Improving corporate governance where the State is the controlling block holder: Evidence from China

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Abstract:
We examine changes in market values and accounting returns for a sample of publicly traded Chinese firms around announcements of large block-share transfers among government agencies ("State Bureaucrats"), market-oriented State-owned enterprises ("MOSOEs") and private investors ("Private Entities"). We find evidence that these large block transfers are true control transactions for all types of block holders, resulting in positive abnormal returns around the transfer announcements. Moreover, we provide evidence that transfers from State Bureaucrats and MOSOEs result in larger increases in market value and accounting returns than transfers from Private Entities—consistent with their superior incentives and expertise relative to State block holders. We also find that CEO turnover occurs more quickly when shares are transferred to Private Entities. We conclude that corporate governance can be improved at State-controlled firms by improving the incentives and managerial expertise of controlling block holders, and that this is better accomplished by transferring ownership to private investors rather than by shuffling ownership among State-controlled entities.

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1. Introduction

The State usually remains the controlling block holder after a share-issuance privatization ("SIP"). In a study of 630 SIPs from 59 countries, Jones *et al.* (1999) find that the median-ownership offering by the State was only 35%, leaving the government not only with a controlling stake but also with majority-ownership in the majority of SIPs. This raises several important questions: Who is the more effective monitor of management of a listed firm—the State or a private owner? Can the State improve performance by making governance changes that go short of full privatization? For example, can the State improve performance by transferring ownership from bureaucrats to managers of corporatized State-owned enterprises, who have better incentives and experience than bureaucrats? In this study, we attempt to shed new light on these important questions by examining 631 negotiated block trades among different State-controlled and private shareholders in China during 1998-2002.

Most empirical studies of privatizations find that full privatizations and, to a lesser extent, partial privatizations lead to improvements in firm performance (see the surveys by Megginson and Netter (2001) and Djankov and Murrell (2002)).[1] Our study analyzes the impact of changes in corporate governance *after* partial privatization of State-owned enterprises (SOEs) has been completed. Focusing on these "second round" changes in ownership, we find that significantly larger improvements in firm performance do occur when control is transferred to private owners than when control is transferred to "market-oriented" SOEs. Thus, consistent with the literature on block-holder identity, we show that the specific managerial *expertise* and *incentives* of block holders are important determinants of firm value (see the seminal article by Barclay and Holderness (1991) and a recent survey by Holderness (2003)).

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[1] *Full privatization* refers to the transfer of control from the State to private owners whereas *partial privatization* refers to the issuance of publicly traded shares by a State-owned enterprise where the State maintains majority ownership and/or control. Sun and Tong (2003) and Gupta (2005) study the impact of partial privatizations in China and India, respectively.

We choose to analyze Chinese firms because intra-governmental block transfers were relatively common in China and reflected efforts by the Chinese government to improve corporate governance, while maintaining ultimate control at the country's largest firms.[2] The Chinese government used two basic ownership structures to participate in the equity of listed companies: (1) direct control through *State Bureaucrats* at government agencies and ministries; and (2) indirect, but ultimate, control through *Market-Oriented State-Owned Enterprises* (MOSOEs).[3]

There are important differences in the *expertise* and *incentives* of these two ownership structures, which are critically important because Barclay and Holderness (1991, p. 887) "document that the specific skills and incentives of large block shareholder, and not just concentration, affect firm value." First, managers of *MOSOEs* have superior industry expertise, as they are actively managing their corporations, which often are in the same industry as the corporations of which they are block holders, whereas State Bureaucrats may have little or no experience in corporate management of any kind. Second, the incentives faced by managers of *MOSOEs* and *State Bureaucrats* differ, in large part, by how they are compensated. *State Bureaucrats* are not directly rewarded based on the financial performance of the firms they monitor (Xu and Wang, 1999), whereas managers of *MOSOEs* are partially rewarded based on their firm's financial performance (Groves *et al*., 1995; Firth, Fung and Rui, 2006). In addition, *MOSOEs* are allowed to retain after-tax profits for internal use, providing their managers with

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[2] Official documents and speeches indicate that the Chinese government intended to maintain ultimate control over a large segment of the Chinese economy, including those that had been partially privatized. See, for example, President Jiang Zemin's speech at the 15th Congress of the Chinese Communist Party in the fall of 1997. According to some observers, Chinese authorities sought to improve the corporate governance of State-controlled firms as a means of avoiding further privatization (Lin, 2000; Cao, 2000).

[3] This classification relies, in part, on the concept of the "ultimate controlling shareholder" introduced in La Porta *et al*. (1999, pp. 475-476). Without the concept of the ultimate controlling shareholder, we would not be able to identify firms controlled by SOEs as being ultimately controlled by the State.

additional incentive to maximize profits. Furthermore, as separate legal entities, *MOSOEs* are expected to be more focused on commercial objectives (Broadman, 1997).

In this study, we investigate changes in value and performance when block transfers occur at firms that have been partially privatized, but where the State maintained a controlling interest. We find large and significant improvements in value and performance when block are transferred, and that these improvements are significantly larger when blocks are transferred from State control to private control rather than transferred between two State-controlled entities.

Our results show the importance of these differences in identity of the block holder. For example, focusing on block transfers of at least 20%, we find the excess returns surrounding the announcement of transfers from a *State Bureaucrat* to a *Private Entity* average 33.6%, as compared with 26.6% for block transfers between a *State Bureaucrat* and a *MOSOE* and 20.9% for block transfers between two *State Bureaucrats*. These large value increases around control transfers to a *Private Entity* are mirrored in significant improvements in accounting performance following block transfers from a *State Bureaucrat* or *MOSOE* to a *Private Entity*. In the two years after the year in which these transfers are announced, the annual return on assets is higher by more than 300 basis points when compared with the two years before the transfer announcement.

Furthermore, CEO turnover is faster when control is transferred to a *Private Entity*. Replacement of the CEO within three months of the block-transfer announcement is significantly less likely when a *State Bureaucrat* is the seller or buyer. These differences disappear when we look at replacements within 12 months of the block-transfer announcement.

We contribute to the literature in at least three important ways. First, we extend the literature on block-holder identity and partial corporate control (Holderness and Sheehan, 1985 and 1990; Barclay and Holderness, 1991; Bethel, Leibeskind, and Opler, 1998; Franks and Mayer, 2001). We provide new evidence from Chinese markets that changes in firm value

associated with negotiated block transfers, and subsequent changes in top management, are functions of the incentives and managerial skills of the new block holders. Specifically, we find that share transfers to *private* block holders are most effective in improving corporate governance and increasing firm value (Grossman and Hart, 1988; Harris and Raviv, 1988; Shleifer and Vishny, 1997). Because many of the world's largest enterprises, both listed and unlisted, have the State as the controlling block holder (La Porta *et al.*, 1999; Claessens, Djankov and Lang, 2000), we regard this as an important extension of current research that has focused exclusively on share transfers between private block holders.

Second, we contribute to the literature on how State ownership affects the performance of partially privatized firms (Kole and Mulherin, 1997; Sun and Tong, 2003; Boubakri, Cosset and Guedhami, 2005a; D'Souza, Megginson and Nash, 2005; Gupta, 2005). Our results show that block transfers at partially privatized State-controlled firms where the State reduces or relinquishes its ownership share are associated with increases in market values and improvements in accounting performance that are significantly greater than those associated with block transfers among other types of block holders. This is innovative because we isolate the effect of privatization, i.e., change from State to private control, from the effects of issuing public equity.[4]

Third, we contribute to the literature on *why* State-owned firms perform poorly. The "political view" posits that politicians interfere and pursue political objectives other than profit maximization (Shleifer and Vishny, 1994), whereas the "managerial view" posits that the State is a poor monitor because there is no individual with strong incentive nor is there a public price

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[4] Gupta (2005) shows that stock market listing of State-controlled firms improves performance because of the role the stock market plays in monitoring and rewarding managerial performance even when there is no change in control. In addition, studies of equity offerings have shown that changes in firm performance around the time of initial public offerings are affected by decisions to issue shares during hot markets (Ritter 1991; Loughran and Ritter, 1995), or to manipulate earnings prior to share issuance (Teoh, Welch and Wong, 1998; Aharony, Lee and Wong, 2000; DuCharme, Malatesta and Sefcik, 2003; Chen and Yuan, 2004).

to provide information (Laffont and Tirole, 1993).[5] It is difficult to separate both effects for SIPs. However, the firms in our sample do have public prices and managers of market-oriented SOEs do have incentives to maximize firm value, yet we find that private monitors are superior to State monitors. Hence, our evidence is more supportive of the political view than the managerial view, and complements Fan, Wong and Zhang (2007), which finds that politically connected Chinese firms perform more poorly than other listed Chinese firms on both a market-value and accounting basis.

The remainder of the paper is organized as follows. In Section 2, we present a brief review of the literature on privatization and block holder identity, and provide institutional details about Chinese stock market and ownership structure of Chinese firms. We discuss the role of the Chinese government and develop hypotheses in Section 3. In Section 4, we describe our data and methodology. In Section 5, we present the results of our empirical analysis and, in Section 6, we provide a summary and conclusions.

2. Literature Review and Institutional Background

2.1 Review of the Privatization Literature

Denis and McConnell (2003) write that "privatization is a natural experiment allowing us to examine how corporate governance mechanisms evolve, interact and affect firm performance." Megginson and Netter (2001) and Djankov and Murrell (2002) provide comprehensive reviews of studies published prior to 2000, which generally find that privately owned firms are more profitable and efficient than similar SOEs. In Appendix Table 1, we briefly summarize the findings of some of the most prominent multi-country studies of privatization (Panel A), as well as some of the more recent studies that look at partial privatization (Panel B). In general, most of the studies of privatizations find that full

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[5] Without share-price information, managers miss important signals about their behaviour, face restrictions on performance compensation and are insulated from the "market for corporate control."

privatizations lead to improvements in performance; and, to a lesser extent, most of the studies of partial privatizations find improvements in firm performance following partial privatization, as well.

2.2. Historical Perspective on the Chinese Privatization Experience

In the traditional Chinese SOE that existed from the 1950s until the early 1980s, the central government held 100% of the control rights and cash-flow rights, although much of the residual cash flows from SOEs were allocated to local governments where the SOEs were located. Managers of SOEs were hired and fired by Communist Party officials who led the government agencies or ministries responsible for overseeing the SOEs and to which the SOE managers reported. Managers were evaluated based upon their ability to meet agency/ministry plans, which involved political as much as economic criteria. Funding for SOEs came in the form of "policy loans" from State-owned banks, which essentially allocated capital to the Chinese economy rather than performing traditional banking functions. So long as an SOE fulfilled its policy role, the central government would ensure that it received funds needed for operations regardless of profitability or solvency. Under such a system, it is not surprising that SOEs were notoriously unprofitable and inefficient.

Beginning in 1984, the Chinese government sought to improve the efficiency of its SOEs through a series of gradual reforms that began with the accordance of "legal-person" status to SOEs, which was intended to make SOEs responsible for performance (see Schipani and Liu (2002)). In addition, the central government transferred both the control rights and residual cash-flow rights to local-government entities. By pairing cash-flow rights with control rights at the local government level, this reform provided local government with the incentive to improve SOE performance.

Local governments responded to the incentives provided by their newfound cash-flow and control rights by implementing a series of governance reforms that Groves *et al*. (1995) classify into three strands: (i) giving SOE managers more autonomy from Communist Party

officials at the agencies and ministries to which they reported; (ii) allowing SOEs to retain a portion of any profits they produced; and (iii) developing governance mechanisms to reward SOE managers for superior firm productivity.

In 1993, the National People's Congress enacted the Chinese Corporate Law of 1993, which paved the way for partial privatization of the largest of SOEs. This law defined two types of corporations: closely held and publicly held. For publicly held corporations, the law required a governance structure consisting of shareholders who exercise their rights at a general meeting, a board of directors and a board of supervisors. The law also established the positions of CEO and Chairman of the Board of Directors. For closely held corporations, the Corporate Law sets forth similar requirements, but with some exceptions.

2.3. Partial Privatization and Official Share Classification

The (partial) privatization of Chinese SOEs began years before passage of the Corporate Law of 1993 when the Shanghai Municipal Government approved a set of regional securities regulations in 1984. That approval was followed in the same year by the issuance of shares in an electronics company, which began to trade on an over-the-counter market run by the Industrial and Commercial Bank of China in 1986 (see Ellman, 1988; Qi, Wu and Zhang, 2000).

The Shanghai Stock Exchange (SHSE) was established in December of 1990, followed by the Shenzhen Stock Exchange (SZSE) in April 1991. Seven SOEs went public during 1991. Also in 1991, the Chinese Securities Regulatory Commission ("CSRC")—the Chinese equivalent of the U.S. Securities and Exchange Commission—was established to monitor and regulate the two stock exchanges and their members.

From 1992-2002, the number of listed firms rose from 53 to 1,224, while the market capitalization rose from $13 billion in 1992 to a peak of $579 billion in 2000. Each exchange accounts for approximately half of the total number of firms in each year.

