

Governance through Debt: Blockholder Structure, Market Timing, and Leverage Recapitalization Decisions

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Abstract:

This study examines how blockholder ownership structures and market timing influence corporate leverage recapitalization decisions in Indonesian non-financial firms. Utilizing a sample from 2014–2023, the research employs logistic regression to analyze recapitalization events exceeding a 5% materiality threshold. Findings reveal that concentrated blockholder ownership significantly shapes recapitalization, employing leverage as a strategic governance mechanism to align management interests and mitigate agency costs. Furthermore, firms demonstrate a pronounced sensitivity to market timing, strategically executing recapitalizations to exploit favorable equity valuations. The high ownership concentration characteristic of the Indonesian market underscores debt's role as a pivotal tool for blockholder monitoring and risk management, thereby defining corporate financial policy in this emerging economy.

Keywords: *Blockholder Structure, Leverage Recapitalization, Market Timing, Corporate Governance, Emerging Markets*

1. Introduction

Corporate financing, the strategic policy governing a firm's use of internal and external funds, requires a nimble approach to navigate dynamic economic landscapes (Zheng & Mo, 2022). At its core lies the fundamental choice between leverage and equity, a decision dictated by strategic ambition and investment scale. This critical choice must be guided by a triad of interconnected considerations; the spectrum of available investment opportunities, the existing capital structure, and the firm's long-term sustainability (Legesse et al., 2021; Moolkham, 2024). Such prudence is paramount, as these financing decisions directly shape the company's cost of capital and risk profile, thereby exerting a profound influence on its financial health and, ultimately, shareholder value (Gan et al., 2022; Liu et al., 2023).

While the strategic application of leverage financing can yield substantial corporate benefits such as tax advantages (Kim & Lotfaliei, 2020), enhanced shareholder value (Y. Chen et al., 2025; Friewald et al., 2022), and an optimized capital structure (Hama et al., 2024; Overesch & Voeller, 2010), its imprudent use introduces considerable peril. The specters of potential bankruptcy (Harrison et al., 2014), the burden of debt servicing (L. Chen & Liu, 2024), and impaired overall performance (Kim & Lotfaliei, 2020) underscore the critical need for firms to strike a careful balance to ensure long-term stability. A pivotal mechanism for achieving this equilibrium is corporate leverage recapitalization, a deliberate policy that enables management

to strategically recalibrate the firm's financial profile ((Al-Hawatmah & Shaban, 2023; Gupta & Rosenthal, 1991).

A leverage recapitalization is a strategic financial maneuver wherein a company restructures its capital by supplanting existing debt with new obligations. This process is often employed to raise equity or fund shareholder distributions, optimizing the firm's capital structure and enhancing its value. It serves as a practical alternative to an Initial Public Offering (IPO) or an outright sale, all while allowing management to retain operational control (Hooke, 2004). The strategic merits of this approach are multifaceted. It can strengthen a company's bargaining position with suppliers (Hennessy & Livdan, 2009), invigorate oversight from external market monitors (Bae & Jo, 2006), and enable the firm to capitalize on favorable market conditions to refinance older costly debt (Kisser & Rapushi, 2022).

Despite its apparent advantages, this strategy is fraught with significant perils. The resulting surge in the leverage-to-equity ratio can severely erode financial flexibility and elevate the firm's overall risk profile (Ima et al., 2024; Shaferi et al., 2018). Among the specific dangers are the heightened costs of financial distress (Bansal et al., 2021), the potential for leverage overhang to stifle new investment (Francia et al., 2013), and an increased vulnerability to default risk and market volatility (L. Chen & Liu, 2024; Koutmos et al., 2018). Consequently, any company considering a leverage recapitalization must meticulously assess the long-term implications to ensure that the pursuit of immediate value does not jeopardize its future financial stability (Kunin & Peshko, 2023).

