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Asian Corporate Governance Association (ACGA)

"The Benefits of Corporate Governance to Emerging Economies"

Jamie Allen
Secretary General, ACGA, Hong Kong

Corporate Governance Seminar
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Bahrain
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Agenda

1. What drives corporate governance reform?
2. Development of corporate governance in Asia.
3. The benefits of corporate governance to emerging economies.

1. What drives corporate governance reform?

- Financial crises and corporate scandals
  - National
  - International
- Financial integration among nations
  - International regulatory institutions
  - Standardisation of principles and rules
  - Cross-border trade and investment
- Changing share-ownership structures
  - The growth of pension, mutual and other institutional fund managers
  - Internationalisation of the shareholder base of listed companies

Factors underlying reform

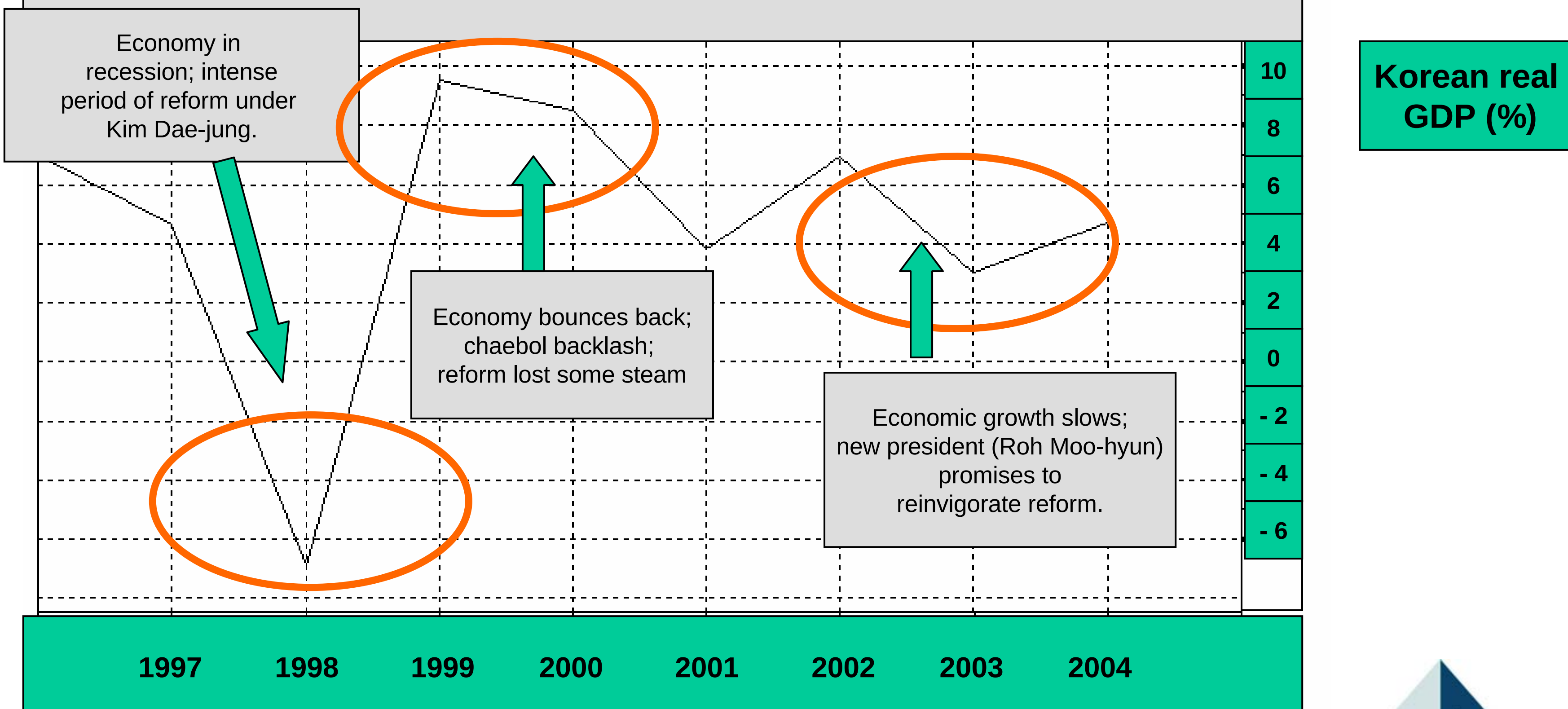
- A failure of trust (and the need to regain it)
- The need to communicate across borders, cultures and languages
- Changing nature and geography of property rights

