



**CORPORATE GOVERNANCE AND
FOREIGN EQUITY OWNERSHIP IN
MALAYSIAN COMPANIES**

By:

Zaimah Abdullah

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School of Business and Economics

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ABSTRACT

In the aftermath of the 1997/1998 Asian financial crisis, there are signs that in Malaysia, corporate governance practices are gradually converging towards the Anglo-American model. Drawing on three key theoretical lenses, namely agency theory, institutional theory and resource dependence theory, this study investigates an unexplored phenomenon in corporate governance reformation, at least in the context of Malaysia. The study examines the relationship between corporate governance elements and the level of foreign equity ownership (FEO) in Malaysian public listed companies (PLCs). More specifically, the aim of this study is to answer the following research question - *Does corporate governance influence the level of FEO in Malaysian companies?*

In the context of this study, corporate governance is taken to be the aggregate of board of directors' characteristics, directors' attributes and ownership structure. On the other side of the equation is FEO, which is taken to be the proportion of equity owned by foreigners. The majority of foreign investors who are making investments in Malaysia originate from Western countries, and are accustomed to the Anglo-American corporate governance system.

Thus, this study examines the influence of governance mechanisms in attracting foreign investors in a unique governance context following a major economic event i.e. the Asian financial crisis of 1997/1998. Accompanied by institutional theory and resource dependence theory, agency theory is used as the key lens to explain the hypothesised relationships. The study's hypotheses are tested using the panel data derived from 1,836 observations over a 12 year period, from 2000 through 2011. By considering the existence of heteroscedasticity and the serial correlation problems, the generalised least square (GLS) method was employed to estimate the model. To enrich the findings, logistic regression analysis was further applied and the potential endogeneity issue was resolved with a GMM test.

The findings indicate that the level of FEO in Malaysian PLCs is significantly related to foreign directorships, the Western educational background of directors, professional directors, and multiple-directorships. However, the results defy the significant relationships of board size and outside directors, as generally proposed in the extant literature. In addition, the role of ownership structure is important in foreign investors' behaviour, since it is found that foreign investors avoid investing in family-controlled companies and in companies with high institutional ownership. Therefore, from the overall results of this study, it can be concluded that there is evidence that corporate governance mechanisms do influence foreign investors' decision making, at least in Malaysian PLCs.

The implications of this study are discussed in terms of the relevant literature, theory, methodology and practice. In brief, this study has great potential impact in many respects including its relevance for policymakers in setting up new policies, designing new rules and strengthening existing regulations, both at country and firm levels.

Keywords: *Corporate governance, foreign ownership, foreign investment, Malaysian companies.*

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LIST OF ABBREVIATIONS

ACCA	-	Association of Chartered Certified Accountants
AFC	-	Asian financial crisis
AGM	-	Annual General Meeting
BNM	-	Bank Negara Malaysia
CA	-	Chartered accountant
CCSA	-	Certification in Control Self-Assessment
CDS	-	Central Depository System
CFA	-	Certified financial analysis
CIMA	-	Chartered Institute of Management Accountants
CPA	-	Certified public accountant
CMA	-	Certified Management Accountant
CMDF	-	Capital Market Development Fund
CMP	-	Capital Market Master Plan
EGM	-	Extraordinary General Meeting
EMIS	-	Emerging Market Information Service
EPF	-	Employees Provident Fund
FCCs	-	Family-controlled companies
FCCG	-	Finance Committee on Corporate Governance
FDI	-	Foreign direct investment
FE	-	Fixed-effects estimation
FEO	-	Foreign equity ownership
FPLC	-	Federation of Public Listed Companies
FRS	-	Financial Reporting Standard
FSMP	-	Financial Sector Master Plan
GAAP	-	Generally Accepted Accounting Principle
GDP	-	Gross Domestic Product
GLCs	-	Government link companies
GLS	-	Generalised least square
GMM	-	Generalised method of moments
GNP	-	Gross National Product
HCSE	-	Heteroscedasticity Consistent - Standard Error
IAS	-	International Accounting Standards

IBR	-	Grant Thornton International Business Report
ICA	-	Industrial Coordination Act
IFRS		International Financial Reporting Standard
IIAM	-	Institute of Internal Auditors Malaysia
IIF	-	Institute of International Finance
IMF	-	International Monetary Fund
KLSE	-	Kuala Lumpur Stock Exchange
LSE	-	London Stock Exchange
MASB	-	Malaysian Accounting Standard Board
MCCG	-	Malaysian Code on Corporate Governance
MIA	-	Malaysian Institute of Accountants
MIBA	-	Malaysian Investment Banking Association
MICG	-	Malaysian Institute of Corporate Governance
MICPA	-	Malaysian Institute of Certified Public Accountants
MICSA	-	Malaysian Institute of Chartered Secretaries and Accountants
MID	-	Malaysian Institute of Directors
MSWG	-	Minority Shareholders Watchdog Group
MTA	-	Multi-theoretical approach
NEP	-	New Economic Policy
NFCC	-	Non-family-controlled companies
NIA	-	National Income Account
NIS	-	New institutional sociology
OECD	-	Organisation for Economic Co-operation and Development
OLS	-	Ordinary least squares
PLCs	-	Public listed companies
RE	-	Random-effects
REITs	-	Real Estate Investment Trusts
ROA	-	Return on assets
ROE	-	Return on equity
RDT	-	Resource dependence theory
SC	-	Securities Commission
SD	-	Standard deviation
SOX	-	Sarbanes-Oxley Act
VIF	-	Variation inflation factors

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CHAPTER 1

INTRODUCTION AND BACKGROUND

1.1 Introduction

This chapter introduces and lays down the foundation for the work that follows in the thesis. In essence, this thesis focuses on elements of corporate governance in relation to foreign equity ownership (FEO) in Malaysian public listed companies (PLCs). The study of corporate governance in Malaysian companies is not considered to be something new. However, this study offers insights from different theoretical perspectives, examining the drivers of FEO, instead of the measurements most commonly used in corporate governance study – i.e. performance variables (ROA, ROE etc.).

In examining the behaviour of foreign investors when making investments in Malaysian PLCs in relation to corporate governance determinants, a different approach is needed. The majority of foreign investors, originating from Western countries, are accustomed to the established set of corporate governance codes of conduct that have become prevalent in their countries. In addition, foreign investors from developed capital market share similar values with each other, which dictate the direction of their decisions. These particular features trigger the focal point in this study, which is to scrutinise the behaviour of foreign investors when making investment decisions in countries with a different corporate governance institutional background. This study focuses specifically on the Malaysian context.

The scope of the research is essential in the context of the so-called “Americanization” (Djelic 2001) of corporate governance. Americanization is the term used to portray the process of convergence towards the American market based

system, which is transparent in its distinctive characteristics such as its diffuse¹ shareholders, strong protection law for minority shareholders, liquid stock market, emphasis on the importance of an efficient board of directors, including outside directors, etc. (Dore 2000).

Corporate governance in Malaysia is claimed to be undergoing a transformation, especially in the aftermath of the Asian financial crisis 1997/1998 (AFC), moving towards the Anglo-American corporate governance practice. This convergence process, however, is seen as difficult, especially in terms of the ownership structure of firms. The resistance to or divergence from Americanization is alleged to be due to a variation in values, cultures, traditions and practices across countries.

In this study, a multi-theoretical approach is used. Agency theory is not the only theory that is applied to explain the variation of foreign investors' behaviour when making investment decisions in different corporate governance institutional settings. It is accompanied by institutional theory and resource dependence theory (RDT), later abbreviated as the multi-theoretical approach (MTA). The use of multiple theories in explaining foreign investors' behaviour seems practical and sensible, as a clash of two institutional backgrounds is witnessed in this study. Thus, by utilising the MTA, this study seeks to explain the impact of corporate governance mechanisms (board of directors and ownership structure) on the level of FEO in Malaysian PLCs.

In summary, while Section 1.1 offers some snapshots of the underlying study, Section 1.2 provides the research background and puts forward some related issues in the corporate governance field which then leads to the engagement of this study. The scope of the study is highlighted in Section 1.3. These discussions establish the impetus for the research objectives set in Section 1.4, which then relates to the research questions in Section 1.5. Next, Section 1.6 outlines the research methodology in brief and finally, Section 1.7 provides an overview of the thesis.

¹There are many small shareholders, but none of them have a significant level of control (Peng 2006).

1.2 Research Background and the Motivation of the Study

This section offers a discussion of the research background. By gaining a thorough understanding of the research context, the rationale for conducting this study can be better understood. Many factors have combined to form the motivation behind this study, particularly in the Malaysian setting. Therefore, this section is organised in such a way that each of the essential factors is given, accompanied by its individual motivation for conducting the study.

First, one of the main motivations for conducting this study is the uniqueness of Malaysia as a setting to examine the association between corporate governance determinants and foreign investors' behaviour. Malaysia can be classified as a country whose governance system represents neither the shareholder system of the US and UK (Shleifer and Vishny 1997) nor the stakeholder system of Japan and Germany (Hall and Soskice 2001). The uniqueness of this Asian country lies in its weak legal environment and its poor governance system (Johnson, Boone, Breach and Friedman 2000), besides its high level of concentrated ownership, with controlling owners (La Porta, Lopez-de-Silanes, Shleifer and Vishny 2000) cross holding and pyramiding (Claessens, Djankov, Fan and Lang 1999; Haniffa and Hudaib 2006; Liew 2007; Lim 1981).

In addition to these special features, the institutional context of Malaysia, at the height of corporate governance reform following the AFC 1997/1998, provides a rich setting to be explored. By utilising an institutional perspective, the adoption of new corporate governance legislations and codes can be regarded as a reaction to radical changes from the external environment (AFC 1997/98). These characteristics are shared with other adversely affected countries simultaneously, thus contributing to the generalisation of the research findings. Clearly, this study will also benefit other emerging countries. At the same time, a comparison can be made with the developed countries and justifications can be derived to explain the differences.

Apart from the above motivations, there is another intriguing factor that can substantiate the decision to choose Malaysia as an ideal setting to examine the issue. It

is generally known that Malaysia's corporate environment has always been influenced by government intervention, policies and regulations (Suto 2003). The political pressure in Malaysia's economy to business players is not something new, albeit they are closely intertwined with each other (Gomez 1994). There are companies in Malaysia, known as government link companies (GLCs) that are very close to government policies. In 2009, for instance, GLCs dominated nearly 40% of the total market capitalisation in Bursa Malaysia. The relationship between the Malaysian government and the GLCs is reciprocal, such that both parties benefit from the connection. Therefore, when the Malaysian government decided to initiate a reformation of the corporate governance system, the GLCs were directly involved. They represent the giants and the PLCs in the Malaysian market. In this study, their reactions are gauged by the choice of corporate governance determinants.

Secondly, in relation to the AFC 1997/1998, many arguments arise which attempt to explain the impetus of the crisis (see Section 2.3.1 The Asian Financial Crisis 1997/1998). Principally, all the arguments lead to one identical premise – the loss of confidence of local and foreign investors in the emerging markets (Johnson et al. 2000). Nevertheless, it is intriguing to understand why the loss of confidence had a huge impact on the exchange rate and the stock market of certain emerging markets but not on others. One of the more persuasive explanations for this is provided by Johnson et al. (2000), who claim that the weakness of the legal institution and corporate governance were the decisive factors that contributed to the stock markets declining at the pinnacle of the AFC 1997/1998. Further, Mitton (2002) argues that although initially the weakness of corporate governance was not the cause of the AFC 1997/1998, once the crisis began, the dysfunctional corporate governance system could have exacerbated the crisis. Without efficient corporate governance practice the countries affected became more vulnerable to financial crisis.

The estimated loss can be depicted by the reversal flows of investors' funds in Table 2.2, and well documented cases illustrative of expropriation by managers in the countries affected by the Asian crisis can be found in Table 2.3. It is alleged that in most expropriation cases, the controlling shareholders did not violate any local law to

accomplish their unethical ends. Moreover, in most emerging countries, the management is also the controlling shareholder (Haniffa and Hudaib 2006; Mat Nor and Sulong 2007), misconduct and expropriation of minority shareholders are easier to achieve (Johnson et al. 2000; Khatri, Leruth and Piesse 2002).

Ho and Wong (2001) assert that following the AFC 1997/1998, most Asian countries endeavoured to strengthen their corporate governance system, enhance the transparency of their reports and increase the level of disclosure. Likewise, Haniffa and Hudaib (2006) claim that a Code of Corporate Governance was established in most of the affected countries in order to increase the level of investors' confidence and ensure the continuous flow of funds to the respective capital markets. A consideration of the significant amount of flow reversal and many well documented cases of expropriation (Johnson et al. 2000; Mitton 2002; Radelet and Sachs 2002) strengthens the need for a study that examines the relationship between corporate governance and investors in emerging countries. Indeed, there is dearth of such studies in the extant governance literature.

Third, as stated beforehand, the implications of AFC 1997/1998 in the affected countries are numerous. In fact, crisis had an impact not merely on the economy itself, but on other aspects as well, such as the corporate governance system. Prior to the crisis, Liew (2007) claims that corporate governance practices in Malaysia were not a matter of concern. According to the report from the World Bank (1993), it was asserted that East Asian countries (including Malaysia) had their basic rights and freedom to determine the direction of their economic management, governance system and public institution. However, this view changed dramatically after the AFC 1997/1998, when corporate governance came to be seen as an expedient way of managing the financial crisis (Haniffa and Hudaib 2006; Liew 2008).

Malaysia, as one of the badly affected countries, is claimed to be suffering the consequences brought about by the country's inefficient corporate governance and the lack of transparency in its financial system, which has led to the erosion of investors' confidence (Noordin 1999). In brief, before Malaysia was struck by the financial

turmoil of 1997, during the period 1987-1996, Malaysia's economy was undergoing remarkable growth. The interest shown by foreign investors in the Malaysian capital market meant that this was fuelled by their capital inflow. Foreign direct investment (FDI) helped to push the average annual growth of the Gross Domestic Product (GDP), and the increase was recorded at 8 per cent. On the other hand, foreign portfolio investment had buoyed the Kuala Lumpur Stock Exchange (KLSE)² composite index up to about 1,300 points, and the market capitalisation reached RM900 billion. However, in the aftermath of the AFC 1997/98, the Malaysian capital market was shunned by foreign investors. Consequently, foreign portfolio investment plummeted by 74 percent, from RM144.9 billion in 1996 to RM37.6 billion in 2001. Further details can be found in Chapter 2, Section 2.3.1 The Asian Financial Crisis 1997/1998.

In addition, the collapse of a few giant companies in Malaysia during the crisis such as Perwaja Steel, Transmile and Technology Resources Industries (TRI), amongst others, is also seen to have emanated from the weakness of the corporate governance system (Khas 2002; Khatri et al. 2002; Kim 1998; Samad and Wilson 2002). Besides this, Mohamad (2002) adds that poor corporate governance, a low level of transparency in disclosing company information, weak investor relations, the ineffectiveness of regulatory agencies in enforcing legislation to punish offenders and protect minority shareholders have to some extent contributed to the collapse of the giant companies. Realising this fact, the Malaysian government has taken prompt action and developed a salvage package to improve the structures of corporate governance in the country (Haniffa and Hudaib 2006).

Therefore, the years following the AFC 1997/1998 are known as the years of corporate governance reformation. It is claimed that there are signs that corporate governance in Malaysia is gradually converging towards the Anglo-American model, especially in the aftermath of the 1997-1998 AFC (Haniffa and Hudaib 2006). The Malaysian government has played its role diligently to regain investors' confidence.

²Recently known as Bursa Malaysia

An earnest effort exhibited by the Malaysian government to improve the corporate governance system in the country can be seen in the establishment of a few formal institutions to take charge of the affairs of corporate governance – e.g., the Finance Committee on Corporate Governance (FCCG), the Malaysian Institute of Corporate Governance (MICG), and the Minority Shareholders Watchdog Group (MSWG). New legislations and Codes have also been formulated. These have portrayed the intense effort taken by the Malaysian government to imitate the best practice of the corporate governance systems of the developed economies such as the Anglo-American model.

From the institutional perspective, this convergence process is known as the “Americanization” of corporate governance (Djelic 2001). Hansmann and Kraakman (2001), for example, claim that the capital market around the world is converging towards the Anglo-American model as it is claimed that this model is a good model and is slightly different to other governance practices in other countries (Shleifer and Vishny 1997). In fact, the new environment of institutions, with the tightening of legislation that pervades corporate governance practice from the end of AFC 1997/1998, has not been sufficiently explored in the recent literature. Thus, this research will try to explain this unique situation in depth with the help of relevant theory.

Fourth, in relation to this study, it has long being noted by many scholars, (e.g. Dunning 1993; La Porta, Lopez-de-Silane and Shleifer 1999) that corporate governance is one of the most important tools for attracting foreign investors. Therefore, studies to comprehend this association are of great importance. As such there is a need to understand how corporate governance impacts on the behaviour of foreign investors when making investment decisions in countries with a different institutional background. Such an appeal suggests a focus on several corporate governance mechanisms, including ownership structure and board characteristics (Chung and Zhang 2011). Thus, the desire of this study is to close this loophole by allowing more dimensions of the corporate governance determinants to be examined in one comprehensive model.

Fifth, in this study corporate governance mechanisms are associated with a distinctive dependent variable, i.e. FEO. Given the growing significance of foreign financing and the fact that access to foreign capital may be unequal across firms and countries, it is important to understand more fully the factors that make investors shy away from providing capital to foreign firms (Leuz, Lins and Warnock 2010). It is argued that domestic sources of outside funding are limited in many countries around the world (Giannetti and Koskinen 2010). In response, many capital markets have been liberalised, and foreign capital has become an increasingly important source of finance (Bekaert, Harvey and Lumsdaine 2002).

Foreign investment is not only important to the companies, but also, this kind of flow helps to finance investments and stimulate economic growth in a country (Suhejla 2010). It is also widely held that foreign investment is a mechanism for improving corporate governance, firm performance and profitability (Bokpin and Isshaq 2009). Leuz et al. (2010), however, argue that only selective companies are able to attract foreigners to invest and inject capital into their companies. A number of articles (e.g. Aggarwal, Klapper and Wysocki 2005; Dahlquist and Robertsson 2001; Kang and Stulz 1997; etc.) have noted that there are certain attributes and criteria that contribute to this event.

Besides this, the empirical evidence concerning the main causes of international capital flows is in general mixed (Hoti 2004). Various factors influence the decisions of foreign investors, whether at a country level or a firm level. Thus, this research extends the previous findings and contributes to knowledge at a firm level by exploring new variables in relation to corporate governance and foreign investors in the unique setting of Malaysian firms.

Sixth, even though there is voluminous research on this particular issue, this study finds that the loopholes are worthy of investigation. Past studies on corporate governance and FEO tend to focus on developed markets (i.e. Kang and Stulz (1997) on the Japanese market, Aggarwal et al. (2005) on the U.S market, Dahlquist and Robertson (2001) on the Swedish market, etc.). Nevertheless, some of the latest

studies on the issue of the corporate governance impact on FEO are those conducted by Bokpin and Isshaq (2009) on the Ghana Stock Exchange (GSE), and by Douma, George and Kabir (2006) on Indian listed corporations. Both are considered as emerging markets. However, there is still a dearth of related literature from other emerging markets, with the exception of the Korean setting, as this country is well covered in a number of research studies, given its unique setting with *Chaebol*³ firms (e.g. Baek, Kang and Suh Park 2004; Kim et al. 2010; Chizema and Kim 2010).

However, the remaining countries that were badly affected by the AFC 1997/1998, especially those from Southeast Asia, have been given less attention in this area, including Malaysia. It is worth pointing out that even though a few studies of foreign ownership have been carried out in certain emerging countries, for instance on the Taiwan stock market by Lin and Shiu (2003) and on the Indonesian capital market by Rhee and Wang (2009) etc., their studies examine the relationship of foreign ownership with other dependent variables, such as a company's financial characteristics (liquidity, ROE, book to market ratio, etc.).

At this point, there is less empirical evidence that attests to the idea that the international capital inflow is associated with corporate governance practices in the emerging markets. Mangena and Tauringana (2007) discovered that much of the empirical literature on the corporate governance impact on foreign investment has focused on developed capital markets, and most of the research has studied the impact of corporate governance alone. Hence, there are many outstanding issues related to the unfinished business of examining this relationship more fully. Thus, this study focuses on the developing market, based on the unique characteristics of Malaysia.

³The chaebol are the large, conglomerate family-controlled firms of South Korea characterized by strong ties with government agencies. The name, which means business association, is properly pronounced jay BOL but the spelling pronunciation chay bol is considered acceptable by Korean speakers.

Empirical evidence claims that foreign investors avoid investing in developing countries because of the weak corporate governance structure and disclosure (Gibson 2003; Johnson et al. 2000; Mangena and Taurigana 2007; McKinsey and Company 2002). This is echoed by the findings of Aggarwal et al. (2005), who suggest that firms with better accounting quality and corporate governance attract more foreign capital. It is widely believed that corporate governance generates investor goodwill and confidence (Bokpin and Isshaq 2009). A considerable numbers of previous studies (e.g. La Porta et al. 1999; Shleifer and Vishny 1997) have associated weak corporate governance with developing countries. Recent studies (Leuz et al. 2010; Kim, Eppler-Kim, Kim and Byun 2010) consistently claim that poor corporate governance is one of the factors that draws considerable attention from outside investors and regulators. In addition, Dahlquist, Pinkowitz, Stulz and Willianson (2003) also suggest that there is a close relationship between corporate governance and the portfolio composition held by foreign investors. Kim et al. (2010) have argued that the valuation effects of corporate governance may differ between foreign investors and local investors, as the former group assigns higher monitoring costs in comparison to the latter group, and therefore may discount corporate governance more severely than domestic investors. Much of the empirical literature on the impact of corporate governance has focused on the developed capital markets (Mangena and Taurigana 2007). This presupposes that there is a dearth of literature from the emerging markets, e.g. from Malaysia.

Next, it is alleged in many studies (e.g. Chizema and Kim 2010) that most of the studies on corporate governance have utilised agency theory as the theoretical lens. Others have used resource dependence theory (Douma et al. 2006). However, it is argued that the insights from these theories are unlikely to provide sturdy justifications (Eisenhardt 1989; Oliver 1997) when there is clash of institutional background (developed market versus developing market), as revealed in this study. Foreign investors, who generally originate from Western (developed) countries, find it difficult to make investments in developing capital markets, as they have certain embedded values which dictate their decisions. Thus, the inclusion of institutional

theory is claimed to be the ideal to explain the behaviour of foreign investors when making decisions about investing in the Malaysian capital market.

This study, however, advocates that multiple theories should be employed (agency theory, institutional theory and resource dependence theory). The combination of these three theories may provide strong justifications to explain the reactions of foreign investors. Besides this, to my knowledge, there is no research study that offers this kind of approach to explain the association between corporate governance mechanisms and foreign investors' investment behaviour. This approach is concomitant with the recent trend of adopting a multi-theoretical approach, which has received heightened interest in debating the issue of corporate governance (e.g. Lynall, Golden, and Hillman 2003; Douma et al. 2006; Ruigrok, Peck, Tacheva, Greve and Hu 2006).

Apart from the above highlighted motivations, it is also important to emphasise that the study of corporate governance is not new. However, recently and over the years, it has been receiving heightened interest (Aggarwal, Schloetzer, Williamson 2014; Bokpin and Isshaq 2009; Letza, Sun and Kirkbride 2004). The issues related to corporate governance have not only been discussed by scholars, but also by many other parties such as shareholders, stakeholders, related institutions, the state, etc. (Aguilera and Cuervo-Caruzza 2004).

There are two significant events that have kindled massive attention to this subject, namely the Asian Financial Crisis of 1997/1998 that hit the South East Asian capital markets, and the shocking scandals which engulfed the US giant company, Enron, three years later. Besides this, many other cases of unethical behaviour, misconduct, malpractice and negligence have been discovered in firms all round the world - e.g. WorldCom and Tyco in 2002 and HealthSouth in 2003, etc. These corporate scandals had a severe impact on public confidence concerning the reliability of the protection systems that are in place to safeguard their interests in firms.

As a consequence, in the aftermath of these financial catastrophes, the need for an efficient corporate governance system has been manifested. The potential consequences that might emerge from the weakness of the corporate governance system have been raised by the key players in the economic system (Claessens 2006). More of the issues concerning the deficiencies in corporate governance are highlighted and more arguments are brought forward. Thus, it is argued that this area of study has never been free from criticism, and changes often occur in its setting, legislation, codes etc., particularly when a new issue arises. Although numerous research studies have been carried out in this area, corporate governance is not a stale issue, since these studies have shed light on unexplored areas of corporate governance which have become the impetus for fresh research. Thus, this research attempts to add to the previous literature, offering a new perspective on corporate governance and foreign equity ownership in emerging countries.

Finally, as discussed above, special features exist in the context of a few of the external events that have impacted on Malaysia and its unique institutional environment, making Malaysia an ideal setting for examining this issue. Apart from this, other factors motivating the study to be carried out in Malaysia is the condition of Malaysia in the aftermath of the AFC 1997/1998. Malaysia is one of the countries severely affected by this crisis. As a developing country, the weakness of corporate governance is considered to be one of the significant factors that contributed to the crisis (Kim 1998; Khas 2002; Samad and Wilson 2002). An understanding of the background of Malaysia, the consequences of the crisis, and the reaction of the government to solve these problems may provide a better analysis of the role of the corporate governance system in this country, thus attracting international capital inflow to the country.

As a developing country, Malaysia has a vision to be achieved. The main aspiration of the country is to transform its economy through industrialisation in order to become a fully developed country by the year 2020 (Vision 2020). Therefore, Malaysia must provide the crucial resources required to be as efficient as possible. Foreign investment has an important role to play in achieving this long term vision. The

findings of this study can assist the Malaysian government to understand more about foreign investors' behaviour when making investment decisions in relation to corporate governance determinants and the institutional background. Therefore, strategies and policies can be generated based on the findings. The findings may offer constraints and limitations as well. However, it is necessary to focus on the constraints that can influence the economy through time. An understanding of the constraints and opportunities may serve as a guide for policymakers in formulating better policy options for the future. More discussion about the Malaysian Vision 2020 can be found in Chapter, Section 2.4.1 Malaysia before the 1997/1998 Financial Crisis.

In summary, based on the discussion provided in this section, the rationale to undertake this study has been provided. Each point of motivation that has emerged from the research background substantiates the need for the study to be undertaken. The successful execution of this study is meaningful in ensuring that the association of corporate governance mechanisms and foreign investors' behaviour in the Malaysian setting is clearly deciphered. Thus, this may benefit the many parties involved.

1.3 The Scope of the Study

This study focuses on examining the association between corporate governance mechanisms (board characteristics, directors' attributes and ownership structures) and FEO in Malaysian PLCs. The sample for the study was 153 companies listed on Bursa Malaysia from the year 2000 until 2011. Eventually, this meant that there were 1836 observations for 12 consecutive years. The study used secondary data that was available in the companies' annual reports, the Bursa Malaysia database, the Thomson One Banker database, individual companies' web sites, data purchased from Bursa Malaysia (FEO) and various other reliable sources. In terms of corporate governance determinants, the variables tested in this study were board size, board independence, foreign directorship, multiple-directorships, women directorships, Western educational background directors, financial expertise directors, family-controlled company, managerial ownership and institutional ownership. These variables were

subsumed into three categories based on the established research questions. The key dependent variable is foreign equity ownership (FEO), represented by the percentage of foreign equity in the firm.

1.4 Research Objectives

The main research objective for this study is: *To examine whether the level of FEO in Malaysian firms is determined by the firm's corporate governance structure.* In essence, the main research objective is achieved only if the following specific sub-research objectives are adequately attained. The following are the specific research objectives of this study:

- i. To examine whether the level of FEO in Malaysian firms is determined by the characteristics of the board of directors.
- ii. To examine whether the level of FEO in Malaysian firms is determined by the directors' attributes.
- iii. To examine whether the level of FEO in Malaysian firms is determined by the firm's ownership structure.

1.5 Research Questions

Referring to the previous discussion, it is argued that in attracting foreign investors, corporate governance mechanisms are central either at the company level or the country level. However, corporate governance alone is widely defined, and consists of many elements. At the firm level, corporate governance practice can be segregated into several internal mechanisms; these include the board of directors, the ownership structure, the overseeing function of the management, the internal auditor, the directors' remuneration package, etc.

Nevertheless, in relation to comprehending foreign investors' behaviour, this study focuses on a few parts of it – the board of directors' characteristics, the directors'

attributes and the ownership structure. Thus, this study seeks to answer the following research questions:

Do the characteristics of the board of directors influence the level of FEO?

Do the directors' attributes influence the level of FEO?

Do the ownership structures influence the level of FEO?

Seeking answers to the three subsidiary questions above leads to an understanding of the association between the corporate governance variables from each category and the level of FEO in a company. Thus, the main research question in this study - *Does corporate governance influence the level of FEO in Malaysian companies?* - can be answered more generally.

1.6 Research Methodology

One of the greatest obstacles encountered in studies of emerging markets is the quality of data and indeed its collection. In the context of this study, data for corporate governance in Malaysian firms has to be collected manually. There is no database that can be accessed to obtain the data. However, the detailed information in companies' annual reports is reliable, as it is audited by the external auditors, and the presentation of the information in the annual reports is also uniform and according to the required accounting standard. Thus, even though the data collection process was lengthy due to the meticulous and tedious procedures that needed to be followed, there is very little doubt about the reliability of the data. The same applies to the data concerning foreign equity ownership. This data is not made publicly available; thus, it has to be purchased from Bursa Malaysia. Since there are no specific requirements imposed on Malaysian firms concerning the ownership by foreign investors. The only data provided by the firms is the percentage of foreign ownership, with the absence of other information, such as the investors' countries of origin, the categories of investors etc.

The focus of this study is on examining the association between corporate governance mechanisms in Malaysian firms and foreign equity ownership. The data was collected

for 12 years in a row from the same companies. Thus, the panel data concept was applied. Therefore, the appropriate panel data analyses were considered for utilisation. There are many options which can be chosen. However, empirically, the generalised least square (GLS) regression method is found to be ideal for the main analysis. In addition, to strengthen the findings from the main analysis, logit regression and generalised method of moments (GMM) are engaged to estimate the models.

1.7 The Organisation of the Study

This thesis is divided into eight chapters. Each of the chapters begins with an introductory section to assist in the understanding of the main consideration of the chapter. The organisation of the sections in the chapter is also briefly presented, thus giving an initial picture of the chapter's direction. At the end of every chapter, a summary section is utilised to briefly highlight the concluding remarks and to provide links to the following chapters. A brief overview of each chapter is given below, starting with Chapter 2.

Chapter 2 presents the background to comprehending the study of corporate governance and foreign equity ownership in Malaysia. This chapter starts by providing a basic understanding of corporate governance in general, such as the definition of corporate governance and the importance of corporate governance which is essentially understood and applied in developed markets. Next, the scope of corporate governance is narrowed down to the Asian case, by focusing on Malaysia in particular. The pattern of corporate governance in this region is discussed by contrasting the model with the shareholder-model versions. In addition, the discussion of the corporate governance issue in Asia is based on the extant literature and the changes that affected the corporate governance institutions in the aftermath of the AFC 1997/1998. The system and agencies responsible for setting the corporate governance framework in Malaysia are also included. This chapter then discusses the foreign investments in Malaysia, which can be linked with the corporate governance practice, as a basis for the central concern in this study.

Chapter 3 is concerned with the development of theories. Three theories (agency theory, institutional theory and resource dependence theory) are posited for use as the underpinning lenses in elucidating the relationship between corporate governance variables and FEO. When these three theories are mentioned together, they will be referred to as the ‘multi-theoretical approach’. This chapter calls for the importance of agency theory (principal-principal model) and institutional theory in examining the institutional background of the current study setting, Malaysia. It is argued that agency theory is relevant to be applied based on the ownership structure of Malaysian capital market while institutional theory can offer a persuasive influence from a different perspective to explain foreign investors’ behaviour when making investment decisions regarding developing markets. Therefore, a single theoretic approach may not provide a comprehensive overview of this subject, as some governance practices in Malaysia may be moving towards the Anglo-American corporate governance model. Hence, a possible explanation can be given when the lenses of institutional or resource dependence theory are applied. In this light, a unitary perspective is inadequate. Thus, this study embraces a multi-theoretical approach which espouses agency theory, institutional theory and resource dependence theory.

Chapter 4 focuses on hypotheses development. This chapter considers the discussions from the previous chapters (Chapter 2 and Chapter 3) in constructing the hypotheses. Before the commencement of the main arguments, the theoretical frameworks presented in Chapter 3 are recapitulated briefly to allow them to be customised to the current study setting. The research question is then restated to provide the main debate of the hypotheses to be proposed. There are 10 hypotheses which are subsumed into three categories in order to answer the three specific research questions.

Chapter 5 covers data and the research methodology. The philosophical approach to acquiring the data and conducting the study is provided. After confirming the appropriate philosophical approach, the process of identifying the sources, determining the sample and designing the research are illustrated. The research is conducted in a spirit of positivism. The definition of each variable is also provided. The chosen statistical software packages and methods of analysis are discussed. This

chapter proposes several analyses that can be utilised. However, the main analysis is determined based on the characteristics of the data, which will be decided after the diagnostic tests are run in Chapter 7.

Chapter 6 presents the results from the descriptive analyses. The method of explanation is twofold – univariate and bivariate. This chapter aims to explore the main features of the data collected by describing its characteristics quantitatively. Moreover, the results of the descriptive analyses presented in this chapter can indicate certain clues to the findings that may be apparent in the main analysis performed in Chapter 7.

Chapter 7 discusses the findings from the multivariate analyses. Standard analyses, such as the correlation matrix and variation inflation factors (VIF), are used to test for multicollinearity in the models constructed. Then, the main analysis used, GLS regression analysis, is singled out based on the diagnostic tests performed beforehand. Additional analyses, such as logistic regression and the GMM are also run to add robustness to the findings derived from the main analysis, which is GLS regression.

Chapter 8 is the last chapter in the thesis. This chapter concludes the findings and links them with the research questions and the research objectives of the study. The impact of this study is discussed, alongside the theoretical and practical implications that it might have for policymakers and regulators in order to improve the practice of corporate governance and appease foreign investors. Further, the limitations encountered in this study are described and potential future works are suggested.

The organisation of the study is presented in Figure 1.1 below, whilst Figure 1.2: Conceptual Framework illustrates the overall picture of this study.

<p>Chapter 1 Introduction and Background</p>	<ul style="list-style-type: none"> • Background and motivation of the study • The scope of the study • Research objectives and research questions • Research methodology • The organisation of the study
<p>Chapter 2 Institutional Background: Corporate Governance in Asia</p>	<ul style="list-style-type: none"> • Corporate governance (CG) in general, in Asean countries and in Malaysia • Asean financial crisis 1997/1998 (AFC 1997/1998) • The development of CG in Malaysia - Institutions and Code of CG • Foreign investment - CG and Malaysia
<p>Chapter 3 Multi-Theoretical Approach: Agency Theory, Institutional Theory, and Resource Dependency Theory</p>	<ul style="list-style-type: none"> • Multi-theoretic approach (MTA) • Agency theory • Institutional Theory • Resource Dependency Theory (RDT)
<p>Chapter 4 Theoretical Framework, Literature Review and Hypotheses Development</p>	<ul style="list-style-type: none"> • Conceptual framework • MTA applied • Hypotheses development
<p>Chapter 5 Data and Methodology</p>	<ul style="list-style-type: none"> • The philosophical approach • Data, population and sample • Variables definitions and measurements • Data analyses and interpretation • Research model and measurement
<p>Chapter 6 Results and Descriptive Analyses</p>	<ul style="list-style-type: none"> • Descriptive statistics • Descriptive analyses and results - Univariate and bivariate tests
<p>Chapter 7 Multivariate Results and Analyses</p>	<ul style="list-style-type: none"> • Panel data related tests • Multivariate Analyses - GLS regression • Additional multivariate analyses - Logistic regression and GMM estimation method • Sensitivity analyses
<p>Chapter 8 Conclusions and Recommendations</p>	<ul style="list-style-type: none"> • Summary of the study • Implications of the study • Limitations of the study • The area of future research

Figure 1.1: The Organisation of the Study

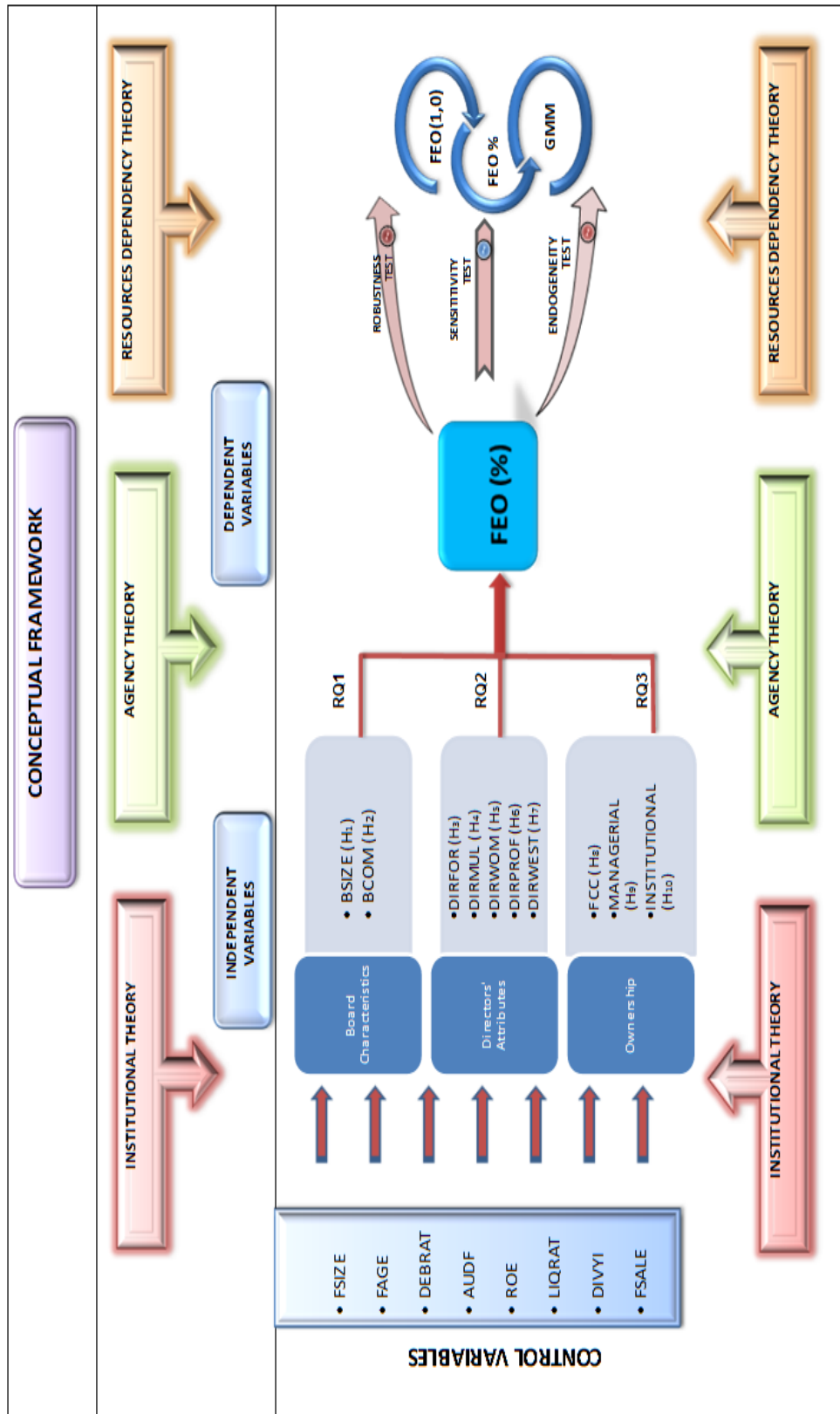


Figure 1.2: Conceptual framework for corporate governance and FEO in Malaysia

CHAPTER 2

INSTITUTIONAL BACKGROUND: CORPORATE GOVERNANCE IN ASIA

2.1 Introduction

Chapter 1 introduced this thesis and explained in brief the whole structure of this research work. The purpose of this current chapter is to provide a background to corporate governance in general, narrowing it down to the Asian case by focusing on Malaysia, in particular. The issue of corporate governance will then be linked to foreign portfolio investment, as a basis for the work that follows in the remaining chapters.

This chapter is organised as follows. Section 2.2 starts by defining corporate governance, as this determines the scope of the issues to be addressed. It also discusses the importance of corporate governance and will provide a view of corporate governance practices around the world. Section 2.3 moves from corporate governance in general to highlight corporate governance in Asia, and offers some insight based on extant literatures and the similarities that exist in Asian countries by focusing on the Asian financial crisis (AFC) of 1997/1998. The pattern of corporate governance in this region will be discussed by contrasting the model with the US and UK versions. In Section 2.4, the Malaysian scenario in corporate governance practice is discussed. This section also deals with the system and agencies responsible for setting the corporate governance framework in Malaysia. Section 2.5 moves from corporate governance to foreign investment in general. Next, Section 2.6 reviews foreign investments in Malaysia with special emphasis on foreign equity investment. In the same section, a discussion of foreign investments is tackled in alignment with the corporate governance impact. Section 2.7 limits the previous discussion of

corporate governance and foreign investment to the Malaysian setting. Finally, Section 2.8 summarises and concludes the chapter.

2.2 Corporate Governance

Corporate Governance has, in recent years, garnered considerable attention as a discussion topic in management, economics, business ethics, company law and other disciplines (Aggarwal et al. 2014; Bokpin and Isshaq 2009; Letza et al. 2004). It has also become a mainstream concern among scholars, shareholders, stakeholders, the state, other related parties, and regulatory bodies as well as practitioners, worldwide (Aguilera and Cuervo-Cazurra 2004; Cheung and Chan 2004). Two significant events have resulted in considerable attention being focused on this area, namely the financial crisis of 1997/1998 that hit South East Asian capital markets, and the corporate governance scandals in the US and Europe three years later that swept away the public belief in the corporate sector. In the aftermath of this, most of the key players in the economic system have begun to comprehend the potential consequences on world economies which stem from the weaknesses in corporate governance mechanisms (Claessens 2006).

Before explaining further why more attention is being paid to corporate governance, definitions of this phrase should be reviewed. In general, the definition of corporate governance widely used is “*the system by which companies are directed and controlled*” (Cadbury Committee 1992:1). On the other hand, the definition of corporate governance varies widely, as it can be defined from many angles. However, following Claessens (2006), there are two categories to be considered in explaining corporate governance. The first set of definitions is concerned with a company’s behavioural patterns, measurements of performance, growth, efficiency, financial structure, and the treatment of its shareholders and other stakeholders. The second set of considerations emphasises the normative framework that is concerned with the rules which are applied for firms to operate, the legal sources of the rules, the judicial systems, the financial markets and the labour markets. This second definition is close to the one given in Shleifer and Vishny’s (1997: 737) seminal paper; “*Corporate*

governance deals with the ways in which suppliers of finance to corporations assure themselves of getting a return on their investment”.

The importance of effective corporate governance has been proposed by many researchers. Franks and Mayer (1997) posit that corporate governance is one of the ideal ways of bringing together the interests of owners and managers translated into mutual objectives, which is for the ultimate benefit of the investors. It is also believed that good corporate governance helps to generate investor goodwill and confidence (Ponnu 2008). Gregory and Simms (1999) claim that corporate governance promotes the efficient use of resources both within the firm and in the larger economy, as well as assisting firms and economies to attract lower-cost investment capital. This is concurrent with the view that better governed firms might have more efficient operations, which results in higher expected returns (Jensen and Meckling 1976). This can happen through the improved confidence of investors and creditors, both domestically and internationally. In addition, Jensen and Meckling (1976) also suggest that corporate governance helps in increasing the responsiveness of firms to societal needs and expectations and in improving the long-term performance of firms. Daily and Dalton (1994), on the other hand, demonstrate that bankruptcy is highly likely to occur in companies with poor governance systems. Briefly explained, corporate performance is expected to reflect the way that the firm is managed, as well as the effectiveness of the firm's governance structure.

In developed countries, the interest in corporate governance of policy makers has grown significantly starting in the early 1990s (Cheung and Chan 2004). Two processes, which occurred in parallel - globalisation (such as the liberalisation and internationalisation of economies, developments in telecommunications, and the integration of capital markets) and transformations in the ownership structure of firm (due to the growth of institutional investors, privatisation, and rising shareholder activism) - have encouraged the perceived need for a more effective mechanism of systems of corporate governance in monitoring investors' investments (Aguilera and Cuervo-Caruzza 2004).

The first code of corporate governance came into being in the USA in the late 1970s, and a decade later, in 1989, the Hong Kong Stock Exchange issued its first ‘Code of Best Practice: Listing Rules’. This was then followed by the Irish Association of Investment Managers’ draft of the ‘Statement of Best Practice on the Role and Responsibility of Directors of Publicly Listed Companies’ in 1991. Despite the non-linear pattern shown, new codes appeared steadily throughout the early 1990s, and particularly since the issuance of the Cadbury Report in 1992 (Aguilera and Cuervo-Caruzza 2004). Codes of good governance are a set of ‘best practice’ recommendations on how to manage firms through many aspects, in order to assure that the owners’ interests are preserved. The main purpose of the Codes is to address any insufficiency in the corporate governance system by recommending “a comprehensive set of norms on the role and composition of the board of directors, relationships with shareholders and top management, auditing and information disclosure, and the selection, remuneration, and dismissal of directors and top managers” (Aguilera and Cuervo-Caruzza 2004).

The publication of the *Cadbury Committee Report: Financial Aspects of Corporate Governance* in 1992 is the first of the large-scale official efforts that were implemented by OECD⁴ countries in the UK and Northern Ireland. The weakness of internal corporate control was given greater attention after a series of high-profile corporate failures, as well as the 1990 British recession. Subsequently, the issue of corporate accountability became a major concern (Monks and Minow 1995). The objective of this first report was to investigate how corporate governance guidelines can be effectively adopted by large public companies. The focus was on the role of the accounting profession and the procedures for producing financial reports (Cheung and Chan 2004). The Cadbury Report also emphasised the need for independent directors, the role of the board directors, shareholder involvement, the standards for financial reporting, directors’ pay, auditors’ accountability and the establishment of board committees (Charkham and Simpson 1999; Cheung and Chan 2004). In order to be

⁴OECD is abbreviation of Organization for Economic Co-operation and Development.

listed on the London Stock Exchange (LSE), companies need to comply with the Codes, otherwise they are required to justify any areas of noncompliance.

This effort then continued three years later with the release of the *Greenbury Report 1995*. The remuneration of executive and non-executive board members was detailed, and the report also provided recommendation for each public company to set up a remuneration committee to determine the compensation packages for the board members. Besides this, suggestions were made about disclosing the remuneration amount, setting up a remuneration policy, the service contract and compensation. Consequently, the issues outlined in the Cadbury Report and the Greenbury Report have resulted in the *Hampel Report 1998* being published in the UK. This report combined the efforts of the previous reports and highlighted four major issues, whilst also offering practical guidelines. The issues raised were: (i) the role of the directors; (ii) directors' compensation; (iii) the role of the shareholders; and (iv) accountability and audit. In the following years, in the UK, several influential proposals were produced in an attempt to settle the practical issues, such as those from the *Turnbull Committee 1999* and *Higgs 2003*.

Even though the compliance with corporate governance codes is voluntary, the response by public listed companies is quite impressive (Gregory 2002). In several countries, as an alternative to noncompliance, the companies need to justify the area of noncompliance and disclose it in their annual reports. According to Aguilera and Cuervo-Caruzza (2004) this 'comply or explain' style encourages more firms to comply. Furthermore, a great deal of research has revealed that adopting some good practices as recommended by the codes of good corporate governance is directly related to higher firm performance (Weir and Laing 2000), increased CEO turnover in the UK due to the need for the separation of chairman and CEO, and sensitivity issues related to poor performance (Dahya, McConnell and Travlos 2002). Others have demonstrated significant changes such as changes in the board structure, the appointment of independent non-executive directors, etc. (Stiles and Taylor 2001). In summary, codes of good governance are becoming increasingly receptive to the

advanced capital markets especially where it has increased firms' transparency and accountability (Aguilera and Cuervo-Caruzza 2004).

It is alleged that the foundation of corporate governance around the world lies in the listed firms' ownership structure and the institutional setting of their capital markets (Bokpin and Isshaq 2009; Cheung and Chan 2004; Samad and Wilson 2002). Public listed companies in developed markets are characterised by significant ownership by institutional investors. The active involvement of institutional investors will provide an avenue for fund managers to demand information matrices through which they can make informed decisions and assure themselves that they are investing in properly monitored public listed companies (Cheung and Chan 2004). Another characteristic that is shared by the OECD countries is dispersed ownership. However, this does not truly reflect the other parts of the world capital market which can be explained through different patterns of ownership and their institutional setting.

There are a few models which explain the nature of corporate governance systems around the world. The models are the result of the institutional setting and the culture within which the corporation is operating. Some current perspectives on corporate governance have been categorised into two contrasting paradigms. The best known model is the Anglo-American model, which is prevalent in the US and UK, and the other is the stakeholder model, which applies to Germany, Japan and some other continental European countries (see for example, Friedman and Miles 2002; Kakabadse and Kakabadse 2001). These divisions hinge upon the ultimate objective of the corporation and its related structure of corporate governance, as understood and justified in theory (Letza et al. 2004).

The Anglo-American model is characterised by dispersed shareholders and the firm's primary objective which is to maximise shareholder wealth (Jensen and Meckling 1976; Shleifer and Vishny 1997). Thus, governance mechanisms that operate in this model, including the separation of ownership and control, are there to ensure that board members and executives work towards the firm's financial goals and at the same time outside investors try to ensure that they are not exploited by the

management (Shleifer and Vishny 1997). This approach is further shared by Stenberg (1998), who sees corporate governance as a means of ensuring that corporate actions, assets, and agents are directed at achieving the objectives established by the corporations. These governance mechanisms operate interdependently, whereby if one fails, automatically the remaining mechanisms or a combination of them may substitute for it and play their own role (Rediker and Seth 1995).

Alternatively, the stakeholder model, which emerged in the late 20th century, is characterised by a significant holding by a parent company, while outside shareholders represent only the smaller portions of the equity. Shareholders are viewed as partners and as one form of stakeholder, together with employees, creditors, suppliers, customers and local communities (Freeman 2010), which is in opposition to the Anglo-American model that considers shareholders as the “risk takers” of the company (Cheung and Chan 2004). From the point of view of this model, the corporation is a locus to serve the interests of wider external stakeholders’ rather than merely focusing on maximising shareholders’ wealth (Letza et al. 2004). In addition, the supporters of this model argue that the current corporate governance system which operates under the shareholder model fails to encourage the involvement of other stakeholders (Letza et al. 2004). The figure below shows the results of a survey conducted in five countries to ascertain how a large company is managed. There were two options given: i) shareholder interest should be given the first priority or ii) a firm exists in the interests of all its stakeholders.

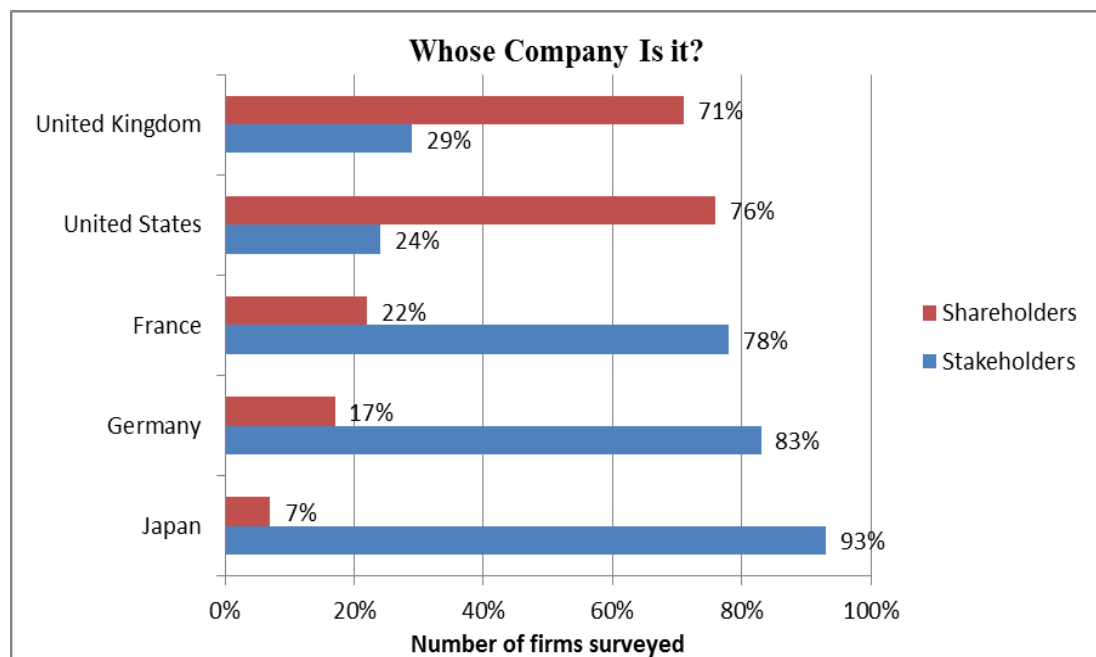


Figure 2.1: Whose Company Is it?

Number of firms surveyed: Japan, 68; United States, 82; United Kingdom, 78; Germany, 100; France, 50. Source: *Yoshimori (1995)*.

This survey provides evidence to suggest that in terms of their corporate governance system, these countries may be divided into two groups, namely supporters of the shareholder model and the stakeholder model. The legal protection of investors is relied on substantially in the US and UK, as large investors are less prevalent, whilst in much of Continental Europe as well as Japan, there is more reliance on large investors and banks. However, even these two models claim their superiority; in reality Letza et al. (2004) argue that dynamic shifts have occurred and that both models are increasingly becoming attractive all over the world, particularly in the last two decades. Shleifer and Vishny (1997) reinforce the idea that governance systems in developed countries like the US, UK, Japan and Germany are among the good and only have slight differences compared to the governance systems of other countries.

Evidence shows that Germany and Japan, which are traditionally categorised under the stakeholder model, are converging more on shareholder-value or the Anglo-Saxon model due to the pressure of globalisation and international competition (Schilling 2001; Stoney and Winstanley 2001). These trends, however, do not reflect the

corporate governance models in Asian countries, where ownership is typically heavily concentrated in families. The next section will discuss, in detail, the corporate governance environment in Asia.

2.3 Corporate Governance in Asia

In many respects, Asian capital markets are very different from developed equity markets in Western countries. Unlike in the USA and UK, the typical characteristics of companies in Asian countries are the smaller size of the capital raised, smaller capitalisation, relatively infrequent turnover and high ownership concentration (Cheung and Chan 2004). Zhuang, Edwards, Webb and Capulong (2000) suggest that concentrated corporate ownership in most of the East Asian companies has provided family-owners/controllers (La Porta et al. 2000) with unwarranted power and has also lessened the effectiveness of essential shareholder protection mechanisms, for instance shareholder participation through voting, information disclosure and transparency. These characteristics not only affect how corporate governance standards can be set up, but also restrict the impact of reforms in the overall link between investors and economic development (Cheung and Chan 2004).

The underlying problem for corporate governance under concentrated ownership is the protection of minority shareholders from expropriation by controlling shareholders. Even though, to a certain degree, this type of ownership helps controlling shareholders to play a crucial role in monitoring management, Morck, Shleifer and Vishny (1988) found an inverted “U-shaped” relationship nexus between the level of ownership concentration and profitability whereby the costs may exceed the benefits when it reaches a certain degree. After this focal point, the profitability may start to drop and the controlling shareholding may react in their own interests at the expense of the minority shareholders. In most of the Asian capital market, the conflicts between the minority and controlling shareholders in a firm arise from principal-principal goal incongruence. Relatively speaking, this is different from traditional agency problems in developed markets where problems arise from principal-agent goal conflicts (Douma et al. 2006). Young, Peng, Ahlstrom and

Bruton (2008) address these problems in the so-called principal-principal model. More discussion on the principal-principal model can be found in Section 3.3.2 Concentrated Ownership in Malaysian Companies and afterwards. Besides this, other factors - such as excessive government interferences, less-developed capital markets, and fragile legal and regulatory frameworks for investor protection - contribute to the deficiencies in corporate governance practices in selected East Asian countries (Zhuang et. al 2000).

In discussing corporate governance in East Asia, their historical backdrops and their institutional frameworks need to be fully taken into account (Suto 2003). In Asian countries, the inquisitiveness concerning corporate governance has been sporadic, but escalated in the late 1990s subsequent to the 1997/1998 financial crisis. The East Asian countries that were hit most by this crisis were Indonesia, Korea, Malaysia, the Philippines and Thailand. The geographic location of these countries is shown in Figure 2.2 below. However, Singapore was less affected and Thailand is claimed to be the origin of the crisis.



Figure 2.2: Countries that were hit hardest by the AFC 1997/1998

This crisis is believed to have started in Thailand in July 1997 (Mitton 2002) with the precipitous collapse of the Thai baht (currency used in Thailand for transactions), which occurred after the Thai government floated the baht against the U.S. dollar. According to Zulkafli, Abdul Samad and Ismail (2005), foreign investors lost their confidence and began to withdraw their capital due to currency devaluation. Then, this

problem disseminated to other neighbouring countries. Studies that have been carried out on the above countries show that they were more fragile on average than the others before the economic meltdown (Zhuang and Dowling 2002). In addition, these countries shared several identical characteristics in varying degrees.

In contrast, Singapore was seen to have a much higher current account surplus throughout the 1990s, which was on average around 10% of GDP in 1990 – 1993, and which rose to about 16% of GDP in 1994 – 1996. Comparisons of current accounts can be made with other East Asian countries as shown in Table 2.1.

Table 2.1: Current Accounts, NIA Definition (% of GDP)

	1990	1991	1992	1993	1994	1995	1996	1997
Korea	-1.24	-3.16	-1.70	-0.16	-1.45	-1.91	-4.82	-1.90
Indonesia	-4.40	-4.40	-2.46	-0.82	-1.54	-4.27	-3.30	-3.62
Malaysia	-2.27	-14.01	-3.39	-10.11	-6.60	-8.85	-3.73	-3.50
Philippines	-6.30	-2.46	-3.17	-6.69	-3.74	-5.06	-4.67	-6.07
<i>Singapore</i>	9.45	12.36	12.38	8.48	18.12	17.93	16.26	13.90
Thailand	-8.74	-8.01	-6.23	-5.68	-6.38	-8.35	-8.51	-2.35

Note: Source: *Corsetti, Pesenti and Roubini (1999)*. NIA = National Income Account.

The possible role of current account deficits in creating troublesome tensions in the financial markets has been reiterated in the literature (Corsetti et al. 1999). As written by Lawrence Summers, the US Deputy Treasury Secretary, in *The Economist*⁵ “close attention should be paid to any current account deficit in excess of 5% of GDP, particularly if it is financed in a way that could lead to rapid reversal”. By this standard, all East Asian countries excluding Singapore provided reasons for concern (Corsetti et al. 1999).

Data on the current account positions yields some preliminary evidence that the currency crises may have been tinged with an external competitiveness problem. In

⁵ *The Economist* 23 December, 1995–5 January 1996, pp. 46–48.

fact, as a group, the countries that were hit the hardest in the 1997 turmoil appeared to link with the countries with a large current account deficit throughout the 1990s. Thus, Singapore was affected, mainly because of the regional contagion crisis (Zhuang and Dowling 2002). This was proven by the fact that Thailand lost 65% of its stock market value in dollar terms, Indonesia lost 71%, Malaysia lost 57%, the Philippines lost 58%, South Korea lost 72% while Singapore lost only 24% of its value. In addition, both currencies and the local stock market plunged in most countries whereby Thailand lost about 33%, Indonesia lost 34%, Malaysia lost 42%, the Philippines lost 32%, South Korea lost 44% and Singapore only lost 10% (Chakrabarti and Roll 2002).

2.3.1 The Asian Financial Crisis 1997/1998

The AFC 1997/1998 affected many Asian countries and raised fears among investors worldwide of financial contagion. Subsequent to the crisis, as a result of investor apprehensions, the foreign investors' capital inflow suddenly dried up and the local market faced a serious liquidity problem (Cheung and Chan 2004). The root of the crisis has been discussed in depth, leading to the emergence of two main arguments. The first of these is that the crisis began when there was a decreasing level of investors' confidence and a swift shift in market expectations, followed by regional contagion which caused financial turmoil and propagation over time in some Asian countries (Chang and Velasco 1999; Marshall 1998; Radelet and Sachs 2000). This macroeconomic imbalance then led to panic among investors, both local and international (Zhuang and Dowling 2002), who subsequently decided to withdraw their investments.

The second argument is that the crisis emerged primarily due to structural and policy distortions (Corsetti et al. 1999; Dooley 1999). This fundamental imbalance triggered the financial and currency crisis in 1997, and once the crisis started, market overreaction caused the plunge of exchange rates, and the plummet of assets' prices. This view has been supported by Zhuang and Dowling (2002), who discriminate between the two arguments, and their findings suggest that weaknesses in the

economic and financial fundamentals in these countries played an important role in triggering the crisis.

Instead of providing two different arguments, Johnson et al. (2000) posit, however, that the above explanations agree that, for some reason, there was a loss of confidence by domestic and foreign investors in all emerging markets. According to Zulkafli et al. (2005), investors had experienced an unanticipated change in their expectations, and their irrational behaviour, compounded by the International Monetary Fund's (IMF) inappropriate responses to the crises, apparently added to the panic among investors. This led to a fall in capital inflows and an increase in capital outflows that triggered, in some cases, a very large nominal depreciation and a stock market crash. Table 2.2, reproduced from a figure presented in a report by Radelet and Sachs (2000), gives a rough estimate of the breakdown of the adverse reversal flows for the five East Asian countries that were badly affected by the crisis (Indonesia, Korea, Malaysia, the Philippines and Thailand).

Table 2.2: Five East Asian Economies: External Financing, 1994 – 98 (billion dollars)

	1994	1995	1996	1997 ^a	1998 ^b
<i>Current account balance</i>	-24.6	-41.3	-54.9	-26.0	17.6
<i>External financing, net</i>	47.4	80.9	92.8	15.2	15.2
Private flows, net	40.5	77.4	93.0	-12.1	-9.4
Equity investment	12.2	15.5	19.1	-4.5	7.9
Direct Equity	4.7	4.9	7.0	7.2	9.8
Portfolio equity	7.6	10.6	12.1	-11.6	-1.9
Private creditors	28.2	61.8	74.0	-7.6	-17.3
Commercial banks	24.0	49.5	55.5	-21.3	-14.1
Nonbank private creditors	4.2	12.4	18.4	13.7	-3.2
Official flows, net	7.0	3.6	-0.2	27.2	24.6
International financial institutions	-0.4	-0.6	-1.0	23.0	18.5
Bilateral creditors	7.4	4.2	0.7	4.3	6.1

Source: Radelet and Sachs (2000)

Note: The five East Asian economies are South Korea, Indonesia, Malaysia, Thailand and the Philippines.

^aEstimate

^bInstitute of International Finance (IIF) forecast

The above Table 2.2 shows that net private capital flows into the most affected Asian economies jumped from \$40.5 billion in 1994 to \$93 billion in 1996. But in the last half of 1997, these inflows suddenly reversed themselves, with net capital flows turning into an outflow of \$12.1 billion. This represents a turnaround of \$105 billion, in just six months, from an inflow of \$93 billion to an outflow of \$12.1 billion, where \$77 billion came from commercial bank lending, \$5 billion came from a decline in non-bank lending, while direct investment was sustained at around \$7 billion. The significant decline came from a \$24 billion fall in portfolio equity. The reversal of foreign capital had several marked interlocking macroeconomic and microeconomic adverse effects. Most dramatically, exchange rates depreciated, and this was followed by a soaring of the domestic interest rate, which led to a tightening of the domestic credit situation (Radelet and Sachs 2000). In Malaysia, for example, after the AFC 1997/1998, foreign capital shunned the Malaysian market so that foreign portfolio investment fell by 74 percent from RM144.9 billion in 1996 to RM37.6 billion in 2001. Figure 2.3 below depicts the plummet of foreign investment in the Malaysian capital market.

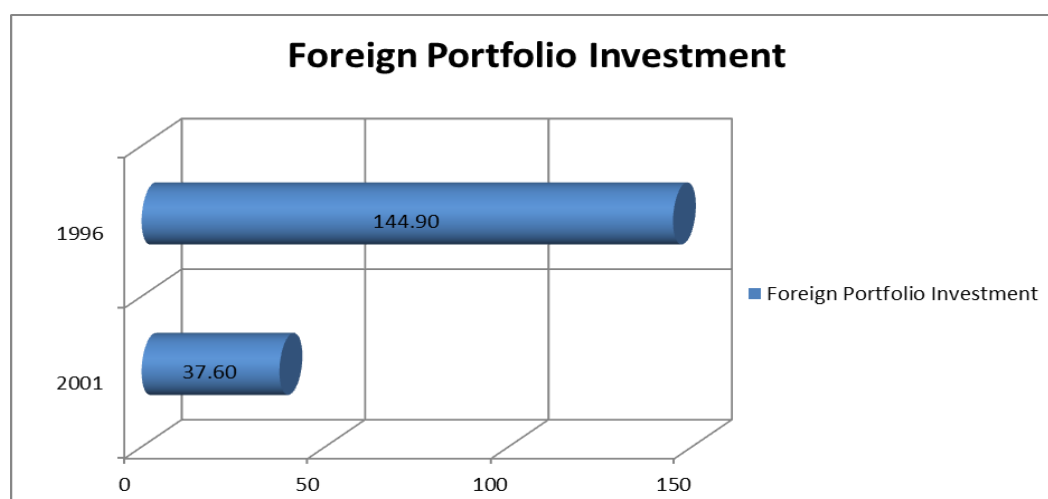


Figure 2.3: Foreign Portfolio Investment in Malaysia 1996 -2001 (RM)

However, the above clarifications do not address precisely why the loss of confidence had such a significant impact on the exchange rate and the capital market in some emerging markets but not others. The “Asian Crisis” of 1997/1998 affected all the

“emerging markets” open to external capital flows. Johnson et al. (2000) present evidence that the ineffectiveness of the legal institutions for corporate governance had a crucial impact on the extent of the devaluation and the slump of the stock market in the Asian crisis. Therefore, in the case of the Asian turmoil, they posit that corporate governance provides a persuasive explanation for the cause of the tragedy. Many other researchers (Suto 2003) have reached the same conclusion (see for example Khatri et al. 2002; Sam 2007).

This argument is further echoed by Mitton (2002), who goes on to claim that even though weak corporate governance may not have caused the East Asian crisis, once it began, the countries with poor governance practices would have been more vulnerable to financial crisis; these poor practices could have exacerbated the crisis severely, or at least accelerated the deterioration (Suto 2003) compared to the countries with strong shareholder protection practices. It has been alleged by Kim and Wei (2002) that foreign investors may have been positive feedback traders, who were eager to copy each other’s behaviour and ignored fundamental information. This was proved during the AFC 1997/1998, since they were rushing to buy when the market was booming and then instantly sold their shares when the price was declining.

This AFC 1997/ 1998, then, has highlighted the importance of high quality financial disclosure (Aggarwal et al. 2005) which resulted in most of the Asian countries seeking ways to strengthen their corporate governance, transparency and disclosure levels (Ho and Wong 2001). In the aftermath of the crisis, it is claimed that policy reforms emerged in a number of emerging markets (Aggarwal et al. 2005). Haniffa and Hudaib (2006) also assert that most of the countries in the region established a Code of Corporate Governance to ensure the continuous flow of funds and to boost the confidence of investors in their capital market.

The theoretical explanation given by Johnson et al. (2000) is straightforward. If stealing by managers increases when the predicted rate of investment return falls, then an unpleasant shock to investor confidence will lead to more theft and a decrease of capital inflow, which simultaneously causes greater attempts at capital outflow for a

country. These, in turn, will result in lower stock prices and diminishing values of the exchange rate. There were many well documented cases illustrating expropriation by managers in countries affected by the Asian crisis. Table 2.3 summarises the details of selected allegations of expropriation in a few countries affected by the Asian crisis.

Table 2.3: Alleged Incidents of Stealing in the AFC 1997/1998

Company	Country	Date	Alleged Incident
Bangkok Bank of Commerce	Thailand	1996-97	Bank managers moved money to offshore companies under their control
United Engineers (Malaysia) Bhd.	Malaysia	1997-98	United Engineers bailed out its financially troubled parent, Renong Bhd., by acquiring a 33% stake at an artificially high price.
Malaysia Air System Bhd.	Malaysia	1998	The chairman used company funds to retire personal debts.
PT Bank Bali	Indonesia	1997-98	Managers diverted funds in order to finance a political party.
Sinar Mas Group	Indonesia	1997-98	Group managers transferred foreign exchange losses from a manufacturing to a group-controlled bank, effectively expropriating the bank's creditor and minority.
Samsung Electronics Co.	Korea	1997-98	Managers used cash from Samsung Electronics to support other members of the Samsung group (notably Samsung Motors) that were losing money.
Hyundai	Korea	1998-99	Managers of a Hyundai-controlled investment fund channelled money from retail investors to loss-making firms in the Hyundai group.

Sources: *Johnson et al. (2000:144)*

There is evidence to suggest that the expropriation of minority shareholders was prevalent and severe during the East Asian crisis (Mitton 2002). One example comes from Malaysia, whereby United Engineers Malaysia (UEM) bought 32.6% of the shares of Renong, its financially troubled parent, in November 1997. This action has been interpreted by UEM's minority shareholders as a financial bailout of Renong at an inflated price, with the result that UEM's stock price fell by 38% on the day that the transaction was announced (Arjuna 2000). In another case from Korea, the minority shareholders of Samsung Electronics protested against the actions taken by

the firm, since it had been providing debt guarantees to a few less-successful Samsung group companies, and these guarantees were often not disclosed (Acemoglu and Johnson 2003). Other cases of expropriation by management or controlling shareholders at the expense of minority shareholders are described briefly, and can be seen from the table. In summary, generally, most debt defaults triggered by the Asian Crisis of 1997/1998 have resulted in investors receiving none of the liquidation value (Johnson et al. 2000). It may be noted that in many of these cases, controlling shareholders did not violate any local laws in order to expropriate minority shareholders. Accompanied by the fact that the management in most of the emerging countries is also the controlling shareholder, this makes these transfers effortless to achieve (Johnson et al. 2000; Khatri et al. 2002).

La Porta, Lopez-de-Silanes, Shleifer and Vishny (1997) assert that the governance mechanisms applied in order to protect the rights of creditors and minority shareholders determine how the firms are funded, which varies between countries. Based on the observations made in 49 countries, their findings suggest that weak shareholder rights and poor company performance leads to underdeveloped capital markets. Johnson et al. (2000) share a similar view, adding that weak enforcement of shareholder rights tremendously impacts the stock market and the extent of exchange rate depreciation.

According to Rajan and Zingales (1998), protecting investors' rights is not important while growth lasts, because during the euphoric inflow period of capital from investors, managers do not want to steal. It may even be possible to attract a great deal of outside capital during the period when the economy is expanding. The investors may at first have ignored the weaknesses of East Asian firms before the crisis begin. However, when the growth prospect declines, the lack of good corporate governance becomes important. In the case of the AFC 1997/1998, investors quickly pulled out their investment because they believed that the region lacked adequate institutional protection for their investment (Rajan and Zingales 1998), where managers are led to expropriate more as the expected return on the investment falls (Mitton 2002).

Without an effective shareholder protection mechanism, a mild shock can entail a huge increase in stealing, which in turn results in a large depreciation. Thus, Johnson et al. (2000) posit that managerial agency problems can cause countries with poor legal systems to become vulnerable to the effects of an abrupt loss of investor confidence. The crisis could become a force factor for investors causing them to recognise and take account of the corporate governance weaknesses in corporations that have existed all along (Mitton 2002). As Asian countries share similarities in terms of controlling shareholders and weakly enforceable minority shareholders rights, then they are particularly vulnerable and could have lost relatively more value during the crisis.

On the other hand, the AFC 1997/1998 can be considered as remarkable in several ways. The crisis struck the most rapidly growing economies during that time and sparked off the largest financial bailouts in history (Radelet and Sachs 2000). It was the least anticipated financial crisis in years (Li 2003). The collapse of the involved countries was not mainly because of the lack of resources to support their economies, but also because of the “euphoria inflow” of capital that could not be retained; this can be understood as a “crisis of success”, which was caused by a significant upsurge of international inflow, followed by an abrupt withdrawal of funds (Radelet and Sachs 2000). Zainuddin⁶ (1998) allege this financial turmoil as a “crisis of confidence”, where a loss in confidence by investors (especially foreign investors) on the capital market had been triggered by a lack of transparency and efficiency in corporate governance.

