



Corporate Governance and Development Finance Institutions In Asia and the Pacific

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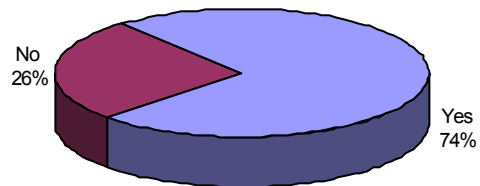
The Asian financial crisis placed a new emphasis on corporate governance in Asia and the Pacific. At the center of the crisis were companies and conglomerates, owned and controlled by generations of families and interlocking interests, which were brought up in a relationship-based (rather than market-driven) environment. As promoters of economic growth, development finance institutions (DFIs) in the region took a central role in advocating corporate governance reforms, but DFIs cannot succeed in promoting good corporate governance within the Asian business community until they establish effective governance mechanisms within their own structures.

Corporate Governance After the Asian Financial Crisis

The Asian financial crisis placed a new emphasis on corporate governance in Asia and the Pacific, as well as all over the world. At the center of the crisis were companies and conglomerates, owned and controlled by generations of families and interlocking interests, which were brought up in a relationship-based environment and were no longer able to compete in the global economy. Governments, the general public, and the private sector have all realized how fast capital flows change direction when investors lose confidence in the market and how fast the corporate sector can collapse when financial flows dry up. The crisis exposed the problems of the corporate world; shed light on the importance of right ownership structures, sound financial institutions, transparent banking regulations, accounting standards, effective bankruptcy codes and availability of accurate and timely information; and showed the fallouts of relationship-based (rather than market-driven) economic activities.

In the aftermath of the financial crisis, business entities in the region advocated their adherence to the principles and practices of corporate governance as a means to improve their competitive advantage and to increase profitability. In fact, in a recent survey conducted by ADFIAP (distributed to 65 member-institutions in 30 countries in the region) three out of four survey respondents stated that their countries have a nationwide policy on good corporate governance; those which stated there was no such national policy, are those from the less-developed countries in the region.

Does your country have a nationwide policy on good corporate governance?



Source: Survey distributed to 65 institutions in 30 countries in Asia and the Pacific

The Center for International Private Enterprise is a non-profit affiliate of the U.S Chamber of Commerce and one of the four core institutes of the National Endowment for Democracy. CIPE has supported more than 700 local initiatives in over 80 developing countries, involving the private sector in policy advocacy, institutional reform, improving governance, and building understanding of market-based democratic systems. CIPE programs are also supported through the United States Agency for International Development.

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But what is good corporate governance, and more importantly, how is it to be approached? Good corporate governance ensures that decisions made and actions taken by executives reflect and protect the interests of stockholders, customers, creditors, and other stakeholders. Since the financial crisis, the focus has been placed on eliminating the features of crony capitalism (political dealing, family ties, nepotism, etc.) and instead creating performance-driven enterprises. That means introducing laws and regulations that protect the rights of minority shareholders; stressing the role of independent directors and external audits; eliminating insider-trading and self-dealing; requiring timely, accurate and relevant information disclosure; and reforming the banking sector. Good corporate governance is empowering today's Boards of Directors to be more proactive in directing the operations of their organizations by making them responsible for their actions and causing them to be extra-efficient in providing shareholder value.

Development Finance Institutions Revisited

Development Finance Institutions (DFIs) - development banks, policy banks, specialized funding agencies, etc. - are financial institutions set up by governments to provide long-term financial and technical assistance to economic sectors of the country that other providers of capital do not necessarily go into. These financial institutions exist in many developing countries in the world. Even in the developed economies of Europe, these types of financial institutions still operate in the mold of "universal banks." In Asia and the Pacific, almost all countries have at least one development bank, including Japan, although its function and structure may differ depending on the stage of the nation's economic development.

Created after World War II, DFIs were used as channels by the World Bank and the Asian Development Bank (ADB) to provide long-term capital to the region's industrialization efforts. In fact, most of them were clones of these two multilateral financial institutions in the manner of evaluating loan proposals and formulating loan conditions and in aspects of project implementation and supervision. But all that has changed now, and development banks have charted their own paths, guided by the present business environment and its complexities, which are balanced by their overarching objective of promoting economic development.

DFIs and Corporate Governance

The financial collapse of 1997 not only stressed the need for corporate reform in the business community, but also brought the need for reform within DFIs. DFIs play a central role in advancing corporate reform in the region. Unlike regular commercial banks, development banks not only provide financial assistance to enterprises, but they are also involved in training and providing management expertise. Thus, to be effective in promoting good corporate governance they must institute good corporate governance practices themselves.

Some DFIs in the region still do not have an effective regulatory framework for good governance in place. In those DFIs, members of the board are appointed by the government (lack of independent board members), and many are still in the process of developing and polishing their corporate governance codes. Those codes should not only outline the roles and responsibilities of the boards, but also hold them accountable for their actions. Many of the members of the boards still lack sufficient training,

ADFIAP's Strategy to Improve Corporate Governance

1. Undertake a membership-wide survey to determine the extent of its members' corporate governance policies and practices.
2. Organize a regional symposium-workshop on corporate governance to develop an action agenda.
3. Organize national workshops (after the regional workshop) to focus on "local" corporate governance programs.
4. Assist members in their respective institutions/countries to develop a framework and to sustain their corporate governance policies and programs.
5. Promote the project through the Association's regular publications and through its website.
6. Visit institutions to assist participating members in developing their corporate governance systems, using best practices learned from the surveys, seminars and other interaction with them.

