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Effects Of Managers' Self-Interest Motivation On Listed Company's Business Performance

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ABSTRACT-

In recent years, managers' self-interest motivation has been attracting more and more attention from both the academia and practice. Therefore, the ways and depth of managers' self-interest motivation influencing listed companies' operating performance has become a hot research area with important theoretical and practical significance. Based on the samples of A-share companies listed in Shanghai and Shenzhen stock exchange during 2012-2014, we studied different effects of managers' self-interest motivation on listed company's business performance under different situations. The innovation of this paper mainly lies in the following two points: on the one hand, we did not adopt the previous research methods which does not distinguish different kinds of company's business performance. Therefore, we divided business performance into two types firstly, then we made empirical text of the influences of managers' self-interest motivation on business performance by virtue of Hausman Model and drew related conclusions under different situations of operating performance. On the other hand, the index measuring managers' self-interest is relatively new.

***Index Terms*-Listed Company, Managers' Self-interest Motivation, Business Performance**

INTRODUCTION

The theoretical basis of managers' self-interest motivation are principal-agent theory and rational economic man hypothesis. Jensen and Meckling first proposed principal-agent theory in 1976: the different targets between managers and shareholders will inevitably lead to interest conflicts [1]. That is, when managers are entrusted by shareholders, they often tend to make decisions damaging shareholders' interests like abusing behavior of free cash flows, excessive investment behavior and so forth. Therefore, managers' self-interest behavior is essentially a form of agency problem, namely, it is an opportunistic behavior for managers to make a sacrifice of shareholders' interests when pursuing their own interests due to asymmetric information and principal-agent problem. And excessive growth and investment behavior led by managers' self-interest will have impacts on enterprise's value and management performance as well. Based on this, we selected A-share companies listed in Shanghai and Shenzhen stock exchange during 2012-2014 as samples to study different effects of managers' self-interest motivation on listed company's business performance under different levels of business performance and put forward relevant suggestions to inhibit managers' self-interest motivation, strengthen the supervision and further enhance listed company's value and operating performance at the same time.

LITERATURE REVIEW

Opler (1999) argued that managers' self-interest motivation with excessive growth and investment

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behavior will lead to the expansion of company scale, significant decline of company value and business performance [2]. Hardford (1999), Richardson (2006) found that the more free cash flows a company owns, the greater the chance of merger and acquisition will become which can't improve operating performance due to the target company may not be the best choice for the acquiring firm, and that is why there will be a decline of business performance[3-4]. Xu Xiaodong and Zhang Tianxi (2009), Liu Yinguo and Zhang Chen (2012) also drew the similar conclusion that if a company has too much free cash flows, the possibility of managers' excessive pursuit of self-interest will become more and more greater along with agent conflict and excessive investment behavior which will have an adverse effect on enterprise business performance[5-6]. Li Zengquan (2000) studied the relationship between incentive mechanism and enterprise performance through empirical research and the result showed that executive compensation is not associated with business performance, and executives' lower shareholding can't have incentive effect. Chen Xinmin and Liu Shanmin (2003) examined the relationship between managers' employment, salary structure and operating performance, and the results showed that Managers' shareholding ratio and salary structure does not have a significant correlation with operating performance. However Zhang Junrui, Zhao Jinwen and Zhang Jian (2003), Du Xingqiang and Wang Lihua (2007) drew the opposite conclusion [7-10]. Li Kai (2007) thought that managers' shareholding ratio has a positive correlation with business performance and then suggested to increase general manager stake and reduce agent cost to improve enterprise performance. Wu Yuhui and Wu Shinong (2010) found that the implementation of equity incentive has certain inhibitory effect on managers' self-interest motivation. Liao Li and Fang Fang (2004) also came to a similar conclusion, namely, the lower level of managers' shareholding will make the deviation between managers' decision and company goal become greater with the possibility of over-investment behavior [11-13]. Shu Youlin (2011) proved that executive power does not have direct impact on equity incentive, but the effects of monetary compensation incentive with greater executive power is better [14]. Jian Jianhui, Yu Zhongfu (2011) further examined the relationship between manager incentive and excessive investment behavior, and drew the conclusion that monetary compensation is positively related to excessive investment behavior while equity incentive is not significantly related to excessive investment behavior [15]. Jiang Ling (2008) further proved that there is a positive correlation between management tenure and business performance through empirical research [16].

Above all, we conclude that different research angles, data and indicators selection will lead to different conclusions. But they all reached an agreement that managers' self-interest motive is essentially a form of agency conflicts influencing company's business performance.