According to the report by the World Bank (1993), during the second half of the twentieth century, East Asia witnessed the world’s highest economic growth. For more than two to three decades, many countries in this region experienced double-digit annual growth. Since this favourable growth was not anticipated, it was known

⁶ Daim Zainuddin was held responsible to 'manage' financial crisis in Malaysia by his appointment as the executive director of the National Economic Action Council (NEAC). This body has played a crucial part in promoting strategies to combat the crisis (Liew 2008).

as the “East Asian Miracle” which was widely acclaimed by the World Bank and international financial institutions like the IMF. The consistent and high interest rates became one of the main attractions for foreign investors to choose this region as their locus of investment. In addition, there are a few other explanations provided by Calvo, Leiderman and Reinhart (1996) for the causes of the capital inflows to Asia in the 1990s, which in brief can be referred to in the footnote number 7 below⁷.

However, there are drawbacks noted by Calvo et al. (1996), who claim that the large capital inflows received by the developing countries on the other hand tend to cause rapid monetary expansion, real exchange rate appreciation, inflationary pressure, and widening current account deficits. These undesirable macroeconomic effects have rendered the economy more vulnerable to foreign shocks. Kim (2000) explains that when the inflow of foreign capital is distracted, the economy experiences inverse adjustments in the current account and exchange rate. These shocks obstruct the functioning of the economy and afterwards the growth momentum (Thanoon, Baharumshah and Rahman 2006). The adjustment process due to these unfavourable shocks in capital movement can be severe, as proven in a few episodes of debt crisis (Kim 2000).

Malaysia is one of those countries that were badly hit by this financial crisis. As a developing country, weakness of corporate governance is considered to be one of the significant factors that contributed to the crisis. The following subsections provide the chronological facts concerning corporate governance in Malaysia before, during, and after the crisis. An understanding of the background of Malaysia, the consequences of the crisis and the reaction by the government to solve this problem will provide a

⁷ In brief, the capital inflows to developing countries in the 1990s are explained by Calvo et al. (1996) as being triggered by a few factors. Among them are i) the recession that hit the United States, Japan and many European countries, made Asian countries more attractive for investment, ii) there was an escalating trend where life insurance companies entered into emerging markets to explore more profitable investments and iii) the changes in regulation in the US and European countries, has facilitated the investors to invest in foreign firms. A more detailed explanation can be found in Calvo et al. (1996).

better analysis of the role of corporate governance in Malaysia and how corporate governance could potentially help to attract international capital inflow to the country.

2.4 Corporate Governance in Malaysia

According to Liew (2007), up until the 1997/1998 AFC, corporate governance practices in Malaysia were not a matter of concern. This was according to the view of many international bodies, in particular the report from the World Bank (1993) which concluded that East Asian countries (including Malaysia) had managed their economies efficiently and had effective public institutions and governance. This view, however, changed precipitately following the 1997/1998 Asian turmoil when the poor practice of corporate governance was blamed as one of the main factors that had exacerbated the crisis.

As mentioned previously, the scandals in the USA, as well as the 1997/1998 AFC, have been viewed as a strong case for healthier corporate governance and transparency among Malaysian corporations. The Malaysian corporate landscape itself has been disgraced by a couple of cases such as Renong, UEM, Perwaja Steel, Transmile, Malaysia Airlines System (MAS) and a few others, due partly to a deficiency in corporate governance mechanisms (Haniffa and Hudaib 2006). It was suggested that the eroding of investor confidence in Malaysia was caused by the country's defective corporate governance standards and the transparency problems in the financial system (Noordin 1999; Sam 2007; Suto 2003; Zainuddin 1998).

Therefore, reforms in corporate governance came to be viewed as a way of managing the crisis. This reformation was advocated by a few international bodies, including the World Bank, the IMF, the Asian Development Bank and the Malaysian government itself. Thus, Zulkafli et al. (2005) posit that the discussion of the historical background of corporate governance in Malaysia, as well as other East Asian countries, should be commenced from the time of the East Asian economic meltdown in the second half of 1997. This is further supported by Suto (2003), who considers that the institutional framework of the country should be sufficiently taken into account. Therefore, the

following discussion will attempt to provide a possible explanation for the historical and institutional development of corporate governance in Malaysia. This will be followed by a discussion of the initiatives taken by the Malaysian government to reform corporate governance, with the intention of creating a better image for the country in order to attract more foreign investors.

2.4.1 Malaysia before the 1997/1998 Financial Crisis

Malaysia just prior to the financial crisis could be described as a fast developing country. Its corporate sector in the 1990s experienced rapid growth compared to other East Asian countries. An average annual growth rate of 10.9 per cent was recorded for listed companies throughout the 1990s in Malaysia, compared to 10 per cent, 7 per cent and 1 per cent in Indonesia, Thailand and South Korea respectively (Khatri 2001). In addition, according to Liew (2007), the total market capitalisation for companies listed on the main and second boards of the Malaysian stock exchange increased at an annual average of 40 per cent which was largely driven by increasing shares and a high level of new equity issues and privatisations. It is believed that the development of the Malaysian corporate sector was closely linked to the government's policies in developing the private sector to promote industrialisation while restructuring society in terms of participation and ownership.

During the period preceding the crisis, Asian countries had several years of strong economic growth. Malaysia, in particular, achieved a real gross domestic product (GDP) growth of 8.5 per cent between 1991 and 1997, with per capita income increasing twofold in terms of U.S. dollars by 1997, and the incidence of poverty falling from 16.5 to 6.1 per cent (Ministry of Finance 2002). It was expected that the sustainable growth rate would continue, propelling Malaysia to achieve its developed status by 2020, generally known as Wawasan 2020⁸ (Vision 2020), one of the

⁸Wawasan 2020 or vision 2020 was articulated by Tun Dr Mahathir Mohamad, 4th Prime Minister of Malaysia. It is where the nation must be fully developed along all the dimensions: economically, politically, socially, spiritually, psychologically and culturally. They also need to be fully developed in terms of national unity and

government's long term visions. However, instead, the Malaysian economy drastically moved to a lower plateau in the aftermath of the AFC 1997/1998 (Thanoon et al. 2006). The precipitous fall of equity prices was reflected in this financial turmoil, which witnessed the plummet of the Kuala Lumpur Composite Index by 72% during the period end-June 1997 to end-August 1998 (Zulkaflī et al. 2005).

Weakness in corporate governance was considered to be one of the significant reasons for the collapse of a few giant companies in Malaysia during the financial crisis of 1997/1998 (Kim 1998; Khas 2002; Samad and Wilson 2002), or it at least accelerated the deterioration (Suto 2003). Poor corporate governance, weak investor relations, a low level of transparency in disclosing information by companies listed on the Bursa Malaysia and the ineffectiveness of regulatory agencies in enforcing legislation in punishing offenders and protecting minority shareholders are all partly blamed as reasons for the collapse of several Malaysian companies (Mohamad 2002; Zainuddin 1998). This led the government to take prompt action, and to produce a rescue package for the country (Haniffa and Hudaib 2006) consisting of a series of reforms that had significant impact on the corporate governance structure.

Despite the harsh criticism of the weakness of corporate governance practice, in reality, corporate governance in Malaysia is not considered to be something new. Starting as early as 1993, efforts had been taken to improve the governance practices of public listed companies (PLCs) in Malaysia when Kuala Lumpur Stock Exchange (KLSE) listing requirements made audit committees mandatory (Haniffa and Cooke 2002). Good corporate governance practices were further emphasised by the Malaysian Securities Commission following the move from a merit-based to a disclosure based regulatory regime in 1995. Although a series of corporate governance mechanisms were introduced, the implementations were very naïve. Othman (1999) claims that the mechanisms for ensuring compliance and enforcement

social cohesion, in terms of economy, in terms of social justice, political stability, system of government, quality of life, social and spiritual values, national pride and confidence.

were inefficient, whilst the penalties imposed for breach were an inadequate deterrent, especially during times of economic tension.

The main features of the corporate sector in Malaysia, like its East Asian neighbouring countries, are the high level of ownership concentration, cross-holdings and the significant participation of owners in management – an insider system of corporate governance (Khatri 2001). According to Khatri et al. (2002), these features have resulted in some innate vulnerabilities in the countries concerned. The cross-holding structures can create incentives for double gearing, thus creating a multiplier effect in the sensitivity of corporate wealth changes in the equity market (Kochhar 1999). In addition, concentration shareholding can lead to poor governance, as a small group can exercise control over a firm and pursue their objectives at the cost of the outsiders or minority shareholders (Claessens et al. 1999).

Lim (1981), in his study of the 100 largest companies in Malaysia, found a high degree of concentration at various structure levels. A major proportion of the financial assets and the productive capacity of the corporate economy were concentrated in a few large companies at the first structure and in the next structure. The concentration was at the level of share ownership, where shares were not widely distributed and were concentrated in the hands of a few institutional and corporate investors. Finally, the concentration was of control over the large companies. A complex system of interlocking and pyramiding share ownership had developed which enabled a few individuals and entities to control an amount of capital which was many times more than what they actually owned (Khatri et al. 2002).

The problem with ownership concentration in Malaysia is not so much the general separation of management and control commonly experienced by most industrialised nations, but the domination in most companies by large shareholders who exercise control rights, putting minority shareholders at high risk (Claessens et al. 1999). Claessens et al. (1999), in their study of 2,980 publicly traded companies, in nine East Asian countries (Hong Kong, Indonesia, Japan, South Korea, Malaysia, the Philippines, Singapore, Taiwan and Thailand), found that 67.2 per cent of the sample

of Malaysian firms was family-controlled and 28.3 per cent of market capitalisation was controlled by 15 families. From further investigation, they also discovered that 39.3 per cent of Malaysian companies used pyramid structures as a means to enhance control, and 14.9 per cent of Malaysian companies had some cross ownership. Other notable percentages are as follows: 37.4 per cent of the sampled Malaysian firms were controlled by mainly a single large shareholder, 85 per cent of the same samples had managers (CEOs and or chairpersons) who were a member of the controlling family or a nominee (Claessens et al. 1999).

In addition, based on the analysis by the World Bank (2001) of the Malaysian capital market, almost half of the public listed companies belonged to the five largest shareholders. These shareholders generally owned 60 per cent of the outstanding shares and more than 50 per cent of the voting shares. La Porta et al. (1999), in their earlier study, also found a high degree of ownership concentration in Malaysia, where the average share of common equity owned by the three largest shareholders in the ten largest companies was 54 per cent compared to 19 per cent and 20 per cent in the UK and US respectively.

The study conducted by Haniffa and Hudaib (2006) verified the findings of La Porta et al. (1999) and Claessens et al. (1999), namely that there is a high concentration of ownership in Malaysia (as elsewhere in Asia). They found that the mean shareholdings of the single and largest shareholder and the five largest shareholders of the companies in their study were 31% and 62% respectively, which implies that the protection of minority shareholders may be problematic. In summary, as concluded by Liew (2007), companies in Malaysia are typically controlled by a small group of related parties and managed by owner-managers. Claessens et al. (1999) claim that the concentration of shareholding can lead to poor governance, as a small group can exercise control over a firm and pursue the objectives of the insiders at the cost of the outsiders, or minority shareholders.

These inheritance problems (high level of ownership concentration, cross-holdings and significant participation of owners in management) have drawn attention to the

requirement for maintaining corporate governance standards, increased transparency and improved investor relations, while the market regulatory agencies such as the Securities Commission (SC), Bank Negara Malaysia (BNM) and Bursa Malaysia should enforce more effective legislations. However, Zulkaflī et al. (2005) claim that the mechanisms that have been used in Malaysia were comprehensive enough, and appropriately covered all areas of corporate governance both internally and externally. The following sections discuss the development of corporate governance in Malaysia and the regulatory bodies or institutions that are responsible for improving corporate governance in Malaysia.

2.4.2 Development of Corporate Governance in Malaysia

The reform agenda for corporate governance in Malaysia has taken place since the AFC 1997/1998. Three main institutions - the Finance Committee on Corporate Governance (FCCG), the SC and the BNM - were responsible for the evolution of corporate governance straight after the crisis by introducing the Codes and guidelines as seen below. The direction, principles, best practices and future prospects of corporate governance in Malaysia are discussed in the three following sections.

2.4.2.1 Malaysian Code of Corporate Governance (MCCG)

The release of the Code marked the importance of the corporate governance system in Malaysia. Corporate governance in Malaysia is set up based on the Anglo-Saxon approach, as in the US and UK (Haniffa and Hudaib 2006). Based on the High Level FCCG Report (1999), corporate governance has been defined as:

“Process and structure used to direct and manage the business prosperity and corporate accountability with the ultimate objective of realizing long term shareholder value, whilst taking into account the interests of other stakeholders”

This definition is retained in the latest version of Malaysian Code on Corporate Governance (MCCG) 2012. The first Code of corporate governance was issued in March 2000. It is the main cornerstone of the corporate governance reforms agenda in Malaysia (Ponnu 2008) as it provides guidelines on the principles and best practices in corporate governance and the direction for the implementation. It also charts the future prospects of corporate governance in Malaysia.

In addition, the Code consists of the optimal corporate governance structures and internal processes. The principles underlying the report focus on four areas including: the board of directors, director's remuneration, shareholders and accountability and audit. The Code became effective through the revamped Listing Requirements of the KLSE in January 2001. Compliance with the Code is not mandatory but listed companies are required - under the listing requirements of Bursa Malaysia - to include in their annual report a narrative account as to how they have applied the principles and best practices set out in the Code. Since the release of the Code, the Malaysian corporate scene has made significant strides forward in its corporate governance standards.

The Code was then reviewed and revised in 2007 to further strengthen corporate governance practice in line with the developments in the domestic and international capital markets. The fifth Prime Minister of Malaysia, Dato' Seri Abdullah Ahmad Badawi, had announced in the Budget 2008 speech that:

“the Code is being reviewed to improve the quality of the board of public listed companies (PLCs) by putting in place the criteria for qualification of directors and strengthening the audit committee, as well as the internal audit function of the PLCs”

Key amendments to the Code are aimed at strengthening the board of directors and audit committees, and ensuring that the board of directors and audit committees discharge their roles and responsibilities effectively. The Code has been revised by

considering the feedbacks and comments made by the related bodies which represent the continued collaborative efforts between the Government and industry.

Then, in July 2011, The SC Malaysia released the Corporate Governance Blueprint 2011, which sets out the desired corporate governance landscape going forward. The crux of the Blueprint is to achieve excellence in corporate governance through strengthening self and market discipline, promoting good compliance and corporate governance culture. From this Blueprint, The *Malaysian Code on Corporate Governance 2012* (Code 2012) was recently issued. Code 2012 focuses on strengthening the board structure and composition, recognising the role of the directors as active and responsible beneficiaries. It has emphasised the duty of directors to be effective stewards and guardians of the company, not just in strategic direction and overseeing the conduct of business, but also in ensuring that the company conducts itself in compliance with laws and ethical values.

2.4.2.2 Capital Market Master Plan (CMP)

The introduction of the CMP by the SC is considered important in that it charts the direction of the Malaysian capital market for the next ten years. It was initially announced by the Second Finance Minister and the Chairman of the SC on August 6, 1999. In December 2000, the Minister of Finance approved and subsequently launched it in February 2001. The vision of CMP is to provide a platform for the efficient mobilisation and allocation of funds, as well as to give a high degree of confidence to market participants. A key strategic point in CMP is the good corporate governance of public listed companies, enabling investors to do business in a better and more conducive corporate environment in Malaysia.

2.4.2.3 Financial Sector Master Plan (FSMP)

Bank Negara Malaysia also plays an important role in charting the future direction of the financial sector after the AFC 1997/98 by launching the FSMP. The FSMP's objective is to develop more resilient, competitive and dynamic financial systems

which contribute to economic growth and technology-driven development. Corporate governance elements have been nurtured in this plan by promoting shareholders' and consumers' activisms, regulatory control and priority sector financing.

2.4.3 Corporate Governance Regulatory Bodies in Malaysia

Complementing the development of corporate governance in Malaysia, institutional development has moved forward. A few institutional bodies have been established, including the High Level FCCG, the MICG and the MSWG, in order to strengthen the changes that have taken place in corporate governance mechanisms and practices. Their functions, objectives and related issues are discussed in the following subsections.

2.4.3.1 High Level Finance Committee on Corporate Governance (FCCG)

On 24 March 1998, the minister of finance announced the establishment of the high level FCCG. The committee, which is comprised of senior representatives of the government, regulatory agencies, industry bodies and professional associations, was given a mandate to review the practice of corporate governance in Malaysia and to recommend legal reforms that potentially strengthen the effectiveness of corporate governance (Haniffa and Hudaib 2006; Nor Azizah and Halimah 2007). A number of deficiencies in corporate governance practices have been recognised in the country, which are mainly attributable to ownership concentration, the efficacy of boards of directors, shareholder passivity, enforcement mechanisms, and the lack of responsibility awareness by directors (Othman 1999). Besides, weaknesses were also identified in a few areas, – e.g. the transparency and disclosure requirement and the right of minority shareholders.

In March 2000, the FCCG issued the MCCG based on the earlier report that they had produced. The MCCG is largely derived from the recommendations of the Cadbury Report (1992) and the Hampel Report (1998) in the UK (Code 2000; Haniffa and Hudaib 2006). The report consists of 70 recommendations relating to three matters: (i)

the proposed Code; (ii) the reform of laws and regulations on the duties of directors and officers, improving disclosures, enhancing the rights of shareholders and improving the effectiveness of company meetings; and (iii) the training and education of directors. The aim is to set the practices for the industry, as part of a series of government measures to boost confidence in the Malaysian economy.

2.4.3.2 Malaysian Institute of Corporate Governance (MICG)

The MICG was established under the Companies Act 1965 in March 1998 by the High Level FCCG. Many objectives have been outlined to be achieved by MICG, among them to provide consistent education and to raise awareness of the practice of good corporate governance among corporate participants, the investing public and corporations. The importance of good governance is emphasised in enhancing long-term shareholder value, company financial viability, and to provide advisory, technical and support services to assure the successful implementation of corporate governance best practice. MICG working closely with the relevant authorities and regulatory agencies to make this feasible.

2.4.3.3 Minority Shareholders Watchdog Group (MSWG)

In order to protect the interests of minority shareholders, the government of Malaysia has taken the initiative of establishing the MSWG in the year 2000. Over time, MSWG has evolved to become an independent research organisation to investigate corporate governance matters in Malaysia's corporate environment. MSWG provides a platform for the collective voices of minority shareholders to encourage good governance practice amongst Malaysian PLCs with the aim of increasing the shareholders' value over time. Among the main functions of MSWG is the provision of advice to minority shareholders during the voting process in the Annual General Meeting (AGM) and the Extraordinary General Meeting (EGM) of public listed companies. The establishment of MSWG is believed to be the first step taken by the government to encourage shareholder activism without recourse to courts.

There are number of ways to achieve the aim of MSWG, and among them are monitoring any breach and non-compliance in corporate governance practice by PLCs, developing and disseminating the educational aspects of corporate governance, becoming a resource center for minority interests and corporate governance matters in Malaysia and a few others as listed in the MSWG objectives as set out in a Charter under its Memorandum and Articles of Association. For more information about the MSWG, please refer to this link: <http://www.mswg.org.my/web/page>.

The structure of the evolution of corporate governance in Malaysia may be summarised in the following figure:

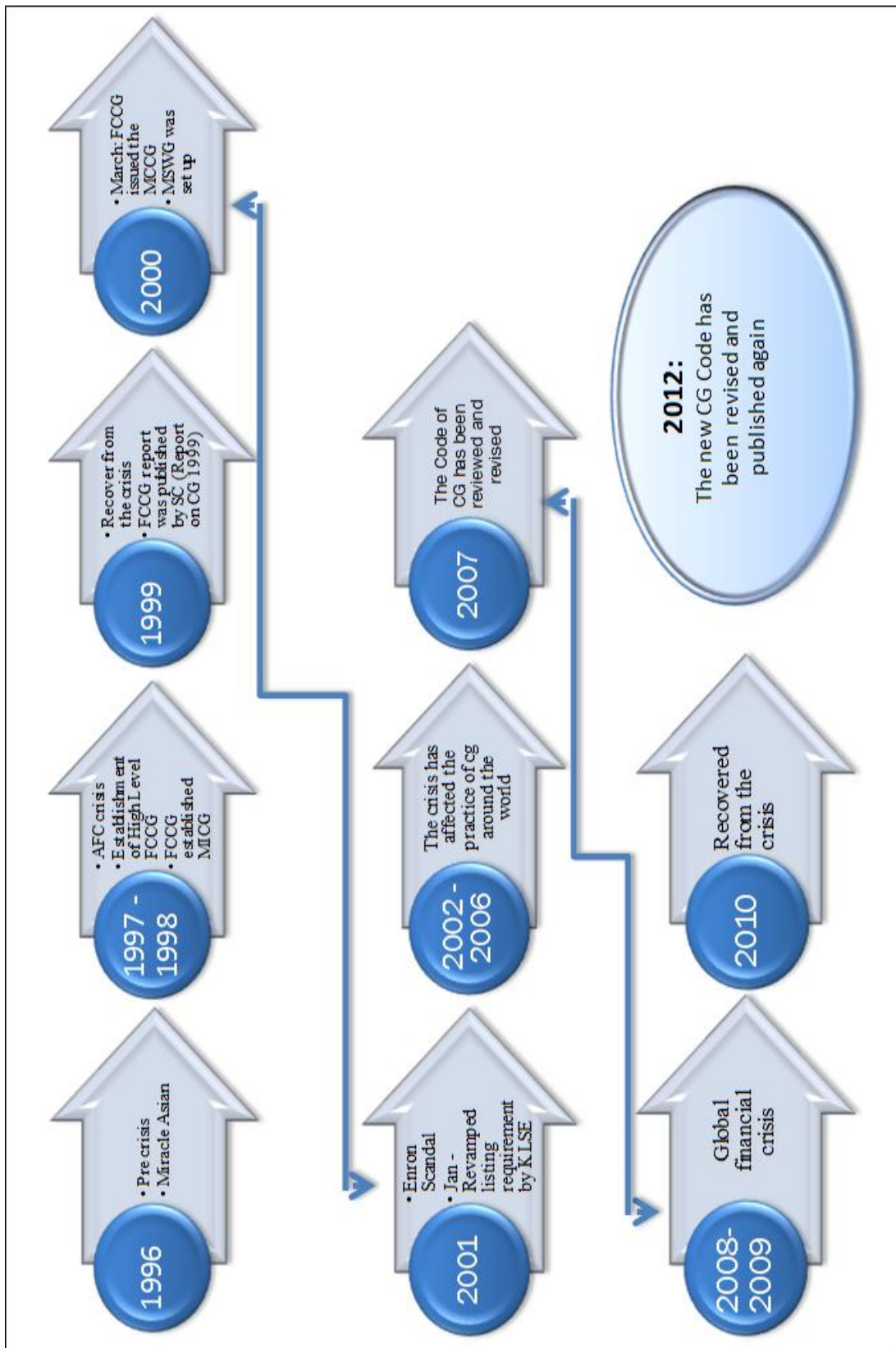


Figure 2.4: Background of the corporate governance structure in Malaysia 1996 - 2012

2.4.4 The Institutions: Performance, Challenges and What Lies Ahead?

Malaysia is one step ahead in promoting and developing a comprehensive corporate governance system compared to her neighbouring countries. This claim is based on the survey conducted by KLSE-PricewaterhouseCoopers in 2002, where the results indicate that 93% of the investors agreed that Malaysia's standard of corporate governance has improved since the introduction of the Code.

Although positive feedback has been received from investors, Malaysian corporations are yet to achieve a satisfactory level of corporate governance practices and compliance. The joint study conducted by the emerging market investment bank CLSA and Asian Corporate Governance 2003, ranked Malaysia as number one (9 out of 10) in terms of rules and regulations but only managed to obtain an average score of 5.5 out of 10 for overall corporate governance practice (Zulkafli et al. 2005).

Considerable numbers of studies have been conducted to measure the impact of the Code. One such study has compared Singapore, Malaysia and Thailand, and it was found that Singapore offers the best corporate governance environment in Asia, while Malaysia has shown significant improvement since 2001. However, Thailand lags behind (CLSA 2001; 2003). A later study by Allen (2005) indicates the same result for Singapore, but that Malaysia and Thailand have improved. Chuanrommanee and Swierczek (2007) have otherwise argued that the practice of corporate governance only applies in the documents of companies and does not have an impact on company performance. The implication of this claim is that corporate governance in Asian countries is more an illusion than a fact.

Tam and Tan (2007) claim that the Code as introduced is not convincing enough to address the significant issue of the expropriation of minority interests by controlling shareholders, as the rapid growth of Malaysia's economy has not diluted the concentrated ownership structure in Malaysian firms. The inception of MSWG provides an avenue to protect the interest of minority shareholders. Unfortunately, the effectiveness and independence of the group still invites scepticism as the board of

directors and the management of MSWG are dominated by the key players from the trust funds, which are also the large institutional shareholders in the corporate sector.

Hence, Tam and Tan (2007) suggest the increasing of independence and transparency among policymakers and officers as a key to more effective corporate governance standards and practices in Malaysia. They further suggest that corporate governance in Malaysia needs to be better at being able to scrutinise and perhaps restrain the power of larger shareholders in order to protect the interests of minority shareholders. The views of many parties - for example shareholders, stakeholders, Bursa Malaysia, MICG, MSWG, etc. - are sought to understand the practicalities, challenges and expectations of inculcating high standards of corporate governance in listed companies and to ensure that the necessary principles and recommendations of best practices, to meet those standards, are available.

Malaysia, as a developing country requires a huge amount of capital in order to sustain its economic growth. Foreign investors are the main capital contributors, and play a crucial part in realising the country's Vision 2020. However, they view investment more cautiously by relying heavily on corporate governance practices, which stress investor protection to ensure that their investments are safe and not expropriated by the substantial shareholders. Thus, the following sections and sub-sections of this chapter will discuss foreign investment and corporate governance in Malaysia's setting in greater detail.

2.5 Foreign Investment

Domestic sources of outside finance are limited in many countries around the world (Giannetti and Koskinen 2010). In response to this, many capital markets have been liberalised (Li 2003). Das (2014) addresses this as a privilege to foreign investors to make cross-border diversification, whilst on the other hand, Bekaert et al. (2002) imply that this is an opportunity for the developing capital market to access sources of finance from outside investors which apparently becomes increasingly important. Therefore, the study of foreign investment is not considered to be something new, as

many researchers believe that the benefits which could be derived from this activity are indisputable (Chihuang and Cheng-Yi 2001; French and Poterba 1993; Leuz et al. 2010; Tesar and Werner 1995)

Flows of international capital to developing countries have had a significant impact on the growth of their economies. According to Hoti (2004), these outside sources for developing countries have fluctuated significantly over the last three decades. They help to finance investments, and simultaneously stimulate economic growth, thereby smoothing out consumption and subsequently increasing the standard of living in the countries (Calvo et al. 1996). In addition, Aggarwal et al. (2005) assert that the demand for emerging firms' shares can lower their capital cost (Das 2014) and enable them to compete more efficiently in the global market. On the other hand, developed countries, through their portfolio investment in developing markets, can gain a better international diversification, which provides support for pension funds and their future retirement accounts (Calvo et al. 1996; Hoti 2004). During the period 1970 - 1990, international capital flows to emerging countries were mainly in the form of direct lending from banks to governments and/or to the private sector. However, in the 1990s, capital flows took the form of foreign direct investment (FDI) and portfolio investment, hereafter in this study referred to as foreign equity ownership (FEO).

This study will focus on FEO, which has played a crucial role, since the investment mostly incurs a large amount of money, which can stimulate the growth of a company as well as the country. Given the growing significance of foreign financing and the fact that access to foreign capital may well be uneven across firms and countries, it is important to have a deeper understanding of the factors that make investors shy away from providing capital to foreign firms (Leuz et al. 2010). It is understood that only selective companies are able to attract foreigners to invest and inject capital into their companies. A number of articles (for example, Aggarwal et al. 2005; Dahlquist and Robertsson 2001; Das 2014; Kang and Stulz 1997; Leuz et al. 2010; Lin and Shiu 2003 etc.) have determined that there are certain attributes and criteria that contribute to this event.

Lin and Shiu (2003) posit that global investors are believed to make their investment selection by considering specific factors that can benefit them. Empirical evidence concerning the main causes of international capital inflows, in general, are mixed. Hoti (2004) believes that there are various factors which have influenced the decisions of foreign investors regarding driving capital inflows into emerging markets whether at country level or firm level. Based on the results exhibited by Aggarwal et al. (2005), steps can be taken at both levels to attract foreign capital and create an environment conducive to foreign investors.

2.5.1 Foreign Investment at Country Level

At the country level, Boubakri, Cosset, Guedhami and Omran (2007) have examined the determinants of foreign investors' involvement in the privatization process of developing countries. Results show that such investors prefer to invest in an investor-friendly institutional environment which is strong in shareholder rights and interest protection (Leuz et al. 2010), in larger firms in high growth economies, and in socially stable countries. Delois and Beamish (1999) studied Japanese behavior in nine countries in the South East Asia region, and reported that international experience is an advantage, and a strong institutional environment can also lead to an increase in the equity acquisition of the foreign investor. Aggarwal et al. (2005) find that US funds invest more in open emerging markets with better accounting standards, shareholder rights, and legal frameworks. High quality accounting information allows foreign investors to monitor, protect their investment and efficiently allocate investment.

La Porta et al. (1997) postulate that investor protection at the country level has a positive impact on market development. For example, even though foreign investors disfavour a company with a high level of insider ownership, which is likely to be associated with opportunistic behavior such as expropriation, they still have the faith to invest if the countries have strong laws and enforcement agencies to monitor their local companies (Leuz et al. 2010). A strong institutional environment, which emphasises investor protection, may make it difficult and costly for insiders to manipulate a firm's wealth and activities. Hence, a strong institutional environment

can be associated with fewer governance problems. However, this finding contradicts the results of Das (2014), who argues that a firm's level of corporate governance plays an important role in attracting foreign investors. It is not a substitute for country level governance as suggested by Leuz et al (2010), but rather they act as a complement to each other.

2.5.2 Foreign Investment at Firm Level

At the firm level, the study conducted on Swedish firms shows that foreign investors favour larger firms, firms paying low dividends, and firms with a large proportion of cash position (Dahlquist and Robertson 2003). They also found that market liquidity and presence in the international market, measured through export sales or listing on other exchanges, seems to attract more foreign holdings. Similarly, Aggarwal et al. (2005) noted the preference of U.S institutional investors for allocating their investments to emerging equity markets. In addition, the qualities of the auditor (Das 2014), the preparing of a consolidated financial statement, and the use of a reliable, internationally-recognised accounting standard are also dominant determinants for foreign investors to allocate their investments.

Associated studies, for example, Kang and Stulz's (1997) study of the Japanese market, have reported that foreign investors favour large firms and firms that have a considerable proportion of export sales in international markets. This is consistent with the findings of Lin and Shiu (2003) concerning the Taiwan stock market. In addition, Kang and Stulz (1999) discovered that foreign investors in Japan tend to underweight smaller and highly leveraged firms. Covrig, Lau and Ng (2006) have investigated foreign funds' manager behaviour in investment allocation decisions and they arrived at similar conclusions. Falkenstein (1996) investigated a cross-section of U.S. open-ended mutual fund equity holdings for the years 1991 and 1992, and revealed that mutual funds have a significant preference for firms with high visibility and low transaction costs.

The analysis by Dahlquist and Robertson (2003) revealed that foreign and institutional ownership can be characterised by similar attributes. Their finding supports the results of Falkenstein (1996) and Gompers and Metrick (1999). Falkenstein (1996) documented that U.S mutual funds tend to diversify their portfolio towards large firms, whilst Gompers and Metrick (1999) found that American institutions invest in firms that are larger, more liquid, and have had relatively low returns during the previous year. These findings mirror the study by Dahlquist and Robertson (2001) regarding foreigner investing in Sweden.

However, Leuz et al. (2010) and Das (2014) contend that information problems are likely to play a major role in investment decisions. Therefore, foreign investors avoid investing in poorly governed firms, as they are at an informational disadvantage compared to the local investors. These information asymmetries are particularly pronounced when it comes to evaluating a firm's governance and ownership structure. Many firms around the world are family-controlled or family businesses. The control structures that arise from this type of management structure are often complicated, and can provide minimal protection to the outside investor's rights (La Porta et al. 1997, 2000). As a consequence, firms with potentially problematic governance structures are particularly avoided by foreign investors as they will add to their information and monitoring cost (agency cost) (Leuz et al. 2010).

2.5.3 Home Bias

Coval and Moskowitz (1999), on the other hand, find evidence of a preference among U.S. investors for geographically close investments. This is consistent with the model proposed by Merton (1987), which indicates that investors rationally invest in firms which are better informed and well protected; as has been phrased by Huberman (2001), "familiarity breeds investment". Another popular term in foreign investment literature is that of "home bias". This refers to the explanation about why investors show a preference for investing in their home countries (Dahlquist and Robertsson 2001). Their explanation is that international investors face barriers, either implicit and/or explicit, in selecting and investing in a firm's shares.

Explicit barriers include foreign exchange control, withholding taxes and other directly observable obstacles. However, many believe (Cooper and Kaplanis 1994; French and Poterba 1993; Tesar and Werner 1995) that explicit barriers no longer exist in developed markets. Implicit barriers, on the other hand, include political risk and informational asymmetries. Investors prefer not to make investment in countries with political uncertainty, as they are afraid of facing trouble in retrieving their income and capital (Dahlquist and Robertsson 2001). Foreign investors also try not to get involved in a country or firm where they find less information available to them, as suggested by Merton (1987), Huberman (2001) and Kim et al. (2010), who argue that investors prefer firms with which they are familiar. This is also suggested by Leuz et al. (2010); information problems faced by foreign investors are more prevalent in countries with low disclosure requirements and poor and weakly enforced governance rules and investor protection. More detail on information asymmetry will be given in the following section.

2.5.4 Information Asymmetries

It is well explained in many studies that foreign investors are in an adverse position in terms of obtaining information in relation to local investors (Choe, Kho and Stulz 2005; Das 2014). In obtaining the information, foreign investors have to incur extra costs, which make the investment more expensive to them. With incomplete information due to cross-border investment, foreign investors are prone to underweight the stock, and prefer to find the stock with which they are familiar (Merton 1987). This predicted behavior is explained by Leuz et al. (2010) when they claim that foreign investors find it difficult to estimate the real value and risks associated with the firms, and are therefore unable to predict how far expropriation can be pervasive. The claim made by Merton (1987) has received special attention, and evidence is offered to support his view (for example, Covrig et al. 2006; Kang and Stulz 1997). The results reinforce the view that foreign investors decline to invest in stock with an information asymmetry problem.

Nevertheless, the information asymmetry problem can be overcome by foreign investors if they invest in firms with better corporate governance practices (Das 2014). It is well accepted that corporate governance is one of the tools which can be used to reduce the information asymmetry problem and it can lower the monitoring cost (Shleifer and Vishny 1997). Furthermore, there are more benefits to be gained from good practice corporate governance, for example in terms of firm performance (Weir and Laing 2000), increased CEO turnover related to poor performance and the CEO duality issue (Dahya et al. 2002), changes in board structure, and the proportion of independent directors (Stiles and Taylor 2001), etc. Therefore, foreign investors and the link with corporate governance is given special attention by researchers, especially after the AFC 1997/1998 (Bokpin and Isshaq 2009).

2.6 Foreign Investment and Corporate Governance

As mentioned above, growing interest in the issue of foreign investment and corporate governance was given a boost especially after the AFC 1997/1998. Other benefits can be generated from the good practice of corporate governance in firms. It is widely accepted that corporate governance generates investor goodwill and confidence (Bokpin and Isshaq 2009) and enhances the flow of information in firms (Ferreira and Laux 2007). Furthermore, there is evidence that countries with effective corporate governance systems attract investors beyond their boundaries (La Porta et al. 1999), and simultaneously, this helps local companies to prosper (World Bank 2000). At the same time, the countries involved will become the investor's choice (Dunning 1993) for making investments, and concomitantly, this will contribute to economic growth (Levine 1999).

Empirical evidence also suggests that foreign investors avoid investing in developing countries because of their weak corporate governance structures and disclosure (Coombes and Watson 2001; Gibson 2003; Johnson et al. 2000; Mangena and Taurigana 2007). This is also echoed in the findings of Aggarwal et al. (2005) who claim that firms with a better accounting quality and corporate governance attract more foreign capital. Considerable numbers of previous studies (for example see La

Porta et al. 1999; Shleifer and Vishny 1997) have associated weak corporate governance with developing countries. Apparently, recent studies (Das 2014; Kim et al. 2010; Leuz et al. 2010) consistently claim poor corporate governance as one of the factors that draws considerable attention from outside investors and regulators. They assert that outside investors discount the price they are willing to pay for shares in a firm with potential governance problems. All the associated studies indicate strong evidence to show that a poor corporate governance system in developing markets may affect the inflow of foreign investment.

In addition, Dahlquist et al. (2003) suggest that there is a close relationship between corporate governance and the portfolio composition held by foreign investors. According to Cheung and Chan (2004), corporate governance has been receiving attention from regulatory bodies and practitioners worldwide since the early 1990s, with the intention of improving investor protection and providing more transparent information. This will result in enhancing the development of local capital markets and promote foreign investment to provide funds for long term economic development.

Kim et al. (2010) further argue that the assessment of corporate governance practice may result in the different decisions between foreign and local investors. The former group needs to assign higher monitoring costs in comparison to the latter group, and therefore may discount corporate governance more severely than domestic investors. Notably, Leuz et al. (2010) found evidence that US investors hold significantly lower shares in firms which have managerial control and significant family ownership, when these firms reside in countries with a poor disclosure requirement, securities regulation and investors' rights. In contrast, firms with significant managerial and family control do not experience lower foreign investment when they are domiciled in countries with a strong disclosure requirement and extensive investor protection. They also found that U.S investors, which represent about half of all foreign investment worldwide, do in fact hold fewer shares in foreign firms with a higher level of managerial and family control, as this kind of ownership structure makes it more conducive for expropriating minority shareholders.

2.7 Malaysia, Foreign Investment and Corporate Governance

The development of the equity market in Malaysia was significantly influenced by the New Economic Policy (NEP) enacted in 1971 and the Industrial Coordination Act (ICA) 1975 (Gomez and Jomo 1997). The ICA 1975 liberalised the NEP to be more “accommodative” towards non-Bumiputera and foreign investors (Heng 1997). In addition, starting in the early 1990s, foreign funds began to increase as a result of the liberalisation of capital flows, which led to a remarkable increase in portfolio investment (Suto 2003). Political stability played an important role in ensuring a business-friendly environment and vigorous growth in foreign investment, which is documented in the increase from M\$287.6 million in 1970 to M\$15 billion in 1996 (Thanoon et al. 2006). Nevertheless, not long after this, the inflow of capital once again tenses as a result of the AFC of 1997 (Tam and Tan 2007).

The Securities Industry Act (1973 and 1983) became a framework for investor protection in Malaysia (Jomo 1995). However, La Porta et al. (2000) argue that the enforcement was not effective, and thus has resulted in an adverse effect on the development of financial markets in Malaysia. In a further investigation, La Porta et al. (2000) claim that foreign investors tend to shy away from making investments in firms if the available legal framework does not guarantee their interests, and their rights cannot be protected.

According to the survey conducted by Thanoon et al. (2006), in the aftermath of the AFC of 1997, the growth of real GNP in nominal terms declined by 4.8 percent in 1998. Per capita income contracted by 1.8 percent to M\$11,835 in 1998, compared with M\$12,051 in the year before. FDI shrank from a high of M\$15.3 billion in 1997 to M\$7.1 billion by the end of 1998, mainly due to the riskiness in turbulent exchange rates following the currency crisis. Both external and internal demand fell steeply, which led to excess capacity and a tensed liquidity position. The overall financial position of the country documented a deficit in 1998 - most certainly due to the shortage of tax revenue collection, which dropped by 13.6 percent to M\$55 million in 1998 (1997: M\$70.2 million). The deficit recorded in the service account was largely caused by the higher net outflow of investment.

Foreign investors played an important role in supporting the growth sustainability of the Malaysian economy before the AFC 1997/1998 (Suto 2003). Indeed, several studies have documented the importance of foreign capital to the economic progress of Malaysia for the past two decades, for example a study by Thanoon and Baharumshah (2003) finds a positive relationship between foreign investment and economic growth in Malaysia. According to Thanoon et al. (2006), Malaysia has actively sought international funding from the United States and Japan. It is to be noted that US institutions, including mutual funds, constitute the largest sources of equity capital in the world, where collectively they hold more or less one-third of the world's foreign investment. Salina and Jarita (2009) reinforce this claim by demonstrating that on average, in 1991-2007, of the total foreign ownership in Malaysian companies, 80% came from four countries – the US, the UK, Singapore and Hong Kong: for example in 2007, the US (20%), the UK (22%), Singapore (23.2%) and Hong Kong (17.4%). More specifically, in 1991, the average value of foreign ownership from these four countries was around 94.4%. Therefore, consistent with the claim made by Leuz et al. (2010) and Thanoon et al. (2006), the major foreign investors investing in Malaysia are the US, the UK, Singapore and Hong Kong.

A considerable number of articles (for example, Dahlquist and Robertson 2001; Kang and Stulz 1997; Merton 1987; etc.) argue that foreign investors have a preference for firms having attributes with which they are familiar and about which they are well-informed. Thus, it is likely that they would place more emphasis on the firm's management, which, subsequently, disciplines them, whilst reducing the information asymmetry problem between managers and shareholders. However, Suto (2003) argues that if foreign investors were 'myopic', or not well-informed, they would not be capable of contributing to mitigating agency cost and would possibly disrupt the disciplinary function of the shareholders.

The above argument, however, was not held to be true when Suto (2003) found a negative relationship between FEO and the debt ratio in most cases. This suggests that increasing foreign ownership contributes to the disciplining of corporate management,

and this can be considered as a positive sign indicating the high profitability or high growth of firms. Interestingly, Suto (2003) also discovered a negative relationship before and after the crisis 1997. Therefore, it is believed that foreign investors, as shareholders, played a certain role in disciplining corporate management in Malaysian firms.

The following Table 2.4 provides a brief comparison of the corporate governance systems in Malaysian companies with the countries providing FEO. Based on the facts presented in the previous discussion, four major investors' countries are the US, the UK, Singapore and Hong Kong.

Table 2.4: The Comparison of Corporate Governance System in Malaysian Companies and Major Investor Countries.

Corporate Governance Practice	Countries			
	US	UK	Singapore	Hong Kong
<p>Malaysia</p>				
<p>A. Stakeholder Interest Shareholders' interest is considered as the top priority to the companies. The main objective of the companies is to maximise shareholders' values. Managers' performance are also evaluated on the basis of how well they have contributed to improving shareholders' values.</p>	/	/	/	/
<p>B. CEO Duality The roles of chairman and chief executive should be separated and not to be exercised by the same individual. The roles and responsibilities for each designation should be clearly established, set out in writing and agreed by the board.</p>	<p>Notes: Having dual role is the norm</p>	/	/	/
<p>C. Board Size There is no fixed number for board size to be applied. It is not prescribed in any of their rules and regulations.</p>	<p>/</p> <p>Notes: Board</p>	/	/	/

However, the size must be sufficient that the balance of skills and experiences is appropriate.	composition should be assessed periodically to ensure the efficient board membership mix.			
D. Board Member Selection Nomination committees should be responsible to oversee the selection of members to be appointed to the company's board of director.	/	/	/	/
E. Independent Non-Executive Board Director Board composition should be composed of significant proportion of independent non-executive directors (INED) in order for the board to be effective. Notes: In Malaysia, it is recommended that INED making up at least 1/3 of the board.	/	/	/	/

Sources: Report of the NACD Blue Ribbon Commission on Director Professionalism, the UK Corporate Governance Code, Malaysian Code on Corporate Governance, the Hong Kong Code on Corporate Governance Practice and Singapore Code on Corporate Governance.

2.8 Summary

This chapter has presented the narrative story of the background to corporate governance around the world. It started with a general discussion of corporate governance, and then proceeded to encompass the corporate governance practices in major developed economies, such as the US and the UK. Next, the discussion steered towards Asian countries, and finally, focused on Malaysia's institutional environment in the aftermath of AFC 1997/1998. The discussion of corporate governance was linked to foreign investment, as a basis for the analyses of the nexus between them in later chapters.

In brief, the chapter contrasted the practices of corporate governance in the developed capital markets (of which there are two major models - the Anglo-American model and the stakeholder model) with the emerging equity markets, which it achieved by outlining their differences regarding characteristics, mechanisms and practices. Next, the chapter proceeded by discussing the typical characteristics found in the Asian markets, which were hit the hardest by the financial turmoil in 1997/1998. Subsequently the chapter focused on Malaysia to obtain a deeper understanding of its unique characteristics, thus enabling the arguments to justify the hypotheses.

In addition, based on the theoretical and empirical literature, the current chapter also assessed the recent developments and reformation of corporate governance in Malaysia. Consequently, the following chapters use this chapter as a fundamental work in justifying the reasons behind the selection of the theories applied for the arguments (see Chapter 3) and in strengthening the hypotheses (see Chapter 4). The final chapter, Chapter 8, concludes the findings by referring to the supply of information from the current chapter.

CHAPTER 3

MULTI-THEORETICAL APPROACH: AGENCY THEORY, INSTITUTIONAL THEORY, AND RESOURCE DEPENDENCE THEORY

3.1 Introduction

Chapter 2 discussed the evolution of corporate governance in Malaysia, mainly stemming from the disastrous Asian financial crisis of 1997/1998. The pressures for the reformation of corporate governance in this country resulted from the exigencies of institutional forces, both inside and outside the country (please revisit Chapter 2). As discussed, there were many reasons for the extreme changes in corporate governance; one of them was to regain investors' confidence, both foreign and local. Therefore, highly credible theoretical explanations are required to justify the relationship between foreign investments and corporate governance practices in Malaysia, with the institutional forces and governance reformation in mind.

Therefore, this chapter posits three theories to be employed as the underpinning lenses in explaining the relationship between corporate governance variables and foreign investments in Malaysia. The theories are agency theory, institutional theory and resource dependence theory. Hereafter, when the three theories are taken together, they will be referred to collectively as the 'multi-theoretical approach'. Even though there are many other theories which are prevalent in corporate governance studies (e.g. stakeholder theory, stewardship theory, etc.), they are less relevant to the current study as the scope of the study is confined to examining foreign investors' investment behaviour. More specifically their reaction towards the corporate governance system in Malaysian companies in relation to the institutional background in Malaysia's unique corporate environment.

This chapter is organised into six sections, and three of them discuss each of the theories individually. After the introduction section, the chapter starts with a discussion of the multi-theoretical approach in Section 3.2, followed by more detailed arguments of each theory: agency theory in Section 3.3, institutional theory in Section 3.4, and resource dependence theory in Section 3.5. Finally, Section 3.6 provides a summary of the chapter and a conclusion.

3.2 The Multi-theoretical Approach (MTA)

Most of the extant literature examines corporate governance variables in relation to foreign ownership using agency theory (Chizema and Kim 2010) and resource dependence theory as their theoretical lenses (Douma et al. 2006). However, the insights from these two theories are inept with respect to the firms in emerging economies with their different institutional backgrounds (Fama and Jensen 1983), which is in contrast to developed economies. Therefore, institutional theory is claimed to be the ideal theory to explain the institutional changes of corporate governance in Malaysia in the aftermath of the Asian financial Crisis (AFC) 1997/1998. Corporate governance in Malaysia is claimed to be undergoing transformation, especially after the AFC 1997/1998, which involves moving towards the Anglo-American corporate governance practice. In fact, the institutional framework is an element that is rarely disputed in the study of organisations (Peng 2002). The reformation of corporate governance is claimed to be influenced by the institutional forces which firms have to abide by in order to stay legitimate. These influences are generally considered as institutional frameworks (Scott 1995). Therefore, institutional theory is also proposed to be utilised in this thesis as an explanatory device for corporate governance changes.

In addition, Eisenhardt (1989) and Oliver (1997) also assert that agency theory is insufficient to explain the event exclusively as the scope of the theory is only part of the world view. This is the main reason why agency theory is incapable of explaining the relationship between foreign ownership and corporate governance in Malaysian firms exclusively. Agency theory is too narrow to stand on its own in explaining this relationship, whilst at the same time the social elements embedded in the organisation

are prone to being ignored. Nonetheless, this theory still receives substantial attention because of its ability to allow researchers to be more circumspect in giving firmer conclusions concerning the investigated relationships. Therefore, it is suggested that resource dependence theory and institutional theory be used to complement the agency theory in order to yield the rich perspectives for explaining certain events or pre-supposed relationships especially in emerging countries.

In this light, a unitary perspective is inadequate. Thus, this study embraces a multi-theoretical approach which espouses agency theory, institutional theory and resource dependence theory. Recently, the use of the multi-theoretical approach has received heightened interest to debate the issue of corporate governance (e.g. Douma et al. 2006; Lynall et al. 2003; Ruigrok et al. 2006). The combination of these three theories assists in articulating the influences of the variables which affect the investment decisions made by foreign investors in emerging markets, by offering a more holistic perspective. Douma et al. (2006) assert that each theory plays its own role in explaining the characteristics of each variable. Sometimes these theories counteract each other, and at times they are in congruence in justifying the featured issues. The effects of each variable are further accentuated with the incremental value infused by the multi-theoretical approach (MTA). Figure 3.1 below depicts the MTA in examining the key variables for this study.

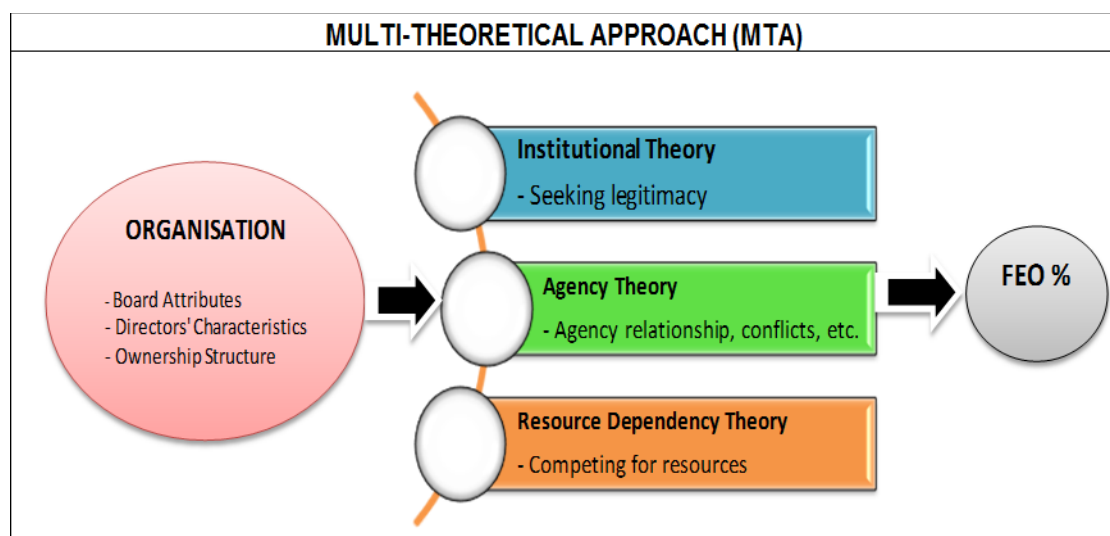


Figure 3.1: The Multi-theoretical approach in examining the relationship of governance variables-foreign ownership in an emerging market.

The figure above presents the relationship between corporate governance variables and FEO. These three dominant theories are utilised to provide reasonable justifications concerning what kind of relationship exists between corporate governance variables and FEO. The following section begins by discussing agency theory, and the subsequent sections discuss the remaining two theories.

3.3 Agency Theory

3.3.1 Overview

According to Jensen and Meckling (1976), agency theory is explained by the principal-agent relationship, or its alternate name is principal-agent problem. The principal is the owner of the company, while the agent is the person or manager who is hired to perform some of the services on their behalf. These two parties have an interest in the same asset but in a different way, which may trigger a conflict of interest between them. This relationship involves the delegation of a certain amount of power to the agent by the company's equity owners in order to make the company's important decisions. On the other hand, the agent, by virtue of the economic contract has certain obligations to the principals (Culpan and Trussel 2005). In fact, agency theory uses the 'contract' to study the nexus between these two actors.

The concept of the "modern corporation", as introduced by Berle and Means in 1932, has led to agency theory becoming one of the more popular explanations for the separation between ownership and control in the company. In the era of the "modern corporation", it is difficult for a corporation to be controlled by the sole owner. The ownership of the modern corporation is widely diffused, whereby the shares in large corporations can be owned by the public at large, due to their huge capital requirements. The extended ownership in a company creates what Berle and Means (1932) call a "quasi-public" company. This refers to its characteristics, which are its tremendous size and its reliance on the public market for capital. Therefore, multiple owners are normally prevalent in tandem with the abrupt growth of modern corporations.

In order to represent the multiple owners of the company, there is a separation of ownership and control, claimed by Jensen and Meckling (1976) to be the main trigger of the agency problem. The actual operations of the firm are carried out by managers, and they are accorded certain powers to control the company to maximise shareholder wealth. Generally, the principals are not the major shareholders of a firm. This is typically associated with hired management working under dispersed ownership, where it is contended that the agency problem is very likely to occur (Turnbull 1977). Moreover, in order to supervise management, additional time and costs are incurred whereby the supervision initiated by a few principals would encourage the 'free rider' issue regarding other principals. However, Berle and Means (1932) assert that this separation has totally eliminated the control powers that have been previously exercised by the owners over the management. The unfettered power given to the management should be exercised wisely by managers and the owner's utmost welfare should always be their top priority.

Unfortunately, a new dilemma has arisen whereby this responsibility turns into a dark opportunity for managers to reap benefits for themselves and level out the shareholders' interests. John and Senbet (1998) propose two possible propensities for managers acting in this situation: (i) to expand their power of control in the organisation at the expense of the company's shareholders and (ii) to finance only conservative and inferior investments to secure their position in the company or for other monetary compensation. As posited by Dimitris and Maria (2010), this theory is premised on the idea that the interests of the agent and the company's owner are not perfectly aligned, or it is difficult or expensive to verify whether the actions taken by managers are for the interest of a principal or not. The difference in attitudes towards risk possessed by the two parties leads to two different courses of action which may not be preferred by the principal.

Eisenhardt (1989) has previously posited that agency theory is the best theory to provide an explanation concerning the divergent goals of the principal and agent in the company, as well as the problem of information asymmetry (Akerlof 1970). Agency theory assumes that both players in the agency relationship (principal vs agent) are

individualistic (Davis, Schoorman and Donaldson 1997) and utility maximisers (Jensen and Meckling 1976). In this context, the agency conflicts that emerge are due to the agent that who is assumed to take actions that is not in the best interests of the company's owners (principals). The actions which maximise the managers' expected utilities are not necessarily perceived by the owners as the actions that can maximise their expected utilities (Watts 1977).

In addition, the related problem of information asymmetry is claimed to arise when managers have superior access to the company's information compared to the principals (Arnold and de Lange 2004). This exacerbates the agency conflict when the principals are not capable of controlling the agent's activity, owing to the fact that there is a separation of ownership and control (Morris 1987). There are two agency problems that may result from the asymmetry of information: (i) the adverse selection problem – where the principals face difficulties in assessing the real skills and abilities possessed by the agent in performing their work and (ii) the moral hazard problem – where principals are not able to tell whether the agent is performing their job commensurate with their ability, or whether there is any shirking or consumption of perks (Arnold and de Lange 2004). This kind of action is very likely to happen when the activities that benefit the principals are costly to the agent. However, for principals to verify what the agent is actually doing is also expensive. Indeed, the principals may choose not to enter into transactions at all due to the fact that they might be exploited by the agents, despite the fact that both parties may gain benefits from the transactions.

In much of the literature, agency theory has been used to shed some light and enhance some understanding of the problems that arise when the interests of the principal and the agent conflict with each other (Jensen and Meckling 1976), or when it is difficult (or expensive) for the principal to verify what the agent is actually doing (Eisenhardt 1989). A 'conflict of interests' arises from the varying goals that are sought by both parties (Eisenhardt 1989). The agent with their divergent interests will be motivated to pursue their own goals (Sundramurthy and Lewis 2003), rather than the value of the firm (Jensen and Meckling 1976). If this is not controlled, there is a likelihood that the

goal of the principals will be jeopardised for the sake of the agents' whims and desires (Douma et. al 2006).

In fact, there are three cost components that are identified as being associated with the agency problem (Jensen and Meckling 1976): i) monitoring costs – the costs that are incurred by the principal to ensure that the agent's actions are aligned with the best interests of the principal, ii) bonding costs – these costs are borne by the agent in order to assure the principal that they will act in the best interests of the principal; otherwise, they will bear the compensation costs, and iii) residual loss - a reduction in the security, well-being and protection faced by the principal, by utilising all the monitoring and binding costs. The agency cost is then referred to as the sum of all these three costs.

Thus, to ensure that the actions taken by the managers are aligned with the owners' interests, they should be monitored. It is claimed that agency theory tries to deal with the goal alignment issue between the principal and the agent as well as reconcile the different risk tolerance between them. However, as emphasised by Eisenhardt (1989), agency costs are associated with these monitoring activities, and the costs of monitoring the agent's actions and decisions are not cheap (Fama and Jensen 1983). Moreover, a standard contract between the agent and the principal seems to be unavailable, especially for a large firm in developed countries. As an alternative, Healy and Palepu (2001) suggest few mechanisms to reduce the agency cost, for instance through formal contracts, board monitoring, executive compensation, information intermediaries, fear of firing, etc.

Prior studies also suggest that the level of information disclosure in the company's annual report may lessen the monitoring cost (Cooke 1993) as well as the bonding cost, as this provides a signal to the principals that the agents are following their agreement (Hossain, Tan and Adams 1994). This is consistent with the suggestions of Fama and Jensen (1983) that effective control procedures are needed to minimise agency costs. In Asian companies, the monitoring mechanisms applied include employing recognised external auditors and being listed in foreign listings (Claessens

and Fan 2002). Without efficient tools, the information asymmetry that emerges from the divergence of information and motivation between the agent and the principal may become more serious.

As stated earlier, agency theory has garnered considerable attention from researchers as the conceptual basis for their studies on factors influencing company performance (Douma et al. 2006), nature, volume and type of information disclosure. In brief, agency theory can be summarised in the following Figure 3.2, whereby actors, issues and elements are inserted into the model to show their interaction with each other. The figure depicts the overall discussion of agency theory, whereby the agency relationship begins with the establishment of a contract between the principal and the agent. In brief, the contract sketches out the obligations that should be shouldered by both parties, but a few issues arise as the agent and the principal are in different positions and have different goals to achieve. Therefore, the issues of monitoring, information asymmetry, risk preference and conflict of interest arise, and hence require further clarification from the perspective of agency theory.

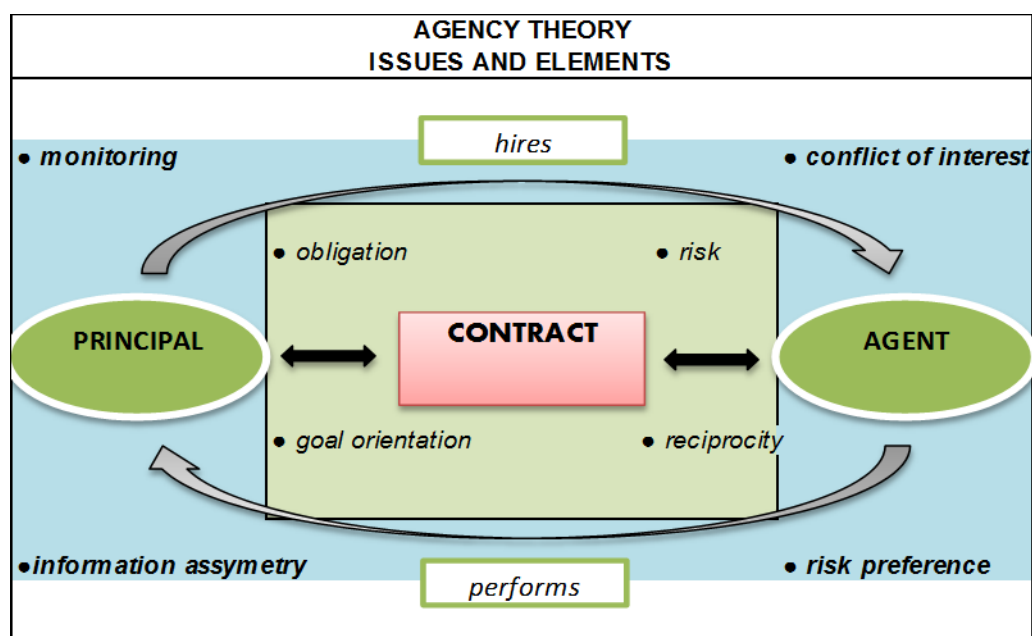


Figure 3.2: Agency theory, its issues and its elements

However, agency theory is frequently applied to countries with dispersed ownership, where there is a separation between ownership and control as in the US and the UK (Short and Keasey 1999). This is the main trigger that causes agency problems, as claimed by Jensen and Meckling (1976). On the other hand, the Malaysian capital market is widely known to be concentrated in ownership. Therefore, the utilisation of agency theory in this work emphasises the principal-principal problems, instead of the principal-agent problem that is prevalent in traditional agency theory. The Malaysian concentrated ownership and the principal-principal problem are discussed in the following section.

3.3.2 Concentrated Ownership in Malaysian Companies

Malaysia is a unique country, whose governance system neither represents the shareholder system of the US and UK (Shleifer and Vishny 1997) nor the stakeholder system of Japan and Germany (Hall and Soskice 2001). In addition, as an Asian country, Malaysia shares the region's common characteristics, such as its weak legal environment and a poor corporate governance system (Johnson et al. 2000). Moreover, the context is highly characterised by high levels of concentrated ownership, with controlling owners (La Porta et al. 2000) cross holding and pyramid corporate structures (Claessens et al. 1999; Haniffa and Hudaib 2006; Khatri 2001; Liew 2007; Lim 1981).

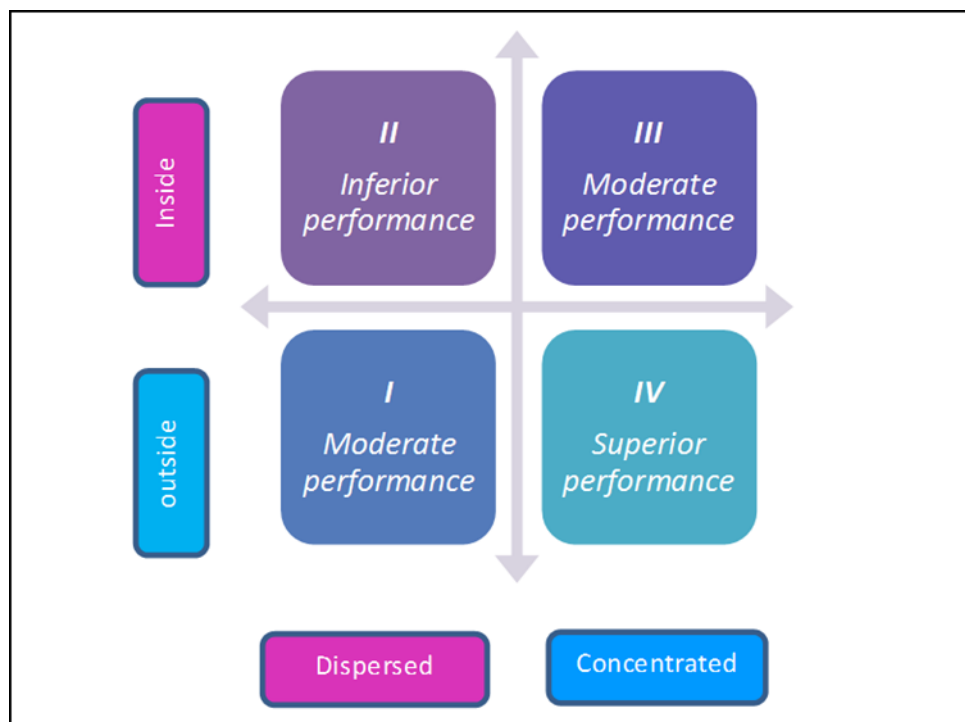
In addition, for an emerging market like Malaysia, there are imperfections in the capital market which should be corrected. The system does not work independently, due to the absence of specialised intermediaries which are prevalent in the developed markets, synonymous with the 'institutional void'⁹ (Khanna and Palepu 2000). This flaw in the emerging markets, coupled with ineffective corporate governance practice, further increases the likelihood of expropriation by large shareholders with regards to

⁹ Institutional void is defined as "the lack of institutional facilities, norms, and regulations needed for a well-functioning economy" (North 1990).

minority shareholders. To remedy this corporate governance shortcoming, the Anglo-American approach is established in Malaysia (Haniffa and Hudaib 2006; Liew 2007).

A different approach should be applied to solve the issue of corporate governance under concentrated ownership. Protection of the minority shareholders from expropriation by the controlling shareholders should become the paramount concern for emerging countries. In relation to the expropriation by managers, powerful shareholders have privileges, such that the agent may easily be ousted by them, or through hostile takeover (Douma et al. 2006). Therefore, controlling shareholders may also be considered as powerful agents for monitoring management action.

Meanwhile, Morck et al. (1988) find an inverted “U-shaped” relationship between a company’s profitability and the degree of ownership concentration. The “U-shape” implies that, at a certain point in the relationship, the costs may outweigh the benefits. Beyond this point, a company’s profit may start to drop and the controlling shareholders may act to fulfil their own interests at the cost of the minority shareholders. On the other hand, the minority shareholders have to face large barriers and incur huge costs in voicing their views. The figure below is reproduced from the work of Douma et al. (2006) who envisage the ownership-performance relationship.



Source: Douma et al. (2006)

Figure 3.3: The agency theory view: Ownership-performance relationship in emerging economies' firms.

As proposed by Douma et al. (2006), the above figure presents the view from agency theory using two dimensions: ownership identity and ownership magnitude. The impact of each relationship is projected in four quadrants. Quadrant three narrates the relationship between the controlling shareholders and the minority shareholders, whereby the performance of the firm is postulated as moderate. In this light, even though the controlling shareholders are inside and concentrated, which is a platform to manage the firm's affairs competently, this also provides an opportunity for the expropriation of the minority shareholders¹⁰ (Bebchuk, Kraakman and Triantis 2000; Claessens, Djankov and Lang 2000).

Given the above, the structure of Malaysian firms can be characterised as unique from the agent-principal point of view, with agency problem appearing to emerge due to

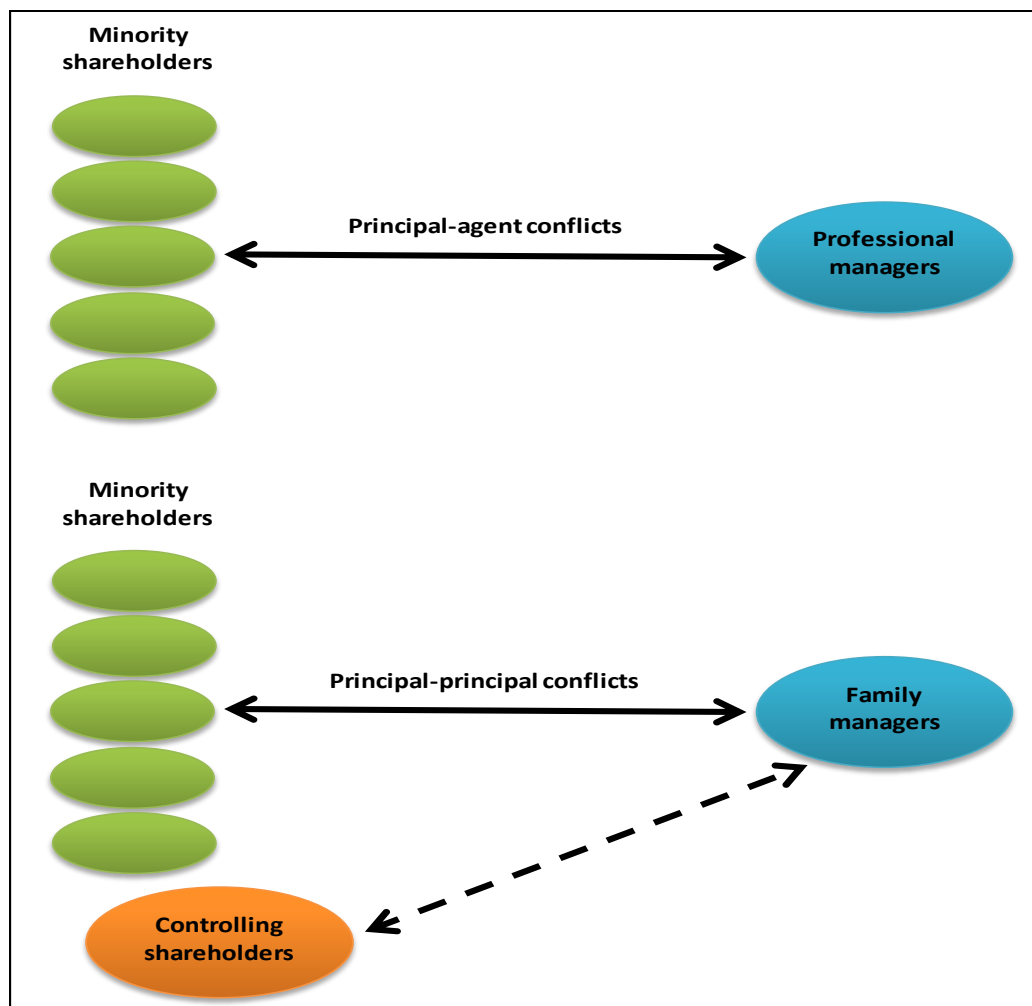
¹⁰ For a more detailed explanation on quadrant I, quadrant II and quadrant IV, please see Dharwadkar, George and Brandes (2000) and Douma et al. (2006).

the exploitation of the minority shareholders, not by the managers, but by the controlling shareholders (Baek et al. 2004; Young et al. 2008). This is consistent with the argument by Shleifer and Vishny (1997), who state that the controlling shareholders are in a strong position to maximise their own goals at the expense of other shareholders.

Considering this, a new perspective on corporate governance has been developed in emerging countries which focuses on the conflicts between the minority and controlling shareholders in a firm – the so called principal-principal model (Young et al. 2008). This perspective arises from principal-principal goal incongruence, in opposition to the traditional agency problems which are based upon principal-agent goal incongruence in Anglo-American economies (Douma et al. 2006). This is believed to stem from the weakness of corporate governance practices in emerging economies (Claessens et al. 2000). Therefore, applying traditional perspective of agency theory as a theoretical lens is inadequate, and thus, emphasis on principal-principal problem should be seriously considered.

3.3.3 Principal-Principal Conflicts

As explained beforehand, concentrated ownership has become a norm in many Asian countries, including Malaysia. This type of ownership has triggered a new conflict, in addition to principal-agent conflicts. The primary conflicts that occur in this type of ownership are between two classes of shareholders: controlling shareholders and minority shareholders – both are principals. These conflicts are largely known as principal-principal problem. It can be illustrated in the following Figure 3.4:



Source: Peng (2006)

Figure 3.4: The Illustration of Principal-Agent Conflicts vs. Principal-Principal Conflicts

The main difference between principal-agent conflict and principal-principal conflicts can be seen from the illustration in Figure 3.4. In the countries with ownership concentration, where controlled by families is a norm, the practice of appointing family members to the board of director is widespread. According to Peng (2006), approximately 57 per cent of the corporations in East Asia have board chairpersons and CEOs appointed from the members of controlling families. These families are capable of dominating the board because they are controlling shareholders.

In this kind of scenario it is argued that family managers may override their traditional professional roles to increase the firm value, where they need to act as both principal

and agent (managers) at the same time when making important decision for the company. As a result, family managers (who represent controlling shareholders) may be involved in the expropriation of minority shareholders in order to safeguard the interest of controlling shareholders (their family members), while the value of minority shareholders is jeopardised. There are many ways that expropriation can be engaged in by family managers, for example – “*tunnelling*”, where managers can divert company’s resources for their family’s personal use (Peng 2006). Even though tunnelling is illegal, family manager may do this by partaking in related transactions that may conceal the expropriation activity, such as selling a company’s asset at lower market price to the related family’s company, purposely incorporated to make this kind of activity look like a normal transaction between two authorised parties (Peng 2006).

Normally, the formal institutional protection of minority shareholders in these countries is often insufficient, and biased in favour of controlling shareholders (Peng 2006). The discussions, implications and effects of concentrated ownership, principal-principal conflicts and minority shareholders’ treatment are further elaborated in the hypotheses development in Chapter 4, and the discussions of the results in Chapter 8.

It is argued that in the Malaysian equity market, foreign investors are a group of investors that can be categorised under the class of minority shareholders. Consistent with the proofs of figures and facts provided by Leuz et al. (2010), Salina and Jarita (2009) and Thanoon et al. (2006) claim that the major foreign investors in Malaysia originate from Anglo-American countries such US and UK. Therefore, they are accustomed to the established set of corporate governance practices in developed countries and share similar values among them. In Malaysian capital market, which is synonymous with the concentrated ownership, family companies with controlling shareholders, the weakness of corporate governance and insufficient shareholders’ protection; the group of foreign investors sceptical and more wary of executing further investment actions. The fear of being expropriated by controlling shareholders is pervasive. Thus, the inclusion of a principal-principal conflicts discussion is worthwhile in gaining a better understanding of this relationship.

