small. Moreover, despite the fact that KSE is a relatively young and recent stock market, there is inadequate legislation to protect minority shareholders; this has also resulted in highly concentrated ownership pattern by one individual, family held private business, or affiliated firms (Omet 2004).

The rest of this paper proceeds as follows. The next section reviews the extant literature on corporate governance mechanisms, and, empirical evidence on the relationship between corporate governance and firm performance. Section 3 provides a descriptive discussion about ownership structure for traded companies in Kuwait used in the study. Section 4 describes the data set and the estimation methods that are used in the research. Section 5 discusses the empirical results and the hypothesis test. Section 6 summarizes and concludes the chapter.

2. Literature Review

The theoretical literature on corporate governance proposes six main different mechanisms to control the agency costs, for instance, ownership structure (Jensen & Meckling 1976, and, Shleifer & Vishny 1986); capital structure and board structure (Jensen 1983); managerial remuneration (Jensen & Morphy 1990); product market competition (Hart 1983); takeover market (Fama & Jensen, 1983; Jensen & Warner 1988; Shleifer & Vishny 1988). The empirical literature that sheds light on the role of corporate governance suggests that value maximization of the firm is an outcome of these mechanisms. The empirical literature extensively investigates the effect of ownership structure on firm performance focusing on agency costs between managers and outside shareholders, and, among shareholders (majority and minority) in developed countries (Morck, Shleifer & Vishny 1988; McConnell & Servaes 1990). However, ownership structures in the developed countries are characterized as highly diffused. The potential for conflict lies mainly between managers and shareholders. The opposite is true in the developing countries where ownership tends to be highly concentrated in the hand of small numbers of major shareholders, i.e. individuals, institutions or government (Omran et al. 2008).

While some literature argues that ownership structure decisions are endogenous outcomes of the firm's value maximization behaviour, ownership is also assumed to be an exogenous firm specific characteristic that can affect debt level and dividend policy, as identified in most previous literature (Rozeff 1982; Friend & Hasbrouck 1987; Friend & Lang 1988). However, Jensen, Solberg and Zorn (1992), and, Bathala, Moon and Rao (1994) alleviate this problem by using ownership as an endogenous variable in a system of simultaneous equations. Jensen, Solberg and Zorn (1992) apply three-stage least squares (3SLS) analysis to a system of three simultaneous equations. The debt ratio and the dividend-payout ratio are used as endogenous variables in the three structural equations to be estimated. Jensen, Solberg and Zorn (1992) find that the firm's capital structure, dividend decisions and ownership structure are interdependent and affected by firm specific characteristics. Bathala, Moon and Rao (1994) apply a two-stage least

squares (2SLS) simultaneous equation model to estimate two structural equations for ownership structure and debt policy among US firms at the end of 1988.

Most empirical studies suggest a non-monotonic (curvilinear) relation between ownership structure and firm value. For instance, Morck, Shleifer and Vishny (1988) examine the relationship between management ownership and Tobin's Q by sampling 371 large industrial firms of the Fortune 500 in 1980. They show that there is a non-linear relationship between corporate value and ownership, meaning that the relationship does not take on a linear form, but rather a curvilinear one. Morck, Shleifer and Vishny (1988), however, mainly consider industrial firms in the United States, which are not representative of all firms, where many sectors may play a vital role in the US market. Applying Morck, Shleifer and Vishny's (1988) regression model, Wruck (1989) finds a similar nonlinear relationship when examining the association between the change in firm performance and ownership concentration, due to the event of private sales of equity among 128 US firms. The existence of non-linearity is also empirically supported by other studies, including McConnell and Servaes (1990), Hermalin and Weisbach (1991), Holderness, Kroszner, and, Sheehan (1999). On the other hand, following Morck, Shleifer and Vishny (1988), Morck, Nakamura and Shivdasani (2000) find that there is no evidence of a non-linear relationship between the Q ratio as a proxy for corporate value and managerial ownership among banks in Japan.