During leverage recapitalizations, blockholders serve as a vital mechanism for safeguarding corporate stability and performance. Moving beyond the classic manager-shareholder conflict (Jensen & Meckling, 1976), the presence of multiple large shareholders (Maury & Pajuste, 2005) establishes a complex yet potent governance structure (Laeven & Levine, 2008). This arrangement shapes corporate outcomes by enhancing resource allocation, investment efficiency, and firm performance, as it better aligns management with owner interests (Bui, 2022; L. Chen & Liu, 2024; Jiang et al., 2022). The net benefit, however, depends on a critical balance between the strategic advantages blockholders provide and the inherent costs of coordinating their actions (Bole et al., 2023; Valenzuela & Chen, 2023).

The strategic pursuit of an optimal capital structure is fundamentally informed by a firm's internal governance, specifically its blockholder ownership and its capacity for market timing through leverage recapitalizations. For corporations in developing economies like Indonesia, this strategic imperative is intensified by the inherent volatility of global leverage markets, demanding financial policies that are resilient to external shocks. Furthermore, the unique dynamics of blockholders within Indonesia's deeply integrated, yet susceptible, capital market remain a critical area of inquiry. It is within this complex nexus of internal ownership structures and external macroeconomic volatility that this research positions its central question: To what extent do blockholder structure and market timing influence corporate leverage recapitalization?

2. literature Review

The blockholder structure, characterized by concentrated voting rights, grants major shareholders profound influence over corporate strategy and governance, presenting a dualistic effect: it can mitigate classic owner-manager agency issues while simultaneously introducing new principal-principal conflicts with minority shareholders (Bar-Isaac & Shapiro, 2020; Basu

et al., 2017). While the single blockholder model is championed for decisive leadership, its risks of expropriation have prompted a more nuanced perspective. In contrast, the multiple blockholder structure creates a complex governance paradigm where competing coalitions balance enhanced monitoring against the risk of internal conflict. This dynamic can foster a competitive landscape for control, driving strategic financial maneuvers such as pro-cyclical leverage recapitalizations, where firms deliberately increase debt to distribute funds, exploiting favorable credit conditions and reinforcing the persistent, cyclical nature of leverage within their capital structure (Rossetto et al., 2023).

The dynamics of ownership and financial strategies manifest differently in emerging economies, as seen in the BRICS countries. Within this context, majority large shareholders (MLS) assume a significant monitoring role that reduces principal-principal agency issues, ultimately diminishing excessive leverage, elevating capital investment, and strengthening ESG performance. This effect is most pronounced in firms characterized by weak external governance (Yan et al., 2023). Diverging from patterns observed in the G7, corporations in BRICS economies employ equity market timing, strategically decreasing leverage during periods of high stock prices which moderated by cultural dimensions, including uncertainty avoidance (Arosa et al., 2015). Despite this, the financial systems of BRICS nations are still confronted with vulnerabilities arising from substantial external debt and market volatility (Akhmadeev et al., 2018).

In contrast, the ASEAN corporate landscape is predominantly characterized by family-owned firms, where the influence of MLS assumes a more ambiguous, and often collusive, character. Rather than providing constructive monitoring, MLS in this context frequently prioritize private benefits, leading to collusive behaviors that can negatively impact ESG outcomes for broader stakeholders (Geraldina et al., 2025). Strategically, ASEAN firms employ leverage recapitalization as a mechanism to access liquidity without ceding control and actively practice equity market timing to issue shares at favorable valuations (Ratih, 2021). However, the speed at which these firms adjust their leverage toward target levels is not uniform, reflecting significant heterogeneity in financial market depth and institutional quality across the region (Chua et al., 2021).

3. Research Methods

3.1. Sample

This study analyzes a sample of non-financial firms listed on the Indonesia Stock Exchange (IDX) from 2014 to 2023. The sample was constructed according to three key criteria to ensure both methodological rigor and relevance to the research questions. First, aligning with conventional financial research, firms in the financial sector were excluded due to their unique capital structures and regulatory requirements. Second, to isolate a meaningful capital structure event, we included only firm-year observations where the recapitalization ratio—measured as the change in total leverage divided by the book value of assets—exceeded 5%. Finally, the sample was restricted to companies that engaged in share repurchases during the period, as this activity is a central variable of interest.

