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Wien, im April 2009

To my parents...

Abstract

In today´s business world *corporate governance* has become one of the most discussed and most important matters. Corporate governance criteria have been put right in the middle of investment decisions - especially in emerging markets. In addition to that, a series of events like business scandals, financial crises or business failures in the last 20 years has made corporate governance a key point in the business community in emerging markets, developing countries and economies in transition.

There exists no general definition for the term corporate governance. Basically it can be viewed as a set of principles and rules by which a company is directed and controlled. Many countries have developed good corporate governance principles to improve the relationship between the shareholders of a company and the management. Factors like financial disclosure, more rights for shareholders and independent boards are crucial for investors who are looking for a stable growth of companies. Countries in the MENA region have put the implementation of such sound corporate governance codes in the middle of their agenda. Their aim is to create better economies and consequently a more attractive investment climate for possible investors in the future.

This thesis tries to give the reader an insight into today´s state of corporate governance in the Middle East and North Africa countries. The discussion is based on a survey which has been undertaken by the Hawkamah Institute for corporate governance in Dubai which focuses on the establishment of good corporate governance codes in this region.

Abriss

Das Thema Corporate Governance hat in den vergangenen Jahren immens an Wichtigkeit und Bedeutung in der Wirtschaftswelt zugenommen. Investitionsentscheidungen werden vermehrt an Corporate Governance Kriterien gebunden – besonders in den „emerging markets“. Des Weiteren hat die Folge von Wirtschaftsskandalen in den letzten zwei Jahrzehnten – man denke an Enron oder Parmalat – dazu geführt, dass die Bedeutung von Corporate Governance wieder ins Bewusstsein der Manager und Unternehmungen geraten ist.

Es existiert keine einheitliche Definition für den Begriff Corporate Governance. Grundsätzlich kann man es als ein Bündel von Richtlinien und Prinzipien sehen, welche festlegen, wie ein Unternehmen geführt und kontrolliert wird. Viele Länder haben gute und effiziente Richtlinien bzw. Prinzipien entwickelt, um das Verhältnis zwischen Aktionären und Management zu verbessern. Bereiche wie finanzielle Offenlegung, mehr Rechte für Aktionäre und unabhängige Vorstände und Aufsichtsräte sind für mögliche Investoren maßgeblich, die ein stabiles Wachstum der Firmen wünschen.

Die Länder der MENA Region haben die Durchsetzung bzw. Implementierung solcher Corporate Governance Codes in den Mittelpunkt ihrer Agenda gestellt. Das Hauptziel ist die Schaffung einer besseren Wirtschaft und – daraus resultierend – eines besseren Investitionsklimas für mögliche Investoren für die Zukunft.

Die Absicht dieser Arbeit ist es, dem Leser einen Einblick in den heutigen Stand der Corporate Governance Codes bzw. deren Entwicklung im mittleren Osten und Nordafrika zu geben. Die Diskussion stützt sich auf die Ergebnisse einer Umfrage des renommierten Instituts Hawkamah in Dubai, welches sich auf die Durchsetzung solcher Richtlinien und Prinzipien in dieser Region spezialisiert hat.

تلخيص

لقد أصبحت حوكمة الشركات واحدة من أكتر المواضيع اهمية ومناقشة, وقد وضعت معايير حوكمة الشركات في الحسبان في قرارات الإستثمار وبخاصة في الأسواق الصاعدة, وبالإضافة إلى ذلك فان الأحداث المتلاحقة مثل فضائح الإعمال او الكوارث الإقتصادية او أنهيار الاعمال خلال العشرون عاما المتقضية جعلت من حوكمة الشركات نقطة محورية في مجتمع الاعمال في الاسواق الصاعدة والدول النامية والإقتصاد في حالة انتقال.

لا يجد مفهموم محدد لحوكمة الشركات وبصفة اساسية فانه يمكن تفسيرها بانها مجموعة القواعد والاساسيات التى يمكن بواصطتها توجية والسيطرة على شركة.
هناك عوامل مثل الكشف عن البيانات المالية وحقوق اكبر لحاملى الأسهم و مجالس الإدارة المستقلة هذه العوامل ضرورية للمستثمر الباحث عن نمو مستقر للشركات.

ولقد وضعت البلاد في منطقة الشرق الاوسط وشمال افريقيا تنفيذ مجموعة قوانين حوكمة الشركات في خططهم, وهدفهم هو خلق اقتصاد افضل ولالتالي مناخ استثمار افضل للمستثمريين المحتملين في المستقبل.
تحاول هذه الدراسة ان تعطى القارئ نظرة في حالة حوكمة الشركات اليوم في بلاد الشرق الاوسط وشمال افريقيا.
ولقد بنيت الدراسة على استقلاع نفذ بواسطة 'معهد حوكمة لحوكمة الشركات' في دبي, والذي يركز على خلق قوانين جيدة لحوكمة الشركات في المنطقة.

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„Good Corporate Governance is Good Business.“

1. Introduction

1.1. What is corporate governance?

In today´s business world we find many different definitions for the term corporate governance. The two most named and used ones in literature describe the term in a very detailed, and brief way. The first definition comes from the Organisation for Economic Co-operation and Development (OECD) and is defined in the following way:

„Corporate governance is the system by which business corporations are directed and controlled. The corporate governance structure specifies the distribution of rights and responsiblities among different participants in the corporation, such as, the boards, managers, shareholders, and other stakeholders, and spells out the rules and procedures for making decisions on corporate affairs. By doing this, it also provides the structure through which the company objectives are set, and the means of attaining those objectives and monitoring performance.“[1] The seond one is shorter and is briefly compared to the first one.

„Corporate governance deals with the ways in which suppliers of finance to corporations assure themselves of getting a return on their investment.“[2] As we can see from these two definitions, corporate

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1 OECD Principles of corporate governance (2004): http://www.oecd.org (November 2008)

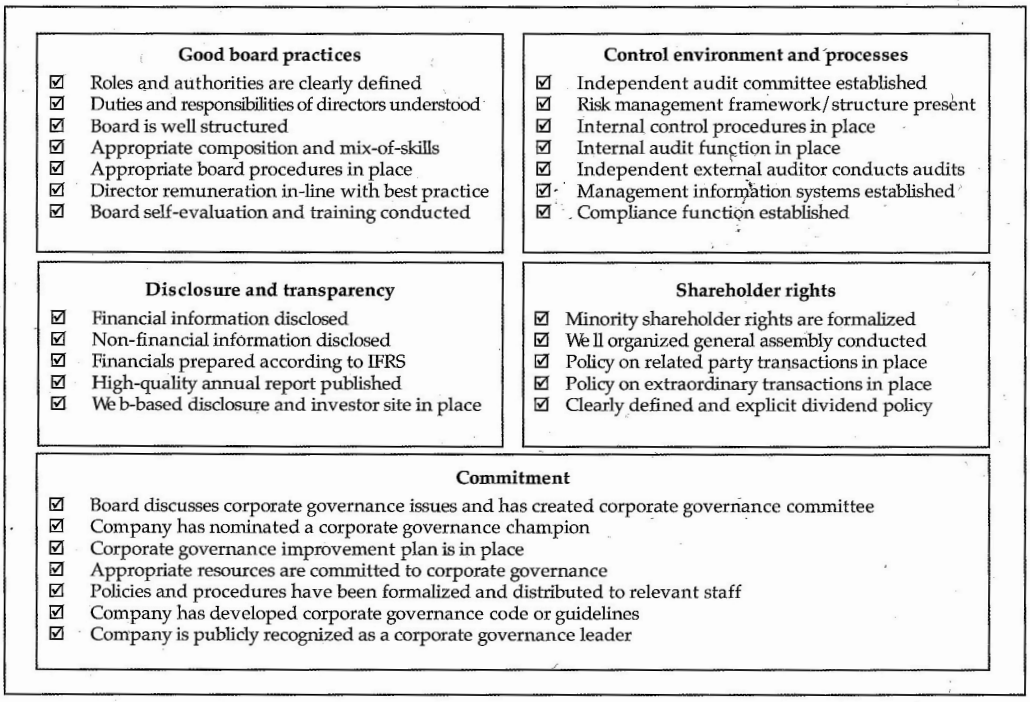
2 Shleifer and Vishny (1996), p. 737

governance can be seen as a set of processes, customs, policies and laws which determine how a corporation is directed and controlled. Furthermore, it describes the relationships among all the stakeholders of a corporation. The principal stakeholders include the shareholders, management and the board of directors. Among the other stakeholders we can find e.g. employees, suppliers, customers, community, banks, environment; in brief: anyone who is dealing with the corporation.

A company which is dedicated to good corporate governance has well-defined and protected rights for their shareholders, a stable control environment, high transparency and disclosure as well as an empowered board. The company´s and the shareholder´s interests are perfectly aligned.

The following table gives the reader an overview of the five elements of a good corporate governance (Figure 1).

Figure 1: Five elements of good corporate govnernance



Source: Hawkamah Institute (2008), A Corporoate Governance Survey, p.11

The elements in this table however do not necessarily represent everybody´s opinion on corporate governance in business today. It is more than just sticking to some guidelines or rules. First of all we might ask ourselves „why is there a corporate problem anyway?“ Why does Adam Smith´s invisible hand not create a proper solution to this problem? Should not be the market in charge of allocating resources in an efficient and appropriate manner?

Luigi Zingales (1998) defines a corporate governance system as „*a complex set of constraints that shape the ex-post bargaining over the quasi-rents generated in the course of a relationship*.“ [3] He refers to the initial contract as incomplete which means that not all possible occur or situations could possibly happen or result from certain actions from the parties and thus can not be covered in the contract because it would be either too costly or simply impossible. The result is that there is some room for bargaining. One has to distinct between decisions which have been made ex-ante (before the two parties entered a contract) and ex-post (when the quasi-rents will be divided). Zingales explains this by means of a machine example. Consider the purchase of a customized machine. Before the production starts, the producer and the buyer agree on certain agreements like final price etc. However, signing this contract does not end the relationship between the two groups. While producing, several incidents may happen which can change the price and costs of the production process. The relationship between the producer and the buyer represents a bilateral monopoly as they signed the specific contract. For the buyer, this machine probably has a higher value than on the market. The producer, however, has presumably the lowest cost to produce the machine. This difference between the two parties (what they generate together and what they could get from the market) describes a quasi-rent, which needs to be divided ex-post.[4] A quasi-rent can be viewed as the

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3 Zingales (1998), Corporate Governance, p. 3

4 Zingales (1998), Corporate Governance, p. 2

difference between the earnings from an investment and the earnings from the next best investment possibility.

