Asia Journal of Social Innovation and Development
https://www.ajsid.org/index.php/pub

Article

Agency Theory vs. Stewardship Theory: Key Differences, Contextual Boundaries, and an Integrated Governance Framework - A Study Based on Game Theory and Social Embeddedness Perspective

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Received: 11 August 2026; **Revised**: 26 August 2026 ; **Accepted**: 5 September 2026 ; **Published**: 8 September 2026

Abstract: For more than 40 years, corporate governance has been a field of research dominated by agency theory and stewardship theory, which have quite different views on the underlying nature of both human behavior and organizational dynamics. Stewardship theory builds on agency theory, which states that managers are self-interested individuals who require monitoring and incentives to work in the best interests of their shareholders, but also argues that managers are intrinsically motivated to act as trustworthy stewards who put organizational success first. Though both traditions have been studied in detail, there has been no consensus so far on how to resolve the theoretical conflicts between the two traditions, nor on the conditions under which they are most applicable. This paper fills this gap by combining the game-theoretic approach with the social embeddedness approach to explore the major distinctions between the two theories' approaches and boundaries. The analysis shows that the differences in predictions from agency and stewardship theory are, in fact, different Nash equilibria due to different psychological and situational factors. In addition, the applicability of each theory is not uniform, but varies with a complex interaction of the micro-level organizational factors and macro-level institutional environments. Based on these, the paper suggests a dynamic integrated governance model, which merges both governance theories to respond to the changing context. The framework offers practical advice on how to create governance systems that are effective and strike a balance between control and collaboration, while enhancing long-term performance.

Keywords: agency theory; stewardship theory; corporate governance; game theory; social embeddedness; contextual boundaries

1. Introduction

Two theoretical traditions—agency theory and stewardship theory—have dominated corporate governance research and have long been viewed as contradictory. Jensen and Meckling's [1] paper established agency theory as the dominant paradigm, as it offers a strong theory to explain conflicts of interest that emerge when ownership and control are separated in modern corporations. Agency theory has, however, been criticized for being too rationalist and for failing to account for the complexities of human motivation in a business environment [2]. Stewardship theory emerged as a response to agency theory, focusing on the intrinsic motivations of managers and the role of trust and empowerment in achieving organizational success [3].

The debate between these two theories has continued for decades, and empirical studies have been conducted in support of each theory in different contexts. Some studies have reported improved firm performance from agency theory practices that focus on monitoring and incentives [4], while others have reported superior results with stewardship-oriented practices such as employee empowerment and long-term investment [5]. The conflicting evidence also indicates that neither theory can account for managerial behavior in all situations and that each is applicable in different contexts.

Despite the growing recognition of the contextual nature of governance, existing research remains largely fragmented. Most studies take an agency or stewardship perspective, with few attempts to combine both lines of thought. In addition, there are few studies that systematically investigate the boundary conditions for the applicability of one theory over the other. This gap makes it difficult to design governance systems appropriate to different organizational scenarios.

The purpose of this paper is to address some of these limitations by developing an integrated theory that bridges the gap between agency theory and stewardship theory. More specifically, the paper focuses on two research questions: (1) What are the key differences between agency theory and stewardship theory regarding their assumptions, mechanisms, and outcomes? (2) When is each theory more relevant in a specific context, and what are the ways of combining both theories to improve governance effectiveness in an organization?

This paper attempts to answer the above questions by using a multi-theoretical approach, namely, by combining game-theoretic analysis with the social embeddedness perspective. The game-theoretic approach provides a formal tool for studying the strategic relationship between owners and managers and why different incentive systems and psychological influences produce different behaviors. However, the social embeddedness perspective is more concerned with the role that social, cultural, and institutional environments play in shaping organizational behavior [6]. This paper merges these two approaches to develop a deeper understanding of the contextual boundaries of agency and stewardship.

This paper has three contributions. First, it provides a systematic comparison of agency and stewardship theories, highlighting their differences and underlying assumptions. Second, it aims to pinpoint the contextual factors that make each theory applicable, including factors at the micro level that relate to the organizational context, and factors at the macro level that are related to the institutional context. Third, it suggests a dynamic integrated governance framework that supports organizations in developing context-specific governance models. This framework has important implications for both research and practice, as it provides a more nuanced understanding of corporate governance and offers practical guidance for managers and policymakers.

2. Theoretical Foundations and Literature Review

2.1. Agency Theory: Core Assumptions and Development

The problems of delegating decision-making authority to another party to act on their behalf came to the fore in the 1970s in the fields of economics and finance, and formed the basis of agency theory [1]. The core of agency theory is that principals and agents are rational utility maximizers with potentially conflicting interests.

The central premise of agency theory is the assumption that human nature is self-interested and opportunistic. Agents are presumed to act in their own interest rather than in the principal's interest, which can give rise to agency problems such as shirking, risk aversion, and self-dealing at the shareholders' expense [7]. Information asymmetry is another challenge, in that agents usually know more about how the firm is run than principals do, which makes it difficult for principals to monitor agent behavior effectively.

Agency theory suggests two main governance mechanisms that can help alleviate these agency issues: monitoring and incentives. Monitoring involves creating systems that oversee the actions of agents, including external audits, financial reporting systems, and boards of directors. Incentive mechanisms, on the other hand, enable agents to align their interests with those of principals by tying agents' pay to firm performance, usually through stock options, bonuses, and other performance-based pay [8].

Over the past four decades, agency theory has been extensively tested and refined. Early research focused primarily on the relationship between shareholders and top managers, but subsequent studies have extended the theory to other principal-agent relationships, such as those between managers and employees, and between majority and minority shareholders [9]. While agency theory has been criticized for its narrow view of human motivation, it remains the dominant framework for corporate governance research and practice worldwide.

