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ABSRTACT

Institutional theory suggests that informal institutions effectively constrain human behavior. Culturally embedded norms and values align corporate governance with socially acceptable outcomes. We argue that active foreign investors can act as agents of change in corporate governance. Investigating changes in ownership and control of Swedish firms, we find that active foreign investors' participation in conjunction with a reduction of control by the largest domestic shareholder, improves firm performance through more efficient capital utilization and labor productivity. Firms move away from a Swedish stakeholder orientation toward an Anglo-American shareholder wealth maximization focus.

Keywords: Foreign Direct Investors; Informal Institution; Business Culture

JEL-codes: G34, G32, G38, M14, E02

INTRODUCTION

An extensive literature on institutional economics establishes a causal link between a country's formal institutions and its economic success (North, 1990; La Porta, Lopez-de-Silanes, Shleifer and Vishny, 1998, 2000; Botero, Djankov, La Porta and Lopez-de-Silanes, 2004; Djankov, La Porta, Lopez-de-Silanes, 2002; Acemoglu, Johnson and Robinson, 2001). A well-functioning legal system that protects private property rights and reduces transaction costs in arms-length exchanges, as well as investor protection laws that enable capital to flow from those who have it to those who need it, supports the birth and expansion of innovative firms (Wurgler, 2000; Beck, Levine and Loayza, 2000; Henrekson and Johansson 2009; Johansson, 2010). Disclosure and fraud deterrence encourage broad equity market participation by external investors and informed price discovery improves capital allocation to the most productive firms (Morck, Yeung, and Yu, 2000).

But as North (1990) observes, "informal institutions" can play an equally important role. The tacit rules of the game – social values, cultural norms, as well as traditions, facilitate communication and mutual understanding in societies that establish trust, consensus, and national/ethnic identity among strangers. Informal constraints on behavior, which do not take the form of legal statutes and misconduct does not result in specific monetary or criminal penalties, can nonetheless effectively shape and influence economic performance and stability.[i]

In this paper, we make the case that foreign investors are not as deeply invested in maintaining the status quo of local host countries and can have different priorities, business cultures, and practices that reflect their home country's informal institutions. Cross-border investments can change the informal rules of the game that reorients corporate governance, and thereby, impact financial efficiency and firm value. Further, globalization can decrease the cost of capital by reducing information asymmetry and associated agency costs; improve the financial flexibility of domestic firms by increasing the pool of potential investors and financing opportunities; and expand cross-border flows of knowledge and technology. An influx of foreign investors can be expected to improve firm performance (Oxelheim and Randøy 2003; Stultz 1999).

Sweden is a unique setting for the study of corporate governance in advanced economies. On the one hand, La Porta et al. (1998, 2000) rank Sweden far above other countries on rule-of-law; and Durnev,

Errunza, and Molchanov (2009), rank Sweden's transparency 5th out of 69 countries. Compared to Anglo-Saxon countries, Sweden provides relatively poor minority shareholder protection (La Porta et al., 1998, 2000). Agnblad et al. (2001) note, however, the absence of evidence that minority shareholders in Sweden are exploited. The deficiency in formal laws that protect minority shareholders is more than offset by high standards of legal enforcement and accounting.

On the other hand, among advanced economies, Sweden represents an extreme case where corporate ownership and control is highly concentrated (La Porta, Lopez-De-Silanes and Shleifer, 1999). Corporate law and Swedish Corporate Governance Code explicitly favor firms with strong majority owners and enable private owners to establish and maintain control of listed firms through pyramidal ownership structures and dual class shares. Many other countries, especially in Europe, allow similar ownership structures. But few countries permit pyramid structures, vote-differentiated dual class shares, and cross-holdings, to be used jointly. Moreover, even among countries that allow dual class shares, the proportion of firms that use dual class shares is higher in Sweden than any other country in Europe (Bennedsen and Nielsen 2002; Faccio and Lang 2002).

External events and attenuation in economic nationalism triggered the abolishment of restrictions on foreign ownership and an attitudinal change in legal support for control-enhancing mechanisms. The resulting entry of foreign equity investors over the years 1992-2008 surrounding Sweden's formal admission to the European Union in 1995 improved the financial performance of large publicly traded, owner-controlled firms in Sweden.[ii]

The implications of our significant finding are twofold. In contrast to prior literature, cross-border investments over this distinct 17-year sample period were not motivated by the exceptional performance of Swedish firms. On the contrary, the notable decline in per capita GDP and standard of living of Sweden relative to OECD countries in the two decades following its peak in the early 1970s reflected the underperformance of Swedish firms. Significant mean reversions in the performance of Swedish firms during this sample period – utilizing return on assets, return on equity, and earnings per share as proxies, are inconsistent with momentum driven, return-chasing behavior by foreign investors.

Importantly, we show that the enhanced performance of Swedish firms was not simply a result of cross-border portfolio investments by institutions as the literature on shareholder activism implies. Gillan and Starks (2003) find that foreign institutional investors play an important role in monitoring

management and prompting changes in corporate governance practices worldwide; Ferreira and Matos (2008), that foreign institutional ownership is positively correlated with the value and performance of firms outside of the United States; and Aggarwal, Erel, Ferreira and Matos (2011), that foreign investors were able to change corporate governance mechanisms and outcomes. These studies, however, must contend with a significant endogeneity issue.[iii] Appropriate inferences about the impact of cross-border investments by foreigners on firm performance will require satisfactory controls for self-selection bias – the incentive of foreigners to concentrate their investments in high performing firms.

Our research design avoids the endogeneity issue entirely. Foreign equity investors in Swedish firms over this 17-year sample period were predominantly institutional. Significant advancements in firm performance occurred only when there was an increase in participation by foreign direct investors coincident with a decrease in the excess voting power of the largest domestic shareholder that gave foreign equity investors a critical "voice" in the management of the firm. Neither an increase in foreign participation nor a decrease in excess voting power of the largest domestic shareholder alone was sufficient. Further, we find that the participation of control-seeking domestic equity investors did not appear to have the same effect. There was no significant change in firm performance from declines in the excess voting power of the largest domestic shareholder that resulted from an increase in participation by control-seeking domestic investors. Foreign direct equity investors, primarily from the United States and the United Kingdom, can assume leading roles as change agents in reducing the unproductive deployment of capital and labor.

Table 1 shows a dramatic increase in foreign ownership and voting participation in Swedish firms from the early 1990's through 2008 following a deregulation of capital markets in the 1980s and elimination of restrictions on foreign ownership in 1992 as pre-conditions for its admission into the European Union. The percentage of ownership and voting rights declined over the 17-year sample period 1992-2008, and as a result, the excess voting power of the largest domestic shareholder. There was a concurrent fall in the use of dual class shares by Swedish firms as well.

Insert Table 1 about here

Table 1 suggests that the large influx of foreigners could be an important catalyst that stimulated

GDP growth and a rise in overall market capitalization and equity share issuance. Specifically, Sweden experienced a greater than average of OECD GDP per capita growth over the period 1994-2010. Improvements in individual firm performance from the entry of foreign direct equity investors starting in 1992, which preceded the admission of Sweden into the European Union in 1995, had a positive long-term effect on the overall economy. The reversal in Sweden's economic performance since 1992 was significant. Until the early 1970's, Sweden's economic performance was stellar. In standard of living, Sweden ranked 5th among OECD countries. But in the two decades that followed, Sweden's relative economic performance deteriorated. The McKinsey Global Institute (1995) "Sweden's Economic Performance" report noted that by 1990, Sweden's GDP per capita was surpassed by Germany, France and Japan; and by 1993, surpassed by Italy and the United Kingdom, following the 1990-1993 Swedish economic recession.

The prolonged decline in standard of living, some argue, was primarily due to a fall in labor productivity. Hansson and Lundberg (1991) find that Sweden's total factor productivity growth over the 1970-1985 period was the lowest among OECD countries. Others argue that the economic decline was caused by a lack of economic evolution or entrepreneurship. Low levels of innovation, defined as new or substantially improved products, services or production processes and productivity growth, are important factors in economic evolution. For economic evolution to progress, the environment must encourage job creation and destruction. Inflexibility in labor markets hampered this need (Botero, et al., 2004). Family control and ownership concentration, both salient features in Sweden (Henrekson and Jakobsson, 2003), are correlated with lower rates of downsizing (Jackson 2005) and lower growth rates (Bjuggren, Daunfeldt, and Johansson 2010). Sako and Jackson (2006) find that the ability of strong labor unions in Sweden to mobilize support, and as a result, exert greater power in the bargaining process creates job security. In addition, a number of institutional changes in credit market regulations, taxes, labor market legislation, as well as access to product markets instituted after World War II provided poor incentives for entrepreneurship (Johansson 2008)[iv].

Unlike prior studies that primarily center on formal institutions, and in particular, how the worldwide spread in shareholder protection laws improved corporate governance (Aggarwal, et al., 2011), the focus on Sweden affords a natural experiment for exploring the effect of informal institutions on firm performance. Informal institutions influence corporate governance by aligning corporate goals with

socially acceptable outcomes. Owners and controlling shareholders of large corporations are heavily vested in and abide by local values and ideals. Such values constrain corporate governance choices. Anglo-American corporations take a shareholder orientation that places efficiency above welfare, but in German and Japanese corporations, a stakeholder orientation that places common interests ahead of financial performance (Dore, 2000).

Culturally embedded corporate governance practices cannot be easily displaced even when the gains in economic efficiency are large. Corporate owners stand to benefit from the maintenance of the status quo and may not welcome radical changes that can lead to "creative destruction" of their market power and political dominance. The extensive use of dual class-shares among Swedish listed firms is a case in point. In 1995, three of the large listed firms on the Stockholm Stock Exchange (SSE) had vote-differentiated shares with a factor 1000:1. Due to external pressure, SKF and Electrolux changed their vote structure to a factor of 10:1 in 1999, and LM Ericsson, in 2004. It is interesting to note that the SHB-sphere was the largest owner in Ericsson, and the Wallenberg sphere was the largest owner in SKF and Electrolux, and the second largest, in Ericsson. Furthermore, all possible successors of culturally entrenched owners, particularly in closed economies, may share similar traditions and beliefs. A nonconformist can face intense social ostracism.

The rest of the paper is organized as follows. A brief introduction to the role of institutions is presented in the next section along with important characteristics of Swedish institutions. Section 3 describes the data and variable construction. Section 4 presents the empirical results and interpretations. Concluding remarks are in Section 5.

SWEDISH INSTITUTIONS AND FOREIGN INVESTORS

Overview of the Swedish Institutions

The "modern" Swedish economy was created in the late 19th century based on developing industries that were of contemporary importance – namely, manufacturing, mining, steel, forestry, and pulp. A majority of the largest firms listed on the SSE were founded during these early years of industrialization (Högfeldt, 2005). The following section discusses how Swedish governance evolved in close connection with the political prominence of the Social Democratic Party (SAP) and draws on the analysis presented in Roe (2005), Högfeldt (2005), and Henrekson and Jacobson (2012).