Recalling this example of the machine, the bargaining outcome will also be affected by other factors as first stated in the initial contract. For example, who is the owner of the machine while it is being produced? Is it costly for the buyer or the producer to delay the final shipment? Furthermore, an important role is played by the institutional environment: is the ability of the producer for producing this good known by future clients? All this makes up a governance system.

Zingales states two necessary conditions for the existence of a governance problem. The first one is that the relationship between buyer and producer has to create quasi-rents. If there were not any quasi-rents, there would not be any room for bargaining. The second requirement which has to be fulfilled is that these quasi-rents are not perfectly allocated ex-ante. There would not be any bargaining in case they were. Several governance mechanisms like the capital structure, allocation of ownership, takeovers, boards of directors etc. can be seen as processes where such quasi-rents are generated and distributed. Governance is not necessary in a world where future incidents or events can costlessly be put into a contract ex-ante.

This approach of incomplete contracts is a good example to describe the corporate governance of entrepreneurs. The allocation of ownership and the way of how the capital structure is chosen can be described through this approach. We find several efficiencies of such a governance system ex-ante as well as ex-post. The incentive to establish relationships with certain investment opportunities can be counted as an ex-ante advantage. Changing the conditions, which create some room for bargaining, can be seen as advantages for the second group.

It can be concluded that there still has to be done a lot of research and investigations on this topic, namely how such corporate governance mechanisms interact with each other or how takeovers affect the resulting quasi-rents.

1.2. Who benefits from good corporate governance?

Considering the two main definitions of corporate governance, the question arises who is interested in a good corporate governance or rather a good governed company? It seems rather logical that possible investors, who are interested to invest in a company, will choose firms which are stable and have a strong economic growth in order to get a return from their investments. A well-defined corporate governance code is desirable to all the stakeholders for very similar reasons.

- *Investors* are interested in companies with a good corporate governance since those firms exhibit a lower risk at expropriation. Well-governed companies can protect their shareholder´s rights better and also offer a better assurance that the management of the firm is acting in the very interest of the company and all of its shareholders. Furthermore, well-governed companies outperform their competitors with respect to financial and operational performance and also provide a better long-term return on investment.[5]
- As the risks which are associated with the corporation decline with a better corporate governance, *companies* benefit. There are two reasons for that. First, the probability of„rent-seeking“[6] by managers is reduced. Second, good corporate governance reduces the cost of capital and consequently increases the firm value. The lower risk results from improved processes inside the corporation due to a better coordination of information and a improved decision-making process. This leads to a better performance.
- The *public sector* also benefits from corporate governance as it eases the development of stronger markets, lowers risk, and

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5 Gompers, Ishii and Metrick (2003): p.738

6 In economics, rent-seeking refers to managers that seek gains by manipulating the environment rather than through productive behaviour.

improves a country´s ability to deal with investments - which helps to advance economic growth.

- All other *stakeholders* like banks, suppliers and employees profit from the better performance of the firm.

During the last years many researchers started to create indices for measuring the quality of corporate governance practices. These indices are then put in relation to the performance of the companies. Several commercial providers are now offering such services like corporate governance research and corporate governance ratings as the awareness on this topic increased due to the demand of institutional investors. In Europe, Déminor is providing investors with information like disclosure, board structure, governance practices of the Financial Times Stock Exchange (FTSE) Eurotop 300 index companies.[7]
Such providers also exist for other markets. Standard and Poor established such services for emerging markets, and Credit Lyonnais Securities Asia (CLSA) released corporate governance ratings for more than 490 companies in 25 countries. The results from a study which was carried out by CLSA in 2001 found a strong correlation between corporate governance and financial performance ratios.[8]

According to another survey from McKinsey[9] the premium investors would pay for a well-governed firm varies by country and region. The premiums in the MENA countries range from 29% (Egypt) to 30% (Morocco). Compared to those countries, the premiums in Europe are slightly lower (e.g. Germany 20%). There exist plenty of reasons why corporate governance has become such a relevant issue during the last two decades. First of all, we can notice a world-wide wave of privatization in

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7 See http://www.deminor.com/ for more information (March 2009)

8 Further information can be found on the website http://www.clsa.com (March 209)

9 McKinsey´s Global Investor Opinion Survey (2002): http://www.mckinsey.com (November 2008)

the economy. Regarding this matter, one has to think about how the newly privatized companies should be controlled and owned. That´s when corporate governance principles are inevitable. More and more households are saving money in order to invest it in equity. This had the consequence that a service industry came into existence that creates voting recommendations and exercises votes for the clients.[10]

Events such as the big financial crises in the past years or the collapse of big international companies like Enron in the US or Parmalat in Italy - due to corruption or deceptive practices - can shake the economies of countries to a huge degree. Fighting corruption needs constant efforts. Therefore it is very important to have proper solutions to fight such problems; through improving transparency and disclosure, accountability, and a good corporate governance. Good corporate governance is fundamental in guaranteeing a stable and well-growing economy. Schleifer and Vishny give a good explanation why corporate governance is important for the business and society: „Understanding corporate governance not only enlightens the discussion of perhaps marginal improvements in rich economies, but can also stimulate major institutional changes in places where they need to be made.“[11]

10 Becht, Bolton, Roell (2002), p. 4

11 Shleifer and Vishny (1996), p. 738

2. MENA countries and their recent development

The term MENA stands for „Middle East North Africa“ and is often used in business writing. They represent an economically diverse group which includes states with a common culture and heritage. The MENA countries can be subdivided into 3 different groups. Countries which belong to the first group are called „Early Reformers“, because they are following economic reform programs since the 1980s. Countries like Egypt, Jordan and Morocco belong to this group.

The second group contains mainly oil-exporting countries like Bahrain, Kuwait, United Arab Emirates and Saudi Arabia. Due to the still rising oil price those countries achieved economic stability. Since 2000 they have also allowed foreign investments in their home market.

The last group contains all other countries whose economy is unstable due to political reasons (West Bank, Gaza, Iraq) or still in early development (Lebanon, Syria, Sudan, Libya). Security markets still do not exist or are of a very small size.[12]

Generally, it can be noticed that the financial sector in those countries primarily is a bank-based sector with still growing securities markets.

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12 Corporate governance in Morocco, Egypt, Lebanon and Jordan (2003), p. 10

Stock exchanges are either controlled and supervised by government or by a securities regulator, as in Egypt and Oman.[13] As for 2007, the Gross Domestic Product (GDP) amounts to about 1,52% of the world´s GDP. Market capitalization of all listed companies in the MENA region increased from about 20% in 2002 to more than 58% in 2007 (% of GDP).[14] For further details see the table below.

Figure 2: Overview GDP and market capitalization

	2005	2006	2007
GDP World	$ 45.053.892.754.518	$ 48.626.696.268.075	$ 54.347.037.614.014
GDP MENA	$ 614.210.445.076	$ 706.222.965.961	$ 828.691.246.709
GDP MENA % World	1,36%	1,45%	1,52%
Market capitalization of listed companies (% of GDP)	48%	48%	58%
Population (MENA)	302.718.938	308.110.570	313.432.951

Source: http://econ.worldbank.org (March 2009)

Many countries in the MENA region announced their commitment to introduce corporate governance to strengthen their market economy and to encourage further private investments in the future. The issue that a good corporate governance is essential for firms to sustain a stable and efficient growth will be discussed in a later chapter.

13 Corporate governance in Morocco, Egypt, Lebanon and Jordan (2003), p. 11

14 The World Bank, World Development Indicators (WDI), Online Database http://econ.worldbank.org (December 2008)

2.1. Corporate governance in the MENA countries - an overview

Most of the countries in the MENA region are in transition and on the way to market-based governance. Economic reforms have been undertaken in Egypt, Morocca and Jordan in the 1990‘s to move closer to a market economy model.[15] About 10 years ago, the concept of corporate governance was unknown in most of the countries in the MENA region. Due to the domestic war in Lebanon, the implementation of corporate governace in this country has not shown any progress for about 20 years. However, a big economic reform program started in the last years and focuses on the corporate sector.

Looking at the companies and corporations in these countries, it can be noticed that many large companies are often controlled by „family groups“ or individuals. They have at least one shareholder who owns more than 20% of the shares.

This fact can be considered as a major problem for the introduction of corporate governance principles because managers do not have the autonomy, flexibility and objectivity for monitoring all the processes inside the company and to follow its objectives. Moreover, many companies in the MENA region are privatized and state-owned. For example, in Egypt the state holds more than 20% of shares in the 20 biggest companies, and more than 50% in another 12 big companies listed on the exchange.[16]

The basis for every corporate governance framework is taken from the company, civil and securities laws. Also the listing rules from the stock exchange regulations and the basic accounting standards are fundamental for the board and the management. Basically the corporate governance framework for those countries in the MENA region refer to two laws: the Corporate Law and the Capital or Securities Market Law.[17] One main aim

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15 Maged Shawky Sourial (2004), p. 7

16 Corporate governance in Morocco, Egypt, Lebanon and Jordan (2003), p. 22

17 Corporate governance in Morocco, Egypt, Lebanon and Jordan (2003), p. 23

of these mentioned laws is the improvement and enforcement of disclosure requirements.

In order to rise the awareness of the importance of corporate governance, many conferences and workshops have been held by many institutions in the Arab countries. So far these events made the implementation of corporate governance rules more attractive for the management of firms.

2.2. Hawkamah Institute for Corporate Governance in Arab countries

The international association Hawkamah Institute for corporate governance (Hawkamah)[18] - with its headquarters in Dubai - is an institution with the mission to promote good corporate governance in the Middle East, North Africa and Central Asia region, as well as assisting the countries in developing and implementing such sound and well-integrated codes adapted to the countries‘ needs and objectives. Hawkamah provides its services to all kinds of enterprises; namely from listed companies to banks, financial institutions, non-listed companies including family-owned enterprises as well as the public sector with a focus on state-owned enterprises.