Therefore, this study investigates the relationship between foreign ownership and corporate governance in Malaysian firms, by taking into account the insights gained from agency theory, emphasises on principal-principal problems as well as institutional theory and resource dependence theory (RDT) in order to improve the theoretical strength of the presupposed hypotheses. The next theory, which of institutional theory, is elucidated in the following section.

3.4 Institutional Theory

3.4.1 Overview

Institutional theory is entrenched in the concepts of institution and institutionalisation (Meyer and Rowan 1977). Thus far, there are no definitive definitions of institution and institutionalisation given by the institutional scholars, and there is little consensus among them. ‘Institutions’ and ‘institutionalisation’ are viewed from different perspectives by scholars, varying in the various disciplines and approaches (Scott 1987). It is claimed that the institutional theory of organisations allows comprehensive views of organisations (Zucker 1987), and thus, this has become a dominant theory for studying organisations (Suddaby 2010). However, Zucker (1987) claims that institutional theory is difficult to explicate and through his work he tries to offer an explanation of this theory in a lucid way.

According to North (1990), institutions can be prescribed as humanly devised constraints that can determine the form of interaction between people. In a similar way, Scott (1995: 33) defines institutions as “cognitive, normative, and regulative structures and activities that provide stability and meaning to social behaviour.” These definitions are consistent with the definition of ‘institutional framework’ advanced by Davis and North (1971: 6) as “the set of fundamental political, social, and legal ground rules that establishes the basis for production, exchange, and distribution.” It is claimed that the existence of institutions can reduce the uncertainties found in everyday life, whereby a set of guidelines are prevailed upon to steer their actions (North 1990). Peng (2002) adds that uncertainties are lessened when institutional

frameworks communicate with organisations by providing clues about which possible courses of action are tolerable and able to be executed.

In a wider context, it is important to note that the concept of institutions is not restricted to legal and regulatory institutions, such that ‘formal and informal aspects’ such as companies’ policies, cultural and societal norms (Aguilera and Jackson 2003) are also included. Institutional frameworks are composed of formal and informal constraints (North 1990). Formal constraints take into account all the political rules, the judicial verdicts and the economic covenant, whilst informal constraints may include embedded societal norms, behaviour and values as their culture and ideology (Scott 1995). These two groups of constraints operate interdependently, whereby if formal constraints fail, informal constraints may automatically substitute the former in the role, in order to reduce the uncertainties and provide constancy to organisations (North 1990).

Scott (2004) argues that institutional theory offers thorough and strong arguments in studying the aspect of social structure embedded in an organisation. He contends that the institution begins with the move to establish rules, norms and routines, which become the recognised guidelines for social behaviour. Thus, the chronology of when and how these elements are adopted, diffused, or created is examined, and how they become disused and subverted is deciphered. This concern echoes the study by Selznick (1996), who asserts that ‘value’ is the locus of institutional theory. Indeed, Selznick (1957) emphasises that “institutionalisation” is a process for instilling ‘value’, which subsequently promotes stability in the structure of the institution, which are claimed to vary with each other. However, the concept of institutionalisation as proposed by Selznick (1957) is argued by Scott (1987) to remain definitional rather than explanatory, which is vague in its occurrence. Selznick (1957) contends that values are instilled, but the process of how these values are being instilled is not described. It is important to understand the values that matter, how to instil them into the organisations’ culture and social structure, and how they can be weakened or subverted.

Institutional theorists are interested in examining organisational structures, and they attempt to understand the process of institutionalisation over time (Meyer and Rowan 1977). Selznick is among the earlier prominent institutional theorists. Selznick (1957), in his view, distinguishes between organisation and institution. He claims that the former is merely a technical instrument with a definite goal, while the latter may be partly engineered with the existence of a “natural” dimension. Nevertheless, later work by Berger and Luckmann (1967) shares the same view as Selznick (1957), whereby they emphasise an historical approach. They argue that every institution has its own history, and it is difficult to grasp the institution sufficiently without knowing its roots. One of their dominant views is the concept of *social order*, which then leads to their main argument that institutionalisation is a process of creating reality. They describe this process through three steps; externalisation, objectivity and internalisation. These steps are explained in the following order: the human actions (externalisation) are interpreted (objectivity) and the interpretations are shared with others (internalisation).

The “routine” actions accepted by others with a similar meaning are defined as institutionalisation by Berger and Luckmann (1967). A social definition of ‘routine’ is elucidated by Zucker (1987) as the repetitive tasks performed by individual workers within an organisation. Thus, when managers, for example, claim that “this is how it should be done”, “everybody does it this way” or “only in this way things are done”, these justifications are referring to institutionalised activities (Oliver 1997). Therefore, in relation to institutions, institutionalisation is seen as a “*process*” of building the social values to be accepted and shared among the individuals concerning the way things are, what is perceived as important and how to do things (Scott 1987).

The concept of institutionalisation held by Berger and Luckmann (1967) then becomes fundamental to the subsequent works by Zucker (1977) and Meyer and Rowan (1977) to analyse the forms of the organisation. Zucker (1977) studies the theory of the organisation, whilst Meyer and Rowan (1977) study the organisation as myth and ceremony. They are in agreement that institutionalisation is the social process, and the actors in the system accept the same meaning believed by others

concerning how things should be done. Nonetheless, there is no universal agreement as to its definition in the institutional school of thought. However, from the sea of definitions, it is interesting to note the definition by Scott (1995:33) which seems comprehensive but is not yet agreed as conclusive:

“Institutions are social structures that have attained a high degree of resilience. They are composed of cultural-cognitive, normative, and regulative elements that, together with associated activities and resources, provide stability and meaning to social life. Institutions are transmitted by various types of carriers, including symbolic systems, relational systems, routines, and artefacts. Institutions operate at different levels of jurisdiction, from the world system to localized interpersonal relationships. Institutions by definition connote stability but are subject to change processes, both incremental and discontinuous”.

From this study’s vantage point, the above stated definition includes all the elements which are considered necessary to determine the emergence of an institution. However, the connotation that institutional theory refers to stability in the social order is not fully acceptable, as in the passage of time it cannot escape being plagued by the conflict and changes in social life (Scott 2004). Notwithstanding, choosing a precise definition of institution and institutionalisation remains arbitrary, as institutional theory can be reflected using several different approaches (DiMaggio and Powell 1991) which hinge upon many factors, and are subject to changes. Among the factors that lead to organisational changes are political, regulatory and technological complexities (Greenwood and Hinings 1996). The changing phases have to be confronted by organisations in order to survive and remain competitive (D’Aveni 1994).

The following Figure 3.5 depicts the above discussion on the institution and institutionalisation from the insights of many institutional scholars. The institution is claimed to be composed of formal and informal aspects (Aguilera and Jackson 2003)

and institutionalisation is defined from many perspectives, such as the process of instilling values (Selznick 1957), creating reality (Berger and Luckmann 1967), promoting stability and providing meaning (Scott 1995).

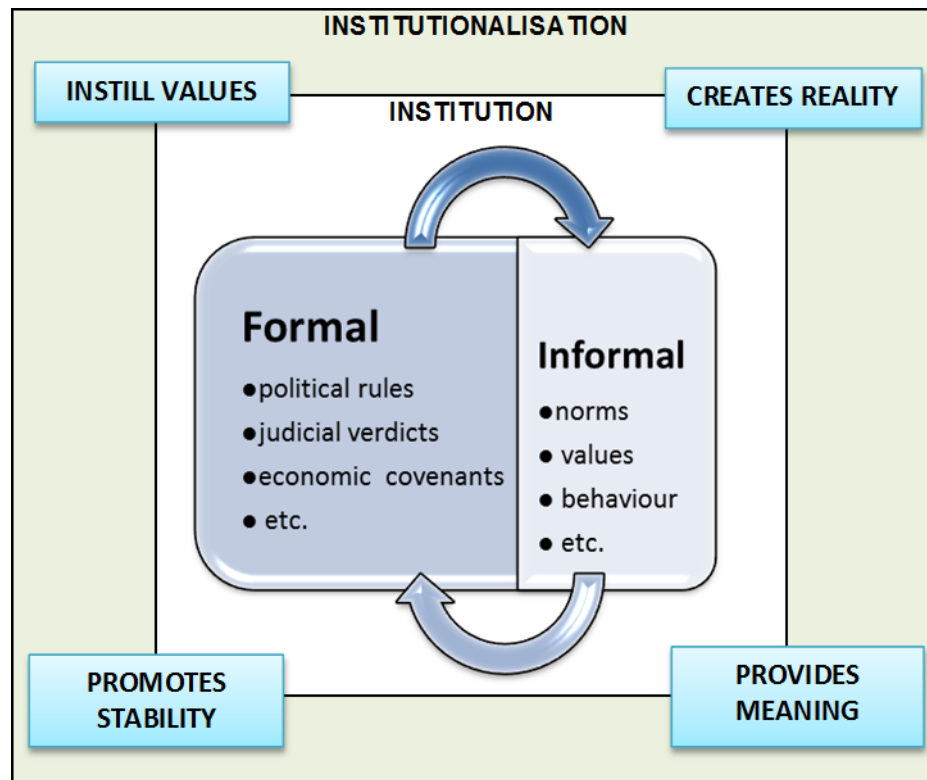


Figure 3.5: Institution and Institutionalisation – Elements and Process.

3.4.2 “Old” and “New” Institutionalism

In order to review the state of institutional theory, there is a discrimination to be made between ‘old’ and ‘new’ institutionalism, as proposed by DiMaggio and Powell (1991). The former was focused on certain issues such as influence, coalitions, competing values, power and informational structures (Greenwood and Hinings 1996; Selznick 1957), whilst the latter accentuated legitimacy. According to Mizruci and Lisa (1999), prior to the 1970s, most of the organisational studies emphasised the ties between organisations and their environment. However, in the late 1970s, after a series of works in this area, the focus shifted and the new basis of organisational studies was formed. The new approach that emerged from the cumulative effect of

these organisational studies is now called the new institutional theory, or neo-institutional theory (Mizruci and Lisa 1999).

Neo-institutional theory, to a large extent, stems from three seminal works by institutional scholars, Zucker (1977), Meyer and Rowan (1977) and DiMaggio and Powell (1983). These three leading organisational studies of the neo-institutional theory have engendered fresh discernment of institutions, and have switched the focus of the institutional perspective (Selznick 1996). DiMaggio and Powell (1991:8), in their view, see new institutional theory as:

“a rejection of rational actor models, an interest in institutions as independent variables, a turn toward cognitive and cultural explanations, and an interest in properties of supra-individual units of analysis that cannot be reduced to aggregations or direct consequences of individuals’ attributes or motives”

From the above view, Selznick (1996) argues that there are no significant differences concerning the definition of institution and institutionalisation. However, several new directions emerge. From the perspective of the classical model of institutions, economic choices are constrained by the technological, informational and income ceiling. However, this is disputed by the neo-institutional perspective, whereby economic choices are claimed to be constrained not only by the factors mentioned above, but also by socially constructed limits such as norms, habits and customs (Oliver 1997).

New institutionalism focuses on expanding a sociological view of institutions by examining their interactions and how they can affect society. Through the view of neo-institutionalism, there is an awareness that institutions operate in an environment that is constituted of other institutions, which is referred to as the institutional environment. It is understood that each of the involved institutions can be influenced by its institutional environment. Each of them has a main goal, which is to assure that they can survive. In order to achieve that, they not only need to strive beyond

economic success, but also establish legitimacy within the institutional environment as well (Oliver 1997). More specifically, the focus of this new strand of theory is to seek legitimation by organisations in order to sustain themselves in business. Legitimacy is seen by Selznick (1996: 273) as the “organisational *imperative* that is both a source of inertia and a summons to justify particular forms and practices”.

In order to achieve legitimacy, Meyer and Rowan (1977) suggest that organisations should formulate stories about the actions they have taken that are compatible with society’s expectations. These stories play a symbolic role in placating the prospective influence of the public. This work is further developed by DiMaggio and Powell (1983) using the same theme, where they explicitly link it with the organisation and sociological theory. DiMaggio and Powell (1983) noticed the tremendous resemblance of organisations in a particular field, which then intrigued their interest to find possible explanations. Consistent with Meyer and Rowan (1977), it is argued that the similarity becomes highly visible as a result of institutional pressures which force organisations to take further actions to attain legitimacy within their wider environments (Mizruci and Lisa 1999). As suggested by Pfeffer and Salancik (1978), organisations depend on resources from their environments to sustain themselves. This process is known as homogenisation, and to describe this process, DiMaggio and Powell (1983) adopted the ecological concept of isomorphism (Mizruci and Lisa 1999).

Two types of isomorphism have been identified, competitive and institutional isomorphism. Competitive isomorphism refers to the pressures that are derived from market competition, which can be from the local as well as the global organisational field (Hessels and Tersejen 2010). On the other hand, institutional isomorphism pertains to organisational competition for political and institutional legitimacy. According to DiMaggio and Powell (1983:150), institutional isomorphism is a useful tool for understanding the politics and ceremony that pervade much modern organisational life. One justification offered by Meyer and Rowan (1977) for isomorphism, is when organisations become similar to their environment either technically or by exchange of interdependencies, or both. It is argued that for this

study, this thread of organisational theory may be used as a premise to offer reasonable justifications of foreign investors' investment behaviour in Malaysian companies. A lengthy discussion of institutional isomorphism can be found in Section 3.4.4 Institutional Isomorphism.

Nevertheless, the use of institutional theory is pertinent to find sensible answers to the questions that are raised in this study. These are questions such as: What are the properties of the different views held by foreign investors when making investment decisions in the Malaysian capital market compared to other capital markets? How can the differences be explained? How can the presumed relationships be justified? and most importantly, which strand of institutional theory can offer the best explanation of the process of investment decision making by foreign investors in Malaysian PLCs?

Therefore, as proposed by Powell (1996:297), to make further theoretical progress, the issues at hand must be tackled wisely and be examined from many angles such as "how they matter, under what circumstance, to what extent, and in what ways". Therefore, institutional theory, under the new institutionalism which is focused on the strand of sociology specifically known as New Institutional Sociology (NIS), is found to be the most relevant organisation theory for responding to the research questions that were raised in Chapter 1.

3.4.3 New Institutional Sociology (NIS)

There are two recognised models of organisational actor that have been employed in most of the social analyses - the rational actor model and the institutional model (Pfeffer 1981). Under the first model, the individual is assumed to act rationally when making decisions by considering all possible alternatives and continually checking the associated costs and benefits. Hence, this individual is perceived to seek the optimal solution when making decisions. On the other hand, the institutional model assumes that the decision made by an individual is mainly based on the existing social norms, and is not influenced by their personal interest. These two opposing views are claimed

to be being two ends of a continuum in the decision making process – thus the most fitting theory to justify these behaviours should be addressed (Tolbert and Zucker 1999).

One of the explanations put forward by NIS is that the behaviour of organisations is influenced by the forces that exist in the wider ‘*society*’. Society is defined by Clark (1962) as being comprised of institutions that interlock comfortably for the sake of efficiency, or as asserted by Parsons (2013) become the dominant value system. Modern organisations studies use this ‘society’ definition as the basis for their work. By adhering to the norms and rules that are valued by society at large, or at a smaller scope by certain institutions in society, legitimacy can be achieved. Institutional isomorphism is one domain in NIS that represents the manner in which organisations adopt similar procedures practiced by other organisations that are surrounded by the same set of environmental conditions (DiMaggio and Powell 1983).

3.4.4 Institutional Isomorphism

The discussion presented in this section is a continuation of the discussion of institutional isomorphism that was made in Section 3.4.2. In the current section, the explication of institutional isomorphism goes deeper in order to substantiate the rationale for selecting this strand of organisational theory to provide a justification for foreign investor behaviour in the Malaysian market. As previously stated, the isomorphism concept is captured in one of the strands of institutional theory, which is the New Institutional Sociology (NIS). NIS primarily focuses on seeking explanations pertaining to the process of institutionalisation, which stems from societal forces (DiMaggio and Powell 1983), and where the focus is particularly on answering questions concerning how and why organisations conform to institutionalised credence in society.

It is argued that, to find legitimacy, the rule is to adhere to the values and norms that are accepted by society. Meyer and Rowan (1977) have previously contended that the influences of political power seem to escalate institutional legitimacy. This is

consistent with the later work by DiMaggio and Powell (1983) who deny the claim that organisations are only concerned with competing for resources and customers. Oliver (1997) asserts that organisations strive beyond economic optimisation, whereby they are contended to strive for political power, social well-being, economic fitness and institutional legitimacy as well. Legitimacy is essential to organisations in order to be recognised by society, and in accessing external resources for sustainability and to compete in the market.

In the early work of isomorphism, the institutional environment is portrayed as fixed. However, Hannan and Freeman (1977) broaden this view by emphasising the process of competition that occurs between organisations, which then leads them to adopt the best structure for organisational layout in order to sustain them in the industry. The effect of institutional isomorphism is homogenisation, hence this will result in a decrease of variation and diversification among organisations. It is claimed that the level of homogeneity among organisations is increasing over time. The inexorable push towards homogenisation (DiMaggio and Powell 1983) forces the changes within the organisation to take place. The changes, however, are largely dependent on the environment in which the organisations operate. Thus, the organisations change to become isomorphic with their environment (Meyer and Rowan 1977; Slack and Hinings 1994).

DiMaggio and Powell (1983: 149) describe isomorphism as the “concept that best captures the process of homogenization” and can be explained as a tendency for countries and organisations to adopt similar institutions (e.g. corporate governance structures). Institutional isomorphism is claimed to emerge due to the desire of organisations to model themselves after other organisations that are perceived to be more successful (DiMaggio and Powell 1991). In this light, it is argued that institutional isomorphism is a domain of NIS that represents the efforts made by organisations to resemble other organisations and reduce the gap of disparity that exists between them. In fact institutional isomorphism is not a means to justify the difference between organisations, but the similarity that pervades organisations in their environment (Greenwood and Hinings 1996). This understanding of the

isomorphism concept is consistent with the description given by Hawley (1968) when he contends that isomorphism is a constraining process that pushes the actor in an institutional environment to resemble other actors as they are facing the same set of environmental conditions.

Meyer and Rowan (1977) assert that there are three important consequences for organisations derived from isomorphism with environmental institutions: i) the elements that have been recognised by society increase the degree of legitimation, rather than increase the organisation's efficiency concomitant with the increasing level of commitment by internal and external participation in the institutional environment, ii) the value of the organisation's structural elements is defined by employing external assessment criteria, thus recognising the organisation as one of the subunits rather than a loose element in the institutional environment, and iii) the stability of the organisation increases while the potential upheaval decreases when organisations depend on the external institutional environment to decide on changes. Hence, for brevity, institutional isomorphism contributes to the success and sustainability of an organisation, which becomes the insulation for an organisation to fend off failure.

DiMaggio and Powell (1983) identify three mechanisms through which institutional isomorphic change occurs, namely *coercive*, *mimetic* and *normative*. A discussion of each mechanism is given in the following sections.

3.4.4.1 Coercive Isomorphism

Coercive isomorphism emanates from political force and seeks for legitimacy (DiMaggio and Powell 1983). It is a result of both the formal and informal forces exerted on organisations by other coercive organisations. The organisations under pressure are the organisations dependent on other coercive organisation, and they need to abide by their insistence in order to survive and for their viability (DiMaggio and Powell 1983). Common examples of these actors (i.e. dependent organisation vs coercive organisation) are public companies vs government institutions. It can also

occur outside the governmental arena, such as parent company vs subsidiary company, etc. For example, the rules that have been enshrined in the Codes have to be followed by related organisations (for the first example), and the standard operating procedures and accounting reporting mechanisms applied in the parent company must be followed by the subsidiary companies (for the latter example).

DiMaggio and Powell (1983) propose that the greater the dependencies on the other organisation, the higher are the forces to become isomorphic with that organisation. This is coupled with the fact that the dependence on the organisation may be caused by them being the single source for vital resource, and further strengthens the pressure. In contrast, it can be understood that an organisation may opt not to obey the demands of an organisation that they are not dependent upon (Pfeffer and Salancik 1978). However, it is asserted that disobedience to the rules, laws, structures etc. imposed by the greater institutions that they depend on, may be to the detriment of the organisations in terms of restrictions to the resources, and obstructions to involvement in any corporate transaction, etc.

Even though the changes made are ceremonial, this does not mean that the changes are inconsequential (DiMaggio and Powell 1983). Pfeffer and Salancik (1978) contend that when organisations are confronted with an uncontrollable situation, they seek for a higher power (e.g. the government) to fix the difficulties or provide for their needs (DiMaggio and Powell 1983). Other than this, coercive power or authority power can ensue from more subtle and less explicit sources than those suggested above. Coercive isomorphism may also stem from the societal expectations or preferences in which the organisation operates. It can be in the form of force, persuasion or as an invitation to join in with the collusion. The adherence to societal expectation is essential in assisting with organisational sustainability, securing economic resources and their power (DiMaggio and Powell 1983; Oliver 1997).

3.4.4.2 Mimetic Isomorphism

The second mechanism is mimetic isomorphism, which results from the uncertainty that pervades organisations. Mimetic action or modelling is the standard response to uncertainty (DiMaggio and Powell 1983). Organisations are claimed to be very sensitive to the cultural environment that surrounds them (Selznick 1996), and thus, uncertainty becomes the powerful push factor (DiMaggio and Powell 1983) to initiate the action of imitation of another peer that is perceived as a successful model. Mimetic action is considered as “a response of uncertainty” rooted in anxiety; it is compulsive rather than rationally taken as a solution to solve the organisation’s problem (Selznick 1996:273). New entrants into a highly uncertainty industry, in particular, will seek an established model in the field in order to imitate their practices to achieve viability and to be recognised by society.

Apart from ‘uncertainty’, other issues that can encourage the imitation process, with respect to a superior model are ambiguous objectives, unclear solutions, less technological acumen, etc. within the company. The lack of well-defined technologies in organisations may permit them to bring in institutionalised rules and practices from well-established organisations that can increase organisational stability. Likewise, the ambiguous goals set by organisations may steer them to find a perceived successful model in order to imitate the design and learn the way they run their business. Even though there is an argument that copying another organisation may lessen the competitive advantage of an organisation, Maggio and Powell (1983) contend that this imitation may enhance organisational legitimacy and sustainability. The closest example for Malaysian companies is the imitation of the innovative management system, known as the 5S concept¹¹, which was imitated by Malaysia from Japan. Malaysia adopted this practice in the mid-1980s.

¹¹ The 5S concept is a systematic guideline, introduced by Japan in the early 1980s to assure the cleanliness, neatness and overall safety of the workplace environment. The application of this method by institutions will help to improve service quality, reduce cost and simplify work.

However, it is claimed that the modelled organisations may not be aware of the modelling process, as the process may be performed unintentionally, either indirectly through employee transfer or explicitly by consulting firms (DiMaggio and Powell 1983). The imitation process aims to enhance the organisation's legitimacy; this effort has been taken to demonstrate that the organisation at least endeavours to improve the uncertainty that faces it. It is contended that the larger the organisation and the wider the customers served, then the pressure for the betterment of the organisation is more intense. Therefore, the organisation should be more serious in considering mimetic isomorphism (DiMaggio and Powell 1983). Organisations are prone to model themselves after identical organisations in their field which they perceive as more successful and legitimate. It may be argued that having fewer exemplary models for imitation, results in a faster rate of isomorphism and more homogeneous organisational structures emerging in that field.

3.4.4.3 Normative Isomorphism

The last mechanism in institutional isomorphism is that of normative isomorphism. Institutional theorists such as DiMaggio and Powell (1983), Meyer and Rowan (1977), and Zucker (1987) suggest that organisations are shaped by the normative pressures which embrace them. Normative pressure may arise from external and internal sources. An example of an external source is the state, while an internal source is within the organisation itself (Zucker 1987). Within the organisation, normative isomorphism is argued to stem primarily from professionalism. Two aspects of professionalisation are the formal education received in a university and the growth and elaboration of professional networks, which enable new practices to be diffused easily across organisations.

It is asserted that universities and professional training institutions play a vital role as a centre for encouraging and nourishing organisational norms and values among professional managers and management staff (DiMaggio and Powell 1983). The formal education received in an established organisation, such as a university, can influence the development of professional norms and inculcate specific values in

people within the same setting. The values that are instilled during their upbringing and adolescence produce lasting effects within the individual. Thus, when they enter employment, they will hold these values within them, which enable them to be diffused easily into and across organisations.

Similarly, professional associations for accountants, engineers, lawyers and financial analysts, amongst others, have escalated this recently. These professionals are bonded strongly with their respective professional bodies, which have embedded certain values to be applied by the members in the circle. As asserted by DiMaggio and Powell (1983), those who have the same background, share common attributes and tend to view problems in parallel with each other, due to this significant influence on them and the values that have been instilled in them. The strong ties with the professional bodies dictate the criteria for comparable professional behaviour (Greenwood and Hinings 2002).

Focusing on the normative isomorphism that can dictate management behaviour, it is argued that managers operate within a standard working environment. They have a common set of rules, and interact with a regular group of people inside and outside the organisation. Their management action is influenced by normative constraints and embedded values, which will determine their 'accepted' and 'proper' professional behaviour (Berger and Luckmann 1967). Despite the location and the range of organisations in which managers work, normative pressure acts as a strong mechanism to create a pool of identical managers possessing a similar orientation, which may override the variation that exists due to the organisation's tradition (Perrow 1974). These conditions lead the organisation to adopt legitimate elements, which expedite isomorphism with the institutional environment, hence securing the position of the organisation within the industry (Zucker 1987).

It is argued that the institutional isomorphism process does not necessarily increase organisational efficiency. In fact, an organisation may take more requisite actions to become similar to the modelled organisation in order to gain more benefits from the parity. By being similar to the prestigious and reputed organisation, the organisation

finds it easier to deal with other organisations, to be recognised as legitimate, and to attract more professional staff etc. (DiMaggio and Powell 1983). It is claimed that in the organisation's field (e.g. hospitals) where most of the professional staff are highly desired, the organisations advance the need for prestige and reputation to attract a professional and highly skilled workforce, because these people are considered as actual consumers that in return can attract more 'real customers' (DiMaggio and Powell 1983). Therefore, pressures for institution isomorphism are highly intense in certain areas of industry or certain fields in order to seek legitimacy and similarity to the modelled organisation in the environment where the organisation is operating.

The following Figure 3.6 presents the mechanisms of the isomorphic changes which drive institutional change from the view of NIS. However, in this study, the discussion of isomorphism is merely focused on institutional isomorphism, which is coercive, mimetic and normative, as depicted in the figure. In fact, institutional isomorphism does not necessarily occur simultaneously for all mechanisms, it can occur through one or a combination of these three mechanisms (DiMaggio and Powell 1983). The end effect would be the changes in the organisational sphere, in terms of organisational structures, systems and activities. Further arguments and justifications based on these mechanisms will be presented in Chapter 4.

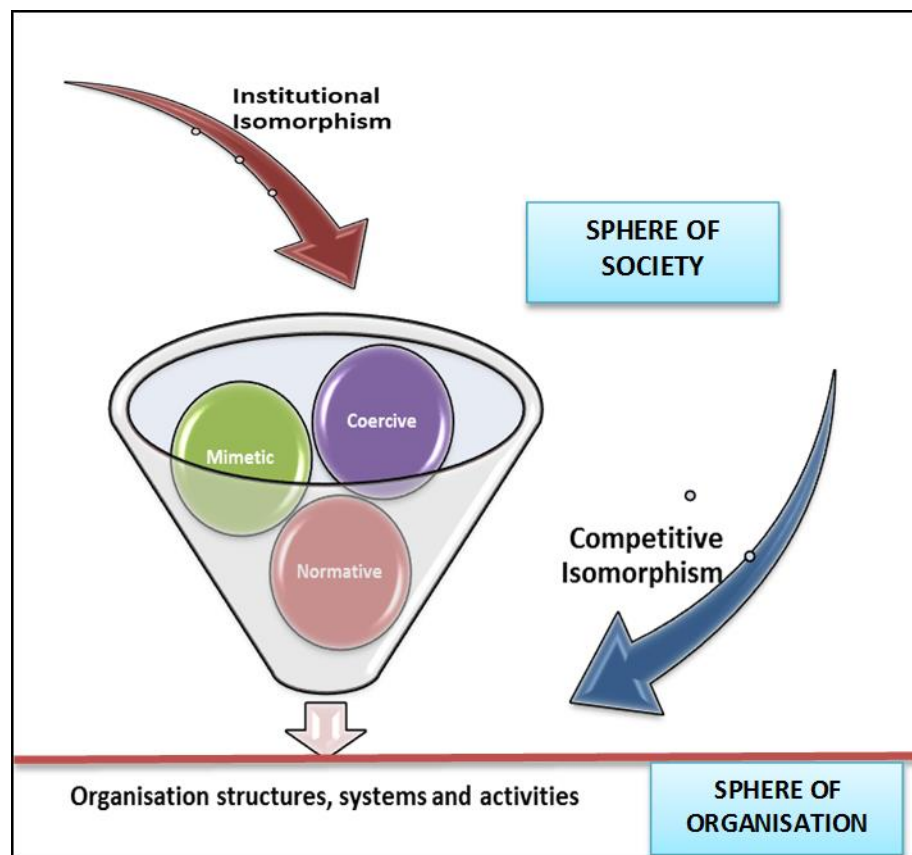


Figure 3.6: Towards the Homogeneity of Organisations

3.4.5 Level of Analysis in Institutionalisation Process

In fact, the basic premise of institutional theory is that firms are trying to conform to societal expectations, whether from their internal or external environments. This will lead to homogeneity among firms that is exhibited through their structures and activities. According to Oliver (1997:700), “*the successful firms are those that gain support and legitimacy by conforming to societal pressures*”.

In order to be acclaimed as a successful firm and achieve sustainability, there is an awareness that each firm should undergo the institutionalisation process (Oliver 1997). In the institutional theory view, institutionalised activities are the result of an interrelated process at three levels of analysis - individual, organisational and inter-organisational (Oliver 1997). The following Figure 3.7 depicts the process.

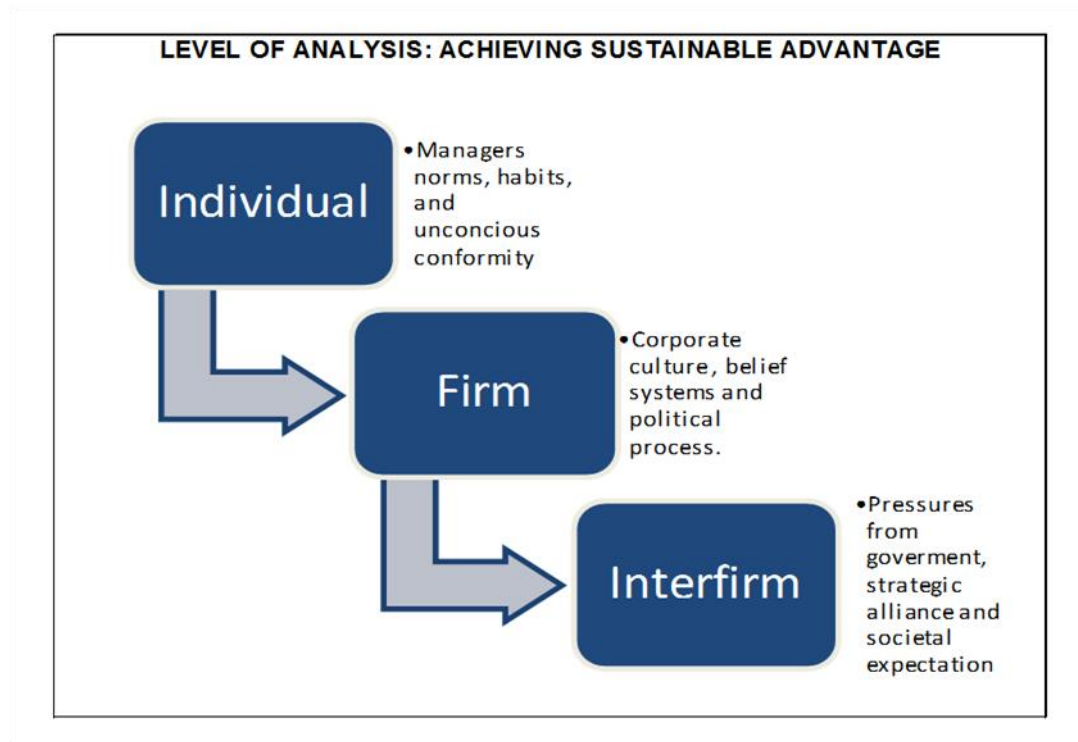


Figure 3.7: Level of Analysis in Achieving Sustainable Advantage

At the individual level, institutionalised activities are influenced by the managers' norms, habits and their unconscious conformity with the organisation's tradition (Berger and Luckmann 1967), whilst at the firm level, corporate culture, shared belief systems within the organisation and political process shape the institutionalised structures. Finally, at the inter-organisational level, pressures emerge from the government, other organisations in an institutional environment, industry alliances and societal expectations (rule, norms, standards, environment etc.). These pressures are consistently experienced by all the organisations in the same institutional background, thus initiating the move to imitate similar structures and activities or become homogenised with each other (DiMaggio and Powell 1983).

Overall, discussion of institutional theory heretofore has been based on the general view of institutional theory at large, without specifying the institutional context. Therefore, the following Section 3.4.6 is drafted specifically to discuss the justifications as to why institutional theory is suitable to be applied to the Malaysian capital market and "isomorphic change" in the context of Malaysia.

3.4.6 Corporate Governance and “*Isomorphic Changes*” in Malaysia

Based on the overview of institutional definitions and concepts, it is instructive for this study to embrace institutional theory as the theoretical lens. In the context of Malaysia, in the aftermath of the Asian Financial Crisis (AFC) 1997/1998, the corporate governance structure has totally changed. Most of the key players in the economic system have begun to realise the potential consequences on economies of deficiencies in corporate governance. Initiatives have been taken by the responsible parties to reform their corporate governance with the intention of creating a better image of the country, subsequently attracting more foreign investors. This reformation has been proposed by many institutions, such as the International Monetary Fund (IMF), in order to regain the confidence of investors. The Malaysian government, for instance, has played a diligent role in ensuring that this goal could be achieved.

The crucial factor that enables the institutional perspective to be more strongly linked to Malaysia’s governance reformation is that large Malaysian firms were substantially dependent on government resources (Gomez 1994; Suto 2003). On the other hand, the government of Malaysia itself, aware of the role played by large firms in the country in stimulating the economy, sought to reform the corporate governance structure, consistent with the recommendations of the IMF for regaining the confidence of investors. DiMaggio and Powell (1983) assert that the institutional forces arising from organisations, in an effort to maximise shareholder value, place extreme pressure on firms in search of legitimacy to imitate or adopt the governance structures of Anglo-American capitalism. This can become an indicator that a process of *isomorphic change* has occurred in the Malaysian institutional environment.

Consequently, a few formal bodies have been established in order to review the corporate governance system and to provide recommendations for better practice. As a result, the Code on corporate governance was released in March 2000, and the adoption of this code can be seen as evidence of corporate governance reform. This marked the significant importance of corporate governance in Malaysia (Ponnu 2008). The reformation of corporate governance is viewed as a global phenomenon (Klapper

and Love 2004). Scott (1987) sees this as a pushing factor from the perspective of institutional theory; it has to be translated as a lawful need coming from society.

Nevertheless, Chizema and Kim (2010) note that most of the literature on corporate governance reformation still employs agency theory as its theoretical premise. Moreover, this approach is claimed by Fama and Jensen (1983) to be suffering from a serious flaw if the capital markets that are examined are not liquid, and shareholder protection is not their precedence. This argument is supported by Dacin, Goodstein and Scott (2002) who suggest that different tools should be applied in different institutional contexts. Notably, institutional theory has been proposed by Aguilera and Jackson (2003) as well as by Buck and Shahrin (2005). They claim that institutional theory is an ideal framework to obtain insights into the analysis of corporate governance reform, and agency theory is under-utilised with respect to the social aspect of firms (Aguilera and Jackson 2003).

Likewise, Douma et al. (2006) assert that by waiving institutional theory, the social facet embedded in the firm's activity is likely to be overlooked, which may make it less easy to explain how the relationship of concern might occur. In order to regain investor confidence, Malaysia has geared up to reinforce its corporate governance practice and has undergone a process of institutional change following the AFC 1997/1998; these actions can be translated as corporate governance reform. Thus, in this light, institutional theory is persuasive to be applied as one of the important theory for this study. Nevertheless, exclusive discussions of institutional isomorphism in terms of coercive, mimetic or normative in Malaysian institutional capital market are made explicit in the hypotheses development section in Chapter 4.

3.4.7 Criticism of NIS

Even though this thesis attempts to offer justifications concerning why NIS has been selected to explicate foreign investors' investment behaviour in Malaysian corporate institutions, this strand of institutional theory is not free from criticism. It is worth emphasising the concerns surrounding this strand as claimed by a few scholars. It is

claimed that this theory is full of contradictions, depicting an organisation as a submissive institution and a passive recipient (Suddaby 2010) of its operating environment, which is claimed to be unduly constraining. However, this view has been corrected by DiMaggio (1988), who insists researchers to be more creative in understanding organisational behaviour that reflects and interacts with its institutional environments (Suddaby 2010). Moreover, it is argued that this theory fails to acknowledge the importance of the conflicts that pervade an organisation with undue concern given to myth and ceremony, thus overlooking the other aspects of the organisation which are power and control (Carruthers 1995).

In addition, Greenwood and Hinings (1996) argue that the theory is less capable of examining and elaborating on the aspect of the internal dynamics of organisational changes, but gravitates towards exploring the similarity (isomorphism) of the organisation to its particular field of organisations. Thus, it is futile to study the process of organisational change as the theory itself does not offer much enlightenment on the change process (Ledford, Mohrman and Lawler 1989). Recently, Suddaby (2010) asserted that current work on institutional theory is still unable to provide an understanding as to why and how organisations serve their institutional environment.

Furthermore, the focus of this theory is merely at the macro level – i.e. the changes in the institutional environment where the organisations operate, thus disregarding the micro level such as the changes in the organisational sphere (Scott 1991). The limited insights offered by this theory are argued to be inefficient, and thus comprehensive views and explanations of organisations cannot be achieved. Therefore, in order to provide an exhaustive understanding of foreign investors' behaviour when making investment decisions concerning Malaysian companies, agency theory and resource dependence theory are brought forward to facilitate the understanding of organisations at the micro level, while institutional theory concentrates on explanations at the macro level, organisational setting and its framework. The following sections discuss the other one supporting theory, resource dependence theory.

3.5 Resource Dependence Theory

Resource dependence theory (RDT) is closely linked to institutional theory in defining the organisation. The organisation in both theories is seen as a structure that is vulnerable to uncertain environmental pressures, and has limited organisational choices as it is constrained by these pressures. Hence the organisation requires constant reinterpretation and negotiation to enable its sustainability, and the acceptance of its legitimacy (Hessels and Terjesen 2010). In fact, both theories are concerned with the existence of external actors in the organisation's environment, how organisations confront the competitive pressures, and what kind of relationship results between them. Thus, both theories attempt to explain the relationship from their individual perspectives, which are quite distinct from each other.

RDT argues that dependence on other actors pertains to the need for resources, whilst institutional theory claims that organisations tend to imitate the behaviour of other organisations which are perceived as successful models in order to obtain legitimation (Hessels and Terjesen 2010). However, in certain areas of explanation, RDT is difficult to distinguish from institutional theory, especially when the degree to which institutionalisation can be measured hinges upon the degree of control by the government, regulation, resource flow, etc. (Zucker 1987). This can be explained by the level of dependence that organisations have on other organisations, which results in resource disruption if noncompliance occurs.

RDT has long been applied in worldwide studies to explain how organisations can minimise environmental interdependence and uncertainty (Hillman, Withers and Collins 2009). It is considered to be one of the most influential theories in organisational theory besides institutional theory. In this light, RDT is seen as one of the auxiliary theories to support the primary theories in this study, namely agency theory and institutional theory. It is argued that when these theories are applied together, they can offer greater predictive power to explain the presupposed relationship between variables (Sherer and Lee 2002). The role of RDT in this study is to put forward arguments to substantiate the existence of an asserted relationship.

This theory has had a far reaching effect on organisation studies over the last 30 years since the publication of a paper by Pfeffer and Salancik (1978), “*The External Control of Organizations: A Resource Dependence Perspective*”. With its slight difference in its focus when compared with institutional theory, RDT tilts towards discussing organisational success and power. As an organisation’s success and power depend on its resources, RDT is claimed to focus on how to access these resources from the other actors in their corporate environment (Pfeffer and Salancik 1978). In defining resource, the work by Hessels and Terjesen (2010: 207) is preferred. According to their work, the term resources can be defined as the “*tangible and intangible assets firms use to conceive of and implement their strategies*”. However, there are limitations to the availability of resources, resulting in multiple organisations striving for the same set of scarce resources (Hessels and Terjesen 2010). Therefore organisations are forced to seek new innovations that can substitute the resources (Pfeffer and Salancik 1978; Sherer and Lee 2002).

According to Pfeffer and Salancik (1978), in order to achieve an understanding of an organisation’s behaviour, the context of the behaviour should be clearly deciphered. They assert that an organisation’s ecology consists of external influences, and likewise internal influences (with less emphasis) (Dill 1981), which revolve around ‘*power*’. The success of an organisation is gauged by how it maximises its power (Pfeffer 1981). Similarly, the links that exist among organisations are claimed to emerge due to the need to exchange resources.

The following Figure 3.8 presents the interaction between organisations and their environments, which leads to coalition, pooling resources and strategy implementation throughout time, in order to ensure the viability of the company.

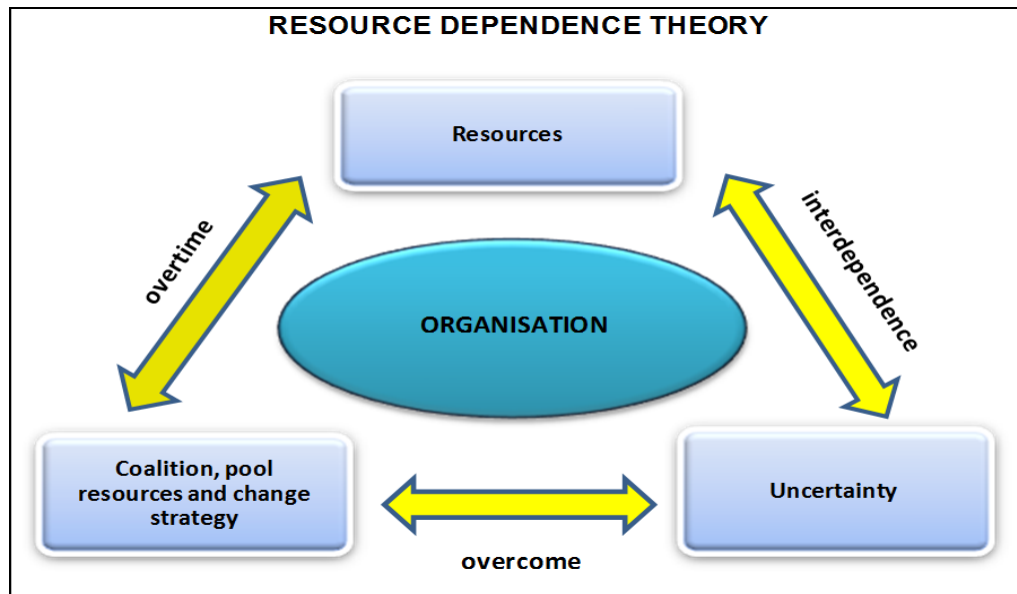


Figure 3.8: The interactions between an organisation's ecology in RDT

RDT views the interaction between the elements in an organisation's ecology as a cyclical process, encompassing three major factors. In relation to power in the context of RDT, organisations seek power by gaining control over resources which can reduce their dependence on other organisations, and at the same time, obtain control over resources that can increase the dependence of other organisations on them. This interdependence leads to uncertainty. In order to overcome this uncertainty, organisations form a coalition, pool resources and change their strategy. The interactions between the elements in the organisations' ecology affect how organisations work, as they are competing for scarce and valued resources which are considered vital for them to survive. However, over time, when balances in the market shift, more uncertainties surge in the environment, stability turns unstable again, thereby triggering the cycle all over again.

In brief, RDT rests on certain assumptions. First, organisations are presumed to consist of internal and external coalitions that emerge due to resource exchange, which then influences the organisation and controls its behaviour. Second, the vital resources needed for the organisation to survive are assumed to be limited, thus leading to the uncertainty in an organisation's resource acquisition. Finally, organisations are surmised to work toward achieving two main objectives: i) acquiring

control over resources, then minimising the dependence on other organisations, ii) similarly, acquiring control over resources helps to maximise the dependence of other organisations on them.

The element of uncertainty in acquiring resources is one of the problems that have to be confronted by the leaders in the organisations. It becomes their responsibility to assess this kind of unpredictability and to find solutions which solve the dependencies in the best way in order to survive. It is broadly defined in RDT that successful organisations are those which can gain control over resources by escalating their power over other organisations. Therefore, to obtain protection against the vicissitudes of their environments, in order to minimise their dependencies, there are five options¹² proposed by Pfeffer and Salancik (1978), one of these being through the board of directors.

The board of directors is widely known as the most vital mechanism in corporate governance practice. This area of research has received considerable attention by researchers, across disciplines and countries. However, most of them implement agency theory as their primary theoretical lens (Hillman et al. 2009). Based on the RDT point of view, the board of directors is the pivotal feature of the resources in organisations, which can minimise their dependence on other organisations. However, RDT is not a prevalent choice as a key theoretical lens. In spite of this, and reinforced by the empirical evidence, RDT is attested as being a persuasive lens for understanding the board of directors' characteristics.

RDT recognises the organisation as an open system which is integrated interdependently with external entities for survival (Pfeffer 1972). Therefore, it is postulated by resource dependence scholars that directors should reflect organisational dependencies (Daily, Dalton and Cannella 2003). Pfeffer and Salancik (1978) contend

¹² The options proposed by Pfeffer and Salancik (1978) to minimize environmental dependencies are: (a) merger/ vertical integration, (b) joint ventures, (c) board of directors, (d) political action and (e) executive succession.

that the resources which are acquired from other connected organisations are made via the directors on the board in order to benefit the organisation. Therefore, the board of directors is considered to be the main linkage mechanism which connects a firm to external resources (Hillman, Shropshire and Cannella 2007).

It is argued that by selecting directors with strong influence, valuable skills and good connections with external resources, the firm's outside dependency can be reduced. Pfeffer and Slancik (1978) proposed three main benefits that can be derived from board linkages: advice and counsel, legitimacy, and a channel to disseminate information. Thus, by first identifying the firms' characteristics, then applying RDT in sketching the framework, Hillman et al. (2009) contend that the best types of directors for benefitting a firm are able to be identified.

Referring to the second of the benefits proposed by Pfeffer and Slancik (1978) above, i.e. the legitimacy which is derived from the directors on the board, this echoes what is emphasised in institutional theory (Meyer and Rowan 1977; Scott 1995). The explanation provided is that societal expectation determines an organisation's legitimacy, whereby it is expected that the appointed directors are observed and recognised by society at large. This recognition leads prestigious members of society, such as institutional investors, to invest in the company, which reflects their acceptance and recognition of the organisation's legitimacy. Nienhuser (2008) also supports this view and claims that RDT has similar independent and dependent variables to institutional theory.

Therefore, although RDT is claimed to be a persuasive theory to explain the board of directors' characteristics, unfortunately it has its own limitations. There are a few organisational factors which are not considered under this theory (e.g. human resource practice, organisational cultures, values, beliefs and social factors), which also important for predicting board characteristics. Thus, RDT should be accompanied by other theoretical lenses, i.e. institutional theory, after considering the above arguments, as well as agency theory for its delicate insights in predicting relationships.

3.6 Summary

This chapter has provided an overview of the multi-theoretical approach, which espouses agency theory, institutional theory and resource dependence theory. Each of the theories is explained in different sections to reinforce the justification for them being applied in this study. The theoretical frameworks presented in this chapter are recapitulated in Chapter 4 to allow them to be customised to the current study setting. It is anticipated that applying this multi-theoretical approach will assist in articulating each of the hypothesised relationships in detail and persuasively.

Agency theory is the salient theory among them, and thus the key lens for our analysis in this study. It is for this reason that this theory has received the large share of discussion, followed by institutional theory in this chapter. The selection of this theory was instigated by the unique ownership structure and changes in Malaysia's institutional environment pertaining to corporate governance reform, which resulted from the macro crisis, i.e. the Asian financial crisis 1997/1998. The other theory (RDT) is underpinning theory to support the theoretical foundation for this study. The applications of these theories in the extant literature are well established, with many arguments pertaining to their far reaching effects in many facets. Thus, this study, which examines the dynamic changes in Malaysia's corporate governance, provides a bridge between agency theory, institutional theory and resource dependence theory in explaining the relationship of governance to foreign ownership.

The development of hypotheses in Chapter 4 will be achieved by interweaving many arguments from the three theories and extant literature. Therefore, the multi-theoretical approach is adopted as an overarching theory to justify the predicted relationships between FEO and corporate governance variables in the Malaysian corporate environment.

CHAPTER 4

THEORETICAL FRAMEWORK, LITERATURE REVIEW AND HYPOTHESES DEVELOPMENT

4.1 Introduction

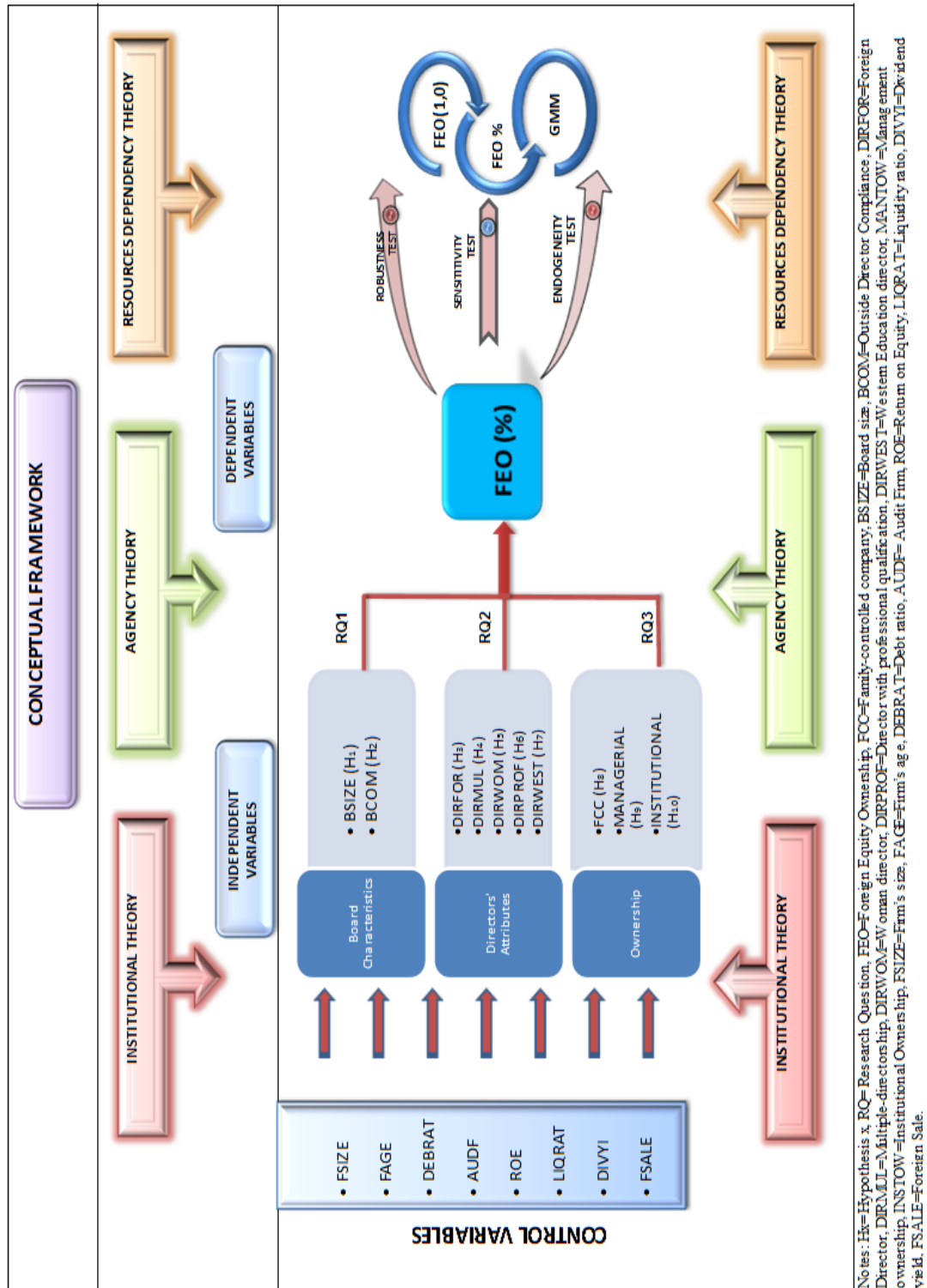
Chapter 2 reviewed the literature of corporate governance in general around the world, comparing Western literature with other parts of the world like Asian countries, and finally focusing specifically on Malaysia. Special emphasis was given to the issue of foreign equity ownership in alignment with the corporate governance impact, as this is the main issue of this study. Next, before testing the relationship in the hypotheses development chapter, Chapter 3 related the theories that can be applied suitably to articulate the unique features of developing countries, particularly Malaysia.

In order to further enhance the understanding of this study, the current chapter draws together the work from the two previous chapters, Chapter 2 and Chapter 3. It does this by discussing the theoretical framework and generating hypotheses using agency theory as an underpinning theory, with insights gained from institutional theory and resource dependence theory. The structure of this chapter proceeds as follows. Section 4.2 presents the conceptual framework as the spine for the whole research work, and briefly recapitulates the idea of base constructs and developing hypotheses on the theoretical underpinning. Section 4.3 restates the research question, while Section 4.4 reviews the related literatures, issues and theories to establish the framework for the hypotheses development. Lastly, Section 4.5 summarises the chapter.

4.2 Conceptual Framework

This section covers the corporate governance mechanisms (board and ownership structure) in relation to FEO, as suggested in this study. The overall process and the

relationships between the components in this study are depicted in the conceptual framework presented below.



Restated Figure 1.2: Conceptual framework for corporate governance and FEO in Malaysia

Before the discussion of hypotheses development proceeds, it is necessary to base construct (ownership structure, board characteristics and composition) on the theoretical underpinning of the study. The construction of conceptual framework, as can be seen from the Figure 1.2 in this current section, should be able to clearly depict the relationships that exist between the components in the constructs. Moreover, the theoretical concept should be well-embedded, thus providing a better picture of how the constructs are developed and related to the theoretical frameworks.

Firstly, it is important to revisit Chapter 3, which was devoted exclusively to discussing in detail the three theories (agency theory, institutional theory and resources dependence theory) that were selected to become the underpinning theories for this study. Secondly, it should be noted that 10 variables (please refer to the conceptual framework) were used as constructs for this study, these being subsumed under three categories, namely: board characteristics, directors' attributes and ownership structure (can be referred from the conceptual framework as well). These variables were chosen for a variety of reasons, such as lack of study, the potential variables of foreign investors' preference, the unresolved issue in existing literatures, the changes in corporate governance setting in Malaysia, etc. that making them essential for inclusion in this study. The detailed discussion for each variable and the reasons for them to be examined can be found in the current chapter, Section 4.4 Hypotheses Development.

Next, the theoretical base to be applied on each variable is justified. Agency theory is applied to all variables in the constructs as this is the main theoretical lens for this study. Agency theory has received substantial attention from researchers to study corporate governance in Malaysian setting. The advantage of this theory is in its ability to lead researcher to comprehend the investigated relationship by providing more precaution in any justifications offered. However, given the empirical evidence provided in a number of studies for example by Claessens et al. (1999), Haniffa and Hudaib (2006), Khatri (2001), Lew (2007), Lim (1981), La Porta et al. (1999), etc., there are argument that Malaysian corporate ownership structure is concentrated, with controlling shareholders being pervasive and minority shareholders' expropriation

being prevalent. Thus, the theoretical argument of agency theory should not be limited only to principal-agent conflicts, but should go beyond this by including the argument from the perspective of principal-principal goal incongruence as strongly recommended by Peng (2006) and Young et al. (2008).

In this study, agency theory is compatible with all variables in examining their relationship with foreign equity ownership in Malaysia. The ownership structure issue especially requires strong theoretical arguments in determining the direction of the relationships coincide with the unique characteristic of Malaysian capital market's ownership structure. Board characteristics and directors' attributes also extensively apply the arguments from agency theory, as the theory offers a justification for determining the positive and negative sides of certain variables to be connected with foreign ownership. For example, based on agency theory's theoretical arguments, foreign investors favour the presence of foreign directors on a board because it is considered to be one of the efficient corporate governance mechanisms to curb monitoring cost. It is believed that the existence of foreign directors (generally from the developed capital market) on the board may secure their interests in the firms as they share similar values and perspectives, which is to maximise shareholder wealth thereby reducing agency conflict.

On the other hand, institutional theory is a practical theory that is applied based on the situation of Malaysian market that has undergone a process of institutional change - moving towards the Anglo-American corporate governance practice following the Asian financial crisis 1997/1998. The process of institutional change can be translated as corporate governance reform. This is compatible with the home countries of foreign investors, the majority of which are Western countries that are accustomed to an established set of corporate governance practice in their countries. Thus, in this light, institutional theory is persuasive in terms of its application as one of the primary theories, in addition to agency theory, in explaining the relationship between variables. In analysing corporate governance reform, agency theory is argued as under-utilised with respect to the social aspect that is embedded in firms (Aguilera and Jackson 2003) which may detract from the whole picture (Douma et al. 2006)

concerning the relationship that might occur between corporate governance variables and the level of foreign equity ownership in Malaysian companies.

Generally, from the perspective of institutional theory, the arguments used to justify the relationship between two variables of study are based on the claim made by DiMaggio and Powell (1983) that the institutional forces arising from organisations are an effort to maximise shareholder value. Therefore, to understand corporate governance practice (proxied by the corporate governance variables) in Malaysian companies, the pressure exerted on them in the search for legitimacy has been translated through their action whether they imitate or adopt the governance structures of Anglo-American capitalism. Each of the components in variable constructs is refined in detail, in accordance with their institutional pressure and institutional background, and in order to justify their relationship with foreign equity ownership.

Therefore, the use of institutional theory to be applied on all variables in this study is considered significant to scrutinise the behaviour of foreign investors when making investment decisions in countries with a different (institutional) corporate governance setting, such as Malaysia. For example based on institutional theory, it is argued that foreign investors prefer companies with Western educational directors, as it is suggested that organisations are shaped by the normative pressures that pervade them (DiMaggio and Powell 1983; Meyer and Rowan 1977; Zucker 1987). Thus, in this scenario, the source of normative pressure is derived from the directors' educational background, which may result in changes in organisational structure in an isomorphic way, in accordance with institutionally prescribed expectation (Slack and Hinings 1994). It is argued that these directors may preserve foreign investors' interests in the company as they share similar values, which is to maximise shareholder wealth.

Lastly, resource dependence theory (RDT) has been used to strengthen the justifications made to hypothesise the relationship, in addition to the existing two theories, agency theory and institutional theory. RDT is used to complement institutional theory, as this theory is closely linked to institutional theory in describing organisation. RDT is used to support the primary theory and it is claimed that, with

the combination of these three theories together, greater predictive power can be offered to explain the presumed relationship (Sherer and Lee 2002). In this study, RDT focuses more on explaining the board director's characteristics and directors' attributes, as RDT sees the board of directors to be the pivotal feature of resources in organisations, which can minimise their dependence on other organisations. For example, from the perspective of RDT, it is argued that foreign investors favour the presence of foreign directors on corporate board as they are considered to be a crucial asset to the company in bringing in prospective resources such as global experiences, foreign networks (Masulis et al. 2012), managerial expertise (Kim et al. 2010), or technical skills that cannot be offered by domestic directors.

4.3 The Research Questions Restated

The contention that changes in Malaysian corporate governance have been taking place has been made in the earlier discussion. Public listed companies (PLCs) in Malaysia seriously started to adopt corporate governance reformation at the pinnacle of the AFC 1997/1998. Some scholars claim that these changes demonstrate a convergence on the Anglo-American governance system (e.g. Kim et al. 2010), while others discern that convergence should be concerned with establishing congruence with the Malaysian corporate culture (Haniffa and Hudaib 2006). Nevertheless, the changes are not uniformly applied to all of the elements in the corporate governance system. There are certain elements of the structure that show some resistance to institutional pressures (Slack and Hinings 1994), such as family ownership.

The present study therefore aims at improving our understanding of the process of investment decision making by foreign investors, particularly those from Anglo-American countries, driven by a few elements of corporate governance practices in developing countries like Malaysia. More specifically, the study seeks to answer the following research question:

Does corporate governance influence the level of FEO in Malaysian companies?

However, answering the main research question is contingent on the answers to the following subsidiary research questions: i) Do board of director characteristics

influence the level of FEO? ii) Do directors' attributes influence the level of FEO? and iii) Do ownership structures influence the level of FEO?

These answers are sought by relying on the argument derived from the multi-theoretical approach and previous literature. Hypotheses are generated accordingly in the next section.

4.4 Hypotheses Development

The hypotheses in this study are based on firm specific factors. These are subsumed into three groups, in order to answer three subsidiary research questions, as shown in the above figure and explained in Section 4.3 The Research Questions Restated. For hypothesis development and variable arrangement, equal weight of concern is given to each variable of corporate governance. The selection of board characteristics to be dealt first does not indicate that a higher level of priority has been given to the board characteristics variables and less to ownership structure variables. The following discussion of hypotheses development begins with the category of board attributes, while the remaining categories are treated equally.

4.4.1 Board Attributes

The board of directors is a crucial element in a firm's corporate governance system and has received special attention from many parties (Jiraporn, Davidson, DaDalt and Ning 2009; Masulis, Wang and Xie 2012). It has long been recognised, notably by Fama (1980) and Fama and Jensen (1983) that the board could become an important mechanism to prevent minority shareholders from expropriation by controlling shareholders, whilst Zahra and Pearce (1989) suggest that the board's main functions relate to organisational performance. Generally, the board of directors plays two crucial roles, which are monitoring roles (Fama 1980; Hermalin and Weisbach 1998) and advisory roles (Fama and Jensen 1983). The effectiveness of the board directors is measured through their performance in making corporate decisions and in creating shareholder value (Masulis et al. 2012). The following sub-sections discuss the role of

the directors on the board and associate this role with the level of foreign equity ownership (FEO) in the firm. Scholarly arguments, related codes and pertinent theories have been taken into consideration in developing the hypotheses.

This section aims to answer the first research question, which is - *Do board of director characteristics influence the level of FEO?* The discussions follow in each of the subsections.

4.4.1.1 Board Size

As specified in the Best Practice in Corporate Governance, board size can impact on its effectiveness. Therefore, it should be carefully examined (Code 2000). The question which arises is what is the ideal size of the board of directors in a company? This is an ongoing issue and has long been debated by both practitioners and researchers. Nevertheless, a conclusive consensus on board size has yet to be achieved.

Monks and Minow (1995) emphasise that board size should be given particular consideration, as it has a bearing on a company's monitoring, controlling and decision making capabilities. From an agency theory perspective, those who advocate a larger board size argue that the monitoring capacity may increase with the addition of director(s) to the board. A larger board size makes it more difficult for CEOs to dominate the board (Zahra and Pearce 1989). However, the claimed benefits may be outweighed by the '*incremental cost*' due to communication problems and the poor decision making processes associated with a larger board size (John and Senbet 1998). Hermalin and Weisbach (2003) also assert that when the size of the board becomes too large, the board becomes more of a symbol within the company rather than being truly involved in the management process. This view is consistent with the previous claim by Jensen (1993), namely that a small board size can increase a company's performance. Therefore, reducing the board size is suggested as a method of improving efficiency.

In contrast, drawing on RDT, it is argued that a larger board of directors produces greater diversity, which can assist a company to secure critical resources (Haniffa and Hudaib 2006) and lessen the uncertainties in the corporate environment (Dalton, Daily, Johnson and Ellstrand 1999; Pfeffer 1987). Correspondingly, Pfeffer and Salancik (1978) have stressed the importance of having a larger board of directors in order to give access to greater and more effective external linkage. Diversity also encourages constructive decision making, as members of the board may have different opinions on certain issues, which require a healthy debate, thus enabling the productive sharing of information. In addition, Pearce and Zahra (1992) contend that a large board is effective in providing advice and charting the strategic direction of the firm. However, the 'free rider' problem is also associated with a larger board size.

Lipton and Lorsch (1992) recommend that the ideal board size is between eight and nine members, whilst Jensen (1993) suggests that the ideal number to be between seven or eight. They have mutual agreement with John and Senbet (1998) that any additional numbers of director(s) will lead to inefficiencies in the decision making process and in monitoring activities. In a different study, Haniffa and Hudaib (2006) found a significant, negative relationship between board size and market performance in Malaysian companies, which indicates that markets perceive a large board size to be ineffective. This result is consistent with previous empirical studies by Yermack (1996) on large US corporations, using Tobin's Q as a market performance indicator. A similar pattern was found by Eisenberg, Sundgren and Wells (1998) in their study of small and mid-size Finnish firms. However, by using a different accounting measurement, Haniffa and Hudaib (2006) found a significant relationship with board size, but in a different direction. This implies that although the market in Malaysia perceives a larger board size as being only symbolic, rather than seriously managing the business, the company actually obtains benefits from the diversity that a larger board can offer. This pool of expertise and experience can become a critical resource in enabling companies to survive in an uncertain corporate environment, as proposed by RDT.

In developed markets like the US, UK and New Zealand, no definite number for the board size has been determined for adoption. Boone, Field, Karpoff and Raheja (2007) in their study found that the board size increases in relation to the firm size. This finding is consistent with other studies, which arrive at the conclusion that board size can increase or decrease in relation to other factors, such as growth opportunities (Mak and Roush 2000), asset characteristics and governance practice in firms (Boone et al. 2007; Linck, Netter and Yang 2008). As alleged by Coles, Daniel and Naveen (2008), adopting a “one-size-fits-all” approach is misguided. Therefore, there is no robust cut off to be followed, as the Anglo-Saxon market, which represents the developed market, does not pronounce any ideal number for the board size that can fit every corporation. However, practitioners believe that the enactment of the Sarbanes-Oxley Act (SOX) in 2002 reflects an attempt to improve corporate governance practice and restrict the corporate board structure in the U.S (Raheja 2005).

Likewise, there is no recommendation in the Malaysian Code on Corporate Governance (MCCG) concerning the ideal number for the board size for PLCs in Malaysia. This is consistent with the practice in developed markets, where the board size is not prescribed in any of their rules and regulations. As a developing market, which expects outside investors to flood the market, the steps taken by the developed markets seem a sensible model to be imitated. Therefore, no fixed number for the board size is proposed for PLCs in Malaysia.

In this context, in regards to the Malaysian case, it is argued that mimetic isomorphism has been applied. The action of the Malaysian government, in imitating the existing structure and practices of countries that are perceived to be more successful, is claimed by DiMaggio and Powell (1983) to be an exercise that has been induced by the uncertainties that have pervaded the corporate environment in Malaysia, especially after AFC 1997/98. After the financial turmoil, there was a high degree of uncertainty in the Malaysian corporate environment due to institutional transition in the country. The MCCG was drawn up by referring to the Cadbury Report (1992) and the Hampel Report (1998) in the UK (Haniffa and Hudaib 2006). However, no specific number for the directors on the board was proposed in either of

the reports. Therefore, the practices undertaken by most of the successful organisations in the developed markets have been imitated. This means that the individual company is free to determine its board size, provided that board effectiveness is not compromised.

Code (2000) does place emphasis on board effectiveness, whereby it is recommended that the board should consist of a balance of executive and non-executive directors (including independent non-executive directors). This is to ensure that “*no individual or small group of individuals can dominate the board’s decision making*” (Code 2000:7). In ensuring its effectiveness, the size of the board must not be too large or too small.

The results of the survey conducted by KLSE and PricewaterhouseCoopers in 1999 found that on average, the board size in Malaysian companies consisted of eight directors and the composition of each board generally constituted of independent non-executive directors, equalling about one third of the board. The committee of Finance Committee of Corporate Governance (FCCG) has only formulated the board composition structure, rather than recommending the ideal size of the board. This approach is preferred, as there are many characteristics which should be considered before prescribing a figure for the board size, such as the size of the listed companies, etc. Therefore, their board size must be varied significantly.

Although the size of the board of directors is not prescribed by the Codes, the impact of choosing the ideal number of directors on the board is significant, as evidenced in many studies. Companies should determine the ideal size of their board in order to ensure that the board of directors can perform its duties effectively for the sake of shareholder value. Foreign investors are believed to monitor the size of the board of directors in a company before making their investment decision. Drawing on agency theory and RDT, both theories favour a larger board. Therefore, it is argued that foreign investors prefer companies with a larger size for the board of directors. Nevertheless, the standpoint of these theories has received much criticism from the scholars that advocate a smaller board (e.g. John and Senbet 1998; Hermalin and

Weisbach 2003). In addition, institutional theory plays its role in strengthening the reasons behind the action taken by the Malaysian government for not having a compulsory board size. Even though foreign investors are highly likely to favour the practice that has been imitated from their home countries, there is a recognition of the significant role that having the right size for the board of directors plays for foreign investors, and it is therefore hypothesised that:

Hypothesis 1: A larger size for the board of directors in Malaysian PLCs is positively associated with the level of foreign equity ownership.

4.4.1.2 Outside Director Compliance

Outside directors are broadly defined by Johnson, Daily and Ellstrand (1996:417) as “all non-management members on the board”. In the Malaysian context, the terms for outside directors are interchangeable with independent directors. However, the concept of ‘independent’ is unique to each country (Code 2000; Rediker and Seth 2005). For Malaysian companies, the term independent refers to two crucial aspects: i) independence from management and ii) independence from a significant shareholder¹³ (Code 2000:25).

The composition of outside directors is an ongoing issue. The effectiveness of having higher proportions of independent outside directors has been widely discussed (e.g. Jiraporn et al. 2009; Johnson, Hoskisson and Hitt 1993; Pearce and Zahra 1992; Peng 2004; Tihanyi, Johnson, Hoskisson and Hitt 2003), since the effectiveness of a board to oversee the management is highly related to that composition (Code 2000:23). In 2000, as an attempt to improve corporate governance, the Malaysian government set out the benchmark for best practice in corporate governance, thereby putting pressure on all PLCs to appoint a certain ratio of independent directors to their board. It is very

¹³Significant shareholder is defined as “a shareholder with the ability to exercise a majority of votes for the election of directors” (Code 2000:10).

important to have a ‘board balance’¹⁴ to ensure that the members of the board play fair and active roles, thus making them an effective board. It is contended that PLCs need to be headed by an effective board to ensure that the companies can be managed and controlled efficiently.

Even though executive directors are undoubtedly important to companies, as they have the skills and knowledge to run the business, the appointment of outside/non-executive directors with a wealth of experience helps to bring a broader view to the company’s affairs as they are capable of exercising independent judgement (Code 2000:23). As alleged by Perry and Shivdasani (2005), outside directors are better at taking the initiative to form a disciplined restructuring programme after any substantial performance decline has occurred in the company.

The appointment of independent directors to the board is one example of good governance practices (Cho and Kim 2007; Payne, Benson and Finegold 2009). Although this practice has long been applied in the Anglo-American governance system, Peng (2004) considers this kind of practice in emerging markets as a type of management innovation. The adoption of corporate governance codes from more developed markets is evidence of corporate governance reformation (Aguilera and Cuervo-Cazurra 2009), which has been taking place in Malaysia in the immediate aftermath of the AFC 1997/1998.

The Code of Best Practice for Corporate Governance¹⁵ - Code (2000) - stated that board composition should be composed of at least one third (1/3) of independent non-

¹⁴Board balance is defined by Code (2000:9) “Non-executive directors should be persons of calibre, credibility and have the necessary skill and experience to bring an independent judgement to bear on the issues of strategy, performance and resources including key appointments and standards of conduct. To be effective, independent non-executive directors need to make up at least one third of the membership of the board”.

¹⁵Best Practice in corporate governance is set out in Part 2 of Malaysian Code on Corporate Governance. It identifies a set of guidelines / practices intended to assist companies designing their corporate governance mechanism system. The

executive directors in order for the board to be effective. This is exactly what was enshrined in the Hampel Report 1998, published in the UK. In the earlier discussion, Chapter 2, Section 2.2 Corporate Governance, a brief history of this report has been given.

