

THE EFFECTIVENESS OF GOVERNANCE MECHANISMS IN EMERGING MARKETS: A REVIEW

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Abstract

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Corporate governance has advanced hugely in the last two decades and many governance best practices have emerged that focuses on measures companies should take in order to improve their governance. These suggested mechanisms are effective in developed markets because they are a remedy for problems that occur in those markets. But are these mechanisms also effective in emerging markets? By reviewing the literature, this paper critically discusses and compares the effectiveness of governance mechanisms (both internal and external) in emerging and developed markets and finds that while the classic mechanisms such as board structure and independence are not effective in emerging markets, there exist some alternative mechanisms such as external audit or dividend policy that are more effective.

Keywords: Corporate Governance, Emerging Markets, Governance Mechanisms

Authors' individual contribution: Conceptualization - M.R.; Methodology - M.R., and N.R.; Writing - M.R., and N.R.

1. INTRODUCTION

The separation of owners and managers creates the need for corporate governance, which comprises of mechanisms that ensure efficient decision-making and maximizing the value of the firm. Corporate scandals such as those involving Enron and WorldCom have exposed failures in corporate governance that shook the economies of developed countries and led to a wide-ranging re-examination of standards for corporate governance. The Sarbanes-Oxley Act of 2002 and the subsequent regulations by SEC and other regulatory agencies resulted in better governance in the US and other developed countries. In developing countries, market crises such as the Asian crisis of 1997 have drawn attention to the weak corporate governance in emerging markets. Moreover, the globalization of investors has increased the need for more effective monitoring mechanisms and better corporate governance systems in those markets. There are several mechanisms that help solve corporate governance problems (Fama, 1980; Fama & Jensen, 1983; Armstrong, Blouin, Jagolinzer, & Larcker, 2015; McCahery, Sautner, & Starks, 2016): internal mechanisms such as managerial compensation, the

board of directors, control by large incumbent shareholders or leverage (Jensen, 1986); and external mechanisms such as the market for corporate control (Del Bo, Ferraris, & Florio, 2017), the market for managers, and the market for products and services. These mechanisms have been widely discussed in the literature in the context of developed countries such as the US, UK and European countries, which has given rise to many governance best practices in the last two decades.

The recommended best practices have been formulated by the regulatory agencies in the developed countries considering the governance challenges that are faced in those countries. That is the reason why these best practices have been effective in developed countries. However, one could argue that these recommended mechanisms may not be effective in emerging markets since those markets have different political, regulatory, and social backgrounds than the developed markets. In fact, emerging markets are associated with higher ownership structure, weaker regulatory systems, weaker transparency and less developed financial markets, thus mechanisms that are effective in developed markets may not be that effective in these markets. Therefore, the application of corporate

governance best practices should be different in developed and emerging markets. Moreover, the recommended best practices are designed to solve the basic agency problem (between the outside shareholders and management) and are unusable in emerging markets in which the highly concentrated ownership results in an agency problem between the owners and minority shareholders. That is the reason why corporate governance standards are lower in emerging markets than in developed countries.

The objective of this article is to organize and summarize existing theoretical and empirical works on corporate governance mechanisms; to identify that the mechanisms are more (less) effective in emerging markets and to highlight the alternative mechanisms that could help the emerging economies to reach a better corporate governance. This article summarizes existing research on corporate governance along three tracks. First, we want to understand the concept of corporate governance and its mechanisms. Second, we will do a critical review of the validity of these mechanisms in emerging economies and third, we find some alternative mechanisms for emerging countries.

The remainder of this paper is divided into five sections. The first section defines the concept of corporate governance; the second section outlines the corporate governance mechanisms; the third section studies the emerging markets and their corporate environments; in the fourth section the challenges of corporate governance implementation in emerging markets will be reviewed and section five highlights the alternative mechanisms that are used in emerging markets; then we conclude.

2. CONCEPT OF CORPORATE GOVERNANCE

Although some of the major problems that emerge with the division of ownership and management have been discussed by Berle and Means in 1932, the term “corporate governance” was not born until the 1980s. “Corporate governance” is relatively a new term and has been used widely only after the mid-1990s. Notwithstanding the enormous interest in corporate governance among researchers, there is no definition that is universally accepted.

Zingales (1998) assert the view that “allocation of ownership, capital structure, managerial incentive schemes, takeovers, board of directors, pressure from institutional investors, product market competition, labour market competition, organizational structure, etc., can all be thought of as institutions that affect the process through which quasi-rents are distributed” (p. 2). He explains “corporate governance” as “the complex set of constraints that shape the ex-post bargaining over the quasi-rents generated by a firm” (Zingales, 1998). Williamson (1985) expresses a similar definition.

Shleifer and Vishny (1997) clarify corporate governance by claiming that it “deals with the ways in which suppliers of finance to corporations assure themselves of getting a return on their investment” (p. 737). John and Senbet (1998) propose the more extensive interpretation that “corporate governance deals with mechanisms by which stakeholders of a corporation exercise control over corporate insiders

and management such that their interests are protected.” They define that stakeholders are not just shareholders, but also debt holders and even non-financial stakeholders such as employees, suppliers, customers, and other interested parties.

There are numerous definitions of corporate governance which all have some elements in common. They all do agree that there are conflicts of interest between insiders and outsiders resulted from the separation of ownership and control over the division of the company’s wealth (Jensen & Meckling, 1976). They also acknowledge that such problem cannot be resolved by complete contracting because of asymmetric information, notable uncertainty and contracting costs in the relationship between insiders and capital providers (Hart & Moore, 1990; Grossman & Hart, 1986). And finally, most of the definitions suggest some external or internal mechanisms to control the resulting conflicts.

2.1. Agency theory

Jensen and Meckling (1976) define the agency relationship as a contract under which one party (the principal) engages another party (the agent) to perform some service on their behalf which involves delegating some decision-making authority to the agent. Corporate managers serve as agents for owners. These agency problems arise because of the impossibility of perfectly contracting for every possible action of an agent whose decisions affect both his own welfare and the welfare of the principal, Brennan (1995). Agency theory analyzes the conflicts of this type of relationship. It is inherently impossible to represent the principals’ viewpoint in all respects (Jensen & Meckling, 1976). Managers are self-interested and they are likely to pursue their own well-being at the expense of shareholders’ value. Growth of the corporation is associated with larger compensation packages, promotions and more power for these executives (Jensen, 1986); therefore, managers’ tendency is to expand the companies they control, sometimes beyond optimal levels. Agency costs arising from divergences of interests between shareholders and corporate managers can be seen as the value loss to shareholders. As with any other costs, agency problems will be captured by financial markets and reflected in a company’s share price. A basic factor in the survival and success of corporations is the control and monitoring of agency problems (Fama & Jensen, 1983).