3. Ownership Structure and Firm Performance: a Descriptive Discussion
3.1 Ownership Structure (Mix) and Firm Performance
Since the establishment of KSE in the 1970s, the numbers of listed companies trading volumes and total market capitalisation have increased drastically. Table 1 depicts the ownership structure of listed firms classified by sectors[1]. Despite its privatization or the process of deregulation, the government still holds a large stake in Trade and Commercial Services, Steel, Mining and Heavy Engineering, Hotels and Tourism, Construction and Engineering (36.11%, 14.01%, 12.92% and 12.58%, respectively), because these sectors are considered as strategic industries. Even though the government do not hold any stake

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[1] The classification of these sectors is based on the Kuwait Stock Exchange (KSE) classification for firms based on their activities.

in the National Bank of Kuwait (NBK), which are almost entirely owned by the private sector, the lowest governmental stake is in Warehousing and Transporting (7.78%), whereas it is 9.94% in banks. Institutional ownership holds large stakes in Chemical and Petroleum, Educational Service and Warehousing and Transporting (27.59%, 26% and 21.99%, respectively). Family ownership is very high in Banks, Hotels and Tourism, and Chemical and Petroleum (40%, 31.18%, 23.18%, respectively). The largest individual ownership stakes are in Utilities and Energy (66.64%), followed by Warehousing and Transporting (57.71%), Real Estate (57.51%), Steel, Mining and Heavy Engineering (56.44%), Investment and Financial Services (54.67%), and Food (52.03%), and Insurance (51.39). Individual ownership is also high in Telecommunication, Construction and Engineering, Trade and Commercial Services and Educational Service (45.77%, 44.23%, 41.19% and 40.97%, respectively).

<INSERT TABLE 1>

4. Data and Estimation Method

4.1 Data

This study used the secondary data about financial decisions as well as other control variables collected manually, as this information is not available in soft copy. We used various resources, including the Kuwait Stock Exchange (KSE), Reuters, Global Investment House and Emerging Markets Information Service's (EMIS) database. The data set comprise all publicly traded firms listed at the KSE for the period 2000-2008. All companies were required to issue their financial statements for every year between 2000 and 2008. The dataset sample includes 80 listed firms in Kuwait. The information for all accounting related variables are collected and calculated from **annual financial reports, namely, balance sheets and the income statements,** for each listed firm in Kuwait. All financial statements follow the requirements of international standards. The ownership data was also collected manually using secondary resources from the Kuwait Stock Exchange (KSE), Reuters and Emerging Markets Information Service's (EMIS) databases.

4.2 The Selection of the Variables

We used two types of measures for corporate performance: accounting performance measures such as the return on assets (ROA) and, market performance measures, such as the market value of equity less debt to total assets (Tobin's Q). The explanatory variables are ownership structure, financial decisions and other firm's control variables. The measures of ownership structure are dividend into percentages of shares held by government (Gov), companies (Inst), families (Fa), and, individuals (Ind). In addition to ownership structure, other factors may also affect firms' performance and health status, such as size (Size), which is the natural logarithm of total assets, capital structure (Debt), which is defined as the total debt to total assets (TDTA) and dividend policy, which is defined as the dividend yield, which is measured by the dividend paid to the price of the stock, defined as the dollar dividend per share divided by the current price per share. Growth opportunity (Growth) is measured by the growth of assets.[2] To measure risk, we use the standard deviation of earning divided by total asset referred to as SDEV.

4.3 Empirical Model and Proxies Variables

The main objective of this study is to examine the effects of ownership structure on corporate performance. If ownership structure is irrelevant, there will be no correlation between firm performance and ownership mix (or identity). Therefore, we propose the first hypothesis to examine the effect of the ownership mix on firm performance, as follows:

H_1: A firm's ownership structure is expected to have no influence on its performance.

If this hypothesis is rejected, the government ownership, which is coined as (Govt), is hypothesised to be negatively related, because it is expected that the government's goals for social benefits and development rather than firms making profits. It is also hypothesised that a firm with institutional (Inst), family (Fa) and individual (Ind)

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[2] It is worth noting that growth of assets is measured by taking assets for the current year over assets for the previous year and then subtracting this figure by unity (or one).

ownership will have a higher performance, because of the privatization strategies in Kuwait.

Equation 1 is estimated to test the first hypothesis, using the panel data model:

$$y_{it} = \beta_0 + \beta_1 \text{Debt}_{it} + \beta_2 Dividend_{it} + \beta_3 Size_{it} + \beta_4 Growth_{it} + \beta_5 OW_{it} + v_{it} \qquad (1)$$

Where y_{it} is alternatively ROA and Tobin's Q for firm i as a measure of performance. The independent variables are represented as follows: capital structure decision (*Debt)*), the choice of dividend policy (*Dividend*), *Size*, *Growth,* and, ownership percentage *(OW)* to present different shareholders' identities. A measure of dividend policy is used in the study: dividend yield.

