Strengthening Corporate Governance Practices in Thailand

Joint Report of the Thai Institute of Directors and McKinsey & Company Thailand

In Collaboration with
The Stock Exchange of Thailand
The Office of the Securities and Exchange Commission

McKinsey&Company

IOD Thai Institute Of Directors Association

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*Included on enclosed CD-ROM

Preface

This report, Strengthening Corporate Governance Practices in Thailand, presents the findings of a joint study by the Thai Institute of Directors and McKinsey & Company Thailand. It was developed in collaboration with The Stock Exchange of Thailand and the Office of the Securities and Exchange Commission.

The Thai Institute of Directors (Thai IOD) : The Thai IOD was established in December 1999 with a mission to develop and support company directors in their efforts to implement good corporate governance. During the past two years, the IOD has provided regular training and professional development programs. One of the key training courses is the comprehensive Directors Certification Program, which provides company directors with the essential skills to carry out their duties effectively. The institute also conducts research related to corporate governance issues in order to support directors and provide input to regulatory agencies in formulating policies related to corporate governance. This baselining survey is one such effort.

McKinsey & Company : McKinsey & Company is a leading global management consulting firm that helps its clients make distinctive, lasting and substantial improvements in their performance. Over the past seven decades, the Firm's primary objective has been to serve as an organization's most trusted external advisor on critical issues facing senior management. With nearly 7,000 consultants deployed from 84 offices in 43 countries, McKinsey advises companies on strategic, operational, organizational and technological issues. McKinsey has had a permanent office in Thailand since 1996, staffed predominantly with Thai professionals well trained in the Firm's best practice consulting methodologies and frameworks. McKinsey also has a dedicated Corporate Governance Practice that has conducted extensive research on governance practices around the world.

The Stock Exchange of Thailand (SET) : As described in Vision 2003, the SET's mission is "to be one of the most attractive capital markets in Asia by providing quality products, representing the Thai economy truthfully, employing effective risk management tools, and complying with international standards of enforcement and corporate governance." In order to achieve this vision, the SET aims to encourage the implementation of good corporate governance

practices among market participants, to ensure the quality of its products, and to provide effective investor protection. The SET is sponsoring a number of academic and business seminars, and is releasing guidelines to promote a more thorough understanding of good governance. As part of its commitment to promoting good corporate governance in Thailand, the SET has agreed to support this baselining survey.

The Office of the Securities and Exchange Commission (SEC) : The SEC's mission is to develop and supervise the Thai capital market to ensure its efficiency, fairness, transparency and integrity. Strengthening corporate governance in listed companies is a key element in fulfilling this mission. During the past several years, the SEC has undertaken various efforts to encourage better governance of listed companies, especially through regulatory measures, legal amendment proposals, educational programs, and incentive schemes. The SEC is also a supporter, financial and non-financial, of the forthcoming Investors Association, the Thai IOD, and the current corporate governance baselining project. The baselining survey fits well with the SEC's objectives, and its findings will benefit not only investors but also regulators, who will be able to better identify areas for improvement and undertake more focused planning of efforts to strengthen corporate governance practices.

The Faculty of Business at the Asian University of Science and Technology conducted the data gathering and analysis for the initiative, ***supported by an ASEM grant from The World Bank (Grant No. TF 024686).***

Asian UST : Asian University of Science and Technology is a new international university located in Chonburi, Thailand. The University, with lecturers from around the world, offers programs in business and engineering with English as the main language of instruction. The Faculty of Business offers undergraduate programs leading to the BBA degree with concentration in Accounting, Economics, Finance, Management, Marketing, and MIS. The University also offers an MBA Program to full-time and part-time students. Finance faculty members have done extensive research on corporate governance in East Asia and have published their work in reputable finance journals, such as the Journal of Financial and Quantitative Analysis, the Journal of Financial Research and the Journal of Financial Markets.