3.2. Operational Definition of Research Variables

This study employs corporate leverage recapitalization as its dependent variable, operationalized as the ratio of the net change in a equity ($\Delta Equity$) to its book value of assets. Adhering to the methodological precedent set by (Hovakimian et al., 2001) and followed in

subsequent studies ((Danis et al., 2014; Kisser & Rapushi, 2022; Leary & Roberts, 2005), a recapitalization is deemed material if this ratio meets or exceeds the 5% threshold. The variable is formally defined by the following equation:

$$\text{Recaps} = \frac{\text{Longterm Debt}_t - \text{Longterm Debt}_{t-1}}{\text{Book Value of Asset}_{t-1}}$$

This study employs the structure of blockholder ownership as its independent variable. Conceptualized as a framework with multiple large shareholders, this structure distinguishes between a single main blockholder and subsequent non-main blockholders (Laeven & Levine, 2008). To operationalize this configuration, we utilize the Herfindahl-Hirschman Index (HHI), a proxy that quantifies the concentration of ownership power among these key investors; a higher HHI value signifies a more pronounced concentration. As established in the literature, this measure of power distribution is a significant determinant of a firm's corporate leverage recapitalization decisions (Jara et al., 2019; Konijn et al., 2011; Pombo & Taborda, 2017; Wei et al., 2017). The HHI is calculated as follows:

$$\begin{aligned} \text{HHI} &= \sum \text{VR}_i^2 \\ &= \sum (\text{VR}_1)^2 + (\text{VR}_2)^2 + (\text{VR}_3)^2 + (\text{VR}_4)^2 \end{aligned}$$

To quantify the concentration of voting rights, this analysis adopts the Herfindahl-Hirschman Index (HHI), a widely accepted measure of market concentration that is readily adapted to corporate ownership contexts. The HHI is calculated by summing the squares of individual voting rights percentages (VR_i) across all shareholders. For this purpose, shareholders are stratified into distinct tiers. The primary category, VR₁, represents the controlling stake of the Main Blockholder(s), defined as an ownership share of 20% or more, a established threshold for significant influence (La Porta et al., 1999). The remaining ownership is then disaggregated into three sub-categories of Non-Main Blockholders: VR₂ (15% to <20%), VR₃ (10% to <15%), and VR₄ (5% to <10%).

The selection of control variables in this study is guided by established practices in the leverage recapitalization literature. Firm size, in particular, is a consistently critical factor due to its profound influence on capital structure decisions. Its inclusion, as seen in seminal works by Denis & Denis (1995) and Frank & Goyal (2009), through to more recent analyses by Elsas et al., (2013) and Kisser & Rapushi (2022). By accounting for the impact of firm size on both dependent and independent variables, this study aims to better isolate the effects of the variables of interest. Accordingly, the following proxies are employed to measure firm size.

$$\text{Size}_{i,t} = \text{Ln}(\text{Total Aset}_{i,t})$$

While elevated capital expenditures (CAPEX) typically signal a promising growth phase, characterized by abundant profitable opportunities, they also create a corresponding need for external financing. Leverage recapitalization emerges as a potential solution to this funding imperative, yet it carries profound implications for corporate investment policy. The resultant debt service burden and intensified creditor scrutiny can pressure firms to curb investment, creating a complex interplay between financing and investment decisions. It is this very intricacy that establishes CAPEX as an indispensable control variable in empirical finance. By accounting for capital expenditures, researchers can better isolate the distinct effect of leverage

recapitalization on financial and operational outcomes, a methodological convention firmly established in the literature.

