The Impact of Corporate Governance in Latin America

A Comparative Approach with other Emerging Economies

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LAW850 Dissertation

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ABSTRACT

The Impact of Corporate Governance in Latin America: A Comparative Approach with other Emerging Economies

by

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Corporate governance is the way in which companies are governed through a series of rules and codes developed at state level. Globally there has been several different ways in which corporate governance principles have been adopted and enforced across varying capital markets. This dissertation aims to explore differences in depth at governance level in different economies, crucially to explore to what extent they may be to blame for Latin America seemingly missing the surge in investment in emerging economies from developed economies following the financial crisis in 2008.

Following an extensive review of existing literature, we will use quantitative data analysis of the WGI 2020 research dataset to explore how corporate governance has changed globally compared to Latin America, determining what the region still lacks in governing principles to attract the same levels of investment seen in other emerging economies over the past decade, and which corporate governance indicators are most relevant to the study of corporate governance in emerging economies. A discussion and conclusion will follow offering suggestions for potential change and potential future research directions will be recommended.

Keywords: Corporate Governance, Latin America, Emerging Economies, Theory

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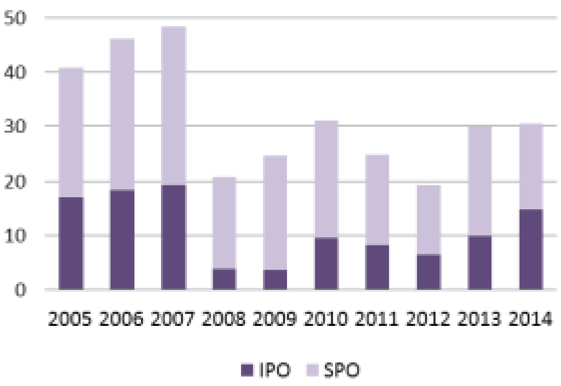

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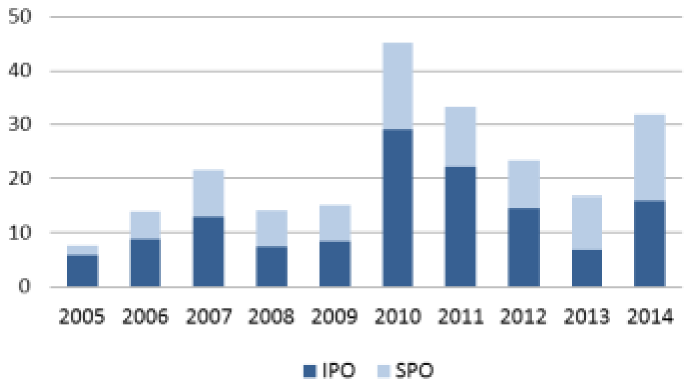

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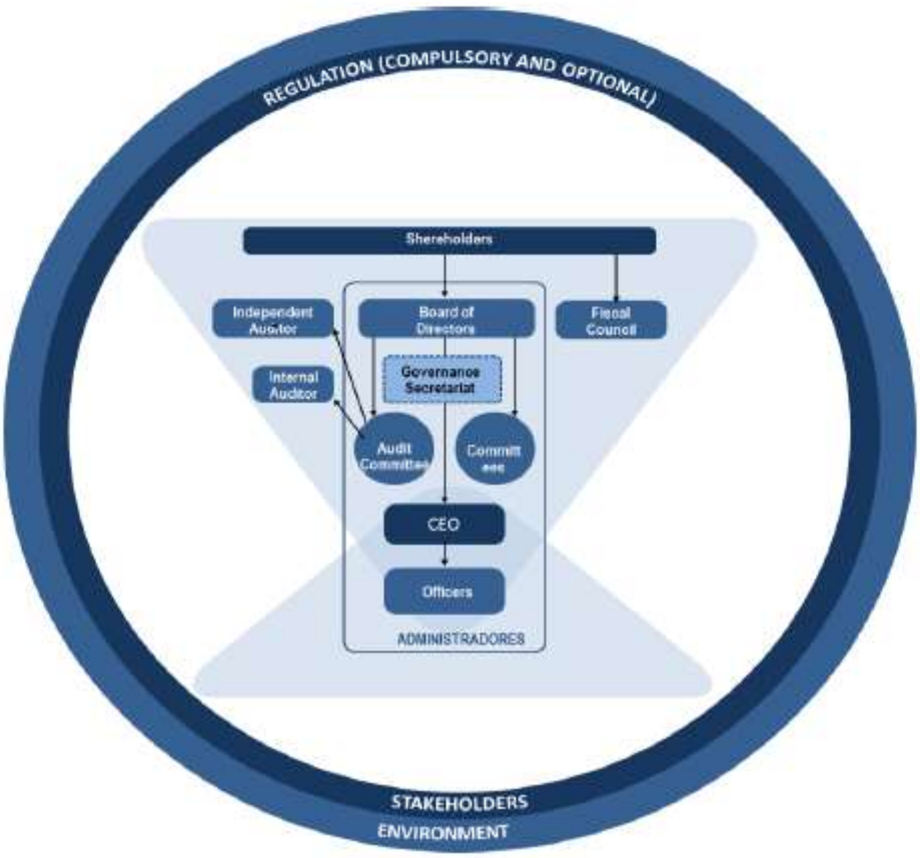

[1] 'OECD Capital Markets 'Growth companies, access to capital markets and corporate governance' OECD Report to G20 Finance Ministers and Central Bank Governors (2015)

[2] Brazilian Corporate Governance Code 2016 – Listed Companies – GT Interagentes Fig 1. 'Context and structure of the corporate governance system' P.16