2.2. Stewardship Theory: Core Assumptions and Development

Stewardship theory emerged in the late 1980s and early 1990s as a critique of agency theory's pessimistic view of human nature. Building on psychology and sociology, stewardship theory states that managers are not necessarily self-interested, but can be motivated to act as stewards of the organization and its stakeholders [2].

Stewardship theory differs from the "economic man" approach of agency theory in that it focuses on the "social man", who has many motives other than monetary rewards: achievement, recognition, responsibility, and personal growth [10]. Stewards are satisfied when the organization succeeds and feel that their personal success is connected to the success of the organization. Consequently, they are willing to sacrifice their own interests and preferences for the good of the group when they feel a sense of belonging to the group's mission and values.

Stewardship theory focuses on the role of trust, empowerment, and cooperation in the performance of an organization. Governance systems based on stewardship, rather than monitoring and control, provide managers with greater levels of autonomy and decision-making power to generate long-term value using their expertise and taking calculated risks [3]. These systems also encourage a culture of shared purpose and mutual respect, further improving employee engagement and commitment. Empirical studies of stewardship theory have supported its predictions in other contexts [5,11].

A large body of work has examined the debate between agency theory and stewardship theory; however, this debate reveals certain limitations in current knowledge about corporate governance. First, the majority of studies take an either-or approach to agency and stewardship theories, instead of seeing them as parallel theories. This "either-or" logic does not reflect the complexity of managerial practices because the latter may involve aspects of both individual and collective interest [8].

Second, the contextual factors that influence the effectiveness of agency- and stewardship-based approaches to governance have received less attention to date. A small number of studies have thoroughly evaluated the extent to which each theory can be applied in various institutional and cultural environments, although some have focused on firm-level factors such as firm size, industry, and ownership [12].

Third, theorizing that links agency theory and stewardship theory is still in its infancy. Some scholars [13] have proposed more integrated approaches, but few have offered specific frameworks that incorporate features of both traditions. This dichotomy hampers the development of governance systems that are suited to the context and can offer control without sacrificing empowerment benefits.

This paper tackles these issues and combines the social embeddedness perspective and game theory to construct a richer understanding of agency-stewardship. This paper provides an in-depth analysis of the scenarios in which each theory is most useful and of how the two theories can be synthesized to achieve better governance performance.

3. Key Differences Between Agency Theory and Stewardship Theory

Agency theory and stewardship theory differ in their assumptions regarding human nature, motivation, and organizational relations. The differences also lead to varying expectations from management and recommendations for governance practice. Table 1 shows the key differences between the two theories with respect to four key aspects: managerial motivation, primary goal, control mechanism, and organizational style.

Table 1. Key Differences Between Agency Theory and Stewardship Theory

Dimension	Agency Theory	Stewardship Theory
Managerial Motivation	Extrinsic: Driven by financial rewards, job security, and personal reputation	Intrinsic: Driven by achievement, responsibility, self-actualization, and organizational identification
Primary Goal	Individual utility maximization	Organizational success and long-term value creation
Control Mechanism	Monitoring and incentives: Hierarchical supervision, performance-based compensation, and formal contracts	Trust and empowerment: Autonomy, participation, shared decision-making, and relational governance
Organizational Style	Hierarchical and control-heavy: Centralized authority, clear lines of command, and formal rules and procedures	Flat and involvement-oriented: Decentralized authority, flexible structures, and collaborative culture

Source: Adapted from [7] and [8].

3.1. Managerial Motivation

Stewardship theory, in contrast, suggests that managers are characterized by both intrinsic and extrinsic motivations, with the intrinsic motivations being more powerful [10]. Rewards such as personal growth and development, satisfaction from achieving difficult goals, and a sense of responsibility for the organization's success are intrinsic. Stewards see their role as a vocation, and they feel good when they contribute to the mission of the organization.

Martin and Butler [8] conducted an extensive literature search on agent and stewardship behavior and found several significant differences in motivational orientation. Agents are usually individualistic and work instrumentally, seeing the organization as a means to accomplish their individual objectives. Stewards, on the other hand, are collectivist and relational, having a strong sense of belonging to the organization and its values.

3.2. Primary Goal

These differing perspectives on the main purpose of management activity stem from the difference in motivational assumptions. Agency theory states that the objective of the manager is to maximize his/her utility [7]. This may involve maximizing their pay, minimizing their effort, enhancing their reputation, or ensuring their job security. Managers may pursue organizational objectives, but only as a means to advance their own self-interest.

The other theory, stewardship theory, assumes that the main concern of managers is to maximize the success of the organization [10]. Stewards see the concerns of the organization as their own, and they are willing to sacrifice their personal interests in order to maintain the viability and success of the firm in the long term. This attention to organizational effectiveness encourages stewards to focus on the long-term aspects of value creation rather than on the short term. Stewards understand that innovation, human capital, and stakeholder relations are investments that will be required for sustainable organizational success.

This distinction in goals is reflected in the time horizon used in managerial decision making. Agency theory suggests that managers will be short-term oriented and will focus on short-term performance results, such as quarterly earnings and other short-term performance measures that affect their compensation. In contrast, stewardship theory suggests that managers will be long-term oriented and make decisions that improve the firm's competitive position and generate value for the firm's long-term shareholders [5].

3.3. Control Mechanism

Contrasting conceptions of motivation and objectives create different prescriptions for governance and control. In agency theory, the recommended approach is based on monitoring and incentives [7]. Monitoring involves developing systems to track managerial behavior and ensure adherence to organizational goals. This could involve monthly or quarterly financial statements, third-party audits, and monitoring by the board of directors.

