



**CORPORATE GOVERNANCE MODELS IN BUSINESS PERFORMANCE:
EMPIRICAL EVIDENCE IN PORTUGUESE COMPANIES LISTED ON EURONEXT
LISBON**

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Abstract

The last few years were marked by differences of interests in the relationships established in the organizational structure and with consequences in terms of its added value created. With this become necessary to introduce mechanisms to align interests and supervise the activities of agents, in general, and shareholders and managers, in particular. This issue intersects with the topic of models of Corporate Governance (CG) and gains relevance following the latest international financial scandals.

In this regard, and based in a sample of 48 enterprises listed on the Lisbon Stock Exchange it was sought to verify the existence of a positive association between the characteristics of the most widely used CG model in Portugal and business performance having been established 8 research hypotheses. The results obtained allowed to validate five of these research hypotheses leading to the conclusion that there is a positive association and statistically significant among the variables model of CG, size of the Board of Directors (CA), the number of independent members on the Board of Directors, existence of different people in the Board of Directors and Chief Executive Officer (CEO) role of president, independence of the CEO and business performance.

Keywords: Corporate Governance; Performance; EBITDA; PSI20.

Introduction

The uncertainty and information asymmetry raise problems of conflict of interests in the relations established in the organizational structure that affect the basic functions of the organization and its value creation potential and, at the same time, make necessary the introduction of mechanisms allowing align interests and oversee the actions of agents in general and of the shareholders and managers in particular.

The question of Corporate Governance (CG) is based in this reality. The need to study the extent to which CG systems fulfil their role in monitoring and results management has been enhanced by the recent financial and social crisis that has proliferated all over the world. In the current context there is a greater perception that the success of the business and the benefits for the agents do not rely solely on maximizing short-term profit. On the other hand, the theoretical concepts, particularly with regard to information asymmetry, have also been confirmed by the recent financial scandals, by proving that the management of organizations have an advantage over shareholders and other stakeholders in what concerns the access to information (Faria, 2013). Underlying this motivation is an agency conflict that develops because the manager has the option of taking advantage, of the flexibility of some accounting principles and results reporting rules.

It is within this problem that this study is developed, which aims seek to analyse and/or identify any kind of relationship between models of CG and business performance in Portugal.

Indeed, the work will be developed building on a quantitative methodology, using as a sample a set of 48 companies in the universe of listed companies in Portugal, and the observations concern the years 2011, 2012 and 2013. According to Ittner and Larcker (2002) this type of research may be the only way to understand the variables and the relationships established between them.

Thus, to meet the objective of the study, this work is developed in addition to this introduction and respective conclusions on three points. At first the theoretical framework in order to discuss the issue under study. In point two will be present the research methodology followed in particular the presentation of the purpose of the study and corresponding research hypotheses, sample size, data collection

and data processing techniques. Finally, the 3rd point will present the results obtained and the respective discussion.

1. Theoretical Framework

The assumption of adopting good governance practices raises and enhances the performance of companies and capital markets in view of the confidence of investors, employees and the general public about the quality of administration, supervision and on the sustainability of company (IPCG, 2014), which is equivalent to saying that a CG system is a set of practices and formal oversight processes of the executive management of a company aimed at preserving the interests of shareholders and minimize conflicts of interest among them (the shareholders) and those involved (Leal, Ferreira, & Silva, 2002). Can in turn be taken as a model that favours an environment of trust, ethics and moral, to give the CA the great mission of ensuring the interests of shareholders and simultaneously maximize the value of the company (Crowther & Seifi, 2011). It can also, in the words of Vaz (2011), be understood as a system by which companies are directed and controlled in a more legal perspective, essentially focused on issues arising from the measurement of ownership and control of companies, addressing, in particular, the relationship between shareholders and managers. It leads to the problem of distribution and control of the exercise of power steering in commercial companies, with particular emphasis on how companies should be governed.