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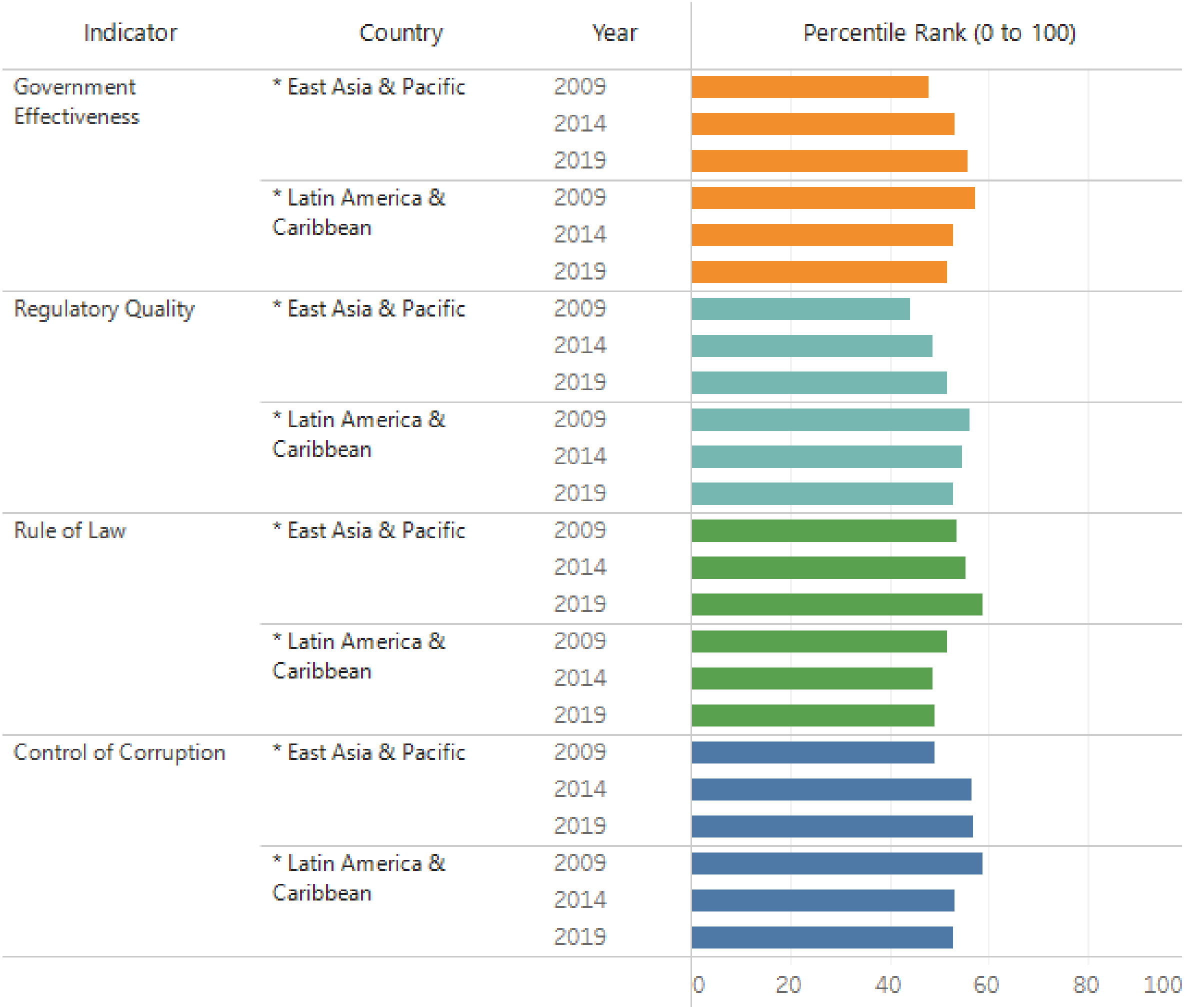