RESEARCH DESIGN

A. HYPOTHESES

Generally speaking, compared to the listed companies with poor operating performance, the corporate governance structure of the listed companies with good business performance is better with certain inhibitory effect on managers' self-interest behavior. Qin Xingjun and Li Liang (2014), and Li Liang (2013) concluded that free cash flows in listed companies with a high level of corporate governance is significantly higher than the low level one during the research of influences of corporate governance on managers' self-interest motivation and cost stickiness [17]. But when operating performance of listed companies is getting worse, managers tend not to choose the investment

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program with a negative net present value even if they own more free cash flows in order to protect their own position and interests from been infringed. Li Liang, Song Zhenkang (2013) also confirmed this point of view when they studied the influences of managers' self-interest motivation on the cost stickiness. Based on this, this article assumes that:

H1a: Listed company with good performance owns more free cash flows than the one with poor performance.

H1b: Listed company with good performance have positive correlation with free cash flows while the one with poor performance have a negative correlation.

Under the existing corporate governance mechanism, executives obtain enterprise residual income mainly through two approaches: fixed salary income and equity incentive. Kanniainen (2000) concluded that the higher the proportion of regular salary executives obtain is, the weaker of managers' self-interest motive will become [18].Executive compensation management system in listed companies with good performance is relatively stable with a higher level of fixed monetary salary. Therefore, fixed monetary compensation can't play a good incentive role while equity incentive can improve executives' enthusiasm to a certain extent leading to the emergence of executives' self-interest motives at the same time. On this basis, this article assumes that:

H2a: The relationship between fixed monetary compensation and operating performance in listed company with good performance is not significant.

H2b: The relationship between fixed monetary compensation and operating performance in listed company with poor performance is significant positive correlated.

All managers do hope to work in a company with better performance, establish influences during their tenure, and then be more likely to be superior to other internal supervision mechanism showing obvious self-interest motive. Phan Hill (1991) found in his study that managers are more likely to expand company scale and optimize remuneration structure to increase their own interests along especially with their longer term [19].Managers work in a company with poor performance are often worried about bankruptcy risk and have no confidence in enterprises' development prospect. In other words, their security needs of Maslow's needs hierarchy are unable to meet, therefore, even if company's performance has improved, management tenure won't get longer. Thus, we put forward hypothesis as follows:

H3a: Management tenure has a positive correlation with operating performance in the listed company with good performance.

H3b: Management tenure has a negative correlation with operating performance in the listed company with poor performance.

Boyd (1984) argued that when the chairman of the board also hold the post of the CEO in a company at the same time taking responsibilities of both decision-making and supervision, it is more easily for the chairman/CEO to make a sacrifice of shareholders' interests with obvious self-interest motive. Tian Zhilong (1998), Xu Erming and Wang Zhihui (2000) also get similar conclusions, holding a concurrent post has a higher negative impacts than its positive impacts and provide the possibility for managers and the chairman to pursue personal gain which is not conductive to the enterprises' long-term development [20-22].And that is the reason why China Securities Regulatory Commission regard authority separation between the chairman of the board and managers as one of the most important measures to improve corporate governance. On this basis, this article assumes that:

H4a: Authority separation between the chairman and managers can improve company's operating performance.

H4b: Authority separation between the chairman

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and managers in the listed company with good performance is positively correlated with operating performance.

B. VARIABLE SELECTION AND DEFINITION

This paper mainly choose ROE (rate of return on common stockholders' equity), ROA (return on total assets), net profit margin, quick ratio, current ratio, asset-liability ratio, total assets growth rate, increase rate of main business revenue, net profit growth rate, primary earnings per share and operating cash flow ratio as 11 indexes and measure operating performance by virtue of principal component analysis according to the research purpose,. Variable selection and definition are shown in Table I and Table II.

C. MODEL BUILDING

The following model is set up for the regression test of influences of managers' self-interest motivation on business performance under different level of performance.

$$GX=\beta_0+\beta_1 FCF+\beta_2 MFP+\beta_3 MT+\beta_4 Power+\beta_5 TobinQ+\beta_6 Size+\beta_7 Industry+\varepsilon$$

In this model, β_0 is a constant term and β_i（i=1,2,……，7）is the coefficient of each explanatory variable. As above, explanatory variables includes free cash flows, executive compensation structure, management tenure and authority separation while operating performance as the explained variable and company size, Tobin Q and industry variables as control variables. Then we studied the relationship between each explanatory variable and listed company operating performance.