Stewardship theory, on the other hand, proposes a cooperative process of trust and empowerment [10]. Instead of having someone tell them what to do, a stewardship-based company allows managers more freedom and authority in making decisions, believing they will do what is beneficial to the company. These organizations also encourage a culture of participation and collaboration, engage employees at all levels of the organization in decision-making, and ensure that they have the resources and support they need to succeed.

Martin and Butler [8] point out that the effectiveness of these control mechanisms depends on managers' motivational orientation. When managers are driven mainly by external rewards, the need for monitoring and incentives to prevent opportunism is obvious. However, if they are intrinsically motivated, excessive monitoring and control can be counterproductive, as it undermines trust and reduces intrinsic motivation [2].

3.4. Organizational Style

Each theory has its own organizational structure and culture that reflect the differences in control mechanisms. Agency theory is linked with hierarchical organizations that are control-oriented, have central authority, clear lines of command, and formal rules and procedures [7]. These structures are put in place to enable monitoring and control and to help managers act in a manner consistent with shareholders' interests.

Stewardship theory is linked with organizations that are flat and involvement-oriented, have centralized power and flexible structures, and have collaborative cultures [10]. These organizational forms enable employees at every level to make decisions and take responsibility for their work, thereby fostering a sense of responsibility and commitment. Stewardship-minded organizations also possess excellent cultures with shared values, respect, and mutual success.

Empirical studies have revealed that each of these organizational structures has some associated performance outcomes. Hierarchical organizations are more efficient when the working environment is stable and predictable, with a focus on compliance and standardization. In contrast, flat, involvement-based organizations are more creative and flexible in dynamic, uncertain settings where innovation and initiative are essential [11].

4. A Game-Theoretic Analysis of Managerial Behavior Choice

For the purpose of better understanding the conditions under which managers choose to act as agents or stewards, this section develops a game-theoretic model of the strategic interaction between owners and managers. Game theory offers a formal framework for studying the influence of various incentive mechanisms and psychological factors on the behavior of rational individuals. The analysis uses standard game-theoretic concepts and incorporates insights from both agency theory and stewardship theory. Detailed Game-Theoretic Derivations can be seen in Appendix A.

4.1. The Basic Game Structure

The game involves two players: an owner (principal) and a manager (agent/steward). The owner has two possible strategies: to monitor the manager or to trust the manager. The manager also has two possible strategies: to act as an agent (to pursue self-interest) or to act as a steward (to pursue organizational interests).

The payoffs for each player depend on the combination of strategies chosen. The following notation is used to represent the payoffs:

- R_A: Total revenue generated when the manager acts as an agent
- R_S: Total revenue generated when the manager acts as a steward (RS > RA, as stewards are assumed to be more productive)
- $F_{(R)}$: Manager compensation, which is a function of total revenue (F'(R) > 0)
- α: Owner cost of monitoring the manager
- β: Penalty imposed on the manager if opportunistic behavior is detected
- V: Additional benefit the manager derives from acting as an agent (e.g., shirking, perquisites)
- $P_{(R):}$ Manager psychological satisfaction from achieving organizational goals (P'(R) > 0)
- T: Psychological cost to the manager of acting as an agent (e.g., guilt, fear of detection)

4.2. Agency Theory Game Model

We first analyze the game from an agency theory perspective. This perspective assumes that managers are motivated only by extrinsic rewards and that they have no psychological cost to acting opportunistically (P(R) = 0, T = 0). The payoff matrix for this game is shown in Table 2.

Table 2. Payoff Matrix for Agency Theory Game

		Owner	
		Monitor	Trust
Manager	Agent	$F(R_A) + V - \beta$, $R_A - F(R_A) - \alpha + \beta - V$	$F(R_A) + V$, $R_A - F(R_A) - V$
	Steward	$F(R_S)$, $R_S - F(R_S) - \alpha$	$F(R_S)$, $R_S - F(R_S)$

Source: Based on standard agency theory game models

The payoffs of this game are given in Table 2. Table 2 shows that the manager's payoff from being an agent is $F(R_A) + V - \beta$, and the payoff from being a steward is $F(R_S)$. When the owner trusts, the manager's payoff from acting as an agent is $F(R_A) + V$, while the payoff from acting as a steward is $F(R_S)$. The payoff for the owner to monitor is $R_A - F(R_A) - \alpha + \beta - V$; the payoff to the owner if he trusts is $R_A - F(R_A) - V$. When the manager acts as a steward, the payoff from monitoring is: $R_S - F(R_S) - \alpha$, while the payoff from trusting is: $R_S - F(R_S)$. β > V (the penalty for opportunism is greater than the benefit derived from it).

This pattern of strategic responses yields a mixed-strategy Nash equilibrium in which both players randomize their strategies. Let γ be the probability that the owner monitors, and let θ be the probability that the manager acts as an agent.

$\gamma_* = (F(R_S) - F(R_A) + V)/\beta$

$\theta_* = \alpha/\beta$

These findings have a number of implications. First, the likelihood that the owner monitors rises as the benefits to the manager of acting as an agent increase and falls as the costs of opportunism increase. This implies that owners will be more vigilant when the possibility of opportunism is high and the penalty is low. Second, the likelihood that the manager acts as an agent increases with the cost of monitoring and decreases as the penalty for opportunism increases. This indicates that the more costly the monitoring and the lower the penalties, the more likely managers are to behave opportunistically.

4.3. Integrated Agency-Stewardship Game Model

Now we extend the model to incorporate insights from stewardship theory by adding psychological factors to the manager's utility function. Specifically, we assume that managers derive psychological satisfaction from achieving organizational goals ($P(R) > 0$) and that they incur a psychological cost from acting opportunistically ($T > 0$). We also assume that excessive monitoring reduces the manager's intrinsic motivation, which leads to lower productivity when the manager is a steward and the owner monitors. Let R_M be the reduction in revenue when a steward is monitored, and let R_T be the increase in revenue when a steward is trusted. The payoff matrix for this integrated model is shown in Table 3.

