THE IMPACT OF MALAYSIAN GOVERNMENT-LINKED INVESTMENT COMPANIES ON THE PERFORMANCE AND EARNINGS MANAGEMENT OF THEIR PORTFOLIO COMPANIES

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ABSTRACT
This research is divided into two parts. The first part explores the impact of ownership control by different types of government organizations on the financial performance of listed companies in Malaysia. Using panel data of companies controlled by government organizations listed on Main Board of Bursa Malaysia between 2004 and 2008, we find that the impact of government control via block ownership and golden shares varies depending on the type of organization which manages the government's ownership stakes.
Government ownership is a characteristic feature of corporate governance in many emerging economies where government often invest in private companies to provide access to additional funds, to further the development of strategic firms and
industries, and to promote corporate governance by improving the supervision and control of their portfolio firms. Understanding how government control impacts on the financial performance of listed companies is of interest to (foreign) minority investors, who might either benefit from the monitoring activities by government investors or might be exploited by government investors' power to direct company resources to pursue political objectives rather than shareholder value.
Depending on the objectives of the investing government organizations and the way their representatives are motivated to pursue those objectives, government ownership and control rights are likely to influence the performance of their portfolio companies in a variety of ways, which might be beneficial or detrimental to private investors' interests. However, there is to date very little research on the effect of government ownership on private (listed) companies, which takes account of differences between sponsoring government organizations and none of them conducted in Malaysia so far.
This paper aims to contribute to our understanding whether differences in the corporate governance of government investment organizations, e.g. with regards to the means by which their representatives are incentivized and controlled, affect how government ownership impacts on the performance of private organizations in emerging market economies and, therefore, on the interests of private (minority) investors. Malaysia is a particularly interesting case to explore in this context, as the organizations, which manage government investments in private companies, so-called
Government-linked Investment Companies (GLICs), fall in three identifiably different groups, with different organizational objectives and control structures. In addition, as golden share provisions in some government-invested companies lead to a disparity between the cash-flow and control rights of GLICs, we explore whether the existence of golden shares impacts on the corporate performance of GLICs' portfolio companies, so-called Government-linked Companies (GLCs).
Moreover, whereas in developed market economies government investments in private companies are often managed at arm's length from parliament and senior politicians to avoid (party) political interference, in Malaysia, senior politicians play a key role in the management of GLICs and GLCs. While public choice theory suggests that politicians might abuse their position to seek private or political benefits by being able to differentiate between different types of GLICs, this paper explores, from a principal-agent and property rights perspective, whether the influence of senior civil servants and politicians via government investment companies differs depending on the organizations' objectives and control structures and whether the differences affects their financial performance.
This paper suggests that in Malaysia the impact of government ownership on the performance of listed companies is affected by the objectives and corporate governance of the investing government organisation. This finding

highlights the importance to consider more closely corporate governance systems of government investment organizations. Given the prevalence of GLC type companies in the stock
markets of many emerging economies, this issue is of importance both to (foreign) minority investors and to government agencies which aim to encourage foreign investment.
One of the major discoveries that are found in the first study above is on the impact of ownership on performance. Measuring corporate performance using accounting measure (return on assets and market performance data (quasi-Tobin's Q), the research showed consistent results. However, the impact of different GLICs on their portfolio firms' performance appeared much more pronounced when performance was measured with accounting performance data rather than market performance data.
One potential reason for this might be that capital market participants discount accounting information published by GLCs as they might be perceived to be more prone to misstate their accounts in order to manipulate the public's perception on their performance. This raised the question whether GLCs with different types of controlling GLIC owners engage more or less in earnings management, and, more generally, whether GLCs engage more or less in earnings management than firms which are not controlled by government investors.
Against this background, further empirical evidence is therefore desirable to shed more light on the impact of government block ownership (GLICs), private blockholder and managerial ownership on earnings management behaviour. Based on
sample of 2696 firm-year observations between 2004 and 2008 (for the second project
– ownership vs earnings management), we found that the magnitude of earnings management activities in the listed companies control by private blockholders more pronounced than the listed firms control by GLICs. We also compare the effects of shareholding by management and shareholding by blockholders on earnings management activities and found that the shareholding by management indeed leads to earnings management in firms rather than shareholding by blockholders
Generally, this study provides evidence on the influence of different type of government sponsoring organizations on corporate performance and earnings management of their portfolio companies from an emerging market viewpoint. In addition, we also take into account the shareholdings by private blockholders and management as their impact on earnings management activities. The findings from this study is particularly important to the foreign investors, who might either benefit from the presence of blockholders or might be exploited by their power to manipulate earnings to pursue self-interest objectives rather than shareholder's value. Considering that there is a difference in terms of institutional setting and governance structure between developed and emerging markets (Leuz et al., 2003), this research might leads to different results from those found in developed markets.