DO STOCK PRICES REFLECT REGULATORY REFORMS IN THE CORPORATE GOVERNANCE MECHANISMS? THE CASE OF GREECE

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Abstract

This study provides evidence on the value relevance of corporate governance mechanisms in a developing stock exchange. It empirically investigates the effect of corporate governance mechanisms prescribed by the corporate governance law (L.3016/2002) on abnormal stock returns for firms listed in the Athens Stock Exchange (ASE). The first corporate governance law in Greece aims to improve the existing corporate governance framework. However, stock prices seem no to be affected by the regulatory reforms in the corporate governance mechanisms. Three reasons are given: (1) the fundamental economic value of a firm is not affected by the introduction of corporate governance mechanisms; (2) the fundamental economic value of a firm is affected by the introduction of corporate governance mechanisms but due to the fact that the Greek stock market is not efficient share prices do not reflect firm's fundamental economic value; and (3) investors may not be convinced that corporate governance mechanisms significantly affect the performance of a company.The findings of this study can facilitate legislators in improving the existing legislation concerning corporate governance and in developing a new one.

Keywords: Corporate Governance, Abnormal Stock Returns, Greece

1. INTRODUCTION

Modern corporations are characterized by dispersion of share capital ownership over a large number of shareholders. Due to this development, the individual shareholder has seen his ability to oversee the conduct of companies' management to diminish (Monsen and Downs, 1965; Demsetz and Lehn, 1985). As a consequence, management has become increasingly independent from shareholders while its effective control over the affairs of a firm has increased . Under these circumstances, questions have been raised regarding the extent to which the management of a firm will maximize shareholders wealth (Berle and Means, 1932; Monsen and Downs, 1965; Williamson, 1981). It has been argued that the management of a firm will pursue its own personal goals, even at the expense of the interests of the owners. Managers' aspirations for security, increased salaries, enhanced power and prestige, can prompt them to direct funds to operations and activities which do not necessarily contribute to the maximization of the utility of owners . In general, it has been maintained that, in the case of separation between management and ownership, a firm's top management is very likely to make financial and investment decisions that do not necessarily aim to maximize shareholders value (Monsen and Downs, 1965; Scherer, 1980; Hunt, 1986). Under these circumstances, the shareholders of a firm may devise mechanisms which will motivate the managers of the firm to pursue policies which will further the interests of owners (Dhaliwal et al., 1982; Watts and Zimmerman, 1986). Corporate governance mechanisms have been introduced in many corporations in order to ensure that the management of a firm works towards the maximization of the value of the firm and as a consequence the maximization of shareholders wealth.

A number of studies have indicated that investors' decisions are influenced by the extent to which a firm implements corporate governance mechanisms (McKinsey Co, 2002). Investors may be more inclined to buy shares of firms in which corporate governance regulations are implemented, because they believe that their interests are more effectively protected in these firms. Besides, they may believe that the implementation of corporate governance mechanisms contributes to the maximization of the firm's value. The present study investigates whether the application of the corporate governance principles by a firm, is positively associated with its stock returns. This issue is investigated within the context of the business environment of Greece. In particular, it is examined whether the introduction of a legislation concerning corporate governance principles (L.3016/2002) affects stock returns of the firms listed in Athens Stock Exchange.

The findings of this study provide insights regarding the extent to which the existing mechanisms of corporate governance, as these are provided by the L.3026/2002, ensure that the published financial statements of Greek corporations provide a fair view of their financial position, results and cash flows. The findings of this study can be

particularly important for investors, since their investing decisions are supposed to be influenced, to a considerable extent, by the published accounting figures. Corporations may be also interested in the findings of this study given that investors are likely to provide finance to a firm, only if they believe that the financial statements of this firm provide a faithful representation of its financial position and income. Furthermore, the findings of this study can facilitate legislators in improving the existing legislation concerning corporate governance and in developing a new one.

2. THE MAIN PROVISIONS OF L.3016/2002

According to the L.3016/2002 the board of directors of all Greek listed companies should include non-executive and independent non-executive members[1]. In particular, the legislation provides that the number of non-executive board members should not be lower than the one third of the total number of board members. Furthermore, at least two members of the Board of Directors should be independent non-executive ones.

Under the provisions of the L.3016/2002 all listed companies are obliged to prepare a statement of Internal Company Policy. In the Statement of the Internal Company Policy the administrative structure of the corporation should be presented. Further, the responsibilities of executive and non-executive Board members should be defined in detail.

The L. 3016/2002 prescribes that an internal audit department should be established. One of the main responsibilities of this department is to monitor the implementation of the statement of Internal Company Policy and to ensure the continuous compliance with its provisions.

3. LITERATURE AND HYPOTHESES DEVELOPMENT

In an efficient stock market share prices reflect the fundamental economics[2] of the firms while stock returns reflect investors' reactions to decisions taken by the management of the firm (Morck and Nakamura, 1999). Corporate governance mechanisms affect the decision-making procedure of a firm and ultimately influence the way a firm operates. As a consequence, provided that stock market is efficient, a change in corporate governance mechanisms of a firm will affect its market value (Gompers et al., 2003).

However, the market value of a company may not be exclusively determined by the fundamental economics of a firm. A change in investors' psychological mood may result in an adjustment of the market value of a firm (Keynes, 1936; Shiller, 1989). When investors feel that their interests are adequately protected, they value a firm at a premium (La Porta et al., 2002). The adoption of corporate governance principles by firms seems to enhance investors' protection feeling. During the Asian markets crisis, the companies that had exhibited the less volatile stock market behavior were those that had developed the most intergraded systems of corporate governance (Mitton, 2002). It has been observed that in countries where the institutional framework for the investors' protection is fully developed stock returns are higher (McKinsey Co, 2002).

