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Founder Management, Government Ownership and Firm Performance: Evidence from Malaysia

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Abstract: *This paper examines first, how founder CEOs affect firm performance and second, whether government ownership moderates the relationship between founder CEOs and firm performance of companies listed in Malaysia between 2002 and 2011. Firms led by founder CEOs perform better than those led by non-founder CEOs. Although a direct-effect test indicates that government ownership may be detrimental to firm performance, there exists a positive relationship between founder CEOs and firm performance in the presence of government ownership from the perspective of growth opportunities. In terms of profitability, however, government ownership may not increase return on assets. These findings suggest that the government may play a crucial role to protect investor's wealth, especially with respect to long-term survival of a company.*

Keywords: Founder CEOs; Government ownership; Firm performance; Growth; Public listed companies

JEL Classification: *G32, G38, and L21*

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1. Introduction

Since 1950s, studies that focused on determinants of firm performance have suggested the following contribute to firm performance: (a) industry structure (Karabag & Berggren, 2014); (b) corporate governance including ownership structure (Andreou, Louca, & Panayides, 2014; Oluwatayo & Amole, 2013); and (c) economic conditions (Pantea, Gligor & Anis 2014). Earlier studies have also examined the relationship between firms led by

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founder CEOs and their performance in particular, (Anderson, Duru & Reeb, 2009; Chen, Gray & Nowland, 2012; Isakov & Weisskopf, 2014; Willard, Krueger & Feeser, 1992). They found founder CEOs can be either value-enhancing or value-diminishing for the company.

Chen et al. (2012) argued that founder management has pros and cons to shareholders. Among its advantages are: potential for shareholder's long term wealth creation as founder CEO dedicates himself or herself to achieving the best performance for the company and ensure its long term survival. Fama and Jensen (1983) explain that founders will utilise their experiences and skills to ensure the success of firms. Furthermore, they are more likely to be influential in executing decisions (R. B. Adams et al., 2005). Founder management is also able to solve problems related to principal-agent more effectively. By ensuring high levels of monitoring and oversight (Jensen & Meckling, 1976).

The disadvantage of founder management is the risk of private benefits to the CEO in terms of siphoning of wealth to the detriment of shareholders. Anderson and Reeb (2003) emphasise that founders will ensure they gain private benefits (e.g. higher compensation or remuneration, attractive dividend payments, lower risk and etc) rather than focusing on the firm's long term achievement. Anderson et al. (2009) conclude that founder management seeks private advantages to the shareholders' detriment. In short, founders may either bring about greater benefit to the company via enhanced monitoring or disadvantages via private gains (Isakov & Weisskopf, 2014).

Therefore, this study provides empirical evidence as to how founder CEOs can improve firm performance by adding a variable, government ownership. Many companies face problems as a result of separation of ownership and control (Yu, 2013). Difference in ownership produces different impact on firm performance. On one hand, government-owned firms are expected to act differently relative to their private counterparts (Pedersen & Thomsen, 2003). On the other hand, government ownership may mean a poor governance structure because a public portfolio allows other shareholders to free ride on the monitoring of management provided by the government (Putterman, 1993). Economists believe that government ownership is usually detrimental to firm performance (Tian & Estrin, 2008).

The role of government in contributing to firm performance is a popular research topic (Ng, Yuce & Chen, 2009; Wolf, 2009; Yu, 2013). In Malaysia, government linked companies (GLCs) play an important role in its economic development. However, GLCs in Malaysia are perceived to be less efficient and profitable. Numerous researches have been undertaken to study how government ownership enhances firm performance in Malaysia (Johnson & Mitton, 2003; Lau, 2013; Lau & Tong, 2008; Razak, Ahmad & Joher, 2011). The empirical significance of these studies with regard to the moderating role

of government ownership on the relation between founder management and firm performance has not been established. This study attempts to provide some preliminary conclusions on this issue.

