CORPORATE GOVERNANCE AND FOREIGN PORTFOLIO INVESTMENT IN SAUDI ARABIA

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ABSTRACT

A corporate governance system has been designed to ensure efficient operations of companies on behalf of shareholders. Good practices of corporate governance principles and high protection of investors would attract foreign portfolio investment. This study aims to investigate the effect of corporate governance mechanisms (i.e. board size, board independence, audit committee size, audit committee independence and firm age) on foreign portfolio investment in Saudi listed firms for the year 2010. This study is significant due to the lack of empirical evidence regarding the field of corporate governance and foreign portfolio investment in Saudi firms since the Saudi code of corporate governance has been enacted in the late 2006. The results of the study show that board independence and audit committee independence are associated with foreign portfolio investment in Saudi listed firms. However, the corporate governance mechanisms, i.e. board size, audit committee size and firm age had no impact on foreign portfolio investment.

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CHAPTER ONE

INTRODUCTION

1.1 Background of the Study

Corporate governance has been a common issue in recent years. It started in 1992 in the UK with the Cadbury Committee Report. This Report, on corporate governance, was the output of many high profile companies that were concerned, mainly, with weak protection of shareholders against the self-interests of managers and directors. In response to the corporate scandals, the US Congress approved the Sarbanes - Oxley Act on July, 2002; this Act aimed to enhance the practice of corporate governance and make it more transparent to shareholders and any users of financial reporting. In addition to this, and according to Organization for Economic Development (Kimberly, 2002), foreign portfolio investments might also assist the home capital market by way of the creation of advanced implementations and methods to observe the portfolios. For example, financial reporting users and shareholders can utilize futures, options, swaps, hedging instruments, etc., to manage portfolio risk. This can be conducive to domestic markets, by improving risk management opportunities for all investors. Foreign portfolio investment can help strengthen and improve the functioning of domestic capital markets, hence bringing about better capital allocation and a healthier economy. Open markets also avail opportunities to foreign investors to diversify their portfolios, improve risk

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