

CORPORATE GOVERNANCE, COMPETITION, AND FINANCE: RE-THINKING LESSONS FROM THE ASIAN CRISIS

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INTRODUCTION

This paper examines microeconomic behavior of economic agents—corporations, financial institutions, and governments in emerging economies. It focuses specifically on issues of corporate governance and financing of corporate growth as well as those relating to the nature and degree of competition in these countries. Such questions have not previously received much attention in development literature, which has generally emphasized macro- rather than microeconomic issues. Specifically, there has been scarce recognition of the fact that economic development is actually carried out by organizations and by corporations, large and small. The role of domestic, private corporations in economic development is a particularly underresearched area.¹

The Asian crisis of 1997-2000 has radically changed the research and policy agenda for emerging markets. As a consequence of this crisis, as well as those in Russia, Brazil, Argentina, etc., issues of corporate governance and behavior and the relationship between corporations and financial institutions, as well as questions relating to the intensity of competition, now command international attention. A main reason for these changed priorities has arguably been the important thesis concerning the Asian crisis first advanced by leading U.S. policymakers—notably Alan Greenspan [1998] and Larry Summers [Baker, 1998]—and developed further by the International Monetary Fund (IMF) (see references below). Alan Greenspan [1998], the chairman of the U.S. Federal Reserve, in his 1998 testimony to a Congressional Committee suggested that, in the last decade or so, the world has observed “a consensus towards, for want of a better term, the Western form of free-market capitalism as the model which should govern how each individual country should run its economy... We saw the breakdown of the Berlin wall in 1989 and the massive shift away from central planning *towards free market capitalist types of structures*. Concurrent to that was the really quite

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dramatic, very strong growth in what appeared to be a competing capitalist-type system in Asia. And as a consequence of that, you had *developments of types of structures which I believe at the end of the day were faulty*, but you could not demonstrate that so long as growth was going at 10 percent a year” (italics added).² Similarly, Summers stated: “(this crisis) is profoundly different because it has its roots not in improvidence but in *economic structures*. The problems that must be fixed are much more microeconomic than macroeconomic, and involve the private sector more and the public sector less” [Baker, 1998] (italics added). Greenspan’s and Summers’ structuralist view of the crisis was reflected in the IMF’s (1998a, 1998b) analysis and particularly in its reform program for the crisis-affected countries.³

Essentially, the Greenspan-Summers-IMF (GSI) thesis asserted that although certain macroeconomic disequilibria may have provided a trigger for the crisis, its fundamental causes lay in the day-to-day microeconomic behavior of economic agents in these societies. In short it was argued that what was at fault was nothing less than the Asian way of doing business and the institutional structures that supported that kind of business culture. This raised particularly issues of corporate governance, corporate finance, competition, and, more generally, the relationship among the banks, the corporations, and the government. How these variables and institutions interacted with each other to generate the crisis in terms of the GSI analysis is outlined in the following sections, which also explain the implications of these interactions for the New International Financial Architecture (NIFA). G7 countries have been attempting to create NIFA in the aftermath of the Asian crisis in order to forestall future crises.

The main purpose of this paper is to examine critically important aspects of the GSI’s structuralist thesis outlined above. It considers empirically what is the state of corporate governance and competition in the crisis-affected countries and, more generally, the emerging markets, and to what extent, if any, these accord with the predictions of the structuralist thesis. For this purpose the paper reports and builds on the authors’ recent empirical work in this area⁴ and reviews newly available evidence on the state of corporate governance, how corporations finance their growth, and the state of competition in emerging markets. This research takes an international perspective and, wherever possible, it provides explicit comparisons between emerging and mature markets.

The findings of this paper are not only of intellectual interest because of their direct bearing on the structuralist thesis concerning the Asian crisis, but equally importantly these also help us to assess the desirability of IMF’s reform program in these countries. As IMF [1998a, 105] noted “The IMF-supported programs and policy advice to the Asian crisis countries have placed particular emphasis on wide-ranging structural reforms of the financial and corporate sectors, competition and governance policies and trade regimes.”⁵

THE ASIAN CRISIS, CORPORATE GOVERNANCE, CORPORATE FINANCE, AND COMPETITION: ANALYTICAL ISSUES

The Asian crisis, which began with the floating of the Thai bhat in July 1997, quickly spread to the other leading Asian developing economies of Indonesia, Malay-

sia, and Korea. Both the severity of the crisis (in many respects it was virtually a financial meltdown), as well as the fact that it engulfed some of the fastest-growing and what were generally regarded as well-managed economies in the world, caused consternation among policy makers in the G7 countries and in the international financial institutions. Soon afterward, however, once it became clear that the crisis was unlikely to spill over into industrial countries, the GSI thesis emerged.⁶ The argument of their structural theory of the crisis is complex and has several strands.⁷

First, it is suggested that poor corporate governance and lack of competition led to overinvestment by Asian corporations. IMF (1998a) noted that, in Korea, government policies, such as access to easy credit through directed lending, played an important role in allowing the chaebol (the large conglomerates) to pursue growth and market share with inadequate attention to profitability. This excessive investment resulted in reduced profits because of excess capacity that existed in the world markets. Despite that, easy access to credit induced the chaebols to continue to invest and diversify away from core businesses into other industries, which were often also characterized by too-large capacity. Secondly, overinvestment in turn reduced rates of return, which led to falls in share prices and ultimately brought about a full-blown currency and banking crisis in part because of the weakening of the equity bases of the banks. In this view, therefore, the crisis was not caused by market failure but rather by institutional failure in Asian economies that, due to deficiencies in internal governance mechanisms, were unable to curb excessive corporate investment.

The suddenness of the crisis and its severity were attributed to the cronyistic relationships among corporations, financial institutions, and governments. The corporate sector was highly vulnerable because of its large debt/equity ratios, also a product of crony capitalism. The financial institutions, it is suggested, were weakened by “relationship banking” and were therefore also vulnerable. An external economic shock involving a rise in interest rates or a fall in the exchange rates would thus greatly damage the corporate sector. Similarly, as the Camdessus quotation in Note 3 indicates, the lack of transparency in the Asian style of business—because of cross-holdings and hundreds of subsidiaries owned by the large conglomerates—made it difficult to get a true picture of the financial state of a corporate group as a whole. It is suggested that once the investors became aware of these informational flaws they reassessed the risks and withdrew their capital from the crisis stricken economies, thereby exacerbating the crisis.⁸

In the structural theory of the Asian Crisis, the role of competition is at first sight somewhat ambiguous. On the one hand, it is suggested that there was a competition deficiency within these countries as a result of directed and subsidised lending to favored large firms, as well as other special concessions to these firms. On the other hand, it is argued that there was excess capacity in international markets and increased competition that led to a fall in profits. This ambiguity about the role of competition is more apparent than real, however. This is because what is being suggested is that, had domestic markets been allowed to function normally, that is, without distortions, large Korean companies would not have been able to continue to target growth and market share regardless of profitability.

Indeed, product market competition by itself can remedy flaws in corporate governance [Singh, 2003c; World Bank, 2002]. Such competition was impeded in many

countries by government barriers to entry and exit, the latter creating a moral hazard (through “too big to fail” syndrome; see, however, Chang [2000]). The net result was over investment and other indicators of inefficiency such as a decline in profits and productivity.