3.1 Board Structure

The participation of independent non-executive members in the board of directors can increase the value of a firm. The independent non-executive directors are supposed to effectively control firm's managers and thus prevent them from taking value-reducing actions. According to Borokhovich et al. (1996) an incompetent CEO is more likely to be removed when independent non-executive participate in the board of directors. The participation of independent non-executive board members in the committees that supervise internal audit procedures guarantees that internal audit department will scrutinize the decisions and actions of firm's management without bias (Menon and Williams, 1994). In addition, independent non-executive board members facilitate the decision-taking procedure of a firm (Cadbury, 1992; Hampel, 1998). Independent non-executive members, by offering their specialized knowledge to the firm, contribute to the improvement of a firm's operation (Fama and Jensen, 1983; Rosenstein and Wyatt, 1990).

The financial statements of a firm are supposed to be more reliable when the board of directors includes independent non-executive members (Besley, 1996). Independent non-executive members, due to the fact that they have limited access to inside information, assign more importance to the existence of an informative external audit. In the same time, independent non-executive members provide more reliable responses to external auditors' questions relating to audit procedures and financial statements preparation (Hampel, 1998).

Empirical evidence indicates that stock market reacts positively when independent non-executive members participate in the board of directors. (Baysinger and Butler, 1985; Rosenstein and Wyatt, 1990).

On the basis of the above analysis it can be hypothesized that the Greek stock market would react positively to the introduction of the L.3016/2002, which obliges firms to include non-executive and independent non-executive members in their board of directors. The following hypothesis has been empirically tested:

H1: Stock returns are positively associated with the introduction of the corporate governance principles provided by the L. 3016/2002.

3.2 Ceo duality

It is common in many companies the offices of the President of the board of directors and the CEO to be held by the same person (CEO Duality). It has been argued, that when a CEO chairs the board of directors, the independence of the boardroom is limited (Fama and Jensen, 1983; Carver, 1990; Millstein, 1992;

[1] Executive members are concerned with daily administrative issues of the corporation. Non-executive members are responsible for all corporate issues (L. 3016/2002, Article 3, par. 1)

[2] Provided that markets are efficient stock prices reflect the value of the future profits of a firm, including its growth rate.

Whittington, 1993; Brickley et al., 1994). As a consequence, the ability of the Board of directors to control effectively managements' decisions is hindered (Finkelstein and D'Aveni, 1994). Given that the president of the Board of Directors is also the CEO of the firm, executive directors may refrain from exercising a comprehensive control on management's actions and decisions (Jensen, 1993).

In the absence of effective control by the board of directors (when CEO is also the board chair), managers may aim to maximize their personal wealth at the expense of shareholders interests (Worrell et al., 1997). Even when a firm has a poor performance, it is not likely that a CEO will be replaced if he/she also holds the office of the board of directors (Morck et al., 1989; Calcagno and Renneboog, 2004). Moreover, empirical evidence suggests that when CEO is also the board chair the information provided to shareholders might not be up to the desired level (Dalton and Kesner, 1987).

Within this context it can be argued that stock market is not likely to value highly firms in which CEO is also the president of the Board (Cadbury Committee Report, 1992). The following hypothesis has been empirically tested:

H2: The existence of CEO who serves also as board chair affects negatively stock returns.

3.3 Shareholders that own more than 5 % of firm's share capital

Management of a firm is more effectively controlled when the ownership of the majority of firm's shares is concentrated in few major shareholders that each of them owns more than 5 % of firm's share capital (henceforth, blockholders). Blockholders are expected to exercise a continuous control upon the management of a company, in order to ensure that the management's decisions lead to shareholders wealth maximization (O'Sullivan, 2000). For instance, blockholders are likely to remove ineffective managers (Calcagno and Renneboog, 2004; Kaplan and Minton, 1994). Therefore, the presence of blockholders contributes in the improvement of the administration of a corporation (Shome and Singh, 1995; Allen and Phillips, 2000). Findings of empirical research indicate that blockholders are associated with positive stock returns (Holderness and Sheeham, 1985; Barclay and Holderness, 1991).

However, it should be mentioned that the mere existence of blockholders does not secure the efficient operation of an entity. Blockholders should participate actively in the supervision of management's actions (Bethel et al., 1998). There are various categories of blockholders. Each category has its own interests and motives and therefore differs from the others with respect to its ability to monitor firm's management (Boycko et al., 1996; Dyck, 2001).

3.3.1 Institutional investors

Shareholders that own more than 5% of company's share capital are usually legal entities. The effectiveness of their control upon management is conditioned upon their type and size (Shivdasani, 1993; Sudarsanam, 1995; Maury and Pajuste, 2005). Institutional investors are one of the categories of blockholders that exercise considerable influence on company's management. Due to the dominant position they hold in the financial markets, the institutional investors can influence firms' share price. Since they control a substantial percentage of voting rights they can influence the agenda of issues that are discussed in the general meetings of the shareholders. Furthermore, institutional investors by demanding high quality financial information (Kane and Velury, 2004), exercise pressure to companies to apply the appropriate accounting standards, and avoid using misleading accounting treatments (Chung et al., 2002). Additionally, institutional investors can induce firms' management to adopt policies that improve the return on the invested capital (Scott, 1986). It seems, therefore, that the ownership by institutional investors of a substantial proportion of a firm's capital is a factor that can affect positively the value of a firm (Nandeltadh and Rosenberg, 2003; Ashbaugh et al., 2004). The main categories of institutional investors are the following: banks, insurance funds, insurance companies and investment companies.