$$CAPEX_{i,t} = (\text{Cash Outflows}_{i,t} / \text{Sales}_{i,t})$$

To analyze the determinants of the outcome, this study utilizes a binomial logistic regression model. This statistical approach is particularly well-suited for estimating the likelihood of a dichotomous result based on a set of predictor variables (Hosmer & Lemeshow, 1980). The model is formally specified by the following equation:

$$\text{Recaps}_{i,t} = \alpha + \beta_1 \text{BLOCK}_{i,t} + \beta_2 \text{MT}_{i,t} + \beta_3 \text{SIZE}_{i,t} + \beta_4 \text{CAPEX}_{i,t} + \varepsilon_{i,t}$$

This empirical analysis investigates the determinants of corporate leverage recapitalization. The model employs a binary dependent variable, $\text{Recaps}_{i,t}$, which equals one if firm i undertook a leverage recapitalization in year t , and zero otherwise. Our primary focus is on the Leverage Recapitalization Ratio (recap), a continuous measure that quantifies the magnitude of the recapitalization event. Grounded in established capital structure research, the model incorporates key firm-specific controls to isolate these effects. These include the firm's Blockholder Structure ($\text{STRBLOK}_{i,t}$), capturing internal governance dynamics (e.g., Berger et al., (1997); Market Timing (MT), reflecting strategic responses to equity market valuations (Baker & Wurgler, 2002); Firm Size (Size), a standard proxy for information asymmetry and default risk; and Capital Expenditure (Capex), which signals investment intensity and corresponding financing needs.

4. Results and Discussions

The descriptive statistics for the study's key variables are presented in Table 1. These initial results provide a foundational overview of the data distribution for subsequent analysis.

Table 1: Descriptive Statistics

	RECAPS	STRBLOK	MT	SIZE	CAPEX
Mean	1,00	30,61	141.3381	1,32	-18,57
Median	0,11	27,90	86.25888	0,53	-9,41
Maximum	62,89	86,71	1800.889	10,78	187,03
Minimum	-40,74	0,0026	-211.0176	0,01	-511,93
Percentile 33	-1,61	20,60	59.80323	0,22	-17,81
Persentile 66	2,29	35,57	134.6314	1,08	-4,78
Std. Dev.	9,38	18,29	160.9065	1,86	39,17
Skewness	0,77	0,67	3.246938	2,25	-5,59
Kurtosis	9,23	3,21	23.08512	8,34	63,41
Jarque-Bera	1.392	62	15038.4	1.647	127.396
Probability	0,00	0,00	0	0,00	0,00
Sum	808	24.798	116383	1.067	-15.045
Sum Sq. Dev.	71.240	270.605	20945728	2.790	1.241.553
Observations	810	810	810	810	810

Note: Recaps5%, representing a 5% Leverage Recapitalization; STRBLOK, denoting the ownership structure of blockholders; MT, which stands for Market Timing; SIZE, indicating Firm Size; and CAPEX, reflecting Capital Expenditure.

Analysis of the sample reveals a discernible trend toward deleveraging, evidenced by an average recapitalization ratio of 1.00%. As the underlying data deviated from normality, a non-parametric approach was employed, utilizing the median as a more robust measure of central

tendency (Hair et al., 2019). This method confirmed a median recapitalization ratio of 0.11%, a value situated between the 33rd and 66th percentiles, which more accurately captures the moderate leverage conditions characterizing the sample. Applying this same robust framework to the Market Timing (MT) variable, a median market-to-book ratio of 0.86 emerges, pointing to a prevailing undervaluation among firms—a finding that the inflated arithmetic mean of 1.65 otherwise obscures. In parallel, scrutiny of ownership concentration, measured by blockholder shareholdings, indicates a pronounced concentration of control. This is underscored by an average Herfindahl-Hirschman Index (HHI) of 3,061 and a distribution of data exhibiting extreme variation, spanning from widely dispersed to heavily concentrated ownership structures.