In Portugal, for example, the last decade has been strongly marked by a significant increase in the CG that is justified by the intensification of the globalization effect and its consequences, in particular with regard to the higher requirement to the ethical standards of managers (Gonçalves, 2007), which has meant that companies with higher level of adoption of best practices in CG present the greatest value creation compared to enterprises that show less progress at this level (Davis, 2005; Gonçalves, 2007; Faria, 2013; Sardines, 2014). In this context, for Almeida Santos, Ferreira and Torres (2010) CG models must be understood as a mechanism of allocation of the rights and responsibilities of the different participants in the company (stakeholders), which

defines and specifies the rules and procedures for making decisions and provides the desired structure for defining the company's objectives and the means to achieve them. Costa and Santos (2011) confirm that the legal aspects and regulations are factors that have a significant influence because they determine the corporate management model in different countries.

In this regard, and in view of La Porta, Silanes and Shleifer (2008), the legal and judicial system is nothing more than the ability of the law to ensure the protection of financial investors regarding the expropriation of which they may be targets by managers or major shareholders. It is an element of great influence and justifies largely the financial policy and corporate capital structure. The current legal, civil law and common law, give expression to two large systems, the continental system and the Anglo-Saxon system, which support the main existing CG models (Batista, 2009). In turn, Djankov, La Porta, Lopes-De-Silanes (2008) argue that countries with a legal system based on common law have a more convincing legal protection system, compared with civil law, and prove to be, in relative terms, more demanding in terms of disclosure of information and have a greater openness to permit small shareholders to be able to demonstrate the existence of unlawful conduct (Hope et al., 2011).

Aspects of sociocultural nature, regulations and institutions, form or determine the model of CG which will prevail in a more or less generalized way in each country. These aspects determine the relationship between the managements of the companies and their shareholders and other groups and that, according to the countries where they are applied, have different features and developments. In this circumstance it is possible to identify different models of CG, including the Anglo-Saxon model, German, Japanese, Latin European or monistic and Latin American. Large part of models and CG processes make use of monitoring and analysis tools for making managers' decisions on shareholders and management to minimize the agency conflicts and optimize the economic and financial results of the company and contribute to their continuity (Arruda, Madruga & Júnior, 2008; Sardinha, 2014). Despite the focus being on shareholders (majority or minority) or in other stakeholders Fernandes (2014) has argued that what in most cases is demanded is to reconcile the CG mechanisms in order to minimize agency costs acting simultaneously with the contractual nature of mechanisms

that lead to an efficient allocation of resources. It is within this problematic that is advocated the selection of CG mechanisms that are not only able to ensure an efficient allocation of resources as an aid in reducing agency costs, based on a set of contracts based on maximizing assumptions utility by agents and the separation of ownership and management (Gillan & Starker, 2003; Duarte, 2007; Almeida Santos, Ferreira & Torres, 2010).

2. Research Methodology

This study aims to evaluate the relationship between the characteristics of CG models and performance of Portuguese companies listed on the Lisbon Stock Exchange. In this line and to meet the main objective of the study were established the Research Hypotheses (HI) that are presented in the following table.

Table 1: Research hypotheses and expected results.

HI	Hypothesis formulation	Expected result
HI ₁	There is a positive association between the pattern of CG and business performance	Relation (+)
HI ₂	There are differences in relating to business performance based on the CG model used	Existence of Differences

It should be noted that the study population included the 57 companies posted on the Euronext at 31 December 2014. But, to meet the goal we used a sample of 48 listed companies of Lisbon stock exchange in the period from 2011 to 2013, the choice of the listed companies is related to the fact that CG practices are mostly adopted within the listed companies, based on the entrepreneurial characteristics of each country or region (Batista, 2009). Were excluded 9 companies in the study with the following characteristics:

- a. Different accounting year (SAD) (3 companies: *Sport Lisboa e Benfica*, *Futebol Clube do Porto* and *Sporting Club de Portugal*);
- b. Financial Companies without information in Annex (3 companies: *Banco Santander*, *Espírito Santo Financial* and *Montepio*); and

- c. Non-financial companies without information in Annex (3 companies: *Estoril Sol P, Isa and Inapa Pref S Voto*).

