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On the Shareholders' Composition of the Composition of the Company and the Governance Mechanisms of the Firm. Can this contribute to the firm performance (including the capacity to attract capital and bank allowances)?

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Introduction

Governance is a central aspect of every social institution, be it the family, a corporation, and most importantly the State.

In etymological terms, the origin of the word “governance” descends from the Greek verb *kybernein*, which meant steering, guiding, or maneuvering a ship or a vehicle. The original connotation of the word, therefore, was mainly attached to the function of direction rather than control. I believe that this original connotation should still be valid today, and that policy makers, businessmen, as well as ordinary people should all recognize the importance of a good governance system, a system aimed at ensuring a principled conduct and a discipline of long-term thinking within every organization.

The object of this thesis, however, is restricted to corporate governance, that is the governance of business corporations. My intention is to devote corporate governance the attention it deserves, in order to raise awareness on this subject and call for the concerted action of decision-makers.

In one of his writings, James Wolfensohn, former President of the World Bank said: “ *the governance of the corporation is now as important in the world economy as the government of countries*”. This is absolutely true, as it has been proved by recent examples of massive corporate collapses resulting from weak systems of corporate governance. In fact, it is not possible to deny the prominent position corporations have come to play both under an economic and social point of view, not to mention their global reach and their political power, which often exceed those of governments themselves.

Moreover, corporate governance is expected to meet the expectations of society, and therefore be aimed at protecting shareholders’ rights, promoting an independent monitoring of management, increasing transparency, ensuring the optimal use of economic resources, and lowering firms’ cost of capital (by improving the confidence of foreign and domestic investors). The first part of this thesis, in particular, investigates how corporate governance helps achieving the goals mentioned above.

This thesis is made up of two parts: the first part, encompassing Chapter 1, is purely theoretical, and is instrumental to a better understanding of the empirical analysis encompassing Chapter 2 and Chapter 3.

The first chapter of this thesis is an attempt to provide an essential overview of previous research on corporate governance.

This chapter is foundational for two reasons. First, it provides some important definitions (such as those of corporate governance itself) and describes the framework through which corporate governance is approached throughout this dissertation, namely the agency theory framework. Moreover, a brief history of the evolution of the firm helps to understand the circumstances which led to the birth of the modern corporation, whose implications under a corporate governance point of view have been reported in so many influential studies.

At the same time, this chapter is foundational because the synthetic overview of prior research on corporate governance helps contextualize the ensuing empirical analysis object of this dissertation. In fact, because academic literature on corporate governance is so broad, often encompassing the most diverse issues, it may be helpful to resort to a sort of conceptual framework allowing to navigate through the complexity stemming from the fact that many studies tend to contradict one another. The main idea is that this is a direct consequence of the fact that there are no golden rules in corporate governance, but rather a set of recommendations that are appropriate under certain circumstances, depending both on the structural characteristics of the firm (for example, ownership structure) and on contextual country features (for example, the level of investor protection). Previous studies on corporate governance, therefore, are important to understand the key issues firms have to consider when configuring their own governance system, so that they can implement appropriate solutions against the challenges they are facing. Thus, while the efforts of corporations with a rather diffused ownership structure will be directed at restraining the conflicts arising between managers and shareholders, corporations with a highly concentrated ownership will be rather facing the conflict arising between controlling and non-controlling shareholders. In a similar fashion, splitting the role of CEO and Chairman of the Board of Directors may be a sound practice under some circumstances, but it could be detrimental to firm performance

if, within a firm, holding both charges constitutes an effective incentive mechanism for aspiring CEOs.

Finally, in Chapter 1 I introduce the topic of corporate social responsibility and I explain the reasons why current research is adopting more and more a broader perspective on the topic of corporate governance. In particular, as I will explain in greater detail, increasing attention has been drawn to the effects that corporate governance exerts on all firm stakeholders, not merely management and shareholders. This is mainly due to the climate of great instability and uncertainty which characterizes modern society and which is pushing towards the implementation of solutions that are beneficial to the whole community, especially is sensible topics such as corporate transparency or environmental sustainability.

In the second chapter of this thesis I will briefly describe the two most widely diffused systems of corporate governance globally: the insider-dominated systems and the outsider-dominated systems. These systems, in particular, lie on the extremes of a continuum, while it is more probable that a country's corporate governance arrangements are found in between these two extremes.

Three cases studies will be presented in order to better understand the differences in corporate governance systems adopted by countries worldwide. The case of the United Kingdom will be used to represent corporate government arrangements which are typical of Anglo-Saxon countries. In these countries, in particular, corporations are characterized by a diffuse ownership, which in turn determines a strict separation between ownership and control. These characteristics, however, are not observed in European and Asian countries, where ownership concentration is very high and leads to the exacerbation of the conflicts between majority and minority shareholders. These countries will be represented by Germany, while Italy, notwithstanding the commonalities with countries which fall under this second categorization, will be presented as a stand-alone case.

The categorization of corporate governance systems is instrumental to the introduction of the empirical analysis that I have carried out together with prof. Mantovani, and which represents the core of this thesis. The first aim of this research, in fact, was to investigate the characteristics of corporate governance across Europe in order to verify whether a convergence in corporate governance

arrangements versus persisting differences between countries should be expected. At the same time, through this research we also wanted to verify whether there are congruencies at country level between the goodness of corporate governance and long-term performance.

In the third chapter of this thesis, which is purely empirical, I present the results of the same relationships between corporate governance and performance, level of indebtedness and merit of credit, but at individual firm level. I will also present the results that we obtained by regressing the structural indicators on governance indicators, in order to find whether the former influence the way corporate governance mechanisms are formed within firms. Finally, I present the results of the investigation of the effects of corporate governance on firms' financing strategy.

To conclude this work I'll present very briefly the main findings of this study.

Corporate Governance Theory

1.1 Corporate Governance: from a narrow towards a broader definition

What is **corporate governance** and why does it matter? In times characterized by severe economic downturns, it is not surprising that governance-related issues are given special attention, emerging among the most sensitive and controversial topics of the public debate. As a matter of fact, improvements of corporate governance practices and mechanisms have often come in response to major scandals, such as those which followed in the wake of the dotcom bubble (pointing out the severe conflict of interest by brokers and analysts), or the Enron/WorldCom failures (pointing out the issues related to auditor and audit committee independence, and deficiencies in accounting standards) (OECD, 2009); (Bainbridge, 2012). Similarly, the recent financial crisis unveiled other failures and weaknesses of current corporate governance arrangements, as these routines failed to help companies cultivate sound business practices, and did not serve their purpose to protect them against excessive risk taking (OECD, 2009).

But before assessing the importance of good corporate governance practices, it is of the utmost importance to provide an explanation of what corporate governance actually means. This task can be more difficult than expected, because a common definition of corporate governance is still missing today. As a matter of fact, despite many scholars have tried to lay down a general working definition of corporate governance, one definition still varies from another, often leading to confusion.

All of the existing definitions emphasize the importance of establishing good corporate governance practices for the good of the economy and the nation, but there is still a perceptible difference in the importance they attribute to objectives, goals, and the means and tools to achieve them (Fernando, 2009).

There are several factors contributing to the large variety of corporate governance definitions. First of all, because corporate governance encompasses standards and practices dealing with different aspects of a company's management, a number of different theoretical frameworks have emerged to explain and analyze firms'

governance. At the same time, countries' legislature and culture also play a very important role in shaping corporate governance and the way it is defined.

Early attempts to define the concept of corporate governance appear in the United Kingdom Cadbury Report (1992), where corporate governance was simply depicted as "the system by which companies are directed and controlled" (Du Plessis, Hargovan, & Bagaric, 2011). This definition, however, is now considered to be highly unsatisfactory. In particular, this widespread feeling emerged from a survey reported in Solomon's book *Corporate Governance and Accountability*, where a large number of UK institutional investors were asked to evaluate different definitions of corporate governance, each adopting a different view of the subject. The survey found that institutional investors slightly agreed on this overly narrow definition of corporate governance, because it fails to stress a broader level of accountability to shareholders and other stakeholders. Hence the need for other, more accepted definitions.

Corporate governance as a subject may be treated on a narrow or broad manner, depending of the viewpoints of scholars of this field.

If broadly defined, corporate governance "consists of the institutional structures, legal rules, and best practices that determine which body within the corporation is entitled to make decisions, how the members of that body are chosen, and the norms that should guide decision making" (Bainbridge, 2012, p. 2). According to this view, corporate governance corresponds to the web of relationships that exists, not only between a company and its owners (i.e. shareholders), but also between the company and a broader range of other stakeholders, such as employees, customers, suppliers, and so on (Solomon, 2007, p. 12).

Another definition adopts a narrower view on corporate governance, which is seen as the "ways in which the suppliers of finance to corporations assure themselves of getting a return on their investment" (Shleifer & Vishny, 1997). In this case, corporate governance is expected to give answers to questions like: How do suppliers of finance get managers to return some of the profits to them? How do they make sure that the capital they supplied is invested in bad projects? How do suppliers of finance control managers? This paradigm is well-known in finance

literature, and is traditionally referred to as agency theory. According to this definition, therefore, corporate governance consists of the set of rules established to constrain the principal-agent problem inherent to the public corporation's structure.

The different frameworks used to analyze corporate governance approach the subject by adopting perspectives and terminologies arising from different disciplines. For example, the agency theory paradigm is inherited from the fields of economic and finance, while the broader, stakeholder approach arise from a more social-oriented perspective on corporate governance (Solomon, 2007, p. 16). However, despite the marked differences arising from the fact that these frameworks adopt different lens when analyzing corporate governance, they tend to overlap theoretically and to share some commonalities.

In business literature, in particular, the most recurring theoretical frameworks on corporate governance essentially are the agency theory already mentioned above, the transaction theory, and the stakeholder theory at the base of all broad definitions of corporate governance.

Because scholars' contribution to each of these theoretical frameworks is massive, I decided to dedicate my thesis to the study of corporate governance under the agency theory theoretical framework, which will be presented in greater detail in the third section of this chapter. But before addressing the issue of how the separation of ownership and control contributes to the manifestation of the principal-agent problem, it may be useful to relate a brief history of the evolution of the firm into the modern corporation.

1.2 The evolution of the firm: how the Modern Corporation was born

Although law considers the corporation to be a fictional person, at its core, it should better be regarded as an organization, whose primary objective is to adapt to environmental changes and to respond to the challenges posed by the growing complexity which permeates modern society. In this respect, the modern corporation is the result of a Darwinian process directed towards the corporation's own perpetuation and growth (Monks & Minow, 2011).

In the popular book *The Modern Corporation and Private Property*, Berle and Means (1932) argued that, starting from the Industrial Revolution, corporations have ceased to be a mere method of property tenure, becoming a major social institution and the means through which economic life is organized. Indeed, corporations have grown to tremendous proportions, in a way that, at the beginning of the XX century, was beyond the imagination of most statesman and businessmen.

Starting from the late XIX century, in fact, companies started to grow larger than had previously been the norm. This was primarily due to the fact that new technological advancements made it necessary for firms to increase market share and achieve a leadership position in the market, taking advantage from the huge benefits offered by economies of scale. This inevitably led to an increase of capital requirements for the typical corporation, with the result that financial resources conferred by what had always been a small group of wealthy individuals were no longer sufficient.

On the contrary, modern corporation are the means whereby the wealth of innumerable individuals has been concentrated under the same central control and surrendered to a unified direction (Berle & Means, 1932).

In addition, it must be noted that, at that particular time, private property of investment ownership had just started to be accepted as a social norm. As a matter of fact, until then, it had always been assumed that most property would belong to the state, the church, or a selected number of wealthy individuals (Monks & Minow, 2011). The advent of the modern corporation, instead, changed the rules of the game, leading to the multiplication of company owners and, consequently, to a greater dispersion of company ownership. As a result, shareholders progressively assisted to a radical change of their status, as they had no other chance than surrendering their own wealth to those in control of the corporation.

This is how public corporations are born, and how the separation between ownership and control, which is the main determinant of the principal-agent problem affecting almost single aspect of a firm's corporate governance, arose. Berle and Means (1932) claimed that it is exactly this separation of control from ownership which makes possible tremendous aggregations of properties.

A very important characteristic of modern corporations is the fact that they are structured in the form of limited liabilities companies. In particular, a limited liability company is a corporate structure whereby the members of the company cannot be considered personally liable for the company's debts and liabilities. Hence, if a corporation goes bankrupt and is sued by its creditors, what it is owed to the corporation is not owed to its shareholders. This means that the corporation is separate from its owners and employees. However, limited liability also entails limited authority, because every partner has equal right to run the company with all of the other partners (unless specific contractual agreements).

Finally, it should be remembered that the attribution of the legal personality to the corporation has contributed to extend its lifetime. This is a fairly recent development, because prior to the XIX century business corporations had a limited lifespan of some tens of years, which usually coincided with owners' life. Legal personality, instead, allows the corporation to act, to own, and to continue past the life span of any individual or group. As a matter of fact, it is because corporations are defined as legal persons that they may own property, including real estate, copyrights, and other assets.

1.3 Agency Theory

Agency theory is a branch of economics focusing on cooperation in situations where externalities, uncertainty, limited observability, or asymmetric information seriously harm the good functioning of the market (Bamberg & Spremann, 1989).

Economic research on agency theory covers a great variety of themes, but its primary focus lies on the so-called principal-agent problem, which has been largely investigated by notable authors, such as Berle and Means (1932) Coase (1937), Jensen and Meckling (1976), Fama and Jensen (1983), and Jensen (1986).

The agency problem, in particular, is a direct consequence of the separation of ownership and control, which characterizes modern corporations. In an extremely simplified situation, the principal-agent problem involves two individuals: the agent, who is the individual in charge of making decisions on behalf of the principal, and the principal, whose welfare is affected by the agent's behavior. In finance, for

example, the typical principal-agent problem concerns the difficulties financiers have in assuring that their funds are not expropriated or wasted on unattractive projects by the company's management.

The principal-agent problem is relevant, because when the agent adopts undesirable behaviors, the principal can be negatively affected. Hence the need to provide incentives to the agent, in return of a certain decision/action/effort.

This typically involves signing a contract which specifies what the agent has to do, and the outcomes expected by the principal. Nevertheless, because most future contingencies are hard to describe and foresee (this situation is referred to as bounded rationality), complete contracts are technologically infeasible (Shleifer & Vishny, 1997). As a consequence, the agent is granted residual control rights, i.e. rights to make decisions in circumstances not fully foreseen by the contract.

At the same time, another peculiar aspect of the principal-agent relationship is the principal's inability to effectively control the agent's course of action, which results in asymmetric information with respect to the agent's behavior (Grossman & Hart, 1986), (Hart & Moore, 1990). This means that agents end up again with significant discretionary power, which gives them the opportunity to adopt self-interested behaviors.

In the last years, a considerable amount of evidence has documented the prevalence of managerial behavior that does not serve the interests of investors (particularly shareholders). A seminal contribution in this area was given by Williamson (1963) and his model of managerial discretion. This model, in very simple words, theorizes that profit maximization is not the primary objective of managers of principal firms (i.e. firms where a separation between ownership and control occurs). Instead, the model assumes that utility maximization represents the manager's main preoccupation.

The essential notion proposed by the model is that certain classes of expenditures provide greater benefits to management. This means that management does not have a neutral attitude towards costs. These expenses, in particular, include, staff expense, expenditures for emoluments, and funds available for discretionary investment.

More precisely, expansion of staff is an activity that offers positive rewards because, since promotional opportunities within a firm of a given size are limited, increased responsibility (through a larger staff) allow managers to achieve the same benefits of a promotion. and therefore it is difficult to resist. In particular, not only the expansion of staff is an indirect means to the attainment of salary, but it is also a source of security, power status, prestige, and professional achievement as well (Williamson O. E., 1963).

Expenditures on emoluments, instead, refer to that fraction of managerial salaries and perquisites that are discretionary. More precisely, emoluments are economic rents and are not associated with managers' productivity. As for expansion of staff, emoluments are a source of material satisfaction and an indirect source of status and prestige.

According to Williamson's utility-maximizing hypothesis, opportunities and managerial preference for discretionary behavior will have a decided impact on the expenditures of the firm. Because the firm is operated by managers attending self-interests, then the expectation is that the expenses mentioned above are expanded beyond the levels called for by strictly profit considerations.

In order to test his hypothesis, Williamson considered only firms characterized by a separation of ownership and control (which typically is found in larger corporations). In particular, Williamson included 50 major industries in his analysis and considered two firms in each. Therefore his sample was made of 100 principal firms.

Th author found that, under the utility-maximizing hypothesis, managerial salaries were positively correlated with opportunities for discretion. These include (((((

At the same time, Williamson found that there is also a positive relationship between composition of the board and earnings-retention policy. As a matter of fact, high internal representation on boards provides the opportunity for management to shift the dividend policy to its advantage, which results in increased opportunities for earning retention at the expenses of other shareholders. Expropriates funds are thus available to the management for the pursuit of expansionary goals, which exceed the amount dictated by profit considerations alone.

According to Jensen (1986) the worst cases of shareholders expropriation occur in firms with poor investment opportunities and excess cash. In this case, managers choose to reinvest the free cash instead of returning it to investors. The majority of evidences against this bad managerial practice come from the stock market where, if stock prices fall when managers announce a particular action, then the common belief is that this action must have served the interests of managers rather than those of the shareholders (Shleifer & Vishny, 1997). In particular, among the actions undertaken by managers, which often proved to be detrimental to investors, it is possible to remember the case of some acquisitions, and diversification and growth policies pursued by managers against investors' objectives.

So, if we apply agency theory to the field of corporate governance, we can ask: why do shareholders invest their money in the company, when both theory and evidence suggest that managers have an enormous discretionary power when it comes to deciding what to do with those financial resources? The simple answer is that, once the money is invested in the company, investors have no special ability with respect to what has to be done with that money, and that's the reason managers were hired in the first place (Shleifer & Vishny, 1997).

At the same time, another possible explanation lies on the idea that managers have reputations to preserve, and this explains why they deliver their agreements despite it would be possible to undertake actions much more convenient for them (Kreps, 1990). According to this view, managers respect their duties because they want to raise funds in the future, and hence need to establish a good reputation, in order to convince investors to trust them. However, models relying on the reputation thesis tend to have problems, because they fall into a backward recursion problem (Shleifer & Vishny, 1997). In fact, if in the last stadium the future benefits to the manager of being able to raise funds are lower than the costs of repaying investors, the manager rationally defaults. But if investors are able to anticipate this behavior, they won't invest any money in the firm. This game unravels and there should not be any possibility of external finance.

However, the reason that principally justifies external financing to firms is that there is a contract between investors and managers, which can be legally enforced in front

of the court. Corporate governance systems worldwide mainly differ in the nature of legal obligations that managers have to investors, as well as in how the courts interpret and enforce these obligations. That's why firms raise more funds in some countries than in others (La Porta, Lopez-de-Silanes, Shleifer, & Vishny, 2000). In particular, the most important legal right shareholders have is the right to vote on important matters, such as mergers and liquidations, or in the election of board of directors. Nevertheless, voting rights can be difficult to enforce, especially in countries with weaker legal systems.

Corporate governance systems, therefore, are needed to help company's owners (i.e. shareholders) and other investors to constrain the principal-agent problem, by introducing appropriate practices and mechanisms aimed at improving control and monitoring systems, and at aligning managers' interests to theirs. In other words, corporate governance can be considered as the set of standards and routines through which owners and outside financier protect themselves against expropriation by the insiders (i.e. the managers) (La Porta, Lopez-de-Silanes, Shleifer, & Vishny, 2000). These standards and practices deal with different aspect of the firm, such as ownership structure, boards' functioning, directors independence and remuneration, internal controls, and so on.

The following section covers some of these aspects, which will later be used to make a comparison of corporate governance systems across different European countries.

1.4 Corporate Governance and Firm's Performance

As far as the relationship between corporate governance and firm's performance is concerned, the existence of a positive relationship between the two has already been established through several studies in business literature.

In the following sections, several aspects of corporate governance and their impact on firm performance are analyzed. In particular, evidences supporting the belief that a better corporate governance results in a higher firm value and a more profitable firm performance are important, because they allow to prove whether the difficulties to heavy invest in corporate governance are source from the

misperception of true benefit for the corporate performance and the value of the company.

1.4.1 Corporate Governance and Ownership Structure and Control

In business literature, the existence of a relationship between the goodness of a firm's corporate governance mechanisms and ownership structure has been largely debated by academics, with no clear understanding on what constitutes a positive impact on the firm. Great part of these studies focuses on firms' ownership concentration, and aim at studying whether there are significant differences (in terms of governance quality) between firms with concentrated or diffuse ownership. A firm's ownership, in particular, is said to be "concentrated" when a large amount of stock is owned by few shareholders, whether they are members of the founding family or institutional investors such as mutual or pension funds.

In the previous section, I have introduced the principal-agent problem, and stated that, when firm owners delegate the running of the company to management, an agency problem arises. This is more likely to happen when a company's ownership is highly dispersed, as it was initially suggested by Berle and Means (1932).

According to Jensen and Meckling (1976), the only possible "zero-agency-cost case"¹ is that of a firm owned solely by a single owner-manager. But when management owns less than 100 percent of the firm's equity, shareholders inevitably incur agency costs, because of an incomplete alignment of the management's and owner's interests. This misalignment, particularly, takes the form of preference for on-the-job perks, shirking, and making self-interested decisions that reduce shareholders' wealth.

At the same time, agency costs may exist even when a single owner controls 100 percent of the stock but hires an outsider to manage the business. According to Ang, Cole and Wuh Lin, in fact, even if agency costs are small because the sole owner can internalize all monitoring costs and has the right to hire and fire the manager,

¹ Because of limitations imposed by personal wealth constraint, exchange regulations on the minimum number of shareholders, and other considerations, no publicly traded firm is entirely owned by management. However, no-agency-cost base case firms can be found among non-publicly traded firms.

there are still residual agency costs to bear, which are due to a failure of the owner's monitoring activities. As a matter of fact, by one hand the sole owner may not be able to monitor perfectly the manager's conduct because of a lack of time. On the other hand, owners of small companies typically lack financial sophistication, and may not be able to perform audits or to fully understand the operating or financial results of their companies. This means that the separation of management and control suggested by Fama and Jensen (1983), may be incomplete or ineffective.