Table 3. Payoff Matrix for Integrated Agency-Stewardship Game

		Owner	
		Monitor	Trust
Manager	Agent	$F(R_A) + P(R_A) + V - \beta - T$, $R_A - F(R_A) - \alpha + \beta - V$	$F(R_A) + P(R_A) + V - T$, $R_A - F(R_A) - V$
	Steward	$F(R_S - R_M) + P(R_S - R_M)$, $R_S - R_M - F(R_S - R_M) - \alpha$	$F(R_S + R_T) + P(R_S + R_T)$, $R_S + R_T - F(R_S + R_T)$

Source: Extended from agency theory model with stewardship theory insights

Under this integrated model, two pure-strategy Nash equilibria are possible, depending on the values of the parameters.

Equilibrium 1: Trust-Stewardship Equilibrium. This equilibrium occurs when the following condition holds: $F(R_S + R_T) + P(R_S + R_T) > F(R_A) + P(R_A) + V - T$

In this case, the manager's total utility from acting as a steward (including both financial compensation and psychological satisfaction) is greater than the utility from acting as an agent (including financial benefits, psychological satisfaction, and psychological costs). When the manager chooses to be a steward, the owner's best response is to trust, because trusting leads to higher revenue ($R_S + R_T > R_S - R_M$) and avoids the cost of monitoring.

If the manager decides to be a steward, the owner's best response is to trust, since it increases revenue and avoids the cost of monitoring. This equilibrium is the outcome that stewardship theory predicts: high organizational performance combined with high levels of trust and empowerment. It tends to occur when: the manager has high intrinsic motivation, the opportunity cost of opportunism is high, the productivity value of trust is high, and the value of acting as an agent is low.

- The manager has a strong intrinsic motivation ($P(R)$ is high)
- The psychological cost of opportunism (T) is high
- The productivity gain from trust (R_T) is high
- The benefit from acting as an agent (V) is low

Equilibrium 2: Monitor-Agency Equilibrium. This equilibrium occurs when the following condition holds: $F(R_A) + P(R_A) + V - \beta - T > F(R_S - R_M) + P(R_S - R_M)$

In this case, the utility to the manager of acting as an agent (even in the presence of monitoring) outweighs the utility of acting as a steward. When the manager decides to act as an agent, the owner's best response is to monitor; if the owner does not monitor, there is no way to impose penalties and thereby curb managerial opportunism. This is the outcome that agency theory recommends: monitoring and incentives to prevent opportunism. It is more likely to occur when: the manager is not intrinsically motivated, the opportunity for opportunism is limited, the productivity loss from monitoring is small, the benefit of being an agent is large, and the cost of opportunism is low.

- The manager has weak intrinsic motivation (P(R) is low)
- The psychological cost of opportunism (T) is low
- The productivity loss from monitoring (R_M) is low
- The benefit from acting as an agent (V) is high
- The penalty for opportunism (β) is low

4.4. Implications of the Game-Theoretic Analysis

The game-theoretic analysis demonstrates that these two theories, agency theory and stewardship theory, are not mutually exclusive: rather, they are two different equilibria that occur in different circumstances. It is important to note that whether managers act as agents or stewards depends not only on the nature of the manager, but also on the owner's strategy and the contextual environment. The analysis also demonstrates the importance of psychological factors in shaping managerial behavior. If managers are highly intrinsically motivated and incur high psychological costs from opportunism, they are more likely to act as stewards, and governance systems based on trust are more effective. Control-based governance systems are required, however, if managers are primarily extrinsically motivated and have a low psychological cost of opportunism. Furthermore, the analysis shows that the owner's decision-making style could have an impact on the manager's decision-making style. The owner's trust in and empowerment of the manager establishes a cycle of behavior that leads to high performance.

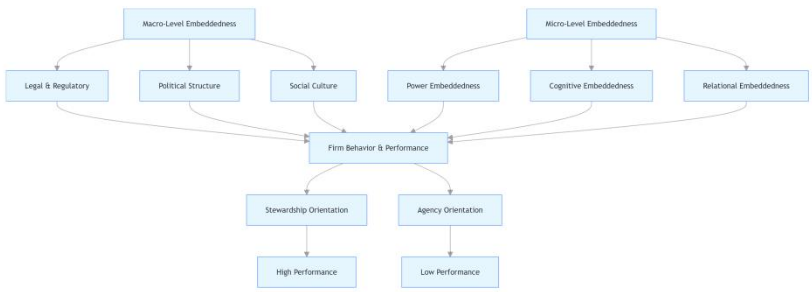
The results have significant implications for governance practice. Organizations should not use a blanket governance model; rather, they should create a form of governance that is suited to the motivational traits of their managers and the environment in which they work. This can be achieved by combining elements of agency theory and stewardship theory to arrive at a balance between curbing opportunism and fostering intrinsic motivation and commitment.

5. Contextual Boundaries: A Social Embeddedness Perspective

At the micro level, the game-theoretic analysis presented in the previous section has identified the psychological and situational factors that affect whether managers act as agents or stewards. However, wider social, cultural, and institutional factors also influence managerial behavior. The social embeddedness perspective was first developed by Granovetter [6] and states that economic action takes place within social relations and institutional arrangements, which frame the preferences, opportunities and constraints of actors.

