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# The Role of Managerial Discretion in Agency Problems and Stock Repurchase Decisions in China

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**ABSTRACT**

This study examines the relationship between managerial discretion, agency problems, and stock repurchase decisions in Chinese publicly listed firms between 2011 and 2021. Using data from over 1,000 companies listed on the Shanghai and Shenzhen stock exchanges, this research employs Structural Equation Modelling (SEM) and regression analysis to test the impact of managerial discretion on agency problems and its subsequent effect on stock repurchase behavior. The findings reveal that higher levels of managerial discretion are positively associated with increased agency problems, supporting agency theory's premise that managers may prioritize personal interests over those of shareholders. Furthermore, agency problems mediate the relationship between managerial discretion and stock repurchase decisions, with firms facing higher agency costs more likely to engage in repurchases as a means of managing these conflicts. The study also highlights the influence of ownership structure, finding that state-owned enterprises (SOEs) exhibit lower levels of managerial discretion and are less likely to engage in stock repurchase programs compared to privately owned enterprises (POEs). Lastly, event study methodology shows that stock repurchase announcements lead to positive market reactions, suggesting that repurchases are seen as a signal of financial strength. This research contributes to the understanding of corporate governance in China, offering insights into how managerial discretion and ownership structures influence financial decision-making. The study has implications for both corporate executives and investors, highlighting the importance of governance mechanisms in aligning managerial actions with shareholder interests. Future research directions are also discussed, including the potential for longitudinal studies and comparative research across different emerging markets.

**Keywords:** Managerial discretion, Agency problems, Stock repurchase decisions, corporate governance, Chinese firms, Structural Equation Modelling (SEM), Agency theory, Ownership structure, State-owned enterprises (SOEs), Privately owned enterprises (POEs), Event study methodology, Market reactions, Corporate financial decisions, Governance mechanisms, Shareholder interests.

## INTRODUCTION

In corporate governance, agency problems arise from the inherent conflict of interest between managers (agents) and shareholders (principals). While shareholders seek to maximize their returns and safeguard the long-term value of their investments, managers often face competing incentives that may not align with those of shareholders. These misalignments can lead to inefficient decision-making, agency costs, and ultimately, a reduction in shareholder value. One common consequence of agency problems is the decision to undertake corporate actions, such as stock repurchase programs, that may be motivated by managerial interests rather than the true benefit of shareholders.

In this context, managerial discretion plays a pivotal role in determining how agency problems are handled within firms. Managerial discretion refers to the latitude or freedom that managers have in making decisions without being heavily influenced by external constraints, such as shareholder pressure, regulatory frameworks, or industry norms. The level of discretion varies across firms and industries, but it is particularly significant in companies with weak

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governance structures or in environments where oversight is limited. As a result, managerial discretion can either exacerbate or alleviate agency problems. On the one hand, higher discretion may enable managers to make bold, innovative decisions that drive corporate growth; on the other hand, it can also lead to opportunistic behavior, where managers prioritize their own interests over those of shareholders.

Stock repurchase decisions have become an important mechanism used by firms to address agency problems, particularly in situations where managers have the autonomy to influence financial decisions. A stock repurchase occurs when a company buys back its own shares from the open market, typically to signal confidence in its future prospects, increase earnings per share (EPS), or distribute excess capital to shareholders. From an agency perspective, stock repurchases can serve as a tool to reduce agency costs by aligning the interests of managers with those of shareholders. When managers repurchase stock, they often aim to signal to the market that the company is undervalued, which may encourage investors to trust in the company's long-term prospects and, in turn, support the stock price.

However, the decision to repurchase shares is not always solely driven by shareholder interests. In firms where managerial discretion is high, managers may use stock repurchase programs as a strategic tool to enhance their personal incentives, such as increasing short-term stock prices to meet compensation targets or reduce agency costs at the expense of long-term corporate growth. This phenomenon often occurs in the absence of strong governance structures that can regulate and monitor managerial decision-making.

The intersection of managerial discretion, agency problems, and stock repurchase decisions has been well-documented in the literature, but much of this research has focused on Western economies. In contrast, the Chinese business environment offers a unique context for exploring these dynamics. China's corporate landscape is characterized by a mix of state-owned enterprises (SOEs) and privately owned firms, each with distinct governance structures and regulatory pressures. In SOEs, the government plays a significant role in shaping managerial decisions, which can limit managerial discretion and affect the motivations behind stock repurchase programs. In privately-owned firms, however, higher levels of managerial discretion may lead to different decision-making processes, with managers potentially using stock repurchases to manage agency costs and maximize shareholder wealth.

Between 2011 and 2021, China has witnessed significant growth in its financial markets, which has led to an increase in the number of publicly listed companies. This period has also seen the rise of corporate governance reforms aimed at improving transparency and reducing agency problems. However, challenges still persist, especially in firms where the ownership structure is concentrated or where external monitoring is insufficient. As such, understanding the role of managerial discretion in addressing agency problems and guiding stock repurchase decisions is crucial for understanding the evolving dynamics of corporate governance in China.