Agency cost will decrease if and when managers can be induced to act in the best interests of shareholders (Jensen & Meckling, 1976). To do so, Denis (2001) proposes three devices that can encourage management to act in this way: contractually bonding management, providing contractual incentives, and monitoring management activities. Monitoring, however, is a necessary condition for using the first two devices. Contractually bonding management requires investigating and monitoring the possible contingencies and actions that a manager should take. Incentive contracts also require monitoring to evaluate the agent’s performance and provide

incentives accordingly (Denis, 2001). Thus, an effective monitoring mechanism is required for all situations to induce management to work in the interests of shareholders (Shleifer & Vishny, 1997).

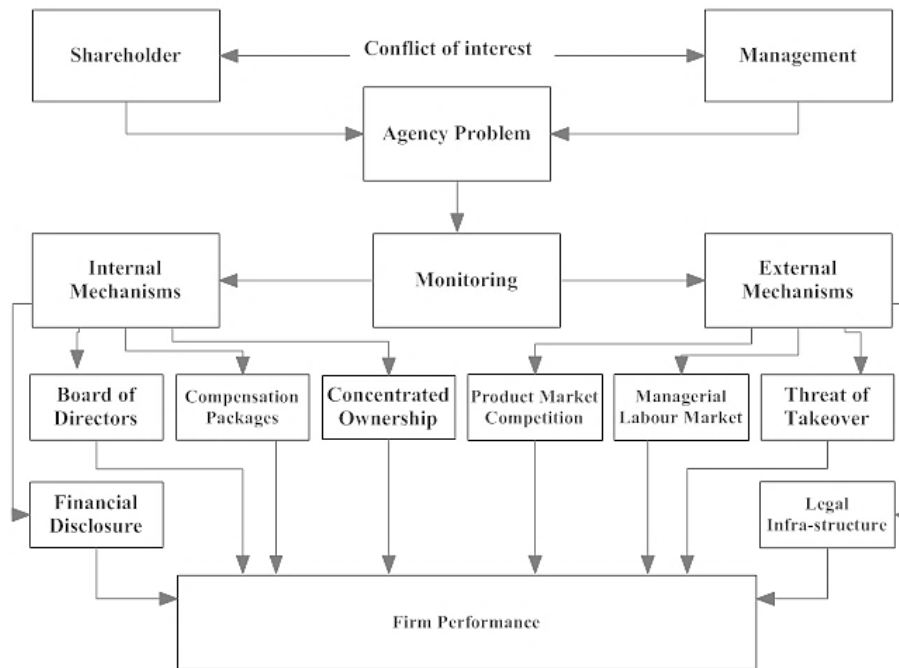
In the next section, we review the corporate governance mechanisms that are widely used in many countries.

3. CORPORATE GOVERNANCE MECHANISMS

To reduce agency costs which lead to better firm performance, the agency theory implies that top

management should be monitored. Corporate governance introduces monitoring mechanisms designed to align management and shareholder interests. These mechanisms are divided into different groups. Internal mechanisms are what the shareholders designed to monitor top management, and the external mechanisms are the pressure by the market to a non- or low-performing company or regulations that the company must comply with. Figure 1 shows how different corporate mechanisms affect corporate performance.

Figure 1. Conceptual model of corporate governance mechanisms and their impact on company performance



Source: Adapted from "Corporate governance mechanisms and their impact on company performance: A structural equation model analysis", by M. I. Azim, 2012, *Australian journal of management*, 37(3), p. 4.

There are numerous studies that investigate the impact of corporate governance mechanisms on firm performance. This literature will be briefly summarized.

3.1. Monitoring by the board of directors

According to Fama and Jensen (1983), the responsibilities of the board of directors are to endorse management decisions and to monitor management performance. The board of directors should act as professional umpires who have the duty of supervising the competition between top managers and monitor managers on the basis of their performance in the company. Also, directors choose the CEO and direct the company to achieve its mission thus they are responsible to shareholders and stakeholders. Shareholders should make sure that the decision-making process in a company is not controlled by an individual or a particular group.

3.1.1. Board size

In the literature, the direction of the influence of the board size on firm performance is unclear (Kent &

Stewart, 2008). Several studies suggest that it takes more effort for a larger group to reach consensus, and thus the final decisions of larger groups reflect more compromises and are less extreme than those of smaller groups (Kogan & Wallach, 1966; Moscovici & Zavalloni, 1969; Sah & Stiglitz, 1986, 1991). Moreover, some researchers assert that larger boards are less effective monitors due to potential free-riding, communication breakdowns and inefficiencies (Boo & Sharma, 2008; Bushman, Chen, Engel, & Smith, 2004; Sakawa & Watanabel, 2018). Jensen (1993) suggests that it is easier for the CEO to influence and control a large board and CEO power in decision-making increases with board size. This line of literature finds a negative relationship between the size of the board and company performance (Yermack, 1996; Gilson, 1990; Loderer & Peyer, 2002). On the other hand, there are prominent other studies that find a positive relationship between size of the board and both company performance (Chiang, 2005; Haniffa & Hudaib, 2006; Scafarto, Ricci, Della Corte, & De Luca, 2017) and board monitoring (Anderson, Mansi, & Reeb, 2004; Williams, Fadil, & Armstrong, 2005). According to them, larger boards usually consist of

directors from various educational backgrounds and skills, and CEO dominion is more difficult in larger boards, therefore, the quality of decisions taken by the board improves and directors would have a greater power in the governance of the firm (Bacon, 1973; Herman, 1981; Abdul Gafoor, Mariappan, & Thyagarajan, 2018).

Too few directors could lead to a suboptimal decision-making body. On the other hand, too large a board may also be negatively related to performance. There exists an optimal board size in which there is equilibrium between the skills and expertise of the board and the difficult dynamics of a large board. At this optimal level, the board is at its best effectiveness.

3.1.2. Independent directors

There is a difference between the counselling power and the monitoring power of the board. Boards of directors' ability to act as effective monitoring mechanisms rely on their independence from management (Beasley, 1996). Researchers have focused on the proportion of executives to independent directors as an indicator of board independence (Davidson, Goodwin-Stewart, & Kent, 2005; Koh, Laplante, & Tong, 2007; Peasnell, Pope, & Young, 2005). Some previous studies have suggested that independent directors are effective monitors because they do not have financial interests in the company or psychological ties to management (Boo & Sharma, 2008). Zahra and Pearce (1989) contend that the existence of independent directors in the board may increase the quality of directors' decisions, provide strategic direction and improve the overall performance because they are in a better position to objectively challenge management. Bedard and Johnstone (2004) also argue that higher independent director representation on the board provides more vigilant oversight of the monitoring process.

In recent research, Onyina and Gyanor (2019) find a significant positive relation between independence and firm value and argue that the efficiency of independent directors relies on their ability to proactively represent shareholders' interest without fear or favour. On the other hand, the theory suggests that in some circumstances less independent boards can benefit shareholders (Adams & Ferreira, 2007; Harris & Raviv, 2008). Bhagat and Black (1999) question the presence of majority independent directors on the board and find that there is no convincing evidence that greater board independence correlates with greater firm profitability or faster growth. Adam and Ferreira (2007) posit that when directors are independent, the CEO is reluctant to reveal private information. This is because revealing what really underlies some proposed policy might prompt the board to intervene in favour of shareholders. The manager thus protects him or herself from monitoring. Less informed directors, in turn, reduce the overall quality of board counselling power. However, they mention that dependent boards cannot supervise and discipline managers efficiently.