The data that supported this study were collected based on a query of the Annual Reports and CG Reports of 48 Portuguese limited liability companies, financial and non-financial listed on the stock exchange in Lisbon, published on its website and in the CMVM website.

After the collection of data and for its treatment it was made an exploratory descriptive analysis and inferential analysis. The aim was to initially understand the behaviour/characterization and evolution of the variables that were studied, so it is produced on the one hand, the absolute and relative frequencies. For the second phase and to support the research hypotheses set was decided to recourse to an inferential analysis.

Should be noted further that for the production of inferential analysis was taken into account the following:

- (i) produced the t-Student parametric test for two independent samples in order to check for differences between two CG models, the Anglo-Saxon and Latin/monist in relation to business performance since they meet the conditions for the test use;
- (ii) to analyse the association between qualitative variables, according their nature and scale in which are measured (nominal and ordinal), is intended to apply the nonparametric tests of association, including the Phi test to measure the degree of association between the variables and its direction.

It should be stressed that we will work only with the Anglo-Saxon CG models and Latino/monist. It was chosen to work with only these two models as the use of the Germanic/dualist CG model was not significant. It is noted that it was decided to use EBITDA to measure business performance. The option has to do with the fact that it is an easy indicator and used for the analysis of the origin and composition of the results of companies by eliminating the effects of financing decisions, i.e. it is able to more accurately measure productivity and business efficiency (Aranha, Oliveira & Dias, 2014). EBITDA is an indicator that includes all the operational components and thus includes much of the earned revenue

and expenses incurred, allowing highlight its extent in relation to the net result in the observation of business performance (Saporito, Henrique & Silva, 2015).

In all the analysis for the validation of decision-making or not of the research study it will be taken a significance level of 5%.

3. Presentation and Discussion of Results

3.1. Sample Characterization

To carry out this study it was taken the identification of the Portuguese entities listed on the Lisbon stock exchange, as at 31st December, for each of the relevant financial years (2011-2013).

Regarding the characterization by sector of activity, which meant the classification adopted by the NYSE Euronext, it can be said that the sectors with greater weight are as follows: about 18.75% are companies in the industrial sector; 14.58% are part of the information and communication sector and 12.5% are of the financial sector. The sectors that have less are as follows: about 8% are companies that are part of the energy sector, and the same percentage for the technology industry and construction, about 4% of the companies are part of the automotive sector and 4.17% of the goods and the consumer sector. The real estate, distribution, health, logistics and telecommunications, services, transport and tourisms are those who have a lower weight, 2.08% respectively.

Regarding the CG model and based on the results obtained it was concluded that:

- i. The CG model adopted and that predominates in Portugal in the companies under study and for three financial years is the Latin/monist model, with a 72.92% registration (35 companies out of 48). The Anglo-Saxon model is the second most widely adopted model, with 22.92% (11) in 2011 and 25% (12) in 2012 and 2013. The German/dualistic model in 2011 was adopted by only 4.17% (2) companies (Orey Antunes and BCP) in 2012 and 2013 by only one (BCP);
- ii. By the results obtained in 2011, about 18.8% (9) of the companies had a CA consisting of a number less than 5 members, 39.6% (19) of the

companies have between 6-10 members in CA and 8.3 % (4) of the companies had a CA consisting of a number greater than 21 members. In the year 2012 the number of companies with fewer than five members in the CA remained, but about 41.67% (20) companies had in CA about 6-10 members and 16.67% (8) companies had the CA composed by over 21 members. In 2013 fewer companies had CA composed of a number less than 5 or more than 21 members (12.5%) and about 41.67% (20) had in the Ca companies about 6 to 10 members;

iii. In 2011 about 46% (22) of the companies had no independent members in CA and only 2.08% (1) had more than 11 independent members in the CA. In 2012 and 2013 about 42% (20) and 44% (21), respectively, had no independent members in its CA. Still, it can be said that mostly the CA of the companies in the study were composed of more than two independent members.

