Ownership Dynamics, Capital Structure, and Agency Costs: Impact on Firm Performance in India

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Abstract

The Indian corporate landscape faces unique challenges related to ownership structure, notably due to high concentrated ownership, stringent debt markets, and overlooked agency issues between owners and managers. This study investigates the critical threshold of shareholding where the interests of promoters and non-promoters align with firm performance, independent of debt and agency costs. Utilizing fixed effects (FE) panel models, we analyze a comprehensive sample of 306 firms listed in the BSE 500 from 2013 to 2022. To address endogeneity concerns, we also employ generalized method of moments (GMM) estimations. We classify shareholding into four ranges: (1) less than 25%, (2) between 25% and 50%, (3) between 50% and 75%, and (4) more than 75% to identify the threshold of shareholding where interests align and impact firm performance. Our findings reveal that all the categories of shareholding held by Indian promoters, foreign promoters, institutional non-promoters, and non-institutional non-promoters positively and significantly influence firm performance represented by ROA, ROE and Tobins Q regardless of debt levels and agency costs. Particularly, promoter ownership within the critical range of 50-75% aligns the interests of both promoters and non-promoters, enhancing firm value. Conversely, firms with less than 25% promoter ownership experience detrimental effects on firm value, while those with promoter ownership exceeding 75% show no significant enhancement. Additionally, we present meta data and sub sample analysis that elucidates the intricate relationship between ownership concentration and firm performance in India, offering recommendations for policymakers to maintain promoter shareholding within the optimal range of 50–75%.

Keywords: Corporate Governance; GMM estimations; Institutional Investors; Meta Data; Shareholding Patterns