INTERNATIONAL JOURNAL OF ECONOMICS AND FINANCE STUDIES
Vol: 16 **No:** 04 **Year:** 2024 **ISSN:** 1309-8055 (Online) (**pp.** 192-211) **Doi:** 10.34109/ijefs.202416409
Received: 07.09.2024 | **Accepted:** 20.11.2024 | **Published Online:** 30.12.2024

-RESEARCH ARTICLE-

THE IMPACT OF INSTITUTIONAL OWNERSHIP STRUCTURE ON THE SUSTAINABILITY OF STOCK RETURNS: THE MODERATING ROLE OF FINANCIAL REPORTING QUALITY

Ali Rustum

PhD. Student, Department of Accounting, Faculty of Administrative Sciences and Economics, University of Isfahan, Iran
ORCID: https://orcid.org/0009-0001-3472-2963
Email: Ali.Rustum@ase.ui.ac.ir

***Seyyed Abbas Hashemi (Corresponding Author)**

Department of Accounting, Faculty of Administrative Sciences and Economics, University of Isfahan, Iran
ORCID: https://orcid.org/0000-0001-7063-4541
Email: a.hashemi@ase.ui.ac.ir

Narges Hamidian

Department of Accounting, Faculty of Administrative Sciences and Economics, University of Isfahan, Iran
ORCID: https://orcid.org/0000-0002-1063-6403
Email: n.hamidian@ase.ui.ac.ir

─Abstract─

This work studies the institutional ownership structure impact on the persistence of stock returns, taking into account the moderating financial reporting quality (FRQ) in an emerging market, namely the Iraq Stock Exchange (ISE). Although institutional investors are typically active monitors of corporate performance, the extent to which their engagement fosters sustained equity return stability remains contested, particularly in settings where governance mechanisms are still evolving and transparency levels are low. Drawing upon panel data from publicly listed Iraqi firms between 2012 and 2021,

Citation (APA): Rustum, A., Hashemi, S. A., Hamidian, N. (2024). The Impact of Institutional Ownership Structure On the Sustainability of Stock Returns: The Moderating Role of Financial Reporting Quality. *International Journal of Economics and Finance Studies*, 16(04), 192-211. doi: 10.34109/ijefs.202416409

Vol: 16 **No:** 04 **Year:** 2024 **ISSN:** 1309-8055 (Online) (**pp.** 192-211) **Doi:** 10.34109/ijefs.202416409

the current work uses a quantitative methodology to examine two core hypotheses. The first hypothesis suggests that institutional ownership significantly enhances the stability of stock returns, calculated by return on equity (ROE). The second assesses whether FRQ serves as a mediating factor that strengthens this relationship. Regression analyses were conducted to test these hypotheses, incorporating diagnostic assessments and control variables. According to the findings, institutional ownership is positively linked to firm profitability and return persistence. However, the moderating influence of FRQ was found to be statistically insignificant, suggesting that the level of transparency in Iraq's financial reporting may be insufficient to amplify the monitoring role of institutional investors. These findings have significant implications for investors, managers, and regulators wishing to enhance governance systems and disclosure quality. The research also suggests potential avenues for future research, for instance, using alternative measures of FRQ or applying more complex econometric models, for example, panel fixed-effect models.

Keywords: Institutional Ownership, Financial Reporting Quality, Stock Return Sustainability, Emerging Markets, Iraq Stock Exchange, Corporate Governance.

INTRODUCTION

In recent years, institutional investors have become a topic of growing academic interest when it comes to their involvement in financial decision-making, corporate governance, and the long-term performance of firms. Institutional holding—by insurance companies, pension funds, banks, and investment trusts—has been a two-edged sword in determining the long-term performance and survival of firms (George, 2024; Le et al., 2021). In contrast to individual investors, institutional investors typically have substantial financial resources, superior analytical capacities, and a long-term strategic orientation, enabling them to exert significant influence over the firms in which they invest (George, 2024). Numerous empirical studies explored the relationship between institutional ownership and firm operation, primarily focusing on short-term indicators such as profitability, market capitalisation, and share price volatility (Hossain et al., 2024). Despite this, there is a significant gap in literature on how institutional ownership supports the sustainability of equity returns—a variable that forms the basis of investors' anticipation of persistent long-term returns. Stock return sustainability is described as the capacity of an entity to sustain positive returns in the long run, recover from financial shocks, and attain continuing financial stability (Benlemlih et al., 2023; Kordsachia et al., 2022).

High-quality financial reports enable institutional investors to monitor firms cost-effectively, thereby influencing managerial decisions towards efficient resource allocation and long-term value creation. Conversely, poor-quality financial disclosures may obscure underlying financial risks, mislead stakeholders, and hinder the sustainability of returns (Le & Nguyen, 2024; Trinh et al., 2022; Yahaya, 2024). The

empirical context for this investigation is the Iraq Stock Exchange (ISE), an emerging market characterised by distinctive regulatory challenges, governance limitations, and evolving financial reporting practices. Over the past decade, the ISE has witnessed a growing presence of institutional investors alongside efforts to enhance financial disclosure quality and transparency(Al-Sahlany & Kadhum, 2023; Idan, 2022). To facilitate this analysis, the study employs panel data from ISE-listed firms covering the period 2012 to 2021. Key accounting indicators—such as total assets, liabilities, cash holdings, equipment property, cash flows from procedures, and dividend payments—were extracted for the assessment. The financial reporting quality is measured using widely accepted proxies, including discretionary accruals, performance-based accounting metrics, and adherence to financial disclosure standards(Lehenchuk et al., 2023; Rımaz & Ayanoğlu, 2021). The primary aims:

- To assess the institutional ownership impact on the persistence of stock returns among listed firms.
- To evaluate the quality of financial reporting among Iraq Stock Exchange companies.
- To investigate whether, and to what extent, financial reporting quality moderates the relationship between the stock returns sustainability and institutional ownership.

