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CORPORATE GOVERNANCE AS ONE OF THE MAIN ISSUES OF CORPORATE COMPETITIVENESS IN EASTERN EUROPE

Abstract

Developing countries aim at implementing new business solutions, which may lend their credibility in the opinion of investors. For this reason, principles of corporate governance are gaining popularity. This is particularly important to Eastern European countries which wish to show that the post-Soviet era was over a long time ago and they want to be perceived as serious business partners respecting fair rules. Principles of good practice which promote streamlining operations and improve company's image shall be submitted to increase the loyalty and trust of business partners. A clear policy, respecting the rights of all shareholders, compliance with laws and rules of good practices allow companies to achieve better financial results. Companies exhibiting high standards of corporate governance create the image of a reliable and responsible business partner, which improves their competitive position, both the national and international ones. Company ensuring the high standard of corporate governance can count on an extra bonus. Near 75 % of investors selecting the company in which they want to locate their saving prefer the companies with higher level of corporate governance. Moreover, this bonus can range from 13 to 34%, which further motivates the company to respect the aspirations of all stakeholders including in corporate governance's rules.

Key words: corporate governance, shareholders, corporate governance rating

Introduction

Using the experiences of the economies that declare a higher economic growth rate, developing countries aim to implement new business solutions, which will make them credible in investors' eyes. Due to this fact, there is an increased interest in corporate governance. This is noted to be happening both at the international and national levels, and then penetrating into companies' internal structures in the form of codes of good practice, adjusted to the social and cultural conditions as well as to the objectives to be achieved with such codes. This is particularly important in case of Eastern European countries, which wish to show that the post-Soviet era has finished and they want to be perceived as serious business partners. It is corporate governance that can help them to improve the companies' operation and their image at the same time. Moreover, an increase in investors' loyalty and trust encourages them to respect the principles of corporate governance.

The definition of corporate governance

Corporate governance may be defined in multiple ways. The approaches differ and depend on the economic and political background of a given country, as well as on the stage of its development. A.Shleifer and R.Vishny claim that corporate governance should be treated as a collection of principles that aim at providing investors with income on the funds invested (Shleifer, Vishny, 1997 : 737). R. A. G. Monks and N. Minow define it as finding a way to maximize wealth creation which would not burden the whole society with inappropriate costs (Monks, Minow, 1996 : 63). Corporate governance is a kind of a system which involves legal and economic institutions. These supervise the correct and economically effective functioning of enterprises, levelling any potential conflicts between the stakeholders involved (Oplustil, 2010 : 5). A. Davis sees them from the point of view of a reconciliation between individual ambitions and the need to meet the common interest of all individuals involved (Davis, 1997 : 7). International Social and Behavioral Science Dictionary in its definition of corporate governance stresses the importance of "such allocation of decisions and controlling rights that is most effective for a company so that the individuals holding adequate decision-making competences and information feel responsible for other stakeholders".

In order to unify the interpretation of corporate governance, OECD explains this idea as a network of relations between executive staff, managing and supervisory bodies, shareholders and other stakeholders on the basis of which the company's objectives, funds to achieve them, as well as funds to monitor results achieved are set (OECD, 2004 : 11). The multiple aspects of the issue under discussion are reflected in building adequate relations between stakeholders within a company, i.e. models which could be helpful in developing the competitiveness of economies.

Models of corporate governance

The culture of corporate supervision as well as principles of corporate governance that are in force in a given country result from its historical and cultural background "… the culturally established concept of a corporation that assists education, and subsequently influences legislation and legal and consulting practice seems to be the basis for institutional solutions" (Lis, Sterniczuk, 2005 : 122). Consequently, they affect both legislature as well as business practice. Recognizing and respecting them by the entities that operate on a given market encourages investors for further allocation of funds. Ignoring them, and thereby ignoring the company's interest and entities involved in its functioning, on the other hand, may give rise to concerns about unfair practices, abuses, cheating, which in turn may lead to a blockage of capital inflow.

The literature investigating the issue of corporate governance presents a few models of corporate governance with the following factors having an influence on the model structure (Weimer, Pape, 1999 : 153):

- concept of the corporation,
- form of a supervising body,

- rights of minority shareholders,
- stock market model
- external market control,
- ownership structure
- salary levels and dependency of management staff;

Based on the above criteria, four models can be distinguished: the English-American, the German, the Latin, and the Japanese one.

