# Corporate governance in Greece: developments and policy implications

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## Abstract

The upgrading of the Greek capital market and the effort to join other mature capital markets has posed corporate governance reform as a first priority. In addition, the 2004 Olympic Games put the Greek market in the international spotlight and will likely invite interest from foreign investors. More than ever, an efficient corporate governance framework is condition *sine qua non* for the competitive transformation of the capital market and the business world. At the same time the European Union (EU) faces both the pressure and challenge for harmonization of the laws and regulations and convergence of corporate governance systems, especially after the entrance of the new member states. The paper has two objectives: (i) to present the main aspects of corporate governance in Greece, contributing to the relevant growing body of literature, and (ii) to place the current corporate governance developments and trends in Greece within the international debate, especially in the light of the recent debate to improve and convergence corporate governance in EU. Firstly, I review the corporate governance debate and its implication at the EU level. Secondly, I describe the corporate governance framework in Greece in the light of the recent key reforms. Finally, I summarize the overall findings and proceed with some critical points and recommendations for the potential future direction of the corporate governance agenda in Greece.

***Keywords*** *Corporate governance, rating, disclosure, ownership, Greece*

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## 1. Introduction

The upgrading of the Greek capital market to mature market status and the global competition for capital has boosted the corporate governance debate in Greece. In addition, the recent corporate failures and financial scandals around the world have increase awareness that proper corporate governance is fundamental to the efficient operation of capital markets. The Greek economy sustained its high growth rate, despite the international economic slowdown, while the Olympic Games of 2004 put the Greek market in the international spotlight and will likely invite interest from foreign investors. Market transparency and investors' confidence is perhaps the greatest corporate governance challenge facing the Greek capital market. This paper provides a comprehensive overview of corporate governance developments in Greece and has two objectives. Firstly, we indent to enrich the debate in this area and to contribute to the increasing body of literature by presenting the main aspects of the Greek corporate governance framework. Secondly, we aim to place the current corporate governance developments and trends in Greece within the international debate, especially in the light of the discussions about the coordination of the efforts taken by and within member states to improve and convergence corporate governance in EU. The structure of the paper is similar to a recent paper published *on Corporate Governance* by Melsa Ararat and Mehmet Ugur. The authors provided an overview of the Turkish corporate governance framework given the increased interest in corporate governance matter and the significance of the Turkey as an emerging market (Ararat and Ugur, 2003). In our paper the overview of the Greek corporate governance may have significant implication, such as the Greek market is a newly mature euro-area market and corporate governance is supposed to be a key factor for the competitive transformation of the capital market and the business world. In addition, the evolutionary path of corporate governance in Greece may have significant implication for the new EU member-states direction in this area.

The remainder of the paper is organized as follows. The first section briefly presents the corporate governance debate and highlights the major trends in the EU. The second section presents the main aspects of the corporate governance in Greece and focuses on the recent developments. The last section summarizes the findings and proceeds with some critical points and recommendations for the potential future direction of the corporate governance agenda in Greece.

## 2. Corporate governance: key issues and the reform agenda

***Corporate governance: definition and agency problems***

Corporate governance has been a widely discussed issue among academics, capital markets' regulators, international organizations and the business world. Shleifer and Vishny (1997), define corporate governance as the way in which the suppliers of finance to corporation assure adequate returns on their investments. Agency theory is the fundamental reference in corporate governance. The agency problems vary, depending on the ownership characteristics of each country. In countries with dispersed ownership structure (mainly the US and the UK) the separation of ownership and control, as posed by Berle and Means (1932), refers to the inherent conflicting interests of opportunistic managers and owners (Fama and Jensen, 1983). Opportunistic behavior by managers has significant economic consequences, such as it reduces the potential willingness of investors to finance the companies (Grossman and Hart, 1986; Williamson 1985). Investors usually use their exit options if they disagree with the management or if they are disappointed by the company's performance, signaling - through share prices reduction - the necessity for managers to improve firm performance (Hirschman, 1970). Hence, the corporate governance debate focuses on the responsibility and accountability of managers and the mechanisms that can assure that they run the companies in the interests of the owners (Tirole, 1999). On the other hand, in countries with concentrated ownership structure (continental Europe, Japan and other OECD countries), large dominant shareholders usually control managers and expropriate minority shareholders, in order to extract private control benefits. The agency problem of corporate governance is therefore posed as how to align the interests of strong blockholders and weak minority shareholders (Becht, 1997).

Corporate governance has significant implications for the growth prospects of an economy. Proper corporate governance practices diminish risk for investor, attract investment capitals and improve corporate performance. Especially, in an era of increasing competition and capital mobility corporate governance has become a key element affecting the industrial competitiveness of countries (Maher and Andersson, 1999). Improving corporate governance practices is particularly important for developing and emerging market economies. These markets are very vulnerable to the market fluctuations, such as the flow of international capital often represents speculative investment portfolio placements. Hence, proper corporate governance mechanisms can effect on investors' confidence and retain economic stability (The World Bank Group, 1998). Moreover, corporate governance seems to affect the exchange rate policy. Castren and Takalo (2000) suggest that a partial reform of corporate governance practices may actually render the exchange rate peg vulnerable to speculative attack. Their reasoning, persistence in emerging market countries, is that when corporate governance rules are very underdeveloped and the firms cannot rise foreign capital, shocks to the revenues do not matter much because the financial accelerator is weak. After a partial reform, the firms can obtain foreign capital, but, as a side effect, the financial accelerator is enhanced. Hence, under a currency peg, the policymaker cannot eliminate the impact of the shocks by adjusting the exchange rate. The socks are thus multiplied by the financial accelerator, increasing expectations of the currency peg collapsing and thus diluting the credibility of the peg. In addition, Johnson et al. (1999) and Mitton (1999) report how the weak corporate governance worsened the 1997 Asian currency crises.

***Corporate governance: the EU debate and transformation process***

Recent events of corporate scandals and failures, mainly in the US, have raised serious questions about the way the public corporations are governed. Corporate governance reforms have been demanded around the world, even if some countries face more serious problems than others do (Mayer, 2003). In the US, the American Congress rapidly responded, by passing the Sarbanes-Oxley Act of 2002. The New York Stock Exchange followed by adopting new rules for listed companies. These actions are supposed to be the most significant reform in the US corporate governance since the creation of the country's security regulation framework in the 1930s (Secretariat of the Economic Commission for Europe, 2003).