This reaction taken by the government of Malaysia to escalate the composition of independent directors on the board, or at least abide to their minimum requirement, was a reaction to the radical changes in the macro environment, specifically the AFC 1997/1998. Furthermore, there was also intense institutional external pressure from the actors (for instance, the IMF) in the economic environment. Scott (1987) argued that these external pressures are to be fulfilled by the institutions in order to obtain their legitimacy and to access external resources. DiMaggio and Powell (1983) suggest that outside directors could be adopted in an isomorphic fashion in many countries. The nature of the institutional environment in Malaysia coincides with the recommendation made by a few scholars (see Aguilera and Jackson 2003 and Buck and Shahrin 2005), to utilise institutional theory as the main theoretical lens in order to analyse the process and antecedents of appointing independent directors on a Malaysian board.

Malaysia's corporate environment has always been influenced by government intervention, policies and regulations. The political pressure in Malaysia's economy towards business players is not something new, albeit they are very intertwined with each other (Gomez 1994). Since 1970, the Malaysian government has encouraged and facilitated many business activities by a group of large firms, designated as government link companies (GLCs¹⁶), to support economic development in Malaysia.

compliance towards the best practice is voluntary; however they need to disclose in their annual reports, the extent of compliance and noncompliance(s), if any, needs to be justified.

¹⁶Government link company (GLC) is defined as company in which the Malaysian government has direct controlling interest of more than 20% through Government-Linked Investment Companies (GLICs) (The Treasurer Circular, Ministry of Finance 1993). However, the extent of government intervention is not just depends on percentage ownership, it refers to the ability of government to

In 2009 for instance, GLCs dominated nearly 40% of the total market capitalisation in Bursa Malaysia. Among the well-known GLCs are the Malaysia Airline System (MAS), PETRONAS, PERWAJA etc., and they are very close to government policies. The significant contributions made by these GLCs and other PLCs to the Malaysian economy cannot be denied as their relationships are reciprocal. These companies play a crucial economic role, and the Malaysian government has never failed to support and reward them. Therefore, in the aftermath of the AFC 1997/98, the Malaysian government decided to initiate a corporate governance reformation programme, in order to regain the confidence of investors, after they shied away from the Malaysian capital market.

The government intervention in the governance matters of PLCs, by exerting pressure to maximise the compliance of the independent director composition on the board, is seen as an action that has to be accomplished by organisations with limited options. This kind of situation is identified as 'forced selection' by Abrahamson (1991), whereby a powerful institution such as the Malaysian government can use its power to exert political pressure on an organisation in order to ensure that it adopts innovations to help it maximise shareholder value, or reject them if it is otherwise. This institutional pressure, as asserted by DiMaggio and Powell (1983), is known as coercive isomorphism. The later study by Oliver (1997) claims that institutional pressure can also be exerted in two ways; legal coercion and voluntary diffusion.

In the Malaysian case, the pressure can be in both forms. The ultimate results of fulfilling the pressure exerted by a more powerful institution were predicted to benefit the organisations as a whole. Therefore, the PLCs in Malaysia seem to be voluntarily receptive to this idea. Apart from enhancing the organisation's legitimacy (Scott 1987), it is also consistent with the RDT perspectives, as argued by Pfeffer and Salancik (1978) that strong interdependence between the superior and its subordinate

make major decisions for companies such as selection of BOD's members, restructuring, policies, acquisitions etc.

(in this case, the Malaysian government and the PLC), and the obedience shown by the latter, enables the dependent organisation to access more resources from the former, concomitantly enhancing the firm's value (Chizema and Kim 2010). Outside directors are seen as having large networking capabilities, thus acting as a corridor to access external resources or potential markets which can benefit a company in many ways, e.g. strategic decision making (Carpenter and Westphal 2001).

From the perspective of agency theory, the role of independent directors in an emerging country like Malaysia is believed to reduce agency problems (Fama and Jensen 1983) as outside directors can assist to monitor owner-managers (Cho and Kim 2007). This claim is consistent with the new corporate governance perspective for emerging markets, which is focused on the conflicts between the minority and controlling shareholders, and is alluded to by Young et al. (2008) as the *principal-principal* model¹⁷. It is also asserted by Jiraporn, Singh and Lee (2009)^b that a large composition of independent directors on the board may lead to the strongest monitoring of management. By having a large number of independent directors on the board, it is highly likely that the majority of compensation, audit, and governance committees members, are comprised of them - as recommended by governance experts (Code 2000:13; Jiraporn et al. 2009^b). Meanwhile, studies by Bonn (2004) and Dahya and McConnell (2007) imply that the benefits of having a high proportion of outside directors on the board can be seen in a significant improvement in companies' operating performance. In Malaysia, the results are echoed in a few studies (Abidin, Kamal and Jusoff 2009; Ameer, Ramli and Zakaria 2010).

In summary, the multi-theoretical approach (MTA) applied in this study advocates a positive effect on compliance of adhering to the minimum requirement composition of independent directors on the board. Thus, based on the lengthy arguments above, it is

¹⁷Principal-principal model is emerged from emerging markets where the concentrated ownership is prevalence. Concentrated ownership, combined with the weakness of corporate governance mechanisms, results in more conflicts arise between controlling shareholders and minority shareholders, and has come to be known as principal-principal (PP) model.

argued that governance practice is enhanced by the high composition of independent directors on the board. The role of the Malaysian government in applying pressure regarding this issue can also be seen as an impetus to encourage more companies to adopt this practice. In addition, relatively speaking, good governance practice leads to a company's high performance. Besides this, the practice of having a relatively high proportion of outside directors on the board has long been practised by the developed market. Therefore, it is in line with the practice recognised by most of the foreign investors in their home countries, which assumes that foreign investors prefer companies which comply with, or work beyond, this compliance. Thus, through the institutional pressure or coercive isomorphism exerted by other powerful institutions, the adoption of this practice is seen by foreign investors as an indicator of good governance practice in a company, which simultaneously mitigates agency costs and accommodates more vital resources for the sustainability of the company. Therefore, it is hypothesised that:

Hypothesis 2: There is a positive association between the presence of outside directors on the board and foreign equity ownership in the firm.

4.4.2 Directors' Attributes

Different attributes among directors lead to board diversity. Board diversity is a term to describe the existence of female, multiracial and cultural elements in the composition of the board of directors. The extant literature (e.g. Erhardt, Werbel and Shrader 2003) typically follows two general distinctions for diversity classifications, (i) observable (demographic) and (ii) non-observable (cognitive). Generally, observable diversities are gender, race, age and ethnicity, whilst unobservable diversities are education, values, knowledge, perception etc. The existence of these multi-elements in the board members is believed to affect a firms' long term and short term financial performance (Carter, Simkins and Simpson 2003). A few selected directors' attributes are discussed in the following subsections. Do these directors' attributes (foreign directorship, multiple-directorship, women directorship,

professional directorship and Western educational directorship) have a bearing on the level of foreign equity ownership (FEO)?

More specifically, this sub-section aims to answer the second research question, which is: *Do directors' attributes influence the level of FEO?* The discussion follows in each subsection.

4.4.2.1 Foreign Directorship

The inclusion of foreign director(s) on the board of directors may bring different cultural dimensions, and therefore affect the overall monitoring system of board performance (Kim et al. 2010). This is consistent with the perspective of RDT, and with the idea that heterogeneity in the resource capabilities of the different directors on the board will lead to a positive impact on firm performance (Douma et al. 2006). The foreign director may bring global experience (Masulis et al. 2012), managerial expertise (Kim et al. 2010) or technical skills to the firm which may not be accessible by the domestic director. Foreign directors also help to improve the board's advisory role by transferring the first-hand experience and knowledge that they have gained from their home countries, thereby enabling the company to expand its foreign networks (Masulis et al. 2012) and operations internationally (Adams, Hermalin, and Weisbach 2010).

Drawing on the agency theory perspective, foreign directors may act more independently in monitoring the management of the company as their personal attachment to it is weaker than that of the local director. Kim et al. (2010) found a positive relationship between foreign ownership and the presence of a foreign outside director, suggesting that foreign portfolio investors prefer firms with a foreign outside director. As asserted by Erhardt et al. (2003), the inclusion of foreign directors on the board, from the corporate governance perspective, relates to the degree to which a CEO may have influence on the board. As proposed by Schleifer and Vishny (1997), CEOs may need independent overseeing; therefore, the inclusion of a foreign director on the board is likely to have a positive impact on the monitoring function and could

be one of the corporate governance mechanisms which minimises potential agency issues. The appointment of a foreign director may be perceived by foreign investors as a sign of improved governance. Subsequently, they may translate this into a positive signal and this may act as a catalyst for them to invest in the firm (Kim et al. 2010).

Nevertheless, there is evidence offered in a few studies which provides a different view on this issue. Masulis et al. (2012), for instance, find that foreign directors are more likely to engage in international misreporting and this is also associated with significantly higher CEO compensation. They also find that a board meeting attendance problem is associated with foreign independent directors. Poor board meeting attendance is due to the geographic distance¹⁸, making them less effective in overseeing management compared to the domestic directors. Therefore, the overall impact of board directors on monitoring and controlling activities is undermined. Attending board meetings is crucial, as emphasized by Adams and Ferreira (2009), Jiraporn et al. (2009) and Masulis et al. (2012), who note that the board meeting is an important avenue for the interactions of directors and management.

Besides this, the geographic distance also triggers another problem. Foreign directors are cut off from local networks, making them less informed pertaining to the current information about a company (Coval and Moskowitz 1999), for instance its performance and operations. Consequently, this can result in detriment to the firms if decision making is based on inadequate information. Apart from being less responsive to current local information, foreign directors are likely to be less familiar with the local accounting rules, laws and regulations, corporate governance standards, and niche management styles; this complicates their decision making process as familiarity plays a crucial roles in comprehending local issues. Considering these

¹⁸Board meetings are usually held in corporate headquarters. If foreign directors are not domiciled in the local country in which they are appointed, then geographical distance is the main constraint for them to perform efficiently. This happens when attending the meeting becomes more difficult and time consuming, especially with different time horizons, which requires more time and energy to be consumed.

constraints, foreign directorship is claimed by a few scholars to be one of the factors that can weaken a board's monitoring effectiveness, which leads to exacerbating the agency problems between shareholders and managers, resulting in poorer company performance (Masulis et al. 2012).

Further evidence of the deficiencies in appointing foreign directors can be seen in the Enron scandal case in 2001. During the fraudulent years, from 1997-2001, its audit committee consisted of two foreign independent directors¹⁹, and later their roles and effectiveness in monitoring the firm's operation and overseeing its financial reporting were questioned.

Institutional theory comes with a perquisite perspective. It is argued that foreign directors on the board, particularly those from the USA and the UK, bring with them the norms and values that emphasise maximising shareholder wealth. These characteristics are favoured by foreign investors as they also share similar attributes when making investment decisions (Ahmadjian and Robbins 2005). Usually, in developed markets, there are two means by which foreign investors can promote their interests. They can either use the threat of *exit* – leaving the company by selling their shares if they are not satisfied with the management, or they can use the *voice* mechanism through shareholder activism. According to Nooteboom (1999), these two options could be achieved through coercive isomorphism. However, it is argued that, for a developing country like Malaysia, these mechanisms do not fit well with its institutional environment, where shareholder activism is weak and the process of promoting shareholder value is still in the undertaking period (especially after the AFC 1997/1998).

¹⁹The two foreign directors included in the Enron audit committee were Chairman of the Hang Lung Group from Hong Kong and a senior executive of Group Bozano from Brazil.

Therefore, different mechanisms are sought by foreign investors in selecting companies for investment. Alternatively, I argue that foreign directorship could be one of the favourite criteria of foreign investors when making their investment allocation. Foreign directors are claimed to bring auxiliary styles to the traditional board of directors by ensuring an ideational shift of boundary in making company decisions and advocating new management practices with the shareholder value maximisation objective in mind. In institutional theory parlance, this is referred to as normative isomorphism.

Given the concomitant benefits and drawbacks of having foreign directors on the board, the net effect on the overall board effectiveness regarding corporate governance, company performance and foreign investor decisions is refined. It is argued by Masulis et al. (2012) that unless the company has major operations in the home regions of foreign directors, the expected advisory benefits derived from the appointment of foreign independent directors onto the board are not great enough to offset the adverse effects due to the value destroying nature of their poor monitoring and disciplinary roles. From the corporate governance perspective, the geographical factor plays a crucial role in ensuring that foreign directors can effectively perform their duties, as it can impede their performance in monitoring management and in comprehending the company's local laws and regulations. However, drawing on institutional theory, foreign directors on the board can be said to represent foreign investors in their decision making processes. Since they share the same norms and values, which place emphasis on maximising shareholder wealth, the approaches that are applied in the decision making processes and management actions proposed by foreign directors are believed to benefit foreign investors.

Therefore, it is argued that, in the Malaysian setting, foreign investors strongly prefer the existence of foreign director(s) on the company's board of directors in order to represent and secure their interest in the company. The appointment of foreign board members is likely to send a positive signal to foreign investors as a sign of good governance practice. Therefore, it is hypothesised that:

Hypothesis 3: Foreign directorship is positively associated with foreign equity ownership.

4.4.2.2 Multiple directorships

‘Director’s busyness’ or multiple-directorships, the preferable term used in the present study, has garnered a great deal of interest among researchers (Ferris, Jagannathan and Pritchard, 2003; Jiraporn et al. 2009). Scholars who advocate multiple-directorships point out the many benefits to be derived from this extra commitment assumed by directors. They regard multiple-directorships as a corporate recognition of directors and, as alleged by RDT, through additional directorships in other companies, directors can bring in more vital resources and help the sustainability of the corporation in an uncertain corporate environment.

Drawing upon RDT, directors with multiple-directorships are gaining precious executive experiences, learning more managerial styles (Carpenter and Westphal 2001), establishing corporate networks (Loderer and Peyer 2002) and this also signals positive recognition of their expertise. Fama (1980) and Fama and Jensen (1983) are inclined to agree with this point, and contend that outside directors, for instance, should aim for multiple-directorships to build their reputation as monitoring experts. It is also considered to be an excellent opportunity to ‘advertise’ corporate receptiveness to their credibility. These positive views are consistent with the argument that these directors (proxied by multiple board seats) are highly honoured and that their services are highly sought-after.

However, there are also different opinions with regards to this contentious issue. Core, Holtausen and Larcker (1999) do not agree with Fama (1980) and Fama and Jensen (1983), questioning the impact on a director’s fiduciary duty, which they claim can be jeopardised. For instance, Ferris et al. (2003) assert that directors who sit on multiple boards may be unable to perform their duties effectively due to their stretching schedules. They face time and energy limitations in performing their duties in specific firms (Fich and Shivdasani 2006). It is more likely that there will attendance problems

with respect to directors with multiple-directorships, because of their highly attached commitment. This view is evident in a later study by Jiraporn et al. (2009) who also found a significant relationship between multiple-directorships and the attendance problem of board directors at meetings. They associate multiple-directorships with ‘director’s busyness’.

Generally, the above views indicate that ‘director’s busyness’ may lead to corporate governance problems in the company (Fich and Shivdasani 2006). Time limitations may hinder a director from attending board meetings as per the schedule (Masulis et al. 2012), which from the point of view of corporate governance is one of the crucial methods of disseminating important information about the company, and for directors to understand and exercise their duties (Adams and Ferreira 2009; Jiraporn et al. 2009; Masulis et al. 2012). Even though failure to attend board meetings does not directly imply that directors are not fulfilling their roles, it is still a visible way to measure how the directors’ responsibilities have been abused. Consistent with the report produced by Core et al. (1999), Jiraporn et al. (2009) claim that the failure to attend board meetings indirectly affects the firm’s value. This statement refers to the results of the study by Vafeas (1999), which provide evidence that the performance of the company improves following the years when the board meetings occur more frequently than usual. Likewise, from the vantage point of agency theory, the ‘busyness’ lessens the management monitoring activity²⁰ performed by the outside directors, and this may therefore increase agency costs which can lead to a deterioration in the firm’s value (Core et al. 1999; Ferris et al. 2003).

The negative consequences of multiple-directorships are further highlighted by Jiraporn et al. (2009)^b. They offer evidence concerning how directors with overloaded commitments have their capacity undermined through their inability to serve on internal board committees. Drawing on the agency theory perspective, internal board

²⁰ In this view, the quality of the monitoring activity reduces when there is the ‘attendance problem’ of directors due to their high commitment in other firms.

committees, (for instance audit committees and compensation committees) could reduce agency problems. These committees are important in monitoring a company's vital activities, for instance, financial reporting. Small board committees are more sensitive to a certain issue, for instance the issue of CEO remuneration, rather than if this is discussed in a large board of directors (Laux and Laux 2009). Unfortunately, directors who seek a higher reputation by serving on the board of more firms have less time to serve on internal committees. As a result, the cost of monitoring has been transferred at the expense of the shareholders. Apart from this, the company itself may be reluctant to appoint busy directors to important tasks that they might not be able to perform in normal conditions, which in the end may create frustration. Therefore, Jiraporn et al. (2009)^b postulate that directors with multiple-directorships should serve on fewer internal board committees.

Nevertheless, from the attributes of a firm's size and total sales, the inverse results are derived, as attested by Jiraporn et al. (2009)^b. The results show that busy directors are associated with larger firms and higher total sales, which is not surprising, albeit a little bit disconcerting. It is to be noted that the expertise and reputation of directors, as sought-after by the larger firms, are built upon many board appointments. In summary, directors with multiple-directorships serve on fewer internal board committees, but there is a turning point when the outside directorships reach a certain value. Beyond this value, serving board committees increases concomitantly with the number of outside directorships.

In addition, the monitoring role, which is assumed to be one of a director's main roles, may be superseded by the existence of efficient regulations (Booth, Cornett and Tehranian 2002). In the developed market, for instance, the SOX Act²¹ was enacted in late 2002. Given the responsibilities outlined in the SOX, directors are burdened with extra risks if they do not perform their roles properly. Thus, it is expected that the existence of additional regulations, like SOX, could help to monitor the performance

²¹The goal of the Sarbanes-Oxley Act was to strengthen the corporate governance mechanism in public corporations.

of directors and this places a greater burden on them if they fail to fulfil their obligations, for example attending board meetings. Jiraporn et al. (2009)^b claim that recent studies have found a significant positive relationship between corporate governance variables and the effects of SOX.

In Malaysia, there is no maximum number of directorships designated by the Code. It is recommended that the responsibility for assessing the most suitable number of directorships is held by a nomination committee. The assessment should be made by considering the individual's other commitments, the allocation of their time which is available for the company, and the resources that are attached to them which may benefit the company.

Even though there is an absence of a specific number for directorships in the Code, the government of Malaysia, aware of the potentially hazardous effects for shareholders of directors sitting on too many PLCs boards, has taken an initiative to restrict the number of directorships held by a director at any one time. Drawing upon the institutional theory perspective, the Malaysian government has used its substantial power to put pressure on the PLCs in Malaysia to deal with this issue. It is feasible to achieve this by implementing the rules through the Listing Requirements of the Bursa Malaysia (Code 2000). The Bursa Malaysia listing requirements of 2002 require a director to hold no more than 10 directorships in public listed companies, while the number of directorships should be 15 or less for non-listed companies. Recently, this restriction has been tightened by limiting the number of directorships in listed companies from 10 to only 5. As claimed by Yoshimori (1995), whenever huge corporate mismanagement has occurred, there is always increased pressure to reduce the maximum number of directorships, often the recommended number is 5. The rationale behind this restriction is to ensure that directors can perform their duties effectively.

Therefore, in order to be listed in the Bursa Malaysia, the PLCs in Malaysia, with few other options, have to follow the prescribed requirements. DiMaggio and Powel (1983) assert that the institutional forces exerted by higher organisations, in an effort

to maximise shareholder value, place extreme pressure on firms in search of legitimacy to adopt the governance structures of Anglo-American capitalism. This kind of pressure, in the form of force, is translated as coercive isomorphism under institutional theory parlance, which has to be abided by in order to stay legitimate and to be perceived by societal members. Foreign investors should be more confident about placing their investments in PLCs that comply with this rule, as they can be assured that the directors on the board can give a reasonable commitment to maximising shareholder wealth, simultaneously mitigating the agency problem.

Therefore, the empirical studies concerning this issue have given equivocal evidence, which at this point needs to be deciphered cautiously. Referring to the arguments, the extant literature, and pertinent theories, it is argued that in Malaysia, multiple-directorships simply a negative signal to foreign investment. In this regard, it is hypothesised that directors with multiple board-sitting status are more likely to dilute their quality time in a company due to their stretching schedule, which apparently affects their fiduciary duty and monitoring activity in the company. This implies a negative effect on corporate governance practice in the company which is not preferred by foreign investors. This hypothesis thus predicts a negative relation between the FEO and the number of multiple-directorships:

Hypothesis 4: The level of foreign equity ownership is negatively associated with multiple-directorships.

4.4.2.3 Female Directorships

In this section, board diversity term solely refers to the female director(s) on the board of directors or women directors. Carter et al. (2003) assert that gender proportion is among the most significant governance issues facing the management, directors and shareholders in the modern corporation. The heightened interest in female directorship coincides with the escalating proportion of women on boards of directors (Daily, Certo and Dalton 1999).

The interest shown in this issue comes from many parties, not only investors but researchers and policy makers as well (Farrell and Hersch 2005). Apart from the fact that, worldwide, women on boards are increasing in number, their proportion on the board is far from uniform across firms (Hillman et al. 2007). Apparently, this trend persists even though there are increasing pressures from many parties, for instance, institutional investors (Singh 2005). Many institutional investors hold the view that investment should be made only in companies with gender diversity on the board, which is then moulded into their policies (Coffey and Fryxell 1991).

Worldwide, gender diversity is amongst the main focal points (Carter et al. 2003) for governance reformation (Adams and Ferreira 2009). Accompanied by the fact that Malaysia has undergone a reformation process in firm corporate governance, gender diversity is an element which needs to be applied to the Malaysian company's board of directors. Many developed countries (for instance, UK, Norway, Spain and Sweden) have stressed the importance of having female directorships (25% - 40% representation on the board) which they claim could enhance board effectiveness in many ways including governance practice (Adams and Ferreira 2009). From the view of institutional theory, this practice of the developed countries becomes a benchmark for companies in Malaysia when considering the proportion of women on the board.

To find legitimacy, as sought by the societal members - for example, institutional shareholding (Singh 2005) - the mechanism that can be used by companies in Malaysia is mimetic isomorphism, one of the isomorphism mechanisms which were identified by DiMaggio and Powell (1983). Based on the explanation of institutional theory, there is a powerful pressure that pushes the organisations that are confronting uncertainty to initiate the action of imitation. This pressure comes from other successful organisations, particularly from the developed capital market.

Institutional theory and RDT are in mutual agreement that the appointment of female directors onto a board is based on the argument that they assist an organisation to seek organisational legitimacy, and that it can be conferred by societal members (Meyer and Rowan 1977; Scott 1995). The pressure coming from influential societal

members, for instance institutional shareholders (Coffey and Fryxell 1991; Singh 2005), to include female director(s) can be a strong factor for an organisation to make such an appointment. A corporation attempts to adhere to the political pressures and thus give more minorities a position on the board as well as on board committees (Jiraporn et al. 2009^b). This pressure is more pronounced in larger organisations (DiMaggio and Powell 1983; Meyer and Rowan 1977) because they are more visible to the public (Salancik 1979) and are bonded to strict regulations. By abiding to gender diversity insistence, the reputation and credibility of organisations may improve and subsequently be recognised by society (Hambrick and D'Aveni 1992), including foreign investors. Thus, it is postulated by Milliken and Martins (1996) that gender diversity on the board helps to increase legitimacy to an organisation.

On the other hand, drawing on RDT, in relation to auxiliary benefits, Kang, Ding and Charoenwong (2010) are of the same view as Fondas (2000), whereby they link the appointment of female director(s) with the positive improvement in the board's control and strategic function. Fondas (2000) argues that women, based on their experiences, have a special ability to comprehend the market. They can go to great lengths to understand consumer need, which in no way can be substituted by men. This claim is attested by the purchasing powers shown by women in relation to men. Thus, the inclusion of female directors on the board simultaneously contributes to a range of experiences and values (Selby 2000). Burke (2000) favours this view, and further adds that women directors create an important symbolic value in the company, which helps in linking the firm with other organisations, compared to men (Hillman et al. 2007). They can promote effective global relationships (Siciliano 1996), which assists the company to access its external constituencies (Burke 2000^b).

The above perspectives, gleaned from two main theories, are taken and fused with the view of agency theory. Drawing on agency theory, it is argued that female directors could assist in reducing the agency cost and protect shareholder wealth (Kang et al. 2010) as they are claimed to be more sensitive than male directors, and thus give extra 'concern' to the issues raised in the company by asking sensible questions (avoiding stereotyped questions) of the board of directors concerning the issues (Selby 2000).

Konrad, Kramer and Erkut (2008) assert that when making company decisions, women directors provide different perspectives on the issues, ask difficult questions, expand the content of the issues, raise any issues that pertain to multiple stakeholders, and use their interpersonal skills to influence the board process.

In addition, in making the financial decision for company, it is argued that by appointing women directors, it is likely that immoderate risk taking is reduced, as the study by Jianakoplos and Bernasek (1998) in the US setting found. Here, it was noted that women avoid excessive risk when compared to men – and they are more likely to be risk-averse. Besides this, Ferreira (2010) also associate female directorship with CEO turnover in relation to the stock return performance, which is one of the methods used to gauge the effectiveness of board monitoring roles. In this controversial area, Konrad et al. (2008) are consistent with what is postulated by principal-agent theory, whereby higher risk should be compensated with higher pay, and women directors have been found to play pivotal roles by raising tough questions and demanding straight answers pertaining to CEO performance. Thus, a CEO should give up their position due to a failure to increase the stock value, which is proved to have a significant relationship with female directorship.

The monitoring role played by women directors is also crucial. Lessons were learned from the unprecedented history of the Enron scandal in 2001, where a lack of independent overseeing and control of the company's financial report, eventually led to the bankruptcy of the Enron Corporation. Erhardt et al. (2003) reviewed the Enron's 1998 annual report, which revealed that of 17 board members, there was only one female director. This shows that Enron's board of directors was not diverse at that time and the board failed in its overseeing function.

According to Hambrick and Mason (1984), people in an organisation make organisational decisions based on their cognitive mould. Males and females are known for their difference in cognitive skills, abilities and processes; these differences derive from different attitudes, norms, perspectives, and beliefs (Pelled, Eisenhardt and Xin 1999). However, to what extent does the gender of the director affect the

corporate governance in a company? In the light of corporate governance, this gender *attitude* issue can be reviewed from the perspectives of two theories, RDT and agency theory. Adams and Ferreira (2009) offer empirical evidence that female directors are more committed to attending board meetings, compared to male directors. Consequently, a higher proportion of female directors on the board could become a positive, contagious factor, which could reduce the likelihood of male directors having an attendance problem.

Attending board meetings is not to be seen as a petty issue; furthermore from the view of corporate governance, this is the primary medium for the company to disseminate important information and for directors to execute their duties (*ibid*, p. 295; Jiraporn et al. 2009). In relation to this, Adams and Ferreira (2009) also conclude that female directors are detailed and meticulous in their monitoring activities, such that they are always appointed to sit on monitoring committees e.g. corporate governance, audit and nominating committees. There are various scopes of commitment enshrined in these committees, which are to be executed by their members, and it is assumed that those who have been placed on these monitoring committees are able to influence the setting of objectives and the company's monitoring activities quite intensively. By adhering to societal pressure, as suggested by institutional theory, more women may be placed on these committees.

Concomitant with the benefits put forward by agency theory, RDT, in addition, postulates that gender diversity on the board of directors promotes a better understanding of the marketplace (Carter et al. 2003), whereby it also can be implied as a good signal for workforce diversity (Rose 2007). By dealing effectively with diversity in the labour and product market, Mattis (2000) asserts that women directors can help to foster competitive advantage. In order to attract investors and penetrate markets, companies should match the diversity in the marketplace with the composition of the board of directors. Investors, on the other hand, when making their investment decisions, respond to the signals provided by the firms to understand the local market and workforce diversity. Erhardt et al. (2003) claim that gender diversity represents the practice of companies, and signals their efforts to overcome the

discrimination problem, one of the preferences attribute to foreign investors and inspiring other women employees to work harder (Mattis 1993). In summary, female directorship epitomises the equal opportunity provided in the workplace, and it is favoured by foreign investors, as it is considered to be a source of competitive advantage for firms (Kang et al. 2010).

Many studies have tried to address the relationship between female board diversity and a firm's value (e.g. Carter et al 2003; Erhardt et al. 2003; etc.), which generally offers mixed results. A critical factor in good corporate governance appears to be the relationship between board diversity and shareholder value creation (Carter et al. 2003), which postulates that good firm value and higher performance is positively associated with good governance (Bokpin and Isshaq 2009); subsequently this attracts foreign investors so that these facets are very intertwined with each other.

Apart from the benefits of having female representatives on the board as already discussed, Adams and Ferreira (2009) highlight that, even though gender diversity seems favourable to the company as a whole, the issue of 'over monitoring' has always been associated with women's leadership. They lend their opinion that excessive monitoring apparently decreases shareholder value (Almazan and Suarez 2003).

As stated beforehand, the increasing pattern of women directorship is proven in many research studies. For instance, Daily et al. (1999) offer evidence of the increasing trend for women assuming a seat on the board of the Fortune 500 firms, albeit not the CEO position. Even though Bilimoria (2000) agrees with this fact, he defies that any substantial effect has emerged from the rising rate. He shares the view with Mattis (2000), asserting that the escalating number of women directorships is not significant, as there are still gender discrimination, stereotyping and tokenism elements in existence on the boards with female director representation.

The 'number' of women on the board is a crucial factor in order to get their voice heard. Being a lone woman, or being in only a small minority on the board, is very

challenging and it is difficult to gain the attention of the other members; women in this situation are likely to be ignored and their presence among the male directors (defined by Kanter 1977 as the ‘majority’) is not welcomed. The only reason for the appointment of women directors onto boards is the pressure from related parties, such as the shareholders. Therefore, one or only a small minority of women are appointed to the board. This is called ‘tokenism’. Frequently, they are viewed as symbols rather than individuals, the symbols of “how-women-can-do, stand-ins for all women” (Kanter 1977).

However, with three or more women in the boardroom, the level of acceptance by other members on board for the women directorship seems to improve and changes to a higher stage. It is claimed that with this number they reach a ‘critical mass’ (Erkut et al. 2008; Konrad et al. 2008), which can influence board decisions significantly without barriers to their communication (Torchia, Calabro and Huse 2011). The collaboration of three or more female directors becomes a dynamic ally, which helps to break the ‘stereotypes’ that are always associated with a solo woman on the board, or the ‘conspiracy’ accusation for coupled ladies on the board.

On the other hand, there are studies which suggest that diversity can worsen a firm’s performance. For example, Hambrick, Cho and Chen (1996) claim that diverse groups were slower in their actions and responses compared to uniform teams. Their explanation for the claim is that they are likely to dispute and create more conflicts, consequently lessening the effectiveness of team consensus. This statement is further reinforced by Knight et al. (1999) in their argument that greater time and effort is allocated to achieve consensus results in decision making. Therefore, due to greater interference, a firm’s performance is negatively affected.

Maznevski (1994) offers a suggestion to overcome this problem by enhancing the integration and communication in a diverse group, which was then argued by Treicher (1995) as being impractical as high expenditures are incurred to accommodate the needs of different types of people, which may cause substantial cost to the company (Cox and Blake 1991). Treicher (1995) further adds that diversity is likely to increase

work group conflicts and break important communication processes. However, Murray (1989) refines this finding, and asserts that diversity and a company's performance are related by the type of market in which the company operates. When the type of market is intense, a homogenous group works more effectively than a heterogeneous group, whilst during rapid and dynamic changes in the market, an adverse relationship is found.

In summary, there are many empirical studies which have provided evidence to associate the benefits gained by companies with the gender diversity of the boards, for instance, in relation to a company's improved performance (e.g. Burke 2000a; Carter et al. 2003; Erhardt et al. 2003; Shrader, Blackburn and Iles 1997). Hillman et al. (2007) anticipate that the appointment of female directors to the board of directors is purposely plagued by the potential benefits attached to them. In the light of this literature, and the link between the board of directors and the benefits outlined from an MTA, the appointment of female director(s) onto the board is believed to have a positive effect on the company's overall performance (Kang et al. 2010), which is claimed by Zahra and Pearce (1989) to be one of the board's crucial functions.

Nevertheless, it could be a good idea to position Malaysia in the Asian context and consider the role of women in order to make a more accurate comparison of the impact of having women on a board to attract foreign investors. However, there is a lack of studies on gender issue in relation to board of directors that specifically focus on the Asian setting as a whole. Therefore, studies from a few specific Asian countries have been scrutinised, such as Singapore, Thailand, Indonesia, China, Sri Lanka, etc. in order to find the gender issues on boards in relation to investor preference and company performance. Generally, most of these studies highlighted the under-representation of women directors on the board. According to the survey conducted in China and India, for example, female representation on a corporate board lags behind their male counterparts, amounting to only around 5 per cent of board seats (Wellalage and Locke 2013). Therefore, the appointment of women to the corporate board is seen as a means of enhancing the ability of the board to utilise the board's

control and strategic roles, which indirectly enhances the firm's value (Kang et al. 2010).

However, there are no clear results for each country. In the study conducted by Kang et al. (2010) on Singapore listed firms, they found a positive response by investors to the appointment of women directors on the company's board. However, a study by Wellalage and Locke (2013) in the Sri Lanka setting shows the significant inverse relationship between the proportion of women on boards and firm value, concomitant with an increase in company's agency cost. Whilst in Malaysia Marimuthu and Kolandaisamy (2009) and Shukeri, Shin and Shaari (2012) found no significant relationship to be recognised. Therefore, it is argued that even though the issues of women on boards have escalated worldwide, in Asian countries, investors' responses towards the inclusion of women directors on corporate board are different depending in which country they invest in. The diverse reactions shown by investors can be explained by the variation of culture embedded in corporate culture of each country.

Thus, given the current arguments and the institutional setting in Malaysia, it puts forward equivocal evidence about the effects of the gender diversity of the board of directors on the level of FEO. It is interesting to note the statistic from the World Population Review²²; the latest data for the population of Malaysia for the year 2013 in total is 29,791,949 people. Of this number, 50.7% (15,106,780) is the male population and the remaining 49.3% (14,685,169) is the female population. This is in tandem with the 40% proportion of women in workforce labour, as revealed in the Grant Thornton International Business Report (IBR) 2013. The previous data from the World Bank showed the rate increasing relatively from 35.81% reported in the year 2010. As females continue to become a larger proportion of the workforce in comparison to males, it is assumed that corporations will experience significant changes in potential candidates wishing to sit on the hot 'chairs' as members of the board of directors.

²²<http://worldpopulationreview.com/countries/malaysia-population/>

Unfortunately, this is not the case. According to the IBR report, Malaysia has the highest number of women in the workforce compared with other Asian countries, yet it has the lowest proportion of senior roles occupied by women, at only 26%. Therefore, it cannot be compared with the developed countries or even other Asian countries. Nevertheless, female directorship or gender diversity on the board of director represents a visible effort to imitate the good practice of corporate governance in a firm. However, in terms of its practicality in corporate work, especially for firms in an emerging market (as discussed above), it is difficult to predict the relation between female directorship and FEO. Even though it is not possible to make this supposition, based on the facts, arguments and prior studies, it is contestably presented that in Malaysia women directorship implies a positive signal to attract more foreign investment. Therefore, it is hypothesised that:

Hypothesis 5: The level of foreign equity ownership in a company is positively associated with women directorship.

4.4.2.4 Directors' Educational Background

(i) Directors with Financial Expertise

Following the wave of accounting scandals around the world, for example at Enron - 2001, WorldCom - 2002, Tyco - 2002, HealthSouth - 2003, etc., the call for more financial experts on boards is highly emphasised. It is argued that "an understanding of generally accepted accounting principles and financial statements" assists in a board's overseeing functions, hence protecting the interests of the shareholders (Burak Guner, Malmendier and Tate 2008:323). From the parlance of agency theory, the appointment of financial experts to the board leads to reduced monitoring costs.

There is a special section enacted in the SOX 2002 that highlights the requirement of having at least one member that is considered to be a financial expert on the audit committee. This practice, it is claimed by Burak Guner et al. (2008), has also been applied by the major stock exchanges around the world. However, it is argued that directors with financial expertise may spend most of their time providing financial

advice rather than monitoring the company's activities (Adams and Ferreira 2007). This advisory role can be really taxing if directors are affiliated with certain financial institutions, which may create personal conflict about whether to pursue their own interests or to maximise shareholder value (Burak Guner et al. 2008).

Even though the crucial role of financial expertise is specified in the 2002 SOX, however, the definition of financial expertise is too broad, so that commercial bankers are becoming common on corporate boards (see the definition in Section 407 of 2002 SOX). Moreover, Olson (1999) justifies that managerial experience is sufficient to assure the effectiveness of the audit committee. But, the empirical results shown by Burak Guner et al. (2008) find an adverse effect on shareholder value whenever directors without a critical accounting qualification, for example commercial bankers, join the corporate board as the financial expertise. It is argued that when bankers act as the financial expertise, they make decisions to acquire loans for a company at an unnecessary time, or not in the interest of the shareholders, but for their perquisite from the affiliated institution (in this case, a banking institution). This can be explained through the actions of managers that may use the fund acquired from a loan to symbolise their power or use the money and invest it in unprofitable projects, etc., which consequently lead to empire-building and overconfident managers (Jensen and Meckling 1976).

On the other hand, in invoking RDT, there are studies that offer evidence that companies may benefit from the presence of financial expertise directors, with specific accounting background, on the board; for example, Agrawal and Chandha (2005) find that directors on audit committees with a CPA, CFA professional qualification or similar degrees reflect fewer of earning restatements, whereas Defond, Hann and Hu (2005) register a positive stock market reaction when directors with an accounting background are appointed to the audit committee board. Hillman, Cannella and Paetzold (2000) add that the skills and expertise possessed by directors assist management in making important decisions, which can thus affect a firm's value. These findings add more credence to the conjecture that directors with accounting or

financial qualifications, or a similar background, can greatly assist in overseeing a firm's financial reporting, thus reducing monitoring costs and mitigating agency costs.

In the context of this study, the objective is to measure the reaction of foreign investors when making their investment decisions, to determine whether they favour the existence of financial expertise (qualified accounting or financial background) on the corporate board, or otherwise. The presence of directors on the board with this kind of financial expertise is expected to be valued, as they can be relied upon for their expertise in understanding the accepted principles of accounting (Burak Gurner et al. 2008). A firm's financial forecasting and financial expertise are also associated with a better quality of financial reporting through the practice of accounting conservatism (Krishnan and Visvanathan 2008). Therefore, the criteria used to define the variable that represents 'director with a professional qualification' in this study is derived from this understanding (see 5.6.2 Independent Variables). In addition, the primary assertion concerning having qualified directors on the board is due to the escalation of high-profile cases in accounting scandals (Krishnan and Visvanathan 2008).

In Malaysia, the revised Code (2007) has pronounced the criteria that should be considered when appointing potential directors to the board. Among the suggested criteria are: skills, knowledge, expertise and experience, professionalism and integrity (Code 2007). These criteria are emphasised to ensure that the newly appointed directors can discharge their roles and responsibilities effectively. In addition, their professional development should be continually assessed. The amendments made to the existing Code (2000) are aimed at strengthening the corporate governance practice of the PLCs in Malaysia. This can be achieved through the selection process for company directors, by putting in place the right and sensible criteria before the final appointment is made, thus improving the quality of the board of PLCs in Malaysia (Budget 2008).

It is believed that the specific clause pertaining to the directors' terms of appointment, as drafted in the revised Code (2007) that came into existence in Malaysia, is

consistent with the practice in developed capital markets. In order to achieve a better level of corporate governance practice, generally, the quality of the board of directors is given special attention. The rise in high-profile accounting scandals and the collapse of giant companies around the world has swept away public confidence in the corporate sector. This catastrophe in the business world has been considered to be a wake-up call, not only for the countries involved, but also for their counterparts as well. The new clause pertaining to improve the directors' monitoring role and their capability to comprehend a company's financial reporting should become the main priority in combating the weakness of the existing corporate governance code. This aims to restore public confidence in the governance practice in the corporate sector.

Therefore, in Anglo-American corporate governance, the 2002 SOX Act was introduced, which mandates the requirement to disclose whether the audit committee includes a financial expert (Krishnan and Visvanathan 2008). Similarly, the requirement for directors with financial literacy has been followed by all major stock exchanges (Burak Guner et al. 2008), without exception, including Malaysia. It is argued that Malaysia has taken serious steps to improve governance practice by imitating the related section from the world's best benchmarking for application in the revised Code (2007).

Drawing on the perspective of institutional theory, the remedial action taken by the Malaysian government to imitate the institution (the tendency to adopt a similar institution, for example corporate governance code revision) of the developed markets in order to regain public confidence can be considered as an effort to seek legitimacy that can only be conferred by society at large. Heeding the previous lesson of the Asian turmoil 1997/1998, swift action was taken to remedy the severe condition of the corporate market after it had been tarnished by a series of corporate scandals. Therefore, the codes and the governance elements of firms, which are mostly from Anglo-American countries (Witt 2004), are adopted in an isomorphic way (DiMaggio and Powell 1983), since these countries are claimed as having an optimal practice of good corporate governance (Aggarwal, Erel, Stulz and Williamson 2010).

In emerging economies, where the system of corporate governance does not operate effectively, foreign investors are relying on proper mechanisms which can protect their investment. In this case, a firm's compliance with the requirement of having a director with financial expertise can be accomplished through a few levels of isomorphism. Mainly, it can be realised through *mimetic isomorphism*, as the Code imitates the requirement imposed on firms in Anglo-American countries, so that it is consequently embodied in the revised Code (2007). This has resulted in *coercive isomorphism*, as the government of Malaysia can use its superior power to pressurise the PLCs in Malaysia to abide by this best practice in the revised Code (2007). Besides this, the emphasising of 'financial expertise' directors insists on the area of critical qualifications and professional association, such as accounting and financial, being aligned with the recognised professional titles awarded by professional institutions such as CPA, CFP, ACCA, CIMA, etc. (again, see 5.6.2 Independent Variables). This kind of enforcement can be seen as *normative isomorphism*, which primarily stems from professionalism.

Therefore, this facet of professionalisation is derived from the growth and elaboration of the professional network. The established networks that encompass accountants and financial experts cause them to be bonded by similar values and attributes. Thus, their shared values can be diffused easily across the organisation. DiMaggio and Powell (1983) assert that by possessing the same background and values, people tend to view problems in a similar manner. Therefore, it is claimed that foreign investors favour the existence of directors with financial expertise as they share similar values, which can lead to similar perspectives in making decisions thus reducing monitoring costs. In addition, the revised Code (2007) also replicates the governance practice of developed markets, which is implied by foreign investors as being good governance practice. Overall, it seems that RDT, agency theory and institutional theory are in mutual agreement with each other that director with accounting and financial qualifications are highly sought by foreign investors. Therefore, it is hypothesised that:

Hypothesis 6: Directors with financial expertise are positively associated with foreign equity investment in a firm.

(ii) Directors with a Western Educational Background

In addition to the above notion of normative isomorphism, there is another aspect that can be considered as appearing under this mechanism, namely formal education received in a university. The formal education received in an established organisation, inculcates specific values in people within the same setting. The values that are instilled during their upbringing produce lasting effects within the individual. Thus, when they enter employment, they will hold these values within them, which enable them to be diffused easily into and across organisations.

Institutional theorists such as DiMaggio and Powell (1983), Meyer and Rowan (1977), and Zucker (1987) suggest that organisations are shaped by the normative pressures which embrace them. The sources of these pressures originate from other regulatory bodies or the state. Adhering to these pressures changes the organisation's structure in an isomorphic way with institutionally prescribed expectations (Slack and Hinings 1994). In this case, directors are the crucial actors that can influence an organisation's structure. The sources of their influence emanate from the system, i.e. the type of education and the corresponding values that they received in their tertiary school. The educational background of the directors is also claimed to be able to assist management in strategy evaluation (Ruigrok et al. 2006). Therefore, it is argued that directors with a Western educational background are favoured by foreign investors when making their investment decisions as they share the same values and perspectives (Ahmadjian and Robbins 2005).

Drawing on the perspective of agency theory, foreign investors may regard directors with a Western educational background as a sign of improved governance, as they have been exposed to a similar institutional background, and share similar values which emphasise the maximisation of shareholder wealth; thereby they are assumed to act in a way that is preferred by foreign investors. Thus, foreign investors can at least hinge upon the expected integrity that these directors uphold while carrying out their fiduciary duties within the company, which results in a decrease in monitoring costs.

Besides this, and consistent with the argument from RDT, the existence of directors with a Western educational background promotes heterogeneity, which therefore helps to break the deadlock in the traditional board of directors. Heterogeneity on a board leads to a positive impact on firm performance (Douma et al. 2006). Directors with a Western educational background are argued to share similar attributes with foreign directors, where they can advise on global experiences (Masulis et al. 2012) and technical skills that are beyond the outreach of directors with a local educational background. They also steer the meeting to run in a different paradigms, which removes the boundary of close proximity thinking in making company decisions; this therefore advocates a new management practice to be adopted, which is centred on the Anglo-American governance practice.

It is widely known that Malaysian companies share the typical characteristics of Asian companies. Unlike in the US and UK, ownership in East Asian companies is relatively high and concentrated (Cheung and Chan 2004), and this can lead to family-owners or controlling shareholders getting more power to rule the companies (Zhuang et al. 2000). La Porta et al. (2000) contend that this type of ownership has weakened the effectiveness of shareholder protection mechanisms. Cheung and Chang (2004) also argued that these characteristics affect investors' view and the way they assess the companies. Thus, it is argued that having the director(s) with Western educational background on corporate board helps to reduce their apprehension of being manipulated by controlling shareholders.

Therefore, it is argued that for emerging countries like Malaysia as part of Asian countries, foreign investors favour the existence of directors with a Western educational background on the corporate board, in order to preserve their interests and uphold their rights since they share similar values, e.g. maximising shareholder wealth. Thus, it is hypothesised that:

Hypothesis 7: Directors with a Western educational background are positively associated with foreign equity investment in a firm.

4.4.3 Ownership Structure

There are many types of equity ownership that can be found in a company. Among them are shareholding by corporations, banks, mutual funds, governments, and individuals. Douma et al. (2006) presuppose that the ownership structure in each firm triggers the differences which exist among them. The differences in the owners' identity, their concentration and their resources determine the company's relative power, incentives and how they monitor managers. In addition, the ultimate goal held by the firm's owner - for instance, their preference to choose either short or long term returns on investment - may also subsequently influence the performance of the firms. The subsections below discuss the three types of ownership to be tested in the hypotheses. This is done in the context of answering the third research question: *Do ownership structures influence the level of FEO?*

4.4.3.1 Family-Controlled Companies (FCCs)

Large and single-family conglomerates are ubiquitous, and have dominated in many emerging countries (Claessens et al. 2000; Johnson et al. 2000). Chang (2003) and Joh (2003) assert that this type of company plays a particularly important role in Asian countries. Most of the studies in developed markets, such as the US and Europe, have discovered that family companies have shown better performance compared to non-family companies (Anderson and Reeb 2003; Daily and Dollinger 1992; Margaritis and Psillaki 2010; Maury 2006; Villalonga and Amit 2006). In contrast, there are a few studies which reach a different conclusion; these suggest that non-family companies are better in terms of performance (Lauterbach and Vanisky 1999; Morck et al. 1988; Nowland 2008; Perez-Gonzalez 2006). Others find no relationship (e.g. Demsetz and Lehn 1985; Demstev and Villalongan 2001). Thus, mixed results are obtained.

In this study, to be identified as a family-controlled company (FCC), one of the conditions is to acquire the minimum of family ownership (direct and indirect) for at least 20% of the company's equity (see Section 5.6.2 Independent Variables). This

controlling power and higher concentration on large shareholders is expected to mitigate agency conflict between managers and outside shareholders by solving the free-rider problems of small shareholders (Suto 2003). Based on the agency theory perspective, the claim made by Suto (2003) has long been noted by Jensen and Meckling (1976) and Fama and Jensen (1983). This is consistent with the previous argument made by Berle and Means (1932) that US corporations with dispersed ownership among small shareholders tend to underperform in terms of company performance. Therefore, they contend that, through the advantage gained by the controlling power that the large shareholders have, this enables them to discipline management (Suto 2003).

The above claim is supported by Grossman and Hart (1988); this kind of concentrated ownership is effective in solving managerial agency problems and is efficient in undertaking costly monitoring or control which benefits other shareholders as well (Gillan and Starks 2000). Put simply by Peng and Jiang (2010:255), “*one does not steal his own money*”. The increased return from efficient monitoring may outweigh the monitoring costs involved with the large shareholders (Gillan and Starks 2000). Therefore, it is argued that the concentrated owner, such as the family owner, has substantial economic incentives to diminish agency conflicts and maximise the firm’s value.

A family-owned or controlled business has its unique characteristics. It has a reputation to be preserved and the survival of the business is the main concern. Therefore, this helps to mitigate the agency cost of outside equity and outside debt (Anderson, Mansi and Reeb 2003; Demsetz and Lehn 1985). The uniqueness of family firms is also underpinned by the family ties that bind them together (Litz 1995), where the family spirit is inculcated from childhood, thus becoming the internal monitoring mechanism which controls the family business (Fama and Jensen 1983). Therefore, FCCs are much governed by family traits (Mishra, Randoy and Jenssen 2001), and provide competitive advantage to the firm (Burkart, Panunzi and Shleifer 2003). In fact, Maury (2006) claims that FCCs in Western Europe seem to benefit minority shareholders rather than harm them. Likewise, less developed

countries, which are associated with weak investor protection, also claim to obtain benefits from equity concentration in relation to the company's performance; whereby these shareholders may act as a substitute for the weak legal protection in that country (La Porta, Lopez-de-Silanes, Shleifer and Vishny 2002; Peng and Jiang 2010; Shleifer and Vishny 1986; Suto 2003).

However, this claim is disputed by Bebchuk et al. (2000) and Claessens et al. (2000), who argue that concentrated ownership creates new agency problems. The agency problem in FCCs may occur between the minority shareholders and the family owners (principal-principal conflicts) (Villalonga and Amit 2006), instead of principal and agent conflicts. According to Claessens et al. (2000), the controlling shareholders may ignore the minority shareholders' interests due to the difference in their ultimate objectives, and may mislead managers into making non-value-maximising investment decisions (Ferris et al. 2003; Kim et al. 2007) and into misallocating corporate resources in unproductive business units (Rajan, Servaes and Zingales 2000).

Whilst there are two sides of agency theory to be grasped, according to RDT, in relation to FCCs, there are benefits to having controlling shareholders participate in a firm's decision making. The controlling shareholders may become the critical resources for the survival of the firm especially during a financial crisis – whereby their decisions and wealth effects are unified to provide benefits for the whole company (Holderness 2003). Minority shareholders, who also benefit from the role that large shareholders play in managing a crisis and preserving a firm's value during difficult times, are aware of the important critical resources that large shareholders can provide to the company (Peng and Jiang 2010).

Referring back to the work by Berle and Means (1932), they advanced the proposition that as firms grow larger, *inevitably*, family concentrated ownership will be replaced by dispersed ownership which separates between ownership and control. This suggests that family control may not encourage creation of value to large firms. As Fama and Jensen (1983) argue, if firms fail to comply with this time adjustment pressure, their competitive advantage will be jeopardised (Morck, Wolfenzon and

Yeung 2005). However, Peng and Jiang (2010) assert that the impact of family control on a firm's value differs across countries; this hinges upon the level of investor protection enshrined in the legal and regulatory institutions of a particular country.

The modern corporations of the US and the UK started with concentrated family ownership (Chandler 1990) and their ownership become dispersed over time (Berle and Means 1932). However, the evolution of ownership is not uniform in other parts of the world, since certain elements of their structure do not change swiftly or as much as others, thus showing resistance to institutional pressures (Slack and Hinings 1994). The main explanation for this is the existence of the country's institutional regulations concerning investor protection (La Porta, Lopez-de-Silanes and Shleifer 2008; Peng and Jiang 2010; Young et al. 2008). In the US and the UK particularly, the interests of shareholders and the rights of minority shareholders are highly important, which encourages family companies to dilute their ownership and delegate their power to the professional managers in order to attract minority shareholders, and over time they become part of the minority shareholders as well (Peng and Jeng 2010).

The above notion might be true for countries that have strong institutional governance regulation. The founding families may submit their responsibilities for managing the corporation to trusted managers, as they are comfortable with the existing regulations that rule the corporate environment. However, with respect to their counterparts elsewhere, especially in Asian countries where investor protection is weak, family firms have no choice and must run their business directly (Peng and Jiang 2010). Appointing outside managers summons scepticism as they may invite "abuse and theft" or "rampant agency problems" in the company (*ibid* p.256) Consequently, prospective minority shareholders such as foreign investors may be less enthusiastic about investing as they are afraid of the fragile investor protection and the expropriation by controlling shareholders, which is apparently associated with countries that are weak in governance institutions and regulations. These situations are making concentrated ownership more visible and prevalent in these countries (La Porta et al. 2000; Young et al. 2008).

Empirical evidence was put forward by Tsamenyi et al. (2007) and Kim et al. (2010), to suggest that foreign investors disfavoured firms with concentrated ownership, especially during the period of financial crisis. This is underpinned by the evidence offered by Mitton (2002) and Baek et al. (2004), who claimed that during the crisis, Asian firms with significant controlling ownership experienced a sharper drop in their share price. Johnson et al. (2000) claimed that, during the Asian crisis, many family companies suffered huge losses, thus expropriations of minority shareholders were severe in order to 'make up' their losses. Peng and Jiang (2010) contend that the greater the control of family companies, the greater the opportunities are for them to expropriate minority shareholders, hence reducing a firm's value.

Hence, based on these theoretical arguments, even though there is evidence that FCCs perform better than non-family-controlled companies, from the institutional theory view, the findings may be contingent upon the distinct institutional framework that pervades particular countries like the US and the UK. In Asian countries like Malaysia, there are many cases which evidence that the expropriation of minority shareholders is severe, especially after the AFC 1997/1998. Thus, the findings cannot be generalised. In addition, the agency theory perspective is prone to associating FCC with high agency cost organisations, even though RDT advocates that controlling shareholders are likely to increase a firm's value. Nonetheless, considering the inverse relationship between agency costs and corporate governance, FCC is associated with being a weak corporate governance proxy in the model. Since foreign investors assign higher monitoring costs compared to domestic investors, they closely monitor corporate governance's internal mechanisms and place more weight on those variables (Dahlquist et al. 2003). Therefore, it is argued that foreign investors, when making investment decisions concerning FCCs that are domiciled in countries with weak institutional and governance regulation, such as Malaysia, perceive them negatively. Thus it is hypothesised that:

Hypothesis 8: FEO is negatively associated with a family-controlled company (FCC).

4.4.3.2 Managerial Ownership

In the light of the agency theory perspective, the separation of ownership and control leads to agency conflict between the owners and the managers of a firm (Jensen and Meckling 1976; Shleifer and Vishny 1986). It is claimed that a manager may manipulate his position to pursue his own interests at the expense of the shareholders. Hence, according to Jensen and Meckling (1976), the best mechanism to solve the agency problem between these two parties is ownership by corporate managers. Managerial-share ownership is thought to lessen the potentially hazardous actions taken by managers (such as engaging in inferior projects, seeking other perquisites, shirking, etc.) that might expropriate shareholder wealth. Therefore, this helps in aligning the principal and managerial interests.

Jensen and Meckling (1976) argue that, concomitant with an increase in managerial ownership, a firm's performance increases, since managers with vested interests are more responsible for maximising a firm's value, rather than shrinking it. On the other hand, zero or low ownership by managers, triggers them to find alternative perquisites outside the firm, for instance, multiple-directorships, which can satisfy their ambition for establishing their reputation or self-fulfilment (Jiraporn et al. 2009^b). Then, they become too busy to reap their private benefits, and neglect their managerial responsibility in the company which is detrimental to the shareholders. Therefore, managerial ownership is considered to be the best mechanism for aligning the divergence of interests between managers and shareholders.

Furthermore, managerial ownership appears to become an inducement for the managers to work more diligently in order to increase the value of the company, and this yields high returns to shareholders, as well as themselves (Coles, Daniel and Naveen 2006). Consistent with the above view, Jiraporn et al. (2009) postulate that the larger the equity ownership held by the director, the better their meeting attendance and the more likely they are to serve on more board committees (Jiraporn et al. 2009^b). This argument favours the finding of Suto (2003) who claims that it can help to mitigate conflict between the owners and the manager and can solve the

information asymmetry problem as well (Jensen and Meckling 1976). It is argued that owner-managers who are involved in the daily operations of the firms are better able to comprehend the firm, thus there will be less of an information asymmetry problem and fewer managerial conflicts, which in turn reduces the need for monitoring and mitigates the agency cost.

In contrast, Fama and Jensen (1983) consider that insider shareholders (managerial-ownership) may be associated with '*adverse entrenchment*' effects. The effect of raising the insider equity can lead to higher '*managerial opportunism*', at the expense of outside shareholders. External shareholders, then, may face difficulties in controlling the manager's action (Morck et al. 1988). High equity possession by managers may become an enticement for them to pursue their own goals, and not the interests of outside shareholders, hence reducing the firm's value (adverse entrenchment effect) (Demsetz 1983). Therefore, the linear relationship between a firm's performance and ownership, which is evidenced by Demsetz and Lehn (1985), is denied by later findings from Morck et al. (1988). Morck et al. (1988) find a non-linear relationship between a firm's performance and managerial ownership, which suggests that, at a certain level of ownership²³, managers may gravitate towards taking actions which benefit them and might reduce the firm's value. Furthermore, they have sufficient control to make them invulnerable to the penalising threats and disciplining actions of other shareholders (Short and Keasey 1999). This significant *positive-negative-positive* relationship result of Morck et al. (1988), however, is argued by Short and Keasey (1999) as only existing for performance which is measured by Tobin's Q and not for accounting profit.

Despite all these arguments, it is debatable as to whether the findings concerning the impact of managerial ownership in Western countries can be generalised to other parts

²³The results suggest that when the managerial ownership is between 0% to 5% and beyond 25%, there is a positive relationship in relation to a firm's performance (measured by Tobin's Q) – (*convergence of interest effects*), however when the ownership is in the range of 5% to 25%, a negative relationship is documented - (*entrenchment effect*).

of the world, especially to countries with different institutional settings and corporate governance systems. Indeed, companies in the US and the UK are often depicted as having widely dispersed ownership (Short and Keasey 1999). Apparently, in Malaysia, their ownership structure is different. As one of the emerging countries, it is widely known that its capital markets are concentrated in the ownership structure.

According to Chang (2003), the main agency problem in Asian firms lies in the fact that little control is in the hands of majority shareholders, in contrast with the little ownership but powerful control by owner-managers. Owner-manager companies are prevalent among PLCs in Malaysia (Mat Nor and Sulong 2007), especially in family companies (Haniffa and Hudaib 2006). Family businesses would normally choose their family members to manage the company, especially for the top management position, and at the same time use their influence to recruit employees and other business relationships (Che Ahmad 2002).

There are streams of agency theory that claim the ineffectiveness of this practice, which may be detrimental to the firm. Agency theorists argue that when family members are appointed as managers, with the ownership they hold, they may gravitate towards adopting investment policies that benefit their family members, instead of outside shareholders. In addition, if the managers are unqualified and incompetent, they may deviate from the objective of maximising shareholder wealth (Peng and Jiang 2010).

There is also some literature that draws on RDT, questioning whether family ties are an appropriate resource for achieving a competitive edge. This is associated with ‘altruism’²⁴, which is commonly found in family firms. The relationships between principals (family owners) and agents (family managers) are likely to be based on emotion and family sentiments. Thus, any inappropriate actions taken by family managers may be concealed and silenced by other family members in order to

²⁴Altruism – selfless or unselfish; concerned more with the well-being of others than with one's own.

preserve their relationship (Peng and Jiang 2010). This may reduce a firm's value (Schulze, Lubatkin and Dino 2003). Instead, it can also happen in an inverse way leading to family *squabbles*, which are the opposite of altruism. In both ways, it may affect a firm's value. For the latter conflicts, additional costs might be incurred such as generation envy, sibling rivalry, irrational strategic decisions and non-merit compensation (Gomez-Mejia, Nunez-Nickel and Gutierrez 2001).

As argued beforehand, the structure of Malaysian firms is unique in terms of the agency relationship, where the exploitation of the minor shareholders arises from the action of the controlling shareholders, and not the managers (Baek et al. 2004; Young et al. 2008). The controlling shareholders are argued to have a strong position to maximise their own goals at the expense of other shareholders (Shleifer and Vishny 1997). Therefore, the conflict is focused between the minority and controlling shareholders, the so called principal-principal model (Young et al. 2008). This is believed to stem from the weakness in corporate governance practice in emerging economies (Claessens et al. 2000).

Even though there are many studies which claim that managerial ownership reduces the conflicts (Fama and Jensen 1983^b) of principal-agent, lower asymmetry information problem, lessens the monitoring cost, and hence mitigates the agency cost (see Mustapha and Ahmad 2011). However, in the current study setting, i.e. Malaysia, it is argued that foreign investors perceive managerial ownership as a proxy of a weak corporate governance mechanism in a firm. Family ownership has a bearing on managerial ownership in Malaysia, which is postulated in the previous argument as one of the mechanisms that is shunned by foreign investors. Foreign investors perceive family-controlled companies in Malaysia negatively due to the weak institutional and governance regulations protecting investors. Therefore, it is argued that managerial-ownership is also perceived by foreign investors as a proxy of a weak corporate governance mechanism. Thus, it is hypothesised that:

Hypothesis 9: The level of foreign equity ownership is negatively associated with managerial ownership.

4.4.3.3 Institutional Ownership

The role of institutional investors has become increasingly important in the developed capital market. Investment companies, insurance companies, bank trust departments, foundation and pension funds are among the institutions that are active in the equity market, and their participation in equity ownership has increased dramatically concomitant with the growth in pension assets (Gillan and Starks 2000). It is widely claimed, with the growth of institutional ownership that their role and capacity as shareholders has also evolved.

Studies have put forward evidence of a significant relationship between institutional shareholding and the corporate governance structures of companies (see Chung and Zhuang 2011). A survey conducted by McKinsey and Company (2002) in 31 countries regarding more than 200 institutional investors shows that institutional investors place greater emphasis on a company's governance quality when they are making investment decisions, at a par with other crucial financial indicators. With the passage of time, institutions have become more active in influencing the governance structure of the corporations within which they have their shareholdings (Gillan and Starks 2000). Among the corporate governance attributes which are preferred by institutional investors is a greater level of information disclosure. This is very helpful and cost effective to investors as they can reduce their monitoring costs, because less outside monitoring is required (Chung and Zhang 2011).

Nevertheless, it is argued that these institutions can simply sell their shares in underperforming companies, rather than involve themselves with the companies' problems. However, depending on the proportion of equity they hold, the threat of *exit* is sometimes not a good option as they may suffer greater losses. Institutional shareholder activism²⁵ is one of the expedient ways to administer their equity possession in the company. In the USA, institutional shareholder activism arose

²⁵For the detailed history of the emergence of institutional shareholder activism, see Monks and Minow (1995).

around the early 1990s by submitting proxy proposals, and the target was a firm that was not achieving the expected performance. The proposals usually pertained to the corporate governance practice in the firm. With the passage of time, the approach has evolved, and the substantial cost incurred to initiate a coalition among the shareholders has reduced as they no longer hinge upon proxy proposals, but direct communication with the management.

It is contended that the initiative of arousing the institutional shareholder activism was due to the goal incongruence between managers and shareholders. Moreover, they have strong fiduciary duties towards their individual shareholders (Chung and Zhuang 2011). Therefore, they should avoid investing in firms with weak governance practices as they are likely to be manipulated by large shareholders or management; they may even fail to obtain a good return, or, in the worst case, preserve their capital. It is asserted that institutional investors have a stronger encouragement to monitor management, rather than the individual shareholder, because they own larger stakes in those companies. Thus, the impact of any undesirable case occurring in the company may be even greater to them. In the UK, for example, despite criticisms that there is a lack of public intervention in issues of corporate governance, in reality, the level of intervention by UK institutions is higher than that publicly reported (Short and Keasey 1999).

Even though there are many corporate governance mechanisms able to tackle this issue, both internal and external, and in developed capital markets, institutional shareholder activism is claimed to be one of the most effective mechanisms (Gillan and Starks 2000). However, there are oppositions to this view. It has been argued that the role of the fund manager should not deviate from its primary function, which is to manage money for beneficiaries. They should not interfere in management decision-making, as they are claimed to have a lack of expertise for giving advice (*ibid* p.280).

However, for this case, the main point to be highlighted is that firms which are favoured by institutional investors are also of the same interest to foreign investors. Thus, the initial conjecture is that firms with high institutional shareholdings will

show the same pattern for foreign investors. This is evidenced by the study of Dahlquist and Robertson (2003) which claims that foreign and institutional ownership can be depicted by similar attributes. This result adds credence to the conjecture that there is a positive relation between institutional ownership and foreign ownership in a firm, which may be driven by the corporate governance practice of a firm. This argument is based on the results of a few studies that analyse the relationship between corporate governance practice and institutional investors' reaction, which mirror Dahlquist and Robertson (2003) their study of foreign investment in Sweden. Among the attributes are that institutional investors favour firms that are well-governed, larger, more liquid, and have had relatively low returns during the previous year (Chung and Zhang 2011; Falkenstein 1996; Gompers and Metrick 1999).

On the other hand, in Malaysia, institutional shareholder activism is not something common, albeit that the backdrop of institutional participation in the equity market is still in its infancy stage and emerged from contrasting roots. In 1996, before the AFC 1997/1998, institutional shareholdings in the PLCs in Malaysia accounted for 47.8%, which was as high as the developed market (Suto 2003). The holding of foreigners was 19.2% and the remaining balance, 43%, was the holdings of non-Malay citizens²⁶. From the perspective of agency theory, when it is applied to developed economies, the large shareholders, including institutional investors, might help in solving the free-rider problems of small shareholders (Pound 1988; Shleifer and Vishny 1986). It is contended that large external equity holders help to mitigate the agency problems by using their strong influence to monitor and discipline management (Shleifer and Vishny 1986). However, in contrast, Villalongan and Amit (2006) claim that large institutional shareholders may not have incentive to monitor management, and they may even coerce with management (Claessens, Djankov, Fan and Lang 2002).

Nevertheless, this kind of statement does not really fit with the capital market environment in Malaysia, where most of the major institutional investors, including

²⁶These figures are taken from various issues of *Investing in the Stock Market in Malaysia*, Kuala Lumpur Stock Exchange and published by Suto (2003).

government agencies and social securities funds, such as the Employees Provident Fund (EPF) and national unit trusts, are state-backed institutions. These institutions have been used by the government to hold equity issues arising from the privatisation of government enterprises and to support equity financing growth sectors since 1980 (Suto 2003). Institutional investors in Malaysia are less likely to monitor the firms they invest in, and this hinges upon the government intervention to manage funds. Therefore, it is suggested by Suto (2003) that the issue of information asymmetry problems must be more serious for firms held by institutional investors with the emergence of the free-rider problem, and also, it does not help to mitigate the agency cost. Despite the fact that a few regulations have arisen to regulate funds in Malaysia since the 1990s, these institutional investors are still enmeshed with government policies, which makes them difficult to separate out when any issues related to institutional investors are highlighted.

Malaysia is a multiracial country. In this country, there are three ethnic structures of ownership: the Malays, non-Malays (Chinese, Indian and other citizens) and foreigners. The Malays are the indigenous people, known as Bumiputra (sons of the soil). According to the *Social Contract*²⁷ made by the country's founding fathers in the Constitution, Malays were granted special rights and privileges, whilst in return, the non-Bumiputra was granted citizenship. Since 1971, in its Second Year Five-year Plan, the government of Malaysia has been very consistent in its objective of eradicating poverty and reducing the income disparity between ethnics, in order to establish the basis of savings for economic growth.

Bumiputra are given various preferential treatment schemes to encourage them to participate in financial transactions. This is attested by the fact that income distribution was still uneven and Bumiputra were found to be in the lower

²⁷The Social Contract in Malaysia is an initiative of the country's founding fathers in the Constitution in an attempt to nourish a spirit of cooperation between multiracial people to gain independence. Articles 14-18 and Article 153 of the Constitution, pertaining to the granting of citizenship to the non-Bumiputra and special rights and privileges to the Malays can be referenced for further details.

occupational categories (Tam and Tan 2007). The New Economic Policy (NEP) 1971, for example, has stated the aim to achieve 30 per cent of Bumiputra ownership and management in the corporate sector by 1990²⁸. Securities investment through collective investments schemes, such as EPF and national unit trusts, are among the platforms to increase the shareholding of Malays²⁹.

The explanation behind this is that the policy pertaining to conserve Bumiputra privileges in institutional investment schemes is thought not to contribute to reducing the agency costs of a company. The increasing ownership by Malays has had no significant effect on the choice of corporate financing; as predicted, Malay shareholders have not played a significant role in disciplining the corporate management of the firms that they invest in. Therefore, the initial conjecture established in the earlier discussion is no longer valid in the context of Malaysia, with its different institutional background. In active and liquid capital markets, shareholder activism, such as the threat of *exit* and through *voice* mechanisms, can be achieved through coercive isomorphism (Noteboom 1999), but this has not held true in the Malaysian capital market. It is argued that, in Malaysia, shareholder activism is still in its infancy phase and promoting shareholder value is an undertaking in progress.

It is suggested that a policy which promotes the social dispersion of ownership coupled with an effort to enhance the awareness or consciousness of Malays as shareholders should be intensified (Suto 2003). Besides this, fund management efficiency should be improved at the institutional level, and then the agency cost can be reduced. If not, the predicted relationship between FEO and institutional shareholding should be negatively related or neutral. In addition, the empirical results of monitoring by institutional investors are mixed. Smith (1996) and Strickland, Wiles

²⁸Bumiputra ownership increased significantly - by 18.8% - in 20 years (from 1.5 per cent in 1970 to 20.3 per cent in 1990), however the initial target of 30 per cent was not achieved (Tam and Tan 2007).

²⁹ 30 per cent Bumiputra ownership, 20 per cent foreign ownership was set as the policy target.

and Zinner (1996) offer evidence of positive effects on corporate value, whilst in contrast Karpoff (1996), Wahal (1996), and Faccio and Lasfer (2000) question the monitoring ability of institutional investors.

Taking into consideration all the points offered and the contrasting institutional background in Malaysia, it is thus hypothesised that:

Hypothesis 10: The level of foreign equity ownership is negatively associated with institutional shareholding.

4.5 Summary

In this chapter, a set of research hypotheses relating to the corporate governance attributes associated with foreign investment behaviour are formulated. This process commenced with a discussion of the rationale for generating hypotheses from a multi-theoretical approach. Understanding the board roles and the ownership pattern in Malaysia requires a multi-theoretical approach that espouses agency theory, institutional theory and resource dependence theory. The use of a multi-theoretical approach has escalated recently in order to comprehend the issue of corporate governance (see Douma et al. 2006; Lynall et al. 2003; Ruigrok et al. 2006).

In an attempt to justify the corporate governance determinants that affect foreign investors' investment decisions in Malaysia, a set of testable hypotheses was developed. More specifically, for Malaysia, the arguments for hypotheses' development hinge upon the reality of institutional change, the unique ownership pattern and the insight from resource dependence theory. Thus, it is hoped that by considering all these elements in Malaysia's corporate environment it will be possible to answer the research questions (see Section 1.5 Research Question), which were again restated in this chapter. Overall, to answer the main research question, it is hypothesised that the level of FEO in Malaysian companies is associated with its corporate governance structure. Hence, the following chapter, Chapter 5, presents the process of data collection and the statistical methods used to test the hypotheses. The

results are presented in Chapter 6 and Chapter 7. Finally, a full length discussion of the results follows in Chapter 8.

CHAPTER 5

DATA AND METHODOLOGY

5.1 Introduction

The previous chapter developed the hypotheses to be tested. In continuance, this chapter is structured to illustrate the process of data collection and presents the procedures for using the statistical method to test these hypotheses. Data was collected from various sources and a number of methods were employed to analyse the data.

The chapter is organised as follows: Section 5.2 provides an explanation of the philosophical approach in acquiring data and conducting the study. Section 5.3 elaborates on the types of data, followed by the selection of the sample. The process of data collection is outlined in Section 5.4. The instruments used in this study are then explained in Section 5.5. The next section provides a description of the measurement employed for the dependent, independent and control variables. Statistical analysis is discussed in Section 5.7. Finally, Section 5.8 summarises and concludes the whole chapter, and indicates some problems and limitations encountered during the data collection process.

5.2 The Philosophical Approach to the Study

The philosophy behind the research work can influence how the researcher sees the things they want to see. Epistemology and ontology are the appropriate branches of philosophy. Epistemology studies knowledge and justified belief. Researcher may justify their belief in the way they see things using their own justification, while it might be different from another person's vantage point; "where you stand can influence what you see" (Fischer 1998:128). As a result, the epistemological stance

influences the design and methods used for data collection. Ontology is the philosophical study of the nature of being, becoming, existence, or reality, which are the very basic categories and relate to the very essence of the issue being investigated (Burrell and Morgan 1979).