The Hawkamah Institute works together with many other prominent institutions such as the *Dubai International Financial Centre* (DIFC), the *International Finance Corporation* (IFC) and the *Dubai School of Government* (DSG). Furthermore, Hawkamah is also fostering communication and policy dialogue both at regional as well as international level, either through seminars, workshops or conferences.

The Executive Director of Hawkamah is Dr. Nasser Saidi who is the former Minister of Economy and Trade and Minister of Industry in Lebanon. His aim is to back the establishment of the institute and to develop sound

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18 For further information see http://www.hawkamah.org (November 2008)

financial markets to improve the future economies for the Golf Coorperation Council (GCC) and the MENA region.

3. Implementing corporate governance: practice vs. theory

3.1. The survey

The Hawkamah Institute for corporate governance has carried out a survey in collaboration with the International Finance Corporation (IFC) on corporate governance of listed companies and banks across the Middle East and North Africa. The aim of the survey was to get more detailed information on the role of corporate governance in today´s companies. In detail, the survey contained 57 non-listed banks, 65 listed banks and 922 listed companies from 11 MENA countries and so had the total number of 1044. Jordan was the country with the most participants in this survey (219 in total), Lebanon the one with the fewest (9 in total). Due to another survey which had been done by the Internation Finance Corporation (IFC), lebanese banks were not included in the survey of the Hawkamah institute.[19] Banks were divided into four different groups according to their amount of assets. Listed companies were also grouped - along sales - into four categories.

A detailed chart of all the countries which have been considered in the survey can be found at the end of the paper (chart 1).

Despite of the high number of questioned firms, only 155 companies did respond (74 banks, 81 listed companies). The countries which were finally included in the survey are Bahrain, Egypt, Jordan, Kuwait, Lebanon, Morocco, Oman, Saudi Arabia, Tunisia, United Arab Emirates and West Bank & Gaza.

The major aim of this survey was to find out how important corporate governance is for these companies or rather how their current state according corporate governance is.[20] Furthermore, this survey should allow stakeholders to get an insight into the company´s implementation of their corporate governance principles.

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19 The survey can be viewed under www.ifc.org/mena/corporategovernance (November 2008)

20 Hawkamah Institute (2008), Corporate Governace Survey

The following discussion is based on this survey and tries to give the reader an overview on today´s development and state of corporate governance in the Middle East and North Africa region.

3.2. General findings

As mentioned before, good corporate governance codes are essential for a good working and stable firm performance. It is important that the interests of the stakeholders and the management are perfectly aligned to keep everyone happy.

The majority of the survey´s respondents also see the implementation of corporate governance codes as important for their corporations (around 40%).[21] The results show that there is no big difference between listed companies and banks.

However, not all participants in this survey were able to give the correct definition of the term corporate governance consistent with common approaches - namely „a system by which business corporations are directed and controlled“. Many of the respondents mixed up the term corporate governance with the term corporate social responsibility (CSR) or corporate management. A fact that shows clearly that corporate governance is still not fully understood by many firms.

CSR tries to describe how companies set their business processes in order to achieve a positive impact on society.[22] It is about the commitment of a firm to behave ethically to improve the workers´ life and the society in general. On the other hand, corporate management deals with the monitoring and controlling of a firm´s performance using indicators such as revenues, Return on Investment (ROI) and other financial ratios.[23] These explanations show that both CRS and corporate management are both two distinct concepts which have to be considered separately from corporate governance.

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21 Hawkamah (2007), Corporate Governance Survey, p. 15

22 Mallenbaker (2007), CRS - What does it mean? - www.mallenbaker.net (November 2008)

23 For a more detailed explanation see http://www.techtarget.com (December 2008)

In more detail it can be claimed that the majority of respondents combines good corporate governance with a better compliance with legal and regulatory requirements. In addition to that, a general improvement of operational efficiency and a mitigation of risk are assumed to be benefits of well-established corporate governance. Only a very small fraction of the firms and banks cited a lower cost of debt and equity. Looking at the survey, which has been undertaken with the top 1.000 listed UK firms, the three benefits, which have been mentioned the most among the participants, are protecting shareholder rights (95%), improving access to external capital (88%) and lowering cost of debt and equity (85%). Only around 1% sees the compliance with regulations as a benefit resulting from corporate governance.[24]

It is crucial for directors and managers of firms to fully comprehend the benefits of good corporate governance codes in theory and also in practice.

3.3. Still at the beginning

The countries in the MENA region are still at the beginning of this implementation phase. Their aim for the upcoming years should be to commit to corporate governance, to build up a robust control environment, to strengthen transparency and disclosure and to have protecting shareholder rights. The Hawkamah Institute - together with the IFC - created certain corporate governance indicators which should help to present or describe the current state of the companies´ codes. There exists a total amount of 32 indicators, grouped into five categories starting from ‚demonstrating commitment', ‚implementing good board practices', ‚building a robust control environment', ‚strengthening transparency and disclosure' and last but not least ‚protecting shareholders´ rights'.

The fact that the majority of the companies and banks are still at the beginning of the introduction phase of corporate governance principles

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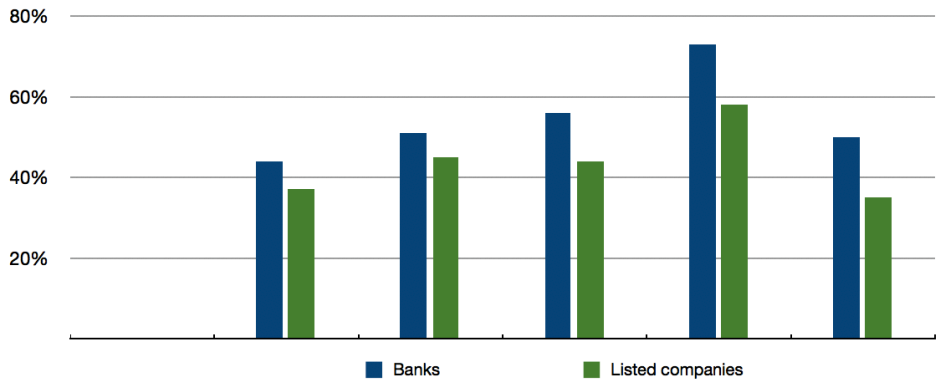
24 Moxey (2004), Corporate Governance and Wealth Creation

can be verified by the number of indicators they applied. 51% of all firms implemented 15 or less indicators and can therefore be put into the „emerging practice“ section. Around 41% of all firms followed up to 23 indicators (‚improved practice‘). However, not a single company or bank out of the sample of 152 firms did follow all 32 indicators.[25]

Banks face special governance problems due to their more diverse and inscrutable activities. Therefore those processes are more difficult to control and monitor. This can be seen as a reason why banks are usually committed to better corporate governance practices compared to listed companies. Transparency and disclosure are very important because of the fact that banks are often highly regulated. A proof for this can also be found in the survey of Hawkamah where the pillar representing transpareny and disclosure is scoring more than 70% and therefore outperforms the other four pillars by far.

The graph on the following page shows how many of the participating firms implemented each of the five pillars of corporate governance (Figure 3). Transparency and disclosure seem to be the most important pillar. We can also notice a trend between banks and listed companies.

Figure 3: Implementing corporate governance principles in the MENA region



	Commitment to corporate governance	Board of directors	Control environment	Transparency and disclosure	Shareholder´s rights
Banks	44%	51%	56%	73%	50%
Listed companies	37%	45%	44%	58%	35%

Source: Hawkamah (2008), Corporate Governance Survey, p. 18

25 Hawkamah (2007), Corporate Governance Survey, p. 17

Both banks and listed companies show similarities in implementing corporate governance principles. As mentioned before, due to the strict regulations and laws which are binding for banks, they generally show a stronger commitment to a good implementation of such governance guidelines.

3.4. Board of Directors

The board of directors in a company represents the shareholders and can therefore be seen as an important control mechanism for corporate governance. It is the place in the company where the key corporate governance issues come together. It normally consists of persons, who got elected, and the board´s major task is to monitor and to control the company´s activities. The question whether the board´s members are independent or not is relevant for good corporate governance.

The main responsibilities of the board lie in

- guiding and monitoring management;
- ensuring good corporate governance rules;
- setting a company strategy;
- selecting and replacing the Chief Executive Officer (CEO);
- setting up a succession policy;
- implementing good board practices;
- improving transparency and disclosure;
- approving annual budgets
- protecting the shareholders´ rights, just to mention the main tasks.

Depending on the legal framework which it operates in, the tasks of the board normally vary from country to country and from organisation to organisation. As the markets globalize and become more complex, the demands of the boards tend to increase. Directors have to handle a larger

amount of issues in a more efficient way in order to stay competitive. Setting up a company strategy is the task of the board in the majority of the surveyed companies in the MENA region. Only 25% of the banks and listed companies assign this task to the CEO.[26]

The development of such company strategies is quite a difficult, time-intensive and complex task which is usually be done by the managers because they are the ones who have a better understanding for the industry and the resources. The directors, however, are better in reviewing and finally approving such strategies.