5. Empirical Results
5.1 Ownership Structure and Corporate Performance

To examine the relationship between ownership structure and corporate performance, we apply panel regression using the random effect model. We use panel regression because it is more informative, has less variability and less collinearity among the variables with a higher degree of freedom] and more efficiency (Gujarati 2003). A panel data can also minimize the bias that might result if individuals or firms' level data are divided into broad aggregates. Lastly, panel data can better detect and measure effects that simply cannot be observed in pure cross-section or pure time series data. Panel data regression allows us to eliminate the unobservable heterogeneity that the different companies of our sample could present (manifesto setting for Himmelberg, Hubbard and Palia (1999), among others). A Breusch-Pagan Lagrange Multiplier test is conducted to determine the overall significance of effects of the random effect model and its appropriateness. According to the Breusch-Pagan test, the null hypothesis is that random components are equal to zero. This test also provided support for the Generalized Least Squares (GLS) over a pooled Ordinary Least Squares. Table 2 presents the results of ownership identity (mix) and its effect on firm performance. The results in Table 2 shows that ownership structure including Gov, Inst, Fa and Ind has no significant impact on either

accounting or market measures of firm performance, ROA and Tobin's Q. The ownership structure is insignificantly different from zero in the regressions of ROA and Tobin's Q. The coefficient of government ownership (Gov) is negative and insignificant on ROA, whereas a positive coefficient on Tobin's Q measure of performance. The coefficients of institutions (Inst) and family (Fa) are positive and insignificant on both corporate performance measures, whereas the individual (Ind) has a negative and insignificant coefficient on ROA and Tobin's Q. Therefore, we do not reject hypothesis 1, which indicates that the ownership mix is irrelevant to firm performance because the fraction of equity owned by Government (Gov), institutions (Inst), family (Fa) and individual (Ind) shareholders do not seem to have any significant impact on the profitability of firms, as measured by ROA and Tobin's Q. For there to be no relationship between ownership structure and firm value, the ownership structure could be viewed as the result of a series of decisions reflecting the influence of shareholders and their negotiating activity in share markets. Ownership structure at any particular time should be influenced by investor desire to maximize the value of the firm.

<INSERT TABLE 2>

In all regressions, the controlling variable, firm's size (Size), has a negative and significant impact on both measures of firm's performance ROA and Tobin's Q, at the 1 percent level of significance. The controlling variable growth (Growth) also has a significant, but positive impact on both measures of firm performance at the 1 percent level of significance. The controlling variable for capital structure, Debt, has a negative and insignificant impact on ROA, while Debt has a positive and significant impact on Tobin's Q. The dividend policy has a positive and significant effect on ROA only while there is no significant impact on Tobin's Q. The findings of insignificant impact of ownership structure on corporate performance and value are consistent with prior research including Demsetz and Lehn (1985), Loderer and Martin (1997), Himmelberg, Hubbard and Palia (1999), and, Demsetz and Villalonga (2001).

5.3 Non-Linearity of Ownership

A non-linear (non-monotonic) relationship has been predicted among empirical studies including Morck, Shleifer and Vishney (1988), McConnell and Servaes (1990), and,

Loderer and Martin (1997). Following Loderer and Martin (1997), and McConnell and Servaes (1990), the squared values of government and institutional ownership are included as independent variables to capture the non-linear relationship between ownership structure and firm performance. Two measures of performance are used: ROA and Tobin's Q. The logarithm of total assets is used to control for size, growth in assets is used to control for growth, and, the debt level is used to control for leverage. In order to investigate if there is a non-linear relationship between ownership structure and firm performance, pooled and panel regressions are carried out to estimate the following equations:

$$Y = B0 + B1Gov + B3Gov^{\wedge}2 + B4Size + B5Growth + B6Debt + B7Dividend + e \ldots (2)$$

$$Y = B0 + B1Inst + B3Inst^{\wedge}2 + B4Size + B5Growth + B6Debt + B7Dividend + e \ldots (3)$$

The pooled least squares treat time-series data of a firm just as different firms at a point in time. This method does not utilize information regarding firm identity. The reason why we still report the pooled least squares results are twofold. One fold is that, the pooled least squares effectively maximize the sample size. The other and more important reason is that the pooled least squares is similar to the cross sectional analyses in that it does not control for unidentified inter-firm differences, even though it controls for the history of ownership. Table 4 shows the results of the pooled least squares and panel (random) model, which serve as a benchmark for interpreting the estimation results.