The analysis of control variables illuminates the sample's composition, revealing a cohort of moderately-scaled firms with a median size of US\$0.53 billion in assets. The positive skew in the size distribution, indicated by a higher mean, points to the presence of a subset of substantially larger entities. Regarding capital allocation, the median CAPEX of -9.41% confirms that a majority of firms were actively investing, likely financed through operational earnings. However, the more negative mean of -18.57%, coupled with the presence of outliers, underscores a significant divergence in strategic priorities, ranging from aggressive investment to notable divestment.

The results of the statistical testing for the research model are presented in Table 2.

Table 2: Result

	α	β_1 STRBLOK	β_2 MT	β_3 SIZE	β_4 CAPEX
Recaps _{5%}	-2,0	0,01**	0,307**	0,06*	-0,02***
z	-4,8	1,015	0,890	0,71	-2,881

Note: Recaps_{5%}, representing a 5% Leverage Recapitalization; STRBLOK, denoting the ownership structure of blockholders; MT, which stands for Market Timing; SIZE, indicating Firm Size; and CAPEX, reflecting Capital Expenditure.

Research indicates that a blockholder structure significantly shapes leverage recapitalization, with a 5% threshold serving as a critical inflection point for governance. At this specific level, blockholders are positioned to employ leverage as a strategic monitoring tool, curbing managerial opportunism and mitigating risks including financial manipulation (Dou et al., 2018), misuse of corporate assets (Jiang et al., 2020), and information concealment (Nikolaev, 2015). A recapitalization of 5% is viewed as operating within a feasible risk tolerance, capable of boosting firm value while avoiding the perils of financial distress. Within this limit, agency costs can be counterbalanced by linking executive compensation to performance. Consequently, this ratio reflects a calculated equilibrium where governance mechanisms, risk tolerance, and the pursuit of shareholder value converge.

The alignment between blockholder structure and management on leverage recapitalization policy at the 5% threshold can be attributed to a predominantly concentrated ownership landscape. This finding resonates with the established ownership patterns in Indonesia, where a significant majority of companies which approximately 66.45% are controlled by a small cohort of large shareholders, often through family-owned structures (Juniarti, 2015; Rusmin et al., 2011). Empirical evidence suggests that such concentrated ownership promotes the use of leverage as a mechanism to mitigate agency conflicts between majority and minority shareholders (Haron et al., 2021). This tendency is particularly pronounced in Indonesian family-owned firms, which frequently maintain high leverage as a dual-purpose strategy to consolidate control and reduce agency problems (Mulyani et al., 2016). In contrast, institutional

ownership exerts a countervailing influence; firms with significant institutional investment tend to exhibit lower leverage, reflecting these investors' preference for less risky capital structures (Purwani, 2017; Utomo & Mawardi, 2024). It is this very complexity that the dynamic interplay between different types of blockholders, likely confines the observable influence of blockholder structure to the 5% recapitalization ratio, even as the median leverage recapitalization ratio across firms remains notably low at 0.11%.

While corporate leverage recapitalization ratios are typically modest, a concentrated blockholder ownership structure may strategically approve a 5% recapitalization for several compelling reasons. These include its function as a monitoring mechanism to mitigate agency costs, risk-return optimization, and as a commitment device to discipline management, the inherent influence of the ownership structure itself which bolstering of the blockholder's bargaining position.

Leverage recapitalization emerges as a strategic tool for blockholders to enforce managerial discipline, effectively employing debt as a governance mechanism. By imposing binding financial obligations, this strategy deliberately restricts free cash flow, compelling a more efficient allocation of capital and curtailing opportunistic behavior. This disciplinary function of leverage is especially critical in environments with weak investor protection or where a divergence between control and cash-flow rights exists (Chong, 2010).

The efficacy of leverage in mitigating agency costs operates through two primary channels. First, long-term debt fosters managerial prudence, incentivizing rigorous investment decisions that enhance firm value (Dabboussi, 2024; Mahadwartha & Ismiyanti, 2008). It acts as a bulwark against the overinvestment in low-value projects that often plagues weakly governed firms (Chung et al., 2018). Second, the very structure of leverage imposes discipline; short-term debt, for instance, promotes transparency and limits managerial discretion by necessitating frequent repayment and external scrutiny (Alderson et al., 2014; Jung & Choi, 2024). Ultimately, within concentrated ownership structures, leverage serves as a vital counterbalance to dominant shareholders, helping to safeguard minority interests from expropriation (Al-Sraheen & Hamdan, 2022; Hassan, 2016).