This part of the paper examines the contextual boundaries of agency and stewardship theory from a social embeddedness perspective. Drawing on the work of Khanna and Yafeh [12] and others, we develop a dual embeddedness framework. This framework takes into account the embeddedness of firms in a family setting (micro-level embeddedness) and the embeddedness of families in wider social institutions (macro-level embeddedness). Figure 1 illustrates the dual embeddedness framework and its effects on firm behavior and performance.

Figure 1. Dual Embeddedness Framework



Source: Adapted from [6] and [12].

5.1. Micro-Level Embeddedness: The Firm-Family Interface

Micro-level embeddedness refers to the ways that firms are embedded in family structures and relationships. This is particularly important for family businesses, as family businesses are the prevailing form of business organization in most countries [14]. Family businesses are unique in that they can be managed according to business logic or family logic, which can lead to one of two forms of family behavior: stewardship and agency.

Three dimensions of micro-level embeddedness are identified: cognitive embeddedness, relational embeddedness, and power embeddedness. Cognitive embeddedness is the influence of the family's shared knowledge and worldview on the values, beliefs, and decision making of the organization [15]. Shared knowledge is shaped by family lineage, experiences, and traditions, and may influence the purpose and goals of the firm. High and positive cognitive embeddedness means that family members have a vision of the firm and feel that they are a part of it. The outcome is a stewardship orientation, as family members are motivated to maintain and grow the business for the next generation [16]. For instance, family companies with a long history of stewardship are more inclined to engage in initiatives that do not generate quick financial returns, such as research and development [5].

5.1.1. Cognitive Embeddedness

There are, however, also negative aspects of cognitive embeddedness. When the family's knowledge is outdated or there is a lack of consensus within the family about the direction the company should take, cognitive embeddedness can result in strategic inertia and conflict. This can lead to agency problems when family members act in their own self-interest at the firm's expense [11].

5.1.2. Relational Embeddedness

Relational embeddedness includes the type and strength of the relationships among family members involved in the firm, as well as the type and quality of the relationships between family and non-family workers [6]. Positive relationships based on trust and respect can foster a stewardship culture, as employees feel valued and develop a sense of responsibility for the organization's success.

In family businesses that are relationally embedded, relational loyalty of family members to the business is likely to be high, as is the degree of family interaction. This may lead to higher levels of organizational commitment, sharing of knowledge, and cooperation among the members of the firm and, in turn, higher firm performance [17]. Relationships with non-family members can also be developed, which can lead to increased trust and involvement.

The other extreme is poor or conflicting relationships, which can result in agency behavior. When there is disagreement and conflict among family members, they may use the firm as a weapon in their family conflicts. This results in suboptimal decisions and suboptimal performance [18]. Non-family staff can also feel left out or undervalued, resulting in reduced motivation and higher turnover.

5.1.3. Power Embeddedness

Power embeddedness concerns the allocation of ownership, control, and decision-making power within the organization, particularly between family members and other stakeholders [15]. The effect of power distribution on the firm's governance and behavior is substantial.

When a family member or a small group of family members exercises control over the entire firm with a long-term commitment to its success, a strong stewardship orientation and efficient decision making are more likely to emerge [19]. This is especially the case for founder-controlled companies, where the founder is personally invested in the business and wants to create a legacy.

But agency problems can also occur because of the exercise of concentrated power. This is a problem when the controlling family does so at the expense of minority shareholders to obtain private benefits. This is referred to as the "principal-principal" agency problem, which is especially common in emerging markets with poor investor protection [9]. For instance, controlling families can engage in tunneling activities such as related-party transactions to siphon value out of the company, thereby lowering the value of minority shareholders' investments.

5.2. Macro-Level Embeddedness: The Family-Society Interface

Macro-level embeddedness concerns the embeddedness of families and their enterprises within wider social institutions such as legal and regulatory frameworks, political systems, and culture. These institutions operate at the level of the overall economy and shape the environment in which firms operate. They also shape the costs and benefits of various governance practices and the relative effectiveness of agency theory and stewardship theory.

We distinguish three types of macro-level embeddedness: legal and regulatory embeddedness, political structure embeddedness, and social culture embeddedness.

5.2.1. Legal and Regulatory Embeddedness

Legal and regulatory embeddedness refers to the formality of the laws and regulations that govern corporate behavior, specifically investor protection, corporate governance, and taxation [14]. The strength of the legal system has a profound impact on the relative effectiveness of agency-oriented and stewardship-oriented governance practices.

Where laws provide good protection for investors, expropriation by controlling families is not a major risk, and minority shareholders are more willing to invest in family firms. This reduces the need for families to closely supervise the company. It enables them to entrust decision making to professional managers and to use a more stewardship-based approach to governance [20].

In common law countries such as the United States and the United Kingdom, for instance, family companies are more likely than in civil law countries to be professionally managed and to have dispersed ownership.

In contrast, in countries where investors are not legally protected, controlling families face little risk of legal action for expropriating minority shareholders. This gives the family a strong incentive to manage the firm closely to protect its own interests and to adopt more agency-oriented governance practices [21]. For example, family companies in many developing countries use dual-class shares and pyramidal structures to gain control of the company with a minimal equity stake. This enhances the possibility of tunneling and other forms of expropriation.

Taxation policies also play an important role in corporate governance. For example, a high inheritance tax can drive families out of the business, leading to the fragmentation of family ownership and more diffuse ownership of the firm [22]. Conversely, if preserving family business is the objective, tax policies that favor family enterprises can lead to centralization of control and ownership.

5.2.2. Political Structure Embeddedness

Political structure embeddedness focuses on family firms' interactions with the political system, such as the degree of family influence and the kind of government policies that are implemented in the economy [12]. Positive and negative effects of political connections on firms' behavior and performance exist.

