

# INTERNATIONAL JOURNAL OF RESEARCH IN COMMERCE & MANAGEMENT

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**STATEMENT OF THE PROBLEM**

**OBJECTIVES**

**HYPOTHESES**

**RESEARCH METHODOLOGY**

**RESULTS & DISCUSSION**

**FINDINGS**

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**BLOCKHOLDER OWNERSHIP STRUCTURE OF SRI LANKAN LISTED COMPANIES****KOPERUNTHEVY KALAINATHAN****RESEARCH SCHOLAR, DEPARTMENT OF COMMERCE, ANNAMALAI UNIVERSITY, ANNAMALAINAGAR****SR. LECTURER****DEPARTMENT OF FINANCE & ACCOUNTANCY****VAVUNIYA CAMPUS****SRI LANKA****VIJAYARANI KALIAPERUMAL****PROFESSOR & HEAD****COMMERCE WING****ANNAMALAI UNIVERSITY****ANNAMALAINAGAR****ABSTRACT**

*The purpose of this study is to identify the blockholder(s) and blockholder ownership structure (BHO) of Sri Lankan listed companies. The study concentrated on 135 companies from 19 sectors except Bank Finance and Insurance during the period from 2007/08 to 2012/13. Firstly, we identified the number of shares issued by the sample companies and the number of shares held by the blockholders. Based on the shares information, the shareholder indices indicate the great disparity between block shareholdings and minority shareholdings. Further, the distribution of BHO proves that nearly 50 per cent of the sample companies' blockholders have more than 75 per cent of equity shares and more than 80 per cent of the blockholders are institutions. Finally, the study identifies that on average 72 per cent of the shares controlled by minuscule number of blockholders and nearly 90 per cent of the companies are under the control of five or less number of blockholders. Therefore, the study proves that the listed companies of Sri Lankan stock market are controlled by the hefty blockholders.*

**KEYWORDS**

Blockholders, corporate governance, control, ownership.

**JEL CLASSIFICATION**

G32, G34.

**1. INTRODUCTION**

The corporate governance determines the relationship and corresponding responsibility among a core group of an organization (OECD, 1999). Several corporate governance theories have evolved in developed market as a result of economic development of industrial capitalism (Chowdary, 2003). Individual nations form its corporate governance based on their economic, political, and legal background. As a result, corporate governance system becomes very complex because it considers legal and institutional frame work; legal provisions; corporate governance guidelines and codes; code of ethics; provisional institutions; and social, political and economic environment (Manawaduge, 2012). However, in emerging market, most of these components are missing and poor corporate governance is considered as one of the main causes of the Asian economic crises (Nam & Nam, 2004).

This financial crises make known that there should be a move towards better corporate governance structure all over the world. Even though, some investors own a significant proportion of voting shares in an entity and could act together, they form a block shareholding (blockholders). If they do act as blockholders, they may be able to influence corporate decisions such as corporate strategies of acquisition policy, on the acquisition and dismissal of directors, financial strategies of dividend policy or capital structuring and investment strategies. Further, minority expropriation is motivated by the private benefit of control enjoyed by the blockholders.

Several companies in various countries are controlled by blockholders. Italian voting trusts or voting syndicates are group of large shareholders. In Sweden, corporate control become concentrated in the second half of the 20<sup>th</sup> century, but controlling ownership is being diluted with the growth of firms and stock market. Blockholder ownership is also significant in South Korea, Russia and China (Tricker, 2009).

**2. LITERATURE REVIEW**

The important problem of principal – principal problem has been articulated in the context of listed public companies in matured capital markets and has recently been tested in emerging markets. The principal – principal problem is described in a firm with one large shareholder and a fringe of small shareholders (Villalonga & Amit, 2006). In such a firm, the traditional principal – agent conflict is alleviated due to the large shareholder's greater incentives to monitor the managers, but a second type of conflict emerges as large shareholders exercise their substantial control and influence over firm matters and, as agency theory suggests, they have incentives to consume the firm's resources at the expenses of minority shareholders (Anderson & Reeb, 2004). It is important to note that the principal – principal problem overshadows the principal – agent problem when the large shareholder is an individual or family or an institution. This is because an individual or family will have incentives for the firm through excessive compensation, related – party transactions, or special dividends (Ibid). These expenses may lead to poor firm performance related to the principal – principal cost.