Throughout the report, the authors have referred to other McKinsey & Company surveys and research on corporate governance. For example, the often quoted *McKinsey & Company Investor Opinion Survey 2000* presents the perspectives of 84 global institutional investors with over US$1 trillion in assets under management. And the recently completed research project, *Using Global Standards to Enhance Value*, assesses corporate governance practices in six emerging market economies: India, Korea, Malaysia, Mexico, Taiwan, and Turkey. While this research has not yet been made public, the authors have used some elements to provide a comparison with Thailand.

We wish to express our sincere gratitude to Mr. Chavalit Thanachanan, Chairman of The Stock Exchange of Thailand (SET) and of the Thai IOD, Mr. Prasarn Trairatvorakul, Secretary-General of the Office of the Securities and Exchange Commission, Mr. Vicharat Vichit-Vadakarn, former President of the SET, and Mr. Kittirat Na Ranong, President of the SET, for their guidance and support. We would also like to thank Mr. Pakorn Malakul Na Ayudhya, Chairman of the IOD's Corporate Governance Benchmarking Committee and all committee members for their valuable comments on the methodology and criteria. We are equally grateful to the members of the Steering Committee and the Working Team for their contributions to this project. Finally, we would like to thank The World Bank for providing support through the ASEM Grant for the data collection and analysis.

We welcome questions and comments related to the research methodology as well as the specific findings.



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Executive summary

The Thai Institute of Directors (Thai IOD) and McKinsey & Company Thailand, in collaboration with The Stock Exchange of Thailand (SET) and the Office of the Securities and Exchange Commission (SEC), jointly launched an effort to baseline governance practices of the top publicly listed Thai companies. The initiative's objective was to encourage the adoption of best practices in governance by systematically evaluating current practices.

The baselining evaluation focused on the top 100 listed companies in market capitalization on the SET and also included a sample of all listed companies in the food and electronics sectors. The evaluation used both international standards in governance and the recently published SET guidelines, ***The Report on Corporate Governance.*** Specifically, the research evaluated companies' governance practices in five key areas:

- Rights of shareholders,
- Equitable treatment of (minority) shareholders,
- Role of stakeholders,
- Disclosure and transparency, and
- Board responsibilities.

The key findings of the baselining evaluation fell into four categories:

Financial importance of corporate governance: A statistically significant, positive correlation was found between a company's market valuation[1] and the quality of its corporate governance, suggesting that improving governance practices may benefit stock performance.

Strengths of Thai companies: Thai companies generally performed well in terms of their board practices and in protecting the rights of their shareholders – for example:

- 76% of surveyed companies had a board with a majority of non-executive directors.
- 68% of companies had boards that were 25-50% independent directors.
- 22% of companies had an independent chairman, compared to 15% in the United States.

[1] Specifically, the company's market-to-book ratio.

- 87% of firms allowed adequate time for shareholders to ask questions at the annual general meeting (AGM), and 76% of companies had their chairman present at the AGM.

Development opportunities: Despite the strengths described above, Thai companies could still improve their performance in the areas of equitable treatment of (minority) shareholders, disclosure and transparency, and stakeholder roles – for example:

- Only 10% of companies had a mechanism, such as cumulative voting, to enable minority shareholders to influence board composition.
- Just 11% of companies used analyst briefings or press conferences to communicate with their shareholders.
- Only 19% of firms explicitly mentioned the safety and welfare of their employees in their governance framework or annual report.

Range of corporate governance performance: Overall, there was a wide disparity in the quality of corporate governance practices in the surveyed companies. However, in every category, examples of best practice companies were found, meaning that Thailand has numerous domestic role models to draw upon in pursuing broad-based improvements in corporate governance.

Baselining results for individual companies will not be made public. It is not the intention of the authors of this report to publicly compare individual companies but rather to provide a benchmarking tool that helps firms improve their corporate governance. Companies can obtain their individual feedback report from the Thai IOD. The report includes the company's overall score and its scores in the five evaluation categories.

The evaluation's aggregate findings will provide important input for Thai companies, policymakers, and the public to identify a path towards improved corporate governance practices. The Thai IOD intends to repeat the evaluation in the future to monitor improvement and to provide a tool to continually identify weaknesses and required areas of focus.