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The effects of corporate governance features on stock price in the companies of Tehran Stock Exchange

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Abstract: Main purpose of the research is studying the effects of corporate features on stock price in the companies operating in Tehran Stock Exchange. Corporate governance properties consist of ownership concentration, institutional ownership, managerial ownership, governmental ownership, CEO duality, independence of managers, size of board of directors and auditing quality. Statistical population of the research is all accepted companies in Tehran Stock Exchange. Obtained data from 136 companies from 2007 to 2012 were used. From standpoint of goal, the research is an applied research and in terms of data collection method, the research is a quasi – experimental research. The results of the research indicated that there is a significant relationship between the variables of ownership centralization, institutional ownership, managerial ownership, independence of managers and auditing quality and stock prince at 5% error level and there is not a significant relationship between banking ownership, governmental ownership, CEO duality and size of board of directors and stock price at 5% error level.

Key words: Ownership centralization; Institutional ownership; Managerial ownership; Banking ownership; Governmental ownership; CEO duality; Independence of managers; Size of board of directors; Auditing quality; Stock price

1. Introduction

After scandals of Enron and WorldCom in 2002, many researches have been conducted in regard of corporate governance (Bai et al., 2004). Some researchers believed that the bankruptcy of these big companies resulted from weakness in corporate governance. One of the best corporate governance mechanisms for reducing interest conflict between managers and owners is to use high – quality independent auditors (Hassas and Yeganeh, 2005). Corporate governance consists of a set of relations among shareholders, managers, auditors and other beneficiaries which guarantees to establish a control system for observing minor shareholders rights, implementation correctly of decisions of the assembly and prevention from possible misuses (Gompers et al., 2003; Brown and Caylor, 2006). Also, the goals of accounting and financial reporting have been rooted from information needs of ex-organizational users. Main purpose of financial reporting is to express financial condition and the performance of business unit for users out of business unit to help them for taking financial decisions. Main tool of information transfer to the users is main financial statements and attached notes to these statements which are considered as final product of financial reporting and accounting process. The research tries to study the effects of corporate governance features on stock price in the companies listed on Tehran Stock Exchange.

2. Theoretical framework

2.1. Corporate governance

Different definitions have been provided in regard of corporate governance which some of them are mentioned briefly in the following:

- Corporate governance consists of applied methods and responsibilities by board of directors with goal of determining strategic path to guarantees achieved goals, control of risks and consumption responsible usage of resources.
- According to Corton et al. (1995) in Belgium, corporate governance is a set of the rules governing on direction and control of the company.
- Process monitoring and control to ensure that the director of the company is in accordance with the interests of shareholders.
- International Monetary Fund (IMF) and the organization for Economic Cooperation and Development (OECD) in 2001, defined corporate governance as: a structure of relations and responsibilities among a main group including shareholders, members of board of directors and CEO to promote better competitive performance for achieving initial objectives of participation.
- Corporate governance describes internal arrangements, power structure of the company and how to conduct duties.

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- Board of directors, ownership structure of the company and mutual relations among shareholders and other beneficiaries, especially human forces and creditors pay attention to it.

2.2. Concentration of ownership

It is referred to a mode that a significant amount of shares belong to major shareholders and indicates that what percentage of the company's shares is in the hands of a limited number. In other words, ownership concentration refers to the distribution of shares among shareholders. There is a negative relationship between number of shareholders and ownership concentration. This variable is calculated via referring to attached notes of financial statements and indicating what percentage is there major shareholders higher than 5 percent.

2.3. Institutional ownership

Institutional shareholders consist of banks, financial institutions, holding companies, organizations, entities and state companies. In another words, a company with institutional ownership is referred to a company which its biggest owners are banks, insurances, investment companies, social security organization, Sepah cooperative fund, Sadiq community and pension fund. The variable is calculated via referring to notes of financial statements and summing what percentage of share is belonged to institutional shareholders.

2.4. Managerial ownership

Managerial ownership indicates amount of shares held by members of management board. Jenson and Mac Ling (1976) believed that managerial ownership in its share contributes to line up interests of shareholders and managers. The issue leads to reduce conflict among managers and shareholders and managers try to company' interests are in accordance with shareholders' benefits. Even if managers have much more ownership, it may take more effort to improve company performance (Jenson and Macling, 1976). The variable is calculated through ownership percentage of managers in capital structure of the company and of total share held by managers divided total numbers of share.

2.5. Governmental ownership

A company with governmental ownership is referred to a company which more than 50 percentages of its shares is belonged to the state, private organization and martyr foundation. The variable is calculated via shares held by state organizations and entities divided by total share.

2.6. Bank ownership

It consists of share held by banks and financial institutes and is calculated total share held by banks and financial institutes divided by total shares.

2.7. CEO duality

If CEO is both chairman and vice of chairman, simultaneously, the situation is called as CEO duality. If CEO of a company is both chairman and vice of chairman, dummy variable is 1, otherwise 0. The variable in the research of Mat Nor. F and Sulong (2010) and Aghae et al. (2009) was used with same definition.