In some cases, political connections can provide family firms with valuable resources such as access to capital, government contracts, and regulatory favors. This can improve the firm's competitiveness and performance, especially in developing regions with weak institutions. However, political connections can also lead to agency problems when families use their political influence to extract rents from the government or to protect themselves from competition [23].

The relationship between political structure and corporate governance is complex and depends on the context. In Sweden, for instance, large family businesses can be said to have formed a symbiotic relationship with the social democratic government. They have received political support and protection from the government in return for undertaking social welfare policies [24]. This has resulted in a distinctive corporate governance model of family control with a strong focus on stakeholder interests.

However, in many developing countries, having political connections has been found to be positively correlated with corruption and rent seeking. Infrastructure projects run by connected government-owned companies may operate as monopolies or be exempt from regulation. This results in inefficiency and less competition [12]. This can lead to opportunistic and agency behavior, as firms focus on rent extraction rather than value creation.

5.2.3. Social Culture Embeddedness

Social culture embeddedness is the impact of cultural norms, values, and beliefs on family firm behavior and governance [25]. Authority, trust, and individualism/collectivism are shaped by culture. This, in turn, impacts the effectiveness of various governance practices.

Collectivist cultures with a strong emphasis on group harmony and loyalty tend to be more conducive to stewardship-oriented governance practices. In collectivist societies, family members are more likely to feel integrated into the firm and to focus on the interests of the firm rather than their own [11]. For instance, family businesses in many Asian countries are known to be deeply loyal to the family and to have a long-term perspective; these traits are linked to higher levels of stewardship behavior.

Individualist cultures, on the other hand, emphasize individual autonomy and self-interest. Agency theory's assumptions about human behavior are more applicable in individualist societies, where control-based governance practices are more effective. Corporate governance in the United States, for instance, is largely based on agency theory principles, in which the primary concern is shareholder value and performance-based pay.

Religion also influences cultural values and corporate governance to a significant extent. Stulz and Williamson [25] found that countries with a Protestant majority have better investor protection than countries with a Catholic majority. This is because Protestant individualism and accountability are more conducive to the development of strong legal institutions and sound corporate governance practices.

5.3. Contextual Boundaries Summary

The dual embeddedness framework reveals how agency theory and stewardship theory can or cannot be applied depending on various micro- and macro-level factors. Table 4 summarizes the conditions under which each theory is more likely to be applicable.

Table 4. Contextual Boundaries of Agency and Stewardship Theory

Contextual Dimension	More Applicable to Agency Theory	More Applicable to Stewardship Theory
Firm Characteristics		
Ownership Structure	Dispersed ownership	Concentrated family ownership
Firm Size	Large, mature firms	Small, entrepreneurial firms
Industry	Traditional, low-innovation industries	High-tech, knowledge-intensive industries
Manager Characteristics		
Motivation	Extrinsically motivated	Intrinsically motivated
Identification	Low organizational identification	High organizational identification
Risk Preference	Risk-averse	Risk-taking
Institutional Environment		
Legal Protection	Strong investor protection	Weak investor protection
Political System	Transparent, market-oriented	Interventionist, relationship-based
Culture	Individualist	Collectivist

Source: Compiled from[12], [14], and [25].

Agency theory has greater applicability in large, mature firms with dispersed ownership, operating in traditional industries and individualistic cultures with strong legal protection. Stewardship theory, however, is more relevant to small, entrepreneurial companies in which ownership is closely held by a family and legal protection is weak, such as knowledge-intensive businesses in collectivist cultures.

Contextual boundaries are not limited to family firms but also apply to other organizational structures. Stewardship theory is well suited to high-tech start-ups in which ownership is concentrated and owners are highly motivated, whereas agency-based monitoring and incentive alignment are needed in mature, publicly listed corporations that face pressure from quarterly earnings reporting and have widely dispersed ownership. State-owned enterprises are a mixed case: they have a high degree of state ownership, which creates potential for good stewardship, but they also have multiple-principal problems, which can give rise to serious agency problems. Beyond adapting the governance mix to the institutional context, multinational corporations need to adapt to the local legal and cultural contexts in which they operate, rather than relying on a pre-designed global template. This suggests that neither theory is always superior, as the applicability of each depends on the interaction among three factors: ownership structure, industry characteristics, and institutional embeddedness.

Note that these are general trends and that there is significant variation within each trend. In some large publicly listed companies, for instance, stewardship-oriented governance has been implemented successfully, whereas some family firms continue to face severe agency problems. Understanding the interplay between the micro and macro contexts and how they influence managerial actions and the outcomes of various governance mechanisms is key.

6. An Integrated Dynamic Governance Framework

The preceding analysis has shown that agency theory and stewardship theory are not mutually exclusive, but are actually complementary perspectives that can be applied under different contextual conditions. This section proposes an integrated dynamic governance framework that combines elements from both theories, in order to help organizations design governance systems that are suitable for their context.

6.1. The Core Principles of Integrated Governance

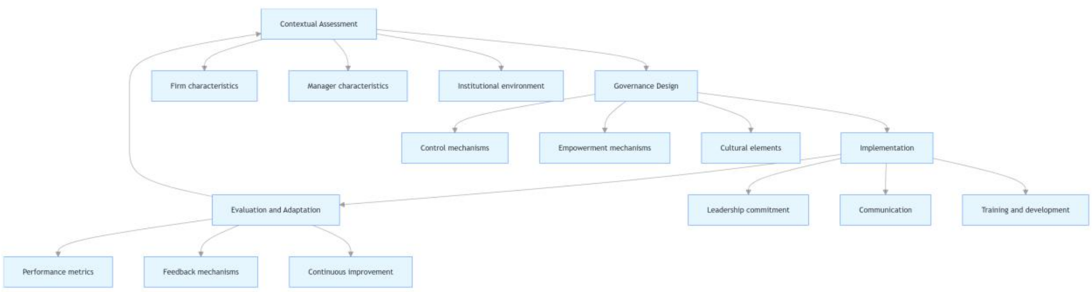
The integrated governance framework is based on three core principles:

Contextual Fit: The governance system must be adapted to the context in which the organization operates (size, industry, ownership, institutional context). Governance is not one-size-fits-all. Dynamic Adaptation: Governance systems should be dynamic and flexible, evolving with the organization and the context in which it operates. What works in the early development of a firm may not be appropriate at a later stage of its development. Balanced Approach: Effective governance involves a balance between control and collaboration. To avoid opportunism, organizations must establish boundaries and accountability and put in place measures that build trust, empowerment, and intrinsic motivation, thereby ensuring innovation and long-term performance.

