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Editorial

International corporate finance and governance

1. Introduction

The financial crisis that started in 2008 has the potential to reshape the orthodox thinking in the world of finance. Although financial markets and institutions underwent a massive cataclysm, the corporate sector has been facing a turbulent period too. The current experience of firms in many Western developed countries has triggered attention to what has already happened during the Southeast Asian crisis of the late 1990s. Among the industrialized countries, momentous changes in corporate financing by means of equity, bonds and bank loans have been taking place. Once it was natural for many growing companies to consider raising new capital by means of going public; these firms mostly thought that it was better to organize initial public offerings. But, the sour memories of the tech crash of early 2000s after the late 1990s bubble and the meltdown in 2008 have made both firms and investors extra alert. Companies have become cautious in making capital investments; dividend payouts and share repurchases have become less popular; mergers and acquisitions – domestic or cross-border – have taken a plunge too. The tightening of lending by banks in many European countries is severely restricting the growth of small and entrepreneurial businesses. Risk management practices are coming under scrutiny. Intense debate is going on whether corporate governance failures, and especially some features of the Anglo-Saxon system, exacerbated the consequences of the financial crisis. Diverse stakeholders are now becoming more active in corporate governance. They are showing resentments over the too generous pay packages of top executives that seemingly do not help to increase corporate performance; they want their voices to be heard by company boards. All these developments make it important for us to know how firms across the globe are coping with the ever changing economic and financial environment; what the long-term consequences of these changes are; and how to rearrange existing contentious accounting and governance practices.

To further promote cutting-edge research on some of these as well as other contemporary issues, and to bring together scholars from around the world to provide valuable insights, a symposium on international corporate finance and governance was held at the University of Twente on October 14–16, 2010. A program committee consisting of Arnoud Boot (University of Amsterdam), Abe de Jong (Erasmus University Rotterdam), Luc Renneboog (Tilburg University), Peter Roosenboom (Erasmus University Rotterdam) and myself had an arduous task of reviewing more than 100 submitted papers in a short span of time. Each of us selected some papers based on our own professional judgment. Afterwards, an attempt was made to fit these papers into a session related to the theme of the Symposium and the authors' interest for publication in the special issue of the Journal of Banking and Finance. Each paper presented at the Symposium was subsequently reviewed and discussed by another scholar. Finally, throughout the last year, the Editor has applied the normal quality standard and refereeing process and has selected five articles for publication in this issue.

2. Brief summary

This special issue covers papers addressing contemporary issues facing firms and investors across the globe. In each paper, the authors meticulously perform an empirical analysis. They also review related prior studies and show how the paper contributes to the extant literature.

2.1. Trade credit, cash holdings and financial deepening

With trade credit, firms can separate payment from delivery of products. The selling firm extends credit to the buyer who is not required to make immediate payment. Trade credit is thus used as a popular source of short-term financing of firms. The study by Wenfen Wu, Oliver Rui and Chongfeng Wu addresses the relationship between trade credit and firm's cash holdings and how it is affected by the development of the financial sector. The authors focus on China because of the large variations in institutional quality and the levels of financial sector development across different regions in China. They argue that a higher level of financial development provides industrial firms the benefits of better services like easier access to finance, lower financing costs and lower transaction costs. These firms are likely to hold less cash to cover their trade payables and substitute more of their trade receivables for cash.

Wu et al. (2012) carry out an empirical examination using a large sample of Chinese listed firms over the period 1999–2009. They find that firms located in regions with higher level of financial development hold less precautionary cash to cover trade payables and have a higher substitute ratio of credit receivables for cash. The study thus re-emphasizes the important role played by financial sector development in not only helping firms to gain access to finance but also in making better use of trade credit as a short-term financing instrument.

2.2. Convertible bond announcements and issuer stock returns

A major source of financing by listed corporations is the issuance of convertible bonds. Event study results of the 1980s and 1990s consistently document that the share price announcement effect of convertibles is negative. Interestingly, convertibles announced from the year 2000 onwards are associated with more

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negative stock returns than those announced in earlier decades. The study of Eric Duca, Marie Dutordoir, Chris Veld and Patrick Verwijmeren analyzing a large US sample of convertible bonds asserts that this additional decline is primarily a result of short-lived price pressures induced by convertible arbitrage hedge funds. These funds purchased nearly three-quarters of convertible debt offerings in the US during the early 2000s. They combine their long position in convertibles with short positions in the underlying common stock and as such create a downward pressure on the stock price.

In their study, Duca et al. (2012) demonstrate that the large difference in announcement period stock returns during the post-2000 period, relative to the 1984–1999 period, is no longer significant once this hedging-induced short selling is controlled for. The authors also document that during the post-crisis period (September 15, 2008 – December 31, 2009), the magnitude of convertible announcement effect is even more negative than in the previous two periods. This decline can partly be explained by arbitrage-induced price pressure. The convertible issues of recent years are also associated with certain features like high issuer and market volatility and large offering underpricing that further depress announcement returns. The implication of the Duca et al. (2012) study is that event studies that do not take into account the arbitrage-induced price pressure effect are likely to draw overly pessimistic conclusions on the true information content of convertible bond announcements.