Several researches identify that large blockholders dominates the emerging market firms (Shleifer & Vishny (1997), Lins, K (2003) Thomson, S. (2004)). But, these markets are usually associated with low shareholder protection. (Ibid). The block ownership is low in the developed countries compared to developing countries. The top five blockholder ownership is 25 per cent in US firms (Demsetz & Lehn, 1985), 33 per cent in Japanese companies (Prowse, 1992), 52.05 per cent in New Zealand companies (Boone, 2011), and 66.29 per cent to 69.56 per cent in Indonesia (Yuliani, 2012). In Sri Lanka, 92 per cent of small – investment shareholders hold 10 per cent of share capital. A small number of large shareholders control a greater proportion of voting rights; on average, 1.25 per cent of shareholders are large shareholders, they own 73 per cent of shares (Samarakoon, 1999). Manawaduge, De Zoysa, & Rudkin (2009) found that the largest one shareholder in Sri Lankan listed companies controlled 10.57 per cent to 83.15 per cent of shares and majority of shares under the control of minority number of shareholders. Kalainathan & Vijayarani (2013) proves that Sri Lankan Finance sector' 66.47 per cent of the equity shares are controlled by 0.22 per cent block shareholders. Blockholders have power to influence on corporate activities and control (Kalainathan & Vijayarani, 2012). The large /block shareholders reduce agency cost and hence increase the firm value (Manawaduge *et al.*, 2009). The effect of blockholder ownership on firm value could be positive or negative; the positive effective may come about because large shareholders have greater power and stronger incentives to ensure shareholders value maximization (Thomsen, 2004). A negative effect may occur, if blockholder ownership above a certain level leads to entrenchment of owner – manager that expropriates the wealth of minority shareholders (Fama & Jensen, 1983).

The blockholders may be individuals, government, directors, financial institutions and corporate blockholders (Boone, 2011). Several countries' institutional ownership is more than the other categories of block ownership (Boone, 2011; Senaratne & Gunaratne, 2007). Konijn, Kraussl, & Lucas (2009) argues that the directors' stake of company is good for value determination and external blockholders are bad for firm value. The financial institutions positively influence the firm value (Boone, 2011).

### 3. IMPORTANCE OF THE STUDY

The present study will contribute to the existing knowledge concerning ownership structure, especially block owners and their types by examining the different blockholders.

In the existing literature, several researchers studied corporate governance, and ownership structure in Sri Lanka (Samarakoon (1999); Senaratne and Gunaratne (2007); Waduge (2010); Waduge (2012); and Wellalage and Locke. (2012)). Most of the studies concentrated on ownership impact on performance of Sri Lankan listed companies (Manawaduge *et al.*, (2009); Heenetigala and Armstrong (2011); Kajanathan R. (2012); and Pathirawasam and Wickremasinghe (2012)).

Further, it is suitable to know the large/block, shareholders in Sri Lankan stock market. At the same time, the blockholder ownership and firm value has not been investigated as a single study in previous research in Sri Lanka. Therefore, this study will contribute to knowledge as this will be the first study to identify the blockholders in Sri Lankan listed companies and the types of blockholders who dominate the stock market.

### 4. STATEMENT OF THE PROBLEM

Several corporate failures – Enron, World com, and Xerox, etc., - show the importance of good corporate governance system in all over the world. The corporate governance safeguards the key players such as managers, employees, suppliers, customers, shareholders, executive managers, and board of directors.

During the period from 1990s, several corporate scandals taken place in Sri Lanka have caused much turmoil in stakeholders of companies. In December 2008, Golden Key Credit Card Company (GKCC) of Ceylinco Consolidated collapsed. It is apparent from the facts revealed so far that the collapse of GKCC is associated with both the mismanagement and mis- appointment of funds by directors and managers of the company. These corporate scandals raise the obvious question as to why such incidents take place and who is accountable for these incidents.

Several studies indicate that the owners' influence on management decisions and most of the countries have large controlling shareholders. (Cleassens *et al.*, 2002; La porta *et al.*, 1997). LaPorta *et al.*, (1997) investigate the issues of ultimate control of large companies and found that the controlling shareholders typically have power over these firms significantly in excess of their cash flow rights, primarily through the use of pyramids and participation in management. Further, Senaratne & Gunaratne (2007) found that in the owner controlling companies, the owners can exert more influence on management as they usually participate in the board and management. This argument supported Jensen & Meckling (1976) finding of owner manager and owner controlled firms do not have the same incentives to divert resources, since they would suffer directly from reduced share values while non – owner manager would not.

Although the owners who have block shares could act as an effective monitoring mechanism in companies, these owner directors or managers are invariably confronted with the situations where their interest as major shareholders conflicts with that of other minority shareholders. Further pyramids and cross holding structures in Sri Lankan listed companies allow blockholders to achieve control rights in excess of cash flow rights in a company. This creates tunnelling in these companies. In Sri Lanka, majority of voting shares are controlled by the minuscule number of shareholders (Manawaduge, *et al.*, 2009). Therefore, in Sri Lankan listed companies, the principal – agent problem mainly lies between the blockholder (controlling owners) and the minority shareholders (Senaratne & Gunaratne 2007).

At the same time, as the experience of Ceylinco Group, it is argued that the failure of corporate performance is an indicator of failure of selection of directors. (Daily Mirror, 10 March 2009). The appointment of board of directors is in the hands of very few equity shareholders who have power to control entire organization. These block shareholders (blockholders) have power to control all organizational activities.

Further, the blockholder ownership motivates shared benefit of control and private benefit of control. This two-control mechanism will lead to decision-making control and value of the firm. Therefore the research focuses on the research question.

What is blockholder ownership structure in Sri Lankan listed companies and the type of blockholders?