3.4.1. Board Structure

Basically, we can distinguish between two different board systems.[27] The most common one is the so called one-tier board which has both executive and non-executive members. On the other side, the monitoring and control activities of the two-tier board - which is predominant in Germany - are split up into two boards: the management board (Vorstand) and the supervisory board (Aufsichtsrat). This, however, is only the case for stock operations. Other types of companies (e.g. the limited liability company GmbH) can freely choose between the one-tier or two-tier board.
In the MENA countries the one-tier board is the dominating model, except for Morocco which has a board structure similar to Germany. This structure is best practice in the case when the position of CEO and chairman are held by the same person. We have seen which problems can arise in recent international corporate crises. However, this separation of chairman and CEO can be difficult to realise in the MENA region due to the fact that the majority of companies are family-owned.[28] This separation is not an easy thing in a family-dominated business. It would not be easy to remove an owner of a family-owned company to let others work with his invested

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26 Hawkamah (2007), Corporate Governance Survey, p. 24

27 Maged Shawky Sourial (2004), p. 22

28 Nasser (2004), p. 12

money. In Lebanon this split is prohibited by law (Lebanon Code of Commerce). It states that the chairman shall also fulfill the responsibilities and tasks of the general manager unless he selects one to act in his interests.[29] In Oman the Code of corporate governance strictly forbids the combination of the role of CEO and general manager.[30]

The benefits of having a board of directors which consists of a balanced mix of executive, non-executive and independent directors are quite intuitive. An executive director or inside director is an employee of the company and is often holding the position of CEO and CFO. They are best informed of what is going on in the company and what the firm is struggling with since they face those problems every day. Non-executive directors or outside directors do not hold any position in the firm. They may or may not be independent. The advantage of having such directors on boards is that they have an outside perspective and useful contacts. They do not have any business tie to the firm aside from their directorship. That is when a director is called independent. Independent directors are said to exercise for the benefit of the company and in the interest of all shareholders. There is no personal interest in the decision-making progress. However, being only independent does not help. Independence may also mean indifference and having less information than inside directors.

Boards in the MENA region seem to have a well-balanced mix of executive, non-executive and independent directors. It is blazing that companies in the Mashrek region (Morocco, Tunisia) are dominated by executives, while boards in other regions have more non-executive directors (Gulf region). We also find evidence in the literature that a poor performance of a company leads to a higher number of outside directors (*reverse causality*).[31] One reason for this phenomena could be that

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29 Maged Shawky Sourial (2004), p. 22

30 see Article No. 3 in the Oman Corporate Governance Code

31 Zechner (2007), Creating Value, p. 200

managers of poorly performing firms try to bring new „views“ into the company that may have a positive effect on the success. Not only skills and knowledge in finance and accounting is a necessity for directors, also knowing what is happening in the industry and outside the company is relevant for developing and setting up strategies for the firm´s future.

3.4.2. Board size

The right size of the board is also essential because a too low or a too high number of members can lead to a slower decision-making progress. A small board might have a lack of experienced members, whereas a big board is difficult to manage. Finding the right board size therefore is not an easy task to fulfill. Empirical studies point out that a larger board size is negatively correlated to firm performance in general. A possible explanation could be again the coordination problem or the problem of free-riders.[32]

According to the survey of the Hawkamah Institute, the majority of the surveyed banks and companies has around two to five non-executive (23%) and executive directors (42%). Having a look on the independence of directors, we see that 55% of all banks and companies have either one or no independent director on the board.[33]

As mentioned before having independent directors on the board can have some positive side-effects for the performance of a company. However, it does not solve all the problems within a board. Factors like experience and expertise, loyality and integrity are just as inevitable to have a good-working and qualified board. Researches on this topic also showed that a company with more outside directors is less sensitive to takeovers as they do a better job than inside directors. Therefore the better performance of the firm leads to a decreasing likelihood of being taken over by another firm.[34]

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32 Zechner (2007), Creating Value, p. 201

33 Hawkamah (2007), Corporate Governance Survey, p. 29

34 Zechner (2007), Creating Value, p. 205

Having a look on the board size of various companies in the gulf region (Bahrain, Kuwait, Oman, Qatar, Saudi Arabia, United Arab Emirates) we can notice rather big differences in the board size.[35] While the average board size in Bahrain and Qatar is around 8.5 members, we only have around 6.2 members in Kuwait and 6.7 in Dubai. Possible explanations for this obseravation have to do with the legal framework of these countries. The law in Abu Dhabi for instance says that a board has to consist of at least 3 members and allows a maximum size of 15. In Kuwait, however, the only requirement is that it has a minimum size of 3 members. Sectors like the banking sector, telecommunications and energy sector have the largest boards with a mean of 8.5 members, on the contrary the financial service sector only has boards with about 6 members. Taking the size of a company into consideration, data clearly show the bigger the firm the bigger its board. However, this relation is not linear as some very large companies like Etisalat[36] would have unrealistic and huge boards.

3.4.3. Establishing board committees

Because of the increased complexity of the board´s tasks it is useful to create certain committees which take over some of the board´s responsibilities. In this way experts and professionals are allowed to focus on certain issues to finally recommend them to the board. Therefore the board is discharged from the responsibilities and can pay more attention on fulfilling their main duties.

A board can have many different committees. Companies tend to implement three committees for the purpose of good corporate governance - namely the audit, nomination and remuneration committee. It is desirable that each of these committees is governed by independent directors or that they have at least one independent director. Although some of the original tasks have been delegated to other committees, the

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35 Hawkamah (2008), Power matters: A survey of GCC boards, p. 9

36 Largest telecommunications company in the UAE (http://www.etisalat.ae)

unit which has the final decision power is still the board. It is responsible for all board decisions.

The audit committee is charged with the role of monitoring the financial reporting and disclosure procedures. It should be composed of independent and outside directors but at least one of them has to be a financial expert. The nomination committee´s main task is to recommend possible candidates for the election to the board of directors. Last but not least the remuneration committee which is considered to determine and agree with the board of the remuneration of the CEO, chairman and other executive members.

In the Middle East and North Africa region a very large majority of firms and banks does have an audit committee (78%). However, the nomination and remuneration committee only exists in 28% of the surveyed banks and companies. Only 26% of the committees consist of a majority of independent members. There still has to be some work done with reference to those committees so that all firms can benefit from their work. Having a look on the boards of the S&P 500 firms, we can see that all firms do have an audit and a remuneration committee and both consist of only independent directors. Almost all companies (98.5%) introduced a nomination committee and nearly all their members are independent.[37]

3.4.4. Board meetings

Board meetings should be held at least four times a year. However, it is often the case that directors have to meet more often to discuss and decide on certain things. The number of board meetings per year varies from banks to listed companies. On the one hand, 46% of the surveyed banks stated that their board meets around three to five times a year, while the percentage rate for listed companies is nearly 60%. The diagram below shows the details.

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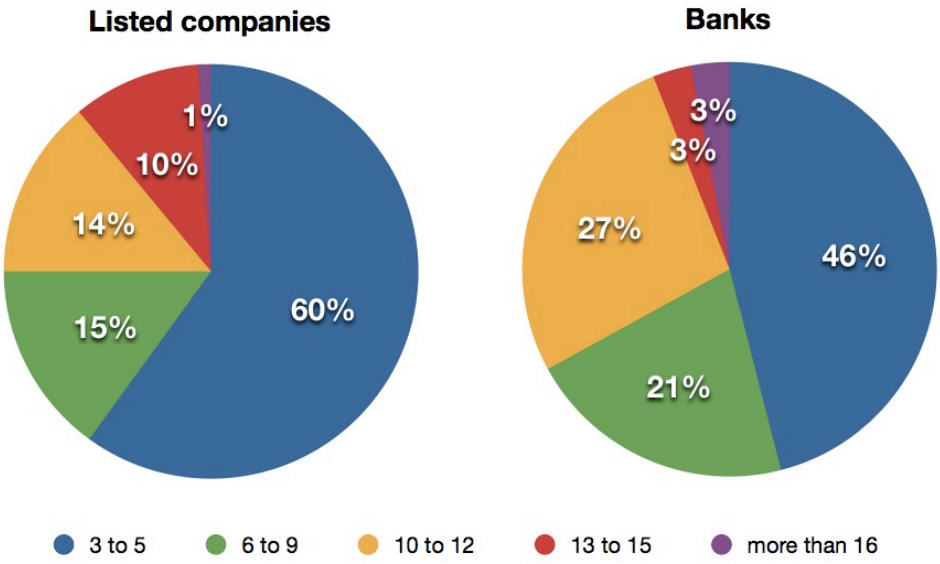
37 The Spencer Stuart Board Index (2005), http://www.spencerstuart.com (Dec 2008)

Figure 4: Board meeting frequency in the MENA region



	3 to 5	6 to 9	10 to 12	13 to 15	more than 16
Listed companies	60%	15%	14%	10%	1%
Banks	46%	21%	27%	3%	3%

Source: Hawkamah (2008), Corporate Governance Survey, p. 35

3.4.5. One director, one board? Multiple Directorships

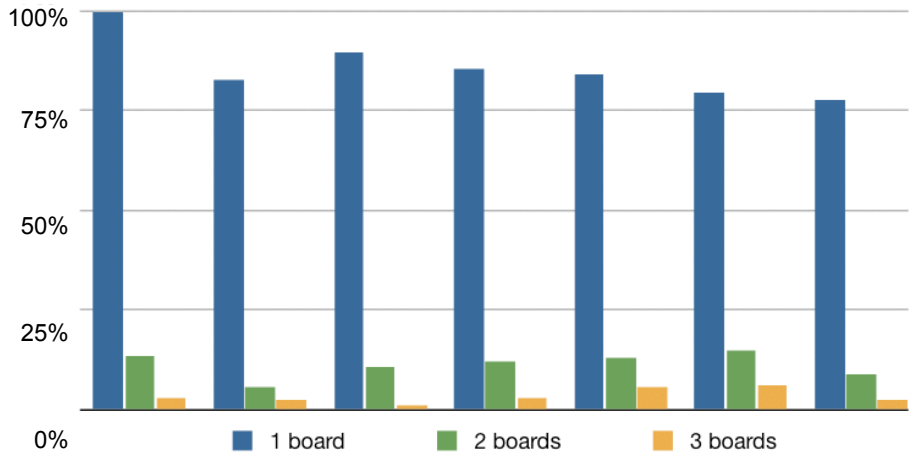
It is not compulsory for a director to be a member of only one board. He or she can sit on two, three or even more boards at the same time. This cross-board representation is very common in the western countries as well as in the MENA region. However, directors should not forget that quality and not quantity counts. There exist certain requirements for directors who wish to become a member of several boards. For instance the fact that he or she can not sit in a rival company.

It is quite interesting to see that the vast majority of directors in the GCC region are only members of one single board. Bahrain is the leader of the group with 89.9% and Qatar is the last one with 78%.[38] Private companies were excluded in this survey. The results would of course have been different if private companies had been included. It is difficult to aquire such information about private companies than it is for public ones. Around

38 Hawkamah (2008), Power matters: A survey of GCC boards, p. 19

12% of all directors in the gulf region are on two boards, only around 4% on three, and nearly 0% on four or more boards.