6.2. The Integrated Governance Framework

Figure 2 presents the integrated dynamic governance framework, which consists of four interrelated components: contextual assessment, governance design, implementation, and evaluation.

Figure 2. Integrated Dynamic Governance Framework



Source: Developed for this study

6.2.1. Contextual Assessment

The first step in designing an effective governance system is to conduct a thorough contextual assessment. This means analyzing the organization's characteristics, the motivational traits of its managers and employees, as well as the broader institutional environment in which it operates.

Questions that should be considered in the contextual assessment include: What is the size, age and industry of the organization? What is the ownership structure of the organization? What are the motivational traits of the top management team? How trusting and informal are the relationships among workers? What is the strength of the legal and regulatory framework? Which cultural norms and values influence the behavior of the organization and its environment?

The results of the contextual assessment will help to determine the appropriate balance between control and empowerment in the governance system.

6.2.2. Governance Design

Based on the contextual assessment, organizations can develop a governance system that incorporates elements of both agency theory and stewardship theory. Control mechanisms, empowerment mechanisms, and cultural elements should be included in the governance system.

Control Mechanisms: These are derived from agency theory and aim to deter opportunism and hold people accountable. These are: clear roles and responsibilities, performance measurement and reporting systems, financial controls, financial audits, board oversight, and performance-based compensation.

Empowerment Mechanisms: These elements are inspired by stewardship theory and are designed to foster intrinsic motivation and commitment. They include: delegation of decision-making authority, employee participation in decision-making, training and development opportunities, mentoring and coaching programs, and work-life balance initiatives.

Cultural Elements: Culture is important in influencing behavior and in strengthening the governance system. The following traits should be fostered within an organizational culture: shared values and purpose, trust and mutual respect, transparency and open communication, ethical behavior, and long-term orientation.

These components will vary according to the contextual assessment. In a situation where agency problems are more likely, for example, the governance system should place greater emphasis on control mechanisms. More attention should be given to empowerment and cultural mechanisms in a context where stewardship behavior is more likely.

6.2.3. Implementation

Effective implementation of any governance system is vital to its success. Strong leadership commitment, communication, and continuous training and development efforts are needed.

Leadership commitment is crucial to ensuring that the governance system is taken seriously and followed throughout the organization. Leaders must set an example for others and act with integrity and accountability, in line with the organization's values.

In addition, communication is of paramount importance, so that all staff are aware of the governance system and their role and responsibilities in it. The reasons for the governance system, and the benefits it will bring to the organization and its employees, need to be explained.

Training and development can help employees acquire the skills and knowledge needed to succeed in an empowering and participatory governance system. This might include the acquisition of decision-making, communication, teamwork, and ethical skills.

6.2.4. Evaluation and Adaptation

Governance systems should be continuously evaluated to gauge their effectiveness and identify areas for improvement. This includes financial and non-financial performance indicators, as well as feedback from staff, managers, and other stakeholders.

Some of the key performance indicators that should be considered are:

- Financial performance (e.g., revenue growth, profitability, return on investment)
- Financial and environmental sustainability (e.g., profitability, environmental impact).
- Employee performance (e.g., productivity, efficiency, job quality)
- Governance outcomes (e.g., compliance, ethical behavior, stakeholder trust)

Based on the evaluation findings, organizations should make appropriate changes to their governance systems. This may involve making small adjustments to the control and empowerment mechanisms, adjusting a particular mechanism, or altering the cultural elements of the system. The governance system should be seen as dynamic and continuously evolving rather than as a static set of rules and processes.

6.3. Practical Implications for Organizations

The integrated dynamic governance framework has a number of practical implications for organizations:

1. Abandon the notion of agency vs stewardship theory: Organizations should move beyond the binary thinking that pits agency theory against stewardship theory. Rather, they must recognize that both theories are valid and that a balanced approach is needed for effective governance.

2. No one-size-fits-all governance – there is no standard governance model that works for every organization. Governance systems should be tailored to the specific circumstances of each organization, taking into account its context, unique characteristics, and the environment in which it operates.

3. Invest in Culture: Culture is an important part of effective governance. It is crucial that organizations invest in fostering a strong culture based on shared values, trust, and ethics. A positive culture can lessen the need for formal controls, and can encourage intrinsic motivation and commitment.

4. Build Leaders at All Levels: Good governance has to be underpinned by good leadership at every level. It is important that organizations invest in building leaders who are able to both control and empower while also inspiring and motivating others to attain organizational objectives.

5. Embrace Continuous Improvement: Governance is not a one-time event but an ongoing process. Governance systems need to be regularly assessed and adapted to ensure that they continue to be effective in an evolving landscape.