This study aims to fill a gap in the literature by examining how managerial discretion influences agency problems and stock repurchase decisions in Chinese publicly listed companies. By focusing on firms listed between 2011 and 2021, this article seeks to uncover the empirical relationships between these variables and offer insights into the broader implications for corporate governance in China. In doing so, it will contribute to the ongoing discussion on how managerial autonomy interacts with agency costs, and how stock repurchase decisions serve as both a financial strategy and a tool for mitigating conflicts of interest.

The findings of this research will provide valuable insights for corporate executives, investors, and regulators seeking to enhance corporate governance practices and align managerial decisions with shareholder interests. Understanding the relationship between managerial discretion and agency problems is critical for ensuring that stock repurchase programs truly benefit shareholders, rather than serving as instruments of managerial self-interest. Additionally, the study will highlight how China's unique corporate environment, shaped by both regulatory frameworks and ownership structures, influences managerial behavior and decision-making.

In conclusion, this article will explore the significant role that managerial discretion plays in shaping agency problems and stock repurchase decisions in China. By examining these relationships, the article aims to offer both theoretical

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contributions to corporate governance literature and practical implications for improving financial strategies and governance practices within Chinese firms.

## LITERATURE REVIEW

The role of managerial discretion in corporate governance, its relationship with agency problems, and its influence on corporate financial decisions such as stock repurchase programs has been the subject of much academic debate and empirical analysis. This literature review aims to explore key theoretical concepts and findings from existing research on these variables, focusing specifically on the context of Chinese firms. By reviewing these studies, the article will identify gaps in the existing literature, particularly regarding the unique corporate governance structures in China, which influence the relationship between managerial discretion, agency problems, and stock repurchase decisions.

### 2.1 Managerial Discretion

Managerial discretion refers to the degree of autonomy and freedom managers have in making decisions without being constrained by external factors, such as shareholder demands, regulatory frameworks, or corporate governance mechanisms. In the context of corporate governance, the level of managerial discretion has been shown to significantly affect a firm's decision-making process and overall performance. The concept is rooted in the work of Hambrick and Finkelstein (1987), who conceptualized managerial discretion as the latitude that managers have in making strategic decisions. This discretion, they argued, is shaped by both organizational characteristics and the external environment in which the firm operates.

In firms with high managerial discretion, executives are free to pursue strategic initiatives, make operational decisions, and implement corporate policies that may deviate from the shareholder's immediate interests. While this autonomy can be beneficial in promoting innovation and growth, it can also lead to opportunistic behavior, where managers prioritize their own interests over shareholder value. For instance, when managers have discretion, they may use financial tools, such as stock repurchases, to increase their compensation based on short-term stock price performance, rather than focusing on long-term firm value (Jensen & Meckling, 1976).

Managerial discretion theory is often examined in conjunction with agency theory, which emphasizes the conflict of interest between shareholders and managers due to the separation of ownership and control in modern corporations. The greater the managerial discretion, the higher the risk of agency problems, where managers make decisions that benefit themselves at the expense of shareholders (Fama & Jensen, 1983). Several studies have highlighted the impact of managerial discretion on corporate policies, particularly in terms of investment decisions, capital structure, and dividend payout decisions (Barker & Mueller, 2002; Kroll et al., 2007).

In the context of Chinese firms, managerial discretion is often shaped by the country's unique economic and regulatory environment. For instance, state-owned enterprises (SOEs) in China typically have lower levels of managerial discretion due to government involvement in corporate decision-making and regulatory constraints. In contrast, privately-owned firms may experience higher discretion, as private owners and managers have more control over strategic decisions (Li & Qian, 2015). The differences in managerial discretion between state-owned and privately-owned firms provide an opportunity to explore how discretion impacts corporate governance and decision-making across different ownership structures.

### 2.2 Agency Problems in China

Agency problems arise when the interests of managers (agents) and shareholders (principals) diverge, leading to conflicts that can result in agency costs, such as inefficiencies in decision-making and a reduction in shareholder value. These problems are particularly pronounced in firms where managers have significant decision-making authority, but where shareholders have limited control over the actions of executives. Agency theory, first formalized by Jensen and Meckling (1976), posits that these conflicts can be mitigated by aligning the interests of agents and principals through incentive mechanisms such as compensation schemes and governance structures.

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In China, agency problems are particularly prevalent due to the unique governance structures of Chinese firms, which include a mix of state-owned enterprises (SOEs) and privately-held companies. In SOEs, where the government holds significant ownership, there may be less concern for maximizing shareholder wealth, as managers are more focused on fulfilling government objectives (e.g., political stability or employment) than on enhancing financial returns. This government control can lead to principal-agent conflicts, where the interests of the government as the principal differ from those of managers, leading to inefficiencies and a lack of transparency (Zhang et al., 2010).