In China, there are several different "official" classes of shares. Shares are classified based on the residency of their owner as *domestic* (A shares) or *foreign* (B, H and N shares). Domestic *A* shares are further divided into *State* shares, *Legal-Person* shares, *Tradable A* shares, and *Employee* shares, of which only *Tradable A* shares, as the name implies, are publicly traded on one of China's two stock exchanges. All shares of a listed company have the same voting rights and cash-flow rights, i.e., one share is entitled to one vote. [6]

The distinction between *State* shares and *Legal-Person* shares is murky, at best, and emanate from a 1994 regulation dealing with restructuring of SOEs. *State* shares are those held by government agencies (e.g., the Bureau of State Property Management and local finance bureaus) and by some types of corporatized SOEs. For most listed companies, *State* shares make up the largest percentage ownership of any classification. *Legal-Person* (LP) shares are those owned by domestic corporations or other non-individual legal persons. Hence, this category includes shares held by the government through legal-person entities, as well as shares held by private entities, both domestic and foreign. Like *State* shares, *Legal-Person* shares cannot be traded on the two exchanges or transferred to foreign investors, but can be transferred to domestic corporations, when approved by the CSRC.

2.4 Alternative Share Classification

There are serious shortcomings in the official share classification for any analysis of corporate governance of listed firms in China. To illustrate the confusion, we refer to Table 5 in Delios *et al*. (2006), where the authors report the overlap between their 17 (ultimate) ownership categories and the official Share Classification. For example, of the 556 times a State Asset Management Bureau (SAMB) was classified as a top-10 shareholder in a listed firm in their

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[6] Tradable A shares are owned by individual Chinese residents and domestic legal persons, but are not allowed to be owned by foreign investors. Individuals are prohibited from holding more than 0.5% of total shares outstanding for any listed company. Regulators typically require that Tradable A shares account for more than 25% of total outstanding shares when a company is listed. The market price of a listed company refers to the price of Tradable A shares. Employee shares are owned by the employees of a listed company. Shareholding by managers is small, with average ownership as low as 0.005%, according to Tian (2001).

sample, the SAMB was officially classified as holder of *State* shares 105 times (19 percent), as a *Legal-Person* shareholder 221 times (40 percent), and in 230 cases the SAMB was classified as *Tradable-A* shareholder or *Other*. Similarly, *Private* corporations were officially classified as holders of *State* shares in 7.4 percent of the cases, as holder of *Legal-Person* shares in 59.8 percent of the cases, and as holder of *Tradable-A* shares or *Other* in 32.8 percent of the cases.

Because of these ambiguities, we adopt the classification scheme of Chinese ownership developed by the National University of Singapore ("NUS") Business School and described in Delios *et al*. (2006). The NUS-classification produces 17 detailed classes of non-tradable shares, which we regroup in four groups of ultimate owners. The groups are as follows (where we refer to the Delios *et al*. (2006) detailed classifications in parentheses). *State Bureaucrat* includes: central government (1); local governments (2); government ministries (3); government bureaus (4); State asset-investment bureaus (6); State asset-management bureaus (7); State research institutes (10); and State-owned banks (16). *Market-Oriented SOE* includes companies that formerly were government ministries (5); market-oriented state-owned enterprises (9) and infrastructure construction companies (8). *Private Entity* includes security companies (11); investment funds (12); private companies (13); private individuals (14); and work unions (17). *Foreign Entity* includes foreign companies and individuals (15).

The distinction between *State Bureaucrat* and *Market-Oriented SOE* ("*MOSOE*") is important because the incentives (e.g., profit-sharing) and expertise (e.g., managerial and industry expertise) of managers of market-oriented SOEs are fundamentally different from those of government bureaucrats. We return to this issue in the next section.

Table 1 shows the distribution of ownership categories of the largest block holder for listed firms by year, from 1993-2002, based upon our classification scheme. Beginning in 1996, *MOSOEs* dominate the sample. The number of *State Bureaucrats* remains relatively constant from 1996-2002, while the number of *Private Entities* steadily increases from 13 in 1993 to 155 in 2002. The number of *Foreign Entities* ranges from 9 in 1993, to 18 in 1996. (The annual total

numbers of firms in Table 1 does not equal the total number of firms each year because NUS

was unable to classify a small number of firms.)

3. Ownership Structures and Hypotheses

3.1 Government Ownership Structures

Because of differences in incentives and residual cash-flow rights, we expect that the

two alternative government ownership structures (*State Bureaucrats* vs. *MOSOEs*) have

differential impacts on firm value, even though the State is the ultimate controlling shareholder

in each case. A *State Bureaucrat* ("*SB*"), such as the Bureau of State Property Management or a

local finance bureau, exercises ownership rights on behalf of the Chinese State. When a *SB*

controls the majority of a company's shares, officials of the block holder have the right to select

managers and board members, and to veto business and investment plans proposed by firm

management. As government officials, however, the officials are prohibited from involvement

in the management of State-controlled firms.[7]

SB officials have no residual cash-flow rights from the companies they monitor; all

dividend revenues from the companies under their control are submitted to the Ministry of

Finance or to local governments. Moreover, *SB* officials are not rewarded based on the

performance of the SOEs that they monitor (Xu and Wang, 1999; Lin 2000).[8]

SB officials typically have little or no management experience and little industry-

specific knowledge (Firth, Fung and Rui, 2006). Hence, it is difficult for them to evaluate

management decisions. The promotion of *SB* officials depends largely on how well they execute

the instructions of central or local government rather than how much they contribute to creating

firm value or dividend revenues. Based on these characteristics, we hypothesize that *SB-*

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[7] In the 1984 "Decision on Reform of the Economic Structure," it is declared that government
departments will not manage or operate enterprises directly (Cao, 2000). This measure was
aimed at transforming State-*run* enterprises into State-*owned* enterprises.

[8] Of course, *SB*-officials (as well as *MOSOE*-officials) enjoy the benefits of indirect perquisites,
which can be substantial, including luxury housing, car with driver, expense accounts, etc.

officials are unlikely to have profit maximization as the primary goal for *SB*-controlled listed firms.

In contrast to *SB* officials, the managers of *MOSOEs* typically receive explicit monetary rewards based on their firm's performance (Groves *et al.,* 1995; Firth, Fung and Rui, 2006). This incentive compensation at *MOSOEs* should mitigate agency problems between the controlling block holders (the MOSOE) and minority shareholders of the listed firm. Furthermore, *MOSOEs* have a degree of autonomy and are allowed to retain their after-tax profits, which can be used according to their own plans. These factors provide managers of *MOSOEs* with greater incentive to focus on profitability than managers of *SBs*.[9]

Finally, changes in the identity of the block holder can increase firm value by improving the quality of management and/or monitoring (Barclay and Holderness 1991). Because of their managerial experience in industry, we expect that *MOSOE* block holders are more efficient and professional than government officials in monitoring the firms under their control. In some cases, *MOSOEs* contribute directly to the listed firms under their control, in the form of management, capital or new technology. According to Zou (2004), the Chairman of the MOSOE-controlled listed firms is also the Chairman of the parent MOSOE in more than 60 percent of the cases. This number is only 16 percent for listed companies that are controlled by *SB*s. Furthermore, Chen and Wang (2004) show that top-executive turnover is significantly more sensitive to firm performance at listed firms controlled by *MOSOEs* than at listed firms controlled by *SB*s.

3.2 Private Ownership Structure

When a private entity is the controlling block holder, the incentives of the block holder are most closely aligned with those of minority shareholders. Private block holders receive

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[9] When we analyze share transfers among State entities, it is unlikely that there is a substantial change in the calculated control rights and cash flow rights of the ultimate owner around the share transfers in our study. Fan, Wong and Zhang (2005) show that, across a sample of 750 State-controlled firms, the average ratio of cash flow to voting rights of the ultimate owner equals 96 percent.

100% of the cash flows to which the block holder is entitled, in contrast to both government ownership structures. Hence, private block holders are more likely than State block holders to pursue the maximization of shareholder wealth. Also, private block holders choose managers on the basis of their ability to maximize shareholder wealth (or, at least, to maximize the controlling block holder's wealth) whereas State block holders choose managers based, often in large part, upon political considerations and the ability to meet social objectives.

However, controlling block holders also have incentives to expropriate wealth from minority shareholders, especially in countries with weak investor protection (La Porta *et al*. 1999; Johnson *et al*. 2000). Fan, Wong and Zhang (2005) show that, across a sample of 750 State-controlled firms, the average ratio of cash flow to voting rights of the ultimate owner equals 0.96. For the 62 listed firms in their sample that are controlled by private entities, they find that the average ratio of the cash flow to voting rights is 0.54. Given the larger wedge between cash flow and control rights at listed firms with private entities as ultimate owner, we conjecture that expropriation of minority shareholder wealth is more severe after block transfers to private owners.[10] We provide more evidence on this issue in our results section.

3.3 Hypotheses

The typical method used to transfer control at listed companies is known as a share-transfer agreement. Once a share-transfer agreement is reached between two parties, the listed company will apply to the CSRC and the Ministry of Finance to obtain approval. At the same time, the firm will make a public announcement regarding the proposed changes in its ownership structure.

First and foremost, we expect that negotiated block transfers are corporate control transactions in China, just as they are in the U.S., and lead to positive abnormal returns—consistent with the findings of Barclay and Holderness (1991). Therefore, our first hypothesis is

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[10] Evidence in Berkman, Cole and Fu (2009) is consistent with this conjecture. These authors find that Chinese firms are more likely to issue loan guarantees to their controlling block holder—a form of tunneling—when the controlling block holder is private rather than State controlled, either directly or indirectly through an SOE.

that we will observe positive and significant abnormal returns around announcements of these block transfers. The null hypothesis is that there are no abnormal returns around these announcements.

Also consistent with Barclay and Holderness, we expect that differences in the incentives and expertise of managers at *SBs*, *MOSOEs* and *Private Entities* will lead to statistically significant differences in the magnitudes of abnormal returns around the announcements of these block transfers. More specifically, we hypothesize that *MOSOE* block holders are more likely to contribute to value creation than *SB* block holders, and that *Private Entity* block holders are more likely to contribute to value creation than either type of *State* block holder. This should be observable in differences in magnitudes of abnormal returns and in the subsequent accounting performance following the announcements of block share transfers from *SB*s to *MOSOEs,* relative to share transfers from *SB*s to *SB*s, and from *SB*s or *MOSOEs* to *Private Entities*; abnormal returns should be larger and accounting performance should be superior. Conversely, abnormal returns should be smaller and accounting performance should be inferior for transfers from *MOSOEs* to *SBs* relative to share transfers from *SB*s to *SB*s, and from *Private Entities* to *SB*s or *MOSOEs*. We refer to this as the *incentive hypothesis*.

One alternative view of block transfers from *SB*s to *MOSOEs* is that such transfers introduce an additional level of bureaucracy that might oppose changes (Broadman, 1997). *MOSOEs* are typically fully owned and controlled by the State. Their weak governance structure might simply be mapped onto the listed company as *MOSOEs* themselves are often owned by *SB*s. If so, then we should expect lower returns around the announcements of block transfers from *SB*s to *MOSOEs*, relative to transfers from *SBs* to *SBs*, and we should expect accounting performance to deteriorate in years following the announcement of transfers from *SBs* to *MOSOEs*. We refer to this as the *added-bureaucracy hypothesis*.

Yet another view of block transfers arises from the widely publicized manipulation of stock prices at Chinese firms. According to this view of the world, negotiated block transfers

are revealed to insiders long before they are publicly announced in the financial press. This

presents insiders who own non-tradable shares the opportunity to accumulate large positions in

Tradeable A shares in the names of family, friends or fictitious parties prior to public

announcement of the block transfer. Once the transfer is made public, along with promises to

restructure the listed firm, investors bid up the stock price. At that point, the insiders dump their

shares, earning substantial profits, but also putting downward pressure on the share price.

Longer term, the attractive restructuring plan that caused the share price increase is never

implemented, so the accounting performance fails to improve or deteriorates during the years

subsequent to the block transfer. We refer to this as the *manipulation hypothesis*. The

manipulation hypothesis predicts positive abnormal returns preceding share transfers,

irrespective of the identity of the initial owner. Moreover, these positive abnormal returns

should be reversed post-announcement as insiders sell off their shares.[11] Appendix 2 documents

several cases of manipulation.

Our final hypothesis deals with the incentive of a controlling block holder to expropriate

wealth from minority shareholders. While all three types of controlling block holders face this

incentive, a private block holder might be able to more easily accomplish expropriation by

tunnelling resources from the listed firm to a privately held company that she also controls, but

where she holds all of the cash-flow rights rather than only a portion. A scandal surrounding the

De Long Group is an example of this type of behaviour, where a private controlling block

holder—Tang Wanxin—expropriated wealth from listed companies that he controlled to a

privately held parent company that he also controlled, but where he held greater cash-flow

rights. We refer to this hypothesis as the *expropriation* hypothesis. This hypothesis predicts that

accounting performance will deteriorate during the years subsequent to the block transfer and

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[11] A closely related hypothesis is that overly optimistic investors trade on rumors and bid up
share prices in the pre-announcement period. Because short sales were not allowed in China
during the sample period, overly pessimistic investors were unable to express their opinions.
The predictions regarding this hypothesis are identical to those of the manipulation hypothesis
so we don't go into more detail.

that this deterioration will be greatest for transfers to private block holders. To the extent that investors anticipate this expropriation, the hypothesis also predicts lower excess returns around the announcement of such block transfers, and that excess returns will be lowest for announcements of transfers to private block holders.

4. Data and Methodology

4.1.1 Sample Selection

We include in our sample all SHSE and SZSE firms that, during the five-year period from 1998 through 2002, reported share transfers that are greater than 5% of the total number of shares outstanding. The announcement dates were obtained from GTA/CSMAR, one of the largest corporate information providers in China. Our sample period starts in 1998, so that all events in our sample were announced subsequent to the September 1997 Chinese Communist Party's 15th Congress where the Central Committee endorsed a major policy shift, committing to a large privatization program. We confirmed each block transfer using ownership data obtained from the database of Chinese ownership developed by the National University of Singapore ("NUS") Business School, and described in Section 3. This database ends in 2002.