3.3.1.1 Banks

Banks due to the better access they have to inside information are expected to control more effectively firms' management (Fama, 1985; Conyon and Peck, 1998; Gorton and Schmid, 2000). On the other hand, it has been argued that banks are primarily concerned about the repayment of the loans they have granted to firms, rather than about defending the interests of shareholders (Morck and Nakamura, 1999; Gomes, 2000; Cremers and Nair, 2004). Empirical evidence suggests that, in many instances, banks discourage corporations to undertake high risk investment projects, even when these projects have positive future cash flows (Eisenberg et al., 1998; Weinstein and Yahef, 1998).

3.3.1.2 Pension funds

Pension funds are supposed to exercise strict control on companies' management, since they do not have any business transactions with companies (Almazan et al., 2005). Pension funds press for the replacement of the management of a firm if they believe that the management is ineffective (Myerson, 1993; Pensions and Investments, 1993)

However, it should be pointed out that pension funds which are controlled by public sector organizations, are more concerned about achieving certain political and economic goals rather than monitoring companies' management (Wahal, 1996; Del Guercio and Hawkins, 1999; Faccio and Lasfer, 2000; Woidtke, 2002).

3.3.1.3 Insurance companies

Insurance companies are supposed to closely monitor firms' management (Black and Coffee, 1994; Monks and Minow, 2004). On the other hand, it has been argued that the insurance companies may not apply rigorous control on the management of corporations, which are also their clients (Borokhovich et al., 2000; Monks and Minow, 2004).

3.3.1.4 Investment funds

In most instances, investment funds aim to short term profits. As a consequence, they are less interested about the long-term prospects of a firm and the effectiveness of its management. Investment funds can easily sell the shares they hold and invest the available funds to the stock of other corporations. (Monks and Minow, 2004). It appears, therefore, that investment funds do not have a strong motivation to closely monitor companies' management.

On the basis of the above analysis, it can be concluded that institutional investors can exercise an effective control on firms' management, only when they are concerned about the long-term prospects of firms and at the same time have no commercial and financial transactions with these companies (Payne et al., 1996; Brickley et al., 1994). The following hypotheses have been formulated and tested:

H3 : Banks, pension funds and insurance companies that own more than 5 % of the outstanding shares of a firm affect positively its stock returns.

H4: Investment funds that own more than 5 % of the outstanding shares of a firm affect negatively its stock returns.

3.4 Internal Shareholders [3]

When senior managers own a small proportion of share capital is less likely to aim towards the maximization of shareholder wealth (Berle and Means, 1932; Jensen and Meckling, 1976). On the other hand, it has been suggested that managerial ownership of a substantial proportion of a firm's share capital can align managers and shareholders interests (Jensen and Meckling, 1976; Singh and Harianto, 1989; Jensen, 1993; Gugler et al., 2003). Empirical findings seem to support this argument (Singh and Davidson III, 2003). It appears that managerial ownership is associated with positive stock returns (Yermark, 1996; Gorton and Schmid, 2000). When managers own a substantial proportion of share capital they have an incentive to prepare financial statements that provide a fair view of firm's financial position (Chow, 1982). Consequently, investors are less hesitant to invest in this firm. It should be noted that when the managerial ownership of the share capital exceeds a certain level, firm's value is negatively affected (Morck et al., 1988; Mc Connell and Sarvaes, 1990; Hermalin and Weisbach, 1991). It seems that when managers control a large proportion of share capital are more reluctant to undertake high-risk / high-return projects that increase firm's value (Stulz, 1988). The following hypothesis has been formulated in order to investigate the association between the internal shareholders' ownership and stock returns:

H5: Internal shareholders that own more than 5 % of the outstanding shares affect negatively stock returns.

3.5 Board size

When board of directors has few members appears to be more effective (Jensen and Meckling, 1976; Jewell and Reitz, 1981; Olson, 1982; Gladstein, 1984; Lipton and Lorsch, 1992). Empirical evidence suggests that small in size boards of directors are associated with positive stock returns (Yermack, 1996; Eisenberg et al., 1998). In contrast, when the board of directors has many members the decision taking procedures can be time-consuming. Moreover, the boards of directors with many members appear to be less inclined to scrutinize and criticize the decisions of the firm's management (Lipton and Lorsch, 1992; Jensen, 1993). Findings of empirical research indicate that if company's performance is not satisfactory senior managers are likely to be removed when the board of directors has few members (Yermarck, 1996; Dahya et al., 2002).

The above analysis indicates that the size of the board of directors of a firm affects the value of the firm. The following hypothesis has been formulated in order to investigate the association between the size of the board of directors and the value of a firm:

H6: Stock returns are negatively associated with the board size.

4. THE SAMPLE AND METHODOLOGY

4.1 The sample

The sample includes companies that were listed in the Athens Stock Exchange for the period 2000-2003. The sample does not include fifty-five companies from the following sectors: banking sector, insurance sector, investment companies, and financial leasing companies. By excluding the above companies from the sample the findings of this study are comparable with the results of other studies.

In the sample were included only firms whose fiscal year coincided with the calendar year. Eleven companies were excluded from the sample because their fiscal years did not coincide with the calendar years. Furthermore, in the sample are not included firms that during the period under investigation merged with other companies, or were acquired by other corporations. From the sample were also excluded companies that changed their line of business during that period, and companies that discontinued their operations in the same period.

