State control can result in good performance for firms

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Following the breakup of the Soviet Union and its Eastern Bloc many researchers anticipated the demise of state-owned enterprises (SOEs). The privatization movement throughout the world since the 1980s suggested that SOEs may simply have been a transitional organizational form destined to become a relic of history. However, even to this day, SOEs still generate approximately 10 percent of world GDP and represent about 20 percent of the global equity market. Their presence and relevance is particularly important in countries from Asia to Latin America and Africa, where they provide around 15 percent of GDP.

We argue that SOEs survived and in some cases thrived because they adapted and have become a type of hybrid organisation. Today's SOEs are unlike their inefficient predecessors of the previous century in that they have created a mixed ownership of state and private ownership. The level of actual government control also varies, at times independently of the level of government shareholding. As such, we find SOEs such as Brazil's Petrobras with a high level of ownership yet a low level of government control, and conversely others such as Energias de Portugal with relatively low government ownership but high level of government control. SOE goals may differ from private firms by having a lower focus on maximizing profits, instead concentrating on increasing market share or employment levels. Therefore, SOEs will behave, and are managed differently than private firms.

Looking at the top academic management journals included in the *Financial Times* list of the top 45 journals for business schools over a 15 year period ending in 2014, we found that out of thousands of articles published only 39 (2.6/year) focused on the management of SOEs. While a vast majority of articles took a dichotomous view of SOEs, most researchers disagreed on the impact of ownership on firm performance. For example, Ralston and colleagues (2006) reported that Chinese managers perceived SOEs to be more competitive that private firms, while Goldeng and colleagues (2008) found that private firms in Norway outperformed SOEs. In addition, a majority (30 out of 39) of articles are focused on Chinese SOEs, and they make a very limited attempt to address whether their findings are relevant elsewhere. Thus, the existing research views state ownership as all or nothing, that is, an organization is either state-owned or not, and if state-owned, its management will fall under state control. We argue for a hybrid model where the state can own a proportion of a firm and exercise varying levels of control.

The limited focus on SOE research may partly stem from the framing of the discussion as socialism versus capitalism, thus making it difficult for Western scholars to highlight the merits of SOEs, resulting in an almost article of faith that SOEs are less efficient than private firms. Thus, employing a comparative case analysis of 36 state firms from 23 countries in four industry sectors — natural resources/energy, transportation, manufacturing, and finance — we provide a fuller understanding of the current hybrid state firms. We highlighted the hybrid nature of SOEs through a 3 x 3 matrix that emphasises the varying levels of government ownership and control respectively.

According to existing research, higher state control can hurt firm performance owing to its association with soft budget constraints, where the state will provide support to firms generating chronic losses, eliminate bankruptcy and minimize the need for restructuring. However, our analysis suggests that state control, whether associated with state ownership or not, can also result in good performance. We found that the highest level of ROI was present in two of the cells exhibiting the highest level of state control. Some explanations include government subsidies, which can be significant, such as free land, or soft budget constraints in terms of longer term outlook. We also noticed that as the economic or strategic importance of a firm's products increases so does the level of government control, even when lacking high levels of ownership.

To expand the insight we looked at the CEO's background; specifically we examine whether they come from either the government or have only worked in the SOE sector on the one hand, or whether they have worked in the private sector on the other. Given that the goal of most governments is job creation and stability, not necessarily economic efficiency, a CEO with government/SOE background is likely to exhibit a mindset that focuses on job maintenance and operations rather than firm efficiency or strategic orientation. We found that CEOs of firms where the state exhibited a low level of control almost always came from private industry, while conversely, in SOEs with high government control the CEOs came from the government/ SOE sector, where the focus may be on social concerns rather than economic performance. The goals of the latter CEO is consistent with the state's, pushing the SOE toward production maximization as opposed to innovation and ROI. CEOs coming from private industry have more skills and experience to reshape SOEs to be more market oriented and innovative.

Overall, rather than state ownership disappearing, the future appears to offer continued use of this hybrid organizational form. Managers and scholars both need to build a greater recognition and understanding of hybrid SOEs.

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Notes:

- *This post is based on the authors' paper* State-owned Enterprises Around the WORLD as Hybrid Organizations Academy of Management Perspectives, *February 1, 2015 vol. 29 no. 1 92-114*
- *This post gives the views of its author, not the position of LSE Business Review or the London School of Economics.*
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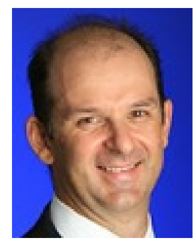
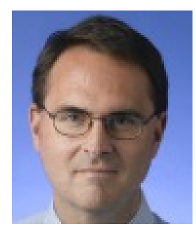
Ciprian Stan is an Assistant Professor in the College of Business at Florida Atlantic University. He received his Ph.D. from the University of Texas at Dallas. His research interests include state-owned enterprises, CEO compensation and slack resources.



David Ahlstrom is a professor at The Chinese University of Hong Kong. He obtained his PhD in Management and International Business from New York University after working several years in government and industry in the U.S., including the data communications field. He has lived in Hong Kong for over 20 years. His research interests include managing in Asia, innovation and entrepreneurship, and influence and leadership. Professor Ahlstrom was Chief Editor of *Asia Pacific Journal of Management* for several years and is now a Senior Editor of *Journal of World Business*.



Mike W. Peng is the Jindal Chair of Global Strategy at the Jindal School of Management, University of Texas at Dallas.

Kehan Xu is a Research Fellow of ARC Research Hub for Australian Steel Manufacturing, Faculty of Engineering and Information Sciences, at University of Wollongong, Australia. He received his Ph.D. from Texas A&M University and an MBA from the University of Miami. His research interests include delegation, innovation, branding strategy, CEO decision-making and executive crimes. Before entering academia, Dr. Xu cofounded software ventures in Singapore and Hangzhou, China. He also served as Executive Director and CFO for a pharmaceutical manufacturer listed in the Hong Kong Stock Exchange.

Garry D. Bruton is a professor at Texas Christian University. He has published or has forthcoming over 100 academic articles in leading journals and has co-authored three text books published by McGraw-Hill and Cengage. In 2005 Professor Bruton was the first holder of the Hall Chair in Entrepreneurship in Emerging Markets offered by the Fulbright Foundation. He is currently associate editor of the *Strategic Management Journal*. Previously he was president of the Asia Academy of Management, and former editor of the *Academy of Management Perspectives.*