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A Comparative Analysis of the Corporate Governance Practices in Multinational and Domestic Banks in Zimbabwe

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Abstract
The Zimbabwean banking sector has been characterised by a number of corporate governance disorders. This study aimed at analysing the corporate governance practices by multinational banks in comparison to domestic banks in Zimbabwe. It was hoped that the research would reveal the corporate governance discrepancies between multinational and domestic banks and hence assist the Reserve Bank of Zimbabwe in pursuing its supervisory role as well as bring awareness to stakeholders in the banking industry. The research adopted a cross-sectional survey research design. The target population consisted of all commercial and merchant banks in Zimbabwe. Primary data was gathered through questionnaires and interviews. Secondary data was also analysed in the research. The selection of the banks to be included in the sample employed stratified random sampling to ensure representation from each key group of banks in the sample. The study revealed that the awareness on the importance of sound corporate governance practices was of substandard levels for both bank categories. Domestic banks, in particular, had more shortfalls compared to multinational banks. Results further revealed that domestic banks did not represent shareholders’ interests in their corporate governance practices and their levels of compliance to Reserve Bank of Zimbabwe’s corporate governance requirements was still lacking. Although corporate governance strategies by multinational banks were superior to domestic banks it was established that multinational banks needed to accept local central bank requirements on corporate governance as an engine to enhance their corporate governance strategies.

Keywords: corporate governance, multinational banks, domestic banks, compliance, strategies, Reserve Bank of Zimbabwe.

INTRODUCTION
In the wake of the large-scale financial collapses of viable corporations such as Enron, Worldcom and Parmalat, the corporate world has awoken to the need for implementation of sound corporate governance practices in the 21st century. In view of these corporate scandals in the global economy, considerable recommendations in the governance of companies have been given. These recommendations include Treadway Commission of 1987, Sarbanes-Oxley Committee, Cadbury Committee of 1992, Greenbury Committee, Higgs Committee of 2003 and King Committee of 2002. Such recommendations have led to the development of various corporate governance acts and codes in different countries. Turning to the Zimbabwean scenario, post-independence Monetary Authorities in Zimbabwe had limited interference with banking operations. Banks appeared to have kept off the demands for corrupt dealings despite widespread corruption in other economic sectors. The banking law was enacted at a time when all the banks were multinational and foreign-owned. Prudential regulation of banks appeared, therefore, to be unnecessary. The Banking Act of Zimbabwe then, was the only operational law, and it took no notice of provisions on insider lending, nothing on the maximum ratio of shareholder funds that could be lent to a single borrower, no definition of risk assets nor the amount of capital required to support bank lending, and no provision for inspection of banks except where a case was made for an investigation into fraudulent or other criminal activities.

According to Harvey (1997), the banking system survived this period relatively well. In that regard,
when the Zimbabwean authorities embarked on the Economic Structural Adjustment Program (ESAP) and financial liberalization programme in the early 1990s, major rehabilitation of the banks was deemed not necessary. There was therefore, reasonable prospect of the banks being able to survive the change of policy successfully. During this period, registration of domestic banks, owned and managed by local people or organizations commenced. This was because financial liberalization was mainly aimed at removing barriers to entry in the banking sector. It is regrettable that the Monetary Authorities uncovered some dishonest dealings by domestic banks in 2004, thereby destabilizing the financial sector. In the interest of recovering this sector, corporate governance standards of all banks have been under review.

The Reserve Bank of Zimbabwe (RBZ) issued two guidelines on corporate governance in 2004, Corporate Governance Guidelines and Minimum Internal Audit Standards in Banking Institutions. These are considered minimum standards on which banks are expected to improve. All banks are compelled to meet these requirements outlined in the corporate governance regulations that include the proportion and selection of executive, non-executive directors and independent directors that will be subject to RBZ’s approval. The RBZ also set up a new department dedicated towards corporate governance, risk management and internal audit. Given that the RBZ is responsible for monitoring corporate governance policies in banks, preceding Monetary Policy Statements of 2004 indicate a transformation in RBZ’s approach. The RBZ has increased its scope of supervision of banks, in light of the growing complexity of the task of preserving financial stability. Numerous supervisory approaches have been adopted. Some banks have also made some independent efforts towards enhancing their corporate governance strategies. Mangena (2006) argued that in light of the increased emphasis on sound corporate governance policies, the Institute of Directors of Zimbabwe (IODZ) has promoted the sound corporate governance by recommending compliance with the UK’s Cadbury Report of 1992, and the South African’s King Report of 1994. However, for survival, it is indisputable that the corporate governance strategies by both multinational and domestic banks should be feasible and effective. Likewise, the unprecedented financial turmoil over the past few years calls for dynamic and proactive corporate governance frameworks by banks. For this reason, the major problem faced by the public, monetary authorities and the banks is the correct determination of appropriate strategies for the current economic environment, which are effective. This formed the main thrust of this analysis.