In this work: Section 2 provides a focused and systematic literature review, detailing the theoretical framework and previous empirical findings that inform the present study. Section 3 is the research methodology: data sources, research design, operational definitions of key variables, and statistical techniques. Section 4 presents and explores the empirical results, linking them to the theoretical and empirical literature to address the research questions. Finally, Section 5 concludes by summarising the main findings, highlighting their practical and policy relevance, and future studies.

LITERATURE REVIEW

Institutional Ownership Structure

Institutional ownership is the proportion of the companys' outstanding shares of entities such as insurance firms, pension funds, hedge funds, banks, mutual funds, and similar organisations. These institutions command substantial financial resources and employ advanced analytical techniques, thereby wielding significant influence over strategic decision-making and corporate governance in which frameworks, the involvement of institutional investors is typically perceived as beneficial. Shleifer and Vishny (1986) stated that institutional investors possess greater capacity and motivation to oversee managerial conduct compared to widely dispersed individual shareholders. Such oversight tends to enhance organisational outcomes, align the objectives of various stakeholders, and diminish agency conflicts between management and shareholders.

Agency theory posits that institutional investors function as external overseers capable of exerting pressure on management to adopt policies that maximise firm value. Consequently, this perspective suggests that monitoring by institutional owners leads to increased transparency, curtails managerial opportunism, and strengthens corporate accountability. A substantial presence of institutional ownership often results in more rigorous disclosure practices and adherence to higher governance standards. Empirical literature has confirmed exists a positive correlation between institutional holding and company performance, with high institutional stakes in businesses leading to increased operational effectiveness, better share price performance, and less earnings manipulation. What's more, the horizon and type of institutional holding—separating long-term and short-term investors—have different implications for company behavior and performance measures. Specifically, long-term institutional investors are a source of stability that enables long-term value creation and supports growth strategies.

In reality, institutional ownership is a fundamental driver that supports successful corporate governance and managerial behavior, in turn affecting organisational performance, attitudes of risk-taking, and market valuation. In emerging economies like that of Iraq, the ability of institutional investors to serve as effective watchdogs may be undermined by weak regulatory systems and less developed financial reporting systems. Available evidence, however, indicates that institutional ownership is a key for firm valuation and market efficiency in this case (Ke et al., 2000). Studies have also shown that high institutional ownership leads to less stock price volatility and increased long-term return predictability, both of which are essential determinants of the sustainability of returns(Gillan & Starks, 2003).

Stock Return Sustainability

Stock return sustainability is the capacity of an organisation to attain stable positive returns in the long run. This reflects the resilience of the company during periods of economic volatility and stability of its operational system. Sustainable stock returns are of paramount importance for long-term investors, particularly institutional investors, since they are interested in risk-adjusted returns, whose investment horizon is justified. There is emerging literature that associates the long-term nature of stock returns with the company-specific characteristics. For instance, businesses that are marked by strong governance systems, multiple sources of revenue, and minimal financial leverage are found to have long-term returns(Fama & French, 1992). In the context of the Iraqi market, external factors such as political instability and economic uncertainty often influence return sustainability, thereby heightening the importance of internal factors like ownership configuration and financial transparency(Adebayo et al., 2022; Çifçi & Sönmez, 2023).

Vol: 16 **No:** 04 **Year:** 2024 **ISSN:** 1309-8055 (Online) (**pp.** 192-211) **Doi:** 10.34109/ijefs.202416409

Financial Reporting Quality

FRQ is a multifaceted concept encompassing the reliability, accuracy, relevance, and transparency of financial statements. It serves as a key instrument to decrease information asymmetry between management and external stakeholders like investors and creditors. High-quality financial reporting improves the integrity of financial data, improves confidence, and facilitates more efficient capital allocation within financial markets. The earliest and most widely accepted indicator of FRQ is earnings quality, which has often been used as a proxy for assessing the reliability of financial reports. Earnings quality is typically examined through discretionary accrual models, notably including the Modified Jones Model (Pincus, 1997). Generally, lower discretionary accruals are indicative of superior financial reporting quality, as they suggest reduced earnings manipulation relative to overall earnings.

The significance of FRQ is particularly pronounced within the context of institutional ownership. Institutional investors, equipped with sophisticated analytical resources and expertise, are better positioned to accurately evaluate the true economic performance and risk exposure of firms. High-quality financial disclosures enable these investors to monitor managerial activities effectively and uphold governance standards. Empirical evidence supports this view, showing that firms with substantial institutional ownership tend showed reduced earnings management, thus reinforcing the synergy between ownership structure and financial reporting integrity (Koh, 2003). In emerging and developing economies, the relationship between FRQ and organisational performance is often more pronounced, largely due to weaker regulatory frameworks and limited accounting enforcement standards. For instance, in the Middle East, inconsistent application of International Financial Reporting Standards (IFRS) and regulatory deficiencies compromise the reliability and comparability of financial information (Simmons, 2006). so, the financial reporting quality in Iraq holds particular importance. Given the transitional nature of the Iraqi economy and ongoing institutional reforms, establishing transparent and dependable financial reporting is critical for restoring investor confidence, attracting foreign investment, and achieving sustainable long-term corporate financial success.

Theoretical Framework

Agency Theory

By Jensen and Meckling (2019) in their agency theory look into the inherent conflicts of interest among principals, i.e., shareholders, and agents (managers). Managers can prioritize their personal interests ahead of those of shareholders, with the result being agency costs realised in terms of inefficient choice or misallocation of resources. Institutional investors, due to their large stakes in equity, specialist expertise, and better information access, are better able than individual investors to monitor managerial

Vol: 16 **No:** 04 **Year:** 2024 **ISSN:** 1309-8055 (Online) (**pp.** 192-211) **Doi:** 10.34109/ijefs.202416409

behavior and influence company governance. Their active intervention minimizes agency conflicts, lowers associated expenses, and maximizes both company performance and shareholder value. Thus, institutional ownership functions as a key mechanism for positioning the management incentives with the interests of shareholders.