There are also two dominant views or paradigms concerning the nature of knowledge: positivist and interpretivist. This study can be claimed to be a positivist study. In epistemological studies, the concern is for the ground of knowledge, where the researcher begins to understand 'reality' and conveys this understanding to be grasped by others as knowledge. The 'reality' which is to be investigated is questioned in ontological terms as to whether it is external to the researcher or whether it is a product of individual consciousness (Burrell and Morgan 1979). For positivists, their epistemological assumption is that external reality may only be observed, not in other ways, for the knowledge to be considered as significant (Easterby-Smith, Thorpe and Lowe 2002). Consistent with this, Yin (2003) argues that positivists of the ontological paradigm assume that reality is external and should be measured through objective methods. Thus, the interpretivist approach is undermined when the objective method is preferred, whereas the subjective approach is inclined to inferences based on human emotions, sensations, reflections or intuition (Hussey and Hussey 1997). There are a few criteria which have been used in this study which reflect ontology and epistemology in the positivist paradigm.

Based on ontological positivism, reality and truth exist out there, and are waiting to be discovered (Yin 2003). Meaning itself exists in the world and knowledge will reflect reality. Thus, accurate knowledge precisely reflects the world as it is. Based on what is argued by Yin (2003), this study has tried to find the knowledge that exists in the business world, particularly foreign investor behaviour. In the context of this thesis, from the view of the ontological approach, the primary source of information is mainly based on objective information. This applies when the analysis of foreign ownership to Malaysian public listed companies is based on factual data obtained from companies' annual reports and the Datastream database.

The differences between positivist and interpretivist work can be seen by way of the following comparison. Positivist work seeks to identify research data with propositions that can be tested or identified in other cases, while interpretivist work seeks to combine these data into a system of belief whose manifestations are specific to a case (Lin 1998). It is stated in this study that the findings will be helpful in linking other companies, or generally other developing countries, to understand the behaviour of foreign investors by imparting knowledge about them. Generalisations can be made to another case in a similar setting. Hence, a key evaluation criterion pertains to the reliability of findings, in the sense that different researchers, or the same researchers on different occasions, would “discover the same phenomena or generate the same constructs in the same or similar setting” (LeCompte and Goetz 1982).

In addition, Lin (1998) also argues that discovering causal relationships is the province of positivist research. Under epistemology based research, positivists claim that knowledge can be predicted and explained by observing the regularities of action and causal relationships between elements in the population (Burrell and Morgan 1979). This statement is in agreement with Neuman (1997) who posits that positivist research discovers causal laws that can be used to predict general patterns of human activity, hence embracing the reductionist approach (Remenyi, Williams and Swartz 1998). Therefore, the need for the formulation of hypotheses is emphasised in conducting empirical testing to search for persuasive explanations for the causal relationships (Easterby-Smith et al. 2002). Indeed, this is what has been done in this study; the findings of this study will explain the role of corporate governance as a conduit between foreign investors and their investment in companies based on the observation of regularities and causal relationship occurring between them. Then, empirical findings can be generalised to the wider population.

Besides, in positivist management research, there is an underlying implicit commitment, whereby according to the theory of truth, the distance between the researcher and the researched should be preserved. The aim is to ensure that the research process and findings are not contaminated by the actions of the researcher

(Johnson, Buehring, Cassell and Symon 2006). In contrast with the view of interpretivists, Burrell and Morgan (1979) claim that those who are anti-positivists contend that knowledge can only be understood by obtaining information directly from the individuals who are involved with the particular issues that are being investigated. However, from this study's perspective, it could be argued that conducting interviews with the respondents would indirectly eliminate the gaps or the distances between the researcher and the respondents. If the researchers interfere in natural phenomena, it would lead to unreliable findings as there is potential bias and 'contamination' in the data collection process. Objective data collection is emphasised in management research so as to test hypotheses by having built in 'extensive means for protecting against personal biases' (Behling 1980).

There are long debates and arguments conducted by scholars who advocate their own paradigms, whether positivist or interpretivist. Notwithstanding the arguments, in reality the points that matter are the impact of the study and the generalisability of the findings. Easterby-Smith et al. (2002) have argued that even though there is a clear distinction between positivist and interpretivist paradigms, when the actual research is performed, the incompatibility is blurred. Nevertheless, the arguments made above favour the use of the positivist approach in this study. In the initial stage of data collection planning, the interview method was proposed to be used as part of the data collection. However, this idea was discarded in the panel meeting as there was a concern that the data from interviews would be biased (see Section 5.3.1 Secondary Data for justifications). Besides, the difficulty of obtaining data through interviews is also one of the key factors which eliminate the use of the interpretive approach as an option.

Thus, the data collection methods, the variables and the statistical methods that are used in a spirit of positivism in this study are discussed in the following subsections.

5.3 Data

The data type, data choice, and the issues associated with the data selection are addressed in detail in the subsections below. To coincide with the ultimate objective of this study, secondary data has been chosen to strengthen the findings and also for the purpose of data robustness.

5.3.1 Secondary Data

Secondary data is extensively used in this study. The data from secondary sources is equally as important as the premier sources as highlighted by Cooper, Schindler and Sun (2003); secondary sources are initially derived from the interpretations of primary data. The secondary data is derived from observations and the interviews process, and then is transformed into text by emphasising the inherent credibility of the documentary data. Quantitative and qualitative data can both be utilised in descriptive and explanatory research (Kervin 1999). The main approach taken to collect data is that of using documentation, consisting of multiple published sources from established institutions. Reports from international institutions (World Bank reports, Asian Development Bank report, International Monetary Fund (IMF) reports, etc.), national institutions reports (such as the Central Bank of Malaysia reports, Malaysian Budget reports, Malaysian Institute on Corporate Governance (MICG) reports, etc.) and companies' annual reports were used extensively at the companies' level. These reports were scrutinised in order to provide meaningful explanations for arguments, justifications, analysis and to support the findings.

Companies' annual reports represent meaningful sources to extract the practice of corporate governance adopted by companies. The data are considered to be more consequential than verbal utterance particularly where it is not easy to approach the board of directors in the company. It is argued that administrative records can offer more reliable information than interviews, especially on a particular topic such as corporate governance practice, directors' profile, directors' education, family relationship etc. Indeed, significant numbers of previous studies on corporate

governance have used data sourced from published sources such as companies' annual reports.

Companies' annual reports were gathered by downloading them from Bursa Malaysia's website, while the financial data for the companies were accessed from Datastream and Thompson Advance Databases. Companies' individual websites were also explored to obtain more information about the companies, especially their backgrounds, including incorporation history. Academic books, and articles in the professional magazines and newspapers, were also extensively used in gaining an insight into corporate governance and foreign investment around the world, in Asian countries and in Malaysia.

There are many advantages in using secondary data for research analysis: it can provide savings in money and time (Ghauri and Gronhaugh 2002); it can result in a higher quality of data than when collecting one's own (Stewart and Kamins 1993); and it gives results in a permanent form which are available to be checked at any point of time by others (Denscombe 2010), either for verification, further research or other purposes. These characteristics of secondary data enhance its credibility. As insisted by Mason (2002), the credibility of documentary evidence is hard to be denied.

Originally, primary data was also planned to be used to complement secondary data. This would have been obtained by conducting a few interviews with key people who witnessed the changes in Malaysia's economic and corporate governance landscape following the Asian Financial Crisis (AFC) 1997/1998. However, this initial plan was discarded. The accuracy of the information provided by the potential interviewees could be questioned and would be difficult to verify. There are four reasons highlighted for this: i) the probability of not having the right 'key' person. The key person is a subjective matter, and it requires further effort to identify those people who are in the right position to justify the changes of corporate governance in relation to the AFC 1997/98; ii) if it is possible to find the key person, the judgement they make could be biased, as they now might be in a different position. Their 'past' and 'current' positions can influence how they portray their views in this issue; iii) the

duration of time since the AFC 1997/1998 should also be considered because the memories of it may have; the vital part is iv) the use of secondary sources alone is consistent and fulfills the ultimate objectives of this study.

In summary, the initial plan to conduct interviews was been discarded as the accuracy of the information provided by these interviewees could be questioned. An imbalanced view may be created and would not represent the whole story of corporate governance in Malaysia before the crisis. The reliability problems associated with the primary data should then be avoided. The most important thing is to use the right sources and types of data to achieve the objectives outlined in this study. Thus, the study only employs secondary data.

5.4 Population and Sample

5.4.1 Population

The main research interest is to investigate the reaction of foreign investors to the practices of corporate governance in Malaysian companies. Thus, the companies listed on Bursa Malaysia were identified as the subject of interest. Public listed companies (PLCs) are chosen for a variety of advantages over non-listed companies. For example, the annual reports of PLCs are publicly available and they can be assessed from the Bursa Malaysia's website³⁰.

In addition, the stringent requirements imposed by Bursa Malaysia and the Companies Act 1965 are to be followed in publishing the annual report, making the reports highly reliable. They are also presented in a uniform way. Besides, the data from PLCs is also available in Thomson Datastream and Thomson ONE Banker databases. These reliable sources complement the annual reports. However, the required data, which were not made available in any of the above mentioned sources (such as the list of foreign equity ownership in Malaysian companies and the details of listed companies

³⁰<http://www.bursamalaysia.com/market/listed-companies/>

each year), were purchased from Bursa Malaysia. Notably, the use of information from PLCs enables a comparison to be made with studies in Malaysia and overseas as the data is reliable and uniformity is almost guaranteed.

As at December 1996, according to the data provided by Bursa Malaysia, a total of 629 companies were reported as listed on this date. Out of these, 413 companies were listed on the Main Board and 216 companies on the Second Board³¹. Advice sought from the Bursa Malaysia pointed to the use of data for PLCs from the year 1997 as this is when records of PLCs started to be properly kept and made up to date by Bursa Malaysia. Thus, the list of companies for the year 1997 was matched with the list of companies for the year 1996. This was done to avoid the possibility of leaving out eligible companies. Companies appearing on the 1997 list but not in the year 1996 needed further checking on their listing status from a few other sources such as companies' websites, annual reports etc. This made the population 644 companies instead of 629 companies. Out of this number, only 413 companies remain listed on Bursa Malaysia by the year 2011. Thus, the total number of public listed companies in the sample is 413 companies.

Upon the completion of population identification, the next process is to refine the population and finalise the sample of the study. This has been done by sorting out the

³¹Prior to 3 August 2009, Bursa Malaysia offered three (3) boards for companies to be listed, Main Board, Second Board and MESDAQ Market. The listing requirements (such as minimum issued and paid up capital, etc.) were different for each board and generally Main Board was for the established companies and had tougher conditions to be fulfilled compared to the Second Board, while MESDAQ was for high growth and technologies companies. However, effective on 3 August 2009, Second Board was merged into Main Board and was renamed as Main Market. MESDAQ on the other hand was revamped as ACE Market. The new framework for listings and equity funds-raising is in line with international practices and aimed at allowing efficient access to capital and investments, as well as making Bursa Malaysia a more attractive platform for Malaysian and foreign companies. More information please refers to <http://www.bursamalaysia.com/market/regulation/rules/listing-requirements/main-market/listing-requirements>.

population group stage by stage according to the written procedure and established sample characteristics. An explanation of the procedures and sample characteristics follows.

5.4.2 Sample

The most important procedure is to remove the companies that do not fulfill the requirements set for the study. The data set includes all Malaysian firms listed in the year 1996 or at any time before the year, but without failing to retain their listing status from the year 1996 to the year 2011. This yielded an initial potential sample $n=413$. For each of the selected firms, the shares of total equity held by foreign investors were acquired at the end of each year.

5.4.2.1 Sample Period

This research applies panel data study which spans for 12 continuous years from 2000 to 2011. The choice of time period was determined by the unique characteristics associated with the time frame which will be explained in Section 5.4.2.2 (i) The Listing Year. A static panel is adopted, where data is collected from the same companies for 12 years in a row. Cavana, Delahaye and Sekaran (2001) favour this kind of data study as it can offer a sensitive measurement of the changes which can happen between points in time.

Data was collected starting from the year 2000 because it is from this year that the annual reports of listed companies in Malaysia are made available and complete from Bursa Malaysia's website. In addition, the year 1999 witnessed the huge impact of corporate governance in Malaysia when the Finance Committee on Corporate Governance (FCCG) report was published by Securities Commission (SC) and is known as the Report on Corporate Governance (1999). Reformation of corporate governance has taken place since the financial crisis, and the year 1999 is considered the ideal year to capture the impact of the AFC 1997/1998 on corporate governance. Therefore, the effect can be seen immediately after one year which is the year 2000. The year 2011 was chosen as the last year for sample selection since this is the latest

of the financial year ends for all companies with a ready and published annual report at the time the process of data collection began. As stated in the Bursa Malaysia's listing requirement, PLCs have a few months after the financial year ends to publish their annual reports³².

While it might be better and more meaningful to cover the data from the year 1996 in order to make comparisons and perform analysis with the pre-Asian financial crisis, data availability is unfortunately very limited. Moreover, further difficulties include the cost of accessing the annual reports and the absence of a standard corporate governance disclosure by firms before 1999. Thus, empirical comparisons cannot be drawn before that period. Despite the lack of conformity, to make meaningful justifications in the discussion of the changes in corporate governance due to the AFC 1997/1998, World Bank reports, Asian Development Bank reports, IMF reports, etc. are important documents that have been used to support the arguments, justifications and findings in this study.

5.4.2.2 Sample Characteristics

The sample items have been chosen based on a few strict rules to ensure that they lead to reliable findings in answering the research questions and to achieve the research objectives. The lists of sample characteristics are explained below:

(i) The Listing Year

As explained briefly in the above sections, the samples comprise Malaysian firms listed on Bursa Malaysia and which retain their listing status without fail between the years 1996 and 2011. This stringent condition is to reveal the pattern of foreign

³²Under Paragraph 9.23 (a) of the BM Listing Requirements," the annual audited accounts together with the auditors' and directors' reports shall, in any case, be given to the Exchange for public release, within a period not exceeding 4 months from the close of the financial year of the listed issuer unless the annual report is issued within a period of 4 months from the close of the financial year of the listed issuer."

ownership in Malaysian firms. The later result or finding can be associated with any possible explanations that would be sought from the pattern(s) based on the earlier constructed hypotheses and the ground theories.

In the years before the AFC 1997/1998 struck the Asian region, Malaysia was considered as a rapidly developing country. This attracted many foreign investors which helped to stimulate the country's economic growth. However, everything changed after this financial turmoil and Malaysia was one of the badly affected countries. Thus, the reason for including the listing year of 1996 is that this is the pre-crisis year with the euphoria inflow of foreign funds. Then, of the years after that, 1997 and 1998 are the crucial years in the middle of the financial crisis.

These events are considered as the significant factors in shaping the pattern of foreign investment in Malaysia. The inclusiveness of these listing years as one of the conditions for sample selection would add some intrinsic value to the data. By considering the year before the crisis, it is well accepted that the selected PLCs have undergone the three phases of the AFC 1997/1998 (pre-crisis, the crisis and post-crisis) and the changes in corporate governance which would lead them to take any possible actions in order to attract and retain foreign investment. On the other hand, foreign investors who were fully aware of the financial environmental changes surrounding them would also take wise actions to protect their investment from the expropriation of any parties.

In the aftermath of the crisis, most Asian countries sought ways to strengthen their corporate governance, transparency and disclosure levels (Ho and Wong 2001). Haniffa and Hudaib (2006) also claim that most of the countries in the region established a Code of Corporate Governance to boost the confidence of investors in their capital market. The Government of Malaysia played an active role in creating an awareness of corporate governance and advocated the reformation of corporate governance. The years after the crisis, more specifically the years 1999 to 2001, witnessed major changes in the structure of corporate governance in Malaysia. Thus, these years would gauge the reaction from foreign investors towards the efforts taken

by the government of Malaysia to regain investors' confidence and attract them back to the Malaysian capital market.

However, the year 2001 also witnessed the collapse of Enron and the same type of scandals due to failures driven by corporate governance in the UK and US which had a world-wide effect. In the following years, most of the key players in the economic system began to realise the potential consequences for economies derived from the deficiencies in corporate governance. As a result, more company-based corporate governance began to exist. Later, in the year 2007, the global financial crisis started to spread and after three years, the year 2010 came to represent the post global financial crisis. The year 2011 is also included as this is the latest year with available data at the time when the process of data collection began. The pattern of foreign investor behaviour can be examined during the period of study.

(ii) Malaysian Companies

Only Malaysian companies were considered in this study. The scope of this study defines a Malaysian company as a public limited liability company, incorporated and domiciled in Malaysia, and quoted on the Main Market of Bursa Malaysia Securities Berhad. The above information was derived from annual reports, corporate information, general information and also from the corporate website. Foreign companies listed on Bursa Malaysia were excluded as they have different characteristics to be considered by the foreign investors in making their investment decisions. As opposed to the definition of a Malaysian company, a foreign company is defined as a company that is incorporated and domiciled in any country other than Malaysia. Foreign companies and "foreign-type" companies were excluded. The definition of Malaysian companies is to be followed strictly, since the inclusion of foreign companies and "foreign-type" companies in the sample would affect the potential results predicted in the hypotheses.

"Foreign-type" companies, on the other hand, are defined as companies that are generally known as international, established and well-known with a foreign image. Even though they are incorporated and domiciled in Malaysia, the influence of their

home country's image has a significant attraction for the foreign investors in Malaysia. Among the companies that have been grouped as "foreign-type" companies are Ajinomoto, Guinness, Shell, and a few others. These companies have already established their international image and have their own goodwill. With those values in mind, they would have no difficulty in attracting foreign investors to invest, regardless of any country in which they are incorporated and domiciled. From the initial observation, the percentage of foreign ownership in these companies is more than 50 percent in a row for the 12 years of the study period and a few companies have exceeded more than 80 percent of foreign investment from the total company's ownership. This proportion of foreign ownership is very different from the proportion of foreign ownership in Malaysian companies in the study sample. Thus, including these companies in the sample study would only invite outliers.

In addition to the above justification, the exclusion of "foreign-type" companies was made based on the other important reason. This study was conducted to understand the behaviour of Malaysian firms. Therefore, only pure Malaysian companies were included in the sample. By including foreign companies or "foreign-type" companies, the understanding of Malaysian companies' behavior might not have been fully achieved.

(iii) Non-Financial Companies

Companies which are subsumed under the financial sector, Real Estate Investment Trusts (REITs) and unit trusts are excluded from the study sample because of the difference in their business activities as well as the unique features of their regulatory frameworks and compliance (Lin and Shiu 2003). It has become an adopted convention for this type of study to exclude companies in the financial, real estates and utility sectors from the sample of the study (Douma et al. 2006). The codes and regulations posed on them do not apply to the other PLCs. In addition, their financial statements are differently structured. Therefore, accounting performance comparisons cannot be made in a straightforward way (Ponnu 2008).

5.4.2.3 Sample Screening Process

In order to arrive at the final sample, the following procedures were used. The first step of the screening process is explained in detail in Section 5.4.1 Population, where the listed companies for the years 1996, 1997 and 2011 were bought from Bursa Malaysia. Then, the lists of companies for the years 1996 and 1997 were matched to assure that no single company dropped out from the initial observation. Next, the current list was matched with the list of companies for the year 2011 based on the stock code identification and the companies' names. This process is important in order to access the list of companies listed at the Kuala Lumpur Stock Exchange (KLSE) in the year 1996 and which continued to survive at Bursa Malaysia until the year 2011.

The process was begun by checking the companies with the same stock code and identical name. These companies were then extracted from the list to be confirmed as the first group of the sample. Next, companies with the same stock code, but with different names in the year 2011 were grouped together. Advice was sought from Bursa Malaysia on how to categorise these companies. The suggestion was to read carefully all the companies' announcements one by one. These are available at the given web site address:

http://www.bursamalaysia.com/website/bm/listed_companies/company_announcements

The above step is crucial to determine why these companies' names have been changed. After the checking process was completed, several explanations were found to justify the reasons behind the changes. One of the reasons was the original intention of the company itself to enhance its corporate image. Other reasons for name changes include: debt restructuring, merger, acquisition, joint venture and the admission of an unrelated company to replace the delisted company by using the same stock code number which had been used previously.

Apparently, not all this information can be found from the announcements in the Bursa Malaysia's web site. Further checking for absent information was done thoroughly using the company's web site and a few other mechanisms such as the

media and other reliable and available information from the internet. After summarising all this information, it was decided only to consider the first reason (a company changes its name for commercial purposes) in order to be included in the sample study. Other reasons have to be declined as the status of the company itself is no longer the same or is totally different.

The third category of companies is the group of companies which appear in the listing of KLSE for the year 1996, but do not exist in the listing of Bursa Malaysia for the year 2011. An initial assumption was made; these companies have been delisted from the Exchange. However, each of these companies' announcements was scrutinised to confirm the assumption. As predicted, this group of companies was no longer listed on the Exchange for the year 2011, and their delisted years varied and were recorded for additional references in the future. Unfortunately, since the main criterion did not meet the sample's requirements, which is to be listed from the year 1996 to the year 2011, this third group was rejected. In the end, the entirety of the companies from the first group was included as a sample, some of the companies from the second group were selected and none of the third group was included.

The data screening process was continued by removing the REITs and financial companies. The reasons for removing these types of companies were explained under Section 5.4.2.2 (iii) Non-Financial Companies. Next, the process of selecting only Malaysian companies took place. Detailed explanations for this action can also be found under Section 5.4.2.2 (ii) Malaysian Companies. Finally, a few more firms with incomplete information were dropped. The observations were also made on any suspicion of typographic errors.

The process of the sample selection implemented in this study is illustrated in the following Figure 5.1.

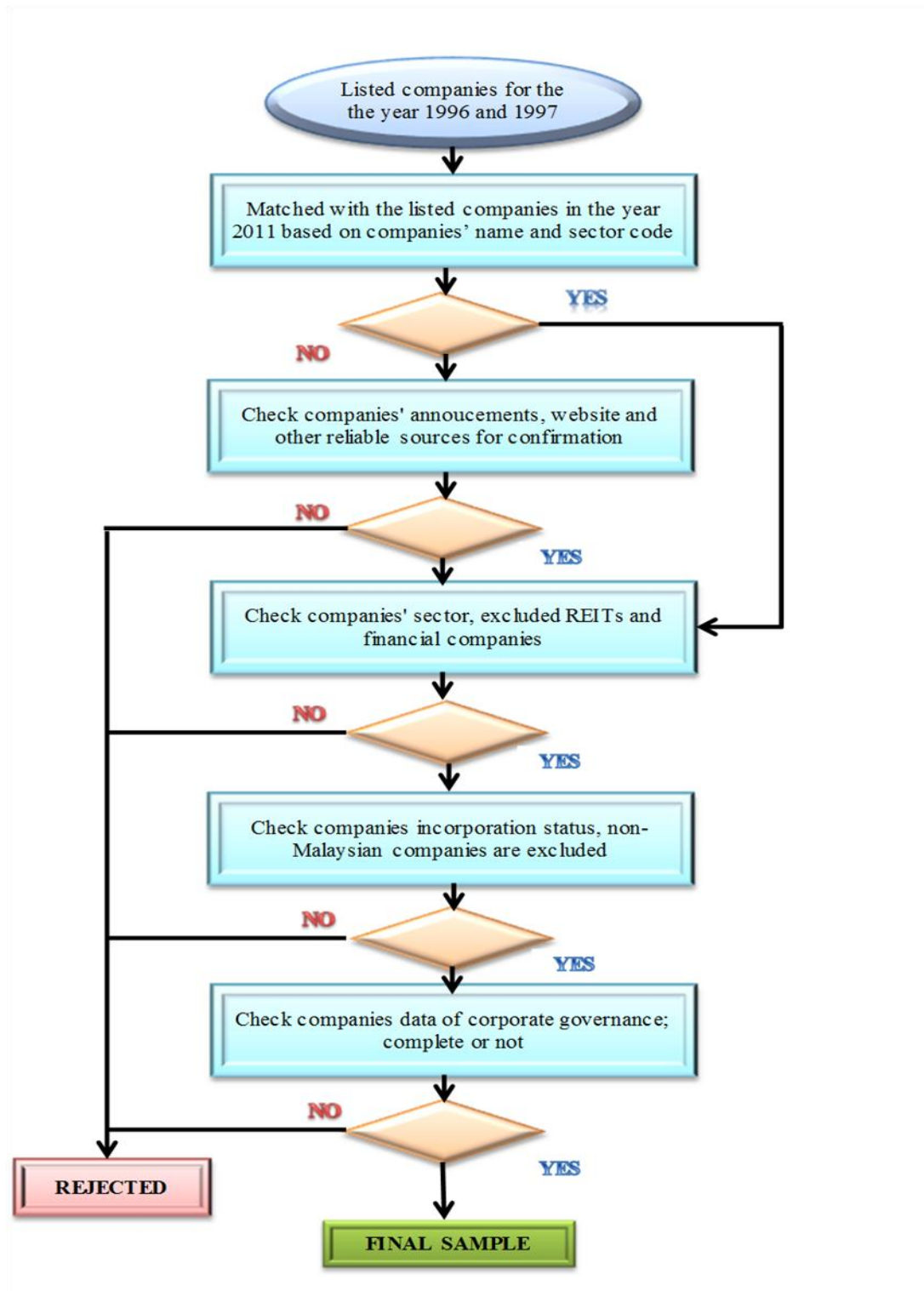


Figure 5.1: Sample Screening Process

5.4.2.4 Sample Selection

These meticulous processes have been applied in order to arrive at the final sample. Starting from the total number of 665 companies listed on KLSE, as at 30 June 1997, 21 companies have been omitted from the sample that were found to be listed after the year 1996. Then, 231 companies were excluded as they were not qualified to be accepted into the group of the sample. These companies were delisted somewhere between the years 1996 to 2011, the main condition which has not been fulfilled. Thus, the initial sample is $n=413$.

The initial sample size was further reduced when another 52 companies classified under the financial sector, unit trusts and REITs were removed because of their unique features in terms of business activities. The remaining non-financial PLCs included 361 companies which were then reduced by the removal of nine companies which do not satisfy the definition of Malaysian companies (see Section 5.4.2.2 (ii) Malaysian Companies).

The third screening process left the sample with the Malaysian non-financial PLCs. At this point, the latest sample was checked for data completeness. Malaysian companies with incomplete financial data, board governance data and ownership data were also removed. Bursa Malaysia was contacted for an explanation before the decision was taken to remove the companies with insufficient data of foreign ownership, which is the dependent variable in this study. Assumptions were made about whether the data actually represented 0 (zero) percentage or whether the data really was unavailable. Then it was explained that these companies did not provide their foreign data for the mentioned years. Thus, Bursa Malaysia was unable to serve the ownership data. Therefore, the actions below were taken.

Three companies that were removed due to insufficient data about foreign ownership are Malton Bhd (6181), Sapura Motors Bhd (7811) and TCL Bhd (6661). They have no data about foreign ownership for two years in a row and the difference between the two blank years was too significant. Thus averaging was not reliable for estimation

purposes. For example, foreign ownership for the year 1999 in TCL Bhd was 30.87%, and after two years of absent data the percentage plummeted to only 5.13%. In this case, the company had to be removed as the averaging method could not be used to estimate the real value. However, in the few cases where the gap of absent data was only one year and the difference between the percentages was not significant, the averaging method was applied. For example, 1.15% was estimated as the percentage of foreign ownership in LBS Bina Bhd (5789) for the year 2001 by considering the percentage of foreign ownership in the year ‘before and after’ (1.88% and 0.41% respectively) the missing data. Companies without a complete set of annual reports, which is the main source for data collection, have also been taken out. The number of companies reduced to only 339 after the process of sample selection.

Table 5.1: Sample Selection

	Number of companies
Total PLCs listed on KLSE/ Bursa Malaysia as at 30 June 1997	665
<i>Exclude:</i>	
Total of PLCs listed on Bursa Malaysia later than the year 1996	21
Total of PLCs delisted from the Exchange for 1997 to 2011	231
Total of Finance, REITs and Unit Trust PLCs	52
Total of PLCs listed on Bursa Malaysia for 1996 to 2011 after excluding Finance, REITs and Unit Trust PLCs	361
<i>Exclude:</i>	
Total of PLCs with the status of foreign / “foreign-type” companies	9
Total of PLCs companies which were defined as Malaysian companies after excluding foreign / “foreign-type” companies listed on Bursa Malaysia	352
<i>Exclude:</i>	
Incomplete company’s annual report from the year 1996-2011	9
Incomplete financial data	-
Incomplete foreign ownership data	4
Total PLCs in the initial sample for the years 2000 to 2011	339
Total PLCs in the research sample for the years 2000 to 2011	153
Total PLCs for observations for the 12 years	1,836

5.4.2.5 Final Sample

Sampling is the process of selecting a sufficient number of elements of the population, so that the study is able to generalise the properties or characteristics of the total population. After determining the potential number of subjects which were feasible for this study, an initial attempt was made to collect the data. However, the amount of time to collect the corporate governance data from the companies' annual report seemed practically impossible. Even if it were possible, it would be prohibitive in terms of human resources (Sekaran 2003).

In order to collect corporate governance, board of directors and ownership data, every single line of the narrative story and the information in the annual report from the related sections had to be scrutinised. This made the process of data collection time-consuming, especially when the data had to be collected for the 12-year period consecutively from the year 2000 until 2011. In addition, as at the date of data collection there was no possible source or database for Malaysian corporate governance data that was available to be accessed. It was therefore decided to reduce the sample size. Eventually, there were 1,836 observations from 153 companies in the final sample.

5.4.2.6 Sample Representativeness

It is believed that adopting an appropriate method for sample selection, rather than taking the entire population to be analysed, is likely to produce reliable results. Given the huge number of elements in a population, Sekaran (2003) claims that taking each of them into consideration would lead to potential error due to human mistakes. As long as the results of the chosen sample are generalisable to the entire population, then it is acceptable and considered as an efficient method as fatigue is reduced which consequently lessens the production of potential error.

The size of the final sample is also large, 153 companies represent half of the initial sample and the total observations for the 12 years is 1,836 (153 x 12) (see Table 5.1:

Sample Selection), which is likely to increase the probability of the sample being representative of the population (Hussey and Hussey 1997; Remenyi et al. 1998).

(i) Probability Sampling

The need for choosing the right sample for a study cannot be underestimated. A representative sample will be able to generalise the population's properties. In this case, probability random sampling has been used for sample selection, whereby each element in the population has a known chance of being chosen as a subject in the sample. However, there are identifiable subgroups of elements within the population that may be expected to have different parameters on a variable. Knowledge of the kinds of difference that exist for the different groups will help to develop useful and meaningful interpretations when evaluating the results (Sekaran 2003). Thus, stratified random sampling was selected, as data needs to be collected in a manner that helps the assessment of needs at each subgroup level.

(ii) Stratified Random Sampling

This kind of sampling involves a process of stratification, followed by the random selection of subjects from each stratum. The companies were divided into mutually exclusive groups that are considered relevant, appropriate and meaningful in the context of the study. In this case they were chosen based on their sector of operation. There are eight sectors or strata and this followed accordingly from the classification made by Bursa Malaysia. The sectors are: industrial products, property, consumer products, construction, technology, trading/service plantation and others. In this study, a stratified sampling design technique helps to answer the question about which sectors are likely to attract foreign investors.

The initial sample was 339 companies, which was justified to be reduced to the minimum of 150 companies (see Section 5.4.2.5 Final Sample and Section 5.4.2.6 Sample Representativeness). The companies have been stratified from each stratum or sector using simple random sampling. They were proportioned to the number of

feasible samples in the respective sector. Please see the following Table 5.2 for details.

Table 5.2: Proportionate Stratified Random Sampling Table

Sector	Number of feasible segments	Proportionate Sampling
Industrial products	105	46
Property	51	23
Consumer products	42	19
Construction	23	12
Technology	7	3
Trading/Service	75	33
Plantation	31	14
Others	5	3
Total	339	153

The final sample chosen for this study is 153 PLCs, and the total number of observations for the 12 years is 1,836 (153 x 12).

5.5 Instruments

Almost the entire data was hand-collected from secondary sources; this was mainly from company annual reports in addition to the Datastream and Thomson One Banker. The process of data collection was performed by checking the items one by one in order to assure their accurateness. Besides this, data was cross-referenced to other sources of references to double confirm the initial information and the figures in hand. For example, the information for each company was rechecked from the company's website and the Datastream, besides the annual report of the company itself. The details relating to the board of directors and ownership structure were also cross-checked from various sources (such as the directors' profile, shareholding statistics, statement of directors' shareholding, and noted to the accounts). The details are given in the following Table 5.3 and Table 5.4. All the data gathered was keyed-in to the worksheets that functioned as templates and these would be used one after the other to

cross check and also to calculate the type of ownership. Five worksheets were prepared to sort the companies' data, corporate governance and financial data.

Table 5.3: Data Sources

	Sources	Related information
Companies' general information	Companies' annual report	Companies' incorporation year and information, listed year.
	Bursa Malaysia website	Companies' sector, listed history, and announcements.
	Companies' website	Companies' history, incorporation year and board of directors.
Board governance data	Annual reports	Directors' name, designation, age, nationality, background (e.g. academic, industry, profession, political, professional qualification), family members of directors, significant shareholders on the board, other directorship and ownership.
	Datastream	Directors' name and designation.
	Companies' website	Board of directors and companies' history
Financial data	Annual report	Income statement, balance sheet and cash flow information.
	Datastream	The book value of total assets, market to book ratio, debt ratio, dividend yield and market value of ordinary shares
	Thomson One-Banker	ROE, book to market ratio (BTM), total assets and total debt.
Ownership data	Annual report	Name of shareholders, number of shareholdings by each director (direct and indirect), number of shareholdings by the family shareholders, management shareholders, and institutional shareholders.
	Bursa Malaysia data	Foreign equity ownership
	Thomson One-Banker	Foreign equity ownership for current year
Control variables	Annual report	Debt and total assets
	Datastream	Debt, total assets, listing date, incorporation date.

Most of the data was collected from the companies' annual report. The information provided is comprehensive and divided into the relevant sections. These reports are prepared according to International Financial Reporting Standard (IFRS), previously known as the International Accounting Standards (IAS), and approved by an

independent external auditor and the statutory accounting standard-setting body, which is under the surveillance of the Malaysian Accounting Standard Board (MASB). Therefore, there is a high degree of confidence in the reliability of the data presented in the annual report. The following Table 5.4 presents the precise locations from where the data was collected in the companies' annual reports. The selected parts of annual report are attached in the Appendix.

Table 5.4: Annual Report Sources

Sections	Related Information
Corporate Information	Directors' name, designation, auditor, listing information.
Corporate Structure	Company's subsidiaries, business segment.
Directors' Profile	Directors' name, designation, age, nationality, background (e.g. academic, profession, political, professional qualification) other directorship, relationship and ownership.
Corporate Governance Statement	Board size, independence, board composition, and family relationship.
Director' Report	Principal activity of the company, directors' rotation date, directors' interests, auditor.
Independent Auditors' Report	Auditor's information.
Financial Statements	Income Statement - revenue, net profit, financial year end Balance Sheets – total assets and total debts. Statement of Changes in Equity – dividend paid. Cash Flow Statement – dividend paid.
Notes to the Accounts	Corporate information – principal activity, incorporation and domiciliation status, listing status. Investment in Subsidiaries – list of subsidiaries, foreign subsidiaries. Segment Information – business and geographical segment.
Statement of Shareholding	Number of shares held, thirty largest shareholders, substantial shareholders, directors' interest, institutional shareholding.

The data were keyed-in to the worksheets accordingly. After all the selected companies had been scrutinised, any missing data was identified. Missing data treatment will be explained in the related subsection (see Section 5.7.2.2 Missing Value Analysis). The following subsections, discussing the dependent and independent variables, further explain the relevant sources of data for each variable.

5.6 Variable Definitions and Measurement

5.6.1 Dependent Variable (FEO)

The research problem focuses on the pattern of foreign ownership in Malaysian companies. Information on the percentage of foreign equity ownership was collected for each company in the sample from the year 2001 to the year 2012. Even though the sample study was taken from the year 2000 to the year 2011, a one year lag was allowed for independent variables, to capture the effect on the dependent variable. For instance, foreign ownership in the year 2001 would be associated with the independent variables from the year 2000. This was performed to ensure that the effect of any changes or actions taken by the companies was considered by foreign investors before they decided whether to increase their shares, to retain their investment or to withdraw their investment from the companies. The nearest time to see the effect is a year after that. Panel data facilitates this by allowing the result of decision making to be considered after a certain period, as it is expected that the impact of it can be seen after some time has passed (Wooldridge 2009).

The percentage of foreign ownership in the company is the source for the key dependent variable and the unit analysis is the company. This data was not provided by the Bursa Malaysia, nor disclosed in the companies' annual report, and was not made available in any database. This is mainly because there is no requirement imposed on the companies to disclose this information. Thus, this data had to be purchased from the Bursa Malaysia. Bursa Malaysia is the only legal party who can access this data from the disclosure made by the shareholders in their Central Depository System (CDS)³³ accounts. Unfortunately, the data of this percentage of FEO in a company is a solid percentage without any further information to be comprehended, for instance, what type of foreign investors are they, what are their

³³A CDS account acts as a means of representing ownership and movement of securities for an individual or a corporate body. In Malaysia, in order to start the transactions in Bursa Malaysia, CDS account is a must besides the trading account. More information can be viewed via this link: <http://www.bursamalaysia.com/market/securities/education/faqs-on-cds/>

countries of origin, are they foreign financial institutions, foreign industrial corporations or foreign individual investors? Thus, no investors' classification can be made. Where the percentage of foreign ownership was not stated for certain years or appeared vaguely, the Bursa Malaysia was contacted for clarification. The procedures taken were explained in Section 5.4.2.4 Sample Selection.

In order to provide meaningful results, the pattern of FEO was scrutinised. Instead of using the actual foreign ownership percentage, the value was changed to a blunter scale e.g. 0/1. In the initial observation, it was discovered that all the companies in the sample study had a proportion of foreign ownership. For the new form of dependent variable, logistic regression is utilised (see Section 5.7.5 Logistic Regression Model). Where the total of foreign ownership was 20% and more, this was categorised as 1, otherwise 0. More detailed explanation can be found in Section 6.2.3 Dependent Variable: Distribution and Skewed Data.

5.6.2 Independent Variables

An independent variable is the predictor variable which is supposed to be the cause of change in the dependent variable. In this study, the independent variables are subsumed into three sub-groups: i) board of directors' characteristics ii) directors' attributes iii) ownership structure. Four different models are built (see Section 5.7.4.1 Research Model and Measurement) in relation to these variables. Information was collected for each of the years from 2000 to 2011.

For the first independent variable in this study, testing Hypothesis 1, board size (BSIZE) H_1 , the number of directors on the board was counted with a few conditions. The director was only counted if he or she had served on the board for the whole financial year. If this condition was not fulfilled, then he or she must sit on the board for at least six months and above, or if less than 6 months he or she must sit on the board at the end of the company's financial year end. Alternate directors were not counted. This data was collected from the corporate information, the board of directors' profiles and the directors' reports.

Outside director compliance (BCOM) H_2 is considered when there is the requirement stated in the Code (2000) that one third (1/3) of the board must be independent; this takes into account the varying board sizes of these companies. A binary variable was set, where firms were coded with 1 if they complied with this best practice and with 0 otherwise. This data was obtained from the corporate information and the board of directors' profiles.

For H_3 - foreign directors on the board (DIRFOR) - the nationality of the directors on the board were meticulously checked and the presence of foreign director(s) on the board was measured as a percentage of the resulting total number of directors on the board. Directors with multiple-directorships (DIRMUL), H_4 , were recorded by referring to the number of additional directorship(s) in other public companies. A dichotomous variable was constructed, 1 was recorded for 7 and above additional board seats, and 0 was recorded otherwise. The measurement is slightly different in Perry and Peyer (2005) and Jiraporn et al. (2009), since they only counted outside directorship in other companies. In this study, for an indication of 'directors' busyness', it is considered practical to include whatever type of directorships they serve outside the firm, since they are time consuming and limit their effective presence in the company. The cut-off point may seem arbitrary. However, it is selected based on the pattern of DIRMUL data distribution, as checked in the STATA software. Nonetheless, all the variables were obtained from the corporate information and directors' profiles.

From the same sections - corporate information and directors' profile - the data for the rest of the variables concerning board characteristics - such as women directorship (DIRWOM), directors' Western education (DIRWEST) and directors' professional qualification (DIRPROF) - were obtained. They are referred to as H_5 , H_6 , and H_7 respectively. DIRWOM is a binary variable which is equal to one for the existence of female director(s) on the board and zero otherwise. Western educational directors (DIRWEST) were counted from the total number of directors on the board. For the directors' professional qualification's variable, they were considered only when the qualification was in accounting and/or finance. The professional qualifications in

these critical purviews are considered crucial in predicting the market and understanding the company's financial stability (Burak Guner et al. 2008). Among the qualification titles are CA, CMA, CPA, CCSA, etc. (see abbreviation for details). The directors' profile was carefully checked and the proportion of directors with these professional qualifications was calculated based on the total number of directors.

For the second part of the corporate governance variables, the ownership structures were categorised into three groups: family-controlled company (FCC), managerial ownership, and institutional ownership. In relation to FCC, the data was collected from various sections in the companies' annual reports such as Directors' Profile, Corporate Governance and Shareholder Statistic. Effective from January 2001, the Code (2000) mandated that companies should disclose the relationships between its directors and managers and among its directors.

Family ownership would be considered if they fulfilled two conditions: (i) Director(s) are related by blood or marriage to other director(s) or if not, at least one of the family members sits on the board and the other(s) who are related by blood or marriage to a director on the board may acquire shares but not sit on the board, (ii) family directors have ownership (direct or indirect) in the company. If these two criteria are fulfilled, then the total ownership held by them is considered as family ownership. In certain cases, a third criteria would be considered which is (iii) if two directors or more are not related to each other, but they have a family relationship with the other director(s) or shareholder(s), then the total of the directors ownership and their family ownership is considered for the variable.

After the process of identification and calculation of family ownership, it would be decided whether they are an FCC or not. In this study, an FCC is determined by the position of the family member on the board and/or the percentage of family total ownership. The minimum of family ownership (direct and indirect) must be at least 20% of the company's equity and one of the family members must at least sit on the board as an executive director for it to be considered as controlling ownership. If these

two requirements have not been fulfilled, then the company would not be considered as an FCC.

There are a few explanations for using a minimum 20% for family ownership. Around the world, there is no uniform percentage applied. Scholars use different measurement and percentage of equity ownership to define family companies, for example – (i) Villalonga and Amit (2006) use at least 5% of the firm's equity as a cut-off point for their study of family firm listed on the Fortune 500, (ii) Smith and Amoaka-Adu (1999) use the minimum of 10% of total votes to determine family firm on Canadian markets, (iii) Yeh, Lee and Woidtke (2001) found that Taiwanese families need only 15% control, on average, to control a firm effectively and (iv) European Union (2009) uses 25% of the decision-making rights mandated by the share capital to define family company, etc.

The 20% ownership as a cut-off point has been used extensively by many scholars in defining family companies. For example, Faccio and Lang (2002) used 20% equity ownership as a threshold point in their examination of the family companies for 13 Western European countries (Austria, Belgium, Finland, France, Germany, Ireland, Italy, Norway, Portugal, Spain, Sweden, Switzerland and the United Kingdom). Meanwhile, Claessens et al. (2000) also used the cut-off level at 20% in their study of family firms on nine East Asian countries (Japan, Taiwan, Hong Kong, Korea, Singapore, the Philippines, Indonesia and Malaysia). The reason why 20% of ownership was used as a cut-off point is also explained in Section 6.2.3 Dependent Variable: Distribution and Skewed Data and also from the footnote number 35, in Chapter 6.

A dichotomous variable was constructed to record family-controlled ownership. An FCC was coded using a dummy variable (0, 1). An FCC was coded as 1, and 0 otherwise. No earlier assumptions have been made to predict the relationship among the directors. Even though the relationship can sometimes be traced from their family names, especially if they are Chinese family, the relationship would only be ascertained from valid sources. Alternative sources such as newspapers, Google,

encyclopaedias, etc. were used to obtain clarification. Without any information, no relationship was recorded.

In computing the total ownership for the group of managerial ownership (MANTOW) H_9 , the percentage of ownership acquired by each director was scrutinised and recorded in one worksheet according to the year and company. The directors' position was then identified and the shares held by the directors in a managerial position were classified as managerial ownership. A different worksheet was used to compute the total ownership. The ownership information was obtained from two sections in the company's annual reports: the directors' report and shareholding statistics.

The third category of ownership, institutional ownership (INSTOW) H_{10} , was gathered from the shareholding statistic section in the company's annual reports. In this case, only the direct shareholding in the company was computed. The institutions refer to a similar definition given in general by the companies: Banks/Finance Co; Trust/foundation/Charities; Clubs/Associations/Societies; Cooperatives and Government Agencies/Institutions. The ownership was taken from the 30 largest shareholders disclosed in the shareholding statistic. The following Table 5.5 lists the variables, acronym and provides the definition as well.

Table 5.5: Independent Variables

Variables	Acronym	Definition
CORPORATE GOVERNANCE ATTRIBUTES		
1. Board size	BSIZE	Number of directors on the board Condition: The Directors who are counted are the directors who served on the board for the whole financial year, if not he/she must sit on the board for at least 6 months and above OR if less than 6 months he/she must sit on the board at the end of the company's financial year end. Alternate director(s) is/are not counted
2. Outside Director Compliance	BCOM	1= if more than 1/3 of BOD is independent non-exec director, otherwise = 0

3.	Presence of foreign director	DIRFOR	The percentage of foreign director(s) on the board. Foreign director is defined as directors that are domiciled in foreign countries.
4.	Multiple-directorships	DIRMUL	1 = if number of additional directorship(s) in other public companies is 7 or above, otherwise = 0
5.	Women directorship	DIRWOM	1 = the existence of female director(s) on the board, otherwise = 0.
6.	Directors' with Western educational background	DIRWEST	The percentage of directors with the US, UK and Australia, etc. Western educational background
7.	Directors with professional qualification(s)	DIRPROF	The percentage of directors with accounting and financial professional qualification (CA, CMA, CPA, CCSA, CCA or CPE)
OWNERSHIP ATTRIBUTES			
8.	Family-Controlled Company	FCC	1 = if the companies are controlled by family members for at least 20% of the company's equity (direct + indirect) with one family member at least sitting on the board as an executive director, otherwise = 0 or NFCC – Non-Family-Controlled Companies. (Companies that not fulfill the definition of FCC)
9.	Managerial total ownership	MANTOW	Total ownership (direct and indirect) by executive directors
10.	Institutional ownership	INSTOW	Percentage of ownership by institutions (direct only)

5.6.3 Control Variables

There are eight control variables that are appropriate to be characterised as continuous variables in this study. These variables are liquidity ratio (current ratio), solvency ratio (leverage ratio), profitability ratio (ROE), firm size, firm age, audit firm, foreign sale and dividend yield.

Based on the extant literature, these control variables are well-known for their important role in influencing foreign investors' decisions, for example, the study by Kang and Stulz (1997) in association to the size of firms. Dahlquist and Robertsson (2001), on the other hand, show foreign investors' preference for firms with high cash on hand (liquidity ratio) and low dividends yields. The rationale for controlling firm size (FSIZE) and firm age (FAGE) is that the bigger and the older the company, the

more experienced they would be and thus in a better position to attract foreign investors. The companies' ages were identified from their annual reports and the Emerging Market Information Service (EMIS) at <http://www.securities.com>, while the size of the companies was formulated from the natural log of the book value of the total assets from Datastream.

Current ratio (LIQRAT), debt ratio (DEBRAT), Return on Equity (ROE) and dividend yield (DIVYI) were obtained from Datastream, supplemented by the Thomson One Banker. At the end of the data collection process, the remaining variables with missing values were retrieved from the financial statements presented in the companies' annual reports.

Audit firm (AUDF) was also used as a control variable since, based on the previous study, foreign investors favour firms which are audited by international and well-known auditors. AUDF is used as a proxy for higher quality disclosure. Finally, a foreign sales (FSALE) was used as a proxy for international recognition. This data was collected from the companies' annual reports. In the following sub-sections, control variables are discussed in further detail.

5.6.3.1 Firm Size

Dahlquist and Robertsson (2001) find that foreign investors favour large firms, and this is supported by the findings of Lin and Shiu (2003), which also repeat similar results demonstrated by Falkenstein (1996), Kang and Stulz (1997) and Gompers and Metrick (1999). In addition, Kang and Stulz (1997) offer evidence that foreign investors in Japan are less interested in smaller firms. This is based on the assumption that the larger firms are more efficient at competing in the international market than smaller companies (Bonaccorsi 1992; Calof 1993) and have lower investment barriers (Lin and Shiu 2003). Therefore, it makes it easier for them to be recognised by foreign investors.

In addition, Cavusgil (1984) asserts that larger firms have various advantages. The other main argument which has been documented is that, compared to small firms, large companies have achieved economy of scale (Short and Keasey 1999), making them more competitive in the international market (Aaby and Slater 1989), enabling them to acquire more resources such as finance, technology and personnel etc. (Cavusgil 1984) and enabling them to create entry barriers (Short and Keasey 1999) which restrain other firms from competing in the market.

The finding of Kim et al. (2010) is consistent with this claim, as they find that during the unstable and volatile period, foreign investors prefer the large firms because the probability of firm survival increases with firm size (Evans 1987). It is also assumed by Lin and Shiu (2003) that a large firm is friendlier for disclosing information. Thus, to minimise the negative impact of information asymmetry, foreign investors favour large firms since informational asymmetry is higher for them compared to local investors. This is consistent with the evidence exhibited by Bujaki and McConomy (2002) who found that larger companies disclose more, based on the arguments that disclosures are costly to small companies, and they are also associated with the informational asymmetry problem which is in agreement with Aksu and Kosedag (2006) and Tsamenyi, Enninful-Adu, Onumah (2007).

5.6.3.2 Firm's Age

It is discovered that a firms' age is an important determinant of firm growth (Evans 1987). Evans (1987) further concludes that the growth and the variability of firm growth decrease with firm age. On the other hand, he implies that the probability of survival increases with age more rapidly for larger firms. Thus, the size and the age of a firm are found to be interrelated with each other.

5.6.3.3 Debt Ratio

Debt ratio (DEBRAT) is used to control for the possibility that debt holders inflict any substantial influence over the operation and behaviour of the firms and its

management (Short and Keasey 1999). It is argued that the debt ratio can be implied to be one of the mechanisms to resolve conflicts between managers and shareholders. The managers are assumed to be responsible for achieving the necessary level of cash flow to pay for the obligation, thus lessening their time consuming excessive perquisites, concomitantly increasing the value of the firm's equity (Jensen and Meckling 1976). Chizema and Kim (2010) argue that firms with a high level of debt face a lot of uncertainty and difficulty in obtaining alternative finance, especially during a crisis (Peng and Jiang 2010). High debt results from lack of managerial control as firms mismanage their funds due to their involvement in unprofitable segments, hence jeopardising their core competencies. Thus, these firms need to send a signal to foreign investors that they will change for the better by adopting a new governance template (Greenwood and Hinings 1996).

Dahya and McConell (2007) suggest that, to solve this problem, the presence of outside directors on the board should be considered. By having a high debt ratio and simultaneously having a high proportion of outside directors on the board, this provides a positive signal to foreign investors that the firm is undertaking a change process to improve its financial position. The need for governance reform is noteworthy for the companies with a high debt issue, as they can derive legitimacy from society, including foreign investors, subsequently having access to resources. Therefore, it is argued that foreign investors do not favour firms with a high debt ratio in the emerging market unless they can be convinced that special vigilance on that issue has been exercised - e.g. good corporate governance practice, for instance the existence of a high proportion of outside directors on the board.

5.6.3.4 Audit Firm

Mitton (2002) used '*auditor quality*' as one of the proxies for higher disclosure. He finds that the quality of the auditor had a strong impact on a firm's performance during the East Asian crisis. In a later study, Aggarwal et al. (2005) also used the same proxy to represent the higher quality of accounting disclosure. The auditor was indicated as 1, which represents 'high quality' if the firms used an international Big-5

auditor, otherwise 0. The results of the study suggest that firms with better accounting quality and corporate governance attract more foreign capital (foreign institutional investors). This study suggests that in allocating their investment in emerging market equities, U.S. institutional investors give preference to the quality of the auditor and it is one of the dominant determinants of foreign investor investment allocation decisions. It is argued that, for reputed audit firm to preserve their status, they are highly likely to ensure that an acceptable level of transparency is applied in presenting the company report (Mitton 2002) as their attachment to the audited firms are weaker than the local audit firms, while their burden of liability is greater for making errors (Dye 1993). In the Malaysian environment, Che Ahmad (2002) attests that foreign companies tend to hire Big 4 auditors.

5.6.3.5 ROE

In this study, ROE is used as a proxy to measure a firm's efficiency in generating profits from every unit of common stock owners. This ratio can tell us how an efficient firm manages its funds to generate earning growth. Based on agency theory, managers in companies with a satisfactory level of profits are prone to highlighting their performance. Hence, they may be able to convince prospective investors that their company is competently managed. It is argued that foreign investors tend to invest in the high-profit companies as high profitability emphasises success. Previous studies find evidence that foreign investors prefer firms with high ROE (see Dahlquist and Robertson 2001; Das 2014), while Bokpin and Isshaq (2009) find no significant relationship.

5.6.3.6 Liquidity Ratio

The liquidity ratio is used to determine the liquidity of the assets in a company and its ability to pay its short term obligations. If the ratio value is greater than one, it is a good sign as it demonstrates the capability of the company to fully repay its short term debts. The evidence offered in many studies indicates that foreign investors favour

firms with a healthy cash position (see for example, Bokpin and Isshaq 2009; Dahlquist and Robertsson 2001; Mangena and Tauringana 2007).

5.6.3.7 Dividend Yield

Foreign investors preferred high dividend yield firms during the pre-crisis period, but showed no particular preference during the post-crisis period (Evans 1987). Dahlquist and Robertsson (2001) also found, in their study that foreigners in the Swedish market prefer to invest in firms which pay low dividends. This is similar to Gompers and Metrick (1999), who found that American institutions invest in firms that have had relatively low returns during the previous year. Thus, the amount of dividend paid is not an important deciding factor in foreign investment. Abdullah, Yahya and Elham (1999) explain that the variable is not important as the dividend declared by Malaysian firms is not substantial.

5.6.3.8 Foreign Sale

In further analysing the preference for larger firms, Dahlquist and Robertsson (2001) also found that market liquidity and presence in the international market, measured through export sales or listings on other exchanges, seems to characterise foreign holdings better than firm size alone. Kang and Stulz (1997), who conducted a research in Japan, also report a higher percentage of foreigner ownership in firms that have a larger portion of export sales. A similar result was found by Covrig et al. (2006). While, Delois and Beamish (1999) reported that international experience and a strong institutional environment also lead to increases in the equity position of the foreign investor. The definitions and acronyms for each of the control variables are presented in the following table:

Table 5.6: Control Variables

Control Variables			
1.	Firm size	FSIZE	Natural log of the book value of total assets
2.	Firm age	FAGE	Number of years since being incorporated until 1 January of the annual report year
3.	Current ratio	LIQRAT	The book value of short term asset divided by short term debt
4.	Debt ratio	DEBRAT	The book value of total debt divided by total assets
5.	Return on Equity	ROE	Net Income divided by shareholders' equity
6.	Audit Firm	AUDF	1 = Big 6/5/4, Otherwise = 0
			<p>The BIG 8: (Prior 1989) Earnst & Whinney Arthur Young Delloitte, Haskins & Sells Touche Ross Arthur Anderson Coopers & Lybrand KPMG Peat Marwick Price Waterhouse</p> <p>The BIG 6: (1989) Earnst & Young (1+2) Delloitte & Touche (3+4) Arthur Anderson Coopers & Lybrand KPMG Peat Marwick Price Waterhouse</p> <p>The BIG 5:(1998) Arthur Anderson and <i>The BIG 4</i></p> <p>The BIG 4:(2001) Earnst & Young Delloitte & Touche (3+4) KPMG Peat Marwick Price Waterhouse Coopers</p>
7.	Foreign sales	FSALE	Percentage of sales in the foreign countries out of the company's total sales in the financial year.
8.	Dividend yield	DIVYI	The dividend yield expresses the dividend per share as a percentage of the shares price. The underlying dividend is calculated according to the same principle as datatype DPSC (Dividend per share, current rate) that it is based on an anticipated annual dividend and excludes special or one-off dividends. OR: The value of all dividends paid during the year divided by the market value of the firm at year-end.

5.7 Data Analysis and Interpretation

5.7.1 Panel Data

Collecting data for a series of time, 12 years in a row and for multiple numbers of the same companies allows for dimensional consideration between cross sectional and time series effects. This structure of data is called a panel or longitudinal data set. The general estimated equation for the panel data model may be formulated as below:

$$Y_{it} = \beta_0 + \beta_1 X_{it} + \beta_2 X_{it} + \dots + \beta_n X_{it} + \varepsilon_{it}$$

That is, i denotes the firms and t denotes time. Meanwhile, Y_{it} and X_{it} are the dependent and independent variables, respectively, of pooling N cross sectional observations and T time series observations. β_0 is the constant term or intercept across sectional observations, and ε_{it} is the error term, where:

$$\varepsilon_{it} = \mu_i + v_{it}$$

This model has a composite error, encompassing μ_i and v_{it} . μ_i denotes the unobservable individual specific effect (heterogeneity) and v_{it} denotes the remainder of the disturbance or idiosyncratic error term.

The analysis of panel or longitudinal data provides a rich environment for the development of estimation techniques while helping to examine the issues and the possible mingled effects that cannot be studied in either cross-sectional or time series settings alone (Arellano 2003). The dynamic changes within the period of study can be examined with the repeated observations on the same units, which allow the researcher to control for certain unobserved time invariant heterogeneity. In this analysis, the causal inference is relatively easy to conclude compared to the single cross-section study (Wooldridge 2009; Arellano 2003). Therefore, this enhances the quality and quantity of data (Greene 2003; Gujarati 2003). An appropriate statistical analysis was designed for this kind of data and the explanations are presented in the next subsection.

5.7.2 Statistical Analysis

The data has to be arranged and various econometrics concepts have to be applied to explain the data in order to draw inferences (Saunders, Lewis and Thornhill 2009). The selection of an inappropriate statistical technique or econometric model may lead to an incorrect interpretation and the study objectives may not be achieved. Statistical software - SPSS Version 19 and STATA version 12 - were used to run the statistical analysis in order to measure the relationship between the dependent variable and the independent variables. STATA appears to have a particularly rich variety of panel analytic procedures. Statistical discussion in this section covers three aspects, namely descriptive statistics, missing value analysis and detecting multicollinearity.

5.7.2.1 Descriptive Statistics

A number of descriptive statistics techniques and analysis can be explored to explain the data set. In this section, the descriptive statistics discuss the normality test and univariate analysis.

(i) Normality Test

Normality essentially refers to the distribution of error (or residuals) which is considered to be in the normal distribution. Data is assumed to have a normal distribution in order to test hypotheses, even though it is not needed to perform multiple regression analyses (Hair, Tatham, Anderson and Black 2006). The assumption must be held true in order to use the parametric test. The distribution of each variable can be checked from the histogram. Several other graphs can also be used such as the kernel density estimate plot, the standardised normal probability plot (P-P normal probability plot) and also the quartile of a normal distribution plot (Q-Q normal probability plot).

In this study, the normality test was conducted in two ways. Firstly, the skewness and kurtosis value of the variables was computed. According to Field (2012), a skewness

of ± 1.96 and a Kurtosis of ± 3.29 are within the normality limits. Secondly, the Kolmogorov-Smirnov test and the Shapiro-Wilk test were performed. In order to be considered as normally distributed, Pallant (2001) suggests that the *p-value* produced in these tests must be non-significant ($p\text{-value} > 0.05$); a significant *p-value* suggests that the assumption of normality is violated. However, even though the relationship between the dependent variable and the independent variables is not linear, there should be no problem, as long as the standard deviation of the dependent variable is higher than the standard deviations of the residual (Hair et al. 2006). In addition, according to the central limit theorem, if sample size $n > 30$ this should not be a problem and the parametric test can still be used (Field 2012).

(ii) Univariate and Bivariate Analyses

Histograms, bar charts, scatter diagrams, box plots etc. are used to understand the data's characteristics. This process is crucial before further tests can be employed. It is always prudent to obtain frequency distributions - such as the mean, the median, the standard deviation, the range and the variance - for each variable. Examining the central tendency and how the data is dispersed or clustered provides a good place to start data exploration. This stage is what Sekaran (2003) calls the *feel for data*. These analyses are helpful in identifying whether the data set is skewed, and also allows the detection of odd patterns of variables that may suffer from data key-in errors or missing values.

In addition, for the categorical variables, the Chi-square test of independence should be applied. This test is used to examine the relationship between the categorical variables (Tabachnick and Fidell 2007). Depending on the type of data distribution, the parametric (t-test analysis) or non-parametric test (Mann-Whitney U Test) will also be explored for application to any suitable variables in order to explain their relationship.

5.7.2.2 Missing Value Analysis

After all the data has been collected, any missing values will be identified. The sources for the missing data were inspected again to determine the reasons for the absence of data. Other alternatives were then explored, for instance financial data could be manually calculated from a company's financial statement presented in the annual reports, instead of being retrieving from the Datastream or Thomson One Banker. By using the best information available, a few justifications have been made for the categorical data which has not yet been categorised due to ambiguous information. A few estimations like averaging have been applied for any suitable missing data as previously explained for foreign equity ownership data (see Section 5.4.2.4 Sample Selection).

For the corporate governance data, the pattern for certain variables in the related companies was seriously scrutinised in order to ensure that the values accorded to the missing data were acceptable and reliable. For example, even though there was a lack of information about the number of independent directors in the year 2000, the percentage of independent directors out of the board size was estimated based on the pattern that the companies have shown for that data in the years 2001 onwards. This was carried out when the number of the board size is equal or only slightly different. This method of treating the missing data is also applied to the other variables of corporate governance. In entering the missing value into the statistical software, dot (.) is applied. This is well recognised and can be read as 'missing value' in the STATA software.

5.7.2.3 Multicollinearity Test

Correlation analysis is part descriptive statistics and is employed to measure the degree of association between two variables and this may vary from -1 to +1. This analysis is also conducted to prevent highly associated variables being fitted in the same model. High multicollinearity causes estimated regression coefficients to become unreliable and unstable. The accurate estimation of the coefficient of the true

model will be difficult to estimate and the small changes that occur in the model might change the result dramatically (Hamilton 2003).

The existence of multicollinearity must be treated by conducting suitable tests. A few analyses can be used: Pearson's product-moment correlation coefficient test, Kendall's correlation coefficient and Spearman's rank correlation coefficient. Additional analysis which can be used to examine the effect of multicollinearity is the Variance Inflation Factor (VIF).

However, Kendall's correlation coefficient and Spearman's rank correlation coefficient behave in almost the same way and can substitute for each other. Pearson's coefficient is a popular analysis for testing the multicollinearity issue between variables and it measures the degree to which the relationship conforms to a straight line. Unlike Pearson, Kendall's coefficient measurement is based on whether the relationship is always increasing or decreasing. VIF, on the other hand, shows how the coefficient's variance and the standard errors of other variables increase due to the inclusion of the variable (Hamilton 2003).

This study is interested in measuring interval scale data and linear relationships. Thus, Pearson's product-moment correlation coefficient test is employed. However, depending on the normality test result, Spearman's rank correlation coefficient may be employed. The other multicollinearity test used in this study is VIF. Gujarati and Porter (2009) suggest that a high pairwise correlation coefficient between two regressors in excess of 0.8 (Bryman and Cramer 1990), indicates an issue of multicollinearity, and a correlation that is above 0.9 indicates a serious problem (Hair et al. 2006; Pallant 2001). For VIF, the variable is said to be highly correlated if the VIF of the variable exceeds 10 (Gujarati 2003; Hair et al. 2006); it is suggested by a few scholars (see Hair et al. 2006; Wooldridge 2003) that one of the collinear variables should be dropped in order to solve the problem.

5.7.3 Multivariate Analysis

This section discusses the multivariate analysis for this study. This analysis, which involves several variables at a time, is in contrast with the previous analyses, univariate and bivariate; a discussion of these can be found in Section 5.7.2.1 (ii). According to Sekaran (2003: 407), multivariate analysis, in brief, examines the relationships of the dependent variable and several independent variables in one regression model. There are four regression models constructed in this study (see 5.7.4.1 Research Model and Measurement).

However, before each model can be tested, diagnostic tests must be implemented to verify whether the assumptions of multiple regressions hold true. Thus, misleading results can be avoided. The diagnostic tests start with checking outliers, normality, multicollinearity, heteroscedasticity and the autocorrelation test. A discussion of normality and multicollinearity has been given in previous sections (see Section 5.7.2.1 (i) and 5.7.2.3). Thus, this section will only discuss the remaining three items.

5.7.3.1 Outliers

Outliers in statistics are defined as observation points that are distant from the other observations (Grubbs 1969). They have unique characteristics which can be differentiated from other observations (Hair et al. 2006). The outliers may exist in any distribution by chance, or be due to the variability in measurement, or it could be that the population itself has a heavy tailed distribution. For each case, different treatments are applied.

For the first type of outliers, they may be discarded from the population, or the statistical analyses that are robust to outliers are used. Capable estimators which can cope with the outliers are said to be robust, such as the median compared to the mean. For the latter case, precaution should be taken where the statistical tools assuming a normal distribution are selected to be used.

In order to obtain a clear picture of the potential outliers, several graphs should be used, such as the histogram box plot and the stem and leaf plot. In this study, the outliers can be detected by identifying an influential observation that may significantly change the estimate of the coefficient when the observation is dropped.

The decision to retain or drop the outlier from the sample depends on its impact on the coefficient of multiple regression analysis. Multiple regression analysis is run with and without the outliers, and the results are then compared. Without significant differences, the outliers should be retained to ensure the generalisation of the entire population. By not deleting the outliers, the robust STATA command will be used and it will treat the outliers with less weight.

Another alternative is winsorising, which is the transformation of statistics by limiting the extreme values in the statistical data to reduce the effect of outliers. Using the trimmed technique, the extreme values are discarded, but in the winsorising technique the extreme values are replaced by a certain percentile (the trimmed minimum and maximum). This command can be executed in the STATA.

5.7.3.2 Heteroscedasticity

Heteroscedasticity is the opposite of homoscedasticity. In regression analysis, the presence of heteroscedasticity is one of the major concerns which need to be addressed. For multiple regressions, the homoscedasticity assumption states that the variance of the unobservable error, u , conditional on the explanatory variable, is constant (Wooldridge 2009: 264). This assumption is violated whenever the variance of error is not constant over the sample of observation.

Heteroscedasticity does not cause the ordinary least squares (OLS) coefficient estimates to be biased. However, OLS no longer has the smallest variance among linear unbiased estimators in the presence of heteroscedasticity. If the heteroscedasticity problem is not addressed, it may also result in higher t and F values,

which may lead to the rejection of the null hypothesis even though otherwise it should have happened (Cheng, Hossain and Law 2001).

There are several methods to test the presence of heteroscedasticity: White General Heteroscedasticity, Breuch-Pagan Godfrey Test, Part Test or Glejser Test (Gujarati 2003; Wooldridge 2003; Green 2003). The null hypothesis that the variance of the residual is homogeneous will be rejected if the value of $p < 0.05$.

Where the existence of heteroscedasticity is proved, there are four common corrections suggested: i) view logged data, ii) use a different specification for the model, iii) apply a weighted least square estimation method, and iv) use the Heteroscedasticity Consistent - Standard Error (HCSE) technique (Hair et al. 2006; Gujarati 2003; Cheng et al. 2001).

5.7.3.3 Autocorrelation

In general, it is claimed that what happened in the past is the best predictor of what will happen in the future or, put statistically, what happens in time t will predict what is likely to happen in time $t + 1$. However, in order to apply the OLS regression model, no serial correlation or autocorrelation is one of its main assumptions. This assumption states that the conditional on x is that the errors in two different time periods are uncorrelated, $\text{Corr}(u_t, u_s | \mathbf{x}) = 0$ or $\text{Corr}(u_t, u_s) = 0$, for all $t \neq s$. In the case of the presence of autocorrelation, it does not bias the coefficient estimates but the standard error tends to be underestimated. Thus, the results produced are less efficient (Drukker 2003). If this assumption is violated, it is believed that the errors suffer serial correlation because they are related across time (Wooldridge 2009).

In this study, the Wooldridge test, derived from Wooldridge (2002), will be applied to detect serial correlation in random and fixed effect models. This test is recommended because it is easy to implement and works well under general conditions (Drukker 2003). For the regression model with the autocorrelation problem, it needs to be transformed; thus, the error term in the transformed model is serially independent.

This process is known as the generalised least square (GLS) and it is suitable for the large observation.

5.7.4 Model Estimation: OLS vs GLS

There are considerations about whether to use the OLS or the GLS for the model estimation. After all the assumptions have been scrutinised and the violations of any assumptions have been detected, the selection of the best method to generalise the model would be decided.

The OLS method minimises the sum of the squared vertical distance, between the observed response in the dataset and the responses predicted by the linear approximation. Using this technique, all the errors are given equal weight, regardless of how much closer they are to the regression function. Thus, if the problem of heteroscedasticity prevails, then OLS is not able to remedy the problem. Therefore, this method requires few assumptions to hold true: issues of multicollinearity, heteroscedasticity, normality and autocorrelation will determine the efficiency of the estimator.

GLS on the other hand is considered as the proper estimation method when it effectively standardises the observations (Baltagi 2008; Greene 2003). It is applied in the presence of heteroscedasticity or in the presence of the serial-correlation problem. Gujarati (2003) stated that GLS is capable of producing the estimator - *Best Linear Unbiased Estimators* (BLUE), and in this case OLS is not reliable as the result is not efficient or may even give misleading inferences. GLS is also suitable for a dataset with a normality problem, and it is claimed as the OLS on the transformed variables that satisfy the standard least square assumptions (*ibid*; p. 396). Between these two methods, the most suitable method will be applied to the dataset based on the assumptions and dataset characteristics.

5.7.4.1 Research Model and Measurement

The full regression model is illustrated by the following basic specification:

$$FEO = f(\text{corporate governance variables, control variables})$$

Next, four main regression models were constructed - beginning with the basic model, followed accordingly by the improved models with the inclusion of the related variables, and finally ending with the full model. The regression models are as follows:

Model 1: Control Variables

$$FEO = b_0 + b_1FSIZE_{it-1} + b_2FAGE_{it-1} + b_3DEBRAT_{it-1} + b_4AUDF_{it-1} + b_5ROE_{it-1} + b_6LIQRAT_{it-1} + b_7DIVYI_{it-1} + b_8FSALE_{it-1} + \alpha_i + \lambda_t + \mu_{it}$$

(Equation 5.1)

Model 2: Board Structure

$$FEO = b_0 + b_1BSIZE_{it-1} + b_2BCOM_{it-1} + b_3DIRFOR_{it-1} + b_4DIRMUL_{it-1} + b_5DIRWOM_{it-1} + b_6DIRPROF_{it-1} + b_7DIRWEST_{it-1} + \text{MODEL 1} + \alpha_i + \lambda_t + \mu_{it}$$

(Equation 5.2)

Model 3: Ownership Structure

$$FEO = b_0 + b_1FCC_{it-1} + b_2MANTOW_{it-1} + b_3INSTOW_{it-1} + \text{MODEL 1} + \alpha_i + \lambda_t + \mu_{it}$$

(Equation 5.3)

Model 4: (Board attributes, ownership structure and control variables) is as follows:

$$FEO = b_0 + b_1BSIZE_{it-1} + b_2BCOM_{it-1} + b_3DIRFOR_{it-1} + b_4DIRMUL_{it-1} + b_5DIRWOM_{it-1} + b_6DIRPROF_{it-1} + b_7DIRWEST_{it-1} + b_8FCC_{it-1} + b_9MANTOW_{it-1} + b_{10}INSTOW_{it-1} + \text{MODEL 1} + \alpha_i + \lambda_t + \mu_{it}$$

(Equation 5.4)

Notes: FEO=Foreign Equity Ownership, BSIZE=Board size, BCOM=Board Compliance, DIRFOR=Foreign Director, DIRMUL=Multiple-directorship, DIRWOM=Woman director, DIRWEST=Western Education director, DIRPROF=Director professional, FCC=Family-Controlled companies, MANTOW=Management ownership, INSTOW=Institutional Ownership, FSIZE=Company's size, FAGE=Company's age, AUDF=Audit firm, ROE=Return on Equity, LIQRAT=Liquidity ratio, DEBRAT=Debt ratio, DIVYI=Dividend yield.

The above models are related to the continuous dependent variable, which is the percentage of FEO. In order to derive a more meaningful explanation, further analysis was performed by transforming the percentage of FEO to the binary variable according to a few specifications which have been discussed in Section 5.6.1 Dependent Variable and Section 6.2.3 Dependent Variable: Distribution and Skewed Data. By transforming this dependent variable, logistic regression is the best analysis option to be run. The detail of logistic regression analysis is presented in the following section.