Table 1 Model type

	English-American model	**German model**	**Latin model**	**Japanese model**
Rudiments of the concept of the Corporation	Instrumental, shareholder-oriented	Institutional	Institutional	Institutional
Corporate supervisory bodies	Single body	Double body	Usually single body	Single body
Key groups of stakeholders	Shareholders	Banks, employees, oligarchic groups	Financial holdings, government, oligarchic groups	Banks, financial institutions, employees, oligarchic
Stock market role	Significant	Medium/Significant	Medium	Significant
Ownership concentration	Low	Medium / High	Medium	High
Correlation between salaries and results	High	Low	Medium	Low
Time horizon	Short	Long	Long	Long
Examples of countries	USA, Great Britain, Canada, Australia	Germany, Holland, Switzerland, Sweden, Austria, Denmark, Norway, Finland, Poland,	France, Italy, Spain, Belgium	Japan

Source: J.Weimer, J.C.Pape, The Taxonomy of Systems of Corporate Governance, "Corporate governance. An International Review" 1999, vol.7, no. 2, s.153, [W:] K. A. Lis, H. Sterniczuk, Nadzór korporacyjny, Kraków 2005, p. 122

The English-American model stresses the priority of the shareholders' interest and maximization of the values appreciated by them (Monks, Minow, 2000 : 75). The institutional system of corporate governance in this model is constructed upon a single-level board of directors, who represent the shareholders in a more direct manner. Nearly half of the board members originate from external groups independent of the directors. The structure of share ownership is highly dispersed here, mostly due to institutional investors collecting individual investors.

The German model provides for, next to stakeholders' groups, the obligations of the corporation towards the employees. The institutional systems of corporate governance assumes a double body: the management board and supervisory board. The structure of ownership in Germany results from its poor protection of minority shareholders (Shleifer, Vishny 1997: 769). The entities that influence corporate governance are banks disposing of their clients investments.

The companies which apply the Latin model have a „network" structure (Lis, Sterniczuk, 2005 : 136). The supervisory board is appointed and recalled under the consent from the majority of the shareholders entitled to vote, with the role of the minority shareholders being very limited. The groups with the biggest influence on the structure of corporate governance are financial holdings, large family Corporation, and Corporation controlled in their smaller or bigger part by the government.

The Japanese model assumes appointing a board of directors, which subsequently defines the corporation strategic objectives. These objectives, next to the shareholders' interest, should also provide for the interests of the entire society. In practice, these interests are dominated by the interest of the Corporation itself as well as its group of employees (Cooke, Sawa, 1998 : 221).

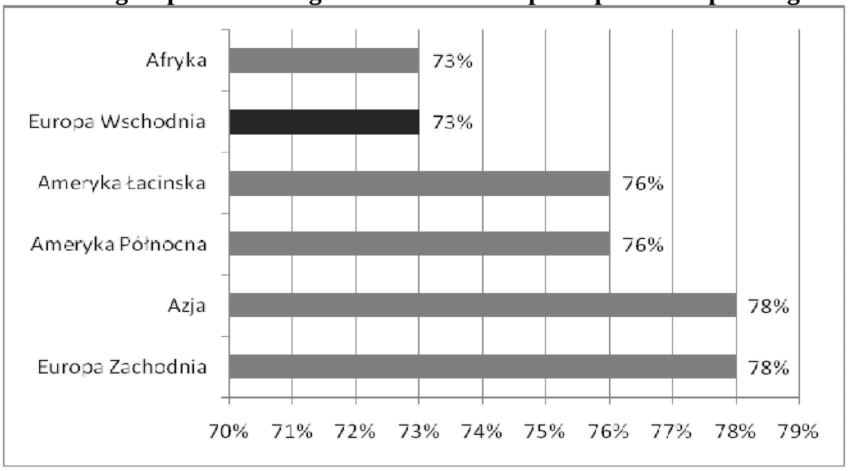
Applying a proper model of corporate governance should contribute to improving the functionality and supervision of companies, as well as to providing them with appropriate level of the owner's supervision. Managing a company according to the principles of corporate governance is to improve the effectiveness and transparency of management, to prevent abuse, reduce misuses, and, consequently, to increase the company's competitiveness.

Acceptance of principles of corporate governance in Eastern Europe

The implementation and observance of principles of corporate governance depend on the awareness level of entities operating on the capital market, with the interest in this issue raising noticeably during the crisis. "The development of market economy in Central and Eastern Europe and the inevitable EU accession by some of the countries from this region have strengthened the belief that corporate supervision is of central importance to the transformation, economic reconstruction and economic growth of former socialist countries" (Hashi, 2003: 5).