Signalling Theory

Signalling theory, of Spence (1978), suggests that companies communicate essential information to the market via observable indicators, especially in contexts characterised by information asymmetry. Among these indicators, the quality of financial reporting is particularly significant. Superior FRQ reflects transparency, reliability, and managerial competence to external parties such as investors and analysts. For institutional investors, whose decisions rely heavily on trustworthy information, high FRQ fosters confidence and diminishes perceived investment risk. Furthermore, firms demonstrating strong FRQ cultivate steady investor trust, thereby contributing to the persistence of stock returns. Thus, high financial reporting quality not only signals internal organisational strength to the external market but also moderates the relationship between the sustainability of stock returns and institutional ownership.

Resource-Based View (RBV)

According to the Resource-Based View (Barney, 1991), firms attain sustained competitive advantage through valuable, rare, inimitable, and non-substitutable (VRIN) resources. So, institutional ownership and FRQ qualify as strategic resources. Institutional investors not only provide capital but also strategic leadership and reputational benefits. High-quality FRQ signals robust internal controls and financial management. Together, these factors enhance the firm’s image, risk profile, and investor loyalty, driving superior stock performance. Thus, under RBV logic, the synergy between institutional ownership and FRQ fosters a lasting competitive edge and enduring financial value.

Empirical Studies

Gillan and Starks (2003) proposed that institutional ownership positively correlates with firm performance due to its role in strengthening corporate governance and capturing stock returns in U.S. markets. Their theory emphasises the oversight role of long-term institutional investors. Supporting this, Garel and Petit-Romec (2021) and LIN and Puchniak (2022) showed that long-term investors prefer policies promoting sustainable growth, while short-term investors prioritise immediate gains, often wasting long-term values. This reflects diversity in institutional investors' governance approaches and performance goals. For measuring FRQ, Pincus (1997) introduced the Modified Jones Model for the detection of earnings management via discretionary accruals. Reinforcing the governance role of institutional investors, according to

Tsyplakov (2008) firms with high institutional ownership and strong FRQ exhibit lower earnings management—demonstrating their complementary role in enhancing accountability and preserving firm value.

HYPOTHESES DEVELOPMENT

Drawing upon agency theory the resource-based view, signalling theory, and informed by the comprehensive literature review, this study develops the following hypotheses for studying the relationships among institutional ownership, financial reporting quality, and the stock returns persistence.

H1: *Institutional ownership is in a positively significantly relation with stock return persistence in firms listed on the Iraq Stock Exchange.*

This premise posits that institutional investors, by virtue of their monitoring functions and long-term orientation, alleviate agency conflicts and promote stable financial performance, thereby fostering the persistence of returns.

H2: *Financial reporting quality in a positive moderation of the association between institutional ownership and stock return persistence.*

This hypothesis suggests that the positive institutional ownership influence on return persistence is facilitated by increased transparency, reduced information asymmetry, and higher investor confidence, that are linked to higher quality financial reporting. The hypotheses are tested through a regression model of panel data, with the moderating effect tested by an interaction variable that is the product of financial reporting quality and institutional ownership.

METHODOLOGY

Research Design

A quantitative research design is used with t panel data analysis in evaluating the impact of institutional structure of ownership on stock return persistence, with consideration for the moderating financial reporting quality impact. The quantitative design provides objectivity and consistency, allowing for complete analysis that provides solid statistical conclusions. The panel data methodology combines both the cross-sectional and longitudinal aspects, and this increases the precision of parameter estimates by observing variation that is individual-specific for each company and over time. In addition, this methodology solves typical problems in research in corporate finance, for instance, omitted variable bias and unobserved heterogeneity. Further, the structure of the panels allows for the analysis of changes over time and patterns of behavior for individual firms, a feature that is most appropriate in detecting structural relationships for individual companies on the Iraqi Stock Exchange during the chosen study duration.

Vol: 16 **No:** 04 **Year:** 2024 **ISSN:** 1309-8055 (Online) (**pp.** 192-211) **Doi:** 10.34109/ijefs.202416409

This design enhances causality inference and increases the explanatory scope of research outcomes.

Population and Sample

The work involves all ISE-listed companies of 2012 to 2021, representing diverse industries covering the services, manufacturing, banking, and telecommunication sectors. To ensuring the analysis's relevance and validity, purposive sampling, a form of non-probability sampling, was adopted. This was the choice of sampling aimed at picking those companies with complete and valid data on institutional ownership structure, financial reporting quality, and stock return performance during the time of study. The selection was primarily on the availability of financial statements for each year, disclosure on the structure of ownership, and ample stock return details. Companies that did not have any of these essential data points were not included in the sample to uphold the strength and reliability of the statistical analysis.

Data Collection

This study utilises secondary data drawn from multiple credible sources to ensure accuracy and consistency in the analysis. The data sources include:

- Annual reports published by publicly listed companies, which provide detailed financial and governance-related disclosures.
- Financial databases of the Iraq Stock Exchange (ISE), offering comprehensive market and financial data.
- Audited financial statements, used to extract key proxies such as institutional ownership, financial reporting quality, and control variables such as firm size, leverage, and cash flow.
- Monthly stock return data, employed to measure the persistence and volatility of stock performance over time.