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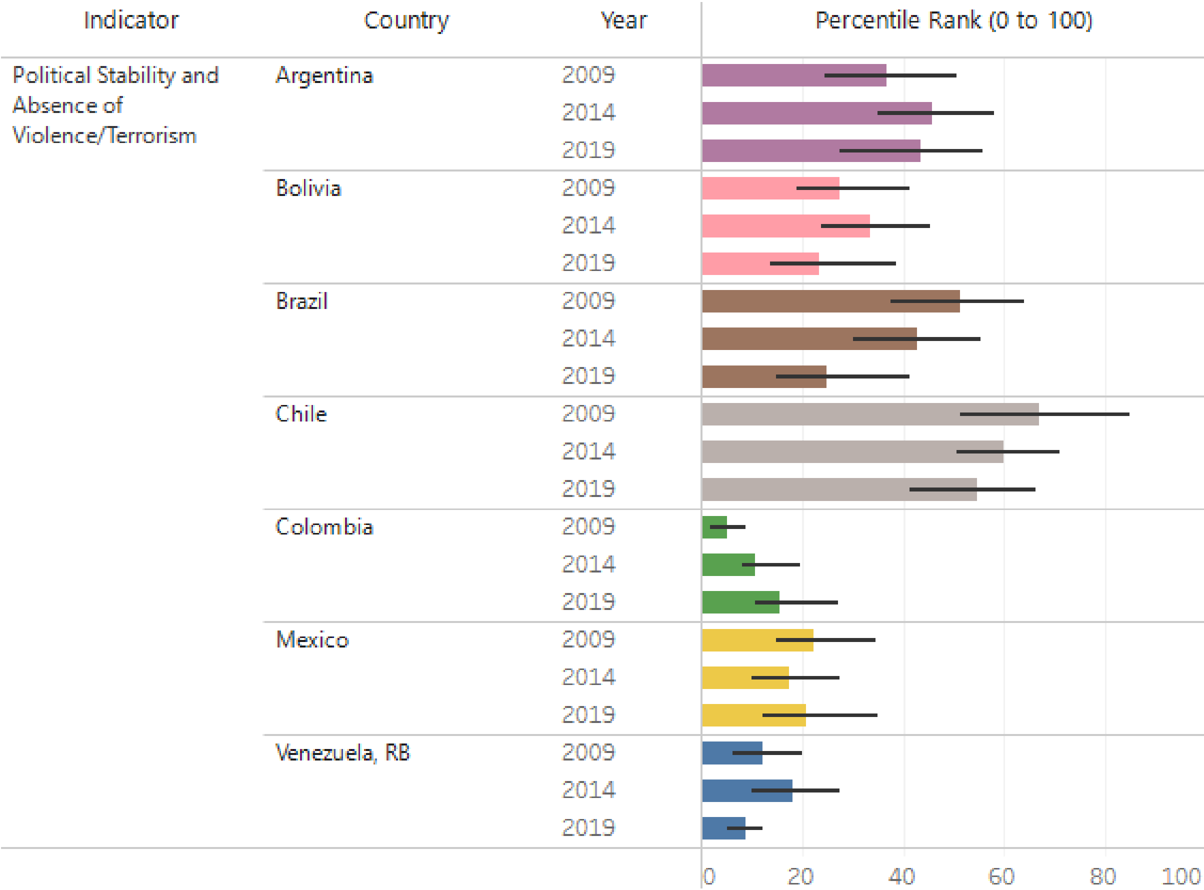
Indicator
Country
Year
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Political Stability and Absence of Violence/Terrorism
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Brazil
Chile
Colombia
Mexico
Venezuela, RB
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2019
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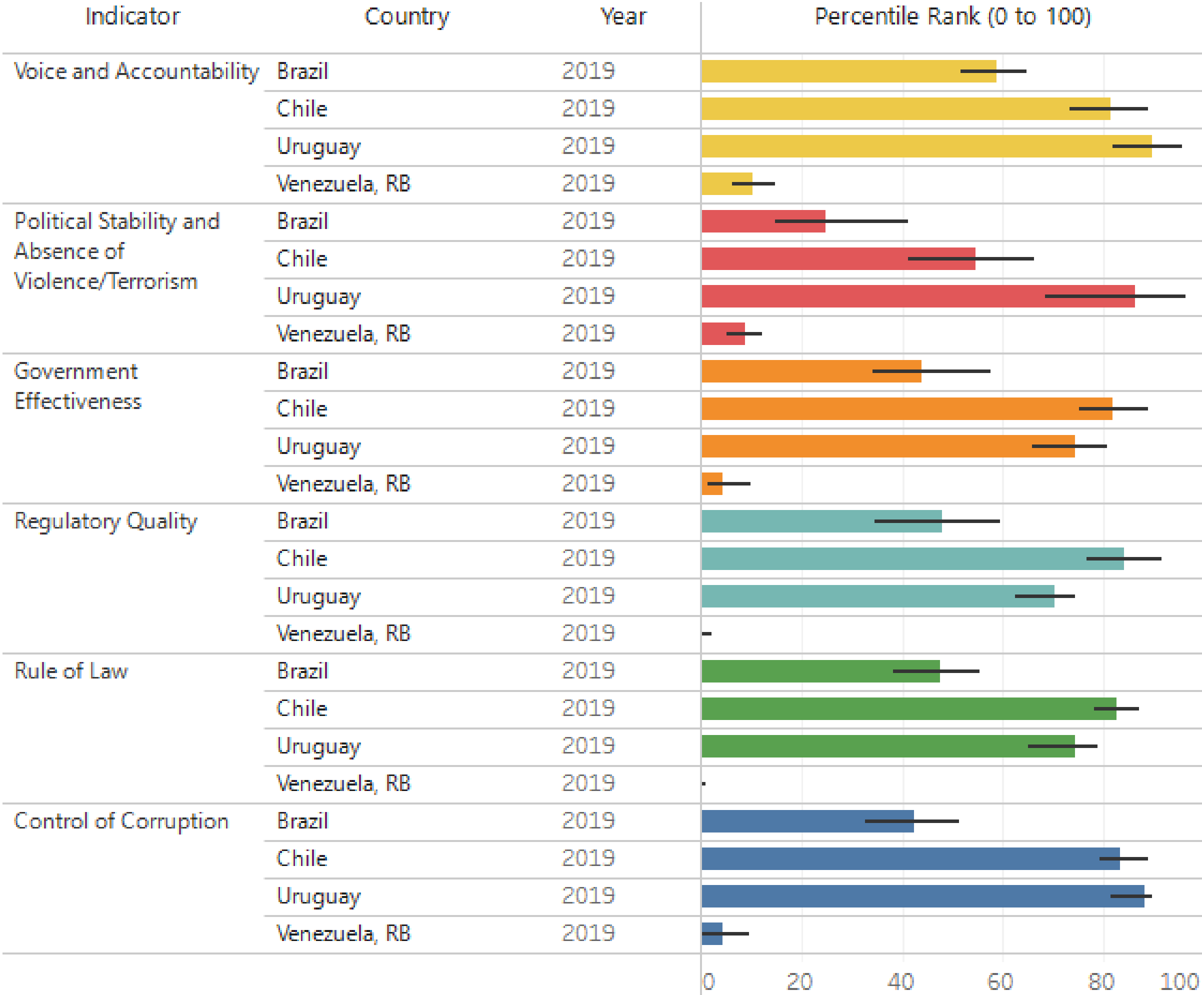
Indicator
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Year
Percentile Rank (0 to 100)
Voice and Accountability
Political Stability and Absence of Violence/Terrorism
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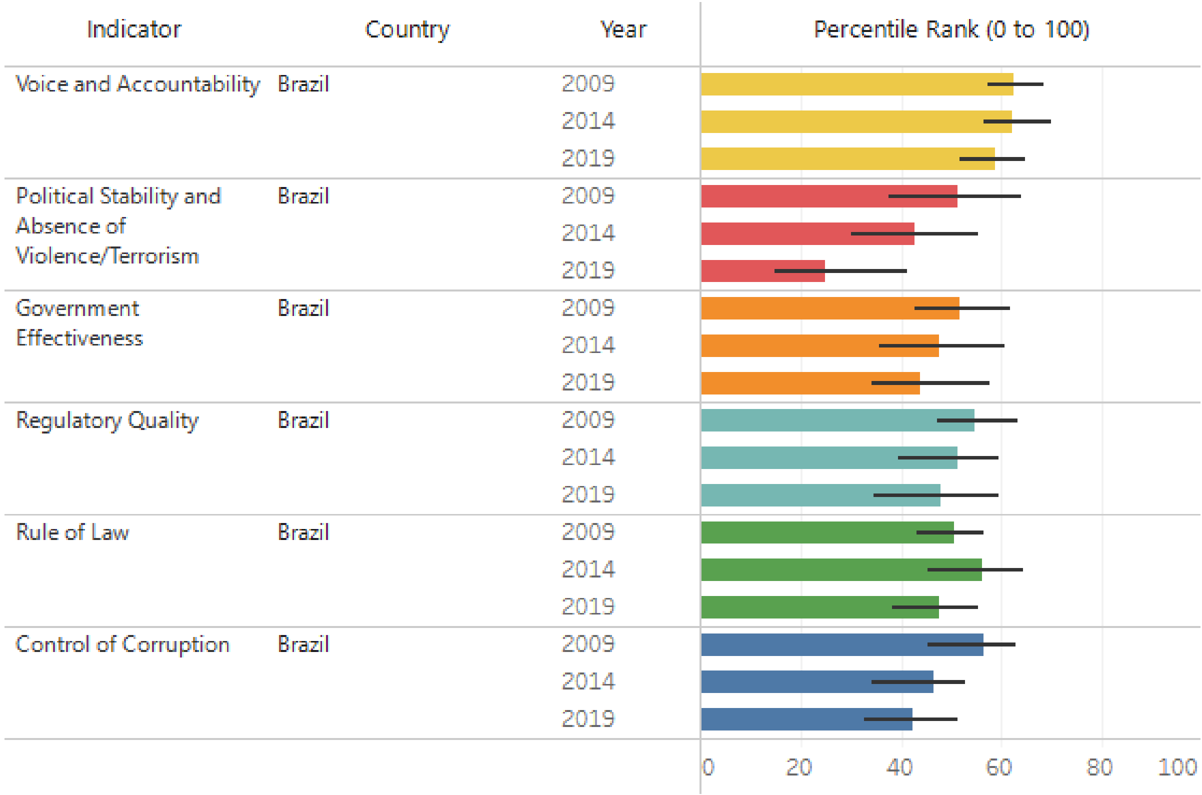
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Political Stability and Absence of Violence/Terrorism
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List of Abbreviations

DCS	Dual Class Shares
IPO	Initial Public Offering
FDI	Foreign Direct Investment
LatAm	Latin America
NYSE	New York Stock Exchange
OECD	Organisation for Economic Co-operation and Development
WGI	Worldwide Governance Indicators

Introduction

Corporate governance can simply be described as the systematic and structured effort to manage the interests of a company's stakeholders, from shareholders to consumers, the government and so on. Corporate governance provides a set of guiding principles by which a company is directed and controlled, intending to promote clear accountability and transparency.

The accepted practices by which a company implements their corporate governance structure largely relies upon which region the company operates. For better or worse, there is no universally accepted standard of corporate governance and, as a result, companies across the globe will differ significantly in their corporate structure and, critical to this dissertation, existing companies will struggle to enter additional markets if corporate governance in the targeted region differs significantly. Nowhere was this seen more than the aftermath of the 2008 financial crisis. Following the crisis, which hugely affected the market stability of modern western economies but was felt globally, a targeted effort from many western parties began to expand into the developing equity market economies in Asia, Figure 1 showing the shift in investment from 2008 onwards. One area of the world that missed this surge following the crisis was the emerging economies in Latin America. As we'll go on to discuss, this was and continues to be, to some extent, the fault of the corporate governance disparities existing within South America. This dissertation will seek to examine the difficulties in entering the Latin American equity markets compared to that faced in Asian markets. We will also research current efforts to engage further within Latin America and how corporate governance has changed and is changing to suit the interests from outside investors.

Emerging market economies are usually plagued by scandal in the form of corruption, collapse, and skulduggery, all of which can be correlated to an insufficient corporate structure brought about by insufficient levels of corporate governance. With a lack of independence on boards of directors which is almost taken for granted in more developed economies, Latin America requires a corporate governance structure with governance committees and auditors that support the trends of companies having few independent directors on the board. Thus, the structures in emerging economies do and will continue to differ to some degree.