5.7.5 Logistic Regression Model

Based on the nature of the dependent variable which is binary, logistic regression can be used to measure the relationship between the dichotomous dependent variable and several independent variables (Long 1997; Menard 1995) using probability scores as the predicted values on the dependent variable. Likewise with GLS, logistic regression also applies the maximum likelihood estimation. An explanation of logistic regression begins with an explanation of the logistic function, which always takes on values between zero (0) and one (1).

$$F(t) = \frac{e^t}{e^t + 1} = \frac{1}{1 + e^{-t}}$$

(Equation 5.5)

Equation 5.5 above views t as a linear function of an explanatory variable. The values of t can vary from negative infinity ($-\infty$) to positive infinity ($+\infty$), whereas the output is confined to values between 0 and 1 and hence it is interpreted as a probability. When the $f(t) = -\infty$, the logistic function $f(t)$ equals 0, otherwise $f(t)$ equals 1.

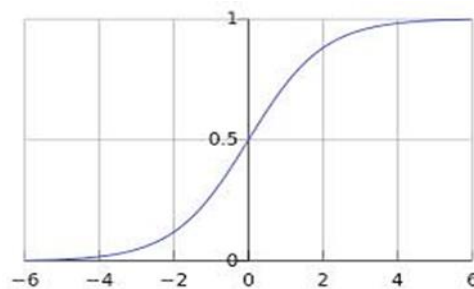


Figure 5.2: Logistic Function Graph

A graph of the logistic function is shown in Figure 5.2 above. The shape derived from this logistic function explains the earlier discussion. If the t value starts at $-\infty$, and moves to the right, then $f(t)$ is close to 0 for a while, but then starts to increase dramatically towards 1, and finally levels off around 1 as t increases towards $+\infty$. This gives the S-shaped picture. It is useful because it can take an input with any value from negative infinity to positive infinity.

The shape of this graph represents the view that the percentage of FEO is categorised as mild if it does not reach 20% of the total equity. Then the value given is 0. It is assumed that the characteristics they preferred in these companies are different from the companies that they have an intention to become seriously involved with (FEO more than 20%). From this analysis, the results are expected to shed some light on the difference between the firms with high FEO and those with low FEO. Thus, the equation for the logistic regression model is as given below:

Model 5: (Board attributes, ownership structure and control variables) is as follows:

$$\text{FEO dummy (1,0)} = b_0 + b_1\text{BSIZE}_{it-1} + b_2\text{BCOM}_{it-1} + b_3\text{DIRFOR}_{it-1} + b_4\text{DIRMUL}_{it-1} + b_5\text{DIRWOM}_{it-1} + b_6\text{DIRPROF}_{it-1} + b_7\text{DIRWEST}_{it-1} + b_8\text{FCC}_{it-1} + b_9\text{MANTOW}_{it-1} + b_{10}\text{INSTOW}_{it-1} + \text{MODEL 1} + \alpha_i + \lambda_t + \mu_{it}$$

(Equation 5.6)

Notes: FEO=Foreign Equity Ownership, BSIZE=Board size, BCOM=Board Compliance, DIRFOR=Foreign Director, DIRMUL=Multiple-directorships, DIRWOM=Woman director, DIRWEST=Western Education director, DIRPROF=Director professional, FCC=Family-Controlled companies, MANTOW=Management ownership, INSTOW=Institutional Ownership, FSIZE=Company's size, FAGE=Company's age, AUDF=Audit firm, ROE=Return on Equity, LIQRAT=Liquidity ratio, DEBRAT=Debt ratio, DIVYI=Dividend yield.

Logistic regression has advantages compared to OLS because it does not require the linear assumption between the dependent variable and the independent variables, the data distribution does not need to be normally distributed, as well as there being no concern with heteroscedasticity. In brief, the characteristics of the data are less emphasised, thus making this analysis easier to perform. The goodness-of-fit³⁴ for the logistic regression model is evaluated using the log-likelihood and the Wald Chi-Square.

The type of data in this study is panel data. Therefore, a panel data model must be specified. For the logistic regression, it can fit random-effect, conditional fixed-effect and population-averaged logit models. The selection of which panel data model to be applied for the model must be based on the characteristics of the explanatory variables. The differences between the panel data models are discussed in Section 5.7.6.1 and 5.7.6.2.

5.7.6 Panel Data Model

For panel data analysis, a natural way to explain the relationship between dependent and independent variables is through two techniques: fixed-effects (FE) estimation and random-effects (RE) estimation. Applying panel data as pooled cross sections is not appropriate because the data is analysed with the strong assumption of its independence, which is not true because the firm's composition is correlated over time. Simply applying OLS to it, is an act that ignores the fact that it is panel data. Ignoring this important fact often misleads due to the existence of unobserved heterogeneity (Baum 2006). Panel data analysis provides ways to deal with unobserved heterogeneity. FE and RE are discussed in the next sections.

³⁴ It is necessary to ascertain how effective the constructed model can be used to predict the relationship between dependent and independent variables. This is referred as *goodness-of-fit*.

5.7.6.1 Fixed-effects Model

A fixed-effects (FE) model would be used if the objective of the study is to analyse the impact of variables that vary over time. It would explore the relationship between the predictor and outcome variables within an entity. Each entity has its own characteristics which may or may not influence the predictor variables. Thus, when using FE, the assumption that something within the entity may impact or bias the predictors should be applied. This individual bias must be controlled. FE will remove the effect of the time-invariant characteristics from the predictor variables and the net effect can then be assessed.

Another important assumption of FE is that time-invariant characteristics are unique to the entity and should not be correlated with the characteristics of another entity. Therefore, the entity's error term and the constant should not be correlated with the others. This model relaxes the assumption that the regression parameters are constant over time and space (Baum 2006) when it allows each cross-sectional unit to have its own intercept while the slope of the coefficient remains constant across companies. If the error terms are correlated then the FE model is not suitable since inferences may not be correlated. The equation for the FE model is:

$$Y_{it} = \beta_1 X_{it} + \beta_2 X_{it} + \dots + \beta_n X_{it} + \alpha_i + \mu_{it}$$

That is, i denotes the firms and t denotes time. Therefore, Y_{it} is the dependent variable of pooling N cross-sectional observations and T time series observations, and X_{it} are the independent variables of pooling N cross-sectional observations and T time series observations. β_j is the coefficient for the independent variable, α_i ($i=1\dots n$) is the unknown intercept for each entity (n entity-specific intercept), and μ_i is the error term.

5.7.6.2 Random-effects Model

Unlike the fixed-effects model, the random-effects (RE) model assumes that the variations across entities are random and uncorrelated with the predictors included in the model (Greene 2008). RE should be used when there is reason to believe that

differences across entities have some influence on the dependent variable. The equation for the RE model is:

$$Y_{it} = \beta_1 X_{it} + \beta_2 X_{it} + \beta_3 X_{it} + \dots + \beta_n X_{it} + \alpha + \mu_{it} + \varepsilon_{it}$$

Comparing the two models, the difference in the RE equation is that time invariant variables can be included, while in the FE equation these variables are absorbed by the intercept. The individual heterogeneity is captured in the composite-error term (a combination of the individual-level effect and the disturbance time) (Baum 2006).

In order to decide between the models, the characteristics of the data have to be scrutinised. The Hausman test can be run as an option to find the best model to suit the panel data in this study (see Section 7.3.3 Hausman Test for further elaboration). However, only after the real tests have been run, can the result be discussed comprehensively.

5.7.7 Robustness Analysis

5.7.7.1 The Generalised Method of Moments (GMM)

Other than those discussed above, there are various statistical methods available to analyse the data-set of interest. These analyses are needed to estimate the parameter of the data. However, in obtaining this estimation, most of these analyses require additional restrictions, restricted proportions, in order to make additional assumptions which are not unjustified by the economic theory. The risk that might occur is the validity issue of the result, which may be undermined.

Most economic data is dynamic by nature. Considering this, it is important that the statistical method chosen fits well with the exact information that has been gathered. Most of the time restrictions implied by the economic theory take the form of the population moment condition. Thus, the GMM is applied in this condition. GMM is a statistical method that combines observed economic data with the information in the population moment condition to produce an estimate of the unknown parameters. The

method was developed by Lars Peter Hansen in 1982 and is known to be consistent, asymptotically normal, and efficient in the class of all estimators.

In the dynamic model, the lagged dependent variable is included as a regressor. The standard form of the dynamic model is as follows:

$$Y_{it} = \lambda \cdot Y_{it-1} + \alpha_i + \varepsilon_{it}$$

In the panel data model where T is small, both fixed and random effects estimators of λ are biased of order $1/T$. In order to eliminate the bias, the value of $T \rightarrow \infty$. In panel data, the T value is considered as small, and serious bias may be encountered if it is less than 10. However, Nickell (1981) suggests that the T value is still considered as small if it is less than 20. In the current study, the T value is 12 and it is under the considerable range of a small value. Therefore, GMM is used in an attempt to eliminate the bias.

This method requires that a certain number of moment conditions get specified for the model. These moment conditions are a function of the model parameters and the data, such that their expectation is zero (0) at the true values of the parameters. The GMM method then minimises a certain norm of the sample averages of the moment conditions. These moment conditions state that the regressors should be uncorrelated with the errors. GMM models tend to be robust with respect to heteroscedasticity and non-normality. Besides this, GMM is a suitable analysis technique for a dataset with endogeneity (see Section 5.7.7.2 Endogeneity for further explanation).

To run GMM, a suitable estimator should be selected. There are a few estimators to be considered: Anderson and Hsiao (1982), Arellano and Bond (1991), Ahn and Schmidt (1995) and Blundell and Bond (1998) estimators. Considering the weakness and the strengths of each of the instruments, the Arellano and Bond (1991) estimator is finally chosen for this study. The Anderson and Hsiao (1981) estimator, for example, does not deal with the residual autocorrelation problem, and in practice it drops a lot of observations. The Arellano and Bond (1991) estimator, one of the popular estimators, has proved to be more efficient than the Anderson and Hsiao (1981) estimator. It uses lagged values of y_{it} as instruments. Using this estimator, the observations for each

individual are stacked together and equations are formed. However, one of its weaknesses is its limitation in using a different set of instruments for different time points. Besides this, many instruments are used as an additional instrument is added every time for the new forward period. On the other hand, the Anh and Schmidt (1995) estimator proposes additional moment conditions, (T-2). Nonetheless, amongst these, the Arellano and Bond (1991) estimator is still considered helpful for the current study.

In order to run the GMM analysis, a few practical guidelines have to be followed: i) choose a reasonable maximum number of lags to be used as instruments, ii) the choice must be made based on theory, the extant literature and computer capacity, and iii) it is advisable to report results from more than one estimator, especially if persistence is high. Further, there are two important relative tests to be performed in GMM estimation: i) the Hansen-Sargan *J*-test (Sargan 1958; Hansen 1982) for over-identifying restrictions - this tests the validity of the moment conditions and ii) the Residual autocorrelation test, in order to ensure that the second order correlation is zero.

In theory, it is relatively complicated. However, practically, STATA helps to ease the use of GMM.

5.7.7.2 Endogeneity

Corporate governance studies are likely to be plagued with endogeneity issue (Bhagat and Jefferis 2002). To put it theoretically, corporate governance practices in a company might be influenced by the level of FEO, rather than the other way round. For example, the higher level of foreign ownership in a company empowers them to give pressure to management to appoint more outside director(s) on board, appoint foreign director(s), hire more directors with preferred background such as directors with professional qualification(s) and directors with Western educational background to sit on the board in order to safeguard their interests in a company. However, in this study, the relationships were hypothesised to emerge from the inverse direction. The

presence of foreign director(s) on the board and other corporate governance variables are argued to influence the level of FEO in a company and not otherwise.

To put it statistically, concerns regarding endogeneity might emerge because of omitted unobservable variable firm characteristics. Omitted variables that affect both the selection of corporate governance variables and the level of firm FEO could lead to spurious correlations between the two variables. It is plausible, for example that some firms are more progressive than others (Adams and Ferreira 2009), so they have better governance as well as high FEO level. In the context of this study, the examined relationships might potentially suffer from reverse causality.

To explore this potential endogeneity issue, the previous literature has been examined. Therefore, this study follows recent literature, and replaces the value of independent variables in each given observation by the value of independent variables in the previous year of the sample (denoted by the $t-1$ in the model). The idea is that the independent variables (especially corporate governance variables) in previous years could not have been caused by FEO in subsequent years; thus the possibility of the endogeneity problem is not likely to be significant. This technique should mitigate the concern that FEO level leads to change in corporate governance practice. If a significant relationship is found, the direction of causality is more likely to run from the independent variables to the percentage of foreign ownership in a company rather than vice versa. This kind of method of dealing with the endogeneity issue has been practised in a number of research studies, such as Jiraporn et al. (2009), Cheng (2008), Bebchuk and Cohen (2005) and Peng and Jiang (2010). In addition, for the purposes of this study, GMM analysis has also been utilised to deal with the potential endogeneity issue in the model.

5.8 Summary

This chapter has discussed the procedures involved in collecting data, as well as the research design and research methods pursued for the empirical analyses. It started by discussing the philosophical approach to the study, which is positivism. This spirit of positivism has been applied both in the data collection method and in the statistical

analysis. However, the whole of the processes involved in obtaining the required data and conducting the necessary analyses are not necessarily easy.

The biggest challenge in this part of the study is the consumption of time in the data collection process. Corporate governance data for Malaysian companies is not available in any database, making it difficult to gather. Thus, it was collected one by one, by reading line by line in the related sections of the companies' annual reports. In addition, data was also collected from a number of sources, such as Datastream, Thompson One Banker, companies' websites, other related web sites, etc. The initial plan for conducting interviews was discarded and the rationale for this has been explained. Even though it is obvious that time is the main obstacle at this stage, eventually, the final sample was derived. Meticulous steps have been taken to ensure the representativeness of the sample, and it has not been compromised in any way.

In the data analysis process, a few models were constructed, referring to the category of the variables, and the last model constituted all the variables. The main analysis is still determining between OLS or GLS, depending on the data characteristics which will be determined after conducting a few analyses, as discussed in this chapter. For the robustness tests, a few other analyses, logistic regression and GMM were planned to be utilised to strengthen the results. These analyses were run using statistical software: SPSS and STATA. The next two chapters - Chapter 6: Results and Descriptive Analyses and Chapter 7: Multivariate Results and Analyses - are devoted only to a discussion of the results yielded by these analyses.

CHAPTER 6

RESULTS AND DESCRIPTIVE ANALYSES

6.1 Introduction

The previous chapter dealt with data and specified the research design employed in this study. This section aims to explore the main features of the data collected by describing its characteristics quantitatively. The method of explaining it is twofold: univariate and bivariate. Section 6.2, Descriptive Statistics, starts with the outlier results and continues with univariate and bivariate analysis for dependent, independent and control variables. Univariate analysis is the simplest form of quantitative analysis, describing the single variable in terms of the applicable unit of analysis: frequency distribution, central tendency and statistical dispersion. Bivariate analysis, on the other hand, describes the relationship between pairs of variables (in this chapter, two tests were run; Chi-Square and Mann-Whitney). Bivariate analysis (correlation test) is continued in Chapter 7 before running multivariate tests. The final part of this chapter, Section 6.3, provides a summary and conclusion.

6.2 Descriptive Statistics

In order to explain the variation of the dependent variable (FEO), there are 10 independent variables and eight control variables analysed (see Table 5.5 for independent variables and Table 5.6 for control variables). Six of the independent variables and seven of the control variables are continuous variables, while the remaining are categorical variables. Continuous variables are briefly defined as those variables where the data is of an infinite type, where the value can change continuously (for example, height, weight, distance, etc.). Categorical data, in contrast, is data which falls into groups or categories (for example, 1 for woman, 0 for man). This chapter starts with the checking of outliers.

6.2.1 Outliers

Before further analyses were run, the existence of potential outliers was identified in the distribution using SPSS software. The detailed elaboration of outliers can be referenced from Section 5.7.3.1 Outliers. Several graphs such as the histogram, box plot, and stem and leaf plot were utilised to find the observations which can be classified as outliers. From the histograms, the tails of the distribution were examined to check for any data points falling away as extremes. Then the box plots were inspected to see whether SPSS identifies any outliers. The outliers were displayed as little circles with an ID number attached. The highest and lowest extreme values for the related variables were also generated in the extreme value table with the ID number. This helps to identify the case that has the outlying values.

After the outliers and their ID numbers were identified, every case was referred back to check whether these outliers arose due to a tendency in measurement error or because of the characteristics of the sample itself which has a heavy tailed distribution. By confirming that there was no variability in measurement, the outliers were not discarded from the total observations. As a precautionary step, the statistical analyses that are robust to outliers were used. However, for the latter case of data distribution where the statistical tools with a normal distribution were assumed, more suggested actions would be taken (see Section 6.2.4.2 on winsorising).

6.2.2 Descriptive Data

Entering the dataset of 1836 observations from 153 companies for the time period of 12 years into the STATA, was recognised by the system as strongly balanced data. This refers to the fact that all the companies have complete data for all the years under observation. From the observation, throughout the system there was no sign of missing data. Thus, there is no concern over the issue of missing data for this study as it was well treated during the data collection process (see Section 5.7.2.2 Missing Value Analysis).

In this study, independent variables were divided into three categories: (i) *board characteristics* (ii) *directors' attributes* and (iii) *ownership structure*. The static panel was adopted, where the same companies were selected over a 12 year period.

This section starts by exploring data characteristics and distributions by obtaining frequency distributions such as the mean, median, standard deviation, range and variance for each variable.

6.2.3 Dependent Variable: Distribution and Skewed Data

The dependent variable, Foreign Equity Ownership (FEO) in percentage is scrutinised in two ways in this section: distribution and the skewed data.

Table 6.1: Data Distribution for the Dependent Variable (FEO)

	Mean	Median	SD	Minimum	Maximum	Skewness	Kurtosis	Sig.
Overall	10.25	5.37	13.18	0.01	87.00	2.63	11.34	
Between			12.11	0.47	66.94			
Within			5.30	-27.03	83.52			
<i>Kolmogorov-Smirnov test</i>								<i>0.0000</i>
<i>Shapiro-Wilk test</i>								<i>0.0000</i>

Table 6.1 presents the distribution of data for the dependent variable, FEO. It reports the overall mean, variation in the overall mean, as well as the variation between and within the firms over the period. All firms in the sample have foreign ownership in their companies, and the range of FEO in Malaysian companies varies from 0.01% to 87% with a mean value of 10.25% and a median value of 5.37%. The overall average distance to the mean is between +/- 13.18%, which is shown by the standard deviation (SD) from the table. It shows the variation over the period and across the sample size.

The high skewness and kurtosis values portrayed in the table suggest that the dependent variable is not normally distributed. This is also supported by the result of Kolmogorov-Smirnov and Shapiro-Wilk tests with p-value less than 0.05. The results indicate that the null hypothesis was rejected and the normal distribution assumption has been violated. In order to overcome this issue, the percentage of FEO was first

transformed to the natural logarithm. However, because the percentage of FEO comprises many values that are close to zero (e.g. 0.3, 0.17, etc.), the natural logarithm of these values produces negative values. Theoretically, this would be incorrect because the ownership in companies cannot be negative. Therefore, the approach of applying the natural logarithm to the FEO is unsuited to the present study and was, therefore, not used.

Previous studies (Dahlquist and Robertsson 2001; Kim et al. 2010) which are close to the current study were reviewed. However, they did not treat the issue of normality. Therefore, during the analysis process, prudent steps would be applied in order to test the data. Suitable analyses that do not require the assumption of normality would be given priority. Nevertheless, the results that are produced from the tests with the normality assumption would be acknowledged for the high skewness and kurtosis which may flaw the estimator for the model. Nevertheless, according to the central limit theorem, if sample size $n > 30$ this should be not a problem and parametric tests can still be used (Field 2012).

To enrich the findings, a further step was taken. Examining only the percentage of foreign equity ownership is inadequate because the results will only show the variables that that varies in relation to the vicissitudes of FEO percentage. Thus, in order to make it more meaningful and represent the characteristics of foreign investors in Malaysia, FEO in data percentage was changed to a dummy variable where 0 implies FEO less than 20% and 1 represents FEO 20% and above. 20% is used as a benchmark to differentiate high and low FEO. This is because 20% ownership in Malaysia implies significant influences³⁵ for the investor, being the power to participate in the financial and operating policy decisions in the companies.

³⁵Referring to FRS 128(5) “If an entity holds, directly or indirectly (e.g. through subsidiaries), 20 per cent or more of the voting power of the investee, it is presumed that the entity has significant influence, unless it can be clearly demonstrated that this is not the case. Conversely, if the entity holds, directly or indirectly (e.g. through subsidiaries), less than 20 per cent of the voting power of the investee, it is presumed that the entity does not have significant influence, unless such influence can be clearly demonstrated. A substantial or majority

In Malaysia, when one company acquires 20% to 50% of shares in another company it is referred as its associate³⁶ company. In this case, 20% is applied to the individual, a group or foreign company which invests in Malaysian companies. This value is also approximately in agreement with Sarkar and Sarkar (2000), where they use 25% ownership in a company as a cut-off point for the shareholders to have a significant influence on the company's value.

By differentiating the significance as 20% of FEO and below, the study would be able to identify the significance variable that is related to the high and low proportion of foreign investment. With this binary classification, it is possible to apply logistic regression.

6.2.4 Continuous Independent and Control Variables

6.2.4.1 Distribution and Skewed Data

The data distribution for the continuous variables is presented in Table 6.2. The results from the normality tests (Kolmogorov-Smirnov and Shapiro-Wilk) show that all the independent continuous data is not normally distributed. However, there are certain variables that are within the normality threshold from the reading of skewness and kurtosis (skewness +/-1.96 and kurtosis +/-3.29) as suggested by Field (2005).

ownership by another investor does not necessarily preclude an entity from having significant influence.”

³⁶ An associate is an “entity over which the investor has significant influence.” (FRS 128).

Table 6.2: Data Distribution for the Continuous Independent and Control Variables

Variable	Mean	Median	SD	Minimum	Maximum	Skewness	Kurtosis	Kolmogorov-Smirnov (Sig)	Shapiro-Wilk Test (Sig)
Independent Variables:									
BSIZE	7.43	7.00	1.71	3.00	13.00	0.346	3.035	0.000	0.000
BOUT	41.84	40.00	12.07	14.29	80.00	0.715	3.473	0.000	0.000
DIRFOR	4.37	0.00	11.59	0.00	80.00	3.485	16.411	0.000	0.000
DIRMUL	9.32	6.00	9.26	0.00	55.00	1.846	7.696	0.000	0.000
DIRWOM	7.09	0.00	9.89	0.00	40.00	1.174	3.486	0.000	0.000
DIRWEST	46.99	44.44	23.16	0.00	100.00	0.153	2.675	0.000	0.004
DIRPROF	20.06	16.67	13.15	0.00	62.50	0.785	3.565	0.000	0.000
MANTOW	29.89	30.63	21.14	0.00	90.66	0.058	1.996	0.000	0.000
FAMTOW	26.26	28.46	22.10	0.00	89.63	0.116	1.685	0.000	0.000
INSTOW	9.87	4.74	13.71	0.00	71.33	2.256	8.832	0.000	0.000
Control Variables:									
FSIZE	19.63	19.56	1.31	16.22	24.13	0.421	3.505	0.000	0.000
FAGE	30.46	29.00	16.05	5.00	89.00	1.149	5.176	0.000	0.000
DEBRAT	0.45	0.42	0.31	0.01	2.16	1.836	9.591	0.000	0.000
ROE	0.03	0.05	0.38	-2.46	2.21	-1.141	23.621	0.000	0.000
LIQRAT	2.91	1.59	4.22	0.10	33.38	4.124	24.016	0.000	0.000
FSALE	11.89	0.00	21.69	0.00	97.60	2.147	7.152	0.000	0.000
DIVYI	2.02	1.07	2.54	0.00	13.07	1.544	5.640	0.000	0.000

Notes: BSIZE=Board size, BOUT=Outside Director, DIRFOR=Foreign Director, DIRMUL= Multiple-directorships, DIRWOM=Woman director, DIRWEST=Western Education director, DIRPROF=Director with professional qualification, MANTOW=Management ownership, FAMTOW=Family total ownership, INSTOW=Institutional Ownership, FAGE=Firm's age, FSIZE=Firm's size, ROE=Return on Equity, LIQRAT=Liquidity ratio, DEBRAT=Debt ratio, FSALE=Foreign Sale, DIVYI=Dividend yield.

From Table 6.2 above, the means of independent variables - board size (BSIZE), outside director (BOUT), Western education director (DIRWEST), managerial ownership (MANTOW) - are positively skewed, with only slight differences compared with the medians. This can be proved by the reading of their skewness and kurtosis values which are still under the mentioned threshold values, even though the normality tests performed did not verify them as normally distributed.

In general, the average number of directors on the board for Malaysian companies is 7, with the maximum number being 13, and the average percentage of outside directors on the board is 41.84%. This is higher than that suggested in the Malaysian Code (2000): 33.33% or more than 1/3 from the total number of directors. The percentage of directors with a Western educational background is almost half of the board in aligning with the average number of foreign directors which is 4.37.

Managerial ownership and family ownership (direct and indirect) is close to 30% of the Malaysian companies. Institutional ownership (direct) is only recorded averagely at 9.87%. However, the maximum value is apparently high, which registers at 71.33%.

The means that directors with a professional qualification (DIRPROF), multiple-directorships (DIRMUL), foreign directorship (DIRFOR) and institutional ownership (INSTOW) are higher than their medians with a wide distribution (refer to their SD in the table). The distribution of the number of multiple-directorships held is given as: 7.4% of the directors in the sample hold no other directorship, 7.5% hold at least one additional directorship and 48% hold more than 6 outside directorships at a time. The highest number of DIRMUL is recorded at 55 seats, which is far too large.

The continuous control variables can be found from the second part of the table. On average, the companies' firm size ranges between 16.22 to 24.13, with a mean of 19.63 after the total assets of the companies were recomputed as the natural log. The average of firms' age is 30.46 years, commensurate with the conditions imposed to be eligible as the sample element (see Section 5.4.2.2 (i) The Listing Year). The mean for the debt ratio is registered at 0.45, while ROE and liquidity ratio are 0.03 and 2.91 respectively. These are the indications that the overall companies in the sample are financially strong and stable. In other words, these companies' total assets are almost double their total liabilities with higher liquidity assets to pay for the debt.

Foreign sales (FSALE) is used as a proxy for the company to be known globally, and dividend yield (DIVYI) is a ratio that shows how much a company pays out in dividend each year relative to its share price. Their means are 11.89% and 2.02% respectively, which are considered as good. Generally, well-established companies tend to have a higher value of dividend yields, compared to the young and growth-oriented companies, while most of the small growing companies rarely document this value as they do not pay out dividends³⁷.

³⁷http://www.investorwords.com/1523/dividend_yield.html

6.2.4.2 Winsorising

In order to deal with the normality and outlier issue, the technique of winsorisation was utilised. Winsorising is a method of censoring data where extreme values are replaced by certain percentiles. In this case, the 99% winsorisation applied where all the data below the 1st percentile was set to the 1st percentile, and the data above the 99th percentile was set to the 99th percentile. Instead of pulling them out of the sample, this technique limits the extreme values in the statistical data to reduce the effect of outliers and simultaneously treat the distribution of many statistics that are heavily influenced by outliers. This command can be executed in STATA.

6.2.4.3 Mann-Whitney Test for the Continuous Variables

Table 6.3: Mann-Whitney Test for the Independent and Control Variables

<i>Variables</i>	<i>Mean</i>		Mann-Whitney (Sig. 2-tailed test)	<i>Overall Mean</i>	<i>Mean</i>		Mann-Whitney (Sig. 2-tailed test)
	FEO = 1 n=251 (13.67%)	FEO = 0 n=1585 (86.33%)			FCC n=1062 (57.84%)	NFCC n=774 (42.16%)	
Independent Variables							
BSIZE	7.87	7.36	0.00	7.43	7.54	7.29	0.002
DIRFOR	14.38	2.79	0.00	4.37	4.25	4.54	0.089
DIRWEST	53.84	45.92	0.00	46.99	44.17	50.87	0.000
DIRWOM	5.01	7.42	0.00	7.09	8.23	5.54	0.000
BOUT	42.72	41.71	0.16	41.84	40.10	44.25	0.000
DIRMUL	13.13	8.72	0.00	9.32	8.40	10.60	0.000
DIRPROF	22.74	19.64	0.00	20.06	18.71	21.92	0.000
FAMTOW	24.80	26.49	0.67	26.26	41.78	4.95	0.000
MANTOW	28.05	30.18	0.53	29.89	41.30	14.23	0.000
INSTOW	10.11	9.83	0.00	9.87	7.49	13.14	0.000
Control Variables							
DEBRAT	0.42	0.46	0.00	0.45	0.45	0.46	0.915
DIVYI	2.27	1.98	0.03	2.02	2.21	1.76	0.000
ROE	0.05	0.03	0.05	0.03	0.04	0.02	0.157
FAGE	36.00	29.00	0.00	30.46	30.82	29.95	0.155
LIQRAT	3.46	2.83	0.00	2.91	2.84	3.02	0.429
FSIZE	20.45	19.50	0.00	19.63	19.63	19.62	0.993
FSALE	17.27	11.04	0.00	11.89	10.55	13.74	0.416

Notes: FEO=Foreign Equity Ownership, FCC=Family-Controlled Companies, NFCC=Non family-controlled companies, BSIZE=Board size, BOUT=Outside Director, DIRFOR=Foreign Director, DIRMUL=Multiple-directorships, DIRWOM=Woman director, DIRWEST=Western Education director, DIRPROF=Director with professional qualification, MANTOW=Management ownership, FAMTOW=Family total ownership, INSTOW=Institutional Ownership, FAGE=Firm's age, FSIZE=Firm's size, AUDF=Audit firm, ROE=Return on Equity, LIQRAT=Liquidity ratio, DEBRAT=Debt ratio, DIVYI=Dividend yield, FSALE=Foreign sales.

The Mann-Whitney test was run to ascertain the relationship between continuous variables. This comparison was made between two independent groups in two categories: high FEO vs low FEO, and family-controlled companies (FCC) vs non family-controlled companies (NFCC). This test is a non-parametric method that makes no distributional assumption, since the earlier distribution test showed that almost all the variables are not normally distributed. From Table 6.3, the results reveal significant differences in 13 of the 17 variables when comparing variables for companies with high FEO and low FEO. While comparisons made for FCC and NFCC show 10 variables to be significantly different. The above table presents the means for both groups in order to make comparisons. Overall means (in *italic* text) are included for extra precaution.

High FEO companies constitute 13.67% of the total 1836 observations. Under this group, for independent variables, other than outside director proportion (BOUT), family ownership (FAMOW) and managerial ownership (MANTOW), the remaining variables have rejected the null hypothesis that the median score is the same for high FEO and low FEO groups. The sig value (p-value) <0.05 rejects H_0 which provides evidence of H_A being true. For the companies with high FEO, the average number of directors on the board is greater than 7 and the Western educational background director is more than half (mean = 53.84%) of the board size. Companies with low FEO show lower values of means for these two variables (7.36 for board size and 45.92% for directors with Western educational background). The difference for both the means is small but statistically significant. Interestingly, the means for the number of female directorships is contradictory; high FEO companies show a lower mean value (mean = 5.0) compared to companies with low FEO (mean = 7.42).

The mean values for multiple-directorships (DIRMUL) and director with professional qualification (DIRPROF) are 13.13% and 22.74%, respectively, providing additional proof that companies with high FEO always have higher percentage values compared to low FEO companies (means = 8.72% and 19.64%, respectively). The Code (2000) requires that boards must have at least one qualified director with an accounting

background. This indicates that the level of compliance among Malaysian companies with the Code (2000) is satisfactory in terms of directors' professional qualification. From the table too, it is interesting to note that the proportion of foreign directors (DIRFOR) on the board is 5 times higher for high FEO companies than for companies with low FEO.

In terms of ownership structure, family and managerial ownership show no evidence of significant difference between the two groups, with the overall means being 25% and 29% respectively. However, in regards to institutional ownership, there is a significant difference in the means of the two groups based on this test. For control variables, all the variables are statistically proven to be different, except ROE which shows a sig-value ($p=0.05$) which is at the borderline.

The second comparison was made between FCC and NFCC. Family-controlled company constitutes 57.84% of 1836 total observations. It provides evidence that all the independent variables except foreign director (DIRFOR) are significantly different between the two groups. It is also interesting to note that the results for this second group (FCC vs NFC) are totally different to the results from the first group (high FEO vs low FEO). All explanatory variables are in an inverse pattern to the first group, except for BSIZE. There are also large differences in the means of FAMTOW and MANTOW (41.78% and 41.30% vs 4.95% and 14.23%, respectively) for the two categories (FCC and NFCC). However, these values were predicted, as the comparison is made between family-controlled company and non-family-controlled company.

In summary, from the values of means presented in Table 6.3, it appears that family-controlled companies favour more female directors, but are lower in the number of foreign directors, Western educational directors, independent directors, multiple-directorships and professional directors on board compared with NFCC. The average of women directorship in FCC is 8, whereas the average in NFCC is approximately 6. Only 44% of the directors have a Western educational background in FCC, while there are more than 50% Western educational directors in NFCC. The remainder of

the means comparisons can be found in Table 6.3. For control variables, all the variables - with exception given to the dividend yield (DIVYI) - are found to be statistically insignificant compared with the opposite group for the differences of their means. There is only 1.76% of dividend yield in NFCC, while there is 2.21% of it in FCC, which is small but statistically significant. The details in terms of means and significant values are shown in the table.

The discussion continues by examining the categorical variables and providing some linkage with the other categorical variables.

6.2.5 Categorical Independent and Control Variables

Table 6.4: Frequency and Percentage of Categorical Variables

	<i>Frequency</i> n=1836	<i>Percent</i> (100%)
High FEO	251	13.67
Low FEO	1,585	86.33
Family controlled (FCC)	1,062	57.84
Non-family controlled (NFCC)	774	42.16
Big Audit Firm	1,084	59.04
Medium/Small Audit Firm	752	40.96
Outside director comply	1,566	85.29
Outside director not-comply	270	14.71
Big board size	1,252	68.19
Small board size	584	31.81
High multiple-directorships	888	48.37
Low multiple-directorships	948	51.63
Women director on board	722	39.32
No-women director on board	1,114	60.68

Notes: FEO=Foreign Equity Ownership, FCC=Family-controlled company, NFCC= Non-Family-Controlled Company

The above table presents the frequency and percentages for the categorical variables in this study. The key variable in this study, foreign equity ownership (FEO), has shown that less than 20% (13.67%) of the Malaysian companies have foreign accumulated equities in their companies of more than 20%. More than 80% of the total number of investments in the companies only managed to attract a slim investment from foreign investors, which is less than 20%. The reason for using 20% as the benchmark to divide the groups is explained in Section 6.2.3 Dependent Variable: Distribution and Skewed Data.

The second variable in the above table shows that the size of sample for family-controlled company is 57.84% (1062) out of the total of 1836 observations. This finding is consistent with the previous studies, which also found that this type of company represented almost 60% of the total PLCs in their studied capital markets (Claessens et al. 2000; Soederberg 2003; World Bank 1999). From the observation for the period of 12 years, out of the 153 companies, 48.36% (74 companies) are pure family-controlled companies. These companies are considered as pure family-controlled companies which fulfilled the stated conditions for 12 years in a row. In contrast, there are 34.64% (53 companies) categorised as non-family-controlled companies which failed to comply with the conditions for 12 years in a row as family-controlled companies. Meanwhile, the other 26 remaining companies in the sample are mixed which fulfilled the conditions in certain years and violated the conditions in the other years. For the clarifications of conditions imposed please see Section 5.6.2 Independent Variables on how to be classified as an FCC.

In general, more than half (59.04%) of the PLCs in Malaysia prefer to hire an established audit firm to audit their accounts as proven in this finding. According to Hossain et al. (1994) and Barako (2004), big audit firms can enhance a firm's reporting quality and simultaneously reflect the image of the company. The percentages shown also represent the general practice both by family-controlled and non-family-controlled companies where almost 60% of the companies from each group tend to choose a recognised audit firm to audit their companies' accounts.

Overall, 1,566 out of the total observations (which represents 85.29%) comply with the suggestion made in the Code (2000) to have at least 1/3 proportion of outside directors from the board size. Board size was divided into two groups, large and small. The mean for this variable is 7. Thus, a board size of 7 and above is considered big and below 7 is considered small. From the table it is shown that only 31.81% of the total observations have less than 7 members on the board of directors. More than half of them (68.19%) prefer to have more than 7 members on the board of directors. A large board size is claimed to be effective in overseeing duties relative to small boards and are capable of monitoring the actions of top management (Zahra and Pearce 1989).

Multiple-directorships refer to the number of other directorships one director can have at the time he/she holds the current directorship under study. After checking the pattern of the sample, 7 is set as the benchmark for high and low multiple-directorship. The percentage shows that there is not much difference between these two groups. However, low directorship is slightly higher than high directorship with only a 3.26% difference. The last categorical variable is women on the board (DIRWOM). From the observation, 60.68% of the samples have no women directors on the board.

Table 6.5: Frequency and Percentage of Companies with Foreign Equity Ownership (FEO) by Industry

<i>Sector</i>	<i>Companies</i>	<i>Percentage (%)</i>
Industrial products	46	30.07
Property	23	15.03
Consumer products	19	12.42
Construction	12	7.84
Technology	3	1.96
Trading/ Service	33	21.57
Plantation	14	9.15
Others	3	1.96
Total	153	100

In the early stage of sample selection, the principle of proportionate stratified random sampling and sector/stratum was followed. The sectors are industrial products, property, consumer products, construction, technology, trading/service plantation and others. For proportionate stratified random sampling according to the sector, please see Table 5.2 in Section 5.4.2.6 (ii) Stratified Random Sampling.

Table 6.5 provides a summary of foreign ownership companies in each industry. These proportions are not based on the amount of ownership, but the volume of companies with the foreign ownership for each industry. The largest category by far is industrial which accounts for about 30.07% of the total sample size. This finding is in agreement with Kim et al. (2010), who find that foreign investors outweigh manufacturing companies in the Korean market. The second, third and fourth largest industries are trading/services, property and consumer products, at about 21.57%, 15.03% and 12.42% respectively. It appears here that foreign investors are not keen on construction companies in Malaysia at only 7.84%. This type of industry is generally shunned by foreign investors (Kim et al. 2010) and one of the reasons could be that the construction industry is typically a local business and, as a consequence, foreign investors know little about the firms in this industry (Dahlquist and Robertsson 2001). It is also clear from the statistic given that technology is not the preferred industry for foreign investors to be involved in, with only a 1.96% proportion.

Table 6.6: Frequency and Percentage of Family and Non-Family Controlled Companies (FCC/NFCC) by Industry

INDUSTRY TYPES	FCC	NFCC	TOTAL
<i>Industrial products</i>	358 64.86	194 35.14	552 100
<i>Property</i>	182 65.94	94 34.06	276 100
<i>Consumer products</i>	137 60.09	91 39.91	228 100
<i>Construction</i>	94 65.28	50 34.72	144 100
<i>Technology</i>	0 0	36 100	36 100
<i>Trading/ Service</i>	211 53.28	185 46.72	396 100
<i>Plantation</i>	74 44.05	94 55.95	168 100
<i>Others</i>	6 16.67	30 83.33	36 100
Total	1062 57.84	774 42.16	1836 100

Table 6.6 above shows the proportion of the sectors according to the category of family (FCC) and non-family controlled companies (NFCCs) in relation to the industry as defined by the Bursa Malaysia. The difference is very obvious in the technology sector where none of the companies from the FCCs group are involved in this industry. Most of the FCCs engage in industrial products, property, consumer products and construction where the percentages show similar patterns with more or less 60%-65%, and NFCCs are more or less 35%-40%.

All the above frequency and percentage information for each variable only depicts the figure derived from the sample observations. No proper association can be claimed from these figures. Table 6.6 tries to define the relationship between industry and

FCCs or NFCCs, but to verify this claim; a valid test should be conducted. For the categorical variables, whether nominal or ordinal, a chi-squared (χ^2) test of association is worthy of application. This test is a hypothesis test of whether there is an association between the attributes. Giving the facts about percentage and frequency between two variables is not sufficient to infer whether the association exists. Thus, a chi-squared (χ^2) is helpful in proving the claim.

6.2.5.1 Pearson Chi-squared Test for the Categorical Independent and Control Variables

Table 6.7: Pearson Chi-squared Test for the Categorical Independent and Control Variables

Variables	Observations				Pearson Chi-squared			
	Total	A		B		A/B	Value	(Sig. 2-tailed test)
		FCC n=1062 (57.84%)	NFCC n= 774 (42.16%)	FEO = 1 n=251 (13.67%)	FEO = 0 n=1585 (86.33%)			
AUDF								
- Big Firms	1084	58%	61%	69%	58%			
- Non-Big Firm	752	42%	39%	31%	42%			
	1836	100%	100%	100%	100%	A	1.815	0.178
						B	10.815	0.001
BCOM								
- Follow	1566	84%	88%	85%	89%			
- Not follow	270	16%	12%	15%	11%			
	1836	100%	100%	100%	100%	A	6.310	0.012
						B	2.922	0.087
INDTY								
- Industrial products	552	33%	25%					
- Property	276	17%	12%					
- Consumer Products	228	13%	12%					
- Construction	144	9%	6%					
- Technology	36	0%	5%					
- Trading/ Services	396	20%	24%					
- Plantation	168	7%	12%					
- Others	36	1%	4%					
	1836	100%	100%					
						A	113.205	0.000
FCC								
-Family company	1062			51%	59%			
-Non-family company	774			49%	41%			
	1836			100%	100%	B	5.590	0.018

Notes: FEO=Foreign Equity Ownership, FCC=Family-Controlled Companies, NFCC=Non-family-controlled companies, AUDF=Audit firm, INDTY=Industry type, BCOM=Outside director compliance.

Table 6.7 above presents the results for the categorical variables, chi-squared (χ^2) test in this study. There are five categorical variables examined to prove their association with two main categorical variables: foreign equity ownership (FEO) and family-controlled companies (FCC). The first categorical variable - audit firm (AUDF) - has proven to have an association (p-value < 0.05) with FEO but not with the FCC. This indicates that there is an association between firms with high FEO or low FEO in choosing an audit firm for their companies, where 69% of high FEO companies choose to hire a big audit firm to audit their accounts compared to only 31% which do not. There is not much difference for low FEO companies where 58% of them hired big audit firms compared to 42% which did not.

The H_A which claims the existence of an association between two categorical variables is accepted for the industry type variables (INDTY) between FCC. This test was not applied to check the association with FEO since the sample was selected based on the principle of the proportionate stratified random sampling according to the sector (see Table 5.2 in Section 5.4.2.6.2 Stratified Random Sampling).

The explanation for the revealed association is that there are types of industries that have been preferred by family-controlled companies. The technology sector is the least attractive sector, where not a single family-controlled company engages in this sector (0%). The earlier discussion has witnessed the preferred sectors of family-controlled companies - industrial products, property, consumer products and construction - where the percentages show similar patterns with more or less 60%-65%, and non-family controlled are more or less 35%-40%.

Outside director compliance is one of the variables which is proved to have an association with the FCC but not with FEO, but at the same time FCC itself has an association with FEO. More than 80% of FCC complies with the Code (2000) to have at least 1/3 or 33.33% of outside directors from the total number of board directors and a similar pattern is shown by the NFCC.

FCC can be associated with the FEO as shown by the p-value < 0.05 from the chi-squared (χ^2) test. Companies with high FEO are associated with FCC less than low FEO companies are associated with FCC (51% vs 59%). The difference, however, is not statistically significant, but the association has been proved by the chi-squared (χ^2) test.

6.3 Summary

This chapter has described the data characteristics quantitatively. They have been explained by referring to the analyses conducted: univariate and bivariate. Suitable analyses and techniques (Mann-Whitney test, Chi-squared test, winsorising etc.) have been run and applied in order for the data to be deciphered before further tests for each model have been applied. Bivariate analysis however is continued in the next chapter -Chapter 7: before multivariate analysis is run.

CHAPTER 7

MULTIVARIATE: RESULTS AND ANALYSES

7.1 Introduction

In Chapter 6, two types of data analysis methods were utilised, univariate and bivariate. The aim of this current chapter is to continue analysing the data by extensively exploring multivariate analyses to explain the association between variables. However, before the main tests were run, a few related tests were performed in order to determine the best type of regression analyses to be applied to the models. Section 7.2 starts with multicollinearity tests, followed by the model specification in Section 7.3. Section 7.4 presents the results of diagnostic tests and Section 7.5 continues with the multivariate tests, beginning with generalised least square (GLS) regression estimation, followed by logistic regression and finally general method of moments (GMM) analysis. The final part, Section 7.6 Summary, concludes this chapter.

7.2 Multicollinearity Tests

In regression models, when two explanatory variables are highly correlated with each other, it is likely that the usefulness of the analysis may be impaired because there is a probability that they may be measuring similar things. Even though the model's predictive power as a whole is unaffected, however, the coefficient estimates of the multiple regressions may change dramatically in response to the small change in the model. Thus, in order to detect the presence of multicollinearity, two tests were run in this study. The following Table 7.1 presents Spearman's³⁸ rank (upper right) and

³⁸ Spearman's coefficient is usually presented for non-parametric data (Field 2005).
Based on the results from the normality tests performed prior to this

Pearson Product-moment³⁹ (lower left) correlation coefficients between the dependent, independent and control variables.

The values from the table can assist in ascertaining the strength of the relationships and determining the direction between the variables. The table also shows that the results of these tests are consistent with only slight differences. Most of the variables are not significant and neither are they highly-correlated. As expected, the exceptions are given to only a few which were predicted earlier.

The correlation of the key dependent variables, are recorded at 0.569 in Spearman's rho test and 0.761 in Pearson Correlation test. This is related to the correlation between the percentage of foreign ownership (FEO) and foreign ownership in dichotomous form (FEO 1/0). This highly correlated relationship was expected as they are related by construction, where the latter variable was derived from the former variable. However, it is not considered as an issue for concern since they are tested in two different models. The results from both tests (Spearman's rho test and Pearson Correlation test) are in mutual agreement for this case and for the rest of the correlation relationships tested in this study. Therefore, afterwards, the discussions of correlation will only refer to the values in Spearman's rho correlation test table as the distributions of almost all variables are not normal (see explanation in footnote number 38).

multicollinearity test, most of the data is not normally distributed. Thus, Spearman's rho was used to ascertain the correlation between variables which are not normally distributed. Spearman's coefficient, like any correlation calculation, is appropriate for both continuous and discrete variables, including ordinal variables. The results from Pearson Product-moment test was attached to cross check the results.

³⁹ Pearson Correlation is not suitable to be performed on the categorical variables because, according to Field (2005: 125), the correlation requires data which are measured at an interval or ratio level for the result to be meaningful.

The highest correlation, -0.771, is documented between liquidity ratio (LIQRAT) and debt ratio (DEBRAT), whilst the second highest correlation value, 0.635, is recorded between managerial ownership (MANTOW) and family-controlled company (FCC). The latter correlation value apparently confirms the earlier prediction that most of the family members sitting on the board are designated as executive director(s) and at the same time they acquire a certain number of company shares. The remaining correlation values in the table are too small to be reported. Overall, the correlation values of all variables are within the suggested threshold values as suggested by Gujarati and Porter (2009: 338) and Hair et al. (2006: 191). The pairwise correlation coefficient between two regressors, which is less than 0.8, is free from the multicollinearity issue. Moreover, utilising panel data analysis methods helps to overcome the multicollinearity issue as well.

As shown in Table 7.1, the tests suggest that FEO has a significant positive relationship at $p < 0.01$ with independent variables, namely BSIZE, BOUT, DIRFOR, DIRMUL, DIRPROF, DIRWEST and INSTOW. FEO also has a positive and significant relationship at $p < 0.01$ with control variables, namely FSIZE, FAGE, AUDF, ROE, LIQRAT, FSALE and DIVYI. FEO dummy reveals the same results with the exception of BSIZE, BOUT and ROE. On the other hand, significant negative relationships at $p < 0.01$ are documented between FEO and FCC, MANTOW, FAMTOW and DEBRAT but FEO dummy only records the negative correlation at $p < 0.01$ with DEBRAT.

In addition, to ascertain the structure of the regression models, a formal detection-tolerance or the Variance Inflation Factor (VIF) was used to measure the multicollinearity among the independent variables. The results of VIF are shown in Table 7.2 (see Section 7.4.1 on VIF test). This test was run before performing regression analysis for each model.

Table 7.1: Spearman and Pearson Correlation

PEARSON PRODUCT-MOMENT CORRELATION COEFFICIENT		SPEARMAN'S RANK CORRELATION COEFFICIENT																				
DV		INDEPENDENT VARIABLES														CONTROL VARIABLES						
	FEO	FEQ(1,0)	FCC	BSIZE	BOUT	BCOM	BFOR	DIRMUL	DIRWOM	DIRPROF	DIRWEST	MANTOW	INSTOW	FSZE	FAGE	DEBRAT	AUDF	ROE	LIQRAT	DVYI	FSALE	
FEO																						
FEQ(1,0)	0.569***																					
FCC	-0.038	-0.055**																				
BSIZE	0.079***	0.064***	0.072***																			
BOUT	0.057***	0.029	-0.166***	-0.254***																		
BCOM	0.036	0.040*	-0.059**	-0.121***	0.532***																	
BFOR	0.436***	0.344***	-0.012	0.016	0.045*	-0.002																
DIRMUL	0.233***	0.163***	-0.114***	0.317***	0.075***	0.055**	0.193***															
DIRWOM	-0.073***	-0.084***	0.134***	0.017	-0.018	0.041*	-0.137***	-0.135***														
DIRPROF	0.052*	0.081***	-0.122***	-0.171***	0.181***	0.110***	-0.001	0.036	0.000													
DIRWEST	0.156***	0.118***	-0.143***	0.030	0.163***	0.117***	0.015	0.289***	0.074***	0.066***												
MANTOW	0.007	-0.035	0.632***	0.024	-0.154***	-0.108***	0.055**	-0.090***	0.120***	-0.096***	-0.202***											
INSTOW	0.005	0.007	-0.203***	0.172	-0.060***	0.029	-0.044*	0.099***	-0.045*	-0.027	0.087***	-0.255***										
FSZE	0.338***	0.252***	0.006	0.334***	0.065***	0.060**	0.044*	0.475***	0.002	-0.068***	0.266***	-0.008	0.212***									
FAGE	0.177***	0.133***	0.026	-0.013	0.123***	0.053**	0.156***	0.189***	-0.020	0.019	0.160***	-0.043*	-0.083***	0.242***								
DEBRAT	-0.101***	-0.046*	-0.037	-0.037	0.007	-0.050**	-0.106***	-0.055**	-0.031	0.022	0.112***	-0.106***	0.008	-0.015	-0.097***							
AUDF	0.154***	0.077***	-0.031	0.020	0.014	0.020	0.107***	0.101***	0.021	0.004	0.155	-0.083***	-0.024	0.099***	0.070***	-0.082***						
ROE	0.030	0.021	-0.012	0.007	0.014	0.012	0.020	0.043*	0.000	0.024	0.049**	0.001	0.005	0.058**	-0.003	-0.001	0.025					
LIQRAT	0.032	0.052**	-0.043*	0.029	0.015	-0.002	0.144***	0.040*	-0.006	-0.027	0.012	-0.011	-0.059**	-0.082***	0.021	-0.269***	0.036	0.009				
DVYI	0.080***	0.039*	0.083***	0.189***	-0.018	0.019	0.116***	0.164***	0.039*	0.003	-0.012	0.140***	0.109***	0.185***	0.009	-0.222***	0.001	0.045*	0.061***			
FSALE	0.170***	0.099***	-0.073***	0.064***	-0.041*	0.029	0.202***	0.141***	0.004	0.049**	0.024	-0.048**	0.092***	0.180***	0.048**	-0.040*	0.035	0.016	0.038	0.082***		

Notes: ***, ** and * denote that the correlations are statistically significant at the 0.01, 0.05 and 0.10, respectively (2-tailed). FEO=Foreign Equity Ownership, FCC=Family-controlled company, BSIZE=Board size, BOUT=Outside Director, BCOM=Outside Director Compliance, DIRFOR=Foreign Director, DIRMUL=Multiple-directorship, DIRWOM=Woman director, DIRPROF=Director with professional qualification, DIRWEST=Western Education director, MANTOW=Management ownership, INSTOW=Institutional Ownership, FSZE=Firm's size, FAGE=Firm's age, DEBRAT=Debt ratio, AUDF=Audit Firm, ROE=Return on Equity, LIQRAT=Liquidity ratio, DIVYI=Dividend yield, FSALE=Foreign Sale.

7.3 Model specifications

Four main regression models (Model 1, Model 2, Model 3 and Model 4) were constructed and an additional model (Model 5) was constructed by switching dependent variable FEO to dummy type. Model 1 was constructed without including corporate governance variables. The aim of this model is to gain a view of how the control variables in this study impact the dependent variable, FEO. Model 2 was developed by incorporating the board of director variables into Model 1. This second model focuses on the understanding of how the board of directors' characteristics influence FEO. Model 3 captures the effect of ownership structure variables, i.e. family-controlled company (FCC), managerial ownership (MANTOW) and institutional ownership (INSTOW) on FEO. Control variables are also included in Model 3. Lastly, Model 4 combines all the variables from Model 1, Model 2 and Model 3 in the full model. For the model specification, please refer to Section 5.7.4.1 Research Model and Measurement. Since panel data is used for the models, the related diagnostic tests are performed. Multivariate tests are then performed by referring to the results from diagnostic tests.

7.4 Panel Data Related Tests

In order to perform multivariate tests for panel data, a few diagnostic tests were run in order to examine whether the underlying statistical assumptions have been violated. The series of diagnostic tests required are discussed in Section 5.7.3 Multivariate Analysis. Therefore, under the current section, only the results of these tests, namely, detection-tolerance (VIF), heteroscedasticity, autocorrelation and Hausman tests are presented. The results will suggest whether the underlying assumptions of ordinary least square (OLS) regression have been followed or violated. Then, based on this information, necessary decisions are taken in order to determine the best analyses to be applied in running the models. Table 7.2 VIF test depicts the first test under the diagnostic tests, followed accordingly by the other related tests. The discussion of the results for each test is given accordingly after the result table.

7.4.1 Variance Inflation Factor (VIF) Test

Table 7.2: VIF Test

<i>Variables</i>	<i>Model 1</i>		<i>Model 2</i>		<i>Model 3</i>		<i>Model 4</i>		<i>Model 5</i>	
	Tolerance	VIF	Tolerance	VIF	Tolerance	VIF	Tolerance	VIF	Tolerance	VIF
<i>FSIZE</i>	0.761	1.31	0.608	1.64	0.726	1.38	0.590	1.69	0.616	1.62
<i>FAGE</i>	0.904	1.11	0.860	1.16	0.877	1.14	0.835	1.20	0.835	1.20
<i>DEBRAT</i>	0.701	1.43	0.670	1.49	0.694	1.44	0.665	1.50	0.670	1.49
<i>ROE</i>	0.984	1.02	0.980	1.02	0.983	1.02	0.978	1.02	0.978	1.02
<i>LIQRAT</i>	0.734	1.36	0.689	1.45	0.730	1.37	0.685	1.46	0.686	1.46
<i>DIVYI</i>	0.868	1.15	0.842	1.19	0.844	1.18	0.823	1.21	0.822	1.22
<i>AUDF</i>	0.959	1.04	0.938	1.07	0.946	1.06	0.929	1.08	0.933	1.07
<i>FSALE</i>	0.950	1.05	0.921	1.09	0.942	1.06	0.914	1.09	0.915	1.09
<i>BSIZE</i>			0.784	1.27			0.770	1.30	0.766	1.31
<i>BCOM</i>			0.943	1.06			0.933	1.07	0.933	1.07
<i>DIRFOR</i>			0.693	1.44			0.689	1.45	0.736	1.36
<i>DIRMUL</i>			0.759	1.32			0.746	1.34	0.740	1.35
<i>DIRWOM</i>			0.913	1.09			0.888	1.13	0.887	1.13
<i>DIRPROF</i>			0.937	1.07			0.929	1.08	0.923	1.08
<i>DIRWEST</i>			0.813	1.23			0.788	1.27	0.790	1.26
<i>FCC</i>					0.586	1.70	0.567	1.76	0.567	1.76
<i>MANTOW</i>					0.553	1.81	0.534	1.87	0.534	1.87
<i>INSTOW</i>					0.842	1.19	0.832	1.20	0.832	1.20
Mean VIF	1.19		1.25		1.30		1.33		1.31	

Note: FCC=Family-controlled company, BSIZE=Board size, BCOM=Outside Director Compliance, DIRFOR=Foreign Director, DIRMUL=Multiple-directorship, DIRWOM=Woman director, DIRPROF=Director with professional qualification, DIRWEST=Western Education director, MANTOW=Management ownership, INSTOW=Institutional Ownership, FSIZE=Firm's size, FAGE=Firm's age, DEBRAT=Debt ratio, AUDF= Audit Firm, ROE=Return on Equity, LIQRAT=Liquidity ratio, DIVYI=Dividend yield, FSALE=Foreign Sale.

The VIF test was run to quantify the severity of multicollinearity in the constructive regression models. Each value represents an index that becomes an indicator of how much the variance of an estimated regression coefficient is increased due to the collinearity problem (please refer to Section 5.7.2.3 Multicollinearity Test for more explanation of VIF). Table 7.2 shows that the VIF values in the models range from 1.02 to 1.87, far below the threshold value of 10, indicating that there are no multicollinearity problems in the model (Gujarati and Porter 2009; Hair et al. 2006; Ho 2006; Neter, Wasserman and Kutner 1990;).

From the Spearman's rank multicollinearity test in Table 7.1, concern was given to the high correlation values between i) FCC and MANTOW and ii) LIQRAT and DEBRAT with the values of 0.635 and -0.771 respectively. By referring to the VIF test, the tolerance level between LIQRAT and DEBRAT in the models are above 0.6,

with the highest VIF at 1.50, while the tolerance level for FCC and MANTOW are above 0.5 and the highest VIF is 1.87. According to Menard (1995:66), “a tolerance score of 0.2 or below is a sign for concern”. O’Brien (2007) also suggests that a tolerance less than 0.2 or 0.1, and/or a VIF of 5 or 10 and above, indicates a multicollinearity problem. Since all the tolerance scores are above 0.5 for all the variables in the model and the VIFs are below 2.00, it can be concluded that multicollinearity is not likely to be an issue for the constructed regression models which allow for the standard interpretation of the regression coefficient.

7.4.2 Autocorrelation Test

Table 7.3: Wooldridge Test

	<i>Model 1</i>	<i>Model 2</i>	<i>Model 3</i>	<i>Model 4</i>	<i>Model 5</i>
<i>FEO</i>	124.753	120.559	125.947	122.016	
<i>FEO dummy</i>					71.001
F (p-value)	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
H ₀	<i>Rejected</i>	<i>Rejected</i>	<i>Rejected</i>	<i>Rejected</i>	<i>Rejected</i>

Note: H₀: no first-order autocorrelation
FEO=Foreign Equity Ownership

Based on the data observation, firms with higher foreign equity ownership in one year are likely to repeat the same pattern in following years. If so, the firms’ residuals may be correlated across years or the presence of serial-correlation is suspected (see 5.7.3.3 Autocorrelation for details). Thus, based on the previous discussion, the Wooldridge test was run to examine whether the issue of autocorrelation should be given any concern in the structured models. If autocorrelation or serial correlation is detected, the error term needs to be transformed, in order to be serially independent and not related across time. In this case, Baltagi (2008) and Wooldridge (2002) suggest the use of other estimators to produce more efficient estimates. Table 7.3 shows an indication of the autocorrelation problem with the models. The results from all the models show that the null hypothesis of no serial correlation is strongly rejected at $p < 0.000$. The consequences of this test will be discussed in the following part - Section 7.4 Multivariate Analyses.

7.4.3 Hausman Test

Table 7.4: Hausman Test

	<i>Model 1</i>	<i>Model 2</i>	<i>Model 3</i>	<i>Model 4</i>	<i>Model 5</i>
Chi2	11.61	43.64	11.2	20.52	7.72
Prob>chi2	0.1694	0.0000	0.4264	0.2483	0.9825
H_0	<i>Not rejected</i>	<i>Rejected</i>	<i>Not rejected</i>	<i>Not rejected</i>	<i>Not rejected</i>

Note: H_0 : difference in coefficients not systematic

The Hausman specification test is a generally accepted way of choosing between fixed-effects (FE) and random-effects (RE) (Greene 2008). The function of this test is to evaluate a more efficient model (RE) against a less efficient but consistent one (FE). The comparison is made in order to ensure that the more efficient model also gives consistent results (Davidson and MacKinnon 1995; Stock and Watson 2007). The null hypothesis in this test is that the coefficients estimated by the efficient RE estimator are the same as the ones estimated by the consistent FE estimator. It is safe to use a random effect if the result produces the insignificant p-value (Prob>chi2 larger than 0.05). Alternatively, FE should be chosen if the result shows otherwise.

The RE model may provide the better p-value as the estimator is more efficient. However, it may not be the most efficient model to run. On the other hand, the FE model has always presented consistent results. Therefore, in this case, the Hausman test was run to justify which test provides better results. Statistically, the initial hypothesis that the individual-level effects are adequately captured by an RE model is resoundingly accepted when the p-value, Prob>chi2 is larger than 0.05 for all the models (except for the second model). Thus, based on this statistical result, RE was chosen as it is the better model to run the panel data analyses.

7.4.4 Testing for Heteroscedasticity

Table 7.5: Breusch-Pagan/ Cook-Weisberg Test

Chi2	Model 1	Model 2	Model 3	Model 4	Model 5
<i>FEO</i>	488.10	1096.72	673.16	1224.37	
<i>FEO dummy</i>					590.00
Prob>chi2	(0.000)	(0.000)	(0.000)	(0.000)	(0.000)
H ₀	<i>Rejected</i>	<i>Rejected</i>	<i>Rejected</i>	<i>Rejected</i>	<i>Rejected</i>

Note: H₀: Constant variance (homoscedasticity)

FEO=Foreign Equity Ownership

A detailed discussion on heteroscedasticity was made in Section 5.7.3.2. The Breusch-Pagan/Cook-Weisberg test is one of several suggested methods to test the presence of heteroscedasticity. Table 7.5 shows the results from this test, which conclude that the null hypotheses were rejected when the p-values were significant ($p < 0.05$) for all the models. This rejection suggested the presence of heteroscedasticity in the models which explains that the variances are not constant. In order to remedy this problem, the robust command in STATA software can be used as one of the options to solve the heteroscedasticity problem. Next, multivariate analyses are run based on the results of the current diagnostic tests.

7.5 Multivariate Analysis

The statistical, mathematical and economic tools most suitable for the type of analysis must be carefully selected (Lind et al. 2005). In order to determine the appropriate analyses to run the models, the results of the diagnostic tests presented in Section 7.3 Panel Data Related Tests, were scrutinised. From the analyses, the Wooldridge test, the Hausman test and the Breusch-Pagan test, the presence of serial correlation and heteroscedasticity in the models are proven. These problems are accompanied by the abnormal data distribution issue, making GLS the proper estimation method to be applied (for further discussion on GLS and OLS, please refer to Section 5.7.4 Model Estimation: OLS vs GLS).

In this case, OLS is not reliable as the results will not be efficient and this leads to misleading inferences (Drukker 2003). GLS, on the other hand, effectively standardises the observations with the presence of heteroscedasticity and serial correlation (Greene 2003; Baltagi 2008) and is also suitable for use with the dataset which is not in normal distribution. Coinciding with the result of Hausman test, the use of GLS regression is consistent with the characteristics of variables in the regression model, as well as the selected technique to analyse panel data, which is random effects. The random effects technique is classified under GLS regression method. This panel data technique is compatible to investigate time-invariant variables in this model. In addition, after performing statistical test to check for variables distribution, one of the notable characteristics found was the variance ‘*between*’ variables is higher than the variance ‘*within*’ variables. Therefore, it is argued that the difference across entities have some influence on the dependent variable. This has strengthened the reason for choosing random effects technique as the most robust technique to be applied and it is fall under GLS regression method. Thus, the results of GLS regression are robust and reliable to be applied in order to infer the population.

It is claimed that GLS is the OLS on the transformed variables that satisfy the standard least square assumptions (Greene 2003). Thus, GLS is used to correct for heteroscedasticity, autocorrelation problems and to suit the pattern of dataset distribution in the models.

7.5.1 GLS Estimation Regression Models

The tests conducted in the previous Section 7.4 Panel Data Related Tests provide evidence that GLS regression is the most suitable method to be applied to the models. The rationale for using GLS regression is explained in the previous Section 7.5 Multivariate Analysis, and further comparisons and explanations of OLS versus GLS regression models can be found in Section 5.7.4.

Hereafter, the discussion focuses on the analyses run for each constructed model. The analyses for all models are based on 1836 observations allocated into 153 groups, for a span of a 12 year period, between 2000 and 2011. The goodness-of-fit for the models are evaluated using the log-likelihood and the Wald Chi-Square.

Table 7.6: Regression Results for GLS Estimation Models

Variables	Expected		Model 1		Model 2		Model 3		Model 4	
	H	Sign	Coefficient	z-statistic	Coefficient	z-statistic	Coefficient	z-statistic	Coefficient	z-statistic
Intercept			-52.410	-11.41***	-55.425	-12.53***	-53.989	-11.65***	-56.610	-12.73***
B _{SIZE}	H ₁	+			-0.015	-0.09			0.043	0.26
B _{COM}	H ₂	+			-0.120	-0.16			-0.041	-0.05
D _{IRFOR}	H ₃	+			0.465	19.33***			0.462	19.14***
D _{IRMUL}	H ₄	-			-1.569	-2.69***			-1.659	-2.83***
D _{IRWOM}	H ₅	+			-0.680	-1.25			-0.674	-1.23
D _{IRPROF}	H ₆	+			0.077	3.75***			0.074	3.63***
D _{IRWEST}	H ₇	+			0.043	3.55***			0.044	3.60***
F _{CC}	H ₈	-					-1.910	-2.59**	-1.114	-1.64*
M _{ANTOW}	H ₉	-					0.027	1.55	0.015	0.92
I _{NSTOW}	H ₁₀	-					-0.059	-2.65***	-0.044	-2.18**
Control Variables										
F _{SIZE}		+	3.055	12.95***	3.200	13.45***	3.180	13.24***	3.271	13.58***
F _{AGE}		+	0.069	3.71***	0.016	0.95	0.066	3.54***	0.015	0.86
D _{EBRAT}		-	-3.148	-2.93***	-4.069	-4.10***	-3.070	-2.85***	-4.052	-4.08***
A _{UDF}		+	2.565	4.41***	1.491	2.80***	2.551	4.37***	1.469	2.74***
R _{OE}		+	0.599	0.81	0.238	0.36	0.592	0.81	0.231	0.35
L _{IQRAT}		+	0.222	2.87***	-0.092	-1.27	0.200	2.59**	-0.106	-1.47
D _{IVYI}		-	-0.016	-0.13	-0.194	-1.74*	0.019	0.15	-0.171	-1.51
F _{SALE}		+	0.065	4.92***	0.019	1.56	0.065	4.94***	0.020	1.64*
Years dummy				<i>Included</i>		<i>Included</i>		<i>Included</i>		<i>Included</i>
N				1836		1836		1836		1836
No of groups				153		153		153		153
Time periods				12		12		12		12
Log likelihood				-7170.5690		-6984.5370		-7163.7780		-6980.8730
Wald Chi-square				370.520***		866.2000***		386.91***		877.01***

Notes:***, ** and * denote that the correlations are statistically significant at the 0.01, 0.05 and 0.10, respectively (2-tailed). B_{SIZE}=Board size, B_{COM}=Outside Director Compliance, D_{IRFOR}=Foreign Director, D_{IRMUL}=Multiple-directorship, D_{IRWOM}=Woman directorship, D_{IRPROF}=Director with professional qualification, D_{IRWEST}=Western Educational director, F_{CC}=Family-controlled company, M_{ANTOW}=Managerial ownership, I_{NSTOW}=Institutional Ownership, F_{SIZE}=Firm's size, F_{AGE}=Firm's age, D_{EBRAT}=Debt ratio, A_{UDF}= Audit Firm, R_{OE}=Return on Equity, L_{IQRAT}=Liquidity ratio, D_{IVYI}=Dividend yield, F_{SALE}=Foreign Sale.

Table 7.6 shows the GLS regression results for all the models. In each model, the coefficient, z-statistic and its standard error (in parentheses/ *** form) are reported.

The discussion starts with the first model, Model 1, which incorporates 8 control variables. This model is significant (at p-value less than 0.01) with Wald Chi-square of 370.52 and log likelihood -7170.569. These values indicate that the model as a whole fits significantly better than an empty model (i.e. a model with no predictor). The equation for Model 1 is presented in Equation 7.1:

$$\text{FEO} = b_0 + b_1\text{FSIZE}_{it-1} + b_2\text{FAGE}_{it-1} + b_3\text{DEBRAT}_{it-1} + b_4\text{AUDF}_{it-1} + b_5\text{ROE}_{it-1} + b_6\text{LIQRAT}_{it-1} + b_7\text{DIVYI}_{it-1} + b_8\text{FSALE}_{it-1} + \alpha_i + \lambda_t + \mu_{it}$$

Equation 7.1

Model 1 consists only of control variables. This model measures the relationship between control variables and FEO without the interference of any other variables. These variables are consistently used in previous literature and their results are highly predicted. It is expected that FSIZE, FAGE, AUDF, ROE, LIQRAT and FSALE will have a positive relationship with FEO, on the other hand, DEBRAT and DIVYI are expected to have a negative relationship. The following models include other exogenous variables with further discussions.

Secondly, Model 2 is structured to examine the relationship between corporate governance mechanisms and FEO. Corporate governance mechanisms in this model are divided into two groups, namely i) board characteristics, ii) directors' attributes and (see Figure 1.2: Conceptual Framework for the details). Control variables from Model 1 are incorporated in this model. GLS regression results show that Model 2, which incorporates 15 variables (7 independent variables and 8 control variables) is significant (at p-value < 0.01) with Wald Chi-square of 866.20 and log likelihood -6984.537. These values indicate that the model as a whole fits significantly better than an empty model (i.e. a model with no predictor) and better than the previous Model 1. The following equation for Model 2 is presented below:

$$\text{FEO} = b_0 + b_1\text{BSIZE}_{it-1} + b_2\text{BCOM}_{it-1} + b_3\text{DIRFOR}_{it-1} + b_4\text{DIRMUL}_{it-1} + b_5\text{DIRWOM}_{it-1} + b_6\text{DIRPROF}_{it-1} + b_7\text{DIRWEST}_{it-1} + \text{MODEL 1} + \alpha_i + \lambda_t + \mu_{it}$$

(Equation 7.2)

The third model, Model 3, is built by inserting ownership variables (FCC, MANTOW and INSTOW), one of the corporate governance mechanism strands, to show their relationship with FEO. These variables are merged with control variables from Model 1. Model 3 GLS Regression Results which consist altogether of 11 variables is significant (at p-value<0.01) with Wald Chi-square of 386.91 and log likelihood - 7163.778. These values indicate that the model as a whole fits significantly better than an empty model (i.e. a model with no predictor), albeit less efficiently than the previous Model 2. The following equation for Model 3 is applied:

$$\text{FEO} = b_0 + b_1\text{FCC}_{it-1} + b_2\text{MANTOW}_{it-1} + b_3\text{INSTOW}_{it-1} + \text{MODEL 1} + \alpha_i + \lambda_t + \mu_{it}$$

(Equation 7.3)

Lastly, the final model, Model 4, combines all the variables from Model 1 to Model 3 into one comprehensive model. 10 corporate governance variables are now examined by combining eight control variables from Model 1 to study their relationships with FEO. In terms of the goodness-of-fit for Model 4, the regression results show the model is significant (at p-value<0.01) with Wald Chi-square of 877.01 and log likelihood -6980.873. These values indicate that the model as a whole fits significantly better than an empty model (i.e. a model with no predictor), and simultaneously surpasses the previous three models. Thus, this model is considered as the final model. The following equation for Model 4 is applied:

$$\text{FEO} = b_0 + b_1\text{BSIZE}_{it-1} + b_2\text{BCOM}_{it-1} + b_3\text{DIRFOR}_{it-1} + b_4\text{DIRMUL}_{it-1} + b_5\text{DIRWOM}_{it-1} + b_6\text{DIRPROF}_{it-1} + b_7\text{DIRWEST}_{it-1} + b_8\text{FCC}_{it-1} + b_9\text{MANTOW}_{it-1} + b_{10}\text{INSTOW}_{it-1} + \text{MODEL 1} + \alpha_i + \lambda_t + \mu_{it}$$

(Equation 7.4)

7.5.1.1 GLS Estimation Regression Results

The preceding section has discussed the models and the goodness-of-fit by evaluating the log-likelihood and the Wald Chi-Square. This section, therefore, is devoted to discussing the interpretation of the regression results, variable coefficients, z-statistics

and significant levels (measured by p-value) for each hypothesis. These values are presented in Table 7.6, in accordance with their respective models. However, the focus of this discussion is on the values of the regression results from the final model, Model 4, unless otherwise indicated as there are insignificant differences between the results for these models. A year dummy is included in all models to reflect the time fixed effect. Significant levels ($p < 0.10$, $p < 0.0$ and $p < 0.01$) are denoted by *, ** and *** respectively. The discussion begins with the regression results of the control variables and is followed accordingly by the hypotheses.