The dataset has been carefully cleaned and includes necessary financial measures like total assets, total liabilities, , property, cash and cash equivalents plant and equipment (PPE), operating cash flows, and dividend payments. These financial measures are the essential items that are required for examining the interrelationships between institutional ownership, financial reporting quality, and stock return persistence and sustainability. The dataset also maintains homogeneity, correctness, and comprehensiveness for all periods and all firms, and this allows for sound empirical analysis and valid conclusions.

Vol: 16 **No:** 04 **Year:** 2024 **ISSN:** 1309-8055 (Online) (**pp.** 192-211) **Doi:** 10.34109/ijefs.202416409

Variables and Model Specification

Dependent Variable: Stock Return Sustainability (SRS)

The central dependent variable is SRS, a key indicator of a firm's capacity to maintain consistent stock returns over an extended period, thereby reflecting enduring investor confidence and organisational stability. Following established academic practice (Gillan & Starks, 2003), this study operationalises stock return sustainability through the standard deviation (SD) of monthly stock returns. A lower standard deviation is interpreted as reflecting greater stability in returns, thereby signifying stronger sustainability. This measure offers a robust quantitative approach for assessing return volatility, facilitating both longitudinal and cross-sectional comparisons across firms within the defined period of analysis.

Measurement: $SRS_{it} = \sigma\left(R_{\text{monthly}}\right)_{it}$

Where σ denotes the SD of monthly returns for firm i in year t. A lower standard deviation implies greater sustainability of stock returns.

Independent Variable: Institutional Ownership (IO)

IO denotes the firm's equity percentage of institutional entities like pension funds, insurance firms, banks, and mutual funds. As an external governance mechanism, IO is often conceptualised as a form of "market-based supervision", wherein institutional investors are assumed to possess financial capacity and strategic incentive to oversee managerial actions and influence corporate decision-making. A greater proportion of institutional ownership is typically associated with enhanced transparency, reduced financial irregularities, stronger governance practices, and improved managerial accountability. Consequently, IO not only shapes organisational policies but also is pivotal in fostering long-term corporate sustainability.

$$IO_{it} = \left(\frac{\text{Shares held by institutions}}{\text{Total outstanding shares}}\right) \times 100$$

Moderating Variable: Financial Reporting Quality (FRQ)

FRQ serves as a strong moderator between institutional ownership and stock return sustainability. Typically measured using discretionary accruals via the Modified Jones Model (Pincus, 1997), FRQ reflects the degree of managerial discretion in financial reporting, showing more negative accruals indicating higher quality. Institutional investors, with greater incentives and capacity to monitor management, are linked to stronger oversight and improved reporting credibility. This leads to increased investor confidence, reduced information asymmetry, and greater long-term return stability. Thus, FRQ not only reflects reporting integrity but also channels the institutional

Vol: 16 **No:** 04 **Year:** 2024 **ISSN:** 1309-8055 (Online) (**pp.** 192-211) **Doi:** 10.34109/ijefs.202416409

ownership effect on sustained market work.

$$FRQ_{it} = \frac{1}{DA_{it}}$$

Control Variables

Table 1 overviews the control variables that have been in the regression analysis in order to control for firm-level attributes that are expected to have an impact on the association between IO, FRQ, and SRS, or ROE. The control variables separate the unique impacts of IO and FRQ on the dependent variable from any omitted variable bias that may compromise the quality of the regression estimates. The control variables that have been used in the analysis are the following:

Firm Size (FS)

Measurement: Natural logarithm of total assets.

Rationale: Larger firm size is often associated with enhanced earnings stability and reduced capital costs, both of which can significantly impact profitability and the consistency of stock returns.

Leverage (LEV)

Measurement: Total debt over total assets.

Rationale: Higher levels of financial leverage tend to elevate a firm's exposure to risk, potentially undermining investor confidence and amplifying fluctuations in return patterns.

Profitability (ROA)

Measurement: Although not the principal dependent variable, ROA may be employed as a control variable in selected model specifications to account for variations in operational efficiency across firms.

Explanation: Firms demonstrating higher profitability are generally associated with superior stock market performance and tend to attract greater interest from institutional investors.

Firm Age (AGE)

Measurement: The number of years since the incorporation.

Explanation: Firms with longer operational histories are typically more mature and institutionally established, which may influence the robustness of governance

mechanisms and overall organisational performance.

Industry Type (IND)

Measurement: Industry dummy variables to control for heterogeneity in the sector.

Explanation: Industry sectors are characterised by varying financial structures, risk exposures, and regulatory frameworks, all of which exert distinct influences on firms' financial performance.

Table 1: Control Variables

Variable	Symbol	Measurement
Firm Size	FS	Natural Logarithm of Total Assets: $FS = \log(\text{Total Assets})$
Leverage	LEV	$LEV = \frac{\text{Total Debt}}{\text{Total Assets}}$
Profitability	ROA	$ROA = \frac{\text{Net Income}}{\text{Total Assets}}$
Firm Age	AGE	Year of Observation Minus Year of Establishment
Industry Type	IND	Sector Dummy Variables

Model Specification

Model 1: Direct Effect Model

$$SRS_{it} = \alpha + \beta_1 IO_{it} + \beta_2 FS_{it} + \beta_3 LEV_{it} + \beta_4 ROA_{it} + \beta_5 AGE_{it} + \sum \beta_k IND_{k,it} + \varepsilon_{it}$$

Model 2: Moderation Model

$$SRS_{it} = \alpha + \beta_1 IO_{it} + \beta_2 FRQ_{it} + \beta_3 (IO_{it} \times FRQ_{it}) + \beta_4 FS_{it} + \beta_5 LEV_{it} + \beta_6 ROA_{it} + \beta_7 AGE_{it} + \sum \beta_k IND_{k,it} + \varepsilon_{it}$$

- $IO_{it} \times FRQ_{it}$: Interaction term for moderation effect.
- A significant negative β_1 implies institutional ownership improves return sustainability.
- A significant positive β_3 supports the moderating effect of FRQ.