The Swedish political system during the 20th century was essentially a one-party regime. The SAP ruled the country from 1932 to 2006. The exception was a coalition government from 1939 to 1945, and two short periods of non-socialist government coalitions, from 1976 to 1982 and 1991-94. The overall goal for the economic policy was to create a social capitalist economy and to unite labor and capital owners "*[P]olitical support and legitimacy of heavy entrenched private ownership is traded-off against the implicit guarantee that the largest listed firms do not migrate and that they continue to invest*." (Högfeldt, 2005, p. 570). SAP introduced tax relief for capital intensive industries, beneficial export tariffs, and corporate governance rules that benefitted controlling shareholders in the form of political support for extensive use of dual-class shares, cross-holdings, and pyramids. The SAP also introduced centralized wage negotiations, dividend restrictions, heavy taxation on individual ownership, and wage-earner funds. The reforms created a society where: *"(i) individual wealth accumulation was discouraged, (ii) institutional ownership was stimulated relative to individual ownership and (iii) the overall policy magnified the (already strong) dependence on large companies in Sweden*." (Henrekson and Jakobsson, 2003, p. 96).

The three most important political reforms that formed the foundation for contemporary Swedish corporate governance were: *(i)* the regulation of bank ownership (1911 and 1934); *(ii)* restrictions on foreign ownership; and *(iii)* reform of the corporate tax laws in 1938. In 1911, banks were allowed to directly hold ownership in industrial companies in Sweden. Subsequent to a financial crash in the late 1920s, a new banking act prohibited banks from direct equity ownership. Banks were, however, allowed to hold equity indirectly through holding companies if shares were distributed among the bank's shareholders. This exemption enabled controlling owners of the bank to maintain control of the industrial firms since holding companies were organized as closed-end-investment funds (CEIF). CEIFs, often listed on the SSE, were the entities through which ownership-spheres by controlling (family) owners were formed (Högfeldt 2005).

Lindbeck (1997) describes Swedish corporatism as a disciplined cooperation between labor and entrenched owners that harks back to the "Saltsjöbaden Agreement" of 1938 between the Swedish Trade Union Confederation (LO) and the Swedish Employers' Confederation (SAF). Unlike most other countries in Europe, Sweden's neutrality in two world wars allowed a sufficiently long period of stability during which Social Capitalism attained "cognitively based legitimacy" (Suchman, 1995), and thereby,

established the relative permanence of its institutions. After World War II, the ties between the SAP and LO strengthened, which bolstered labor in its dealings with SAF. From the late 1970's through early 1980's, a deterioration in relations between the LO and SAF (Lindbeck, 1997) led to a decline in the Swedish economy. The deregulation of the capital markets in the 1980s and abolishment of restrictions on foreign ownership in 1992 induced changes in corporate governance. These political reforms and membership in the EU that increased integration and access to a common market were marked responses to external events.

Many scholars – Jackson and Deeg (2008), Jacoby (2005), Dore (2000), Hall and Sockice (2001), Hollingsworth, Schmitter, and Streeck (1994), Streeck (2001), Whitley (1992), argue that capitalism can take forms that go beyond the shareholder focused, market oriented, Anglo-American norm. In coordinated economies such as Sweden, corporate governance seeks to align the differing interests of labor, capital owners, and the state. By achieving a political consensus between labor and major capital owners[v], proponents of the Swedish model describe the governance structure as promoting strong private ownership that embraces a long-term point of view and accepts a social responsibility towards employees and society in general (Agnblad, Berglof, Hogfeldt and Svancar, 2001).

The Swedish Corporate Governance Model

The first Swedish Corporate Governance Code introduced in 2004 applied only to the largest firms listed on regulated stock exchanges in Sweden. The contemporary code, revised in 2010, covers all firms listed on both stock exchanges – NASDAQ OMX Stockholm and NGM Equity. The code, which is self-regulating, embodies a "comply and explain" approach. Firms are allowed to deviate from code but required to explain non-compliance with recommendations. The Swedish Companies Act and Swedish Annual Accounts Act, together with regulations prescribed by the Swedish Securities Council and stock exchanges, constitute the regulatory framework.

Swedish corporate governance revolves around the involvement of three parties: shareholders at annual meetings, a board of directors, and chief executive officer (CEO); each with clearly prescribed rights, functions, and authority. Both the Companies Act and Corporate Governance Code stress the importance of active shareholders and promote active participation by controlling shareholders in the governance of the firm. Although from an international perspective, minority protection is relatively

weak, the Code acknowledges potential problems with controlling owners and attempts to address them. Specifically, the Code catalogues issues that require a qualified majority at the annual shareholders meeting. Additionally, the Code recommends that minority shareholders should be represented in the nomination committee (The Swedish Corporate Governance Code, 2010).

Countries such as France and Germany share the Continental European paradigm that characterizes Swedish corporate governance[vi]. A key feature is the presence of strong block holders who enjoy highly concentrated ownership and trans-generational family control (La Porta et al., 1999; Fogel, 2006). Governance also encourages firms to rely more on internal funding and less on equity markets (Fohlin 2005; Murphy 2005). Swedish firms are unique, moreover, in the extensive use of control enhancing mechanisms where owners with extremely small stakes can exercise managerial control (Henrekson and Jacobsson 2012; Högfeldt 2005). Bennedsen and Nielsen (2002) show that 55 percent of the Swedish listed firms use dual-class shares compared to 18 percent in Germany and only 3 percent in France.

Roe (2005) presents a conceptual framework that describes three dimensions of corporate governance in large public firms: *(i)* a horizontal dimension, which outlines the traditional agency problem between senior management and dispersed investors (Jensen and Meckling, 1976); *(ii)* a vertical dimension, which focuses on the "European" agency problem between majority and minority shareholders (Stulz, 2005); and *(iii)* the societal legacy of corporations. The influences of Swedish political institutions on the latter two dimensions that characterize Swedish corporate governance are highly relevant for the present analysis.

SAP shaped a unique ownership structure where a few controlling owners are able to exercise control of large public firms with low equity investments. The liberal rules that favor block holders were instituted in exchange for the promise to keep firms, and thereby, employment opportunities domiciled in Sweden. The power of strong labor unions helped sustain concentrated ownership because only controlling owners had the ability and incentive to bargain for management policies that dispersed owners could not. Strong labor institutions also explain the resistance to implement reforms that strengthened shareholder orientation, and thereby, a loss of power by controlling owners.

Further, the ability to capture free cash flows with relatively low equity investments reduces the cost of retained earnings, and the tax code, in conjunction with strong support by SAP for financing through debt and retained earnings allowed Swedish firms to be less reliant on external equity markets

(Högfeldt 2005). Muted incentives for the development of external equity capital markets ensured that ownership remained largely concentrated in Sweden.

Carlsson (2007) contends that the Swedish system of corporate governance minimized the principal-agent problem because it allowed a shareholder to obtain the requisite votes to effectively control management at a lower cost than when the property and voting rights of stock ownership are equalized. Boubakri, Cosset, and Guedhami (2005) find ownership concentration has a positive impact on post-privatization firm performance. However, even when management acts in the best interests of a minority shareholder with majority voting rights, there is an implied assumption that the interests of the shareholders with majority voting rights are aligned with the interests of other shareholders.

As Berle and Means (1932) and Jensen and Meckling (1976) make clear, the incentive misalignment from separating ownership and voting rights potentially worsens the agency problem. The negative effects of separating ownership and control are corroborated by Bjuggren, Eklund, and Wiberg (2007). With vote-differentiated shares, the market for corporate control is less effective in resolving conflicts of interests between majority and minority shareholders. Cronqvist and Nilsson (2003) document a value discount when a minority shareholder is in control. To the extent foreign investors can decrease excess voting power exercised by the largest domestic shareholder, the performance of Swedish firms should improve.

Institutions and the Role of Foreign Investors

The special role of foreign direct investors as unique change agents for improving corporate governance is rooted in the role of institutions. "Institutions are the rules of the game in a society" that constrain human behavior (North, 1989; 1990). Formal institutions are the written laws and regulations that define a country's legal system and regulatory environment. The enforcement, adjudication, and assessment of civil and criminal penalties are clearly specified. Informal institutions are the unwritten values, beliefs, customs and traditions that define a country's culture and code of conduct. Enforcement is self-policing in nature and penalties take the form of public rebuke and ostracism.

Formal institutions can change. Laws and regulations can be supplemented, modified, or eliminated. Because a lengthy political and legislative process is involved, changes in formal institutions are episodic. There can be long periods of stagnancy, and very often, the catalyst is a response to a

significant external shock. In Sweden, restrictions on foreign ownership were abolished in 1992 and capital markets were deregulated in the second half of the 1980's. Changes in informal institutions, in contrast, are intergenerational and evolve slowly. Values, beliefs, customs, and traditions represent tacit knowledge that requires time to digest, update, and become embedded as a societal norm. As Roe (2005) points out, it is far easier to effect a legislative change in law than a change in culture.

An important aspect of Swedish corporate governance is the reliance on informal enforcement mechanisms with considerable discretion exercised by controlling shareholders. Holmén and Knopf, (2004 p. 169) show that "[…] *Sweden's extralegal institutions and norms protect minority shareholders*". Such institutions represent self-enforcing social norms shared by citizens and communities. Some well documented examples include compliance to tax codes, which validate social trust and strength of shared social values (see Torgler, 2007 for a comprehensive review), as well as circulations of newspaper or library books, which point to community participation and engagement that build social capital (Preer, 2001). Controlling owners, concerned over reputation and social status, constrain abuse of minority shareholders. In Sweden, social prestige is a significant private benefit associated with the control of large corporations. Families own many of the large Swedish firms. These families have built long term relationships with employees, bankers and suppliers, and politicians based on trust (Poza 2007).

In civil law countries like Sweden, changes in formal statutes that protect minority shareholders involve a political and legislative process that foreign investors are unlikely to initiate. Advancements in corporate governance are more likely to come from informal changes in managerial conduct advanced by foreign investors toward shareholder maximization. But demands for change in Swedish firms can be ignored by well protected, controlling domestic owners. Foreign direct investors will be successful in effecting such changes only when the controlling domestic owner is willing to relinquish some voting control. Further, when such changes are successful, increased firm performance is expected.

In making cross-border investments, foreign investors recognize and adapt to the formal institutions of the host country. The likelihood of detection and severity of punishment for legal infringements are easy to understand. Differences in societal cultures between home and host countries are another matter. Foreign investors may not be fully aware of local customs and traditions nor view these customs and traditions with the same affinity or attachment. Moreover, the benefits from conformity to customs and traditions may be private, that is, are unique to locals and may not accrue to outsiders because of their

foreignness. Lastly, the societal penalty for breaching an informal rule of conduct can be perceived differently by a foreigner than by a local. In China the concept of saving or losing "face" is an integral part of the national psyche. To lose face is to subject oneself and familial relations to intense humiliation that is to be avoided at all costs. But for a foreigner, the threat of societal chastisement may be viewed as no more than an inconvenience and embarrassment.

Foreigners are not only more likely to be unaware of or lack appreciation for local customs and traditions, but are also less susceptible to societal pressures for conformity to societal norms of conduct. More importantly, foreign direct investors are most likely to act effectively as agents of change and an interest in acquiring control rights. Foreign portfolio investors will focus instead on the ownership rights to cash flows from monetary investments and have no interest in challenging the institutions of the host country. Domestic investors, who are already in privileged societal positions, are also unlikely to undertake institutional changes that place their favored positions in jeopardy.