### 5. OBJECTIVES

- 1) Identify the distribution of shares and ownership to blockholders and its changes in Sri Lankan stock market
- 2) Identify the blockholder ownership structure and blockholders in Sri Lankan stock market.

### 6. METHODOLOGY

#### 6.1. SAMPLE SELECTION

In order to identify the blockholder ownership in Sri Lankan stock market a set of data are needed. As on 31<sup>st</sup> December 2013, the Colombo Stock Exchange (CSE) had 289 listed companies representing 20 business sectors. According to the Manawaduge *et al.*, (2009), Wellalage & Locke (2012); Imam & Malik (2007), the Banking Finance and Insurance sector is excluded because its applicable regulations vastly differ from other sectors, especially in shareholding. To avoid this bias on analysis, the sample companies comprised 19 sectors.

At the end of 2013, out of 289 companies, 66 companies were listed and 12 companies were delisted during the study period. These companies were excluded from the study. Out of 235 companies, 100 companies did not upload their all annual reports in the CSE web site during the study period. So, the sample consisted of 119 companies except 16 finance companies.

#### 6.2. PERIOD OF STUDY

The data include six years information which were gathered from financial reports for the financial years from 2007/08 to 2012/13. The samples include companies whose financial year ends in December or March. For the purpose of estimation of blockholder ownership, financial year ending in December of a given year and March of the following year are treated as corresponding to one financial year.

Institute of Chartered Accountants of Sri Lanka (CA Sri Lanka) issued the voluntary codes of best practices on corporate governance in 2003 and in 2007, corporate governance standards were made mandatory for all listed companies for the financial year commencing on 1<sup>st</sup> April 2008. The new Company Act No.07 of 2007 was introduced with effect from March 3, 2007. Therefore, the study period comprised from 2007/08 financial years to 2012/13 financial year.

#### 6.3. VARIABLES

**Blockholder Ownership (BHO)** - A blockholder is defined by the literatures as the shareholders that own 5 per cent or more of the company's common shares. This blockholder ownership is divided into the following categories:

- i. **Institution Block Ownership** - The institutions both financial institutions and corporate directly invested in a company's common stock.
- ii. **Director Block Ownership** - These are shareholders who are present in the Board of directors.
- iii. **Individual Block Ownership**- These are shareholders who own shares of companies with an intention of earning future dividends and for the potential of growth in the value of investments.
- iv. **Government Block Ownership** – This ownership is classified as governments block ownership when either the Sri Lankan Government or related Government Agencies are one of the blockholders.

## 7. RESULTS AND DISCUSSION

### 7.1 DISTRIBUTION OF SHARES

The blockholder ownership has been studied in many countries. The details of blockholder information will support to know the disparity between blockholders and minority holders in a stock market. In order to provide real facts related to blockholders in Sri Lankan stock market, it identified the shareholders information such as total number of shares, number of shareholders, number of shares held by blockholders and number of blockholders in each sample years.

TABLE 1: SHAREHOLDERS INFORMATION

Year	Number of Shares (in millions)	Number of Shareholders	Shares held by Blockholders (in millions)	Number of Blockholders
2007/08	15,469.34	398,796	12,217.04	374
2008/09	16,379.84	406,105	12,652.47	380
2009/10	17,130.69	418,859	13,124.60	366
2010/11	20,920.27	467,007	15,798.82	358
2011/12	22,179.47	477,545	16,628.34	359
2012/13	24,750.67	466,698	18,799.64	354

Source: Annual reports of sample companies

Based on the shares and shareholders information gathered in each sample years, the Table 1 shows that the number of shares issued over 2007/08 is 15,469.34 million and this number increased to 24,750.67 million in 2012/13. During the sample period, the number of shares in sample companies increased by right, bonus and new issue. Number of shareholders in sample companies is 398,796 in 2007/08 and this number increases as 466,698 in 2012/13. Compare to number of shareholders in 2011/12, number of shareholders decreased by 10,847 in 2012/13. This downward trend is a sign of loss of investors' confidence in Sri Lankan stock market. Further, shares held by blockholders in 2007/08 are 12,217.04 million and this number increased as 18,799.64 million in 2012/13. Number of blockholders in 2007/08 is 374 and this number decreased as 354 in 2012/13. Other than 2008/09 financial year, falling number of blockholders illustrate about blockholders downward trend during the sample period. Further, number of shareholders and number of blockholders notify that great disparity between majority holders and minority holders, that is minority of block holders control hefty shares and majority of minority holders have power over a very small proportion of equity shares.