The ten-year transformation period of Central and Eastern European countries still reveals some distance in terms of the maturity of their corporate governance structure and undercapitalization of their companies. Nevertheless, the former Eastern Bloc countries show progress in engaging the legal and regulatory environment, even the countries with the weakest jurisdiction. The most serious obstacle is the difficulty to implement and execute the principles and norms of corporate governance (Bokros, 2001 : 12). In order to improve this situation some role models are assumed, which, acting as certain guidelines, will facilitate the improvement of relations between stakeholders and control within both the internal and external structures, neutralizing misunderstandings.

Picture 1 Investor groups demanding the observance of principles of corporate governance

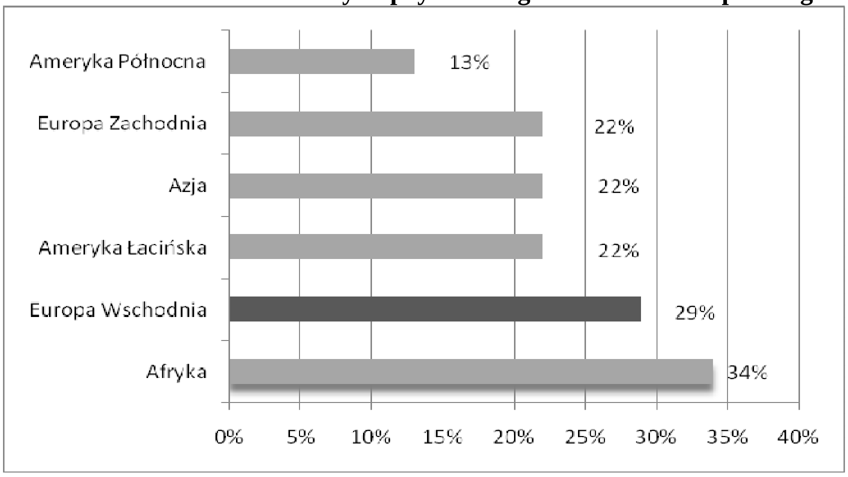


Source: McKinsey Global Investor Opinion Survey on Corporate Governance, 2002

Guided by the instructions of world organizations, Eastern European countries aim to develop instruments which would prevent abnormalities and abuses by any of the stakeholders' groups engaged in the functioning of a company. They see the need to ensure their investors a feeling of security, therefore they respect the principles accepted at the international level and prepare national documents that follow these principles, which in turn provide a basis for codes of good practice at the level of an individual enterprise. The mentality of a society and some historical background could be a serious obstacle. An example can be the approach to the „whistleblowing" phenomenon, which should be understood as a disclosure by a member of a given organization an illegal, immoral or unlawful practice taking place with the consent from the managing bodies (Rogowski, 2007 : 1). Due to the historical context it may be misperceived as a denunciatory activity. Such interpretation may stem from the mistrust towards state authorities, as well as from the belief in solving problems inside a given structure.

Respecting the principles of corporate governance is one of the key criteria that determine the level of capital inflow in the form of company shares. There is a correlation between the level of corporate governance and company's competitiveness. On one hand, companies which use their resources effectively, respect all stakeholders' rights, and run a clear and transparent policy show a higher level of corporate governance.

Picture 2 Bonus that investors are ready to pay for a high standard of corporate governance



Source: McKinsey Global Investor Opinion Survey on Corporate Governance, 2002

Companies offering a high level of corporate governance can count on an extra bonus of about 29%, which only proves its significance as about 76% investors in Eastern Europe take it into consideration. What is more, the bonus may range from 13% to 34% depending on the region (McKinsey, 2002 : 5), which is taken into account when attracting foreign investors. This only proves the thesis stated in the title above that corporate governance can be one of the factors of corporate competitiveness in Eastern Europe, which additionally motivates companies to respect all the stakeholders' rights.

Conclusion

The experiences of well-developed countries encourage central and Eastern countries to apply the rules of corporate governance. An additional argument are the numbers referring to the investor groups willing to give their capital to companies that respect codes of good practice. The transparency of and free access to company's activities as well as openness towards investors allow such companies to obtain a bonus by several percent higher for the shares purchased. Furthermore, respecting the principles of corporate supervision according to a model adjusted to individual structures of the economy indicates its unquestionable development as well as its promotion to a higher level. Respecting the principles of corporate governance results in increased investors' loyalty and trust, which means the capital market of a given country joining the group of the world business partners.

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