The EU has also set as a key priority the modernization of the company law, including corporate governance. The increasing interest to reconstruct corporate governance arises also from the aspiration to create an integrated European capital market with common rules and a high degree of transparency by 2005. Hence, there is pressure to harmonize the national regulatory frameworks and perhaps ultimately create a single European market for corporate control (ESFRC, 2002; Soderstrom et al. 2003).

The corporate governance debated poses always the dilemma of self-regulation versus mandatory rules. Although a significant degree of company law standardisation has been achieved throughout the EU in recent years, significant legal differences remain among member states. To a great extent, theses differences are the ones most deeply grounded in national attitudes and cultures, and hence, the most difficult to unify. On the other hand, voluntary corporate governance codes tend to express a relatively common view of what constitutes good corporate governance practices and how to apply them (Weil, Gotshal and Manges, 2002). However, the corporate governance structures are shaped according to the special needs and priorities of each country. These needs and priorities vary across countries. Even within a particular economy the corporate governance priorities may vary across companies, depending on size and sectoral characteristics. What constitutes a best practice for a large traditional manufacturing company may not apply for a small high tech firm. Hence, any attempt to homogenize and regulate corporate governance practices, which, by their nature, present great degree of heterogeneity across countries, activity and time, may not be the best policy (Mayer, 2003). On the contrary, the EU policy, by respecting the diversity in corporate governance among member states, should focus on the real potential sources of minority shareholders' expropriation by controlling blockholders or managers, pursuing their own interests. These potential sources of conflicting relationships are largely associated with the information disclosure regime, the transparency and the auditing practices in place. Investors need regular, timely and accurate information in order to make decisions and to efficiently exercise their voting rights. High quality audit standards and independence are prerequisites for reliable examination of the company's performance. However, disclosure and auditing practices cannot be sufficiently addressed by self-regulation alone and regulatory actions should be taken. Whether regulatory actions should be taken at EU level (through European rules or Directives) or at national level is a matter of discussion.

The European Commission (EC) on May 2003 presented an action plan on corporate governance. The action plan closely follows the recommendations of the "High Level Group of Company Law Experts" chaired by Jaap Winter. The experts' Group appointed by the EC in order to make recommendations on a modern regulatory framework in the EU for company law. The Group addressed a number of issues related to corporate governance and proceeded with a set of recommendations to the EC (Winter Report, 2002). Some of the recommendations are suggested to formulate a European framework rule or a Directive. Other recommendations, according to the Group, should be a member state decision. The proposed rules provide the potential future direction of the corporate governance framework in the EU with significant implication to the listed companies in each member state.

Especially, the Group suggests that:

(i) Listed companies should be required to include in their annual report and accounts and in their website a corporate governance statement.

(ii) The rights and obligations of accountholders and securities intermediaries in the securities holding systems in member states be regulated at EU level, to ensure that accountholders across the EU can effectively exercise the voting rights on shares they hold through these systems

(iii) The shareholders' right to vote and their standard right to information to be supplemented by a European framework rule on the right of shareholders to require a special investigation and the procedure for it. T

(iv) The EC should issue a Recommendation to member states that they have effective rules in their company laws or in their national corporate governance codes, ensuring that the nomination and remuneration of directors and the audit of the accounting of the company's performance is decided upon by non-executive or supervisory directors who are at least in the majority independent.

(v) The EC should issue a Recommendation to member states for what is considered to be independent[1]. The EC should also include provisions on the role and responsibilities of audit committees in its Recommendation on the role of non-executive and supervisory directors.

(vi) The EC should adopt a Recommendation defining an appropriate regulatory regime for directors' remuneration in listed companies. It also recommends that the principle of accounting for the cost of share incentive schemes be recognised in a European framework rule.

(vii) The collective responsibility of the board for financial and key non-financial statements should be confirmed as a matter of EU law.

(viii) The EC should review whether director's disqualification can be imposed as a sanction across the EU, at least for misleading financial and key non-financial disclosures, or more generally for misconduct by directors.

The Group also recommends the introduction of a European framework rule on wrongful trading, which would hold company directors (including "shadow" directors) accountable for letting the company continue to do business when it should be foreseen that it will not be able to pay its debts. A European wrongful trading rule would enhance, according to the Group, creditors' confidence and their willingness to do business with companies. Finally, a wrongful trading rule would introduce an equivalent level of protection for creditors of companies across the EU, without any need to harmonise the whole body of directors' liability rules in all member states.

The above recommendations can be seen as an effort to design a sufficient and flexible corporate governance framework in the EU. The mandatory recommendations refer to areas where self-regulation has proven insufficient (disclosure of information, transparency and auditing). On the other hand, the necessary flexibility, regarding for example board structure matters, is recognized. It is worth to mention that the Winter Report (2002) clearly states that the adoption of an EU corporate governance code would not achieve full information for investors and it would not contribute significantly to the improvement of corporate governance in Europe. There is of course an active role for the EU to play in corporate governance, especially in coordinating the efforts of member states in order to facilitate convergence. Although,

[1] The Group itself recommends a minimum list of what makes a non-executive director not to be independent (former and current employees and advisors of the company, those who receive performance related pay by the company, those who have interlocking relationships, and controlling shareholders. Related parties and family relationships should be also taken into account).

member states should be required to participate in the co-ordination process, the Group suggests that the results should be non-binding.

## 3. The corporate governance framework in Greece

Corporate governance failures have been identified as one of the key reasons of the Greek capital market's underperformance during the last three years. Specific corporate abuses reduced investors' confidence in corporations, such as they had (the investors) flocked to the stock market during the last years. Investor protection reform and measures to enhance market's transparency were introduced as key-elements in order to restore public trust. Moreover, there developed a hot discussion on the amendment of corporate law, characterized by the controversy between the representatives of the Federation of Greek Industries (FGI) and the State. The FGI opposed most of the proposed amendments and stated that corporate governance has to be adopted on a voluntary basis. A new law was finally released in May 2002 and laid down fundamental corporate governance obligations. The legislative framework of the Greek capital market is now fully harmonised with the guidelines and directives of the EU. Although improvements in corporate governance have occurred in Greece, they are confined to an elite of large listed companies that are more in tune with the international corporate stage.