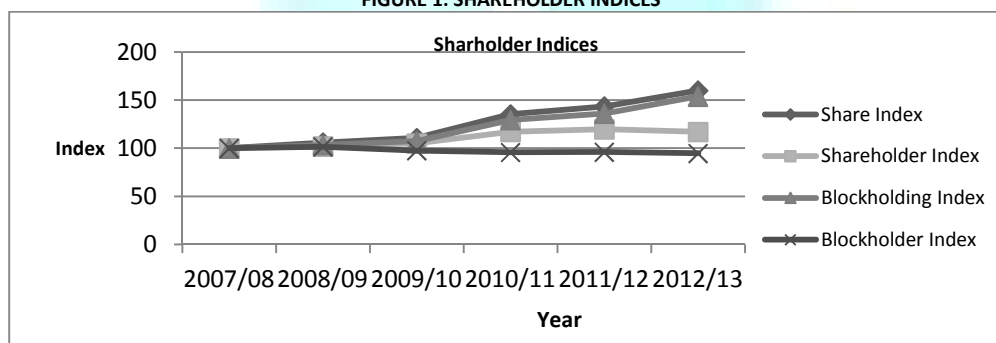
The movement of disparity among number of shares, number of shareholders, number of shares held by blockholders and number of blockholders computed by indices such as Share Index, Shareholder Index, Blockholding Index and Blockholder Index. Financial year 2007/08 is considered as base year for index calculation because corporate governance standards were made mandatory for all listed companies from the financial year commencing on 1<sup>st</sup> April 2008. The new Company Act No.07 of 2007 was introduced with effect from March 3, 2007. Therefore, based on the financial year 2007/08 as base year, the Table 2 provides movement detail of indices from 2007/08 to 2012/13 financial years.

TABLE 2: SHAREHOLDERS INDICES

Year	Share Index	Share holder Index	Block holding Index	Block holder Index
2007/08	100	100	100	100
2008/09	105.89	101.83	103.56	101.60
2009/10	110.74	105.03	107.43	97.60
2010/11	135.24	117.10	129.32	95.72
2011/12	143.38	119.75	136.11	95.99
2012/13	160.00	117.03	153.88	94.65

Source: Calculated from shareholders information in annual reports of sample companies

FIGURE 1: SHAREHOLDER INDICES



Shares Index reports that the shares issued by sample companies increased by 60 per cent from 2007/08 to 2012/13. In 2010/11, number of shares shows a distinct shift by 25 per cent from 2009/10 and then gradually increases year by year. The Blockholding Index also increases simultaneously with Share Index. The trend of Share Index and Blockholding Index confirm that most of the shares issued during the sample period were purchased by blockholders. The Figure 1 obviously indicated that both the lines of Share Index and Blockholding Index move together with same pattern of upward trend without much gap. The Shareholder Index reports that an upward trend from 2007/08 to 2011/12 and down by 2.74 per cent in 2012/13 compared to 2011/12. Total trend of Shareholder Index shows that the majority of new shares issued by sample companies during the sample period were distributed to blockholders and a small number of shares issued to minority holders. Further, a lesser number of new investor's arrival is observed during the survey period. The Blockholder Index reveals that the number of blockholders decreases while blockholding increases. This leads to a gap between Blockholding Index and Blockholder Index deviating year by year. This is an indication that the existing blockholders boost their strength and disparity between Blockholder Index and Blockholding Index significantly increases. This kind of movement shows that the companies voting rights and control system move towards autocratic system.

Great disparity between blockholding and total shareholding indicates that the minority holders are dissatisfied with the company's activities and these dissatisfied - minority shareholders "walked away" by selling their shares. This situation informs that the minority holders are reluctant to keep their investment in this stock market. Any dissatisfied - large shareholders can follow "investor activism"<sup>1</sup> or "relationship investing"<sup>2</sup> (Lashgari, 2004). This situation leads to concentrated and cross holding. Sri Lankan legal system allowed concentrated and cross holding. Further, the system allowed large shareholders to be a combination of aggressively controlling management as well as a friendly one.

<sup>1</sup> Investor activism is a way in which shareholders can influence a corporation behavior by exercising their rights as owners (Investopedia.com)

<sup>2</sup> There is an established committed link between a company and one or more shareholders (Bloomberg Business week)/ Interaction between institutional investors and managers (Chidambaram & John (1998).

This shareholders' activism involves the task of aggressive monitoring and controlling the firm's management for the purpose of enforcing changes in the firm's structure of internal control and increasing shareholders wealth.

### 7.1.1 DISTRIBUTION OF BLOCKHOLDER OWNERSHIP AND BLOCKHOLDERS

It is important to understand the blockholder distribution among sample companies. Based on the control power we have identified four BHO ranges such as Very Low (5% ≤25%), Low (25% ≤50%), High (50% ≤ 75%) and Very High (75% ≤100%). The Table 3 provides information on blockholder distribution for sample period. Panel A of Table 3 provides details of number of companies based on different ranges of BHO and Panel B of Table 3 provides details of number of blockholders based on different ranges of BHO.