For the firms operating in Greece, the only source of information regarding the corporate governance principles they apply is their annual report. As a consequence, the data used in this study relating to the corporate governance has been derived from the companies' annual reports. The sample does not include sixty-seven companies that have failed to publish annual bulletins for the full study period. Data regarding stock returns have been derived from the commercial database of "*EFFECT Computer Applications*".

[3] Internal shareholders are those shareholders who have a professional relationship with the company. For instance directors, managers and other employees can be characterized as internal shareholders if they own shares of the corporation in which they offer their services This study is mainly concerned about firm's directors and managers.

Table 1. Sample selection

Listed Companies (from 01/01/2000 until 31/12/2003)	269
(-)Companies in the Financial Sector	36
Companies Total	**243**
(-) Companies whose annual reports fail to disclose detailed information about their corporate governance mechanisms	67
Sample Total	**176**

The distribution of firm-year observations across sectors is presented in Table 2.

Table 2. Firm-year observations distributed across the industry sectors

SECTOR	*Firm-year observations of the sample*	*Firm-year observations with information about corporate governance related issues*
HOLDINGS COMPANIES	22	13
TELECOMMUNICATIONS	4	3
REFINERY	1	1
WATER SUPPLIES	1	1
PASSENGER SHIPPING	4	4
INFORMATION TECHNOLOGY	10	10
PUBLISHING & PRINTING	10	9
TELEVISION-ENTERTAINMENT	2	2
GAMING	1	1
HEALTH SERVICES	3	3
BASIC METALS	11	9
METALLIC PRODUCTS	6	5
MACHINERY & APPLIANCES	2	2
CABLES	2	2
ELECTRONIC EQUIPMENT	1	1
NON METALLIC MINERALS-CEMENT	7	6
WHOLESALE COMMERCE	30	19
I.T. EQUIPMENT - SOLUTIONS	7	4
RETAIL COMMERCE	13	6
MOBILE RETAIL SERVICES	1	1
FOOD	15	10
ANIMAL FEEDS	2	2
DISTILLERIES	2	0
TOBACCO PRODUCTS	1	1
HOTELS & RESORTS	5	2
RESTAURANTS	4	4
TRANSPORTATION RELATED FACILITIES & SERVICES	1	1
ADVERTISEMENTS	1	0
TEXTILE INDUSTRIES	15	11
CLOTHING	5	3
REAL ESTATE	4	3
CONSTRUCTION	22	16
CHEMICALS	3	2
PLASTICS-RUBBER	6	4
PAPER PRODUCTS	2	2
WOOD & CORK PRODUCTS	3	3
FURNISHING INDUSTRIES	3	3
VEHICLES MANUFACTURING	1	1
VEHICLES COMMERCE, MAINTENANCE	1	1
RENTAL SERVICES	2	1
TRANSPORTATIONS	1	1
JEWELLERY MANUFACTURING	1	0
PISCICULTURE	3	1
AGRICULTURE - FARMING	2	2
TOTAL	**243**	**176**

4.2 The methodology

Before examining the impact of the introduction of corporate governance principles on the abnormal stock returns, it has been examined whether there was a statistically significant change in the abnormal stock returns between the periods prior to and after the adoption of the corporate governance legislation. The mean and median values of the abnormal stock returns for the year 2001 have been compared with the corresponding values of the year 2003.

In order to determine whether stock returns are associated with the applied principles of corporate governance the following model (Model 1) has been estimated for the period 2000-2003.

$$ABNRET = \alpha_0 + \alpha_1\ INTAUD_{i,t} + \alpha_2\ D^*\ OUTDIR_{i,t} + \alpha_3 CEODUAL_{i,t} + \alpha_4 INSTBLOCK_{i,t} + \alpha_5 INTBLOCK_{i,t} + \alpha_6\ D^*BOARDSIZE_{i,t} + \alpha_7 GROWTH_{i,t} + \alpha_8 CODESECTOR_{i,t} + \alpha_9 DIREXP_{i,t} + \alpha_{10} PRETUR_{i,t} + \alpha_{11} CEOTUR_{i,t} + \varepsilon_{i,t} \quad (1)$$

Where:

$ABNRET_{i,t}$: Abnormal stock returns, estimated as the return of the stock of company i for the year t[4] minus the return of the General Index of the Athens Stock Exchange

D : Dummy variable, equals to one for the period after the adoption of the principles of corporate governance by the companies

$INTAUD_{i,t}$: Dummy variable, equals to one when there is an internal audit department in the company i in year t,

$D^*OUTDIR_{i,t}$: A variable that represents the impact of the application of corporate governance principles on the proportion of independent non-executive members of the board of directors (OUTDIR) for the company i in year t,

$CEODUAL_{i,t}$: Dummy variable, equals to one if the CEO is also the president of the board of directors for the company i in year t

$INSTBLOCK_{i,t}$: Percentage of the outstanding shares owned by the institutional blockholders for the company i in year t

$INTBLOCK_{i,t}$: Percentage of the outstanding shares by the blockholders who have professional relationship with the company i in which they own shares in year t

$D^*BOARDSIZE_{i,t}$: Variable which represents the interaction between the adoption of the principles of corporate governance by a firm i and its board size in year t

$GROWTH_{i,t}$: The growth rate[5] of the corporation for the company i in year t ,

$CODESECTOR_{i,t}$: The sector in which a company i belongs in year t,

$DIREXP_{i,t}$: The experience of the members of the board of directors of company i in year t. Determined by the number of the boards of directors in which a board member participates[6].