We begin with a sample of 1,040 successful block-share transfers. We are unable to match 189 of these transfers with the NUS database, leaving 851 share transfers. Of these transfers, 171 involve more than one transaction on the same day for the same firm. We delete 36 of these transfers from our sample because the sellers or buyers involved in the multiple transfers are from different ownership categories. We combine the percentage of shares transferred for the remaining transactions if the parties involved in the multiple transfers are the same, or if the sellers involved are from the same ownership category (*State Bureaucrat*, *MOSOE* or *Private Entity*), and the buyers involved are from the same ownership category (*State Bureaucrat*, *MOSOE* or *Private Entity*). This procedure leaves us with 717 observations.

In order to have a sharp distinction between the three main ownership groups—*State Bureaucrats*, *MOSOEs* and *Private Entities*—we exclude 50 transfers involving parties that are classified as 'companies that formerly were government ministries' (NUS category 5); State research institutes (NUS category 10); State-owned banks (NUS category 16) and work unions (NUS category 17).

We also exclude 21 transfers involving foreign entities (NUS category 15). Most of these transfers only involve transfers between two foreign entities, and only three of these transfers are larger than 20 percent of the shares. This leaves us with 646 transfers.

In the final step in the sample selection, we require that the firms in our sample have accounting data and stock-price data in the year prior to the transfer. This requirement reduces our final sample to 631 block transfers.

4.1.2 Descriptive Statistics

Table 2 presents descriptive statistics regarding the pre-transfer ownership structure and firm characteristics of the sample. Panel A of Table 2 reports the results for the total sample, while Panels B-F of Table 2 report the results for the different subsamples based on the identity of the seller and buyer.

In Panel A of Table 2, we see that the average percentage of shares being transferred is 22.0 and ranges from 5 percent to 74.8 percent. We measure firm size by the natural logarithm of the book value of total assets. Our financial data were obtained from GTA. The average size of firms in our sample is RMB1.18 billion (US$143 million), and firm size ranges from RMB 70 million to RMB 22.1 billion.

We calculate the leverage ratio for each firm as its book value of total liabilities divided by its book value of total assets. The average leverage ratio is 46.8%.[12] The high leverage ratios in our sample reflect the fact that most listed Chinese companies use bank loans as their primary source of capital. The four largest banks in China, which control the majority of

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[12] There are no finance companies in the sample.

banking assets in the country, are directly controlled by the Chinese government. These banks typically allocate credit to individual firms on the basis of national policy, but do not have the power to force a firm into liquidation.

We calculate peer-adjusted return on assets (ROA) as the firm's core EBITDA divided by the book value of total assets as of year-end less core EBITDA divided by the book value of total assets as of year-end for a matched firm. We define core EBITDA as profit or loss from core operating activities.[13] We select a matched firm for each of our sample firms where the matched firm is in the same industry and has the lowest absolute value of the difference in the ratio of core EBITDA over total assets in the pre-transfer year relative to the sample firm across all firms in the same industry. We define industry sectors at the level of two-digit SIC codes, which we obtained from the CSRC. The average peer-adjusted ROA for our sample firms in the year before the transfer is significantly negative at −0.8 percent (*t*-statistic is −3.0).

We follow Berkman, Cole and Fu (2010) in calculating the annual level of firm-specific expropriation as the sum of the value of potentially harmful related-party transactions in a particular year, scaled by total assets of that firm as of year-end. Δ*EXPROP* is defined as the level of expropriation in the year after the block transfer less the level in the year prior to the year of the block transfer. Data on related-party transactions come from GTA. The average change in the level of expropriation is close to zero.

In Panels B through G of Table 2, we present the descriptive statistics for each of the nine seller-buyer pairs. From Panel B, we see that *State Bureaucrats* were involved as seller in 167 transfers, and as buyer in 85 transfers. *MOSOEs* were sellers in 340 transfers and buyers in 308 transfers. Finally, *Private Entities* were involved as seller in 124 transfers and as buyer in 238 transfers. These numbers reflect a clear shift in ownership from *State Bureaucrats* to *Private Entities* over our five-year sample period.

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[13] China's standardized income statement separates the operating results into (1) "profit or loss from core operating activities" and (2) "profit or loss from non-core operating activities". Chen and Yuan (2001) documents that earnings management is more likely to involve non-operating profits.

Panel C of Table 2 shows that transfers involving *State Bureaucrats* as sellers are largest, on average, at 26.5 percent of the shares outstanding. When *State Bureaucrats* are involved in the transfers as buyers, the average transfer size is 25 percent. *Test 1*, shown in the last column of the panel, reports the results of an *F*-test for equality of the mean transfer percentages across the three ownership categories, and shows the percentage of shares transferred is significantly different across the three seller categories. Similarly, *Test 2*, in the bottom row of the panel, indicates significant differences in the percentage of shares transferred across the different types of buyers.

In Panel D of Table 2, we see that transfers where *State Bureaucrats* or *MOSOEs* are involved in transfers as buyers or sellers are significantly larger than transfers to or from private owners.

Panels E, F and G in Table 2 show the leverage, peer-adjusted ROA, and change in the level of expropriation, respectively, for each pair of seller and buyer. Average leverage is 0.47, average peer-adjusted ROA is -0.008, and average change in the level of expropriation is 0.009, but there are no significant differences across types of seller/buyer.

4.2 Methodology

The purpose of our empirical analysis is to evaluate the efficiency of alternative categories of block owners of listed firms in China. First, we analyze share-price responses around block-transfer announcement dates for the full sample, and for several portfolios, based on the ownership of the seller and the buyer. Second, we analyze the change in accounting performance in the years around the block transfer. Finally, we examine changes in the top management during the period following the block transfer announcements.

We use the market-adjusted return model to calculate daily abnormal returns as the difference between the realized return and the market return.[14] To estimate the market-adjusted

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[14] Our results are robust to use of the market model for estimation of abnormal returns.

model, we use as the market index either the SHSE or the SZSE composite index, depending on where the firm's stock is listed. Both composite indices are value-weighted, consisting of all listed companies on each stock exchange. Our primary event window spans day $t–210$ through day $t+40$.[15] We use a long event window motivated by concerns that market information leakage and insider trading are not unusual in the Chinese markets.[16] For robustness, we also examine abnormal returns from a more traditional five-day event window spanning day $t–3$ to day $t+1$. In addition, we analyze changes in peer-adjusted return on assets and peer-adjusted return on equity around ownership transfers, as well as CEO turnover in the three months and twelve months following the transfer announcement.

Our event-study approach to analyze the impact of ownership changes might help to reduce endogeneity problems, which affect studies using cross-sectional regressions of firm value against ownership variables (see Holderness (2003)). If changes in ownership structure are exogenous, changes in firm value and performance would directly result from these ownership changes. However, it is possible that both changes in ownership and changes in valuation are caused by a third factor, e.g., good business prospects. In this case, the new block holders do not cause superior future performance; rather, they simply are able to identify and negotiate block transfers of shares in firms with better future prospects, or the State simply decides to order such ownership changes.

To address this possibility, we employ a two-stage sample-selection model as suggested by Heckman (1979) in our multivariate analysis of changes in ownership and firm performance/value, where, in the first stage, we estimate the probability that a firm will experience a change in ownership as a function of past firm performance and other

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[15] For some companies, trading is halted on the event day. In these cases, we use the closing price for the next day as the day $t–0$ share price.
[16] See, for example, the article 'Stocks, Lies and Manipulation', *Business China*, September 11, 2000, pp. 4-5, and several cases in Appendix 2. When we use a 150-day window starting on day t-125, we obtain similar results.

characteristics. We then calculate the inverse Mill's ratio from this first-stage regression and include it as an explanatory variable in our second-stage regressions.

5. Results

First, we present the results from our univariate analyses, where we focus on the relation between the variable of interest (changes in firm value, accounting performance and CEO turnover) and the identity of the buyer and the identity of the seller. In the second part of this section, we present the results of cross-sectional regression models, where we account for characteristics of the transfer, characteristics of the listed firm whose shares are transferred, and sample selection bias.

5.1 Univariate Analysis

5.1.1 Cumulative Abnormal Returns

Figure 1 graphs the cumulative abnormal returns from day *t–240* to day *t+100* for our full sample of 631 transfers ("*All*") and, separately, for 38 transfers between *State Bureaucrats* ("*SB2SB*") and for 49 transfers from *State Bureaucrats* to *Private Entities* ("*SB2PE*"). Clearly evident in set of CARs is the share-price run-up from approximately day *t–210* through day *t–1*, suggestive of information leakage and insider trading. Somewhat surprisingly, Barclay and Holderness (1991, p. 865) document a similar pattern for negotiated block transfers between private U.S. firms for day *t–240* through day *t–1*.

Also evident in Figure 1 is the large run-up in the share prices of 49 firms experiencing *SB2PE* transfers and the 28 firms experiencing *SB2SB* transfers, supportive of first hypothesis—that, first and foremost, block transfers are control events associated with positive abnormal returns. Moreover, the run-up in share prices of the 49 firms experiencing SB2PE transfers is much larger than for the 38 firms experiencing SB2SB transfers—supportive of our hypothesis regarding the superior incentives and experience of private block holders relative to State Bureaucrat block holders. Finally, note that the gains prior to *t–1* are not reversed

subsequent to the announcements—evidence that is inconsistent with the manipulation

hypothesis.

Panel A of Table 3 presents descriptive statistics for the cumulative average abnormal

returns (CAR) for day $t–210$ through day $t+40$, and day $t–3$ through day $t+1$. We present these

results for the full sample of 631 transfers that are larger than 5% of the shares outstanding, and

for a smaller sample of 292 transfers that are larger than 20% of the shares outstanding.

As shown in Panel A, the average CAR for the full sample over the period from day $t–$

210 through day $t+40$ is a statistically significant 17.1% (t-statistic = 11.59), which is

approximately the same as the average CAR for the period from day $t–240$ through $t+40$

reported by Barclay and Holderness (1991) for block transfers between private U.S. firms.[17] In

contrast, Franks and Mayer (2001) analyze a sample of block transfers at German firms and find

that the benefits of control transfers do not accrue to minority shareholders. They attribute this

result to the weak protection of minority shareholders in Germany. In light of their finding and

given the relatively weak minority shareholder protection in China[18], the large value increase

around the block transfers in China is remarkable and suggestive of substantial improvement in

firm performance after the block transfer.

The average CAR over the period $t−210$ through $t+40$ for the 292 transfers of blocks

transfers greater than 20% of the shares outstanding is a statistically significant 21.0%

(t-statistic = 8.91).[19] The average CAR over the shorter five-day window from day $t–3$ through

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[17] When making this comparison, it is important to keep in mind the significant differences in
the Chinese stock market, where insider trading is rampant and the U.S. market, where insider
trading is closely monitored and, when identified, is vigorously prosecuted by the U.S.
securities regulators.

[18] MacNeil (2002) estimates that the LLSV index of minority shareholder protection for China
is only two out of a possible score of six, compared to an average score of four for common-law
jurisdictions and an average of three for all countries. He also discusses the difficulties of
enforcing minority shareholder rights in China.

[19] The average CAR of the 339 transfers that are smaller than 20% of the shares outstanding is
13.7% and is significantly smaller than the average CAR of the large transfers at the 1% level.
We have also split the sample according to whether or not the transfer resulted in a change in

day $t+1$ is 1.1 percent for the whole sample and 1.7 percent for the block transfers in excess of 20 percent of the shares outstanding.[20] Each of these CARs is statistically significant at better than the 1% level, with a t-statistic greater than 6.00.

In Panel B of Table 3, we present the average 250-day CARs for the nine different buyer/seller groups of block transfers greater than five percent of common shares. With the exception of transfers from *Private Entities* to *State Bureaucrats* and to *MOSOEs*, the CARs in all cells are positive and significantly different from zero.

Transfers where the *State Bureaucrats* are sellers have the largest average CAR of 21.6%. Within this group, CARs for transfers to *State Bureaucrats*, to *MOSOEs* and to *Private Entities* are 17.2%, 21.4% and 25.0%, respectively. For transfers from *MOSOEs*, the average CAR is 16.7%. Within this group, CARs for transfers to *State Bureaucrats*, to *MOSOEs* and to *Private Entities* are 11.1%, 18.5% and 15.8%, respectively. For transfers from *Private Entities*, the average CAR is 11.9%. Within this group, CARs for transfers to *State Bureaucrats*, to *MOSOEs* and to *Private Entities* are 10.6%, 10.6% and 12.8%, respectively.

The difference in CARs between different sellers is significant at the 5% level (Test 1 in the last column of Table 4, Panel B). There is no evidence that the identity of the buyer is significantly related to the CAR (Test 2 in the last row in Table 4, Panel B). For the full sample, the CAR ranges from 13.8% if a *State Bureaucrat* is the buyer to 18.1% if an *MOSOE* is the buyer.

The results in Panel C of Table 3, for transfers in excess of 20% of the shares, show even larger differences. Again, CARs are largest for transfers from *State Bureaucrats* at 26.4%. Within this group, CARs for transfers to *State Bureaucrats*, to *MOSOEs* and to *Private Entities* are 20.1%, 26.6% and 33.6%, respectively. For transfers from *MOSOE*s, the average CAR is

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control (i.e., a new largest shareholder). There is no significant difference in CARs based on this classification (results are not reported).