Too few independent directors on the board could lead to a bigger agency problem. On the other

hand, the supermajority independent board may also be negatively related to performance. There should exist an optimal percentage of independent directors on the board which counselling power of the board is in equilibrium with its monitoring power. At this optimal level, the board is at its best effectiveness.

3.1.3. CEO and chairman role separation

As the Chairman leads the company, a chief executive officer runs it. A number of studies discuss the relationship between leadership structure and performance. The leadership structure of the company refers to the relationship between the CEO and the Chairman of the Board. CEO duality is a situation where the CEO of the firm is simultaneously the Chairman of the Board. Some studies show that CEO duality increases agency problem because the chairman is supposed to monitor the performance of the CEO. The dual role of the CEO as board chairman threatens the ability of the board of directors to maintain its independent judgment. CEO duality can increase the conflict of interest as reported by Fama and Jensen (1983), and Jensen (1993).

Empirical studies on the effects of CEO duality on corporate performance have yielded mixed results. Berg and Smith (1978), and Chaganti, Mahajan, and Sharma (1985) find no association; Pi and Timme (1993) indicate the firms with separation of roles have better performance compared to those with CEO duality. Scafarto et al. (2017) find a positive association between CEO duality and firm performance and Baliga, Moyer, and Rao (1996) find mixed results on this question. Scafarto et al. (2017) find that combining both roles into a single position is detrimental to firm performance because it weakens board control efficiency. In the gap of concrete results on the effects of CEO duality, this paper proposes that CEO duality will affect the board's performance.

3.1.4. Board meetings

The Board of Directors should meet frequently to discuss and to find a solution to the issues of the company. A common criticism of corporate boards is that outsiders are not given enough time to interact with other directors to perform their monitoring role which might lead to low performance of the firm. Vafeas (1999) reported that board meeting frequency is often linked with improved operative performance. Lipton and Lorsch (1992) and Byrne (1996) argue that boards that meet frequently are more likely to perform their duties diligently and are beneficial to shareholders. Similarly, Stein and Zhao (2019) argue that board meeting time can improve the effectiveness of a board. Although there is no worldwide agreement on the number of meetings of the board, too few meetings can be a threat to effective board monitoring and may indicate the directors are not paying proper attention to the company.

3.1.5. Directors' busyness

The monitoring role of the board of directors is an important component of corporate governance. The board of directors performs the monitoring function on behalf of shareholders. It would be difficult for the directors who serve on too many boards to execute their monitoring role efficiently. There are two opposing hypotheses on this issue.

The "reputation hypothesis" posits that the number of outside directorships may indicate director quality (Fama & Jensen, 1983). This hypothesis postulates that directors who serve on many outside boards may be more experienced, provide a better recommendation, and offer better monitoring. Mace (1986) asserted that most CEOs are willing to accept outside directorships because they provide executives with prestige, visibility, and commercial contacts. Gilson (1990) finds that the number of reputed outside directors who sit on the financially distressed firms' board is linked to firm performance.

More recent literature doubts the rationale of holding too many board seats. The "busyness hypothesis" promoted by Ferris, Jagannathan, and Pritchard (2003a) argues that directors with too many outside board seats may become so busy that they do not act as effective monitors. The presence of busy directors on a firm's board reduces oversight of management which might reduce a firm's market value (Masulis, Wang, & Xie, 2012). Fich and Shivdasani (2006) find that firms with busy directors are linked with lower market-to-book ratios, weak corporate governance, less effective boards, the lower sensitivity of CEO turnover to firm performance and weaker profitability. Cashman, Gillan, and Jun (2012) find evidence that busy directors are associated with lower firm performance. However, Tan, Bany-Ariffin, Kamarudin, and Abdul Rahim (2019) argue that directors experience mitigates the negative impact of the busy directors on firm efficiency.

3.1.6. Board committees

Board committees improve the efficiency of board monitoring by affecting closer scrutiny of management activities and decision-making. Also, board effectiveness is actuated through board committees (Jiraporn, Singh, & Lee, 2009). Not only are some of the most significant decisions initiated at the committee levels (Kesner, 1988), functioning and structure of important committees like finance and accounting committees may influence corporate performance (Klein, 1998). Committees influence corporate strategies (Vance, 1983) and reduce agency problems (Davidson, Pilger, & Szakmary, 1998). Establishing three different committees of the board is recommended: audit, nominations and remuneration committees.

A board audit committee focuses on issues relevant to the integrity of the company's financial reporting (Chen & Zhou, 2007; Davidson et al., 2005). Audit committees have received considerable attention following corporate scandals (Sarens, De Beelde, & Everaert, 2009). Prior research has found that an audit committee meeting frequently can

reduce the incidence of financial reporting problems (Farber, 2005; Kang, 2019). It is recommended to the audit committee to consist of independent directors, to meet frequently (Farber, 2005) and directors should be familiar with accounting mechanisms (Karamanou & Vafeas, 2005).

A board remuneration committee is an efficient mechanism for focusing the company on appropriate remuneration policies that correspond with the performance of senior executives. Appropriate remuneration packages motivate top management to perform more efficiently in order to increase firm performance (Kanapathippillai, Gul, Mihret, & Muttakin, 2019). It is recommended to the remuneration committee to meet frequently and to consist of independent directors (Bosch, 1995).

The monitoring ability of the nomination committee depends on their independence and the frequency of meetings (Leblanc, 2004). As provided by the literature, active committees provide the board with quality decisions that can increase the effectiveness of the board (Lamoreaux, Litov, & Mauler, 2019; Appiah & Chizema, 2016).

3.1.7. Compensation packages

In order to create strong incentives for the CEO to act in the firm's best interest, the board of directors provides CEOs with compensation packages. Therefore, the level of compensation and the extent of pay-for-performance for CEOs have been a topic of considerable controversy in the academic and business communities. It is remarkable that, although numerous papers have studied the subject, there is no real consensus on the relationship between executive pay and firm performance. Defenders of high CEO pay point to skilled CEOs' ability to lead the firms to exceptionally strong performance. From their perspective, high payments to CEOs are considered as an investment in the company. Critics of CEO compensation practices argue that because the board of directors is influenced by the CEO, the board does not structure the CEO's compensation package to maximize value for outside shareholders (Core, Holthausen, & Larcker, 1999). However, effective boards can evaluate and effectuate a proper amount of CEO compensation to align the interest of CEOs to the ones of shareholders.

3.2. Ownership structure

The ownership structure of a company is considered as one of the corporate governance mechanisms to align shareholders' and managers' interests. More concentrated ownership is associated with less agency problem because large shareholders and block holders have a bigger influence on the board and have the ability and incentive to closely monitor management. However, concentrated ownership usually is accompanied by the expropriation of minority shareholders.