2.8. Audit quality

One of the most common definitions in regard of audit quality has been provided by DeAngelo (1971). He defined audit quality as market valuation of the probability that the auditor 1) discovers important misstatements in financial statements and or accounting system of employer 2) reports discovered misstatements. The possibility of discovering important misstatements by auditor will depend on the auditor's competency and the possibility of reporting important misstatements by auditor will depend on auditor's independency. Audit quality has been defined as a nominal variable, while if a firm is an auditing firm; it is 1, otherwise 0.

3. Research background

Ebrahim and Samad (2011) studied representative cost, mechanisms of corporate governance and performance of the companies in Malaysian Stock Exchange from 1999 to 2005. The variables of performance consist of return on assts and Tobin' Q ratio. The results of the research indicated that market value of family companies is lesser than other companies. There is a significant relationship between size of board of directors, managers' independency, CEO duality and performance in family companies. Also, the results indicated that corporate governance variables have not effect on representative cost.

Citaak et al. (2012) studied there is a significant relationship between corporate governance and value – oriented financial performance criteria or not. They conducted the research in Turkish Stock Exchange from 1998 to 2007. 41 companies were selected. The results indicated that CEO duality has significant effects on economic added value and market added value criteria and there is not a significant relationship between concentration of ownership and market added value and between managerial ownership and financial criteria and finally foreign investors lead to increase economic added value and reduce market added value. Priya and Shanmughan studied the relationship between foreign ownership structure and company performance using 425 Indian companies from 2003 to 2009 and tested can existing differences in ownership structure of companies explain their differences in performance in a developing country such as India or not? Tobin Q indicator was used to measure company performance. The results indicated that there is a positive relationship between the companies with foreign ownership and performance.

4. Research method

The research is a post – event and applied research and because the data has been collected without researcher' intervention, the research is a quasi – experimental research. According to the analysis, the relationship between variables is from type of correlation. Eviews and Excel applications were used for calculating and preparing data to needed information for researcher.

5. Empirical results

5.1. Descriptive statistics of quantitative variables

Descriptive Statistics of Quantitative Variables have been provided in this section. Descriptive statistics consist of average, mean, maximum, minimum and standard deviation. Because stock price is estimated by stock price at the end of year divided by stock price at the beginning year, the results of average stock price indicate that stock prince has experienced a 6 % increase than early year. Average of concentration of ownership is 74%, institutional ownership, 39%; managerial ownership, 65%, bank ownership, 32 and the average of governmental ownership is 13 percent.

The average of managers' independency is 27 percent that indicates about a quarter of the managers had been non – aligned during the research. Leverage ratios indicated that about 68% of assets are composed of debts and the companies have used debt for financing. Sales growth rate was 6% that indicates average sales growth in the period of investigation has been positive.

Table 1: Descriptive statistics of variables

Description	Average	Mean	Maximum	Minimum	Standard deviation
P	1.06	0.94	5.57	0.02	0.61
CONS	0.74	0.8	1	0	0.2
INS	0.39	0.29	1	0	0.35
MANAGE	0.65	0.71	1	0	0.27
GOVERN	0.13	0	0.99	0	0.22
BANK	0.32	0.09	1	0	0.35
INDEP	0.27	0	1	0	0.32
BSIZE	0.71	0.69	1	0.69	0.04
SIZE	5.76	5.75	8	4	0.39
LEV	0.68	0.66	3.69	0.09	0.34
GROWTH	0.06	0.11	0.78	-0.29	0.32

Source: researcher's calculations

5.2. Descriptive statistics of qualitative variables

Descriptive Statistics of Qualitative Variables have been provided in this section. Descriptive statistics consist of average, mean, maximum, minimum and standard deviation. The results indicate that about one-fifth of managers had been chairman during the research and also about one-fourth of the companies had been audited by auditing firms during the research.

Table 2: Descriptive statistics of variables

Description	Average	Mean	Maximum	Minimum	Standard deviation
DUAL	0.19	0	1	0	0.39
AUD	0.24	0	1	0	0.43

Source: researcher's calculations

6. Test of Hypotheses

First Sub – Hypothesis: there is a significant relationship between ownership concentration and stock price

According to the results in Table 3, F-statistics and significance level indicate a significant model for testing the hypotheses. The results of Watson – Durbin test indicate that there is not an autocorrelation between (Disrupting sentences) (it should be between 1.5 and 2.5). The results show that the coefficient of ownership concentration is 4 percent and positive and its T-statistics equals with 3.46. Because absolute amount of T-statistics is bigger than 2 and significance level is lesser than 5% (error level is 5% in the research), it can be said that there is a significant relationship between ownership concentration and stock price.

Second Sub – Hypothesis: there is a significant relationship between institutional ownership and stock price.

Following results indicate that the coefficient of institutional ownership is 2 percent and positive and its T-statistics equals with 4.53 and because absolute amount of T-statistics is bigger than 2 and significance level is lesser than 5%, it can be mentioned that there is a significant relationship between institutional ownership and stock price.