$PRETUR_{i,t}$: Dummy variable equals to one if there have been a replacement of the president of the board of directors of the company i in the previous year

$CEOTUR_{i,t}$: Dummy variable equals to one if there have been a replacement of the CEO of the company i in the previous year

Given that each category of institutional investors follows different investment policies, the association between the institutional shareholders and stock returns are examined separately for each category of institutional investor. The institutional investors are analysed to the following categories: banks (BANKS), insurance companies (INSCO), investment companies (INVCO), pension funds (PENS) other legal entities (OTHERCO).

In order to determine whether stock returns are associated with the ownership by institutional investors the following model (Model 2) has been estimated for the period 2000-2003.

$$ABNRET = \alpha_0 + \alpha_1\ INTAUD_{i,t} + \alpha_2\ D^*\ OUTDIR_{i,t} + \alpha_3 CEODUAL_{i,t} + \alpha_4 INTBLOCK_{i,t} + \alpha_5 BANKS_{i,t} + \alpha_6 INSCO_{i,t} + \alpha_7 INVCO_{i,t} + \alpha_8\ OTHERCO_{i,t} + \alpha_9\ D^*BOARDSIZE_{i,t} + + \alpha_{10}\ GROWTH_{i,t} + \alpha_{11} CODESECTOR_{i,t} + \alpha_{12} DIREXP_{i,t} + \alpha_{13} PRETUR_{i,t} + \alpha_{144} CEOTUR_{i,t} + \varepsilon_{i,t} \quad (2^7)$$

Where:

$BANKS_{i,t}$: Dummy variable equals to one if a bank is a blockholder of the company i in the year t.

$INSCO_{i,t}$: Dummy variable equals to one if an insurance company is a blockholder of the company i in the year t.

$INVCO_{i,t}$: Dummy variable equals to one if an investment company is a blockholder of the company i in the year t

$OTHERCO_{i,t}$: Dummy variable equals to one if another legal entity is a blockholder of the company i in the year t.

(The rest of the variables are analyzed as the model 1 is developed)

4.3 Control Variables

A firm exhibits high growth rates when its return on equity is greater than its cost of capital. Investors seek to buy shares of firms with high growth rates because growth (GROWTH) is usually associated with positive stock returns. Economic conditions prevailing in the industry (CODESECTOR) in which a firm operates affect company's performance and therefore its stock prices. Additionally, the value of a firm can be influenced by certain qualitative characteristics. An important qualitative variable that may have an impact upon firm's performance is the experience of the members of the board of directors (DIREXP). Moreover, the performance of a firm is dependent, to a considerable extent, on the decisions taken by the CEO and the president of its board of directors. The longer the period a person holds one – or both - of these posts, the stronger is the influence he/she can exercise on the board members. Therefore, the replacement of the president of the board of directors (PRETUR) and/or the CEO (CEOTUR) safeguards board members independence and as a consequence maximise firm's value.

[4] The return of a share is calculated by the following formula (Padjt+Divt–Padjt–1)/Pt–1. The return of the share price covers the period from the beginning to the end of the fiscal year. The fiscal year coincides with the calendar year.
$Padj_{t-1}$ the share price adjusted to the changes in firm's share capital from the beginning of the fiscal year, $Padj_t$ the share price adjusted to the changes in firm's share capital in the end of the fiscal year, Div_t dividend paid in the first six months after the end of the fiscal year.

[5] The growth of a company is estimated by the ratio of the market value of a firm to the book value of its equity.

[6] According to Ferris et al. (1990), when board members of a firm participate in the board of directors of other corporations they acquire valuable experience and as a consequence they can contribute to the efficient administration of the firm. (See also Fama and Jensen, 1983).

[7] In model 2 is not included the variable (PENS) since in the sample examined in this study there was no company in which a pension fund owned more than 5 % off its share capital.

5. RESULTS

In tables 3a, 3b, 3c, and 3d are presented the descriptive statistics regarding the abnormal returns (ABNRET) of the shares included in the sample. In the same tables are presented the descriptive statistics of the corporate governance variables that have been hypothesized to explain the observed abnormal returns.

Table 3. Descriptive statistics

Table 3a

Year 2000	*Mean*	*25%*	*Median*	*75%*	*Std. Dev.*	*Observations*
ABNRET	0.0379	-0.3074	-0.1741	0.0050	0.6125	176
OUTDIR	0.0000	0.0000	0.0000	0.0000	0.0000	176
DIVER	0.6152	0.4883	0.6309	0.7347	0.1822	176
INSTBLOCK	0.2081	0.0000	0.0526	0.5001	0.2671	176
INTBLOCK	0.2736	0.2051	0.2253	0.4426	0.2445	176
DIREXP	3.8032	0.0000	4.0000	6.0000	2.5115	176
BOARDSIZE	7.1557	5.0000	7.0000	9.0000	2.5745	176

Table 3b

Year 2001	*Mean*	*25%*	*Median*	*75%*	*Std. Dev.*	*Observations*
ABNRET	-0.0322	-0.1926	-0.0873	0.0780	0.3029	176
OUTDIR	0.0000	0.0000	0.0000	0.0000	0.0000	176
DIVER	0.6172	0.5001	0.6490	0.7329	0.1754	176
INSTBLOCK	0.2360	0.0000	0.0950	0.5014	0.2725	176
INTBLOCK	0.2637	0.0000	0.1954	0.4415	0.2512	176
DIREXP	3.9855	1.0000	4.0000	6.0000	2.5969	176
BOARDSIZE	7.1884	5.0000	7.0000	9.0000	2.3785	176