The First Century of CG

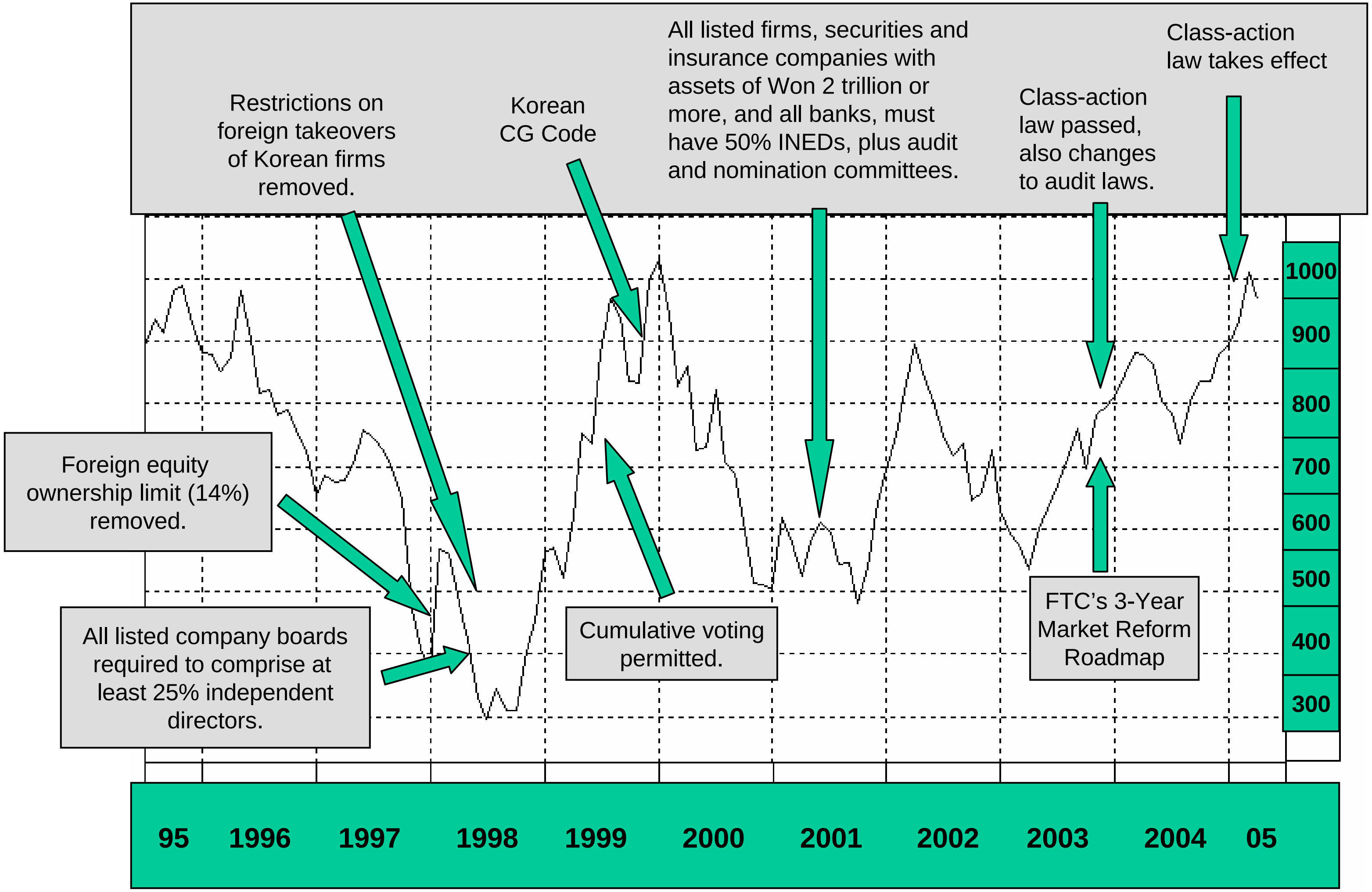
- **Late 19th century to 1926:**
  - Financial crises and scandals prompted New York Stock Exchange (NYSE) to issue rules on substantial financial disclosure, distribution of annual reports, annual shareholder meetings, quarterly reporting, and "one-share, one-vote".
- **1929 to late 1950s:**
  - Great Crash of 1929, followed by the mandating of independent audits in 1932, then US Securities Act of 1933 and the Securities Exchange Act of 1934. NYSE rule on two outside directors in 1956.
- **1970s:**
  - Bankruptcy of Penn Central, largest railroad in US, in 1970; followed by oil shock of 1973. Audit committees with independent directors required by NYSE in 1977.
- **Late 1980s/early 1990s:**
  - Mirror Group and other scandals in the UK led in 1992 to the "Cadbury Report", a basic template for corporate governance codes.
- **1997/98:**
  - Asian Financial Crisis led to "convergence" with global standards.