TABLE 3: BLOCKHOLDER OWNERSHIP DISTRIBUTION

BHO Ranges	2007/08	2008/09	2009/10	2010/11	2011/12	2012/13
<b>Panel A – Number of companies based on BHO</b>						
Very low (VL)	1	1	1	1	1	0
Low (L)	7	6	9	9	9	9
High (H)	53	48	50	54	53	50
Very High (VH)	58	64	59	55	56	60
<b>Total</b>	<b>119</b>	<b>119</b>	<b>119</b>	<b>119</b>	<b>119</b>	<b>119</b>
<b>Panel B – Number of Blockholders based on BHO</b>						
Very low (VL)	2	2	1	1	2	0
Low (L)	18	18	27	20	21	24
High (H)	177	158	160	166	159	150
Very High (VH)	177	202	178	171	177	180
<b>Total</b>	<b>374</b>	<b>380</b>	<b>366</b>	<b>358</b>	<b>359</b>	<b>354</b>
<b>Panel C – Average Number of Blockholders</b>						
<b>Overall</b>	<b>3.14</b>	<b>3.19</b>	<b>3.08</b>	<b>3.01</b>	<b>3.02</b>	<b>2.97</b>

Source: Annual reports of sample companies, twenty largest shareholders schedule.

Different ranges of ownership structures influence in different ways on corporate activities and firm value. 5 per cent of equity ownership is the minimum threshold to determine blockholder ownership. Table 3 classifies blockholders' equity ownership from 5 per cent. Very low level BHO range and Low level BHO ranges show the Low level of control on firm activities and more than 50 per cent of BHO ranges shows the full control on firm activities.

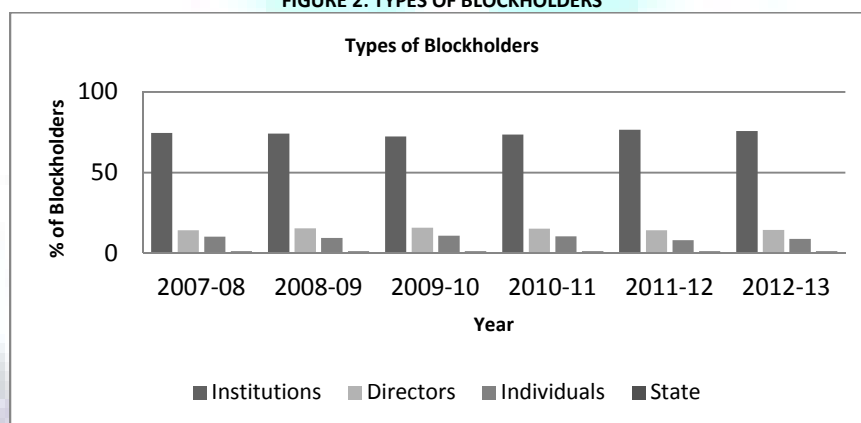
Very low level block equity shares are in one company for first five sample periods and these shares are controlled by two and one shareholder/s from 2007/08 to 2011/12. In 2012/13 none of the companies' block equity shares come under this Very Low level. Low level equity shares are under the control of blockholders in seven companies, six companies and nine companies in 2007/08, 2008/09 and from 2009/10 to 2012/13 respectively. Numbers of blockholders with low level control are fluctuated from 18 to 27 in this survey period. But, more than 50 per cent of shares are controlled by blockholders in 111, 112, 109 and 110 companies out of 119 companies in 2007/08, 2008/09, 2009/10 to 2011/12 and 2012/13 respectively. These absolute control go to 354, 360, 338, 337, 336 and 330 blockholders in 2007/08, 2008/09, 2009/10, 2010/11, 2011/12 and 2012/13 respectively. Nearly 50 per cent of the sample companies' blockholders have more than 75 per cent of the equity shares.

These results prove that rigid blockholders control the sample companies and these numbers of blockholders gradually decrease. This result is further strengthened by Panel C of Table 3. It shows that average number of blockholders decrease from 3.14 to 2.97. Therefore, the Table 3 proves that the Sri Lankan listed companies are controlled by hefty blockholders.

### 7.1.2 TYPES OF BLOCKHOLDERS

According to the number of blockholders presented in the Panel B of Table 3 the categories of blockholders are presented in the Table 4. Based on the previous literatures (Lee (2010) as cited by Wellalage & Locke (2012); Waduge, 2010; Jensen & Meckling (1976); Lins, K. 2003; Boone, 2011; Senaratne & Gunaratne, 2007; Kalainathan & Vijayarani, 2013) related to Sri Lanka and other countries major groups of blockholders are the institutions, directors, individuals and state identified as types of blockholders in this stock market. Different types of blockholders have different purpose to invest in a particular company. According to their purpose, the influence on decision making may differ. Therefore, it is essential to identify the types of blockholders.

FIGURE 2: TYPES OF BLOCKHOLDERS



Institutions are the major equity holders in CSE. 74.6 percentages of blockholders are institutions in 2007/08 and this percentage increases as 75.7 percentages in 2012/13 financial year. At the same time, numbers of institutions are 279 in 2007/08 and this number decreased as 268 in 2012/13. During this study period, the number of institutions and percentage of shares held by institutions show smaller differences on trend. In addition to this total trend, all ranges, Very Low, Low, High and Very High level of institutional BHO prove that there are minute fluctuations on shareholdings.