[20] Again, the average CAR around large transfers is significantly larger than the 0.6% average CAR around the transfers smaller than 20% of the shares outstanding.

20.5%. Within this group, CARs for transfers to *State Bureaucrats*, to *MOSOEs* and to *Private Entities* are 17.1%, 19.8% and 24.6%, respectively. For transfers from *Private Entities*., the average CAR is 9.3%. Within this group, CARs for transfers to State Bureaucrats, to MOSOEs and to Private Entities are -2.6%, 3.9% and 16.8%, respectively.

Again, the differences across the three types of sellers are significant at the 5% level (Test 1 in the last column of Table 4, Panel B). Focusing on the buyers, we see that the CARs range from 17.6% for transfers where a *State Bureaucrat* is the buyers to 24.9% for transfers where a *Private Entities* is the buyers. Even though these differences in CARs have the expected ordering, the differences are not statistically significant (Test 2 in the last row in Table 3, Panel C).

In general, the results in Panels B and C show that transfers from *State Bureaucrats* to *Private Entities* generate the highest CARs while transfers from *Private Entities* to *State Bureaucrats* generate the lowest CARs. Only transfers to *Private Entities* are consistently positive and significant and only transfers from *State Bureaucrats* are consistently positive and significant. Transfers from *State Bureaucrats* to *State Bureaucrats*, from *MOSOEs* to *MOSOEs* and from *Private Entities* to *Private Entities* all are positive and significant, consistent with the results of Barclay and Holderness (1991), and suggestive of heterogeneity with each of these three ownership classifications, i.e., there are "better" and "worse" monitors within each type of ownership.

Overall, the results in Table 3 are supportive of the *incentive hypothesis,* which states that block transfers from *State Bureaucrats* result in the largest wealth gains to shareholders. The results in Table 3 are inconsistent with the *added-bureaucracy hypothesis* that a transfer from a *State Bureaucrats* to *MOSOEs* simply adds an additional level of bureaucracy to the governance structure, thereby reducing the quality of the government control. On the contrary, further tests show that the average CAR is significantly higher around transfers when *State Bureaucrats* are the sellers, than around transfers where *MOSOEs* are the sellers (the *p*-value

for this difference in average CAR of 4.9% for the full sample is 0.04). The results in Table 3 are also inconsistent with the idea that expropriation by private entities results in value decreases after private entities obtain control over the listed firm.

The substantial value increase before the announcement is consistent with the *manipulation hypothesis* as well as the *incentive hypothesis*. In order to distinguish between the two, we partition our event window into a pre-announcement period from day *t–210* through day *t–0* and a post-announcement period from day *t+1* through day *t+40*. According to the *manipulation hypothesis*, we would expect positive CARs during the pre-announcement period, negative CARs during the post-announcement period, and a negative and significant correlation coefficient between the CAR in the pre-announcement period and the CAR in the post-announcement period. According to the *incentive hypothesis*, we would expect positive CARs during the pre-announcement period, non-negative CARs during the post-announcement period, and a non-negative correlation coefficient between the two.

Consistent with both hypotheses, the average CAR during the pre-announcement period for the full sample is a statistically significant 16.0%. However, the average CARs during the post-announcement period is positive 1.1% (insignificant), which is inconsistent with the *manipulation hypothesis* but supportive of the *incentive hypothesis*. Moreover, the correlation between pre-announcement (*t–210* through *t–0)* and post-announcement (*t+1* through *t+40)* CARs is 0.01 and statistically insignificant, which also is inconsistent with the *manipulation hypothesis*, but supportive of the *incentive hypothesis*.

We repeat these tests for each of the nine classes of block transfers and find no evidence of significant negative correlations for any of these classes. We also obtain qualitatively similar results analyzing the correlations between the CARs from a 50-day pre-announcement window and the CARs from a 10-day post-announcement window.

5.1.2 Changes in Accounting Performance

According to the *incentive hypothesis*, we expect to find significant improvements in accounting performance following the block transfers, and we expect these improvements to be significantly related to the 250-day CAR and five-day CAR.

For each firm involved in a block transfer, we collect accounting data on firm performance for two years before, and two years after, the year of the block transfer announcement (thus excluding the year of the transfer). We test two alternative measures of firm performance: peer-adjusted return on assets and peer-adjusted return on equity.[21] Peer-adjusted performance each year is calculated by subtracting the peer's performance measure for that year from the firm's performance measure for that year. We select peers based upon industry and pre-event performance, where the peer firm is the firm with the lowest absolute value of the difference in ROA relative to the sample firm across all firms in the same industry in the pre-transfer year.

Return on assets (*ROA*) is defined as core EBITDA divided by total assets, and return on equity is defined as core EBITDA divided by total equity. For 106 firms, we were unable to obtain the required accounting data in the pre- or post-announcement periods and these 106 firms are omitted from this part of our analysis.

We average peer-adjusted performance for the two years in the pre-announcement period and for the two years in the post-announcement period. We then subtract the performance in the pre-announcement period from the performance in the post-announcement period to obtain the changes in accounting performance. Results of this analysis appear in Table 4.

From Panel A of Table 4, we see that, for the full sample, peer-adjusted ROA increased by 140 basis points and peer-adjusted ROE increased by 190 basis points—both significant at the 5% level. Focusing on the group of block transfers in excess of 20%, the improvement in

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[21] We obtain similar results when we measure performance using industry-adjusted ROA and industry-adjusted ROE.

peer-adjusted ROA is 170 basis points, and the improvement in adjusted ROE is 290 basis points. Again, the improvement in each performance measure is significant at the 5% level.[22]

Panel B of Table 4 reports the changes in peer-adjusted ROA for the nine different combinations of sellers and buyers of transfers greater than 5%. Among the three groups of sellers, the largest increase in peer-adjusted ROA is 190 basis point for *MOSOEs*, closely followed by *State Bureaucrats* (170 basis point); for transfers where the seller is a *Private Entity*, peer-adjusted ROA falls by 30 basis points. However, these differences across sellers are not significant for the full sample (*p*-value=0.15). The results in Panel C of Table 4, where we only examine transfers greater than 20%, the results among sellers are similar but stronger. The changes in peer-adjusted ROA are 230 basis points, 240 basis points and -190 basis points, respectively, for *State Bureaucrats*, *MOSOEs* and *Private Entities*. The differences among these three groups are statistically significant at the 10% level (*p*-value=0.07).

Among buyers, we find the opposite ordering, with the *Private Entities* and *MOSOEs* showing large increases in peer-adjusted ROA, while State Bureaucrats show small declines in peer-adjusted ROA. Among the transfers greater than 5% (Panel B), the differences are statistically significant at the 5% level (*p*-value=0.04); among the smaller sample of transfers greater than 20% (Panel C), the differences lack statistical significance (*p*-value=0.31).

In general, the results in Table 4 suggest that accounting performance improved following the block transfers, again favoring the *incentive hypothesis* over the *manipulation hypothesis*, the *expropriation hypothesis*, and the *added-bureaucracy hypothesis*. The differences in improvement based on the identity of the parties involved, suggest that *State Bureaucrats* are less efficient monitors than *Private Entities*, with *MOSOEs* somewhere in between.

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[22] There is no significant difference in the change in peer-adjusted ROA and peer-adjusted ROE between the transfers that are larger than 20 percent and the transfers that are smaller than 20 percent.

In Table 5, we report the correlations between the two performance measures and the two CAR measures. For both the long-term window and the short-term window, and for both peer-adjusted ROA and peer-adjusted ROE, we find significant positive correlations, ranging from 0.168 to 0.309. These highly significant correlations suggest that investors were able to successfully anticipate future improvements in operating performance subsequent to share transfers.

5.1.3. Post-transfer Changes in Top Management

According to Barclay and Holderness (1991), a block transfer is a control event if it is associated with large abnormal stock returns and top-management turnover. Even though firms in China operate in a very different control environment than in the U.S. and other developed countries, it is still instructive to analyze cross-sectional differences in top management turnover at our sample of firms undergoing block transfers.

The results of this analysis appear in Table 6. Panel A of Table 6 shows that, for our full sample, the CEO was replaced at 22% of the firms within 3 months of the transfer, and at 38% of the firms within 12 months of the transfer. For the subsample of block transfers larger than 20%, CEO turnover is 30% within the 3 months of the transfer, and is 50% within the 12 months of the transfer.[23] By comparison, Barclay and Holderness (1991) report a 33 percent CEO turnover rate within the 12 months following negotiated block trades at a sample of U.S. listed firms. Also note that the turnover rates after block transfers are high compared to the average frequency with which CEOs are replaced at the typical listed Chinese firm, which, for our sample period, was 24 percent per annum.

In Panels B and C of Table 6, we document the impact of the identity of the seller and buyer on CEO turnover within the first 3 months after the transfer for our full sample of transfers greater than 5% (Panel B) and for our subsample of transfers greater than 20% (Panel

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[23] The likelihood of CEO turnover in the 3 months (12 months) following the transfer announcement for the 339 transfers that are smaller than 20 percent of the shares outstanding is 15 percent (27 percent), and is significantly smaller than the likelihood of CEO turnover following large transfers.

C). In Panel B, we see that the overall 21.7% frequency of CEO replacement within three months depends significantly on the seller, and is highest at 29% when *Private Entities* are the sellers and lowest when at 18% when *State Bureaucrats* are the sellers. The difference in CEO turnover across sellers is significant at the 10% level (p-value=0.07). We see a similar pattern across buyers, where CEO replacement is 22.3% when the buyers are *Private Entities* and lowest at 17.6% when the buyers are *State Bureaucrats*; however, differences across buyers are not statistically significant (p-value=0.62).

When we look only at block transfers in excess of 20 percent (Panel C), we find that the overall CEO replacement rate is much higher at 29.8%. Among sellers, we find statistically significant differences (p-value=0.03), ranging from 24.5% at *State Bureaucrats* to 28.9% at *MOSOEs* and 46.3% at *Private Entities*. We also find statistically significant differences (p-value=0.04) among buyers, ranging from 18.8% at *State Bureaucrats* to 28.9% at *MOSOEs* and 39.4% at *Private Entities*. These results are supportive of the hypothesis that the identity of the block holder is an important determinant of CEO turnover and suggest that CEO turnover is more likely when a *Private Entity* is involved and less likely when a *State Bureaucrat* is involved as either buyer or seller.

Finally, in Panel D of Table 6, we explore the reasons for CEO turnover using data from the GTA corporate governance database. GTA classifies the reason for CEO turnover into twelve categories that we collapse into seven: (1) *Change in Work Assignment*; (2) *Expiration of Term in Office*; (3) *Change of Controlling Shareholder*; (4) *Resignation*; (5) *Corporate Governance Improvement*; (6) *Missing*; and (7) *Other*.

In Columns 2-4 of Panel D are the results for CEO turnover during 1998-2002 at all listed Chinese firms. There are a total of 5,272 firm-years covered by these data. In Columns 5-7 of Panel D are the results for our full sample of 631 firms covering CEO turnover during the 3 months following the transfer announcements. There are a total of 631 firms × (3 months / 12 months) = 157.75 firm-years in this group. In columns 8-10 are the results for our full sample of

631 firms covering CEO turnover during the 12 months following the transfer announcements. There are 631 firms × (12 months / 12 months) = 631 firm-years in this group. For each of these three groups, we report the total number of CEO changes (columns 2, 5 and 8), the number of CEO changes per firm-year (columns 3, 6 and 9), and the percentage of the total number of CEO changes for that group accounted for by each reason identified in Column 1 (Columns 4, 7 and 10).

Most relevant are the numbers of CEO changes per firm-year (Columns 3, 6 and 9). CEO turnover attributable to a *Change of Share Controlling Rights* is 0.023 per firm year for all listed firms, 0.368 per firm year for our sample during the 3 months following the block transfer announcement and 0.124 for our sample during the 12 months following the block transfer announcement. Using the binomial test, we find that these proportions are significantly higher for our sample firms than for the total sample at better than the 1% level. The same result holds for the categories *Expiration of Term of Office*, *Resignation* and *Missing* in the three-month sample, and for *Expiration of Term of Office* and *Other* in the twelve-month sample.

Also relevant are the percentage of all CEO changes in each group accounted for by the *Change of Share Controlling Rights*. For all listed firms, *Change of Share Control Rights* accounts for 10% of all CEO turnovers; but for our sample, it accounts for 42% of the CEO changes that occur with 3 months and 33% of the CEO changes that occur with 12 months, of the block-transfer announcements. Clearly, these results demonstrate that the high incidence of CEO turnover in our sample is a direct result of the block transfers.

5.1.4 Univariate Robustness tests

We also reran the univariate analyses of CARs, ROA/ROE and CEO turnover appearing in Panels C of Tables 3, 4 and 6 where we subset our data based upon the 306 observations where transfer resulted in a change in the controlling shareholder (*Largest Change* = 1) rather than the 292 observations where the transfer was greater than 20% of the outstanding common shares. In general, these results, which are available from the authors upon request, are

qualitatively similar to those obtained where we subset based upon transfers greater than 20%. Relative to the full sample of 631 observations where the transfer is greater than 5%, average Seller CAR is larger (19.3% vs. 17.1%, average Seller ROA is larger (240 basis points vs. 140 basis points), and average Seller CEO turnover is greater (29.6% vs. 21.7%). However, the results of Test 1 (an *F*-test for statistically significant differences in the averages for the three types of sellers) are weaker (*p*-values = 0.68, 0.13 and 0.12 for Tables 3, 4 and 6, respectively) than those obtained where we subset on transfers greater than 20% (*p*-values = 0.05, 0.07 and 0.03 for Tables 3, 4 and 6, respectively). These univariate results suggest that differences among sellers are greater when new large block holders are included in the analysis, regardless of whether the transfer created a new controlling block holder.