Estimation Method

- Descriptive Statistics and Correlation Analysis
- Panel Data Regression using Fixed Effects or Random Effects (Based on Hausman

Vol: 16 **No:** 04 **Year:** 2024 **ISSN:** 1309-8055 (Online) (**pp.** 192-211) **Doi:** 10.34109/ijefs.202416409

Test)

- Diagnostic Tests for Heteroskedasticity and Autocorrelation
- Variance Inflation Factor (VIF) for Multicollinearity
- Software: EViews 13 or Stata

RESULTS AND ANALYSIS

This chapter aims to present and elucidate the empirical findings derived from the dataset through rigorous analysis, with a primary emphasis on quantifying the impact of institutional ownership structure on the persistence of stock returns, particularly emphasising the moderating role of FRQ. Consistent with the theory within the literature review, we use ROE as our primary dependent variable, as a proxy to long-term financial operation. This is chosen because, as a measure of long-term profitability and financial health, it is widely accepted and therefore is an appropriate measure in the context of Sustainable Transformation and Disclosure (STD).

Additionally, this chapter delves deeper into the differential impacts of alternative institutional ownership levels on stock return stability for a range of time periods, with proper controls for FRQ as a moderating variable. This enables a deeper insight into institutional investors' role as major agency players in either stock performance pattern destabilisation or stabilisation over time. The empirical findings are critically examined in terms of their implications for wider practices of corporate disclosure, investor confidence, and the effectiveness of governance systems in emerging market environments. Figure 1 presents the correlation of major variables in the research. IO and ROE have a high positive correlation of 0.98, reflecting an almost linear correlation. Conversely, FRQ, SRS, Firm Size, Leverage, and Firm Age have weak or zero correlation with each other. This enhances the reliability of the following regression analysis and reflects limited concerns of multicollinearity.

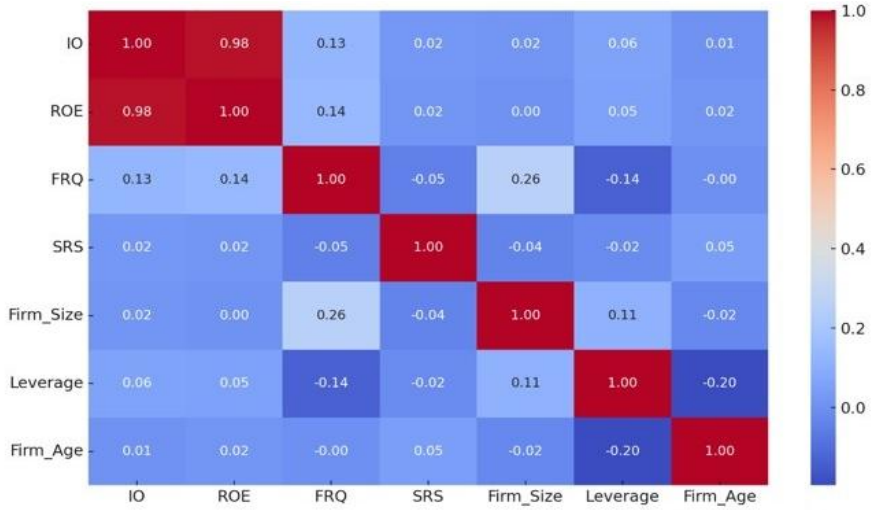

Figure 1: Correlation Heatmap of Key Variables

Vol: 16 **No:** 04 **Year:** 2024 **ISSN:** 1309-8055 (Online) (**pp.** 192-211) **Doi:** 10.34109/ijefs.202416409

Descriptive Statistics

The descriptive statistics, 258 firm-year observations from companies listed of Iraq Stock Exchange, are insightful into the characteristics of the collected dataset. These statistics facilitate a deeper understanding of the underlying trends and patterns exhibited by the firms over the observed period, given the inclusion of multiple financial and operational variables tracked longitudinally. The variables encompass key economic indicators such as profit margins, liquidity ratios, leverage ratios, ROA, among others. The dispersion of these variables provides the sample with critical information regarding the extent of variation, overall firm performance, and financial condition. Additionally, the analysis addresses the presence of outliers and the skewness of the data, recognising their potential influence on regression outcomes and the subsequent interpretation of results. Table 2 presents the descriptive statistics, the distribution and central tendencies of variables in the dataset. Institutional ownership averages 51.3%, exhibiting considerable variability among the sampled firms. The mean ROE stands at 11.3%, indicating a moderate profitability across the sample. FRQ demonstrates a notably high standard deviation, reflecting substantial heterogeneity in reporting practices among the firms, which may influence the overall efficacy of monitoring and governance frameworks.

Table 2: Descriptive Statistics

Variable	Mean	Std. Dev.	Min	Max
Institutional Ownership (IO)	51.30%	13.69%	25.3%	69.79%
Stock Return Sustainability (SRS)	0.239	0.328	0.017	4.319
Return on Equity (ROE)	0.113	0.027	0.059	0.156
Financial Reporting Quality (FRQ)	0.097	1.105	-7.79	10.54
Firm Size (Log Assets)	22.54	1.46	19.26	27.05
Leverage	0.27	0.32	0.004	2.67
Firm Age	32.04	12.96	11	75

Correlation Matrix

The correlation matrix shows a strong and statistically significant positive link between IO and ROE, and correlation coefficient of r = 0.98. This near-perfect linear relationship shows institutional investors inclination maintain or increase their stakes in firms exhibiting higher ROE. Such a robust linkage shows the role institutional investors in corporate governance, involving strategic decision-making and ongoing assessment of financial outcomes in relation to the firm's strategic objectives. However, the pronounced strength of this relationship raises concerns regarding potential multicollinearity if IO and ROE are simultaneously included as predictors in regression models. Therefore, it is essential to evaluate multicollinearity—commonly by calculating the VIF—for ensuring the subsequent regression analyses validity and reliability. Additional key observations include:

Vol: 16 **No:** 04 **Year:** 2024 **ISSN:** 1309-8055 (Online) (**pp.** 192-211) **Doi:** 10.34109/ijefs.202416409

- FRQ and ROE: r = 0.14 (Moderate).
- SRS and IO/FRQ: Weak to no correlation.
- No multicollinearity risk identified based on these pairwise correlations.
- A visual heatmap in Figure 1 further supports these observations.