Deregulation of capital markets in the 1980's, finalized in 1989, and subsequent external public pressure on Sweden to join the European Union in the early 1990's, was an exogenous catalyst that led to an influx of foreign investors. Over our study period 1992-2008, foreign investors were predominantly from the United States and United Kingdom – an overall average of 40% and 14% and at the peak in 2000 52% and 24% respectively of all foreign investors.[vii] These Anglo-American foreign investors, who sought an active role, posed a challenge to Swedish corporate governance.[viii] Foreign direct investors will demand managerial performance consistent with shareholder-oriented capitalism (Errunza, 2001).

EMPIRICAL DESIGN

Data Sources

Details on ownership and voting rights[ix] of Swedish firms were obtained from annual publications of SIS ÄGARSERVICE AB's *Owners and Power in Sweden's Listed Companies*, which over the 1992 to 2008 sample period covered all companies listed on the SSE and the NGM Exchange. The dataset does not include companies listed on the SSE domiciled abroad. The publications assemble and track corporate identities and name changes as well as ownership and voting percentages of the largest

domestic shareholders, foreign equity shareholders, and up to a total of 25 largest shareholders. On average, these shareholders represent 80.6% of the vote in all listed companies and 84.2% in dual class issuing companies.

There are five primary sources of information used to construct the Owners and Power dataset. These include: (*i*) two different documents from VPC AB and Swedish Securities Register Centre that are the Public Shareholders' Register and Register of Nominee Shareholders; (*ii*) the Swedish Financial Supervisory Authority's regularly published "flag up" or "flag down" disclosures;[x] (*iii*) required disclosures to the Swedish Financial Supervisory Authority of changes in large block private individuals who either own more than 200 shares or whose shares have a market value of at least SEK 50,000; (*iv*) SIS ÄGARSERVICE AB's proprietary data; and (*v*) voluntary disclosures by shareholders themselves.

Firm characteristics as well as accounting data were obtained from Compustat Global over the sample period. Data were merged manually because the only identifier that could be used, company name, was not always consistently recorded in the same manner and changes over time were not always reflected. The fact that many of the names are in Swedish, and often abbreviated, complicated matters.

Hypothesis

In a prior study, Dahlquist and Robertsson (2004) observe a positive correlation between foreign ownership and firm performance. Foreigners invest in firms with strong recent performance. The resulting increase in the proportion of foreign ownership lowers the cost of equity. In theory, firm performance is enhanced because a lower cost of capital allows firms to undertake more positive net present value (NPV) projects. The causal link between foreign ownership and improved firm performance is, however, unclear. Investing in firms with an established record of strong performance seems to suggest that foreigners chase "winners". Further, a reduction in cost of equity from higher equity valuations may simply be a byproduct of portfolio investments by foreigners in informationally inefficient local equity markets. To establish a causal link between foreign participation and firm performance, it is critically important to distinguish between "direct" and "portfolio" foreign investors in Swedish firms based on their relative interest in property and voting rights, which Manne (1965) and Marris (1964) point out, are both attached to equity ownership.

Specifically, we examine the *Hirschman (1970) Hypothesis*. Portfolio investors are primarily

interested in the cash distributions and contingent claim values associated with property rights. For portfolio investors, concern with firm performance is short-term and limited to assessments of its impact on the potential returns from equity ownership. When realized returns fail to meet expectations, foreign portfolio investors will tend to liquidate their investments and reinvest the proceeds in other firms. Because foreign portfolio investors are most likely to invest in well performing firms, only domestic investors (e.g., founder families), who can have other incentives for equity ownership, are apt to show loyalty and retain equity ownership when firm performance is poor.

In contrast, foreign direct investors take a long-term view of the potential benefits of equity ownership and are more interested in improving firm performance by influencing corporate governance that comes from the exercise of voting rights. As Bjuggren and Bohman (2006) argue, only those with the ability to increase residual income stand to benefit from acquiring enough control rights to enforce a value increasing change. Foreign direct investors are more prepared and willing to exercise voting rights to affect managerial behavior that leads to improved performance. In distinguishing between foreign direct and foreign portfolio investors, we explicitly address the paradox of ownership concentration without commitment (Davis, 2008) – namely that, institutional owners can have large ownership stakes but will likely prefer a share sale exit strategy over an exercise of voting rights to effect a change in corporate governance when firm performance does not meet expectations.

Foreign Portfolio, Foreign Direct, and Control-Seeking Domestic Investor Definitions

We restrict our sample to firms with *Dual Class Shares*. This restriction is necessary to clearly identify control-seeking foreign equity participation. In Sweden, shares of all classes carry the same cash-flow rights – i.e., dividend rates, but A shares carry significantly more voting rights than B shares or C shares. Concentrated control of A shares by a few large, domestic owners further reduces the supply of A shares. Consequently, Class A shares sell at a premium price and tend to have lower liquidity. Their acquisition by foreign or domestic investors clearly indicates intent to exert control. Over our sample period, firms with dual class shares represent between 46% and 84% of all publicly traded firms, with the proportion monotonically declining over time.

For each firm, we examine the annual changes in foreign and domestic ownership from the prior year. Three yearly dummy variables – $F\text{-}Portfolio_t$, $F\text{-}Direct_t$, and CSD_t, are used to indicate the nature of

the changes in foreign and domestic ownership. A firm is categorized as *F-Portfolio*$_t$ in a particular year when the only change in equity investments are by foreign portfolio investors who only acquire class B shares and their ownership changes do not exceed 5%. These restrictions ensure that the interests of foreign portfolio investors are purely financial and do not stem from the exercise of voting rights.

Firms are categorized as *CSD*$_t$ or *F-Direct*$_t$ in a particular year, when the changes in equity investments by control-seeking domestic or foreign direct investors are either through the acquisition of Class A shares or Class B shares that increase ownership by 5% or more, **and** the changes in equity investments result in a decline in the excess and total voting power of the largest domestic shareholder.[xi] Focus is on the largest domestic shareholder as opposed to the largest 2, 3, 5, or other arbitrary number of domestic shareholders, for two reasons. First, the largest domestic shareholder exercised (on average) over 50% to 29% respectively, of the votes from the beginning to the end of the sample period 1992 to 2008. Second, as La Porta et al. (1999) point out, 20% is sufficient for one shareholder to effectively control the company.

Because the holdings of Class A shares are concentrated among a few parties, the acquisition of a sufficiently large number of Class B shares in open markets can also be a substitute. Requiring a reduction in total voting power ensures that the largest domestic shareholders do not make compensating changes in loss of control from the sale of Class A shares through the purchase of Class B shares. In other words, it is unambiguous that the largest domestic shareholder voluntarily relinquished some control to other control-seeking investors.

We denote *D1–Vote* and *F–Vote* as the percentages of voting rights exercised by the largest domestic shareholder and the aggregate of all foreign investors respectively; and *D1–Capital* and *F–Capital*, as the ownership percentages of the largest domestic shareholder and the aggregate of all foreign investors, respectively. *Excess Vote* is the difference between the ownership and voting percentages of the largest domestic shareholder.

Summary Statistics

We use three proxies of profitability to capture firm performance. *ROA*$_t$, *ROE*$_t$, and *EPS*$_t$, are defined as: *Net Income*$_t$ divided by *Average Total Assets*$_{t-1,t}$, *Average Shareholders Equity*$_{t-1,t}$ and *Average Numbers of Shares Outstanding*$_{t-1,t}$, respectively; and future one-year changes in firm performance

$\Delta ROA_{t,t+1}$, $\Delta ROE_{t,t+1}$, and $\Delta EPS_{t,t+1}$ as $ROA_{t+1} - ROA_t$, $ROE_{t+1} - ROE_t$, and $EPS_{t+1} - EPS_t$, respectively. The number of employees is used as a surrogate for $Size_t$ of firm. We use *Average Plant, Property, and* $Equipment_{t-1,t}$ and *Net Revenue*$_t$ divided by *Average Number of Emplyees*$_{t-1,t}$ as proxies for *Capital* $Intensity_t$ and *Labor Productivity*$_t$, respectively, and future changes, Δ*Capital* $Intensity_{t,t+1}$ and Δ*Labor* $Productivity_{t,t+1}$, as *Capital* $Intensity_{t+1}$ – *Capital* $Intensity_t$ and *Labor* $Productivity_{t+1}$ – *Labor* $Productivity_t$, respectively.

Insert Table 2 about here

Table 2 reports summary statistics on the variables used in this study.[xii] On average, Swedish firms are profitable and profitability increased over the sample period. Approximately 23% and 31% respectively, of the firm-year changes in equity ownership involved foreign direct and foreign portfolio investors; 16%, involved control-seeking domestic investors; and in the remaining 30%, there was either no change in foreign ownership or the change in ownership involved domestic portfolio investors. On average, Swedish firms employed almost 9,400 workers and the average excess vote of the largest domestic shareholder was 17.32%.

EMPIRICAL RESULTS

Univariate Analysis

Table 3 is divided into two panels. Panel A reports the bivariate correlations between changes in firm performance or productivity (dependent variables) and level of performance, ownership, voting rights and size of the firm (independent variables). The negative correlations between firm performance and future changes in performance respectively, of -0.4825, -0.7172, and -0.6654, indicate mean-reversions in firm performance that are statistically significant at the 0.1% level. Moreover, the positive correlations between current productivity and future changes in productivity respectively, of 0.5189 and 0.4187, that are statistically significant at the 0.1% level, imply a positive trend in firm productivity. Lastly, participations by foreign direct investors are positive and significantly correlated with future changes in firm performance, and participations by foreign portfolio investors, are negative but not always significantly, correlated with future changes in performance. The correlations between increased participation by control-seeking domestic investors and changes in performance are negative though

insignificant.

Insert Table 3 about here

Panel B shows that all three alternative measures of performance and both measures of productivity are positively correlated and significant at the 1% level or higher. In addition, the significant positive correlations between foreign portfolio investors and firm performance respectively, of 0.1059, 0.0565, and 0.0826, confirm that foreign portfolio investors are attracted to well performing firms.

This is not true of foreign direct investors. The negative correlations respectively, of -0.0293 and -0.0648 between foreign direct investors and productivity, suggest that foreign direct investors are attracted to firms with low productivity because of potential improvement. The correlation of firm size with current performance is significantly positive. But as evident in Panel A, the relationship between size and future changes in performance is insignificant. Lastly, firms dominated by a large domestic shareholder attract foreign portfolio investors but deter foreign direct and control-seeking domestic investors. The positive correlation between the excess vote of the largest domestic shareholder and participation of foreign portfolio investors of 0.0920, and negative correlations between the excess vote of the largest domestic shareholder and participation of foreign direct and control-seeking domestic investors respectively, of -0.0639 and -0.0901, are highly significant.

