

Emerging Markets Corporate Governance Research Network (EMCGN) Newsletter

February 2011

[From Our Chair](#)

Dear Colleagues,

This newsletter is the first in a new series from the Emerging Markets Research Network. Its purpose is to update members and others interested in corporate governance in emerging markets on recent research and upcoming events. The newsletter will identify and summarize recently published articles in key journals and working papers. It will focus on identifying those papers with important implications for reforms or practice. It will also serve to inform the network of corporate governance researchers and practitioners about new events (conferences and workshops) on corporate governance in emerging markets.

I think this newsletter will be a good first step to fill a gap internationally. It will help disseminate valuable work and activities on corporate governance in emerging markets. Conversely, the newsletter will be a good tool to increase collaboration and communication among members of the Emerging Markets Research Network. Accordingly, I encourage Network members to inform us of any publications, events, or other information to be included. Looking forward to hearing from you!

Stijn Claessens, University of Amsterdam

[In this Issue](#)

In this issue, we first highlight a review, by J.P.H. Fan and his co-authors, of the ongoing corporate governance research in the emerging markets. Let us remind you that this outstanding paper is recently published in *Journal of Corporate Finance*. We then follow in the Publications section with two papers that aim to identify the channels, through which firm-level corporate governance affects firm performance in India and Korea. These two papers by Bernard Black and his distinguished co-authors aim to enlighten the relationship between firm-level governance and firm value. The paper on Korea follows a line of earlier investigations. Ararat and Yurtoglu's investigation of the effect of board independence on firm performance in Turkey contributes to the same endeavour by looking at the effects of independent directors. They find controversial results, which challenge the usefulness of independent directors as internal corporate governance devices in Turkey. Howson and Khanna examine a phenomenon observed in many countries: the persistence of business organizations and ownership structures to changes in capital markets laws. We conclude the Publications section with a paper by Hamdani and Yafeh, who explore the corporate governance role of institutional investors in Israel—a market where concentrated ownership and business groups are quite common.

We are happy that all of the papers we have selected for this issue are authored by members of our Network. It wasn't deliberate! On the other hand, we are absolutely sure that we still missed some important papers. Please help us with the next issue by drawing our attention to papers that serve our purpose. This newsletter is distributed to more than 3,000 researchers, regulators, and practitioners. We hope that, with your help, it will contribute to the appreciation of the role of science in this crucial field.

Publications

Corporate Finance and Governance in Emerging Markets: A Selective Review and an Agenda for Future Research

Joseph P.H. Fan, K.C. John Weib, and Xinzhong Xu

J. Fan, J. Wei and X. Xu propose a neat top-down approach to identifying the factors that shape structures and behaviours of firms in the emerging markets differently from the ones in the developed markets. The authors also pinpoint a wide array of prior studies that identify government quality, state ownership, and financial development as critical institutional effects that shape the financing and governance of emerging market firms. Additionally, they suggest that future research should pay close attention to unanswered topics such as informal enforcement, government incentives, family firms, and network organizations.

http://ihome.cuhk.edu.hk/~b109671/doc/research_published_paper/17.pdf

Institutional Investors as Minority Shareholders

Assaf Hamdani, Yishay Yafeh

Using a hand-collected Israeli dataset, the authors aim to explain the corporate governance role of institutional investors in a market where concentrated ownership and business groups are common. Institutional owners have only a limited role as minority shareholders. Furthermore, the presence of certain types of influential families creates new potential conflicts of interest for institutional investors. The authors establish the following facts: (i) legal intervention plays an important role in shaping the vote behaviour, (ii) voting against company proposals is more likely in compensation-related proposals, even when institutional investors are unlikely to influence the outcomes, (iii) institutional investors that have certain business activities or that are affiliated with public companies are more likely to support insider-sponsored proposals than “pure-play” standalone investors, (iv) large firms tend to enjoy a more favourable treatment from institutional investors, whereas firm performance has no affect on voting, and (v) for the institutions to play a role in corporate governance, what matters most is not the legal power granted to minority shareholders but rather the absence of conflicts of interest.

http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1641138

The Relation between Firm-Level Corporate Governance and Market Value: A Study of India

N. Balasubramanian, Bernard S. Black, Vikramaditya Khanna

The authors provide an overview of the practices of publicly traded Indian firms and identify where corporate governance practices are relatively strong or weak. In addition, they build a broad Indian Corporate Governance Index (ICGI) and examine its relationship to firm market value. They find a positive and significant association between ICGI and firm market value in India, which is consistent with prior research in other countries. The result is more significant in the more profitable firms. However, a subindex for board structure is insignificant, along with disclosure, board procedure, and related party transactions. The nonresults for board structure contrast with other recent studies, and suggest that India's legal requirements are so strict that overcompliance does not produce valuation gains.