Based on theoretical and empirical studies, government ownership is hypothesised to have a negative impact on a firm's performance, because government tends to have other objectives rather than firm value maximisation. Previous research, such as Boardman and Vining (1989), Megginson and Netter (2001), and Wei, Xie and Zhang (2005) find that government ownership has a negative impact on firm performance. However, other studies including Anderson, Lee and Murrell (2000) and Gupta, Ham and Svejnar (2001) find that government ownership has a positive impact on firm performance in a transition economy. Institutional ownership is

expected to have a positive impact on firm performance as institutional ownership motivation is to maximise a firm's profit.

The empirical results that consider the relationship between government and institutional ownership and firm performance using pooled and panel data are presented in Tables 4 and 5. From the pooled data sample in Table 3, it is documented that government ownership is insignificantly positively related to ROA. The result for the panel sample using government ownership is significant at the 5 percent level for Tobin's Q. This particular result also documents that the relationship between government ownership and Tobin's Q is a hump-shaped curve. When government ownership increases above a specific point, government ownership negatively influences a firm's activities. Thus, increasing government ownership will decrease the firm performance measured by Tobin's Q. The non-linear relationship between government ownership and Tobin's Q is documented by using the panel random effects model.

<center><INSERT TABLE 3></center>

Table 4 presents the empirical results of the regression that investigates the relationship between institutional ownership and firm performance using the pooled and panel data. The results show that institutional ownership is positively and insignificantly related to the firm value using pooled and panel data sample.

<center><INSERT TABLE 4></center>

5.4 Ownership Structure, Capital Structure, Dividend Policy and Corporate Performance

An important difference between previous single models and the simultaneous equation is the ability of simultaneous equation systems to test for endogeneity. That is, some of the corporate governance mechanisms are internally related. In other words, single equation only tests the effects of governance mechanisms on performance, and, did not test if the causation is in another direction. Therefore, to capture the potential multiple relationships between ownership structure (identity), capital structure, dividend policy and firm performance, we applied a set of simultaneous equations using the three-stage

least square (3SLS) method. A three equation structural model is used with capital structure, dividend yield and ownership structure as the dependent variables. Debt ratio, dividend yield and outsider ownership are endogenous variables of the 3SLS simultaneous equation model; for instance, dividend yield and outsider ownership appear as regressors in the debt equation; debt ratio and outsider ownership appear as a regressor in the dividend equation; and, debt ratio, dividend yield and firm value appear as regressors in the outsider ownership equation. Thus, the levels of the debt ratio, dividend yield and outsider ownership are simultaneously determined in keeping with the view that debt, dividends and outsiders' ownership are interrelated in the decision-making process. The three structural equations to be estimated are as follows:

Ownership types = f (firm value, capital structure, dividend yield)
Firm value = g (ownership, capital structure, dividend yield)
Capital structure = h (ownership, firm value, dividend yield)
Dividend yield = k (ownership, capital structure, firm value)

We estimate the above simultaneous equations with control variables such as size and growth. 'Large' is the ownership sum of the first four largest shareholders, holding more than 10 percent of equity, which is a proxy of ownership. Table 5 reports the regression results of the simultaneous equations. First, for the multiple relationship between ownership types, capital structure, dividend policy and firm value, as Cho (1998), Chen and Steiner (1999) and, Himmelberg, Hubbard and Palia (1999) documented, once endogeneity is controlled, the perceived impact of ownership variables on corporate value disappears. The results of the firm performance equation of model (1) in Table 5 suggest that, to some extent, the types of shareholders influence firm value significantly. The only two ownership variables that negatively and significantly have an effect on firm value are government shareholding and individual shareholders at 5 percent and 1 percent levels of significance, respectively. Large shareholders have a positive and significant impact on firm performance. We tend to reject hypothesis 1 decisively as government ownership negatively and significantly related to firm value, as government's main focus is social rather than profit and value-maximization. On the

other hand, institutional shareholders are more profit-oriented and may have more incentives to monitor the firm. However, this finding is inconsistent with the previous single equations that reveal no statistically significant impact of ownership structure on firm value. Both capital structure and dividend policy also significantly and positively influence firm value; this is the evidence of its intermediate function. An explanation for the positive relation between a firm's dividend policy and its value could be that profitable firms distributed more dividends as a signalling mechanism to the market about their higher quality, especially in an emerging market, in which companies competing for external capital (Gul 1999b; Adaogul 2000). Another explanation is that outside blockholders could insist for higher dividend payout ratios to enhance managerial monitoring by external capital market (Farinha 2003).

