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# **A STUDY ON THE SHAREHOLDERS' BEHAVIOR OF LISTED COMPANIES BASED ON SYMBIOSIS THEORY: A RESEARCH FRAMEWORK**

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**Abstract:**

*Research on shareholder's behavior is a hot topic in recent years. Most researches are based on the theory of agency, which proposal that equity decentralization is the major way to solve the conflict problem between large shareholders and minority stockholders. Actually, major shareholder will never be eliminated. This paper introduces the symbiosis theory-ecology theory to explain the motives and consequences of the behavior of different type shareholders in China's from a new perspective. The paper established a research framework for the behavior of shareholders based on symbiosis theory, which includes four major parts: symbiosis model; symbiosis income distribution mechanism; symbiosis stability and persistence. The idea of the framwwork lies in that the economic consequences of symbiosis model must be the realization and sharing of symbiosis income by both minority and controlling shareholders, which result is more in line with the prerequisite of economic man hypothesis. Symbiosis model and symbiosis income sharing mechanisms are most important factors that affect the symbiosis stability. The dynamic role of these three factors (Symbiosis model, symbiosis income sharing mechanisms and symbiosis stability) finally determines the ability of symbiosis unit for creating value, which is symbiotic persistence.*

**Key words:** *shareholder behavior, symbiosis, agency theory*

## **1. Introduction**

In recent years, much attention has been paid to shareholders behavior for listed companies. Most studies focused on expropriation of the rights of minority shareholders. There was that large shareholders (mainly referring to controlling shareholder) would inevitably usurp the interest of the minority shareholders to seek

benefits from their control right. In reality, many scandals can be corroborated in Chinese listed companies. From major shareholders' behavior in KMK CO., LTD ,999 Pharmaceutical CO., LTD, Feitian Corporate Group and Top Corporate Group, we can learn how serious was the expropriation of minority shareholders in those companies. Almost all research papers in this area are committed to Agency Theory as a fundamental principle. According to that theory, the conflict of interest between minority and controlling shareholder is the third category agent problem. Ownership centralization is the main cause of the behavior of major shareholder usurping the interest of the minor stockholders and listed companies. Therefore, it seems that equity decentralization is the only way to solve the problem.

Unlike the background analyzed by Berle and Means (1932) during an earlier period when they proposed the classical Agent Theory, Demsetz (1983), Shleifer and Vishny (1986) and Morck (1988) showed that many firms in the United States have a high concentration of ownership. La Porta et al. (1988, 1989) proved that there is much higher concentration of equity in other developed countries or developing countries. In China, problem with controlling shareholders are more evident. Most of the listed companies are controlled by state ownership. In fact, state owned shareholding accounts for much more than 50% of the listed companies. Major shareholders will still exist even after the stock restructuring completed in Chinese listed companies. As a matter of fact, major shareholder will never be eliminated. The system will always exist any time and any where in the modern world. From this point of view, it can be seen that decentralization is not a wise answer to the problem.

Another interesting phenomenon can be identified in China's stock market. According to the statistics of the China Securities Regulatory Commission, the number of investment accounts in China's capital market has an increasing trend each year. During 2001 and 2005, the total number of China's Shanghai and Shenzhen stock markets accounts was 68,986,700 and 73,360,700 .By the end of 2006, the total number investment accounts in Shanghai and Shenzhen stock exchange increased to 78,540,100. The number of Shanghai and Shenzhen stock market accounts rose to 131,272,200 on the end of Sep., 2013. The fast growth of minority shareholders poses an interesting question: whether the major shareholders have a natural desire to usurp the interest of listed companies and the minor-stockholders? Knowing the major shareholders' expropriation, why do many minority shareholders still stay in that company rather than leave to protect themselves? Of course, information asymmetry maybe one of the possible explanation, but by no means the full answer. Minority shareholders have their own interest orientation and judgment criteria. If the controlling shareholders do have a natural tendency to usurp the interests of the minority shareholders, the latter would certainly not invest in listed companies as they do now. Clearly, the agency theory can not explain this phenomenon.

Assuming that the natural tendency of the controlling shareholder to usurp interests against the minority shareholders would not be true, we so assume that the small shareholders and the controlling shareholder have a harmonious arrangement. In fact, some studies proved the propping phenomenon that major shareholders transfer

interests to listed companies. On the basis of this assumption, following questions emerge: How can controlling shareholders and small shareholders achieve a common interest? How these two types of shareholders survive in balance under an environment which involves potential conflicts? What are the balanced conditions? Up to date, these questions have not been given a credible theoretical or empirical explanation.