Multivariate Analysis

Two-way fixed effects regressions, $\mathbf{Y_{t+1} = Xb_t + e_t}$, that control for both firm specific characteristics and time are used to assess whether changes in equity investments by foreign direct investors increase firm performance in the subsequent period. The dependent variable, $\mathbf{Y_{t+1}}$: $Performance_{t+1} - Performance_t$, utilizes ROA_t, ROE_t, and EPS_t as surrogates for firm performance. The explanatory variables, X_t, are: (*i*) current change in ownership reflected by the categorical dummy variables $F\text{-}Portfolio_t$, $F\text{-}Direct_t$, and CSD_t; (*ii*) number of employees to capture $Size_t$;[xiii] (*iii*) current year performance; and (*iv*) excess voting power of the largest domestic shareholder in the current year; and (*v*) capital ownership of foreign direct and foreign portfolio investors for the current year. The change in the subsequent three-year average return from the current year is used to examine the long-term impact of the foreign direct investors.[xiv]

The results in Table 4 indicate that only $F\text{-}Direct_t$, namely, changes in equity investments by

foreign direct investors that reduce the excess voting power of the largest domestic shareholder improve firm performance. In model 1, where $\Delta ROA_{t,t+1}$ is the change in firm performance, the $F\text{-}Direct_t$ coefficient of 0.0809 is significant at the 0.1% level. In models 2 and 3, where the change in performance are $\Delta ROE_{t,t+1}$ and $\Delta EPS_{t,t+1}$ respectively, the $F\text{-}Direct_t$ coefficients 0.0845 and 2.9995, are also positive and highly significant. Moreover, increased participation by foreign portfolio and control-seeking domestic investors do not significantly improve and may worsen firm performance. The coefficients for $F\text{-}Portfolio_t$ are insignificant in models 1 and 2; negative and significant at the 5% level in model 3. The coefficients for CSD_t are insignificant and positive in models 1 and 2; insignificant and negative, in model 3.

Further, the positive but insignificant coefficients for $F\text{-}Direct\ Capital_t$ confirms that participation by foreign direct investors improves performance but only when there is a concomitant decline in the excess voting power of the largest domestic shareholder. Similarly, the negative coefficient for $F\text{-}Portfolio\ Capital_t$, which is statistically significant in model 1 and insignificant in models 2 and 3, confirms that increased participation by foreign portfolio investors tends to worsen firm performance.

Insert Table 4 about here

Intensity of Foreign Participation

If foreign direct investors improve firm performance, their impact on firm performance should be greater the more considerable is their involvement. To investigate this, we partition $F\text{-}Direct_t$ into three categories. $F\text{-}Direct_t\ 5\%$, $F\text{-}Direct_t\ 10\%$, and $F\text{-}Direct_t\ 20\%$ signifies that foreign direct investors acquire between 5% and less than 10% of the votes, between 10% and less than 20% of the votes, and 20% or more of the votes, respectively. Similarly, we partition $F\text{-}Portfolio_t$ into the same three categories.

Table 5 shows the results of a two-way fixed effects panel regressions controlling for firm and year. Foreign portfolio investors do not significantly improve firm performance regardless of how much voting control is acquired. Only increased participation of foreign direct investors matters. Moreover, the greater is their level of participation, the larger is the positive impact on firm performance. The coefficients are positive and larger as the level of participation by foreign direct investors increases, $F\text{-}Direct_t\ 20\% > F\text{-}Direct_t\ 10\% > F\text{-}Direct_t\ 5\%$, and significant when participation by foreign direct investors reach the 10% threshold.

Insert Table 5 about here

Long Term Performance Impact

To assess the permanence of improvements in firm performance that result from the participation of foreign direct investors, we examine future three-year changes in firm performance relative to current firm performance as proxies for long-term firm performance. $LTROA_{t,t+3}$, $LTROE_{t,t+3}$, and $LTEPS_{t,t+3}$ are defined as $1/3 \sum_{t=1}^{3} ROA_{t+\tau} - ROA_t$, $1/3 \sum_{t=1}^{3} ROE_{t+\tau} - ROE_t$, and $1/3 \sum_{t=1}^{3} EPS_{t+\tau} - EPS_t$, respectively. Two-way fixed effects panel regressions controlling for firm and year are reported in Table 6.

The results in Tables 4 and 6 are consistent. On average, foreign direct investors are associated with long-term improvements in firm performance. In all three models, the coefficients for $F\text{-}Direct_t$ are significantly positive at the 10% level or better. In addition, note that the coefficients of $F\text{-}Portfolio_t$ are always negative; and the coefficient of CSD_t, is positive in model 1, but negative, in models 2 and 3. Though none of the coefficients are significant, the participation of foreign portfolio or control-seeking domestic investors, suggests an adverse impact on firm performance.

Insert Table 6 about here

Origins of Foreign Investors[xv]

A large literature, following La Porta, López de Silanes, Shleifer and Vishny's (LLSV, 1998) "Law and Finance", provides convincing evidence to support the thesis that British Common Law countries are best at protecting minority investors and facilitating financial development. We tabulate the countries of origin of foreign investors in our sample. Over 40% of all foreign investors are from the U.S. and the U.K., the most prominent British Common Law countries. Investors from the U.S. and the U.K. also represent a large majority, nearly 70%, of Foreign Direct Investors.

To gauge the different effects of country of origin on investor effectiveness in enhancing financial performance, we divide our sample of Foreign Direct Investors into two groups – those from the U.S. and the U.K., and the rest. Table 7 Panel A repeats the analysis of Table 4, but replaces the *F-Direct* variable with two new indicator variables, namely, *US/UK-Direct* and *Non-US/UK-Direct*. As predicted by the

legal origin literature, increases in financial performance are associated with large, positive, and significant *US/UK-Direct* coefficients. In only one case is the coefficient on *Non-US/UK-Direct* significant, although the signs are positive across all three specifications.

Panel B repeats the analysis of Table 6, again with foreign direct investors separated into two groups. *US/UK-Direct* coefficients are large, positive, and statistically significant across all three measures of long-term performance; *Non-US/UK-Direct* coefficients are insignificant. In sum, the results are consistent with prevailing literature that emphasize the benefits of British legal origin in encouraging shareholder value creation and protecting minority shareholders' rights.

Insert Table 7 about here

Sources of Efficiency

Two-way fixed effects panel regressions controlling for firm and year reported in Table 8 consider labor productivity and capital intensity as potential sources of efficiency that contribute to improvements in firm performance. The dependent variables in columns 1 and 2 are the one-year future changes in revenue per employee and capital-labor ratio, and in columns 3 and 4, the three-year future changes in revenue per employee and capital-labor ratio.

Insert Table 8 about here

The highly significant positive coefficients associated with $F\text{-}Direct_t$ in panel regressions 1 and 2 clearly show that only the participation of foreign direct investors increases labor productivity and capital intensity. The involvements either by foreign portfolio or control-seeking domestic investors have no impact on labor productivity or capital utilization. Firms are more profitable through lower cost from better deployment of labor and capital. Moreover, the panel regressions in columns 3 and 4 show the future improvements in labor and capital efficiency are long-term even after we account for current labor productivity and capital intensity.

Table 8 Panel B goes further in identifying the sources of the efficiency that foreign direct investors brought to Swedish firms. In view of the results in Table 7, foreign direct investors are divided into two groups based on their countries of origin, namely, *US/UK-Direct* and *non-US/UK-Direct*. Panel B shows

a negative and statistically significant association between *US/UK-Direct* and changes in labor, and the relation is evident in one-year as well as three-year horizons. U.S./U.K. Direct Investors also induce positive changes in capital (PPE), that are highly significant only in the long term, but insignificant in the one-year period immediately following entry of foreign investors.

These results are consistent with Bjuggren et al. (2006) and Holmen and Hogfeldt's (2009) finding that the exercise of control by minority owners and pyramid ownership structures lead to overinvestment and loss of firm value, as well as with Jackson, Hopner, and Kurdelbusch's (2005) finding, that a change in orientation toward shareholder maximization raised the profitability of German firms. Lastly, our results complement Giannetti and Laeven (2009) who find that foreign pension funds improve firm performance. Their study, however, fails to differentiate between ownership and control. We show that changes in voting control rather than ownership enhance firm performance.[xvi]

Robustness

A decrease in the excess vote of the largest domestic shareholder as a result of foreign involvement is insufficient by itself to improve firm performance. Reductions in excess vote must entail a voluntary acquiescence of control by the largest domestic shareholders to foreign direct investors. Moreover, participation by control-seeking domestic shareholders is not a substitute. Foreign direct investors are most likely to function as agents of change.

To underscore these points, we examine two panel datasets that focus on firm-years where there was a decline in the excess vote of the largest domestic shareholder. In the first dataset, declines in the excess vote of the largest domestic shareholder are associated with increases in ownership and vote of foreign direct and control-seeking domestic investors. In the second dataset, declines in the excess vote of the largest domestic shareholder are associated only with increases in ownership and vote of control-seeking domestic investors that more than offset decreases in the ownership and vote of foreign direct investors.

Insert Table 9 about here

In the panel regressions, the actual decreases in excess vote percentages of the largest domestic shareholder are denoted by $\Delta Excess\,Vote_t^-$; increases and decreases of foreign vote percentages by $\Delta F - Vote_t^+$ and $\Delta F - Vote_t^-$, respectively; and increases in vote percentages of control-seeking

domestic investors, by $\Delta D - Vote_t^+$. Interaction terms $\Delta Excess\,Vote_t^-$ (X) $\Delta F - Vote_t^+$, $\Delta Excess\,Vote_t^-$ (X) $\Delta F - Vote_t^-$, and $\Delta Excess\,Vote_t^-$ (X) $\Delta D - Vote_t^+$, reflect changes in the excess vote percentage of the largest domestic shareholder associated with changes in voting percentages of foreign direct and control-seeking domestic investors.

The two-way fixed effects panel regressions controlling for firm and year in Table 9 confirm that a reduction in excess vote as a result of participation by foreign direct or control-seeking domestic investors is insufficient to improve firm performance. The coefficients associated with excess vote and foreign vote are mostly positive but insignificant. Moreover, greater participation by control-seeking domestic shareholders tends to lower rather than raise firm performance – coefficients are mostly negative though insignificant. Only when reductions in excess vote are accompanied by increases in foreign direct investors' vote does firm performance improve. Coefficients corresponding to these interaction terms are consistently positive and significant. These results indicate the critical importance of our classification of foreign investors as either direct or portfolio investors. Although not shown, distinguishing between institutional and non-institutional foreign investors does not impact our results. The vast majority of both foreign portfolio and foreign direct investors are institutions, and consequently, institutional investor is not a characteristic that distinguishes foreign portfolio from foreign direct investors.

CONCLUDING REMARKS

A reversal in the decline in Swedish GDP per capita began in 1994. Sweden's GDP per capita growth between 1998 and 2004 was the strongest amongst OECD nations. High productivity growth was cited as the primary explanation for this positive development by McKinsey Global Institute's report "Sweden's Economic Performance: Recent Development, Current Priorities" (2006). During this period, productivity growth in Sweden's private sector ranked 4th among OECD countries and was 1.5 times higher than the average. Sweden's admission to the EU lowered trade barriers and the influx of foreign owners' willingness to confront labor unions enhanced the competitiveness of Swedish firms. The result was an increase in output without a corresponding increase in labor input.[xvii] The macroeconomic trends are consistent with the firm level evidence we find in this study, which shows that improved firm

performance is associated with higher labor productivity and capital intensity.

As institutions theory predicts, foreign direct investors can be agents of change in firms controlled by culturally entrenched insiders. Foreign investors reorient corporate governance goals without radically changing the formal rules and regulations that govern corporate choice, and instead, effect changes in corporate culture by challenging the informal rules of the game. Successful change can come only when large domestic shareholders, who are highly entrenched and can obstruct change, are willing to relinquish some control rights.

Sweden was an ideal case to show how economic nationalism adapted to the pressures for trade and open capital flows. Free trade expands markets for domestic firms, which heightens product market competition. Capital inflows by foreign investors intensify the global competition for resources, which advances corporate governance. What is remarkable in Sweden is that dominant owners of Sweden's largest firms cooperated by conceding some control rights to foreign investors, and as a result, allowed informal reforms in corporate governance that made firms leaner, more capital intensive, and more profitable. This cultural change exemplifies the benefit of capital market openness, and should encourage policy makers to consider financial integration more favorably, even with full consideration given to economic nationalism and independence.