Table 3c

Year 2002	*Mean*	*25%*	*Median*	*75%*	*Std. Dev.*	*Observations*
ABNRET	0.0381	-0.1088	0.0182	0.1634	0.2527	176
OUTDIR	0.3015	0.2222	0.2857	0.3813	0.0976	176
DIVER	0.6305	0.4879	0.6462	0.7452	0.1697	176
INSTBLOCK	0.2245	0.0000	0.0533	0.4855	0.2787	176
INTBLOCK	0.2757	0.0000	0.2349	0.4679	0.2398	176
DIREXP	4.0967	0.0000	4.0000	6.0000	2.6046	176
BOARDSIZE	7.4623	6.0000	7.0000	9.0000	2.3245	176

Table 3d

Year 2003	*Mean*	*25%*	*Median*	*75%*	*Std. Dev.*	*Observations*
ABNRET	0.0114	-0.1752	-0.0318	0.1369	0.3940	176
OUTDIR	0.3067	0.2222	0.2857	0.3750	0.0981	176
DIVER	0.6191	0.4799	0.6368	0.7431	0.1705	176
INSTBLOCK	0.2372	0.0000	0.1335	0.4881	0.2682	176
INTBLOCK	0.2643	0.0000	0.2227	0.4539	0.2371	176
DIREXP	4.3239	3.0000	4.0000	7.0000	2.8844	176
BOARDSIZE	7.8776	6.0000	7.0000	9.0000	2.2919	176

Where, $ABNRET_{i,t}$: Abnormal stock returns estimated as the return of the share of company i for the year t minus the return of the General Index of the Athens Stock Exchange , DIVER : The percentage of shares owned by blockholders, $OUTDIR_{i,t}$: proportion of independent members of the board of directors (OUTDIR) for the company i in year t, $INSTBLOCK_{i,t}$: Percentage of the outstanding shares owned by institutional blockholders for the company i in year t $INTBLOCK_{i,t}$: Percentage of the outstanding shares owned by blockholders who have professional relationship with the company in which they own shares for the company i in year t, $BOARDSIZE_{i,t}$: The number of the members of the Board of directors for the company i in year t, $DIREXP_{i,t}$: The experience of the members of the board of directors of company i in year t.

In year 2002 (the first year of the corporate governance law implementation) the value of median for the abnormal stock returns has a positive sign, while for the years 2000, 2001 and 2003 the corresponding values have negative signs.

The percentage of independent non-executive directors (OUTDIR)[8] is around 29% of the total number of the board memberss. This percentage is considered to be high, if it is taken into consideration that according to the relevant Law there should be at least two independent members among the non-executive directors. The total percentage of the non-executive directors constitutes the 33 % of the total number of the board members for the companies included in the sample.

The percentage of share capital controlled by blockholders (DIVER) does not appear to vary significantly during the period 2000-2003. This

[8] The term «independent non-executive members of the board of directors» was used in the companies' annual reports before the introduction of the legislation about corporate governance. However, since the particular legislation provides a precise definition of what constitutes an independent non-executive board member and obliges the firms to appoint independent non-executive board members, it is assumed that in the period before the introduction of the relevant legislation there were no independent non-executive members in the sense that is described in the relevant legislation.

percentage varies between 63% and 65%. No significant change is observed regarding the proportion of share capital owned by internal shareholders (INTBLOCK), which during the period under investigation was around 22%. A significant change is observed concerning the percentage of shares controlled by institutional investors (INSTBLOCK). The average percentage of share capital controlled by institutional investors for the period 2000-2002 was 6,69%, while the corresponding percentage for the year 2003 is 13,35%.

As it has been mentioned earlier, the legislation requires that non-executive directors should constitute at least the 33% of the total number of the board members. Both the mean and the median regarding the number of the board members (BOARDSIZE) indicate that companies have appointed new non-executive directors in order to achieve this percentage. Both the mean and the median regarding the experience of the members of the board of directors (DIREXP), has not changed significantly during the period 2000-2003.

The comparison of the mean values (Table 4) and the median values of the abnormal stock returns (Table 5) for the years 2001 and 2003 indicate that there is no statistically significant difference in the corresponding values for the period prior to and after the implementation of the corporate governance principles.

Table 4. Comparison of the mean values of abnormal stock returns

Variables	*Mean*	*t-test*	*P-value for difference*
ABNRET01	-0.0322	1.1548	0.2490
ABNRET03	0.0114		

Table 5. Comparison of the median values of abnormal stock returns

Variables	*Mean*	*t-test*	*P-value for difference*
ABNRET01	-0.0873	1.2512	0.2109
ABNRET03	-0.0318		

ABNRET01: Abnormal stock returns for year 2001.
ABNRET03: Abnormal stock returns for year 2003.

In order to investigate which corporate governance mechanisms influence stock returns, the model (1) has been estimated by using as a dependant variable the abnormal stock returns of the companies listed in the Athens Stock Exchange and as independent variables certain corporate governance mechanisms (Table 6).

The value of F-statistic indicates that the particular regression model explains 2,63% of abnormal stock returns.

The coefficients for the proportion of independent board members (OUTDIR) and the existence of internal audit mechanism (INTAUD) are not significantly associated with abnormal stock returns. This result can be attributed to three factors:

- The corporate governance variables imposed by the L.3016/2002 do not improve the decision taking process of a firm. As a consequence the fundamental economic value of a firm is not affected by the introduction of corporate governance mechanisms.