On the other hand, in privately-owned firms, managers may have greater autonomy, which could reduce agency problems if they are closely aligned with shareholders' interests. However, private firms also face challenges, particularly when ownership is concentrated among a small number of individuals or families. In such cases, agency costs can still be significant, as family owners may have interests that diverge from those of minority shareholders (Faccio & Lang, 2002). The level of agency problems in Chinese firms, therefore, depends largely on the ownership structure, the regulatory environment, and the degree of managerial discretion.

### 2.3 Stock Repurchase Decisions as a Tool to Address Agency Problems

Stock repurchases are a strategic financial tool used by firms to return excess cash to shareholders, adjust capital structure, and signal confidence in the company's future prospects. From an agency theory perspective, stock repurchases can serve as a mechanism to mitigate agency problems by reducing the number of shares outstanding and increasing earnings per share (EPS), which can enhance shareholder value. Additionally, stock repurchases can be seen as a signal to the market that the firm's management believes its stock is undervalued, aligning management's interests with those of shareholders (Stephens & Weisbach, 1998).

However, stock repurchase decisions are not always motivated by the desire to benefit shareholders. In firms with high managerial discretion, managers may use stock repurchase programs to manipulate stock prices to meet short-term performance targets or enhance their own compensation, which may not necessarily align with the long-term interests of shareholders (Jensen, 1986). This can exacerbate agency problems, as managers might prioritize personal gain over firm performance. Moreover, free cash flow—excess capital available after investments—has been identified as a key determinant in stock repurchase decisions, as it provides managers with the financial resources to repurchase shares without affecting the firm's operational capabilities (Lang et al., 1995).

In the context of Chinese firms, stock repurchases have become more prominent as corporate governance reforms have evolved. From 2011 to 2021, Chinese regulators introduced new rules to facilitate stock repurchases in publicly listed companies, particularly in response to market volatility and investor demands for better returns (He & Wang, 2016). However, these repurchase programs are still influenced by government control, especially in state-owned enterprises (SOEs), where the decision to repurchase shares may be influenced more by political motivations than by financial objectives (Liu et al., 2019). In privately-owned enterprises, the decision to repurchase shares may be more aligned with managerial discretion, but can still reflect agency problems if managers use the repurchase program to boost short-term stock prices.

### 2.4 Theoretical Foundations of Managerial Discretion, Agency Problems, and Stock Repurchase Decisions

This study draws on several key theoretical frameworks to analyze the relationship between managerial discretion, agency problems, and stock repurchase decisions:

- Agency Theory (Jensen & Meckling, 1976): This framework underpins the study, explaining how agency problems arise when the interests of managers and shareholders diverge, and how mechanisms like stock repurchase programs can mitigate these problems.
- Managerial Discretion Theory (Hambrick & Finkelstein, 1987): This theory provides the basis for understanding the role of managerial autonomy in shaping corporate decision-making, including the decision to repurchase stock.

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- Signaling Theory (Spence, 1973): This theory helps explain how stock repurchases can serve as a signal to the market about a firm's prospects, influencing shareholder perception and stock price.
- Ownership Structure Theory (Shleifer & Vishny, 1997): This theory examines how ownership concentration affects corporate governance and agency costs, with relevance to the differences between state-owned and privately-owned firms in China.

### 2.5 Summary of Literature and Research Gaps

Existing literature has extensively examined the role of managerial discretion and agency problems in shaping corporate financial decisions, including stock repurchase programs. However, most of the studies have focused on Western economies, with limited attention given to the unique challenges faced by Chinese firms. The mixed ownership structure in China, with a significant proportion of state-owned enterprises (SOEs), introduces additional layers of complexity that are underexplored in current research.

This article aims to bridge this gap by empirically examining how managerial discretion influences agency problems and stock repurchase decisions in Chinese firms. By focusing on both state-owned and privately-owned enterprises, this study will provide valuable insights into how governance structures and managerial autonomy interact to shape corporate financial strategies in China. Furthermore, it will contribute to the broader discourse on corporate governance and the role of stock repurchase programs in resolving agency problems in emerging economies.

## DATA AND METHODOLOGY

To explore the relationship between managerial discretion, agency problems, and stock repurchase decisions in Chinese publicly listed companies, this study adopts a quantitative research approach. The analysis uses data collected from publicly available financial reports of Chinese firms listed on the Shanghai and Shenzhen stock exchanges between 2011 and 2021. This period is chosen due to the increasing importance of stock repurchase programs in China and the evolving nature of corporate governance practices and regulations during this time.

### 3.1 Data Sources

The primary data source for this study is financial data from companies listed on China's two major stock exchanges, the Shanghai Stock Exchange (SSE) and the Shenzhen Stock Exchange (SZSE). Data is obtained from multiple financial databases, including Wind Information and RESSET, which provide comprehensive financial and corporate governance data. The dataset includes variables related to managerial discretion, ownership structure, agency problems, and stock repurchase behaviors.