Nevertheless, while some authors suggest that a greater ownership dispersion (because of the separation of ownership and control) causes the aggravation of agency problems and therefore the deterioration of corporate governance (Berle & Means, 1933; Jensen & Meckling, 1976; Fama and Jensen, 1983); other authors claim that when ownership is highly concentrated, agency problems simply shift from those between ownership and management to those between controlling shareholders and minority shareholders.

In their paper '*Corporate Ownership Around the World*' La Porta, Lopez de Silanes and Shleifer presented data on ownership structure of large corporations in 27 wealthy economies. The authors found that, with the exception of economies with very good shareholders' protection, firms characterized by a dispersed ownership structure were not as common as argued by Berle and Means. More precisely, only one third of companies of the wealthiest countries were widely held, while almost half of the countries were either family-controlled or state-controlled.

The authors further divided the 27 countries included in their sample into two groups: one including countries with better than median shareholder protection rights, and the other including countries with median and worse than median shareholder protection rights. They found that high levels of ownership concentration tend to characterize countries with poor investor protection rights.

The hypothesis that owners prefer to keep control of their firms in countries with poor investor protection rights was investigated also by Goergen and Renneboog (2003), who analyzed the discrepancy in the levels of control concentration between listed continental European and Anglo-American firms. La Porta et al. had already found that while about 90% of companies listed on the London Stock Exchange did

not have a major shareholder owning 25% or more of the voting rights, 85% of the listed German companies had larger shareholders. These same differences were observed also by Georgen and Renneboog, who also suggested that the relative cost of holding large control stakes is different across countries. In fact, in countries with low protection of shareholders rights (like Germany), shareholders prefer to hold larger stakes, taking advantage of private benefits of control, while in countries with high investor protection (like the United Kingdom) investors are better protected than in Germany, that's why the relative cost of control is higher.

Regulatory determinants of control concentration levels appear to be stock exchange listing requirements, shareholder protection regulation, control disclosure, fiduciary duties and composition of the board of directors, voting rules and practice, informational transparency, and takeover code. When the regulatory and legal environment is favorable, control is less valuable to shareholders.

Given the results of these analysis, therefore, it is clear that, for most countries, corporate governance practices should be directed at preventing the expropriation of minority shareholders by controlling shareholders, rather than at preventing agency problems arising from the misalignment of management and shareholder's interests (La Porta, Lopez-de-Silanes, & Shleifer, 1999).

Large investors' interests, in fact, may also not necessarily coincide with the interests of other investors in the firm. When this happens, the presence of large shareholders in a company ownership inevitably leads to expropriation of other (minority) investors, pursuit of personal (nonprofit-maximizing objectives), and expropriation of other stakeholder (Shleifer & Vishny, 1997).

However, blockholders' ability to enjoy the private benefits of control greatly depends on the extent to which their control rights exceed their cash flow rights. Corporation securities, in fact, may be designed so that their claim to vote is disproportionately larger or smaller than their claim to income, deviating from the one share-one vote rule that it is largely considered beneficial to corporate governance practices (Grossman & Hart., 1988; Harris & Raviv, 1988). Indeed, academic research provided evidence of the existence of disproportional ownership in many publicly listed companies, resulting from the adoption of mechanisms that

significantly deviate from the proportionality principle implied by the one share-one vote rule (typically pyramidal structures, cross-shareholdings, multiple voting shares, non-voting shares, priority shares, golden shares, voting-rights and ownership ceilings, and other similar mechanisms). In firms ruled by such ownership tools, large shareholders can exert the majority of voting rights, appoint most board directors and condition strategic and operating options of companies, despite they hold minority cash-flow rights (Saggese, 2016).

Grossman and Hart (1988) and Harris and Raviv (1988), in particular, suggest that deviations from the one share-one vote rule tend to be larger when private benefits of control are higher. These benefits include perquisites of control, synergy benefits realized by controlling shareholders, the possibility of excluding minority shareholders at a price below the value of their shares, and in extreme cases the diversion of company resources to controlling shareholders subsidiaries.

As far as concerns the specific mechanisms devised by companies to increase their control over the corporation, there are multiple studies in business literature dealing with the topic.

For example, La Porta et al. (1999), in the cross-country analysis already mentioned above, described some of the mechanisms through which controlling shareholders exercise their power in large firms.

In particular, the authors suggested that multiple classes of shares are not a central mechanism for gaining control over the corporation, as didn't find significant deviations from the one share-one vote rule both for countries with high investor protection rights and for countries with low investor protection rights. More precisely, they found that it took on average 17.7% of capital to buy 20% of votes in countries with poor investor protection, against 19.7 in countries with good investor protection.

Instead, the authors found that 18% of firms within the group of countries with good investor protection rights and 31% of those in the group with poor protection rights were controlled through pyramidal structures. Thus, pyramid structures represent a more important control mechanism for large shareholders than multiple classes of shares.

Finally, La Porta and al. found that cross-shareholdings were rather rare among the firms included in their sample (but it should be noted that they are considered illegal in many countries).

In another study, Faccio and Lang (2002) analyzed the ultimate ownership and control in 13 Western European countries, in order to find discrepancies between ultimate ownership and control. The final objective of this study was to document how ultimate controlling owners achieve control rights in excess of their ownership rights through mechanisms such as one-share-one-vote rule, pyramiding, and cross-holding. If evidence supporting the existence of such mechanisms was found, then it could be concluded that it was possible for a small number of families to control firms representing a large percentage of stock market capitalization.

The study included a large number of medium and small-sized corporations, and both financial and non-financial companies. The authors found that Western European firms are more likely to be widely held (36.93%) or family controlled (44.29%), and reported the use of multiple classes of shares, pyramidal structures, holdings through multiple control chains, and cross-holdings as devices to that give the controlling shareholders control rights in excess of their cash-flow rights.

In a later study, Faccio, Lang and Young investigated ownership concentration in 9 of the most advanced East Asian countries, where family control is even more pronounced than in Western European countries. The research documented an extraordinary ownership concentration in those countries, as it was found that 8 group controlled more than 25% of the corporations. This control, moreover, was obscured behind layers of corporations, hence insulated against the forces of competition on less-than-transparent capital markets. Once again, evidence supported the idea that, for high levels of ownership concentration, the salient agency problem in these economies is expropriation of outside shareholders by the controlling shareholder.

As noted by Lucian Bebchuk et al. (1998), Daniel Wolfenzon (1999) and Stijn Claessens et al. (1999a), particularly rich possibilities for expropriation arise when the corporation is affiliated to a group of corporations, all controlled by the same shareholder, which Faccio, Lang and Young (2000) found to be true for about half the corporations in in East Asia. Corporate wealth can then be expropriated by the

insiders who set unfair terms for intra-group sales of goods and services and transfers of assets and control stakes.

In conclusion, while a higher ownership concentration can be beneficial to firm performance, as it is suggested by the monitoring hypothesis, once concentration levels are too high, firm's performance get worse, as it is suggested by the expropriation hypothesis. This is particularly true during a crisis period, when controlling shareholders' incentives to expropriate minority shareholders negatively affect the goodness of a firm's corporate governance (Bae, Baek, Kang, & Liu, 2012).

The result is that the effect of ownership concentration on the goodness of a firm's corporate governance depends greatly on how control by large shareholder is exerted over the corporation.

1.4.2 Managerial Ownership

Another important issue to address is whether firm ownership structure is characterized by the presence of managers among shareholders.

Early analysis on this subject found a linear relationship between managerial ownership and firm performance.

Jensen and Meckling (1976) claimed that managerial ownership helps aligning the interests of shareholders and managers. This means that, the higher managerial ownership in a firm, the higher the firm's performance, because managers are less inclined to divert resources away from value maximization. Over certain levels of ownership, in fact, managers' consumption of perquisites, such as an attractive salary, may outweigh the loss they suffer from a reduced value of the firm. This hypothesis is known as 'convergence of interests hypothesis' (Short & Keasey, 1999).

Other studies ((Demsetz, 1983); (Fama & Jensen, 1983)), instead, claim that market discipline will force managers to adhere to value maximization even at very low levels of ownership. In fact, even at low levels of managerial ownership, market discipline, particularly the managerial labor market (Fama, 1980) and the market

for corporate control (Jensen & Ruback, 1983) may still force managers towards value maximization.

That's why later analysis on the relationship between firm's performance and managerial ownership have started to consider also non-linear forms, which allow for two possible effects influencing the relationship between firms' performance and managerial ownership: alignment and entrenchment.

Morck et al. (1988), for example, found that, while low and very high level of managerial ownership are consistent with the alignment hypothesis, sufficiently high levels of managerial ownership could lead to entrenchment, as external shareholders find it difficult to control the actions of company management. At sufficiently high level of managerial ownership, in fact, managers have sufficient control to pursue their own objectives without fear of discipline from other shareholders. This combination of the convergence of interest and entrenchment, then, determines a non-linear relationship between firm performance and managerial ownership. More precisely, using Tobin's Q as a measure of performance and the percentage of shares owned by the board directors as a measure of ownership, Morck et al. found that the convergence of interest effects are dominant within the 0% to 5% range and above the 25% ownership level, while the entrenchment effects are dominant within the 5% to 25% ownership range.

Similarly, McConnell and Servaes (1990) regressed Tobin's Q against managerial ownership and managerial ownership squared. They found that the coefficient on managerial ownership was statistically significant and positive, whereas the coefficient on managerial ownership squared was statistically significant and negative. This implies a non-linear relationship between managerial ownership and firm's value. In particular, the authors found that the link between firms' performance and managerial ownership was positive for managerial ownership between 0% and approximately 40–50%. These findings, therefore, differ from those of Morck et al., who found entrenchment to occur in the 5% to 25% ownership range.

Later, Short and Keasey (1999) conducted a similar study to those of Morck et al. (1988) and Mc Connell and Servaes (1990). In order to test whether there is a non-

linear relationship between firm performance and managerial ownership, they analyzed a random sample of 225 firms listed on the London Stock Exchange. Their data suggest that UK firms become entrenched at higher level of managerial ownership than US firms. More precisely, the authors found the alignment effects prevail in the 0% to 12.99% ownership range and when managerial ownership exceeds 49.99%, whereas the entrenchment effects prevail in the 12.99% to 41.99% ownership range. Therefore, Short and Keasey concluded that managers in the UK need higher stakes to protect themselves from shareholders monitoring.

The results of these later studies, therefore, find evidence that the alignment hypothesis is valid both for low and high levels of managerial ownership, while the entrenchment hypothesis is valid for managerial ownership levels staying in the middle.

However, none of these studies addressed the issue of endogeneity, and therefore managerial ownership should be considered as an explanatory variable rather than as an explained variable. Himmelberg et al. (1999) conducted a study in order to document the extent to which managerial ownership is endogenously determined by the contracting environment. The explanatory variables used in the model were stock price variability, firm size, capital intensity, R&D intensity, advertising intensity, cash flow, and investment rate. The variables were used as proxies for moral hazard. The authors also used panel data to estimate the importance of unobservable time-invariant elements. The aim was to investigate the hypothesis that managerial ownership is related to observable and unobservable characteristics influencing contracts. In particular, the authors found that the proxies for the contracting environment faced by the firm (i.e. the observable characteristics) strongly predict the structure of managerial ownership. Moreover they found that managerial ownership and firm performance are determined by common characteristics, some of which are unobservable. The main implication of this study is that, because there are common characteristics affecting both managerial ownership and firm performance, the relationships between the two found in previous studies should be considered spurious.

1.4.3 Board's Role and Director Independence

Board's Traditional Functions

The most basic principle of corporate governance is that firms should be subject to the direction of a board of directors. Previous studies on agency theory, however, suggest that corporations, in reality, are run neither by the board of directors, nor the shareholders, but rather by the firm's senior management. The consequence of this empirical evidence is that firms' performance may be negatively affected by the principal-agent conflict implied by this governance mechanism.

Starting from 1970s, though, a combination of new legal requirements and enhanced market expectations succeeded at empowering both boards and shareholders against senior management. In parallel, other provisions improved the level of boards' independence. As a result of all these changes, modern boards of directors typically are smaller than their antecedents, more independent from senior management, have better access to information, own more stock, and are expected to meet more often (Bainbridge, 2012, p. 44).

Notwithstanding, despite boards' evolution has contributed to significantly improve the goodness of firms' corporate governance, the transformation remains incomplete, as the board is still affected by considerable influences from senior management, particularly powerful CEOs.

But before stating the positive contribution of boards' composition and independence on firms' performance, it is important to remember which are the functions that are traditionally attributed to the Board of Directors.

By looking exclusively to corporations' statutes, one would assume that the board of directors plays a very active role in the running of the company, as there are specific mandates that only the board can fulfill. These include, for example, the approval for mergers and related transactions (such as sales of all or substantial corporate assets), the issuance of stock, the distribution of dividends, and amendments to the articles of incorporation (Bainbridge, 2012, p. 45). These activities, however, cannot be really considered as daily operations, but rather as extraordinary activities that require the intervention of an independent supervisory

body. The Board of Directors, therefore, is called to express an opinion only on very important matters, as well as supervising senior managers, who instead are responsible for the conduct of day-to-day business. Members of the Board of Directors, in fact, typically are outsiders with a full-time job elsewhere and little time to devote to the running of the company's business.

Of course, members of the Board of Directors also retain some managerial functions, such as broad policy making or, at least, review and approval of major policies (Bainbridge, 2012, p. 46). Moreover, they are responsible for hiring the top management team, especially the CEO, and setting their compensation.

Despite the Board of Directors is entitled to carry out some managerial functions, however, the fundamental role of members of the Board is the monitoring of senior management. The law, in fact, acknowledges that modern corporations are large, complex organizations, whereas members of modern boards have little time to devote to operational roles. This situation implies that members of the board are forced to delegate almost all management functions to senior management, who in turns will delegate most decisions to subordinate employees.

The monitoring function of the board, in particular, is expected to serve as a constraint on the principal-agent problem implied by the separation of ownership and control. However, it also raises another question: who monitors the monitors? The answer to this question is that shareholders, being the corporation's residual claimants, should act as ultimate monitors. Nevertheless, even if the law ensures shareholders some enforcement and electoral rights, these are reserved only for extraordinary situations. Moreover, shareholders of public companies often do not exercise the kind of control necessary for meaningful monitoring of company's agents (this aspect is known as the free-rider problem and will be addressed in the following sections).

Finally, there is still another function fulfilled by members of the Board of Directors: they can provide a number of services to senior management, from admittance to networks for gathering resources and obtaining businesses, to an easier access to capital.

At the same time, besides providing a contact between the firm and the lender, financial institutions' representatives who are also members of the Board of

Directors can help to reduce the firm's cost of capital, because they can use their board membership to better monitor the company (with respect to what would be possible for an outsider), which in turn leads to risks reduction (and hence a reduction of the cost of capital for the firm).

Moreover, members of the Board of Directors can offer counsel to the CEO, providing alternative point of views from different areas such as accounting, finance, management, and law.

Finally, if a board member is politically connected, then his access to legislators and regulators can help the firm in dealing with the government, for example for obtaining contracts.

It is useful to remember that the relative weight of the functions traditionally attributed to the Board of Directors has shifted over time. In the 1970s, in fact, boards had a mainly advisory role. Starting from the 1990s, by contrast, increased emphasis was placed on managerial functions in the sense of broad policy making and setting strategy. Finally, by the end of the 1990s, boards were becoming active and independent monitors of senior management (Adams, Hermalin, & Weisbach, 2010)

Board's Independence

A very important aspect related to the contribution of the Board of Directors to the quality of a firm's corporate governance concerns directors' independence. As a matter of fact, a board made up predominantly of insiders, i.e. senior managers, is not very well suited to monitor CEO's actions. Hence the acceleration towards Board independence after the financial crisis.

How is it possible to assess whether a member of the Board of Director is independent? Typically, a director is said to be independent if he is not linked through personal or other relationships to management.

This definition, however, is too general and requires further specifications. In particular, in order to assess the degree of independence of a firm Board it is possible to resort to Moody's criteria for assessing the degree of directors independence. Every year, in fact, Moody's evaluates the level of board

independence of North American companies as part of its corporate governance assessment of these companies.

In particular, according to Moody's criteria, current or former executives and founders cannot be considered as independent members of the Board.

At the same time, members of the Board of directors who are also assigned to a consulting or financial position within the firm, appear to be non-independent, because consulting or financial arrangements can significantly change the nature of the relationship between the firm and the director.

Negative implications for directors' independence are also given by related party transactions, including legal, supplier, customer, financial, or professional service arrangements. This would be the case, for example, of a business between the firm and a director, such as a contract to perform renovations to the corporation's offices involving a major shareholder and the corporation.

Family or founder links are another kind of directors dependence. Instead, it is difficult to determine whether links to shareholders adversely affect the quality of the firm's corporate governance. In general, having shareholders on the board reduces the danger that professional management acts in its own interests and not those of the shareholders, which is good for the company. However, there are some circumstances in which connections to shareholders can have a negative effect on directors' independence. This can happen, for example, in case of links to private equity firms that used to, or currently, control the company; in case of cross-shareholdings (5% or over); in case of directors elected by a shareholder with key managerial positions, who has the control of the company through majority or near-majority voting power.

Board independence is threatened also when in case of board interlocks, i.e. when two senior executives from different companies sit on each other's boards; or in the case of a director who recently held a senior role at an audit firm that provides external or internal audit services to the company.

Finally, directors independence is affected when a company makes donations to charities or universities affiliated with a director, especially if these donations are considerable or when the director holds an executive role in the charity or university.

Why is directors independence so important for firms' corporate governance? Remembering that the Board of Directors has three basic functions: management (in the circumstances I have already discussed above), monitoring and services (such as networking, consulting, or other professional services). Independence is potentially relevant to all three board functions.

As for the management and services functions, board independence is important in order to ensure that the expertise and contact networks provided by directors to the firm are really offered in the best interest of the latter.

As for the monitoring function, instead, conventional wisdom considers board independence to be an important device for constraining agency costs. However, it is not clear whether independent directors really represent an effective constraint on self-interested actions by senior management, because there are some factors, such as the lack of time, that impede effective monitoring from the board. Moreover, outside directors are generally dependent upon management for information. Another problem is that collective actions often cause free-rider problems, because a director may assume that other directors will do the hard work of supervising the conduct of senior management. This will obviously lead to sub-optimal levels of monitoring. Therefore, before independent directors can become effective monitors of management, the firm should incur costs to remedy the information asymmetry between outsiders and insiders (Bainbridge, 2012, p. 89).

Although directors' independence is important to ensure the goodness of firm corporate governance, insider board representation should not be considered as something negative in absolute terms. In fact, such kind of board representation may provide better information into adverse outcomes for the firm, which were beyond management's control and for which senior management should not be held accountable before the Board of Directors. In such cases, insider representation on the board provides a credible source of information for an accurate assessment of managerial performance, and, more importantly, creates a strong bond between Board of Directors and top management (Klein, 1998).

CEO Duality

Finally, there is still another important topic to address when dealing with Board of Directors, that is the issue of separating the titles of Chief Executive Officer (CEO) and Chairman of the Board of Directors. This issue has been largely investigated by academics, so much so that it can be considered one of the most researched topics in corporate governance.

The term “CEO Duality”, in particular, refers to the rather common practice of conferring to the same person both the title of Chief Operating Officer and the title of Chairman of the Board of Directors. Finkelstein & D'Aveni (1994) refer to this practice as “double-edge sword” because of the trade-off arising between the unity of command granted by duality and the independent monitoring granted by a separate board chair.

Proponents of the independent structure tend to base their arguments on the assumption that a separation of the titles would improve the board’s ability to fulfill its monitoring function, as well as improve firm performance.

Rechner and Dalton (1991), for example, examined a sample of 250 firms (randomly selected from the *Fortune* 500) over the 6-year period 1978-1983. In particular, after identifying companies that experienced no change in the governance structure over the period under analysis, the final sample was made of 141 firms, 21.3% of which with separate titles, while the remaining 78.7% with one individual holding both titles². As for the dependent variable, ROE, ROI, and profit margin were used as alternative measures of firm performance³. The authors found that firms with separate titles consistently outperformed firms with combined titles. These results were also found by Pi and Timme (1993) who analyzed a sample of banks from 1987 to 1990 (25% with separated titles and 75% with combined titles), and found that, after controlling for firm size and other variables, that performance was better for firms with separated titles.

² Data on board members and senior management were derived from *Standard and Poor's Register of Corporations, Directors, and Executives*.

³ All performance data were derived from COMPUSTAT sources and *Standard and Poor's Stock Reports*.

Baliga et al. (1996) analyzed a sample of 181 industrial companies over the period 1986 to 1991. Their final sample was made of 12 firms having a pure nonduality managerial structure (i.e. having a separate CEO and Chairman of the Board for all years); 58 firms having a partial nonduality (i.e. having a separate CEO and Chairman of the Board for one or more (but not all) years); 111 firm having a pure duality structure (if the positions of Chairman of the Board and CEO were held by the same individual for all years). At the same time, Return on Equity, Return on Total Assets, Operating Cash Flow/Total Assets, and Operating Cash Flow/Sales were used as measures of firm performance.

The authors, however, didn't find significant differences in the longer-term firm performance between duality and nonduality structure firms, and concluded that nonduality should not be considered the panacea to firm performance problem.

Other authors tried to challenge the conventional wisdom that the separation of the titles of CEO and Chairman of the Board leads to superior firm performance. According to Brickley et al. (1997; 2000), for example, reformers have overlooked important costs connected to the separation of titles, so that it is not theoretically obvious which leadership structure is best. In particular, the authors believe that the frequently-cited statistics on the frequency of separate titles overstate the incidence of firms with fundamentally different leadership structures. Rather, they largely reflect cross-sectional differences in the timing of CEO successions (Brickley, Coles, & Jarrell, 1997).

The authors, therefore, claimed that for each firm the optimal structure is likely to vary according to the economic circumstances facing the firm.

Their sample was made up of firms from the 1989 *Forbes Survey of Executive Compensation*, which contains information about the CEOs of 737 firms for the 1988 fiscal year. Moreover, the authors consulted the Dunn and Bradstreet's, *Reference Book of Corporate Management*, to obtain the exact title of each CEO in the Forbes survey at the end of 1988.