- The fundamental economic value of a firm is affected by the introduction of corporate governance mechanisms but due to the fact that the Greek stock market is not efficient share prices do not reflect firm's fundamental economic value.

- The investors have reservations regarding the positive influence that corporate governance principles have on the companies' performance. As a result, they do not have a psychological incentive to buy shares of companies that implement corporate governance principles. Therefore, the stock value of a firm is not affected by the adoption of corporate governance mechanisms.

The findings of this study with respect to the association between abnormal stock returns and the existence of independent non-executive board members are consistent with the findings of Bhagat and Black (2002). Bhagat and Black (2002) did not find any evidence to support the argument that there is an association between the two variables. Conyon and Peck (1998) maintain that the asymmetry of information that exists between executive and non-executive board members can explain the above observation.

According to Nickell (1995), the prime concern of independent non-executive board members is to secure that they will be reappointed to the board of directors. Hence, they do not have a particular motive to replace the senior managers of a firm when the firm's performance is not considered to be satisfactory. Chalevas (2007) points out that after the year 2002 (the first year of the Law 3016/2002 implementation) independent non-executive members get used to the privileges with which board membership is related and tend to go along with managers' wishes.

The fact that there is no significant association between the existence of the internal audit mechanism and the abnormal stock returns can be mainly attributed to the perceived lack of independence of internal auditors from the firm's management (Quick and Warming-Rasmussen, 2005). On the basis of these results, it can be concluded that the hypothesis (**H1**) that stock returns are positively associated with the implementation of corporate governance principles cannot be accepted.

CEO duality (CEODUAL) is not associated with stock returns. As a consequence the hypothesis (**H2**) that the existence of CEO who serves also as board chair affects negatively stock returns cannot be accepted. This finding is consistent with relevant findings of Baliga et al. (1996) and Brickley et al. (1997).

Table 6. Model 1

$ABNRET = b_0 + b_1 INTAUD_{i,t} + b_2 D^* OUTDIR_{i,t} + b_3 CEODUAL_{i,t} + b_4 INSTBLOCK_{i,t} + b_5 INTBLOCK_{i,t} + b_6 D^*BOARDSIZE_{i,t} + b_7 GROWTH_{i,t} + b_8 CODESECTOR_{i,t} + b_9 DIREXP_{i,t} + b_{10} PRETUR_{i,t} + b_{11} CEOTUR_{i,t} + \varepsilon_{i,t}$													
Ex. Sign	+	+	-	+	-	-	+	?	+	+	+		
b_0	b_1	b_2	b_3	b_4	b_5	b_6	b_7	b_8	b_9	b_{10}	b_{11}	Adj. R^2	F-statistic
0.0638	-0.0663	-0.1342	0.0212	0.0090	0.1769	0.0122	1.43E-05	-0.0026	-0.0088	-0.0265	0.0709	0.0263	(2.2710)**
(0.7517)	(-0.9557)	(-0.9461)	(0.5792)	(0.1230)	(1.9476)*	(1.9407)*	(1.4121)	(-1.8932)*	(-1.1524)	(-0.5772)	(1.3659)		

$ABNRET_{i,t}$:Abnormal stock returns, estimated as the return of the share of company i for the year t minus the return of the General Index of the Athens Stock Exchange, D : dummy variable, equals to one for the period after the adoption of the principles of corporate governance by the companies, $INTAUD_{i,t}$: dummy variable, equals to one when there is an internal audit department in the company i in year t, $D^*OUTDIR_{i,t}$: A variable that represent the impact of the application of principles of corporate governance on the proportion of independent members of the board of directors, OUTDIR) for the company i in year t,,$CEODUAL_{i,t}$: Dummy variable, equals to one if the CEO is the president of the board of directors for the company i in year t, $INSTBLOCK_{i,t}$: Percentage of the outstanding shares owned by the institutional blockholders for the company i in year t,INTBLOCKi,t : Percentage of the outstanding shares owned by the blockholders who have professional relationship with the company in which they own shares for the company i in year t , D*BOARDSIZEi,t : Variable which represents the interaction between the adoption of the principles of corporate governance by a firm and the size of the Board of directors for the company i in year t, GROWTHi,t : The growth rate of the corporation for the company i in year t , CODESECTORi,t : The sector in which a company i belongs in year t, DIREXPi,t : The experience of the members of the board of directors of company i in year t. It is measured through the number of firm's directors that they members of the board of directors of other corporations, PRETURi,t : Dummy variable equals to one if there have been a replacement of the president of the board of directors of the company i in the previous year, CEOTURi,t : Dummy variable equals to one if there have been a replacement of the CEO of the company i in the previous year
The regression is calculated by the least squares method.
White's (1980) t-statistics in parentheses
* Significant at the 10%.confidence level
** Significant at the 5%.confidence level
*** Significant at the 1%.confidence level.