Based on the above consideration, this article introduces an ecology theory - symbiosis theory-for the first time. This theory will attempt to explain the motives and consequences of the behavior of different type shareholders in China's from a new perspective. We will attempt to find a new interpretation for the relationship between shareholders of listed companies and also find a symbiotic harmony strategy so that major shareholders and small shareholders can achieve a win-win situation.

## **2. Overview of the shareholder's behavior studies analysis**

There are many studies about the behaviors of controlling shareholders [1] in the existing literature. Many of these focus on controlling shareholder's expropriation. A small number of papers concern the controlling shareholders propping to the listed companies. Correspondingly, the main problem related to minority shareholders is how to protect the interests of small shareholders.

### ***The perspective of controlling shareholder's expropriation***

Demsetz (1985), Morck et al. (1988) and La Porta et al. (1999) suggest that the conflicts of interest between controlling shareholders of listed companies and minority shareholders are serious. The controlling shareholders will attempt to enhance their own interests at the expense of the interests of small shareholders. On that basis, Johnson et al. (2000a) proposed a concept-tunneling [2] – to describe benefits expropriation by major shareholders, the controlling shareholders of enterprises will transfer corporate assets and profits into their own hands through lawful or unlawful activities, which directly leads to violations of minority shareholders' interests. They argue that tunneling by major shareholder was the main reason for the Asian Financial Crisis in the period of 1997-1999. Johnson et al. (2000b) further confirms that, even in developed countries which have a sound legal environment, "tunneling" by major shareholders still widely exists, with a legal basis in majority. This has led to a focus of theoretical and empirical research on "tunneling." In China, Wei (1998), Lu and Wang (1999) confirm that major shareholders transfer the interests of listed companies in the distribution of dividends in China. Lee and Xiao (2002) suggest that cash dividend policy is the important means by which controlling shareholders excavate benefit expropriation "tunnels." Tang and Jiang (2002) provide further evidence that the degree of expropriation large shareholders of China's listed companies against small shareholders is much higher than in the Anglo-American countries.

Regarding the determination of tunneling, the main viewpoints of scholars at home and abroad mainly are summarized as follows: the level of protection of investors (La Porta et al., 1999a, b); the shareholding structure (Claessens et al., 1999; Bennedsen and Wolfenzon, 2000; Li Zengquan, 2004; Yu Minggui, Xia Xinping, 2004); the degree of separation between cash flow rights and control rights (Claessens et al., 2000; Lemmon and Lins, 2003; Yang Shue, Han Zhili, 2006; Wang Peng, Zhou Lian, 2006); debt ratio (Nicodano and Sembenelli, 2000; Banerjee et al., 1997); corporate size (Barclay and Holderness, 1989); the external market environment (Luo Dangling, Tang Qingquan, 2006); and split share structure (He Weidong, 2004).

Regarding the means of tunneling, Johnson et al. (2000a) holds that there are mainly two ways: First, major shareholders transfer resources from the enterprise through self-dealing. Second, the controlling shareholders make financial transactions with the enterprise on its advantage in the enterprise. Specifically, the direct misappropriation of funds, related party transactions, stock allotments, guarantees for other firms, cash dividend policy, can become tunneling carriers. Chinese scholars have also conducted fruitful research on this aspect; representative literatures include Wang and Tong (2006), Li (2005), Xiao (2005), Tang et al. (2005).

### ***The perspective of protection of minority shareholders' right***

Complementary to the perspective of controlling shareholders usurping minority shareholders' interest, scholars were studied the issue of protecting the interests of minority shareholders. The main viewpoint of those scholars is that the most effective means for controlling shareholder's expropriation situation is through power balance with the shareholder structure (Gomes and Novaes, 1999; Bennedsen and Wolfenzon, 2000; Bloch and Hege, 2001, etc.). Chinese scholars were also devoted to in-depth research to the issues of protection of small shareholders' interests within the Chinese environment (He Jun, 1998; Chen Xiangyong, 2000; Pei Wuwei, 2001, etc.). The main conclusion of those studies focused on the creation of a more equitable environment for minority-sized shareholders, by means of improving and perfecting the institutional environment, market mechanism, and corporate governance and so on.