2.3. Corporate taxes, strategic default and cost of debt

Corporate taxes play an important role in financing decisions of firms. Firms need to weigh the benefits derived from the tax shield against the costs of financial distress that occur as a result of debt financing. The corporate tax system in the US allows corporations with net operation losses to carry it back or forward as a deduction in other tax years. In their paper, Ali Nejadmalayeri and Manohar Singh argue that this tax subsidy creates an incentive for the firm to continue to service its debt and hence keep the firm afloat longer. A firm's attempt to strategically postpone its default would influence the relative bargaining position of stockholders vis-à-vis bondholders: the former can persuade the latter to accept a lower credit spread.

Nejadmalayeri and Singh (2012) test this conjecture using a large sample of US firms for the period 1994–2009. They find that higher corporate tax rates are indeed associated with smaller credit spreads. Analyzing specifically the financial crisis period, they also observe that firms with relatively larger losses experience a greater reduction in the credit spread. The paper thus demonstrates the importance of corporate taxation as one of the determinants of the credit spread, particularly when a firm's default and/or recovery risk is high.

2.4. Government ownership and corporate governance

Many studies demonstrate the role played by different types of owners (individuals, families, managers, banks, pension funds, etc.) in influencing diverse corporate governance practices of firms. The paper by Ginka Borisova, Paul Brockman, Jesus Salas and Andrey Zagorchev is particularly interesting because it investigates the impact of share ownership by governments from 14 European Union countries. Governments typically affect the policies of private corporations by legal means, taxations and regulations. But, what is exactly the impact of government ownership on the corporate governance quality of firms?

In their paper, Borisova et al. (2012) examine this question using a sample of 133 government–owned companies for the period 2003–2008. They analyze the ownership stakes held by both national and local governments. The authors observe that government ownership is generally associated with inferior quality of corporate governance. National government ownership reduces the number of board committees and increases the power of chief executive officers of firms. Borisova et al. (2012) also investigate the influence of a country's legal system. The law and finance literature postulates that countries in civil law system employing greater direct government control tend to have weaker shareholder rights than those in common law system, where government share ownership is less prevalent. The empirical analysis of the authors shows that government ownership has a positive impact on corporate governance among common law countries while it is detrimental to governance quality among civil law countries. They also find that the ownership of a golden share that grants a government special controlling powers reduces the quality of firm's corporate governance.

2.5. Corruption, growth and governance

Corruption and fraud are widespread all over the world. The focus is typically on (developing) countries and the public sector, whereby bureaucrats are responsible for offering valuable services. Developed countries and the private sector are not immune from these practices too. For example, the US Securities and Exchange Commission has since 2009 filed charges of wrongdoing during the financial crisis against more than 100 people and firms. Many of the individuals are top executives of financial companies. The literature on the effect of corruption on economic growth shows mixed evidence. One strand suggests that a country's growth and development is adversely affected by corruption, whereas another suggests the opposite. Mathijs van Dijk and Thuy Thu Nguyen provide an empirical examination of the impact of corruption in Vietnam which, throughout the past several years, has continuously been experiencing annual growth in its gross domestic product. This paper is interesting for two main reasons. The authors focus on both private and state-owned firms; the latter group has been playing a vital role towards the economic growth of Vietnam. They also investigate how local public governance affects the severity of corruption across provinces in Vietnam. The study is one of the few that focus on firm-level analysis of corruption within a specific country context.

Van Dijk and Nguyen (2012) utilize two surveys to assemble a dataset comprising of 741 private firms and 133 state-owned enterprises spread over 24 provinces in Vietnam. They find that the effect of corruption differs significantly across types of firms: corruption in Vietnam negatively affects the growth of private firms, while it does not hamper the growth of state-owned enterprises. The authors state that the close connection between public officials and state-owned firms may help these relatively inefficient firms to continue to operate. While making further examination, van Dijk and Nguyen (2012) observe that the quality of local public governance (for example, better land access, promotion of private sector development and the implementation and consistency of policies) determine the severity of corruption.

3. Conclusion

These five papers collectively provide a rich scientific analysis of a few topics on international corporate finance and governance. I hope that the findings of these studies will provide significant insights and will be useful to academics, practitioners and policy makers world-wide. New empirical research on corporate finance and governance issues, especially from the European and emerging countries with their fascinating institutional features, is nonetheless necessary to continue to provide fresh perspectives on voluminous stuff that we do not know yet.

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Guest Editor
Rezaul Kabir
School of Management and Governance, University of Twente, Enschede, The Netherlands
Tel.: +31 53 489 3510.
E-mail address: r.kabir@utwente.nl

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