The study will focus on the relationship between founder CEOs and firm performance among companies listed in Malaysia. It also attempts to identify whether government ownership plays a significant role in moderating the relationship between founder CEOs and firm performance. This paper makes several contributions. First, this study documents the role of founder CEOs on the performance of Malaysian public listed firms. Second, government ownership is used as a moderator to test the association between founder CEOs and firm performance. Third, two measures of firm performance, namely return on assets (ROA) and growth opportunities, are used. While the former represents profitability, the latter reflects firm performance from a wider perspective. Overall, the findings highlight the impacts of founder CEOs and government ownership, both separately and jointly.

This paper is organised as follows. Part Two contains review of main literature on this topic while Part Three consists of data and methodology. Part Four discusses findings and results of the study and the final part concludes the paper.

2. Literature Review

2.1 Founder management and firm performance

Extant empirical studies show no specific pattern on the effect of founder management on firm performance. Gagné and Deci (2005) define roles as a typical behaviour that characterises a person in a specific social context, specifically leaders. The CEO's role as founder of the firm (relations-oriented role) would shape his or her opinions in relation to firm decisions. Fama and Jensen (1983) suggest that when ownership and control rest with the same individual, it will reduce the monitoring cost by external shareholders, thus enhancing firm value. McConaughy, Walker, Henderson, & Mishra (1998) indicate that founding family-controlled firms are more efficient as the founder focuses on long term wealth creation for shareholders and firms. Fischer and Pollock (2004) also assert that founder involvement in the firm ensures the CEO is committed to the success of the firm.

According to Anderson and Reeb (2003) who studied firms in US, founders are associated with greater firm values suggesting that they bring unique, value-adding skills to the firm that result in superior accounting performance and market valuations. Similarly in China, Xia (2008) finds that investors are better protected if the firm is managed by founder CEO. The finding is consistent with that of Anderson and Reeb (2003) who agree there

is a positive relation between founder management and accounting profitability measures. In Taiwan, Chen et al. (2012) focus on multi-founder firms and define multiple founder firms as those "that were founded by multiple individuals with no family connections but actively involved in the firms as directors." The result shows that founder-managed firms are valued greatly. In Switzerland, Isakov and Weisskopf (2014) found that companies with active founders as leaders have higher profitability. They argue that company founders with their superior skills and incentives will enhance the firm's profitability

On the other hand, Singell and Thornton (1997) argue that family managed firms with founders as CEO are less profitable. This is supported by Gomez-Mejia, Larraza-Kintana & Makri (2003) who also agree that founder CEOs are potentially less accountable to shareholders. The entrenchment hypothesis suggests corporate opacity allows these controlling shareholders to accrue private benefits of control (Anderson et al., 2009). Consistently, In Norway, Randøy and Goel (2003) find that large shareholders' ownership is significantly negative to firm value in founder-led SME firms. Anderson et al. (2009) find that founder firms exhibit a negative relation to firm performance as founder management in a firm seeks for private benefits at the cost of other shareholders for 2,000 largest industrial firms in the US. Jameson, Prevost & Puthenpurackal (2014) examine founders who are actively managing their firms and their findings indicate that founders on boards may expropriate the minority shareholders' interests.

Findings of studies on how founders affect firm performance are mixed and no consistent pattern can be found. In other words, there is no clear prediction about the overall effect of founder management on the performance of firm. Therefore, we develop the following hypothesis in a non-directional alternate form:

Hypothesis 1: Founder management is significantly related to firm performance.

2.2 Government Ownership and Performance

Besides founder management, prior studies have also shown that government ownership determines firm performance. Some studies like Dewenter and Malatesta (2001) document a negative association between government ownership and firm performance because governments may not be oriented towards maximising profit. Besides, there are more government bureaucracy and thus, bigger agency problems (Sun & Tong, 2003). Similarly, Tian and Estrin (2008) suggest that government shareholding (with a small voting right) does not allow it to monitor and control the manager, and which leads to reduction in firm performance. Zeitun and Tian (2007) suggest a reduction

government ownership in order to increase firm performance. Ng et al. (2009) support the negative relationship between government ownership and its performance and conclude that privatisation is beneficial to firm performance. Mykhayliv and Zauner (2013) point out the negative effect of government ownership on firm performance. Ting and Lean (2015) also concur on the negative relationship between government ownership and firm performance.