TABLE I : INITIAL VARIABLES OF BUSINESS PERFORMANCE

Variable Name	Calculation Method
ROE(X_1)	ROE=Net Profit / Shareholder's Equity
ROA(X_2)	ROA= Earnings Before Interest and Tax /Total Assets
Net Profit Margin(X_3)	Net Profit Margin = Net profit/Sales Revenue
Quick Ratio(X_4)	Quick Ratio =（Monetary Fund+ Transactional Financial Assets+ All Kinds of Accounts Receivable)/Current Liabilities
Asset-liability Ratio(X_5)	Asset-liability Ratio = Total Debt/Total Assets
Current Ratio(X6)	Current Ratio = Current Assets/Current Liabilities
Total Assets Growth Rate(X_7)	Total Assets Growth Rate =(Total Assets of This Year- Total Assets of Last Year)/ Total Assets of Last Year
Increase Rate of Main Business Revenue(X_8)	Increase Rate of Main Business Revenue =(Current Operating Income-Operating Income of Previous Period)/ Operating Income of Previous Period
Net Profit Growth Rate(X_9)	Net Profit Growth Rate =(Net Profit of This Year - Net Profit of Last Year)/ Net Profit of Last Year
Primary Earnings Per Share(X_{10})	Primary Earnings Per Share = Net Profit / Weighted Average of Common Shares
Operating Cash Flow Ratio(X_{11})	Operating Cash Flow Ratio =Net Operating Cash Flow / Current Liabilities

Note: Xi in parentheses is variable code.

TABLE II: VARIABLE SELECTION AND DEFINITION

Variable Type	Variable Name	Variable Definition
Dependent Variable	Operating Performance(GX)	Principal component comprehensive index of business performance by selecting top five

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		principal component comprehensive score
Independent Variable	Management Tenure(MT)	Average office term of Chairman and general manager
	Executive Compensation Structure(MFP)	Executives monetary compensation/(Executives Monetary Compensation + market price of Executives shareholding)
	Free cash flows(PCF)	(operating profit + accumulated depreciation - annual payment of taxes and fees - distribution of dividends, profit or interest paid in cash) / current assets
	Authority Separation(Power)	If the chairman of the board is also the CEO, the value is 2, if not, the value is 1.
Control Variable	Tobin Q (Tobin Q)	Market value of shares outstanding + Market value of non-tradable shares + short-term liabilities+ long-term liabilities)/total assets
	Company Size(Size)	Take the relative
	Industry Variable(Industry)	Total of 12 industry virtual variables (in addition to the financial sector) according to the classification standard of the CSRC

Note: what in parentheses is variable symbol.

D. SAMPLE SELECTION

By reason of sample data' authenticity, validity and integrity will have an important impact on regression model's estimation and testing, we try to remove the influence of abnormal samples to ensure the data validity, and we choose the financial data of A-share listed companies in Shanghai and Shenzhen stock exchange during 2012-2014 which are still operating normally until December 31, 2014 as original samples, and then selected according to the needs of our study: 1) Excluding the finance and insurance industry considering it is too special with no physical marketplaces and different accounting standards;2) Eliminate the ST and PT strands of listed companies with abnormal financial situation or continuous loss;3) Eliminate the one lacks complete financial data and other related information to guarantee the data's continuity and stability. Eventually we obtained 5919 sample firms (1562 in 2012, 2146 in 2013, 2211 in 2014). All sample data are from the CSMAR database.

EMPIRICAL RESEARCH

A. BUSINESS PERFORMANCE MEASUREMENT

Factor analysis is a kind of dimension reduction method considering the relationship between multiple variables as research objects and selects common factor among them with the basic idea of different variables are based on their correlation, and we start from the correlation matrix, divide the variables closely linked into a same category. Variables in a same category which are affected by a common factor will be highly related with each other while the correlation between different types of variables is low.

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Using statistical analysis software of SPSS17.0 to make a correlation test and analyze the 11 operating performance indicators of sample companies, and the results as shown in Table III.

TABLE III: KMO AND BARTLETT ANALYSIS

Select and measure Kaiser-Meyer-Olkin with enough depress	0.566
Sphericity test of Bartlett （Approximate chi-square）	5754.333
df	55
Sig.	0.0000

We use the KMO value which was 0.566(＞0.5) to measure the correlation among each variable, this means the business performance indicators we selected could be analyzed by principal component analysis method. The value of Bartlett test is 0.000(less than the significant level of 0.05) showing strong linear correlation between variables. Therefore, there do exist common factors in the 11 operating performance indicators to carry out factor analysis.