La Porta et al. (1999) underline and analyze the importance of a legal approach to corporate governance. They state that when outside investor's (minority shareholders) rights are protected through the enforcement of regulations and laws (e.g. disclosure and accounting standards, the rights to vote for directors and to call extraordinary shareholders' meetings) the investors are willing to finance firms, encouraging the development of equity markets. Even if there are significant variations in law and regulations between countries, it is empirically documented that strong investor protection is associated with effective corporate governance (La Porta et al., 1998, 1999). In this way, investor protection affects the real economy, accelerating economic growth[2].

La Porta et al. (1998) classified countries into legal families and examined whether laws pertaining to investor protection differ across countries and whether these differences have consequences for corporate governance, by constructing different indices. An index that aggregates the shareholders' rights is formed by adding six different variables (proxy voting by mail, shares not blocked before meeting, cumulating voting or proportional representation of minorities in the board of directors, oppressed minorities mechanisms, preemptive rights and percentage of share capital to call an extraordinary shareholders' meeting not above 10%). The judicial system efficiency index provides an assessment of the "efficiency and integrity of the legal environment as it affects business, particularly foreign firms" and it "may be taken to represent investors' assessments of conditions in the country in question". The rule of law index assesses the law and order tradition in the country. The accounting standards index is created by rating companies' annual report on their inclusion or omission of 90 items, which fall into seven categories (general information, income statement, balance sheets, fund flow statements, accounting standards, stock data and special items). La Porta et al. scored a total of 49 countries

[2] The linkage between financial development and economic growth has been well documented by Rajan and Zingales (1998), Carlin and Mayer (1999) and Beck et al. (1999). The latter find that financial development can enhance savings, increase real investments and improve resource allocation.

classified into four legal families (English common law, French civil law, German civil law and Scandinavian civil law).

Greece, a French origin company law country, is rated 2 out of 6 for the shareholders' rights, which is lower compared both with the French family and the total sample average (Greece is rated better than Belgium, Italy, Germany, but worse than France, Spain, Portugal and others). Greece is also rated 7 out of 10 and 6.18 out of 10 for the efficiency of the judicial system and the rule of law respectively. In both indices Greece is scored better than the average French legal family, but worse than the total sample average. Finally, the accounting standards score of 55 out of 90 in Greece outperforms the French family and underperforms the total sample average. These evidences suggest that French civil law countries, including Greece, afford low legal protection to shareholders, especially regarding voting by mail and laws protecting oppressed minorities. The results also suggest that Greece be placed close to the world average regarding the quality of law enforcement and accounting standards. Its worth mentioning that Greece is rated worse than all the EU member states with respect to the rule of law and accounting standards (excluding Portugal). However, after 1996 large reforms took place. Anew regulations have been recently introduced to restore pubic confidence, to protect (minority) shareholders rights and to improve corporate governance mechanisms. Certain rules and laws mandate a number of corporate governance standards for the listed companies in Greece (e.g. independent internal controls over financial reporting, timely and reliable information and disclosure for important corporate events, non-executive and independent directors to the boards, new framework for takeover bids, high administrative sanctions and fines in case of non-compliance).

In parallel with the regulatory actions, corporate governance has been largely debated among academics and the business world, resulting on many voluntary activities. The Committee on Corporate Governance in Greece (under the coordination of the Hellenic Capital Market Commission) and the Federation of Greek Industries have developed voluntary corporate governance codes. Moreover, the University of Athens has recently established a rating system for the listed companies in Greece based solely on corporate governance criteria. Finally, the Athens Stock Exchange announced in July 2002 the voluntary qualitative criteria covering corporate governance, transparency and communication with investors.

**Table 1**
**Law and the quality of its enforcement**
***(Average ratings)***

| | **Shareholders' rights (0-6)** | **Efficiency of the judicial system (0-10)** | **Rule of law (0-10)** | **Accounting standards (0-90)** |
|---|---|---|---|---|
| Greece | 2.00 | 7.00 | 6.18 | 55.00 |
| French origin | 2.33 | 6.56 | 6.05 | 51.17 |
| English origin | 4.00 | 8.15 | 6.46 | 69.62 |
| German origin | 2.33 | 8.54 | 8.68 | 62.67 |
| Scandinavian origin | 3.00 | 10.00 | 10.00 | 74.00 |
| World | 3.00 | 7.67 | 6.85 | 60.93 |

*Source: La Porta et al. (1998)*
**Higher score indicates better rating.*

***Legal system overview***

The Greek companies are governed by Law 2190/1920. In addition, listed companies are governed by Law 3016/2002. The general meeting of shareholders is the main decision-making organ of the company and has exclusive competence in key areas (e.g. to make amendments to the company's articles of association, to elect board members, to appoint statutory auditors and to approve the annual accounts and dividends). Shareholders exercise their rights through the shareholder meeting, which must be called at least once a year. The shareholders' right of vote in the general meeting corresponds to the shares they possess. There are two forms of shares, bearer and registered. In principle all shares are equal, with an exception to the preference shares, which give some exceptional rights to their owners. These exceptional rights include preferential payment of the first dividend, preferential repayment of the contribution in the case of liquidation and the right to collect a cumulative dividend for financial years during which no dividend was declared.

One-tier board predominantly governs the listed companies in Greece, where shareholders directly elect the directors through the shareholder general meeting. The board, by law, combines supervisory and management functions, but generally delegate day-to-day management to hired executive managers. Although, under the law, the board has significant discretionary power, a company's bylaws may impose stricter limits and guidelines. The board must be made up of at least three members and is required to meet at least once a month. For the listed companies, at least 1/3 of the total directors must be non-executive, of which at least two must be independent[3]. The liability of the managing director (equivalent to a Chief Executive Officer) is much stricter than that of other senior managers of board members.

The remuneration and other compensation of non-executive board members are determined according to Law 2190/1920 and are proportional to the time they devote to the board meetings and the fulfilment of the responsibilities delegated to them according to this Law. The total of the remuneration and other compensation of non-executive board members should be reported in the annex of the annual financial statements.

It is also worth to mention the special characteristics of the state-owned companies. Until 1996, the stated-owned companies in Greece were operated under a totally protective regime. The government was appointing the board of directors and the top management. The main corporate goal departed largely from profit maximisation. Low profits, losses, underinvestment and low product quality were the case in most Greek stated-owned corporations. Although a new law was enacted in 1996, mandating state-owned corporations to operate like other private companies, there are many problems to be solved. CEO and board members' selection is still not independent from political interventions and preferences, especially for listed companies where the dispersion of ownership is very low and the state is the dominant shareholder. Contemporary corporate governance mechanisms have not been introduced yet (e.g. board committees, competent directors, performance-based compensation scheme) reducing international investment attractiveness.