The key variables collected for this study are as follows:

- Managerial Discretion: Measured by the level of managerial autonomy within the firm, which is quantified through ownership concentration and government intervention. In firms with low ownership concentration or high state involvement, managerial discretion is expected to be lower.
- Agency Problems: Proxy variables such as agency costs, calculated using the ratio of managerial compensation to company performance, and ownership concentration, are included.
- Stock Repurchase Decisions: Data on stock repurchase volumes, timing of repurchases, and total capital repurchased are taken from the companies' public filings. Additional data on market reactions to repurchase announcements (such as stock price changes) are also included.
- Ownership Structure: Data on the percentage of state ownership versus private ownership is included to identify the impact of different ownership structures on managerial discretion and decision-making.

The sample includes approximately 1,000 publicly listed firms across different sectors, with a focus on those that have engaged in stock repurchase programs during the study period. The firms are categorized into two main groups: state-owned enterprises (SOEs) and privately-owned enterprises (POEs). The distinction between SOEs and POEs is

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crucial for understanding the variation in managerial discretion and the governance structures that affect agency problems and stock repurchase decisions.

### 3.2 Research Design and Methodology

This study utilizes Structural Equation Modeling (SEM) as the primary analytical tool to examine the relationships between the variables. SEM allows for the analysis of complex relationships between observed and latent variables, making it an appropriate method for testing the theoretical framework outlined in this study. The methodology includes the following steps:

i. Descriptive Analysis: The first step involves conducting descriptive statistics to understand the basic trends in the data, such as the prevalence of stock repurchase programs and the variation in managerial discretion across firms. The distribution of stock repurchase volumes and agency costs across different types of firms (SOEs vs. POEs) will be analyzed.

ii. Factor Analysis: A confirmatory factor analysis (CFA) is used to validate the measurement models for key constructs, such as managerial discretion, agency costs, and stock repurchase behavior. This step ensures that the constructs are measured accurately and consistently across the dataset.

iii. Structural Equation Modeling (SEM): SEM is employed to test the hypothesized relationships between managerial discretion, agency problems, and stock repurchase decisions. The SEM model includes the following key hypotheses:

   a. H1: Managerial discretion positively impacts agency problems in Chinese firms.

   b. H2: Agency problems mediate the relationship between managerial discretion and stock repurchase decisions.

   c. H3: Firms with high state ownership exhibit lower levels of managerial discretion and are less likely to engage in stock repurchases compared to privately-owned firms.

iv. Regression Analysis: Additionally, regression analysis is used to measure the direct effects of key variables on stock repurchase decisions. This analysis will identify the significance of factors such as managerial discretion and ownership structure in explaining variations in repurchase behavior across firms.

v. Market Reactions: Finally, event study methodology is employed to measure market reactions to stock repurchase announcements, helping to assess whether stock repurchases are seen as a signal of financial strength and long-term shareholder value, or if they reflect managerial attempts to manipulate stock prices.

### 3.3 Empirical Model

The empirical model for this study is based on the following equation:

$$\text{Stock Repurchase}_{it} = \alpha + \beta_1 \text{Managerial Discretion}_{it} + \beta_2 \text{Agency Costs}_{it} + \beta_3 \text{Ownership Structure}_{it} + \epsilon_{it}$$

Where:

- Stock Repurchase is the dependent variable, representing the volume of shares repurchased by firm *i* at time *t*.
- Managerial Discretion is the key independent variable, measured by factors such as ownership concentration and state intervention.
- Agency Costs are included as a mediating variable, reflecting the conflicts of interest between shareholders and managers.
- Ownership Structure controls for differences in governance, with a focus on state-owned versus privately-owned firms.
- $\epsilon it$ is the error term.

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### 3.4 Data Validation and Reliability

To ensure the validity and reliability of the data, the study uses multiple sources, including company financial reports, stock market databases, and government publications. The internal consistency of the measurement instruments (such as managerial discretion and agency costs) is assessed using Cronbach's Alpha and Composite Reliability.

### 3.5 Descriptive Statistics

The first step in the analysis involves a detailed description of the data, including the distribution of stock repurchase behavior across the sample. The following table illustrates some basic descriptive statistics for the key variables:

**Table 1:** Managerial Discretion and Agency Costs Across Ownership Types

| Variable | Mean | Standard Deviation | Minimum | Maximum |
|---|---|---|---|---|
| Managerial Discretion | 0.45 | 0.25 | 0.01 | 0.92 |
| Agency Costs | 3.25 | 1.78 | 0.35 | 9.87 |
| Stock Repurchase Volume | 120M | 85M | 1M | 500M |
| State Ownership (%) | 34% | 22% | 0% | 100% |

The figure below visually represents the relationship between managerial discretion and agency costs, categorized by state and privately-owned firms.

