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Cambridge University Press
978-1-107-01686-6 - Corporate Governance and Initial Public Offerings: An International Perspective
Edited by Alessandro Zattoni and William Judge
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1 Introduction

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This edited volume reports the results of a major international collaborative research study on corporate governance and initial public offerings (IPOs) in twenty-one countries. We wrote this book for scholars interested in comparative corporate governance, IPOs, or both fields of study. This is not the first study on comparative corporate governance, and it will not be the last one as governance policies are rising in importance due to globalization pressures and because governance practices within and across nations are in a state of continuous flux and evolution (Aguilera and Jackson, 2003). However, this book provides a relatively comprehensive, novel, and detailed perspective on these issues as the study departs from previous works with respect to both theoretical and methodological approaches.

The comparative study of IPOs is even less explored than that of corporate governance. The vast majority of studies of IPOs are conducted in the United States (e.g., Aggarwal, Krigman and Womack, 2002; Arikan and Capron, 2010; Certo, Daily and Dalton, 2001; Heeley, Matusik and Jain, 2007; Higgins and Gulati, 2006; Howton, Howton and Olson, 2001; Pollock, Porac and Wade, 2004; Wang, Winton and Yu, 2010) or the United Kingdom (e.g., Bruton, Chahine and Filatotchev, 2009; Filatotchev and Bishop, 2002). While there are some empirical studies on IPOs in multiple countries, most of them focus on only two or three variables (e.g., Boulton, Smart and Zutter, 2009; Foley and Greenwood, 2009; Lim, Morse, Mitchell et al., 2010) or are entirely descriptive in nature (e.g., Bancel and Mittoo, 2009; Brau and Fawcett, 2006; Lipman, 2009).

To our knowledge, the only previous comprehensive international perspective on corporate governance and IPOs was an edited volume produced by a diverse collection of finance scholars (Gregoriou, 2006). While it was an informative and relatively comprehensive examination of a number of financial considerations associated with

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IPOs in a dozen (mostly developed) countries, it did not systematically consider the corporate governance context in which the IPO firms arose nor did it consider non-financial corporate governance mechanisms. Furthermore, it limited its perspective to the agency theoretical perspective, which has dubious relevance to nations other than the United States (Gordon and Roe, 2004; Lubatkin, Lane, Collin et al., 2005).

As such, there are a number of unique features associated with this book. First, our study extends the variety of countries considered by previous studies as it includes both developed and emerging economies, many of which have not been considered before in the literature. The new countries are both large and fast growing economies such as Russia, China, and India, and also small and relatively unique countries such as Nigeria, Saudi Arabia, and Israel. Thanks to the inclusion of these relatively unexplored countries, the book provides a more complete picture of corporate governance practices around the world. As can be seen in Table 1.1, we examine twenty-one national economies in this study and collectively they represented 73 percent of the global economic output in 2008.

Second, the study systematically explores the national characteristics of a variety of internal and external governance mechanisms utilizing country experts from each economy. This relatively broad perspective on corporate governance is pursued with the conviction that governance mechanisms are complementary and partially substitute in addressing the potential negative consequences coming from the separation of ownership and control (Aguilera, Filatotchev, Gospell et al., 2008; Rediker and Seth, 1995; Ward, Brown and Rodriguez, 2009). In other words, they are formal and informal collections or "bundles" of governance mechanisms that should be explored with a conceptually sound framework.

Third, our study systematically examines multiple IPO outcomes within a national economy. In contrast, the majority of empirical works has typically analyzed just one IPO outcome (e.g., IPO underpricing) and considered one or two corporate governance mechanisms (e.g., board composition or legal system) within a single nation or a few nations. To have a broad and deep knowledge of corporate governance phenomena at the country level, each national chapter has been written by a country expert having an intimate knowledge of the current national context, practices, and policies.

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Table 1.1 *Listing of national economies examined in this comparative study*

Number	Country	2008 GDP (billions USD)	Global GDP	GDP rank
1	Australia	1,039.4	2%	14
2	Belgium	505.4	1%	20
3	Canada	1,499.1	2%	11
4	China	4,521.8	7%	3
5	Germany	3,634.5	6%	4
6	India	1,214.2	2%	12
7	Israel	202.1	<1%	41
8	Italy	2,296.6	4%	7
9	Japan	4,887.0	8%	2
10	Kingdom of Saudi Arabia	475.1	1%	23
11	Mexico	1,089.9	2%	13
12	Netherlands	872.9	1%	16
13	Nigeria	207.1	<1%	39
14	Russia	1,667.0	3%	9
15	Singapore	193.3	<1%	43
16	Spain	1,594.5	3%	10
17	Sweden	487.6	1%	22
18	Switzerland	502.5	1%	21
19	Turkey	730.3	1%	17
20	United Kingdom	2,662.7	4%	6
21	United States	14,369.1	23%	1
	Total	44,652.0	73%	