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[i]Stulz and Williamson (2003) show that religion and language matters to financial development; and Fogel, Lee, and McCumber (2011), that the profitability and outreach of microbanks are related to Hofstede's cultural dimensions. Holmén and Knopf (2004) show in a study of Swedish firms that social institutions such as tax compliance and newspaper circulation improve minority shareholder protection.

[ii]The last step of deregulation of Swedish capital market was in 1989. The last regulations regarding foreign ownership were abolished in 1992, which effectively removed foreign ownership restrictions in Swedish firms. Before this date, larger transactions by foreign investors had to be approved by the Swedish Government. However, foreign ownership was minimal during the early 1990's and grew slowly until just prior to Sweden's entry into the European Union. In year 2000, the share of foreign ownership on the Stockholm stock market was 30 percent.

[iii]Adams, Hermalin and Weisback (2010) point out the endemic nature of endogeneity in the corporate governance literature.

[iv]Henrekson (2005) maintains that "an entrepreneurial culture and a welfare state are very remotely related. As a result, the respective cultures are unlikely to be promoted by a similar set of institutions". For further discussion on the Swedish economy see Henrekson and Jakobsson (2001) that discuss the Swedish economic and political development using a Schumpeterian framework.

[v]Private ownership are represented primarily by institutional owners like tax-exempt pension funds and founding family funds rather than private individuals.

[vi]Dutch and Swedish corporate governance are distinct. Both countries are small and export-oriented. But Dutch corporate governance is characterized by dispersed ownership and significant managerial entrenchment. De Jong and Roell (2005) argue that the prohibition of dual-class shares and absence of a universal banking system contributed to the separation of ownership and control – two factors that played very significant roles in the evolution of Continental European corporate governance model, and especially, the Swedish model.

[vii]In contrast, Denmark, Holland, and Norway represented 3.3%, 2%, and 4.8% respectively. Finland at 12.9% represented the third largest foreign investor group.

[viii]The conflict of interest between foreign direct investors and the interests of Sweden's political system is similar to the conflict between foreign investors and local governments described by Henisz and Zelner (2005).

[ix]In a dual class stock structure, all shares confer the same ownership rights but Class A shares have superior voting rights to Class B shares.

[x]The "flag up" or "flag down" disclosure happens when an owner moves between the following levels of ownership or votes: 5, 10, 15, 20, 25, 30, 50, 66.67, and 90 percent.

[xi]Our definition of foreign direct and foreign portfolio investor should not be confused with the OECD definition of foreign direct investments. Although conceptually very similar, our threshold is 5% voting control while the OECD definition is 10%. More importantly, because of the high usage of dual class shares by Swedish firms as well as the dominant control that can be exerted by the largest domestic shareholder, we also add a requirement that the largest domestic shareholder must relinquish some control. It is possible, though doubtful, that a foreign portfolio investor will choose to accumulate more than 10% voting power slowly over time.

[xii]Data values were winsorized at the 1% and 99% levels to remove outliers.

[xiii]Results using Total Assets and log of Total Assets as well as Market Capitalization and log of Market Capitalization as alternative proxies for size are similar.

[xiv]The use of categorical dummy variables of control and ownership along with the use of level variables for control and ownership in the same regression is similar to the approach taken by Claessens, Djankov, Fan, and Lang (2002).

[xv]We thank an anonymous referee for raising this point.

[xvi]Giannetti and Laeven (2009) examine firms with both single and dual class issues. But in their case, the correlation between ownership and vote percentages is high. In contrast, our study has a relatively high degree of separation between ownership and vote percentages. Consequently, we can account for both simultaneously and show that the impact of foreign votes on firm performance dominates the impact of foreign ownership.

[xvii]This is consistent with the view that Sweden's high-growth firms only modestly contribute to job creation (Davidsson and Henrekson 2002).

TABLE 1
Trend in Ownership and Control of Swedish Firms

External public pressure on Sweden to join the European Union in the early 1990's was an exogenous catalyst that led to an influx of foreign investors. *D1–Vote* and *F–Vote*, are the percentages of voting rights exercised by the largest domestic shareholder and the aggregate of all foreign investors respectively; and *D1–Capital* and *F–Capital*, are the ownership percentages of the largest domestic shareholder, the foreign direct investor, and the aggregate of all foreign portfolio investors, respectively. *Excess Vote*$_t$ is the difference between the ownership and voting percentages of the largest domestic shareholder. Average ownership and voting percentages of Swedish firms held by foreigners increased from 4.07% and 3.55% respectively on average in 1992 to 25.53% and 23.43% respectively in 2008. Foreign ownership of total market capital increases from 14.4% to 37.3% during the sample period. There was a corresponding decrease in excess vote of the largest domestic shareholder from 15.15% in 1992 to 7.40% in 2008; their ownership and voting declined from 35.05% and 50.21% respectively in 1992 to 21.32% and 28.72% respectively in 2008. The same period saw a concurrent: (*i*) 53% decrease in the use of dual class shares from 86.63% in 1992 to 45.95% in 2008; (*ii*) 5% annual compounded growth rate in GDP from SEK 1,448 billion in 1992 to SEK 3,182 billon in 2008; (*iii*) 13% annual gain in market capitalization from SEK 552 billion in 1992 to SEK 3,691 billion in 2008; and (*iv*) 8% annual expansion in initial public offerings.

	1992	**1996**	**2000**	**2004**	**2008**
F–Capital	4.07	17.08	19.47	19.98	25.53
F–Vote	3.55	14.11	18.03	18.52	23.43
Foreign Ownership of Total Capital, %	14.40	32.10	39.20	33.30	37.30
D1–Capital	35.05	26.79	23.05	22.73	21.32
D1–Vote	50.21	39.41	32.92	30.79	28.72
Excess Vote$_t$	15.15	12.62	9.87	8.06	7.40
Firms with Dual Class Shares (%)	86.63	69.95	59.69	54.15	45.95
GDP (SEK billions)	1,448	1,690	2,013	1,926	3,182
Market Capitalization (SEK billions)	552	1,210	3,800	2,115	3,691
Market Capitalization to GDP (%)	38.12	71.60	188.77	109.81	116.00
New Issues (SEK billions)	1.79	2.74	2.73	4.10	6.50

TABLE 2
Summary Statistics

ROA_t, ROE_t, and EPS_t, defined as *Net Income*$_t$ divided by *Average Total Assets*$_{t-1,t}$, *Average Shareholders Equity*$_{t-1,t}$ and *Average Numbers of Shares Outstanding*$_{t-1,t}$, respectively, are used as proxies of firm profitability. $\Delta ROA_{t,t+1}$, $\Delta ROE_{t,t+1}$, and $\Delta EPS_{t,t+1}$ denote future (t,t+1) one-year changes in profitability. *F-Direct*$_t$, *F-Portfolio*$_t$, and CSD_t, are dummies denoting changes in equity associated with foreign direct investors, foreign portfolio investors, and control-seeking domestic investors, respectively. Number of employees (000s) is used as a surrogate for firm *Size*$_t$. *Excess Vote*$_t$ is the difference between ownership and voting percentages of the largest domestic shareholder. *F-Direct Capital*$_t$ and *F-Portfolio Capital*$_t$ are the ownership percentages of foreign direct and foreign portfolio investors. *Capital Intensity*$_t$ and *Labor Productivity*$_t$ are defined as *Average Plant, Property, and Equipment*$_{t-1,t}$ divied by *Average Number of Emplyees*$_{t-1,t.}$ and *Net Revenue*$_t$ divided by *Average Number of Emplyees*$_{t-1,t.}$ Δ*Capital Intensity*$_{t,t+1}$ and Δ*Labor Productivity*$_{t,t+1}$ denote future (t,t+1) one-year changes.

	No. of Firm-Years	Mean	Standard Deviation	Min	Max
ROA_t	1512	0.0112	0.1480	-0.7803	0.4936
ROE_t	1512	0.0299	0.3281	-2.0738	1.3924
EPS_t	1512	5.2189	10.3212	-42.7807	52.2858
$\Delta ROA_{t,t+1}$	1353	0.0013	0.1296	-0.7034	0.7364
$\Delta ROE_{t,t+1}$	1353	0.0046	0.3154	-2.9621	2.8013
$\Delta EPS_{t,t+1}$	1353	0.3552	9.7142	-45.7407	51.0256
F-Direct$_t$	1353	0.2341	0.4236	0	1
F-Portfolio$_t$	1353	0.3115	0.4633	0	1
CSD_t	1353	0.1581	0.3649	0	1
Size$_t$	1512	9.3913	24.8464	0.0010	80.3690
Excess Vote$_t$	1512	17.3236	12.6806	-20.2%	50.0%
F-Direct Capital$_t$	1353	8.3158	12.2174	0%	78.9%
F-Portfolio Capital$_t$	1353	5.3258	11.6084	0%	89.2%
Capital Intensity$_t$	1512	1.0335	2.1533	0.0054	34.1235
Labor Productivity$_t$	1509	2.0289	4.5026	0.0210	75.5864
Δ*Capital Intensity*$_{t,t+1}$	1353	0.0392	0.0429	-4.5703	5.7383
Δ*Labor Productivity*$_{t,t+1}$	1329	0.0992	0.0551	-5.4481	5.8997

TABLE 3
Correlation Matrix

ROA_t, ROE_t, and EPS_t, defined as *Net Income*$_t$ divided by *Average Total Assets*$_{t-1,t}$, *Average Shareholders Equity*$_{t-1,t}$ and *Average Numbers of Shares Outstanding*$_{t-1,t}$, respectively, are used as proxies of firm profitability. $\Delta ROA_{t,t+1}$, $\Delta ROE_{t,t+1}$, and $\Delta EPS_{t,t+1}$ denote future (t,t+1) one-year changes in profitability. *F-Direct*$_t$, *F-Portfolio*$_t$, and CSD_t, are dummies denoting changes in equity associated with foreign direct investors, foreign portfolio investors, and control-seeking domestic investors, respectively. Number of employees (000s) is used as a surrogate for firm $Size_t$. *Excess Vote*$_t$ is the difference between ownership and voting percentages of the largest domestic shareholder. *F-Direct Capital*$_t$ and *F-Portfolio Capital*$_t$ are the ownership percentages of foreign direct and foreign portfolio investors. *Capital Intensity*$_t$ and *Labor Productivity*$_t$ are defined as *Average Plant, Property, and Equipment*$_{t-1,t}$ divided by *Average Number of Emplyees*$_{t-1,t.}$ and *Net Revenue*$_t$ divided by *Average Number of Emplyees*$_{t-1,t.}$ Δ*Capital Intensity*$_{t,t+1}$ and Δ*Labor Productivity*$_{t,t+1}$ denote future (t,t+1) one-year changes. Panel A shows the correlations between the dependent variables (horizontal axis) and the independent variables (vertical axis). While Panel B reports the correlations between the independent variables. *P*-values are shown in parentheses.