### ***The perspective of propping from controlling shareholders to listed companies***

Another action of controlling shareholders different from tunneling was considered by Friedman et al. (2003). They pointed out that the controlling shareholders not only have motive to transfer resources out of companies, but also provide private resources to the company, i.e. propping. They found that in the Asian market, with weak protection of investors, when the financial crisis leads a large number of listed companies to financial difficulties, the controlling shareholders support listed companies more than engaging in tunneling. Their research confirmed that the controlling shareholders used private resources to help listed companies tide over the

crisis and difficulties. Propping theory provided a new research field of controlling shareholder's behavior. The support of a listed company by the controlling shareholders provide minority shareholders a mechanism of insurance, to a certain extent, can explain a motivation for why small shareholders to invest. At present, however, there are only a small number of papers in China to support this point of view. Cheung et al. (2004) studied the relationship between the support from controlling shareholders to listed companies, enterprises liabilities, operating performance, and market returns. Their study shows that companies supported by cash have more liabilities, but companies supported by assets have a normal level of liabilities. Liu et al. (2004) adopted the case of Wu Liangye Company for a comprehensive study of tunneling and propping. It presents a basic relationship between control right of the major shareholders of listed companies, performance of listed companies and benefit transmission by major shareholders.

### ***The perspective of different types of relationship between shareholders***

Existing works support the arguments developed by Jensen and Meckling (1976). They believe that there are two kinds of relationship between shareholders. With the proportion of shares for the first major shareholder held in a high or low situation, the alignment effect and entrenchment effect will appear, respectively. At the low level of shareholding, the motive of controlling shareholders to usurp interests of small and medium shareholders increases along with an increase in the shareholding of major shareholder, which causes an alignment effect. When the shareholding of major shareholders achieves a certain high level, major shareholders have a great benefit in listed companies, and the proportion of benefit through expropriation on small and medium shareholders would decrease; this causes an entrenchment effect to weaken major shareholder's tunneling. Stijn et al.(2002 b) provided evidence of these two effects for 1,301 listed companies in eight countries of East Asia, by measuring the relationship between cash receipts and the control right. In China, Li (2004) provided an empirical test on the relationship between the ownership structure of China's listed companies and the misappropriation of funds by controlling shareholders on the basis of 2000-2003 annual reports of China's listed companies. The results show that the misappropriation of fund by controlling shareholders of listed companies and their shareholding has a nonlinear relationship,being positive first,and negative afterwards (that means an alignment effect first ,and then entrenchment effect).

### ***Limitations of Agent Theory-based research***

Although identification of tunneling and propping behaviors was supported by some empirical evidence, few researchers pay much attention to the linkage of those two different activities. There are two main tendencies for this viewpoint on tunneling and propping theory at present: First, the tendencie is to split the two behaviors and

think only about the harmful aspects of tunneling, regardless of the positive side. Second, try to find new evidence to verify that the reason of controlling shareholder support listed company at the moment is just for more tunneling in the future. While these views are not entirely convincing, what determines the controlling shareholders and minority shareholders to choose their behavior? This issue has gradually attracted the attention of some scholars. Shen and Long (2005) pointed out that, at present, there are little or no research study large shareholder's expropriation behavior from the economic point of view. It seems that a large shareholder "should" bear the responsibility of supervising company because he holds most of the shares. Criticizing major shareholders not only encouraged other shareholders "free-rider" behavior, but dampened the enthusiasm of shareholders supervision also.

In short, agency theory is still the fundamental theory in the research of shareholders' behaviors of listed companies so far. Under the circumstances of concentrated ownership in the company, the relationship between controlling shareholder and small shareholders are the representatives of two different agent groups. They are contradictory in natural. Existing research results prove the fact that the controlling shareholder usurping on the minority shareholders and support the listed companies, and try to seek answers from the agent theory. However, we believe that the agent problem maybe a part of the explanation, but not all answers. Although agency theory is reasonable in certain cases, it has many limitations on the in-depth analysis in various aspects, such as behavior of shareholders, causes, conditions and consequences. The shackles of the premise make academic research focus on the major shareholder usurping on the interests of minority shareholders and proceed benefits from control right, but ignore the economic man essential of minority shareholders and their dynamic role. It also neglect the major shareholders' the positive role in governance. As a result, current research use the agent theory as a starting point will bring a biased foundation of study the behavior of shareholders.