As part of a regional roundtable on corporate governance from the OECD “Good corporate governance plays a critical role in the process of building strong domestic capital markets”[4] and compared to similar roundtables in other regions, this is specifically important in Latin American markets. In the age of globalisation, it may have been the OECD’s intention to promote a similar policy direction across the region of Latin America. The argument for a global approach to corporate governance is also an interesting one that will crop up during this dissertation at different stages. Some regions see similar approaches and other countries seem to align themselves with countries they have strong ties with, such as Hong Kong shadowing the approach of the UK in many instances.

Many commentators refer to the economic problems in Latin America and point to the institutional framework across the board letting down the capital markets and preventing them from exponential growth[5]. Growth which has been seen in other emerging economies capital markets which have proven less difficult to penetrate. This dissertation will include comparative research into corporate governance’s influence on emerging economies and the differences seen specifically with Asia and Latin America. After evaluating the literature around key areas, we will carry out research into an existing dataset to identify comparisons and make suggestions for growth in the corporate governance methods in the region to promote growth and investment in the equity markets of Latin America.

[4] OECD (2003) ‘White Paper on Corporate Governance in Latin America’ ch.2 pp. 7
[5] Chafuen, A. (2020) ‘The Economic Debacle in Latin America’ Forbes, Policy.

Literature Review

In this chapter we will investigate a broad spectrum of theories and ideas surrounding the literature available on corporate Governance. There is much of it available, but we will be as specific to our research as possible while also making reference to surrounding ideas and literature that may also be of interest. This is not an attempt at an all-encompassing literature review of Corporate Governance and rather that of existing comparative research where available of other emerging economies, as well as some lone research into Latin America itself and some theory to tie it together.

When looking into corporate governance in emerging economies, especially in a comparative nature, it's impossible to avoid agency theory. Agency theory is the term used to define relationships between the two main actors in a company, the 'principals' and the 'agents', critically the difference between ownership and control/management. First derived in an article by Alchian and Demsetz[6] and developed more by Jensen and Meckling[7]. Corporate governance can be a method by which these relationships are governed and enforced as agency theory warns that breaches of these relationships and their key principles can have a detrimental effect on the company. The principals employ agents to management positions to run the company to the goals of the principals, part of which includes the principals not being always savvy to the actions of the agents. Separation and lack of information to the principals, it is argued, is crucial in a successful relationship here. Agents should have incentives to follow to meet the goals of the principals and an ideal scenario sees the agents free to pursue goals independently but still benefitting the company, both parties being motivated by self-interests. Corporate governance can be a method to govern these relationships and maintain the positions independent of each other and prevent a principal-agent problem which occurs when the goals of both parties are not aligned. Creating a theory that tries to encompass the wholly intricate topic of corporate governance is tricky but the theory of agency; the shareholder theory; the stockholder theory; the resource dependency theory; Stewardship or Management theory and other

[6] Alchian A. A, Demsetz, H. (1972) 'Production, Information Costs and Economic Organization'
[7] Jensen, M, Meckling, W. (1976) 'Theory of the firm: Managerial behavior, agency costs and ownership structure'

ethical theories have certainly tried. We won't going into these in detail as they are not in the scope of this research but may reference them again in the later discussion.

Latin American states have a commonly accepted practice to split the relationships between principal and agent in the form of non-voting shares, either restricted or outlawed voting rights for certain class of shares. Another way in which they do this currently is through pyramid designs of governance as shown in the example of Figure 2. This example is an interpretation of Brazil's regulations, Chile and Mexico have this type of system but to a much greater extent. The pyramid allows corporate insiders to control the resource allocation for use by management and they are frequently used in Latin American systems of governance.

A key topic to refer to due to disparities in their use in emerging economies is Dual Class Shares, which can be described as a company that holds 2 or more classes of stock. Usually there exists a class of stock with weighted voting rights attached, allowing insider minority shareholders to maintain a large amount of control over the company compared to their actual level of equity in the company. In the markets this enables potential investors to preference the shares that suit their individual needs and allow for initial investors (insiders) to maintain control over the company as it grows. A big advantage of this as argued by those in favour of dual class share models is that it protects the long-term plans of the company from any new outside investors.

In 2021, as major markets in Asia seem to be benefiting from the introduction of dual class shares, there is a growing sense that markets like that of the UK's should consider implementing dual class structures to attract IPOs from big tech companies[8]. The makeup of the developed and underdeveloped markets 15 years ago could be strongly correlated to the heavy use of dual class shares. However, more recent change in restrictions in Asia and western markets have confused this. That is to say that the supporters of corporate

[8] Yan, Min (2021) 'The myth of Dual Class Shares: Lessons from Asia'

governance for years would class dual class shares as an inherently poor form of governance that sacrificed a lot of the protection given through the 'one share one vote' philosophy. The key was that dual class shares would damage the accountability and stability of the corporate structure in the long term, which was not considered worth the advantages it gave. As discussed previously with the implementation of dual class shares in Asian markets, there may be a way to remove the risk in the disadvantages through independent safeguarding measures attached to the shares. The validity of this can still be argued either way but early evidence suggests the cost benefit could be worth it in emerging and developed economies. In fact, some academics have criticised the stances of those of the UK and Hong Kong to persist restrictions to protect investors regardless of debates attempting to attract high-profile tech companies[9]. There is still question marks around whether DCS based companies can survive in the upper echelons with some of the larger companies in the markets, and this will remain to be seen likely for some time.

What Latin American economies lack compared to those mentioned integrating dual class shares into their structures is additional safeguarding measures that should be enforced by governments in the area. However, Latin America lacks enforcement and promotion of good practices like this in the form of regulations and an active judiciary which some have argued is the difference maker in this region compared to developed economies[10]. Other academics have highlighted the difficulty of investment in emerging economies with "underdeveloped legal and business environments"[11] compared to those with better integrated systems of corporate governance. A factor that certainly played a part in Asian investment was the unilateral approach from the region compared to that of Latin America which can differ greatly by country.

The important controlling factor to the successful integration of dual class shares are additional safeguarding systems. When this isn't in place within a countries corporate

[9] Huang, Flora (2017) 'Dual Class Shares Around the Top Global Financial Centres' p. 21-22
[10] Lefort, F (2005) 'Ownership Structure and Corporate Governance in Latin America' P. 79
[11] Filatotchev et al (2007) 'FDI by firms from newly industrialised economies in emerging markets: corporate governance, entry mode and location' p.557

governing principles, certain scandals can occur such as the Brazilian Petrobras scandal which started in 2014. The Petrobras case will go down as one of the most prominent corruption scandals in the modern markets. Its effect sent Brazil's economy into freefall and caused the worst recession the country had seen in a century. Petrobras was a majority state-owned company that was accused in 2014 of selling contracts for bribes. Largely in part to a poor corporate governance over the shareholders who were mostly members of the Brazilian government. The system of corporate governance in place restricted the rights of minor shareholders within Brazil but American investors were able to sue Petrobras. Motivation to invest regardless of the risk of being a minority shareholder with no control over the company usually exist in the reputation and trust of the majority shareholders within the company. A more effective form of corporate governance in situations such as to protect the investors of Petrobras would be safeguarding measures discussed prior which were and are significantly lacking in Latin American countries compared to other emerging economies. As a generally accepted theory of corporate governance, greater protection of investors should equal a lower cost of capital investment and thus more access to finance.