Figure 5: Cross-board representation in the MENA region



	Abu Dhabi	Bahrain	Dubai	Kuwait	Oman	Qatar	Saudi
1 board	82,80%	89,80%	85,70%	84,30%	79,60%	78,00%	87,00%
2 boards	13,70%	5,80%	11,10%	12,40%	13,10%	15,10%	9,40%
3 boards	3,00%	2,90%	1,40%	3,10%	5,80%	6,20%	2,80%

Source: Hawkamah (2008), Power matters, p. 19

3.5. Managerial Labor Market

The managerial labor market does have an influence on corporate governance. The question whether there is a connection between a firm´s performance and the turnover of the executive directors has been discussed by Gibson.[39]

Many researchers have found out that there exists a positive correlation between the CEO turnover and a poor firm performance.[40] However, a poor performance is not the only reason for a high turnover. Other factors like pressure from outside shareholders must also be taken into consideration. As there are no surveys or researches on this topic for the MENA region, we presumably can take results from other emerging markets (e.g. Asia) and draw conclusions for the countries in the Middle East and North African region.

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39 Gibson (2002), Is Corporate Governance Ineffective in Emerging Markets?

40 Zechner (2007), Creating Value, p. 202

A study from Gibson from the year 2002 showed that Chief Executive Officers from firms with a poor performance are more likely to get replaced than those in good performing companies. Gibson tested this for companies in emerging countries (Brazil, Chile, India, Korea, Malaysia, Mexico, Taiwan, and Thailand) over a period of 4 years.[41]

More generally said, CEO turnover is more sensitive to a firm´s performance when the board is dominated by outside directors. Furthermore, current studies found out that there is an even stronger relationship between the performance of a company and CEO turnover when the firm has a smaller board.[42] If we also have a look on the executive compensation, Perry states that in case that the directors are paid by using incentives (equity-based arrangements), the relationship between performance and turnover is even higher.[43]

As stated before, there have not been carried out any surveys for the MENA region up to now. It is questionable whether the results from other studies can also be taken into consideration for the Middle East region due to the fact that many companies in the MENA area are dominated by families. The probability that a director will get repelled from his own firm or company is quite unlikely.

3.6. Executive Compensation

As mentioned before, only 25% of all surveyed banks and companies in the MENA region do have a remuneration committee which deals with setting up an appropriate remuneration package for the executive members of the company. It is desirable that this package is aligned with the interests of the firm and its shareholders - if possible in the long-run. In order to ensure that managers will create value for the shareholders, it is quite common for them to have incentive compensation packages - which

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41 Gibson (2002), Is Corporate Governance Ineffective in Emerging Markets?

42 Zechner (2007), Creating Value, p. 203

43 Perry (2000), Incentive Compensation for Outside Directors and CEO Turnover p. 13

means that the salary is typically splitted into a base salary, an annual bonus tied to the accounting performance and long-term incentive plans like stock options. There for sure exist additional fees which are paid out for additional responsibilities like a committee membership, meeting fees or for being chairman of a board. Figure 6 on page 30 represents the board remuneration structure and practices of the surveyed banks and companies in the MENA region. It shows the percentage of executives and non-executives who receive such remuneration packages in detail.

The use of such remuneration packages is not common. Only 35% of executives do receive variable packages and more than 53% do not. It is quite interesting to see that stock options are only offered to 10% of the executives and less than 4% to non-executives. Stock options would be a good incentive for the long-run as they would tie the manager´s salary to the performance of the company. Looking at the pay mix of CEOs in the USA, we see that in 2004 more than 62% of the total salary consisted of long-term incentives (e.g. stock options) and only 15% contributed to the salary. Comparing the United States with the rest of the world, there is also a big difference between the breakdown of stock options and base salary. In the USA, nearly half of the total salary consists of long-term incentives, whereas in Europe or Asia they only represent a fraction of the total salary. [44]

The majority of the banks and companies in the surveyed region do not offer any insurance or pension funds which probably would bring executives and the company closer together as they are considered to be long-term incentives. The question is whether the remuneration committee or the board is responsible for setting the executives´ and non-executives´ salary. For approving the salaries of the executives, more than 80% of the banks and nearly 90% of the companies delegate this matter to the board. However, if stock options are also offered to the managers, it is

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44 Zechner (2007), Creating Value, p. 134

recommended that the company includes the shareholders in the decision-making process - in case shares get diluted. For approving the salaries of non-executives, on the other side, the majority of banks and companies assigns this task to the shareholders (banks 63% and companies 69%).[45] It would be better to delegate this matter to a remuneration committee which then decides on the salaries. This policy could then be disclosed to the shareholders.

Shleifer and Vishny (1997) state that such compensation contracts do not offer incentives for solving the agency-problem that comes up with the separation of ownership and control or management and finance in public companies.[46] The reason for this is that such incentive contracts motivate managers to act in their very own interest rather than the shareholders´ (problem of self-dealing).
As mentioned in the first chapter, good corporate governance practices reduce the risk of rent-seeking by insiders. Managers could manipulate accounting numbers and investment policy to raise their salary.
However, according to a study from Jensen and Murphy in 1990, an increase in the shareholders´ wealth by $1000 changes the salary of CEOs by only $2.59.[47] This explains the argument of Shleifer and Vishny that such incentive contracts do not solve the agency problem at all.

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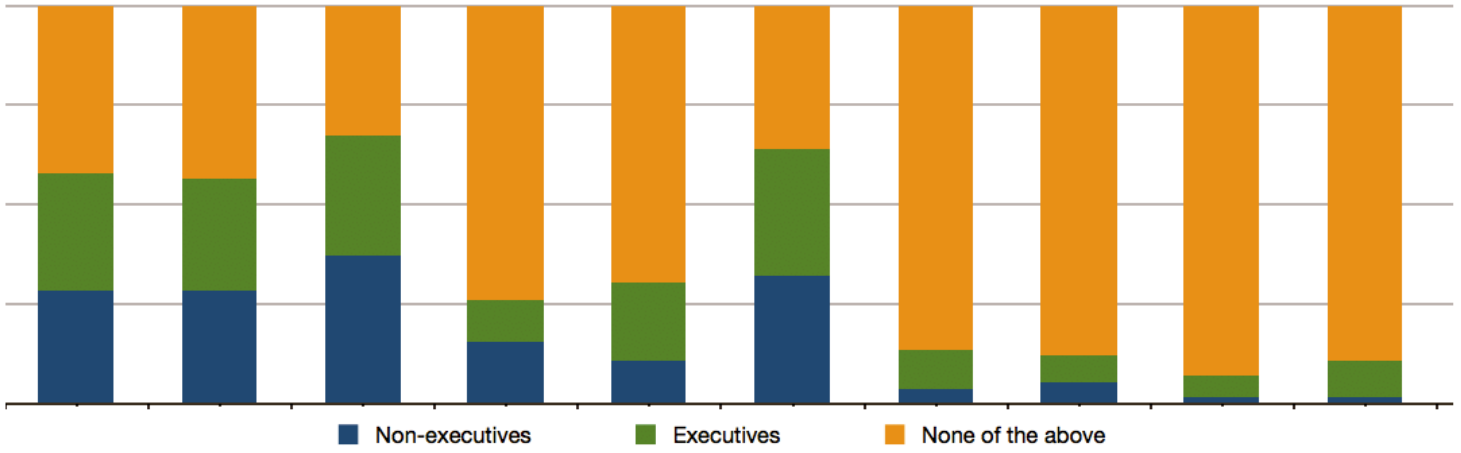
45 Hawkamah (2007), Corporate Governance Survey, p. 37

46 Shleifer, Vishny (1997), p. 745

47 Jensen, Murphy (1990), p. 6

Figure 6: Board remuneration structure and practices

→ shows the percentage of executives and non-executives who receive such remuneration packages



	Annual fee (fixed package)	Annual fee (variable package)	Attendance fee	Fees for additional work	Fees for being chairman	Reimbursed for travel costs etc	Stock option	Insurance	Contribution to pension funds	Ability to use assets
Non-executives	33,90%	35,30%	48,90%	16,10%	11,30%	40,90%	3,60%	5,40%	1,80%	1,80%
Executives	34,70%	34,50%	39,10%	11,00%	20,20%	40,20%	9,80%	7,20%	5,40%	9,20%
None of the above	50,00%	53,80%	42,90%	77,10%	71,80%	45,50%	86,60%	90,10%	93,70%	89,90%

Source: Hawkamah (2008), Corporate Governance Survey, p. 37

3.7. Risk Management

Several events like financial crises, business scandals or fraud took place in history and are still happening. Cases of accounting improprieties in several big firms like Enron, WorldCom or McKesson HBO were in the media and aroused the attention of investors. The reasons for the occurence of such crises are a weak control environment which assures that things like mismanagement, financial fraud or other abuses in a company are minimized. Referring to good governance practices, one of the board´s major duties should be to set up a policy which ensures that the management´s tasks and actions are being controlled and overseen. The implemention of such a policy should pay attention to risk management, internal controls and the internal and external audit. As described in the chapter about establishing certain comittees in a company, the audit committee should be in charge of overseeing a firm´s control environment.

The advantages of having such a control mechanism for managing the risk of a company are obvious. Firms which are effective in risk-management are also more effective in the long-run - referring to profits. On the other side, those which do not pay much attention on risk may also not profit over the longer term. Companies which absolutely do not pursue risk management can be seen as lost - sooner rather than later.
Less than half of the surveyed banks and companies do have a risk manager or a department for risk management. In more detail, 62% of banks and only 23% of listed companies.[48] The reason for this big gap between banks and companies possibly results from the fact that banks are exposed to more risks and do have to follow more regulations regarding risk.

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48 Hawkamah (2008), Corporate Governance Survey, p. 41

3.7.1. Internal controls

Internal controls can be described as means by which the resources of a firm are monitored and directed. Furthermore it helps to detect and prevent fraud inside a company. Internal control can support the management to achieve all the objectives which have been set. The CEO should be responsible for designing and implementing such effective control mechanism. In the MENA countries, 59% of banks and only 36% of listed companies have an internal control - e.g. a control department.
In 75% of those banks and companies, which do have such an internal control function, the board is responsible for this matter. Best practice sees the CEO in the implementing role, and the board in the monitoring role.