Directors are the second large blockholders in Sri Lankan stock market. Among all blockholders in sample companies, nearly 15 per cent (on average) are directors. In 2007/08, 14.2 per cent are directors and this value increases as 14.4 per cent in 2012/13. During the sample period, percentages of directors fluctuated minutely. Numbers of directors are 56 in 2007/08 and decreased as 51 in 2012/13. Both, percentages and numbers of director blockholders show that there is an insignificant change in directors' blockholdings and blockholders. All ranges of director blockholders also prove this result.

Individual blockholders are the third category. They are 10.2 per cent in 2007/08 and decreased as 8.8 per cent in 2012/13. During the sample period, individual blockholders have a small fluctuation as other category of blockholders.

State BHO also remains unchanged as 1.1 percentages in all sample periods. Therefore, all categories of blockholders are remaining unchanged to hold their shareholdings. These results prove that the blockholders are very rigid to keep their shareholdings and institutions dominate the stock market.

## 7.2 BLOCKHOLDER OWNERSHIP STRUCTURE AND BLOCKHOLDERS

Identification of BHO will provide clear information regarding the importance of blockholders and types in CSE. The BHO is calculated as a percentage of total number of equity shares to total shares and percentage of blockholders as a percentage of total number of equityholders. The total BHO of sample companies and their different types of BHO are presented in the Table 5. Panel A of Table 5 explains the percentage of BHO and the types of BHO and Panel B of Table 5 explains the percentage of blockholders and their type. The analysis focuses on two key statistics of BHO structure; the mean percentage of BHO and the mean percentage of blockholders in each sample period.

TABLE 5: BLOCKHOLDER OWNERSHIP STRUCTURE

Blockholder	2007/08	2008/09	2009/10	2010/11	2011/12	2012/13
<b>Panel A - Blockholder Ownership (in percentage)</b>						
Institutions	61.81	63.78	62.07	61.89	63.92	64.42
Directors	6.05	6.61	6.51	6.27	5.67	5.21
Individuals	4.17	3.22	3.41	3.41	2.62	2.87
State	0.61	0.61	0.52	0.51	0.52	0.52
<b>Total</b>	<b>72.64</b>	<b>74.22</b>	<b>72.51</b>	<b>72.08</b>	<b>72.73</b>	<b>73.02</b>
<b>Panel B - Blockholders (in percentage)</b>						
Institutions	0.279	0.266	0.223	0.197	0.181	0.165
Directors	0.109	0.111	0.100	0.071	0.067	0.047
Individuals	0.081	0.070	0.066	0.061	0.042	0.050
State	0.000	0.000	0.000	0.000	0.000	0.000
<b>Total</b>	<b>0.469</b>	<b>0.447</b>	<b>0.389</b>	<b>0.329</b>	<b>0.289</b>	<b>0.262</b>

Source: Annual reports of sample companies, twenty largest shareholders schedule

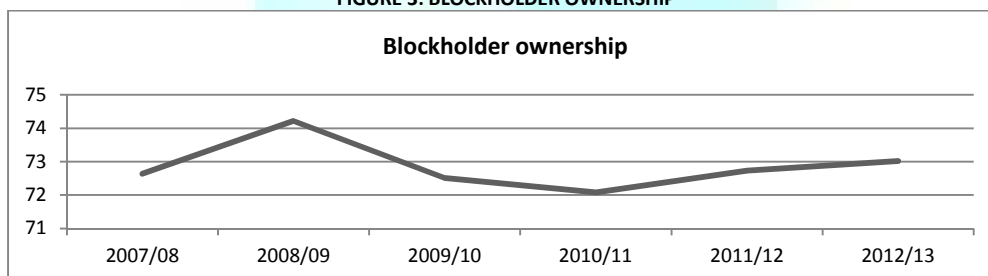
Institutions are the large blockholders and they hold a good grasp of ownership, which is 61.81 percentages equity shares in 2007/08 in the sample companies. These institutional grasps of ownership increases as 64.42 percentages in 2012/13 and BHO values vary between these two values during the sample period. As Lee (2010) mentioned, it is observed that as an undeveloped equity market and weak investor protection, domestic investors are reluctant to invest in emerging market. Therefore, institutional investors dominate this market. While institutional investors are dominant shareholders in this market, they raise their power to monitor and control Board of Directors (BOD) and management. According to Vittas (2000), this kind of dominant institutional shareholders can no longer exist without disturbing the market; instead they exercise their voice mostly through various collective bodies. Waduge (2010) argues that the increase of institutional investors in Sri Lankan stock market positively influence for best governance practice.

Directors are the second large blockholders and they hold 6.05 percentage of shares in 2007/08 and 5.21 percentages in 2012/13. Directors BHO gradually increases up to 2009/10 and from 2010/11 it gradually decreases. Individuals are the third category of blockholders owning only 4.17 percentages of shares in 2007/08 and this value slowly decreases with little fluctuation and reaches 2.87 percentages in 2012/13. State BHO is the last category owning only 0.61 percentages of shares and this value fluctuate up to 0.52 per cent and 0.51 per cent in these sample periods. The state ownership is in plantation sector only. Total BHO during the sample period fluctuates from 72.64 per cent in 2007/08 to 73.02 per cent in 2012/13 and this fluctuation is insignificant.

