

CORPORATE GOVERNANCE IN ROMANIAN METALLURGY INDUSTRY

Received – Primljeno: 2013-04-24
Accepted – Prihvaćeno: 2013-06-25
Review Paper – Pregledni rad

In this paper we propose to assess the quality of the corporate governance of the metallurgy industry operating in the Romanian capital market. The results are compared with the averages recorded in companies listed on Bucharest Stock Exchange. The study highlights that companies listed on Bucharest Stock Exchange which activate in the metallurgical sector have successfully managed to adapt to the requirements of the globalization of the capital market involving the adoption of the best practices of corporate governance.

Keywords: metallurgic industry, corporate governance, best practices, listed companies

INTRODUCTION

Metallurgical industry occupies an important position in the Romanian economy as a whole, as evidenced by the share of total industrial production and exports: 6,8 % of the industrial output of the country (in 2009), 8,9 % of the value of manufacturing output (in 2009), 11,9 % of the country's total exports (2010). [1]

In the evolution of the industrial production in the metallurgical industry over the period 2006-2010, the year 2009 marks a decrease of 39,6 % over the previous year. In 2010 it was recorded an industrial production redress, with an increase of 37,6 %, the recorded level being higher than in 2006-2007.

During 2010, the activity in the metallurgy sector returned to the level of 127 % of productivity in 2009, and the number of employees decreased from 34 000, reaching 32 900 people which led to an increase in labor productivity by approx. 21% in late 2010.

At the current date (March 2013) there are 20 large metallurgy companies trading on the capital market but only three of them are traded on the Bucharest Stock Exchange (BSE) as a primary market, namely (ALRO SA Company listed at Category I and MECHEL TARGOVISTE SA Company and TMK - ARTROM Company listed at Category II) and other 17 companies listed on the secondary market Rasdaq.

CORPORATE GOVERNANCE IN ROMANIA

Once the benefits of corporate governance practices have been understood and assimilated, the emerging developing countries have begun to adopt "the best practices" in corporate governance especially because this

need is acutely felt with the changes required by the transition to a market economy.

In 2001, the OECD with the support of USAID, developed a specific program to improve corporate governance in Romania. The OECD/USAID views envisaged by the program were pointing out the following objectives: (i) evaluate corporate governance in Romania; (ii) offer a set of key recommendations for improving corporate governance in Romania and bring it closer to the international standard of the OECD Principles; (iii) identify needed technical assistance in the area of corporate governance; (iv) improve the understanding of present corporate governance practices in Romania, informing the international community about progressive national reform Initiatives; and (v) facilitate full Romanian access to the ongoing international dialogue on corporate governance. In conducting the assessment and program formulation, the OECD Principles of Corporate Governance was considered the benchmark (OECD, 2001). [2]

The key recommendations constituted a comprehensive agenda for reform, including legislative changes, enforcement, institution building and private behavior/capacity building. [3]

The Bucharest Stock Exchange has only begun the first trading in 1995. Only in 2001, BSE created Plus Class ("with more transparency") for admission to BSE, and adopted the first code of corporate governance. The listed companies could promote Plus Class only after they have fully adopted in their Constitution Acts the Code of Corporate Governance issue. This process is not expected with success because only one company has required a promotion to the Plus Class level.

In 2008, BSE has adopted a new Corporate Governance Code which is based on the OECD principles of corporate governance. The code came into force from the financial year 2009 and it is applied voluntarily by

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companies traded on the regulated market operated by BSE. Companies that decide to entirely or partially adopt the Code must annually submit to BSE a statement of compliance or non-compliance with the Code of Corporate Governance (“Comply or Explain Statement”), stating that the recommendations have actually been implemented and also the way of implementation. [4]

DATA AND METHODOLOGY

Data

In order to assess the corporate governance quality system for metallurgic companies, we will use the information contained in the “Comply or Explain Statement” that companies should voluntarily report to BSE. These statements are publicly posted on the company’s website. If the companies do not prepare such a statement, the data source is represented by the data published by the BSE listed companies on their own website (directors’ annual reports, financial reporting or any other useful documents or information presented on the company’s website).

Since the application of “Comply or Explain Statement” is relatively new in Romania (starting with the financial year 2009), it takes some time for the companies to comply with the new requirements.

Thus, only since 2011, the concerns to do corporate governance reports are consistent and therefore representative for our study. Therefore we analyzed the “Comply or Explain Statements” for the financial year 2011, statements that are reported to the BSE together with the financial reports (April 2012).

Sample selection

We have analyzed in our study the metallurgy companies listed on BSE which are the first three companies in Romania: ALRO (ALR), TMK – ARTROM (ART), and MECHEL TARGOVISTE (COS). For any comparisons we consider all the companies listed on the Bucharest Stock Exchange, which are a number of 81 (at a moment of our study-March2013)

Methodology

In evaluating the quality of corporate governance system we will rely on the results of numerous studies which enhance that the main component of corporate governance consists in *transparency and disclosure practices* (Cromme, 2005; Karamanou and Vafeas 2005; Bhat et al., 2006; Aksu and Kosedag, 2006; Junarso, 2006; Ben Ali, 2008; Kuznecovs 2011; Desouki & Mousa, 2012; Ionaşcu and Olimid, 2012.) It is also relevant that the international rating agencies (Standards & Poor’s, Credit Lyonnais Securities Asia-CLSA) pay particular attention to the practices of transparency and dissemination of information about the company, as an important component in order to develop the company’s performances scores, including also a corporate governance score.