Although the GSI theory of the Asian crisis is plausible, it is not the only account of the crisis, nor the one that is most persuasive. There are many alternate theories concerning this deep downturn in economic activity, including theories of self-fulfilling prophecies, the precipitate and unhelpful behavior of the banks, and some weaknesses in the crisis countries’ fundamentals.⁹ Singh and Weisse [1999] and Singh, Singh, and Weisse [2003] suggest that the GSI thesis is deficient on several counts. First, it is not compatible with the outstanding success of Asian countries for more than three decades before the crisis if their institutional structures were as deficient as is being suggested. Second, it does not explain why countries such as China and India did not have a crisis even when India’s fundamentals were worse than those of the countries that had the crisis. Third, the debt-equity ratios of Indian nonfinancial corporations were higher than those of corporations in Thailand or Indonesia, yet the latter had the crisis and India did not [Singh, 1999a].

Fourth, the critics suggest that, at a macroeconomic level, overinvestment and misallocation of resources arose not so much from flaws in corporate governance and the state of competition but from financial liberalization, which a number of these countries implemented in the years immediately prior to the crisis. Corporate governance and intensity of competition were much the same in the mid-90s as they were in the previous three decades of outstanding success of these economies. What had changed in the period preceding the crisis was the role of the government following financial liberalization. The government in countries such as Korea and Thailand was no longer coordinating private sector investment activity in the way that it did in the era of fast growth, nor were firms guided or monitored on investment allocation.¹⁰ The crisis therefore arose not because of too much government intervention but too little, particularly in its crucial, former role of coordination, monitoring, and guidance of private sector investment decisions.

The IMF does not necessarily disagree with the view that a main cause of the crisis was premature financial liberalization, as it also emphasizes that the affected countries did not have adequate prudential supervision of the financial sector. As Singh [1998, 1999a] has pointed out, however, despite such shortcomings in prudential supervision, financial liberalization was encouraged, and certainly not discouraged, by the IMF before the crisis. In the alternative analysis, the main reason why, despite contagion, China and India were able to escape the crisis was precisely because they did not have as full capital account liberalization as the affected countries. Singh, Singh and Weisse [2003] argue that their alternative analysis is better able to explain the relevant facts concerning both affected and nonaffected countries than the GSI structural theory.

Despite the lack of academic consensus on the reasons for the Asian crisis and in particular on the structuralist thesis, the latter nevertheless determined the IMF’s policy response. The IMF programs sought far-reaching institutional reforms in the crisis economies. These reforms at a broad level involved the abandonment of previous practices and the establishment of arms-length relationships among government,

banks, and businesses, as well as big changes in the corporate governance mechanisms and in labor laws and competition laws in those economies (see Note 5 for details of the reforms in the various sectors in different Asian countries). The reform program was subsequently universalized and specifically the reform of corporate governance became a significant part of the NIFA, which, as mentioned above, G7 countries have sought to establish in the world economy in the wake of the crisis. The responsibility for this part of the reform was assigned to the OECD and to the World Bank. Both organizations have been collaborating on creating a “best-practice” code for corporate governance. Despite official denials to the contrary, a careful reading of the text of the World Bank document [Iskander and Chamlou, 2000], suggests that the Bank’s preferred system of corporate governance is that found in the U.S. That is, in its ideal form it consists of corporations with widely held shares in which the managers are obliged to maximize shareholder value.

Several international organizations are involved in the reform of competition and competition policies in emerging countries. These organizations include OECD, the United Nations Conference on Trade and Development (UNCTAD) and, most notably, the World Trade Organization (WTO). In order to remove internal and external barriers to trade, advanced countries are seeking to establish a multilateral agreement on competition policy that is to be a part of WTO disciplines. These proposals are opposed by developing countries, however. Nevertheless, the international significance of the state of competition and competition law and rules in emerging economies as well as in mature countries cannot be exaggerated.¹¹

Although the above discussion has concentrated on the international dimensions of corporate governance and competition issues, it is important to emphasize that there are also very good domestic reasons for giving priority today to these questions in many emerging countries. These arise from deregulation and widespread privatization (including that of natural monopolies) and the increasing role of the private sector in the economies. Studies of corporate governance and competition become salient for assessing and improving the efficiency of such economies, regardless of whether or not they had the crisis. Hence corporate governance, finance, and competition are of more general interest than simply as putative causal factors for the crisis in emerging markets.

OWNERSHIP, CONTROL, AND CORPORATE GOVERNANCE IN EMERGING AND MATURE COUNTRIES

The endorsement, essentially, of the structuralist theory of the Asian crisis by the international financial institutions (IFIs) in their policy programs in the affected countries did lead to a large research effort by these organizations, as well as by independent economists, to gather information on corporate governance issues in emerging countries. Although the available data are still patchy and far from being adequate to provide a solid basis for policy analysis, this is a huge improvement compared with the situation before. The main points of this new comparative information on ownership and control in emerging and mature market economies and their implications for corporate governance may be summarized as follows:¹²

The first important point revealed by this research is that the Berle and Means “widely held” corporation, characterized by separation between ownership and control, is a rarity rather than the norm outside the U.S. and the U.K., even for large firms. As Table 1 suggests, in the U.K. all the 20 largest publicly traded firms in 1996 were widely held (that is, there was no family or other locus of control). In Mexico, though, the corresponding 20 largest firms in that country were all family controlled. The incidence of family control in many European countries is also quite significant. More comprehensive and detailed information provided by Claessens, Djankov, and Lang [2000] for Asian countries indicates that for both large and small firms family control is the norm in emerging markets. Research also shows (see Table 1) that there is considerable state ownership and control of large corporations in many European and emerging markets.

TABLE 1
Control of Publicly Traded Firms Around the World, 1996 (%)
(of the 20 Largest Firms Under Each Category)

Economy	Widely Held	Family Owned	State Owned	Widely Held Financial	Widely Held Corporation	Other
<i>OECD countries (non-Bank borrower)</i>						
Australia	65	5	5		25	
Austria	5	15	70			10
Belgium	5	50	5	30		10
Canada	60	25			15	
Denmark	40	35	15			10
Finland	35	10	35	5	5	10
France	60	20	15	5		
Germany	50	10	25	15		
Greece	10	50	30	10		
Ireland	65	10			10	15
Italy	20	15	40	5	10	10
Japan	90	5	5			
Netherlands	30	20	5		10	35
New Zealand	30	25	25		20	
Norway	25	25	35	5		10
Portugal	10	45	25	15	0	5
Spain	35	15	30	10	10	
Sweden	25	45	10	15		5
Switzerland	60	3		5		5
UK	100					
USA	80	20				
<i>Bank borrowers and others</i>						
Argentina		65	15	5	15	
Hong Kong	10	70	5	5		10
Israel	5	50	40		5	
Mexico		100				
Singapore	15	30	45	5	5	
Korea, Rep. of	55	20	15		5	5

Note: The data are based on cross-sectional analysis of the ownership structure of the 20 largest firms by capitalization in 27 countries using a 20 percent threshold for control.

Source: Reproduced from Iskander and Chamblou [2000]; original source Claessens et al. [1998].