5.2 Multivariate Cross-sectional Regressions

To provide additional evidence on the sources of abnormal returns, the changes in accounting performance and CEO turnover, we also perform cross-sectional regressions. For our multivariate analysis, we utilize the two-stage methodology suggested by Heckman (1979), where we first estimate the probability that a firm experienced a block transfer, and then estimate the relation between changes in ownership and performance, including the Inverse Mills' Ratio estimated from our selection equation to mitigate endogeneity concerns.

5.2.1 First-Stage Probit Regression

Table 7 presents the results from our first-stage probit regression to explain differences in firms that did and did not experience negotiated block transfers in each year. We have a total of 5,678 firm-year observations over the 1998-2002 period, of which 631 identify firm-years in which a block transfer took place. As explanatory variables, we focus on firm and performance characteristics. We include firm size and peer-adjusted return on assets in the previous year to account for the possibility that smaller and less profitable firms were chosen for these block transfers. We also include dummy variables indicating controlling ownership by *State*

Bureaucrats and *MOSOEs* to account for the possibility that these types of firms were chosen for block transfers disproportionately relative to the omitted category of *Private Entities*. Finally, we include the percentage ownership of the controlling shareholder to account for the possibility that smaller controlling blocks are more likely to be involved in transfers.

As shown in Table 7, each of our explanatory variables is negative and statistically significant at better than the 1% level. Because we estimate this equation primarily to obtain the inverse Mills' ratio for inclusion in subsequent regressions, we do not discuss these results in any more detail, other than to note that there are strong and significant differences in firms that did and did not experience block transfers, supporting the importance of employing a selection equation in our estimation.

5.2.2 Second Stage Regressions

In our second-stage regressions, we use various performance measures as our dependent variables and use the type of seller and buyer as our explanatory variables, along with several control variables and the Inverse Mills Ratio *Lambda* from our first-stage regression. For each of the dependent variables, we estimate the following cross-sectional regression model:

$$DV_i = \beta_0 + \beta_1 \text{ Seller Bureaucrat}_i + \beta_2 \text{ Seller MOSOE}_i + \beta_3 \text{ Buyer Bureaucrat}_i$$

$$+ \beta_4 \text{ Buyer MOSOE}_i + \beta_5 \text{ Related}_i + \beta_6 \text{ Largest Change}_i + \beta_7 \text{ PCT}_i$$

$$+ \beta_8 \text{ Leverage Ratio}_i + \beta_9 \text{ Size}_i + \beta_{10} \text{ } \Delta EXPROP + \beta_{11} \text{ Lambda}_i + \varepsilon_i$$

where:

DV_i is, for firm *i*, the 250–day or 5–day cumulative abnormal return; the change in peer-adjusted return on assets or peer-adjusted return on equity; or a dummy variable that is equal to one if the CEO was replaced in the first 3 months or 12 months after the transfer announcement.

Seller-Bureaucrat$_i$, Seller-MOSOE$_i$ Buyer-Bureaucrat$_i$ and Buyer-MOSOE$_i$ are dummy variables indicating the type of negotiated block transfer; *Seller-Private* and *Buyer-Private* are the omitted categories, so the coefficient on each of the *Seller* and *Buyer* dummy variables

measures the difference in the dependent variable (DV) of that category and the dependent variable of transfers involving *Private Entities*.

Related$_i$ is a dummy variable indicating that the buyer is a related party of the seller. Parties are related if, one party is directly or indirectly controlling or controlled by another party, or both parties are under the control of the same enterprise. We expect the benefits of block transfers to be lower when the transfer is to a related party.

Largest Change$_i$ is a dummy variable indicating that the transfer created a new controlling block holder for firm *i*. It might be important to distinguish between a transfer that creates a new controlling block holder and one that does not. When the block transfer creates a new largest shareholder, there has been a change in corporate control. According to Barclay and Holderness (1991), block transfers as small as 10% of outstanding shares can transfer *de facto* control rights. Because of the strong position of the controlling shareholder in China, we expect the positive effects of the block transfers to be larger when the new block holder obtains a controlling share.

Percentage Transferred $_i$ is defined as the number of shares that is transferred in the block transfer as percentage of the shares outstanding.

As general control variables, we include:

Leverage Ratio as measured by the ratio of total debt to total assets;

Firm Size as measured by the natural logarithm of the firm's total assets;

Lambda, the Inverse Mills Ratio from the first-stage probit selection model; and

ΔEXPROP, our ex-post measure of the change in the level of expropriation.

We expect that excess returns and operating performance improvement will be larger at firms with greater informational asymmetries, as agency costs are expected to increase with the level of informational asymmetries. Because larger firms are less opaque than smaller firms, we hypothesize that excess returns will be inversely related to firm size. In Western economies, firms with greater leverage are subject to more stringent monitoring by large creditors,

including commercial banks, so that informational asymmetries should be smaller than at firms with greater leverage. However, in China, commercial banks are often directed by the State to make policy loans, so that banks do not serve this monitoring role in China. Instead, banks are directed by the State to make additional loans to poorly performing firms, increasing their leverage over time. Hence, we expect that excess returns will be positively related to the debt-to-asset ratio, as the worst performing firms have the most to gain from improved governance.[24] We include *Lambda* to mitigate concerns about endogeneity, and *ΔEXPROP* to control for changes in the level of expropriation of minority shareholders.

Table 8 presents the results of our cross-sectional regression models. For each dependent variable, we first present the results for the full sample of transfers greater than 5%, and then, in the next column, report the results for the subsample of transfers greater than 20%.

5.2.3 Cumulative Abnormal Returns

In Columns 2 and 3 of Table 8, we use the 250–day CAR as our dependent variable. Column 2 reports the results for the full sample, and Column 3 reports the results for the sample of transfers that are larger than 20% of the shares outstanding. Both *Seller Bureaucrat* and *Seller MOSOE* are positive and statistically significant at better than the 5% level. Both *Buyer Bureaucrat* and *Buyer MOSOE* are negative, as expected, but lack statistical significance. The dummy variables also are economically significant. *Ceteris paribus*, transfers from *State Bureaucrats* to *Private Entities* result in a 250-day CAR that is 12.4% larger than that for transfers between *Private Entities* (the omitted dummy variables) for the full sample; for the subsample of transfers greater than 20%, this difference is 25.8%.

The results using the 5-day CARs appear in Columns 4 and 5 of Table 8, and generally are consistent with those using the 250-day CARs; both Seller Bureaucrat and Seller MOSOE are positive and statistically significant at better than the 5% level, although the magnitudes are

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[24] We have estimated all models including year dummy variables, industry dummy variables and exchange dummy variables. Our results are robust to inclusion of these dummy variables.

much smaller, in the range of 1% to 2%. These results again suggest that investors perceive *Private Entities* to be superior monitors relative to *State Bureaucrats* and *MOSOEs*.

The coefficient of *Related* is insignificant in all four models, indicating that investors do not perceive the value change resulting from transactions between related parties as different from transactions between unrelated parties.

The coefficient of *Largest Change* is insignificant. We had expected that transfers creating a new controlling block holder would be associated with greater cumulative abnormal returns, but this does not appear to be the case when we control for the type of block transfer. Similarly, *Percentage* is only weakly related to the 250-day or the 5-day CARs.

Contrary to our expectations, we find that firms with lower *Leverage* experience larger value increases over the 250-day period. Consistent with our expectations, *Firm Size* is negative and statistically significant at better than the 1% level in all four models, indicating that size is negatively related to the increase in firm value. This smaller value increase for larger firms could reflect the lower information asymmetry at larger firms. The negative relation between firm size and the value change could also indicate that it is more difficult to restructure a larger firm.

In summary, the cross-sectional analysis of cumulative abnormal returns shows no consistent evidence that *State Bureaucrats* are less effective monitors than *MOSOEs*. However, we do find consistent evidence that investors perceive *Private Entities* as the most effective monitors of listed firms.

5.2.4 Changes in Accounting Performance

Columns 6-9 of Table 8 present the results for changes in peer-adjusted return on assets (Columns 6-7) and peer-adjusted return on equity (Columns 8-9). The evidence in these four columns consistently shows that improvements in operating performance are larger and statistically significant where *Private Entities* replace *State Bureaucrats* or *MOSOEs* as the block holder. The coefficients indicate that, relative to transfers between *Private Entities* (the

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omitted dummy variables), very substantial improvements in ROA of 260 basis points or more are realized after block transfers from *State Bureaucrats* or *MOSOEs* to *Private Entities*. The results for the subsample of transfers greater than 20% are even stronger at 530 basis points or more.

Using ROE as performance measure (columns 8-9), we find that relative improvements are 520 basis points or more in the full sample, and 810 basis points or more in the subsample of transfers greater than 20%. If a block is sold to a *State Bureaucrat*, performance is significantly worse relative to having a *Private Entity* as the buyer. However, when a *MOSOE* is the new owner, the listed firm does not significantly under-perform listed firms where a *Private Entity* is the new owner.

The coefficients of *Largest Change* and *Percentage* are insignificant. As before, we had expected that transfers creating a new controlling block holder would be associated with greater improvements in accounting-based performance measures, but this does not appear to be the case when we control for the type of block transfer.

With the exception of firm size, all control variables are insignificant. The negative relation between the improvement in firm performance and firm size suggests that it is more difficult for new block holders to transform larger firms.

5.2.5 CEO turnover

In Columns 10 through 13 of Table 8 are the results from a logistic regression, where the dependent variable is an indicator variable that is equal to one if the firm's CEO was replaced within 3 months (Columns 10-11) or twelve months (Columns 12-13) of the block trade announcement. In each cell, we now report the marginal effect with the *t*-statistic underneath.

After inclusion of the control variables, we find only limited evidence that the ownership type affects CEO replacement. For the full sample, replacement of the CEO within 3 months is significantly lower by 10 percentage points when a *State Bureaucrat* is seller. This

coefficient falls to 8 percent when we use CEO replacement within 12 months as dependent variable, and loses statistical significance at standard levels (*p*-value=0.15).

The control variables are more effective in explaining CEO turnover. The variable *Related* is negative and significant, suggesting that the probability of CEO replacement within 12 months is lower if the block is transferred to a related party. The variable *Largest Change*, which indicates that the new block holder is also a new controlling block holder, is positive and generally significant, indicating that changes in direct control lead to a greater probability of CEO turnover. Contrary to our expectations, we do not find that *Leverage* is related to CEO turnover. However, *Size* is negative and generally significant, indicating that larger firms are significantly less likely to experience a change in top management following a block transfer. We speculate that this result also may be a consequence of the stronger political connections of CEOs at China's larger firms.

6. Summary and Conclusions

In this study, we analyze share price reactions and changes in accounting performance around the announcements of negotiated block transfers between different ownership structures, using a sample of firms that are publicly traded on Chinese stock exchanges. We also analyze top-management turnover following these block transfers.

First and foremost, we find positive abnormal returns around the announcements of the block transfers, consistent with Barclay and Holderness (1991) that block transfers are control events. Moreover, we find that both changes in firm value and accounting performance are significantly greater when ownership is transferred from *State Bureaucrats* or *Market-Oriented SOEs*, than when ownership is transferred from *Private Entities*. The improvements in performance following block transfers from State-controlled entities to private owners indicates that the latter are better equipped and have greater incentives to monitor and discipline firm management than are the former. This result is consistent with a superior incentives and

expertise of private block holders relative to State-controlled block holders. We find no consistent evidence that *Market-Oriented SOEs* are superior monitors relative to *State Bureaucrats*. This result is important, as it suggests that the intermediate step of "corporatizing" organizations that act as block holders is an ineffective mechanism for dealing with the agency problems that result from State ownership.

Our results provide strong evidence that the block transfers between the different ownership categories are true control events, as defined by Barclay and Holderness (1991). First, they result in large positive cumulative abnormal returns of more than 10%, and the cross-sectional variation in these abnormal returns can be explained by differences in identities of the block holders. Second, the block transfers are followed by top management changes within 3 months of the transfer at more than 20% of the sample firms. Our interpretation of these block transfers as significant control events is further corroborated by the evidence that the value changes around transfers are strongly correlated with improvements in accounting performance around the block transfer. Hence, we contribute new evidence from Chinese markets confirming that the identity of the block holder is an important determinant of firm value.

Finally, it is remarkable that the improvements in performance around the block transfers to private entities in our sample are substantially larger than the changes in performance observed after Share-Issue Privatization (SIP) in China (see Sun and Tong, 2003). The common explanation for the limited success of the SIP process in China is that the SIPs failed to transfer true control from the State to the private sector and only helped to create many dispersed and powerless owners of Tradable A shares. Our evidence is consistent with this explanation and shows that substantial value increases are realized when the State relinquishes substantial control rights to private block holders. Of great interest is how further or complete privatization of listed State-controlled firms will affect firm value. Many such transfers of control are now taking place in China, and we leave this as an interesting avenue for future research.