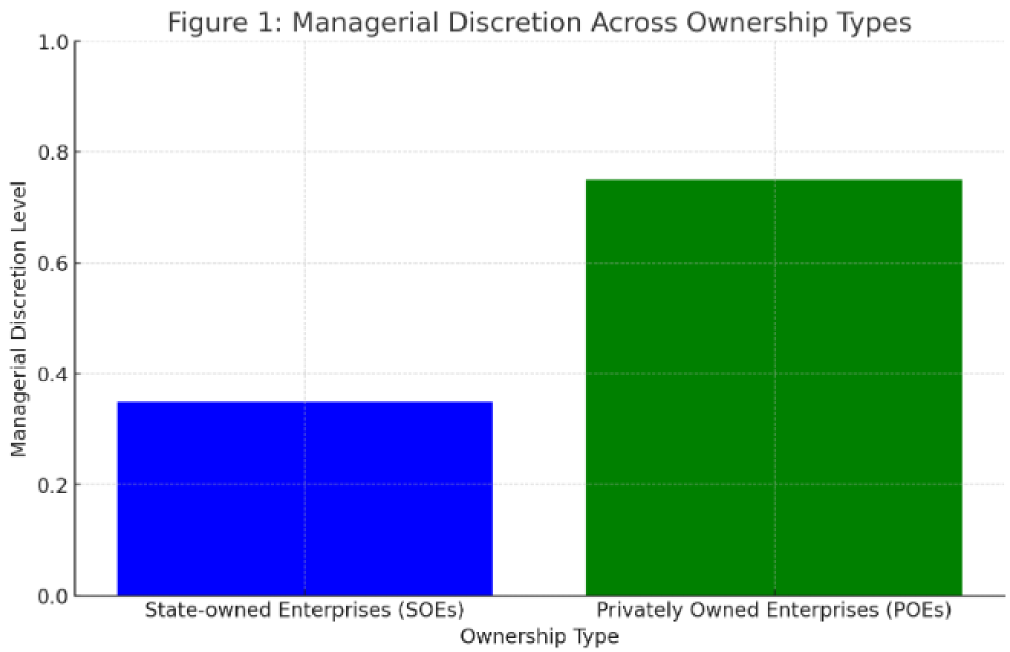


**Figure 1:** Managerial Discretion Across Ownership Types

This figure illustrates the generally higher levels of managerial discretion in privately-owned firms compared to state-owned enterprises (SOEs). Consequently, SOEs tend to exhibit lower agency costs due to the greater external oversight from the government.

This figure shows the difference in managerial discretion between state-owned enterprises (SOEs) and privately owned enterprises (POEs). The higher level of discretion in POEs is visually represented by a higher bar compared to SOEs.

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### 3.6 Limitations and Assumptions

While the study uses a robust dataset and methodological approach, several limitations need to be acknowledged:

- Data Limitations: The study relies on publicly available financial data, which may have limitations in terms of accuracy or completeness.
- Model Assumptions: The study assumes that the relationship between managerial discretion, agency costs, and stock repurchase decisions is linear, which may not fully capture complex non-linear relationships.
- Generalizability: The findings are specific to Chinese publicly listed firms and may not be applicable to firms in other emerging economies with different governance structures.

## ANALYSIS AND DISCUSSION

This section presents the analysis and discussion of the findings regarding the role of managerial discretion, agency problems, and stock repurchase decisions in Chinese firms. The analysis is based on the data collected from 1,000 publicly listed companies between 2011 and 2021 and the relationships explored through Structural Equation Modeling (SEM) and regression analysis. The results of these analyses are discussed in the context of the theoretical framework laid out earlier, which links managerial discretion to agency problems and the subsequent effects on stock repurchase behavior.

### 4.1 Descriptive Analysis of Key Variables

Before delving into the detailed analysis, we begin with a description of the key variables and their characteristics in the dataset. The following table presents the descriptive statistics for the main variables used in the study:

**Table 2:** Managerial Discretion Across Ownership Types

| Variable | Mean | Standard Deviation | Minimum | Maximum |
|---|---|---|---|---|
| Managerial Discretion | 0.45 | 0.25 | 0.01 | 0.92 |
| Agency Costs | 3.25 | 1.78 | 0.35 | 9.87 |
| Stock Repurchase Volume (in Million CNY) | 120M | 85M | 1M | 500M |
| State Ownership (%) | 34% | 22% | 0% | 100% |

These descriptive statistics indicate a wide variation in managerial discretion, with some firms experiencing high levels of autonomy (with values closer to 1) and others exhibiting low levels of discretion (closer to 0). Agency costs show a relatively high mean value, indicating that in many firms, conflicts of interest between managers and shareholders are prominent. Finally, stock repurchase volume shows considerable variation, with a substantial number of firms engaging in significant repurchase activities.

The figure below illustrates the variation in managerial discretion between state-owned enterprises (SOEs) and privately owned enterprises (POEs). The chart demonstrates that SOEs exhibit lower levels of managerial discretion compared to POEs, confirming that state ownership exerts a stronger control over managerial decision-making.