Conversely, several studies point to a positive relationship. Yu (2013) finds that government ownership is positively related to performance of China listed companies after 2006 because government provides both financing and resource-related support. In Singapore, Ang and Ding (2006) conclude that GLCs have greater valuations than their counterparts in Singapore. They explain that Singaporean GLCs have better governance mechanisms and stronger monitoring, in addition to being leaner organizations. Kang and Kim (2012) find that firms from marketised state-owned enterprises perform well in China.

In view of the contradicting associations between government ownership and firm performance, this paper investigate the potential moderating effect of government ownership in the Malaysian context. The hypothesis is thus as follows:

Hypothesis 2: Government ownership moderates the relationship between founder management and firm performance.

3. Data and Methodology

The study has the following criteria for sample selection. First, it excludes financial services companies due to their different regulatory mechanism. Each firm must have the required 12-year data from 2002 to 2013. Balanced panel data is used in order to maintain the fairness of observations and dynamics could be monitored closely. Additionally, the firm has full information of CEO profile, especially on founder information. Government ownership information is available in the 30 largest shareholders' list of the company. After screening through the samples, the collected dataset consists of 183 public listed firms between 2002 and 2013.

3.1 Variables and Measurement

This section explains regression-related variables. For dependent variables, ROA, a widely used measure of firm performance, is calculated as net income divided by total assets (Anderson & Reeb, 2003; McConnell & Servaes, 1990). As for growth opportunities (GROWTH), following McConnell and Servaes (1990) and Weir, Laing & McKnight (2002), it is

computed as subtraction of prior-year sales from current-year sales divided by the prior-year sales. In terms of independent variable, the study follows Adams, Almeida & Ferreira, (2009) with dummy variable to measure founder management. We set FOUNDER_CEO as 1 if the CEO of the firm is also a founder, otherwise, 0. For moderating variable, this study measures government ownership (GVO) as the percentage of shares held by the government. With respect to control variables, this study uses firm size, debt ratio and tangibility. The natural logarithm of total assets is used to represent firm size (SIZE) (Ang & Ding, 2006; Deesomsak, Paudyal & Pescetto, 2004; Rajan & Zingales, 1995; Sogorb-Mira, 2005). The debt ratio (DEBT) is the ratio of total debt to total assets (Ting & Lean, 2011). The tangibility (TANG) is computed as the ratio of fixed assets to total assets (Zeitun & Tian, 2007).

3.2 Research model

In order to examine the impact of founder management on firm performance, the study proposes Model 1 as follows.

$$PERF_{it} = \beta_o + \beta_1 Founder\_CEO_{it} + \beta_2 GVO_{it} + \beta_3 SIZE_{it} + \beta_4 DEBT_{it} + \beta_5 TANG_{it} + \varepsilon_{it}$$

(Model 1)

In where subscripts *i* and *t* represent firm (cross-section) and time (time-series) respectively. $PERF_{it}$ = Performance (ROA or GROWTH) for firm *i* in year *t;* $FOUNDER\_CEO_{it}$ =1 if the CEO of the firm is also a founder, 0 otherwise for firm *i* in year *t*; GVO_{it} = Percentage of government ownership for firm *i* in year *t;* $SIZE_{it}$ = The natural logarithm of total assets for firm *i* in year *t;* $DEBT_{it}$ = Total debt divided by total assets; $TANG_{it}$ = Fixed assets divided by total assets.

To test government ownership as the moderator on the association between FOUNDER_CEO and PERF, this study uses it as an additional variable in Model 2.

$$PERF_{it} = \beta_o + \beta_1 Founder\_CEO_{it} + \beta_2 GVO_{it} + \beta_3 Founder\_CEO*GVO + \beta_4 SIZE_{it} + \beta_5 DEBT_{it} + \beta_6 TANG_{it} + \varepsilon_{it}$$

(Model 2)