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Appendix 1

Shares are classified based on the residency of their owner as *domestic* (A shares) or *foreign* (B, H and N shares). The B, H, and N shares are traded on the Chinese, Hong Kong, and New York Stock Exchanges, respectively. *Tradable B* shares used to be available exclusively to foreign investors and some authorized domestic securities firms. However, the Chinese government recently opened the B-share market to domestic investors. The B-share market is separated from the A-share market, with SHSE B-shares denominated in U.S. dollars, and SZSE B-shares denominated in Hong Kong dollars. *Tradable H* shares and *Tradable N* shares are essentially the same as *Tradable B* shares, except that they are issued and traded on the Hong Kong Stock Exchange and the New York Stock Exchange, respectively.

Appendix 2:
Examples of Share Price Manipulation in China

One example of share price manipulation is the Zhongke Changye scandal (See Business China, March 26th 2001, pp. 2-3, "Scam of the century"). This particular case started with a sharp decrease in the stock price of Zhongke Changye—a listed chicken farm—due to an outbreak of bird flu in 1998. The share price dropped to around 14 Rmb in Oct 1998. Mr. Lu convinced the largest holder of tradable shares of Zhongke Changye—Mr. Zhu—to transfer blocks of tradable shares to him and persuaded several block holders to transfer their State shares to high tech companies owned by him. Mr. Lu, who now effectively controlled the firm, was in a position to manipulate the flow of public information. In addition, he used thousands of ID cards to open new individual share holder accounts, which were used to buy shares. In this process, Mr. Lu used the newly purchased shares as collateral to buy even more shares. The share price increased to about 40 Rmb in May 1999 when Mr. Zhu (unbeknownst to Mr. Lu) started selling. Still, the share price increased further and reached a high of 84 Rmb in February 2000 before it collapsed and the scam was revealed.

Another example is the Yellow River Chemical scandal (SHSE ticker 600091). This case began on December 23, 1998, with the sale of a subsidiary of Yellow River to Baotuo Chuangye. Baotuo Chuangye, in turn, was partially owned by Beida Tomorrow Materials Science & Technology Co., Ltd. ("Beida Materials")—a firm linked to the Beijing University group. Sale of the subsidiary resulted in more than 30 percent increase in Yellow River Chemical's profits, which would give the firm the right to issue new shares. On July 29, 1999, press reports announced that Beida Materials had bought 47 percent of the shares of the parent of Yellow River—Baotou Chemical Industry Group. When the transfer was announced, the share price of Yellow River Chemical was 24.5 Rmb—almost double its 12.8 Rmb price two months earlier. The gradual increase in share price during the two months before the announcement was allegedly attributable to insider trading. Supposedly, insiders were buying Yellow River Chemical shares in anticipation of a positive reaction of investors to the share

transfer, which suggested a move away from the chemical industry into the high tech industry. However, in the six weeks following the announcement, the share price of Yellow River Chemical dropped almost 20 percent, which was attributed to profit taking by insiders. (See Larry Lang in New Fortune magazine, August 2001)

A very similar incident, where a block transfer suggested a link to Beijing University, took place on August 25, 1999 when 51 percent of the shares in the second largest shareholder of Huazi Shiye (SHSE ticker 600191) were transferred to Beida Materials. In the three months prior to the transfer announcement, the share price of Huazi Shiye increased from 13.3 RMB to 22.58 RMB; in the three months subsequent to the transfer announcement, Huazi Shiye's share price declined to 15.6 RMB.

It is noteworthy that, in both the Yellow River Chemical and Huazi Shiye examples, the block transfer took place in the shares of a firm that controlled a listed firm, rather than in the shares of the listed firm itself. It is easier to conduct such transfers anonymously because disclosure requirements are much less stringent for share transfers of unlisted firms.

Appendix 3:
Reasons for CEO Turnover

The 13 categorized reasons for CEO turnover available from the GTA corporate governance database are: (1) change of work assignment—the CEO was removed from the position because of being assigned another position; (2) retirement—the CEO no longer held the position because of retirement or age; (3) expiration of term of office—the CEO no longer held the position because her term expired and she was not re-elected; (4) change of share-controlling rights—the CEO no longer held the position because of a change in the identity of the controlling shareholder ; (5) resignation—the predecessor voluntarily resigned the position for unknown reasons; (6) dismissal—a listed company dismissed the predecessor for unknown reasons; (7) health related reason—the predecessor no longer held the position because of bad health, including death; (8) personal reason—the CEO no longer held the position because of personal reasons; (9) corporate governance improvement—improving corporate governance led to the CEO no longer holding the position; (10) litigation involved—the CEO was removed from office because of involvement in litigation; (11) others; (12) end of proxy—the CEO holding the position in deputy no longer exercised the duty because of end of the deputy; and (13) not disclosed. We combine (2), (6), (7), (8), (10), (11) and (12) into our "other" category because of the small numbers of CEO turnovers accounted for these categories.

Appendix Table 1:
Panel A
Summary of Privatization Studies

Authors	Sample	Finding
Multi-Country Studies		
Boardman and Vining (1989)	500 largest non-U.S. industrial firms as compiled by Forbes magazine in 1983.	Find that mixed enterprises perform at least as well as SOEs, and that private enterprises outperform both mixed enterprises and SOEs in terms of profitability.
Megginson, Nash and Randenborgh (1994)	61 SOEs from 18 countries in 32 industries that were partially or completely privatized during 1961-90.	Find significant increases in sales, profitability, capex spending, dividend payouts, operating efficiency and employment and significant decreases in leverage.
Boubakri and Cosset (1998)	79 SOEs in 21 developing countries that underwent partial or complete share-issuance privatizations during 1980-92.	Find significant increases in profitability, operating efficiency, capex spending, output, employment and dividends.
D'Souza and Megginson (1999)	85 share-isuance privatizations from 28 industrialized countries that occurred from 1990-96.	Find significant increases in profitability, output, operating efficiency and divdend payments and significant decreases in leverage following privatization.
Jones, Megginson, Nash, and Netter (1999)	630 share-issuance privatizations in 59 countries during 1977-97	The State consistently underprices SIP offerings, favor domestic investors in share allocations, impose control restrictions, and typically use fixed-price issues.
Boubakri, Cosset and Guedhami (2005a, b)	209 privatized firms from 325 emerging-market and 14 industrial countries during 1980-2001.	Private ownership, primarily by local institutions, grows more concentrated over time. Investor protection and both social and political stability, as well as firm size, growth and industry, are important determinants of ownership concentration.
D'Souza, Megginson and Nash (2005)	129 share-issuance privatizations from 23 OECD countries during 1961-1999.	Post-privatization performance improvements in developed countries result from changes in government and foreign ownership affecting employment and capital expenditures.
Kole and Mulherin (1997)	17 U.S. firms owned by German and Japanese companies and seized by the government during and following WWII.	Performance of government-owned firms was not significantly different from that of privately owned firms in the same industry.
Dewenter and Malatesta (2001)	1,369 firm-year observations on government-owned and privately owned firms sampled from the 500 largest corporations worldwide as reported by Forbes magazine in 1975, 1985 and 1995.	Government-owned firms are consistently less profitable than privately owned firms. Profitability improves prior to, but declines subsequent to, share-issuance privatization of government-owned firms.

Appendix Table 1:
Panel B
Summary of Partial Privatization Studies

Authors	Sample	Finding
Partial Privatization		
Groves, Hong, McMillan and Naughton (1995)	769 Chinese SOEs surveyed during 1980-89.	When authority shifts from the State- to the firm-level and firms were allowed to retain more of their profits, firm managers improved workers' incentives, resulting in increased productivity.
Li (1997)	Panel data on 272 Chinese SOEs between 1980 and 1989.	New incentive mechanisms put into place led to greater product market competition and better factor allocation, even without formal privatization.
Aivazian, Ge and Qiu (2005)	429 Chinese SOEs restructured into corporations under the Corporate Law of 1993	Corporatization significantly improved performance as measured by profitability and efficiency.
Allen, Qian and Qian (2005)	State, listed and private sectors of the Chinese economy during 1997-2002.	Rapid economic growth was driven by the private sector. Within the listed sector, dividend yields and firm values are lower than those of comparable firms in countries with better legal protection.
Sun and Tong (2003)	634 Chinese firms that were partially privatized by IPOs during 1994-98.	Sales, earnings and productivity improve but profitability deteriorates following partial privatization by initial public offerings.
Wei, Varela, D'Souza and Hassan (2003)	208 Chinese corporations that were partially privatized during 1990-97.	Following share issuance, real output, real assets and sales efficiency improve while leverage declines, but profitability is unchanged.
Gupta (2005)	339 Indian SOEs partially privatized during 1990-2000.	Partial privatization significantly improves performance and the source of the gains is a reduction in agency costs that improve firm efficiency.
Wei, Xie and Zhang (2005)	5,284 firm-year observations for Chinese firms that were partially privatized during 1991-2001.	State and legal-person ownership are negatively related while foreign ownership is positively related to firm value as measured by Tobin's Q.
Fan, Wong and Zhang (2007)	790 partially privatized Chinese firms during 1993-2001.	Politically connected firms exhibit sigificantly inferior performance relative to their unconnected counterparts, on both accounting and market-value bases.
Deng, Gan and He (2007)	295 Chinese SOEs that went public during 1997 - 2000.	Parent-company block holders are more llikely to tunnel resources from listed firms than are other types of block holders.

Table 1:
Share classifications for the Chinese Stock Market for 1993-2002 based upon NUS ownership categories

	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002
State Bureaucrat	53	77	121	166	179	160	144	153	154	155
MOSOE	46	71	141	277	462	572	681	796	836	888
Private Entity	13	12	23	35	44	63	78	103	121	155
Foreign Entity	9	10	13	18	16	13	11	15	13	13

This table reports share classifications for the Chinese Stock Market for 1993-2002 based upon NUS ownership categories. *State Bureaucrat* is a dummy variable equal to one if the largest block holder classified as a State Bureaucrat; *MOSOE* is a dummy variable equal to one if the largest block holder is a market-oriented State-owned enterprise; *Private Entity* is a dummy variable equal to one if the largest block holder is a private entity. *Foreign* is a dummy variable equal to one if the largest block holder is a foreign entity. Because of their small number, we exclude foreign entities from the remainder of our analysis, so that we are left with only three ownership categories. Classifications are based upon 17 detailed categories of ultimate ownership established by researchers at the National University of Singapore ("NUS") as described in Delios *et al*. (2006). Note that NUS researchers were unable to classify ultimate ownership for a small number of firms in some years. *Source*: Authors' tabulations based upon NUS ownership categories.

Table 2:
Descriptive Statistics for Negotiated Block Transfers

Panel A: Descriptive Statistics

	Mean	Std. Dev.	Minimum	Maximum
Shares Transferred	22.0	15.5	5.0	74.8
Size	20.5	0.8	18.1	23.8
Leverage	0.47	0.29	0.01	4.87
Peer-adjusted ROA	-0.008	0.067	-0.403	0.284
Change in EXROP	0.009	0.141	-2.310	1.550

Panel B: Number of Transfers for each Seller/Buyer pair

	Buyer			
	State		*Private*	
Seller	*Bureaucrat*	*MOSOE*	*Entity*	*All*
State Bureaucrat	38	80	49	167
MOSOE	39	187	114	340
Private Entity	8	41	75	124
All	85	308	238	631

Panel C: Transfer Percentage for each Seller/Buyer pair

	Buyer				
	State		*Private*		
Seller	*Bureaucrat*	*MOSOE*	*Entity*	*All*	
State Bureaucrat	28.24	31.12	17.64	26.51	
MOSOE	22.67	25.18	16.34	22.01	Test 1:
Private Entity	21.05	17.76	14.80	17.64	p-value = 0.01
All	25.01	25.73	16.12	22.01	

Test 2: p-value = 0.01

Panel D: Firm Size for each Seller/Buyer pair

	Buyer				
	State		*Private*		
Seller	*Bureaucrat*	*MOSOE*	*Entity*	*All*	
State Bureaucrat	20.61	20.57	20.37	20.52	
MOSOE	20.66	20.61	20.47	20.58	Test 1:
Private Entity	19.92	20.09	20.21	20.09	p-value = 0.01
All	20.57	20.53	20.37	20.48	

Test 2: p-value = 0.05

Panel E: Leverage for each Seller/Buyer pair

		Buyer				
		State		*Private*		
Seller		*Bureaucrat*	*MOSOE*	*Entity*	*All*	
State Bureaucrat		0.445	0.485	0.483	0.48	
MOSOE		0.475	0.468	0.486	0.48	Test 1:
Private Entity		0.381	0.440	0.441	0.43	*p*-value = 0.46
All		0.45	0.47	0.47	0.47	
		Test 2: *p*-value = 0.87				

Panel F: Peer-Adjusted ROA for each Seller/Buyer Pair

	Buyer				
	State		*Private*		
Seller	*Bureaucrat*	*MOSOE*	*Entity*	*All*	
State Bureaucrat	-0.006	-0.006	-0.018	-0.009	
MOSOE	0.003	-0.015	-0.009	-0.011	Test 1:
Private Entity	0.019	0.004	0.002	0.004	*p*-value = 0.11
All	0.001	-0.010	-0.007	-0.008	
	Test 2: *p*-value = 0.44				

Panel G: Change in Level of Expropriation for each Seller/Buyer Pair

	Buyer				
	State		*Private*		
Seller	*Bureaucrat*	*MOSOE*	*Entity*	*All*	
State Bureaucrat	0.006	0.018	0.02	0.016	
MOSOE	-0.005	0.028	-0.018	0.009	Test 1:
Private Entity	0.006	-0.009	0.008	0.001	*p*-value = 0.70
All	0.001	0.021	-0.002	0.009	
	Test 2: *p*-value = 0.12				