**MOTIVATION**

It is regrettable that the Zimbabwean banking industry continues to experience corporate governance triggered financial turbulence. Amazingly, multinational banks seem to have withstood the challenges that have been bedeviling the Zimbabwean banking sector. Therefore, this paper sought to evaluate the effectiveness of corporate governance practices between multinational and domestic banks in Zimbabwe.

**RESEARCH AIMS**

The primary objective of the study was to evaluate the effectiveness of corporate governance practices being taken by multinational and domestic banks in Zimbabwe. The research also intended to determine the extent of banks’ compliance to RBZ’s corporate governance requirements as well as the effect of corporate governance practices on banks’ performance.

**LIMITATION OF THE STUDY**

The target population of this research were senior executives of banks who have busy schedules and found it difficult to spare time to respond to the research questionnaire. In addition, corporate governance is a sensitive and confidential matter, thus respondents were not comfortable with the research. Appointments and follow-ups were made to ensure that the questionnaires were responded to and respondents were assured anonymity to guarantee confidentiality.

**LITERATURE REVIEW**

Mathiesen (2002) defined corporate governance as an economic field, which concentrated on how to secure effective management of organizations by use of incentives like organizational structure and legislation. He added that corporate governance was concerned with finding ways of improving financial performance of an organization. Shleifer and Vishny (1997) shared a similar view to Mathiesen (2002), by defining corporate governance as the means by which a company’s financiers guaranteed themselves of getting significant returns on their investments. However, Maw (1994) avoided defining corporate governance pointing out that definition of the topic still had blurred edges. Nonetheless, he noted that other analysts believed that corporate governance referred to the system through which the board of directors, management and financial auditors handled their responsibilities towards company shareholders.

On the other hand, Takahashi and Shimizu (2006) indicated that corporate governance referred to the functions of the directors and auditors in monitoring the entire business practices.
Corporate Governance and Risk Management
The Cadbury Report (1992) and the OECD Principles (1998) emphasized the importance of integrating a risk management framework within the corporate governance activities of the board of directors. They clarified that it was the ultimate responsibility of the board to ensure all potential risks had been identified and mitigatory measures were put in place. In the same vein, the Cadbury Report (1992) noted that directors needed to maintain a system of internal control, with measures aimed at minimizing risk of fraud.

Although David (2003) acknowledged that risk management needed to be integrated into a company’s corporate governance framework, he highlighted that risk assessment process was hard to perform due to the complexity and changing of the operating environment. David (2003) thus, identified a set of indicators that could assist directors in setting up a risk management internal control system. These indicators related to the operating environment, health, safety, ethical behavior and restructuring an organization towards sustainability.

In light of the above, corporate governance mechanisms need to be supplemented by a risk management framework for them to be effective. Boards of directors were therefore encouraged to be attentive to the probable risks in an organization and organize some control measures.

Corporate Governance in Multinational Banks
According to Weston (1980) the corporate governance structures of multinational banks in most countries were made firmer in the late 1970s due to regulatory controls of some countries, which were not meeting home country standards. These regulations included the solvency and liquidity requirements. Tightening of corporate governance strategies was necessitated by the reason that domestic banks could easily approach central banks as the lender of last resort unlike multinational banks. In that regard the justification of tightening corporate governance structures was for the protection of depositors’ funds; need to have control over the volume of money and credit and the curbing of every tendency of monopoly power in the banking industry.

Gamal (1963) in his survey of the Islamic financial sector established that corporate governance of multinational banks was mainly concerned with aligning management’s interests with those of shareholders who were the owners. He explained that this task was being accomplished through shareholder representation on the board of directors and competitive manager remuneration schemes.

