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6-2020

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Citation
JOSHI, Havovi Heerjee. Corporate governance: Of misses, awareness and improvements. (2020). *Asian Management Insights (Singapore Management University)*. 7, (1), 62-63.
Available at: https://ink.library.smu.edu.sg/ami/137

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CORPORATE GOVERNANCE

Of misses, awareness and improvements.

By Havovi Joshi

Nissan in Japan, Samsung in Korea, Pioneer Industries in Hong Kong, Kingfisher Airlines in India–what do these firms have in common? Each is a poster child firm from Asia known for its corporate governance failures. That is not to say that the Western world has not had its fair share of such companies; think Enron, WorldCom, Lehman Brothers, and Royal Bank of Scotland. The picture, however, is grimmer in the East because most Asian countries are not reputed for good corporate governance, commonly described as "the structures and processes by which companies are directed and controlled".[1] While key markets like Singapore, Hong Kong and Japan have already adopted corporate governance as well as stewardship codes, most other Asian economies, especially the frontier ones like Myanmar and Laos, are still struggling to ensure governance at the most basic levels.

Why is this so? History provides a perspective. Even as the developed world started pursuing the establishment of 'modern corporations' with dispersed shareholding, businesses in most parts of Asia continued to have a concentrated ownership structure. This was either due to the dominance of family firms, as seen in India, or substantial state ownership, such as in China and Vietnam. Colonialism did not help the matter, as the ruling powers were typically more interested in pursuing their own economic interests than establishing codes of governance and institutional safeguards. Hence, corporate governance in Asian countries, with the notable exception of Japan, really started only after the colonial period and the two World Wars.

Growing awareness

Asian countries began focusing on strengthening corporate governance after the 1997 Asian financial crisis. The crisis led to a surge of interest by governments in implementing robust frameworks in line with the OECD-listed corporate governance norms that ensured adequate protection of the interests of all stakeholders. However, with a weak institutional system set-up in most countries, and oftentimes a strong nexus between the political and business leaders of the country, the onus for ensuring corporate governance fell largely on the firm's board of directors. As Ma Cherry Trivedi, CEO, Myanmar Institute of Directors, argues, "Most businesses in Myanmar are family-run, with both the board and management run by the same set of people. So while we have a rulebook on corporate governance and the role of a director, who will investigate all the violations and ensure that penalties are enforced?"

This period also coincided with strong Asian economic growth when firms began to aggressively expand overseas. Consequently, they had to dilute their family/minority shareholding and go public, convincing the market that they had strong corporate governance frameworks in place. In Korea, businesses were dominated by the massive, family-run, global conglomerates, the *chaebols*, which were forced to move away from their largely paternalistic, Confucian style of working to adopt governance structures that were in line with the requirements of the international financial community. They had to adopt more of the Anglo-American style of corporate governance–increasing corporate transparency and accountability, recruiting independent directors and improving their financial reporting.[2] Also, in Japan, firms followed the traditional *keiretsu* structure of deep and strong invisible crossholding networks among companies, and their suppliers and customers. These firms needed to access capital from international finance markets to fund overseas growth, and along with that came the condition to adhere to best practices of corporate governance. In China, there was a surge in corporate governance improvements that happened on account of a need to strengthen the governance of state-owned enterprises that were being listed abroad.[3]

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The situation today

Today, while most countries in Asia have implemented a Corporate Governance Code or similar principles, there is still a considerable degree of variation across the continent–these could be 'binding' as in the case of Bangladesh, India and Vietnam; 'voluntary' as in China and Korea; or 'comply or explain' as seen in Hong Kong, Singapore and Thailand.[4]

The widely-awaited biennial survey by the Asian Corporate Governance Association and the Asia-focused brokerage CLSA on the ranking of corporate governance in Asia, released in December 2018, put Australia in the top spot, followed by Hong Kong and Singapore, and then Japan, which tied with India.[5] Both Hong Kong and Singapore were criticised because their stock exchanges had changed the rules in 2018 to allow companies to list with dual-class shares. These shares offered extra voting power to top executives but could also be potentially misused by company insiders. As for Japan, it had taken initiatives to improve corporate governance standards, with Prime Minister Shinzo Abe instituting Japan's Stewardship Code that applied to company boards in 2014, followed by the Corporate Governance Code for institutional investors in 2015. However, the country has since suffered the repercussions of the Carlos Ghosn/Nissan scandal. In India, there have been several high-profile cases like Satyam Computer Services, where the founders/promoters were perceived as adopting autocratic management styles that brushed aside good governance norms. In addition, a number of sectors like banking and telecoms have been plagued by corporate governance challenges; the near collapse of Yes Bank in the earlier part of 2020 is yet another striking example of corporate governance failure. Overall, the report ranked China, the Philippines and Indonesia at the bottom as these countries were perceived as still having a way to go in terms of improving corporate governance.

> Investors today will pay a premium for a well-governed company, particularly in emerging markets.

But why is corporate governance getting so much more attention today? The 2018 Global Competitiveness Report published by the World Economic Forum affirmed that poor performance on the 'institutions' pillar of its global competitiveness index, which includes corporate governance, continues to pull down the competitiveness of many Asian countries. It is quite clear that investors today will pay a premium for a well-governed company, particularly in emerging markets, and for the Asian growth story to continue uninterrupted over the next few decades, there needs to be a shift to a more robust and effective corporate governance framework. This framework will also have to be forward-looking, and include a focus on environmental and social factors, which we now term as 'ESG' (environmental, social and governance). Accordingly, organisations will need to adapt to this new focus and change how they behave, work and create value to stay relevant in the future.

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