7. Conclusion

This paper has examined the salient differences between agency theory and stewardship theory, as well as their contextual boundaries and areas of overlap, through a game-theoretic analysis and the social embeddedness perspective. The analysis has shown that the two theories predict different equilibria—so-called Nash equilibria—which can be reached under different psychological and situational conditions. Furthermore, the applicability of each theory is not universal, as it depends on multiple micro-level (organizational) and macro-level (institutional) factors.

The main contributions of this paper are threefold. First, it provides a systematic comparison of agency theory and stewardship theory and clarifies the distinctions between them and the assumptions underlying each. Second, it develops a dual embeddedness framework—encompassing both micro-level and macro-level perspectives—to identify the contextual factors that determine the applicability of each theory. Third, it proposes an integrated dynamic governance framework, combining elements from both theories, to help organizations develop governance systems appropriate to their context.

The results of this study have some implications for research and practice. For researchers, this study highlights the importance of transcending the binary approach to the study of corporate governance and of developing more contextual and comprehensive theories. The integrated framework proposed in this paper should be empirically tested in the future to examine the impact of contextual variables on the effectiveness of different governance practices.

For practitioners, this study provides practical guidance on how to create governance systems that strike a balance between control and collaboration. With governance that is tailored to their situation and is flexible and adaptable, organizations can improve their performance and create lasting value for their shareholders and stakeholders.

The present study contributes to agency theory and stewardship theory, but it has certain limitations. First, the analysis is largely theoretical, and there is a need for empirical research to test the propositions advanced in this paper. Second, the integrated framework is fairly general and further guidance is required on how it can be applied to specific contexts. Third, the study is mainly concerned with the owner–manager relationship, and future studies should consider the framework's applicability to other stakeholder relationships.

Despite these limitations, this study is a step toward reconciling agency theory with stewardship theory and building a more complete understanding of corporate governance. In an increasingly complex and dynamic world, understanding the complementary nature of these two perspectives and the importance of context can help create more effective, flexible, and responsive governance systems for organizations and their stakeholders.

Funding

No.

Data Availability Statement

Not applicable.

Acknowledgments

No.

Conflicts of Interest

The authors declare no conflicts of interest.

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Appendix A: Detailed Game-Theoretic Derivations

A.1. Derivation of Mixed Strategy Nash Equilibrium for Agency Theory Game

The mixed strategy Nash equilibrium occurs when each player is indifferent between their two strategies, given the probability distribution of the other player's strategies.

For the manager to be indifferent between acting as an agent and acting as a steward, the expected utility from both strategies must be equal:

$$\gamma \cdot [F(R_A) + V - \beta] + (1 - \gamma) \cdot [F(R_A) + V] = \gamma \cdot F(R_S) + (1 - \gamma) \cdot F(R_S) \quad (1)$$

Simplifying the right-hand side:

$$\gamma \cdot F(R_S) + (1-\gamma) \cdot F(R_S) = F(R_S) \quad (2)$$

Simplifying the left-hand side:

$$\gamma F(R_A) + \gamma V - \gamma\beta + F(R_A) + V - \gamma F(R_A) - \gamma V = F(R_A) + V - \gamma\beta \quad (3)$$

Setting the two sides equal:

$$F(R_A) + V - \gamma\beta = F(R_S) \quad (4)$$

Solving for γ:

$$\gamma * = (F(R_S) - F(R_A) + V)/\beta \quad (5)$$

For the owner to be indifferent between monitoring and trusting, the expected utility from both strategies must be equal:

$$\theta \cdot [R_A - F(R_A) - \alpha + \beta - V] + (1-\theta) \cdot [R_S - F(R_S) - \alpha] = \theta \cdot [R_A - F(R_A) - V] + (1-\theta) \cdot [R_S - F(R_S)] \quad (6)$$

Simplifying both sides:

$$\theta R_A - \theta F(R_A) - \theta\alpha + \theta\beta - \theta V + RS - F(R_S) - \alpha - \theta R_S + \theta F(R_S) = \theta R_A - \theta F(R_A) - \theta V + RR_S - F(R_S) - \theta R_S + \theta F(R_S) \quad (7)$$

Canceling out common terms:

$$-\theta\alpha + \theta\beta - \alpha = 0 \quad (8)$$

Solving for θ:

$$\theta(\beta - \alpha) = \alpha \quad (9)$$

$$\theta_* = \alpha/\beta \quad (10)$$

A.2. Derivation of Pure Strategy Nash Equilibria for Integrated Game

Trust-Stewardship Equilibrium

For this equilibrium to exist, two conditions must hold:

1. Given that the owner trusts, the manager prefers to be a steward:

$$F(R_S + R_T) + P(R_S + R_T) > F(R_A) + P(R_A) + V - T \quad (11)$$

2. Given that the manager is a steward, the owner prefers to trust:

$$R_S + R_T - F(R_S + R_T) > R_S - R_M - F(R_S - R_M) - \alpha \quad (12)$$

Since $R_S + R_T > R_S - R_M$ *and* $F'(R) > 0$, *the second condition is always true as long as* $\alpha > 0$. *Therefore, the first condition is sufficient for the trust-stewardship equilibrium to exist.*

Monitor-Agency Equilibrium

For this equilibrium to exist, two conditions must hold:

1. Given that the owner monitors, the manager prefers to be an agent:

$$F(R_A) + P(R_A) + V - \beta - T > F(R_S - R_M) + P(R_S - R_M) \quad (13)$$

2. Given that the manager is an agent, the owner prefers to monitor:

$$R_A - F(R_A) - \alpha + \beta - V > R_A - F(R_A) - V \quad (14)$$

Simplifying the second condition:

$$-\alpha + \beta > 0 \Longrightarrow \beta > \alpha \quad (15)$$

This is one of our standard assumptions, so the first condition is sufficient for the monitor-agency equilibrium to exist.

Source: Derived from standard game-theoretic principles