In addition to Gamal (1963), Allen and Gale (2000) argued that corporate governance in multinational banks was mainly concerned with aligning management’s interests with those of shareholders was insufficient. The underlying reality being that, multinational banks had depositors who were considered as creditors with first claimants on a bank’s assets. They explained that depositors’ interests were taken into account in determining in the corporate governance strategy. Allen and Gale (2000) pointed out that; regulators through deposit insurance boards and capital adequacy ratios among many normally guarded depositors’ interests. This meant there was more to the task corporate governance in multinational banks than just aligning the interests of managers and shareholders.

In that regard, Kamel (2004) suggested that there was need for synchronization of interest in multinational banks, which put the depositors on the same level with stockholders. He added that this enabled depositors to have similar corporate governance advantages as shareholders through internal representation. Kamel (2004) highlighted that investigations in Malaysia and Egypt revealed this synchronization in multinational banks, which was inspired by European banks. As a result, Kamel (2004) recommended that the interests of managers, depositors and shareholders needed to be aligned in multinational banks to limit the principal-agency problem.

According to Barlett and Ghoshal (1995), multinationals chose from a range of corporate governance strategies, this included international, global and multinational standards. They however highlighted that; the most commonly practiced corporate governance strategy was the multinational strategy, which gave emphasis to adoption of policies based on variations in the operating environments. Multinationals adjusted their services and management practices accordingly in each country. This strategy also gave management independence, which were normally nationals of the hosting country and thus familiar with that country’s corporate governance requirements. Barlett and Ghoshal (1995) concluded that whatever strategy was pursued by a multinational, it influenced the overall composition of the parent corporate governance strategy.

Costello (2002) in his study to establish the nature and effectiveness of corporate governance in multinationals explained the corporate governance process through, figure 1 below:
FIGURE 1: Multinational Model of Corporate Governance Source: Costello (2002): Corporate

**Governance in Multinational Corporations: Aligning the Interests of Subsidiaries and Headquarters**

The above diagram indicated that Costello (2002) agreed to Barlett and Ghoshal (1995) that multinationals assessed the applicability of host and home country’s corporate governance systems before implementing a corporate governance strategy.

Claessens et al (2000) established that the entrance of multinational banks in a country had a positive impact on the entire banking system as they practiced sound corporate governance strategies. In support of this, empirical studies by Roe (2002) suggested that the presence of multinational banks reduced the likelihood of banking crisis and could result in banks becoming more prudently sound through adoption of proper strategies.

In conclusion, despite, the indicated bureaucracy experienced by some multinational banks in executing their corporate governance strategies which were based on their home countries; highlighted literature largely indicated that multinational banks generally had effective corporate governance strategies.

**Corporate Governance in Domestic Banks**

La Porta (2002) highlighted that it was a common feature to find the majority of domestic banks being owned by the government. Arun and Turner (2002) further explained that such ownership facilitated the solving of corporate governance challenges such as insufficient disclosure and transparency of bank dealings and liquidity problems. They, however, indicated that achievement of resolving such challenges largely depended on the credibility and political stability of the government. They indicated that a working example was India whose government-owned banks brought no significant changes in the quality of corporate governance strategies. The Basel Committee (1999) also added that government shareholding in domestic banks had potential to alter the banks policies and the overall corporate governance structure thereby enhancing the corporate governance practices. This was because
with government shareholding, banks had little overall autonomy by thereby were forced to follow directives from the government.

On the other hand, Banaji and Mody (2001) in a study of the Indian economy established that domestic banks without government shareholding had no incentive to introduce sound corporate governance principles. They indicated that the principal agency problem flourished in these banks.

Simanjuntak (1999), in a study of the East Asian economy, particularly Indonesia, observed that deregulation during the period of 1983 to 1997 saw an increase in the number of domestic banks from 63 to 144, government-owned banks also expanded their operations. He however, highlighted that these institutions were deeply characterized by principal-agency problems and management opportunism through information asymmetry. The severity of the principal-agency problem and opportunism greatly contributed to the Indonesian crisis. Of the 144 domestic banks, 16 were liquidated while the rest were restructured based on their levels of capital adequacy ratio.

Meyerman (1999) in a similar study in East Asia, particularly in Thailand, Korea and Malaysia established that the financial crisis was partly a result of domestic banks with and without government shareholding having non-transparent accounting systems, weak minority shareholder rights and control through a small group of individuals. Meyerman (1999) further indicated that in Korea and Malaysia domestic banks held 90% of corporate debt while in Thailand they held 50% of the debt reflecting the large contribution to the financial crisis by domestic banks through bankruptcy. He detected that the crisis led to capital flight through to loss of confidence by investors. Meyerman (1999), in his study recommended a comprehensive approach to corporate governance by domestic banks. Among his recommendations were protection of shareholder rights, development of improved accounting standards and presence of sound banking regulations.