Table 7. Model 2

$ABNRET = b_0 + b_1 INTAUD_{i,t} + b_2 D^* OUTDIR_{i,t} + b_3 CEODUAL_{i,t} + b_4 INTBLOCK_{i,t} + b_5 BANKS_{i,t} + b_6 INSCO_{i,t} + + b_7 INVCO_{i,t} + b_8 OTHERCO_{i,t} + b_9 D^*BOARDSIZE_{i,t} + b_{10} GROWTH_{i,t} + b_{11} CODESECTOR_{i,t} + + b_{12} DIREXP_{i,t} + + b_{13} PRETUR_{i,t} + b_{14} CEOTUR_{i,t} + \varepsilon_{i,t}$																
Exp. sign	+	+	-	-	+	+	-	+	-	+	?	+	+	+		
b_0	b_1	b_2	b_3	b_4	b_5	b_6	b_7	b_8	b_9	b_{10}	b_{11}	b_{12}	b_{13}	b_{14}	Adj. R^2	F-statistic
0.0767	-0.0643	-0.1413	0.0231	0.1537	-0.0255	0.0679	-0.0499	-0.0254	0.0126	1.47E-05	-0.0026	-0.0094	-0.0304	0.0823	0.0248	(1.9435)**
(0.9149)[a]	(-0.9172)	(-1.0090)	(0.6262)	(1.6132)	(-0.4942)	(0.9976)	(-0.2729)	(-0.5987)	(2.0760)**	1.4531	(-1.8944)*	(-1.2858)	(-0.6339)	(1.5404)		

Where:
$BANKS_{i,t}$: Dummy variable equals to one if a bank is the major block-holder of the company i in the year t, $INSCO_{i,t}$: Dummy variable equals to one if an insurance company is the major block-holder of the company i in the year t, $INVCO_{i,t}$: Dummy variable equals to one if an investment company is the major block-holder of the company i in the year t, $OTHERCO_{i,t}$: Dummy variable equals to one if another legal entity is the major block-holder of the company i in the year t.
Refer to table 6 for the other variables definition.
White's (1980) t-statistics in parentheses
* Significant at the 10%.confidence level
** Significant at the 5%.confidence level
*** Significant at the 1%.confidence level.

A significant positive association has been observed between abnormal stock returns and the existence of inside shareholders (INTBLOCK) who control more than 5 % of firm's share capital. Although the sign of the coefficient was expected to be negative (**H5**), the results indicate that the association is a positive one. A possible explanation for this result is that, owner-managers' interests are aligned with shareholders interests and as a consequence they aim to maximize firm's value (Berle and Means, 1932; Jensen and Meckling, 1976; Singh and Harianto, 1989; Jensen 1993; Vafeas 1999; Gugler et al., 2003). On the basis of these results it can be concluded that the hypothesis according to which internal shareholders that own more than 5 % of the outstanding shares (INTBLOCK) affect negatively stock returns cannot be accepted.

A significant positive association is observed between the size of the board of directors (BOARDSIZE) and the abnormal stock returns. The sign of the coefficient is not the expected one. Therefore, the hypothesis that the stock returns are negatively correlated with the size of the board of directors (**H6**) cannot be accepted. Lipton and Lorsch (1992) argue that in large boardrooms, an allocation of duties and responsibilities takes place. As a result, board members can monitor and control management more effectively. Anderson et al. (2004) maintain that when the board of directors has many members, a more accurate recording and reporting of firm's transactions is achieved. Within this framework, it appears that as the number of the board members increases, a more efficient use of firms' resources is achieved. As a result, the value of the firm increases.

Stock returns do not appear to be associated with the percentage of the outstanding shares owned by institutional investors (**H3** and **H4**). This result is consistent with the findings of Karathanasis et al. (2004). Karathanasis et al. (2000) argue that stock returns are mainly affected by firm's reported results and not from the fact that institutional investors control a proportion of firm's share capital.

The effectiveness of the control exercised by institutional investors is conditioned upon the type of the institutional investor (Maury and Pajuste, 2004; Shivdasani, 1993; and Sudarsanam, 1995). The institutional investors are analyzed in the following categories: banks, investment companies, insurance companies and other legal entities (Table 7). The values of the coefficients are not statistically significant. Hence, hypotheses 3 and 4 cannot be accepted. These findings are in line with the findings of Gorton and Kahl (1999). They point out that institutional investors cannot effectively control the firm's management. Thus, the fact that they are shareholders of a firm does not affect firm's share price.

The independent variables of the estimated models have been controlled for a multicolliniarity problem. According to Belsey et al. (1980), an indication of multicolliniarity exists when Condition Index takes values above 30. The Condition Indexes for the models (1) and (2) are 11,84 and 12,05 respectively. Therefore, no indication has been found that the two models suffer from a multicolliniarity problem.

6. CONCLUSIONS

This study empirically investigates the effect of corporate governance mechanisms, introduced by the corporate governance law (L.3016/2002), on abnormal stock returns for firms listed in the Athens Stock Exchange.

It has been hypothesized that the introduction of corporate governance principles will positively affect firms' values. No evidence has been found to support this hypothesis. Neither of the two corporate governance mechanisms provided by the legislation (i.e. internal audit, and independent non-executive directors) is significantly associated with abnormal stock returns. On the basis of these results it can concluded that the fundamental economic value of a firm is not affected by the introduction of corporate governance mechanisms. Alternatively, it can be argued that the fundamental economic value of a firm is affected by the introduction of corporate governance mechanisms but due to the fact that the Greek stock market is not efficient share prices do not reflect firm's fundamental economic value. Besides, investors may not be convinced that corporate governance mechanisms significantly affect the performance of a company.

A further investigation is required in order to explain why investors do not seem to believe that the introduction of corporate governance principles contributes in the increase of a firm's value. For instance, it can be examined the extent to which internal audit mechanism is independent – or perceived to be independent - from interventions by the management of a firm. In addition, it can be investigated the extent to which independent non-executive board members execute effectively their duties as safeguards of shareholders interests.

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