GLS regression results for FEO also reveal the control variables' predictive properties. Firm size (FSIZE) is found to be significantly and positively related to FEO, as suggested by Dahlquist and Robertsson (2001), such that foreigners show a preference for a large firm. The finding illustrates that the larger the firm, the higher the level of FEO in the company. This argument is based on the perspective that the larger firms are more likely to attract more foreigners to invest in the company as they feel more secure with the back-up of resources that belong to the firm. It is also consistent with the finding by Kim et al. (2010) that during the unstable and volatile period, foreign investors outweigh the large firm because the probability of firm survival increases with firm size (Evans 1987). FSIZE consistently portrays a positive and significant relationship with FEO at $p\text{-value} < 0.01$, regardless of any models.

As for the firm age (FAGE), it is not surprising to see that the result is consistent with the FSIZE, which is positively significant with FEO. The probability of survival increases with size more rapidly for older firms, and the probability of survival increases with age more rapidly for larger firms (Evans 1987). However, the significant positive relationship ($p\text{-value} < 0.01$) between FAGE and FEO is only consistent in Model 1 and Model 3. FAGE indicates insignificant results in Model 2 and Model 4 after the directors' elements were incorporated into the models.

Debt ratio (DEBRAT), on the other hand, is found to be negatively significant with the FEO in all models. Meanwhile, the selection of audit firm (AUDF) by firms shows a significant ($p < 0.01$) and positive relationship with the FEO regardless of any

models. This is likewise for liquidity ratio (LIQRAT) and foreign sale (FSALE). However, LIQRAT repeats the relationship pattern shown by FAGE, whereby the significant results are only portrayed in Model 1 and Model 3, whilst FSALE is found to be insignificant only in Model 2. On the other hand, return on equity (ROE) and dividend yield (DIVYI) are found to be non-significant with the FEO level in almost all models.

Turning to the independent variables, the first hypothesis, (H_1), tests the association between board size (BSIZE) and the level of FEO. Based on the arguments given in the hypotheses development section, invoking the multi-theoretical perspective, the higher the number of directors on the board, the higher the level of FEO in the company. As shown in Table 7.6, the coefficient for BSIZE is 0.043, in the expected direction with z-statistics of 0.26. However, the BSIZE is not statistically significant ($p\text{-value} > 0.1$) in determining FEO level in the two models involved. The results indicate that the board size does not affect FEO level in the firm. Therefore H_1 is not supported.

The second association (H_2) is tested between board outside director compliance (BCOM) and FEO level. A positive relationship is expected between BCOM and FEO, where companies that comply with the minimum number required for outside directors are expected to have higher FEO. As reported in Table 7.6, the coefficient between BCOM and FEO is -0.041 with $p\text{-value}$ more than 0.10, which is not statistically significant. Thus, H_2 is also rejected. This implies that BCOM does not have a significant influence on the level of FEO in the company.

A similar association is hypothesised between foreign director (DIRFOR) and FEO through H_3 . As explained in the hypotheses development chapter (see Section 4.4.2.1 Foreign Directorship), H_3 proposed that the higher the number of foreign directors on the board, the more likely it is that the level of FEO in the firm is also high. This expectation is based on the notion that foreign investors prefer to invest in a company with a high proportion of foreign directors on board whom they believe can bring their global expertise, experience and share their cultural dimension, in order to enhance

the company's performance. Table 7.6 shows that the coefficient between DIRFOR and FEO is 0.462 in a positive direction with z-statistic of 19.14. The coefficient value postulates that, for every one-unit increase in percentage of foreign director, it is expected that foreign ownership in the company will increase by 0.46 percent, holding all other independent variables constant. The p-value indicates that this association is statistically significant at $p < 0.01$. Therefore, H_3 is strongly supported. This finding implies that the numbers of foreign directors on the board is important to foreign investors in making investment decisions.

The next relationship to be examined is between multiple directorships (DIRMUL) and FEO. Multiple-directorships is likely to indicate 'directors' busyness' which may lead to the corporate governance problem in the company. Therefore, it is hypothesised (H_4) that DIRMUL will have a negative relationship with FEO. As reported in Table 7.6, the result shows that the direction of the relationship is negative and significant ($p < 0.01$) between them. The coefficient for this variable is -1.659. This means that for a one-unit increase in DIRMUL (in other words, the number of directorships going from 6 to 7 and above), the FEO level is expected to decrease by -1.65 percent. This result also implies that DIRMUL is a matter of concern for foreign investors in making their investment decision. Thus, H_4 is supported.

Further, the association between women directorship (DIRWOM) and FEO is examined through H_5 . As argued in Chapter 4, it is proposed that DIRWOM will bring a positive effect on the level of FEO in company. Table 7.6 shows that the coefficient between these variables is -0.674 with z-statistic of -1.23. The result, however, denies the hypothesised prediction as p-value has shown the insignificant value. Therefore, H_5 is rejected.

Hypothesis six (H_6) tests the association between professional director (DIRPROF) and FEO. It is argued that a higher number of professional directors will attract more foreign investors to invest in the company. The regression results confirm a positive and significant association between DIRPROF and FEO at $p\text{-value} < 0.01$. The coefficient value 0.074, suggests that an increase of one percent in DIRPROF,

subsequently increases the FEO level by 0.074 percent, holding other variables constant. This finding implies that the higher the number of professional directors on the board, the higher the FEO level in the company. Thus, H_6 is strongly supported.

The next hypothesis, (H_7), examines the association between a Western educational background director (DIRWEST) and FEO. Based on the arguments made in Chapter 4, it is postulated that the higher the number of directors with a Western educational background the more favourable it is for foreign investors when making decisions to invest in a company. The regression results show the positive coefficient level at 0.044 and z-statistic of 3.60 at $p\text{-value} < 0.01$. This indicates the 0.044 percent increase in FEO level if the percentage of DIRWEST increases by one percent, holding other variables constant. The significant level shown, supports H_7 .

The association between a family-controlled company (FCC) and FEO is examined in hypothesis eight (H_8). The lengthy arguments in Chapter 4 shed some light on the expectation that foreign investors will react negatively towards FCC. Consistent with the prediction, the regression results in Table 7.6 support this view. The coefficient value is -1.64. This suggests that the decrease of FEO level when FCC changes by one unit (when NFCC becomes FCC), holding other variables constant. However, the significant level is marginal at $p\text{-value} < 0.10$. Nonetheless, H_8 is supported.

Next, hypothesis (H_9) tests the relationship between managerial ownership (MANTOW) and FEO. H_9 proposes a negative relationship between MANTOW and FEO. The regression result is in the predicted direction (0.015) with z-statistics of 0.92. However, the p-value shows an insignificant impact of MANTOW and FEO. The result implies that MANTOW does not influence FEO level in the company. Thus, H_9 is not supported.

The final hypothesis for GLS regression posits an association between institutional ownership (INSTOW) and FEO. It is hypothesised that the higher the institutional ownership in the company, the lower the FEO level in the company. Table 7.6 shows that INSTOW and FEO have a negative relationship with a correlation coefficient of -

0.044. This value represents the decrease in FEO level with a one percent increase in INSTOW. The p-value is significant at the 5% level. This result implies that higher institutional ownership hinders foreign investors from investing in the company. Therefore, the final hypothesis, H_{10} , is supported.

Generally, the results shown in all the models are consistent. The results of the final model are consistent with those shown in the previous models. Succinctly, board attributes - DIRFOR, DIRPROF and DIRWEST variables - are positively significant (at $p < 0.01$) with the FEO, while DIRMUL is negatively significant (at $p < 0.01$). The other three (3) - BSIZE, BCOM and DIRWOM - show no significant relationship with FEO. This output mirrors the results from Model 2. For the ownership variables, FCC and INSTOW are found to be negatively significant at $p < 0.10$ and $p < 0.05$ respectively. INSTOW was previously found not significant in Model 3, but with the inclusion of board attributes variables, the model has improved and its significant level has changed.

Control variables - FSIZE, AUDF - are positively significant ($p < 0.01$) and FSALE is found to be marginally significant ($p < 0.10$). The other significant control variable is DEBRAT in a negative direction at $p\text{-value} < 0.01$, as predicted earlier. The results for control variables in this final model are nearly consistent with the output in Model 2 and 3.

Further, this study also seeks to explain the difference between firms with a high level of FEO and firms with a low level FEO in terms of corporate governance practice. Thus, additional analysis, logistic regression analysis, is conducted. The results are displayed below in Section 7.5.2 Logit Estimation Regression Models.

7.5.2 Logit Estimation Regression Models

For this additional analysis, the same model - Model 4 - is utilised and the same independent variables are involved. However, the type of dependent variable is changed, from a continuous variable to a dummy variable. For this type of variable,

logistic regression is applied. Further explanation of this dummy variable can be found in Section 6.2.3: Dependent Variable: Distribution and Skewed Data. The equation for Model 5, (adjusted from Model 4) is applied below, and the results of the analysis are presented in the following Table 7.7:

$$\text{FEO dummy} = b_0 + b_1\text{BSIZE}_{it-1} + b_2\text{BCOM}_{it-1} + b_3\text{DIRFOR}_{it-1} + b_4\text{DIRMUL}_{it-1} + b_5\text{DIRWOM}_{it-1} + b_6\text{DIRPROF}_{it-1} + b_7\text{DIRWEST}_{it-1} + b_8\text{FCC}_{it-1} + b_9\text{MANTOW}_{it-1} + b_{10}\text{INSTOW}_{it-1} + \text{MODEL 1} + \alpha_i + \lambda_t + \mu_{it}$$

(Equation 7.5)

Table 7.7: Regression Results for Logit Estimation Models.

<i>Model 5</i>		
Variables	Coefficient	z-statistic
Intercept	-56.781	-6.91***
<i>BSIZE</i>	0.520	2.95***
<i>BCOM</i>	1.133	1.87*
<i>DIRFOR</i>	0.135	3.56***
<i>DIRMUL</i>	1.043	1.52
<i>DIRWOM</i>	0.063	0.09
<i>DIRPROF</i>	0.024	1.16
<i>DIRWEST</i>	-0.035	-2.09**
<i>FCC</i>	-1.557	-1.72*
<i>MANTOW</i>	0.005	0.35
<i>INSTOW</i>	-0.015	-0.59
Control Variables		
<i>FSIZE</i>	2.136	5.35***
<i>FAGE</i>	0.051	1.53
<i>DEBRAT</i>	2.217	2.45**
<i>AUDF</i>	0.780	1.01
<i>ROE</i>	-0.027	-0.06
<i>LIQRAT</i>	-0.137	-1.22
<i>DIVYI</i>	-0.020	-0.23
<i>FSALE</i>	0.045	3.65***
Years dummy		<i>Included</i>
<i>N</i>		1836
<i>No of groups</i>		153
<i>Time periods</i>		12
Log likelihood		-255.7257
Wald Chi-square		82.80***

Notes:***, ** and * denote that the correlations are statistically significant at the 0.01, 0.05 and 0.10, respectively (2-tailed). *BSIZE*=Board size, *BCOM*=Outside Director Compliance, *DIRFOR*=Foreign Director, *DIRMUL*=Multiple-directorship, *DIRWOM*=Woman director,

DIRPROF=Director with professional qualification, DIRWEST=Western Education director, FCC=Family-controlled company, MANTOW=Management ownership, INSTOW=Institutional Ownership, FSIZE=Firm's size, FAGE=Firm's age, DEBRAT=Debt ratio, AUDF= Audit Firm, ROE=Return on Equity, LIQRAT=Liquidity ratio, DIVYI=Dividend yield, FSALE=Foreign Sale.

Consistent with the previous four models, the analysis for Model 5 is based on 1836 observations allocated in 153 groups for a span of a 12 year period, between 2000 and 2011. The goodness-of-fit for the models is evaluated using the log-likelihood and the Wald Chi-Square. The log likelihood of the final model is -255.725, which indicates that it fits significantly better than an empty model (with log likelihood of -732.465). This model is statistically significant given the p-value is less than 0.000 (Prob>chi2 = 0.0000). The likelihood ratio chi-square test, Wald chi2 (29) = 82.80, represents the difference between the starting and ending log likelihood and it indicates the degrees of freedom for this model, which is 29. Significant effects for p-value<0.10, <0.05 and <0.01 are denoted by *,** and ***. A year dummy effect is included to eliminate certain aspects of cross-year heterogeneity.

Utilising logistic regression analysis, it is presumed that there is an association between good corporate governance practice and high FEO firms. It is argued that the high level FEO firms favour the good corporate governance practice in the company. Table 7.7 shows the results, which indicate the positive and significant relationship between high FEO firms and BSIZE, DIRFOR (at p-value<0.01) and BCOM (at p<0.1), while a negative relationship is documented between high FEO firms with DIRWEST (at p<0.05) and FCC (at p<0.1). This result implies that when the level of foreign ownership in one company reaches 20% or beyond, the corporate governance variables that have predictive properties are board size, number of foreign directors on board, outside director compliance, directors with Western educational background and family-controlled company. Given the number of corporate governance variables associated with this dummy variable, this presupposition is supported, thus strengthening the results from GLS regression. Further discussion of the similarities and contradictory results between GLS estimation and logistic regression can be found in Chapter 8, Section 8.3 Summary of the Analyses.

7.5.3 Generalised Methods of Moments (GMM) Estimator

After running two main analyses, GLS and logistic regression, GMM analysis is further applied. The detailed explanation of GMM can be found in Section 5.7.7.1.

GMM can be considered as a robustness check. Besides, as explained in Chapter 5, Section 5.7.7.2. Endogeneity, GMM analysis is also a suitable analysis for a dataset with an endogeneity case. In the context of this study, there is a potential for endogeneity problems to exist. The results from the two previous analyses may not be accurate, due to the endogeneity issue. Therefore, GMM analysis is utilised to correct the potential problem caused by endogeneity. However, it is interesting to note that endogeneity in this study is unlikely to pose a serious problem, since in the earlier formation of the models it was taken into account by using a lagged dependent variable to tackle this issue (see Section 5.7.7.2 Endogeneity).

Table 7.8: GMM Estimation Model.

<i>Model 4</i>		
Observations	Coefficient	z-statistic
Intercept	-3.491	-0.74
<i>B</i> SIZE	0.030	0.36
<i>B</i> COM	-0.653	-2.71***
<i>DIR</i> FOR	0.054	3.19***
<i>DIR</i> MUL	0.275	1.13
<i>DIR</i> WOM	0.445	1.69*
<i>DIR</i> PROF	-0.006	-0.71
<i>DIR</i> WEST	-0.019	-2.79***
<i>F</i> CC	-0.241	-0.58
<i>M</i> ANTOW	-0.002	-0.41
<i>I</i> NSTOW	-0.064	-4.34***
Control Variables		
<i>F</i> SIZE	0.660	2.76***
<i>F</i> AGE	-0.056	-8.37***
<i>D</i> EBRAT	-1.268	-3.04***
<i>A</i> UDF	-0.799	2.21**
<i>R</i> OE	0.062	0.38
<i>L</i> IQRAT	0.000	0.01
<i>D</i> IVYI	0.075	2.60***
<i>F</i> SALE	-0.007	-1.05
Years dummy		<i>Included</i>
<i>N</i>		1377
<i>No of groups</i>		153
<i>Time periods</i>		12
<i>No of instruments</i>		82
<i>Wald Chi-square</i>		3512.54***

Notes:***, ** and * denote that the correlations are statistically significant at the 0.01, 0.05 and 0.10, respectively (2-tailed). *B*SIZE=Board size, *B*COM=Outside Director Compliance, *DIR*FOR=Foreign Director, *DIR*MUL=Multiple-directorship, *DIR*WOM=Woman director, *DIR*PROF=Director with professional qualification, *DIR*WEST=Western Education director, *F*CC=Family-controlled company, *M*ANTOW=Management ownership, *I*NSTOW=Institutional Ownership, *F*SIZE=Firm's size, *F*AGE=Firm's age, *D*EBRAT=Debt ratio, *A*UDF= Audit Firm, *R*OE=Return on Equity, *L*IQRAT=Liquidity ratio, *D*IVYI=Dividend yield, *F*SALE=Foreign Sale.

For this GMM analysis, the Arellano-Bond estimator is used. It uses lagged values of y_{it} as instruments. Using this estimator, observations for each individual are stacked together and equations are formed. The number of instruments used in this analysis is 82. The number of observations was reduced to 1377 from the original number of observations, which was 1836. The GMM model for this analysis is statistically significant, at $p < 0.01$, whilst Wald chi2 (29) = 3512.54. As generally practiced,

significant effects for $p\text{-value} < 0.10$, < 0.05 and < 0.01 are denoted by *, ** and ***. The year dummy effect is also included to eliminate certain aspects of cross-year heterogeneity.

The GMM analysis is run with two lags of dependent variable included as regressors. All are assumed to be exogenous. The equation 7.6 below is derived from previous Model 4, but it is improved to the dynamic version.

$$\text{FEO}_{it} = \lambda_1 \cdot \text{FEO}_{i,t-1} + \lambda_2 \cdot \text{FEO}_{i,t-2} + b_1 \text{BSIZE}_{it-1} + b_2 \text{BCOM}_{it-1} + b_3 \text{DIRFOR}_{it-1} + b_4 \text{DIRMUL}_{it-1} + b_5 \text{DIRWOM}_{it-1} + b_6 \text{DIRPROF}_{it-1} + b_7 \text{DIRWEST}_{it-1} + b_8 \text{FCC}_{it-1} + b_9 \text{MANTOW}_{it-1} + b_{10} \text{INSTOW}_{it-1} + \text{MODEL 1} + \alpha_i + \lambda_t + \mu_{it}$$

(Equation 7.6)

There are two specification tests required following system GMM estimation (Arellano and Bond 1991) as previously mentioned in Section 5.7.7.1 The General Method of Moments (GMM). The first test is the Sargan test and the second test is the Arellano-Bond test. The null hypothesis for the Sargan test is that over-identifying restrictions are valid. The results in Table 7.9 Sargan Test show that the null hypothesis is not rejected. This indicates that the moment restrictions are valid for this analysis.

Table 7.9: Sargan Test

	Model 4
Chi2(52)	65.12
Prob>chi2	0.104
H_0	<i>Not rejected</i>

Note: H_0 : Over-identifying restrictions are valid

The second test, the Arellano-Bond Test, is applied to test whether a second order autocorrelation is zero (0). Table 7.10: Arellano-Bond test shows that the null hypothesis is accepted. The null hypothesis for this test posits that there is no second autocorrelation in the residuals.

Table 7.10: Arellano-Bond Test

	<i>Model 4</i>	
	<i>z</i>	<i>Prob > z</i>
<i>Order</i>		
1	-3.949	0.0001
2	-0.645	0.5188
H_0	<i>Not rejected</i>	

Note: H_0 : No autocorrelation

Based on the results of these two specification tests, this GMM estimation model is accepted. The results from the GMM estimation analysis are discussed in the following paragraph. However, it is important to note here that the standard errors might be biased since the robust estimator of Windmeijer was not operationalised for these analyses (Windmeijer 2005).

The results displayed in Table 7.8 show the positive and significant association between DIRFOR (p-value<0.01) and DIRWOM (p-value<0.1) and FEO. However, the inverse and significant relationship is found for BCOM, DIRWEST and INSTOW at p-value<0.01. The findings for DIRFOR (H_3) and INSTOW (H_{10}) are consistent with those shown in the GLS regression analysis. However, a few variables which were previously significant in GLS estimation are found to be otherwise in GMM analysis, and they are DIRMUL, DIRPROF and FCC. Apart from this, BCOM (H_2) is found to be significant, even though it was not significant in the GLS estimation. Interestingly, the direction also changes for DIRWEST (H_7). The consistency and inconsistency of the results in GMM analysis and GLS analysis are discussed in Chapter 8. However, it is interesting to note that from all the types of tests conducted, DIRFOR reveals its strong predictive properties to explain FEO.

7.5.4 Sensitivity Analyses

To further attest the robustness of results from the main analysis, a number of checks were carried out to determine the sensitivity of the results. The models are re-estimated by dropping and adding back each of the control variables to the models. All results replicate, which indicates that no serious flaw is attached to the models

pertaining to their control variables, thus corroborating the performed analyses. Therefore, the results are not presented here as there are no new results to be reported.

7.6 Summary

This chapter has outlined the findings from a few analyses: GLS estimation regression, logistic regression and the GMM estimator. Five models were constructed and analysed. In this chapter, the discussion starts with correlation analyses and is followed by diagnostic tests for panel data. Next, multivariate analysis results from three types of regressions analyses - GLS estimation regression, logistic regression and GMM estimation analysis - are provided. However, GLS regression is the main analysis for this study. The other two analyses (logistic regression and the GMM estimator) can be considered as robustness tests to complement the main analysis. Altogether, there are 10 hypotheses ($H_1 - H_{10}$) being tested. They are structured in a few models, which can be determined from Table 7.6: Regression Results for GLS Estimation Models. A summary of these results under three types of analyses is shown in Table 7.11 below, which emphasises the prominent theory for each hypothesis. Only explanatory variables are shown in this table.

Table 7.11: Summary of Results for All Analyses

Variables	Hypothesis Number	Main Analysis			Additional Analyses			
		GLS regression			Logistic regression		GMM estimation	
		Outcome	Expected Sign	Prominent Theory	Outcome	Expected Sign	Outcome	Expected Sign
<i>BSIZE</i>	H_1	+	/	IT	+++	/	+	/
<i>BCOM</i>	H_2	-	X	AT	+	/	-	X
<i>DIRFOR</i>	H_3	+++	/	IT	+++	/	+++	/
<i>DIRMUL</i>	H_4	-	/	IT	-	/	+	X
<i>DIRWOM</i>	H_5	-	X	AT	+	/	+	/
<i>DIRPROF</i>	H_6	+++	/	IT	+	/	-	X
<i>DIRWEST</i>	H_7	+++	/	IT	-	X	-	X
<i>FCC</i>	H_8	-	/	IT	-	/	-	/
<i>MANTOW</i>	H_9	+	X	AT	+	X	-	/
<i>INSTOW</i>	H_{10}	-	/	IT	-	/	-	/

Notes: +, ++ and * denote that the correlations are statistically significant at the 0.01, 0.05 and 0.10, respectively (2-tailed). "/=" Outcome as per expectation, "X"= Outcome is not as per expectation, IT=Institutional theory, AT=Agency theory, BSIZE=Board size, BCOM=Outside Director Compliance, DIRFOR=Foreign Director, DIRMUL=Multiple-directorship, DIRWOM=Woman director, DIRPROF=Director with professional qualification, DIRWEST=Western Education director, FCC=Family-controlled company, MANTOW=Management ownership, INSTOW=Institutional Ownership.

Overall, the results from all regression analyses are technically consistent with each other, however with slight differences. There are a plethora of reasons for the difference between what was predicted and what has been found. It is worth noting that foreign directorship (DIRFOR) persistently shows its significant value with a positive direction, regardless of any models or any regression analyses. This result is robust even after controlling for the time-fixed effect, firm-specific characteristics and endogeneity. A detailed discussion in regards to this table can be found in Chapter 8, Section 8.3 Summary of the Study.

CHAPTER 8

CONCLUSIONS AND RECOMMENDATIONS

8.1 Introduction

Chapter 1 specified the research objectives – to examine whether the level of foreign equity ownership (FEO) is determined by a firm’s corporate governance structure. The background to corporate governance is presented in Chapter 2. Here, the discussion of corporate governance is linked to FEO as a basis for the subsequent chapters. The thesis proceeds to use a multi-theoretical approach (as discussed in Chapter 3) as a framework for the development of the hypotheses provided in Chapter 4. Chapter 5 illustrates the process of data collection and the procedure for using the statistical method to test the hypotheses. Preliminary findings in the form of descriptive statistics are presented in Chapter 6 and the multivariate results are summarised in Chapter 7. In this chapter, the empirical results from the statistical tests are discussed and summarised in the light of the theoretical and practical implications, limitations and avenues for future research.

This concluding chapter is organised as follows. Section 8.2 reviews the key findings. Section 8.3 provides a summary of the analyses performed, Section 8.4 considers the possible incremental knowledge contributed to the academic debate, the use of the theoretical approach that can enhance the understanding of foreign investors’ behaviour, the impact that it might have on policymakers, the new measurement that may benefit the methodological view and lastly, the actual corporate governance practice which can be used in firms to appease foreign investors. Section 8.5 discusses the limitations of the research, and at the same time, proposing an avenue for future research. Finally, Section 8.6 concludes the study.

8.2 Discussion of Key Findings

More specifically, this study has focussed on answering the following research questions: i) Do the characteristics of the board of directors influence the level of FEO? ii) Do directors' attributes influence the level of FEO? and iii) Do ownership structures influence the level of FEO? These three questions (sub-research questions) may be taken as constituents of one big, one namely: *Does corporate governance influence the level of FEO in Malaysian companies?*

In the following sub-sections, the above questions are discussed accordingly, in terms of existing knowledge, along with the results of this study, in an attempt to enhance our understanding of the relationship between corporate governance and foreign investment decisions. Starting from the next sub-section, the discussion will be based on the results from the main analysis. In other words, we refer to generalised least square (GLS) regression results in our discussion of findings and their implications (see Table 7.6: Regression Results for GLS Estimation Models).

8.2.1 Board Characteristics Determinants for Foreign Investors' Investment Decisions

In this study, there are two corporate governance variables used as proxies to answer the first research question. The first variable is board size (BSIZE) and the second one is outside director compliance (BCOM). These independent variables, suggested by corporate governance mechanisms and the multi-theoretical approach, proved to be insignificant in predicting the probability of attracting foreign investment. The justifications for these findings will be discussed in the following sub-sections.

8.2.1.1 Board Size

The results for BSIZE were insignificant in both Model 2 and Model 4. The results appear to defy the findings of Haniffa and Hudaib (2006) which provide evidence of a significant relationship between board size and company performance. Even though a significant association cannot be statistically proved, the result is consistent with the

earlier supposition, namely that there is a positive direction between board size and foreign equity level in Malaysia. Nevertheless, this finding leads to the conclusion that foreign investors do not have a significant interest in board size when making their investment decisions. Even though the Code (2000) emphasises that board size should be carefully examined, it fails to provide the ideal number of directors who should sit on the board.

In Malaysia, foreign investors disregard board size in making their investment decisions. It is argued that the size of the board does not have a significant bearing on a company's monitoring or controlling, or on shareholder value. Drawing on the Anglo-American governance system, no ideal number for the board size has been dictated. Thus, foreign investors may place less weight on the size of the board to determine their investment, as they have in mind that this has no particular impact on the firms.

By referring to a previous table in Chapter 6 (Table 6.2: Data Distribution for the Continuous Independent and Control Variables), the average number for the board size for Malaysian firms is 7.43, the median is 7 and the standard deviation is only 1.71. Even the previous survey conducted by Kuala Lumpur Stock Exchange (KLSE) and PricewaterhouseCoopers in 1999 found that, on average, the board size in Malaysian companies consisted of 8 directors and the composition of each board was generally constituted of independent non-executive directors, equalling about one third of the board (Thillainathan 2001). These figures provide the essential explanation that in Malaysian firms, the size of the board of directors is almost uniform. Therefore, the issue of whether the size is large or small is not relevant to the debate.

Drawing on resource dependence theory (RDT) and agency theory, the advocates of a larger board argue in terms of the diversity advantage, critical resources (Haniffa and Hudaib 2006), reducing the uncertainties in the corporate environment (Dalton et. al 1999; Pfeffer 1987), and access to external linkages (Pfeffer and Salancik 1978). On the other hand, those who disfavour the larger board make counter arguments such as

communication problems, poor decision making (John and Senbet 1998), and monitoring problems etc.

In the context of this study, neither agency nor resource dependence theories explain the reason why foreign investors give no particular preference to board size when making investment decisions. Drawing on the institutional theory explanation, foreign investors are aware of the fact that ‘one-size-fits-all’ is misleading and the ideal number for the board size depends on the circumstances of the individual firm. Therefore, no robust cut-off for the board size is sought by foreign investors. Moreover, as claimed beforehand, there is no particular code in developed markets like the US, UK and New Zealand, marking any specific size for the board of directors. Each individual company is free to decide the ideal number for its board size in accordance to the companies’ specific characteristics, provided that board effectiveness is not compromised.

8.2.1.2 Outside Director Compliance-Independence of the Outside Director

The earlier presupposition drawing on a multi-theoretical approach (MTA), and mainly from institutional theory, views the presence of outside directors on the board as one of the main determinants which attracts foreign investors. On the contrary, the result of this study refutes the idea that the proportion of outside directors could affect foreign investors’ investment decisions. In fact, it is also suggested that the composition of outside directors on the board does not influence foreign investors to make an investment in the company.

This puzzling finding has to be explained carefully, especially in Malaysia’s capital markets. It is argued that the definition of ‘independent’ for directors in Malaysia can invite scepticism. Even though it is clear from the Code (2000: 25) that the term ‘independent’ refers to two crucial aspects, i) independence from management and ii) independence from significant shareholders, unfortunately, the compliance with the Code (2000) is doubtful. The concern is - Are independent directors in Malaysia really ‘*independent*’? Abdullah and Nasir (2004: 23) assert that it is difficult to justify

whether independent directors in Malaysian PLCs are truly independent as “Malaysian companies are very closely held and mostly are family controlled”. There is evidence of the ineffectiveness of independent directors in discharging their duties in Malaysian companies, such as the study by Leng and Mansor (2005) in which it was found that independent directors in Malaysian PLCs have no influence on a company’s profitability. Nevertheless, the evidence from empirical studies on the effectiveness of independent directors in Malaysian companies whilst carrying out their duties is limited, and not clearly deciphered (Abdullah and Nasir 2004).

Despite many arguments that propose the benefits of a high proportion of outside directors on the board, derived from many perspectives (see Section 4.4.1.2 Outside Director Compliance), foreign investors find independent directors in Malaysia to be less relevant to their investment decision making. One of the explanations is that the ‘*independent*’ status can be disputed. During the data collection process, while studying the directors’ backgrounds, it was discovered that amongst the current independent directors was a former employee, or people that used to be appointed as executive directors, or had held the position of independent director for too long, thus, the clause of ‘*independence from management*’ was not fulfilled. Many cases were found to be similar⁴⁰, and it is believed that the same issue arises in family companies, where independent directors may have a blood relationship with the family members who control the firm. In this case, an argument from the principal-principal concept is applied. The foreign investors’ fears of being manipulated by controlling shareholders could not be quelled despite the presence of outside directors on corporate board. A suggestion in relation to this issue can be found in 8.4.4 Practical Contribution.

⁴⁰ At this point in time, this presumption has no empirical support, as a statistical number cannot be provided. In future work, it might be beneficial to come up with the specific percentage of the sample to attest this claim.

The second argument is based on the descriptive data from Table 6.4: Frequency and percentage of categorical variables. It has been shown that out of the total observations, 85.29% of them comply with the suggestion made in the Code (2000) to have at least a 1/3 proportion of outside directors on the board. The great compliance shown by companies may provide an overview to foreign investors that generally, Malaysian companies have no problem in abiding by this rule. Study by Shamsul Nahar (1999) provides evidence for this claim in finding that Malaysian PLCs are dominated in numbers by outside directors. Thus, foreign investors give no preference to the variable, as the adherence to the presence of independent directors' on the board is followed equally by the majority of firms.

Nonetheless, this study does not lessen the importance of the independent directors' role in monitoring companies as it is seen as one example of good governance practice (Cho and Kim 2007; Payne et al. 2009). This has long been applied in the Anglo-American governance system, and the adoption of this practice is evidence of corporate governance reformation (Aguilera and Cuervo-Cazurra 2009).

8.2.2 Directors' Attributes as Determinants for Foreign Investors Investment Decisions

The discussion of this section is centred on answering the second research question. In this context, there are five corporate governance variables that are utilised to predict the foreign investors' behaviour in making investment decisions. These are foreign directorships (DIRFOR), multiple-directorships (DIRMUL), women directorships (DIRWOM), professional directors (DIRPROF) and Western educational background for directors (DIRWEST). All variables were significant except for DIRWOM. Discussions of these significant results are given in the sub-sections below.

8.2.2.1 Foreign Directorship

As expected, the results support the hypothesis that foreign directorship is positively associated with foreign equity investment. The findings in this study are consistent with Kim et al. (2010). The fact that firms with foreign directorships (DIRFOR) are more likely to attract foreign investors, could possibly suggest that societal pressure plays an important role in the investment decision process. These societal pressures that *coercively* push firms to adopt shareholder value principles, in this case, the representation of foreign directors on the board, are certainly a cornerstone of Anglo-American style corporate governance. The appointment of foreign directors to the board is perceived by foreign investors as a sign of improved governance, which then becomes the impetus for them to invest in the firm (Kim et al. 2010).

In addition, the appointment of foreign directors to the board is also mutually agreed by agency theory as one of the efficient corporate governance mechanisms that can curb monitoring costs. Foreign investors may believe that the existence of foreign directors (generally from the developed capital market) on the board secures their interests in the firms as they share similar values and perspectives, which is to maximise shareholder wealth, and reduce agency conflict. Besides this, foreign directors may assist in improving the board's advisory role through their first-hand experience from their home countries. It could also be argued that from the perspective of RDT, foreign directors are a crucial asset to the company in bringing in prospective resources such as global experiences, foreign networks (Masulis et al. 2012), managerial expertise (Kim et al. 2010), or technical skills that cannot be offered by the domestic directors. Access to these crucial resources is facilitated by the presence of foreign directors.

Even though there is an argument that the benefit of having foreign directors on the board can be better explained by RDT, it is well documented that in institutional theory parlance, in order to obtain legitimacy, firms need to adhere to societal expectations, which results in facilitating access to resources (DiMaggio and Powell 1983). Another possible explanation pertains to mimetic isomorphism. This is one

case that leads to the diffusion of the appointment of foreign directors onto boards - through mimicking best practices. In summary, all the underlying theories seem consistent in explaining the outcome of the analyses. However, in practical terms, institutional theory surpasses the other theories in its justification concerning the presence of foreign directors on the board in relation to the level of foreign equity ownership in the companies.

In addition, based on the observations from the study sample, Malaysian firms with foreign directors on the board registered only 18% of the total observations. This figure is relatively small, but the presence of foreign directors on the board is highly sought after by foreign investors in Malaysia. This has been proven by the significant regression results shown, regardless of any models or statistical analyses used (see Table 7.11: Summary of Results for All Analyses). Indeed, this result is robust even after controlling for the time-fixed effects, firm-specific characteristics and endogeneity.

8.2.2.2 Multiple-Directorships

The literature on directors with multiple board seats shows two different directions. In brief, scholars who advocate directors with multiple-directorships put forward their arguments that directors with multiple-directorships are gaining precious executive experiences, learning more managerial styles (Carpenter and Westphal 2001), establishing corporate networks (Loderer and Peyer 2002), signalling positive recognition of their expertise, and building their reputation as a monitoring expert, etc. (Fama 1980; Fama and Jensen 1983).

The results, however, provide evidence that, in Malaysia, foreign investors perceive directors with multiple directorships negatively, as their stretching schedules may impact their fiduciary duty, which can jeopardise the firm's value. In matters of time and energy limitations (Fich and Shivdasani 2006), directors who sit on multiple boards may be unable to perform their duties effectively (Ferris et al. 2003), they are associated with absence from board meetings (Jiraporn et al. 2009; Masulis et al.

2012), and they have a limited capability to serve on internal board committees (Jiraporn et al. 2009). All in all, this ‘busyness’ problem may lead to corporate governance problems in the company (Fich and Shivdasani 2006), which indirectly affects the firm’s value (Jiraporn et al. 2009; Vafeas 1999).

Therefore, consistent with the finding, from the lens of agency theory, outside directors’ ‘busyness’ may reduce the management monitoring activity and lessen their participation in small board committees, hence resulting in the incremental cost of agency problems. Consequently, this deteriorates the firm’s value (Core et al. 1999; Ferris et al. 2003). Moreover, the monitoring role in an emerging market like Malaysia is one of the supreme concerns of foreign investors, compared to the developed market, as the directors’ monitoring role may be superseded by the steady existence of efficient regulations to protect investors’ investments (Booth et al. 2002), for example the Sarbanes-Oxley Act 2002, as previously discussed.

In Malaysia, even though there is no maximum number of directorships prescribed in the Code, it is recommended that the appointment of a new director to the board must go through a screening and assessment process held by a nomination committee. One of the objectives of this assessment is to consider the level of commitment that they can offer to benefit the company. Nonetheless, aware of the potentially hazardous effect of over-committed directors, the government of Malaysia has used its superior power to pressurise PLCs in Malaysia to restrict the number of directorships at any one time for each director on their board, through the Listing Requirements of the Bursa Malaysia. The motive behind this restriction is to ensure that the directors can discharge their responsibilities efficiently.

Drawing on the institutional theory perspective, in order to search for legitimacy and to be recognised by society, the PLCs in Malaysia have to follow the prescribed requirements. The pressure placed upon the PLCs by the government of Malaysia is an effort to maximise shareholder value in the form of *coercive isomorphism*, adopting the governance structures of the Anglo-American system (DiMaggio and Powel 1983). Foreign investors are argued to be selective in this context, in their

attempt to avoid investing in companies where the directors have too many outside commitments, as this can dilute their quality time in the company. Foreign investors are more confident in placing their investment in PLCs that abide by this rule, whereby the directors are expected to give a reasonable commitment to increasing shareholder value, simultaneously mitigating the agency problem. Hence, as indicated by the findings in this study, multiple-directorships imply a negative signal to foreign investors as equally perceived by investors in developed markets. However, in this context, institutional theory plays a major role in explaining the relationship between multiple-directorship variables and the level of FEO in Malaysian companies.

8.2.2.3 Female Directorships

The earlier presupposition, drawing on a multi-theoretical approach, views the presence of women directorships on the board as one of the crucial factors that could attract foreign investors. However, the results depict a different picture and disprove the idea that the female director(s) could affect foreign investors' investment decisions. Despite many empirical results which present a positive association between women directorships and firm value, which indirectly translates as good governance practice and is preferred by foreign investors in Malaysia, in the light of this study, no significant relationship is recognised.

According to the Grant Thornton International Business Report (IBR), Malaysia has the highest number of women in the workforce compared with other Asian countries, yet has the lowest proportion of senior roles occupied by women, at only 26%. The data also shows that Malaysia is ranked third globally to have women on the board of companies in the role of chairperson, chief executive officer, chief financial officer, executive and non-executive director. This corporate environment does not seem to be very promising for nurturing the involvement of women directors on Malaysian boards, or is still in its infancy phase. This is one of the explanations why the relationship between women directorship and foreign equity is found not to be significant, and is a negative relationship.

It is believed, at this stage that the institutional environment in Malaysia cannot be compared with other developed economies, even though it is moving forwards to achieve that level. At this point, it may be seen that foreign investors' decisions do not hinge upon the presence of women directors on the board as they are still sceptical about the roles played by women directors in Malaysia. Thus, the presence of women directors on the Malaysian board makes no difference to foreign investors as they view them as only 'tokenism' (Wellalage and Locke 2013) (see 4.4.2.3 Female Directorships where the concept of tokenism is discussed).

Relatively speaking, in developed countries, for example in the year 2005, *Fortune 500* boards documented that 15% of the total boards had three women directors or more and 36% of the boards had at least one woman on the board (Konrad et al. 2008). These figures show a huge different with what is happening in Malaysia. The table below depicts the percentage for the scenario of PLCs in Malaysia.

Table 8.1: Women Directorship on Malaysian Boards

	WOMEN DIRECTOR ON BOARD			
	One (1)	Two (2)	Three (3)	> three (3)
<i>Observation</i>				
n=1836	26%	12.15%	0.82%	0.00%

From 1836 observations, 26% of the companies have only one female director, 12.15% do not exceed two female directors and 0.82% of the observations have more than two females on the board or exactly three. From the sample observation, no company is found to provide more than three women directorships. The majority of companies in Malaysia (more than 50%), have no female directors serving on their boards, while 39% of the companies have at least one female director, but only 13% have more than one. This slim percentage of female representation on the board, which has apparently occurred in Malaysia, can be regarded as evidence of 'tokenism' (Branson 2007).

As argued in Chapter 4, the existence of gender diversity on the board can increase the level of board independence. This can be achieved when people with different gender have different views about any issue arising in the company, which from the

perspective of agency theory will reduce the principal-agent monitoring cost. However, the effectiveness of monitoring also depends on the proportion of gender representation on the board. A small proportion may only provide a marginal effect and not be significant in influencing board decisions. Hermalin and Weisbach (2003) suggest that, despite the insights derived from the theory pertaining to board diversity, it is not particularly useful for explaining board-specific phenomena.

For example, the study by Konrad et al. (2008) implies that even though women directors can make a positive contribution, the 'number' is pivotal in order to make a difference. 'Three' women on the board is considered an 'ideal' number for women to speak more freely and to assure that their points are not taken lightly. The reality in Malaysia is quite different, however, with only 0.82% (see Table 8.1) out of the total observations following this implicit 'rule'. Thus, making their presence felt is not significantly appreciated by the foreign investors in making investment decisions concerning Malaysian companies. Indeed, from the view of the observed data, foreign investors consider female directorships on Malaysian boards as a negative influence on the board, as the appointments are not made purely based on the director's expertise.

The above claim is underpinned by the fact that most of the women on the board come from family-controlled companies. During the data collection process, from the general observation⁴¹, it is common to see the presence of women directors on family-controlled company boards. After further investigation, most of them are found to have a family relationship with the other directors. From the total group of companies (n=722) with women on the board, 67% are family-controlled companies (n=485). Therefore, it is strongly believed that no stringent conditions have been imposed to make them appoint a minority (woman director) onto the board, in terms of the expertise or qualifications needed for corporate directorship. The motive is more

⁴¹Observations were made during the execution of the data collection process. However, no empirical records are made to prove this claim. Future study is sought to examine this issue.

about expanding the family business empire by controlling the board of directors. This is contrary to the suggestion made by Konrad et al. (2008), which is that the selection of women directors should be based on the required skills needed on the board for obtaining future benefits (Hillman et al. 2007), and they should not be brought in as a token.

Nevertheless, it is interesting to note the argument made by Carter et al. (2003) that either significant negative or non-significant estimates of this relationship do not mean that women are poor in their directorship. In Malaysia, it may be plausible to assume that a firm using women as “tokenism” means that the culture of the firm is not conducive to their success as directors. Therefore, with this in mind, the explanation of the negative but insignificant relationship has been answered. The results are also consistent with the empirical studies by Marimuthu and Kolandaisamy (2009) and Shukeri et al. (2012), who found that gender effects have no significant relationship with regard to Malaysian companies’ financial performance. Thus, it is concluded that in Malaysia, given the rational of country and corporate culture (Kang et al. 2010; Shukeri et al. 2012), foreign investors are not interested in considering women directorships in making their investment decisions in a company. In this context, institutional theory is argued to be the most applicable theory in explaining this situation.

8.2.2.4 Financial Expertise of Directors

The hypothesis drawn from the multi-theoretical approach was that directors with financial expertise are positively associated with the level of foreign investment in a firm. This implies that a higher proportion of professional directors with financial expertise on the board will attract more foreign investors to make investments. This hypothesis is supported by the significant association revealed in the main statistical analysis.

The ability of professional directors to read, comprehend, analyse and translate financial statements is likely to influence the investment decisions of foreign

investors. This underscores the fact that the wave of accounting scandals around the world is not taken lightly by foreign investors. Thus, directors with the right qualifications (Code 2007) are desired, consistent with the escalation of high-profile cases of accounting scandals (Krishnan and Visvanathan 2008). Foreign investors prefer directors with financial acumen to assist in the overseeing function, therefore, protecting shareholders' interests (Burak Gurner et al. 2008). It can be argued from the perspective of agency theory that the appointment of directors with financial expertise onto the board leads to a decrease in the monitoring cost. Besides, directors with a professional qualification are likely to cling to the same values, which are centred on maximising shareholder value, thus mitigating agency problems.

As argued, directors with financial expertise are able to understand the financial information presented in companies' reports (Burak Gurner et al. 2008). Thus, in turn, the reports produced by the company are more likely to be at a higher quality level (Krishnan and Visvanathan 2008). Invoking an RDT, amongst the benefits of having financial expertise on the board are: fewer earning statements (Agrawal and Chandha 2005), positive stock reaction (Defond et al. 2005), and the skills and expertise possessed by these directors can assist management in making important decisions for the company, which can increase a firm's value (Hillman et al. 2000).

In Malaysia, where investor protection mechanisms are still in process, directors with accounting and financial acumen are highly sought after by foreign investors in order to protect their investment. Indeed, the use of standard accounting practice such as the International Accounting Standards (IAS), and the application of US GAAP is oriented based on shareholder value (Tuschke and Sanders 2003). IAS has been adapted in Malaysia, with the name Financial Reporting Standard (FRS), and PLCs in Malaysia must comply with the accounting standard in preparing their financial reports. In institutional theory terms, this can be viewed as *coercive isomorphism*.

Recalling the previous discussion on directors with financial expertise in Chapter 4, invoking an institutional theory, in summary, there are three levels of the isomorphism process that have been adopted, which are in close proximity to the Anglo-American

mechanisms, and they are coercive, mimetic and normative isomorphism (see Section 4.4.2.4 (i) Directors with Financial Expertise). *Mimetic* refers to the imitation of mechanisms, codes and practices from the Anglo-American markets. *Coercive* refers to the fact that these were later enforced on the PLCs (by the government of Malaysia) through the revised Code 2007. *Normative* refers to the idea that this led to the diffusion of values and practices by the professional directors (this stems from professionalism) across the firms which derived from the growth and elaboration of their professional network.

Therefore, in this study, the financial expertise of directors is viewed as a strong determinant for foreign investors in deciding their investment allocation. The similarity, familiarity and the values held by professional directors are favoured by foreign investors. Foreign investors discern that the effort to mimic the best practices of corporate governance from Anglo-American capitalism is an attempt to obtain legitimacy in order to gain access to more resources for the company to survive and remain competitive. Thus, it can be concluded that institutional theory leads the other two theories in explaining the relationship between two variables.

8.2.2.5 Directors with a Western Educational Background

An extension to the above arguments, explaining the role of professional directors in attracting foreign investments, is relevant here, where firms with a higher proportion of directors with a Western educational background are more likely to draw the attention of foreign investors. The result supports the hypothesis whereby the relationship between directors' Western educational background is positively and significantly associated with the level of foreign equity ownership.

The values embedded by the directors on the board, received during their formal education in Western institutions, are highly favoured by foreign investors when making investment decisions. It is argued that foreign investors place a high reliance on directors to make company decisions in the best interests of shareholders. Directors' educational background is claimed to assist management in strategy

evaluation (Ruigrok et al. 2006). Thus, with the same values and perspectives emanating from the same educational system, foreign investors infer that these directors will act towards maximising shareholder value.

It is suggested that organisations are shaped by the normative pressures that pervade them (DiMaggio and Powell 1983; Meyer and Rowan 1977; Zucker 1987). In this scenario, the source of normative pressure is derived from the directors' educational background, which may result in changes in the organisational structure occurring in an isomorphic way according to institutionally prescribed expectation (Slack and Hinings 1994). In the case of PLCs in Malaysia, foreign investors seem to express a strong preference for companies with a presence of directors with a Western educational background on the board. It is argued that these directors may preserve foreign investors' interests in the company as they share similar values, which is to maximise shareholder wealth.

Drawing on the perspective of agency theory, foreign investors may view the existence of directors with a Western educational background on the board as a positive signal of improved governance. The exposure, values and educational background received by these directors share similarities between the directors and the foreign investors. Therefore, foreign investors feel they can depend upon the expected integrity that these directors uphold when making important company decisions or while performing their duties in the company, which results in decreasing monitoring costs.

From the view of RDT, the existence of directors with a different educational background may promote heterogeneity, which is claimed to have a positive impact on a firm's performance (Douma et al. 2006). They can advise on global experiences (Masulis et al. 2012), breaking the traditional board deadlock by provoking the board meeting with different thought paradigms to solve any issues raised in the company. These directors seem to advocate a new management practice, which is centred on the Anglo-American governance practice. Instead, consistent with the institutional theory perspective, this is referred to as normative isomorphism. Again, for this variable,

institutional theory has offered better justifications to explain the explicit outcome from the hypothesised relationship.

8.2.3 Ownership Structures as Determinants for Foreign Investors' Investment Decisions

The following discussion is aimed at answering the third research question. In this regard, three ownership variables were tested to understand their relationships with the foreign equity level in a company. These variables are family-controlled companies (FCC), managerial ownership (MANTOW) and institutional ownership (INSTOW). Of these three variables, two – FCC and INSTOW were found to be significant. These significant results will be discussed in detail in the next sub-sections.

8.2.3.1 Family-Controlled Company (FCC)

One of the tenets of shareholder value is diffuse ownership. There are many studies which demonstrate the significance of diffuse ownership in achieving the ultimate objective of shareholder value maximisation (LaPorta et al. 2000). Kim et al. (2010) find that foreign investors outweigh firms with low ownership concentration, indicating that they disfavoured family companies during the unstable and volatile period. The results documented in this study seem to reinforce the claim, which is also consistent with the findings by Tsamenyi et al. (2007).

Even though many studies offer evidence that family companies are better in terms of performance (Anderson and Reeb 2003; Daily and Dollinger 1992; Margaritis and Psillaki 2010; Maury 2006; Villalonga and Amit 2006), this notion seems true with certain limitations. In particular provinces, the differences in institutional environment hinder the generalisation from being applied uniformly. As asserted by Peng and Jiang (2010), the impact of family control on a firm's value hinges upon the level of investor protection enshrined in the legal and regulatory institutions of a particular country. For a country like Malaysia, the controlling power and higher concentration

of large shareholders, especially by family members, are prevalent, whereas the investor protection is weak (Peng and Jeng 2010). The structure of ownership elements in this country shows resistance to institutional pressures – inconsistent with the development of the modern corporations of the US and the UK which started with concentrated family ownership (Chandler 1990) but then, over time their ownership became dispersed (Berle and Means 1932). These resisting elements, either stay static, do not change rapidly, or do not change as much as the others (Slack and Hinings 1994). Therefore, foreign investors perceive a family business through a different lens when making investments in two different countries.

It is argued that the main explanation for this is the existence of the country's institutional regulations concerning investor protection (La Porta et al. 2008; Peng and Jiang 2010; Young et al. 2008). Consequently, prospective minority shareholders such as foreign investors may be less passionate about making investments, as they are sceptical of the ineffective investor protection and the expropriation by controlling shareholders. These situations encourage concentrated ownership, for example family ownership becomes more visible and prevalent in these countries (La Porta et al. 2000; Young et al. 2008).

Likewise, by invoking a branch of agency theory, based on principal-principal conflict it is asserted that the greater the control of family companies, the greater the opportunities to expropriate minority interests, which results in reducing a firm's value. Even though there are two sides to agency theory to be grasped, based on the results, it is likely to associate FCC with high agency cost organisations, even though RDT advocates otherwise.

Hence, based on the theoretical arguments, from the institutional theory perspective, foreign investors, when making investments in countries with weak institutional and governance regulation, such as Malaysia, discern FCC in a negative manner. In addition, agency theory associates FCC with high agency cost, but resource dependence theory is weak in explaining the negative relationship between foreign investors and FCC. Thus, for this variable, agency theory plays a prominent role in

explaining the reaction of foreign investors towards the family-controlled companies when making decisions on investment in the Malaysian equity market.

8.2.3.2 Managerial Ownership

The earlier conjecture tried to suggest that there is a negative relationship between managerial ownership (MANTOW) and foreign equity ownership (FEO). However, the results reveal that managerial ownership does not influence foreign investors' in their investment decision process. The study failed to demonstrate any relationship between managerial ownership and foreign equity ownership, regardless of any of the models utilised or any of the analyses conducted.

The fact that the firms with high managerial ownership appear to prevent foreign shareholders from making their investment was refuted by the recent finding. The managerial ownership factor has been given no preference by foreign investors when investment decisions have to be made. It is argued that the results are highly connected to the institutional settings and corporate governance system in the particular countries. Therefore, the impact of managerial ownership in the developed markets cannot simply be generalised to other counterparts. In Malaysia, where the common type of ownership is concentrated ownership, owner-managers are prevalent among PLCs (Liew 2007; Mat Nor and Sulong 2007), especially in family companies (Haniffa and Hudaib 2006). Thus, the top management are usually selected from their family members (Peng 2006).

Therefore, it can be postulated that foreign investors are not sensitive to managerial ownership in Malaysia as it may be argued that foreign investors will scrutinise the factors that emanate from the form of managerial ownership, rather than the managerial ownership itself, (e.g. family-controlled companies) when making their investment decisions. The factors that influence the form of managerial ownership will dictate whether the firms will benefit from or be harmed by the possession of ownership by the managers. Thus, the practicality of relying on managerial ownership

to decide on investment seems to be less relevant (see the arguments from the perspective of theoretical approach discussed in Chapter 4).

This finding can be explained by the uniqueness of corporate ownership in Malaysia as depicted in Chapters 2 and 4. From the data observed, out of the total observations (N=1836), 67% (1237) of them are firms with the total managerial ownership (direct or indirect) of 20% or above. Interestingly, out of 1237 firms with substantial managerial ownership (above or equal to 20%), 80% (985) of them are family-controlled companies. This figure (985) represents 92% of total FCC. The figures demonstrate that the ownership in Malaysia is concentrated and it is asserted that the ownership structure in Malaysia is resistant to institutional pressures. Hence, it remains in its initial structure or if changes happen they are at a slower pace (Slack and Hinings 1994).

Therefore, foreign investors heed the warnings from the series of financial turmoil, accounting scandals and the weakness in corporate governance systems, to examine the basic form of company ownership, which later may exercise its influence on the managerial ownership of the firm. The arguments made from agency theory: principal-principal conflicts, offer sturdy justifications as to where foreign investors should place extra precaution when making investment decision in capital market with concentrated ownership like Malaysia as the possibilities for being manipulated by controlling shareholders are higher. The controlling shareholders can exercise their control by the appointment of their proxies in the companies or precisely choose their selected manager(s) to run the company. Thus, the managerial ownership should be scrutinised beyond the ownership itself, to consider the real structure of company's ownership. In the continuation, institutional theory provides a sensible explanation that foreign investors give priority to understanding the company's basic ownership form, whether dispersed or concentrated (etc. family-ownership), as the institutional background in Malaysia is not strong enough to protect shareholder interests. In addition, managerial ownership can easily be manipulated by controlling shareholders.

An important point here is that despite the voluminous literature, which yields mixed results on managerial ownership, this study provides an interesting argument from the multi-theoretical perspective. Corporate governance in Malaysia, which is claimed to be moving towards Anglo-American methods, is found to be left far short of convergence to the system when comparing their ownership structure. Obviously, there are difficulties in transferring Anglo-American institutions to certain countries that are resistant to the changes as they have different cultures, traditions and practices. Therefore, foreign investors place less emphasis on managerial ownership in their investment decision making in Malaysia, and place extra precaution on the determinants that may influence managerial ownership, rather than the managerial ownership itself. Thus, the arguments made from the perspective of the multi-theoretical approach, especially agency theory, are relevant to explain the outcome explicit for the hypothesis of managerial ownership with the level of FEO.

8.2.3.3 Institutional Ownership

Institutional shareholding was found to be significant and negatively related to FEO in both models, as shown in Table 7.6: Regression Results for GLS Estimation Models. This indicates that foreign investors act differently to institutional investors. This opposes the argument made by Dahlquist and Robertson (2003) that institutional and foreign shareholders can be depicted in similar ways, which is evidenced by Smith (1996) and Strickland (1996), to provide a positive impact on a firm's value. The result, however, is in agreement with the finding by Kim et al. (2010) which documents the opposite reactions of the two groups toward similar variables, for instance 'foreign directors' and 'foreign listing' are two variables that are favoured by foreign investors but negative signs are shown by institutional investors. The study also mirrors the findings by Karpoff (1996), Wahal (1996), and Faccio and Lasfer (2000), who questioned the monitoring ability of institutional investors. On the other hand, Mangena and Tauringana (2007) found a significant and positive relationship between FEO and institutional investors in the Zimbabwe Stock Exchange. However, it can be explained that these companies are found to be strong in corporate governance mechanisms.

Nevertheless, the result of this study can be explained by the arguments proposed by Suto (2003). He suggests that the major proportion of institutional shareholders in Malaysia consists of Malay shareholders. Malay shareholders are claimed to be passive shareholders, since most of the time they just follow what is stated in the government's policy. Instead, the government is actually the real player that charts the direction for institutional shareholders in Malaysia. Therefore, it is argued that as long as the Malay people are given preferential treatment in government policy pertaining to the equity in leading institutions in this country, more silent shareholders are produced. Therefore, the free-rider problem is not resolved and can become more severe. Further, Malay shareholders are claimed as not being capable of disciplining the management in the firm in which they invest (Suto 2003). Thus, the agency problem is not mitigated.

However these claims are disputed by Mahathir Mohamad⁴² (2013), the prominent leader and the former prime minister of Malaysia. In his argument, the make-up of the Malaysian government, whereby the majority of the officers and employers are dominated by Malays, has proven that they can rule the country efficiently. Malaysia has thrived in many respects and its economy has flourish rapidly, if compared with the countries that achieved their independence within close proximity. In fact, the currency crisis that hit Asian countries in 1997/1998 was able to be managed efficiently by the Malay-dominated administration. Therefore, the people in Malaysia, regardless of their race, equally enjoy the country's prosperity (read more in <http://chedet.cc/?p=1103>).

Nevertheless, in the context of Malaysia with its different institutional background, foreign investors take more precautions. In the developed capital market, institutional

⁴² Tun Dr Mahathir Mohamad is an active Malaysian politician. He was the fourth Prime Minister of Malaysia. He held the post from 1981 to 2003, equal to 22 years in administration; making him Malaysia's longest serving Prime Minister. His political career spanned almost half a century and, indeed, he is a very influential political figure in Malaysia and is respected worldwide.

investors have the capacity to ensure that their voices are heard (Seki 2005), and that they play an active role. Indeed, they can use the mechanisms of ‘*exit*’ and ‘*voice*’. However, as previously claimed, in Malaysia, shareholder activism is still in its infancy phase and promoting shareholder value is an undertaking in progress. Therefore, foreign investors do not substantially rely on institutional ownership to gauge the effectiveness of the corporate governance system practiced in a company. Based on the previous arguments, theoretical justifications (mainly institutional theory) and the documented results, institutional ownership is even discerned by foreign investors to be a negative determinant when deciding whether to invest in a firm. Therefore, it should be avoided.

8.3 Summary of the Analyses

Restated: Table 7.11: Summary of Results for All Analyses

Variables	Hypothesis Number	Main Analysis			Additional Analyses			
		GLS regression			Logistic regression		GMM estimation	
		Outcome	Expected Sign	Prominent Theory	Outcome	Expected Sign	Outcome	Expected Sign
<i>B</i> SIZE	<i>H</i> ₁	+	/	IT	+++	/	+	/
<i>B</i> COM	<i>H</i> ₂	-	X	AT	+*	/	-.***	X
<i>DIR</i> FOR	<i>H</i> ₃	+++	/	IT	+++	/	+++	/
<i>DIR</i> MUL	<i>H</i> ₄	-.***	/	IT	-	/	+	X
<i>DIR</i> WOM	<i>H</i> ₅	-	X	AT	+	/	+*	/
<i>DIR</i> PROF	<i>H</i> ₆	+++	/	IT	+	/	-	X
<i>DIR</i> WEST	<i>H</i> ₇	+++	/	IT	-.**	X	-.***	X
<i>F</i> CC	<i>H</i> ₈	-.*	/	IT	-.*	/	-	/
<i>M</i> ANTOW	<i>H</i> ₉	+	X	AT	+	X	-	/
<i>I</i> NSTOW	<i>H</i> ₁₀	-.**	/	IT	-	/	-.***	/

Notes: ***, ** and * denote that the correlations are statistically significant at the 0.01, 0.05 and 0.10, respectively (2-tailed).). “/”= Outcome as per expectation, “X”= Outcome is not as per expectation, IT=Institutional theory, AT=Agency theory, *B*SIZE=Board size, *B*COM=Outside Director Compliance, *DIR*FOR=Foreign Director, *DIR*MUL=Multiple-directorship, *DIR*WOM=Woman director, *DIR*PROF=Director with professional qualification, *DIR*WEST=Western Education director, *F*CC=Family-controlled company, *M*ANTOW=Management ownership, *I*NSTOW=Institutional Ownership.

Table 7.11 is restated. This section is put forward to reiterate the results of three different analyses (GLS regression, logit regression and GMM) in order to elucidate the differences that come into view with more caution. In summary, the results from the three analyses are technically consistent with each other, albeit with slight

differences. First, it is remarkably interesting to find the potent relationship between foreign directorship (DIRFOR) and the level of foreign equity ownership in the firm. The results from the three analyses for DIRFOR are persistently significant in a positive direction, regardless of any models or any types of regression analyses. The result is robust even after controlling for time-fixed effects, firm specific characteristics and endogeneity.

From the Table 7.11, too, the explanatory variables have been classified in terms of the most applicable theory to successfully explain, or which is close to perfect in explaining the hypothesised relationships. To shed some light on this, institutional theory seems to dominate the discussion of outcome analyses and surmount the other two theories in giving realistic justifications as to the emerging correlation between the two variables. However, agency theory that was applied beyond the principal-agent relationship in this study, or more specifically the principal-principal conflict, also played an important role in offering a profound understanding of a particular issue in the Asian corporate environment, especially the Malaysian capital market (for example; concentrated ownership, minority shareholder expropriation, controlling shareholders, etc.). Nevertheless, despite not being the main theory, the importance of RDT's role cannot be disputed as it helps to strengthen the justifications given to explain the outcome of the analyses.

The results of the main analysis, GLS regression, are presented and discussed in detail throughout the chapter. Thus, in this section, the results of the additional analyses (logit regressions and GMM) are featured to find possible explanations that might be important to be deciphered. For Logit regression, (see Table 7.7: Regression Results for Logit Estimation Models) the positive and significant relationship between high FEO firms and BSIZE, DIRFOR and BCOM were documented, while a negative relationship was found between high FEO firms and DIRWEST and FCC. This result implies that when the equity acquired by foreign investors is at 20% or higher, the corporate governance variables that have predictive properties are board size, the number of foreign directors on the board, outside director compliance, directors with a Western educational background and family-controlled companies. Given the number

of corporate governance variables associated with this dummy variable, it corroborates the generalisation derived from the main analysis, GLS regression that corporate governance attributes do influence foreign investors' decision making with regard to Malaysian companies.

However, there are some changes in the determinants of foreign investment in terms of significant values and direction, whereby the variables that were previously insignificant (BSIZE and BCOM) were found significant. On the other hand, the variables that were previously significant (DIRMUL, DIRPROF and INSTOW) were found to be insignificant. Besides, there is a variable that previously showed a positive direction (DIRWEST) which conversely showed a different direction (negative). The other two variables (DIRFOR and FCC) remain in a similar pattern with the GLS regression results. These changes can be simply explained as resulting from the changes in the foreign equity proportion, which leads to the power to exert a significant influence on the company's direction.

Therefore, as the proportion of a firm's foreign equity increases, corresponding to the foreign investors' influence in the firm, the board size and the board composition become important. Previously, these variables were not favoured in making investment decisions in Malaysian firms (the discussion was provided in Section 8.2.1.1 Board Size and 8.2.1.2 Outside Director Compliance). However, with the accumulated equity possessed and the escalation of power, the preference has now diverged. The change in foreign investors' preference is argued to emerge from the increase of power to influence management and to dictate the company's direction. The significant influence gained by foreign investors enables them to at least intervene in deciding the size of the board (BSIZE) and to select the outside directors (BCOM).

It is important to note here that the results from the second additional analysis, logistic regression was run to understand the differences between two groups of companies, those with high and low FEO – thus, it cannot be used to replace the main results from GLS regression as they measure different things. As previously explained,

logistic regression was applied to provide an additional explanation, but not to transcend the main GLS regression results which were principally applied to answer research objectives of this study. The results from logistic regression are considered as a complement to better understand foreign equity ownership in Malaysian companies.

Next, the results from the GMM estimation model further reinforced foreign directorship (DIRFOR) as the powerful explanatory variable to attract foreign investors when making investments in Malaysian PLCs. Likewise, institutional ownership (INSTOW) reiterated a similar result as well. However, apart from these two variables, the GMM estimation model showed a lack of consistency with the GLS regression results, and this can be explained from four angles.

First, based on the justifications and empirical results, GLS regression analysis was chosen as the main econometric technique that is suitable to analyse the data efficiently. Thus, an additional test is run to strengthen the results further, and any deviation from the main results may not impair the result (see Section 7.4 Panel Data Related Tests and its subsections and Section 7.5 Multivariate Analysis). Second, the use of the GMM estimation model was aimed at dealing with the potential endogeneity issue in the model. However, this issue has been well defined (see Section 5.7.7.2 Endogeneity) by following a few of the researchers' practices such as Jiraporn et al. (2009), Cheng (2008), Bebchuk and Cohen (2005) and Peng and Jiang (2010). Next, even though Blundell and Bond (1998) claim the superiority of the GMM estimator over other estimators, there is a validity issue with the results when the number of observations is small (Soto 2007).

Finally, in this study, GMM used only 'lag of time' as an instrument which considered as the basic instrument. More appropriate instruments are needed to yield more competent results, in order to infer the population. However, it will take a significant amount of time to identify the instrument, and collecting the data consequently prolongs the entire research process. Nevertheless, in future study, the appropriate instrument(s) will be identified and scrutinised to construct a more efficient model, and yield more reliable results. Therefore, the results produced by the current GMM

estimation model are used to support the results derived from the main analysis, GLS regression, but not to transcend the main results.

8.4 Research Contribution

This section discusses the contributions of this study to the body of knowledge – in terms of its theoretical and methodological implications – for regulators and policymakers. An analysis is made based on the relevance of the study to the literature and theoretical development in the corporate governance purview, alongside the methodological standpoint. Its implications are also put forward in terms of the future practical actions to be taken by the related parties in setting up a new policy, designing new rules and strengthening the existing regulations in terms of corporate governance practices for Malaysian companies in order to attract foreign investors. Overall, the contribution of the study is discussed in terms of its literature, theoretical, methodological and practical contributions.

8.4.1 Literature Contribution

Overall, this study contributes to the extant literature in four notable ways. First, this study applies and extends our understanding of corporate governance mechanisms in the context of foreign investment in Malaysian firms. This is important, given the nature of corporate ownership peculiar to Malaysia, while taking into account the institutional framework and the historical background of the Malaysian corporate governance structure in the aftermath of the Asian financial crisis of 1997/1998. Although there is a growing literature on corporate governance issues on Malaysia, however, there is an absence of research examining the relationship between corporate governance mechanisms and FEO. Indeed, previous research has focused on the effects of corporate governance on firm performance, without consideration for other dependent variables (Ponnu 2008). The findings of empirical studies carried out in the US, the UK, Sweden, Japan, Korea, and other countries regarding corporate governance and FEO were found to be slightly mixed. Thus, by conducting this study, it contributes to the extant literature and provides more evidence on the corporate

governance system in relation to foreign investment based in the Malaysian setting, with a great possibility of applying the findings to other Asian countries that have culture and institutions closer to Malaysia.

Correspondingly, the setting of this study is focused on the institutional background which is designated in Malaysia, at the peak of corporate governance reform in the aftermath of the Asian financial crisis 1997-1998. Drawing upon institutional theory as the main insight, the analyses of governance variables in Malaysian firms are viewed from the reworking of corporate governance due to the harsh changes in the macro institutional environment (Chizema and Kim 2010) – or specifically the Asian currency crisis 1997/1998. This study reinforces and extends the extant literature on the relationship of corporate governance and foreign ownership in Malaysia by considering its macro environment, social, socio-cultural, beliefs, values, judicial systems, etc. These elements are embedded in every organisation and should be heavily reviewed (Peng 2002). Therefore, the behaviour of foreign investors in making investment decisions in particular countries, such as Malaysia, can be comprehended.

Furthermore, the use of PLCs in Malaysia as a sample may provide useful information in making comparative studies with corporate governance and FEO in other countries, either from the same region, or a different continent. To date, there is a lack of studies concerning corporate governance and FEO in Malaysia, as well as in many emerging economies. The findings of this study may shed some light on investors' investment behaviour in relation to corporate governance in Malaysia. In particular, the factors that are key to foreign investors' preferences should first be analysed profoundly before further assumptions in terms of its resemblance or dissimilarity across countries are proposed.

Finally, this study leads to the contemporaneous debate pertinent to the reformation of Malaysian corporate governance in line with the Anglo-American system. There are disconcerting views regarding the convergence, either the reformation process is persistently applied, staggered, or there is a resistance element in the institutional

environment of Malaysia that hinders the convergence process. To my knowledge, this kind of study has yet to be done in a Malaysian institutional setting. Thus, discussion on this issue is very limited and indeterminate. Nevertheless, this study has not provided evidence as to whether convergence is taking place or otherwise. However, efforts have been made to demonstrate any possible influences which might impact the adoption of particular governance innovations – one of the signals that represent the undertaking of the convergence process towards the Anglo-American corporate governance system.

Nonetheless, this observation contributes to identifying and measuring the contribution of different institutional variables to a particular governance innovation.

8.4.2 Theoretical Contribution

In terms of theoretical contribution, this study regards institutional theory as one of the main theories to provide explanations concerning foreign investors' behaviour toward corporate governance practices when making investments in Malaysian firms. It is contended that the prevalent theories applied in corporate governance studies, such as agency theory and resource dependence theory, have argued for the positive and negative sides of certain variables to be connected with foreign ownership. However, this study took a step forward when, at the same time, it explored the Malaysian institutional context in order to provide arguments for the hypothesised relationships. Thus, this study advances an understanding of institutional theory by applying the lens in an environment distinguished by unique corporate ownership structure following a period marked by changes in the external environment as a result of the Asian financial crisis 1997/1998. The institutional-based views may assist in explaining several of the findings that seem to contradict each other. Drawing on the institutional theory perspective, the differences emerged due to the divergence of the institutional frameworks in each country, not due to the corporate governance variables that are 'favourable' or 'unfavourable' to foreign investors, as these foreign investors do not perceive these variables uniformly across countries. They hinge upon the institutional background in the respective countries (Peng 2002).

Secondly, this study underscores the salience of the institutional context to the study of corporate governance reformation. Peng (2002) asserts that no firms are immune to the institutional framework of the environment in which they operate, thus, the issue of institutions is important. More specifically, it contends the institutional force and dynamic changes of corporate governance that have been experienced by the Malaysian business environment in the aftermath of the Asian financial crisis 1997/1998. There are sturdy signs that in Malaysia, corporate governance is gradually converging towards the Anglo-American model (Haniffa and Hudaib 2006). This converging process has been undertaken in order to strengthen the system (Ho and Wong 2001) and regain investors' confidence to ensure the inflow of fund to the country. Thus, the universal application of agency theory in this kind of corporate governance study is questioned for its applicability (Aguilera and Jackson 2003).

Next, this study puts forward some arguments as to the insufficiency of theoretical arguments to support the hypothesised relationship based on only a unitary perspective. Agency theory and resource dependence theory are the common theories applied in corporate governance studies. However, the insights from these two theories are of little value to the firms in emerging economies with different institutional backgrounds (Fama and Jensen 1983), in contrast with developed economies. Therefore, institutional theory is affixed to better explain the institutional changes of corporate governance in Malaysia, especially after the Asian financial crisis 1997/1998. In referring to the Table 7.11, it may be seen that the theory which works best for this study is institutional theory. Institutional theory seems to dominate the discussion of outcome analyses and surmount the other two theories in giving realistic justifications for the outcome of hypotheses tested.

However, Table 7.11 also indicates the importance of agency theory as a theoretical lens in explaining the outcome of analyses conducted. In this regard, it is argued that this study offers an additional perspective of agency theory which rarely applied in the extant literature for Asian capital market, especially Malaysia. There are some exceptions, such as the study of China's capital market by Peng (2002), Peng (2004), Peng and Jiang (2010), etc., where the arguments were made beyond the basic

principal-agent conflict, to place greater emphasis on principal-principal's goal incongruence (revisit Section 3.3.3 Principal-Principal Conflicts for details). Thus far, the studies that examine the capital market in Malaysia merely focus on applying the basic model of agency theory in explaining the variables by ignoring the characteristics of Malaysian firm that generally associated with concentrated ownership, controlling shareholders, family-companies and minority shareholders expropriation. Therefore, this study provides an additional perspective for understanding the relationship between the examined variables in the Malaysian capital market which are considered to coincide and be relevant to the Malaysian setting.