*For more information, please visit
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and some institutions are not subject to external (i.e., independent) audit. Some DFIs have also failed to put together effective disclosure mechanisms and are not effectively reporting to either the government or to the public.

Effective boards of directors are vital if efforts to “corporatize” DFIs are to be successful. Simply recognizing that corporate governance is important is merely not enough; board members must clearly understand their responsibilities and must have sufficient training and knowledge. Independent directors will play a key role in ensuring effectiveness of the boards, and they must be present in each of the institutions. Simply put, DFIs cannot succeed in promoting good corporate governance within the business community until they establish effective governance mechanisms within their own structures. Or, in other words, the business community will not be successful in developing corporate governance mechanisms until a good corporate governance culture is implemented within the development banks themselves.

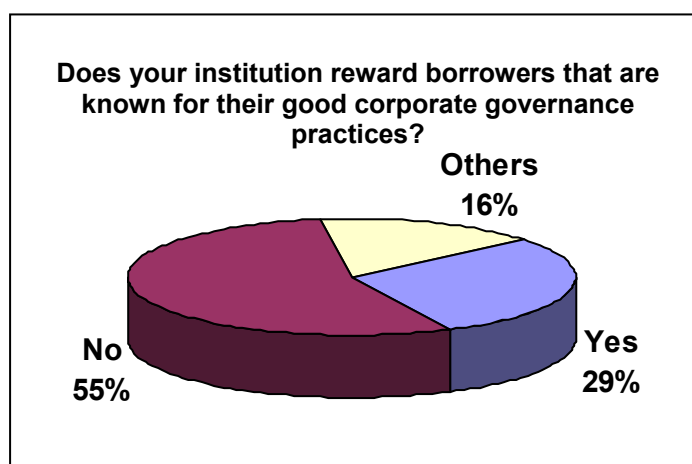
The Role of the ADFIAP

ADFIAP, by bringing together the national development banks, promotes mechanisms of good corporate governance as a key to business sustainability in the region. ADFIAP’s work is a response to the need of financial institutions that are engaged in the financing of development initiatives in their respective countries to embrace and institutionalize good corporate governance policies and practices in their organizations not only because it is a “right thing to do,” but also because it is essential to business success. ADFIAP addresses the lack of corporate governance in the region by pursuing Boards of Directors to develop, write, and accept Codes of Corporate Governance, as well as to appoint a senior officer (or unit) to oversee, direct, and manage a sustainable good corporate governance program in their institutions.

Through its “DFIs for Corporate Governance” program, the Association undertook a membership-wide survey to determine the extent of its members’ corporate governance policies and practices. The survey examined the corporate governance situation on national and institutional levels, existing corporate governance programs instituted, and organizational changes made, if any, to reflect corporate governance issues. The survey revealed that even though DFIs have been effective in promoting and instituting corporate governance mechanisms, much work remains to be done.

While 70% of institutions surveyed by ADFIAP state that they have Board-approved governance policies and practices in their respective organizations, only half carry a section on corporate governance in their annual reports. In fact, 48% need assistance in preparing their Codes of Corporate Governance and 68% require assistance in training directors and managers. Also, 45% of respondents do not use outside consultants for directors’ corporate governance training, and in almost 50% of the cases an institution’s Corporate Governance Code is not endorsed by all members of the Board. More importantly, only about a third of the respondents “reward” their borrowers who are known for good corporate governance practices.

By organizing regional workshops on corporate governance, ADFIAP encourages its members to develop an action agenda, and through national workshops, the Association develops specific corporate governance programs tailored to the local conditions and demands. ADFIAP also combines best practices learned from the surveys and regional/national workshops to assist participating members in “hands-on” management of their respective corporate governance systems.



Concluding Remarks

National DFIs were set up by their governments as specialized financial institutions to provide long-term financing and technical assistance to sectors that promote the country’s economic development and growth but which are not normally looked after by commercial banks that are in their formative years. DFIs have an important role to play in a country’s development and are an integral part of its

financial system. In some countries, DFIs are deemed “trailblazers” in the sense that they finance start-up projects that other financial institutions shy away from because of inherent risks and long-term gestation. From ADFIAP’s point of view, the practice and institutionalization of corporate governance in DFIs is one such trailblazing initiative that it is proud to have undertaken. With effective communication between member-DFI’s and a strong commitment to reform the development banks in the region, ADFIAP has provided its member institutions a chance to become model good corporate governance institutions.

Octavio B. Peralta serves as Deputy Secretary General of the Association of Development Financing Institutions in Asia and the Pacific (ADFIAP). ADFIAP is the focal point of all development banks and other financial institutions engaged in the financing of development in the region. Founded in 1976 under the auspices of the Asian Development Bank, ADFIAP has 65 member-institutions in 30 countries. ADFIAP is also a founding member of the 300-member World Federation of Development Financing Institutions (WFDFI) composed of similar regional associations in Africa, Latin America, Europe, and the Middle East. ADFIAP is a non-governmental organization in consultative status with the United Nations’ Economic and Social Council. For more information please visit <http://www.adfiap.org>.

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