Modern shifts in corporate governance like that seen in Asia may seem, on the hopeful side, to be motivated by a desire for a more effective and responsible form of corporate governance. The reality is that new methods of corporate governance have come about because of competition in the markets to accelerate IT investment and potentially address issues over privacy and regulation that come along with companies like Facebook[12]. An important step forward in regulation of these areas, which has been a grey area for some time, could involve corporate governance. Big tech companies have shown a tendency to protect their company management from the shareholder which is a trend that complicates regulation around areas of privacy, taxation, and competition[13].

One thing that the growing Asian markets have in common with Latin American comparisons is the nature of shareholding. Insider shareholders are dominant in south

[12] Phan, P. (2001) 'Corporate Governance in the Newly Emerging Economies' P.133
[13] Papadopoulos, K (2019) 'Dual-Class Shares: Governance Risks and Company Performance'

America, many of which are public and controlled by family members. According to 2016 statistics of the 10 largest family businesses in Latin America, 9 are public listed, all but 1 have at least 40% family shareholding or voting rights and the largest company was 97% family controlled[14]. These types of business make up 9.8% of Latin America's GDP. Asia has the same trend with less of the insider shareholders being family oriented, but the ownership principles remain similar. High concentration of family-owned shares within a company can be potentially treacherous. It can significantly limit the scope given to management of the company 'entrenching' shareholders in positions which may not be beneficial to the company. Where a company has many family members holding a significant number of shares, any conflict within that family can have an adverse effect on the health of the company especially where it escalates to a power struggle over the company, inheritance can also cause issues where those involved with the creation of the company pass their powers on through inheritance which can often result in a reduction in quality of management.

Highly concentrated family ownership sometimes also ties into another threat in emerging economies, business group led ownership where groups of potential part family-owned conglomerates have a high concentration of share in a company. Holding some of the fears of family ownership, business groups also threaten minority shareholders positions and run the risk of dealing with affiliated businesses that may not make sense to the original company, potentially damaging it for the benefit of affiliates that shareholders have no stake in. Furthermore, a popular sighting in emerging economies is majority state-owned business where the state own shares or political agents own shares of some of the country's biggest companies. Threats arise on two sides with emerging economies in this respect where there is a risk that the state being too involved can cause accountability and transparency issues leading to corruption and misdealing. Too little state intervention in growing companies in emerging markets can also lead to the same result on the other side. State owned companies present a new risk for minority shareholders where the companies' goals are less clear and will likely be more aligned with government policy than the promotion of the goals of the company. These issues are particularly important in Latin

[14] Family business in Latin America: facts and figures (2016)

America compared to other emerging markets as according to The World Bank[15], Latin America & Caribbean have the worst protecting minority investors score besides Sub-Saharan Africa on a global scale.

High ownership concentration is not a problem exclusive to Latin America, however it is one that the whole of the region has in common. In the interest of comparing emerging economies, Asia can see changes based on jurisdiction whereas Latin America are united in their concentration. A basic comparison can be seen below[16]:

Jurisdiction	Ownership Concentration (%)*
United Kingdom	19
United States of America	15
France	60
China	51
Japan	27
Hong Kong	75
Brazil	61
Mexico	60
Chile	79

*Of companies where the 3 largest shareholders control more than 50% of shares.

The above is an example of 3 of the largest developed economies with 3 emerging large Asian economies and 3 emerging large Latin American economies to show differing approaches in two regions and how Latin America are quite high across the board according to the OECD factbook on the matter.

[15] The World Bank (2020) 'Protecting Minority Investors'
[16] OECD (2021) Corporate Governance Factbook 2021, Table 1.1 p.28

In 2019, the OECD tested several systems in the Latin American markets to gauge response[17]. What they found was a lack of a sufficient 'capital markets culture' to bring interest into their markets. They found significant misunderstanding from companies over costs of making their company public and the benefits it could bring to open their stocks. They recommended educational campaigns to increase understanding inside and outside the capital markets to remove the 'culture gap'. They also found concerns over regulatory changes if their company was subject to governance legislation more like that of developed or other emerging economies. The influence of the OECD on global corporate governance is quite significant. Initial rules and regulations in Latin America came about from recommendations by the OECD and certain case studies. We will look later at this influence in the discussion section and how this can compare to other regions in the last 20 years.

Despite modern integration of dual class stocks in emerging markets and some developed, including the New York Stock Exchange in some instances, some academics still argue on the side of 'one share one vote' and hold shareholder democracy as a key component of an effective corporate governance system to protect outside investors, seeing dual class shares as a moral hazard[18]. In earlier research from the same authors, they found that weak minority shareholder rights protections are cause for the high rates of ownership concentrations within Latin American companies[19]. Many contemporary academics hold the view that protection of the minority shareholder should be the focus of much of what corporate governance sets out to achieve. These authors, among others, argue in favour of the old 'one share one vote' theory which is rooted in corporate governance principles. This is a theory that is obviously in question recently and one that we will go into more after our research.

There are, in essence, two forms of corporate governance; that which is led by the country/state; and that which is led by the firm itself, known as firm-level corporate

[17] OECD (2019) 'Equity Market Development in Latin America: Enhancing Access to Corporate Finance'
[18] Aguilera, R et al. (2019) 'Corporate Governance in Latin America: Towards Shareholder Democracy pp. 13
[19] De Castro, L et al. (2012) 'Corporate Ownership in Latin American Firms: A Comparative Analysis of Dual-Class Shares'

governance. Firm-level corporate governance takes significant standing in Latin America compared to other regions. Investor protection in the region and analysis of how it has progressed over time would lead us to believe that 'drastic' action would need to be taken to the legal, regulatory, and judicial spheres of corporate governance for state-level governance to be enough by itself and thus an argument can be made for firm-level corporate governance as an easy alternative[20]. Much research has been done into firm-level governance, making a strong case for regions like Latin America where a mix of country-level and firm-level may lead to better dividend pay-outs[21]. Three main options are available at this level of corporate governance. Either the firm could seek cross-country or foreign methods to integrate into their structure, more commonly they could look to a commonly accepted 'opt-in' set of proven and critiqued principles which may already be in use with similar, local, or affiliated firms. Finally, they could try and implement their own reforms into their corporate structure, being careful to abide by the codes in place in their jurisdiction while doing so. This is a far more flexible approach to corporate governance principles than we've seen previously and changes the makeup significantly. These methods in the long-term could prove costly as every new firm, rathe than complying with a set list of codes and regulations, must seek out their own hybrid version of principles for themselves. Similarly, it breaks down the unilateral approach to corporate governance that some academics call for.

If no answer is found to Latin America's problems, then it might be to incorporate a flexible way to manage corporate governance such as this country and firm-based hybrid mechanism. Conflicting research has been done to this end, some academic studies claiming the levels complement each other, the others claiming the opposite[22]. If this was an avenue to be explored in serious detail, further research would need to be completed with updated data and methodologies before any implementation or official recommendations were made, an interesting alternative all the same.