Example: Korea

Corporate governance reform began after a recession (and was then impeded by a return to growth).



Kospi Index (1995-2005) & CG Reforms



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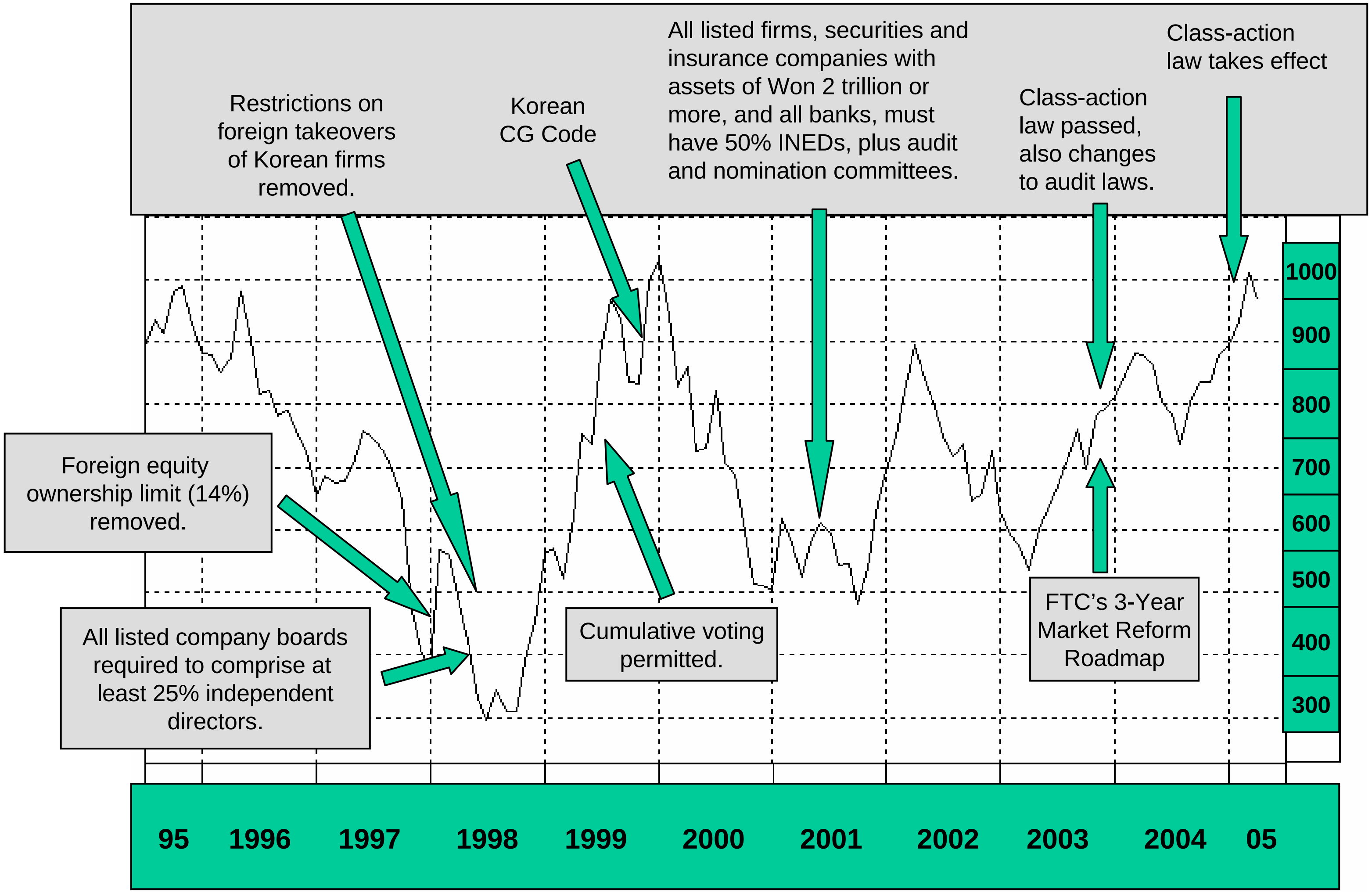