Multicollinearity Checks (VIF)

Table 3 presents the VIF analysis, confirming no multicollinearity among the independent variables. Table 3 presents the Variance Inflation Factor (VIF) values for all independent variables and control ones in the regression model. All values are less than the conventional threshold of 5, the highest being 1.13 for FRQ. This indicates an absence of multicollinearity, confirming that the variables are not linearly dependent and that the regression estimates are stable and reliable.

Table 3: VIF

Variable	VIF
IO	1.02
FRQ	1.13
Firm Size	1.10
Leverage	1.09
Firm Age	1.04

Regression Results

Two Ordinary Least Squares (OLS) regression models were estimated:

Model 1: Direct Effect of IO on ROE

$$ROE_{it} = \alpha + \beta_1 IO_{it} + \beta_2 FS + \beta_3 LEV + \beta_4 AGE + \epsilon$$

- 10 Coefficient $= +0.0020, \mathrm{p} < 0.001$
- R-Squared $= 0.970 \rightarrow 97\%$ of variation in ROE is explained

Final Point: A clear and robust relationship exists between ownership structure and profitability, thereby supporting the initial hypothesis. This demonstrates that institutional investors are significant in enhancing corporate governance, in turn contributing to better firm performance.

Figure 2 presents a scatter plot depicting the positive correlation between Institutional Ownership (%) and ROE. The distribution of data points reveals a clear positive linear pattern, higher institutional ownership likely corresponding to improved ROE. This visual evidence supports the research hypothesis asserting that institutional investors serve as key drivers of enhanced firm profitability through their active monitoring and governance roles.

Vol: 16 **No:** 04 **Year:** 2024 **ISSN:** 1309-8055 (Online) (**pp.** 192-211) **Doi:** 10.34109/ijefs.202416409

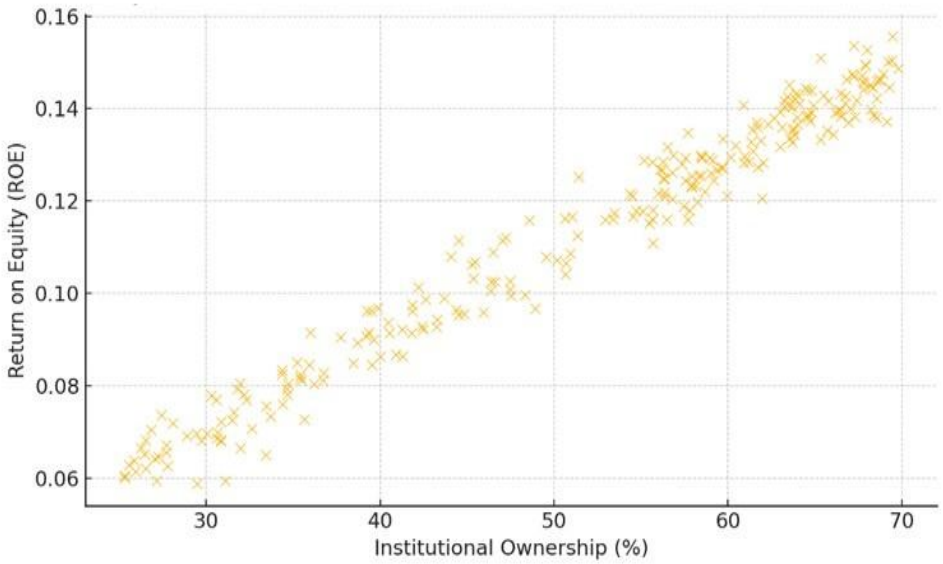

Figure 2: Scatter Plot of Institutional Ownership and ROE

Model 2: Moderating Role of Financial Reporting Quality

$$ROE_{it} = \alpha + \beta_1 IO + \beta_2 FRQ + \beta_3 (IO \times FRQ) + \text{ Controls } + \epsilon$$

- FRQ Coefficient: Not significant ($p = 0.346$)
- Interaction Term (IO × FRQ): Not significant ($\mathrm{p} = 0.159$)
- R-Squared $= 0.971$

In the End: Although the statistical association observed is not particularly strong, the overall model still provides valuable insights. The findings do not support Hypothesis 2 and suggest that FRQ has no significant moderation of the relationship between IO and ROE here.

Robustness Checks

- Durbin-Watson Statistic = 1.84: Indicates no autocorrelation.
- Jarque-Bera Test: Confirms normality of residuals.
- No Heteroscedasticity or Misspecification observed in residual diagnostics.

Figure 3 presents a boxplot illustrating the distribution of ROE within the sample. The median ROE is approximately 0.12, with most values ranging between 0.09 and 0.14, indicating a moderate spread. The absence of extreme outliers and the central placement of the median suggest that firm profitability is generally well-distributed and stable across the sample.