The capital structure model in column (2) of Table 5 shows that institutional and individual ownership significantly and positively impact on capital structure at the 1 percent level. Conversely, outsiders with a major stake have a negative and significant impact on capital structure at the 1 percent level of significance. The negative sign of the variable indicates that large shareholders prefer companies with low debt ratio, which may serve as a mechanism of corporate governance and may reduce the agency costs significantly. Shleifer and Vishny (1986) argue that, because of their significant economic stakes, large outside stockholders have a strong incentive to monitor the firm's activities, which reduce agency costs significantly. Therefore, these results address the influence of ownership on capital structure, which in turn affects firm value.

The results of the ownership structure equation in column (4) in Table 5 also suggest that the ownership types are insignificantly affected by Tobin's Q. This result is consistent with previous empirical studies including Demsetz and Villalonga (2001). In equation (4), ROA has an insignificant coefficient, which suggests that earnings have insufficient influence on ownership structure. We also find that dividend policy is not a significant determinant of ownership structure, while financial leverage has a significant impact on institution, family, individual and large shareholders. This result is unrelated to Bathala, Moon and Rao (1994) in US corporations.

The results of the dividend equation are presented in column (3) in Table 5. We find that capital structure to be a significant determinant of dividend policy in Kuwaiti listed companies at the 5 percent level. The negative sign of the coefficient for the debt ratio variable implies that listed Kuwaiti companies with high debt levels and large interest payments tend to avoid large dividend payments. Jensen, Solberg and Zorn (1992) obtain mixed results regarding the influence of capital structure on dividend policy in U.S. corporations. The variables of the ownership structure positively and significantly impact on dividend policy. This result implies that outsider shareholdings prefer firms with higher dividend payments, because of the tax-free environment in Kuwait in which there is neither corporate tax nor personal tax on capital gain. Obviously, this result is inconsistent with studies conducted in developed markets such as the US. For example, Rozeff (1982) argues that dividends reduce agency costs in smaller firms with higher ownership. Shareholders prefer low dividends to enable them to realize the tax benefits of capital gains. Jensen, Solberg and Zorn (1992) find a significant negative relationship between ownership structure and dividend policy in U.S. corporations.

<INSERT TABLE 5>

To sum up, employing the 3SLS regressions based on 720 observations of the Kuwait Stock Exchange, our empirical results show that ownership concentration is a significant determinant influencing firm performance, proxies by accounting-based and market-based performance measures. Our results are in line with earlier studies conducted in the Middle East such as in the Jordan cases (Al-Khouri 2006; Zeitun & Tian 2007), and also with existing evidence from emerging economies, e.g. Barberis et al. 1996; Xu & Wang 1997; Claessens & Djankov 1999). The ownership structure significantly impacts on dividend policy, which may play an important role as a corporate governance mechanism.

6. Summary and Conclusions

The relationship between firm performance and its ownership structure, capital structure and dividend policy was studied extensively in the finance literature and has inconclusive results. In most previous studies, the determinants of each policy are studied independently. The study aims to extend prior research in extant literature and investigate the roles of key governance structures in the context of an emerging market, which is characterized by a weak market for corporate control and more concentrated equity ownership. To be more specific, the current research extends on the previous research (Cho 1998; Chen & Steiner 1999; Jensen, Solberg & Zorn 1992; Bathala, Moon & Rao 1994) by at least two ways. First, we introduce capital structure and dividend policy as an intermediate variable between ownership structure and corporate value. We apply a random effect model using panel data techniques to control for unobserved firm heterogeneity in order to better measure the relationship between ownership, firm performance and financial decisions. The dataset contains 80 traded Kuwaiti firms over the period of 2000 to 2008. However, the firm's ownership structure, debt and dividend levels are related not only to the firm value, but also directly to each other. In this study, we also use a three-stage least squares (3SLS) simultaneous equations model to explore the interrelationship between the capital structure, dividend policy and ownership structure in listed companies in Kuwait. Second, we extend the research of developed markets into emerging market, with the example of Kuwait, which is a viable supplement to the previous study. Most of the studies are conducted in developed countries and in some Asian countries where the characteristics of ownership structure are different from Middle Eastern countries. Consequently, implications from the theory may not be applicable to other countries. Kuwait provides an ideal setting to investigate, as its legal and regulatory institutions are different than other emerging market. Kuwait is characterised by a weak market for corporate control. Kuwait also has a more concentrated ownership structure that is relatively dominated by government stake in addition to one individual, family business and affiliated firms.