[20] Chong, A, Lopez-de-Silanes, F. (2007) 'Corporate Governance in Latin America' p.29-30
[21] Chang, B et al. (2015) 'Beyond Country-Level Governance: Does Firm-Level Governance Quality Matter in Dividend Policy?'
[22] Von Kock, C et al. (2013) 'The interaction between Country-Level and Firm-Level Corporate Governance'

Latin American justice models, despite reforms, continue to be lacklustre in many ways. Often criticised for being a very bureaucratic system that struggles to include affected parties and cannot keep up with rapidly changing policy, often leading to policy and enforcement following two different codes. It is important to note the failing legal systems of Latin America as it will be a continuing theme throughout. A weak infrastructure and lack of enforceability of policy are limiting factors to companies competing on a global stage in the long run. This is an issue, not completely exclusive to Latin America, but exclusive in the sense of the region-wide problem it has with legal enforceability. Not mentioning the questionable independence of some legal entities, the lack of consistency and certainty around whether certain policy will be enforced properly and to what extent further leaves firms with an increased incentive to avoid policy change if it won't be enforced properly anyway. The legislation for areas of corporate governance is not hard to find, enforceability or lack thereof renders it useless if not conducted properly.

Methodology

To identify disparities in factors affecting corporate governance across regions we will be comparing statistics from the OECD and the WGI. Aswell as comparing region wide specifics we'll be taking the largest emerging and developed economies and comparing them directly. These include the UK, the USA, Brazil, Mexico, China, and Indonesia. We will include this cross country/region comparison and include time frame analysis where appropriate to see how these have changed since the financial crisis caused a shift in foreign investment in emerging economies.

The WGI dataset contains 6 variables that influence corporate governance:[23]

1. Voice and Accountability – This refers to a country's citizens perceived ability in selection of their government, freedom of expression and association, and free media.
2. Political Stability and Absence of Violence (incl. Terrorism) – This measures the perception within the country of possible violence or instability, including acts of terrorism.
3. Government Effectiveness – This is the perceived quality of things like the civil service, including their political independence, public services, and the credibility of government policymakers.
4. Regulatory Quality – Perceptions of the ability of the government to implement, enforce and follow through on sound policy and regulation specifically to promote development of the private sector.
5. Rule of Law – Captured perceptions of the quality of enforcement of contracts, the police, and the courts. Also, the trust in companies to follow policy and rules.
6. Control of Corruption – As it sounds, the perceived ability of a country to handle acts of petty and grand corruption, the use of public power for personal gain.

[23] Kaufmann, D et al. (2010) 'The Worldwide Governance Indicators: Methodology and Analytical Issues' p.4

The source data of the WGI project has been collected since 1996 every year. Working with a significant amount of data, we will impose certain restrictions to suit the comparative approach taken here. For our purposes we will use 5-year increments since 2009. The provided dataset's access offers seven different means of comparison. All figures used will be from the 'Graph View' where we will be acquiring data from the six indicators above and comparing regions and countries in various ways. Other data views may be used to support findings but will not be incorporated into the list of tables. Graph view enables us to see aggregates of the indicators for country and region for use of comparison. All countries are available in the view without restriction, as are regions. Applicable regions used are 'North America', 'Latin America & Caribbean' and 'East Asia and Pacific' which will provide a good level for comparison across developed economies, emerging Latin American economies, and emerging Asian economies.

Predictions

Of the indicators, it's not predicted that the first two will come up with any surprising results or provide any useful comparative data for use. Regulatory quality and rule of law will likely be the key indicators for comparison and control of corruption will also likely have a higher threshold in emerging Asian economies. Government effectiveness is an unknown modifier here, at this stage it cannot be guessed to what extent this indicator will differ by jurisdiction.

Findings

Progression and Regression

Displayed in Fig.3, four out of six of the indicators are shown with the absence of Voice and Accountability and Political Stability and Absence of Violence, which plateaued in both regions. In all other four instances since 2009 a clear trend emerges that shows how Asian markets have perceived a percentile rank increase in each area whereas Latin American trends have been in decline. In this respect, the perception of Asian markets corporate governance has increased because of the influence from developed economies. A contributing factor here is also that the increase of trust in the emerging economies in Asia are diminishing statistics in Latin America in direct comparison.

Political Stability

Either a generally low or declining level of political stability shown in Figure 4 is a common trend among Latin American markets. This is supported by the World Bank who calculated the only two countries in South America with a positive score on the political stability index, Uruguay, and Chile. In the 1990's the markets were used as a political legitimising tool in South America. Economic stability through the markets were used by states to legitimise themselves[24]. The idea that the economic market would bring peace and harmony to the political stages in Latin American countries by many at the time seemed to pay dividends to begin with, but some argue the lack of separation of economic and political markets, the mismanagement of supporting structure and lack of further investment has caused the opposite effect thirty years later. Political instability compounds any existing issues within a weak governing framework with any political decision and the threat of such decisions able to expose the fragility of the structures.

Chile and Uruguay

Following the previous finding and through further research into general stability indexes in Latin America, we can compare data from Chile and Uruguay with countries on the other

[24] Lewis, C (2005) 'States and Markets in Latin America: The political economy of economic interventionism'

end of the spectrum to see how they shape up in the region. From Figure 5 we can see comparisons with Brazil and Venezuela with some interesting results. From the dataset we can see that the political stability in other sources of Chile and Uruguay does well compared to two other large markets in the region. Where Venezuela does very poorly across the board, Brazil differs in each category but almost without fail Chile and Uruguay perform very well in each category. This may feed well into further discussion below and research in the future.

Brazil

The figures in figure 6 could be slightly misleading in the sense that it suggests a gentle decline on all indicators in Brazil over time. Looking further back as the dataset allows, we can see from 1996 many areas were either growing or plateauing and most seem to peak in around 2009. From there however the statistics are clear, the largest country in land, population and in economy in Latin America is declining in all indicators across the board. The struggles in Brazil are bound to have a negative effect across Latin America as the largest economic powerhouse struggling in any region is bound to have a negative effect on its neighbours. Some high-profile cases such as the Petrobras corruption scandal have either had an affect on these statistics or give a tangible example of the impact of them.

Key Indicators

Through extensive review of the dataset, we compared the USA with two emerging economies in Latin America in Brazil and Mexico with three from Asia in China, Thailand, and South Korea. These countries were chosen due to the scope of their market size and the USA to use as a control as it is a developed economy. We done this to review each indicator, how it has been affected since 2009 in each region to help determine how meaningful each one is to the research. A summary will review findings but below can be seen specific findings when evaluating each indicator in detail. Voice and Accountability and Political Stability, though a pressing issue in Latin America, are not all that useful for the case of our research with little relevance, Government effectiveness's starting point might give some guidance as to why Asian markets were chosen for investment following the financial crisis. Regulatory quality was almost indistinguishable between regions with a few outliers. Finally, Rule of Law and Control of Corruption have seen development in Asia but the same cannot be said for Latin America.

1. Voice and Accountability

It would perhaps be too brash to say the Voice and Accountability indicator does not matter for the purposes of our study, but prior assumption was close to this, a claim that seems to be substantiated by the statistics in the dataset. In Asia alone, China ranks terribly here, Thailand poorly yet South Korea has almost passed the USA in this metric while Latin American countries also perform reasonably well. There was no further metrics that drew any substantial correlation between Voice and Accountability and effective governance. This does raise other issues within the states corporate system, but none related to governance. It does however answer a question that would certainly be asked if it was not included in the data.

2. Political Stability and Absence of Violence/Terrorism

No country in the inputs scored particularly well on this and it does not seem to be a major contributing factor to effective governance but would be wrong to rule out to the same extent as Voice and Accountability. Latin America is known for political instability at times, and it will be of detriment to any potential policy reform. China and Thailand, although improving, are in a low percentile here but this doesn't seem to have a detrimental effect on their overall quality of governance.