Corporate Governance and Bank Performance (Success/Failure)

Gompers et al (2003) did a study in the United States incorporated companies and established that; companies with better corporate governance strategies in terms of stockholder rights had returns that were 8.5% more than those with weak rights. Although the scores of shareholders' rights alone were not adequate to improve firm performance, it was proved that scores of board effectiveness had contributed to enhanced firm performance. Also, in an investigation by Klapper and Love (2002) for the emerging stock markets it was established that sound corporate governance was highly correlated to better operating performance and higher market valuation. Firm performance was measured using Tobin’s Q which is the ratio of market value to book value of a firm.

Mangen and Tauringeana (2006) studied the relationship between quality of corporate governance and firm profitability for the Zimbabwe Stock Exchange Listed Companies. The results revealed that firm performance was positively related to the standards of corporate governance. They concluded that sound corporate governance strategies were required especially for companies operating in unstable economies like Zimbabwe.

In a study by Drobetz et al (2003) for the German economy it was proved that stock prices adjusted quickly to any changes in a company’s corporate governance, which revealed the importance of corporate governance to firm performance. They however, highlighted that that components of corporate governance strategies that markets pay attention to varied across countries but the most common strategy was the nature of board of directors’ composition and performance.

Laixiang (1999) studied the Chinese companies in Shanghai and established that the presence of independent directors was positively correlated to higher returns for the firms. However, a positive relationship could not be established in other corporate governance indicators like board size and shareholder activism. In contrast, Smith (1996) had reported that in a study in California shareholder activism proved to have a positive relationship to with firm performance. This view was shared by Smith (1996) who did a similar study in Sweden.

Maher and Anderson (1999) argued that if corporate governance mechanisms had no effect on firm performance then there would be no reason why most governments would show concern for enhancing their corporate governance policies. They analyzed other empirical studies and established that enhanced corporate governance mechanisms were believed to lead to improved performance basically by avoiding expropriation of controlling shareholders and ensuring quality decision making. Further, Maher and Anderson (1999) clarified, that there were different ways through which corporate governance strategies could affect a company’s performance. For instance, the principal-agency problem suggested that management was less likely to engage on profit maximizing behavior in the absence of shareholder supervision. In that light, since owner-controlled firms provided better monitoring that resulted in improved performance.

Franks and Mayer (1994) established that a large base of shareholders enabled greater effectiveness in terms
of monitoring a company by its shareholders and that such monitoring was in line with the recommended sound corporate governance policies. Effectively, shareholder supervision of a company was proved to result in increased profit levels for companies. Franks and Mayer (1994) concluded that the benefits of having a large shareholder base outweighed the costs of low diversification opportunities.

**METHODOLOGY**

The research adopted a cross-sectional survey research design. This design enabled the measuring of corporate governance practices from respondents at one point in time and it was inexpensive to run. Since this design measured corporate governance aspects at only one point in time, the research tried to overcome this drawback by seeking respondents' views concerning past events. This design was practical as the attributes of corporate governance in multinational and domestic banks were measured by means of distributing questionnaires and carrying out follow-up interviews on responses which needed clarification. The target population consisted of all commercial and merchant banks in Zimbabwe. Data from the survey was analyzed using SPSS version 16.

Due to the need to maintain confidentiality some banks officials were not at liberty to disclose some of the relevant information as required by the researcher. The researchers had to assure the respondents that the information gathered would only be used for academic purposes and the names of the banks in questionnaires will remain anonymous to maintain confidentiality.

**RESEARCH FINDINGS**

The structures of the board of directors for the two bank categories had limited differences; both bank categories had the sizes of their boards of directors increasing over the review period. The ratios of independent directors to executive directors were similar owing to the regulatory requirements. However, domestic banks proved to have more board meetings unlike multinational banks, which explained that they delegated a number of issues to board committees. In that regard multinational banks generally had more board committees than domestic banks. Correspondingly, it was established that multinational banks generally had smaller boards than domestic banks.