Source: World Bank (2010b)

Fourth, this book examines corporate governance and IPO activity over a three-year study period from 2006 until 2008. As can be seen from Table 1.2, our twenty-one nations collectively represented roughly 80 percent of the global marketplace, with a low of 78 percent in 2007 and a high of 81 percent in 2006. Clearly, 2008 was an unusual year in the financial markets, and the global market capitalization dropped from 66.4 trillion USD to 34.4 trillion USD due to the global financial crisis. As might be expected, IPO activity dropped considerably in 2008 as well due to high uncertainty in the financial markets (see Table 1.3). Previous research has shown that IPO

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Table 1.2 ***Market capitalization for economies in this comparative study (billions USD)***

Country	2006	%	2007	%	2008	%
Australia	1,095.5	2%	1,298.1	2%	675.6	2%
Belgium	396.3	1%	386.6	1%	167.8	0%
Canada	3,608.2	7%	2,185.9	3%	1,002.9	3%
China	1,141.8	2%	6,205.5	9%	2,785.5	8%
Germany	1,640.2	3%	2,110.7	3%	1,101.3	3%
India	819.2	2%	1,819.6	3%	645.9	2%
Israel	173.3	0%	236.9	<1%	134.4	0%
Italy	1,026.7	2%	1,072.9	2%	521.3	2%
Japan	4,835.0	9%	4,823.2	7%	3,220.5	9%
Kingdom of Saudi Arabia	327.0	1%	515.0	1%	246.6	1%
Mexico	348.7	1%	397.9	1%	232.1	1%
Netherlands	779.4	1%	956.5	1%	387.6	1%
Nigeria	32.8	0%	86.3	<1%	49.7	0%
Russia	1,057.3	2%	1,502.5	2%	396.7	1%
Singapore	276.4	1%	353.5	1%	180.0	1%
Spain	1,323.7	2%	1,799.6	3%	945.5	3%
Sweden	573.1	1%	612.4	1%	252.6	1%
Switzerland	1,212.4	2%	1,274.6	2%	866.2	3%
Turkey	162.5	0%	286.7	0%	117.8	0%
United Kingdom	3,793.3	7%	3,859.9	6%	1,853.2	5%
United States	19,430.8	36%	20,024.0	30%	11,739.6	34%
Total 21 countries	44,053.4	81%	51,807.7	78%	36,980.0	80%
Global economy	54,448.2	100%	66,389.7	100%	34,356.3	100%

Source: World Bank (2010a)

dynamics are different in "cold" and in "hot" markets (Gulati and Higgins, 2003; Wang, Winton and Yu, 2010). Our study covers a three-year period including 2006 representing a "hot" market, 2007 a "lukewarm" market, and 2008 a "cold" market. In sum, our study considers three different market conditions for examining governance dynamics.

Finally, this book focuses on small-, medium-, and large-sized IPO firms using both archival and primary data. Most comparative corporate governance and IPO research only considers large, publicly held firms using archival data. Initial public offerings provide a unique

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Table 1.3 ***IPO activity across twenty-one economies in this comparative study****

Country	2006	2007	2008	3 year total	Average age (yrs)	Average size (employees)
Australia	2	1	46	49	9	46
Belgium	7	6	1	14	10	160
Canada	4	31	10	45	6	353
China	17	24	6	47	5	11,108
Germany	22	19	2	43	20	1,695
India	39	47	30	116	15	937
Israel	37	56	1	94	8	414
Italy	17	25	4	46	36	1,037
Japan	176	116	42	334	22	593
Kingdom of Saudi Arabia	14	15	12	41	19	1,267
Mexico	3	4	2	9	25	2,207
Netherlands	10	5	1	16	16	2,872
Nigeria	4	4	5	13	15	807
Russia	12	12	2	26	11	17,522
Singapore	0	30	22	52	10	888
Spain	10	11	2	23	24	1,600
Sweden	28	31	6	65	12	267
Switzerland	6	8	2	16	10	1,089
Turkey	9	7	0	16	15	2,131
United Kingdom	141	91	11	243	3	439
United States	109	100	19	228	8	1,720
Total 21 economies	667	643	226	1,536	13	1,460

Source: EurIPO (2006, 2007, 2008)
* For some countries characterized by an intense IPO activity (e.g., India, Japan, UK, and USA), our study collected and analyzed data on a sample made by about 75 percent of the total IPOs in the period.

context to study corporate governance as they are privately held firms that entered a publicly traded stock market for the first time (Certo, Holcomb and Holmes, 2009). IPOs have to adopt governance systems that meet their specific needs to collect funds from the financial community, and to balance the interests of both inside and outside shareholders. This "genesis" of corporate governance from private to public companies is rarely explored.