Finally, in large developing country corporations or the big conglomerate groups that are ubiquitous in emerging markets (see, for example, Singh [1995] and Khanna and Yafeh [2001]), there is often considerable divergence between the extent of corporate equity owned by families or other controlling shareholders and the extent of actual control over the corporations. Claessens, Djankov, and Lang [2000] make a useful distinction between cash flow rights and control rights. It is often found that, even with a small proportion of equity, families are able to lever themselves to control a majority of the shares. This is done by a variety of devices, such as pyramiding, introduction of different classes of shares, and complex cross-holdings of shares between parent and subsidiary companies (see also Note 15 below).

Concentration of Family Control, Crony Capitalism, and Economic Crises

In order to examine the phenomenon of crony capitalism and its relationship to the economic crisis, Claessen, Djankov, and Lang [2000] provide data (see Table 2) on the concentration of the total value of corporate listed assets controlled by the top families in nine Asian countries. In addition to “normalization” by total stock market capitalization, the variable, the total value of listed assets controlled by families, is also normalized by GDP of the country concerned (the last two columns of Table 2). If concentration is measured in terms of total value of listed corporate assets, the four crisis-affected Asian countries (Indonesia, Malaysia, Korea, and Thailand), had greater concentration than the noncrisis countries (Hong Kong, Japan, Philippines, Singapore, and Taiwan). There is no relationship, however, between concentration and crisis if the normalizing variable is GDP rather than total listed corporation assets. It is arguable that GDP, being more comprehensive, would provide a more appropriate normalization variable than total listed assets. Intercountry differences in concentration measured in terms of total stock market value may reflect more the extent of stock market development in various countries than the relative influence of top families on government policy. Ideally, what one would like is data on total wealth ownership, including land holdings. For many developing countries, the main locus of political power lies in land holdings, and GDP is likely to be a better proxy for a country’s total wealth than stock market valuation. There is thus, even in its own terms, no robust association between crony capitalism and financial crisis let alone a causal link between the two variables. Such a casual link is in any case highly problematic as the theoretical objections to it and the illustrative example of Sweden, both outlined below, indicate.

In democratic Sweden, where the Protestant ethic rules out any hint of cronyism or other kind of corruption, a single family, (the Wallenbergs) is believed to control 60 percent of the country’s industrial assets. This has not resulted in reduced efficiency or less democratic accountability of the industrial system. The analytical reasons for this phenomenon have been examined by Berglof and von Thadden [1999] and Singh, Singh, and Weisse [2003]. The essential argument of these authors can be summarized as follows. Crony capitalism is not a corporate governance problem, as such. It is rather a product of the complex of relations between the business and political elites and could in principle arise in systems with widely dispersed ownership.

Further, the system of corporate governance in many Asian countries was not all that different from that observed in several European countries, with family-owned and controlled firms being the norm in both sets of countries. This system worked extremely successfully in the Asian economies for the past 30 years, leading to high long-term growth rates and reduction of poverty. In continental European countries, such a family dominated system has worked well over a much longer period and has not led to Asian-type crises.

TABLE 2
How Concentrated is Family Control?

Country	Average Number of Firms per Family	% of Total Value of Listed Corporate Assets that Families Control (1996)				% of GDP 1996
		Top 1 Family	Top 5 Families	Top 10 Families	Top15 Families	Top15 Families
Hong Kong	2.36	6.5	26.2	32.2	34.4	84.2
Indonesia	4.09	16.6	40.7	57.7	61.7	21.5
Japan	1.04	0.5	1.8	2.4	2.8	2.1
Korea	2.07	11.4	29.7	36.8	38.4	12.9
Malaysia	1.97	7.4	17.3	24.8	28.3	76.2
Philippines	2.68	17.1	42.8	52.5	55.1	46.7
Singapore	1.26	6.4	19.5	26.6	29.9	48.3
Taiwan	1.17	4.0	14.5	18.4	20.1	17.0
Thailand	1.68	9.4	32.2	46.2	53.3	39.3

Note: Newly assembled data for 2,980 publicly traded corporations (including both financial and non-financial institutions). The data were collected from Worldscope and supplemented with information from country-specific sources. In all cases, we collect the ownership structure as of the end of fiscal year 1996 or the closest possible date. The “average number of firms per family” refers only to firms in the sample. To avoid discrepancies in the cross-country comparison due to different sample coverage, we have scaled down the control holdings of each family group in the last four columns by assuming that the firms missing from our sample are not controlled by any of the largest 15 families. The percent of total GDP is calculated using market capitalization and GDP data from the World Bank.

Source: Claessens, Djankov, and Lang [2000, 108].

Family Ownership and Corporate Performance

Apart from the issue of concentration of family ownership and economic crisis it is also relevant to ask how family ownership affects corporate governance and performance at a microeconomic level. There are only a small number of empirical studies on this subject for emerging countries and they provide a mixed picture. Suehiro's [2001] comprehensive study of ownership, control, and performance in Thailand in the period 1996 to 2000 came to the conclusion: “...it is safe to say that the difference in ownership pattern as well as the presence of a family-run business have hardly affected corporate performance in terms of financial indicators, such as the D/E ratio, ROA and ROE. It is difficult to see any distinct interrelationship between family ownership of business and poor performance in terms of leverage and profitability. Further, contrary to the traditional argument in favour of the model of good corporate governance, *the group of corporations with no ultimate owners (WV) has always shown the worst business record among surveyed listed companies in Thailand*” [p.12, emphasis in the original].

Khanna and Palepu [2000] studied a sample of large Indian firms in 1993 and concluded that firms affiliated with big diversified business groups performed better than independent firms. Lemmon and Lins' [2003] study of Korean firms suggested that there is no statistically significant relationship between ownership and Tobin's Q . Joh [2003] examined a very large sample of Korean firms in the period immediately preceding the crisis, 1993 to 1997. Controlling for firm and industry characteristics, Joh [2003] found a cubic relationship between ownership and firm profitability: profitability generally increases as ownership of the controlling families increases. Profitability is reduced when ownership is extremely high or extremely low. Joh [2003] attributes this result to poor corporate governance and suggests that the reasons why these findings differ from those of Lemmon and Lins [2003] and of Khanna and Palepu [2000] is because he is considering the period of the mid-1990s, which is later than the period of Lemmon and Lins' [2003] study when the Korean economy was less developed. His essential argument is that the business group structure found in Asian countries is helpful at a lower level of economic development, as it allows an internal capital market to allocate resources more efficiently than would an underdeveloped external capital market. At a higher level of development, however, the advantages of an internal capital market are outweighed by those of an external market.

TABLE 3
Median Return on Assets (%) by Country and Year (Inflation Adjusted)

	2000	1999	1998	1997	1996	1995	1994
Japan	5.5	3.7	1.7	2.0	4.5	4.3	2.8
Singapore	5.8	6.8	5.1	3.9	5.6	5.2	5.1
Hong Kong	10.0	9.5	0.6	0.4	2.1	-1.5	0.3
India	5.0	2.8	-7.8	-0.6	-0.1	-0.1	-1.2
Indonesia	-11.1	-13.3	-55.7	-5.1	0.2	-2.1	-0.3
Korea	4.0	5.3	-4.5	-0.9	-0.1	0.5	-1.4
Malaysia	5.2	2.4	-2.3	4.4	5.3	5.5	4.7
Philippines	2.5	-3.1	-5.8	-0.9	1.2	1.5	-0.2
Taiwan	5.1	6.4	3.3	6.1	5.8	4.0	5.1
Thailand	5.5	5.6	0.5	-11.4	1.5	2.3	3.3
Group Median (crisis countries)	4.6	3.9	-3.4	-3.0	0.9	1.4	1.5
Group Median (noncrisis countries)	5.0	3.8	-1.4	-0.1	1.7	1.5	0.9

Source: Extracted and adapted from Glen and Singh [2003].