3.2. Validation of Research Hypotheses

In order to respond to the 1st research hypothesis '*There is a positive association between the pattern of CG and business performance*', could observe by the results that the Phi correlation coefficient obtained was 0.31 with a p-value=0.722 (Table 2). Thus, it can be concluded that there is a positive and direct association between the variable model of CG and EBITDA, although weak. This association was not statistically significant (p-value greater than 0.05 significance level) however the model of CG is associated with business performance (EBITDA), but not validate the hypothesis because the p-value is not significant. This result is in line with the studies of Morck, Wolfenzon and Yeung (2005), Cunha and Martins (2007), Reis (2013) and Ferreira (2013). These authors found that there is a direct positive association, but not statistically significant between the variable models CG and business performance (EBITDA).

For the 2nd research hypothesis '*There are differences in relating to business performance based on the CG model used*', was applied to the t-Student test where one might conclude that there is sufficient statistical evidence to confirm the presence of significant statistical differences for the business performance

based on the type of CG model used (CG Anglo-Saxon model or CG Latino/monist model) ($p\text{-value}=0.035$ less than the significance level assumed) (Table 2). That is, the average business performance using the CG Anglo-Saxon model is different from the average business performance using the CG Latino/monistic model. This result is consistent with that obtained by Garner and Kim (2010), Piccoli, Sousa and Silva (2014) and Ferreira (2013), who have found that there are statistically significant differences with respect to business performance variable and the use of CG models . By the presented is validated the research hypothesis.

Table 2: Results of statistical tests to validate the research hypothesis.

Research Hypotheses	Test	Test value	p-value
<i>H1: There is a positive association between the pattern of CG and business performance</i>	<i>Phi</i>	0,31	0,722
<i>H2: There are differences in relating to business performance based on the CG model used</i>	<i>t-Student</i>	2,175	0,035

The following table presents a summary of the results expected and obtained for each established research hypothesis as well as the decision concerning the respective validation.

Table 3: Summary of expected and obtained results for each research hypothesis.

Research Hypotheses	Result		Validation
	Expected	Obtained	
<i>H1: There is a positive association between the pattern of CG and business performance</i>	Relation (+)	Relation (+)	Not Validated by not showing a statistically significant association
<i>H2: There are differences in relating to business performance based on the CG model used</i>	Existence of differences	Existence of differences	Validated

Conclusions, Limitations and Future Research Lines

The need to study the extent to which CG systems fulfil their role in monitoring and management results has been enhanced by the recent financial and social crisis that has proliferated all over the world. In the current context there is a greater perception that the success of the business and the benefits for the agents do not rely solely on maximizing short-term profit.

The main conclusions to be drawn from the work done, and which we list, are the following:

1. Companies tend to adopt the Latin/monistic model;
2. There is a positive and direct association between the variable model of CG and EBITDA, although weak. As this association was not statistically significant it can only be concluded that the CG model is associated with business performance (EBITDA) but not more than that, that is not valid to H1 hypothesis concerning the existence of a positive association between the model of CG and business performance because the probative value is not significant. This result is in line with the theory (Morck et al., 2005; Cunha & Martins, 2007; Reis, 2013 and Ferreira, 2013);
3. That there are differences relating to business performance based on the use of the CG model. The results show that there is sufficient statistical evidence to be able to confirm the presence of statistically significant differences in relation to business performance based on the type of CG model used. This result confirms H2 and corroborates the theory (Garner & Kim, 2010; Ferreira, 2013).

It should be noted that throughout the conduction of this study, it was subjected to some limitations, so, the findings presented here should be interpreted in the context of these same limitations and which relate essentially to the small sample size which leads to the use of statistical techniques not so robust.

However, if the sample size is a limitation it presents itself also as the suggestion basis for the development of future investigations. It is suggested, for example, the development of works to the same purpose but with a more representative sample and the use of other statistical methods, capable of imparting greater

resistance to analysis and to allow another reach to the conclusions drawn. Also analyse the impact of corporate governance on business performance, using an econometric model that best fits the data collected.

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