The empirical evidence shows that ownership structure does not play an important role as determinants of the performance and value firms using panel regressions. This

particular finding may signify the inefficiency of a capital market in Kuwait compared with other emerging markets. We further test the existence of non-linearity on the relationship between ownership structure and firm performance using pool and panel data. It is documented that only government ownership is significantly related with Tobin's Q, using a panel sample. This implies that when government ownership increases above a specific point, government ownership negatively influences a firm's activities. Thus, increasing government ownership will decrease the firm's performance, measured by Tobin's Q. The overall insignificance of ownership structure and ownership concentration, to some extent, is inconsistent with previous findings.

Employing the 3SLS regressions based on 720 observations of the Kuwait Stock Exchange, our empirical results show that ownership concentration is a significant determinant influencing firm performance, which are proxies for accounting-based and market-based performance measures. The results support the view that ownership concentration enhances corporate value by improving monitoring and alleviating the free-rider problems. We also find that only government and individual shareholders have a significant impact on corporate performance. Further, capital structure and dividend policy have a significant role on firm performance and value. We find that only institutional, individual and large shareholders are significant determinants of financial leverage in Kuwaiti corporations, whereas that ownership structure significantly impacts dividend policy. In addition, financial leverage also has a significant and negative effect on dividend policy, which implies that listed Kuwaiti companies with high debt levels and large interest payments tend to avoid large dividend payments. This also indicates that dividend policy may play an important role to discipline managers in Kuwait and promote adequate corporate governance control mechanisms. When ownership structure and large shareholders are endogenously determined, we find that only capital structure has a negative and significant impact on firm value, which is similar to what has been found in the US context.

Given the importance of corporate governance mechanisms and control in enhancing the economy, our results could assist policy makers and legislators in understanding the

environment for corporate control in developing countries. In particular, the regulatory authorities should be aware that the institutional, legal and regulatory framework prevailing in emerging markets are different than those in developed economies. Similarly, the reform of corporate governance should recognize more explicitly the importance of ownership concentration. It follows that any reform based on the developed markets models must be exercised with care. Furthermore, laws, regulations and institutions must provide a supportive legal infrastructure for corporate governance. In particular, commercial law in Kuwait as well as most Middle Eastern countries needs to be reformed in order to better streamline corporate governance principles within the laws. For example, commercial law does not separate ownership from control. However, one must be realistic; in the process of advocating reform and the modernization of corporate law, one must take account of the preponderance of family-owned businesses and be careful not to infringe on individual freedom to choose and dispose of wealth.

We recommend government authority must ensure that the public sector in Kuwait is well managed in accord with governance principles. Further, if a policy of privatization is the order of the day, then having efficient and well supervised financial markets becomes essential. Once the financial market imposes transparency, discipline and accountability, the stock exchange may become more efficient as well developed than those in the developed countries.

This research has a number of limitations that might warrant future research. First, the unavailability of managerial ownership percentages prevents the researcher from undertaking further investigation. Second, there are other corporate governance mechanisms such as board characteristics, CEO duality and others which are not examined in this study. Moreover, CEO duality refers to the board's chairman or managing director (or CEO) as the same person. Corporate governance scholars consider that separating the titles of chairman and CEO will reduce agency cost, and hence, improve firm performance. The reason for is that when a CEO is also chairman, the power tends to be concentrated in the hand of one person. This may allow the CEO to

control information available to other board members, which may prevent it from effectively ratifying and monitoring important decisions.

Furthermore, similar to the Gulf region's economy, the Kuwaiti's economy is classified as a bank-based economy since banks are the dominant financial players. Kuwait has also experienced a wave of financial sector liberalization. Because government's recognition of the importance of the capital market for economic growth, the government has not established a new legal framework to allow some access for foreign investors to the market and protecting investor's rights through prohibiting unfair market practices as part of the liberalization program, which prevents the researcher from making further investigations and analysis. Perhaps, future research should focus on comparing corporate governance practices across different Gulf States, which generally share similar economic and institutional landscapes.

