

Chapter 24

Institutional Structures and the Prevalence of Foreign Ownership of Firms: Empirical Evidence From Africa

Otuo Serebour Agyemang
University of Cape Coast, Ghana

ABSTRACT

This chapter examines how country-level institutional structures influence the prevalence of foreign ownership of firms in Africa. It reinforces the new institutional economics perspective by empirically highlighting that institutional structures influence the prevalence of foreign ownership of companies in an economy. Using archival data from 39 African economies, the authors found that there is a significant positive association between regulatory quality and foreign ownership prevalence. Also, foreign ownership is prevalent in African countries that are politically stable and embrace rule of law. However, the authors found that countries with high voice and accountability structures are associated with low foreign ownership prevalence.

INTRODUCTION

At the onset of developing, it is anticipated that the prevalence of foreign ownership of companies would become one of the significant sources of growth and development in developing economies. Firms with a higher share of foreign ownership should be more efficient than companies with no or small foreign stake (Blomstrom & Sjöholm, 1999). Foreign investments are anticipated to take the shape of transfer of new technologies and ideas, which eventually can be emulated by local corporate organisations (Naciri, 2008; Yudaeva et al., 2003). An opportunity to emulate Western style of managerialism is also a major reason for luring foreign investors into developing countries and economies in transition (Yudaeva et al., 2003). The prevalence of foreign ownership could possibly renew shareholders' meetings, which will eventually bring about a change in attitudes of management toward shareholders (Bien et al., 2008).

DOI: 10.4018/978-1-5225-3247-7.ch024

However, in an incrementally globalised economy, competition is fierce and country-level institutional structures can make an unambiguous difference, by influencing the way and manner in which domestic corporate organisations are perceived by foreign investors (Naciri, 2008; Jalilian et al., 2003; Rodrik, 2000; Campos et al., 1999). National institutions, which include governance structures and practices based on international norms and standards would enable economies particularly, developing economies to post-modernize their corporate sector, which could possibly increase the prevalence of foreign ownership in their economies (Altomonte, 2000; Morisset, 2000; North, 1991).

A plethora of studies have examined the preferences of institutional investors and how economic factors tend to influence these preferences (Uhlenbruck et al., 2006; Kirkpatrick et al., 2006; Habib & Zurawicki, 2002). However, foreigners tend to invest less money in corporate organisations that reside in economies that are characterised by weak institutional structures, weak investor protection and flawed accountability system (Kirkpatrick et al., 2006). This implies that foreign investors invest in companies that are resided in economies, characterised by strong institutional structures, which can help ensure transparency, accountability, information symmetries, among others. Foreign investors shy away from firms located in economies with unsound institutional structures, in that they are more likely to incur huge costs in relation to their information and monitoring costs (Wei, 2000; Shleifer & Vishny, 1993).

This chapter is concerned with how country-level institutional structures influence the prevalence of foreign ownership instead of examining how economic factors influence the prevalence of foreign ownership, given that disparities across economies in economic circumstances offer only a fractional explanation of the locational choices of foreign investors and that the effectiveness and efficiency of an economy's institutional structures could have a considerable influence on their choices (see Uhlenbruck et al., 2006; Kirkpatrick et al., 2006; Habib & Zurawicki, 2002). Without a doubt, this chapter offers insight into how institutional structures influence the holdings of foreign investors in African countries. The objective therefore, of this paper, is to examine how country-level institutional structures influence the prevalence of foreign ownership in African economies.

BACKGROUND

A considerable number of works have been conducted on the determinants of Foreign Direct Investment (FDI) and Foreign Portfolio Investment (FPI) inflows to developing countries in particular, African economies. However, the focus on the rationale behind the decision of foreign investors to own shares in companies situated in African economies has been given little attention. Even the inconsiderable number of studies on the determinants of foreign ownership in African economies have focused essentially on economic factors that induce foreign investors to invest in these economies. This implies that a repertoire of factors can in principle explain foreign ownership trends. The possible determining factors include macroeconomic variables, tax variables, indices of market access for foreign investors and proxies for financial market development. The hypothesis that connects foreign ownership to these variables is, in some instances, rather immediate. In other cases, the possible association between foreign ownership and possible explanatory variables is not a clear-cut (Huizinga & Denis, 2003). This is the case of the quality of governance and other institutional structures (among these are indicators of control of corruption, political stability, voice and accountability, rule of law, regulatory quality, government effectiveness, shareholder safeguard, and the quality of accounting and auditing standards), which are always given

23 more pages are available in the full version of this document, which may be purchased using the "Add to Cart" button on the publisher's webpage:
www.igi-global.com/chapter/institutional-structures-and-the-prevalence-of-foreign-ownership-of-firms/197607

Related Content

Low Density Tourism in the Global South: Second Home Tourism in South Africa as a Form of Visiting Friends and Relatives

Unathi Sonwabile Henama, Lwazi Apleniand Jankie Kgalabi Phale (2022). *Analyzing Sustainability in Peripheral, Ultra-Peripheral, and Low-Density Regions* (pp. 261-275).

www.irma-international.org/chapter/low-density-tourism-in-the-global-south/307799

The Effect of ICT-Based Market Information Services on the Performance of Agricultural Markets: Experiences from Ghana

Irene S. Egyir, Ramatu M. Al-Hassanand James K. Abakah (2013). *Technology, Sustainability, and Rural Development in Africa* (pp. 59-71).

www.irma-international.org/chapter/effect-ict-based-market-information/75586

A Survey on Techniques Used for De-Speckling of SAR Images

Bibek Kumar, Ranjeet Kumar Ranjanand Arshad Husain (2022). *International Journal of Social Ecology and Sustainable Development* (pp. 1-14).

www.irma-international.org/article/a-survey-on-techniques-used-for-de-speckling-of-sar-images/298331

The Effects and Costs of Air Pollution on Health Status in Great Britain

Eleftherios Giovanisand Ozgur Ozdamar (2016). *International Journal of Sustainable Economies Management* (pp. 52-67).

www.irma-international.org/article/the-effects-and-costs-of-air-pollution-on-health-status-in-great-britain/161631

Investigating Impact of Dynamic Pricing and Sustainability-Dependent Demand on Production: A Comparative Study of Metaheuristic Algorithms

Mamta Keswani (2025). *Adaptive Strategies for Green Economy and Sustainability Policies* (pp. 127-142).

www.irma-international.org/chapter/investigating-impact-of-dynamic-pricing-and-sustainability-dependent-demand-on-production/371820