### **3. A new theoretical foundation: Symbiosis Theory**

Symbiosis (symbiosis) originated from Greek word, and firstly proposed by the German fungi Jurists Anton de Bary in 1879. It defined as some different species living together, such as a symbiotic parasitic. Watkins (1998) has analyzed the significance of symbiotic to the economic theory from the point of view of social development. Some literatures have used the concept of a symbiosis theory in the cultural and legal aspects of research, but it rarely used in the field of corporate finance. On the contrary, China has some of the leading studies in this area. Yuan (1998) introduced the symbiosis theory into the study of small business, which become the precedent of the symbiotic theoretical research and application on economics. Yuan (2002) explicitly pointed out that the symbiotic on economics mean to the persistent physical relationship existed between economic entities. In short the symbiosis modules form a

symbiotic relationship model under a certain symbiotic environment. Yuan (2002) studies the symbiotic relationship between enterprises and banks in the financial sector. Cheng (2003), He and Xu (2006) and He (2007) applied symbiosis theory to the development of enterprise clusters, the bank and the enterprise, as well as financial and other research fields.

As a theory study for general sense of nature, relationship (between the organizational patterns and behaviors) and the evolution of symbiotic unit (organization or individual), symbiosis theory is suitable for the socio-economic phenomenon research (Yuan, 1998). From the point of view of system, the listed companies is a balance of organizations, minority shareholders and controlling shareholders are integral parts of listed companies. They were symbiotic units in listed companies. Therefore, the nature of the relationship between small shareholders and controlling shareholder is symbiotic relation first. In the process of symbiosis, it may have different symbiotic mode. Because of this, using symbiosis theory as a starting point to study the behavior of shareholders of listed companies is not only feasible, but objectivity and impartiality. It will help us to correctly understand and grasp the characteristics of the behavior of shareholders.

**4. Research framework for the behavior of shareholders of listed companies based on symbiosis theory**

Symbiosis theory reflects the simple theory of historical materialism. Research should be start from observation of the phenomenon. Its main focus should be on the role and integrated effect of symbiosis modules in symbiosis unit. In our opinion, there are four parts in the framework of research on the behavior of shareholders of listed companies based on the symbiosis theory: symbiosis model of controlling shareholder and minority shareholder, symbiosis income distribution mechanism, symbiosis stability measurement, the influencing factors of symbiosis persistence. Research Framework is shown as figure 1.

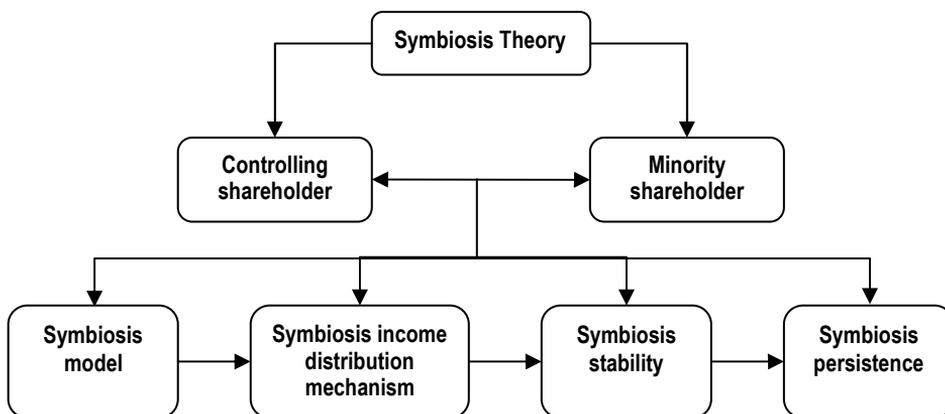


Figure1. Research framework

**Symbiosis model of controlling shareholder and minority shareholder**

Symbiosis model of controlling shareholders and minority shareholders refers to the manner in which the two parties co-exist in listed companies. It is the prerequisite elements for the analysis of how the minority shareholders and controlling shareholder choose their behavior and what its consequences is. It could also clear the strength of the interaction impact between controlling shareholder and minority shareholders.

According to controlling shareholders' shareholding, listed companies can be divided into two types: listed companies under the absolute control of controlling shareholders and listed companies under the control of a minority controlling shareholders. The former represents the major shareholder with more than 50 percent of shares in the company's total equity; the latter refers to the controlling shareholder has a less than 50% of company's equity, but the right to vote more than 50% [3]. Under different circumstances of absolute controlling shareholder mode and minority controlling shareholder mode, the interest orientation of the controlling shareholder is not entirely consistent. In absolute controlling shareholder mode, the controlling shareholder's right to vote and the right to obtain benefit are consistent, so the interests of controlling shareholder will be more consistent with the overall interest of listed companies. In a minority controlling shareholder mode, as the cash flow right of controlling shareholder is less than the right to vote, they can exercise the control right over a small risk. Accordingly, transfer the interests of the listed companies was more strongly motivated. In China's securities market, the absolute controlling shareholder mode is in the majority. But because the development of the family holding company and enterprise groups recent years in China, more and more minority controlling shareholders obtain control over the separation of control and cash flow rights which provides a good opportunity for our study.