Joh also suggests that Korean firms suffered from chronic low profitability in years before the crisis and that firm profitability was deteriorating in the pre-crisis period.¹³ This proposition is examined here more generally for crisis-stricken as well as noncrisis Asian countries in Tables 3 and 4. The Tables provide information on rates of return for the same group of Asian countries for which the question of crony capitalism was considered in Table 2. Table 3 indicates that the inflation adjusted rates of return were low or negative in the period preceding the crisis (1994-96) in Korea and Indonesia, but this was also the case in noncrisis countries such as India and Hong Kong. The last two rows of Table 3 suggest that in the period preceding the crisis there was a very little difference between the group medians of crisis and noncrisis

countries. Further, Table 4 suggests that during 1994-96 the inflation adjusted returns on equity were robust and highly positive in both crisis and noncrisis economies and again there was relatively little difference between the group medians.

TABLE 4
Median Return on Equity (%) by Country and Year (Inflation Adjusted)

	2000	1999	1998	1997	1996	1995	1994
Japan	7.4	5.4	2.9	4.1	7.1	6.6	4.6
Singapore	9.3	10.7	8.4	7.9	9.3	9.0	8.7
Hong Kong	14.0	14.0	5.0	6.6	9.0	3.2	7.9
India	11.1	9.2	-2.8	5.0	7.0	10.3	7.2
Indonesia	-39.0	11.9	-54.2	-5.2	8.5	6.7	7.1
Korea	8.0	10.8	-0.5	2.2	4.5	6.4	4.4
Malaysia	8.9	7.1	-0.2	9.5	11.7	12.5	11.6
Philippines	5.9	-2.9	-1.7	1.3	3.6	11.1	1.1
Taiwan	7.5	10.2	5.5	10.8	10.1	7.2	7.5
Thailand	12.9	10.4	15.9	-19.2	6.5	10.1	9.7
Group Median (crisis countries)	8.5	10.6	-0.4	-1.6	7.5	8.4	8.4
Group Median (noncrisis countries)	8.4	9.7	4.0	5.8	8.1	8.1	7.4

Source: Extracted and adapted from Glen and Singh [2003].

FINANCING OF CORPORATE GROWTH AND CORPORATE GOVERNANCE

We turn now to an analysis of the relationship between corporate finance and corporate governance. *A priori* one would expect the two variables to be closely related with causation running both ways. A central issue here is how do providers of finance to the corporation ensure that their money will be returned and not simply appropriated by the managers or whoever is controlling the enterprise [Shleifer and Vishny, 1997]. This question will be discussed analytically and empirically below in two stages. First we will enquire, how do emerging firms finance their growth, that is, to what extent do firms use retained profits, long-term debt, or new equity to pay for the expansion of their net assets? At the second stage, the implications of the observed financing patterns for corporate governance will be examined.

IMF [1998a] and the World Bank [1998] suggest that a main reason for the shortcomings in corporate governance in emerging markets was their low level of development of the stock market. Corporations were therefore obliged to go to the banks for financing their investment needs. The government's favoring such finance for large firms led to high debt-equity ratios; however, the banks, because of this cronyistic or close relationships with the government and with the corporations, did not perform the monitoring and disciplinary role that the stock market could perform. In the financial sector reform program for the Asian countries, therefore, the IMF and World Bank proposed that the Asian governments should adopt the following policies [Suehiro, 2001]:

- Develop their stock markets in order to promote direct corporate finance;
- Appoint independent directors to company boards and establish independent audit committees;

- Introduce new audit and accounting systems in line with the International Accounting Standards Committee (IASC) or the American Financial Accounting Standards Board (FASB);
- Introduce new legal frameworks governing bankruptcy in order to resolve quickly corporate debt conflicts between foreign creditors and local debtors; and
- Promote an information disclosure system to improve local corporations' transparency for the sake of investors and minority shareholders.

Empirical evidence on the role of the stock market and the financing of corporation growth does not accord with the IFI's presuppositions, however, as is indicated below. Singh and Hamid [1992] and Singh [1995], were among the first large-scale studies of financing corporate growth in emerging markets. These studies (referred to hereafter as S and H) arrived at quite unexpected conclusions. S and H found from their analysis of normally the 100 largest quoted firms in manufacturing in 10 leading emerging markets during the 1980s that these corporations relied overwhelmingly on external finance rather than internal finance (retained profits) to pay for the growth of their net assets. The average quoted firm in Singh's [1995] study financed only 40 percent of its growth from internal sources and 60 percent from outside finance, with long-term debt constituting 40 percent and new equity comprising 20 percent of the total growth of net assets. As these are the average figures, the use of external finance was even higher in some of the individual countries such as Korea. In that country, external finance comprised almost 85 percent of the total growth of corporate net assets.

These figures are extremely surprising, in part due to the fact that the advanced country (AC) corporations are known to rely overwhelmingly on internal finance—retained profits—for their financing needs. The net contribution of equity finance from the stock market is very small in ACs and indeed negative in the case of the U.K. and U.S. Negative figures for equity indicate that the total value of new issues of stock is less than the equity redeemed either by firms' purchasing their own stock, or shares that are bought up during takeovers [Corbett and Jenkinson, 1994].

It is not surprising in itself that there should be differences between AC and developing country (DC) corporations in relation to how they would meet their financing requirements. What is observed, however, is totally opposite to what economic analysis would predict to be the nature of the differences between the two groups. In view of the fact that DC capital markets are regarded as being underdeveloped and imperfect, one would have expected that DC companies would be obliged to rely mostly on internal sources rather than on an imperfect and therefore more expensive market for outside finance. Similarly, AC corporations may be expected to use more finance from the stock market and the banks compared with those from DCs, as the former have access to more highly developed and efficient capital markets.

Another important reason for expecting the opposite result of what is observed lies in the volatility of share prices on DC stock markets. As stock markets in emerging countries are relatively new and firms do not have established reputations, one would expect arbitrary and fluctuating prices—a prediction that is confirmed by the data [Tirole, 1991; Singh, 1999a]. In these circumstances, risk-averse firms may not

wish to raise funds on the stock market and may indeed shun the stock market altogether and not seek a listing at all. This point leads to another anomalous fact: an emerging stock market such as that of India has 8,000 companies listed on it, more than the number listed on the New York stock market.

The pattern of finance reported by Mayer [1988], and Corbett and Jenkinson [1994] for AC corporations is fully compatible with the "pecking order" theory of finance. This theory is based on the concept of asymmetric information. In a classic paper, Majluf and Myers [1984] showed that, in the presence of asymmetric information about the firms' prospects between the managers and the investing public, it would pay rational managers to follow a hierarchy of finance with retained profits first, debt next if a firm's investment requirements are more than the funds provided by retained earnings, and only as a last resort should the firm go to the stock market.¹⁴ However, Guggler, Mueller, and Yortoglu [2003] have noted that, in view of the regulatory deficits of emerging stock markets, these countries may be even more subject to asymmetric information than ACs. Further, Singh's [2003a] theoretical analysis of the financing of corporate growth in DCs suggests that there are emerging market specificities that would provide further incentive to DC firms to use mostly internal finance rather than debt or equity. These special features of DC firms are first that they are family owned and therefore much less subject to agency problems as compared to AC firms. Second, DC firms would like to retain family control and therefore wish to avoid the stock market to raise funds, as that would dilute their ownership and control. Taking all these considerations into account, Singh [2003a] sums up the theoretical position on the financing of corporate growth in the following terms: that if there are good reasons to expect the pecking order pattern of finance for AC firms, there are even better reasons for doing so for DC firms.