Finally, this study may be seen to coincide with the current trend for corporate governance study that embraces a multi-theoretical approach to assist in explaining the predicted relationship. Recently, the use of a multi-theoretical approach has received heightened interest in terms of the issue of corporate governance (e.g. Douma et al. 2006; Lynall et al. 2003; Ruigrok et al. 2006). To the best of my knowledge, there is no study that uses this approach for the study of corporate governance in Malaysia. The combination of three theories assists in articulating the influences of variables through a more holistic perspective, which affects the investment decisions made by foreign investors in emerging markets. In essence, the effects of each variable are further accentuated by the incremental value infused from the multi-theoretical approach.

8.4.3 Methodological Contribution

Empirically, cross-sectional data has been used extensively in corporate governance studies to find the answer to predicted relationships. This research aims to look at the same problem but seeks a better and more robust data analysis to give a finer-grained view of the final results. For this reason, the study obtained data from the same firms over multiple years (the term longitudinal study is often used). In this case, the data was collected from the year 2000 to 2011, 12 years in a row. The panel data is particularly useful in answering questions about the dynamics of change and in

predicting long-term or cumulative effects that are normally difficult to analyse in a case study or cross-sectional study. Therefore, it is argued that this study provides more reliable results. Moreover, by using panel data, many analyses can be utilised (for example, fixed-effects estimation and random-effects estimation – see Section 5.7.6 Panel data model). The use of panel data can benefit the final results by increasing their reliability.

In terms of measurement, this study has given meticulous effort to ensure that the definitions of each of the variables included in this study reflect the Malaysian picture, with the rules and regulations applied. However, previous literature was constantly reviewed to ensure the reliability of the defined measurement. Therefore, concomitant with the credibility postulated during the data collection process, the final results of this study are argued to represent Malaysia's corporate governance in its entirety.

In addition, besides the main analysis, which is GLS regression (see Section 7.5.1 GLS Estimation Regression Models), a few other analyses were performed to verify the results and to add robustness to the main findings. The second analysis, Logit regression (see Section 7.5.2 Logit Estimation Regression Models) was performed by transforming the main dependent variable to a binary variable, and the third analysis - GMM (see Section 7.5.3 Generalised Method of Moments (GMM) Estimator) - was then run by adding a lag of the dependent variable into the model to transform it into a dynamic model and also to tackle the endogeneity issue in the model. The additional analyses designed in this study are appropriate to add credibility to the results and they also act as a robustness check for the main analysis. It is argued that the combination of several analyses provides an edge to this study as it will help to establish the findings, could contribute to enrich the field of study, and leads to results that are hard to be disputed and repudiated.

Finally, from the methodological standpoint, the inclusion of a few new variables (e.g. the presence of foreign directors on the board, Western educational directors, female directorship), which were claimed to be variables that obviously represent the convergence elements in line with Anglo-American corporate governance, may

trigger a new platform for discussion in the corporate governance purview in Malaysia. The previous board of directors' literature of corporate governance in Malaysia revolves around board independence, board size, audit committee, etc. Thus, this study offers a new paradigm which allows corporate governance issues to be highlighted.

8.4.4 Practical Contribution

Apart from its theoretical contribution, the findings of this study may also be significant to many stakeholders, such as policymakers, regulators, companies, and also investors, in a number of ways. At the company level, this study helps companies to identify the corporate governance variables that foreign investors favour. Thus, it should be possible for company managers to initiate appropriate actions to attract more foreign investors to invest in their firms.

In referring to the outcome of analyses presented in Table 7.11, the lessons learned from this study are, *inter alia*: i) the appointment of directors to the board should be made based on their qualifications and skills, not merely to safeguard the interests of the family; ii) directors with financial expertise should be sought as an important mechanism to protect the interests of investors, as their financial acumen may help them to understand the risks and the company's financial stability; iii) foreign investors favour directors with a Western educational background, professional directors and foreign directors on corporate board, as these directors are claimed to share the same norms, principles and values. Thus, the decisions made by these directors are consistent with the aim to maximise the wealth of shareholders, and iv) directors with too many board seats on other firms are perceived negatively by foreign directors as their 'busyness' may harm the firm's value by making them lose their quality time in undertaking their fiduciary duties. Therefore, companies may benefit from the recent insights discovered in this study. The necessary actions should then be taken if the companies are interested in pulling more investments from foreign investors.

The findings from this study may have a wider impact on the regulator bodies in Malaysia, such as the Malaysian Institute of Corporate Governance (MICG), the Minority Shareholder Watchdog Group (MSWG), the Securities Commission (SC), and other interested parties, in setting up a new policy, designing new rules and strengthening the existent regulations in terms of corporate governance for Malaysian companies in order to attract more foreign investors (See Section 2.4.3 Corporate Governance Regulatory Bodies in Malaysia, for the roles played by each institution). The understanding of how to increase the effectiveness of corporate governance practices at the firm level is not commensurate with the absence of an effective institutional monitoring system at the country level. Beyond the firm level, policymakers should strive to recuperate the poor image of the corporate governance institution embedded in the foreign investors' perception of emerging markets. The low confidence level of investors towards Malaysian capital market can be seen from Table 7.11, in which the negative relationships are documented for family-controlled companies (FCC) and institutional ownership with the level of foreign equity ownership in the companies.

In order to regain investor confidence, the weak institutions of corporate governance should be eliminated. MSWG for example, should think of better ways to ensure that minority shareholders' interests can be protected from the expropriation of controlling shareholders and ensure this group of investors unruffled when making investments in Malaysian firms. The current operational systems of MSWG do not square well with the objective to protect the interests of minority shareholders, when in fact they are still sceptical about making investments in this country.

The Government of Malaysia may also benefit from this study in deciding the appropriate governance mechanisms for adoption in this country, as portfolio investment from foreigners plays a significant part in economic growth. Policy options can be considered at the national level to encourage more foreign investors to make investments in Malaysia. A lengthy discussion was advanced in Chapter 2 concerning the state of Malaysia's business economy before the Asian financial crisis 1997/1998. Briefly, Malaysia was a fast growing country, however, the potential

growth rate of the Malaysian economy moved to a lower plateau in the aftermath of the financial turmoil. The significant fall in foreign portfolio equity (see Table 2.2: Five East Asian Economies: External Financing, 1994 – 98 (billion dollars) had terrible consequences for the Malaysian economy.

Therefore, this study enlightens the government concerning the behaviour of foreign investors, and how this group of investors discerns the corporate governance issue when making investment decisions. Since this study focuses on corporate governance, there are many elements of the system that can be scrutinised in order to make improvements to attract more foreign investors. The main concern is on the institutional background, whereby the claim that the Malaysian corporate governance system has undertaken major convergence towards the Anglo-American model is not entirely true. There are certain parts of the corporate governance elements that show resistance to the changes, for example, the form of corporate ownership.

The prevalent ownership forms in the Malaysian corporate environment are family ownership and domestic institutional ownership. The results show that foreign investors perceive family ownership and institutional ownership as negative signs for the corporate governance attributes (see Table 7.11 Summary of Results for All Analyses). Therefore, realising the pessimistic influence emerging from these kinds of ownership, the Malaysian government should come up with staggered solutions to overcome these negative reactions of foreign investors. A special code of corporate governance may have pertinence to be applied to family-controlled companies in order to signal to foreign investors that their concerns are being heard. Besides, this study also provides wider implications for governance reform. In essence, the results in this study should be utilised to comprehend foreign investors' perceptions. Therefore, a possible solution could be proposed by the responsible parties. Afterwards, the following discussion is referring to the results presented in Table 7.11 as well.

First, in this study, it is found that foreign directorship (DIRFOR) has a significant influence in attracting foreign investors to invest in a firm. Therefore, the presence of

foreign directors on the board should be considered as an integral part of the Code of Corporate Governance. This will encourage more firms to adopt this practice. A second example is women directorship (DIRWOM) – even though, worldwide, the trend of appointing female directors is escalating due to the intense pressure of many parties, in Malaysia, foreign investors give no preference to this practice. The reason behind this should be carefully investigated and action should be taken by responsible institution(s) to rectify the image of female directors in Malaysian PLCs, hence foreign investors may give some weight to female directors in their investment decision process. If the presence of female directors is appreciated by foreign investors, this mechanism can be a crucial factor in attracting foreign investors when making their investment, as in the other counterparts of the world, foreign investors place so much emphasis on the presence of female directors on the board. Therefore, each of the corporate governance variables examined in this study should be scrutinised, plausible answers should be offered, and realistic actions should be taken to attract more foreign investors to invest in Malaysian companies.

On the other hand, managerial ownership (MANTOW) is disregarded by foreign investors as a determinant for investing in a firm. This is argued to stem from the institutional background and prevalent ownership structure in Malaysia. Managerial ownership is influenced by the controlling power in the firms. Thus, foreign investors pay no attention to managers' equity but to the controlling power of the firms, as this power will steer the firm's direction. The commitment and value creation of managers' ownership may be counted only after the shareholder-value orientation is translated clearly. Hence, again the institutional background and ownership pattern in Malaysia should be given more attention by higher authority powers, e.g. SC, MICG, etc., either to sculpt the appropriate guideline in the form of Codes or to promote a healthy equity distribution within the company. In this regard, institutional theory has played a major role in explaining the institutional setting in Malaysian corporate governance, as can be seen by the categorisation made for the most theory applied in explaining the relationships between corporate governance variables and FEO (see Table 7.11).

In addition, the definition of independent or more generally outside directors (BCOM) should be clearly explained and effectively applied to increase the confidence level of foreign investors. In this study, the findings show that foreign investors place no preference on this variable in making their investment decisions. It is argued that the 'independence' term applied to directors can be questioned. Therefore, there is no point for foreign investors in emphasising this factor as an important determinant to make investment decisions. One of the suggestions which can be offered is to establish an independent body to monitor the appointment of independent directors to the board of directors. This body should be free from any influence and should be established at the higher level, not at the company level. Should the company require any independent director(s), the selection of the director(s) should be authorised by this body. This would ensure that the director(s) appointed are 'really independent' and this may persuade foreign investors to rely on independent directors as guardians of their interests.

In fact, for the remainder of the corporate governance variables in this study, the appropriate parties, such as the government of Malaysia, MICG, SC, MSWG etc., should take collaborating action to further enhance the effectiveness of the corporate governance mechanisms in Malaysian firms. Concern should be given to the adoption of the national corporate governance codes from the developed markets. The compliance with the prescribed codes should be carefully defined either to be mandatory or voluntary, based on a spirit of "comply or explain".

Finally, this study strives to assist local investors by providing them with a better picture of how foreign investors make their investment decisions. It is asserted by Grinblatt and Keloharju (2001) that the degree of sophistication matters when studying foreign investors in the Finnish market. They contend that domestic investors, presumably less sophisticated, take the opposite position to that of the more sophisticated foreign investors. In this case, it is expected that the domestic investors can learn something from this study, such as how to react to and analyse corporate governance and firms' characteristics to make wise, profitable, and secure investments.

8.5 Limitations and Future Research Directions

Notwithstanding the relevance of this study and its timeliness, there are limitations encountered during the process that are worthy of discussion. These suggest a number of avenues to be considered for further research as given below.

Firstly, there is the issue of a ‘single source’ used to collect foreign equity ownership data. There are a few explanations for using this “one source” for data. In Malaysia, as a developing country, in order to be compared with developed countries like the UK and US, it is hard to find available data. An exception can be given to data that need to be publicly disclosed. However, a company’s foreign equity ownership is a part of a company’s private data, and no disclosure needs to be made. To the best of my knowledge, after extensive searching, the data of foreign equity ownership for each Malaysian public listed companies from the year 2000 to the year 2012 (12 consecutive years) could only be obtained from Bursa Malaysia.

However, there are several other sources as well such as the Thompson One Banker, Readers Digest Magazine and company annual reports. However, each of these sources has its own limitation. The limitations are explained as follow:

- (i) *Thompson One Banker database* – this database only provides current year data for foreign equity ownership. However, the data was required for 12 consecutive years, so this was too far away from expectations.
- (ii) *Investors Digest Magazine* – this magazine provides data only for a few years and there are large gaps in the latest data over recent years.
- (iii) *Company’s annual report* - there is a section which presents equity ownership for the highest 30 shareholders. The data of foreign ownership may be obtained from this section. However, there is a limitation, insofar as the disclosure is only made for the highest 30 shareholders. The remaining foreign ownership may be overlooked, and they may hold a smaller number of shares, meaning that they are not included in the disclosure list, but the accumulation of shares held by foreign shareholders may be higher, and significant.

“One source” of data that can only provide this extensive foreign ownership data is Bursa Malaysia. Bursa Malaysia is the only legal party who can access this data from the disclosure made by the shareholders in their Central Depository System (CDS) accounts. Bursa Malaysia is the Malaysian Stock Exchange, and approved under Section 15 of the Capital Markets and Services Act 2007. The data provided by this entity is reliable, widely recognised and used extensively by many scholars to examine Malaysian capital market such as Haniffa and Cooke (2002), Amran and Ahmad (2010), etc. The data relating to foreign ownership provided by the Investors Digest magazine are also sourced from Bursa Malaysia. Therefore, it is argued that there is no issue of data reliability in regards to the “one source” used for foreign ownership data. However, for the purposes of future studies, extensive effort will be made to discover the potential reliable source to enhance the level of data reliability.

Secondly, the study does not make a distinction in regards to the source of foreign investment. It would be more interesting if the countries of origin of the foreign investors can be traced, as the behaviour of investors could differ by country. However, this is a practical limitation, as advice was sought from the Bursa Malaysia in order to access this information – from their feedback it was understood that this information is not made available to the public and is not provided to Bursa Malaysia as well. All PLCs are requested to provide the proportion of foreign ownership out of the total ownership, but not the investors’ countries of origin. However, the countries of origin of the investors may be accessed from The Thompson One Banker database, but this is only available for the current year. Given this limitation, an alternative means of gaining access to the countries of origin of the foreign investors could be determined for future research. There is a possibility that the results would differ if the foreign investors’ countries of origin are identified. Their background may influence their investment pattern. However, given that the largest group of foreign investors in Malaysia is from the US, the discussion is generalised based on this fact.

A third limitation is that this study does not make the important distinction between the two prominent categories of foreign equity holders, namely foreign financial institutions and foreign industrial corporations. Therefore, a coarse-grained picture of

‘foreign investors’ may have been presented. Even though both refer to foreign shareholders in local firms, these two classes of investors differ in their motivations and preferences. The study by Douma et al. (2006) shows the necessity of disentangling foreign ownership into foreign corporate shareholding and foreign institutional shareholding, since they are vastly different in their governance and investment objectives. Thus, it is suggested, for future study that these categories of foreign investors be analysed separately, to obtain a better picture of investors’ behaviour. In terms of investment choices, foreign corporations are prone to invest in local companies which are related to their core business. Their experiences and skills will be utilised to achieve the maximum results from their investment, considering that they are enabled to set a particular benchmark for it (*ibid.*, p. 642). For instance, Honda, one of the foreign transportation corporations, is potentially making an investment in a transport company rather than in a food related company. Apart from this interesting finding, unfortunately, in this current study, it is difficult to obtain this data, as explained previously in Section 5.6.1 Dependent Variable (FEO).

Fourthly, another limitation of the study concerns the generalisability of the results to smaller companies. The sample is drawn from the public listed companies in Malaysia. Although, the sample was observed for a 12 year consecutive period, they represent only large Malaysian companies. However, it is well postulated that public companies are chosen for a variety of reasons over non-listed companies, or smaller companies (see Section 5.4.1 Population). The difficulties associated with obtaining the relevant information from small firms and the uniformity issue means that small firms can automatically be considered peripheral. In addition, foreign investors generally invest in well established firms, as they are in an adverse position in terms of obtaining company information in relation to local investors (see Section 2.5.4 Information Asymmetries). Nevertheless, in order to comprehend the whole picture of foreign investors’ behaviour in the Malaysian market in relation to the companies’ corporate governance practices, it would seem interesting if an extension of the research considered data from small and medium firms. In essence, there are no apparent reasons why the results would differ for smaller companies. However,

further study on the segregation of large and small companies may give substance to this claim.

Fifth, even though the use of the methodology and the data collection mechanism selected in this study were argued to be the most suitable and efficient choices to understand foreign investors' behaviour concerning changes in corporate governance, more could be done to achieve triangulation. For example, if the right 'key person' can be identified (see Section 5.3.1 Secondary Data), in a future study, the interview method of data collection could be used to complement the data collected from the annual reports and database.

Additionally, it is acknowledged that this study used foreign investors as the key dependent variable. However, corporate governance mechanisms (independent variables) can also be utilised to understand the behaviour of other groups of investors, not just foreign investors. The study conducted by Kim et al. (2010) concerning the Korean stock market, for example subsumed the category of investors into four groups – foreign investors, institutional investors, retail investors and government investors. The similarities and the differences between the groups of investors are identified. Therefore, the investment pattern of foreign investors can be distinguished in relation to the groups of domestic investors. Different strategies can be used by the responsible parties to attract different investor groups. In the future, an extension of this study may aim to discriminate the groups of investors to arrive at firmer conclusions regarding foreign investors' behaviour towards corporate governance practice in firms.

Another limitation concerns the period of the study. This study applies a longitudinal approach, which spans 12 consecutive years from 2000 to 2011. The study was to examine the effect of the pinnacle of the Asian financial crisis 1997/1998 on the corporate governance system in Malaysia. Therefore, the period covered only the years after the financial turmoil. It might be more meaningful to discriminate between the periods; however, data availability is unfortunately very limited (see Section 5.4.2.1 Sample Period). In the future, there is a possibility that the data can be

manipulated and the effect of corporate governance on foreign investors' behaviour can be examined comprehensively. The specified period, for example before, during and after the Asian financial crisis 1997/1998, if possible, can be separated and the comparison between each period of foreign investors' behaviour towards corporate governance practice can be made, similar to the work carried out by Kim et al. (2010) in the setting of the Korean stock market.

Next, another limitation of this study is the cause-and-effect relationship between foreign investors' behaviour and corporate governance practice. Even though in this study there is empirical evidence that certain relationships are significant, in the real and complex world of business such relationships cannot simply be explained by corporate governance variables. Care should be taken in making decisions as there are other potential determinants that could influence foreign investors' decision making, for example the political stability of the countries. Certainly, special vigilance should be taken by any related parties when making decisions based on the results put forward in this study. Future studies could use more variables in order to improve the quality of the study.

Besides this, a single country study does not offer much contribution in terms of generalisation to other countries in relation to the institutional environment pressure, corporate governance changes and foreign investors' behaviour. Even though the characteristics of the countries - Asian countries for example - are touted to be similar, nevertheless, empirical evidence is required to prove the claim. Therefore, by employing the same variables and the same multi-theoretical lenses, future work could consider a multi-country approach. This kind of research is capable of providing a better understanding of institutional changes across countries by controlling the country specific variables - such as the culture's values, the political background and the economic environment.

From the methodological standpoint, there are two matters that should be given great emphasis in a future study. The key dependent variable, foreign equity ownership, should reflect the firm's market capitalisation. A 1% ownership in a large firm is not

equivalent to a 1% ownership in small firms. The same percentage value carries a different value of dollar investment. The second methodological limitation is the absence of interactional terms in the analyses. It is argued that interactional terms can be included in the analyses by defining a specific variable that can influence certain variables in the model. Therefore, in a future study, appropriate actions can be taken to ameliorate both of these methodological limitations.

Finally, the focus on the institutional contexts of Malaysia may be flawed by the specific attention given to the legal and regulatory institutions. In a wider context, it is important to note that institutions are not restricted to the legal and regulatory institutions, since *'formal and informal aspects'* - such as companies' policies, cultural and societal norms (Aguilera and Jackson 2003) - are also included. Therefore, in future work, it will be useful to explore other parts of the institutional aspects to enrich the findings.

8.6 Conclusion of the Study

The main aim of this study is to enhance the understanding of the foreign equity ownership in Malaysian firms and its association with corporate governance mechanisms, in a unique institutional background, i.e. Malaysia. In summary, it can be concluded that foreign investors allocate disproportionately more shares to firms that appoint more foreign directors, more directors with a Western educational background, and more professional directors, but disfavour firms with high multiple directorships on the board. In addition, the role of ownership structure is decisive upon foreign investors' behaviour, since it is found that foreign investors avoid investing in family-controlled companies and companies with high domestic institutional ownership.

The findings and the discussion offered (see Section 8.2.1 Board Characteristics Determinants for Foreign Investors' Investment Decisions) lead to the suggestion that the first research question – i) *Does the board of director's characteristics influence the level of FEO?* – is likely to have an indeterminate answer where hypotheses 1 and

2 (H_1 and H_2) being rejected. The second research question - ii) *Do directors' attributes influence the level of FEO?* – however, seems to have a positive answer with the majority of the hypotheses (4 out of the 5 hypotheses - H_3 , H_4 , H_6 and H_7) being empirically supported (see Section 8.2.2 Directors' Attributes Determinants for Foreign Investors' Investment Decisions for a discussion of the findings). Lastly the third research question – iii) *Do ownership structures influence the level of FEO?* – is also positively answered with two out of three hypotheses (H_8 and H_{10}) being empirically supported. These three questions lead to answering the main research question which is - *Does corporate governance influence the level of FEO in Malaysian companies?* Therefore, from the overall results of this study, it can be concluded that there is evidence that corporate governance attributes do influence foreign investors' decision making in Malaysian companies. However, with five of the ten hypotheses being supported at a high level of significance, and one with moderate significance, the conclusion that corporate governance practices in Malaysian companies affect the level of foreign investors' ownership cannot be strongly justified. Thus, the related parties that might use this study for any practical reason(s) should take reasonable precautions.

Nevertheless, this study had certain limitations (see Section 8.5 Limitations and Future Research Directions). These limitations are to be further refined and can provide a platform for future research advancement. Notwithstanding its limitations, this study has made significant contributions in terms of its theoretical, practical, and empirical implications (see Section 8.4 Research Contribution). An additional perspective is also offered for comprehending the relationship of corporate governance and FEO level in Malaysia, by exploring the corporate governance institutional background through an institutional theory lens, the corporate ownership structure in Malaysia through agency theory with principal-principal based conflicts, as well as using insights from resource dependence theory. In summary, the findings of this study improve our understanding of the association between firms' corporate governance mechanisms and foreign equity ownership.

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APPENDIXES

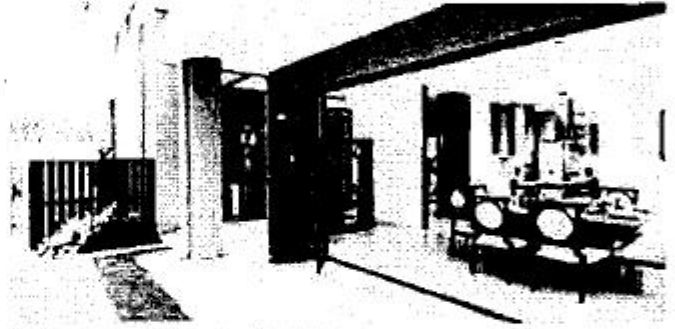
The selected sections of annual report from where the data was collected are attached in the appendixes.

Sources: A & M Realty annual report



A & M REALTY BERHAD
(077214-10)

Building on
Our **Experience**



Annual Report
2010

contents



A & M REALTY BERHAD
(177214-11)

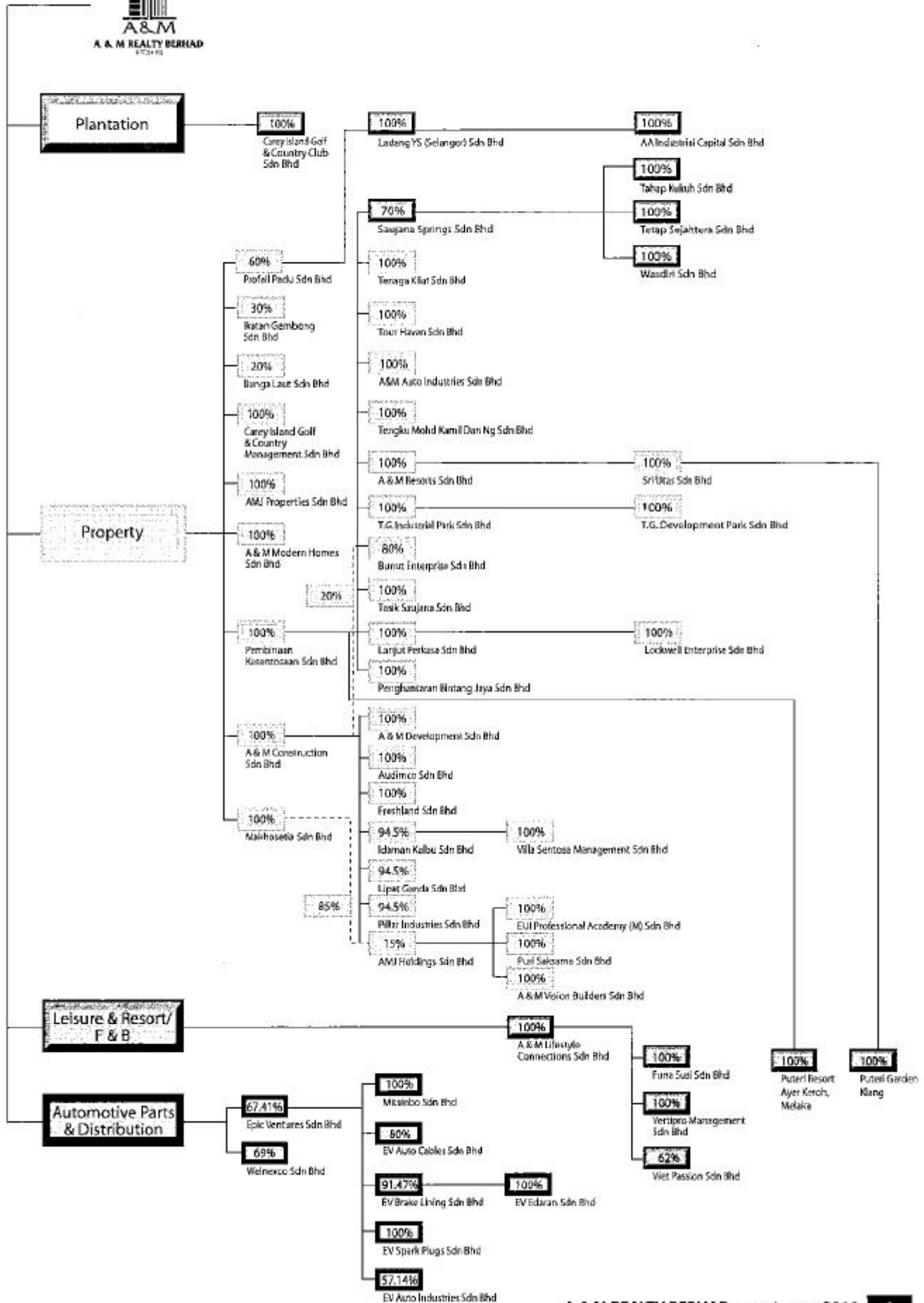


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CORPORATE INFORMATION

BOARD OF DIRECTORS	Dato' Ir. Ng Boon Thong @ Ng Thian Hock Dato' Setia Abdul Halim bin Dato' Haji Abdul Rauf Dato' Ambrose Leonard Ng Kwee Heng Datin Catherine Yeoh Eng Neo Tan Sri Dato' Dr. Sak Cheng Lum Datuk Ng Thian Kwee Ng Thian Ann Mat Ripen bin Mat Elah Tan Jiu See Steven Junior Ng Kwee Leng Malcolm Jeremy Ng Kwee Seng Ooi Hock Guan	<i>Chairman</i> <i>Deputy Chairman</i> <i>Managing Director</i>
AUDIT COMMITTEE	Tan Sri Dato' Dr. Sak Cheng Lum Mat Ripen bin Mat Elah Ooi Hock Guan	<i>Chairman</i>
COMPANY SECRETARIES	Bernard Lim Boon Siang (MACS 01153) Wong Siew Peng (MIA 21215) (<i>appointed on 13 August 2010</i>) Chong Sook Ling (MIA 15282) (<i>resigned on 13 August 2010</i>)	
REGISTERED OFFICE	PHK Management Services Sdn Bhd No 36A, Lorong Gelugor, Off Persiaran Sultan Ibrahim, 41300 Klang, Selangor Darul Ehsan. Tel: +603-3343 8148 Fax: +603-3341 4426	
BUSINESS OFFICE	10th Floor, Menara A & M, Garden Business Centre, No 3, Jalan Istana, 41000 Klang, Selangor Darul Ehsan. Tel: +603-3373 2888 Fax: +603-3372 8858	
REGISTRAR	Tricor Investor Services Sdn Bhd Level 17, The Gardens North Tower, Mid Valley City, Lingkaran Syed Putra, 59200 Kuala Lumpur. Tel: +603-2264 3883 Fax: +603-2282 1886	
AUDITORS	HLB Ler Lum, Chartered Accountant, A Member of HLB International	
PRINCIPAL BANKERS	OCBC Bank (Malaysia) Berhad United Overseas Bank (Malaysia) Berhad Malayan Banking Berhad	

CORPORATE STRUCTURE



CHAIRMAN'S STATEMENT

“ On behalf of the Board of Directors, it is my pleasure to present to you, the Annual Report and Audited Financial Statements of A & M Realty Berhad (“A & M” or the Company”) and its group of companies (“the Group”) for the financial year ended 31st December 2010.”

OVERVIEW

After the downturn in 2009, the Malaysian economy experienced a strong resumption of growth in 2010 with an expansion of 7.2%. The growth was driven by sustained expansion in domestic demand and growth in external demand. The monetary policy by Bank Negara remained supportive of the economic activity although its Overnight Policy Rate has been raised from 2.00% to 2.75% in year 2010. This will help to prevent financial imbalances in an environment of low interest rates while supporting fundamental and sustainable demand which augurs well for the property sector.

Overall, the property market in Klang Valley remained active with good take up rates for affordable residential units and exclusive high end residential and commercial developments at prime locations.

For the financial year ended 31 December 2010, the Group registered a lower profit before taxation of RM15.59 million on revenue of RM125.37 million. This represented a decrease of RM17.79 million or 12% lower than the revenue in the previous financial year of RM143.16 million, while profit before taxation has decreased by RM2.82 million or 15%. The lower revenue and profit contribution were mainly attributable to the lower sales contribution from the property and construction division following the completion of certain ongoing projects.

Nevertheless, the Group remains financially sound with strong cash flow from operations and a healthy balance sheet. The management is positive that the Group will continue to be a major player in the property market, following the uptrend and success of the Groups ever-striving goal of producing high end lifestyle properties.

For the period under review, the Group registered the basic earnings per share attributable to the shareholders at 2.86 sen, a decrease of 1.01 sen or 26% and the net assets per share had further strengthen to RM1.31, up from the previous year of RM1.28.

BUSINESS REPORT

Property Division

The Property Division remains the major contributor to the Group, contributing 56% and 54% of the Group's total turnover and profitability respectively.



Major on-going project

In 2007, the team at A&M embarked on a quest to develop a boutique brand name, namely the Amverton series of developments, of which focused on delivering innovative and conceptual homes within safe and sustainable communities.

Our Australian Inspired Bungalows, namely Amverton Park @ Bukit Kemuning Golf & Country Resort was the first of the series and since its maiden launch in 2008, sparked never-ending success stories and has continuously been receiving strong interest and positive feedback from existing as well as new buyers. Phase 1, 2 and 3 have been successfully sold out with vacant possession being handed over for the first 2 phases of over 45 units in February 2010.

Its true 'jewel in the crown' location gives Amverton Park residents almost instant access to shopping centres like Carrefour, medical establishments like Columbia Asia Hospital and educational institutions such as national and international (Chinese Taipei) schools that cater for children of all ages.

Its ease of accessibility to Subang Jaya, Petaling Jaya and other surrounding established neighbourhoods such as Kota Kemuning and Bukit Rimau, is enhanced via the Bukit Rimau interchange along the KESAS highway. Furthermore, residents enjoy a direct link from Federal Highway to Amverton Park via the Lebuhraya Kemuning-Shah Alam (LKSA), which also places residents a mere breeze away Subang and Shah Alam town.

With the overwhelming response for the first 3 phases of Amverton Park which have been fully sold out, we are excited with the new offerings of Phase 4 and 5 to come. We are confident that more and more home buyers will appreciate the differentiations and added advantages that the Amverton series of developments have to offer, and are upbeat about our upcoming 2011 launches.

Up and coming project

We are very upbeat about our high-end luxurious condominiums project Amverton Kiara, located in the much sought-after address, Mount Kiara. Amverton Kiara, consists of 190 units of generously sized homes situated at the highest point of Mount Kiara, is expected to be launched end 2011.

Our goal is further enhanced with the Group continuously looking to increase its landbank as well as passive income contributors. Garden Business Center (“GBC”), our 12 storey corporate office and adjoining 6 blocks of 8 storey office building, continue to report steady recurring rental income contributing to the Group's revenue with its high occupancy rate.

PROFILE OF BOARD OF DIRECTORS

Dato' Ir. Ng Boon Thong @ Ng Thian Hock

Nationality: Malaysian

Directorship: Executive Chairman (Non-Independent and Executive Director)

Age: 63

Appointed Date: 22 November 1994

Dato' Ir. Ng Boon Thong @ Ng Thian Hock graduated with an Honours Degree in Civil Engineering from the University of Malaya. Prior to founding the Company, he began his career in 1970 as an engineer in Perbadanan Urus Air Selangor Berhad before appointed as a Municipal Councillor of Majlis Perbandaran Klang to assist in the development and growth of the Klang district. He was also the State Executive Councillor for the Selangor Government, State Assemblyman for the Barisan Nasional Party for the Selat Klang and Pandamaran constituencies and a Senator for the Government. Dato' Ng was appointed to the Board of Hil Industries Berhad ("Hil") on 4 July 2002 as Executive Chairman. Dato' Ng is a substantial shareholder of the Company. He is the spouse of Datin Catherine Yeoh Eng Neo, father of Dato' Ambrose Leonard Ng Kwee Heng, Mr. Steven Junior Ng Kwee Leng and Mr. Malcolm Jeremy Ng Kwee Seng. He is also the brother of Datuk Ng Thian Kwee and Mr. Ng Thian Ann.

Dato' Setia Abdul Halim bin Dato' Haji Abdul Rauf

Nationality: Malaysian

Directorship: Executive Deputy Chairman (Non-Independent and Executive Director)

Age: 73

Appointed Date: 1 February 2002

Dato' Setia Abdul Halim bin Dato' Haji Abdul Rauf, was appointed to the Board of Director on 1 February 2002 and was subsequently appointed as Executive Deputy Chairman on 24 April 2002. He holds a Bachelor of Arts Degree from the University of Malaya and Master Degree in Public and International Affairs from University of Pittsburgh USA. Before joining the private sector, he held key position in government authorities and agencies. Amongst key positions held were Director-General of Implementation Coordination Unit in the Prime Minister's Department, State Secretary of State Government of Selangor, Director-General of Immigration Department Malaysia, Deputy Director, Bureau of Research and Consultancy, National Institute of Public Administration, Malaysia and Senior Deputy Director-General, Rubber Industry Smallholders Development Authority. He has vast experience in the management and strategic business planning. Dato' Setia Abdul Halim was appointed to the Board of Hil on 7 February 2003 as Executive Deputy Chairman. Presently, he is also the Chairman of Kontena Nasional Global Logistic Sdn. Bhd. and Golden Plus Holdings Berhad. Dato' Setia Abdul Halim does not have any interest in the securities of the Company, neither does he have any family relationship with any Director and/or major shareholder of the Company.

Dato' Ambrose Leonard Ng Kwee Heng

Nationality: Malaysian

Directorship: Managing Director (Non-Independent and Executive Director)

Age: 43

Appointed Date: 22 November 1994

Dato' Ambrose Leonard Ng Kwee Heng graduated with a Commerce Degree from the University of Western Australia. Being a Chartered Accountant, he is a member of the Australian Society of Certified Practising Accountants (CPA, Australia) and also a member of the Malaysian Institute of Accountants. He is experienced in the property and construction industry, having hands-on involvement in the management, financial and project management of the Group. In addition, he was formerly Deputy Chairman of Selangor Real Estate and Housing Developers' Association Malaysia and Chairman of Klang/Shah Alam Zone Committee. He is presently a committee member of the Majlis Tindakan Membenters Dadah Selangor. He is also a member of the Remuneration Committee and Nomination Committee of the Company. Dato' Ambrose Ng is a substantial shareholder of the Company by virtue of his parents' shareholdings. He is the son of Dato' Ir. Ng Boon Thong @ Ng Thian Hock, brother of Mr. Steven Junior Ng Kwee Leng and Mr. Malcolm Jeremy Ng Kwee Seng and nephew of Datuk Ng Thian Kwee and Mr. Ng Thian Ann.

Datin Catherine Yeoh Eng Neo

Nationality: Malaysian

Directorship: Non-Independent and Executive Director

Age: 65

Appointed Date: 2 July 2009

Datin Catherine Yeoh Eng Neo holds a Bachelor of Arts majoring in Economics from University of Malaya. Datin Catherine Yeoh Eng Neo is a substantial shareholder of the Company by virtue of her spouse' and sons' shareholdings. She is the spouse of Dato' Ng Boon Thong @ Ng Thian Hock and mother of Dato' Ambrose Leonard Ng Kwee Heng, Mr. Steven Junior Ng Kwee Leng and Mr. Malcolm Jeremy Ng Kwee Seng.

PROFILE OF BOARD OF DIRECTORS (CONT'D)

OTHER INFORMATION

- (a) None of the Directors has any conflict of interest with the Company and none has convicted of any offences in the past ten years.
- (b) By virtue of their interests in the Company, Dato' Ir. Ng Boon Thong @ Ng Thian Hock, Datin Catherine Yeoh Eng Neo, Dato' Ambrose Leonard Ng Kwee Heng, Steven Junior Ng Kwee Leng and Malcolm Jeremy Ng Kwee Seng are also deemed to be interested in the shares of all the subsidiaries to the extent of the Company's interests in the respective subsidiaries. In addition, their direct and indirect interests in the share capital of the subsidiaries during the financial year were as follows:-

	Number of ordinary shares of RM1.00each			Balance at 31.12.2010
	Balance at 1.1.2010	Acquired	Disposed	
Dato' Ir. Ng Boon Thong @ Ng Thian Hock, Datin Catherine Yeoh Eng Neo, Dato' Ambrose Leonard Ng Kwee Heng, Steven Junior Ng Kwee Leng, and Malcolm Jeremy Ng Kwee Seng				
- deemed interest				
Idaman Kalbu Sdn. Bhd.	74,250	-	-	74,250
Lipat Ganda Sdn. Bhd.	99,046	-	-	99,046
Pillar Industries Sdn. Bhd.	161,910	-	-	161,910
Profail Padu Sdn. Bhd.	1,600,000	-	-	1,600,000

CORPORATE GOVERNANCE

The Board of Directors is committed to ensuring that the highest standard of corporate governance are practised throughout the Group as a fundamental part of discharging its responsibilities to protect and enhance shareholders' value and the financial performance of the Company and the Group. To this end, the Board fully supports the recommendations of the Malaysian Code of Corporate Governance. The Board is pleased to provide the following statements, which outlines the main corporate governance practices that were in place throughout the financial period, unless otherwise stated:

THE BOARD OF DIRECTORS

Duties and Responsibilities

The Group acknowledges the pivotal role played by the Board of Directors in the stewardships of its direction and operations. To fulfill this role, the Board is responsible for the overall corporate governance of the Group, including its strategic direction, establishing goals for Management and monitoring the achievement of these goals.

The Group is lead by a strong and experienced Board under a Chairman, who is an Executive Director. The roles of the Chairman and Managing Director are separate and each has a clearly accepted division of responsibilities to ensure a balance of power and authority. The Chairman is primarily responsible for orderly conduct and working of the Board whilst the Managing Director is responsible for the day to day running of the business and implementation of Board's policies and decisions.

The Board meets at least four (4) times a year, with additional meetings convened when necessary. All Board members bring an independent judgement to bear on issues of strategy, performance and resources and standard of conducts. The Non-Executive Directors are all independent. During the year ended 31 December 2010, five (5) Board Meetings were held. Every Directors attended a majority of the Board meetings held during his/her tenure in the period. Details of the Board Meetings and the attendance of the Directors are disclosed in the Statement Accompanying Notice of Annual General Meeting on page 5.

The Board has delegated specific responsibilities to three (3) sub-committees (Audit, Nomination and Remuneration Committees). The details of the Audit Committee are set out on page 16 to 18 while the details of the Nomination and Remuneration Committee are set out below. These Committee have the authority to examine particular issues and report back to the Board with their recommendations. The ultimate responsibility for the final decisions on all matters, however, lies with the entire Board.

Board Balance

The Board currently has twelve (12) members, comprising four (4) Independent Non-Executive Directors and eight (8) Executive Directors (including the Chairman and Managing Director). Together, the Directors bring a wide range of business and financial experience relevant to the direction of a large, expanding Group. A brief description of the background of each Director is presented on pages 12 to 14.

There is balance in the Board because of the presence of four (4) Independent Non-Executive Directors who are the calibre necessary to carry sufficient weight in Board decisions thus enabling adequate Board representation of the interest of minority shareholders. Although all the Directors have an equal responsibility for the Group's operations, the role of these Independent Non-Executive Directors is particularly important in ensuring that the strategies proposed by the executive management are fully discussed and examined, and take account of the long term interests, not only of the shareholders, but also of employees, customers, suppliers and the many communities in which the Group conducts business.

Tan Sri Dato' Dr. Sak Cheng Lum acts as the senior Independent Non-Executive Director. Any concerns concerning the Group may be conveyed to him.

Supply of Information

All Board meetings are structured with a pre-set agenda. Board papers providing updates on operation, financial and corporate development as well as minutes of meetings of the Board Committee are circulated prior to the meetings to give Directors time to deliberate on the issues to be raised at the meetings. The Directors have full access to senior management and the advise and services of the Company Secretaries. In addition, the Board may seek independent advise should the need rise.

Appointment of the Board

The Malaysian Code on Corporate Governance endorses as good practice, a formal procedure for appointments to the Board, with a Nomination Committee making recommendation to the Board. The Code, however, states this procedure may be performed by the Board as a whole, although, as a matter of best practice, it recommends that this responsibility be delegated to a committee. As a result, on 29 March 2002, the Board has set up the Nomination Committee comprising the following Directors to execute the followings:

Nomination Committee

Tan Sri Dato' Dr. Sak Cheng Lum/Independent and Non-Executive Director/Chairman

Mat Ripen bin Mat Elah/Independent and Non-Executive Director

Dato' Ambrose Leonard Ng Kwee Heng/Non-Independent and Executive Director

The Nomination Committee recommends to the Board:

- Candidates for all directorships to be filled by shareholder or the Board, including those proposed by the Managing Director or any senior executives of the Company; and
- Directors to fill the seats on Board Committees.

In addition, this Committee assesses:

- The effectiveness of the Board as a whole and the Committees of the Board;
- The contribution of each Individual Director; and
- The required mix of skills and experiences and other qualities, including core competencies which Non-Executive Directors should bring to the Board.

Directors' Training

All members of the Board have attended and successfully completed the Mandatory Accreditation Programme and accumulated the requisite Continuing Education Programme points for the years 2003 and 2004 as specified by Bursa Malaysia Securities Berhad.

Under the revised Bursa Malaysia Listing Requirement, the Board will assume the onus determining or overseeing the training needs of their Directors from year 2005 onwards. Directors are encouraged to attend relevant seminars and training programmes to equip themselves with the knowledge to effectively discharge their duties as Directors.

Re-election of the Directors

In accordance with the Company's Articles of Association, all Directors who are appointed by the Board are subject to election by shareholders at the first Annual General Meeting after the appointment.

In accordance with the Articles of Association, one-third (1/3) of the remaining Directors, are required to submit themselves for re-election by rotation at each Annual General Meeting. In compliance with the Bursa Malaysia Securities Berhad's Listing Requirements, which came into force on 1 June 2001, all Directors are required to submit themselves for re-election at least once every three (3) years. Directors over seventy years are required to submit themselves for re-appointment annually in accordance with Section 129(6) of the Companies Act, 1965.

Objective of Director's Remuneration Committee

The Company has set up the Remuneration Committee on 29 March 2002 as recommended by the Malaysian Code on Corporate Governance to determine the remuneration for a Director so as to ensure that the Company attracts and retains the Directors needed to run the Company successfully. The component parts of remuneration are structured so as to link rewards to corporate and individual performance, in the case of Executive Directors. In the case of Non-Executive Directors, the level of remuneration reflects the experience and level of responsibilities undertaken by the particular Non-Executive Director concerned.

CORPORATE GOVERNANCE (CONT'D)

Remuneration Committee

Tan Sri Dato' Dr. Sak Cheng Lum/Independent and Non-Executive Director/Chairman

Dato' Ambrose Leonard Ng Kwee Heng/Non-Independent and Executive Director

Mat Ripen bin Mat Elah/Independent and Non-Executive Director

The Remuneration Committee recommends to the Board the framework of the Executive Directors' remuneration and the remuneration package for each Executive Director in all its forms, drawing from outside advice if necessary. Executive Directors should play no part in decision on their own remuneration. It is, nevertheless, the ultimate responsibility of the entire Board to approve the remuneration of these Directors.

The determination of the remuneration of Non-Executive Directors is a matter for the Board as a whole. The individuals concerned should abstain from discussion of their own remuneration. The Company reimburses reasonable expenses incurred by these Directors in the course of their duties as Directors.

Directors' Remuneration

The remuneration of Directors for the financial year ended 31 December 2010 is as follows:

1. Aggregate remuneration of Directors categorized into appropriate components:

	Executive Director RM	Non-Executive Directors RM	Total RM
Fees	72,000	48,000	120,000
Salary & Allowances	2,059,600	-	2,059,600
Bonus	128,480	-	128,480
EPF	168,264	-	168,264
	2,428,344	48,000	2,476,344

2. The number of Director as at 31 December 2010 whose total remuneration falls within the following bands:

Range of Remuneration	Executive Directors	Non-Executive Directors
Below RM50,000	1	2
RM50,001 - RM100,000	2	-
RM150,001 - RM200,000	1	-
RM200,001 - RM250,000	1	-
RM400,001 - RM450,000	1	-
RM700,001 - RM750,000	2	-

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DIRECTORS' REPORT

The Directors have pleasure in submitting their Report together with the audited financial statements of the Group and of the Company for the financial year ended 31 December 2010.

PRINCIPAL ACTIVITIES

The Company is principally engaged in investment holding and the provision of management services. The principal activities of the subsidiaries are set out in Note 13 to the Financial Statements.

There have been no significant changes in the nature of these activities during the financial year.

FINANCIAL RESULTS

	Group RM	Company RM
Profit for the financial year	11,510,578	11,324,547
Attributable to : Equity holders of the Company	10,397,656	11,324,547
Minority interests	1,112,922	-
	11,510,578	11,324,547

DIVIDENDS

No dividends have been paid or declared by the Company since the end of the previous financial year.

RESERVES AND PROVISIONS

All material transfers to or from reserves and provisions during the financial year are shown in the financial statements.

SHARE CAPITAL

During the financial year, the following shares were issued by the Company :

Class of shares	Number of shares	Term of issue	Issue price (RM)	Purpose of issue
Ordinary	2,329,400	Cash	0.50	Exercise of warrants

The new ordinary shares rank pari passu in all respects with the existing ordinary shares.

TREASURY SHARES

The shareholders of the Company granted a mandate to the Company to repurchase its own shares at the Annual General Meeting held on 29 June 2010. The Directors of the Company are committed to enhance the value of the Company to its shareholders and believe that the repurchase plan can be applied in the best interest of the Company and its shareholders.

The repurchase transactions were financed by internally generated funds. The shares repurchased are being held as treasury shares in accordance with Section 67A of the Companies Act, 1965.

There are no repurchase of own shares during the financial year ended 31 December 2010.

WARRANTS

The Warrants 2000/2010 were constituted under a Deed Poll dated 8 September 2000.

The subscription right of the warrants expired on 10 September 2010. The last day for trading of the warrants was on 24 August 2010 and was suspended from quotation on the Bursa Malaysia Securities Berhad ("BMSB") effective 25 August 2010. Accordingly, the warrants were removed from the official list of BMSB effective 13 September 2010.

DIRECTORS' REPORT (CONT'D)

DIRECTORS

The name of the Directors of the Company in office since the date of the last Report and at the date of this Report are :-

- Dato' Ir. Ng Boon Thong @ Ng Thian Hock
- Dato' Setia Abdul Halim Bin Dato' Haji Abdul Rauf
- Dato' Ambrose Leonard Ng Kwee Heng
- Datin Catherine Yeoh Eng Neo
- Tan Sri Dato' Dr. Sak Cheng Lum
- Datuk Ng Thian Kwee
- Ng Thian Ann
- Mat Ripen Bin Mat Elah
- Tan Jiu See
- Steven Junior Ng Kwee Leng
- Malcolm Jeremy Ng Kwee Seng
- Ooi Hock Guan

DIRECTORS' INTERESTS

The following Directors of the Company who held office at the end of the financial year had, according to the Register of Directors' Shareholdings, interests in shares of the Company and related companies as follows :-

	Number of ordinary shares of RM0.50 each			Balance at 31.12.2010
	Balance at 1.1.2010	Acquired	Disposed	
The Company				
Dato' Ir. Ng Boon Thong @ Ng Thian Hock				
- direct interest	26,582,412	5,030,000	-	31,612,412
- deemed interest	200,210,280	25,222,500	-	225,432,780
Datin Catherine Yeoh Eng Neo				
- direct interest	5,229,800	400,000	-	5,629,800
- deemed interest	221,562,892	29,852,500	-	251,415,392
Dato' Ambrose Leonard Ng Kwee Heng				
- direct interest	2,588,000	-	-	2,588,000
- deemed interest	220,804,692	27,744,600	-	248,549,292
Steven Junior Ng Kwee Leng				
- direct interest	1,000,000	-	-	1,000,000
- deemed interest	220,804,692	27,744,600	-	248,549,292
Malcolm Jeremy Ng Kwee Seng				
- direct interest	1,000,000	2,507,900	-	3,507,900
- deemed interest	220,804,692	27,744,600	-	248,549,292

DIRECTORS' REPORT (CONT'D)

DIRECTORS' INTERESTS (CONT'D)

	Number of ordinary shares of RM1.00each			Balance at 31.12.2010
	Balance at 1.1.2010	Acquired	Disposed	
Holding company - Dalta Industries Sdn. Bhd.				
Dato' Ir. Ng Boon Thong @ Ng Thian Hock				
- direct interest	7,000,000	-	-	7,000,000
- deemed interest	3,000,000	-	-	3,000,000
Datin Catherine Yeoh Eng Neo				
- direct interest	400,000	-	-	400,000
- deemed interest	8,600,000	-	-	8,600,000
Dato' Ambrose Leonard Ng Kwee Heng				
- deemed interest	10,000,000	-	-	10,000,000
Steven Junior Ng Kwee Leng				
- deemed interest	9,000,000	-	-	9,000,000
Malcolm Jeremy Ng Kwee Seng				
- deemed interest	9,000,000	-	-	9,000,000

	Number of ordinary shares of RM0.50each			Balance at 31.12.2010
	Balance at 1.1.2010	Acquired	Disposed	
Related company - Hil Industries Berhad				
Dato' Ir. Ng Boon Thong @ Ng Thian Hock				
- direct interest	21,392,166	11,721,400	-	33,113,566
- deemed interest	159,048,874	12,300,600	-	171,349,474
Datin Catherine Yeoh Eng Neo				
- direct interest	4,771,600	2,053,300	-	6,824,900
- deemed interest	175,669,440	21,968,700	-	197,638,140
Dato' Ambrose Leonard Ng Kwee Heng				
- direct interest	3,053,400	-	-	3,053,400
- deemed interest	165,961,240	23,163,000	-	189,124,240
Steven Junior Ng Kwee Leng				
- direct interest	2,841,500	200,000	-	3,041,500
- deemed interest	165,961,240	23,163,000	-	189,124,240
Malcolm Jeremy Ng Kwee Seng				
- direct interest	2,867,500	208,100	-	3,075,600
- deemed interest	165,961,240	23,163,000	-	189,124,240

DIRECTORS' REPORT (CONT'D)

DIRECTORS' INTERESTS (CONT'D)

	Number of ordinary shares of RM1.00 each			Balance at 31.12.2010
	Balance at 1.1.2010	Acquired	Disposed	
Related companies				
Dato' Ir. Ng Boon Thong @ Ng Thian Hock, Datin Catherine Yeoh Eng Neo, Dato' Ambrose Leonard Ng Kwee Heng, Steven Junior Ng Kwee Leng, and Malcolm Jeremy Ng Kwee Seng				
- deemed interest				
Idaman Kalbu Sdn. Bhd.	74,250	-	-	74,250
Lipat Ganda Sdn. Bhd.	99,046	-	-	99,046
Pillar Industries Sdn. Bhd.	161,910	-	-	161,910
Profail Padu Sdn. Bhd.	1,600,000	-	-	1,600,000

By virtue of their interests in Dalta Industries Sdn. Bhd., Dato' Ir. Ng Boon Thong @ Ng Thian Hock, Datin Catherine Yeoh Eng Neo, Dato' Ambrose Leonard Ng Kwee Heng, Mr. Steven Junior Ng Kwee Leng and Mr. Malcolm Jeremy Ng Kwee Seng are also deemed to be interested in the shares of all the subsidiaries to the extent of the Company's interests in the respective subsidiaries as disclosed in Note 13 to the Financial Statements.

Other than as disclosed above, the Directors who held office at the end of the financial year did not have interests in the shares or debentures of the Company or related companies during the financial year.

DIRECTORS' BENEFITS

During and at the end of the financial year, no arrangement subsisted to which the Company is a party, with the object or objects of enabling Directors of the Company to acquire benefits by means of the acquisition of shares in or debentures of the Company or any other body corporate.

Since the end of the previous financial year, no director has received or become entitled to receive any benefit (other than a benefit included in the aggregate amount of remuneration received or due and receivable by Directors as shown in the financial statements of the Group) by reason of a contract made by the Company or a related corporation with the Director or with a firm of which he is a member, or with a company in which he has a substantial financial interest except as disclosed in the Notes to the Financial Statements and that certain Directors received remuneration from the Company's related companies.

INDEPENDENT AUDITORS' REPORT TO THE MEMBERS OF A & M REALTY BERHAD

Report on the Financial Statements

We have audited the financial statements of A & M REALTY BERHAD, which comprise the Statements of Financial Position as at 31 December 2010 of the Group and of the Company, and the Statements of Comprehensive Income, Statements of Changes in Equity and Statements of Cash Flow of the Group and of the Company for the financial year then ended, and a summary of significant accounting policies and other explanatory information, as set out on pages 46 to 104.

Directors' Responsibility for the Financial Statements

The Directors of the Company are responsible for the preparation of financial statements that give a true and fair view in accordance with Financial Reporting Standards and the Companies Act, 1965 in Malaysia and for such internal control as the Directors determine are necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with approved standards on auditing in Malaysia. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on our judgment, including the assessment of risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the entity's preparation of financial statements that give a true and fair view in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the Directors, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements have been properly drawn up in accordance with Financial Reporting Standards and the Companies Act, 1965 in Malaysia so as to give a true and fair view of the financial position of the Group and of the Company as of 31 December 2010 and of their financial performance and cash flows for the financial year then ended.

Report on Other Legal and Regulatory Requirements

In accordance with the requirements of the Companies Act, 1965 in Malaysia, we also report the following:

- a) In our opinion, the accounting and other records and the registers required by the Act to be kept by the Company and its subsidiaries of which we have acted as auditors have been properly kept in accordance with the provisions of the Act.
- b) We are satisfied that the accounts of the subsidiaries that have been consolidated with the Company's financial statements are in form and content appropriate and proper for the purposes of the preparation of the financial statements of the Group and we have received satisfactory information and explanations required by us for those purposes.
- c) The audit reports on the accounts of the subsidiaries did not contain any qualification or any adverse comment made under Section 174(3) of the Act.

Other Reporting Responsibilities

The supplementary information set out in Note 41 is disclosed to meet the requirement of Bursa Malaysia Securities Berhad and is not part of the financial statements. The Directors are responsible for the preparation of the supplementary information in accordance with Guidance on Special Matter No. 1, Determination of Realised and Unrealised Profits or Losses in the Context of Disclosure Pursuant to Bursa Malaysia Securities Berhad Listing Requirements, as issued by the Malaysian Institute of Accountants ("MIA Guidance") and the directive of Bursa Malaysia Securities Berhad. In our opinion, the supplementary information is prepared, in all material respects, in accordance with the MIA Guidance and the directive of Bursa Malaysia Securities Berhad.

**STATEMENTS OF COMPREHENSIVE INCOME
FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2010**

		Group		Company	
	Note	2010 RM	2009 RM	2010 RM	2009 RM
Revenue	3	125,368,719	143,160,219	11,800,113	413,550
Cost of sales	4	(92,735,306)	(113,286,130)	(10,113)	(10,113)
Gross profit		32,633,413	29,874,089	11,790,000	403,437
Other operating income	5	2,890,500	6,233,779	-	83,538
Selling & distribution costs		(291,238)	(218,516)	-	-
Administration expenses		(19,285,403)	(17,041,712)	(393,947)	(277,173)
Other operating expenses		(312,906)	(365,753)	-	-
Finance costs	6	(45,132)	(66,491)	-	-
Share of profit/(loss) of associated companies		1,049	(1,997)	-	-
Profit before tax	7	15,590,283	18,413,399	11,396,053	209,802
Income tax expense	9	(4,079,705)	(3,512,814)	(71,506)	(42,879)
Profit for the financial year		11,510,578	14,900,585	11,324,547	166,923
Other comprehensive income, net of tax		-	-	-	-
Total comprehensive income for the financial year		11,510,578	14,900,585	11,324,547	166,923
Attributable to :-					
Equity holders of the Company		10,397,656	14,047,550	11,324,547	166,923
Minority interests		1,112,922	853,035	-	-
		11,510,578	14,900,585	11,324,547	166,923

	Note	Group	
		2010 RM	2009 RM
Earnings per share for profit for the financial year attributable to equity holders of the Company (sen)	10		
- Basic		2.86	3.87
- Diluted		2.86	3.85

The notes set out on pages 46 to 104 form an integral part of these financial statements.

**STATEMENTS OF FINANCIAL POSITION
AS AT 31 DECEMBER 2010**

	Note	2010 RM	Group 2009 RM	1.1.2009 RM	Company 2010 RM	Company 2009 RM
ASSETS						
Non-current assets						
Property, plant & equipment	11	113,371,315	106,320,784	105,193,910	748,160	759,850
Investment properties	12	21,221,802	17,711,127	17,923,385	-	-
Investment in subsidiaries	13	-	-	-	256,268,381	104,641,717
Investment in associated companies	14	1,482,604	1,481,555	1,483,552	-	-
Land held for property development	15	60,584,451	57,929,293	115,551,626	-	-
Other investments	16	587,480	587,480	3,087,482	150,982	150,982
Goodwill	17	19,407,046	20,388,821	20,508,690	-	-
Fixed deposits	18	1,666,480	1,502,886	1,384,245	-	-
Deferred tax assets	19	724,399	700,399	601,390	-	-
Biological assets	20	3,356,610	3,309,598	2,477,379	-	-
		222,402,187	209,931,943	268,211,659	257,167,523	105,552,549
Current assets						
Inventories	21	69,428,850	69,154,832	61,109,413	-	-
Property development costs	22	212,136,048	237,081,968	174,902,910	-	-
Trade & other receivables	23	47,645,107	67,130,341	61,772,038	8,453	1,858,453
Amount due from related parties	25	-	78,840	-	89,846	182,829,343
Income tax assets		1,463,784	1,147,754	1,015,293	273,922	244,504
Fixed deposits	18	28,883,348	31,794,770	27,775,333	142,562	139,258
Cash & bank balances	26	23,172,674	8,261,055	4,253,604	59,741	47,173
		382,729,811	414,649,560	330,828,591	574,524	185,118,731
Total assets		605,131,998	624,581,503	599,040,250	257,742,047	290,671,280

The notes set out on pages 46 to 104 form an integral part of these financial statements.

STATEMENTS OF CHANGES IN EQUITY
FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2010

Group	Attributable to equity holders of the Company					Total equity RM
	Share capital RM	Non distributable Share premium RM	Distributable Retained earnings RM	Minority interests RM	Total RM	
Balance at 1 January 2009	181,367,200	35,073,512	222,535,611	11,580,840	438,976,323	450,557,163
Total comprehensive income for the financial year	-	-	14,047,550	853,035	14,047,550	14,900,585
Dividend paid to minority interests	-	-	-	(118,849)	-	(118,849)
Arising from changes in composition of the Group	-	-	-	(33,471)	-	(33,471)
Disposal of subsidiary	-	-	-	(104,679)	-	(104,679)
Issue of shares by subsidiary to minority interests	-	-	-	57,000	-	57,000
Balance at 31 December 2009	181,367,200	35,073,512	236,583,161	12,233,876	453,023,873	465,257,749

The notes set out on pages 46 to 104 form an integral part of these financial statements.

**STATEMENTS OF CASH FLOW
FOR THE FINANCIAL YEAR ENDED 31 DECEMBER 2010**

	Group		Company	
	2010 RM	2009 RM	2010 RM	2009 RM
Cash flows from operating activities				
Profit before tax	15,590,283	18,413,399	11,396,053	209,802
Adjustments for :-				
Bad debt written off	365,683	-	-	-
Biological assets written off	-	5,954	-	-
Depreciation	2,972,313	2,796,338	11,690	11,690
Dividend income	(3,139)	(673)	(11,763,561)	(243,397)
Deemed gain on disposal of subsidiary	-	(36,471)	-	-
Loss/(Gain) on disposal of subsidiaries (net)	-	81,594	-	(61,496)
Impairment loss				
- goodwill	981,775	131,948	-	-
- trade receivables (net)	(107,886)	122,843	-	-
Interest expense	45,132	66,491	-	-
Interest income	(1,080,821)	(963,368)	(6,552)	(140,153)
Inventories write-down	57,629	51,073	-	-
Loss on disposal of investment	-	136,576	-	-
Loss/(Gain) on disposal of property, plant & equipment (net)	5,199	54,035	-	-
Negative goodwill	(217,223)	(3,843,844)	-	-
Property, plant & equipment written off	2,195	83,286	-	-
Share of (profit)/loss of associated companies	(1,049)	1,997	-	-
Unrealised gain on foreign exchange	(3,381)	(9,004)	-	-
Operating profit/(loss) before working capital changes	18,606,710	17,092,174	(362,370)	(223,554)

The notes set out on pages 46 to 104 form an integral part of these financial statements.

NOTES TO THE FINANCIAL STATEMENTS

1. GENERAL INFORMATION

The principal activities of the Company are those of an investment holding and management company. The principal activities of the subsidiaries are set out in Note 13 to the Financial Statements.

The Company is a limited liability company, incorporated and domiciled in Malaysia, and is listed on the Main Market of the Bursa Malaysia Securities Berhad.

The address of the registered office of the Company is as follows :-

No 36A, Lorong Gelugor,
Off Persiaran Sultan Ibrahim,
41300 Klang,
Selangor Darul Ehsan.

The address of the principal place of business of the Company is as follows :-

10th Floor, Menara A & M,
Garden Business Centre,
No 3 Jalan Istana,
41000 Klang,
Selangor Darul Ehsan.

2. SIGNIFICANT ACCOUNTING POLICIES

(a) Basis of preparation

The financial statements of the Group and of the Company have been prepared under the historical cost convention (unless stated otherwise in the significant accounting policies below) and comply with the Companies Act, 1965 and Financial Reporting Standards.

The preparation of financial statements in conformity with the Financial Reporting Standards and the Companies Act, 1965 requires the Directors to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reported period. Actual results could differ from those estimates.

The areas involving a higher degree of judgment or complexity, or areas where assumptions and estimates are significant to the financial statements are disclosed in Note 37 to the Financial Statements.

The financial statements are presented in Ringgit Malaysia, which is the Group's functional and presentation currency.

NOTES TO THE FINANCIAL STATEMENTS (CONT'D)

12. INVESTMENT PROPERTIES

	2010 RM	Group 2009 RM
At cost		
At beginning of the financial year	19,298,161	19,298,161
Transfer from inventories	3,722,934	-
At end of the financial year	23,021,095	19,298,161
Less: Accumulated depreciation		
At beginning of the financial year	1,587,034	1,374,776
Charge for the financial year	212,259	212,258
At end of the financial year	1,799,293	1,587,034
Carrying amounts	21,221,802	17,711,127

As at 31 December 2010 the Directors have appraised the fair value of the freehold land and buildings to be RM48.2 million (2009: RM35.8 million).

The Group's freehold land with net book value of RM1,698,766 (2009: RM1,698,766) has been pledged to a financial institution for banking facilities granted to the Group.

13. INVESTMENT IN SUBSIDIARIES

(a) Investment in subsidiaries

	2010 RM	Company 2009 RM
Unquoted shares		
- at cost	104,750,781	104,641,717
- equity capital contribution	151,517,600	-
	256,268,381	104,641,717

NOTES TO THE FINANCIAL STATEMENTS (CONT'D)

13. INVESTMENT IN SUBSIDIARIES (CONT'D)

Name of Company	Principal Activities	Effective Equity Interest	
		2010 %	2009 %
A & M Auto Industries Sdn. Bhd.	Investment holding	100	100
A & M Construction Sdn. Bhd.	Building construction, housing development, property management and investment holding	100	100
A & M Development Sdn. Bhd.	Housing development, property management and investment holding	100	100
A & M Lifestyle Connections Sdn. Bhd.	Investment holding and provision of management services	100	100
A & M Modern Homes Sdn. Bhd.	Property development	100	100
A & M Resorts Sdn. Bhd.	Investment holding, management of hotel and recreational facilities	100	100
A & M Vision Builders Sdn. Bhd.	Building construction	100	100
AA Industrial Capital Sdn. Bhd.	Plantation	60	59.99
AMJ Holdings Sdn. Bhd.	Housing development, property management and investment holding	100	100
AMJ Properties Sdn. Bhd.	Property development	100	100
Audimco Sdn. Bhd.	Property development and investment holding	100	100
Bunut Enterprise Sdn. Bhd.	Housing development and building construction	100	100
Carey Island Golf & Country Club Sdn. Bhd.	Dormant	100	100
Carey Island Golf & Country Management Sdn. Bhd.	Dormant	100	100
Epic Ventures Sdn. Bhd.	Investment holding	67.41	65.85
EUI Professional Academy (M) Sdn. Bhd.	Cultivation and sale of oil palm fruits	100	100
E.V. Auto Cables Sdn. Bhd.	Inactive	53.93	52.68
E.V. Auto Industries Sdn. Bhd.	Trading and assembling of automotive horns and other related products	38.52	37.63
E.V. Brake Lining Sdn. Bhd.	Manufacturing and distribution of automotive brake lining products	61.66	60.23

32. SEGMENT INFORMATION (CONT'D)

	Property development, construction & services rendered		Manufacturing & trading		Hotel & leisure related services		Plantation		Group	
	2010 RM	2009 RM	2010 RM	2009 RM	2010 RM	2009 RM	2010 RM	2009 RM	2010 RM	2009 RM
REVENUE										
Total revenue	71,030,250	90,353,784	42,300,695	40,007,724	10,291,164	10,605,455	2,242,511	2,573,414	125,864,620	143,540,377
Inter-segment sales	(453,611)	(363,397)	-	-	(42,290)	(12,572)	-	(4,189)	(495,901)	(380,158)
External sales	70,576,639	89,990,387	42,300,695	40,007,724	10,248,874	10,592,883	2,242,511	2,569,225	125,368,719	143,160,219
RESULTS										
Interest income	743,565	639,377	40,657	21,059	239,263	186,426	57,336	116,506	1,080,821	963,368
Finance costs	(5,185)	(5,735)	(37,398)	(58,767)	(2,549)	(1,989)	-	-	(45,132)	(66,491)
Share of results of associated companies	1,049	(1,997)	-	-	-	-	-	-	1,049	(1,997)
Profit before tax	8,524,734	11,430,209	2,900,709	2,335,742	3,274,407	3,607,821	890,433	1,039,627	15,590,283	18,413,399

ANALYSIS OF SHAREHOLDINGS AS AT 3 MAY 2011

Authorised Capital	:	500,000,000
Issued Capital	:	182,531,900
Class of Shares	:	Ordinary shares of RM0.50 each
Voting Rights	:	One vote per shares
No. of Holders	:	2,760

ANALYSIS OF EQUITY STRUCTURE

Size of Holdings	No. of Holders	%	No. of Shares	%
1-99	19	0.69	442	0.00
100-1,000	107	3.88	66,996	0.02
1,001-10,000	2,064	74.78	9,011,066	2.47
10,001-100,000	496	17.97	14,589,592	4.00
100,001-18,253,189 (*)	70	2.54	79,789,124	21.85
18,253,190 and above (**)	4	0.14	261,606,580	71.66
Total	2,760	100.00	365,063,800	100.00

Remarks : * Less than 5% of issued Shares
 ** 5% and above of issued Shares

LIST OF DIRECTOR' SHAREHODINGS

Name	Direct Holdings		Indirect Holdings	
	No	%	No	%
Dato' Ir. Ng Boon Thong @ Ng Thian Hock	31,612,412	8.66	225,432,780	61.75
Dato' Setia Abdul Halim bin Dato' Haji Abdul Rauf	-	-	-	-
Dato' Ambrose Leonard Ng Kwee Heng	2,588,000	0.71	248,549,292	68.08
Datin Catherine Yeoh Eng Neo	5,629,800	1.54	251,415,392	68.87
Tan Sri Dato' Dr. Sak Cheng Lum	-	-	-	-
Datuk Ng Thian Kwee	-	-	-	-
Ng Thian Ann	-	-	-	-
Mat Ripen bin Mat Elah	-	-	-	-
Tan Jiu See	-	-	-	-
Steven Junior Ng Kwee Leng	1,000,000	0.27	248,549,292	68.08
Malcolm Jeremy Ng Kwee Seng	3,507,900	0.96	252,749,292	69.23
Ooi Hock Guan	-	-	-	-

LIST OF SUBSTANTIAL SHAREHODINGS

No	Name	Direct Holdings		Indirect Holdings	
		No	%	No	%
1.	Delta Industries Sdn Bhd	211,307,080	57.88	-	-
2.	Dato' Ir. Ng Boon Thong @ Ng Thian Hock	31,612,412	8.66	225,432,780	61.75
3.	Permodalan Nasional Berhad	20,546,500	5.63	-	-

ANALYSIS OF SHAREHOLDINGS AS AT 3 MAY 2011 (CONT'D)

LIST OF THIRTY (30) LARGEST SHAREHOLDERS

No.	Name	No. of Shares	%
1.	Delta Industries Sdn. Bhd.	132,536,312	36.30
2.	Delta Industries Sdn. Bhd.	76,911,568	21.07
3.	Dato' Ir. Ng Boon Thong @ Ng Thian Hock	31,612,200	8.66
4.	Permodalan Nasional Berhad	20,546,500	5.63
5.	Permodalan Negeri Selangor Berhad	14,400,000	3.94
6.	Mujur Cemerlang Sdn. Bhd.	9,743,400	2.67
7.	HSBC Nominees (Asing) Sdn. Bhd. (DZ Bank INTL For UNI EM Fernost Treuhandkonto, Luxembourg)	5,234,000	1.43
8.	Datin Catherine Yeoh Eng Neo	5,152,800	1.41
9.	Lim Hui Y'ng	4,200,000	1.15
10.	Amal Restu Sdn. Bhd.	4,012,000	1.10
11.	Malcolm Jeremy Ng Kwee Seng	3,507,900	0.96
12.	Mujur Cemerlang Sdn. Bhd.	3,454,500	0.95
13.	Mujur Cemerlang Sdn. Bhd.	3,021,200	0.83
14.	Pandang Usaha Sdn. Bhd.	2,217,436	0.61
15.	Dato' Ambrose Leonard Ng Kwee Heng	2,188,000	0.60
16.	Amal Restu Sdn. Bhd.	1,917,244	0.53
17.	Delta Industries Sdn. Bhd.	1,859,200	0.51
18.	Mujur Cemerlang Sdn. Bhd.	1,485,044	0.41
19.	IOI Corporation Berhad	1,000,000	0.27
20.	Milton Norman Ng Kwee Leong	1,000,000	0.27
21.	Steven Junior Ng Kwee Leng	1,000,000	0.27
22.	Pacific Strike Sdn Bhd	850,000	0.23
23.	Affin Investment Bank Berhad (CLR For Lembaga Tabung Angkatan Tentera)	777,600	0.21
24.	Koh Bee Lan	682,900	0.19
25.	Teo Kwee Hock	634,600	0.17
26.	Citigroup Nominees (Asing) Sdn. Bhd. (CBNY For Dimensional Emerging Markets Value Fund)	603,400	0.17
27.	Westurine Sdn. Bhd.	559,200	0.15
28.	Ng Thaim Peng	540,000	0.15
29.	CIMSEC Nominees (Tempatan) Sdn. Bhd. (CIMB Bank For The Swee Heng [MM1118])	535,900	0.15
30.	Dato' Ambrose Leonard Ng Kwee Heng	400,000	0.11
TOTAL		332,582,904	91.10