This table reports descriptive statistics for our sample of 631 observations of block-share transfers between different ownership categories during 1998-2002. Panel A presents descriptive statistics for five variables: *Shares Transferred* is the percentage of total common shares transferred in the block trade; *Size* is the natural logarithm of the book value of total assets; *Leverage* is measured by ratio of the book value of total liabilities to the book value of total assets; and *Peer-Adjusted ROA* is the firm's core EBITDA divided by the book value of total assets as of year-end less core EBITDA divided by the book value of total assets for a matched firm, where matched firms are in the same industry and have the lowest absolute value of the difference in the ratio of core EBITDA over total assets in the pre-transfer year relative to the sample firm across all firms in the same industry. *EXPROP* is the level of expropriation as proxied by the value of potentially harmful related-party transactions observed during the year before and during the year after the year of the block transfer and scaled by total assets, as described in Berkman, Cole and Fu (2010). Panel B presents the number of transfers for each seller/buyer pair. Panel C presents the percentage of shares transferred for each seller/buyer pair. Panel D presents the firm size for each seller/buyer pair. Panel E presents firm leverage for each seller/buyer pair. Panel F presents peer-adjusted ROA for each seller/buyer pair. Panel G presents the change in EXPROP for each seller/buyer pair. *Seller* refers to the party selling the block of shares while *Buyer* refers to the party purchasing the block of shares. There are three ownership categories (*State Bureaucrat*, *MOSOE* and *Private Entity*) so there are nine combinations of buyer and seller. *State Bureaucrat* is a dummy variable equal to one if the largest block holder is classified as a State Bureaucrat; *MOSOE* is a dummy variable equal to one if the largest block holder is classified as a market-oriented State-owned enterprise; *Private Entity* is a dummy variable equal to one if the largest block holder is classified as a private entity. Classifications are based upon 17 detailed categories of ultimate ownership established by researchers at the National University of Singapore ("NUS") as described in Delios *et al*. (2006). Test 1 (Test 2) refers to the *p*-value from an *F*-test for equality of means across the three different types of sellers (buyers).

Table 3:
Cumulative Abnormal Returns around Announcements of Negotiated Block Transfers
By Type of Block Transfer

Panel A: Cumulative Abnormal Returns around transfer announcements

		N	Mean	Std. Dev.	t-statistic	Minimum	Maximum
Transfers	CAR(-210,40)	631	0.171 ***	0.370	11.59	-1.46	2.33
Greater than 5%	CAR(-3,1)	631	0.011 ***	0.043	6.57	-0.32	0.20
Transfers	CAR(-210,40)	292	0.210 ***	0.402	8.91	-1.47	1.49
Greater than 20%	CAR(-3,1)	292	0.017 ***	0.048	6.21	-0.10	0.20

Panel B: CARs for transfers > 5% of Common Shares by Type of Transfer

	Buyer				
Seller	*State Bureaucrat*	*MOSOE*	*Private*	*All*	
State Bureaucrat	0.172 ***	0.214 ***	0.250 ***	0.216 ***	
	38	80	49	167	
MOSOE	0.111 ***	0.185 ***	0.158 ***	0.167 ***	
	39	187	114	340	
Private	0.106	0.106	0.128 ***	0.119 **	Test 1:
	8	41	75	124	*p*-value=0.04
All	0.138 ***	0.181 ***	0.166 ***	0.171 ***	
	85	308	238	631	

Test 2: *p*-value=0.62

Panel C: CARs for transfers > 20% of Common Shares by Type of Transfer

	Buyer				
Seller	*State Bureaucrat*	*MOSOE*	*Private*	*All*	
State Bureaucrat	0.209 ***	0.266 ***	0.336 ***	0.264 ***	
	27	56	19	102	
MOSOE	0.171	0.198 ***	0.246 ***	0.205 ***	
	17	99	33	149	
Private	-0.026	0.039	0.168 **	0.093	Test 1:
	4	18	19	41	*p*-value=0.05
All	0.176 ***	0.203 ***	0.249 ***	0.210 ***	
	48	173	71	292	

Test 2: *p*-value = 0.58

This table presents cumulative abnormal returns around announcements of block transfers, by the type of block transfer. Cumulative abnormal returns around announcements of block transfers are calculated as the difference between the realized return and the market return using the market-adjusted return model. To estimate the market-adjusted model, we use as the market index either the Shanghai Stock Exchange (SHSE) or Shenzhen Stock Exchange (SZSE) composite index, depending on where the firm's stock is listed. Our primary event window spans day *t–210* through day *t+40*. We also examine abnormal returns from a shorter five-day window from day *t–3* through day *t+1*. The sample consists of 631 observations of block share transfers of more than five percent of common shares between different ownership categories during 1998-2002. There are three ownership categories (*State Bureaucrat*, *MOSOE* and *Private Entity*) so there are nine combinations of buyer and seller. *State Bureaucrat* is a dummy variable equal to one if the largest block holder is classified as a State Bureaucrat; *MOSOE* is a dummy variable equal to one if the largest block holder is classified as a market-oriented State-owned enterprise; and *Private Entity* is a dummy variable equal to one if the largest block holder is classified as a private entity. Classifications are based upon 17 detailed categories of ultimate ownership established by researchers at the National University of Singapore ("NUS") as described in Delios *et al.* (2006). Panel A presents results for the full sample of 631 transfers, while Panel B presents detailed results by ownership classification for the full sample of 631 transfers greater than 5% of shares, and Panel C presents detailed results for 292 block transfers greater than 20% of shares.
*, ** and *** indicates statistical significance at the 10%, 5% and 1% levels, respectively.

Table 4:
Changes in Accounting Performance
Surrounding Negotiated Block Transfers at Listed Chinese Firms
Panel A: Changes in ROA and Changes in ROE

		N	Mean	Std. Dev.	t-stat	Minimum	Maximum
Transfers	Δ ROA	525	0.014 ***	0.100	3.19	-0.396	0.517
> 5%	Δ ROE	525	0.019 **	0.172	2.28	-0.526	0.679
Transfers	Δ ROA	249	0.017 ***	0.105	2.55	-0.396	0.381
>20%	Δ ROE	249	0.029 **	0.179	2.29	-0.455	0.527

Panel B: Changes in ROA for Transfers > 5% of Common Shares by Type of Transfer

			Buyer			
Seller	*State Bureaucrat*	*MOSOE*	*Private*	*All*		
State Bureaucrat	0.012	0.014 *	0.024 **	0.017 ***		
	34	67	36	137		
MOSOE	-0.026 **	0.026 **	0.023 **	0.019 ***		
	34	162	89	285		
Private	-0.021	-0.002	-0.002	-0.003	Test 1:	
	7	36	60	103	p-value=0.15	
All	-0.008 *	0.019 ***	0.016 **	0.014		
	75	265	185	525		

Test 2: p-value=0.04

Panel C: Changes in ROA for Transfers > 20% of Common Shares by Type of Transfer

			Buyer			
Seller	*State Bureaucrat*	*MOSOE*	*Private*	*All*		
State Bureaucrat	0.008	0.018	0.057 ***	0.023 **		
	24	48	15	87		
MOSOE	-0.009	0.025 **	0.038 **	0.024 **		
	15	84	27	126		
Private	-0.067	0.000	-0.024	-0.019	Test 1:	
	2	17	17	36	p-value=0.07	
All	-0.004	0.020 **	0.026 **	0.017		
	41	149	59	249		

Test 2: p-value=0.31

This table reports changes in accounting performance surrounding negotiated block transfers at listed Chinese firms. Changes in accounting performance are measured by the changes in peer-adjusted return on assets (ROA) or peer-adjusted return on equity (ROE) from the two years prior to the block transfer to the two years subsequent to the block transfer. The sample consists of 631 observations of block share transfers of more than five percent of common shares between different ownership categories during 1998-2002. There are three ownership categories (*State Bureaucrat*, *MOSOE* and *Private Entity*) so there are nine combinations of buyer and seller. *State Bureaucrat* is a dummy variable equal to one if the largest block holder is classified as a State Bureaucrat; *MOSOE* is a dummy variable equal to one if the largest block holder is classified as a market-oriented State-owned enterprise; *Private Entity* is a dummy variable equal to one if the largest block holder is classified as a private entity. Classifications are based upon 17 detailed categories of ultimate ownership established by researchers at the National University of Singapore ("NUS") as described in Delios *et al.* (2006). Panel A presents results for the full sample of 631 transfers, while Panel B presents detailed results by ownership classification for the full sample of 631 transfers greater than 5% of shares, and Panel C presents detailed results for 292 block transfers greater than 20% of shares.

*, ** and *** indicates statistical significance at the 10%, 5% and 1% levels, respectively.

Table 5:
Correlations between CARs and Changes in Accounting Performance

	CAR (t-210, t+40)	CAR (t-3, t+1)
Change in ROA	0.258 ***	0.111 ***
Change in ROE	0.309 ***	0.168 ***

This table presents the Spearman correlation coefficient between the cumulative abnormal return around 525 block transfers of listed firms in China in the period 1998 through 2002 and changes in peer-adjusted return on assets and return on equity. We use the market-adjusted return model to calculate daily abnormal returns as the difference between the realized return and the market return. The CAR is measured over a window that spans day t-210 through day t+40, and a 5-day window from day t-3 through day t+1. *ROA* is the firm's core EBITDA divided by the book value of total assets as of year-end less EBITDA divided by the book value of total assets for a matched firm, where matched firms are in the same industry and have the lowest absolute value of the difference in the ratio of EBITDA over total assets in the pre-transfer year relative to the sample firm across all firms in the same industry.   Peer-adjusted return on equity (ROE) is defined analogously, but is based on the firm's core EBITDA divided by the book value of equity as of year-end.   Change in ROA/ROE is the difference in the average for the two years prior to the announcement and the average for two years subsequent to the announcement. The year of the announcement is excluded from the analysis.

*, ** and *** indicates statistical significance at the 10%, 5% and 1% levels, respectively.

Table 6:
CEO Turnover following Announcements of Block Transfers

Panel A: CEO Turnover in the 3 Months, or 12 Months, After Transfer Announcement

	N	Mean	Std Dev.	t-stat	Minimum	Maximum
Transfers > 5%						
Within 3 months	631	0.22 ***	0.41	13.2	0	1
Withing 12 months	631	0.38 ***	0.49	19.5	0	1
Transfers > 20%						
Within 3 months	292	0.30 ***	0.46	11.1	0	1
Within 12 months	292	0.50 ***	0.50	16.9	0	1

Panel B: CEO Turnover in the 3 months After Announcements of Block Transfers > 5%

	Buyer				
Seller	*State Bureaucrat*	*MOSOE*	*Private Entity*	*All*	
State Bureaucrat	0.211 ***	0.175 ***	0.163 ***	0.180 ***	
	38	80	49	167	
MOSOE	0.103 ***	0.214 ***	0.237 ***	0.209 ***	Test 1:
	39	187	114	340	p-value=0.07
Private Entity	0.375 ***	0.366 ***	0.240 ***	0.290 ***	
	8	41	75	124	
All	0.176 ***	0.224 ***	0.223 ***	0.217 ***	
	85	308	238	631	

Test 2: p-value=0.62

Panel C: CEO Turnover in the 3 Months After Block Transfers > 20%

	Buyer				
Seller	*State Bureaucrat*	*MOSOE*	*Private Entity*	*All*	
State Bureaucrat	0.185 ***	0.232 ***	0.368 ***	0.245 ***	
	27	56	19	102	
MOSOE	0.118 ***	0.293 ***	0.364 ***	0.289 ***	Test 1:
	17	99	33	149	p-value=0.03
Private Entity	0.500 ***	0.444 ***	0.474 ***	0.463 ***	
	4	18	19	41	
All	0.188 ***	0.289 ***	0.394 ***	0.298 ***	
	48	173	71	292	

Test 2: p-value=0.04

Panel D: Reason for CEO Turnover

	All Firms 1998-2002			Transfer >5% Sample CEO Change < 3 months			Transfer >5% Sample CEO Change < 12 months		
Reason for CEO Turnover	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)
Change of Work Assignment	345	0.065	0.28	14	0.089	0.10	43	0.068	0.18
Expiration of Term of Office	290	0.055	0.23	28	0.178 ***	0.20	54	0.086 ***	0.23
Change of Share Controlling Right	120	0.023	0.10	58	0.368 ***	0.42	78	0.124 ***	0.33
Resignation	229	0.043	0.18	24	0.152 ***	0.18	37	0.059 *	0.16
Corporate Governance Improvement	31	0.006	0.03	0	0.000	0.00	3	0.005	0.01
Missing	77	0.015	0.06	9	0.057 ***	0.07	14	0.022	0.06
Other	148	0.028	0.12	4	0.025	0.03	9	0.014 ***	0.04
Total	1,240	0.235	1.00	137	0.869	1.00	238	0.377	1.00

This table reports CEO turnover during the 3 months, or 12 months, following announcement of 631 negotiated block transfers of at least 5% of common shares between different ownership categories for listed firms in China during 1998–2002. There are three ownership categories (*State Bureaucrat*, *MOSOE* and *Private Entity*) so there are nine combinations of buyer and seller. *State Bureaucrat* is a dummy variable equal to one if the largest block holder is classified as a State Bureaucrat; *MOSOE* is a dummy variable equal to one if the largest block holder is classified as a market-oriented State-owned enterprise; *Private Entity* is a dummy variable equal to one if the largest block holder is classified as a private entity. Classifications are based upon 17 detailed categories of ultimate ownership established by researchers at the National University of Singapore ("NUS") as described in Delios *et al*. (2006). Panel A presents results for the full sample of 631 transfers, while Panel B presents detailed results by ownership classification for the full sample of 631 transfers greater than 5% of shares, and Panel C presents detailed results for 292 block transfers greater than 20% of shares. Panel D reports the reasons for CEO changes during 1098-2002 at all Chinese listed firms and separately for the 137 (238) firms in our sample that experienced a CEO change during the three (twelve) months following announcement of a block transfers greater than 5% of common shares outstanding. The total number of CEO changes appear in Columns 2, 5 and 8; the number of CEO changes per firm-year appear in Columns 3, 6 and 9; and the percentage of the total number of CEO changes for that group accounted for by each reason identified in column (1) appear in Columns 4, 7 and 10. Next to Columns 6 and 9 are significance results from a binomial test of proportions relative to the proportion in Column 3.