On the other side, in dispersed ownership because of the free-rider problem and the costs, shareholders are reluctant to closely monitor the management. This leads to higher agency costs.

3.2.1. CEO equity ownership

Agency problem occurs when the agent and the principals have different interests. Increasing management shareholding mitigates the problem of agency and aligns the interest of agent to that of principals. Jensen and Meckling (1976) argue that managers perform better when they hold ownership stake within the firm. They argue that the managers who have a higher fraction of shares in hand may work harder to improve the performance of the corporation, which leads to an increase in firm value and hence an increase in the managers' private wealth. The agency problem does not exist when the management owns 100 percent of equity. Empirically, Murphy (1985), Morck, Shleifer, and Vishny (1988), Denis and Sarin (1999), Ang, Colwm, and Wuh Lin (1999), and Benson, Lian, and Wang (2016) find that there is an inverse relationship between the manager's ownership share and agency costs.

Managers usually own a very small fraction of the firm's equity. Therefore, for managers, private benefits of control are much higher than their small shareholdings. Even after providing the managers with equity ownership, managers still do not have the proper incentive to act in shareholders' best interest. CEO equity ownership per se is not enough to mitigate agency costs in a firm.

3.2.2. Directors' equity ownership

Kren and Kerr (1997) show that equity ownership by board members provides an incentive to them to act like owners in terms of their monitoring efforts. Higher equity ownership should reduce agency costs. Singh and Davidson (2003) tested the linear relationship and find weak evidence that higher managerial ownership reduces agency costs. Other studies have found a significant non-linear relationship between internal ownership and performance (Morck et al., 1988; McConnell & Servaes, 1990; Denis & Sarin, 1999). They find that high levels of ownership lead to managerial entrenchment. Instead of looking for the effects of internal ownership on firm performance, the relationship between director's equity ownership and effectiveness of the board can be investigated.

3.2.3. Institutional ownership

Due to the free-rider problem, it is costly for small shareholders to act as monitors of management (Grossman & Hart, 1986). On the contrary, larger investors (such as institutional investors) have an incentive to monitor firm management due to the size of their holdings and provide an additional method of monitoring the actions of management. Pound (1988) argues that institutional investors have greater expertise and resources and can monitor management at lower costs than the average. Because of their voting blocks, institutional investors can effect change and mitigate agency problems in the firm (Shleifer & Vishny, 1997; Alderighi, Cleary, & Varanasi, 2019; Lou, Lu, & Shiu, 2020).

Many studies examine the role of institutional

investors as a governance mechanism on the decision-making process of firms. For example, research has examined the influence of institutional investors on anti-takeover charter amendments (Borokhovich et al., 2006), on shareholder voting rights (Li, Ramaswamy, & Pettitt, 2006), on major corporate decisions such as forced CEO turnover (Parrino, Sias, & Starks, 2003), on executive compensation (Hartzell & Starks, 2003; Almazan, Hartzell, & Starks, 2005), and on mergers (Chen, Harford, & Li, 2007). Singh and Davidson (2003) find no evidence that outside block ownership affects agency costs and Doukas, Kim, and Pantzalis (2000) argue that institutions may have neither the time nor expertise to act as effective monitors. These studies provide mixed results as to whether institutional investors act as effective monitors of management and/or whether their governance actions are profitable.

In the real world, institutional owners own large size of the shares and therefore can appoint someone or influence other shareholders to send someone to the board. Due to the large stake of institutional investors in the firm, their representative on the board act in the best interest of that institution. Although the interest of the institution is different than the interest of other small shareholders, the presence of such representative on the board prevents the management to act on their interest and it mitigates the principal-agent problem. Also, the presence of such representative may mean bringing the expertise and resources of that institution to the board that may affect the effectiveness of the board.

3.3. External mechanisms

3.3.1. Debt

Debt holders are the external stakeholders who give loans to corporations and can also function as the corporate governance mechanism. Jensen and Meckling (1976) argue that debt is an important influence on agency costs. McConnell and Servaes (1990) argue that an increase in the proportion of debt may result in increased investment in high-risk projects in an attempt to cover the interest payments so firms with higher levels of debt are more closely monitored by debt holders and therefore managers have less opportunity to pursue non-value maximizing activities. Also, a debt contract will make the manager's work as being part of the owners by making investment decisions and optimal financing, in order to maximize the corporate value for the owners (John & Senbet, 1998).

3.3.2. Takeover market

When the internal governance mechanisms are weak or ineffective, takeovers can alarm the agent as the act of last resort (Jensen & Ruback, 1983; Jensen, 1993; Holmstrom & Kaplan, 2001). Financial economists contend that the existence of external takeover pressure can be a good warning to self-serving agents. The principle can take advantage of the takeover threat to maintain a high management

quality, and accordingly, construct an efficient contract to motivate the agent (e.g., Grossman & Hart, 1986; Jensen, 1993; Shleifer & Vishny, 1997).

A takeover bid may be a “wake-up call” signalling that the target firm was managed inefficiently. Jensen (1988, 1993) argues that the takeover attempts are the signs of ineffective internal governance mechanism. Fama (1980) contends that the takeover bid provides the board an opportunity to review the performance of the manager and accordingly adjust its compensation policy following the bid. These theories all suggest that the market observes a poorly performing firm and bids on them. As a result, either managers take that bid or try to increase their level of governance and performance. Takeover bid happens when internal mechanisms are weak or inefficient. Takeover bid can be a sign of weak effectiveness of the board.

In this section, we discussed and reviewed the classic governance mechanisms in developed countries. However, these mechanisms are the answers to an agent-principal problem that arises in developed countries with widely held companies. In the next section, we will discuss the definition of emerging markets and find the differences between emerging and developed markets.

4. EMERGING MARKETS AND CORPORATE GOVERNANCE

Corporate governance has received much attention in emerging markets. In Asia, many blamed poor corporate governance as one of the causes of the Asian financial crisis of 1997 (Johnson, Boone, Breach, & Friedman, 2000a). In emerging markets, investors have been loudly calling for corporate governance reforms and some institutional investors mentioned corporate governance as a key factor affecting their decision to invest. These are clear messages to the countries in emerging markets: in order to survive, the level of corporate governance should be increased.

The effectiveness of corporate governance mechanisms might be quite different in developed and emerging markets. In emerging markets companies are often closely held (by the founding family), shareholders' legal rights are not protected (due to lower regulations); companies show low transparency; moreover the legal system is feeble, law enforcement is weak and financial markets are malfunctioned. These characteristics in developing countries are often contended to be associated with poor corporate governance. While across many countries in emerging markets policymakers have begun efforts to encourage companies to adopt higher governance standards, corporate governance standards in emerging markets are still far behind those in developed countries.