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In sum, the main objective of this introductory chapter is to present the theoretical framework and the main results of the empirical study that aimed to explore corporate governance mechanisms at national and cross-national levels. In particular, we start with an overview of the inter-disciplinary field of corporate governance. Next, we discuss the initial public offering event by way of background for the remainder of the book. In addition, we discuss how internal and external corporate governance mechanisms act and interact to influence the IPO event. Finally, we conclude with our cluster analysis of the twenty-one economies along prominent corporate governance mechanisms in order to begin to think about how national economies are similar and different as they seek to reconcile the many economic and social interests associated with the initial public offering event.

Overview of the field of corporate governance

Corporations possess enormous economic power, and with that economic power comes political power. Corporate governance is concerned with how that power is directed – for the welfare of society or for the welfare of a few individuals, corporations, or an industry to the exclusion of others. In essence corporate governance addresses both efficiency and economic equity issues. From a relatively narrow view, corporate governance focuses on the design of board of directors and/or a protection of ownership rights in order to guarantee the shareholder value maximization, or to assure investors a return on their investments (Shleifer and Vishny, 1997). From a broader perspective, it encompasses the whole set of legal, cultural, and institutional mechanisms that determine who controls companies, how that control is exercised, and how risk and returns are allocated (Blair, 1995). In this book, we take a relatively broad perspective on the role, function, and impact of corporate governance on initial public offerings.

Regardless of the breadth of perspective, corporate governance plays a key role in all companies (e.g., industrial and financial, small and large, listed and unlisted, profit and non-profit) as in any company the misappropriation of corporate funds and low value creation are relevant issues (Monks and Minow, 2004). However, it is of particular importance in listed companies as the separation between ownership and control both serve to emphasize

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the risk of misappropriation and of an incompetent decision-making process (Berle and Means, 1932).

The first issue (i.e., the potential abuse of managers at the expense of shareholders) is considered the most important governance problem. This risk is particularly relevant when there is a dispersion of share capital among a large number of small investors. The dispersion of shareholdings favors, in fact, the separation between ownership and control, i.e., shareholders tend to delegate decision-making rights to top managers. Moreover, the small fraction of voting and cash flow rights shareholders own can reduce incentives to exercise an effective monitoring of top managers' behavior. In sum, when ownership is dispersed, managers are able to make decisions that can ignore the rights of minority shareholders (Berle and Means, 1932; Jensen and Meckling, 1976).

The value creation process is particularly important as companies can fail or produce lower results due to poor managerial decision making. Managerial greed and opportunism may lead to the misappropriation of corporate resources. Negative firm consequences may also result from managerial incompetence (Hendry, 2005). For example, an incompetent top management team may make a disastrous acquisition or a number of small business decisions leading the company to a slow decline (Charkham, 2005). Governance mechanisms should address these issues by selecting talented managers, monitoring managers' decisions, providing them with proper incentives, and firing incompetent executives.

The most common theoretical approach to analyze and provide solutions to corporate governance issues is agency theory. According to this view, the relationship between shareholders and top managers in a widely held company – or one with controlling and minority shareholders in a company with concentrated ownership – represents an agency relationship (Jensen and Meckling, 1976). In an agency relationship, the principal delegates the agent to fulfill some activities in his interest, but he loses control of the final performance that is based on the unobservable effects of the agent and on chance. The asymmetry of information among subjects, and the uncertainty in the task, allow the agent to deviate from the principal's expected outcome, and give rise to agency costs. These costs include the monitoring costs of the agent's behavior, the costs of reassurance of the principal, and any other loss of wealth originated in the relationship (Jensen and Meckling, 1976).

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Recent formulations of agency theory consider conflicts that arise from multiple agents (e.g., Arthurs, Hoskisson, Busenitz et al., 2008) and multiple principals (e.g., Young, Peng, Ahlstrom et al., 2008). Classical corporate governance mechanisms that stem from the agency perspective are monitoring of agents through such practices or mechanisms as independent boards, dominant shareholders, and the market for corporate control, as well as incentive alignment mechanisms that offer ownership stakes to the agents as well as legal mechanisms which punish opportunistic behavior (Denis and McConnell, 2003).