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[3] During their tenure, the independent non-executive board members are not allowed to own more than 0.5% of the company's share capital and to have a relation of dependence with the corporation or persons associated with it.

The Ministry of National Economy has the responsibility to monitor and analyze the developments in the domestic and foreign capital markets, the processing and formation of proposals of government policy on capital markets issues, the harmonization of legislation with European Law and supervision of observance of the law by all agencies of the capital market and the Stock Exchange.

The Hellenic Capital Market Commission (HCMC) is the main independent regulatory decision-making body, operating under the supervision of the Ministry of National Economy. The HCMC issues statutory rules and regulations aiming at investors protection, the safeguarding of capital market's normal operation, the improvement of market transparency, the enhancement of efficiency of the trading, clearing and settlement systems and the efficient operation of capital market agencies and institutions. The capital market entities supervised by the HCMC are the brokerage firms, the investment firms, the mutual fund management firms, the portfolio investment companies and the firms for the reception and transmission of stock exchange orders with respect to compliance with the code of conduct. Entities and organizations such as the Athens Stock Exchange, the Athens Derivatives Exchange, the Athens Derivatives Transactions Clearing House and the Central Depository of Securities are also subject to supervision by the HCMC. A central means for exercising prudential supervision of capital market entities by the HCMC is the license authorization function and the imposition of fit and proper European Union (EU) standards for the granting of license. In order to ensure the smooth function of the capital market, the HCMC introduces rules and regulations and supervises compliance with them, aiming at safeguarding the normal and smooth operation of market systems and the establishment of appropriate transparency standards (disclosure of information on financial performance, market transactions, ownership, structural changes, notification of corporate actions etc.). An essential means for the establishment of the smooth operation of the capital markets, based on European standards and practices, is the introduction of statutory codes of conduct. The HCMC has enacted four codes of conduct of business, whose statues are compulsory for relevant regulated entities. The codes regulate the conduct of business of (a) brokerage firms and investment services companies, (b) mutual fund management companies and portfolio investment companies, (c) underwriters and underwriting services and (d) companies listed on the Athens Stock Exchange. In addition, the HCMC has enacted a take-over code regulating tender offers in the capital market. The enactment of codes of conduct of business for investment service providers is a result of the incorporation of the European Union Investment Services Directive (ISD) into Greek law.

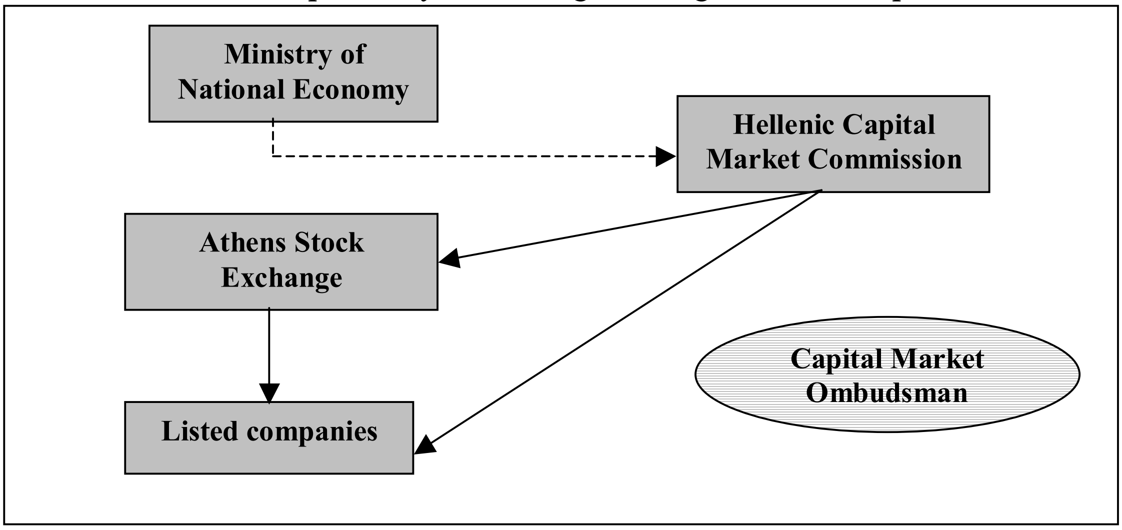
The responsibility for the monitoring of compliance with the codes of conduct rests with the HCMC. The HCMC is endowed with the authority to impose administrative sanctions (suspension and revocation of license, trading halts, imposition of fines) on all supervised legal and physical entities that violate capital market law and the rules. It is also endowed with the authority to submit indictments to prosecution authorities when punishable financial law violations are detected.

Investor service was decisively enhanced by the creation of a new market institution: the Capital Market Ombudsman. All market agents are responsible for the operation of this institution, which is expected to provide a major assistance to the settlement of disputes between financial intermediation firms and their clients on the basis of consent. The main objective of the new institution is the friendly settlement and mutual resolution of disputes occurring between individual investor-clients and market intermediaries that fall into the Ombudsman's jurisdiction, in a just and unbiased manner and through transparent and concise procedures.

The Athens Stock Exchange (ASE) was founded in 1876 as a regulatory independent government agency. The procedure of its privatization started in 1997 and continued through 1998. In the end of 1998, the Greek Government, being the major shareholder of the ASE, declared that it consents to the listing of its shares to the ASE's Main Market, under any form. Currently, 5 different markets operate under the ASE: (a) Main Market, (b) Parallel Market, (c) New Market, (d) Greek Market of Emerging Capital Markets, and (e) Secondary Listings on ASE from Stock Exchanges outside Greece. For the issuing company to be listed on the Main Market, it should employ own funds amounting to at least €11,738,811.45, while for the Parallel Market, the company should employ own funds amounting to at least €2,934,702.86.

The fundamental supervisory relations governing the Greek capital market are illustrated below:

Figure 1
The fundamental supervisory relations governing the Greek capital market




***The developments of the capital market***
The Greek capital market has been transformed largely during the last four years. New markets were established and the HCMC completed a wide range of institutional changes. HCMC's regulatory activities were mainly directed at the protection of investors, the enhancement of market transparency, the protection of the systems of trading and clearing, the enactment of codes of conduct and the assurance of the smooth function of the capital market.