3.7.2. Internal audit

In order to improve a firm´s or bank´s operations and to increase the value in general, auditing is inevitable. The internal audit process can be seen as an assurance and consulting activity within the corporation that helps the organisation to focus on its goals by evaluating and monitoring risk management and the governance processes. It plays an immense important role in identifying possible risks that could harm the overall performance of the organisation. In the MENA region, the great majority of banks (85%) and listed companies (92%) do have such an internal audit function. Best practice calls the board to monitor and control the internal audit processes. 93% of banks and 76% of listed companies follow this best practice as they put the board in charge of this audit procedure.[49]

3.7.3. External audit

In addition to the internal audit, an external audit should also be conducted by an independent, professional auditor. An external audit shall provide an external view on the bank´s or firm´s situation regarding the financial statements and their fairly representation covering all aspects.

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49 Hawkamah (2008), Corporate Governance Survey, p. 44

International standards require the external auditor to find out if the bank´s or firm´s financial statements are in compliance with accouting principles or certain standards or which standards have not been taken into consideration while preparing the statements. A large majority of banks and listed companies in the Middle East and North Africa region - namely 86.1% banks and 68.8% listed companies - employ international audit firms for overseeing and reviewing the financial papers. A rather small group of banks and companies relies on local audit firms (11.1% banks and 27.3% companies) and a very small percentage uses the services of individual auditors (2.8% and 3.9% respectively).[50]

Good corporate governance practices proved that it is necessary to change or rotate auditors from time to time to improve auditor independence. The reason for this is that there can be a problem if the auditor establishes a strong connection with the organisation he is reviewing. However, an argument against this issue is that it normally takes more than one year for an auditor to adapt to a new firm - so changing him or her every year would not be useful as he or she is unfamiliar with the business and may commit errors during this first period. In some business, a permanent auditor is also beneficial due to the low number of qualified audit firms. The surveyed banks and listed companies in the MENA region do not have a rotation-policy and therefore do not practice the auditor rotation. 59% of them stated that their external auditor has not been replaced during the last five years. 32% of banks and companies do have an effective audit-rotation policy. Among this 32% around 7% changed their last auditor due to his or her poor auditing performance and 3% claimed they rotated the auditor because of cost considerations.[51]

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50 Hawkamah (2008), Corporate Governance Survey, p. 45

51 Hawkamah (2008), Corporate Governance Survey, p. 46

3.7.4. Audit committee

The audit committee is providing help and support to the board in questions like establishing internal control mechanisms, audit policies, overseeing the relationship with external auditors and more. Some board of directors also demand from the audit committee to set up risk management frameworks in cooperation with the board. Selecting the external auditors as well as choosing their fees is also one task of the audit committee.

3.8. Transparency & Disclosure

Recalling the Enron[52] scandal from the year 2001, it was found out that the firm´s financial health was sustained by willful and creatively implemented accounting fraud. Enron created so-called offshore entities which were partly used to avoid taxes and to pretend the company was generating profits while the firm was losing money. Resulting from this, the financial statements of the firm did not include any information about debts or losses. The price of Enron´s stocks dropped from $90 to just a few pennies over night. The scandal of Enron can be seen as the perfect example of how critical and important transparency is.

Financial transparency and disclosure are one of the most important and inevitable elements of a good corporate governance system. Shareholders, stakeholders and other participants in a market want to know what is going on inside the company. Those companies which do have a high level of transparency are also more highly rated and valued by investors. Firms, which neglect or fall short of this important point risk, damage the credibility of the management. Setting up transparency and disclosure guidelines or a policy is usually done by the board. Implementing, however, is the work of the firm´s management. This best

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52 Enron was one of the world´s leading energy company, based in Houston (Texas)

practice is realized by most of the banks and companies throughout the MENA region (80.6%).[53]

3.8.1. What is being disclosed?

The company´s corporate governance should make sure that all necessary information regarding the corporation are disclosed timely. Listed companies in the MENA region are required by law to publish its financial and non-financial situation on a regular basis. This can either be done quarterly, semi-annually or annually.

Financial disclosure

The financial disclosure of a firm includes all the financial information that arise within the company. This covers the bank´s or company´s balance sheet, income statement, cashflow statement, statement of equity and additional notes to the statements. There exist certain capital market regulations that enforce both banks and companies to adhere to. Non-compliance with those requirements is sanctioned.

Most of the banks and companies in the MENA region publish their financial information through the local press (94.7%) and in the general assembly (93.4%). 88% of the surveyed banks and companies stated that they disclose it in the annual report and 85.9% use their website for publishing the relevant information.[54]

Non-financial disclosure

Non-financial information include everything from board composition, ownership and voting rights, general corporate governance information, operating results, company objectives, dividend policy, remuneration, other relevant policies etc. As the legal requirements for this kind of information are insufficient in the region, we can see that the disclosure is weak among banks and companies. However, firms promise to send the

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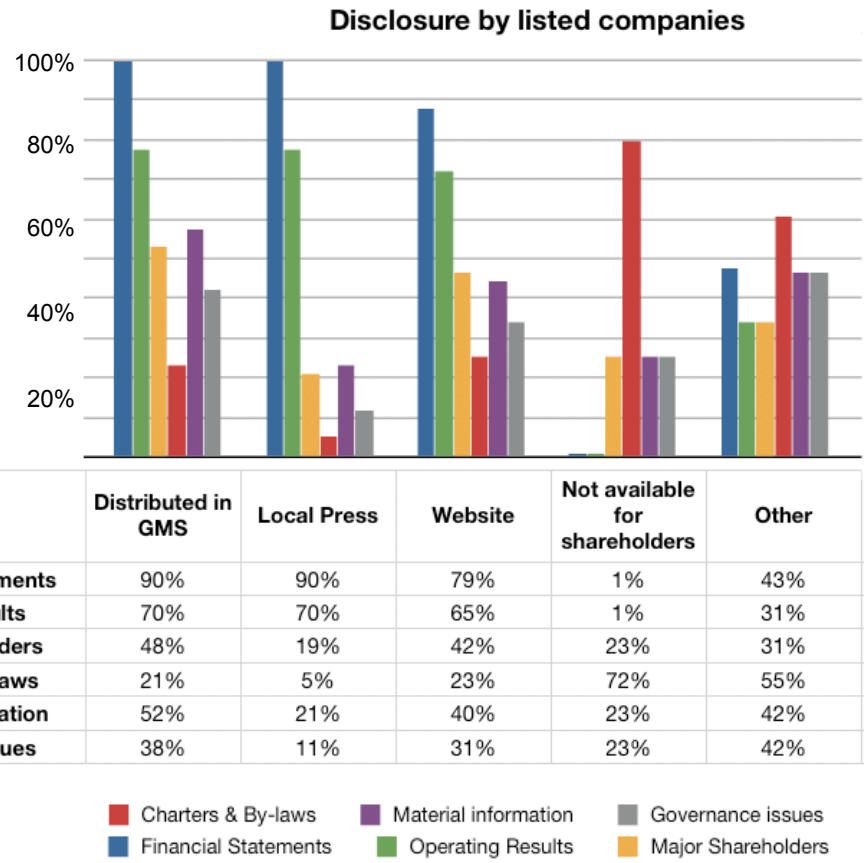
53 Hawkamah (2008), Corporate Governance Survey, p. 54

54 Hawkamah (2008), Corporate Governance Survey, p. 49

requested data upon request. Having a look on the following graphs we can see where banks and companies disclose their relevant information in the MENA region.

Figure 7: Which information is being disclosed?



	Distributed in GMS	Local Press	Website	Not available for shareholders	Other
Financial Statements	90%	90%	79%	1%	43%
Operating Results	70%	70%	65%	1%	31%
Major Shareholders	48%	19%	42%	23%	31%
Charters & By-laws	21%	5%	23%	72%	55%
Material information	52%	21%	40%	23%	42%
Governance issues	38%	11%	31%	23%	42%

	Distributed in GMS	Local Press	Website	Not available for shareholders	Other
Financial Statements	94%	96%	88%	10%	42%
Operating Results	74%	78%	88%	21%	54%
Major Shareholders	57%	38%	52%	21%	31%
Charters & By-laws	30%	6%	22%	21%	42%
Material information	54%	30%	43%	52%	52%
Governance issues	35%	10%	32%	65%	77%

More and more banks and companies use the internet for publishing their financial and non-financial data. A slight difference between banks and companies is noticable - namely that banks use the internet more often for publishing their annual reports than do listed firms. Regarding non-financial information, the extent to which they are disclosed is rather weak compared with the financial information - for both banks and listed companies. Banks seem to be more transparent than companies in publishing non-financial data.

It is not only important which data to disclose, but also how to publish them. Financial and non-financial data should be disclosed in compliance with certain quality standards of disclosure. The most common standard in this point is the so-called *International Financial Reporting Standard* (IFRS) which has the aim to improve the quality, transparency, reliability and comparability of such information and therefore to make financial information comparable to various countries. 59.6% of banks and companies in the Middle East and North African region stated that their disclosure policy follows the IFRS. The majority, however, discloses information along certain local standards, and only 4.6% report according to US GAAP. Nonetheless, many countries in the MENA region still have not adopted the IFRS completely yet.[55]

3.8.2. Any barriers preventing disclosure?

There exist several reasons why firms and banks do not fully implement or realize best practice regarding disclosure in the Middle East and North Africa region. For instance, one main reason for firms and banks not to adhere to several disclosure rules is that there is no legal requirement. 76% of banks and 69% of firms state that this is one explanation that prevents disclosure. Other possible reasons - also stated by the surveyed participants - are that there is no demand to disclose all the necessary data (37% banks, 33% firms), no economic value for the bank or firm (34%

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55 Hawkamah (2008), Corporate Governance Survey, p. 53

banks, 29% firms) or certain security issues (7% banks, 12% firms). Only 4% of the firms see the lack of resources inside the company as means that prevent proper disclosure.[56]

3.9. Shareholder rights

Shareholders represent the owners of a public corporation. It is in their interest that the management of the firm acts on behalf of them. They generally enjoy certain rights like

- voting rights on corporation issues in the general assembly;
- transfer shares;
- receiving dividends as declared by the board;
- having insight into the books and financial records;
- sharing proceeds in case company got liquidated etc.