Leverage thus functions as a dual-edged mechanism in corporate governance: it disciplines managerial behavior while concurrently enhancing investment efficiency and protecting blockholder interests. The strategic orchestration of short- and long-term debt creates a robust, multi-faceted monitoring system. This synergy elucidates why blockholders may countenance leverage recapitalizations of up to 5%, as the accrued governance benefits countervail the accompanying financial risks (Margaritis & Psillaki, 2007).

As major shareholders, blockholders exert a distinct influence on corporate strategy, particularly regarding risk and financing. Although they demonstrate a higher risk tolerance than dispersed shareholders, their substantial investments and active oversight paradoxically serve to mitigate stock price crash risk through powerful monitoring mechanisms (Eugster & Wang, 2023; Rossetto et al., 2023). This nuanced relationship is further reflected in their financing preferences, where a pronounced inclination toward leverage is evident. Driven by the dual motives of capital acquisition and ownership consolidation, blockholders often favor private debt arrangements with stringent covenants to avert dilution (Haron, 2017; Nikolaev, 2015). Moreover, they strategically calibrate the maturity structure of debt, employing an optimal mix of short- and long-term leverage to sharpen their supervisory control over management (Pan & Tan, 2019).

The governance role of blockholders is channeled through two principal avenues, active oversight and the latent threat of exit. This influence manifests directly in financial policy; for instance, through board representation, they ensure corporate leverage adheres to strategic targets (Nguyen et al., 2022). Conversely, the mere specter of divestiture can compel management to improve financial reporting quality (Dou et al., 2018). However, this influence is not inherently benign. In jurisdictions with weak legal protections, leverage can be perverted into a tool for expropriating minority shareholders (Bai et al., 2013). This places blockholders in a quandary, torn between retaining control and confronting financial constraints, a dilemma particularly acute in young family firms averse to ownership dilution (Keasey et al., 2015). Ultimately, the efficacy of these governance mechanisms is not absolute but is critically contingent on the regulatory landscape, as robust creditor protection has been shown to encourage longer debt maturities (Martins et al., 2020).

Leverage recapitalization can be strategically justified to blockholders by framing debt not merely as financing, but as a commitment mechanism that enhances corporate governance. This approach is especially advantageous for firms with volatile cash flows, as it mitigates creditor coordination problems and streamlines renegotiation during financial distress (John et al., 2021). A dominant blockholder, frequently also a major creditor, plays a crucial governance role in this context by influencing the behavior of dispersed smaller creditors, thereby reducing the risk of coordination failures and preventing premature asset liquidation (F. Takeda & Takeda, 2005; K. Takeda, 2003). The strategic use of leverage is further solidified by formal contractual mechanisms, such as collective action clauses and exit consents, which align creditor interests ex-ante. These tools help avert costly litigation and facilitate smoother debt renegotiations, ultimately reinforcing the governance efficacy of the leveraged position (Bi et al., 2016).

5. Conclusions

Empirical analysis of Indonesian non-financial firms reveals that leverage recapitalization is a primary channel through which blockholders govern. The data confirm that blockholder structure directly shapes recapitalization decisions, with a statistically significant influence (5% level) on leverage ratios. This active governance through debt is complemented by a keen sensitivity to market timing, as firms strategically execute recapitalizations to capitalize on favorable equity conditions (Baker & Wurgler, 2002). The high concentration of ownership in Indonesia (average HHI of 3.061) intensifies this dynamic, making debt a strategic tool to align management and safeguard investments. Thus, the interplay of blockholder monitoring and opportunistic market timing converges to define the leverage recapitalization policies of firms in this developing market.

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