4. Findings and Analysis

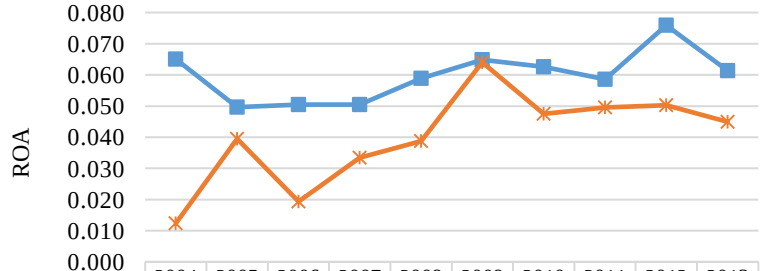
4.1 Univariate Analysis

Table 1 presents the statistical description of the sample. The average ROA and TBQ is 4.62 per cent and 98.72 percent, respectively. The sample companies derive approximately 4.6 percent of profits using their total assets, as shown by the average ROA. The mean GROWTH value of 0.0070 suggests that the sample firms have low growth opportunities. Approximately, 31.04 per cent of the sample firms went public with a founder CEO at the helm. The statistics also indicate that government ownership of Malaysian listed companies averages at about 42.93 percent. Furthermore, the firm size of 12.2494 shows that the average total assets of the study's sample firms total RM1.774 trillion (the average logged value is 12.249). The average ratio of total debt to total assets for the observed period is about 31.05 per cent. The tangibility of 0.5176 shows that 51.76 percent of the total assets is fixed assets.

Table 1: Descriptive analysis

Variables	Mean	S.D.
ROA	0.0462	0.1201
GROWTH	0.0070	0.1381
FOUNDER_CEO	0.3104	0.4628
GVO	0.4293	0.2829
SIZE	12.2494	1.5271
DEBT	0.3105	0.3284
TANG	0.5176	0.3344

Figure 1: ROAs of founder and non-founder firms, 2002-2013



	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013
Founder	0.065	0.050	0.050	0.050	0.059	0.065	0.063	0.059	0.076	0.061
Non-founder	0.012	0.039	0.019	0.033	0.039	0.064	0.048	0.050	0.050	0.045

Figure 1 indicates ROA of the founder and non-founder firms between 2002 and 2013. It shows that firms with founder-CEO outperform the rest. This result is consistent with those of previous studies (Gao & Jain, 2012; He, 2008; McConaughy et al., 1998; Randøy & Goel, 2003). The univariate comparison of ROA between founder-CEO's firms and non-founder-CEO's firms in Figure 1 confirms that founder management enhances firm performance. This could be explained as the increment of monitoring as a founder CEO provides a better alignment of interests between owner and manager (Isakov & Weisskopf, 2014).

4.2 Correlation analysis

To ensure there is no multicollinearity among variables, Pearson correlation analysis is conducted and shown in Table 2. The highest absolute value found is of -0.6018, indicating no likelihood of multicollinearity problem. Besides, there are significant correlations between ROA, GROWTH and explanatory variables. Moreover, the value of VIF are all less than 2 (O'brien, 2007) (VIF for FOUNDER_CEO = 1.0666, VIF for GVO = 1.1402, VIF for SIZE = 1.0779, VIF for 1.6535 = 1.15 and VIF for TANG = 1.5833 respectively), suggesting again no multicollinearity problem among the variables. With that, no variables should be left out from the multivariate analysis (O'brien, 2007).

Table 2: Correlation Analysis

	ROA	TBQ	FOUNDER _CEO	GVO	SIZE	DEBT
ROA	1.0000					
GROWTH	-0.1810***	1.0000				
FOUNDER _CEO	0.0748***	0.0876***	1.0000			
GVO	-0.0815***	-0.2194***	-0.0642***	1.0000		
SIZE	0.3035***	-0.5075***	-0.0103	0.1292***	1.0000	
DEBT	-0.1677***	-0.0126	0.0365	0.1679***	0.0326	1.0000
TANG	0.2645***	-0.0313	0.0146	-0.1340***	-0.0191	-0.6018

Note: * and *** denote the coefficients are significant at the 1 and 10 per cent levels, respectively.

4.3 Regression analysis

4.3.1 Main effect

To ensure the most appropriate model for panel data estimation, the Lagrange Multiplier (LM) test (Breusch & Pagan, 1980) was conducted. The

LM statistic (P > 0.10) suggests that pooled ordinary least square (OLS) regression could provide better estimations than panel data regression. Hence, pooled OLS regression is employed to test the constructed models. Potential heteroscedasticity problem was diagnosed using the White (1980) test. Since the diagnostic check indicates heteroskedasticity problems, the problem is rectified using OLS with heteroskedasticity robust standard error (Hoechle, 2007).