Vol: 16 **No:** 04 **Year:** 2024 **ISSN:** 1309-8055 (Online) (**pp.** 192-211) **Doi:** 10.34109/ijefs.202416409

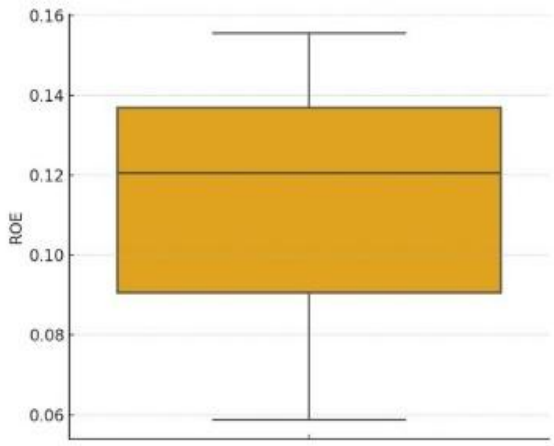

Figure 3: Distribution of Return on Equity

DISCUSSION OF FINDINGS

The significant positive effect of IO on ROE highlights the pivotal role institutional investors can play in bolstering firm performance, particularly in emerging market contexts characterised by less mature or evolving regulatory frameworks. This result is in accordance with earlier research (Gillan & Starks, 2003; Tsyplakov, 2008) that indicates that increased institutional ownership reduces the cost of agency by ensuring tighter alignment between shareholders and managers. Institutional investors are better informed, have the expertise and financial means necessary for effective monitoring, and are less likely to have short-term time orientations, all of which is necessary in order for investor confidence to be increased and for the value of the company in the long term be maintained. Furthermore, monitoring by institutional investors usually leads to more prudent and strategic managerial decisions, which protect the long-term financial welfare while minimizing the chances of short-term earnings management. In this way, institutional ownership does not act merely as a passive equity stake, but as an active governance mechanism that increases operating efficiency and long-term profitability.

In governance systems that are poorly developed, institutional ownership is specifically significant function in checking managerial discretion and opportunism. The findings of the study confirm the argument that institutional investors serve as active agents of governance, not passive players. This function is most relevant in weak regimes, in which institutional investors can fill governance deficiencies by enforcing better standards of accountability. In addition, they have direct policy implications for regulators and policymakers in emerging economies, in that institutional ownership may be a strategic tool for improved corporate governance and, in turn, better financial performance for the individual firm. However, a lack of significant moderating effect for FRQ can be taken either as a limitation of the selected proxy variables that are

Vol: 16 **No:** 04 **Year:** 2024 **ISSN:** 1309-8055 (Online) (**pp.** 192-211) **Doi:** 10.34109/ijefs.202416409

widely considered reasonable for this research agenda or a structural flaw in the Iraqi system of financial reporting. This result provides scope for further research that uses alternative FRQ measures or high-level econometric analysis, for instance, fixed-effects panel models, in order to gain insight into otherwise hidden dynamics.

CONCLUSION AND RECOMMENDATIONS

This research posits that institutional structure positively and significantally affect firm profitability in terms of ROE. The evidence is in favor of increased institutional investors being linked with increased governance practices and monitoring that, in turn, boost the performance of the firm. The expected moderating effect of FRQ between this link was not supported by the evidence. This can be explained by deficiencies in the proxy for measuring the financial reporting quality or in the context of the market, including poor accounting rule enforcement or a lack of financial transparency.

Recommendations

- For Firms: Promote institutional investment to improve monitoring, enhance accountability, and ultimately boost financial performance.
- For Policymakers: Reinforce financial disclosure regulations and encourage the implementation of superior reporting standards.
- For Future Research: Utilize more precise proxies for financial reporting quality, such as discretionary accruals, and apply panel data techniques to better account for firm-specific differences over time.

IMPLICATIONS FOR PRACTICE AND POLICY

The results carry important implications for business managers, policymakers, and regulatory authorities in developing economies.

For Corporate Management

- The clear institutional ownership has a positive relationship with profitability suggesting that companies actively striving to attract and retain institutional investors.

- Management ought to prioritise transparency and strengthen internal controls to increase their firms' appeal to institutional investors.

For Policymakers and Regulators

- Strengthen the regulatory framework to safeguard institutional investors and ease their contribution in the capital markets.

- Enhance the enforcement of financial reporting requirements and promote the adoption of international accounting standards to improve overall financial transparency.

For Auditors and Accounting Professionals

- Strengthen audit quality and align reporting procedures with leading international standards to foster greater confidence in financial reporting.
- Provide training for financial professionals in evaluating financial reporting quality through established techniques such as accrual analysis and forensic accounting.

These findings underline the critical ownership structure and financial disclosure significance in building an effective financial market. As Iraq's capital market evolves, improving investor protection and financial regulation will be vital to attracting long-term investment and supporting sustained economic growth.

REFERENCES

Adebayo, T. S., Akadiri, S. S., Uhunamure, S. E., Altuntaş, M., & Shale, K. (2022). Does political stability contribute to environmental sustainability? Evidence from the most politically stable economies. *Heliyon*, *8*(12). https://doi.org/10.1016/j.heliyon.2022.e12479

Al-Sahlany, A. M., & Kadhum, H. J. (2023). The Impact of Micro Factors on the Performance of the Iraq Stock Exchange Index for the Period 2005-2021. *International Journal of Professional Business Review*, *8*(9), 1-16. https://doi.org/10.26668/businessreview/2023.v8i9.3462

Barney, J. (1991). Firm Resources and Sustained Competitive Advantage. *Journal of Management*, *17*(1), 99-120. https://doi.org/10.1177/014920639101700108

Benlemlih, M., Arif, M., & Nadeem, M. (2023). Institutional ownership and greenhouse gas emissions: A comparative study of the UK and the USA. *British Journal of Management*, *34*(2), 623-647. https://doi.org/10.1111/1467-8551.12613