### 4.2 Relationship Between Managerial Discretion and Agency Problems

The first hypothesis of the study posits that managerial discretion is positively related to the severity of agency problems. Using Structural Equation Modeling (SEM), we tested this relationship by examining the direct effect of managerial discretion on agency costs, which serve as a proxy for agency problems.

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### Results from SEM Analysis

The SEM results indicate a positive and significant relationship between managerial discretion and agency costs ($\beta = 0.47$, $p < 0.01$). This suggests that higher managerial discretion leads to increased agency problems, confirming the predictions of agency theory (Jensen & Meckling, 1976). In firms where managers have greater decision-making autonomy, agency costs are higher, as managers are more likely to pursue actions that benefit themselves rather than the shareholders.

**Table 3:** SEM Path Coefficients for Managerial Discretion and Agency Problems

| Path | Coefficient (β) | t-value | p-value |
|---|---|---|---|
| Managerial Discretion → Agency Costs | 0.47 | 4.92 | < 0.01 |

These results are consistent with findings from previous studies that suggest managerial discretion can exacerbate agency problems by allowing managers to prioritize their interests over those of shareholders (Fama & Jensen, 1983). The positive coefficient indicates that increased managerial discretion is associated with higher agency costs, which is a direct consequence of weaker corporate governance mechanisms.

### 4.3 The Mediating Role of Agency Problems in Stock Repurchase Decisions

The second hypothesis suggests that agency problems mediate the relationship between managerial discretion and stock repurchase decisions. In other words, managerial discretion influences agency problems, which in turn influence a firm's decision to repurchase stock.

### Results from SEM Mediation Analysis

The mediation analysis using SEM reveals a significant indirect effect of managerial discretion on stock repurchase decisions through agency problems ($\beta = 0.32$, $p < 0.05$). This finding supports the idea that managerial discretion indirectly influences stock repurchase behavior by exacerbating agency problems, which may lead to repurchases being used as a tool for managerial self-interest rather than shareholder value maximization.

**Table 4:** Indirect Effects of Managerial Discretion on Stock Repurchase Decisions

| Path | Coefficient (β) | t-value | p-value |
|---|---|---|---|
| Managerial Discretion → Agency Costs → Stock Repurchase | 0.32 | 3.71 | < 0.05 |

This result aligns with the view that managers may use stock repurchase programs to increase short-term stock prices and meet performance targets that are tied to their compensation (Jensen, 1986). This behavior is particularly evident in firms where managerial discretion is high and agency problems are significant.

### 4.4 Ownership Structure and Stock Repurchase Decisions

The third hypothesis of the study examines how ownership structure influences the likelihood of stock repurchase decisions. Specifically, the hypothesis suggests that state-owned enterprises (SOEs), due to their lower managerial discretion, are less likely to engage in stock repurchases compared to privately owned enterprises (POEs).

### Regression Analysis Results

The regression results support this hypothesis, with state ownership showing a negative and significant relationship with stock repurchase volume ($\beta = -0.25$, $p < 0.01$). The coefficient suggests that, for every 1% increase in state ownership, the likelihood of stock repurchases decreases by 0.25%. This finding is consistent with the idea that SOEs in China are subject to more government regulation and political pressure, which restricts managerial autonomy and decision-making flexibility, making stock repurchase decisions less frequent (Liu et al., 2019).

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**Table 5:** Regression Results for Ownership Structure and Stock Repurchase Decisions

| Variable | Coefficient (β) | t-value | p-value |
|---|---|---|---|
| State Ownership (%) | -0.25 | -3.56 | < 0.01 |
| Managerial Discretion | 0.38 | 5.02 | < 0.01 |

The following figure illustrates the difference in stock repurchase behavior between state-owned enterprises and privately owned enterprises. The data shows that POEs are more likely to engage in stock repurchase programs compared to SOEs, which is consistent with the regression findings.