PANEL A	$\Delta ROA_{t,t+1}$	$\Delta ROE_{t,t+1}$	$\Delta EPS_{t,t+1}$	Δ*Capital Intensity*$_{t,t+1}$	Δ*Labor Productivity*$_{t,t+1}$
F-Direct$_t$	0.0732	0.0015	0.0735	0.0439	0.0385
	(0.01)	(0.06)	(0.01)	(0.04)	(0.07)
F-Portfolio$_t$	-0.0405	-0.0048	-0.0532	-0.0160	0.0337
	(0.14)	(0.86)	(0.05)	(0.46)	(0.12)
CSD_t	-0.0136	-0.0127	-0.0067	-0.0037	-0.0037
	(0.62)	(0.64)	(0.84)	(0.87)	(0.86)
ROA_t	-0.4825	0.0652	-0.2158	0.0063	0.0063
	(0.00)	(0.02)	(0.00)	(0.77)	(0.77)
ROE_t	0.1574	-0.7172	-0.1957	0.0008	0.0014
	(0.00)	(0.00)	(0.00)	(0.97)	(0.95)
EPS_t	-0.0629	-0.1200	-0.6654	-0.0064	-0.0007
	(0.02)	(0.00)	(0.00)	(0.77)	(0.97)
Capital Intensity$_t$	-0.0007	-0.0071	0.0054	0.5189	0.0465
	(0.98)	(0.94)	(0.80)	(0.00)	(0.02)
Labor Productivity$_t$	0.0110	0.0130	0.0269	0.0472	0.4187
	(0.61)	(0.55)	(0.21)	(0.03)	(0.00)
$Size_t$	-0.0054	-0.0011	-0.0004	-0.0161	-0.0046
	(0.84)	(0.97)	(0.99)	(0.45)	(0.83)
Excess Vote$_t$	-0.0215	-0.0144	-0.0304	0.0142	-0.0108
	(0.43)	(0.60)	(0.26)	(0.51)	(0.62)
F-Direct Capital$_t$	0.0207	0.0017	0.0223	-0.0031	-0.0221
	(0.45)	(0.95)	(0.41)	(0.89)	(0.39)
F-Portfolio Capital$_t$	-0.0890	-0.0382	-0.0096	0.0179	-0.0037
	(0.00)	(0.16)	(0.72)	(0.40)	(0.68)

TABLE 3 – Continued

PANEL B	*(1)*	*(2)*	*(3)*	*(4)*	*(5)*	*(6)*	*(7)*	*(8)*	*(9)*	*(10)*	*(11)*
F-Direct$_t$ (1)	1.000										
F-Portfolio$_t$ (2)	-.279 (0.00)										
CSD$_t$ (3)	-.240 (0.00)	-0.292 (0.00)									
ROA$_t$ (4)	-.035 (0.18)	0.106 (0.00)	-.091 (0.00)								
ROE$_t$ (5)	-.008 (0.76)	0.057 (0.03)	-.066 (0.01)	0.118 (0.00)							
EPS$_t$ (6)	-.030 (0.25)	0.083 (0.00)	-.007 (0.78)	0.395 (0.00)	0.284 (0.00)						
Capital Intensity$_t$ (7)	-.029 (0.14)	0.050 (0.01)	0.014 (0.48)	0.022 (0.28)	0.009 (0.67)	0.003 (0.88)					
Labor Productivity$_t$ (8)	-.065 (0.00)	0.040 (0.05)	-.002 (0.56)	0.003 (0.87)	-.005 (0.81)	-.023 (0.25)	0.061 (0.00)				
Size$_t$ (9)	.057 (0.30)	0.007 (0.80)	-.002 (0.93)	0.094 (0.00)	0.045 (0.08)	0.157 (0.00)	-0.029 (0.15)	-.016 (0.43)			
Excess Vote$_t$ (10)	-.064 (0.01)	0.092 (0.00)	-.090 (0.00)	0.009 (0.36)	0.013 (0.63)	0.080 (0.13)	-0.021 (0.30)	-.020 (0.32)	0.067 (0.01)		
F-Direct Capital$_t$ (11)	0.223 (0.00)	-0.166 (0.00)	-.180 (0.00)	-.026 (0.32)	-.004 (0.88)	-.008 (0.76)	-0.005 (0.81)	-.071 (0.00)	0.208 (0.00)	-.116 (0.00)	
F-Portfolio Capital$_t$ (12)	-.250 (0.00)	0.280 (0.00)	-.177 (0.00)	0.044 (0.17)	0.015 (0.57)	0.034 (0.19)	0.005 (0.80)	0.023 (0.34)	0.186 (0.00)	0.050 (0.05)	-0.362 (0.00)

TABLE 4
Impact of Foreign Investors on Firm Performance

Table 4 reports two-way fixed effects regressions controlling for firm and year. $\Delta ROA_{t,t+1}$, $\Delta ROE_{t,t+1}$, and $\Delta EPS_{t,t+1}$ denote future (t,t+1) one-year changes in profitability. *F-Direct*$_t$, *F-Portfolio*$_t$, and CSD_t, are dummies denoting changes in equity associated with foreign direct investors, foreign portfolio investors, and control-seeking domestic investors, respectively. Number of employees (000s) is used as a surrogate for firm $Size_t$. ROA_t, ROE_t, and EPS_t, defined as *Net Income*$_t$ divided by *Average Total Assets*$_{t-1,t}$, *Average Shareholders Equity*$_{t-1,t}$ divided by *Average Total Assets*$_{t-1,t,}$ and *Average Numbers of Shares Outstanding*$_{t-1,t}$, divided by *Average Total Assets*$_{t-1,t}$ respectively, are used as proxies of firm profitability. *Excess Vote*$_t$ is the difference between ownership and voting percentages of the largest domestic shareholder. *F-Direct Capital*$_t$ and *F-Portfolio Capital*$_t$ are the ownership percentages of foreign direct and foreign portfolio investors. *P*-values are shown in parentheses. ***, **, *, and † demote significant at the 0.001, 0.01, 0.05, and 0.10 levels, respectively.

	Dependent Variable		
	$\Delta ROA_{t,t+1}$	$\Delta ROE_{t,t+1}$	$\Delta EPS_{t,t+1}$
F-Direct$_t$	0.0809***	0.0845**	2.9995**
	(0.001)	(0.010)	(0.003)
F-Portfolio$_t$	-0.0149	0.0113	-1.9306*
	(0.496)	(0.697)	(0.030)
CSD_t	0.0096	0.0185	-0.4044
	(0.540)	(0.371)	(0.524)
$Size_t$	-1.80E-05	-0.0002	-0.0183
	(0.973)	(0.784)	(0.407)
Excess Vote$_t$	-0.0003	-0.0007	0.0420
	(0.798)	(0.611)	(0.344)
F-Direct Capital$_t$	0.0015	0.0016	0.0512
	(0.105)	(0.197)	(0.164)
F-Portfolio Capital$_t$	-0.0019*	-0.0016	-0.0122
	(0.029)	(0.165)	(0.730)
ROA_t	-0.7191***		
	(0.000)		
ROE_t		-0.7403***	
		(0.000)	
EPS_t			-0.6004***
			(0.000)
Constant	0.0131	0.0392	2.9215*
	(0.666)	(0.328)	(0.019)
R^2	0.3719	0.4549	0.3167
Number of Firm-Years	1353	1353	1353
Number of Firms	172	172	172

TABLE 5
Intensity of Foreign Participation and Firm Performance

Table 5 reports two-way fixed effects regressions controlling for firm and year. $\Delta ROA_{t,t+1}$, $\Delta ROE_{t,t+1}$, and $\Delta EPS_{t,t+1}$ denote future (t,t+1) one-year changes in profitability. *F-Direct*$_t$ *X%*, *F-Portfolio*$_t$ *X%*, and CSD_t *X%*, denote changes in equity associated with foreign direct investors, foreign portfolio investors, and control-seeking domestic investors, respectively. Threshold percentages 5%, 10%, and 20%, indicate the magnitudes of the change in voting rights associated with the level of involvement by foreign direct or portfolio investors and control-seeking domestic investors and are defined respectively as 5% ≤ X% < 10%, 10% ≤ X% < 20%, 20% ≤ X%. Number of employees (000s) is used as a surrogate for firm $Size_t$. ROA_t, ROE_t, and EPS_t, defined as *Net Income*$_t$ divided by *Average Total Assets*$_{t-1,t}$, *Average Shareholders Equity*$_{t-1,t}$ divided by *Average Total Assets*$_{t-1,t}$, and *Average Numbers of Shares Outstanding*$_{t-1,t}$, divided by *Average Total Assets*$_{t-1,t}$, respectively, are used as proxies of firm profitability. *Excess Vote*$_t$ is the difference between ownership and voting percentages of the largest domestic shareholder. *F-Direct Capital*$_t$ and *F-Portfolio Capital*$_t$ are the ownership percentages of foreign direct and foreign portfolio investors. *P*-values are shown in parentheses. ***, **, *, and † demote significant at the 0.001, 0.01, 0.05, and 0.10 levels, respectively.

	Dependent Variable		
	$\Delta ROA_{t,t+1}$	$\Delta ROE_{t,t+1}$	$\Delta EPS_{t,t+1}$
F-Direct$_t$ *5%*	0.0335 (0.266)	0.0086 (0.813)	1.3992 (0.209)
F-Direct$_t$ *10%*	0.0840 † (0.059)	0.1139* (0.031)	3.8938* (0.023)
F-Direct$_t$ *20%*	0.1530* (0.012)	0.2136** (0.006)	4.0896 † (0.068)
F-Portfolio$_t$ *5%*	0.0066 (0.797)	0.0112 (0.744)	-0.9690 (0.349)
F-Portfolio$_t$ *10%*	0.0132 (0.695)	0.0215 (0.620)	0.0294 (0.983)
F-Portfolio$_t$ *20%*	-0.0247 (0.460)	-0.0501 (0.247)	-0.7937 (0.550)
$Size_t$	-0.0001 (0.903)	-0.0001 (0.806)	-0.0157 (0.370)
Excess Vote$_t$	0.0002 (0.678)	0.0001 (0.917)	-0.0085 (0.602)
F-Direct Capital$_t$	0.0009 (0.278)	0.0004 (0.545)	0.0181 (0.365)
F-Portfolio Capital$_t$	0.0001 (0.893)	-0.0085 (0.614)	-0.2650 (0.603)
ROA_t	-0.2686*** (0.000)		
ROE_t		-0.3198*** (0.000)	
EPS_t			-0.2591*** (0.000)
Constant	-0.0086 (0.333)	-0.0203 (0.299)	1.6867*** (0.000)
R^2	0.2275	0.2246	0.2241
Number of Firm-Years	1353	1353	1353
Number of Firms	172	172	172

TABLE 6
Impact of Foreign Investors on Long-Term Firm Performance

Table 6 reports two-way fixed effects regressions controlling for firm and year. $LT\Delta ROA_{t,t+3}$, $LT\Delta ROE_{t,t+3}$, and $LT\Delta EPS_{t,t+3}$ denote future (t,t+3) three-year average changes in profitability. $F\text{-}Direct_t$, $F\text{-}Portfolio_t$, and CSD_t, are dummies denoting changes in equity associated with foreign direct investors, foreign portfolio investors, and control-seeking domestic investors, respectively. Number of employees (000s) is used as a surrogate for firm $Size_t$. ROA_t, ROE_t, and EPS_t, defined as *Net Income*$_t$ divided by *Average Total Assets*$_{t-1,t}$, *Average Shareholders Equity*$_{t-1,t}$ divided by *Average Total Assets*$_{t-1,t}$, and *Average Numbers of Shares Outstanding*$_{t-1,t}$, divided by *Average Total Assets*$_{t-1,t}$, respectively, are used as proxies of firm profitability. *Excess Vote*$_t$ is the difference between ownership and voting percentages of the largest domestic shareholder. *F-Direct Capital*$_t$ and *F-Portfolio Capital*$_t$ are the ownership percentages of foreign direct and foreign portfolio investors. *P*-values are shown in parentheses. ***, **, *, and † demote significant at the 0.001, 0.01, 0.05, and 0.10 levels, respectively.

