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Ownership patterns and control of top 100 Malaysian listed companies

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Abstract. The incentive of this study stems from the significance of protecting minority shareholders' rights. It analyses the most dominant ownership structure practices within listed firms in Bursa Malaysia (BM), in which controlling shareholders (CSs) hold control on many firms despite relatively small portion of investment. Malaysian firms are characterised by high levels of concentrated ownership with families owning more than 70% of the listed firms in BM [9]. This study finds that the separation between cash flow rights (real investment) and control rights (voting rights) for Top 100 Malaysian listed firms is accomplished through pyramidal ownership and golden share arrangements. Hence, the divergence between cash flow rights (CFRs) and voting rights (VRs) exacerbates Type II Agency problem. This study calls for future studies in the area of accounting and finance to introduce and operationalise new measurement of Type II Agency Cost in order to better understand the agency conflicts within this unique market. It also better explains the state of the minority shareholders in the BM.

1. Introduction

Previous literature has examined various firms' ownership structure in many countries. Many of previous studies compared between dispersed ownership and concentrated ownership, in which individual or families represent controlling shareholders (CSs) through ownership on almost all equities [2]. In comparison, this study examines an ownership structure in which individuals practise control on many affiliated firms with less stake of real investment. In Malaysia, there are two predominant methods to separate between CFRs and control rights (CRs) or voting right (VRs). They are pyramidal ownership and golden share [20]. These kinds of ownership structure permit CSs to maintain their control on many firms with relative small portion of equities. The separation between CFRs and VRs entrenches the CSs position and maintains corporate control in their hand far from market competition with relative small stake of equities [9]. Despite of the fact that this separation reduces agency conflicts between agent and principle that is known as Type I Agency Problem, Type II Agency Problem would emerge [15]. The separation between CFRs and CRs also enhances majority shareholders incentives to expropriate minority shareholders wealth [3]. CFRs in this study are defined as CSs rights to claim in the firm's liquidity and profits. Meanwhile, CRs indicates CSs capability to influence firms' strategic decisions for instance, in terms of board of directors' selection. These types of ownership structures distort CSs motivations to place more attention on governance mechanisms, extending from legal protection of minority shareholders to reputational boundaries on CSs. The same reason encourages political and market scrutiny in numerous countries to focus on problems to innate pyramidal ownership and golden share. Therefore, this paper addresss ownership structure practices within Malaysian listed firms. To the best of our knowledge, there is no study that addressed the sectorial concentration of wedge using pyramidal ownership and golden shares in BM. The study's main objective is to explain the mechanisms of divergence between CFRs and CRs practiced in BM market, which provides a useful ground for future studies to investigate Type II Agency Problems in Malaysian business environment. With respect to theoretical contribution, this paper extends agency theory literature by analyzing deeper the agencies conflicts and provides measurement of such conflict in the unique Malaysian market. Previous study documents the ownership-control structure as the most significant elements that exacerbate Type II Agency Problem [2]. The practical contribution of this study is that it would offer strong foundation for policy makers to suggest an optimal policy to improve the corporate governance mechanisms and provide protected and conducive environment for minority shareholders.

2. Mechanisms for Separating Cash Flow and Control

This study addresses Malaysian listed firms in term of ownership-control structure mechanisms are pyramidal-ownership structure and golden share [6].The following section addresses pyramidal ownership structure and golden shares.