*, ** and *** indicates statistical significance at the 10%, 5% and 1% levels, respectively.

Table 7:
Probit Selection Equation to Identify Chinese Firms that Experienced a Negotiated Block Transfer

Variable	Marginal Effect	t-statistic
ROA $_{i, t-1}$	-0.003 ***	-5.0
Firm Size $_{i, t-1}$	-0.028 ***	-6.0
Largest Percentage $_{i, t-1}$	-0.003 ***	-13.7
State Bureaucrat $_{i, t-1}$	-0.076 ***	-6.0
MOSOE $_{i, t-1}$	-0.043 ***	-3.8

This table reports results from estimating a probit selection equation to identify Chinese listed firms that experienced a negotiated block transfer during 1998-2002. The sample consists of 5,679 firm-year observations on Chinese listed firms during 1998 – 2002 where 631 negotiated block transfers of more than five percent of common shares between firms occurred. The dependent variable takes on a value of one for the 631 firm-years in which a negotiated block transfer took place and a value of zero for all other firm-years. The explanatory variables are: accounting performance measured by $ROA_{i, t-1}$, the peer-adjusted return on assets in *t-1*, the year prior to the block transfer; *Firm Size* $_{i, t-1}$ as measured by the natural logarithm of a firm's total assets in year *t-1*; *Largest Percentage* $_{i, t-1}$, the percentage of shares owned by the largest shareholder in year *t-1*; and ownership classifications *State Bureaucrat* $_{i, t-1}$ and *MOSOE* $_{i, t-1}$. The three ownership categories are *State Bureaucrat*, *MOSOE* and *Private*. *State Bureaucrat* is a dummy variable equal to one if the largest block holder classified as a State Bureaucrat in year *t-1*; *MOSOE* is a dummy variable equal to one if the largest block holder is a market-oriented State-owned enterprise in year *t-1*; and *Private* is a dummy variable equal to one if the largest block holder is a private entity in year *t-1*, and is the omitted category to avoid collinearity. Classifications are based upon 17 detailed categories of ultimate ownership established by researchers at the National University of Singapore ("NUS") as described in Delios *et al*. (2006).
*, ** and *** indicates statistical significance at the 10%, 5% and 1% levels, respectively.

Table 8:
Cross-sectional Regression Results Analyzing Outcomes Following Announcements of Negotiated Block Transfers
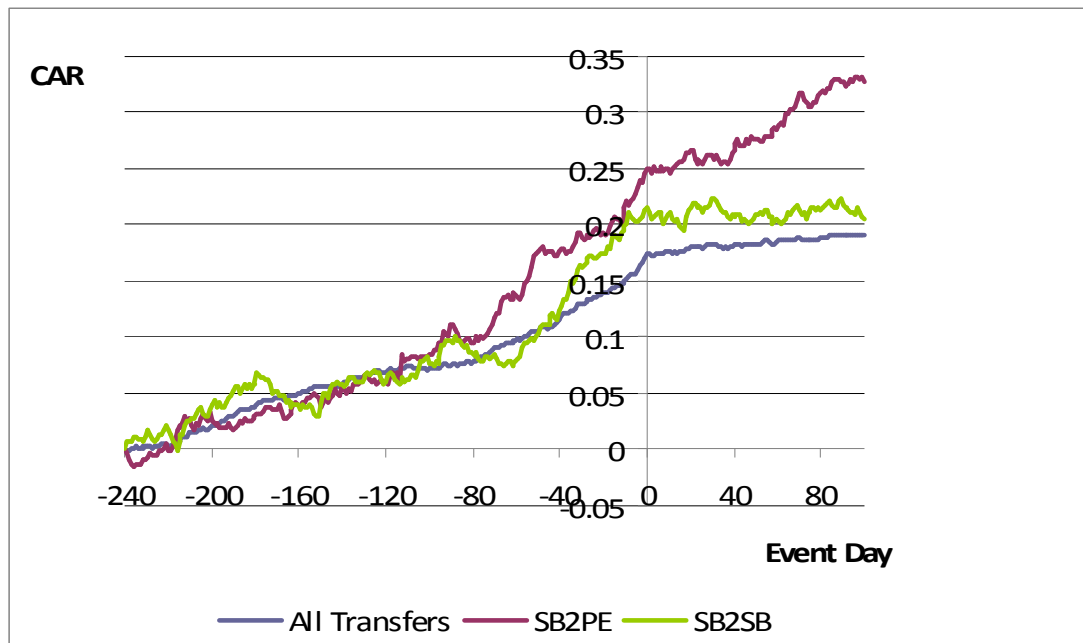
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)	(13)
	Block Transfer		Block Transfer		Block Transfer		Block Transfer		Block Transfer		Block Transfer	
	>5%	> 20%	> 5%	> 20%	> 5%	> 20%	> 5%	> 20%	> 5%	> 20%	> 5%	> 20%
	CAR_250	CAR_250	CAR_5	CAR_5	ROA	ROA	ROE	ROE	CEO_3	CEO_3	CEO_12	CEO_12
Intercept	1.953	2.616	0.133	0.225	0.174	0.425	0.984	1.134				
	5.0 ***	4.1 ***	2.9 ***	2.9 ***	1.5	2.2 **	4.5 ***	3.2 ***				
Seller												
State Bureaucrat	0.124	0.258	0.008	0.019	0.027	0.060	0.052	0.081	-0.100	-0.118	-0.080	-0.117
	2.7 ***	3.3 ***	1.5	2.0 **	2.0 **	2.8 ***	2.1 ***	2.0 **	-2.1 **	-1.4	-1.4	-1.3
MOSOE	0.077	0.189	0.011	0.020	0.026	0.053	0.056	0.089	-0.058	-0.089	-0.035	-0.061
	2.0 **	2.6 ***	2.4 **	2.3 **	2.3 **	2.7 **	2.5 **	2.3 **	-1.4	-1.2	-0.7	-0.7
Buyer												
State Bureacrat	-0.052	-0.087	-0.007	-0.008	-0.021	-0.019	-0.052	-0.073	-0.001	-0.096	0.032	-0.089
	-1.1	-1.1	-1.3	-0.9	-1.5	-0.9	-2.0 **	-1.8 *	0.0	-1.0	0.5	-0.9
MOSOE	-0.007	-0.055	-0.010	-0.019	-0.003	-0.002	-0.004	-0.035	0.016	-0.037	0.063	0.002
	-0.2	-0.9	-2.4 **	-2.7 ***	-0.2	-0.1	-0.5	-1.1	0.4	-0.5	1.5	0.0
Related	0.028	0.007	0.002	0.006	0.008	0.022	0.016	0.017	-0.056	-0.037	-0.139	-0.177
	0.6	0.1	0.4	0.8	0.6	1.1	0.7	0.5	-1.0	-0.5	-2.2 **	-2.1 **
Largest Change	0.002	-0.037	0.005	0.003	0.008	0.000	-0.011	-0.025	0.107	0.120	0.192	0.175
	0.1	-0.6	1.1	0.3	0.7	0.0	-0.5	-0.7	2.7 ***	1.5	4.1 ***	2.2 **
Percentage Transferred	0.001	0.001	0.000	0.000	0.001	0.002	0.001	0.002	0.004	0.003	0.001	0.000
	1.0	0.3	1.9 *	0.9	1.2	2.3 **	1.0	1.6	2.3 **	0.9	0.8	0.1
Leverage	-0.045	-0.216	0.002	0.017	0.039	0.045	-0.013	-0.072	0.011	0.002	0.007	0.161
	-1.9 *	-2.0 **	0.6	1.4	2.9 ***	1.5	-0.3	-1.0	0.6	-0.2	0.2	1.1
Size	-0.091	-0.116	-0.006	-0.011	-0.008	-0.022	-0.047	-0.052	-0.048	-0.047	-0.101	-0.096
	-4.4 ***	-3.3 ***	-2.7 ***	-2.7 ***	-1.2	-2.1 **	-3.9 ***	-2.7 ***	-2.0 **	-1.1	-3.7 ***	-2.1 **
Δ EXPROP	0.005	-0.032	-0.012	-0.011	-0.015	-0.021	-0.038	-0.032	0.014	0.035	-0.083	0.072
	0.1	-0.2	-0.9	-0.5	-0.5	-0.4	-0.7	-0.4	0.1	0.2	-0.5	0.3
Lambda	0.000	-0.035	0.000	-0.002	-0.037	-0.057	-0.028	-0.064	-0.194	-0.208	-0.063	-0.117
	0.0	-0.3	-0.1	-0.1	-2.1 **	-1.7	-0.8	-0.9	-2.8 ***	-1.6	-0.8	-0.9

This table reports results from a series of cross-sectional regressions analyzing outcomes following announcements of negotiated block transfers at Chinese listed firms during 1998-2002. Column (1) identifies the independent variable being analyzed. Columns (2) and (3) present the results for analysis of the 250-day cumulative abnormal return from $t-210$ to $t+40$ around the announcement of block transfers. Columns (4) and (5) present the results for analysis of the five-day cumulative abnormal returns from t-3 to t+1 around announcements of block transfers. Columns (6) and (7) present the results for analysis of changes in profitability as measured by ROA during the two years before to the two years after the year of block transfers. Columns (8) and (9) present the results for analysis of changes in profitability as measures by ROE during the two years before to the two years after the year of block transfers. Columns (10) and (11) present the results for analysis of CEO turnover during the 3 months following announcements of block transfers and columns (12) and (13) present the results for analysis of CEO turnover during 12 months following announcements of block transfers. For each pair of columns, the first presents results for block transfers greater than 5% of common shares outstanding while the second presents results for block transfers greater than 20% of common shares outstanding.

The sample consists of 631 observations of block share transfers of more than five percent of common shares between different ownership categories during 1998-2002. There are three ownership categories (*State Bureaucrat*, *MOSOE* and *Private Entity*) so there are nine combinations of buyer and seller. *State Bureaucrat* is a dummy variable equal to one if the largest block holder is classified as a State Bureaucrat; *MOSOE* is a dummy variable equal to one if the largest block holder is classified as a market oriented State-owned enterprise; *Private* is a dummy variable equal to one if the largest block holder is classified as a private entity. Classifications are based upon 17 detailed categories of ultimate ownership established researchers at the National University of Singapore ("NUS") as described in Delios *et al*. (2006). *Related* is dummy variable indicating that the buyer is a related party of the seller. *Largest Change* is a dummy variable indicating that the transfer created a new controlling block holder. *Percentage Transferred* is size of the block transfer as a percentage of outstanding shares. *Leverage* is the ratio of total debt to total assets. *Size* is the natural logarithm of total assets. *ΔEXPROP* is the change in the level of expropriation as proxied by the value of potentially harmful related-party transactions scaled by firm assets, as described in Berkman, Cole and Fu (2010). *Lambda* is the Inverse Mills Ratio estimated from an equation explaining the probability that a firm is involved in a negotiated block transfer, as shown in Table 7.

*, ** and *** indicate statistical significance at the 10%, 5% and 1% levels, respectively.

Figure 1:
Cumulative Abnormal Returns around
Announcements of Negotiated Block Transfers at Chinese Firms

This figure shows cumulative abnormal returns around announcements of block transfers at Chinese listed firms. Cumulative abnormal returns are calculated as the difference between the realized return and the market return using the market-adjusted return model. To estimate the market-adjusted model, we use as the market index either the Shanghai Stock Exchange (SHSE) or Shenzhen Stock Exchange (SZSE) composite index, depending on where the firm's stock is listed. The sample consists of 631 observations of block share transfers of more than five percent of common shares between different ownership categories during 1998-2002, of which 38 involve transfers from a *State Bureaucrat* to a *State Bureaucrat* ("*SB2SB*") and 49 involve transfers from a *State Bureaucrat* to a *Private Entity* ("*SB2PE*"). There are three ownership categories (*State Bureaucrat*, *MOSOE* and *Private Entity*) so there are nine possible buyer-seller combinations. *State Bureaucrat* is a dummy variable equal to one if the largest block holder is classified as a State Bureaucrat; MOSOE is a dummy variable equal to one if the largest block holder is classified as a market-oriented State-owned enterprise; and *Private Entity* is a dummy variable equal to one if the largest block holder is classified as a private entity. Classifications are based upon 17 detailed categories of ultimate ownership established researchers at the National University of Singapore ("NUS") as described in Delios *et al.* (2006). The graph shows CARs for the full sample and separately for the *SB2SB* and *SB2PE* subgroups.