4.1. Definition of emerging markets

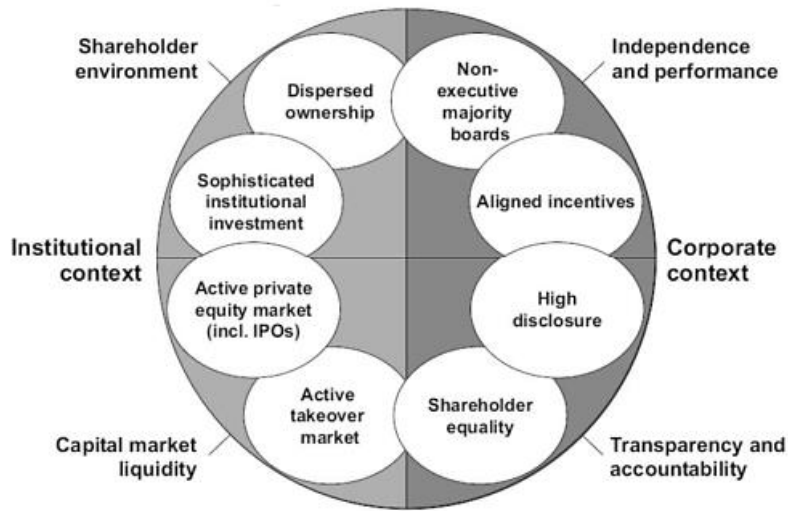
There are a number of ways to define or classify a group of emerging market countries from other transition or less developed economies. According to Hoskisson, Eden, Lau, and Wright (2000) emerging economies are “low-income, rapid-growth countries using economic liberalization as their primary engine of growth” (p. 249). World Bank argues a cut-off point of \$10,000 per capita income to distinguish emerging markets from other less developed economies. According to Chan and Cheung (2008) emerging markets are the markets with newly developed financial market, a short operating history, a smaller capital market and lower trading volume. The strength of economic and political institutions, such as the rule of law, regulatory controls and enforcement of contracts are also important features which may help to distinguish emerging markets from other less developed markets.

4.2. Differences between emerging market and developed market

The governance models in developed countries depend heavily on a particular institutional context, one that has efficient equity markets and dispersed ownership. Together, these contexts characterize the ‘market model’ of corporate governance which is shown in Figure 2. In market-based corporate governance, ownership is dispersed with high engagement of institutional investors; corporate boards have a high proportion of outside or independent members to align managers and shareholders' interest; the external aspects of corporate governance such as audit firms certify the flow of information from managers to capital markets to have more transparency, and the takeover market executes the final mechanism on poorly performing firms, who face a higher risk of a takeover.

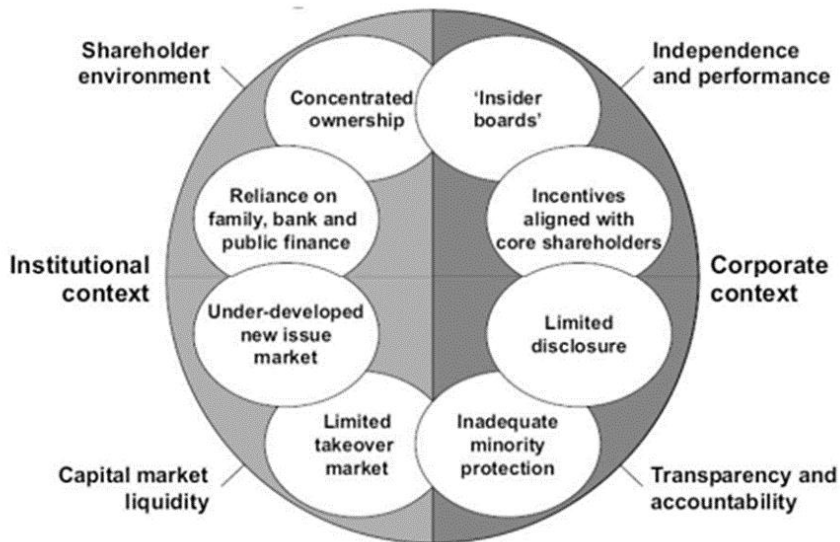
The corporate and institutional context in emerging markets differs significantly from that in the developed countries. Corporate governance practices are tailored to suit the needs of core shareholders. Figure 3 depicts the control model of corporate governance. In this model, equity markets are less developed, ownership is concentrated, boards consist of insiders, disclosure is limited and the reliance is more on family finance. These characteristics are visible in emerging markets. Taking into account these differences between developed and emerging markets, there are numerous challenges to overcome in order to achieve effective corporate governance.

Figure 2. The “market model” of corporate governance



Source: Adapted from “Giving new life to the corporate governance reform agenda for emerging markets”, by P. Coombes, and M. Watson, 2001, *Directorship*, 27(7), 4-8, p. 2.

Figure 3. The “control model” of corporate governance



Source: Adapted from “Giving new life to the corporate governance reform agenda for emerging markets”, by P. Coombes, and M. Watson, 2001, *Directorship*, 27(7), 4-8, p. 3.

4.3. Corporate governance best practice implementation in emerging markets

Emerging markets tend to display weaker measures of corporate governance. There is a great need for corporate governance reform in emerging markets thus a corporate governance best practice must be implemented. But does one size fits all? Policymakers emphasize that there is no one corporate governance best practice. Different environments and backgrounds give rise to specific governance needs; however, emerging market countries may not have enough leverage to develop their own forms of governance and standards and end up employing the OECD principles. These principles may not be appropriate to the immediate

need of these countries and they may be difficult to implement quickly. Also, implementation of these principles is particularly challenging; many emerging economies lack the institutional and human requirements that are critical to the implementation of corporate governance principles. Moreover, there are various political, social, cultural, and economic barriers to the effective implementation of OECD’s corporate governance principles in developing countries. More recent research by Chen, K. C. W., Chen, Z., and Wei (2011) also shows that simply adhering to OECD prescribed best governance practices do not result in better corporate governance in emerging markets, given that corporate governance practices in OECD countries

are not designed to solve the conflicts that arise from a highly concentrated ownership.

In emerging economies, the companies are closely held, and the rule of law and transparency are weak. We discussed that implementing the best practices may not increase the quality of corporate governance in emerging markets. In the next section, we analyze the corporate environment of emerging markets to find the challenges of corporate governance mechanisms' effectiveness.

5. CORPORATE ENVIRONMENT IN EMERGING MARKETS

To understand better the challenges of implementing corporate governance best practices in emerging markets, its corporate environment should be investigated. Corporate environment and characteristics of emerging markets may cause challenges that corporate governance may face in emerging markets.

5.1. Ownership concentration

Unlike companies in the USA or the UK in which shareholders are dispersed, companies in emerging markets are closely held. A typical corporation in emerging economies is owned by members of a family and it may be affiliated to a business group. The group can consist of several family-owned public or private companies that can be controlled by the same family. Often these family-owned companies engaged in cross-shareholding within the business group or with other business groups. These characteristics make the ownership structure very complicated in emerging markets.