On the basis of classification above, through a depth analysis of the intrinsic of nature or factors that influence behaviors of different types of controlling shareholders and minority shareholders, we can define corresponding qualitative parameters, which can be used to calculated the symbiosis degree and symbiosis coefficient. Basic calculation model can be simply summarized as:

Define symbiosis units as  $A, B$ , accordingly, the qualitative parameters [4] are  $Z_A, Z_B$ .

$$\text{Symbiosis degree } \delta_{AB} = \frac{dZ_A / Z_A}{dZ_B / Z_B} = \frac{Z_B}{Z_A} \bullet \frac{dZ_A}{dZ_B}$$

To the main qualitative parameters  $m$ , symbiosis coefficient of  $A$  and  $B$  is

$$\theta_A^m = \frac{|\delta_{AB}^m|}{|\delta_{AB}^m| + |\delta_{BA}^m|} \quad \theta_B^m = \frac{|\delta_{BA}^m|}{|\delta_{AB}^m| + |\delta_{BA}^m|}$$

Through the calculation of symbiosis degree and symbiotic coefficient in different circumstances, the symbiosis model of controlling shareholder and minority

shareholders can be classified. As the interests implementation mechanism of the shareholders is changing after shareholder structure reform in China (Wu, 2007), the interests sharing platform between shareholders will be clearer, the traditional internal games in company will gradually change to the game between the company and the market. Therefore, the split share structure should serve as an environmental control variable in the study of symbiosis model.

### ***Symbiosis income distribution mechanism***

Existing literature generally agree that the value of control right is the main driving force for the controlling shareholder access to it. Shleifer and Vishny (1986), Holderness (1991, 1992) proved the existence of shared benefit of control. But subsequent studies put forward a new view. The controlling shareholder can share not only shared benefit, but also access to private benefit of control (Dyck and Zingales, 2003). Private benefit of control is exclusive, that is to say, minority shareholders have no chance to share it. Just from this perspective, the controlling shareholder usurping on minority shareholders almost become the sole awareness. Public and private benefits of control are conceptually easy to distinguish, but its measurement is very difficult because of the hidden nature of private benefit. Although many western scholars put forward some ideas (such as Barclay and Holderness, 1989; Lease et al., 1983, 1984; De Angelo, 1985; Zingale, 1994, 1995, etc.), much efforts are still needed. Particularly, China's capital market environment was very different with the western countries, how to measure the premium of control is also worthy study.

In theory, private benefit is unobservable, if private benefit can easily be identified, it will not exist. In accordance with such logic, undoubtedly, there is a paradox to measure private benefit.

Under the premise of the controlling shareholder in symbiosis with minority shareholders, we should focus on symbiosis income – the consolidated income created by both controlling and minority shareholders. As a result, symbiosis theory can be used to prove the existence of symbiosis income, analyze of symbiosis income distribution mechanism under different symbiosis model, so as to provide new ideas and evidence of control benefits.

### ***Symbiosis stability***

Symbiosis stability of controlling shareholder and minority shareholders would determine the stability and quality of symbiosis unit (listed companies). It was influenced by symbiosis model and symbiosis income distribution mechanism. Symbiosis stability is also determined by the behaviors of the controlling shareholder and minority shareholders.

In this section, we can use a game theory to analyze the behaviors of controlling shareholders and small shareholders. We can start with a simple game model in the current stock market circumstances, which will make the controlling

shareholders behaviors more proactive. In the basic game model, the controlling shareholders have two main strategies: (expropriation, no expropriation). Relatively, from the consideration of impact on minority shareholders, they may act passively corresponding to the controlling shareholders, their strategic options are: (litigation | expropriation), (no litigation and but withdraw from the company | expropriation), (no litigation and not withdraw from the company| expropriation), (exit | no expropriation), (not withdraw from the company | no expropriation). In this model there are five Nash equilibrium and equilibrium have different parameters set.