However, the Greek capital market has been experiencing a cycle of self-fulfilling expectations during the second and third quarters of 1999. At the end of the year 1999 the ASE General Index realized a total annual increase of 102.2%. Due to the rise of share prices of listed companies the total ASE capitalization recorded an annual increase of 194.7% (from €67,024.8 millions in 1998 to €197,537 millions in 1999), among the highest in the OECD countries. The total value of transactions increased from €41,708.1 millions in 1998 to €173,027 millions in 1999, realizing an increase of 194.7%. An increasing number of companies raised funds through the capital market. The total funds raised through initial public offerings (IPO's) amounted to €1,842.3 millions in 1999 against €1,157.2 millions in 1998 and €59.0 millions in 1997, corresponding to an increase of 59.2% and 3,022.5% respectively. Listed companies raised €8,128.0 millions in 1999, an amount that was 472.9% higher than in the previous year (see table 2).

The massive entrance of individual and institutional investors in the capital market, mostly through placements on small-and-medium-capitalization stocks, increased rapidly both stock prices and liquidity in the second and third quarters of 1999. Prosperity and wealth appeared to be created. This prosperity and wealth led investors (demand side) to buy more creating further rises in stock prices. While the standard theory of stock valuation suggests that a stock should sell for the discounted present value of the stream of future returns, stock prices appreciation was both unjustifiable and unsustainable. Investors proceeded to short-term speculative placements and in a state of euphoria were betted, in full certainty that stock prices will increase further. The cycle of self-fulfilling expectations resulted on a significant divergence between actual prices and prices justified by corporate fundamentals (equilibrium prices). However, the manic phase always has an end. A virtuous circle spirals upward until there remain no people coming in to buy stocks at ever-higher prices. A phase of self-feeding panic occurs, characterized by extensive liquidation of securities. The Greek capital market's severe underperformance in 2000, 2001 and 2002 has been largely resulted on the previous speculative process. The ASE General Index realized an annual decrease of 38.8% in 2000, 23.5% in 2001 and 32.5% in 2002. Both the total value of transactions and the ASE capitalization decreased. In 2002, the total values of transaction in the ASE decreased by 38.9% and 85.7% in relation to 2001 and 1999 respectively. Total market capitalization during 2002 amounted to €65,759.7 millions showing a decrease of 47.4% and 66.7% in relation to 2001 and 1999 respectively.

Throughout history, many speculative bubbles have been evidenced[4]. However, what make the bubble more complicated are its social impacts. The group, not the individual, gives birth to a speculative bubble, making the task of improving judgment and confidence more difficult. The speculative events in the Greek capital market during 1999 led the HCMC and the state to take an active role, introducing rules, regulations and codes of conduct. All these measures were aiming at the protection of investors against market abuse, the improvement of the transparency of the market and the establishment of appropriate business ethics.

**Table 2**

[4] The first speculative bubble took place in Holland from 1620 to 1637 and involved rare and collectible tulips. Since then, it is well known the speculative short life of the South Sea Company in England (1711-1720), the Florida real estate craze (1924-1926), the speculative bubble during 1926-1929 in the US stocks, the "tronics" stocks (1962) and the crash of 1987 (Galbraith, 1993).

**The growth of the capital market in Greece, 1997 - 2002**
***(Amounts in millions of Euros)***

| Year | Value of transactions | | Market capitalization | | | Fund raised through IPO's | | ASE General Index, % change |
|---|---|---|---|---|---|---|---|---|
| | *Amount* | *% change* | *Amount* | *% change* | *% of GDP* | *Amount* | *% change* | |
| 1997 | 17,081.4 | - | 28,793.3 | - | 29.6 | 59.0 | - | 58.5 |
| 1998 | 41,708.1 | 144.2 | 67,024.8 | 132.8 | 63.6 | 1,157.2 | 1,861.4 | 85.1 |
| 1999 | 173,027.0 | 314.9 | 197,537.0 | 194.7 | 169.4 | 1,840.0 | 59.0 | 102.2 |
| 2000 | 101,675.7 | -41.2 | 117,956.3 | -40.3 | 95.5 | 2,557.8 | 39.01 | -38.8 |
| 2001 | 40,529.8 | -60.1 | 96,949.5 | -17.8 | 74.1 | 1,075.6 | -137.8 | -23.5 |
| 2002 | 24,771.0 | -38.9 | 65,759.7 | -47.4 | 46.9 | 92.5 | -1,062.8 | -32.5 |

*Source: Athens Stock Exchange, Hellenic Capital Market Commission*

***Disclosure and transparency***

Timely and accurate disclosure of information is fundamental for sound corporate governance system, because it enables transparency and accountability. Commitment by a firm to increased levels of disclosure should lower the firm's cost of capital (Leuz and Verrecchia, 2000). Efficient disclosure levels attract investors who want to know where to put their investment and retain market confidence (OECD, 1999). In most developed countries, disclosure requirements exist for the listed companies, on an annual basis, at a minimum.

The disclosure framework in Greece is quite strong and in line with the EU trends. A major contribution during 2000 to the enhancement of transparency and disclosure regarding the behavior of listed companies in the Greek capital market has been the enactment of HCMC rule: "A code of conduct for companies listed in the Athens Stock Exchange and their affiliated persons" (HCMC Rule 5/204/2000). The code sets behavior standards for ASE listed companies and specifies duties and obligations of companies' major shareholders, the members of the board of directors, the executive management or other individuals or legal entities relating to them. In general, according to the code, each company shall ensure the prompt disclosure of information or fact occurring in its domain of activity, which are not accessible by the public and which may cause significant fluctuation in the price of its shares. Furthermore, the code specifies the organisation, structures and internal operation mechanisms necessary for best serving shareholders' interests and investor interests in general. The aim is to eliminate uncertainty in the market on corporate affairs and avoid speculation by company insider or other persons that may have inside information.