2.1 Pyramids

This section allocates to illustrate the nature of CFRs and CRs and Pyramidal structure. Firms involve with pyramidal ownership structure have divergence between CFRs and CRs that has a negative implementation on minority shareholders protections. This is a consequence of high incentives of Ultimate Ownership (UO) to expropriate minority shareholders wealth [22]. CFRs are a real ownership of investors through buying shares. That is because ownership is a consequence of investment and CFRs represent as an indicator of investors investment in the corporation [19]. While, CRs indicates to UO voting rights [9]. Reasonably, CFRs shall be equal to CRs in corporation as indicators of shareholders real investment. Notwithstanding that pyramid structure leads to divergence between CFRs and CRs. Pyramidal structure is defined as "a situation in which the same entrepreneur, through a chain of control relations, controls many firms" [7]. This means that UO own the majority of ownership of one firm that in turn owns the majority ownership of another firm. The clearest example of pyramidal structure is that of Halim bin Saad, an entrepreneur from Malaysia. Halim owns about 28.3 real stake ownership of Renong Berhad as shows in figure (1). Accordingly, Halim represents the UO of the Renong Berhad. At the same time, Renong Berhad possesses about 32.5 of share ownership of United Engineers Malaysia (UEM). Consequently, Renong Berhad represents a UO of UEM. It can be seen that Halim controls Renong Berhad that in turn hold a major control on UEM. This indicates that Halim directly controls Renong Berhad in the first level of the pyramidal structure and in the second level Halim controls UEM indirectly. In addition, Halim controls through both of Renong and UEM on Kinta Kelas indirectly. Halim ownership in Kinta Kelas arises from his real ownership in Renong Berhad and UEM. As a result of this pyramidal ownership structure Halim own real ownership about 5.73 in Kinta Kelas. The ownership value is finds out using the following method:

Halim's CFR in Kinta Kelas = 28.3% x 32.5% x 62.4% = 0.05739 ~ 5.73%

Meanwhile, the theoretical ownership comes through individual investment in the corporation. According to [18] the ownership arises as a consequence of investment. If Halim stake of ownership is about 5.73 per cent, this indicates that his investment stake in Kinta Kelas is 5.73 per cent. The following example illustrates Halim stake of ownership in Kinta Kelas in dollar value. For instance, Kinta Kelas worth is about 100,000,000

Malaysian Ringgit (MR). Therefore, Halim controls Kinta Kelas worth that is about (100,000,000) with an investment about 5,730,000 (5.53 per cent × 100,000,000). Halim has indirect control rights in Kinta Kelas. This is achieved through Halim's direct control on Renong Berhad at first level that in turn own major control on UEM at the second level of the pyramidal, and at the final level Halim controls Kinta Kelas through UEM. Based on the definition provided by [12] CRs represent the weakest link in the chain of control relationship. Accordingly, Halim has CRs about 28.3 per cent and this consider as the weakest link in the chains of control relationship through the three levels of the pyramidal structure. Obviously, Halim with 5.73 per cent of CFRs or 5,730,000 RM worth of investment hold about 28.3 per cent of CRs in Kinta Kelas with worth about 100,000,000 RM. This align with [13] propose that pyramidal ownership structure creates sharp divergence between ownership and CRs that deviates from the traditional view of one share-one vote. Importantly, UO incentive to expropriate shareholders wealth increased as a result of the separation between CRs and CFRs [9]. The divergence between CRs and CFRs find out following [14] whether via the ratio of cash flow rights to control rights or the difference between cash flow rights and control rights.

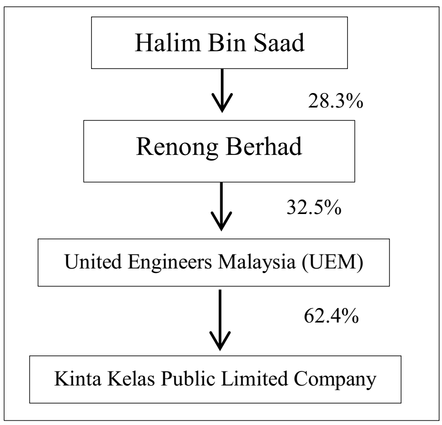

Figure 1: Pyramidal ownership structure
Source : [16]

The divergence between CFRs and CRs for Kinta Kelas finds out using the following two methods:

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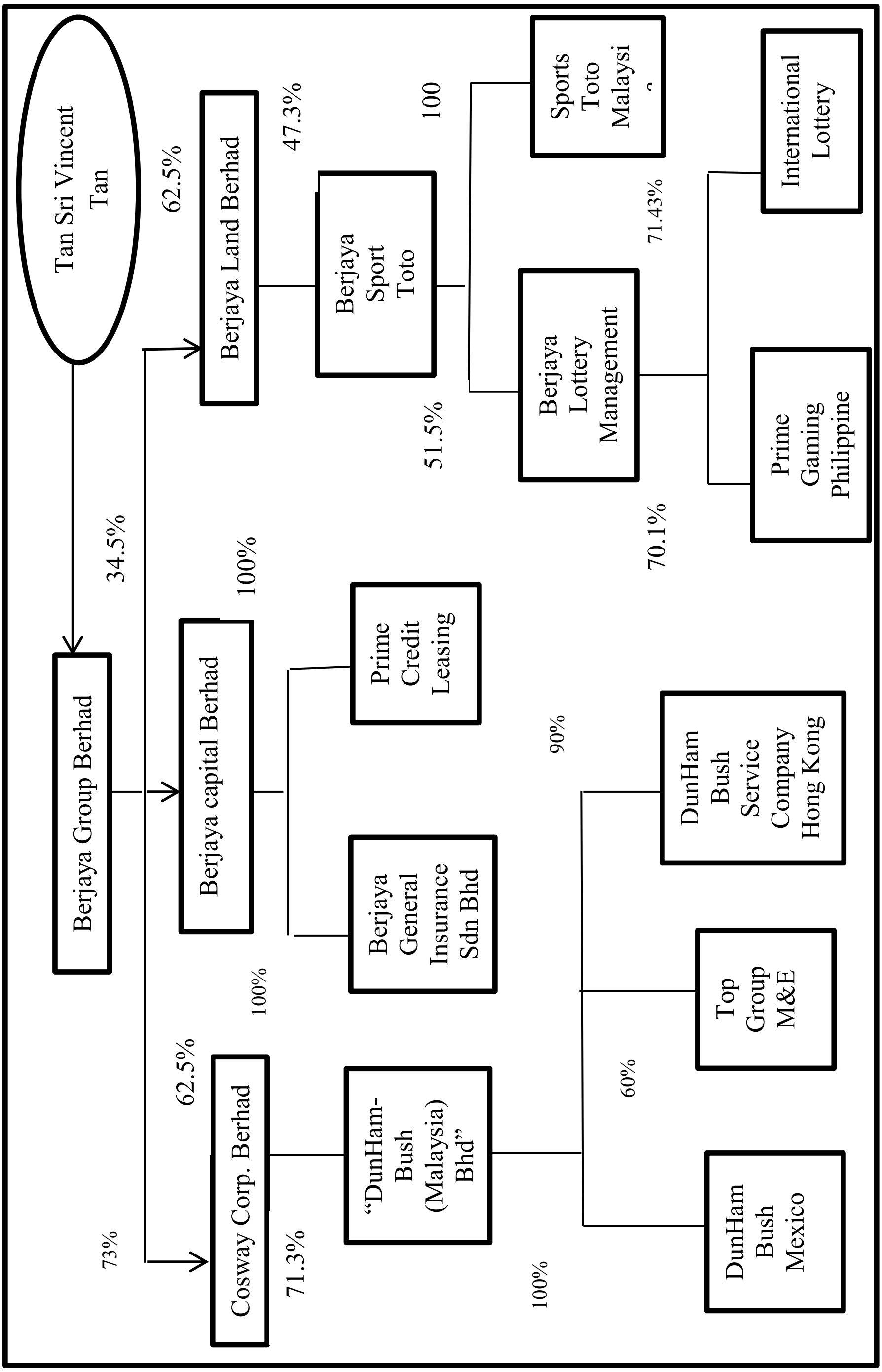

Source: [6]

Figure 2. DunHam-Bush (Malaysia) Bhd

1-Ratio of cash flow to voting rights = Halim’s cash flow rights/ Halim’s voting rights = 5.73%/ 28.3% = 0.2024	2- the variance between cash flow rights and voting rights = Halim’s cash flow rights - Halim’s voting rights = 5.73% - 28.3% = 22.57%

According to previous techniques, the larger divergence between CFRs and CRs reflects the sharper differences between investment and voting rights and verse versa. The second case is DunHam-Bush (Malaysia) Berhad Figure 2. The UO of this firm is Cosway Corporation Berhad with ownership stake about 71.3%. The UO of Cosway Corporation Bhd on the other side is Berjaya Group Bhd with about 73% of CFRs. Tan Sri Vincent Tan is a UO with stake about 34.05% of Berjaya Group Bhd. To figure out the CFRs and CRs of Tan Sri Vincent Tan in DunHam-Bush (Malaysia) Bhd, this work first considered the holding of Cosway Corporation Bhd in DunHam-Bush (Malaysia) Bhd, the holding of Berjaya Group Bhd in Cosway Corporation Bhd and finally Tan Sri Vincent Tan's holding in Berjaya Group Bhd.