In the final sample, for over 80% of the firms, the same person held both the CEO and the Chairman title, about 5% did not have a Chairman, while the remaining 14% showed a separation of the titles. Moreover, 76 out of the 93 sample firms with separate chairs had Chairmen who were either former CEOs, founders, or other top

officers of the company. Only 17 firms had independent chairmen (i.e. chairmen who were neither current or former employees of the company). This means that almost no major firm in the U.S. in 1988 had an independent outsider as chairman. At the same time, the authors found that a significant number of firms used the titles of Chairman and CEO as part of their succession plans. This is a common practice among firms, which is typically referred to as “passing the baton”.

Brickely et al. observed that firms with separate titles had younger CEOs with less tenure, ownership, and lower compensation levels compared to those holding also the Chairman title. More precisely, the authors found that CEOs who were not also holding the title of Chairman of the Board had a mean tenure of 4.2 years, compared to 7.3 years of CEOs holding also the Chairman title plus an operating title and to 10.4 years of CEOs holding the Chairman title but any operating title. These results are quite consistent with the pass-the-baton pattern of CEO succession mentioned above, and suggest that firms with no separation of the titles are at a transition stage. If the power that comes with combined titles is granted as a reward for sustained high performance, not splitting the titles may actually be beneficial to the company, as it may be used as an incentive for new CEOs. For these companies, therefore, requiring a separation of the titles implies forcing them to alter this basic incentive system.

In conclusion, Brickley’s study found that, at least in the USA, achieving combined titles is the equilibrium and that separate titles signify normal succession periods or extraordinary, transitory events. This widespread practice of splitting the titles, instead, is efficient and generally consistent with shareholders' interests for the typical large U.S. company.

1.4.4 The role of institutional investors

Institutional Shareholders Activism

Members of the board of Directors are not the only people with responsibility for ensuring effective corporate governance. Shareholders, particularly institutional investors, also play a very important role (Solomon, 2007, p. 89).

Institutional investors, such as banks, insurance companies, pension funds, mutual funds, and other large institutions, are entities which pool money to purchase

securities, properties, and other investment assets, or originate loans. Historically major institutional investors are autonomous pension funds, insurance companies and mutual funds, while other forms of institutional investors such as sovereign wealth funds, hedge funds and private equity represent only a smaller share of the industry (OECD, 2011).

In recent years, institutional investors have started to gain increasing importance, especially because they are growing more and more large and influential. According to OECD, in fact, institutional ownership of publicly listed company has dramatically increased during the last decade. In the United Kingdom, for example, only 10% of all public equity is currently held by physical persons, and new institutions are gaining increasing reputation alongside the more traditional institutional investors (OECD, 2011).

The role of institutional shareholders in corporate governance had already received significant attention in the Cadbury Report (1992), which reported:

“Given the weight of their votes, the way in which institutional shareholders use their power to influence the standards of corporate governance is of fundamental importance. Their readiness to do this turns on the degree to which they see it as their responsibility as owners, and in the interest of those whose money they are investing, to bring about changes in companies when necessary, rather than selling their shares”.

Institutional shareholders, therefore, are now encouraged to play an active role in the companies they manage. This activism, in particular, can take different forms, and must be regarded as an important governance mechanism.

First, because institutional investors are expected to be highly skilled and well-resourced professionals, the hope is that their presence in the boards of underperforming companies will promote best-practices implementation, especially with regard to board structure and composition.

At the same time, institutional investors are expected to play an important role in preventing management from adopting decisions that could be detrimental to shareholders, because institutional investors provide active monitoring that is

difficult for smaller, more passive or less-informed investors (Almazan, Hartzell, & Starks, 2005).

Agrawal and Knoeber (1996), for example, emphasized that the involvement of institutional investors can have a positive effect on corporate financial performance. In this study, Agrawal and Knoeber analyzed a sample of nearly 400 firms for which the following variables were measured: insider shareholding, institutional shareholding, shareholding of large block-holders, representation of outsiders on the board of directors, use of debt, use of external labor market for managers, and takeover activity. The aim of this research was to examine the effects of this broad set of control mechanisms on firm performance. More precisely, the objective of study was twofold. By one side, authors wanted to find evidence of interdependence among these control mechanisms; by the other side they wanted to examine the empirical relationship between control mechanisms and firm performance. What the authors found is that concentrated shareholdings by institutions can increase managerial monitoring and, consequently, improve firm performance.

At the same time, Almazan, Hartzell and Starks, (2005, 2014) examined the relationship between institutional monitoring and executives compensation. The objective of this study was to verify whether institutions' influence on managers' level of compensation was enhanced when the cost of monitoring was lower.

The authors developed a stylized model of a firm owned by three classes of shareholders with different monitoring styles: the first two classes are potential monitoring shareholders (institutions) who can assess managerial performance at a different cost, while the third class consists of other shareholders (individuals) who cannot monitor, because monitoring costs would be prohibitive for them.

At the same time, with regard to monitoring shareholders, the authors suggested that costs of monitoring could vary among institutions, as these latter tend to differ in many aspects, including the skills of their employees and the amount of resources or incentives required to gather information. As a result, institutional investors were divided into two groups: potentially active institutional investors and potentially passive institutional investors. Potentially active investors include institutions with more skilled employees, more likely to collect information, facing less regulatory and legal restrictions on their investments, and having less potential for business

relations with the corporation. Institutions responding to these requirements typically are investment advisors and investment companies. Potentially passive investors, on the other hand, consists of the bank trust department and insurance companies. Obviously, monitoring costs were expected to be lower for potentially active investors.

Moreover, according to the model developed by the authors, there are also some firm-specific costs of monitoring, which basically consist in the costs of gathering information about a specific firm. These firm-specific costs, particularly, can be estimated by considering the firms' stock price liquidity, which can proxy for the information available for a firm.

The sample was made of 1,914 firms included in the Standard & Poor's ExecuComp⁴ database over the 1992 through 1997 time period. For each firm, details concerning executive compensation packages (including salary, bonus, long-term incentive plan payouts, stock and option grants and similar compensation) were retrieved.

Almazan, Hartzell and Starks found: i) that active institutions (investment advisors and investment companies) actually face lower costs of monitoring than passive institutions (banks and insurance companies); ii) that the level of executive compensation is decreasing in the concentration of both types of institutional investors' ownership; iii) that institutions' monitoring is attenuated when the firm's stock price is less liquid, which can be interpreted as an indication of an important firm-specific cost of monitoring.

The study of Almazan, Hartzell and Starks supports the common view that institutional investors are concerned with the economics of their commitment to investors. As a matter of fact, institutional investors not only care about the returns (generated through an improvement in corporate governance practices and careful monitoring) from the companies in which they have invested, but they also care about the costs of such activism. Engagement, in fact, is expensive and must be matched against potential revenues. However, because the costs of monitoring are significant, while the benefits are shared with all the other shareholders, a free

⁴ This database covers firms from the S&P 500 Index, from the S&P Midcap Index, and from the S&P Smallcap Index.

riding problem arises, possibly leading to a subsequent suboptimal monitoring by institutional investors (OECD, 2011).

Institutional ownership can also have positive effects on financial reporting practices. Rajgopal and Venkatachalam (1997) and Shang (2003) already suggested that institutional ownership leads to more conservative accounting practices as evidenced by its negative association with the use of discretionary accruals. Burns, Kedia, and Lipson (2005) also found that firms' financial reporting practices may be influenced by investment styles of institutional investors. In particular, if investment monitoring places emphasis on short-term performance, firms may be tempted to opt for less easily monitored practices, which could potentially result in a restatement. Therefore, it is plausible that institutions with short investment horizons degrade the quality of financial information, with negative effects on the firm's access to capital and future performance.

There is also another important form of activism (apart from monitoring) from institutional shareholders, i.e. the possibility to submit issues for subsequent presentation at the annual general meeting. Shareholders' proposal resolutions, particularly, can be an effective instrument for institutional shareholders to pursue their agendas, as they provide a formal mechanism through which concerns about corporate governance and corporate performance can be raised. Obviously, sound proposals will be voted.

Gillan and Stark (2000) analyzed data on shareholder activism, consisting of 2042 shareholder proposals submitted at 452 companies from 1987 to 1994. All of these proposals were related to the governance of the corporation. The authors suggested two measures of the effectiveness of this shareholder activism: i) the voting outcomes on these proposals; ii) and the stock market reaction to these same proposals. Evidence suggested that both measures of effectiveness depend on the issues addressed by the proposals as well as on the identity of the proposal sponsor. As a matter of fact, proposals sponsored by active individual investors obtain fewer votes and are associated with a slight positive impact on stock prices, while proposals from active institutional investors or coordinated groups of investors receive significantly more votes and appear to have some small but measurable negative impact on stock prices. This may be due to the belief that the appearance

of the proposal is the signal of the management's unwillingness to negotiate with such investors.

It may be useful to remember that proposals that have been supported through a high number of votes can be employed by their sponsors in negotiations with company management. However, shareholders' proposals are advisory only, which means that, even if they receive the majority of the vote, management is not obliged to take action. The use of these proposals in the direct negotiation process may be reflected in the increased number of negotiated removals of such proposals, which can be considered as a sign of the influence that such active investors have. Therefore, the removal of a proposal means that the sponsor (the proposing institutional investors) has successfully bargained against senior management and succeeded to have senior management accepting the content of such proposal before the vote at the annual general meeting.

Institutional Investors Short-termism

Another problem connected to institutional investors (besides the concern for low levels of engagement and activism) is that they are not actually the shareholders. The real shareholders, in fact, are the clients of the institutional investment organizations. For example, in the case of a pension fund investing a large stake in a company, if the pension fund manager does not ensure that the various investee companies pursue shareholder wealth maximization, pension payments will not be maximized (Solomon, 2007, p. 93). Therefore, from an agency theory perspective there is an added agency problem, because the clients of the institutional organizations not only have to worry about the conduct of investee company management but they also have to worry about the conduct of the institutional organization management.

This is typical of many countries, especially Anglo-Saxon countries, where ownership is no longer characterized by a straight and uncompromised relationship between the company and its shareholders. The investment chain, indeed, is often long and complex, with numerous intermediaries that stand between the ultimate beneficiary and the company (OECD, 2015).

One of the consequences arising from this complex ownership structure is that there tends to be an emphasis on short-termism in investment. As a matter of fact, it is known that institutional investors are interested in short-term profit maximization in order to make their returns look as healthy as possible in the short run (Solomon, 2007, p. 93). Institutional investors, therefore, could lead corporate managers to make decisions aimed at boosting short-term earnings at the expense of long-run value, which can be detrimental to long-term company survival. This concept is known as myopic institution theory, and suggests that institutional shareholders are more short-sighted in their investment decisions than individual investors. Nevertheless, studies conducted by several researchers have led to conflicting conclusions, with the results that there is still no clear answer to this matter.

One of the earliest studies on the myopic institution theory is that of Hansen and Hill (1991) who examined this popular myth in high-technology industries. The authors examined the relationship between R&D expenditures and institutional ownership over a 10-year period for 129 firms of four research-intensive industries, testing whether those firms were more likely to alter their critical R&D investments in response to the short-term profit pressures by large institutional shareholders. However, authors found that, contrary to the view that institutional shareholdings has damaging effect on R&D spending, higher levels of institutional ownership may be associated with greater R&D expenditures.

The results of this research were confirmed by a later research by Wahal and McConnel (2000), who studied corporate expenditures for property, plant, equipment, and research and development for over 2500 US firms from 1988 to 1994. Again, no support was found for the contention that institutional investors cause corporate managers to behave myopically. Indeed, the study found positive relation between industry-adjusted expenditures for property, plant and equipment, R&D and the fraction of shares owned by institutional investors.

In another study, Graves and Waddock (1994) studied the relationship between institutional ownership and firms' corporate social performance (CSP), in order to test whether institutional investors are more inclined to invest in companies with higher CSP. Because investments in corporate social performance tend to be long-term, the institutional owner's time horizon and the time needed to realize the

benefits of such a social performance may be divergent. Notwithstanding, because institutional shareholdings has increased dramatically since the mid-1980s, institutional investors can no longer divest easily from non-performing companies. Thus these investors have become longer-term holders by necessity, and many have become actively involved in the governance of companies that they own. For these reasons, authors concluded that the argument for a short time horizon among institutional investors is no longer supported by evidence.

Similar results were found in later studies. According to these studies, once “locked in” institutional investors find it difficult and costly to sell their holdings for fear of selling at a discount or to convey information to the markets (Faccio & Lasfer, 2000).

Bushee (1999), instead, studied whether institutional investors exhibit preferences for expected near-term earnings at the expense of expected long-run value and whether such preferences have any implications for the relative weighting of these components in firms’ stock prices. Evidences of such preferences among institutional investors, in fact, would support the claim that managers feel pressure from institutions to myopically maximize near-term earnings. Using the Ohlson model (1995), the author separated firm value into three different components: book value, expected near-term earnings, and expected long-term (terminal) value. Then the author tested whether institutional investors prefer firms which are expected to realize more short-term earnings instead of long-term earnings. The results indicate that institutions as a whole have weak preferences for short-term earnings, providing limited evidence in support of institutional investor myopia. However, once institutional investors were disaggregated into groups based on their incentives to prefer short-term earnings, significant heterogeneity in institutional preferences were found. In particular, institutions that face the strictest fiduciary standards (banks) and have the shortest investment horizons (transient institutions) exhibit stronger preferences for short-term earnings. Thus, managers of firms with high levels of ownership by banks and transient institutions are more likely to face pressures from institutional investors to make myopic decisions to please their investor bases.

To summarize the issues discussed in this section, institutional investors have a responsibility as majority owners of companies to influence company management. Therefore, it is highly recommended that institutional shareholders take an active interest in the companies in which they have investment, avoiding to remain passive observers.

1.4.5 Corporate Governance and Corporate Financing Strategy

Corporate Governance, as already mentioned, can have a big impact on various aspect of firms' management, including decisions on capital structure. In particular, the issue of how capital structure, i.e. the choice of financial leverage by companies, can be affected by corporate governance mechanisms is one of the most important and debated topics in corporate governance literature. This is due to the fact that the inclusion of debt in capital structure may affect the performance and the market value of the firm (Yaseen & Al-Armaneh, 2015).

An important contribution to literature on corporate governance and capital structure was given by Williamson (1987). In his article, debt and equity were not treated as alternative financial instruments, but rather as alternative governance structure.

Williamson argues that I argue that investment attributes of different projects need to be distinguished. More precisely, the author's approach is to distinguish the various firm's projects on the basis of their asset-specificity characteristics. Then, the argument is further simplified by assuming that there are only two forms of financing and that that projects must be financed entirely by debt or by equity but not both.

Debt is a governance form that works mainly out of rules: i) interest payments have to be made at regular intervals, ii) the principal will be repaid at the loan expiration date, iii) in the event of default, the debt-holders will exercise pre-emptive claims against the assets in question. If everything goes well, interest and principal will be paid on schedule, if not failure to make scheduled payments thus results in liquidation. However, debt-holders will benefit from liquidation only if the assets in question are redeployable, which depends on the degree of their asset-specify. A higher level of asset-specificity implies that the asset will be hardly redeployed.

Knowing that the firm can use borrowed funds to finance specialized investments, the firm might be preventively forced to sacrifice some of the specialized investment features in favor of greater redeployability. As a result, production costs may increase or quality decrease. Instead, the firm can resort to equity, which is more forgiving than debt, as efforts are made to work things out when things go bad.

According to Williamson, therefore, debt is a governance structure that is well-suited to projects where the assets are highly redeployable, whereas equity is a governance structure that allows discretion and is used for projects where assets are less redeployable.

Williamson's approach, was developed under the transaction-cost framework, but the impact of corporate governance on firms' capital structure has been analyzed much more extensively under the agency theory framework. Under this framework, a higher equity contribution to corporate financing changes the agency relationship context in the corporation, therefore the strength of the decisions sourced by the equity owners.

The agency framework also helps explain how governance characteristics can affect the level of indebtedness of a firm. According to Jensen and Meckling (1976), because debt limits managerial flexibility, managers tend to prefer less leverage than it is optimal to the corporation. This concept was further examined by Jensen (1986) who argues that, when firms have internal resources that exceed positive net present value investment opportunities, the presence of debt in the firm's capital structure forces managers to pay out funds that might otherwise have been invested in negative net present value projects. Management, in fact, has an incentive to undertake projects that expand the scale of the firm because they are rewarded for doing that, even if this is detrimental to shareholders' interests. In this case, debt represents an effective constraint to managerial discretion, limiting a phenomenon which has been labeled the 'overinvestment problem'. Fundamentally, the overinvestment problem arises because of a separation between corporate equity ownership and management. In Jensen's analysis, in fact, managers have an incentive to increase the size of the firm at shareholders' expense. However, if they

are committed to pay interests at regular intervals to service debt, they are left with less resources to be invested in wasteful projects.

Notwithstanding, for firms with growth opportunities debt could negatively affect the value of the firm. According to Myers (1977), 'too much' debt may induce managers to forego positive net present value projects, because of their commitment to repay debt. In case, the problem is the opposite, and is known as 'underinvestment problem'.

A firm's level of debt, therefore, can be considered as an effective corporate governance mechanism, because creditors' monitoring may discourage managers from accepting excessive debt financing for highly risky investments. As a matter of fact, debt implies a commitment to a fixed stream of future repayments, which prevents managers from undertaking risky projects that benefit themselves personally but impact shareholders unfavorably.

At the same time, there are two other different ways through which the level of leverage adopted by a firm may reduce the expected benefits of control (Harris & Raviv, 1988): 1) debt increases the probability of bankruptcy; 2) debt often imposes restrictive covenants that will inevitably limit the benefits of control. In particular, with respect to bankruptcy, it should be remembered that, although the manager is not personally liable for his corporation's debts, default would force him to search for re-employment, just when his reputation had been crippled (Jensen, 1986). This means that managers should pay attention not to endanger the financial stability of the company they work for, by failing to meet debt obligations.

As already stressed by Jensen, the disciplining role of debt within a firm is effective only in the context of agency problems that arise in corporations with a clear separation of ownership and control (i.e. between shareholders and managers) (McConnel & Servaes, 1990). This means that, when ownership is highly concentrated, as it is the case of Continental Europe, the role of debt as an effective control mechanisms can be considerably reduced. In this case, agency problems may still arise, but they involve the controlling and the minority shareholders, instead of shareholders and managers. The controlling shareholders, in fact, could increase the debt ratio as a mechanism of expropriation of minority shareholders, because the choice of debt allows the controlling shareholder to control more

financial resources without diluting his control stake (Faccio & Lang, Debt and Corporate Governance, 2001).

In both cases, whether ownership is highly concentrated, as it is in the case of companies in Continental Europe, or it is sufficiently diffuse, as in the case of companies in the United States and United Kingdom, the choice of the level of leverage within a firm (and so of the level of equity) depends on corporate governance arrangements, especially their shareholding patterns (ownership concentration) (Kumar, 2015).

1.5 Corporate Governance after the crisis: where are we going?

According to OECD, The purpose of corporate governance is to “*help build an environment of trust, transparency and accountability necessary for fostering long-term investment, financial stability and business integrity, thereby supporting stronger growth and more inclusive societies*” (OECD, 2015).

This statement is powerful, because it broadens the perspective on corporate governance, by extending the paradigm from a narrow agency theory perspective to a stakeholder theory perspective.

Nowadays, growing global concerns, such as the fear of a global environmental disaster, terrorism and nuclear war, have shifted people’s attention more and more towards environmental and social issues (Solomon, 2007, p. 187).

This growing concern for global risks has been researched extensively by several famous authors on modernity, who coined the expression of “risk society” to refer to the contemporary world. According to the British sociologist Anthony Giddens, in particular, a risk society is “*a society increasingly preoccupied with the future (and also with safety)*”, whereas the German sociologist Ulrich Beck defines it as “*a systematic way of dealing with hazards and insecurities induced and introduced by modernisation itself*”.

Indeed, the whole world is on the knife’s edge, and societies all over the world are trying to find solutions to avoid to fall off the cliff. This is why policies and corporate governance initiatives, today, are increasingly focusing on the importance of broadening the corporate governance agenda to incorporate a more inclusive

approach. The main implication of this modern tendency is that corporate governance mechanisms that focus exclusively on the needs of shareholders appear to be insufficient. Hence the need for a corporate governance framework that takes into account also the needs and requirements of all corporate stakeholders.

In this context, the notion of 'Corporate Social Responsibility' (CSR), is considered to be particularly relevant. This expression, in particular, refers to initiatives carried out by corporations in order to assess and take responsibility for the company's effects on the environmental and social wellbeing. These efforts involve incurring short-term costs that do not provide an immediate financial benefit to the company, but instead promote positive social and environmental change.

But are companies engaged in corporate social responsibility activities also performing better than those who do not? In the academic literature there are a number of studies on this subject, some of which found a positive relationship between corporate social responsibility and corporate financial performance.

Moskowitz (1972), for example, found that the share returns of a small sample, comprising 14 US listed companies, which he deemed being socially responsible had increased at a higher rate than major market indices.

At the same time, Bowman and Haire (1975), analyzed the annual reports of 82 food-processing firms listed in the 1973 Moody's Industrial Manual. The authors, in particular, took the percentage of content in sample firms' annual reports pertaining to corporate responsibilities and activities as a measure of social involvement. The authors, then, formed three classes of firms on the basis of the Corporate Social Responsibility Performance, and tested whether there were significant group mean differences in financial performance (measured through ROE). They found that the group with the medium CSR performance was the best in terms of ROE, whereas the group with the best CSR performance was average in terms of ROE, but still better than the group with the worst CSR performance. Consequently, Bownan and Haire interpreted these results as a support for the assumption of an inverted U-shaped curve relation between financial performance and corporate social performance.

One of the reasons why corporate financial performance may be positively related to corporate social performance could be that managers who act in a socially responsible manner are more likely to possess the skills to run a healthy business, improving its financial performance and making it an attractive investment (Solomon, 2007, p. 192). However, some authors have argued that a positive link may be found simply because companies with a better financial performance may also be better able to afford to act in a socially responsible manner (McGuire, Sundgren, & Schneeweiss, 1988). This latter assumption implies that it is a good financial performance that causes a subsequent good corporate social performance, not the other way around.

Other studies on this subject, instead, found a negative relationship between corporate social responsibility and corporate financial performance. Alexander and Buchholz (1978), (Prowse, 1992) for example, examined the relationship between social responsibility and stock market performance of corporations in the U.S. for the period 1970-1974. The authors calculated differential returns⁵ and risk measures for the companies included in the sample for the five-year sample period 1970-1974 and a three-year subperiod 1970-1973. They found that few securities had differential returns different from zero, and that there was no significant effect of corporate social responsibility on stock market performance. Differential returns were also ranked in descending order and then rank order correlations were calculated between survey rank and differential return rank. Again, the correlations indicated a low insignificant relationship between risk-adjusted performance and the degree of social responsibility.