An important element to the financial disclosure is the requirement for the listed companies to publish an annual report and a cash flow statement. The cash flow statement is structured along international accounting standards and constitutes the first step of implementing International Accounting Standards (IAS) in Greece (Hellenic Capital Market Commission, 2000). Audits regarding the disclosure of additional information in the financial statements published by listed companies continued, with the aim of providing investors with complete information concerning the use of the funds raised. There were also further audits regarding the disclosure of additional

The existence and operation of an audit department is a prerequisite for the approval of initial public offering of company shares or other securities. Auditing is performed by the appropriate department. Auditors are obligated to be independent in performing their responsibilities, do not report to any other company department and be supervised by one to three (1-3) non-executive board members.

In addition, investment firms are now most strictly obliged to prepare semi-annual and annual financial statements, audited by certified auditors, which will be submitted to the HCMC within two months from the end of the semester and the calendar year. There was also an amendment of the value of transactions announced by brokerage firms, regarding shares of companies under probation.

***Ownership structure and control***

In Greek listed companies ownership, like in other European countries, is concentrated. Large families usually control most of the companies and members of the controlling families are usually serving as the top manager. In addition, the state controls large percentages of votes in a significant number of listed companies. Large capitalization firms display a more dispersed ownership and control structure than medium and small capitalization firms. Therefore, the agency problem arises as a conflict between "strong blockholders and weak minority owners", rather than between "strong managers and weak owners".

**Table 3**
**Ownership dispersion of the ASE listed companies**

| | ASE Main Market | ASE Parallel Market | New Market | Total Market | FTSE-20 companies | FTSE-40 companies |
|---|---|---|---|---|---|---|
| Ownership dispersion | 48.74% | 30.42% | 25.05% | 47.22% | 54.04% | 44.40% |
| Number of major shareholders* | 653 | 317 | 4 | 974 | 52 | 101 |
| Capitalization (mil of €) | 91,500 | 8,204 | 46 | 99,750 | 55,411 | 15,630 |

*Source: Hellenic Capital Market Commission, Research Division (2001)* www.hcmc.gr
** Shareholders owning a stake of at least 5% of the company's share capital*

According to the HCMC (2001), in 370 listed companies in Greece average ownership dispersion was 47.22% when the major shareholder is defined as the shareholder owning at least 5%. In total, according to the study, the 370 listed companies were held by 974 major shareholders, while the major shareholders per listed company were around 3. The results indicate that competition for control at the company level is quite little. However, the large capitalization companies (FTSE-20) presented a higher degree of dispersion of ownership than the middle capitalization companies (FTSE-40). In the former, ownership dispersion was 54.04% (52 major shareholders), in the latter 44.4% (101 major shareholders).

The rules specify transactions pre-announcement obligation, securing a transparent ownership structure. Especially, company shareholders, owing at least 10% of any class of shares, who intend to purchase, within the next three months or less, shares of the same class corresponding to at least 5% of the company's share capital, or intend to transfer shares of the same class corresponding to at least 5%of the company's share capital, shall disclose the whole transaction. Shareholders have to disclose the intended volume and the time period of the transaction, as well as the Investment Company through which the transaction is to be executed and the underwriters of the relevant notice.

The high degree of ownership concentration is consistent with the results in most other continental Europe countries. In Italy, Bianchi et al. (1997) showed that the largest shareholder in listed companies held on average 48% of total voting rights, while the largest three shareholders held 62%. Bloch and Kremp (1997) reported a significant degree of concentration of ownership (56%) for listed firms in France. A recent study by Facio and Lang (2001), in a sample of 3,740 companies in five Western European countries (France, Spain, Italy and UK) documented a small degree of ownership dispersion (38.3% of companies are widely held). They also reported significant ownership concentration within a small number of families (families control 43.9% of Western European companies). Large shareholders may act as an effective monitoring mechanism of management and, thereby, enhances firm performance. However, controlling blockholders can use their power to extract own private benefits, at the expense of minority shareholders. This kind of expropriation leads to sub-optimal levels of investment by minority. Thus, in countries where corporate governance framework is weak and legal system is unable to block such expropriation, policies aimed at protection of minority shareholders may be particularly needed (Maher and Andersson, 1999).

***Corporate governance actions: voluntary codes***

A number of financial scandals and corporate failures in the 1980s in the US and the UK boosted the debate on how best to make managers accountable to shareholders. Corporate collapses such as Maxwell, BCCI and Barings, and vast executive compensation increases resulted on a variety of domestic and international initiatives to restore public confidence. These initiatives consisted of a set of voluntary principles and regulations on corporate governance. Increasing attention in corporate governance is also associated by the common belief that a sound corporate governance regime enhances market liquidity and efficiency. Institutional investors according to the investor opinion survey released by McKinsey & Company are prepared to pay a premium for companies exhibiting high governance standards (McKinsey & Company, 2002). Premiums averaged 12-14% in North America and Western Europe, 20-25% in Asia and Latin America, and over 30% in Eastern Europe and Africa. More than 60% of investors state that governance consideration might lead them to avoid individual companies with poor governance.

The publication of the Cadbury Report in 1992 introduced several new corporate governance guidelines, while the initial impetus was given by the Principles and Recommendations of the American Law Institute (1984) and the Treadway Commission (1987) in the US. Moreover, supranational authorities, like the OECD and the World Bank, developed a set of voluntary principles and recommendations driving the attention for a minimum respect of basic corporate governance rules worldwide. These developments encouraged other countries to look into the necessity of establishing relevant voluntary corporate governance codes. In the European Union a total number of 35 corporate governance codes have been developed from a variety of entities, ranging from government authorities and stock exchange-related committees, to business, investor and academic associations (Weil, Gotshal and Manges, 2002). Different priorities and needs are reflected in the countries' codes. Although national corporate governance codes reflect different cultural, legal and economic patterns and frameworks, they also share significant similarities. The convergence of corporate governance codes is best described by the OECD Principles of Corporate Governance (1999), which are intended to sufficiently apply to whatever national legal regime.

Throughout the last five years, many countries established various regulations and started to review their company law. Discussions focus on how to protect minority shareholders, enhance transparency and disclosure of information, improve board functions and structures, limit the rule of anti-take-over devices, and improve auditing process. In many cases, the new regulations and laws are based on the previously developed voluntary corporate governance codes.

In April 1999 the HCMC, expressing its interest in the establishment of efficient corporate governance practices created the Committee on Corporate Governance (CCG) in Greece. The CCG introduced in October 1999 a White Paper, titled: "Principles of Corporate Governance in Greece: Recommendations for its Competitive Transformation". The voluntary corporate governance code was developed in collaboration with all relevant agents in the Greek economy and was made on the basis of internationally accepted corporate governance practices. The principles and best practice rules incorporated were closely modeled according to OECD Principles on Corporate Governance (OECD, 1999).