Transparency of accounting standards for the two bank categories was of appropriate levels as the results revealed compliance with the international accounting standards. This could be attributed to the disclosure requirements by the RBZ. However, transparency on executives' remuneration was higher in multinational banks than domestic banks.

The findings also indicated that all banks had codes of ethics, which were distributed to employees exclusively, through different methods. Multinational banks had more methods of distribution than domestic banks.

The results also revealed that both multinational and domestic banks generally agreed that directors were the most significant stakeholders in corporate governance of banks and were ultimately responsible for performance of the company. The roles of Chief Executive Officers were numerous in multinational banks unlike in domestic banks. In that regard, the roles chief executive officers proved to be of greater significance in multinational banks than domestic banks.

The motivations of sound corporate governance were established to be identical for both bank categories; however, domestic banks had fewer respondents for most motivating factors highlighted than multinational banks thereby confirming conclusions by Banaji and Mody (2001) who indicated that domestic banks had less enthusiasm for practicing sound corporate governance strategies.

The study also indicated that, in the main, multinational banks had higher share prices than domestic banks. Additionally, results on the 2004 banking crisis established that failure by the majority of troubled banks was due to poor corporate governance strategies. In that regard, multinational banks were noted to have sounder corporate governance practices than domestic banks which was in line with the RBZ’s conclusions.

Finally, the results showed that multinational banks had higher compliance levels to corporate governance requirements by RBZ than did domestic banks.

**CONCLUSIONS**

The research concluded that domestic banks had lower standards of corporate governance than multinational banks in terms of size and election of the board of directors, transparency of executives’ remuneration, principal-agency problem and distribution of the code of ethics. In addition, the comparatively better share prices by multinational banks over domestic banks implied that multinational banks had more effective corporate governance strategies than domestic banks. The research also affirmed the conclusions by RBZ (2004) that the domestic banks that were put under curatorship had corporate governance weaknesses.

Although multinational banks did not acknowledge compliance to RBZ’s requirements on corporate governance as one of the indicators of the effectiveness of corporate governance it was established that they complied with these
requirements more than domestic banks. It was noted that their home countries determined their set of regulations. Domestic banks lacked of exposure to global financial markets thus they had low levels of compliance to these requirements.

RECOMMENDATIONS
Since the research established that both multinational and domestic banks were moving towards a tendency of increasing their board sizes, it is recommended that both bank categories need to maintain relatively small sized boards of directors to enhance effectiveness of their corporate governance frameworks. In view of the fact that, executives’ remuneration was not very transparent for both bank categories, there is need for banks to ensure that they publicize these remunerations and they involve other stakeholders especially shareholders in determining such packages to develop transparency. There is need for both bank categories to distribute the codes of ethics to all company stakeholders, not only employees as established by the findings. Enhanced distribution of the codes of ethics to all stakeholders assists in educating them on the importance of sound corporate governance practices. Domestic banks in particular need to enhance their distribution of the codes of conducts through various methods since they primarily employed a single method of distributing the codes of ethics.

Domestic banks, particularly those without government shareholding, need to promote effective participation of shareholders in decision making through arranging meetings with them and ensuring that they enjoy shareholders’ rights of voting. Both banks categories need to employ a compressive approach to governance through the integration of empowerment and accountability which involve all stakeholders especially employees in multinational banks. Employee representations in board meetings will aid in promotion of transparency and loyalty thereby ensuring the long-term welfare of banks.

Since domestic banks were mostly motivated by increase in profits, great focus on a single corporate governance benefit can mislead banks as they may opt for other behaviors that can meet the same incentive of increase in profits but disregarding other benefits from sound corporate governance practices. Both banks therefore need to be fully aware of all the benefits of corporate governance, which mainly include improvement in shareholder value. Appreciation of all benefits will incentivize banks to observe high standards of corporate governance.

Domestic banks need to enhance their levels of compliance to RBZ’s corporate governance requirements. Like multinational banks, domestic banks need to employ self-regulating initiatives that outperform those required by the RBZ.

Although multinational banks seemed to have corporate governance practices, which complied with RBZ’s requirements there is still need for them to appreciate and observe RBZ’s requirements as a sufficient indicator of corporate governance in Zimbabwe. Not accepting RBZ’s requirements as a sufficient indicator of effective corporate governance may threaten compliance to these requirements in the long run. These requirements are specifically for banks operating in the Zimbabwean economy, which has unique corporate governance needs from other economies.

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