Panel B of Table 5 shows the percentage of blockholder. Institution blockholders are 0.298 per cent in 2007/08 and gradually decreases as 0.165 per cent in 2012/13. Directors and individuals blockholders percentages also gradually decrease and State has very tiny percentage equal to 0.0 percentages. Total blockholders percentages show that the blockholders on the total shareholders decrease every year and their shareholdings do not change considerably.

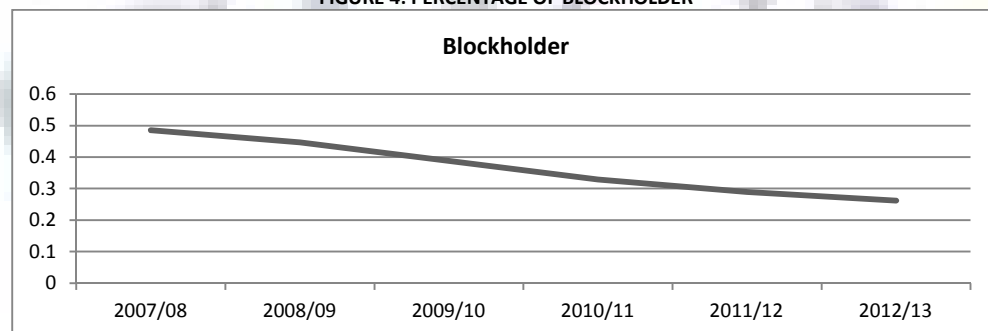
The following figures 3 and 4 show the BHO and percentage of blockholders.

FIGURE 3: BLOCKHOLDER OWNERSHIP



From 2007/08 to 2012/13, the BHO fluctuates with minute differences. In the financial year of 2008/09, there is a distinct shift of BHO structure. End of civil war in May 2009 might be the reason for this peak. After this peak pattern of BHO structure becomes its normal level. This result confirms that the BHO has rigid power over equity shares.

FIGURE 4: PERCENTAGE OF BLOCKHOLDER



The blockholders percentages slowly but surely decrease from 0.485 percentages to 0.262 percentages. This figure proves that the numbers of total shareholders increase during the sample period by new issues and sales of shares, but the new issues and sales failed to bring new shareholders into companies. Therefore, the Table 5 and the Figures 3 and 4 proves that majority of voting shares are controlled by minuscule percentage of shareholders. This kind of share ownership pattern may lead to minority expropriation.

### 7.2.1 NUMBERS OF BLOCKHOLDERS IN COMPANIES

In addition to BHO structure, the numbers of blockholders may influence on companies' activities. Less numbers of blockholders have more power on voting than high numbers. Numbers of blockholders in the sample companies are presented in the Table 6. There are maximum ten blockholders that control majority of the equity shares in the sample companies. Numbers of companies, percentage of companies are identified based on numbers of blockholders.

TABLE 6: NUMBER OF BLOCKHOLDERS IN COMPANIES

Number of Block holders	2007/08		2008/09		2009/10		2010/11		2011/12		2012/13	
	Companies	Percentage	Companies	Percentage	Companies	Percentage	Companies	Percentage	Companies	Percentage	Companies	Percentage
10	1	0.84	1	0.84	1	0.84	1	0.84	1	0.84	1	0.84
8	1	0.84	1	0.84	1	0.84	1	0.84	1	0.84	1	0.84
7	2	1.68	3	2.52	1	0.84	3	2.52	2	1.68	2	1.68
6	6	5.04	6	5.04	6	5.04	5	4.20	5	4.20	5	4.20
5	13	10.9	15	12.6	15	12.61	9	7.56	8	6.72	8	6.72
4	21	17.7	19	16.97	18	15.13	19	15.97	22	18.49	19	15.97
3	24	20.2	25	21.01	26	21.85	29	24.37	31	26.05	31	26.05
2	34	28.6	30	25.21	29	24.37	30	25.21	27	22.69	31	26.05
1	17	14.2	19	15.96	22	18.48	22	18.49	22	18.49	21	17.65
<b>Total</b>	<b>119</b>	<b>100</b>	<b>119</b>	<b>100</b>	<b>119</b>	<b>100</b>	<b>119</b>	<b>100</b>	<b>119</b>	<b>100</b>	<b>119</b>	<b>100</b>

Source: Annual reports of sample companies, twenty largest shareholders schedule

One blockholder is in seventeen companies in 2007/08 and this numbers of companies increased as twenty one in 2012/13. During the sample period, one blockholder companies increase every year. Two and six blockholder companies are thirty four and six respectively in 2007/08 and these numbers of companies gradually decrease during the sample period. Three and five blockholders companies show an increasing trend and four blockholders companies fluctuated during this period. Eight and ten blockholders are in one company and none of the companies has nine blockholders.

These calculations in the Table 6 reveal that more than 96 per cent of the companies have six or less blockholders and more than 62 per cent of the companies have three or less blockholders. These results prove that minuscule numbers of blockholders control entire companies in CSE.