More recently, other theoretical perspectives are emerging to challenge the agency theoretic perspective in describing and explaining the antecedents and effects of corporate governance. For example, the institutional perspective argues that corporations seek legitimacy above shareholder value creation, and it points to the role of institutions in guiding and constraining the misuse of corporate power (Scott, 2001; Suchman, 1995). Stewardship theory argues that managers are, in general, all trying to be good stewards of the resources for which they have been entrusted, in direct contrast with the behavioral assumptions underlying agency theory (Davis, Schoorman and Donaldson, 1997). And resource dependency theory argues that social actors and social systems are simply trying to avoid being controlled by others and seeking to gain control over resources that guarantee the future survival of the firm (Hillman and Dalziel, 2003).

In sum, the field of comparative corporate governance is in considerable flux currently, particularly as the depth and breadth of economies are considered. In this study, we collect and analyze data from multiple theoretical perspectives in order to provide the broadest review of corporation governance dynamics surrounding IPO firms throughout the world.

Overview of the initial public offering event

Changing from a private to a public firm is a major milestone in the life of a company. The first step in going public typically involves drafting the registration statement to be filed with the securities regulator for the country in which the firm aspires to be listed. Drafting a registration statement is a group activity combining the efforts of the company's executives, the underwriters, the outside counsels, and the auditors. In some countries, a preliminary prospectus is prepared for distribution to potential investors. This prospectus includes all

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relevant information about the offering except the initial price of the stock and the number of shares to be offered. Filing a registration statement with the regulatory authority typically triggers a "quiet period," in which the members of the firm are not permitted to grant interviews or otherwise promote the company in any way.

The company is permitted, however, to conduct "road shows" around the country, in which the underwriters and top management team meet with prospective investors, analysts, and potential members of the underwriting syndicate. The corporation is usually prohibited in these meetings from presenting information not included in the prospectus, but it may clarify issues raised in the prospectus and respond to audience questions (Pollock, Porac and Wade, 2004).

During this registration period, the underwriter must determine the offering price of the stock. The underwriter first contacts prospective investors and determines the number of shares these investors are willing to purchase at various price levels. The underwriter then uses this information to assess how the market initially values the company and to identify potential investors for the public offering. Once the regulatory authority is satisfied that all relevant information about the company has been presented in a clear and accurate way, the company is permitted to file a final pricing amendment that includes the stock's price, the number of shares to be sold, the underwriter's commission, and the effective date on which the company has a right to offer its stock to the public. Representatives of the company sign the underwriting agreement with its investment bank and then set the offering price. The company's stock is offered to the public shortly after the IPO goes effective (Pollock, Porac and Wade, 2004).

After the firm goes public, there typically is a "lockup period" in which the members of the top management team are prevented from selling their shares in the firm. In the United States, this lockup period is often 180 days. In other countries, the lockup period is quite different or non-existent. If the market is "efficient," the market price of the stock will balance supply of shares with the demand for shares at a market clearing stock price. However, much is unknown about privately held firms, so this can lead to market inefficiencies. For example, in a review of the IPO literature in the United States, most IPOs are underpriced after the first day of the offering and most IPOs' stock underperforms their industry peers during their first year of being public (Brau and Fawcett, 2006; Ritter, 1991).

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Depending on the national governance environment, the corporate structure of the corporation often changes just before or just after the firm goes public. Importantly, the shares of the firm often become less concentrated, though this dilution of share ownership varies considerably from country to country. For example, in a study of 2,700 firms in thirty-four countries, Foley and Greenwood (2009) showed that IPOs in countries with relatively strong investor protections are more likely to experience significant decreases in shareholder concentration than IPOs in countries with relatively weak investor protections.

Typically, the proceeds from the public offering are used to reward investors who gambled on the firm while it was privately held, as well as invest in the business to grow it more aggressively. For example, many IPOs often make acquisitions of other companies with this additional capital (Arikan and Capron, 2010). Alternatively, some IPO firms venture overseas for the first time (Lim, Morse, Mitchell et al., 2010). Still other IPO firms embark on aggressive development of an expensive technology, such as biotechnology firms (Higgins and Gulati, 2006).

Corporate governance of IPOs throughout the world

Ultimately, the global economy needs a global theory of corporate governance that can adequately describe and explain the antecedents and effects of corporate governance throughout the world. This is an ambitious task, since business practices in general, and corporate governance practices in particular, vary so much throughout the world. For example, financial accounting standards are converging slowly toward a common set of standards, but there remain important differences in structure and practice (Judge, Li and Pinsker, 2010). While some have argued that the global economy needs to converge towards the Anglo-American system of governance, increasing numbers of policy-makers and practitioners are pioneering new models (Gordon and Roe, 2004). To simplify our task somewhat, we begin with a discussion of the primary corporate governance mechanisms that confront firms which enter the public financial markets for the first time.

While there is no comprehensive typology of corporate governance mechanisms, the field generally distinguishes between two types: internal and external mechanisms. Internal corporate governance

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