http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1586460

How Corporate Governance Affects Firm Value: Evidence on Channels from Korea

Bernard Black, Woochan Kim, Hasung Jang, Kyung-Suh Park

This is an update on an article that has been in circulation since 2005. Using their Korean Corporate Governance Index (KCGI), the authors first confirm the association between corporate governance and value, and then they provide the channels through which corporate governance affects the firm value. Governance may produce either a higher firm value without higher overall firm value, through reduced benefits to insiders, or it may produce a more efficient operation and hence an increase in the overall firm value. They find evidences for the following channels for firms with higher KCGI: (i) related party transactions are less adverse to firm value; (ii) firm profitability is more sensitive to shocks to industry profitability, suggesting reduced tunneling for insiders; (iii) capital expenditures are lower, but investment is more sensitive to profitability and growth opportunities; (iv) sales growth is lower; (v) profitability is more sensitive to growth opportunities; (vi) lagged board structure predicts higher profitability; and (vii) dividends are higher, controlling for profits, and are more sensitive to profits. The first two channels are consistent with governance producing reduced insider tunneling of profits; the remainder are consistent with governance producing higher overall firm value.

http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1365945

The Effects of Board Independence in Controlled Firms: Evidence from Turkey

Melsa Ararat, Hakan Orbay, Burcin Yurtoglu

The authors analyze the relationship between board structure and firm performance for a sample of companies in Turkey. Their conclusions suggest the following: (i) board independence is unrelated to equity issues, (ii) independent directors are unlikely to curb the extent of related party transactions, and (iii) the presence of independent board members and firm performance are negatively correlated. The last two findings challenge the usefulness of independent directors as internal corporate governance devices in Turkey. The policy implications of these findings are related to the quality of independent directors and their incentives. On the quality of independent directors side, boards can be mandated to identify and nominate independent members. Introduction of a classified voting system can be an alternative approach. On the incentives side, reputational concerns can motivate directors, if development of a market for human talent can be supported by making a certain level of independence mandatory.

http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1663403

The Development of Modern Corporate Governance in China and India

Nicholas Howson, Vikramaditya Khanna

Both China and India cases suggest that the “legal origins” (common law or civic law) account doesn’t provide the best explanation for the development of their corporate governance templates or domestic capital markets. Rather, a nuanced political “account” provides a greater explanatory power. Despite a good deal of evidence of partial formal convergence in corporate law, they cannot identify convergence in ownership or corporate structure. This creates an odd fit between corporate and securities law and the corporations they shape and regulate, suggesting some path dependence.

http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1687757

Upcoming Events

Fourth Annual Academic Conference on Corporate Governance will be held on April 1, 2011, in Drexel University in the United States.

<http://www.lebow.drexel.edu/Event/2011CallforPapers>

The Third International Conference on Corporate Governance in Emerging Markets will be held May 28–29, 2011, in Korea.

<http://www.gcgf.org/ifcext/cgf.nsf/Content/Call2011>

Yale Governance Forum will be held June 16–17, 2011, in the United States.

<http://millstein.som.yale.edu/>

The European Academy of Management (EURAM) Annual Conference, Management Culture in the 21st Century, will be held July 1–4 in Tallinn, Estonia.

http://www.euram2011.org/r/default.asp?iId=EJHIDF#Corporate_Governance

Opinions

How Can Financial Supervisors Improve the Effectiveness of Corporate Governance? This paper by John Palmer and Chang Su Hoong suggests measures that financial supervisors can take to improve governance in regulated financial institutions.

http://www.gcgf.org/ifcext/cgf.nsf/Content/PSO_18

From Our Coordinator

Dear EMCGN Members,

We encourage all of our members to notify us regarding their ongoing research or the events or conferences they want to share with the Network. We also welcome other relevant information, your feedback, and suggestions for ways to improve this newsletter.

Please get in touch with Mehmet Ihsan Canayaz, our Associate Editor, for potential contributions or inquiries, using the contact information below. Your contributions are greatly appreciated.

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Meanwhile, we are happy to note that more than 200 papers were submitted for the Korea Conference. The organizing committee is looking forward to seeing you all in Seoul.

Melsa Ararat, Sabanci University

The Emerging Markets Corporate Governance Research Network is supported by the Global Corporate Governance Forum, the leading knowledge and capacity building platform dedicated to corporate governance reform in emerging markets and developing countries. The Forum is a multi-donor trust fund facility located within the IFC, co-founded in 1999 by the World Bank and the Organisation for Economic Cooperation and Development (OECD). For more information about the Forum's activities and publications, visit GCGF's website www.gcgf.org. For more information about the EMCGN's activities, go to <http://www.gcgf.org/ifcext/cgf.nsf/Content/Research> or contact melsaararat@sabanciuniv.edu.