An explanation for the existence of a negative relationship between financial performance and corporate social performance could be that socially responsible companies may be at a competitive disadvantage due to the added expense incurred by socially responsible behavior (Vance, 1975) .

Finally, numerous empirical studies that have found no evidence of a positive or a negative link between financial performance and corporate social performance.

⁵ Differential returns are a risk-adjusted performance measure. More specifically, they can be considered as a risk-adjusted excess return.

These results could be interpreted as positive evidence by those supporting corporate social responsibility. In fact, if acting in a socially responsible manner is costless in terms of financial performance, then even solely from a pure ethics perspective it is better to pursue social responsibility (Solomon, 2007, p. 193).

One of the problems in comparing the results of large number of studies, however, is that researchers have adopted a wide range of different techniques in their studies. Moreover, corporate social performance is difficult to measure, and there is no perfect technique or methodology that can be applied. Hence the limitations in empirical research. It is nonetheless possible to conclude that the weight of evidence in the literature seems to point more to a positive relationship between corporate social responsibility and corporate financial performance (Griffin & Mahon, 1997).

1.6 Objective of this study

The basis for this paper is Mantovani and Castellan (2015), who studied the relationships between corporate governance characteristics, and firm's performance, credit allocation and merit of credit for a set of ten countries. The aim of the authors was to find evidences of the impact of corporate governance characteristics on a firm's ability to achieve superior economic results and an easier access to financial resources.

First of all, the authors wanted to investigate whether there were significant differences in terms of corporate governance practices and mechanisms for a set of ten different European countries, in order to identify possible congruencies between corporate governance characteristics, firm's performance (measured in terms of ROI, return on investment), intensity of indebtedness (measured as the ratio between debt and the operating revenues, in terms of DEBT/OPRE) and the merit of credit (measured through the Integrated Rating methodology) at country level.

The results of the t-tests of differences for all of the selected indicators for corporate governance indicators, in particular, confirmed the hypothesis of the existence of substantial differences in corporate governance characteristics among the ten countries included in the sample. Nevertheless, when the authors ranked these Countries according to the quality of their corporate governance, few congruencies

were found between the goodness of corporate governance and firms' performance, level of indebtedness and the merit of credit. This means that not always the countries with the best corporate governance characteristics are not always also even those that shows the best performance, the highest level of debt , and the highest merit of credit.

At the same time, the same relationship was investigated at individual firm level, by regressing the corporate governance characteristics on firm's performance, level of indebtedness and the merit of credit. In all the three cases, no relevant relationship was observed, apart from that (but not particularly strong) between corporate between the corporate governance characteristics and the merit of credit (even if this is not particularly strong).

The authors themselves called for further investigations. In particular, the objective of this thesis is to give an answer to the following research hypotheses:

HP1: *There are stronger significant relationships between ownership and corporate governance characteristics between the different countries included in the 10-Countries sample.*

This is an important topic to be investigated, because, should evidence confirm suggestion that no homogeneity is found in corporate governance mechanisms and practices at country level, then the introduction of a uniform body of standards aimed at encouraging harmonization between EU countries (e.g. Basel Regulation and the International Financial Reporting Standards (IFRS)), could not be an appropriate solution.

Moreover, we are interested in studying whether there are congruencies between corporate governance characteristics and firm performance for each of the countries included in our sample. Therefore, we formulate the second research hypothesis:

HP2: *The Countries with better Corporate Governance solutions are also those which achieve better performances with respect to countries with the worsted Corporate Governance system.*

Should evidence support this hypothesis, then we can claim that tuning Corporate Governance through financing drivers is indeed a business decision affecting firm

performance. In the previous sections, evidences of the existence of a positive relationship between corporate governance and firms' performance, particularly, through several studies in business literature (Weisbach, 1988; Rosenstein & Wyatt, 1990; Byrd & Hickman, 1992; Brickly et al., 1994; Rajan & Zingales, 1998; Williams, 2000; Drobotz et al., 2003; Hossain et al., 2000; Gemill & Thomas, 2004). This analysis, therefore, aims to confirm this belief that a better corporate governance will result in a higher firm value and a more profitable firm performance.

At the same time, we are interested in investigating the relationship between Corporate Governance, firm performance, banks' allowances, and the merit of credit at individual firm level. Thus, we introduce the third hypothesis of this research:

***HP3:** There is a significant relationship between the characteristics of corporate governance of a firm and its performance, bank's allowances decisions, and its merit of credit.*

Finally, since an extensive literature supporting the belief that corporate governance influences a firm's level of indebtedness exists, we are interested in testing whether this belief holds for the companies included in our sample.

***HP4:** There is a significant relationship between the characteristics of corporate governance and the level of leverage of a firm.*

This being the natural consequence of any of the possible evidences on HP3. The higher the merit of credit which is driven by the corporate performance (as possible consequence of the adopted corporate governance) the higher should be bank's allowances. We all know that credit crunches might bias this relationship since macroeconomic trends might impact on it. In the paper, this is analyzed by comparing the overall Country evidence with the one sourcing at Corporate level.

Chapter 2

The purpose of this chapter is to highlight the differences in corporate governance practices and mechanisms in countries from different parts of the world.

In particular, the first part of the chapter is devoted to present the two best-known models of corporate governance: the insider corporate governance system and the outsider corporate governance system.

The second part of the chapter, instead, is aimed to analyze the differences in corporate governance characteristics for a set of ten countries: Czech Republic, Germany, Spain, France, Hungary, Italy, Poland, Slovakia, the United Kingdom, and the United States.

2.1 Categorizing corporate governance systems: the insider/outsider model

Attempts have been made to categorize countries' corporate governance systems, even if this can lead to extreme oversimplification. However, some broad categorization of corporate governance systems is needed, particularly for research studies on this subjects.

One well-known and generally accepted means of categorizing corporate governance systems is the 'insider/outsider' model, discussed by Franks and Mayer (1994) and Short et al. (1998). According to this model, some governance systems such as those of the United States and the United Kingdom, can be depicted as an outsider systems, as they are characterized by a large number of public corporations, widely dispersed ownership (though with growing concentrations of institutional shareholdings), and well-developed takeover markets (Franks & Mayer, 1994). By contrast, countries like Germany and France can be depicted as insider systems, in which the founding families, banks, or other companies exert a strong control, at the expense of outside (often minority) shareholders (Franks & Mayer, 1994).

Obviously, any corporate governance system perfectly falls into a category or another. Indeed, most systems of corporate governance fall somewhere in between these two, sharing some characteristics of both extremes.

2.1.1 Insider-dominated systems

An insider-dominated system of corporate governance is one in which publicly listed companies are owned and controlled by a small number of major shareholders. Majority shareholders, in particular, can be members of the companies' founding families, lending banks, other companies (through cross-shareholdings and pyramidal ownership structures) or the government.

Insider systems are also referred to as 'relationship-based systems', because they are characterized by the existence of a close relationships between companies and their controlling shareholders. As a consequence, these systems appear to be less affected by agency problems, because it's easier to align the interests of management and shareholders. However, as a result of the low level of separation of ownership and control, there can be abuse of power by controlling shareholders, and minority shareholders may not be able to obtain information on the company's operations.

Many East Asian countries, particularly, show an insider-dominated corporate governance system, where the weak legal protection of minority shareholders allowed majority shareholders to increase their power (Prowse, 1992; Rajan and Zingales, 1998; Claessens et al., 2000).

2.1.2 Outsider-dominated systems

Outsider-dominated systems of corporate governance are characterized by a strict separation between ownership and control, as outlined by Berle and Means (1932). The UK and the USA have traditionally been considered outsider-dominated systems, where the outsiders tend to be predominantly financial institutions, but also smaller individual shareholders.

According to this model, although companies are controlled directly by their managers, they are also controlled indirectly by the outsiders. As a matter of fact, shareholders have voting rights that provide them with some level of control. The problem with large shareholders, as already mentioned in the previous chapter, is that they tend to be short-termist and rather passive. Nevertheless, in recent years, we are witnessing to the increase of shareholders' activism and engagement,

especially by institutional investors. In the UK and the United States, in fact, institutional shareholder are becoming more and more like insiders, as they are gaining the largest proportion of shares in companies and are exacting strong influence on company management, taking on the role of an insider majority shareholder (Solomon, 2007, p. 150).

2.1.3 Where do these differences come from?

A growing area of the finance literature devoted to international comparisons of corporate governance systems seeks to explain the factors that determine countries' corporate governance.

Shleifer and Vishny (1997) focused on the influence of countries' legal systems on corporate governance. In particular, the authors claimed that a high degree of legal investor protection was necessary to persuade investors to invest their money into companies, because otherwise they incur the risk of being expropriated by the company's management. The authors found that legal systems characterized by low levels of investor protection were found to be associated with poorly developed capital markets.

In absence of a good legal investor protection, the only way to gain power is by being significantly large. Moreover, according to Shleifer and Vishny large shareholders exercise control via voting rights, which means that their level of control is determined by legal protection of these rights. However this consideration no longer applies, as engagement has usurped voting as a primary form of shareholder activism (Solomon, 2007, p. 152).

The most influential studies in the area of international corporate governance are those initiated by the works of La Porta et al. (1997, 1998). These authors focused on the links between legal systems and corporate governance for a sample of 49 countries around the world. In particular, they argued that the origin of a country's commercial/company law helps explain the country's law on creditor, shareholder and private property rights.

More precisely, there are three general legal traditions in the world. The French civil law legal system is known to have the lowest level of investor protection

whereas the English common law legal system affords the highest level of investor protection. The German and Scandinavian legal systems lie somewhere in between these two extremes.

In summary, countries with poor legal investor protection (such as Germany, France, Italy, Spain) tend to fall into the insider-dominated system of corporate governance, while countries with a good legal investor protection and a well-developed capital markets (such as the United Kingdom and the United States) tend to fall in the outsider-dominated system of corporate governance.

In the next sections, I am going to provide some case studies of corporate governance. In particular, the United Kingdom will be used as a case study for outsider-dominated governance systems, while Germany will serve as a case study for insider-dominated governance systems. I'll also present the case of Italy, which was traditionally classified among the insider-dominated systems, but which has some characteristics which made the country a stand-alone case in academic literature.

2.2 United Kingdom

2.2.1 The evolution on the British Governance System

UK is generally acknowledged as a world leader in corporate governance reform (Solomon, 2007, p. 45).

In particular, the first attempts to formalize corporate governance practices in the United Kingdom, was the publication of the Cadbury Report (1992), which covered three broad aspects of corporate governance: the board of directors, auditing, and shareholders (with a particular attention given to institutional shareholding).

A very important aspect of the Cadbury Report is the fact that it emphasized the importance of adopting an approach that encouraged compliance with a voluntary code of best practice (Solomon, 2007). This means that if a company does not comply with the best practices described in the Cadbury Report, then it should indicate the reasons to do so in its corporate governance annual report. This choice was not followed by all countries. The United States, for example, prefers a more regulated, rules-based environment.

Later, in 1995, a second corporate governance committee was created, with the aim of addressing the growing concern of directors' remuneration. It was at this time that the term 'fat cat' was coined to refer to directors who awarded themselves huge remuneration packages which bore little relation to firm performance. This led to the publication of the Greenbury Report, which reports comprehensive recommendations concerning the disclosure of directors' remuneration packages. The report, particularly, focused on the need to tie directors' remuneration to firm performance. This does not necessarily imply a reduction of directors' salaries, as the report itself recognized that offering high salaries was necessary to attract directors of adequate caliber.

In 1995 the Hampel committee was also set up. Its task was to review the implementation of the Cadbury and Greenbury committee recommendations. The committee reported in 1998 and, as with the earlier reports, it emphasized the important role played by institutional investors.

In 1998 the Combined Code drew together the recommendations of the Cadbury, Greenbury and Hampel reports. Later, in 1999, The Turnbull Committee was established with the aim to provide guidance on the implementation of the internal controls required in the Combined Code.

Additional recommendations followed the Higgs Review, in 2003. These recommendations were mainly directed to corporate governance practices regarding the board of directors. Most of them had already been included in the revised Combined Code, with the exception for the recommendation concerning the separation of the roles of CEO and Chairman of the Board. This practice, in fact, was amended so that it would be possible for the same person, after consultation with major shareholders, to hold both the titles.

2.2.2 Characteristics of the British Governance System

After this brief discussion about the evolution of corporate governance guidelines in the United Kingdom, I'll present in detail the characteristics of the Anglo-Saxon governance system.

As for the board of directors, the Cadbury Report recommended that there should be a clear division of responsibility at the top of the company, which in turn implies the separation of the titles of CEO and Chairman of the Board. The Higgs Report re-emphasized the importance of splitting the titles, but, as it was already mentioned above, it also introduced a change of provision, allowing company to entitle the same person with both charges with prior public justification. This does not happen in the United States, where the titles of CEO and Chairman of the Board are often held by the same person, and this is recognized as an usual practice.

Another important issue concerns the composition of the board of directors, specifically its combination of executive and non-executive directors. This stems from the fact that inside directors provide valuable information about the firm's activities, while outside directors may contribute both expertise and objectivity in evaluating the managers' decisions (Solomon, 2007, p. 68). The Cadbury Report, in particular, recommended that the board of directors should include a minimum of three non-executive directors, and that at least two of the minimum requirement of three non-executive directors should be independent.

After the Cadbury Report, The hamper Report and the Combined Code readdressed the issue of boards composition, but the situation remained substantially unchanged until the publication of the Higgs Report. In particular, the Higgs Report recommended that at least half of a company's board of directors should be independent non-executive directors. At the same time, the Higgs Report addressed the issue concerning the relationship between non-executive directors and institutional investors. More precisely, the report recommended that one or more non-executive directors should take direct responsibility for shareholders concerns and to attend regular meetings with the company's shareholders.

Finally, another question related to the functioning of the board of directors is the issue of executive remuneration. This is an important aspect to be considered because directors' pay should be established at a level that incentivizes management to pursue the interests of the shareholders.

As it was already mentioned, the issue of directors' remuneration was addressed by the Greenbury Committee, whose aim was to create a remuneration committee that

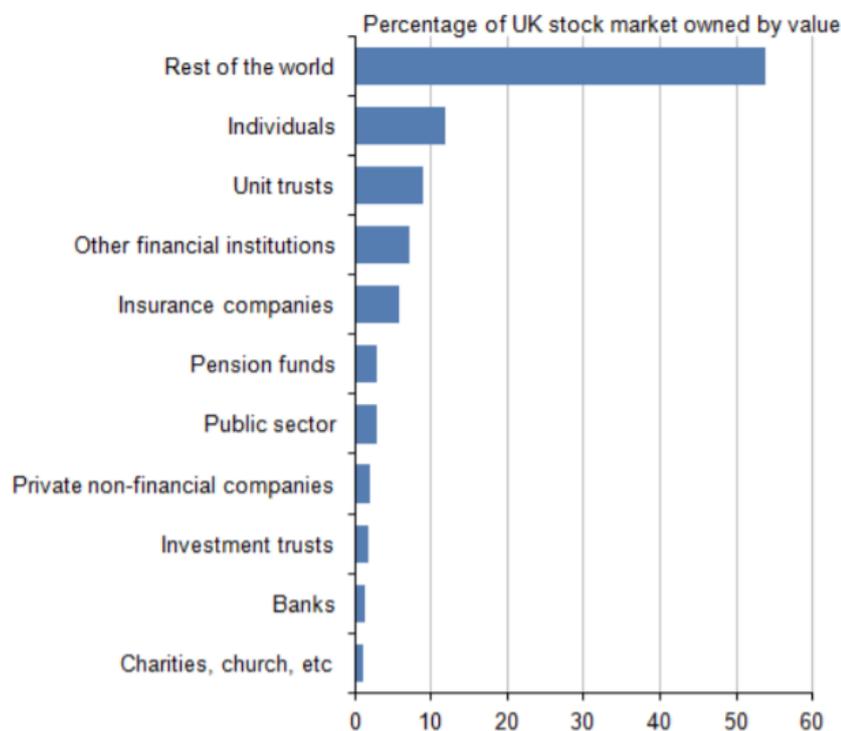
would determine directors’ pay packages able to attract and retain highly qualified directors. By one hand this was an initiative intended to improve transparency, by the other it was intended to prevent executive directors from designing their own pay packages.

To complete the discussion on corporate governance developments in the United Kingdom, it is necessary to describe also its patterns of share ownership.

The United Kingdom, in fact, has witnessed a significant change in ownership structure in the last 40 years, with institutional shareholders becoming more and more influential (Mallin, 2006).

According to the Office for National Statistics (2015), at the end of 2014, the largest sector was the rest of the world, with 54% of the total value of UK owned shares. Individuals owned the next largest proportion of shares with 12% of the total, higher than the 10% they held in 2010 and 2012 (Table 1).

Table 1: *Ownership of quoted shares in UK domiciled companies (at 31 December 2014)*



Source: Office for National Statistics

Table 2 shows the evolution of ownership of quoted shares in UK from 1998. As it is possible to notice, there has been a substantial increase of foreign investors ownership. In 1998, in fact, ownership of UK shares of the rest of the world was only the 30.7%, while in 2014 ownership of foreign investors achieved almost 54%.

Table 3: Ownership of UK shares (1998-2014)

	Per cent				£ billion			
	1998	2010	2012	2014	1998	2010	2012	2014
Rest of the world	30.7	43.4	53.6	53.8	460.9	760.9	862.4	928.6
Individuals	16.7	10.2	10.1	11.9	250.8	179.0	162.0	206.2
Unit trusts	2.0	8.8	9.5	9.0	30.1	153.8	152.0	155.2
Other financial institutions	2.7	12.3	6.6	7.1	40.4	215.0	105.6	123.0
Insurance companies	21.6	8.8	6.2	5.9	325.5	153.8	99.6	101.8
Pension funds	21.7	5.6	4.7	3.0	325.8	98.7	75.7	51.7
Public sector	0.1	3.1	2.7	2.9	1.4	54.4	44.0	50.2
Private non-financial companies	1.4	2.3	2.4	2.0	20.9	40.1	38.5	34.7
Investment trusts	1.3	2.1	1.7	1.8	19.2	37.5	27.9	31.1
Banks	0.6	2.5	1.9	1.4	8.4	44.3	30.3	24.3
Charities, church, etc	1.4	0.8	0.6	1.2	20.4	14.9	9.8	20.1
Total²	100.0	100.0	100.0	100.0	1,503.7	1,752.3	1,608.0	1,726.8

Table source: Office for National Statistics

In particular, as for the composition of the “rest of the world” category, Table 3 shows that the majority of investors are institutional investors. In particular, the dominant sectors are Unit Trusts (48.7% for North America and 23.7% in other countries), Other Financial Institutions (25.4% for North America and 26.8% in other countries), and Pension Funds (19.7% in North America and 9.6% in Other

Countries). For the Other Countries category, it is important also the contribution of the Public Sector (23.4%) and Banks (8.6%).

Table 4: *Rest of the world holdings of UK quoted shares*

	Per cent		£ billion	
	North America	Other RoW	North America	Other RoW
Unit trusts	49.7	23.7	211.1	119.4
Other financial institutions	25.4	26.8	107.8	135.0
Pension funds	19.7	9.6	83.7	48.6
Insurance companies	1.4	0.7	5.8	3.5
Individuals	1.3	1.3	5.4	6.7
Public Sector	0.9	23.4	3.9	118.1
Charities	0.8	0.1	3.2	0.4
Banks	0.6	8.6	2.7	43.4
Private non-financial companies	0.2	5.8	0.8	29.1
Investment trusts	0.0	0.0	0.0	0.0
Total¹	100.0	100.0	424.4	504.2

Table source: Office for National Statistics

Thus, to conclude, these data show that the presence of institutional shareholders in UK ownership structure has increased dramatically, so much so that they are gaining substantial power and influence. For this reason, it is important that shareholders of this kind are exhorted to be more activist in their approach to their investee companies and to be more proactive in intervening in underperforming companies (Mallin, 2006).

2.3 Germany

German Corporate Governance gained particular attention abroad, because the German system of Corporate Governance differs significantly from the predominant Anglo-American one (Wereder & Talaulicar, 2006).

To begin with, German Corporate Governance has been traditionally characterized by relationship-based, internal control mechanisms. On the contrary, the Anglo-American corporate governance system, is characterized by external control via the

market, which means that alignment of management and shareholders' interests is achieved predominantly by the market for corporate control. This system ensures that poorly performing companies become hostile takeover targets, which can lead to a consequent dismissal of company management (Weredr & Talaulicar, 2006); (Solomon, 2007, p. 167)). However, the market for corporate control requires a highly developed stock market and dispersed ownership, neither of which are a characteristics of the German system.

As far as concerns ownership concentration, ownership of German corporations is today highly concentrated in the hands of families and other companies (Franks, Mayer, & Wagner, 2006). At the same time, another common aspect of German ownership structure is the presence of the so-called 'hard-cores', i.e. specific patterns of cross-ownership linking large industrial firms, banks, and insurance companies (Amable, 2003). This structure, in particular, is aimed at preserving ownership stability and the capacity to implement long-term industrial strategies. This is why the notorious short-termism problem, blamed for constraining British industry, was less evident in Germany, where long-term relationships between companies and their providers of finance led to long-term investment (Solomon, 2007, p. 167).

As for the development of the German stock market, of the 3.7 million enterprises in Germany in 2012, just over 11,000 were public limited companies. These public limited companies accounted for roughly 18% of aggregate revenues and employ just under 9% of employees subject to social security contributions (Deutsche Bundesbank, 2014). In 2014, only 711 companies were publicly listed, with market capitalization of around €1,200 billion (Deutsche Bundesbank, 2014). In market capitalisation terms, this makes the German stock market the seventh largest worldwide and number three in Europe after the United Kingdom and France. However, Germany's equity market capitalization to gross domestic product (GDP) ratio is relatively inadequate for international standards.

One of the consequences of the limited possibility to resort to capital market-based financing is that the German system tend to be bank-centred. German companies, in fact, tend to have a higher debt to equity ratio compared to Anglo-Saxon

countries, and bank managers are frequently appointed to the supervisory boards of their borrowing companies (Wereder & Talaulicar, 2006).

Finally, another characteristic of the German corporate governance system is related to board characteristics.