The Greek code contains 44 recommendations compiled on seven main categories:

- The rights and obligations of shareholders

The CCG encourages shareholders, and particularly institutional investors to use their voting rights in a manner that promotes the efficiency of the corporation and the market and do not oppose to the interests of small private investors. It also discourages multiple voting procedures and the issuance of non-voting privileged shares.

- The equitable treatment of shareholders

The CCG states that all shareholders of the same class should be treated equally and that actions and transactions based on insider information or undertaken for private benefit should be prohibited.

- The role of stakeholders in corporate governance

According to the code, the corporate governance framework should recognise the rights of stakeholders in the corporation, as established by law, and encourage active participation between corporations and stakeholders in creating wealth, jobs and the sustainability of financially sound enterprises.

- Transparency, disclosure of information and auditing

The CCG principles recommend that the corporate governance framework should ensure the full, timely and detailed disclosure of information on all material matters, including its financial situation, performance, ownership structure and governance of the corporation. The code also recommends the establishment of an Internal Audit Committee consisting solely of non-executive directors.

- The board of directors

A maximum board size of 13, with a majority of non-executive directors is recommended, as well as, the separation of the CEO and board chair. The code also recommends the establishment of procedures allowing the board of directors to obtain external advice.

- The non-executive members of the board of directors

The code sets the criteria that every director should meet in order to be considered as an independent. It also recommends that the compensation of non-executive directors should be comparable to the time they devote for board meetings and decision-making and that should not be tied to the corporation's performance. Total compensation of non-executive directors should also be reported separately and with the required justification in the corporation's annual report.

- Executive management

The code recommends performance-based compensation for executives, proposes the establishment of a compensation committee consisting of a majority of non-executive directors to review management compensation, and recommends the appointment of the Chief Financial Officer (CFO) in the top management team.

In August 2001 the Federation of Greek Industries (FGI) introduced the Principles of Corporate Governance for all companies, but especially for the companies listed on the Athens Stock Exchange. Compliance with the Principles is voluntary. The main recommendations include:

- The establishment of board level committees consisting of a majority of non-executive directors.
- The implementation of internal control by a specific department or individual

The FGI Principles do not address the issue of equal/fair treatment of shareholders and the rights of stakeholders. They do not also contain any provisions dealing specifically with the protection of shareholders' rights, the ratio of non-executive directors, the compensation of non-executive directors and the separation between the CEO and the board chair.

***Corporate governance rating and evaluation***

In a period of volatile and uncertain markets, as shown by the recent corporate failures and poor governance structures, demanding institutional investors seek to place their funds in well-governed companies. Mainstream investors tend to examine and include in their overall investment strategy whether companies comply with specific internationally accepted corporate governance standards. At the same time, as more investors evaluate corporate governance when purchasing stocks and mutual funds, an increasing number of listed companies feel the pressure to take actions in order to adopt efficient corporate governance policies and practices. As a response to the increase in demand for corporate governance evaluations, some investment research firms and academic institutions are now developing corporate governance rating services. A corporate governance score is derived mainly by analyzing to what extent a company adopts codes and guidelines of generally accepted corporate governance best practices, and the extent to which local laws, regulations, and market conditions encourage or discourage corporate governance practices (Xanthakis, Tsipouri and Spanos, 2003).

A quite limited number of studies use a corporate governance index in order to investigate whether within-country variation in corporate governance affects firms' market value. Black (2001) examined the relationship between corporate governance behavior and market value for a sample of 21 Russian firms by using corporate governance rankings developed by the Brunswick Warburg investment bank. The author reported a powerful correlation between the market value and corporate governance of Russian firms. Durnev and Kim (2003) found that higher scores on both the CLSA corporate governance index and the S&P disclosure and transparency index predict higher firm value for a sample of 859 large firms in 27 countries. Gompers, Ishii and Metric (2001) showed the existence of a striking relationship between corporate governance and stock returns. The authors used the incidence of 24 different provisions (primarily takeover deafness) to build a "Governance Index" and then they studied the relationship between this index and firm performance. The "Governance Index" is highly correlated with firm value. Klapper and Love (2002) used data on firm-level corporate governance rankings across 14 emerging markets and found a wide variation in firm-level governance across countries. Black, Jang and Kim (2003) constructed a multifactor corporate governance index based primarily on responses to a survey of all listed companies by the Korea Stock Exchange. They found a strong positive correlation between the overall corporate governance index and firm market value, which is robust across OLS, 2SLS and 3SLS regressions, in subsamples, in alternate specifications of the corporate governance index, and with alternate measures of firm value.

The University of Athens (2002) developed a corporate governance rating system for the listed companies in Greece. The listed companies' corporate governance practices were assessed for the year 2001 through five main corporate governance indicators:

- The rights and obligations of shareholders (includes criteria concerning the respect of the one-share one-vote principle, anti-takeover devices, voting right restrictions, voting issues, shareholder proposals and voting procedures).

- Transparency, disclosure of information and auditing (examines the quantity and quality of the disclosed information, such as the accounting standards, relationship between external and internal auditors, information on major shareholders of the company, etc.).

- The board of directors (examines all issues relating to the governance of a board, such as independent directors, division between the role of chairman and chief executive, succession planning, election of the board, director remuneration, the workings and authorities of board committees, etc.).

- Executive management (analyses matters concerning the duties and responsibilities of the CEO and the executive management, executive remuneration, etc.).

- Corporate governance commitment, the role of stakeholders and corporate social responsibility (includes criteria such as the presence of company-owned specific corporate governance guidelines, awareness on social responsibility, philanthropy, etc.).