5.1.1. Family ownership

In emerging economies, often a family controls a firm (Chen, 2001; Claessens, Djankov, & Lang, 2000; La Porta, Lopez-de-Silanes, Shleifer, & Vishny, 1999; Ilhan-Nas, Okan, Tatoglu, Demirbag, & Glaister, 2018). Family ownership has an informal but powerful influence on the way that organizations are run. The family achieves effective control of the companies in the group by means of stock pyramids and cross-shareholdings. La Porta et al. (1999) investigate the ownership structure in East Asia and show that family owners execute and expand their control over the firm and the group, by the use of pyramiding, management appointments, cross-ownership and the (infrequent) use of shares that have more votes.

Family ownership may reduce agency costs by helping to align ownership with control (Fama & Jensen, 1983; Jensen & Meckling, 1976). Also, it may reduce monitoring costs and increase performance (Lubatkin, Schulze, Ling, & Dino, 2005; ElBannan, 2017). On the other hand, family control may increase the likelihood of expropriation of minority shareholders and can decrease performance (Bloom & Van Reenen, 2006). Sibling rivalry, generational envy, non-merit-based compensation, and 'irrational' strategic decisions can destroy firm value in family businesses (Gomez-Mejia, Nunez-Nickel, & Gutierrez, 2001). Moreover, Schulze, Lubatkin, Dino, and Buchholtz (2001) find that family relations may make agency conflicts "more difficult to resolve"

(p. 102), because relations between principals (family owners) and agents (family-member managers) are based on emotions, sentiments, and informal linkages, resulting in less effective monitoring of family managers.

5.1.2. Business groups

Business groups are pervasive in emerging markets. A business group is "a collection of legally independent firms that are bound by economic (such as ownership, financial and commercial) and social (such as family, kinship and friendship) ties" (Yiu, Bruton, & Lu, 2005, p. 184). Business groups consist of firms that may be a distinct legal entity that publishes its own financial statements, has its own board of directors, and is responsible to its own shareholders. Business groups allow large family businesses with different affiliated companies being run by various family members or branches (Biggart & Hamilton, 1992; Wilkinson, 1996). Business group networks, together with family structure, are some of the key institutions identified by Hamilton and Biggart (1988) as characterizing emerging economies. In business groups, informal ties - such as cross-holdings, board interlocks, and coordinated actions - are strong (Chung, 2006; Dieleman & Sachs, 2006; Chauhan, Dey, & Jha, 2016).

Although business groups can substitute for weak institutional environments in capital, labour, and product markets and provide certain competitive advantages (Guillen, 2000; Li et al., 2006; Wan, 2005) they tend to be large cumbersome organizations that carry coordination and administration costs that causes poor performance (Claessens, Djankov, Fan, & Lang, 2002; Ferris, Kim, & Kitsabunnarat, 2003b). More importantly, due to the low transparency of such loosely affiliated business groups, it is difficult for minority shareholders to determine where control resides. It also makes it hard to identify and control unfair transactions within the group (Chang, 2003) since such networks provide an opportunity for collusion or other unethical actions (Hoskisson et al., 2000). Moreover, controlling shareholders can expropriate the minority shareholders through pyramiding when the control rights of the controlling shareholders are greater than the cash flow rights (Bertrand & Mullainathan, 2002; Claessens et al., 2002). In short, business group affiliation provides a means by which controlling shareholders can expand control and thus increases the likelihood of expropriation of minority shareholders, which causes principal-principal conflicts.

5.1.3. Causes of ownership concentration in emerging markets

Shleifer and Vishny (1997) suggest that the benefits from concentrated ownership are relatively larger in countries that are generally less developed, where property rights are not well defined and not well protected by judicial systems. La Porta et al. (1999) confirm this proposition empirically, showing that the ownership stakes of the top three shareholders of the largest listed corporations in a broad sample of countries around the world are associated with weak legal and institutional environments. The weak state enforcement of property rights is the most

probable cause of the concentrated ownership in emerging market corporations, as they often confront weak legal systems, poor law enforcement, and corruption. The reason for the prevalence of business groups may be the poorly developed external markets (financial, managerial and other factor markets) which tend to favour internal markets for the allocation of resources (Claessens et al., 2002).

5.1.4. Concentrated ownership and agency problems

The ownership structure of a corporation will affect the nature of the agency problems that occur in the firm. When ownership is dispersed, agency problems will arise from the conflicts of interest between managers and outside shareholders (Jensen & Meckling, 1976). Alternatively, when ownership is concentrated to the degree that one owner or one family has effective control of the firm, the nature of the agency problem shifts away from principal-agent conflicts to principal-principal (PP) conflicts where the interests of controlling owner (who may also be the manager) collides with the interests of minority shareholders (Claessens et al., 2002).

5.1.5. Expropriation of minority shareholders

Controlling shareholders may be entrenched or use pyramiding to expropriate minority shareholders. Controlling owners who have the effective control of a firm not only run the company but also decide how profits are being shared. The minority shareholders should receive the profits corresponding to their cash flow rights; Entrenchment occurs when an entrenched owner deprives the minority shareholders of their rights. The separation between ownership rights and control rights can exacerbate the entrenchment problems raised by concentrated ownership (Gonzalez, Molina, Pablo, & Rosso, 2017).

A typical pyramidal business group consists of a collection of legally independent firms, controlled by the family through a chain of ownership stakes. Because the family does not need to retain 100% of the shares to retain control at each chain of the pyramid, pyramidal ownership structures allow for separation of cash flow and control rights and can facilitate family control. Pyramiding occurs when a controlling owner who is on the top of other firms through a chain of ownership, controls a particular corporation indirectly through other corporations. Through pyramid ownership, it is common for a firm's ultimate owners to have formal control rights that are greater than cash flow rights, and this increases the probability of expropriation of the firm. Faccio, Lang, and Young (2001, p. 56) give an example of an investor, who owns 50 per cent of the shares of Company X, which owns 40 per cent of the shares of Company Y, which owns 30 per cent of the shares of Company Z. The investor ends up with 6 per cent (50% x 40% x 30%) of the cash flow rights of Z but 30 per cent of its control rights. While the controlling shareholder is not a majority shareholder of X, Y or Z, but is a controlling shareholder of each of these companies. This creates a moral hazard situation, as the financial benefits

from expropriation outweigh the financial costs for the ultimate owner.

5.2. Weak regulatory systems

According to La Porta et al. (1998), the legal system of a country and specifically the extent of investor protection affect the quality of corporate governance and the development of equity markets (Shleifer & Wolfenson 2002). Adequate regulatory system to protect shareholders' rights is a major consideration to improve the government system in emerging markets. Investor protection and minority shareholder protection laws neither exist nor effectively enforced, thus it is easier for managers or controlling shareholders to expropriate investors' or minority shareholders' rights.

5.3. Weak public governance

The quality of public governance is a crucial determinant of corporate governance practices. In some of the corrupted emerging economies, rent-seeking has often been reported to be an important source of corporate profit (Claessens et al., 2002). Furthermore, in economies where politicians and entrepreneurs collude to extract or protect monopoly rents, high-quality corporate governance practices are unlikely to arise. Also, the quality of public governance affects the level of law enforcement and, in turn, the extent of bribery and other forms of corruption. These factors influence the quality of corporate governance in a country.