3. Government Effectiveness

The first of the indicators that starts to yield some comparatively useful results, this indicator refers to the independence of political entities which will be relevant to things like independent auditors. This metric is quite high in 2009 in Asian emerging economies but still improving, where it is quite low comparatively in Latin American equivalents. One of the more interesting indicators but not the most surprising or telling at this stage but may arise to some supporting arguments in the discussion. It may also help to show why Asian markets were penetrated post-financial crisis rather than Latin American counterparts.

4. Regulatory Quality

Prior to research one had assumed this would be one of, if not the, most important indicator. Surprisingly, emerging economies are almost interchangeable in the results. This was true with the sample listed above but also with a wider sample of emerging economies, Korea and Chile performed along the lines of developed economies but otherwise both regions of emerging economies performed similar.

5. Rule of Law

Rule of Law can otherwise be referred to as trust in enforcement ability of the state. Here Asian emerging markets started on a slightly higher level than Latin American markets in 2009 but seen a lot more improvements over time, where Latin American either stayed where they were or deteriorated. We identified enforceability as a key issue in the literature thus rule of law is an important indicator in the research.

6. Control of Corruption

Surprisingly, control of corruption was not a defining indicator in the review process. Assumptions had been that control of corruption would need to be very high in successful emerging economies, but this wasn’t strictly the case. What did show however was that the Asian emerging economies generally seen improvement here since 2009, taking the year back to 1998 showed that not much progress was made between then and 2009 but since 2009 there had been improvements across the board. The Latin American representatives here and as discussed elsewhere in the findings; corruption control has been declining for some time.

Discussion

As predicted, the first two indicators didn't provide much in the research for meaningful comparison. Political stability is still an important variable in Latin America that continues to affect more than just the capital markets in the region. From the outside looking in Brazil has been unstable politically for some time with most recent unrest coming from Chile and Ecuador over 'entrenched inequality'[25] and poverty rates rising. It is not within the scope of this dissertation to comment on the geo-political problems of modern Latin America, nor is it to claim that a rise in equity market investment would be a solution to this problem and provide some stability. However, these facts must be acknowledged when considering the complex nature of the region and its macroeconomics.

Government Effectiveness was an indicator that was difficult to grasp initially and make predictions over, mainly being unsure of how public service credibility would improve over time by region if at all. Resulting figures were not expected but they were not surprising either. What stuck out was the starting level in 2009 was higher in Asia compared to other emerging markets which may, as mentioned, provide one reason of many for why investment went in that direction. More political independence of things like the civil service, public services and so on may have supplied a more attractive venue to invest in when foreign investment picked up. Control of Corruption was an indicator with a similar level of uncertainty and the statistics for 2009 were surprising as it was thought if Government Effectiveness was slightly better in one emerging economy than another that corruption control would maybe follow the same guiding principle, but this was not the case. Like Rule of Law however, a distinct improvement since then was seen after the influence of foreign investment, one that was not paralleled by Latin America.

Rule of Law both started at a higher level and increased in quality since 2009 as quality of enforcement and trust in companies to follow codes and procedures got better with time in Asian markets. Something that backs up the literature which suggested enforcement and

[25] Sanchez-Ancochea, D (2021) 'Latin America: Inequality and political instability have lessons for the rest of the world'

trust to be major issues in the existing systems in Latin America and a major barrier in the way of growth in the capital markets. It was expected that the indicator Regulatory Quality would have a similar effect but surprisingly not. What we can take from this is the actual regulations being implemented aren't too far different across economies with similar motivations, it's more an emphasis on looking at enforceability and the companies themselves to see if loopholes are easily found or if the regulations are just ignored in favour of old accepted practices, furthermore, alluding to the lack of a good 'market culture' in the markets of the emerging economies in Latin America.

Many emerging markets in Asia have shown significant progress towards positive and effective regulation. They have incorporated corporate governance regulations to suit their needs and revise and update these regulations when required. This is something that may be lacking to an extent in the Latin American markets. One problem identified in the literature was the independence of the board. Generally considered one of the priorities in governance in any market, it is a concern in emerging economies. This is no less relevant in Latin America which notoriously have low independence of boards. Luckily, following a global trend this is improving over time however does remain quite low compared to not only developed economies, but other emerging economies too. This has been largely in part due to the stressed importance of governance codes and practices being legislated on a country basis since the financial crisis. Where in board independence Latin America appear to be making ground to other emerging economies, where it is not doing so is in, arguably, the next most important area, the independence of committees, which is lacking across the board either in existence of some committees or the political independence of them. This is a particular problem when these committees could be the only saving grace for protection of minority shareholders in the existing systems that include high concentration of ownership and DCS systems eating away at the protections of the minority shares.

In their white paper in 2003[26] the OECD made several recommendations again across Latin America to try and encourage further reform and revision of existing lacklustre policy. They

[26] OECD (2003) ibid.

were concerned about the corporate governance infrastructure in place and urged policy makers across the region to focus on a few areas; voting rights; equitable treatment of shareholders in situations of large-scale corporate changes; defining the roles of stakeholders in corporate governance; working on and improving reporting integrity, disclosure and transparency; board of directors responsibilities; general regulatory framework and finally to encourage cooperation across the region. This white paper could be posted in 2021 with the same key issues and it would still be relevant. Little has been done overall to improve some of the areas that were recommended to them 18 years ago. A specific one of interest is the independence of the board of directors. It was stated then in the white paper that through legal framework and accepted practice, each board member should act independently of outside influence of shareholders to serve the interests of the company[27]. These were sentiments sent in similar white papers at the time to other regions, but Latin America still faces problems around directors today. Minority shareholder security is at risk when directors act on the influence of majority shareholders as is the case across the region, independence of the board can have a big effect on protecting the minority shareholder. Independence leads to protection, which leads to easier capital and more foreign investment. Although Latin America has seen some growth in this area recently, with many countries having independence of the board as a requirement for newly listed firms[28], this has come 15 years after it was suggested and has no doubt been a contributing factor as to why the region has evaded foreign investment more akin to other emerging economies.

From the literature we seen that codes and procedures in Latin America have in fact been updated and reviewed on a relatively regular basis for the protections of minority shareholders. The trouble and difference from other markets is the enforceability measures tied to an ineffective judiciary. Lack of scrutinization of policy in the drafting phase has also been blamed for loopholes being easily found in new provisions. The data examined and analysed in our research appears to back up these fears and puts them at the forefront of reasons for lack of growth in Latin American equity capital markets.

[27] Ibid. p.24
[28] Orton, O (2019) 'Independent Directors in Latin America, a time for change?'

The cost and benefits of DCS have long since been debated as well as the functionality of it withing a system with good corporate governance. It has long been an accepted practice that DCS are a breach of the 'one share one vote' principles present within developed economies, and they fracture the integrity of a good governance culture. However, the view on this is, as it should be, changing with the times. Asian capital markets still prospering since integration in a proper way and promotion for wider use for the sake of IT company investment in countries like the UK, DCS seem to be making a mark in effective corporate governance systems. Of course, it will take some time and new data to catch up to the emerging trend to evaluate its efficacy properly and crucially whether they can perform at the same level as large companies without DCS. But this is a good sign for the struggling emerging markets in Latin America, instead of having to uproot their system of shares they can continue to use DCS. As with many things already discussed they will have to make changes around it, adding additional artificial controls to protect minority shareholders that would naturally be in place if DCS were not in use. Management entrenchment being perhaps the largest concern in the system, where shareholders become essentially entrenched within the management of the company and very difficult to displace, also violating theories such as the agency theory discussed in the literature review. The jury is largely still out on systems with and without DCS but as we wait to find out any more evidence to the contrary of claims that they work well, DCS and single share single vote systems will likely continue both to survive and thrive beside each other in different regions and jurisdictions, so it is the reality that DCS systems in Latin America are unavoidable and not necessarily a negative at face value.