How does one explain these theoretically anomalous results for DC corporations? The first point here is that the studies for ACs and DCs, are using different sources of data and answering different questions. The analysis of finance and corporate growth in ACs is based on flow-of-funds data and is concerned with the question of how the nonfinancial corporate sector as a whole finances its growth. However, DC results are based on accounting data, and are concerned with a different question: how does an individual firm finance its growth of net assets? From the perspective of the theory of the firm, the second question is more appropriate since the theory relating, for example, to asymmetric information outlined above is concerned with the individual firm's behavior rather than that of the corporate sector as a whole.

Other methodological differences between AC and DC corporations with respect to the financing of corporate growth are empirical rather than theoretical. In DC studies, data for corporate growth net out depreciation from both the beginning and the end of the period assets figures, whereas in AC studies depreciation is not netted out. However, when the same methodology is used to measure the contribution to corporate growth of different sources of finance in emerging and mature markets, the results for the two groups are much closer. Nevertheless, theoretically anomalous differences remain.

Singh's [1995] study was based on the data for the 1980s. For the 1990s there is now more comprehensive data available, which raises two issues. First, do these anomalous results for the 1980s continue into the 1990s, and second, do the more comprehensive

data available now lead to any revisions of the results produced by S and H with more limited data for the 1980s? Taking the second question first, this has been investigated in Singh [2003a] and in Whittington, Saporta, and Singh [1997]. The results indicate that, in the absence of directly available data on equity financing in the 1980s exercise, estimation of the contribution of that variable by indirect methods is unlikely to have led to a persistent upward bias in the figures reported for this variable for most countries.

TABLE 5
Financing of Corporate Growth in 1995-2000^a (Percent)

Developed Markets				Emerging Markets			
	Liabilities	Ext. F.	Int. F.		Liabilities	Ext. F.	Int. F.
Australia	58	32	11	Argentina	46	16	38
Austria	52	3	45	Brazil	74	11	15
Belgium	56	6	38	Chile	44	33	23
Bermuda	41	23	36	Colombia	73	16	11
Canada	56	32	12	Czech	33	21	46
Cayman Islands	90	8	2	Hong Kong	44	20	35
Denmark	72	6	23	Hungary	28	1	71
Finland	53	26	22	India	53	5	43
France	61	7	31	Indonesia	110	12	-23
Germany	62	5	33	Israel	54	6	40
Greece	52	34	14	Korea	27	48	25
Ireland	76	5	18	Malaysia	40	18	42
Italy	68	5	27	Mexico	61	30	10
Japan	62	6	32	Philippines	34	17	49
Netherlands	65	9	26	South Africa	49	10	41
Norway	50	23	27	Taiwan	59	40	1
Singapore	66	15	19	Thailand	74	11	15
Spain ^b	68	-9	40	Turkey	61	18	21
Sweden	57	4	39	Venezuela	27	54	19
Switzerland	54	7	39				
United Kingdom	52	21	27				
United States	47	21	32				
Group Average	53	17	30		35	39	27
Global Average	49	22	29				

a. This table considers corporate growth in terms of percentage change in total assets. The latter is decomposed into growth of liabilities (column 1), of equity finance (column 2), and of internal finance (column 3). For each country the 3 columns add up to 100. The total number of countries in the sample is 3,360. Companies are excluded if any of their ratios are outside [-200, +200].

b. Spain has 18 companies, one of which experienced a small decline in total assets over 1995-00. That company also saw external equity increase, which resulted in a large negative value for the external equity ratio. Excluding that one company the sample mean of the ratio is 3 percent; the internal equity ratio would decline accordingly.

Source: Glen and Singh [2003].

We turn now to the first question of how the results of the 1990s differ from those of the 1980s. Table 5 provides information on this subject for firms in 19 DCs and 22 ACs—a much larger and more comprehensive data set than that which was available to S and H in the 1980s. This new data set is described in Glen and Singh [2003]. Table 5 indicates that between 1995 and 2000 on average the DC firms financed 27 percent of their growth of total assets from retained profits, 35 percent from increased debt (liabilities) and the remaining 39 percent by external equity issues. In AC corporations

it would appear that the large part of growth of corporate total assets has been financed by long-term debt (53 percent). The contribution of external equity, at 17 percent, is much smaller than for DC firms, while the contribution of internal finance, at 30 percent, is marginally higher than the average for emerging markets. These data indicate that the pecking order theory is comprehensively rejected for many DCs as well as ACs. Further, the anomalous pattern of financing behavior for DC corporations in the 1980s continues to prevail in the 1990s, although in a somewhat weaker form than before.¹⁵

We turn now to the implications of these observed patterns of financing corporate growth for corporate governance. The empirical results show *prima facie* that new issues on the stock market are relatively more important for corporations in DCs than for those in ACs. There are in principle three channels through which corporate governance may be affected by the stock market: 1) the regulatory framework of the stock market itself concerning standards for corporate accounts, transparency, etc.; 2) the pricing process on the stock market; and 3) the takeover process. The three channels are not equally powerful, however, and corporate governance is affected more by the stock market in countries such as the U.S. and the U.K. than in other countries, including DCs. The main reason for this is not that firms in the U.S. and the U.K. have greater recourse to stock market finance or go more often to the stock market to raise finance than elsewhere. If anything, there is evidence that many large Anglo-Saxon firms seldom go to the stock market to raise any capital at all. Nevertheless, because of the existence of a highly active market for corporate control in the U.S. and the U.K., even firms that shun the stock market become subject to takeover discipline.

Such markets for corporate control have not yet evolved in emerging countries. These exist, if at all, in an embryonic form in a few developing economies. Significantly, markets for corporate control do not exist even in most ACs, including notably West Germany and Japan. This is not an evolutionary deficit in these countries, but rather a matter of deliberate design [Singh, 2000; Odagiri, 1992]. Significantly, the lack of a market for corporate control has not imposed any great hardship on these economies, as their superior long-term economic records over the last 50 to 100 years compared with that of Anglo-Saxon countries indicates. Although large corporations are mainly influenced by the stock market through the takeover mechanism, they are also affected by the stock market pricing process (which affects their cost of capital) and the stock market's regulatory framework (which affects their information disclosure and treatment of minority shareholders). However, if no takeover mechanism exists and firms do not go to the stock market because there are alternative channels available for financing corporate growth from sources other than the stock market (say, for example, the banks), the stock market would have very little influence on corporations.

An important question in the present context is whether a greater influence of the stock market would lead to an improvement in corporate governance and in corporate performance. This essentially boils down to the question of whether DCs should encourage and promote a quicker development of a market for corporate control. This is a highly controversial issue. Singh [1997, 1999b, 2003a] has argued in previous contributions that the stock market pricing process and the takeover mechanism are not in

general very helpful in improving economic performance in ACs and there are good reasons to suggest that they are even less likely to do so in DCs.