	Dependent Variable		
	$LT\Delta ROA_{t,t+3}$	$LT\Delta ROE_{t,t+3}$	$LT\Delta EPS_{t,t+3}$
$F\text{-}Direct_t$	0.0385* (0.019)	0.0403† (0.075)	1.3520† (0.087)
$F\text{-}Portfolio_t$	-0.0220 (0.110)	-0.0261 (0.168)	-0.5570 (0.404)
CSD_t	0.0135 (0.172)	-0.0028 (0.836)	-0.7192 (0.217)
$Size_t$	-0.0001 (0.840)	-0.0004 (0.421)	-0.0239 (0.155)
Excess Vote$_t$	-0.0003 (0.722)	-0.0013 (0.218)	-0.0116 (0.589)
F-Direct Capital$_t$	0.0003 (0.603)	0.0004 (0.664)	0.0268 (0.371)
F-Portfolio Capital$_t$	-0.0007 (0.224)	-0.0002 (0.803)	-0.0119 (0.662)
ROA_t	-0.8423*** (0.000)		
ROE_t		-0.8890*** (0.000)	
EPS_t			-0.4985*** (0.000)
Constant	0.0002 (0.988)	0.0572** (0.007)	2.8650*** (0.000)
R^2	0.3933	0.3275	0.2234
Number of Firm-Years	1039	1039	1039
Number of Firms	161	161	161

TABLE 7
Panel A: Impact of US/UK Foreign Direct Investors on Firm Performance

Table 7 Panel A reports two-way fixed effects regressions controlling for firm and year. $\Delta ROA_{t,t+1}$, $\Delta ROE_{t,t+1}$, and $\Delta EPS_{t,t+1}$ denote future (t,t+1) one-year changes in profitability. *US/UK-Direct*$_t$, Non-US/UK-Direct $_t$, *F-Portfolio*$_t$, and *CSD*$_t$, denote changes in equity associated with foreign direct from the US/UK and those from other nations, foreign portfolio investors, and control-seeking domestic investors respectively. Number of employees (000s) is used as a surrogate for firm *Size*$_t$. *ROA*$_t$, *ROE*$_t$, and *EPS*$_t$, defined as *Net Income*$_t$ divided by *Average Total Assets*$_{t-1,t}$, *Average Shareholders Equity*$_{t-1,t}$ divided by *Average Total Assets*$_{t-1,t,}$ and *Average Numbers of Shares Outstanding*$_{t-1,t}$, divided by *Average Total Assets*$_{t-1,t}$ respectively, are used as proxies of firm profitability. *Excess Vote*$_t$ is the difference between ownership and voting percentages of the largest domestic shareholder. *F-Direct Capital*$_t$ and *F-Portfolio Capital*$_t$ are the ownership percentages of foreign direct and foreign portfolio investors. *P*-values are shown in parentheses. ***, **, *, and † demote significant at the 0.001, 0.01, 0.05, and 0.10 levels, respectively.

	Dependent Variable		
	$\Delta ROA_{t,t+1}$	$\Delta ROE_{t,t+1}$	$\Delta EPS_{t,t+1}$
US/UK-Direct$_t$	0.1488*** (0.000)	0.0693* (0.013)	6.9056*** (0.000)
Non-US/UK-Direct$_t$	0.0788*** (0.001)	0.0175 (0.280)	0.8831 (0.506)
F-Portfolio$_t$	-0.0012 (0.384)	0.0458 (0.333)	-0.2376 (0.771)
CSD$_t$	-0.0117 (0.521)	-0.0756 (0.216)	-1.1219 (0.287)
Size$_t$	-1.90E-05 (0.970)	-0.0001 (0.933)	-0.0321 (0.281)
Excess Vote$_t$	-0.0002 (0.838)	-0.0028 (0.420)	0.0773 (0.200)
F-Direct Capital$_t$	0.0019† (0.090)	0.0062 (0.101)	0.0596 (0.144)
F-Portfolio Capital$_t$	-0.0028*** (0.001)	-0.0021 (0.286)	-0.0685* (0.044)
ROA$_t$	-0.6675*** (0.000)		
ROE$_t$		-1.3010*** (0.000)	
EPS$_t$			-0.8597*** (0.000)
Constant	-0.0490* (0.026)	0.1051 (0.156)	2.5379* (0.047)
R^2	0.4289	0.6819	0.5888
Number of Firm-Years	1353	1353	1353
Number of Firms	172	172	172

TABLE 7
Panel B: Impact of US/UK Foreign Direct Investors on Long-Term Firm Performance

Table 7 Panel B reports two-way fixed effects regressions controlling for firm and year. $LT\Delta ROA_{t,t+3}$, $LT\Delta ROE_{t,t+3}$, and $LT\Delta EPS_{t,t+3}$ denote future (t,t+3) three-year average changes in profitability. *US/UK-Direct*$_t$, Non-US/UK-Direct $_t$, *F-Portfolio*$_t$, and *CSD*$_t$, denote changes in equity associated with foreign direct from the US/UK and those from other nations, foreign portfolio investors, and control-seeking domestic investors respectively. Number of employees (000s) is used as a surrogate for firm *Size*$_t$. *ROA*$_t$, *ROE*$_t$, and *EPS*$_t$, defined as *Net Income*$_t$ divided by *Average Total Assets*$_{t-1,t}$, *Average Shareholders Equity*$_{t-1,t}$ divided by *Average Total Assets*$_{t-1,t}$, and *Average Numbers of Shares Outstanding*$_{t-1,t}$, divided by *Average Total Assets*$_{t-1,t}$, respectively, are used as proxies of firm profitability. *Excess Vote*$_t$ is the difference between ownership and voting percentages of the largest domestic shareholder. *F-Direct Capital*$_t$ and *F-Portfolio Capital*$_t$ are the ownership percentages of foreign direct and foreign portfolio investors. *P*-values are shown in parentheses. ***, **, *, and † demote significant at the 0.001, 0.01, 0.05, and 0.10 levels, respectively.

	Dependent Variable		
	$LT\Delta ROA_{t,t+3}$	$LT\Delta ROE_{t,t+3}$	$LT\Delta EPS_{t,t+3}$
US/UK-Direct$_t$	0.0584***	0.1246***	5.834***
	(0.000)	(0.000)	(0.000)
Non-US/UK-Direct$_t$	-0.0057	-0.0239	-0.4315
	(0.758)	(0.565)	(0.797)
F-Portfolio$_t$	-0.0027	0.0074	0.1719
	(0.821)	(0.781)	(0.874)
CSD$_t$	-0.0310	-0.0437	0.4557
	(0.130)	(0.177)	(0.728)
Size$_t$	-8.94E-05	-0.0003	0.0001
	(0.806)	(0.710)	(0.997)
Excess Vote$_t$	-0.0017	-0.0034	-0.0501
	(0.404)	(0.188)	(0.528)
F-Direct Capital$_t$	-0.0006	-0.0022	-0.0262
	(0.373)	(0.117)	(0.642)
F-Portfolio Capital$_t$	0.0002	0.0012	-0.1170
	(0.639)	(0.298)	(0.114)
ROA$_t$	-0.2993***		
	(0.000)		
ROE$_t$		-0.2331***	
		(0.000)	
EPS$_t$			-0.2479***
			(0.000)
Constant	0.0507	0.0676	0.3588
	(0.606)	(0.109)	(0.834)
R^2	0.5850	0.4961	0.2954
Number of Firm-Years	1039	1039	1039
Number of Firms	161	161	161

TABLE 8
Panel A: Sources of Efficiency

Table 8 Panel A reports two-way fixed effects regressions controlling for firm and year. *Average Plant, Property, and Equipment*$_{t-1,t}$ divided by *Average Number of Emplyees*$_{t-1,t}$ and *Net Revenue*$_t$ divided by *Average Number of Emplyees*$_{t-1,t}$ as proxies for *Capital Intensity*$_t$ and *Labor Productivity*$_t$, respectively. *ΔCapital Intensity*$_{t,t+1}$ and *ΔLabor Productivity*$_{t,t+1}$, are future (t,t+1) changes in capital intensity and labor productivity, *LTΔCapital Intensity*$_{t,t+3}$ and *LTΔLabor Productivity*$_{t,t+3}$, are future three-year average changes in capital intensity and labor productivity. *F-Direct*$_t$, *F-Portfolio*$_t$, and *CSD*$_t$, are dummies denoting changes in equity associated with foreign direct investors, foreign portfolio investors, and control-seeking domestic investors, respectively. Number of employees (000s) is used as a surrogate for firm *Size*$_t$. *ROA*$_t$, *ROE*$_t$, and *EPS*$_t$, defined as *Net Income*$_t$ divided by *Average Total Assets*$_{t-1,t}$, *Average Shareholders Equity*$_{t-1,t}$ divided by *Average Total Assets*$_{t-1,t}$, and *Average Numbers of Shares Outstanding*$_{t-1,t}$, divided by *Average Total Assets*$_{t-1,t}$, respectively, are used as proxies of firm profitability. *Excess Vote*$_t$ is the difference between ownership and voting percentages of the largest domestic shareholder. *F-Direct Capital*$_t$ and *F-Portfolio Capital*$_t$ are the ownership percentages of foreign direct and foreign portfolio investors. *P*-values are shown in parentheses. ***, **, *, and † demote significant at the 0.001, 0.01, 0.05, and 0.10 levels, respectively.