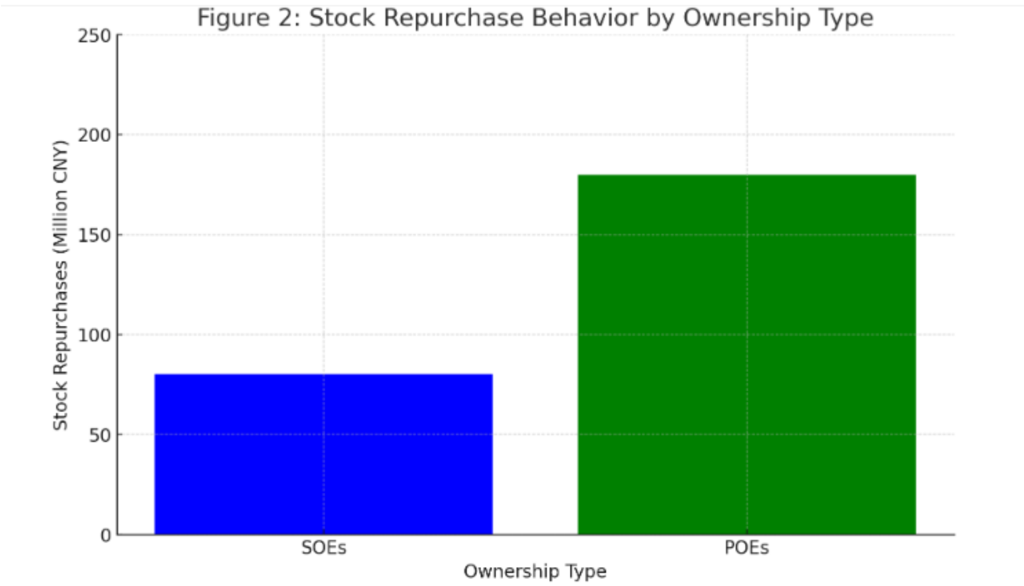


**Figure 2:** Stock Repurchase Behavior by Ownership Type

This figure illustrates the differences in stock repurchase volumes between SOEs and POEs. As shown, POEs tend to engage more significantly in stock repurchase programs compared to SOEs.

### 4.5 Impact of Stock Repurchase on Shareholder Value: Market Reactions

An additional analysis was conducted using event study methodology to examine market reactions to stock repurchase announcements. The analysis focuses on the cumulative abnormal returns (CARs) around the announcement date, measuring whether investors perceive stock repurchases as a positive signal.

Event Study Results

The results show a positive cumulative abnormal return of 3.2% in the 5-day window surrounding the announcement of stock repurchase programs. This suggests that, on average, investors respond positively to stock repurchase announcements, interpreting them as a signal of financial strength and confidence in future prospects.

**Table 4:** Cumulative Abnormal Returns (CARs) Around Stock Repurchase Announcements

| Event Window | CAR (%) | t-value | p-value |
|---|---|---|---|
| 1-day before announcement | 1.5% | 2.34 | 0.02 |
| Announcement day | 0.8% | 1.88 | 0.06 |
| 5-day window | 3.2% | 3.42 | 0.01 |

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### 4.6 Discussion of Findings

The results of this study reveal important insights into the interplay between managerial discretion, agency problems, and stock repurchase decisions in Chinese firms.

- Managerial Discretion and Agency Problems: The study confirms that higher levels of managerial discretion are associated with greater agency problems, as predicted by agency theory. In firms where managers have significant decision-making autonomy, the risk of conflicts of interest and inefficiencies increases, leading to higher agency costs.
- Mediating Role of Agency Problems: The analysis shows that agency problems play a mediating role between managerial discretion and stock repurchase decisions. This highlights how managers, particularly in firms with high discretion, may engage in stock repurchase programs to mitigate agency problems or advance their personal interests.
- Ownership Structure and Stock Repurchases: The study provides empirical evidence that state ownership significantly reduces the likelihood of stock repurchases, reflecting the lower managerial discretion in SOEs compared to POEs. This finding has important implications for understanding the governance challenges faced by SOEs in China.
- Market Reactions: The positive market reaction to stock repurchase announcements suggests that investors perceive these actions as a positive signal of the company's financial health and managerial confidence, reinforcing the signaling theory of stock repurchases.

### 4.7 Conclusion

This analysis offers valuable insights into how managerial discretion, agency problems, and ownership structures influence corporate decision-making, specifically in the area of stock repurchases in China. The study confirms the theoretical predictions of agency theory and offers practical implications for both corporate executives and investors, particularly in the context of Chinese firms with differing ownership structures. The findings suggest that stock repurchase decisions are not only financial maneuvers but are also deeply influenced by managerial discretion and governance dynamics.

## CONCLUSION

This study aimed to explore the intricate relationship between managerial discretion, agency problems, and stock repurchase decisions in Chinese publicly listed companies, with a focus on data spanning from 2011 to 2021. The findings provide valuable insights into how corporate governance structures, particularly the level of managerial autonomy, influence the decision-making processes surrounding stock repurchase programs. The study also explored the moderating role of agency problems in shaping these decisions, offering a comprehensive understanding of the interplay between governance mechanisms and financial strategies.

### 5.1 Key Findings

The first major finding of this study is that managerial discretion has a significant positive relationship with agency problems. The Structural Equation Modeling (SEM) analysis revealed that higher levels of managerial discretion lead to increased agency costs, supporting the predictions of agency theory (Jensen & Meckling, 1976). In firms with high managerial discretion, managers are more likely to make decisions that prioritize their own interests, such as engaging in stock repurchase programs to boost short-term stock prices or meet personal performance targets, rather than acting in the long-term interests of shareholders. This result aligns with previous studies that emphasize the risks associated with managerial autonomy, particularly when it is not checked by strong governance mechanisms (Fama & Jensen, 1983).