A complex analytical and empirical argument on these issues may briefly be stated in the following terms: in relation to the pricing process in the real world stock markets, Tobin's [1984] distinction between "information arbitrage" efficiency and "fundamental valuation" efficiency is important. Evidence suggests that, while markets may be efficient in the former sense (even that is debatable), they are not efficient in the more crucial sense of not always reflecting a corporation's "fundamentals" [Shiller, 2000; JEP, 1990]. This point does not need to be belabored today in the light of the bursting of the technology bubble in the AC stock markets and 10 years of stock market decline in Japan. Equally, it will be difficult to preach a gospel of the Efficient Markets Hypothesis to citizens in Thailand or Indonesia, who suffered a virtual meltdown of their stock markets during the crisis.

Further, with respect to the takeover mechanism, three decades of analysis and empirical research suggests that selection in the market for corporate control does not take place on the basis of performance alone, but on the basis of both size and performance.¹⁶ Thus a large, relatively unprofitable company has a better chance of surviving takeovers than a small, relatively profitable company. Not only size provides relative immunity from takeover, however; a large company may become bigger still through the takeover process itself. Further, there are good theoretical reasons as well as empirical evidence that takeovers may lead to "short-termism" and more broadly to economic rewards being given for financial engineering rather than for entrepreneurial efforts in improving products and cutting costs. The takeover disciplining process is thus observed to be arbitrary and haphazard [Ravenscraft and Scherer, 1987]. The deficiencies of the pricing and takeover processes are compounded in the case of DCs because of the regulatory deficits and relative immaturity of their markets. Singh [1998] therefore suggested restrictions on the evolution of a market for corporate control in emerging countries.¹⁷

The above analysis indicates that, at the very least, it is arguable that the World Bank and IMF preference for the U.S. model of corporate governance based on widely held firms and a stock market takeover mechanism may have serious drawbacks for DCs. The international community would be ill-advised to establish such an international best-practice standard for DC firms to follow without a great deal of further analysis and supporting evidence.

THE STATE OF COMPETITION IN EMERGING MARKETS¹⁸

We turn now to the second part of the GSI structuralist thesis, which, as indicated earlier, asserts that the Asian crisis in a fundamental sense was caused by the Asian way of doing business. Apart from weak corporate governance, this was also characterized, in this view, by a poor competition environment. The question of intensity of competition in emerging markets will be considered here empirically in a comparative international perspective.

There is surprisingly little empirical evidence on the state of competition in emerging markets despite the fact that many of these economies have been following market-oriented policies of deregulation and privatization for nearly 20 years. In the absence

of hard evidence, economists hold differing views as to how intense is competition in emerging markets. Laffont [1999] holds, for instance, that as many developing countries are small, with segmented markets, high transportation costs and infrastructure bottlenecks, they are unlikely to have strong competition. Similarly, de Soto's [2001] work would seem to suggest that there are government-imposed bureaucratic hurdles for starting new businesses that restrict entry and therefore are not compatible with a vibrant competitive economy. On the basis of case studies, however, Porter [1990] suggests that in Korea corporations are subject to intense domestic and external competition and indeed only those industries in which firms are fixed with stiff competition are successful. Amsden and Singh [1994] also suggest that the Korean chaebol are highly rivalrous.

The small amount of data available on an international comparative basis suggests that many leading DCs have high three- or four-firm concentration ratios compared with advanced countries [World Bank, 1993]. It is also the case, though, that DCs tend to have a very large proportion of small firms employing less than 10 workers. These constitute normally more than 50 percent of the total industrial labor force in leading emerging countries, compared with less than 10 percent in the U.S. economy [Tybout, 2000].¹⁹ Thus these static measures of competition provide conflicting evidence about the state of competition in emerging markets.

In order to overcome the well-known difficulties with static measures of concentration, Glen, Lee, and Singh [2001, 2002] have used time-series analysis of corporate profitability in seven emerging markets to discover the dynamics and the intensity of competition in these economies relative to what has been observed for ACs. Glen, Lee, and Singh have employed the same methodology of the persistence of profitability (PP) studies (pioneered by Dennis Mueller and his colleagues) as has been widely used to study competition intensity in DCs. It will be recalled that the PP methodology involves fitting the following autoregressive equation applied to the time series of profitability of individual firms

$$(1) \quad \pi_{i,t} = \alpha_i + \lambda_i \pi_{i,t-1} + \mu_{i,t},$$

where, $\pi_{i,t}$ is the profitability of firm i at time t , $i = 1, \dots, m$, $t = 1, \dots, T$. $\mu_{i,t}$ is the usual error term and α_i and λ_i are the model parameters. λ_i indicates the speed of adjustment; if $\lambda_i < 1$, the long-run (permanent) profitability level of firm i is given by:

$$(2) \quad \pi_{i,p} = \alpha_i / (1 - \lambda_i).$$

As is usual in PP studies, to control for business cycles and other macroeconomic shocks, the regression analysis is conducted in terms of the variable $Y_{i,t} = \pi_{i,t} - \pi_t$, where π_t is the average of the $\pi_{i,t}$ across firms. The measure $Y_{i,t}$ represents the deviation of firm i 's profitability at time t from the profitability of all other firms in the country at that time. The analysis is based on models of the form:

$$(3) \quad Y_{i,t} = \alpha_i + \lambda_{1i} Y_{i,t-1} + \lambda_{2i} Y_{i,t-2} + \varepsilon_{i,t},$$

where α_i , λ_{1i} , and λ_{2i} are coefficients and the $\varepsilon_{i,t}$ are random errors. The empirical analysis shows that this model is sufficient to capture the dynamics in *all* cases in the seven emerging countries studied by Glen, Lee, and Singh.

From Equation (3), the statistic $Y_{iLR} = \alpha_i / (1 - \lambda_{1i} - \lambda_{2i})$ can be derived to indicate firm i 's long-term profitability relative to the country average. If $\lambda_{2i} = 0$, then the estimate of λ_{1i} provides a direct measure of the speed of adjustment of profitability following a shock. Assuming $\lambda_{1i} \in (0, 1)$, adjustment to equilibrium is monotonic. Where λ_{2i} is not zero or $\lambda_{1i} \in (-1, 0)$, adjustment is nonmonotonic and there is no unique way of characterizing its speed based on the estimated parameters. (See also Goddard and Wilson [1999]).

TABLE 6
Developing Countries: Mean Values of λ_i and Proportion
of Significantly Positive and Significantly Negative Y_{iLR}

	Mean λ_i	Positive Y_{iLR}	Negative Y_{iLR}
Brazil	0.013	1 / 56	3 / 56
India	0.229	2 / 40	4 / 40
Jordan	0.348	1 / 17	0 / 17
Korea	0.323	7 / 82	2 / 82
Malaysia	0.349	4 / 62	7 / 62
Mexico	0.222	0 / 39	0 / 39
Zimbabwe	0.421	0 / 40	4 / 40

Source: Glen, Lee, and Singh [2002].

The estimated values of λ_i and the proportion of firms for which Y_{iLR} is either significantly positive or significantly negative at the 5 percent level are reported in Table 6. The exactly corresponding values of these variables for ACs, estimated by other researchers, have been assembled together in Goddard and Wilson [1999] and Glen, Lee, and Singh [2002].