2. Development of CG in Asia

The state of play in 1997			
Country/market	**Was there an official code of best practice?**	**Did the idea of the "independent director" exist?**	**Did the idea of the audit committee exist?**
China			
Hong Kong	Yes (but very short)	Yes	Yes
India			
Indonesia			
Japan			
Korea			
Malaysia		Yes	Yes
Philippines			
Singapore		Yes	Yes
Taiwan			
Thailand			

Source: ACGA research

Today

Country	Date of main code(s)	Are independent directors required?	Are audit committees required?
China	2002/2005	Yes	Yes
Hong Kong	1993/2004	Yes	Yes
India	1999/2005/2007	Yes	Yes
Indonesia	2001/2006	Yes	Yes
Japan	(2003)/2004	Optional	Optional
Korea	1999/2003	Yes	Yes (large firms)
Malaysia	2001/2007	Yes	Yes
Philippines	2002	Yes	Yes
Singapore	2001/2005	Yes	Yes
Taiwan	2002	Yes (certain firms)	Yes (certain firms)
Thailand	1999/2006	Yes	Yes

3. Benefits of CG to emerging economies

- **Economic development in emerging economies is based on a combination of factors:**
  - Investment (direct and portfolio)
  - Growing export markets (good and services)
  - Economic policies that foster entrepreneurialism
  - A government that can keep corruption under control—or is at least trying its best
  - An increasingly credible set of laws and regulations governing economic interaction
  - Ongoing capacity building within government and legal institutions (including the judiciary)

What is the link to corporate governance? How can it help?

Trust

Area	How sound governance builds trust and economic value:
Investment	• Higher standards of corporate governance raise the long-term confidence of public-equity institutional investors, both domestic and foreign, in countries and companies. This in turn influences liquidity. (Why are most listed companies so small?)
Exports	• Addressing "ESG" issues and reporting on them strengthens trust in your supply chain and helps your company avoid becoming a target of criticism or vilification (eg, for your labour or environmental policies and practices). • Greater transparency can open up export markets (eg, where the product is a customised service and reliability and quality are paramount). Why would foreign customers rely on service providers they do not know or trust?
Corruption	• Private-sector governance reform helps to focus attention on public-sector governance and corruption. Sustained economic and capital market development requires minimising the negative effects of corruption. This in turn requires a clean legal and judicial system.

Communication

Area	How sound governance aids communication:
Investment	• In early stage foreign direct investment (FDI), especially in joint ventures, a greater commitment to transparency and a willingness to discuss issues/risks at the board level can help to avoid some of the common problems that affect later stage FDI. •Both public- and private-equity investors need timely and frequent disclosure of corporate results and material information to make informed investment decisions. Standardisation of rules and best practices across national borders lowers transaction costs and allows investors a wider array of investment choices—and companies a broader range of financing options.
Entrepreneurialism	• Entrepreneurs seeking private equity funding or that plan to undertake an IPO will benefit from taking corporate governance seriously.

Property rights

Area	How sound governance strengthens property rights:
Investment	• Strong systems of corporate governance enhance the legal rights of shareholders and allow them to play their rightful part in the governance of companies (eg, by voting shares, attending meetings, engaging with management). Many large institutional investors now have policies that explicitly recognise their fiduciary duties to beneficial owners and require specific actions to be taken.
Regulatory system	• Effective regulatory institutions are a basic feature of strong corporate governance regimes. They help to build investor confidence and protect property rights. Strong capital markets depend upon trust and credibility.

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Comparing corporate governance in Asia

Scores from “CG Watch 2007”

Market	CG Rules & Practices	Enforcement	Political/ Regulatory	IGAAP	CG Culture	TOTAL
1. Hong Kong	60	56	73	83	61	67
2. Singapore	70	50	65	88	53	65
3. India	59	38	58	75	50	56
4. Taiwan	49	47	60	70	46	54
5. Japan	43	46	52	72	49	52
=6. Korea	45	39	48	68	43	49
=6. Malaysia	44	35	56	78	33	49
8. Thailand	58	36	31	70	39	47
9. China	43	33	52	73	25	45
10. Philippines	39	19	38	75	36	41
11. Indonesia	39	22	35	65	25	37

Source: “CG Watch 2007”, ACGA & CLSA Asia-Pacific Markets

Figures in %

Contact details

Jamie Allen
Secretary General
Asian Corporate Governance Association Ltd

Room 203, 2F, Baskerville House
13 Duddell Street, Central, Hong Kong

Tel: (852) 2160 1788 (general)
Tel: (852) 2872 4048 (direct)
Fax: (852) 2147 3818
Email: jamie@acga-asia.org
Website: www.acga-asia.org