It is important that the interests of both the shareholders and the directors align and that the shareholders are treated equitable. However, this does not mean that each shareholder is treated the same way. As there are larger and smaller shareholders, everyone has different interests in the company and may also have different goals. Nevertheless, the directors have to ensure that each shareholder is treated fairly, namely with equal regard and respect.

As mentioned before, one right shareholders enjoy is the right to participate in the general assembly of the corporation. They should be interested in what is going on in the company. The majority of banks and listed companies throughout the surveyed region confirmed high shareholder attendance rates (33% of all shareholders) during the last meetings.[57]

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56 Hawkamah (2008), Corporate Governance Survey, p. 55

57 Hawkamah (2008), Corporate Governance Survey, p. 56

As mentionend before, shareholders are the owners of a corporation. The more shares a shareholder possesses, the greater are his rights and the greater is his power inside the company. This implies that small shareholders - so called minority shareholders - may have difficulties to exert their rights in their interests. They may see that the company is run in the interest of majority shareholders rather than by the minority. In a country where we find effective shareholder rights systems there is no chance for big shareholders to cheat on the small ones. However, there are some ways in which the majority shareholders may favour themselves regarding certain topics in the company. For protecting the minority shareholder in the Middle East and North African region, we find two rights which are dominant. Firstly, the protection through pre-emptive rights and secondly, the use of tag-along rights. Through the practice of those two rights, shareholders are treated equally.

Whenever a corporation issues new shares, the use of pre-emptive rights allow a shareholder to maintain his or her proportion of ownership. If this had not been the case, the percentage of ownership would be diluted. Most of the corporation laws in the MENA countries do have such pre-emptive rights.[58] Furthermore, existing shareholders of a firm do have a higher priority when buying new shares than new shareholders.

The second type of rights minority shareholders have are the so-called tag-along rights. They represent a contractual obligation for protecting the minority´s rights. Whenever a majority shareholder sells his or her stake of the company, then the minority shareholders also have the right to join them by selling their stakes under the same conditions (e.g. at the same price). The figure below showes the percentage of banks and listed companies which do have such tag-along rights in use (Figure 8).

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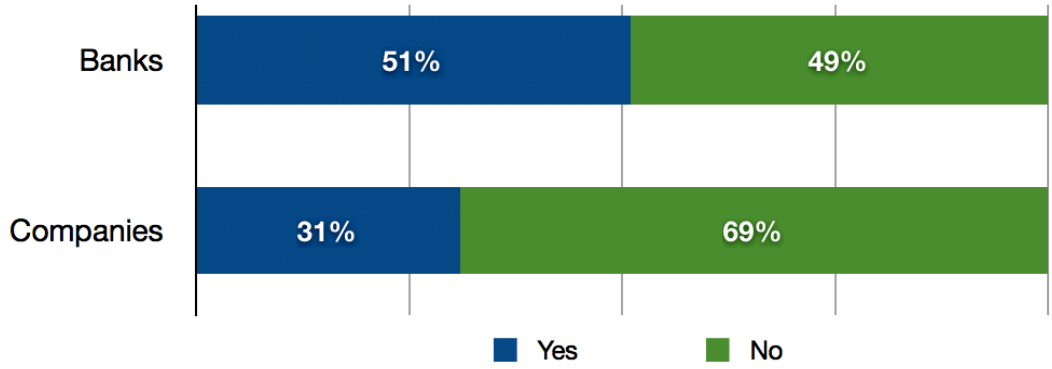
58 Hawkamah (2008), Corporate Governance Survey, p. 60

Figure 8: The use of tag-along rights in the MENA region



Source: Hawkamah (2008), Corporate Governance Survey, p. 60

As we can see, around half of the banks protect their minority shareholders through tag-along rights, whereas only 31% of listed companies do have such rights.

In the chapter about disclosure and transparency the necessity of publishing relevant information about the company is described in detail. Concerning the rights of the shareholders, it is best practice to provide them all necessary information about the company at the right time. As the shareholders are participating in the general assembly, they should be informed in an adequate time prior to the assembly so that they have enough time to prepare for it. They should have time to read the agenda, to think about voting items, to make arrangements concerning the assembly and more. It is recommended to provide this information at least 20 days before the general assembly. In the MENA region, banks follow this best practice more than the listed companies. In detail, about 55% of banks provide all relevant information to the shareholders at least 20 days prior the meeting, whereas only 22% of listed companies do so. The majority of listed companies distributes its information 15 days before the assembly (75%).[59]

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59 Hawkamah (2008), Corporate Governance Survey, p. 61

The majority of all surveyed banks and companies (80%) include all the necessary information for their general assembly to the shareholders; namely the agenda, time and place, the annual report, instructions for the proxy voting, report of the external auditor, financial statements and some additional information on the agenda.

4. Family power in the MENA region

The economy in the MENA region - especially in the gulf region - is partly controlled by families. Many prominent families like the Qassimi and the Maktoums in the United Arab Emirates have family members[60] sitting on the boards of companies. The family concentration in the GCC region seems to be quite high. The numbers vary from country to country. There should be some limitations regarding the maximum board seats held by one family in a company. Most of the GCC regions do not have more than 50% or 60% of the boards being occupied by the same family. For example the highest percentage of seats held by one family in Dubai is 50%, in Abu Dhabi 66.7% and Saudi Arabia 75%. The only country which does not seem to pay attention to good governance practices regarding this issue is Kuwait. Some companies in Kuwait do have boards where all seats are held by one single family.[61] In general, between 19% and 30% of board seats are occupied by family members in the GCC region.

It is interesting to see to which extent families control companies. In regions like Dubai, Oman or Kuwait around 15% to 20% of the firms are controlled and influenced by the „Top 10 families“[62] in this area. In Qatar, the „Top 10 families“ controll nearly up to 50% of all firms. Surveys also show that prominent families which are usually thought of leading a country or emirate, seem to be absent in boards. The table (Figure 8) gives an overview of some prominent families in the gulf region and the number of seats they occupy.

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60 Family members involve all persons with the same surname.

61 Hawkamah (2008), Power matters: A survey of GCC boards, p. 21

62 weighted by market value of board seats

Figure 8: Family overview GCC region

Region	Family	Number of seats held by prominent family	% of all board seats
Abu Dhabi	Nahyan	6	1,3%
Bahrain	Khalifa	9	2,2%
Dubai	Maktoum	4	1,5%
Kuwait	Sabah	45	4,1%
Oman	Bu‘ Saidi	15	1,5%
Qatar	Thani	78	24,2%
Saudi Arabia	Saud	5	0,6%

Source: Hawkamah (2008), Power matters, p. 23

Except of the Thani family in Qatar, all other families only hold a very little amount of the total seats in their region. Of the 38 listed companies in Qatar, the Thani family has a board seat on 29 firms. We can say that the Thani family is present in more than 76% of all firms in Qatar.

Another surprise is that the Qassimi family in the United Arab Emirates (which governs the smaller emirates Ras Al Khaimah and Sharjah) nearly owns 8% of all board seats in the UAE - that is close to three times more than the Maktoums and Nahyan own together.

A study from Nowak, Erhart and Weber (2006) confirmed that family owned enterprises (FOE) outperform non-family business in terms of sales, profits and other measures.[63] The reasons are a strong commitment to the business through the family members, trust and reliability among the members, passing the knowledge and experience from one generation to another.

63 Nowak, Ehrhart, Weber (2006)

However, many family business fail for several reasons during the third or fourth generation of ownership. Due to a probably poor management, insufficient cash, no adequate controlling and monitoring and other conditions it might be recommendable for FOE´s to think about a serious corporate governance. Referring to the Hawkamah Institute in Dubai, establishing a so-called family constitution is a good way to improve a FOE´s business processes by setting the family´s core values, vision and goal of its business. In addition to that, it should also be defined who is responsible for which task, compositions of boards, succession plans and a family member employment policy. In general, such a family constitution is a good way to distinguish between the interests of the family and the company. In the MENA region, 50% of the listed companies stated that they have such a family constitution in use. On the other side, no bank has set up such a constitution. Banks usually have to follow strict regulations regarding the ownership structures and therefore maybe would not benefit from such a policy.

The development of a family member employment policy should also not be thrown in the wind. The performance of a FOE can suffer essentially in case the company did not set up an employment policy which regulates how many family members the company should hire or how many employees are needed. A too large number of members in the company can lead to a company´s downfall. Ensuring that every family member has a position within the firm is not desirable for a smooth working and efficient company. The majority of family-owned banks (67%) and family-owned companies (75%) stated in the survey that they have family employment policies for members who wish to apply for a position.[64]

In many cases, the position of the CEO in banks and listed companies throughout the MENA region is held by a family member. More detailed results are represented in the following graph (Figure 9).

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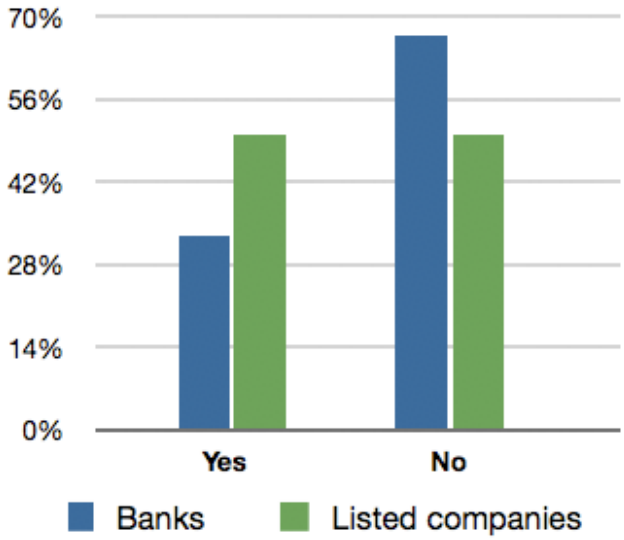
64 Hawkamah (2008), Corporate Governance Survey, p. 71

Figure 9: CEO position held by family member?