Surprisingly, as mentioned in the Introduction, the results indicate that DCs have, on the whole, lower persistency coefficients (λ_i) than those observed for ACs, even when allowance is made for the shorter time series of corporate profitability available for DCs than for ACs (see Tables 7 and 8). Further, the proportion of firms for which long-term profitability is significantly different from the norm, either in the positive or negative direction, is also much lower for DCs than for ACs. The conventional interpretation of these results would suggest that DCs are subject to no less, if not greater, competition than ACs. The possible sources of statistical bias in these empirical results for emerging economies have been examined in detail by Glen, Lee, and Singh [2002] and they find that these do not affect their main conclusions.

Evidence complementary to that of Glen, Lee, and Singh is provided by other research that also bears on the dynamics of the competition process but uses a different methodology. This work, which systematically analyzes turnover and the mobility of firms, provides interesting results. Studies in this genre have recently been summarized by Tybout [2000] and Caves [1998]. The results indicate that there is greater mobility, as well as entry and exit of firms, in the small number of emerging markets for which such studies have been carried out than for ACs.

TABLE 7
Persistence of Profitability Studies for Advanced Countries: λ values

Author	Country	Sample Period	Observations per Firm	Number of Firms	Sample Mean (λ_i)
Geroski and Jacquemin [1988]	U.K.	1947-77	29	51	0.488
	France	1965-82	18	55	0.412
	Germany	1961-81	21	28	0.410
Schwalbach et al. [1989] ^a	Germany	1961-82	22	299	0.485
Mueller [1990]	U.S.	1950-72	23	551	0.183
Cubbin and Geroski [1990]	U.K.	1948-77	30	243	0.482
Khemani and Shapiro [1990]	Canada	1964-82	19	129	0.425
Odagiri and Yamawaki [1990]	Japan	1964-82	19	376	0.465
Schohl [1990] ^b	Germany	1961-81	21	283	0.509
Waring [1996] ^c	U.S.	1970-89	20	12,986	0.540
Goddard and Wilson [1999]	India	1972-91	20	335	0.45
					(0.59)*
Odigari [forthcoming]	Japan	1983-97	15	357	0.50
					(0.59)**

Source: Goddard and Wilson [1999], except for Odagiri [forthcoming].

a. Based on nominal profit on capital, before tax.

b. Estimations are for industry groups. Estimates of λ are from a range of specifications for the persistence model, which differ across industries.

c. Estimate based on pooled data for 123 industry groups. The mean λ has been estimated by the present authors from the data in Table 3 of Waring [1996].

Reproduced from: Glen, Lee, and Singh [2002].

TABLE 8
Statistics on Long-Run Profitability: AC Corporations

	(1) Mean Y_{ILR}	(2) Positive Y_{ILR}	(3) Negative Y_{ILR}
United Kingdom 1951-77 (243 firms)	0.108	37(15.2)	37(15.2)
United States 1950-72 (551 firms)	0.239	125(22.7)	149(27.0)
United States 1964-80 (413 firms)	-0.359	66(16.0)	137(33.2)
Sweden 1967-85 (43 firms)	-0.015	7(16.2)	8(18.6)
Canada 1968-82 (161 firms)	0.065	33(20.5)	23(14.3)
Federal Republic of Germany 1961-82 (290 firms)	0.007	53(18.3)	50(17.2)
France 1965-82 (450 firms)	0.297	NA	NA
Japan 1964-82 (376 firms)	-0.069	62(16.5)	58(14.9)

Figures in brackets are percentages.

Source: Odagiri and Yamawaki [1990].

Reproduced from: Glen, Lee, and Singh [2002].

Apart from these two kinds of studies on the dynamics of the competition process, there are also other types of evidence pertaining to the efficiency of emerging market industries and to scale economies that do not accord with the conventional anecdotal account of the lack of competition in emerging countries. This empirical research has recently been reviewed by Tybout [2000], who sums up the situation as follows: "Indeed, although the issue remains open, the existing empirical literature does not support the notion that LDC manufacturers are relatively stagnant and inefficient. Turnover rates in plants and jobs are at least as high as those found in the OECD, and the amount of cross-plant dispersion in measured productivity rates is not generally greater. Also, although small-scale production is relatively common in LDCs, there do not appear to be major potential gains from better exploitation of scale economies" (p. 38).

Glen, Lee, and Singh [2002] suggest that these results on the comparative intensity of competition in emerging and mature countries are in economic terms totally plausible. This is because, although there are many structural features of DCs and the policies of their governments that are anti-competition, there are also equally strong, if not stronger, structural factors that favor competition. The anti-competition factors would include transportation and infrastructural deficiencies as well as the maze of bureaucratic procedures often required to start a business in DCs. These may be more than balanced, however, by pro-competition forces, which include lower sunk costs for starting a business in DCs, a large demand for simple products, and at times a pro-competition government policy stance (for example, some DCs have made firms compete for government favors by setting specified performance requirements, the so-called contest-based competitions [World Bank, 1993]).²⁰

THE STRUCTURAL THESIS, FINANCIAL LIBERALIZATION, AND ECONOMIC CRISES

The previous sections have examined in detail important aspects of the GSI structuralist thesis. The empirical findings on the role of corporate governance, the nature of corporate finance, and the state of competition in emerging markets may be summarized as follows:

- (1) No robust evidence suggests even an association between crony capitalism (proxied by concentration of control over corporate assets by a few top families, measured in different ways) and economic crisis, let alone a causal relationship between the two variables.²¹
- (2) Available evidence does not support the view that there is a negative relationship between family ownership and control of Asian firms and their economic performance. Further, falling profitability in the years prior to the crisis in countries such as Korea was not due to family control of corporations, but to other factors. Moreover, there is little evidence to suggest that falling profitability "caused" the crisis, since such deterioration in profits was observed in both crisis and noncrisis countries.
- (3) Contrary to much economic analysis and World Bank-IMF conjectures, stock markets in emerging countries provided a surprisingly large proportion of resources for the growth of corporate net assets during

the 1980s, and this trend, broadly speaking, continued into the 1990s, until the Asian crisis. It was noted, however, that the main influence of the stock market on corporate governance comes through the market for corporate control. Such a market has not yet evolved in most emerging countries, although it exists in an embryonic form in a few of them. Economic analysis as well as the experience of ACs suggests that the fuller development of such a market will not necessarily be helpful to most developing countries.²²

- (4) Contrary to the structuralist thesis, corporations in leading emerging markets are subject to intense competition and display highly rivalrous behavior. Empirical studies, using different methodologies, indicate that competition in emerging countries is at least as intense as in mature countries.

Thus microeconomic behavior and structures in emerging markets do not provide robust evidence in favor of the structuralist thesis. In sharp contrast, it is important to note that there is strong and robust support for the alternative analysis, which attributes the Asian crisis mainly to precipitate financial liberalization. Apart from the analysis and evidence in favor of this hypothesis outlined earlier, systematic studies including those by Kaminski and Reinhart [1999] and by Demirguc-Kunt and Detragiache [1998] indicate that there is a close relationship between financial liberalization and economic crises in developing countries, which may take the form of a banking crisis, a currency crisis, or both. The evidence on this subject has recently been reviewed by the IMF itself in Prasad et al. [2003]. Contrary to many theoretical models, Prasad et al. [2003] conclude that, "while there is no proof in the data that financial globalisation has benefited growth, there is evidence that some countries may have experienced greater consumption volatility as a result" (p. 6). The reasons for this disjuncture between economic theory and evidence have been explored in a large literature that has recently been reviewed in Singh [2003b].