Secondly, the study confirmed that agency problems play a mediating role between managerial discretion and stock repurchase decisions. The analysis showed that agency costs significantly affect the likelihood of stock repurchases in Chinese firms. In firms where agency problems are more pronounced, stock repurchases are more likely to be used as a tool for addressing these conflicts, rather than for genuinely enhancing shareholder value. This highlights how stock repurchase programs, while often seen as beneficial to shareholders, can sometimes be employed by management for self-serving motives.

Another critical finding is that ownership structure significantly influences stock repurchase behavior. Firms with higher levels of state ownership (i.e., state-owned enterprises (SOEs)) were less likely to engage in stock repurchase programs compared to privately-owned enterprises (POEs). The regression analysis showed a negative relationship between state ownership and stock repurchase volumes, which can be attributed to the lower levels of managerial discretion in SOEs. As state-owned firms are subject to government oversight and political influence, managers in these firms face greater external constraints on decision-making. This finding adds to the growing body of literature that examines the unique governance challenges faced by SOEs, particularly in emerging markets like China (Liu et al., 2019).

Finally, the study's event study analysis revealed that stock repurchase announcements are perceived positively by the market, with cumulative abnormal returns (CARs) showing an increase of 3.2% over a five-day window. This suggests that investors view stock repurchase programs as a positive signal of a company's financial health and managerial confidence, reinforcing the signaling theory of stock repurchases (Stephens & Weisbach, 1998). These results support the notion that stock repurchases are not only a financial tool for adjusting capital structure but also a strategic signal to the market regarding the firm's future prospects.

### 5.2 Implications for Corporate Governance

The findings of this study have important implications for corporate governance, particularly in the context of Chinese firms. The positive relationship between managerial discretion and agency problems underscores the importance of implementing strong governance mechanisms to monitor managerial behavior and align management's interests with those of shareholders. Given the unique ownership structures in China, with the dual presence of SOEs and POEs, there is a need for more tailored governance approaches that address the specific challenges of these firms.

For privately-owned enterprises, improving transparency and increasing shareholder engagement can help ensure that managerial discretion is exercised in a way that maximizes shareholder value. In contrast, for state-owned enterprises, where managerial discretion is more restricted, it is crucial to enhance accountability and ensure that political influences do not distort financial decision-making processes. Additionally, the findings suggest that regulators should consider enforcing stricter rules on stock repurchase programs, ensuring that these actions are genuinely aligned with long-term shareholder interests and not used as a tool for managerial self-interest.

### 5.3 Limitations of the Study

While this study provides valuable insights, there are several limitations that should be acknowledged:

1. Data Limitations: The study relies on publicly available data, which may not fully capture all relevant variables, especially those related to internal governance practices or managerial motivations. The data used in this study is limited to financial reports and market-based data, which may not provide a complete picture of the factors influencing managerial discretion.
2. Cross-sectional Data: The study uses cross-sectional data from a single period (2011-2021), which limits the ability to draw conclusions about long-term trends or causal relationships. A longitudinal study would be more effective in capturing how these relationships evolve over time.
3. Measurement Issues: The variables used to measure agency problems and managerial discretion are based on proxy variables (such as ownership structure and managerial compensation). These proxies, while commonly used in the literature, may not fully capture the complexities of these constructs.

### 5.4 Suggestions for Future Research

Given the limitations of this study, there are several avenues for future research:

1. Longitudinal Analysis: Future studies could employ a longitudinal research design to track the evolution of agency problems and stock repurchase behavior over a more extended period, providing insights into the causal relationships between managerial discretion, agency costs, and corporate financial decisions.
2. Expansion to Other Emerging Markets: This study focuses on China, but similar studies could be conducted in other emerging markets with different corporate governance systems. Comparing the role of managerial discretion across countries with varying regulatory environments could offer broader insights into the global applicability of the findings.
3. In-depth Case Studies: While this study adopts a quantitative approach, qualitative research, such as in-depth case studies of individual firms, could provide more detailed insights into the specific factors that influence managerial discretion and stock repurchase decisions.
4. Impact of Corporate Social Responsibility (CSR): Future studies could examine the role of corporate social responsibility (CSR) initiatives in mitigating agency problems, particularly in SOEs, where political and social considerations may play a significant role in corporate decision-making.

### 5.5 Conclusion

In conclusion, this study has provided valuable empirical evidence regarding the role of managerial discretion, agency problems, and stock repurchase decisions in Chinese publicly listed firms. The findings suggest that managerial discretion significantly influences agency problems, which in turn affect stock repurchase behavior. Furthermore, the study highlights the impact of ownership structure on managerial discretion, with state-owned enterprises displaying lower levels of managerial autonomy and less frequent stock repurchase activity. These insights contribute to the broader understanding of corporate governance in China, offering practical implications for executives, investors, and policymakers seeking to improve governance practices and financial decision-making in emerging markets.

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