5.4. Weak transparency

Public corporations in emerging markets suffer from have low levels of transparency and disclosure quality (Fan & Wong, 2005; Bae & Jeong, 2002; Srairi, 2019). Fan and Wong (2005) report that accounting transparency of firms in seven Asian economies is generally low. They argue that low transparency is related to agency problems and relationship-based transactions. Earnings figures are less informative when controlling owners possess high voting rights and when voting rights substantially exceed cash flow rights. Bae and Jeong (2002) report that firms that are affiliated with business groups show weaker earnings informativeness in Korea. Srairi (2019) reports that only two out of five countries of the Gulf Cooperation Council have a good level of transparency. Millar, Eldomiaty, Choi, and Hilton. (2005) point out that the cost of investing increases in countries where the level of transparency is low. Because of the weak law regulations and enforcement and also low efficiency of board of directors, firms in emerging markets show low transparency. In the absence of adequate laws, controlling shareholder prefers not to disclose company information in order to hide his activities to expropriate minority shareholders or investors.

5.5. Competition restriction

Another problem with corporate governance in a developing country is the restriction of competition. Barriers to competition vary from anti-competitive practices by companies to entry restrictions. Khemani and Leechor (1999) suggest that entry

impediments are normally disguised as regulations that supposedly protect the public interest. They suggest the lack of competition increases the concentration of ownership.

5.6. Financial market

Without a developed financial market, having good corporate governance is impossible. Financial markets in many emerging economies can be characterized as underdeveloped because they operate with various flaws, for example, government overregulation, inefficient legal systems, and direct government lending that competes with private companies. Two particularly important imperfections that recent research focuses on are poorly enforced financial contracts and shallow or immature capital markets (Dimic, Kiviaho, Piljak, & Äijö, 2016; Alhassan & Naka, 2020). In shallow capital markets, the domestic bond and equity markets are generally not big or active enough to offer a lot of liquidity, and only the largest firms can raise domestic financing for their operations. Such immature and illiquid capital markets not only raise the cost of financing, but they also tend to be poor at channelling resources to good investment opportunities. Many times, lending just goes to the largest firms with the most established relationships with banks, and small productive firms are often unable to get the financing they need. This makes an unhealthy environment that impedes corporate governance to flourish.

The corporate environment of emerging markets differs from developed markets. In emerging markets, ownership is concentrated, which causes an agency problem between the controlling and minority shareholders. This principal-principal agency problem combined with the weak rule of law and less transparency in emerging markets results in the expropriation of minority shareholders. Therefore, the effectiveness of classic governance mechanisms may be challenged by the described corporate environment. In the next section, we will discuss in detail the effectiveness of governance mechanisms in emerging markets.

6. CORPORATE GOVERNANCE MECHANISMS AND CHALLENGES IN EMERGING MARKETS

Because of the special environment in emerging markets which is discussed in the last section, the effect of corporate governance mechanisms is different than those in developed countries. In this section these mechanisms and their challenges are studied.

6.1. Monitoring by shareholders

Controlling shareholders in emerging markets are usually the managers that run the firm. They have all kinds of information relating to the firm and they have a big influence on the management. On the contrary, minority shareholders may directly monitor the firm if they hold significant equity stakes. However, it is uncertain whether minority shareholders are effective in monitoring or challenging the usually powerful controlling owners since laws and regulations to protect minority shareholders are weak or may not exist. As it

discussed earlier, due to the nature of ownership in emerging markets and principal-principal agency problem, minority shareholders are often expropriated by block shareholders or owning families who own voting rights more than cash-flow rights. Moreover, recent research suggests that in emerging markets, even large but non-controlling shareholders are not able to contest the power of the main block holders (Crisóstomo, Brandão, & López-Iturriaga, 2020). Expropriation of minority shareholders by controlling shareholders is one of the biggest challenges facing corporate governance in emerging markets.

6.2. Monitoring by the board of directors

In emerging markets boards of directors are typically dominated by insiders and seldom have any outsider as a member. Controlling shareholders can appoint the members of the board of directors and this effectively nullifies a board's ability to monitor controlling shareholders. Therefore, the board is less likely to play a strong monitoring and control role (Peng, 2004; Peng, Buck, & Filatotchev, 2003; Young, Ahlstrom, Bruton, & Chan, 2001; Onyina & Gyanor, 2019).

Saeed, Belghitar, and Yousaf (2016) report that only 34% of the boards of emerging countries (BRIC) consist of independent directors. This number reduces in Russia where boards consist of only 27% independent directors. Yeh (2002) reports that boards of Taiwan corporations are populated with insiders and controlling owners are more likely to insert family members on boards when their voting rights substantially exceed the cash flow rights of the firms. In China, politicians and state-controlling owners occupy most board seats (Chen, Fan, & Wong, 2002). Moreover, they find that the politicians, who lack expertise in accounting or finance, use their administrative power to influence both the markets and the firms in creating economic rents and enforcing transactions. Moreover, Azeez (2015) find the presence of independent directors on the board of Sri Lankan companies is not associated with better performance. In emerging markets, professional directors are in low demand because skillful directors may reveal information that can endanger the firms' rent-seeking activities.

6.3. Institutional investors

When ownership is concentrated, instead of agency conflict between managers and dispersed shareholders, firms are subject to agency conflict between controlling owners and minority shareholders. In order to mitigate such a problem, the firm may invite institutional investors' equity participation so that it can borrow their reputation to enhance its credibility to minority shareholders (Claessens et al., 2002). However, the presence of institutional investors is not necessarily accompanied by active monitoring and improvement of corporate governance. As in any situation with rent-seeking and relationship-based transactions, institutional and other minority investors may prefer to let controlling owners continue to protect their rents and not force them to disclose all information, as otherwise their own values are negatively affected (Claessens et al., 2002).

The sparse empirical evidence shows that in reality, having institutional investors as equity owners does not improve corporate governance. Sarkar, J. and Sarkar, S. (2000) find no evidence that institutional investors are active in governance in India. Chhibber and Majumdar (1999) find that institutional investors may bring good corporate governance only if they own more than half of the share. In their parts, Lou et al. (2020) find that although institutional ownership does not associate with the announcement return, it correlates positively with long-run performance. More recent evidence on the emerging market suggests that institutional investors play active roles in improving corporate governance (Guo & Platikanov, 2019; Baghdadi, Bhatti, Nguyen, & Podolski, 2018; Ozkan, 2012; Solomon, J. F., Solomon, A., Joseph, & Norton, 2013; Alderighi et al., 2019).