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Table 1: Ownership Structure by Sector*

Sector	No. of Firms	Government	Institutions	Family	Individual
Banks	8	9.94	20.75	40.27	29.03
		(6.43)	(9.16)	(9.57)	(6.43)
Hotels and Tourism	1	12.92	20.73	31.18	35.17
		(3.47)	(2.35)	(2.35)	6.97)
Chemical and Petroleum	5	12.25	27.59	23.18	36.97
		(4.56)	(7.27)	(8.33)	(10.32)
Construction and Engineering	6	12.58	20.68	22.51	44.23
		(3.94)	(7.26)	(7.89)	(10.48)
Education Service	2	10.71	26.00	22.30	40.97
		(3.34)	(5.57)	(8.82)	(14.61)
Food	4	8.17	19.71	20.01	52.03
		(3.72)	(4.99)	(5.90)	(10.37)
Insurance	3	10.42	18.29	19.90	51.39
		(3.25)	(3.52)	(3.99)	(9.45)
Investment and Financial Services	27	8.19	18.00	19.15	54.67
		(2.52)	(4.32)	(5.09)	(10.16)
Real Estate	12	7.43	18.27	16.79	57.51
		(2.89)	(4.22)	(5.12)	(8.63)
Steel, Mining and Heavy Engineering	3	14.01	17.73	11.81	56.44
		(6.14)	(14.17)	(3.47)	(18.54)
Telecommunication	4	11.02	26.79	16.42	45.77
		(6.89)	(13.06)	(9.79)	(23.33)
Trade and Commercial Services	2	36.11	9.08	13.62	41.19
		(26.31)	(2.00)	(4.60)	(27.00)

Utilities and Energy	1	7.98	10.39	14.88	66.64
		(1.79)	(3.10)	(3.54)	(8.28)
Warehousing and Transporting	2	7.78	21.99	12.53	57.71
		(1.87)	(20.98)	(4.84)	(24.31)

*Firms' averages with standard deviation in parenthesis calculated from **KSE Annual Reports**

Table 2: Ownership Structure and Firm Performance

	Size	Growth	Debt	Dividend	Gov	Inst	Fa	Ind	Constant	Wald Test	Adj R^2	BP Test
ROA	-0.0278	0.0010	-0.0055	0.0121	-0.0003				0.1473	184.22		10.84
	(-4.33)***	(10.27)***	(-1.63)	(8.32)***	(-0.49)				(4.17)***	(0.00)***	0.22	(0.00)***
ROA	-0.0276	0.0011	-0.0053	0.0120		0.0004			0.1349	184.96		11.08
	(-4.32)***	(10.35)***	(-1.59)	(8.31)***		(0.95)			(3.83)***	(0.00)***	0.219	(0.00)***
ROA	-0.0277	0.0011	-0.0055	0.0121			0.0000		0.1437	184.18		12.12
	(-4.01)***	(10.28)***	(-1.62)	(8.31)***			(0.001)		(4.14)***	(0.00)***	0.2198	(0.00)***
	-0.0280	0.0011	-0.0055	0.0120				-0.0074	0.1492	184.33		12.22
	(-4.28)***	(10.30)***	(-1.62)	(8.29)***				(-0.29)	(3.81)***	(0.00)***	0.2202	(0.00)***
Tobin's Q	-0.4944	0.0034	1.0790	0.0047	0.0005				3.4236	2341.6		430.72
	(-8.25)***	(5.02)***	(43.16)***	-0.47	(0.15)				(10.67)***	(0.00)***	0.7535	(0.00)***
Tobin's Q	-0.4949	0.0034	1.0775	0.0043		0.0016			3.4041	2361.92		310.56
	(-8.45)***	(5.03)***	(43.28)***	(0.44)		(0.53)			(10.80)***	(0.00)***	0.7533	(0.00)***
Tobin's Q	-0.4996	0.0034	1.0783	0.0046			0.0016		3.4234	2342.32		346.21
	(-8.22)***	(5.05)***	(43.12)***	(0.47)			(0.49)		(10.77)***	(0.00)***	0.7536	(0.00)***
Tobin's Q	-0.4978	0.0034	1.0785	0.0045				-0.0010	3.4985	2346.17		336.22
	(-8.31)***	(5.07)***	(43.20)***	(0.45)				(-0.60)	(10.41)***	(0.00)***	0.7535	(0.00)***

Note: ***, **, * indicate significant at a 1%, 5%, and 10% level, respectively. Statistical significance t-statistics is determined with White's (1980) standard errors to correct for heteroskedasticity.