According to this ownership structure, Tan Sri Vincent Tan's cash flow rights in DunHam-Bush (Malaysia) Bhd is about 17.723%, (=71.3%×73%×34.05%) whereas his CFRs is about 34.05%. The CFRs is determined according to the weakest link in the chain of controlled rule [14]. The ratio of CFRs is about 52.05%. This value shows that there is violation of one share–one vote policy in DunHam-Bush (Malaysia) Bhd and it might enhance controlling shareholders incentive to expropriate the interests of minority shareholders.

2.2 Golden shares

The Malaysian government holds a single unit “golden share” which uses it to veto on essential decisions that is relate to national interest consequences [16]. Golden share define as a set of Government’s special authority and legal constrictions on privatize firms [8]. This kind of control-ownership is dominant amongst major privatized utilities, for instance Tenaga Nasional Berhad and Malaysian Airlines [1]. The Malaysian government is able to influence on the strategic industries of some Government Linked Corporations (GLCs) using Golden share [12]. This share is directs by the Ministry of Finance’s investment organization (MOF Inc.). Golden share are typically own by government, given it veto power in major decision of the company or privilege to select board of director, right to speak at general assembly meeting and to oppose any decision made by the board of directors that conflicts with the government policies [21] . The same view is documented by [11] that golden share uses in order to improve control on many affiliated firms with small stake of real investment. For instance, Tenaga Nasional Berhad issue golden share with privilege to select board of director of the company, but not more than 6 directors in each time. In addition, the holder of special shares in Telekom Malaysia Berhad have the concession to issue additional shares which carry more than one voting rights or substantial disposal of firm assets and the decisions relate to merger and takeover as shows in the figure 3.

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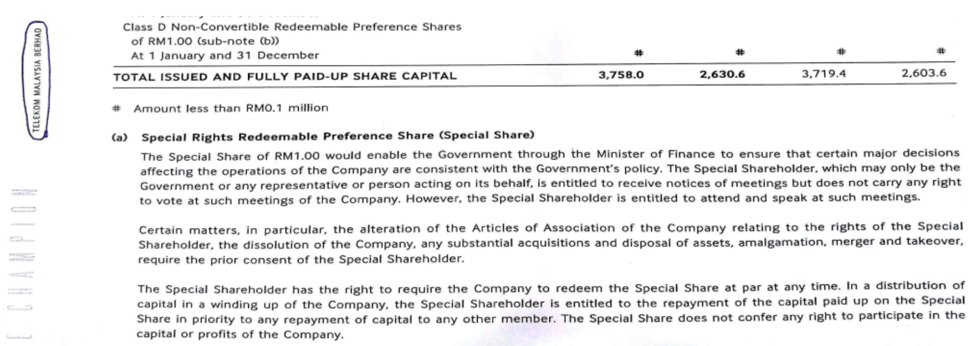

Class D Non-Convertible Redeemable Preference Shares of RM1.00 (sub-note (b)) At 1 January and 31 December	#	#	#	#
TOTAL ISSUED AND FULLY PAID-UP SHARE CAPITAL	**3,758.0**	**2,630.6**	3,719.4	2,603.6

\# Amount less than RM0.1 million

(a) Special Rights Redeemable Preference Share (Special Share)

The Special Share of RM1.00 would enable the Government through the Minister of Finance to ensure that certain major decisions affecting the operations of the Company are consistent with the Government's policy. The Special Shareholder, which may only be the Government or any representative or person acting on its behalf, is entitled to receive notices of meetings but does not carry any right to vote at such meetings of the Company. However, the Special Shareholder is entitled to attend and speak at such meetings.

Certain matters, in particular, the alteration of the Articles of Association of the Company relating to the rights of the Special Shareholder, the dissolution of the Company, any substantial acquisitions and disposal of assets, amalgamation, merger and takeover, require the prior consent of the Special Shareholder.

The Special Shareholder has the right to require the Company to redeem the Special Share at par at any time. In a distribution of capital in a winding up of the Company, the Special Shareholder is entitled to the repayment of the capital paid up on the Special Share in priority to any repayment of capital to any other member. The Special Share does not confer any right to participate in the capital or profits of the Company.

