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Research Paper

The Effect of Ownership Structure on The Relationship Between Liquidity and Company Value[1]

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INTRODUCTION AND OBJECTIVE

In a series of papers, Amihud and Mendelson (1988, 1991, 2000, 2008) advocate that firms can and should actively pursue corporate policies aimed at increasing the liquidity of their publicly traded shares. The incentive is that improved liquidity leads to a lower cost of equity capital and higher stock price, which increases the market value of the firm (Chia, et al. 2020). Evidence from Fang et al. (2009) shows that companies have a positive effect on firm value through strategies to increase liquidity, including stock price information channels and stock-based management rewards. Although these authors outline five positive theoretical channels (liquidity premium, sentiment, positive feedback, pay-for-performance sensitivity, and block holder intervention), they also highlight two negative mechanisms (activist exit and negative feedback) through which liquidity might reduce firm value. In practice, maintaining liquidity is not a costless effort, and thus corporate managers must often weigh the tradeoff between potential costs and the well-reported valuation premium. For instance, Amihud and Mendelson (2000, 2008) highlight the direct costs incurred when providing more information to investors and expanding the investor base, and their

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indirect effects on firms' competitive advantage and agency costs, respectively. While the negative channels are not dominant in developed markets, the same cannot be expected for emerging stock exchanges due to differences in an institutional setting, regulatory framework, level of information efficiency, shareholder activism, and investor sophistication. According to different theories and different and sometimes contradictory results that previous research has presented and given the countervailing positive and negative effects, as predicted by competing theoretical models, there is expected to be a non-linear relationship between liquidity and firm value. Also, research has shown that company owners, through the corporate governance channel and stock price information, affect the relationship between liquidity and company value, and given the possibility of feedback effects from stock prices to firms' real investment decisions (Chia, et al. 2020). According to the above discussion, the purpose of this study is to study the effect of ownership structure on the relationship between liquidity and the value of companies listed on the Tehran Stock Exchange. Given the purpose, this study seeks to answer the question of whether there is a relationship between liquidity and company value? Also, does corporate governance have a significant effect on the relationship between liquidity and firm value?

MATERIALS AND METHODS

The sample consists of all companies listed on the Tehran Stock Exchange that have been active in the stock exchange between 1393 to 1399. In selecting the companies, the following conditions have been considered: to control the time effect and to increase the comparability, the end of the fiscal year of the studied companies should lead to the end of March in each year; to homogenize the statistical population, companies did not change the financial year during the research period; some listed companies include banks and financial institutions (investment companies, financial intermediaries, holding companies, banks, and leasing companies) in which the financial disclosures and structures of the company's governing principles are different, are deleted; for companies' shares to be fluid, and as a result, stock prices and returns to be reliable, and for better comparison, companies should not have a trading interval of more than three months; the necessary data in the research period should be fully available. The 125 companies that met the above conditions were selected to test the research hypotheses. After collecting the data, Excel software was used to summarize and calculate. Then, the final analysis was performed by multivariate regression patterns using Eviews software.

RESULTS AND DISCUSSION

The results of testing the hypotheses showed that there is a significant nonlinear (U-shaped) relationship between stock liquidity and corporate value. This finding means that at the basic levels of liquidity (before the threshold point of 2.194), there is a negative and significant relationship between liquidity and the value of companies. However, at levels above the baseline level of liquidity, there is a positive and significant relationship between liquidity and the value of companies. Also, institutional shareholders, real shareholders, and the largest shareholder have a moderating (inverse U) effect on the nonlinear relationship between liquidity and firm value. Findings from the inverted U-curve show that, before the threshold point, a higher percentage of liquidity is associated with a higher firm value. However, when the liquidity base exceeds a certain threshold level and becomes too large, the value of the company decreases.

CONCLUSION AND SUGGESTIONS

The nonlinear (U-shaped) relationship between stock liquidity and corporate value shows that after the threshold point, enhanced liquidity leads to a lower cost of equity and higher stock prices and, consequently, increases the market value of the firm. But before the threshold point, this relationship becomes negative. The results also showed that stocks with higher institutional owners, higher real owners, and shares of the largest shareholder should have a relatively lower level of liquidity (before the threshold of 3.176 for institutional owners, 3.662 for real owners, and 2.988 for the largest shareholder) to be traded to increase the value of the company. This indicates the dominance of information competition and the costs of incorrect selection on all sides of the threshold. Regarding the experimental comparison of the evidence obtained from this study with other studies, it should be said that these results are fully consistent with previous studies such as Chia et al. (2020). To justify these findings, it should be noted that the nonlinear relationship not only challenges the existing view that "more is better", but rather, it recommends a maximum level of liquidity threshold beyond which the firm's value will increase or decrease. Therefore, the managers of companies listed on the stock exchange can provide the grounds for the growth and development of the company by managing their company's share liquidity. Also, the capital market officials of the country can make policies and legislations by considering the threshold levels introduced in this research.

Keywords: Institutional Shareholder, Largest Shareholder, Ownership Structure, Real Shareholder, Stock Liquidity.

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