As a matter of fact, German corporations are characterized by a two-tier (or dual board) structure which strictly separates the roles of management and monitoring. As a consequence of this strict separation, one person cannot be appointed simultaneously to the management and supervisory boards of the company (Wereder & Talaulicar, 2006). Moreover, in the case of multipersonal management boards, which are mandatory in stock corporations having more than 2,000 employees, all board members are considered on equal terms, which means that even the Chairman of the Board is considered a *primus inter pares*, not allowed to instruct other Board members (Wereder & Talaulicar, 2006). Finally, in Germany, the supervisory board is often codetermined, i.e. members of the supervisory board are elected not only by the company's shareholders, but also by its employees. More precisely, the supervisory board of stock corporations is generally composed of one-third employee representatives, while in enterprises having more than 2,000 employees half of the board members are elected by the workforce (Wereder & Talaulicar, 2006). However, the Chairman of the Supervisory Board must be representative of the shareholders.

2.4 Italy

The Italian system of Corporate Governance is characterized by two core elements: 1) the preponderance of internal controls; 2) an underdeveloped equity market and a relatively poor capital market orientation (La Porta, Lopez-de-Silanes, & Shleifer, Legal determinants of external finance, 1997), which are responsible for the limited role played by the market for corporate control (Volpin, 2002).

In particular, because of its unique features, the Italian system of Corporate Governance cannot be compared neither to the other insider-dominated corporate governance systems such as that in Germany, because banks are not involved in the formulation and implementation of corporate strategies, nor to Anglo-American corporate governance systems, because Italy is not characterized by powerful

senior managers and a diffuse ownership, but rather by the presence of large shareholders with a clear incentive to exercise monitoring over company's management (Melis, 2006).

As far as concerns ownership structure, Italian corporations are characterized by a high level of concentration. According to CONSOB (Commissione Nazionale per la Società e la Borsa), in fact, in 2014 data on control model and ownership structure of Italian listed firms show persisting high ownership concentration and limited contestability of control. More precisely, out of 238 publicly listed, 199 (almost 83%) were controlled either by a majority shareholder holding more than half of the ordinary (116 'majority controlled companies'), or by a shareholder playing a dominant role (51 'weakly controlled companies'), or by a group of shareholders organized in a coalition (32 companies) (CONSOB, 2015).

Table 5: *Control model of Italian listed companies*

	controlled companies						non-controlled companies						total	
	majority controlled ¹		weakly controlled ²		controlled by a shareholders' agreement ³		cooperative companies		widely held ⁴		non-widely held ⁵		no.	% market cap ⁶
	no.	% market cap ⁶	no.	% market cap ⁶	no.	% market cap ⁶	no.	% market cap ⁶	no.	% market cap ⁶	no.	% market cap ⁶		
1998	122	31.2	33	21.8	28	8.3	10	3.1	10	24.1	13	11.5	216	100.0
2010	128	20.6	53	43.0	51	12.4	8	3.4	11	20.3	19	0.3	270	100.0
2011	123	22.3	55	45.8	48	12.0	8	3.2	8	16.4	18	0.3	260	100.0
2012	125	22.8	49	44.0	42	10.1	8	3.2	10	19.2	17	0.7	251	100.0
2013	122	24.1	48	40.1	38	10.4	8	3.3	10	21.6	18	0.5	244	100.0
2014	116	25.0	51	36.8	32	9.6	8	4.0	13	24.0	18	0.5	238	100.0

Source: Consob

At the same time, ownership concentration has been declining over time. At the end of 2014, in fact, the average stake held by the largest shareholder was approximately 46% of the ordinary shares, while the stakes held by other major shareholders (on average 16.5% of the ordinary shares) and by the market (i.e. by shareholders with less than 2%) (37.5%) are slightly higher than their long term values (respectively, 14.7% and 36.5%). Finally, the controlling stake is almost 4 percentage points lower than it was in 1998 (respectively, 48.0% and 51.7%) (CONSOB, 2015).

Table 6: Ownership concentration in Italian listed companies

	largest shareholder ¹		other major shareholders ²		market ³		controlling share ⁴	
	simple mean	weighted mean ⁵	simple mean	weighted mean ⁵	simple mean	weighted mean ⁵	simple mean	weighted mean ⁵
1998	48.7	34.7	14.7	10.0	36.5	55.3	51.7	35.0
2010	46.2	34.0	17.7	13.5	36.1	52.5	49.6	34.6
2011	46.1	35.7	17.6	11.4	36.3	52.9	49.7	35.7
2012	46.8	34.8	16.9	9.4	36.4	55.8	49.6	34.4
2013	46.8	34.8	16.5	10.2	36.7	55.0	48.9	34.2
2014	46.0	34.5	16.5	9.2	37.5	56.3	48.0	33.3

Source: Consob

Finally, as for the identity of the controlling person, families still play a major role as 'ultimate controlling shareholders' in 61% of the firms, especially for small companies operating in the industrial sector. Institutional investors, instead, held a major shareholding in 11 firms (4,6% of the market) (CONSOB , 2015). State and local authorities, instead, are gradually (but significantly) reducing their control stake, but are still relevant in large firms.

Table 7: Identity of the 'ultimate controlling agent' in Italian listed companies by market capitalization

	Ftse Mib			Mid Cap ¹			Star ¹			other			total		
	no.	weight ²	% market cap ²	no.	weight ²	% market cap ²	no.	weight ²	% market cap ²	no.	weight ²	% market cap ²	no.	weight ²	% market cap ²
families	14	36.8	21.3	20	54.1	52.8	48	72.7	78.0	63	64.9	36.7	145	60.9	27.7
state and local authorities	9	23.7	36.9	3	8.1	12.5	2	3.0	3.6	5	5.2	19.7	19	8.0	32.2
financial institutions	--	--	--	2	5.4	4.2	1	1.5	1.1	8	8.2	12.2	11	4.6	0.9
mixed ⁴	4	10.5	7.3	4	10.8	10.6	2	3.0	6.8	6	6.2	3.6	16	6.7	7.5
no UCA ⁵	11	28.9	34.6	8	21.6	19.9	13	19.7	10.5	15	15.5	27.8	47	19.7	31.7

Source: Consob

Table 8: Identity of the 'ultimate controlling agent' in Italian listed companies by industry

	financial			industrial			services			total		
	no.	weight ¹	% market cap ²	no.	weight ¹	% market cap ²	no.	weight ¹	% market cap ²	no.	weight ¹	% market cap ²
families	18	34.6	10.9	100	76.9	50.6	27	48.2	18.0	145	60.9	27.7
state and local authorities	--	--	--	6	4.6	39.4	13	23.2	68.1	19	8.0	32.2
financial institutions	2	3.8	1.0	6	4.6	1.2	3	5.4	0.3	11	4.6	0.9
mixed ³	4	7.7	5.7	5	3.8	6.2	7	12.5	12.0	16	6.7	7.5
no UCA ⁴	28	53.8	82.4	13	10.0	2.7	6	10.7	1.5	47	19.7	31.7

Source: Consob

These data confirm that, in Italy, Berle and Means-type public companies, i.e. companies with a dispersed ownership structure determining a separation between

ownership and control, are an exception (Melis, 2006). However, even if the presence of large shareholders reduces the agency problems that arise between management and shareholders, these agency problems are simply shifted towards the relationship between controlling shareholders and minority shareholders. As a matter of fact, the key corporate governance issue in Italy has always been the lack of protection of minority shareholders (Melis, 2000); (La Porta, Lopez-de-Sinanes, & Shleifer, 2000). In the Italian context, therefore, the absence of an institutional framework facilitating more dispersed ownership, pyramidal groups may be used as a mechanism to maximize the ration between the amount of controlled resources and the capital invested to maintain the control of a company (Faccio & Lang, 2001).

In order to improve minority shareholders' protection, in 1998, the Draghi Law was introduced. This law, in particular, has brought significant changes in the area of minority shareholders' rights (Melis, 2006).

First, minority shareholders with at least a 5 percent stake were given the right to bring derivative actions against directors (Draghi Law 1998: art.129) as well as the right to file a complaint to the courts for relevant regularities by directors or statutory auditors (art. 128).

At the same time, voting by email is no longer prohibited, and the threshold required for a group of shareholders to ask directors to set up a shareholder's meeting was reduced from 20 to 10 percent.

Minority shareholder's representation has been granted on the board of statutory advisors. According to Art. 148 of the Draghi Law, in fact, at least one statutory auditor has to be appointed by minority shareholders, at least two when the board is composed of more than three auditors. Obviously, the size of the board matters with regard to minority shareholder's protection.

Finally, Draghi Law has introduced a regulation more similar to that of other European countries. With regard to public bids, for example, the following measures were introduced:

- *Full mandatory public bids*: according to this provision, an investor acquiring more than 30 percent of the equity of a company is obliged to make a full offer for all the company's ordinary shares. This is aimed to give

minority shareholders of a target company the opportunity to gain the same economic benefit as the majority shareholder.

- *Residual mandatory public offer*: according to this provision, any shareholder who owns at least 90 percent of a company's stake must make an offer for the remaining voting shares. This is aimed to grant minority shareholders a fair exit price when a company is substantially owned by a single shareholder.

In 2002, in order to fill the main gap left by the Draghi Law, that is the issues relating to board of directors, the Preda Code was introduced.

But before addressing the content of these dispositions, it is important to discuss briefly the characteristics of the Italian boards of directors. Italian listed companies, in fact, are characterized by a complex accountability and monitoring system (Melis, 2006). In particular, the prevailing board structure is known to be halfway between the British unitary board and the German dual board structure. More precisely, the board is composed of a board of directors (known as *Consiglio di Amministrazione*) and a board of statutory auditors (known as *Collegio Sindacale*). Both boards are appointed by shareholders at the general meeting. The role of the statutory board of auditors is different from that of external auditing firms. As a matter of fact, while external auditing firms are concerned with the auditing of financial statements, the board of statutory advisors is given the responsibility to check the compliance of the board decisions with the law and the observance of the principles of correct administration by executive directors.

The Preda Code did not modify this structure, even if, after the Parmalat scandal companies were given the freedom to choose between three different board models: the Italian traditional board structure, the British unitary board structure, and the German dual board structure.

The Preda Code recommends that the board of directors should deal with corporate strategy, and that it should be composed both by executive and non-executive directors. Non-executive directors, however, usually make up the majority of board directors and should play a significant role in the board's decision making process. At the same time, the Preda Code recommends that the board of director should be made up of an adequate number of independent directors. Nevertheless, while in

public companies the independence of directors should be granted with respect to executive directors (especially the CEO), in presence of large shareholders independence should be granted with respect to controlling shareholders. Finally, according to the Preda Code, the roles of CEO and Chairman of the Board entail entirely different responsibilities, but it also acknowledges that “*it is not infrequent in Italy for the same person to hold both positions*”. Therefore, the Code does not impose the splitting of the roles, even if this practice is highly recommended in other countries. However, the Code recommends that when the same person holds both positions, adequate information about the Chairman’s responsibilities should be provided in the corporate annual reports.

To conclude, as Stanghellini (1999) noted “*writing about Italian corporate governance is like shooting at a rapidly moving target*”. As a matter of fact, regulation and corporate practices have been changing rapidly in the last years, even if the issue concerning the relationship between controlling and minority shareholders has not been fully overcome (Melis, 2006).

2.5 Corporate Governance Across Europe: a Cross-country analysis

This section is dedicated to the differences in corporate governance mechanisms and practices for a set of nine European countries plus the United States. This research was carried out by me and Prof. Guido Mantovani from October 2016 to January 2017. The results of this study and the related scientific paper have been admitted for oral presentation at the 24th Annual Conference of the *Multinational Finance Society*, held between June 25-28 2017 in Bucharest.

2.5.1 Sample and methodology of analysis

In order to draw our sample, we resorted to ORBIS, a database providing complete balance sheets in the global standard format for companies from all around the world.

We extracted financial data of companies from the following European countries: Czech Republic, Germany, Spain, France, Hungary, Italy, Poland, Slovakia, and the United Kingdom. The United States of America were also included in order to allow some benchmarking. For each country, we initially extracted about 6,000

companies. These were both manufacturing and services firms that responded to the following requirements:

- Availability of balance sheet from 2006 to 2015;
- Availability of total assets from 2006 to 2015;
- Availability of shareholder's funds from 2006 to 2015.

After drawing this initial sample, we cleaned the data, eliminating companies with not enough information to compute the 25 indexes required by the Integrated Rating methodology that will be explained in greater detail later in this chapter.

The final sample was made up of 10,546 firms. More specifically, the number of firms for each country was as follows: 1,466 in Czech Republic, 245 in Germany, 2011 in Spain, 455 in France, 188 in Hungary, 2914 in Italy, 16 in Poland, 2869 Slovakia, 372 in the United Kingdom and 10 in the United States.

For each company, we considered a panel of 10 years' balance sheet. Therefore, we analyzed 10,546 firms for 10 years, which means 105,460 financial reports. This was the basis to calculate the 25 indexes required for estimating T(ROI), the long-term threshold ROI according to Integrated Rating methodology.

The same 10,546 firms were taken into consideration when computing the 10 governance variables included in our analysis.

At the same time, in order to determine the corporate governance profile for each of the countries under analysis, the following variables were considered:

1. The **Ownership Concentration** transforms the BvD Independence Index into a figure where the less this numeric variable, the less the ownership concentration.

The BvD Independence Index is an indicator of the degree of independence of a company with regard to its shareholders, and it is assigned to each company according to the following logic:

- Indicator A is attached to any company with known recorder shareholders none of which having more than 25% of direct or total ownership;
- Indicator B is attached to any company with a known recorded shareholder none of which with an ownership percentage (direct or total) over 50%, but having one or more shareholders with an ownership percentage above 25%;

- Indicator C is attached to any company with a recorded shareholder with a total ownership over 50%;
 - Indicator D is allocated to any company with a recorded shareholder with a direct ownership of over 50%;
 - Indicator U is allocated to companies that don't fall in the categories A, B, C or D, indicating an unknown degree of independence;
 - Indicator “-“ attached to any entity which is considered independent by nature (States and individuals) or to inactive companies.
2. The **Presence of a Manger in the Ownership Structure** is a variable constructed as the percentage of managers in the ownership structure on the total of managers. We hypothesize that, in terms of good governance practices, the presence of a manager in the ownership structure is indication of better governance quality.
 3. The **Team Size** counts the number of people in the BVD Board of Directors, in the BVD Board of Advisors and in the BVD Management team, but it adjusts the value by firm size. We hypothesize that the higher the adjusted team size, the better the governance practice;
 4. **One Manager** variable is constructed as a dummy, where the value equals 1 if the company is managed by one person, only. We think that it's important for a good governance that the firms are managed by a team and not by a single person (i.e. the value of the variables equals zero);
 5. **CEO Duality** it is a binary variable that equals 1 if the Chairman of the Board of Directors is also the CEO. We hypothesize is it important for a good governance that the roles of CEO and Chairman of the Board of Directors are perform by two different persons (i.e. the value of the variable equals zero);
 6. **The Board of Directors Independence** is a binary variable that equals 1 if two or more managers are also present in the Board of Directors. If the value equals to 0, the governance is better.
 7. **The Board of Directors Size**, same as Team Size but instead of counting all the people, it only counts how many people are present in the Board of Directors. Then, the same division by firm size is performed. We

hypothesize that the higher the adjusted BoD Size, the better the governance is.

8. **The Equity Ratio**, is simply the ratio between Shareholder's Funds and Total Assets. This ratio is a good indicator of the level of leverage used by a company.
9. **The percentage of institutional investors on total investors** is the ratio between the total number of institutional investors (i.e. investors that according to the ORBIS database fall into one of these categories: Banks; Financial Companies; Public Authority, State and Government; Mutual & Pension funds / Nominees / Trusts / Trustees; Insurance companies; Trade & Industry organizations Foundations / Research Institutes; Private Equity Firms; Venture Capital and Hedge Funds) and the number of total shareholders. We suppose that the higher this ratio, the better the governance is.
10. **The C-3 Index** is the sum of the direct control percentage of the three company's shareholders with the highest percentage of total ownership. A high C-3 index means that the ownership is very concentrated. This variable can be considered as an alternative to the Ownership Concentration variable already mentioned above.

It is important to notice that we considered punctual governance data, while for the financial statements time series are concerned. This is a direct consequence of the time length of corporate cycles, which makes the governance characteristics more stable over time.

The first aim of our research was to verify whether there are relevant differences in ownership control and corporate governance characteristics between the different countries included in our sample. We did this by performing a t-test of difference.

At the same time, we wanted to rank countries, both according to their level of governance (better, middle, worst) and according to their performance at operating level, financial capability and long-term merit of credit. In order to do this, we considered the following proxies:

- 1) The operating performance was measured through corporate ROI, computed according to equation (1):

$$ROI_t = \frac{EBIT_t}{(FIAS_t + WKCA_t + FIAS_{t-1} + WKCA_{t-1})/2} \quad [1]$$

- 2) The financial performance was measured by the intensity of debt, as in equation (2):

$$\text{Intensity of debt} = \frac{DEB}{OPRE_t} = \frac{[(NFP_t + NFP_{t-1})/2]}{OPRE_t} \quad [2]$$

Where:

EBIT = Earnings before interest and taxes

FIAS = Fixed Assets

WKCA = Working Capital

NFP = Net Financial Position = total debts – cash and cash equivalents

OPRE = Operating Revenue

- 3) The long-term merit of credit performance according to the Integrated Rating methodology, i.e. on the spread between the persistent ROI and T(ROI) by Mantovani et al. (2014). The calculation of T(ROI) is based on a specific panel regression for each of the ten countries under analysis, in order to find the threshold level of ROI, given a confidence level based on the investor's risk aversion. If the spread between persistent ROI and T(ROI) is positive, than the probability of the forthcoming business performance is compliant with the risk tolerance, hence the company is creditworthy.

In order to verify our second research hypothesis, instead, we will compare country ranking based on corporate governance and country ranking based on firms' performance, level of indebtedness and merit of credit, in order to prove whether the countries with the best corporate governance are also those that present the better performance, the highest level of debt and the better merit of credit.

2.5.2 Empirical results and discussion

As previously mentioned, to assess whether there are relevant differences in ownership control and corporate governance characteristics between the different

countries included in our sample, we performed a t-test of differences analysis⁶ for each variable.

Table 8 analyses Ownership Concentration. We observed that, the countries with the highest mean in Ownership Concentration are Hungary (4,7515) and Czech Republic (3,773261), even if France and Slovakia, too, show similar values (respectively 3,7663 and 3,7444). On the other hand, the country with the lowest mean is the United States (1,0311), followed by the United Kingdom (2,6907). This confirms the different approach in Anglo-Saxon countries with respect to other European countries.

While performing the t-test of differences we also observed that, within this variable, there are some similarities between Czech Republic, France, Poland and Slovakia; between Germany and Poland; and between Spain and Poland.

⁶ In this paper, the analyses are based on a level of significance established at 10%.

Table 9: Ownership Concentration sample statistics (t-test of difference)

Ownership Concentration	Czech Republic	Germany	Spain	France	Hungary	Italy	Poland	Slovakia	United Kingdom	USA
Mean	3.7732	3,4514	3.2739	3.7662	4.7515	3.0259	3.6025	3.7444	2.6907	1.0311
Variance	1.3187	1.7029	1.8505	0.9527	0.4691	2.2604	1.4916	1.5695	2.3009	1.2395
n.a. (%)	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%

Ownership concentration	Czech Republic	Germany	Spain	France	Hungary	Italy	Poland	Slovakia	United Kingdom	USA
Czech Republic		0.0003	0.0000	0.8989	0.0000	0.0000	0.5859	0.4489	0.0000	0.0736
Germany			0.0463	0.0010	0.0000	0.0020	0.6391	0.0008	0.0000	0.0001
Spain				0.0000	0.0000	0.0000	0.3009	0,0000	0.0000	0.0002
France					0.0000	0.0000	0.6032	0.6712	0.0000	0.0000
Hungary						0.0000	0.0019	0.0000	0.0000	0.0000
Italy							0.0792	0.0000	0.0683	0.0006
Poland								0.6495	0.0101	0.0431
Slovakia									0.0000	0.0808
United Kingdom										0.0019
USA										

Table 9 analyses the presence of one or more managers in the ownership structure. In our sample, we observed that Slovakia is the country with the highest mean (0,4468), but we also observe a similar value for Italy (0,4374). The country with the lowest mean is the United States (0,0397). This result confirms again the differences between Anglo-Saxon and European Countries.

As far as concerns similarities, these were found between Czech Republic and Poland; between Spain and Poland; between France and Poland; between Hungary, Italy and Poland; between Poland, Slovakia and the United Kingdom.

Table 10: Presence of a Manager in the Ownership Structure sample statistics (t-test of difference)

Presence of a Manager in the Ownership Structure	Czech Republic	Germany	Spain	France	Hungary	Italy	Poland	Slovakia	United Kingdom	USA
Mean	0.3723	0.0696	0.3079	0.1393	0.3871	0.4374	0.2687	0.4468	0.1834	0.0397
Variance	0.1995	0.0243	0.1177	0.0789	0.1939	0.1469	0.1663	0.2195	0.0557	0.0019
n.a. (%)	0%	0%	0.15%	0%	0%	1.37%	0%	0.24%	0%	0%

Presence of a Manager in the Ownership Structure	Czech Republic	Germany	Spain	France	Hungary	Italy	Poland	Slovakia	United Kingdom	USA
Czech Republic		0.0000	0.0042	0.0000	0.6699	0.0025	0.3272	0.0004	0.0000	0.0000
Germany			0.0000	0.0321	0.0000	0.0000	0.0707	0.0000	0.0000	0.1068
Spain				0.0000	0.0175	0.0000	0.7058	0.0000	0.0000	0.0000
France					0.0000	0.0000	0.2253	0.0000	0.0169	0.0293
Hungary						0.1286	0.2824	0.0731	0.0000	0.0000
Italy							0.1195	0.3887	0.0000	0.0000
Poland								0.1014	0.4110	0.0413
Slovakia									0.0000	0.0000
United Kingdom										0.0000
USA										

As per the Team Size, Table 10 shows that the country with the highest mean is Italy (5,9166), but the United Kingdom (5,7275) and the United States (5,6666) also show similar values, whereas the country with the lowest mean is Slovakia (1,2360).

Moreover, when we performed the t-test of difference, we found that there were similarities between Czech Republic, France, and Poland; between Hungary and Poland; and between Italy, United Kingdom, and the United States.