6.4. Takeover market

Unlike the USA and UK, the takeovers market as a mechanism of corporate governance is weak in most underdeveloped countries and emerging markets (Muhammad, Waqas, & Migliori, 2019). In Asia, hostile and disciplinary takeovers are extremely rare. Mergers in Asia do not occur to resolve or mitigate agency issues. Bae, Kang, and Kim (2002) report evidence that acquisitions by Korean business groups are used as a way for controlling shareholders to increase their own wealth at the expense of minority shareholders through tunnelling. They find that when a group affiliated firm makes an acquisition, its stock price on average falls, but the controlling shareholder of that firm on average benefits because the acquisition enhances the value of other firms in the group, evidence consistent with the tunnelling hypothesis.

6.5. Debt

The disciplining role of debt is mostly applicable in the context of agency problems that exist in widely-held corporations (McConnell & Servaes, 1995). On a sample of Chinese firms, Wang, Zhou, and Xu (2018) show a positive interactive relationship between debt and internal governance mechanism. However, debt in closely-held corporations where managers who are often controlling shareholders and want to expropriate minority shareholders may have a reverse role. Controlling shareholder has the incentive and ability to use and expropriate resources from affiliated companies lower down the pyramid and to send those resources high up the pyramid where they have more cash-flow rights (tunnelling) (Bertrand & Mullainathan, 2002; Johnson, La Porta, Lopez, & Shleifer, 2000b). Thus, when a company in the lower pyramid asks for a debt, the money may tunnel up to a company atop the pyramid.

Sarkar, J. and Sarkar, S. (2008) find empirical evidence that debt can be used as a mechanism for expropriation in group affiliated firms that are located in the lower levels of the pyramid. They also find that debt as a corporate governance mechanism is sensitive to ownership and control structures of corporations and institutional features of the country.

6.6. Alternative mechanisms

Even though minority shareholders are expropriated by the controlling shareholders in emerging markets, managers still need minority shareholders to provide them with finance. As has been discussed, due to a high concentration of ownership in emerging markets, minoring by owners, boards and takeover markets are not effective. To alleviate agency problems in these firms, the manager often uses alternative governance mechanisms. These governance mechanisms may play more important roles in emerging markets than in more developed markets, where substitutive mechanisms are more effective.

6.6.1. External audit

In order to mitigate minority shareholders' concerns of being expropriated, controlling shareholders may employ high-quality external auditors to ratify financial statements. Fan and Wong (2002) look at whether the problems arising from concentrated ownership can be mitigated by effective auditing and whether independent external auditors can serve a corporate governance mechanism. They use a broad sample of firms from eight Asian countries and find that firms are more likely to employ Big Five (now Big Four) auditors when they are subject to agency problems imbedded in their ownership structure. Big Five auditors charge a higher fee and set a lower audit modification threshold, while other auditors do not. Taken together, their evidence suggests that Big Four auditors in Asia do have a corporate governance role. Jacoby, Liu, Wang, Wu, and Zhang (2019) show that external control strategies help mitigate owner-manager agency conflicts. Furthermore, Gao and Kling (2012) show that the external audit leads the Chinese company to better compliance with disclosure requirements. External audit hence sends positive signals to the market that the firm is managed efficiently and that managers commit to promote shareholders' interest.

6.6.2. Equity analysts

Controlling managers tend to hide information from the public in order to facilitate their private benefits of control. Equity analysts could not make much contribution to information discovery for opaque firms because they may not have the ability and resources to do so. Furthermore, in a weak property rights environment, inside investors and analysts with private information, may even trade on the information before it is disclosed to the public. However, if an analyst chooses to follow any firm, he has a certification role. Lang, Lins, and Miller (2002) examine analyst activity in 27 countries and find that analysts are less likely to follow opaque and family-owned firms. The situation is the same for state-owned enterprises (Zhang, Tong, Su, & Cui, 2015).

6.6.3. Dividend policy

The agency theory points that dividends may mitigate agency costs by distributing free cash flows that otherwise would be spent on unprofitable projects by the management (Jensen, 1986).

Shareholders may prefer dividends, particularly when they fear expropriation by insiders. In emerging markets, a manager can opt to pay minority shareholders dividends to alleviate their concern about agency problems. Mitton (2004) shows that better-governed firms pay higher dividends to shareholders. O'Connor (2012) suggests that opaque firms pay dividends larger than transparent firms in emerging markets. Atanassov and Mandell (2018) obtained the same results within a sample of limited liability companies. Basically, these opaque firms substitute poor governance with higher dividends.

6.6.4. Foreign direct investment

Foreign investors may have a double effect on corporate governance. From one side, foreign equity investment (in any form like joint ventures, multinational subsidiaries, takeovers, or even institutional portfolio investment) results in foreigners becoming outside shareholders with the significant share in the firm giving them the ability (through voting rights) and the incentive (through cash-flow rights) to monitor top management (Shleifer & Vishny, 1986). In addition, because often foreign corporate practices are superior to the host economy, foreign ownership may provide information about, and encourage the adoption of, superior practices in areas such as information disclosure, internal checks and balances, and accounting standards (Taran, 2019; Likitwongkajon & Vithessonthi, 2020; Cai, Kim, & Wu, 2019; Wang, Yuan, & Wu, 2017). On the other hand, if they acquire a controlling stake in a domestic firm, foreign investors may then have the same incentive as other insiders to exploit minority shareholders. Furthermore, the same sizeable ownership stake that positions foreign owners to monitor management can also give them an incentive to oppose governance reforms that weaken the position of the dominant block holder. Ananchotikul (2007) investigated Thai firms and find evidence suggesting that foreign industrial investors have adverse effects on corporate governance. Bhaumik et al. (2019) suggest that foreign investments by emerging economy firms strengthen their governance capabilities.

7. CONCLUSION

This paper offers a review of the research on corporate governance in emerging markets. We point out that the corporate governance landscape in emerging markets is unique due to their weak rule of law, weak transparency and inefficient financial markets. After the corporate scandals in developed countries and the market crises in emerging countries, there has been a call for corporate governance reforms. Due to the inherent differences in market models of developed and emerging markets, those reforms cannot be the same. Developed countries rely on their board of directors, management remuneration and the market for corporate control as their mechanisms of corporate governance. However, implementing those mechanisms in emerging markets may face some challenges because in emerging markets ownership is concentrated, rule of law is weaker, institutions are less developed, financial markets are less advanced, corruption is more prevalent and competition is restricted. In this environment, most of the corporate governance mechanisms which are suitable in developed markets become useless; boards are inefficient, management is not compensated regarding the performance of the firm and takeover markets are nonexistent, therefore the minority shareholders are expropriated. The literature, however, introduces some alternative mechanisms that are effective in emerging markets to attract investors. Although these alternative mechanisms may attract investors, still there is a long way ahead of emerging countries to increase their level of corporate governance to those of the developed world.

This paper is not free of limitations. To the best of our ability, we discuss the relevant literature about corporate governance in emerging markets. However, due to the numerous articles that have been published in recent years on this topic, it is impossible to discuss all the aspects of corporate governance in emerging markets. For future research, one could empirically analyze the effectiveness of each governance mechanisms in different emerging countries. Moreover, greater research may be required to understand exactly what mechanism works, when it works, where it works, and most importantly why it works.

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