Blockholder ownership structure in Sri Lankan listed companies is higher than the developed countries. This ownership pattern has encountered hurdles to trading coming from both major private investors and errant government elements. At the same time, as an emerging market CSE is so small and a small group of investors with deep pockets can manipulate prices. That is the reason that CSE had not grown since then to keep pace with the growth of the economy.

The manipulation in CSE includes pumping and dumping and insider trading created by these dominant group of blockholders. During the period from 2008 – 2012, it is identified that 182 instances of suspected dealing have been found by investigation unit of the SEC (Eye Sri Lanka).

The pumping and dumping involves the overvaluing of shares at an artificially inflated price. However, this is happen at the expenses of another party. In early 2011, the bubble burst and the index was reached around 5,000 points. Foreign investors have withdrawn funds and CSE is rated as one of the world's "worst performing" market (Gunadasa, 2012). Further, the Employees' Provident Fund (EPF) loss of Rs.1389 million in July 2012 (Position paper, Transparency International, Sri Lanka) is the one example of pumping and dumping activity during the study period.

Insider trading is another problem of market manipulation. Position paper (Transparency International, Sri Lanka) indicates peculiar detail of Sri Lankan investor community; geographical distribution of stock market players aids in the speedy transparency of material information. Therefore, some investors including regulators become as a close – knit society. These controversial remarks highlight not only ease with which the material information pass through investor circles, but also the callousness with which perpetrators may publicly claim their nefariousness. National Saving Bank (NSB) purchased 13 per cent of The Finance Company (TFC) shares for Rs.49.74 per share, where typical share prices were at Rs.30 at the same day. These TFC shares purchased from two of the company directors.

Market manipulation may occur by several reasons. But, it is pointed out that it could be greed in the mind of the controlling interest or senior marketing director or it could very well be poor corporate governance.

As seen in the NSB scandal, the saving of the Sri Lankan people was plundered in order to artificially inflate stock prices. Another consequence of market manipulation is the shareholders fatigue; this fatigue occurs when minority shareholders do not receive dividends on their preferred stock while company directors tied up with profit reaping on their manipulations.

Therefore, share market manipulation makes serious losses to minority shareholders and weak investors as well as society. This white collar crime has to be changed; it is not that whether the rich are stealing from the rich; it is quite evident that the rich are stealing from society as a whole.

## 8. FINDINGS

1. Most of the issued shares in CSE are controlled by the blockholders. The new issues also purchased by the blockholders. This result is proved by the total trend of Shareholder Index. Further, a lesser number of new investor's arrival is observed during the survey period. The Blockholder Index reveals that the number of blockholders decreases while blockholding increases. This leads to gap between Blockholding Index and Blockholder Index deviating year by year.
2. It is observed that rigid blockholders control these sample companies and these numbers of blockholders gradually decrease. This result proved in the study by the average number of blockholders decreased from 3.14 to 2.97.
3. Majority, 75 (on average) percentages of blockholders are institutions in the study period, nearly 14 (on average) percentages of blockholders are directors, nearly 10 (on average) percentages of blockholders are individuals and only 1percentage of the blockholder is government.
4. More than 72 per cent of the equity shares are controlled by the blockholders and these blockholders are only less than 0.4 per cent (on average) on total shareholders.
5. Maximum of 10 blockholders are in the sample companies and more than 90 per cent of the companies have five or less numbers of blockholders.

## 9. RECOMMENDATIONS

1. The government of Sri Lanka should take necessary action to make CSE as an efficient market. Therefore, government should consider small investor protection schemes.
2. The Securities and Exchange Commission (SEC) must take strong stance against white collar crime, resisting political, dominant families and individual interferences.
3. Public awareness campaigns on the misuse of public funds by the dominant shareholders should be made by the SEC and code of best practices should be strengthened to encourage small investors to invest in the stock market.

## 10. CONCLUSION

The study identifies the blockholder ownership of Sri Lankan listed companies. Most of the issued equity shares are controlled by the blockholders and disparity between block shareholding and minority shareholding is very high in CSE. Further, it is observed that the majority, more than 90 per cent, of the blockholders control more than 50 per cent of the share. This situation shows that majority of the companies ultimate control is in the hands of minority blockholders and majority of companies are controlled by high and very high level ranges of BHO and majority of blockholders are institutions. More than 90 per cent of

companies have 5 or less blockholders. Therefore, this study proves that blockholders control is very high in Sri Lankan stock market than in other countries stock markets.

## 11. LIMITATIONS

Notwithstanding the findings, the present study does have its own limitations, which point to potentially fruitful further research.

1. The research focuses on the blockholder ownership structure of Sri Lankan listed companies. Generalization of these findings to other countries needs to be done with caution.
2. Nearly 50 per cent of non – financial companies are included because of availability of data.
3. The study excluded financial related firms because applicable regulations from the finance sector are vastly different from other sectors.

## 12. SCOPE FOR FURTHER RESEARCH

The blockholder ownership is higher in Sri Lanka than in other developed countries. Therefore, the scope for further researches is:

1. How blockholders influence on corporate activities, especially decision making and controlling.
2. How blockholder ownership determines the value or performance of companies.

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