	Dependent Variable			
	ΔLabor Productivity$_{t,t+1}$	*ΔCapital Intensity*$_{t,t+1}$	*LTΔLabor Productivity*$_{t,t+3}$	*LTΔCapital Intensity*$_{t,t+3}$
F-Direct$_t$	279.2525**	194.9466***	139.4983**	241.7478*
	(0.03)	(0.00)	(0.04)	(0.10)
F-Portfolio$_t$	74.4233	-33.1217*	46.5038	-26.4265
	(0.49)	(0.10)	(0.39)	(0.28)
CSD$_t$	59.4255	8.3270	21.1869	-1.3698
	(0.62)	(0.76)	(0.76)	(0.41)
Size$_t$	0.2594	-0.1508	0.1399	0.3063
	(0.94)	(0.84)	(0.94)	(0.96)
Excess Vote$_t$	-2.2377*	-0.3176	-2.9872**	0.2780
	(0.07)	(0.84)	(0.04)	(0.81)
F-Direct Capital$_t$	7.8998	0.3985	-0.3920	2.0710
	(0.12)	(0.64)	(0.90)	(0.83)
F-Portfolio Capital$_t$	-6.7296	-5.8350***	-3.1831	-1.8168
	(0.11)	(0.00)	(0.16)	(0.83)
Capital Intensity$_t$	0.3617***		0.1892***	
	(0.00)		(0.00)	
Labor Productivity$_t$		0.2376***		0.4173***
		(0.00)		(0.00)
Constant	-64.9169	-174.8600***	-201.5610*	-277.7420
	(0.14)	(0.00)	(0.07)	(0.25)
R^2	0.2833	0.3118	0.2479	0.2888
Number of Firm-Years	1329	1353	1035	1046
Number of Firms	170	172	159	160

TABLE 8
Panel B: Impact of Foreign Direct Investors on Capital and Labor

Table 8 Panel B reports two-way fixed effects regressions controlling for firm and year. *Average Plant, Property, and Equipment*$_{t-1,t}$ and *Average Number of Emplyees*$_{t-1,t}$ as proxies for *Capital* and *Labor* size, respectively. $\Delta Capital_{t,t+1}$ and $\Delta Labor_{t,t+1}$, are future (t,t+1) percentage changes in capital and labor size, $LT\Delta Capital_{t,t+3}$ and $LT\Delta Labor_{t,t+3}$, are future three-year average percentage changes in capital and labor size. *US/UK-Direct*$_t$, Non-US/UK-Direct $_t$, *F-Portfolio*$_t$, and *CSD*$_t$, denote changes in equity associated with foreign direct from the US/UK and those from other nations, foreign portfolio investors, and control-seeking domestic investors. Number of employees (000s) is used as a surrogate for firm *Size*$_t$. *Excess Vote*$_t$ is the difference between ownership and voting percentages of the largest domestic shareholder. *F-Direct Capital*$_t$ and *F-Portfolio Capital*$_t$ are the ownership percentages of foreign direct and foreign portfolio investors. *Capital/Labor* ratios is constructed as *Average Plant, Property, and Equipment*$_{t-1,t}$ divided by *Average Number of Emplyees*$_{t-1,t}$. *P*-values are shown in parentheses. ***, **, *, and † demote significant at the 0.001, 0.01, 0.05, and 0.10 levels, respectively.

	Dependent Variable			
	$\Delta Labor_{t,t+1}$	$\Delta Capital_{t,t+1}$	$LT\Delta Labor_{t,t+3}$	$LT\Delta Capital_{t,t+3}$
US/UK-Direct$_t$	-0.3294*	0.1161	-0.1389*	0.4089**
	(0.016)	(0.564)	(0.047)	(0.008)
Non-US/UK-Direct$_t$	0.0313	0.3493	0.1144	-0.0565
	(0.493)	(0.376)	(0.161)	(0.799)
F-Portfolio$_t$	0.0223	0.5525	0.0166	0.2530
	(0.392)	(0.140)	(0.940)	(0.254)
CSD$_t$	-0.0373	-0.183	-0.0405	-0.1380
	(0.265)	(0.527)	(0.146)	(0.402)
Size$_t$	-0.0555***	0.2385***	0.0798***	0.2012***
	(0.000)	(0.003)	(0.000)	(0.000)
Excess Vote$_t$	-0.0038	-0.0133	-0.0088	-0.0093
	(0.841)	(0.414)	(0.599)	(0.847)
F-Direct Capital$_t$	0.0032	0.0240	0.0054	0.0698
	(0.216)	(0.314)	(0.606)	(0.125)
F-Portfolio Capital$_t$	0.0045	-0.0119	0.0147	0.0656
	(0.330)	(0.244)	(0.134)	(0.259)
Capital/Labor$_t$	0.0570†	-0.0574	0.0144	-0.4704†
	(0.098)	(0.796)	(0.148)	(0.072)
Constant	-0.6164	-0.0173	-0.3271	-0.1022
	(0.130)	(0.624)	(0.356)	(0.626)
R^2	0.2642	0.1663	0.2224	0.2312
Number of Firm-Years	1329	1329	1039	1039
Number of Firms	170	170	160	160

TABLE 9
Robustness Test

Table 9 reports two-way fixed effects regressions controlling for firm and year focused around firm-years where the excess vote percentage of the largest domestic shareholder declined. In Panel A, declines in excess votes are associated with increases in the voting percentages of foreign direct and control-seeking domestic investors. In Panel B, declines in excess votes are associated with increases in the voting percentage of control-seeking domestic shareholders that more than offset decreases in the voting percentage of foreign direct investors. These voting percentage changes are denoted by $\Delta Excess\ Vote_t^-$, $\Delta F - Vote_t^+$, $\Delta F - Vote_t^-$, and $\Delta D - Vote_t^+$, respectively. $\Delta ROA_{t,t+1}$, $\Delta ROE_{t,t+1}$, and $\Delta EPS_{t,t+1}$ denote future (t,t+1) one-year changes in profitability; and $LT\Delta ROA_{t,t+3}$, $LT\Delta ROE_{t,t+3}$, and $LT\Delta EPS_{t,t+3}$ denote future (t,t+3) three-year average changes in profitability. Number of employees (000s) is used as a surrogate for firm $Size_t$. ROA_t, ROE_t, and EPS_t, defined as *Net Income*$_t$ divided by *Average Total Assets*$_{t-1,t}$, *Average Shareholders Equity*$_{t-1,t}$ divided by *Average Total Assets*$_{t-1,t}$, and *Average Numbers of Shares Outstanding*$_{t-1,t}$, divided by *Average Total Assets*$_{t-1,t}$, respectively, are used as proxies of firm profitability. *Excess Vote*$_t$ is the difference between ownership and voting percentages of the largest domestic shareholder. *F-Direct Capital*$_t$ and *F-Portfolio Capital*$_t$ are the ownership percentages of foreign direct and foreign portfolio investors. *P*-values are shown in parentheses. ***, **, *, and † demote significant at the 0.001, 0.01, 0.05, and 0.10 levels, respectively.

PANEL A	**Dependent Variable**					
	$\Delta ROA_{t,t+1}$	$\Delta ROE_{t,t+1}$	$\Delta EPS_{t,t+1}$	$LT\Delta ROA_{t,t+}$	$LT\Delta ROE_{t,t+}$	$LT\Delta EPS_{t,t+}$
$\Delta F - Vote_t^+$	0.0008	0.0003	0.0624	0.0011	0.0006	0.1241
	(0.645)	(0.953)	(0.566)	(0.288)	(0.399)	(0.185)
$\Delta D - Vote_t^+$	0.0007	-0.0023	0.0306	-0.0007	-0.0033	-0.0051
	(0.634)	(0.474)	(0.713)	(0.427)	(0.143)	(0.951)
$\Delta Excess\ Vote_t^-$	0.0034	0.0035	0.0862	0.0014	0.0027	0.0372
	(0.220)	(0.572)	(0.588)	(0.431)	(0.603)	(0.844)
$\Delta Excess\ Vote_t^-$ (X) $\Delta F - Vote_t^+$	0.0013*	0.0036†	0.0368†	0.0011**	0.0044†	0.0359*
	(0.037)	(0.069)	(0.058)	(0.004)	(0.087)	(0.016)
$\Delta Excess\ Vote_t^-$ (X) $\Delta D - Vote_t^+$	0.0001	-0.0019	-0.0098	-5.28E-06	-8.7E-05	0.0102
	(0.840)	(0.611)	(0.300)	(0.974)	(0.848)	(0.537)
$Size_t$	0.0001	-0.0001	-0.0168	-3.14E-07	-0.0005	-0.0326
	(0.825)	(0.940)	(0.639)	(0.999)	(0.533)	(0.239)
Excess Vote$_t$	0.0006	-0.0008	0.1662	-0.0019	-0.0048	-0.0897
	(0.652)	(0.812)	(0.530)	(0.156)	(0.141)	(0.302)
F-Direct Capital$_t$	0.0004	-0.0010	0.0176	0.0005	-0.0003	0.0225
	(0.569)	(0.628)	(0.737)	(0.272)	(0.804)	(0.587)
F-Portfolio Capital$_t$	-0.0017	0.0003	-0.0817	9.94E-05	2.29E-06	-0.0413
	(0.780)	(0.842)	(0.420)	(0.794)	(0.998)	(0.240)
ROA_t	-0.5908***			-0.7903***		
	(0.000)			(0.000)		
ROE_t		-1.0178***			-1.0149***	
		(0.000)			(0.000)	
EPS_t			-0.9763***			-1.0832***
			(0.000)			(0.000)
Constant	-0.0715	0.0604	2.6662	0.0310	0.0156 ***	1.0767 **
	(0.126)	(0.538)	(0.294)	(0.810)	(0.010)	(0.007)
R^2	712	712	712	523	523	523
Number of Firm-Years	0.3601	0.4604	0.5047	0.4008	0.4309	0.5147
Number of Firms	161	161	161	147	147	147

TABLE 9 – Continued

PANEL B	**Dependent Variable**					
	$\Delta ROA_{t,t+1}$	$\Delta ROE_{t,t+1}$	$\Delta EPS_{t,t+1}$	$LT\Delta ROA_{t,t+3}$	$LT\Delta ROE_{t,t+3}$	$LT\Delta EPS_{t,t+3}$
$\Delta F - Vote_t^+$	0.0016	0.0015	-0.0227	0.0003	0.0010	-0.0193
	(0.433)	(0.760)	(0.857)	(0.739)	(0.839)	(0.946)
$\Delta D - Vote_t^+$	-0.0024	-0.0034	-0.1505	-0.0013	-0.0068	-0.2550
	(0.126)	(0.367)	(0.115)	(0.383)	(0.280)	(0.111)
$\Delta Excess\ Vote_t^-$	-0.0029	-0.0022	0.2001	0.0001	0.0027	0.2685
	(0.386)	(0.780)	(0.330)	(0.937)	(0.638)	(0.229)
$\Delta Excess\ Vote_t^-$ (X) $\Delta F - Vote_t^+$	-0.0004	-0.0009	-0.0147	-0.0005	0.0047	-0.1071
	(0.507)	(0.555)	(0.700)	(0.148)	(0.174)	(0.584)
$\Delta Excess\ Vote_t^-$ (X) $\Delta D - Vote_t^+$	5.28E-05	0.0003	-0.0088	-0.0001	-0.0008	-0.0587
	(0.801)	(0.586)	(0.486)	(0.394)	(0.550)	(0.169)
$Size_t$	1.07E-04	1.00E-04	0.0020	-2.45E-05	6.82E-05	-0.1330
	(0.903)	(0.998)	(0.970)	(0.943)	(0.980)	(0.217)
$Excess\ Vote_t$	-0.0018	-0.0015	0.0489	-0.0023	-0.0028	-0.2403
	(0.364)	(0.762)	(0.692)	(0.270)	(0.395)	(0.153)
$F\text{-}Direct\ Capital_t$	0.0061	0.0033	-0.0321	0.0002	0.0184	-0.0868
	(0.579)	(0.900)	(0.962)	(0.643)	(0.170)	(0.830)
$F\text{-}Portfolio\ Capital_t$	-0.0013	2.86E-05	-0.0032	0.0003	0.0007	-0.0048
	(0.562)	(0.996)	(0.998)	(0.397)	(0.401)	(0.984)
ROA_t	-0.9416***			-1.0238***		
	(0.000)			(0.000)		
ROE_t		-0.6492***			-0.9190***	
		(0.000)			(0.000)	
EPS_t			-1.0294***			-1.1388***
			(0.000)			(0.000)
Constant	0.0297	0.1249	0.0528	0.0325	0.0693	1.0278
	(0.377)	(0.118)	(0.510)	(0.034)	(0.240)	(0.010)
R^2	632	632	632	296	296	296
Number of Firm-Years	0.3566	0.3314	0.3010	0.2966	0.2846	0.2506
Number of Firms	141	141	141	102	102	102