Çifçi, G., & Sönmez, A. R. (2023). Is sustainability important for returns? *Environment, Development and Sustainability*, *25*(12), 15119-15137. https://doi.org/10.1007/s10668-023-03781-1

Fama, E. F., & French, K. R. (1992). The cross-section of expected stock returns. *the Journal of Finance*, *47*(2), 427-465. https://doi.org/10.1111/j.1540-6261.1992.tb04398.x

Garel, A., & Petit-Romec, A. (2021). Engaging Employees for the Long Run: Long-Term Investors and Employee-Related CSR. *Journal of Business Ethics*, *174*(1), 35-63. https://doi.org/10.1007/s10551-020-04572-8

George, A. S. (2024). Finance 4.0: The Transformation of Financial Services in the Digital Age. *Partners Universal Innovative Research Publication*, *2*(3), 104-125. https://doi.org/10.5281/zenodo.11666694

Gillan, S., & Starks, L. T. (2003). Corporate governance, corporate ownership, and the role of institutional investors: A global perspective. *Weinberg Center for Corporate Governance Working Paper*(2003-01). https://doi.org/10.2139/ssrn.439500

Hossain, R., Ghose, P., Chowdhury, T. M., Hossen, M. D., Hasan, M. N., & Mani, L. (2024). Ownership Structures and Firm Performance: A Correlation and Regression Analysis of Financial Institutions in Bangladesh. *Pakistan Journal of Life and Social Sciences*, *22*(2), 6278-6295. https://doi.org/10.57239/PJLSS-2024-22.2.00473

Idan, A. M. (2022). Effect of Oil Prices, Inflate Rate, Energy Consumption, Gross Domestic Product on Stock Market Performance of Iraq Stock Exchange. *Cuadernos de Economía*, *45*(128), 45-52. https://cude.es/submit-a-manuscript/index.php/CUDE/article/view/259

Jensen, M. C., & Meckling, W. H. (2019). Theory of the firm: Managerial behavior, agency costs and ownership structure. In *Corporate governance* (pp. 77-132). Gower. https://doi.org/10.1016/0304-405X(76)90026-X

Ke, B., Petroni, K. R., & Shackelford, D. A. (2000). The impact of state taxes on self-insurance. *Journal of Accounting and Economics*, *30*(1), 99-122. https://doi.org/10.1016/S0165-4101(00)00030-6

Koh, P.-S. (2003). On the association between institutional ownership and aggressive corporate earnings management in Australia. *The British Accounting Review*, *35*(2), 105-128. https://doi.org/10.1016/S0890-8389(03)00014-3

Kordsachia, O., Focke, M., & Velte, P. (2022). Do sustainable institutional investors contribute to firms' environmental performance? Empirical evidence from Europe. *Review of Managerial Science*, *16*(5), 1409-1436. https://doi.org/10.1007/s11846-021-00484-7

Le, T. D., & Nguyen, N. (2024). Institutional ownership stability and product quality failures. *International Journal of Managerial Finance*, *20*(4), 1021-1047. https://doi.org/10.1108/IJMF-03-2023-0154

Le, V. P. M., Meenagh, D., & Minford, P. (2021). State-dependent pricing turns money into a two-edged sword: A new role for monetary policy. *Journal of International Money and Finance*, *119*, 102496. https://doi.org/10.1016/j.jimonfin.2021.102496

Lehenchuk, S., Zeytinoglu, E., Hrabchuk, I., Zhalinska, I., & Oleksich, Z. (2023). Nexus between intellectual capital, financial performance and sustainable growth: evidence from the Turkish ICT Industry. *Marketing i menedžment innovacij*, *14*(2), 152-162. https://doi.org/10.21272/mmi.2023.2-14

Lin, L., & Puchniak, D. W. (2022). Institutional investors in China: Corporate governance and policy channeling in the market within the state. *Columbia Journal of Asian Law*, *35*(1), 74. https://doi.org/10.52214/cjal.v35i1.9190

Pincus, K. V. (1997). Discussion of Educating for Accounting Expertise: A Field Study. *Journal of Accounting Research (Wiley-Blackwell)*, *35*(3), 63-74. https://doi.org/10.2307/2491453

Rımaz, M., & Ayanoğlu, Y. (2021). The Effect of Free Cash Flow and Capital Structure on The Company's Efficiency and an Application in ISE 100. *IBAD Sosyal Bilimler Dergisi*(9), 267-290. https://doi.org/10.21733/ibad.840673

Shleifer, A., & Vishny, R. W. (1986). Large shareholders and corporate control. *Journal of political economy*, *94*(3, Part 1), 461-488. https://www.journals.uchicago.edu/doi/abs/10.1086/261385

Simmons, R. S. (2006). Does recent empirical evidence support the existence of international corporate tax competition? *Journal of International Accounting, Auditing and Taxation*, *15*(1), 16-31. https://doi.org/10.1016/j.intaccaudtax.2006.01.002

Spence, M. (1978). Job market signaling. In Uncertainty in economics. In P. Diamond & M. Rothschild (Eds.), *Uncertainty in Economics* (pp. 281-306). Academic Press. https://doi.org/10.1016/B978-0-12-214850-7.50025-5

Trinh, Q. D., Haddad, C., & Salameh, E. (2022). Financial Institutional Ownership and Reporting Quality: Evidence from International Listed Firms. *Available at SSRN 4207691*. https://ssrn.com/abstract=4207691

Tsyplakov, S. (2008). Investment frictions and leverage dynamics. *Journal of Financial Economics*, *89*(3), 423-443. https://doi.org/10.1016/j.jfineco.2007.09.004

Yahaya, P. D. O. A. (2024). o Foreign And Institutional Ownerships Enhance The Quality Of Financial Reports? *Available at SSRN 5020721*. https://doi.org/10.2139/ssrn.5020721