Through the Game Analysis, we can determine the critical point which affecting the controlling shareholders' strategic choice. The Variables may include shareholding ratio, litigation costs, benefits, and other major variables. Then, we can establish a symbiosis evaluation model for symbiosis stability. Holderness (2003) proved that, when controlling shareholder reached a certain degree of control, expropriation of small and medium shareholders is not the optimal strategic choice. The absolute control right owned by controlling shareholders would make them improve the value of listed companies to maximize its benefit. This increase of overall value will undoubtedly become the symbiosis income which shared also by the small shareholders. The symbiosis stability of the organizations will be consolidated.

The stability of symbiosis organization depends on its internal structure. The symbiotic process between minority shareholders and controlling shareholder is essentially a process for information to expose and exchange. Under the information asymmetry, change in abundance of information will lead to withdraw or enter by symbiosis unit. The symbiosis income distribution mechanism also has an important influence on the structure of stability. Therefore, when measuring the symbiosis stability, we should pay much attention to the following two factors: information state between minority shareholders and controlling shareholders, and whether the distribution of symbiosis income achieves optimal incentive compatible state.

From the existing researches, we can see the sharing of symbiosis income is difficult to achieve full equality. If  $S_k$  represents the proceeds sharing coefficient of symbiosis stability,  $S_m$  refers to the actual extent of deviation, and  $S_k = (1 + a) S_m$ , where  $a$  defined as non-symmetrical distribution coefficient, and  $a_0$  is asymmetrical distribution coefficient for a critical state of symbiosis stability. When  $a \leq a_0$ , the symbiosis organizations is stable. Therefore, solving  $a_0$  under different conditions is the key of the research.

### ***Symbiosis persistence***

Symbiosis persistence between minority shareholders and controlling shareholder depends on whether the symbiosis organizations (listed companies) could develop continuously, or keep on creating values.

Base on the research of several themes above, it is necessary to define the conditions and main factors of symbiosis persistence for controlling shareholder and minority shareholders at first. Then we should clarify joint function of controlling

shareholder and minority shareholders, which help to found sustainable development mechanisms and organized rules of listed companies, the manifestations and economic consequences of symbiosis persistence. On this basis, we can establish a set of theoretical system to analyze the ability of sustainable development of China's listed companies. The system will provide an operational evaluation tool to assess the overall quality of listed companies, and provide some foreshadowing role for the academic study of listed company's shareholders.

## **5. Conclusion**

Although the agency theory can make a reasonable explanation for the tunneling behavior of controlling shareholder, but it exposed some limitations and inadequacies when it was used as the theoretical cornerstone in researching behaviors of different categories shareholders of listed companies. To this end, this paper presents a research framework and some ideas based on the symbiosis theory for studying behaviors of listed companies' shareholders. We believe that, minority shareholders and controlling shareholder, in essence, have a symbiotic relationship, but there are different patterns of symbiosis in different environments and conditions. Tunneling and propping by controlling shareholder of listed companies in current study are only two symbiosis patterns, but not all. The economic consequences of symbiosis model must be the realization and sharing of symbiosis income by both minority and controlling shareholders. This result is more in line with the prerequisite of economic man hypothesis. Symbiosis model and symbiosis income sharing mechanisms are most important factors that affect the symbiosis stability. The dynamic role of these three factors (Symbiosis model, symbiosis income sharing mechanisms and symbiosis stability) finally determines the ability of symbiosis unit for creating value, which is symbiotic persistence.

We believe that using the symbiosis theory as the starting point to study the controlling shareholders and minority shareholders' behaviors and relating economic consequences will be more objective and comprehensive. Based on this theory, researchers have a new basis for future study. It provides new research ideas for further research. It will bring new vigor and vitality into shareholders' behavior study. Based on this theory, researchers can provide theoretical and empirical evidences to help standardizing the behavior of shareholders of listed companies and improving the quality of listed companies. This paper just only establishes a preliminary research framework and research suppositions. More in-depth, specific theoretical analysis and empirical researches are needed in further studies.

## **6. Notes**

[1] Large shareholder means to the controlling shareholder in literature review, so the two shareholders are no difference in this paper.

[2] In other literatures, tunneling also refer as expropriation, usurping, or benefit transportation.

[3] Bebuchuk et al (1999) define this type of shareholder as Controlling Minority Shareholder, and call the phenomenon which controlling minority shareholder has inconsistent control right and cash flow right as “the separation of control and cash flow rights”.

[4] Qualitative parameters are determinants of the nature and its change of symbiosis units, generally speaking, qualitative parameter is not unique, but a group of parameters.

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