Table 11: Team Size sample statistics (t-test of difference)

Team size	Czech Republic	Germany	Spain	France	Hungary	Italy	Poland	Slovakia	United Kingdom	USA
Mean	1.4042	2.7975	4.2775	1.4949	1.7660	5.9166	2	1.2360	5.7275	5.6666
Variance	0.8333	5.9374	4.5222	1.7747	1.2665	11.557	2.3639	0.6967	32.462	18.703
n.a. (%)	0.82%	0%	0,15%	0%	0%	1.37%	0%	0.24%	0%	0%

Team Size	Czech Republic	Germany	Spain	France	Hungary	Italy	Poland	Slovakia	United Kingdom	USA
Czech Republic		0.0000	0.0000	0.1752	0.0341	0.0000	0.1425	0.0000	0.0000	0.0182
Germany			0.0000	0.0000	0.0000	0.0000	0.0707	0.0000	0.0000	0.0817
Spain				0.0000	0.0000	0.0000	0.0266	0.0000	0.0024	0.3637
France					0.0090	0.0000	0.2134	0.0700	0.0000	0.0200
Hungary						0.0000	0.5597	0.0000	0.0000	0.0268
Italy							0.0000	0.0000	0.5274	0.8735
Poland								0.0660	0.0000	0.0358
Slovakia									0.0000	0.0153
United Kingdom										0.9759
USA										

Table 11 analyses the variable One Manager. The country with the highest mean for this variable is the United States (0.333), while the country with the lowest mean is Czech Republic (0,0013). Similarities were found between Czech Republic, Hungary, and Poland; between Germany, France, Hungary, Poland and Slovakia; between Spain and Poland; between Italy and the USA; and between Poland, Slovakia, the United Kingdom and the USA.

Table 12: Only One Manager sample statistics (t-test of difference)

Only one manager	Czech Republic	Germany	Spain	France	Hungary	Italy	Poland	Slovakia	United Kingdom	USA
Mean	0.0013	0.0082	0.1024	0.0200	0.0053	0.3075	0.0625	0.0042	0.1436	0.3333
Variance	0.0014	0.0081	0.0924	0.0195	0.0053	0.2133	0.0625	0.0042	0.1244	0.2500
n.a. (%)	0.82%	0%	0.15%	0%	0%	1.37%	0%	0.24%	0%	0%

Only one manager	Czech Republic	Germany	Spain	France	Hungary	Italy	Poland	Slovakia	United Kingdom	USA
Czech Republic		0.2464	0.0000	0.0055	0.4682	0.0000	0.3437	0.0671	0.0000	0.0815
Germany			0.0000	0.1803	0.7118	0.0000	0.4007	0.5052	0.0000	0.5052
Spain				0.0000	0.0000	0.0000	0.5341	0.0000	0.0355	0.2036
France					0.0834	0.0000	0.5094	0.0195	0.0000	0.0970
Hungary						0.0000	0.3762	0.8476	0.0000	0.0846
Italy							0.0013	0.0000	0.0000	0.8808
Poland								0.3663	0.2291	0.1582
Slovakia									0.0000	0.0837
United Kingdom										0.2899
USA										

As far as concerns CEO duality, in Table 12 it is possible to observe that the highest mean is found in the United Kingdom (0,0131), while the lowest is found in Hungary (0) and Poland (0).

Looking at the t-test of differences, we found similarities between Czech Republic, the United Kingdom and the USA; between Germany, Hungary, Poland; Slovakia, the United Kingdom and the United States; between Spain, Hungary, Poland and the USA; and between Italy and the USA.

Table 13: CEO Duality sample statistics (t-test of difference)

CEO Duality	Czech Republic	Germany	Spain	France	Hungary	Italy	Poland	Slovakia	United Kingdom	USA
Mean	0.0298	0.0082	0.0010	0.0890	0	0.2671	0	0.0131	0.0271	0.1111
Variance	0.0287	0.0081	0.0010	0.0823	0	0.1987	0	0.0128	0.0370	0.1111
n.a. (%)	0%	0%	0,15%	0%	0%	1.37%	0%	0.24%	0%	0%

CEO Duality	Czech Republic	Germany	Spain	France	Hungary	Italy	Poland	Slovakia	United Kingdom	USA
Czech Republic		0.0033	0.0000	0.0344	0.0000	0.0000	0.0000	0.0008	0.8035	0.4857
Germany			0.2187	0.0000	0.1577	0.0000	0.1577	0.4264	0.1047	0.3820
Spain				0.0000	0.1574	0.0000	0.1574	0.0000	0.0100	0.3508
France					0.0000	0.0000	0.0000	0.0000	0.0002	0.8488
Hungary						0.0000	n.a.	0.0000	0.0073	0.3466
Italy							0.0000	0.0000	0.0000	0.1985
Poland								0.0000	0.0073	0.3466
Slovakia									0.1760	0.4038
United Kingdom										0.4727
USA										

In terms of Board Size, the highest mean is observed in Italy (3,1863) while the lowest is observed in Hungary (0.3930). There are similarities between Czech Republic, France and Poland; between Germany and Spain; between Spain and the USA; between France, Hungary, Poland and Slovakia, and between the United Kingdom and the USA.

Table 14: Board Size sample statistics (t-test of difference)

Board Size	Czech Republic	Germany	Spain	France	Hungary	Italy	Poland	Slovakia	United Kingdom	USA
Mean	0.5513	1.4297	1.6030	0.4720	0.3930	3.1863	0.6250	0.4840	2.4820	2.3888
Variance	0.8818	5.0173	2.3618	1.1968	0.9819	7.3304	2.1750	0.8005	2.1499	2.2830
n.a. (%)	0.82%	0%	0,15%	0%	0%	1.37%	0%	0,24%	0%	0%

Board Size	Czech Republic	Germany	Spain	France	Hungary	Italy	Poland	Slovakia	United Kingdom	USA
Czech Republic		0.0000	0.0000	0.1700	0.0403	0.0000	0.8446	0.0252	0.0000	0.0064
Germany			0.2452	0.0000	0.0000	0.0000	0.0557	0.0000	0.0000	0.0991
Spain				0.0000	0.0000	0.0000	0.0183	0.0000	0.0000	0.1578
France					0.3774	0.0000	0.6868	0.8257	0.0000	0.0051
Hungary						0.0000	0.5457	0.2234	0.0000	0.0040
Italy							0.0042	0.0000	0.0000	0.1531
Poland								0.7080	0.0001	0.0119
Slovakia									0.0000	0.0053
United Kingdom										0.8592
USA										

In terms of Board Independence, the country with the highest mean is Italy (0,3075), whereas the country with the lowest mean is Czech Republic (0,0013). The t-test of difference analysis shows that there are similarities between Czech Republic, Germany, Spain, Hungary, and Poland; between Germany, France, Hungary, Poland and Slovakia; between Spain, France, Hungary and Poland; between Italy and the USA; and between Poland, Slovakia, United Kingdom and the USA.

Table 15: Board Independence sample statistics (t-test of difference)

Board Independence	Czech Republic	Germany	Spain	France	Hungary	Italy	Poland	Slovakia	United Kingdom	USA
Mean	0.0013	0.0082	0.1024	0.0200	0.0053	0.3075	0.0625	0.0042	0.1436	0.3333
Variance	0.0014	0.0081	0.0924	0.0195	0.0053	0.2133	0.0625	0.0042	0.1244	0.2500
n.a. (%)	0.82%	0%	0.15%	0%	0%	1.37%	0%	0.24%	0%	0%

Board Independence	Czech Republic	Germany	Spain	France	Hungary	Italy	Poland	Slovakia	United Kingdom	USA
Czech Republic		0.2464	0.2464	0.0055	0.4682	0.0000	0.3437	0.0671	0.0000	0.0815
Germany			0.0161	0.1803	0.7118	0.0000	0.4007	0.5052	0.0000	0.0869
Spain				0.1803	0.7118	0.0000	0.4007	0.5052	0.0000	0.0869
France					0.0834	0.0000	0.5094	0.0195	0.0000	0.0970
Hungary						0.0000	0.3762	0.8476	0.0000	0.0846
Italy							0.0013	0.0000	0.0000	0.8808
Poland								0.3663	0.2291	0.1582
Slovakia									0.0000	0.0837
United Kingdom										0.2899
USA										

Table 15 analyses the variable Equity Ratio. We observe that the highest mean is found in Spain (0,4794), while the lowest is found in Italy (0,3513), but also Slovakia shows a similar value (0,3545). Looking at the results of the t-test of differences, we find similarities between Czech Republic, France, Poland and the USA; between Germany, Italy, Poland, Slovakia and the USA; between Spain, Hungary and the USA; between Hungary, Poland, the United Kingdom and the USA; and between Poland, Slovakia, the United Kingdom and the USA.

Table 16: *Equity Ratio sample statistics (t-test of difference)*

Equity Ratio	Czech Republic	Germany	Spain	France	Hungary	Italy	Poland	Slovakia	United Kingdom	USA
Mean	0.3886	0.3668	0.4794	0.3959	0.4593	0.3513	0.3748	0.3545	0.4339	0.4079
Variance	0.5770	0.0370	0.0421	0.0473	0.0285	0.0405	0.0389	0.0841	0.0476	0.0367
n.a. (%)	0%	0%	0%	0%	0%	0%	0%	0%	0%	0%

Equity Ratio	Czech Republic	Germany	Spain	France	Hungary	Italy	Poland	Slovakia	United Kingdom	USA
Czech Republic		0.3489	0.0088	0.7445	0.0025	0.06626	0.7977	0.09675	0.0473	0.7798
Germany			0.0000	0.0687	0.0002	0.2371	0.8758	0.3607	0.0660	0.5440
Spain				0.0000	0.1278	0.0000	0.05162	0.0000	0.0002	0.2963
France					0.0860	0.0615	0.6810	0.0003	0.0127	0.8577
Hungary						0.0000	0.1149	0.0000	0.1301	0.4505
Italy							0.6421	0.6509	0.0000	0.4030
Poland								0.6872	0.2591	0.6873
Slovakia									0.0000	0.4288
United Kingdom										0.6977
USA										

With regarding to the percentage of institutional investors, in Table 16 we find that the country with the highest value are the United States (0,8134), whilst the country with the lowest mean is Slovakia (0,0617). There are similarities between Czech Republic, Spain, France, Hungary, Italy and Poland; between Germany, Poland and the United Kingdom; between France, Hungary and Poland; and between Poland, Slovakia and the United Kingdom.

Table 17: Percentage of Institutional Investors in the Ownership Structure sample statistics (t-test of difference)

Institutional Investors/Total Investors	Czech Republic	Germany	Spain	France	Hungary	Italy	Poland	Slovakia	United Kingdom	USA
Mean	0.0921	0.2952	0.1010	0.1425	0.1012	0.0737	0.2528	0.0617	0.2365	0.8134
Variance	0.0741	0.1486	0.0684	0.0958	0.0686	0.0444	0.1738	0.0471	0.1149	0.0173
n.a. (%)	22.10%	11.02%	3.49%	11.23%	3.19%	14.69%	12.50%	25.37%	2.14%	0%

Institutional Investors/Total Investors	Czech Republic	Germany	Spain	France	Hungary	Italy	Poland	Slovakia	United Kingdom	USA
Czech Republic		0.0004	0.1014	0.1297	0.2490	0.2161	0.3500	0.0090	0.0000	0.0947
Germany			0.0037	0.0583	0.0008	0.0000	0.8795	0.0000	0.8745	0.0001
Spain				0.5740	0.5950	0.0011	0.2699	0.0000	0.0000	0.0001
France					0.8766	0.03011	0.3071	0.0019	0.0000	0.0689
Hungary						0.1302	0.3314	0.0373	0.0735	0.0217
Italy							0.1920	0.0120	0.0000	0.0001
Poland								0.1557	0.8381	0.0045

Finally, Table 17 analyses the variable C-3 Index. We observe that the country with the highest mean is Slovakia (97,3660), closely followed by Chzech Republic (97,2069), while the country with the lowest mean is the United States (26,5444). Again, we find that ownership is more concentrated in Continental Europe than in the United Kingdom and the United States. Moreover, the t-test of differences shows that there are similarities between Czech Republic, Poland and Slovakia; between Germany, France, Hungary, Italy and Poland; between Spain, Hungary and Poland; and between France, Hungary, Italy and Poland.

Table 18: C-3 Index sample statistics (t-test of difference)

C-3 Index	Czech Republic	Germany	Spain	France	Hungary	Italy	Poland	Slovakia	United Kingdom	USA
Mean	97.2069	88.5504	85.0137	88.5681	83.4326	86.9438	89.1553	97.3660	73.0720	26.5444
Variance	120.165	453.904	597.058	386.793	616.934	402.107	280.467	85.9208	1070.15	180.090
n.a. (%)	23.87%	12.24%	13.12%	13.66%	87.77%	16.71%	18.75%	29.52%	14.21%	0%

C-3 Index	Czech Republic	Germany	Spain	France	Hungary	Italy	Poland	Slovakia	United Kingdom	USA
Czech Republic		0.0000	0.0000	0.0000	0.0144	0.0000	0.1091	0.6815	0.0000	0.0000
Germany			0.0247	0.9920	0.3503	0.2880	0.9028	0.0000	0.0000	0.0001
Spain				0.0021	0.7644	0.0068	0.3932	0.0000	0.0000	0.0008
France					0.3400	0.1309	0.9035	0.0000	0.0000	0.0003
Hungary						0.5061	0.4167	0.0134	0.0697	0.0000
Italy							0.6437	0.0000	0.0000	0.0008
Poland								0.1027	0.0053	0.0000
Slovakia									0.0000	0.0002
United Kingdom										0.0012
USA										

Observing the previous results, we can conclude that consistent differences exist for the variables considered in our analysis, although some similarities in ownership and governance characteristics between the countries are reported (142 similarities over the overall 450 comparisons, i.e. 31,55%). The inner similarities are found in the Equity ratio variable (23 over 45 comparisons, i.e. 51,11%) and in the Board Independence variable (19 over 45 comparisons, i.e. 0.4222).

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By taking into consideration the means of the governance and ownership variables and t-statistics among countries, it is now possible to build-up a country ranking based on previous literature about good governance characteristics. In particular, for each of the 10 indicators considered in our analysis, we assigned a mark between 1 and 10 to each country, where 1 is the worst and 10 is the best. Then, the 10 marks for every country were summed: the higher the final mark, the better is the corporate governance. The ranking is shown in Table 18.

Table 19: *Ranking by corporate governance and ownership characteristics*

Best Governance	Ownership Concentration	Presence of a Manager in the Ownership Structure	Team Size	Only one manager	CEO Duality	Board of Directors Independence	Board Size	Equity ratio	Institutional Investors/Total Investors	C-3 Index	Total
UK	9	4	8	3	5	3	9	8	7	9	65
ES	7	6	7	4	8	4	7	10	4	7	64
HU	1	8	4	8	10	8	1	9	5	8	62
US	10	1	10	1	2	1	8	7	10	10	60
DE	6	2	6	7	7	7	6	3	9	5	58
PL	5	5	5	5	10	5	5	4	8	3	51
IT	8	9	9	2	1	2	10	1	2	6	50
CZ	2	7	2	10	4	10	4	5	3	2	49
SK	4	10	1	9	6	9	3	2	1	1	46
FR	3	3	3	6	3	6	2	6	6	4	42

The ranking shown in Table 18 allowed us to divide the 10 countries included in the sample into three separate clusters: United Kingdom, Spain, Hungary and United States are the countries with the best system of governance, because they reach a mark greater than 60, i.e. at least 6 as average for each variable. Germany, Poland and Italy have, on average, a medium level of corporate governance. Finally, Czech Republic, Slovakia and France are the countries with the worst system of corporate governance, because on average they never obtain a mark of 5.

At the same time, firms included in our sample contribute to rank the Countries according to the averages for ROI, DEBT/OPRE and P(ROI)-T(ROI). The ranking is shown in Table 19.

Table 20: *Rankings by firm performance*

Countries	Median ROI	Median DEBT/OPRE	Median P(ROI)-T(ROI)
Czech Republic	9.09%	14.08%	-17.29%
Germany	5.91%	25.27%	-6.57%
Spain	5.00%	28.33%	-1.30%
France	10.47%	15.39%	-12.82%
Hungary	10.51%	16.59%	-9.98%
Italy	3.70%	29.29%	-3.14%
Poland	13.24%	15.27%	17.88%
Slovakia	6.42%	15.13%	-12.03%
UK	9.68%	20.68%	-6.00%
USA	10.81%	16.21%	-11.44%

Table 21: *Congruence between Corporate Governance, ROI, DEBT/OPRE and P(ROI)-T(ROI)*

		Worsts	Middles	Betters
ROI	Worsts	Czech Republic Slovakia	Germany Italy	Spain
	Betters	France	United States Poland	United Kingdom Hungary

		Worsts	Middles	Besters
DEBT/OPRE	Worsts	Czech Republic Slovakia France	Poland United States	
	Besters		Germany Italy	United Kingdom Hungary Spain

		Worsts	Middles	Besters
ROI-T(ROI)	Worsts	Czech Republic Slovakia France	United States	Hungary
	Besters		Germany Italy Poland	United Kingdom Spain

Observing Table 20 we found that there are some congruencies at country level between corporate governance characteristics and firm's performance. As a matter of facts, in almost half of the countries included in our sample, Countries with the best corporate governance are also those reporting the best average performance (United Kingdom and Hungary), while those with the worst corporate governance are also those with the worst firm performance (Czech Republic and Slovakia). For France and Spain, instead, we did not find any congruence at all.

In terms of level of debt, we found congruencies for the majority of the countries included in our sample. Out of ten countries, in fact, we found that three countries (Czech Republic, Slovakia, and France) have a low rank both in terms of corporate governance and in terms of Intensity of Indebtedness, whereas three countries (United Kingdom, Hungary, and Spain) have a high rank both in terms of corporate governance and in terms of Intensity of Indebtedness. There is no country which scores high in terms of corporate governance and low in terms of level of indebtedness, or vice versa.

Finally, as far as concerns the merit of credit, we also found that in half of the cases there is a correspondence between a country rank in corporate governance and a country rank in the merit of credit. More precisely, we found that Czech Republic, Slovakia, and Spain, have a low rank both in terms of corporate governance and in terms of merit of credit, while United Kingdom and Spain have a high rank both in terms of corporate governance and in terms of merit of credit.

Therefore, we can conclude that there are some congruencies at country level between the rankings based on corporate governance characteristics and firm performance. This means that the countries with the best corporate governance arrangements are also those achieving the best performances with respect to countries with the worst corporate governance systems. Thus, HP2 is verified.

3. Do Ownership Structure and Governance mechanisms contribute to firm performance (including the capacity to attract capital and bank allowances)?

This chapter represents the core of our analysis. In the previous chapter, the existence of a relationship between corporate governance characteristics and firm performance, level of indebtedness, and merit of credit (calculated through the Integrated Rating methodology) was found at country level. However, we also wanted to verify whether the same relationships held at individual firm level, too. At the same time, we wanted to verify whether the structural governance variables (i.e. ownership concentration measured through the C-3 index, the presence of institutional investors in ownership structure, and the equity ratio) have an impact on the other seven governance variable. If a positive relationship is found, in particular, we can conclude that firms characteristics play a major role in shaping the firm's corporate governance system.

Finally, we were interested in verifying whether corporate governance influences the firm choice of capital structure.

In particular, in order to verify HP3 we regressed firm's ROI, DEBT/OPRE, and the spread between P(ROI) and T(ROI) versus the ten governance indicators introduced in chapter 2. Therefore, we considered ROI, DEBT/OPRE and P(ROI)-T(ROI) as dependent variables, whereas corporate governance indicators were considered as independent variables.

3.1 Empirical Analysis and Discussion

In this section, we investigate the relationship between corporate governance characteristics, ROI, DEBT/OPRE, and the merit of credit at firm's level inside each Country. More specifically, we run three multivariate regressions for each of the countries included in our sample. Before presenting the results of our analysis, however, it must be said that, as far as concerns the United States, attention should be paid when interpreting the results of the regressions, as the scarce number of observations does not allow for reliable estimates.

Table 21 shows the results that we obtained by regressing firm's operating performance (i.e. ROI at year 2015) with the ten previously identified corporate governance indicators. The outcomes, however, identified no statistically significant relationship between historical performance and corporate governance characteristics for all the countries included in the sample.