Table 3 shows the pooled OLS regression results of using ROA as dependent variable. The F-statistic points to the model's overall significance. Based on the finding, founder CEO is found to have significantly positive impact on ROA. This finding is in line with Saito (2008), Xia (2008) and Isakov and Weisskopf (2014) that founder management enhances firm value. The CEOs who are also the founders do care about their companies as they their wealth is largely derived from it (Arregle, Hitt, Sirmon & Very, 2007). Isakov and Weisskopf (2014) argue that founders may be able to exploit more investment opportunities to increase their firm performance. They would try to ensure longevity and growth which are consistent with the objectives of an owned business.

Table 3. Regression Analysis – Main Effect

Variable	**DV = ROA**		**DV = GROWTH**	
Intercept	- 0.3110 (- 5.1483)***	- 0.3122 (- 5.1796)***	0.6113 (11.1832)***	0.6095 (10.9052)***
Testing variable				
FOUNDER_CEO	0.0195 (4.0262)***	0.0196 (3.9453)***	0.0188 (2.8905)**	0.0199 (3.0488)**
GVO	- 0.0376 (- 4.1932)***		- 0.0792 (- 7.8353)***	
DUMGVO		- 0.0199 (- 3.4507)***		- 0.0263 (- 4.5466)***
Control variable				
SIZE	0.0253 (9.0134)***	0.0251 (9.2303)***	-0.0460 (- 11.6294)***	- 0.0471 (- 11.7415)***
DEBT	- 0.0030 (- 0.0763)	- 0.0024 (- 0.0594)	- 0.0075 (- 0.6690)	- 0.0098 (- 0.8403)
TANG	0.0884 (2.0252)*	0.0889 (2.0353)*	-0.0298 (-3.2211)**	-0.0284 (-2.9291)**
Year fixed effect	Yes	Yes	Yes	Yes
Industry fixed effect	Yes	Yes	Yes	Yes
Adjust R^2	0.1810	0.1801	0.2960	0.2806
F-statistic	21.2091***	21.0855***	39.4545***	36.6766***

Notes: *t*-statistics are given in parentheses. ***, ** and * denotes the significance level at 1%, 5% and 10%, respectively.

Model 1 shows a significantly negative association between GVO and ROA, indicating that firms that has government interventions are less profitable because of their poor investment decisions (Ting & Lean, 2015). More importantly, as shown in Table 3, the results remain when using DUMGVO as an alternative proxy of government ownership. This implies that firms with government ownership has poorer governance mechanisms that weaken their performance.

This study performs another robustness check by replacing ROA with GROWTH as a measure of firm performance. This study re-estimates Model 1 with pooled OLS regression and the results remain qualitatively the same. The findings reconfirm that firms (i) who have their founders in the active management are more profitable, (ii) with government intervention are detrimental as its reduce their performance.

The coefficients of SIZE and TANG are significantly positive when ROA is used as the dependent variable, in line with Ang and Ding (2006). However, SIZE and TANG are found to be significantly and negatively associated with GROWTH. Moreover, the insignificant effects of DEBT on firm performance show that DEBT does not directly affect firm performance.

4.3.2 Moderating effect

Based on Model 2, the moderating effect of GVO (FOUNDER_CEO*GVO) on the association between founder management and firm performance, particularly GROWTH is proven to be significantly positive at 1 per cent level. This finding suggests that government ownership strengthens the positive association between founder management and firm performance. Put differently, a large government ownership of a firm will increase the positive effect of founder management on GROWTH. To check for robustness, this study tests the interaction effects between founder management and government by replacing government ownership with its dummy variable, giving us FOUNDER_CEO*DUMGVO in Model 2. The moderating effect of government ownership on the association between founder management and GROWTH is proven to be significantly positive at 10 per cent level. This implies that government ownership plays a crucial role to protect investor wealth, especially with respect to the long-term survival of a company.