Third Sub – Hypothesis: there is a significant relationship between managerial ownership and stock price.

Following results indicate that the coefficient of managerial ownership is 4 percent and positive and its T-statistics equals with 3.59 and because absolute amount of T-statistics is bigger than 2 and significance level is lesser than 5%, it can be mentioned that there is a significant relationship between managerial ownership and stock price.

Fourth Sub – Hypothesis: there is a significant relationship between governmental ownership and stock price.

Following results indicate that the coefficient of governmental ownership is 8 percent and negative and its T-statistics equals with 1.74 and because absolute amount of T-statistics is lesser than 2 and significance level is bigger than 5%, it can be mentioned that there is not a significant relationship between institutional ownership and stock price.

Fifth Sub – Hypothesis: there is a significant relationship between bank ownership and stock price.

Following results indicate that the coefficient of bank ownership is 5 percent and negative and its T-statistics equals with 1.76 and because absolute amount of T-statistics is lesser than 2 and significance level is bigger than 5%, it can be mentioned that there is not a significant relationship between bank ownership and stock price.

Sixth Sub – Hypothesis: there is a significant relationship between managers' independency and stock price.

Following results indicate that the coefficient of managers' independency is 3 percent and positive and its T-statistics equals with 5.77 and because absolute amount of T-statistics is bigger than 2 and significance level is lesser than 5%, it can be mentioned that there is a significant relationship between managers' independency and stock price.

Seventh Sub – Hypothesis: there is a significant relationship between the sizes of board of directors.

Following results indicate that the coefficient of size of board of director is 6 percent and positive and its T-statistics equals with 0.22 and because absolute amount of T-statistics is bigger than 2 and significance level is lesser than 5%, it can be mentioned that there is a significant relationship between size of board of director and stock price.

Eighth Sub – Hypothesis: there is a significant relationship between CEO duality and stock price.

Following results indicate that the coefficient of CEO duality is 4 percent and negative and its T-statistics equals with -1.33 and because absolute amount of T-statistics is lesser than 2 and significance level is bigger than 5%, it can be mentioned that there is not a significant relationship between CEO duality and stock price.

Ninth Sub – Hypothesis: there is a significant relationship between audit quality and stock price.

Following results indicate that the coefficient of audit quality is 8 percent and negative and its T-statistics equals with -3.03 and because absolute amount of T-statistics is lesser than 2 and significance level is bigger than 5%, it can be mentioned that there is not a significant relationship between audit quality and stock price.

Table 3: The results of hypotheses

Description	Coefficient	t-statistics	Significance level
C	1.32	5.89	0.000*
CONS	0.04	3.46	0.000*
INS	0.02	4.53	0.000*
MANAGE	0.04	3.59	0.000*
GOVERN	-0.8	-1.74	0.08
BANK	-0.05	-1.76	0.07
INDEP	0.03	5.77	0.000*
BSIZE	0.06	0.22	0.82
DUAL	-0.04	-1.33	0.18
AUD	-0.08	-3.03	0.000*
LEV	-0.02	-4.61	0.000*
GROWTH	0.14	3.98	0.000*
Adjusted R-squared		0.54	
F-statistics		14.46	
Prob (F-statistics)		0.000*	
D.W		1.98	

Significance at 5% error level
Source: researcher's calculation

7. Conclusion

The results indicate that there is a significant relationship between the variables of ownership concentration, institutional ownership, managerial ownership, managers' independency and audit quality with stock price at 5% error level and there is not a significant relationship between the variables of bank ownership, governmental ownership, CEO duality and size of board of directors at 5% error level. In this regard, Jenson and Macling

(1976) believed that the ownership of managers contribute to align shareholders' benefits and managers' interests. This leads the conflict among shareholders and managers reduce and managers strive to line up company' interests and shareholders' interest. Even if managers have more ownership, it might that they try to improve company performance. Hence the managers strive to increase their benefits via increasing stock price. Hence it is expected there is a significant relationship between managerial ownership and stock price.

In regard of significant effect of ownership concentration on stock price, it should be noted that more ownership concentration leads make hidden and undisclosed profits and opportunities for controlling shareholders. Because of high share, these owners have more control and surveillance on management decisions and its consequences. In result, they have direct effect on company performance. in regard of significant impact of managers' independency on stock price, it should be mentioned that the appearance of non – aligned managers (non – executives) in board of directors and their monitoring performance, as independent members, lead to reduce conflict for existing interests among shareholders and managers. Of course, it should be noted that executive managers play important role for constituting a proper composition from aligned and non – aligned members among board of directors. The existence of such arrangement is considered as one of main elements of an effective board of directors. While executives provide valuable information about company's activities, non – aligned mangers judge neutrally managers' decisions.

In regard of institutional ownership, it can be noted that institutional investors are regarded as another alternative solution for a strong strategic system that can monitor the management. Because they both can have significant effect on management and can line up the interests of shareholders and managers which generally it is introduced in representative theory. The importance of monitoring role of institutional investors has been promoted ever – increasingly, because they are very big and influential and meanwhile ownership concentration has been received significantly attention.

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