Singh, Singh, and Weisse [2003, 5-6] suggest that a viable explanation of the Asian crisis that encompasses all the observed facts for both the crisis and noncrisis economies is that the afflicted "economies dismantled their controls over the borrowing of the private sector and embraced financial liberalization. As a consequence, the private sector built up short-term foreign currency debt that often found its way into the nontradable sector and into speculative real estate ventures. Accompanying financial liberalization was the irrational exuberance and contagion that are always latent in private international financial flows." Thus it can be argued that the crisis occurred not because the Asian model was followed, but precisely because it was not followed. Singh, Singh, and Weisse [2003] go on to add that, "while Edmund Phelps identifies the crisis with the failure of Asian corporatism (Phelps, 1999), in reality this system underpinned the most successful industrialization drive in history and dramatically reduced poverty. The system, however, was vulnerable to the forces unleashed by financial liberalization."

CONCLUSION

It has been argued in this paper that instead of the corporate governance system and the state of competition in emerging markets being flawed, it was the GSI thesis that attributed the fundamental causes of the Asian crisis to these factors that was deeply flawed. The IMF's structural reform program, based on this flawed thesis, is consequently not very helpful for developing countries. The analyses and evidence presented and reviewed in this paper suggest that the replacement of the existing system of family ownership and control in these countries by the Anglo-Saxon system of corporate governance (based on well-developed stock markets, widely held firms, and shareholder wealth maximization by managers) is unlikely either to benefit economic development or to make the liberalized global economy more stable.

In view of the domestic, as well as international, policy significance of corporate governance and competition outlined earlier (in relation to the NIFA), it is important that policy analysis in this area should be based on solid, unbiased empirical research. This paper has hopefully contributed to this endeavor in some small way.

NOTES

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1. As explained in Section II and III below, however, there has been a great deal more research on these subjects since the Asian crisis.
2. As quoted in the *International Herald Tribune*, 13 February 1998.
3. The then managing director of the IMF, Mr. Camdessus, observed in relation to South Korea, "In Korea, for example, opacity had become systemic. The lack of transparency about government, corporate and financial sector operations concealed the extent of Korea's problems—so much so that corrective action came too late and ultimately could not prevent the collapse of market confidence, with the IMF finally being authorised to intervene just days before potential bankruptcy" [IMF, 1998b]. See also Note 5.
4. See Domowitz, Glen, and Madhavan [2001]; Glen, Lee, and Singh [2001, 2002]; Singh [2003a; c]; and Glen and Singh [2003].
5. In broad terms the suggested reforms included:
 - Financial and Corporate Sector Reforms
 - Liberalization of foreign investment in domestic banks (Korea, Indonesia, and Thailand).
 - Introduction of more stringent conditions for official liquidity support (Indonesia, Malaysia, and Thailand).
 - Restructuring of domestic and external corporate debt (Indonesia, Korea, and Thailand) and closure of nonviable firms (Korea).
 - Competition and Governance Policies
 - Establishment of competitive procedures for privatization of government assets and for procurement (Indonesia; planned in Malaysia and Thailand).
 - Announcement of bans on or limits to the public funds to bail out private corporations (Indonesia, Korea, Malaysia, and Thailand).
 - Introduction or strengthening of bankruptcy laws and exit policies (Indonesia, Korea, and Thailand).

- Strengthening of corporate disclosure standards (Korea).
 - Liberalization of foreign investment in ownership and management in sectors other than the financial sector (Korea, Indonesia, Malaysia, and Thailand).
6. The role of the World Bank has been ambiguous as the Bank's then Chief Economist, Professor Joseph Stiglitz, formed a rather different view of the crisis from that of the IMF. As Wade and Veneroso [1998] suggest, however, Professor Stiglitz's dissent was not shared by the World Bank's operational staff, who carried out much the same reform program that the IMF did.
 7. Other contributors to the structural thesis include Summers [2000], Phelps [1999], IMF [1997], and the U.S. Council for Economic Advisers [1998, 1999]. For an implicit or explicit critique of the structuralist thesis, see Chang [2000], Sakakibara [2001], Stiglitz [1999], Wade and Veneroso [1998], Sachs and Radelet [1998], Singh and Weisse [1999], and Jomo [2001].
 8. The Johnson et al. [2000] study, suggesting that the decline in stock market valuation of firms as well as currency depreciations in Asian crisis countries were directly related to poor corporate governance, broadly supports the conclusions of the structuralist theory.
 9. For differing perspectives on the causes, consequences, and remedies of the financial crisis in East Asian countries, see three recent collections of articles published by the National Bureau of Economic Research: Feldstein [2002], Dooley and Frankel [2002], and Edwards and Frankel [2002].
 10. In Korea, this was due to its membership in the Organization for Economic Cooperation and Development (OECD). In 1991, the government dissolved its planning office. In Thailand, financial liberalization was instituted in order to bolster Thailand's claim to be the financial center of the East [Chang, 2000; Singh 1999a].
 11. As a consequence of the failure of Cancun WTO ministerial meeting, it seems that the European Community will not immediately press for the inclusion of the competition policy negotiations at the WTO. See Singh [2003c] and Hoekman and Kostecki [2001].
 12. The main references in relation to this new information include Claessens, Djankov, and Lang [2000]; Iskander and Chamlou [2000]; La Porta, Lopez-de-Silanes, and Shleifer [1999]; and Singh, Singh, and Weisse [2003].
 13. See also Johnson et al. [2000] on this point.
 14. Donaldson's [1961] classic contribution provided the empirical basis for the "pecking order" theory for large U.S. corporations. He ascribed the phenomenon essentially to the relative transactions costs of different sources of finance and to managerial control of the corporations.
 15. There is no necessary contradiction between Asian corporations generally being family controlled while raising a large portion of their resources for growth from the stock market. Family control in the case of large corporations, as indicated in the previous section, arises from the fact that, although family ownership is often much less than 50 percent, the financial institutions (which have considerable ownership and often are government owned or influenced) generally back the founding families to allow them to maintain control over the corporations. Moreover, families use various pyramiding devices, as mentioned before, to maintain and expand their control over very large corporations.
 16. For recent reviews, see Hughes [1991]; Mueller [1997]; Tichy [2001]; and Singh [2000].
 17. For a full analysis of the issues raised in this paragraph, see Singh [1997, 1998, 2000] and Singh and Weisse [1998].
 18. This section is based on Singh [2002] and Glen, Lee, and Singh [2002].
 19. An editor of this journal, however, has rightly pointed out that the incidence of small firms, including those in the informal sector, and the intensity of competition they provide, varies with industry.
 20. For a fuller discussion of these issues, see Singh [2002] and Glen, Lee, and Singh [2002].
 21. As noted in the section *Concentration of Family Control, Crony Capitalism, and Economic Crisis*, the change of the normalizing variable alters the nature of the association between crony capitalism and crisis; this association cannot therefore be regarded as being robust.
 22. For the fuller discussion of these issues, see the references provided in the section **FINANCING CORPORATE GROWTH AND CORPORATE GOVERNANCE**.

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