Figure 3: Wedge using golden shares
Source: Annual report of Telekom Malaysia Berhad 2015

3. Research design

3.1 Sample and data collection

The population of this study is limited to the top 100 firms listed in BM as obtained from the Bursa website as at 31 December 2015. The period covered is 2015 including financial and non-financial firms. This study uses the data stream in order to collect firms' total assets. In order to determine the top 100 firms this study arrange firms from bigger to smaller size of firms total assets. This work sought to illustrates the extent to which the top 100 firms listed in BM for the year-end 2015 used wedge. In order to get wedge data this study uses BM website and firms' annual reports. Financial institution for instance financial intermediaries, insurance companies and banks are about 21% of the top 100 firms listed in BM. firms classified within trade and services sector are about 30% per cent. Plantation, consumer products and IPC are about (8%, 7%, 2%) respectively. Construction firms are about 14% of the top 100 firms listed in BM. The remaining industry product, construction and REITS are about (7%, 5%, 6%) respectively.

4. Data analysis and results

Figure 4 shows the statistic descriptive of ownership structure of the top 100 firms listed in BM. The Malaysian pyramidal firms are about 85% of the top 100 firms listed in BM. They are using wedge to deviate between CFRs and CRs. Firms using golden shares are about 5% of the top 100 firms listed in BM. While non-pyramidal firms listed within the top 100 firms in BM are about 10%. Non-pyramidal firms dose not practice any kinds of separation between CFRs and CRs. The bar graph in Figure 5 display the sectorial concentration of wedge (pyramidal, Non-pyramidal and golden shares) practiced by the top 100 firms listed in BM in 2015. The prevalent ownership structure to divergence between CFRs and CRs is pyramidal ownership, with 21%, 22%, 13% of firms working in the finance, trade and services and properties respectively. While Non-pyramidal ownership structure is about 3%, 2%, 2% of firms working in the trade and services, consumer products and construction respectively. Firms using golden shares own by government are about 5% of the top 100 firms listed in BM and that classified within trade and services sector.

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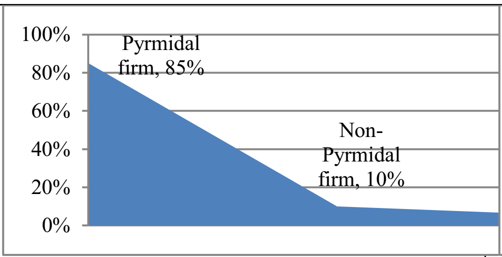

Figure 4 Control-ownership patterns in the top 100 listed firms in BI
Source: authorial computation

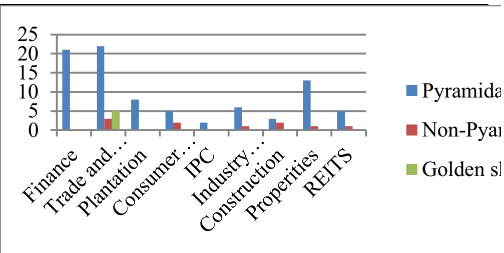

Figure 5 sectorial distribution of wedge
Source: authorial computation

5. Conclusion

This paper illustrates the ownership-control structure of the top 100 firms listed in BM using pyramidal structure and golden shares. The majority of listed firms are family own firms, these families control on many affiliated firms using pyramidal ownership structure. Thus, the insider system is the most common structure in the Malaysian capital market, and this increase insider wealth. The controlling shareholders utilize wedge mechanism to separate between CFRs and CRs. This assists controlling shareholders to control on many affiliated firms with small stake of real investment. Whereas, golden shares allow government to direct firms' strategic decisions for instance, nominate the board directors. Previous literature reports that wedge improve controller incentive and ability to maximize their interest at the expenses of minority shareholders and this kind of agency conflicts known as Type II Agency Problem [5, 10]. This study recommends regulator and policy maker to operationalize and introduce new measurement of corporate governance in order to offer a protected environment for minority shareholders. For instance blocking minority position through some policies that allow minority shareholders to recall for general assembly meeting (challenging management manipulation), participate in firm's decision making particularly that's relate to dividend policy and selecting independent directors.

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