After KMO and Bartlett test, we performed factor analysis by virtue of statistical analysis software (SPSS17.0), then we extracted five factors from 11 original indexes according to the gravel figure shown in Table IV.

As shown in Table IV, we arranged the five extracted factors according to their contribution rate of the original index, and the contribution rate of original index is 75.706%. Specifically, the first principal component accounted for a larger proportion in quick ratio, asset-liability ratio and operating cash flow ratio respectively are 0.906, 0.806 and 0.877 with the contribution rate of 20.378% while other indicators with a small proportion; the second principal component accounted for a larger proportion in net profit margin, net profit growth rate and operating cash flow ratio respectively are 0.756,-0.632 and 0.799 with the contribution rate of 15% while other indicators with a small proportion; the third principal component accounted for a larger proportion in total assets growth rate, increase rate of main business revenue respectively are 0.887 and 0.823 with the contribution rate of 14.876% while other indicators with a small proportion; the forth principal component accounted for a larger proportion in ROA and primary earnings per share respectively are 0.762 and 0.816 with the contribution rate of 13.321% ; the fifth principal component accounted for a larger proportion in ROE respectively are -0.964 with the contribution rate of 9.455%.

After calculating the score of five factors, we weighted sum each factor according to its contribution, and finally came to a comprehensive score of sample companies' business performance, what we derived is the business performance in 2014 from the calculation steps above which can also be concluded operating performance of selected listed companies in 2012 and 2013 similarly. Then, we divided the samples into two groups according to the median of the comprehensive score: sample firms with a better business performance and others with a poor business performance which laid a foundation for the following empirical research.

TABLE IV: PRINCIPAL COMPONENT ANALYSIS AND FACTOR ANALYSIS

Evaluation Index	Components				
	1	2	3	4	5
ROE	-0.003	0.005	0.015	-0.018	-0.964
ROA	-0.003	0.037	-0.032	0.762	-0.18
Net Profit Margin	-0.015	-0.756	0.055	0.433	0.119
Quick Ratio	0.906	0.017	-0.011	0.008	-0.016
Asset-liability Ratio	0.806	0.013	0.019	-0.004	0.015

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Current Ratio	0.877	-0.029	0.012	-0.013	-0.007
Total Assets Growth Rate	0.019	0.067	0.887	0.078	0.007
Increase Rate of Main Business Revenue	-0.002	0.048	0.823	-0.073	0.021
Net Profit Growth Rate	0.017	-0.632	0.392	0.135	-0.122
Primary Earnings Per Share	-0.004	-0.172	0.047	0.816	0.165
Operating Cash Flow Ratio	-0.019	0.799	-0.106	-0.021	0.147
Eigenvalue	2.246	1.941	1.68	1.145	1.021
Variance Contribution%	20.38%	15.00%	14.88%	13.32%	9.46%
Contribution Rate of Accumulated Variance%	20.38%	35.38%	50.25%	63.58%	73.03%

B. HAUSMAN TEST AND MODEL SELECTION

The basis of fixed-effect model is individual differences, and for a specific individual, there is no time sequence difference. Under the non-significant hypothesis of individual effect, we can use F-statistics to test the hypothesis. We can reject the null hypothesis which the fixed effect is not significant, and that is why we argued that fixed-effect model is better. Compared with the random-effect model, fixed-effect model does not need to consider the individual effect and the assumption which is not related to other explanatory variables, and we regard this as the basis of model selection. The basic idea of the Hausman test is that under the original hypothesis with fixed effects and other explanatory variables which were not related, the parameter of fixed-effect model estimated by OLS and random-effect model estimated by GLS are consistent, but the former one has no validity. Under the null hypothesis, there should be no difference in the parameter estimation of the two, if we reject the null hypothesis, we will choose the fixed-effect model (the test results are shown in Table V).

TABLE V: HAUSMAN TEST AND MODEL SELECTION

	Hausman Test Results	Model Selection
Under Good Performance	81.88 （0.0000）	Fixed-effect Model
Under Poor Performance	44.42 （0.0000）	Fixed-effect Model

C. DESCRIPTIVE STATISTICS

We obtain the comprehensive score of operating performance based on principal component analysis, divide sample companies into two groups including one group with good performance and the other with poor performance according to the median line, and then make a descriptive statistics of the two groups respectively which is shown in Table VI.