Table 22: Regression statistics – Dependent Variable: ROI

Dependent variable: ROI													
Independent variables	CZECH REPUBLIC	GERMANY	SPAIN	FRANCE		HUNGARY	ITALY	POLAND	SLOVAKIA	UNITED KINGDOM	UNITED STATES		
Const	0.1602 (0.0861)	-0.1379 (0.1340)	0.0592 (0.0711)	0.8344 (0.2444)	***	0.1934 (0.4358)	-0.2267 (0.0887)	* (0.2775)	0.1524 (0.2413)	0.0292 (0.2001)	0.1043 (0.2001)	-- 0.9336 (n.a.)	
Ownership Concentration	-0.0024 (0.0126)	0.0015 (0.0225)	0.0015 (0.0043)	-0.1210 (0.0490)	*	-0.0283 (0.0941)	0.0247 (0.0123)	-0.0720 (0.0496)	0.0023 (0.0247)	-0.0215 (0.0361)	-0.0215 (0.0361)	0.1767 (n.a.)	
Presence of a Manager among shareholders	0.0024 (0.0017)	-0.3054 (0.1882)	0.0004 (0.0003)	0.3360 (0.1625)	*	0.0040 (0.1167)	0.0018 (0.0008)	* (0.1132)	0.1030 (0.0044)	0.0075 (0.0044)	-0.1463 (0.2165)	-0.6611 (n.a.)	
Team Size	-0.0019 (0.0032)	0.0204 (0.0521)	0.0000 (0.0005)	-0.1548 (0.1142)		-0.0548 (0.1163)	0.0012 (0.0008)	0.0697 (0.0748)	0.0123 (0.0072)	-0.0004 (0.0026)	-0.0004 (0.0026)	-0.1174 (n.a.)	
Only one Manager	0.0349 (0.0962)	-0.0910 (0.3444)	0.0393 (0.0180)	* (0.3178)		0.0377 (0.7773)	0.1759 (0.0431)	0.0302 (0.1901)	-0.1344 (0.2576)	-0.1754 (0.1255)	-0.0333 (0.1255)	0.3396 (n.a.)	
CEO Duality	-0.0096 (0.0659)	n.a. (n.a.)	-0.0454 (0.0672)	0.1209 (0.1531)		n.a. (n.a.)	-0.0295 (0.0356)	n.a. (n.a.)	0.0983 (0.1975)	0.0962 (0.2139)	0.0962 (0.2139)	0.1862 (n.a.)	
Board Independence	n.a. (n.a.)	n.a. (n.a.)	n.a. (n.a.)	n.a. (n.a.)		n.a. (n.a.)							
Board Size	-0.0048 (0.0038)	-0.0066 (0.0560)	-0.0003 (0.0006)	0.1317 (0.1370)		0.0457 (0.1332)	0.0000 (0.0011)	-0.0923 (0.0755)	-0.0083 (0.0093)	-0.0043 (0.0065)	-0.0043 (0.0065)	0.2874 (n.a.)	
Equity Ratio	-0.0013 (0.0146)	0.4487 (0.1399)	** (0.0264)	-0.0149 (0.1886)		-0.1426 (0.2782)	-0.0327 (0.0799)	* (0.2963)	0.1685 (0.0834)	0.1367 (0.0834)	0.1306 (0.1810)	0.3210 (0.1810)	-0.1348 (n.a.)
Institutional Investor	0.0008 (0.0045)	-0.0084 (0.0019)	0.0007 (0.0003)	-0.0013 (0.0047)		-0.0118 (0.0139)	0.0000 (0.0007)	0.0255 (0.0386)	0.0088 (0.0130)	0.0002 (0.0017)	0.0002 (0.0017)	0.9851 (n.a.)	
C-3 Index	0.0001 (0.0004)	-0.0013 (0.0008)	0.0000 (0.000)	0.0003 (0.0009)		0.0226 (0.0215)	0.0000 (0.0000)	0.0094 (0.0165)	-0.0013 (0.0007)	0.0003 (0.0006)	0.0003 (0.0006)	n.a. (n.a.)	
Adjusted R-squared	0.0076	0.0522	0.0008	0.0312		-0.0288	0.0009	-0.232	0.0024	-0.0116	-0.0116	n.a.	
F-stat (p-value)	0.0173	0.0078	0.297	0.0058		0.9467	0.2302	0.7233	0.0637	0.8561	0.8561	n.a.	

Table 22 investigates whether there is a relationship between banks' financing decisions (i.e. DEBT/OPRE for year 2015) and the corporate governance indicators. Again, the outcomes of the regression identified a weak statistically significant relationship between historical data of credit allocation and corporate governance characteristics for the majority of the countries included in our sample. Exceptions emerged only for three countries: Czech Republic, Germany and the United Kingdom. More specifically, banks' financing decisions in Czech Republic are positively influenced by Team Size and Board Size, and negatively influenced by the One Manager variable and CEO duality. In Germany, instead, credit allocation is positively influenced by the percentage of institutional investors present in the ownership structure, and negatively influenced by Team Size and Equity Ratio. Finally, in the United Kingdom, banks' financing decisions depend positively on Board Size.

Table 23: Regression statistics – Dependent Variable: DEBT/OPRE

Dependent variable: DEBT/OPRE	CZECH REPUBLIC	GERMANY	SPAIN	FRANCE	HUNGARY	ITALY	POLAND	SLOVAKIA	UNITED KINGDOM	UNITED STATES
<u>Const</u>	1.6029 (0.3650) ***	2.0374 (0.4038) ***	10.8759 (17.5793)	1.2545 (0.9301)	0.0560 (0.1297)	24.7193 (16.1995)	0.1735 (0.1708)	1.5810 (1.9070)	0.1143 (0.1675)	-0.9336 (n.a.)
<u>Ownership Concentration</u>	0.0259 (0.0535)	-0.1462 (0.0680) *	-1.0394 (1.0735)	-0.3231 (0.1865)	-0.0005 (0.0280)	-0.3899 (2.4280)	-0.0080 (0.0305)	-0.0802 (0.1955)	0.0200 (0.0302)	0.1767 (n.a.)
Presence of a Manager among shareholders	0.0171 (0.0072) *	-0.9236 (0.5706)	0.0642 (0.0651)	-1.0160 (0.6182)	0.0607 (0.0347)	-0.0939 (0.1608)	-0.0249 (0.0697)	-0.0107 (0.0348)	0.0199 (0.1812)	-0.6611 (n.a.)
Team Size	0.0813 (0.0135) ***	-0.5167 (0.1563) **	-0.0699 (0.1356)	-0.0098 (0.4346)	0.0559 (0.0346)	-0.3058 (0.1470) *	-0.0111 (0.0460)	-0.0332 (0.0567)	-0.0016 (0.0022)	-0.1174 (n.a.)
Only one Manager	-1.5425 (0.4077) ***	1.2414 (1.0427)	11.4732 (4.4654) *	-0.5922 (1.2091)	-0.3337 (0.2313)	-2.1566 (7.8787)	-0.1390 (0.1170)	0.2380 (2.0358)	-0.1585 (0.1051)	0.3396 (n.a.)
CEO Duality	-0.8190 (0.2793) **	n.a. (n.a.)	-16.6141 (16.6264)	0.7808 (0.5826)	n.a. (n.a.)	-1.0706 (6.5122)	n.a. (n.a.)	-0.7011 (1.5611)	-0.1190 (0.1790)	0.1862 (n.a.)
Board Independence	n.a. (n.a.)	n.a. (n.a.)	n.a. (n.a.)	n.a. (n.a.)	n.a. (n.a.)	n.a. (n.a.)	n.a. (n.a.)	n.a. (n.a.)	n.a. (n.a.)	n.a. (n.a.)
Board Size	0.0798 (0.0161) ***	0.3944 (0.1684) *	0.1792 (0.1425)	0.0663 (0.5211)	-0.0095 (0.0396)	0.4384 (0.1965) *	0.0628 (0.0465)	0.0474 (0.0733)	0.0194 (0.0054) ***	0.2874 (n.a.)
Equity Ratio	-0.0167 (0.0620)	-1.3737 (0.4244) **	-3.5261 (6.5358)	1.4202 (0.7178) *	-0.1150 (0.0828)	-10.1553 (14.5903)	0.0930 (0.1823)	1.2543 (0.6589)	0.0255 (0.1515)	-0.1348 (n.a.)
Institutional Investor	0.0182 (0.0192)	0.0410 (0.0058) ***	-0.0156 (0.0865)	0.0008 (0.0179)	0.0050 (0.0041)	0.1351 (0.1439)	-0.0044 (0.0238)	0.1290 (0.1025)	-0.0004 (0.0014)	0.9851 (n.a.)
C-3 Index	-0.0026 (0.0016)	0.0058 (0.0025) *	-0.0036 (0.0080)	0.0007 (0.0033)	0.0082 (0.0064)	-0.0238 (0.0113) *	0.0005 (0.0101)	0.0016 (0.0057)	0.0001 (0.0005)	n.a. (n.a.)
Adjusted R-squared	0.1485	0.2862	0.0023	0.0054	0.0482	0.0009	0.3169	0.0015	0.0154	n.a.
F-stat (p-value)	0.0000	0.0000	0.1352	0.2499	0.0305	0.2302	0.2122	0.1524	0.1010	n.a.

Finally, Table 23 examines the relationship between the integrated rating (ROI-T(ROI)) and the ten governance indicators. The table shows no statistical significant relationship apart from Germany, where the Equity Ratio variable negatively influences the integrated rating.

Table 24: Regression statistics – Dependent Variable: ROI-T(ROI)

Dependant variable: ROI-T(ROI)	CZECH REPUBLIC	GERMANY	SPAIN	FRANCE	HUNGARY	ITALY	POLAND	SLOVAKIA	UNITED KINGDOM	UNITED STATES	
Const	-0.1937 (0.0184) ***	0.1176 (0.1200)	-0.0400 (0.1047)	-0.0377 (0.4401)	0.3292 (0.3934)	0.0180 (0.0562)	0.1226 (0.7150)	-0.3686 (0.7577)	-0.0914 (0.1338)	-1.4055 (n.a.)	
Ownership	0.0052 (0.0027)	-0.0006 (0.0201)	-0.0001 (0.0064)	-0.0635 (0.0882)	0.0177 (0.0850)	-0.01352 (0.0084)	-0.0356 (0.1277)	0.0192 (0.0777)	0.0150 (0.0242)	0.0369 (n.a.)	
Concentration	0.0000 (0.0004)	0.2841 (0.1686)	-0.0002 (0.0004)	-0.0636 (0.2926)	-0.0506 (0.1053)	-0.0005 (0.0006)	0.0273 (0.2916)	0.0027 (0.0138)	0.1189 (0.1448)	-2.4390 (n.a.)	
Presence of a Manager among shareholders	0.0013 (0.0007)	-0.0130 (0.0467)	0.0005 (0.0008)	0.0177 (0.2057)	0.0813 (0.1050)	-0.0005 (0.0005)	0.0840 (0.1927)	0.0087 (0.0225)	0.0006 (0.0017)	0.0738 (n.a.)	
Team Size	-0.0029 (0.0205)	0.0555 (0.3084)	0.0195 (0.0266)	-0.0390 (0.5722)	0.0055 (0.7017)	0.0052 (0.0273)	-0.1139 (0.4897)	0.2028 (0.8089)	0.0131 (0.0840)	0.5500 (n.a.)	
Only one Manager	CEO Duality	-0.0118 (0.02056)	n.a. (n.a)	-0.03962 (0.0905)	0.2157 (0.2757)	n.a. (n.a.)	0.0096 (0.0225)	n.a. (n.a.)	-0.1566 (0.6203)	-0.0520 (0.1431)	-0.0717 (n.a.)
Board Independence	n.a. (n.a.)	n.a. (n.a.)	n.a. (n.a.)	n.a. (n.a.)	n.a. (n.a.)	n.a. (n.a.)	n.a. (n.a.)	n.a. (n.a.)	n.a. (n.a.)	n.a. (n.a.)	
Board Size	-0.0002 (0.0008)	0.0020 (0.0502)	-0.0003 (0.0008)	-0.0065 (0.2466)	0.0131 (0.1202)	0.0000 (0.0007)	-0.1181 (0.1946)	0.0004 (0.0291)	0.0030 (0.0043)	-0.4644 (n.a.)	
Equity Ratio	0.0003 (0.0031)	-0.4332 (0.1253) ***	0.03717 (0.0389)	-0.0909 (0.3397)	-0.1703 (0.2511)	-0.0411 (0.0506)	0.0112 (0.7634)	0.2471 (0.2618)	-0.1935 (0.1211)	-0.2140 (n.a.)	
Institutional Investor	0.0014 (0.0031)	-0.0007 (0.0017)	-0.0001 (0.0005)	0.0047 (0.0085)	0.0023 (0.0125)	0.0002 (0.0005)	0.0530 (0.0994)	-0.0550 (0.0407)	-0.0001 (0.0011)	2.8977 (n.a.)	
C-3 Index	0.0001 (0.0001)	0.0011 (0.0007)	0.0000 (0.0000)	0.0008 (0.0015)	-0.0366 (0.0194)	0.0000 (0.0000)	0.0098 (0.0424)	0.0002 (0.0023)	-0.0002 (0.0004)	n.a. (n.a.)	
Adjusted R-squared	0.0134	0.0134	-0.0019	-0.0150	0.0462	-0.0014	-0.9095	-0.001	0.0154	n.a.	
F-stat (p-value)	0.0007	0.0007	0.8244	0.9850	0.0350	0.8460	0.9974	0.7297	0.1010	n.a.	

Thus, according to the results of the three multivariate regressions above, corporate governance is weak, as it doesn't seem to determine a significant impact both on firm performance and the integrated rating. Therefore, we reject HP3.

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Given the results above, we decided to investigate whether structural characteristics (equity ratio, presence of institutional investors in the ownership structure, and the C-3 Index) have an impact on the others seven corporate governance indicators. Evidences confirming this hypothesis would lead us to conclude that ownership structure has an influence on corporate governance, but that this latter is not strong enough to influence firms' performance and merit of credit.

Table 24 investigates the relationship between Ownership Concentration and ownership characteristics. We found a strong statistically significant relationship for most of the countries included in our sample. To be more specific, across the ten different countries, the presence of institutional investors in the ownership structure is the variable that mostly influences the Ownership Concentration variable, with the exception of Germany, Hungary, and Poland. The relationship between the C-3 Index and the Ownership Concentration variable is also highly statistically significant for the majority of the countries, apart from Czech Republic, Poland, United Kingdom and the United States. Finally, the variable Equity Ratio is strongly significant for Italy, and weakly significant for France and Hungary.

More precisely, the effect of the percentage of the presence of institutional investors on Ownership Concentration is positive for all the countries for which this relationship is significant, with the exception of the United Kingdom and the United States. This means that when the percentage of institutional investors is high, ownership is more concentrated. In the United Kingdom and the United States, instead, when the presence of institutional investors among shareholders is stronger, ownership concentration is more diffuse. The C-3 index is also positive for all of the countries included in our sample. The opposite is true for Equity Ratio. Therefore, when this variable takes higher values ownership is more diffuse.

Table 25: Regression statistics – Dependent Variable: Ownership Concentration

Dependant variable: Ownership Concentration																				
Independent variables	CZECH REPUBLIC		GERMANY		SPAIN		FRANCE		HUNGARY		ITALY		POLAND		SLOVAKIA		UNITED KINGDOM		UNITED STATES	
Const	3.2074 (0.0410)	***	3.0704 (0.1943)	***	3.0991 (0.0801)	***	3.5664 (0.0951)	***	3.4664 (0.1640)	***	2.7380 (0.0561)	***	3.9155 (0.7104)	***	3.0842 (0.0334)	***	3.4210 (0.1786)	***	5.3893 (1.1493)	**
Equity Ratio	-0.0168 (0.0332)		0.0317 (0.4227)		-0.2359 (0.1456)		-0.4400 (0.1943)	*	-0.5700 (0.2279)	*	-0.7533 (0.1199)	***	-3.4787 (1.5241)		-0.1011 (0.0676)		-0.4999 (0.3338)		2.4881 (0.4736)	**
% Institutional Investors	0.1786 (0.0072)	***	0.0088 (0.0053)		0.0078 (0.0018)	***	0.0205 (0.0046)	***	-0.0172 (0.0102)		0.0250 (0.0010)	***	0.3862 (0.2262)		0.1834 (0.0081)	***	-0.0189 (0.0024)	***	-6.9162 (1.0519)	**
C-3 Index	-0.0009 (0.0008)		0.0074 (0.0023)	**	0.0013 (0.0002)	***	0.0049 (0.0009)	***	0.1590 (0.0135)	***	0.0003 (0.0000)	***	0.0492 (0.0876)		0.0018 (0.0006)	**	-0.0013 (0.0011)		0.0095 (0.0105)	
Adjusted R-squared	0.2966		0.0546		-0.0019		0.1592		0.4258		0.2555		0.3336		0.3274		0.1537		0.9509	
F-stat (p-value)	0.0000		0.0009		0.8244		0.0000		0.0000		0.0000		0.0495		0.0000		0.0000		0.0003	

Table 25 investigates the impact of ownership characteristics on the variable “Presence of Manager in the Ownership Structure”. Again, for the majority of the countries included in our sample there is a strongly significant relationship between the independent and the dependent variable, with the exception of Poland and the United States. The C-3 index is also highly statistically significant for all the countries of our sample, apart from Czech Republic, Germany, Poland and the United States. Finally, the Equity Ratio variable is strongly statistically significant for Spain, and weakly statistically significant for France and Italy.

The impact of the presence of institutional investors in the ownership structure is negative for all of the countries for which this relationship is statistically significant, with the exception of the United Kingdom. This means that, for this country, the higher the presence of Institutional Investors in the Ownership structure the lower the presence of a manager in the Ownership Structure.

As far as concerns the C-3 Index, this variable has a positive impact for all the countries of our sample. Therefore, when ownership is more concentrated, the presence of a manager in the ownership structure is lower, which is detrimental to the governance of a firm.

Finally, Equity Ratio has a positive effect on the presence of a manager for Spain and France, whilst the effect is negative for Italy.

Table 26: Regression statistics – Dependent Variable: Presence of a Manager in the Ownership Structure

Dependant variable: Presence of a Manager																			
Independent variables	CZECH REPUBLIC		GERMANY		SPAIN		FRANCE		HUNGARY		ITALY		POLAND	SLOVAKIA	UNITED KINGDOM	UNITED STATES			
Const	13.1857 (0.3082)	***	0.1243 (0.0227)	***	22.3939 (1.3001)	***	0.1074 (0.0289)	***	-0.0063 (0.1257)		39.6458 (0.8618)	***	0.7056 (0.2818)	*	12.8352 (0.1862)	***	0.0807 (0.0295)	**	-0.2282 (0.1477)
Equity Ratio	-0.0168 (0.2500)		-0.0854 (0.0494)		8.1438 (2.3642)	***	0.1829 (0.0590)	*	0.3220 (0.1747)		-3.9736 (1.8417)	*	-0.4108 (0.6047)		-0.0394 (0.3765)		0.1006 (0.0550)		-0.1024 (0.0608)
% Institutional Investors	-1.3887 (0.0542)	***	-0.0030 (0.0006)	***	-0.5161 (0.0288)	***	-0.0061 (0.0013)	***	-0.0429 (0.0078)	***	-0.4812 (0.0149)	***	-0.0571 (0.0897)		-1.4810 (0.0453)	***	0.0014 (0.0004)	***	0.2927 (0.1352)
C-3 Index	0.0053 (0.0064)		0.0005 (0.0003)		0.0191 (0.0028)	***	0.0000 (0.0002)	***	0.0358 (0.0104)	***	0.0042 (0.0014)	**	-0.0349 (0.0348)		0.0144 (0.0032)	***	0.0004 (0.0002)	*	0.0030 (0.0014)
Adjusted R-squared	0.3112		0.0939		0.1528		0.0635		0.1843		0.2863		0.0591		0.4088		0.0501		0.4746
F-stat (p-value)	0.0000		0.0000		0.0000		0.0000		0.0000		0.0000		0.3153		0.0000		0.0000		0.1100

Table 26 shows the results of the regression of the variable Team Size on the variables describing ownership characteristics. The variable which is statistically significant for the majority of the countries of the sample is the presence of Institutional Investors (with the exception of Italy and Poland). C-3 Index, instead, is strongly statistically significant only for France, Hungary, and Slovakia, and weakly statistically significant for the United Kingdom and the United States. Finally, the Equity Ratio variable is strongly relevant only for Slovakia, and weakly relevant for France and the United States.

In particular, the sign of the impact of the presence of institutional investors among shareholders is positive for all the countries for which this variable is statistically significant with the exception of Spain. Thus, the stronger the presence of institutional investors among shareholders, the better the governance of the firm, because a bigger team improves the way a company is managed.

As for the C-3 index, ownership concentration has a negative impact on Team Size for France, Hungary and Poland, while it has a positive impact on Slovakia and the United Kingdom.

Finally, Equity Ratio has a positive impact on Team Size, because the higher its value, the higher the number of people involved in the management of the firm, thus the better the corporate governance.

Table 27: Regression statistics – Dependent Variable: Team Size

Dependant variable: Team Size													
Independent variables	CZECH REPUBLIC	GERMANY	SPAIN	FRANCE	HUNGARY	ITALY	POLAND	SLOVAKIA	UNITED KINGDOM	UNITED STATES			
Const	6.9110 (0.2294) ***	2.1644 (0.3601) ***	35.5884 (0.6841) ***	1.2480 (0.1378) ***	6.9119 (0.2294) ***	52.7892 (0.9285) ***	2.3810 (1.0731) *	6.1773 (0.1461) ***	34.2693 (1.9845) **	4.0563 (22.632)			
Equity Ratio	-0.1629 (0.1861)	-0.1350 (0.7834)	1.3160 (1.2440)	0.1921 (0.2817) *	-0.1629 (0.1861)	-0.7094 (1.9841)	0.6738 (2.3025)	1.4987 (0.2956) ***	1.2156 (3.7081)	-3.2532 (9.3262)			
% Institutional Investors	0.5898 (0.0403) ***	0.0393 (0.0098) ***	-0.0382 (0.0151) *	0.0335 (0.0066) ***	0.5898 (0.0403) ***	0.0088 (0.0161)	0.2128 (0.3417)	0.2619 (0.0355) ***	0.1699 (0.0265) ***	6.6028 (20.716)			
C-3 Index	-0.0013 (0.0047)	0.0043 (0.0043)	0.0003 (0.0015)	-0.0011 (0.0012) ***	-0.0013 (0.0047) ***	0.0013 (0.0015)	-0.2118 (0.1324)	0.0204 (0.0025) ***	0.0149 (0.0124) *	-0.0917 (0.2072)			
Adjusted R-squared	0.1262	0.0688	0.0022	0.0512	0.1262	-0.0004	0.0403	0.1610	0.1016	-0.2614			
F-stat (p-value)	0.0000	0.0002	0.0608	0.0000	0.0000	0.5889	0.3481	0.0000	0.0000	0.7299			

Table 27 shows the results of the regression of the variable Board Size and ownership characteristics. The presence of institutional investors in the ownership structure is relevant for all the countries of the sample, with the exception of Poland and Slovakia. As far as concerns the other variables, instead, the C-3 index is strongly significant for Spain and Italy and weakly significant for Hungary, whereas Equity Ratio is statistically significant for Spain only.

The sign of the effect of the presence of institutional investors on Board Size is positive for all the countries for which this relationship is statistically significant. This means that the stronger the presence of institutional investors, the higher the number of people involved in the decision-making of the firm, which has a positive impact on corporate governance.

The C-3 index, instead, has a positive impact for Spain and Italy, thus contributing to improve the governance of the firm when ownership is more concentrated. The impact is negative for Hungary, which means that when ownership is more diffuse, corporate governance (measured through Board Size) improves.

Finally, the sign of the relationship between the Equity Ratio and Board Size is positive. Therefore, the higher the Equity Ratio the bigger the Size of the Board of Directors, the better the governance of the firm.