In general as a first sign of effective corporate governance, the manifestation of choice to report the “Comply or Explain Statement” is considered, this reflects that company voluntarily chose to express their desire to adhere to the principles of good corporate practice.

The concept of corporate governance is based on stakeholder theory, developed by Freeman in 1984 and which involves managing a company by adopting many partnerships approaches that reconcile the interests of all interested partners (stakeholders). [5]

The concept is synonymous with corporate social responsibility (CSR) and with a meaningful communication of the financial, social, environmental and corporate governance performances of the company. Involvement in CSR activities comes to meet the requirements of successful corporate governance. In conclusion, we can also assess the quality of the corporate governance in terms of meeting the social and environmental needs of the stakeholders.

In conclusion to all of the above, we consider that the methodology for evaluating the quality of corporate governance system can be reduced by using one of the three main methods:

- a) In the beginning, we investigate whether the companies from our sample choose to prepare and report the “Comply or Explain Statement”.
- b) We develop a corporate governance score based on transparency and disclosure practices reflected in “Complain or Explain Statement”.

In order to assess the compared conclusions at the European or international level, we have reclassified the 51 questions contained in the Declaration “Complain or Explain” into five main investigating areas, according to Standard and Poor’s methodology to assess a corporate governance score. [6]

The structured questions contained in “Complain or Explain Statement” on the five areas are as follows:

- i) Governance structure-G: 10 questions
- ii) Investor relations-I: 10 questions
- iii) Board and management-B: 20 questions
- iv) Financial disclosure-F: 10 questions
- v) Corporate social responsibility-CSR: 1 question (we will treat this area in Section C)

At each of the above questions can be answered with YES/NO/If NO then EXPLAIN. For our reason to develop a corporate governance score, we will give 1 point for each correct answer YES and 0 points for NO. The minimum governance score obtained by a company is 0 and the maximum is 50.

- c) We investigate whether the Romanian metallurgy sampled companies perform *CSR activities*.

RESULTS

A. Preparing and reporting the “Comply or Explain Statement”.

Our study reflects that all Romanian listed metallurgy companies report the “Complain or Explain State-

ment”, as a voluntary requirement of the BSE Corporate Governance Code. For the comparisons, the market average is 73 % representing that 73 % of the companies listed on BSE agree to report such a declaration of compliance with the best practices of BSE.

With a share of 73 %, Romania is below the EU countries (86 %) in the number of companies choosing to report Comply or Explain statement. [7] But in comparison, in Croatia the average is much higher (95 %). [8]

B. Corporate governance score value for the metallurgy companies overall and by component as it follows:

Table 1 **Corporate governance score for Romanian metallurgical companies**

	CG (max. 50)	G (max 10)	I (max 10)	B (max 20)	F (max 10)
ALR	41	10	10	15	6
COS	36	10	10	14	2
ART	34	9	8	8	9
Average metallurgy	37	10	9	12	6
Total market average	30	5	8	10	5

Source: own preelucration

According to the study, we find that the Romanian metallurgy companies listed on BSE achieved an average corporate governance score of 37 points (on a scale from 0 to 50), above the average of stock market (30 points).

Analyzing the CG' score components we see that the average values registered for the Romanian metallurgy industry are above the average of the Romanian market. We note that the metallurgy companies record a double value compared to the average of the market, in terms of Governance Framework. In other words, the metallurgy companies listed on BSE, adopt a clear and transparent structure of governance which are adequately disclosed to the general public in a double proportion compared to the market average.

The main provisions of the code that the Romanian metallurgic companies do not agree with refer to: the administrative system which is a unitary system for all metallurgic companies, no company owns nomination committee, there is no audit committee (ALR, ART), there is no remuneration committee (ALR, COS) or the financial statements are not disseminated according to IFRS and also to the English language (COS).

C. Corporate social responsibility

With the development of corporate social responsibility activities, Romanian metallurgic companies record very good results, all the metallurgic companies in our sample perform CSR activities, compared to an average of 77% of the entire capital market.

CONCLUSIONS

The globalization of the capital markets, the competition for fundraising also requires greater adoption of standards and procedures of corporate governance internationally recognized. This aspect is particularly important for the emerging economies and for those in transition, which typically have regained their credibility to the investors.

According to the study, we find that Romanian companies listed on BSE operating in the metallurgical industry have successfully managed to adapt to the requirements of the capital market. The corporate governance structure is showing a pretty solid adoption of the best corporate practices on a general basis, higher than the market stock in Romania. Despite all of the efforts, however, metallurgical industry in Romania witnessed a significant restriction compared to what it was before in the 90s.

And the difficulties do not apply only to Romanian metallurgy economy but in many countries, regardless of their economic development. A lot of Romanian metallurgy companies namely Mechel, Oltchim, Arpechim Pitesti, Astra Cars Arad, Hunedoara Steel Plant, are just a few examples of plants about to be entirely or partly closed. Even private plants, which are owned by international corporations, have big problems.

Economic globalization has imposed very tough competition rules now, virtually all developed economies are under pressure because of the Chinese economic model that fails to provide the lowest prices.

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Note: The responsible translator for English language is the lector from Babeş-Bolyai University, Cluj-Napoca