TABLE VI: DESCRIPTIVE STATISTICS OF SAMPLE FIRMS' SELF-MOTIVATION UNDER DIFFERENT OPERATING PERFORMANCE

Measured Variables of Self-motivation	State Group	Sample Size	Average	Standard Error	Min	Max
Free cash	0	295	-0.14	1.43	-9.05	75.2

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flows		9	186	73	612	685
		296	-0.08	0.20	-4.80	1.37
	1	0	537	313	734	202
Executive		295	0.305	0.45	-0.00	1.00
	0	9	92	526	013	000
Compensation		296	0.317	0.46	0.00	2.66
Structure	1	0	72	113	000	008
		295	2.645	1.35	0.00	8.47
Management	0	9	695	499	000	365
		296	2.806	1.39	0.00	7.86
Tenure	1	0	503	247	000	667
Authority		295	1.737	0.44	1.00	2.00
	0	9	411	011	000	000
Separation		296	1.789	0.40	1.00	2.00
	1	0	456	776	000	000

Note: if State=0, it represents the group of sample companies with poor performance; if State=1, it represents the group of sample companies with good performance.

From Table F, we can conclude that free cash flows average (-0.0853791) of listed companies with good performance is greater than listed companies with poor performance (-0.1418608); the executive compensation structure average (0.3177269) of listed companies with good performance is greater than listed companies with poor performance (0.3059295); the management tenure average (2.806503) of listed companies with good performance is greater than listed companies with poor performance (2.645695); and the authority separation average of listed companies with good performance is also greater than listed companies with poor performance. The conclusion above-mentioned in Table F is consistent with the hypothesis we put forward in this paper above.

D. EMPIRICAL TEST

According to the model selected by Hausman test, we used STATA11.0 software to make a specific estimation of the model and the results shown in Table VII.

TABLE VII: REGRESSION RESULTS OF EXECUTIVES SELF-MOTIVATION INFLUENCES ON BUSINESS PERFORMANCE

	Sample Companies under poor performance			Sample Companies under good performance		
Variables	Coefficient	t	Sig.	Coefficient	t	Sig.
FCF	-0.022336	-5.22	0.000	0.5535064	8.83	0.000
MFP	0.0649364	1.86	0.062	-0.007585	-0.29	0.772
MT	-0.0230706	-4.55	0.000	0.0093772	2.45	0.015
Power	0.0205314	0.58	0.561	0.0932239	3.61	0.000
Size	0.1673627	4.61	0.000	0.0404955	1.62	0.105
Tobin's	0.021487	2.35	0.019	-0.008476	-0.87	0.383
Industry	omitted			omitted		
Ftest	9.23(0.000)			16.76(0.000)		

Note: the number in parentheses is the p value of F-test.

In Table 7, free cash flows (P = 0.000) of sample companies under good performance is positively correlated with operating performance at a significant level of 5% while it is negatively related to operating performance in sample companies under poor performance also at a significant level of 5% testifying the H1 hypothesis; management fixed compensation ratio of sample companies under good performance does not have a significant statistical relationship with operating performance, namely fixed monetary compensation can't play an incentive role when the performance is getting better while fixed monetary compensation is significant positive correlated with operating performance in listed

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companies under poor performance at a significant level of 10% testifying the H2 hypothesis; management tenure of sample companies under good performance is positively correlated with operating performance at a significant level of 5% while it is negatively related to operating performance in sample companies under poor performance at a significant level of 5% which can verify the H3 hypothesis; authority separation (P = 0.000 with a positive coefficient) of sample companies under good performance is positively correlated with operating performance while it is negatively related to operating performance in sample companies under poor performance (P=0.561) proving the H4 hypothesis.

CONCLUSIONS

We can draw conclusions through empirical analysis above: 1） Listed companies with good performance owns more free cash flows than the ones with poor performance; 2）The relationship between fixed monetary compensation and operating performance of listed companies with good performance is not significant while it has a negative correlation in listed companies with poor performance; 3）Management tenure is positively correlated with operating performance in the listed companies with good performance while it is negatively correlated in the listed companies with good performance; 4）Authority separation between the chairman and managers in the listed companies with good performance is positively correlated with operating performance which can also improve operating performance at the same time.

Conclusions above shows that there is a big difference in the impacts of managers' self-interest motive on operating performance under different level of operating performance, therefore, we should adopt different policy and measures to restrain managers' self-interest motive in the view of different business performance. For example, improving the proportion of managers' non-monetary rewards due to monetary compensation in a company with good performance has reached a higher level and its incentive effect is small in order to combine managers' personal interests and business interests and improve company's long-term development. Similarly, we can mainly adopt monetary compensation in a company with poor performance for its significant incentive effect.

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