Source: Hawkamah, Survey of Corporate Governance, p. 71

5. Women on boards

The situation of women in the MENA region is not the same as in the western countries. The results of surveys regarding the situation of women in the boards of companies in the Middle East and North African region are not surprising. However, it is interesting to see to which extent women are participating in the economy. According to the survey of the Hawkamah Institute, 63 board seats are held by women; that´s 1.5% of a total of 4,254 seats. In America, the percentage of women represented in the boards is between 13% and 19% - depending on the business sector.[65] As the statistics only involve the gulf countries, it is interesting to see that Oman and Kuwait have the highest rates of women on boards (2.3% and 2.7%). It is not surprising that Saudi Arabia faces the lowest rate with 0.1% female participation. In Europe, rates also differ between the countries. Norway is the leader with 22% women on boards, Italy and Spain the laggards with just 3%.[66]

Reasons for the rather low representation of women in high positions can be found in the social and cultural structure of the countries. Those having a strong patriarchal society tend to have a low rate of women in the economy (e.g. Japan). Also the religious beliefs do have an influence on the female participation rates. This is an explanation for the low rates in Italy and Spain. Those countries have a high concentration of Catholics (more than 95%) and therefore a low female rate compared to other European countries. Islamic countries show a similar result.

But it is not always the social or cultural structure that explains the female representation in the economy. In Norway, for instance, the law states that at least 40% of the directors have to be occupied by women.

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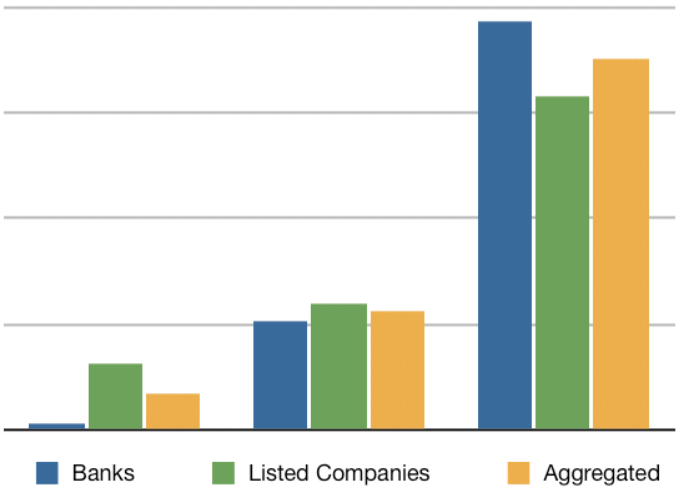
65 More info at www.catalyst.org - Expanding Opportunities for Women and Business (Dec 2008)

66 Hawkamah Institute (2008), Power matters: A survey of GCC boards, p.14

However, we see that there are large discrepancies in the gulf countries. Participation rates go from 0.1% in Saudi Arabia to more than 2.7% in Kuwait; even higher than in some south-european countries. The key parameters explaining the differences in the various countries are social and religious factors. The graph gives an overview over what has been said about the gulf region (Figure 10). The majority of the firms has no women on board.

Figure 10: Women on boards in the MENA region



	2 to 5	1	0
Banks	2%	21%	78%
Listed companies	13%	24%	63%
Aggregated	7%	23%	70%

Source: Hawkamah, Survey of Corporate Governance, p. 32

6. Conclusion

The importance of good corporate governance practices and rules shows a steady increase during the last years due to business scandals, which occurred all over the world. Managers and boards of companies have to be aware of the fact that such governance guidelines are inevitable for a stable and efficient growth and performance of a firm. It is not only the company itself which benefits from the implementation of sound governance codes, also possible investors and the public sector are interested in their development, as well as other stakeholders of the firm like banks, suppliers and employees.

The basic intention behind this process in the Middle East and North Africa (MENA) countries is to strengthen their market economy and to encourage further private investments in future by focusing on the implementation of corporate governance rules.

The results from a survey which has been carried out by the prominent Hawkamah Institute in Dubai proved that corporate governance codes are still not fully understood and developed by the managers in the Middle East and North Africa region. Banks and firms are still at the beginning of this complex implementation process.

The fields which are usually covered in the corporate governance practices range from the board of directors, shareholders´ rights and executive compensation over to financial disclosure and auditing. Factors like board composition, board size and board meetings all contribute to the performance of a company.

Financial disclosure can be seen as one of the most important matter in this corporate governance discussion. It is in the interest of investors, banks, suppliers and employees to get access to relevant data like financial statements. As mentioned in the beginning, aligning the interests of the shareholders and the management is one major task of corporate governance. Shareholders enjoy certain rights like voting rights, receiving

dividends and having insight into the books and financial records. Minority shareholders should be protected by so-called tag-along rights which are still not fully established in the Middle East and North Africa region.

Looking at the economy in the gulf region, we notice that many board seats in companies and banks are occupied by prominent family members. Families like the Maktoums and the Qassimi in the United Arab Emirates have members sitting on the boards of big companies. However, we see that the number of seats being occupied by one family is rather small compared to the total number of board seats in this area. A too high number of members of the same family clan can lead to a company´s downfall. It should not be the strategy of a firm to provide every family member a position within the company.

The situation of women in the MENA region is not the same as in the western countries. However, statistics show that some Arab countries do have higher female participation rates on boards than some European countries. Saudi Arabia faces the lowest rate with only 0.1% female participation. Reasons for the rather low participation of women in high positions can be found in social and cultural structures of the countries. Also the religious beliefs do have an influence on the female participation rates.

The results which have been explained in this thesis vary from good developed corporate governance practices in some listed companies and banks to less developed ones in the surveyed area. It takes time to establish such a corporate governance framework in the Middle East and North Africa region as this is a very complex and sophisticated process.

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8. Figures

Figure 1 (p. 4) Overview five elements of good corporate governance

Source: A Corporate Governance Survey across the MENA countries, 2008, p. 11

Figure 2 (p. 11) Overview GDP and market capitalization

Source: Worldbank (http://econ.worldbank.org)

Figure 3 (p. 18) Implementing the five pillars of good corporate governance

Source: A Corporate Governance Survey across the MENA region (200), p. 18

Figure 4 (p. 25) Overview board meeting frequency of listed companies and banks in the MENA region

Source: A Corporate Governance Survey across the MENA region (200), p. 35

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Source: Power matters: A Survey of GCC boards (2008), p. 19

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Source: A Corporate Governance Survey across the MENA region (200), p. 37

Figure 7 (p. 37) Disclosure by banks and listed companies: Which information is being disclosed?
Source: A Corporate Governance Survey across the MENA region (200), p. 50

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Source: A Corporate Governance Survey across the MENA region (200), p. 60

Figure 9 (p. 44) Family overview GCC region
Source: Power matters: A survey of GCC boards (2008) p. 23

Figure 10 (p. 46) Is the CEO position held by a family member?
Source: A Corporate Governance Survey across the MENA region (200), p. 71

Figure 11 (p. 48) Women on boards in the MENA region
Source: Power matters, A Survey of GCC boards (2008), p. 32

9. Charts

Chart 1: Distribution of banks and listed companies included in survey by country and total number of listed companies in MENA region[67]

	Included in Survey			
	Non-listed banks	Listed banks	Listed companies	Total Number of listed companies MENA region
Bahrain	1	6	41	56
Egypt	21	17	125	448
Jordan	13	2	204	253
Kuwait	1	6	164	207
Lebanon	0	0	9	30
Morocco	5	0	52	80
Oman	1	5	139	160
Saudi Arabia	2	9	71	128
Tunisia	5	9	35	67
UAE	5	7	57	131
WB & Gaza	3	4	25	37
Total	57	65	922	
	Total 1044			**Total 1597**

67 Data taken from Worldbank http://econ.worldbank.org (March 2009)

10. Curriculum Vitae

EDUCATION

October 2004 until March 2009 *University of Vienna*

- Master in International Business
  Majors: Corporate Finance
  Controlling
  International
  Management

  Thesis: Corporate Governance in
  Arab Countries

- Master in Arabic Studies

September 1998 until June 2003 *Technical College Pinkafeld*
Department “Electronic Data
Processing and Management”

Graduation with “excellent success”

September 1990 until June 1994 *Primary School Oberwart*

WORK EXPERIENCE

March until August 2009	**Henkel CEE, Vienna**
Internship Finance/ Controlling	• Responsible for monthly and quarterly financial reports for all CEE countries for the headquarters in Düsseldorf
August 2008	**Landesmuseum Innsbruck, Tirol**
Archaeological Assistant	• Excavations of a 2500 year old village and cemetery in Tirol
August 2006	**Henkel Egypt, Cairo**
Training Financial Analysis	• Responsible for monthly financial reports for headquarters in Düsseldorf • Analysis of rentability of newly introduced products on the Egyptian market • Calculation of balance sheet numbers for comparing Egyptian and German markets
August 2002	**Metropolitan Datenservice GmbH, Vienna**
Internship IT	• Programming of Graphical User Interfaces for the automatic creation of insurance contracts
July 2002	**mobilkom austria AG, Vienna**
Internship Postal Office	• Administration of the daily post of mobilkom austria

Since November 2005	mobilkom austria AG, Vienna
CS Data Management	• Administrative tasks with reference to residential and business clients • Distribution and processing of client offers • Training for new employees

LANGUAGES

- German Mother tongue
- English Proficient
- Arabic Good
- Egyptian Dialect Good
- Spanish Basics
- French Basics

TECHNICAL AND OTHER SKILLS

- CISCO Networking Program – Semesters 1 to 4
- Business English Certificate (University of Cambridge)
  →Graduation with “Grade A”
- Programming languages: C, C++, Java, HTML, MatLab
- Basis knowledge: SQL, PL/SQL
- MS Office, Windows, Mac OSX, SAP R/3, Clarify CRM, Amdocs

PERSONAL SKILLS

- September 1990 to June 1998 - School of Music Oberwart
  → 8 years education on instrumental drums

HOBBIES

- Traveling, Sport, Music, Cooking, Reading, Friends

DRIVING LICENSE

- Class A, B