Table 4: Moderating Effect

Dependent variable:	**ROA**		**GROWTH**	
	Model 1	**Model 2**	**Model 3**	**Model 4**
Intercept	- 0.3109 (- 5.1393) ***	- 0.3123 (- 5.1789)***	0.6159 (11.3769)***	0.6105 (11.0408)***
Testing variables				
FOUNDER_CEO	0.0183 (2.4589)*	0.0210 (2.8942)**	- 0.0156 (- 1.2598)	0.0049 (0.4690)
GVO	0.0383 (- 3.5994)***		- 0.0993 (- 8.56881)***	
DUMGVO		0.0191 (2.67726)**		- 0.0347 (- 4.9413)***
FOUNDER_CEO * GVO	0.0029 (0.1684)		0.0841 (3.5030)***	
FOUNDER_CEO * DUMGVO		0.0026 (- 0.2816)		0.0268 (2.0795)*
Control variables				
SIZE	0.0253 (8.9955)***	0.0251 (9.2216)***	-0.0457 (-11.6468)***	-0.0467 (-11.7058)***
DEBT	-0.0031 (-0.0781)	-0.0023 (-0.0572)	-0.0100 (-0.9199)	-0.0107 (-0.9368)
TANG	0.0885 (2.0267)*	0.0888 (2.0350)*	-0.0284 (-3.0817)**	-0.0276 (-2.8590)**
Year fixed effect	Yes	Yes	Yes	Yes
Industry fixed effect	Yes	Yes	Yes	Yes
Adjusted R^2	0.1805	0.1797	0.3009	0.2822

Notes: ***, ** and * denotes the significance level at 1%, 5% and 10% respectively.

4.3.3 Robustness Check- Two-stage least squares (2SLS)

This study adopts two-stage least squares (2SLS) to address potential endogeneity issues. FOUNDER_CEO, which is used as the main proxy for founder management, is the dependent variable. The 2SLS results shown in Table 5 corroborate with those of the pooled OLS regression. Therefore, the pooled OLS method provides reliable estimates.

Table 5: Regression results of ultimate owners' control, family control and leverage – 2SLS

Stage	**Stage 1**	**Stage 2**	
Dependent Variable	**FOUNDER_CEO**	**ROA**	**GROWTH**
Model	Model 1	Model 2	Model 3
Intercept	0.0354	-0.3016	0.6204
	(070757)	(-5.0209)***	(11.4003)***

Table 5: (Continued)

Testing variables			
FOUNDER_CEO		0.0196	0.0188
		(4.0308)***	(2.8857)**
GVO	-0.5304	-0.0396	-0.0812
	(-2.6599)**	(-4.4237)***	(-8.0317)***
Control variables			
SIZE	-0.0486	0.0251	-0.0462
	(-1.3919)	(8.9849)***	(-11.6915)***
DEBT	0.3584	-0.0017	-0.0063
	(2.2218)*	(-0.0429)	(-0.5566)
TANG		0.0884	-0.0299
		(2.0242)*	(-3.2262)**
Year fixed effect	Yes	Yes	Yes
Industry fixed effect	Yes	Yes	Yes
Adjusted R^2		0.1810	0.2960

Note: *t*-statistics are given in parentheses. ***, ** and * denotes the significance level at 1%, 5% and 10%, respectively

5. Conclusion

This paper examines how founder CEOs affect performance of publicly-listed companies in Malaysia. The results show that firms led by founder CEOs performed better those led by non-founder CEOs. This positive association between founder management and firm performance is consistent with the findings of Chen et al. (2012), confirming that founder involvement in firms could result in more wealth creation for shareholders. Moreover, the result also indicates that government ownership plays an important role in strengthening the positive relationship between founder CEOs and growth opportunities. However, investors believe that government may not serve as an effective control mechanism to mitigate the risk that founders may prioritise their personal interest. Hence, firms led by founder CEOs are more profitable with higher government ownership from the perspective of growth opportunities.

This paper contributes to the literature on firms led by founder CEOs as well as to policy makers. In particular, the positive effect of founder CEOs on firm performance suggests that performance of firms is driven primarily by CEO founders with the helping hand of government. Although government intervention may be not welcomed by companies, when interacting with founder management, government ownership actually

results in increased benefits. Future studies can explore the effect of different generations of founders in firms to compare their effect on firm performance.

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