Table 28: Regression statistics – Dependent Variable: Board Size

Dependant variable: Board Size														
Independent variables	CZECH REPUBLIC	GERMANY	SPAIN	FRANCE	HUNGARY	ITALY	POLAND	SLOVAKIA	UNITED KINGDOM	UNITED STATES				
Const	1.4142 (0.1991)	*** 0.6404 (0.3227)	* 8.1436 (0.6666)	*** 0.1865 (0.1120)	0.3889 (0.2783)	20.4055 (0.6912)	*** -0.0316 (1.0023)	* 6.1773 (0.1461)	11.1515 (0.8477)	*** -0.1467 (6.4904)				
Equity Ratio	0.2993 (0.1616)	-0.0707 (0.7020)	6.7549 (1.2121)	*** 0.2811 (0.2289)	0.5400 (0.3868)	0.8830 (1.4771)	2.3491 (2.1504)	1.4987 (0.2956)	1.1898 (1.5840)	-0.3158 (2.6745)				
% Institutional Investors	0.8724 (0.0350)	*** 0.0432 (0.0088)	*** 0.1009 (0.0147)	*** 0.03120 (0.0054)	*** 0.1152 (0.0173)	*** 0.1280 (0.0120)	*** 0.2224 (0.3191)	0.2619 (0.0355)	0.1554 (0.0113)	*** 4.5191 (5.9407)				
C-3 Index	-0.0010 (0.0041)	0.0067 (0.0038)	0.0059 (0.0014)	*** -0.0007 (0.0010)	-0.0544 (0.0230)	* 0.0126 (0.0011)	*** -0.1327 (0.1324)	0.0204 (0.1236)	-0.0008 (0.0053)	-0.0381 (0.0594)				
Adjusted R-squared	0.3023	0.1152	0.0485	0.0709	0.2098	0.1229	0.0403	0.0902	0.3378	0.1502				
F-stat (p-value)	0.0000	0.0000	0.0000	0.0000	0.0000	0.5889	0.3481	0.2656	0.0000	0.3286				

Table 28 investigates the relationship between ownership characteristics and Board Independence. There is a highly statistically significant relationship between equity ratio and board independence for the United States, while for the variable “percentage of institutional investors” the relationship with the dependent variable is strongly significant for the United Kingdom and fairly strong for Italy and Hungary. The C-3 index, instead, is weakly relevant for Hungary only.

With respect to the percentage of institutional investors in the ownership structure, the sign of this relationship is positive for Hungary and the United Kingdom, meaning that the stronger the presence of institutional investors, the stronger the presence of managers in the board of directors (i.e. the Board Independence takes a value next to 1). On the contrary, for Italy the relationship is positive, thus the higher the percentage of institutional investors in the ownership structure, the better the governance, because Board of Directors is more independent (i.e. the Board Independence variable takes a value next to zero).

Table 29: Regression statistics – Dependent Variable: Board Independence

Dependant variable: Board Independence												
Independent variables	CZECH REPUBLIC	GERMANY	SPAIN	FRANCE	HUNGARY	ITALY	POLAND	SLOVAKIA	UNITED KINGDOM	UNITED STATES		
Const	2.415 *** (0.0078)	0.01647 (0.0138)	1.0900 *** (0.0188)	0.0242 (0.0149)	0.0399 (0.0225)	1.3880 *** (0.0215)	0.0310 (0.1977)	1.0040 *** (0.0038)	0.0749 (0.0428)	0.7098 (2.0711)		
Equity Ratio	0.0008 (0.0063)	-0.0380 (0.0301)	0.0187 (0.0341)	-0.0255 (0.0303)	-0.0082 (0.0313)	-0.0760 (0.0460)	0.1303 (0.4241)	-0.0096 (0.0077)	-0.0526 (0.0799)	-1.7856 (0.8534)		
% Institutional Investors	-0.0014 (0.0014)	0.0003 (0.0004)	0.0003 (0.005)	0.0003 (0.0007)	0.0037 ** (0.0014)	-0.0011 ** (0.0004)	-0.0002 (0.0629)	0.0014 (0.0009)	0.0038 *** (0.0006)	0.2832 (1.8957)		
C-3 Index	-0.0002 (0.0002)	0.0000 (0.0002)	0.0003 (0.0004)	0.000 (0.0001)	-0.0040 * (0.0019)	0.0000 (0.0000)	-0.0034 (0.0243)	0.0000 (0.0000)	0.0001 (0.0003)	0.0046 (0.0190)		
Adjusted R-squared	-0.0005	-0.0026	-0.0008	-0.0034	0.0441	0.0044	-0.2314	0.0041	0.1034	0.2098		
F-stat (p-value)	0.5188	0.5030	0.7113	0.6881	0.0102	0.0013	0.9796	0.0021	0.0000	0.2800		

As far as concerns the variable “One Manager”, Table 29 shows that for the variable “percentage of institutional investors in the ownership structure”, the relationship with the dependent variable is strongly significant for the United Kingdom and fairly strong for Italy and Hungary, while the relationship between the C-3 Index and the dependent variable is statistically significant for Hungary only.

In particular, the effect of the percentage of institutional investors in the ownership structure is positive for Hungary and the United Kingdom. Therefore, the higher this variable, the more it is likely that the dependent variable takes a value of 1, meaning that the company is managed by one person only. For Italy, instead, the higher the percentage of institutional investors in the ownership structure the better the governance, because the company is managed by more than one person (i.e. the value of the One Manager variable is next to zero).

As for the C-3 index, the effect of this variable is negative, thus the higher the value of the C-3 index the lower the value of Board Independence, the better the governance.

Table 30: Regression statistics – Dependent Variable: One Manager

Dependant variable: One Manager											
Independent variables	CZECH REPUBLIC	GERMANY	SPAIN	FRANCE	HUNGARY	ITALY	POLAND	SLOVAKIA	UNITED KINGDOM	UNITED STATES	
Const	1.0260 (0.0078)	*** 0.01647 (0.0138)	1.0900 (0.0188)	*** 0.0242 (0.0149)	0.0399 (0.0225)	1.3880 (0.0215)	*** 0.0310 (0.1977)	1.0040 (0.0038)	*** 0.0749 (0.0428)	0.7098 (2.0711)	
Equity Ratio	0.0008 (0.0063)	-0.0380 (0.0301)	0.0187 (0.0341)	-0.0255 (0.0303)	-0.0082 (0.0313)	-0.0760 (0.0460)	0.1303 (0.4241)	-0.0096 (0.0077)	-0.0526 (0.0799)	-1.7856 (0.8534)	
% Institutional Investors	-0.0014 (0.0014)	0.0003 (0.0004)	0.0003 (0.005)	0.0003 (0.0007)	0.0037 (0.0014)	** -0.0011 (0.0004)	** -0.0002 (0.0629)	0.0014 (0.0009)	0.0038 (0.0006)	*** 0.2832 (1.8957)	
C-3 Index	-0.0002 (0.0002)	0.0000 (0.0002)	0.0003 (0.0004)	0.000 (0.0001)	-0.0040 (0.0019)	* 0.0000 (0.0000)	-0.0034 (0.0243)	0.0000 (0.0000)	0.0001 (0.0003)	0.0046 (0.0190)	
Adjusted R-squared	-0.0005	-0.0026	-0.0008	-0.0034	0.0441	0.0044	-0.2314	0.0041	0.1034	0.2098	
F-stat (p-value)	0.5188	0.5030	0.7113	0.6881	0.0102	0.0013	0.9796	0.0021	0.0000	0.2800	

Finally, Table 30 examines the relationship between ownership characteristics and CEO duality. We find that the only variable that is relevant is the percentage of institutional investors in the ownership structure. More specifically, the variable is highly statistically significant for the United Kingdom, and fairly significant for Italy and Hungary. The sign of this relationship is positive, meaning that a higher percentage of institutional investors in the ownership structure implies that, on average, the Chairman of the Board of Directors is also the CEO of the firm. This means that the presence of institutional investors does not promote the separation of these two roles, which instead would be beneficial to corporate governance.

At the same time, we find that in two of the countries of our sample, Italy and the United States, Equity Ratio also impacts on CEO duality. More precisely, the effect of this variable on CEO duality is negative in Italy (a higher equity ratio implies that the roles of Directors of the Board and CEO are played by two different people) and positive in the United States (a higher equity ratio does not imply a separation of the two roles).

Finally, in Hungary and Slovakia, the C-3 Index positively influences CEO duality.

Table 31: Regression statistics – Dependent Variable: CEO Duality

Dependant variable: CEO Duality																			
Independent variables	CZECH REPUBLIC		GERMANY		SPAIN		FRANCE		HUNGARY		ITALY		POLAND		SLOVAKIA		UNITED KINGDOM		UNITED STATES
Const	1.0330 (0.0104)	***	0.0164 (0.0383)		1.0330 (0.0104)	***	0.0581 (0.0304)		0.0000 (0.0000)		1.3810 (0.0267)	***	0.0000 (0.0000)		1.0010 (0.0048)	***	0.0126 (0.0238)		-0.5664 (1.8904)
Equity Ratio	0.0031 (0.0085)		-0.0380 (0.0300)		0.0031 (0.0084)		0.0025 (0.0621)		0.0000 (0.0000)		-0.2029 (0.0572)	***	0.0000 (0.0000)		-0.0101 (0.0097)		-0.0255 (0.0445)		0.4321 (0.7790)
% Institutional Investors	0.0037 (0.0018)	*	0.0003 (0.0004)		0.0037 (0.0018)	*	0.0012 (0.0015)		0.0000 (0.0000)	**	0.0010 (0.0005)	*	0.0000 (0.0000)		0.0038 (0.0012)	**	0.0017 (0.0003)	***	0.5274 (1.7303)
C-3 Index	0.0000 (0.0002)		0.0000 (0.0002)		0.0000 (0.0002)		0.0005 (0.0003)		0.0000 (0.0000)	*	0.0000 (0.0000)		0.0000 (0.0000)		0.0002 (0.0000)	*	-0.0002 (0.0001)		0.0027 (0.0173)
Adjusted R-squared	0.0011		-0.0026		0.0011		0.0058		n.a.		0.0052		n.a.		0.0178		0.0642		-0.4812
F-stat (p-value)	0.2063		0.5030		0.2063		0.1307		n.a.		0.0004		n.a.		0.0000		0.0476		0.9359

Thus, given the above results we can say that, generally speaking for the ten countries included in our sample, ownership structure influences corporate governance characteristics through ownership concentration (measured by the C-3 Index) and the presence of institutional investors. Nevertheless, as shown by the results of the regressions above, corporate governance is not strong enough to influence firms' performance, ability to attract financial resources and merit of credit.

--- § ---

We also wanted to investigate whether it is the Equity Ratio that depends on the corporate governance indicators, rather than the other way around. As a matter of facts, we hypothesized that capital structure could reasonably be influenced by corporate governance mechanisms. The results of the regression of Equity Ratio with the corporate governance variables are shown in Table 31. In particular, what we found is that, as far as concerns the countries included in our sample, Equity Ratio seems to depend on two governance indicators: the presence of a manager in the ownership structure (in Spain, France, Hungary, and Italy) and Board Size (in Czech Republic, Spain and Slovakia). Equity Ratio also depends, but less prominently, on Ownership Concentration (in Italy and Slovakia), on Team Size (in Czech Republic and Spain) and on the One Manager variable (in Italy and Slovakia).

As far as concerns the impact of the Presence of a Manager in the Ownership Structure on Equity Ratio, the sign of the coefficients is positive for all the countries for which this relationship is statistically significant, meaning that the higher the presence of a manager in the ownership structure, the higher the equity ratio. The opposite is true for Italy, where the equity ratio depends negatively on the presence of a manager in the ownership structure.

As for the Board Size, instead, in all the countries where this variable is statistically significant, the sign of this relationship is positive. Therefore, the higher the number of people in the board of directors, the higher the Equity Ratio.

Finally, with respect to the other less prominent variables, Team Size and Ownership Concentration, they both have a negative impact on the equity Ratio, while the One Manager variable has a positive impact in Italy and a negative impact in Slovakia.

Table 32: Regression statistics – Dependent Variable: Equity Ratio

Dependant variable: Equity Ratio										
Independent variables	CZECH REPUBLIC	GERMANY	SPAIN	FRANCE	HUNGARY	ITALY	POLAND	SLOVAKIA	UNITED KINGDOM	UNITED STATES
Const	0.6073 *** (0.1533)	0.3850 *** (0.0565)	0.4437 *** (0.0599)	0.4361 *** (0.0578)	0.5709 *** (0.1087)	0.4757 *** (0.0186)	0.7234 ** (0.2103)	0.5156 *** (0.0532)	0.3980 *** (0.0541)	-1.1744 (n.a.)
Ownership	-0.0348 (0.0226)	-0.0036 (0.0104)	0.0020 (0.0037)	-0.0131 (0.0123)	-0.0575 * (0.0249)	-0.02273 *** (0.0031)	-0.0763 (0.0527)	-0.0122 * (0.0055)	-0.0059 (0.0105)	0.2070 (n.a.)
Presence of a Manager among shareholders	-0.0017 (0.0030)	-0.1503 (0.0868)	0.0009 (0.0002)	0.0947 * (0.0406)	0.0726 * (0.0308)	-0.0008 *** (0.0002)	-0.0668 (0.1330)	0.0001 (0.0010)	0.0708 (0.0627)	-2.1137 (n.a.)
Team Size	-0.0200 *** (0.0057)	-0.0008 (0.0239)	-0.0010 * (0.0005)	-0.0271 (0.0287)	-0.0200 (0.0311)	0.0000 (0.0002)	-0.0751 (0.0852)	-0.0009 (0.0016)	0.0002 (0.0008)	-0.0851 (n.a.)
Only one Manager	-0.1139 (0.1722)	-0.1912 (0.1591)	-0.0123 (0.0153)	-0.0696 (0.0798)	-0.3438 (0.2066)	0.0006 (0.0100)	-0.0942 (0.2244)	-0.1696 ** (0.0577)	-0.0378 (0.0363)	-0.0444 (n.a.)
CEO Duality	0.0541 (0.1180)	n.a. (n.a.)	0.0074 (0.0565)	-0.0023 (0.0385)	n.a. (n.a.)	-0.0194 * (0.0083)	n.a. (n.a.)	-0.0241 (0.0443)	-0.0499 (0.0620)	0.0079 (n.a.)
Board Independence	n.a. (n.a.)	n.a. (n.a.)	n.a. (n.a.)	n.a. (n.a.)	n.a. (n.a.)	n.a. (n.a.)	n.a. (n.a.)	n.a. (n.a.)	n.a. (n.a.)	n.a. (n.a.)
Board Size	0.0270 *** (0.0068)	0.0017 (0.0258)	0.0032 *** (0.0005)	0.0455 (0.0343)	0.0479 (0.0355)	0.0002 (0.0002)	0.0920 (0.0841)	0.0153 *** (0.0021)	0.0013 (0.0019)	0.2882 (n.a.)
% Institutional Investors	0.0095 (0.0081)	0.0004 (0.0009)	0.0003 (0.0003)	-0.0010 (0.0012)	0.0041 (0.0037)	-0.0004 (0.0002)	0.0617 (0.0406)	0.0019 (0.0029)	0.0001 (0.0005)	1.3181 (n.a.)
C-3 Index	0.0005 (0.0007)	0.0000 (0.0004)	0.0000 (0.0000)	0.0005 * (0.0002)	0.0141 * (0.0057)	0.0000 (0.0000)	-0.0156 (0.0189)	0.0001 (0.0002)	0.0002 (0.0002)	0.0071 (n.a.)
Adjusted R-squared	0.0138	-0.0047	0.0270	0.0244	0.0672	0.0278	0.2388	0.06808	0.0039	n.a.
F-stat (p-value)	0.0004	0.5574	0.0000	0.0147	0.0064	0.0000	0.2432	0.0000	0.3085	n.a.

Conclusions

The purpose of this thesis was twofold: by one hand I wanted to present an essential review of some of the most important scientific contributions to the topic of corporate governance, by the other I wanted to present the results of a research I have recently conducted with Prof. Mantovani on corporate governance mechanisms and practices within a set of nine European countries and the United States.

In the first chapter, I introduced the topic of corporate governance by providing its definition both under a narrower and under a broader perspective, the latter representing the current trend. I also introduced agency theory, which has been the most common framework in scientific literature so far. I then used this framework to highlight key issues in corporate governance research and practice, namely: ownership concentration and control, managerial ownership, board of directors' responsibilities and independence, CEO duality, the role of institutional investors, and the effects of corporate governance on firms' financing strategy. In particular, for each of these issues, I provided a synthetic review of the main contributions by academics. I did so because I wanted to compare contrasting results on the same issue. In fact, there is a number of studies on several aspects of corporate governance which have often led to conflicting conclusions, with the results that it is hard to understand the circumstances under which the specific corporate governance arrangements under examination truly affects firm performance. The idea that I want to instill is that attention should be paid when evaluating what constitutes a corporate governance best practice, because the solutions that have proved to be successful under a particular set of circumstances (some depending on firm characteristics, others depending on contextual elements such as the characteristics of a country system) may simply be ineffective under others.

In the first chapter I stated that one of the most researched topic in corporate governance is the issue of ownership concentration and control. From the review of the most influential literature on this topic, in particular, it is possible to notice that while earlier studies focused on the governance implications arising from the separation of ownership and control typical of companies characterized by a dispersed ownership, the same implications are not valid for companies characterized by the presence of large investors,

where agency problems are instead found between controlling and non-controlling shareholders.

At the same time, from the review of academic literature on managerial ownership emerged that the relationship between the latter and firm performance may not be linear as it was initially hypothesized by researchers. In fact, empirical evidence suggested that while low and very high level of managerial ownership lead to a convergence of interests between managers and shareholders, when managerial ownership is sufficiently high entrenchment effects are more likely to occur.

As for the issue of board independence, the main implication resulting from the literature review is that although directors' independence is important to ensure the goodness of firm corporate governance, insider board representation should not be considered as something negative in absolute terms. Insiders, in fact, can provide to the board relevant information about the firm, especially in critical times.

Another controversial aspect concerns the separation of the titles of CEO and Chairman of the Board. Again, a careful examination of prior literature is useful to understand under what circumstances splitting the roles may contribute to firm performance and when the same practice can be detrimental, because it constitutes an efficient system of incentives for managers who want to become CEOs.

The issue of the contribution of the presence of institutional investors to firm performance is also somewhat controversial. In fact, if by one side institutional shareholders are expected to play an active role in the companies they own, by the other it has been recognized that they could be rather short-termist in their investment decisions, even if this hypothesis has gained little support from empirical evidence.

Finally, as far as concerns the disciplining role of debt within a firm, prior research on the topic proved that while this mechanism is effective in corporations with a clear separation of ownership and control, in case of high concentration (as it is the case of Continental Europe) the role of debt as an effective control mechanism can be considerably reduced. In this case, controlling shareholders may be tempted to increase the debt ratio as a mechanism of expropriation of minority shareholders, because debt allows them to control more financial resources without diluting their control stake.

I concluded the first chapter by highlighting the future trends in corporate governance research, particularly the issue of corporate social responsibility. In particular, I argued

that policies and corporate governance initiatives are increasingly focusing on the importance of broadening the corporate governance agenda in the attempt to respond to the increased sensibility towards social and environmental issues. The main implication in terms of corporate governance is that companies are adopting a more inclusive approach, shifting their attention from shareholders to the broader spectrum of stakeholders.

In the second chapter, I introduced the widespread categorization of corporate arrangements into two broad systems: the insider-dominated systems and the outsider-dominated systems. I also explained where do the differences between these systems come from. Then, I introduced some case studies in order to better explain the characteristics of both types of systems. In particular, the United Kingdom was used as a case study for the outsider-dominated systems, while Germany was used as a case study for the insider-dominated systems. I also presented the case of Italy, whose corporate governance system is rather peculiar.

Introducing the categorization of corporate governance systems was instrumental to the presentation of the subsequent empirical analysis, which involves nine European countries and the United States. Through this analysis, particularly, we wanted to verify whether evidence supports of the existence of differences in corporate governance practices and mechanisms among European countries. In this regard we found that, despite some similarities can be found, there are still relevant differences among countries which mainly reflect the characteristics of their legal system. This supports the view that common law countries are characterized by ownership patterns that significantly differ from civil law and German legal systems.

At the same time, we wanted to verify whether there are congruencies at country level between the goodness of corporate governance and long-term performance. We found that, at least at country level, better corporate governance characteristics are also able to drive better corporate performances, to increase firms' capability of attracting financial resources and to improve firms' merit of credit.

Finally, in the third chapter I presented the core of the empirical analysis. In particular, when comparing corporate governance characteristics with firm performance, intensity of indebtedness, and the merit of credit, the congruencies between corporate governance and performance that had been observed at country level disappear.

We found that corporate governance is influenced by structural variables such as ownership concentration and the presence of institutional investors. Therefore, we argued that structural variables have an influence on corporate governance, but the latter is not strong enough to influence firms' performance and merit of credit.

We then studied the relationship between corporate governance and firms' capital structure policies. We found that the corporate governance indicators that affect the level of equity (and consequently the level of indebtedness) for most of the countries of our sample are the Presence of a Manager among Shareholders and Board Size. Therefore, empirical evidence supports theory suggesting that corporate governance influences, through its mechanisms, the capital structure chosen by a firm.

Nevertheless, it must be said that the results of this study could be affected by the quality of information provided by the database. As a matter of fact, it is not possible to have reliable conclusions for all of the countries included in our sample. In particular, the lack of information for the computation of the merit of credit for companies in Hungary, Poland and the United States does not allow an adequate number of observations for the analysis of corporate governance characteristics. In order to address this problem, our research team is considering to compute the merit of credit through a smaller number of indexes, given that some information is not available for a very large number of firms in many countries, typically the number of employees and material costs. By removing the two indexes calculated by using these figures, namely work productivity and difference between delays on payments to creditors and payments from debtors, we are able to draw a significantly higher number of firms for the three countries mentioned above.

To sum up, a comprehensive analysis of prior literature leads to the conclusion that there are no golden rules when it comes to corporate governance. The implementation of governance practices and mechanisms, in fact, should follow the appraisal of both firm and contextual characteristics, both of which play a very important role in determining the effectiveness of corporate governance arrangements. In fact, we found that there are significant differences in terms of corporate governance practices between countries, which mainly reflect the origin of their legal system. At the same time, we found that firms corporate governance may be influenced by internal characteristics, particularly ownership concentration and the presence of institutional investors among shareholders. Given these results, the main implication for corporate governance is that companies

should not follow a one-size-fits-all rule, but rather assessing their structural and contextual constraints, so to implement corporate governance solutions that are both optimal and effective.

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