

Ownership Concentration and Executive Compensation in Closely Held Firms: Evidence from Hong Kong

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Summary

Firms with concentrated ownership may be subject to agency costs arising from conflicts of interest between majority and minority shareholders. The focus of our paper is the extent to which ownership concentration affects executive compensation, since owner-managers effectively decide on their own compensation. We analyze a sample of 412 publicly traded Hong Kong firms during the period 1995-1998. Hong Kong combines an Asian family-controlled business environment, characterized by high family ownership of listed corporations, and an Anglo-Saxon legal and corporate governance system. Our principal result is that in small market-capitalization firms, there is a positive relationship between managerial ownership and the cash emoluments received by the CEO and the Chairman, for levels of ownership of up to 25 percent, while in large market-capitalization firms the relationship holds only for up to 5 percent ownership. Furthermore, we find no sensitivity of executive compensation to firm performance for small firms. These findings may indicate that in the presence of information asymmetry between owners-managers and outside investors (which is more likely in small firms) the former may use their ownership rights to extract higher salaries for themselves. Finally, with the exception of boards having an audit committee, we find that boards of directors are not sufficiently strong to limit managerial compensation, despite the mandatory introduction of independent non-executive directors.