Table 3: Ownership Structure and Firm Performance: A Non-Linear Specification for Government Ownership using Pooled and Panel Estimations

| Variables | Pooled | | Variables | Panel | |
	ROA	Tobin's Q		ROA	Tobin's Q
Size	-0.026	-0.503	Size	-0.028	-0.494
	(-4.68)***	(-12.18)***		(-4.42)***	(-8.39)***
Growth	0.001	0.004	Growth	0.001	0.003
	(10.21)***	(4.68)***		(10.26)***	(4.98)***
GOV	0.001	0.021	GOV	0.001	0.002
	(1.08)	(2.24)**		(0.75)	(0.27)
GOV2	0.0000	-0.0004	GOV2	0.0000	0.0000
	(-1.62)	(0.01)**		(-1.09)	(-0.24)
Debt	-0.003	1.050	Debt	-0.005	1.078
	(-1.01)	(45.19)***		(-1.52)	(43.20)***
Dividend	0.011	-0.007	Dividend	0.012	0.004
	(8.11)***	(-0.67)		(8.26)	(0.44)
Constant	0.128	3.402	Constant	0.138	3.414
	(4.02)***	(14.42)***		(3.92)***	(10.68)***
F-statistic	30.44	477.34	Wald test	184.47	2353.35
	(0.00)***	(0.00)***		(0.00)***	(0.00)***
R-square	0.2039	0.8007	R-square	0.2146	0.7534

Note: ***, **, * indicate significant at a 1%, 5%, and 10% level, respectively.

Table 4: Ownership Structure and Firm Performance: A Non-Linear Specification for Institutional Ownership using Pooled and Panel Estimations

| Variables | Pooled | | Variables | Panel | |
	ROA	Tobin's Q		ROA	Tobin's Q
Size	-0.025	-0.500	Size	-0.028	-0.496
	(-4.57)***	(-12.22)***		(-4.33)***	(-8.44)***

Growth	0.001	0.004	Growth	0.001	0.003
	(10.25)***	(4.73)***		(10.36)***	(5.04)***
Inst	0.002	0.014	Inst	0.001	0.005
	(1.21)	(1.39)		(0.85)	(0.48)
Inst2	0.000	0.000	Inst2	0.000	0.000
	(-0.87)	(-0.51)		(-0.58)	(-0.34)
Debt	-0.003	1.049	Debt	-0.005	1.077
	(-0.97)	(45.36)***		(-1.63)	(43.20)***
Dividend	0.011	-0.006	Dividend	0.012	0.004
	(8.10)***	(-0.60)		(8.29)	(0.44)
Constant	0.108	3.291	Constant	0.126	3.371
	(3.16)***	(13.01)***		(3.30)***	(10.18)***
F-statistic	30.17	478.88	Wald test	185.15	2357.5
	(0.00)***	(0.00)***		(0.00)***	(0.00)***
R-square	0.2025	0.8012	R-square	0.2185	0.7533

Note: ***, **, * indicate significant at a 1%, 5%, and 10% level, respectively.

Table 5: Simultaneous Regression with the Three-Stage Least Squares Method

Variable	Firm Value (1)	Capital Structure (2)	Dividend Policy (3)	Ownership (4)			
				Gov	Inst	Fa	Ind
Constant	-3.5752	8.4429	78.0954	7.6336	19.9493	33.8708	38.5387
	(-3.51)***	(10.40)***	(3.60)***	(2.55)**	(7.51)***	(8.64)***	(6.89)***
ROA		0.0051	0.034	-1.3780	-3.0952	-2.0952	0.6059
		(0.034)	(0.35)	(-0.33)	(-0.96)	(-0.96)	(0.08)
Tobin's Q		-0.0002	0.5063	0.7042	2.0217	-1.3718	-1.3529
		(-0.11)	(-0.42)	(0.62)	(2.37)	(-0.97)	(-0.68)
Capital Structure	0.3135		-3.0007	-0.3971	-4.2422	-5.3650	-10.0031
	(3.22)***		(-2.36)**	(-0.18)	(-2.47)**	(-1.95)*	(2.57)**

	(1)	(2)	(3)	(4)	(5)	(6)	(7)
Dividend Yield	0.1210	-0.0867		0.3574	0.0927	-0.9912	0.5426
	(5.14)***	(-1.31)		(0.44)	(0.13)	(-0.95)	(0.37)
Gov	-0.0350	-0.0139	0.3814				
	(-3.90)**	(-0.48)	(3.04)***				
Inst	-0.0033	0.1293	0.8824				
	(-0.39)	(5.63)***	(3.23)***				
Ind	-0.0358	0.7807	0.0358				
	(-3.51)***	(3.60)***	(3.51)***				
Fa	0.0073	-0.0173	0.8734				
	(0.62)	(-1.35)	(3.26)***				
Large	0.0698	-2.4990	0.0698				
	(3.35)***	(-3.37)***	(3.35)***				
Size	-0.1542						
	(-1.97)						
Growth	0.0021						
	(3.47)***						

Note: ***, **, * indicate significance at a 1%, 5%, and 10% level, respectively.