It is evident from the findings that Latin American economies are generally lacking in a couple of key areas with little progress being seen anywhere when compared to the world's other economies. Remaining static is almost what they cannot afford to do as no change will come. Assessing where this has fallen, we can look at how often governance legislation is revisited across jurisdictions. When we look at this and the contents of the regulations, they seem to be well aligned with other emerging economies and developed economies. The problem is obviously not with the nature of the regulations themselves but how they are applied to the region specifically, the issue is one of enforcement. Weak legal infrastructure has been a problem in Latin America for decades and continues to play havoc here. Unless there is a major overhaul at some stage, corporate governance mechanisms may need to adapt to be more firm-based and flexible, following an example from other countries rather than expecting regulations to be upheld in Latin America. It does seem that a pan-Latin America, politically independent judicial body to deal with issues of corporate governance and such would be the answer to many of the region's problems. Each jurisdiction will have specific needs but in order to provide a baseline to work off and to unequivocally put in place protections of minority shareholders which has proven to be a problem and might just be the key that open the gates to outside investment, a regional body with proper enforcement of its policy might be the answer, even if it is a hard one to see coming to fruition. A lengthy and expensive process either way that might not be worth it. It is also feared that such a solution to the age-old problem may come too late. These claims and continuation of the old enforcement problem in Latin America appear to be backed up too by the Rule of Law indicator findings, furthermore substantiating claims of an ineffective judicial system of enforcement.

In Europe there exists block holders to keep shareholders in check, in Latin America such a similar phenomenon could be seen soon in the form of pension funds, investors in these areas have a lot of capital to invest and the pension funds in the region are only expected to grow in the coming years. They could be the answer to a lot of Latin Americas corporate governance problems. This has already been seen to an extent with success in Chile, one of the more successful corporate governance systems in Latin America. However, this practice isn't accepted across the whole region and even banned in some countries. There are many reasons for why this level of investment for pension funds hasn't been seen everywhere in Latin America, including the legality previously mentioned. Another is a disproportionate amount of funds are allocated to government bonds and a confused incentive system. A short-term fix to many problems could simply be to open the door for this level of investment and allow those with significant capital in pension funds become minority investors in Latin American firms. This could be a good example of the flexible hybrid approach to both country and firm-based approaches to corporate governance in the region, with the state allowing for the investment to flow in this way and the firm creates controls like that seen with block holders. Holding this back in a major way is the outdated pension fund legislation restricting movements to be done to this extent. They could also be used as an incentive for companies showing good corporate governance principles, to be rewarded with a very wealthy minority shareholder. Slightly more controversially and much less proven as a solution is to have these minority shareholders on the board.

Transparency has come up a couple of times during the research. It is one area that is less talked about than other big money ideas and theories but one that Latin America must also get better at. There exist issues with independence of these reports from shareholder interaction before release and as a result cannot always be trusted. There has been some improvement in certain jurisdictions, but fundamental problems still exist with the system that limits how reliable they can be. This feeds into a feeling of trust from potential investors and the existing management and shareholders. Firms with greater transparency are more likely to receive outside investment. This then also feeds into the running theme of a good ‘capital markets culture’, that intangible factor that remains throughout with many aspects, most of which cannot be measured. It is interesting due to the difficulty of its explanation, a difficult factor to quantify or measure and one with no fix. Instead, gentle, and precise nudges in the right direction are being made by the OECD and other bodies to try and promote this culture that is lacking in Latin America. Mentioned a small amount in the literature and never the focus of it, it would be a place to start for further research to try and put more detail to this aspect of the ‘capital market culture’.

Conclusions

It is a matter of fact that regions and states with more protection for minority shareholders provide a more attractive venue for outside and foreign investment. If the legislation, regulations, and common practice of good forms of corporate governance align with an adequate form of enforcement, shares in companies would be both higher in value and more sought after by outside investors. Until Latin American states align themselves with this philosophy they will continue to plateau as an emerging economy compared to the likes of Asian emerging markets who have excelled in the last decade thanks to outside investment because of proper safeguarding of that investment. There is a general sense of fear from controlling shareholders that any change to the norm will affect their companies negatively and part of this is due to the unforeseen 'culture' factor of the markets.

Emerging market corporate governance should be seen in isolation. A direct comparison to developed markets and their form of corporate governance would be an unfair comparison. Without a doubt, the developed economies will have some influence on the structures implemented in emerging economies but a corporate governance approach that is more tailor-made to the economy it inhabits may be more viable. Similarly, to expect rapid change in the short term would be wrong as integrating an appropriate 'capital market culture' is a long-term goal to be worked towards in capital markets that are rapidly developing in emerging economies. We briefly discussed some corporate governance theories, yet none seem to cover the complex nature of corporate business in its entirety, not to mention that governance can vary due to varying cultural, political, social, and historical circumstances[29]. High ownership concentration is a fact across the whole of the region and a start for the most fundamental of corporate governance principals would be to develop strategies around this fact to provide protection for minority shareholders.

There are those that believe that in the age of globalisation, there should be a global approach to corporate governance. Through the study done in this piece and the current situation of corporate governance in a region such as Latin America, not only in the

[29] Abdullah, H, Valentine, B (2009) 'Fundamental and Ethics Theories of Corporate Governance' p.94

comparison of regions and economies but in the comparisons between countries in those regions themselves shows how complex and determinate on cultural, political, historical, and other factors that corporate governance truly is. The same is true with this as it is with the theories in corporate governance, no one theory fits all and no one system will fit all. Despite this, a Latin American region-based set of guiding principles might be what the region needs to kick start corporate governance or provide a baseline to work from, to support minority shareholders, enforce independence of the board and provide recommendations on how to use country-based and firm-based governance in unison and aid countries to expand their own enforcement of such principles.

There are two main facets that stick out above all else during this research and review. One being the aspect of enforcement. Backed up by the research, it shows that no matter how good and effective your policy is, it may be for nothing if there is not enforcing judicial system in place and if firms are unwilling to cooperate with them. This should be the major focus for Latin American countries looking to reform their corporate governance systems. Certain specific suggestions such as a change in approach to how we view corporate governance in emerging economies right up to a complete redo of the judiciary systems in place in Latin America have been referred to in this piece. Secondly, the unseen culture aspect that has came up a lot. There seems to be a general distrust from owners of companies in Latin America of the changing of principles to allow minority shareholders to have a piece of their firm, even when the recorded benefits could be huge. The OECD finding this and recommending educational means to encourage people to change their governing codes is telling. That and the unwillingness to adhere to the principles of the agency theory, separating ownership from management continues to cause problems for the region.

It would be of interest to see what an OECD white paper on corporate governance in Latin America since their flurry of such documents in the early 2000's. It is of my opinion that many of the recommendations raised then would again be raised as if they had little been addressed in almost 20 years. If countries focused on recommend change to corporate governance now, they might just be kicking themselves that they hadn't done it 13 years earlier to gain the same benefits to their capital markets as similar emerging economies have been.

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