The five main indicators were composed of a total of 37 of partial indicators. The final outcome was based on the answers, through face-to-face interviews, of 120 listed companies which together represented more than 85% of the capitalization of the market. The listed companies, on average, were scored with 70.4 points out of 100. The score indicated a relevantly satisfactory compliance level with the principles of corporate governance. The first two indicators (the rights and obligations of shareholder and transparency, disclosure of information and auditing) received the highest rating, while the last (corporate governance commitment, the role of stakeholders and corporate social responsibility) the lower. These results are justified, such as the regulatory framework is quite strong regarding disclosure and investors' protection, while companies' awareness on corporate governance commitment and social responsibility is limited (e.g. there are less than 5 listed companies that have already issued their own corporate governance guidelines). The bigger the company, the grater its effort to be in line with best corporate governance practice. However, the sample did not include the majority of small capitalization firms, which are expected to have very low degree of compliance. The adoption of an active policy of compliance to the international "good practices" had started by certain large listed companies in Greece, but sooner or later all should realize this. Even if some individual points are a little premature for the Greek capital market or they present differences from the traditional models of administration, the foreign investors, as well as an increasing number of Greek institutional investors will consider them as being necessary. Therefore, the companies with a low degree of compliance are at risk to have a reduced demand for their shares, despite their profitability.

The Athens Stock Exchange has also recently established an evaluation process for the listed companies in Greece, based on qualitative criteria covering corporate governance, transparency and communication with investors. Such qualitative criteria have been developed following a study by the R&D department of the Athens Stock Exchange and were finalized in consultation with listed companies and the associations that represent them. Application of these criteria is optional and they are additional to the requirements that listed companies are under an obligation to fulfill, according to the legislation currently in force. The criteria are as follows:

- Establishment and content of corporate website covering the four subject areas: company organization, corporate profile, and financial and stock market data.
- Organization, by an Investor Relations Unit, of road shows and additional activities.
- Features of corporate governance
- Free float ratio (25% for the Main Market and 20% for the Parallel Market).

Each of the above four groups of criteria, covered by a relevant questionnaire, represent recommendations that contribute mainly to listed companies' more effective communication with investors. The adoption of the criteria is at the discretion of the listed companies (without prejudice to the existing legal requirements relating to corporate governance). As of March 2003 a total of 33 listed companies, of which around 50% represent high capitalization companies, have adopted the ASE qualitative criteria.

The above evaluation and rating efforts indicate that corporate governance reform has been posted as a top priority in many large listed companies. However, the majority of medium and small capitalization companies has adopted the minimum mandatory requirements and lack further efficient corporate governance mechanisms. Such as the competition for capital is increasing the listed companies have to realize that proper corporate governance is a prerequisite.

**Table 4**
**The evolution of corporate governance in Greece**

| Date | Corporate governance activity |
|---|---|
| 1998 | The Athens Stock Exchange conducts a study on corporate governance |
| 1999, April | OECD Principles on Corporate Governance |
| 1999, October | Corporate governance code (voluntary) by the Committee on Corporate Governance in Greece (under the coordination of the Capital Market Commission) |
| 2000 | The Ministries of National Economy and Development set up a law making committee on corporate governance (Rokkas Committee) |
| 2000, July | Capital Market Commission rule: "Tender offers in the capital market for the acquisition of securities (CMC Rule 1/195/2000) |
| 2000, November | Capital Market Commission rule: "A code of conduct for companies listed in the Athens Stock Exchange and their affiliated persons" (CMC Rule 5/204/2000). |
| 2001, August | Principles of Corporate Governance by the Federation of Greek Industries |
| 2002, March | A corporate governance rating system is presented by the Center of Financial Studies of the University of Athens (a project funded by the Athens Stock Exchange) |
| 2002, May | Law 3016/2002: "On corporate governance, board remuneration and other issues" |
| 2002, July | The Athens Stock Exchange establishes qualitative criteria covering corporate governance, transparency and communication with investors |

## 4. Conclusions, discussion and policy implications

The Greek capital market has been experiencing a large development during the last years. However, the development path was quite volatile. After the cycle of self-fulfilling expectations during the second and third quarters of 1999 and the severe underperformance in the following years, the investors' confidence have been reduced. Listed companies alone were unable to restore public confidence. In this framework, voluntary and regulatory initiatives were proposed or adopted in response to external and internal forces, in order to restore public confidence. The main regulatory actions addressed issues like corporate transparency, disclosure of information and independent auditing. In this way, it is hoped that the Greek capital market will be an attractive investment option where the (minority) shareholder rights are sufficiently protected and exercised.

However, the majority of the listed companies in Greece lack sufficient corporate governance mechanisms. The ownership concentration of the listed companies is still high, resulting on strong ties between the main shareholder and the management team. Internationally recognised board structures, such as board committees, directors' independence and qualifications, and directors' education, have not been adequate established. In this way, the board is mostly acting as a passive organ in the company where follows the decisions of the management. Non-executive board members, rather than act as shareholders' agents, do not efficiently supervise the management. Even the rules mandate specific requirements regarding board independence, its difficult in practice to identify whether the board meets these rules. The existence of efficient board structure and procedures is mostly a matter of self-regulation. Listed companies have to realise that a well-functioned board is a comparative advantage in a competitive business world. It is recommended that an increasing number of listed companies have to re-examine its corporate governance policy and to adopt contemporary standards. The mandatory publication of a corporate governance statement would probably help in this direction.

In addition, the role of institutional investors has to be re-examined. In Greece, institutional investors usually follow a passive voting for management and they rarely provide sufficient information for their investment policy to beneficiaries. Institutional investors need to re-examine their strategy and focus on well-governed companies. Full disclosure and comprehensive explanation of their voting policies to their beneficiaries will help in this direction.

Moreover, the political forces have to play a constructive role in the all process. Political forces that set the rules have affected the developments of corporate governance in Greece. In continental European countries and in Greece too, employment protection is high, in a sense that the State is charged with the task of sustaining a social pact between social parties. The market for corporate control, however, cannot efficiently operate when a new controlling shareholder is unable to break up employment contacts. In this way, the frequency of corporate control change (through take-overs) is negatively correlated with the degree of employment protection (Shleifer and Summers, 1988; Pagano and Volpin, 1999). Hence, significant policy implications emerge, such as many stated-owned companies are privatized through public offerings of shares in Greece.

The potential convergence in corporate governance across EU suggests that the Greek capital market have to move quite fast in order to achieve proper corporate governance mechanisms. The latter may prove a strong competitive advantage for companies that try to attract international capital. Hence, efficient corporate governance regime may prove as a significant policy tool for the investment and growth prospective of the Greek economy. The regulatory framework of the Greek capital market has been largely co-ordinate with the EU standards. The challenge is now mostly for the business world to react and voluntarily adopt the appropriate corporate governance structures, in order to achieve real convergence with the business systems of the developed world.

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