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INSTITUTIONAL INVESTORS AND CORPORATE GOVERNANCE

Empirical study

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Segment reporting
Transparency

JEL Classification:
G32, M41

Abstract

This study aims to review previous developed studies regarding the institutional investors' issue, as the influence they exert in the companies they invest in is growing in importance. In the first part, the paper tries to review the existing literature regarding the institutional investors' research theme, especially regarding their attitude towards investment, while the second main part will try to describe the presence of institutional investors in Romanian listed companies. Also, the paper aims to review previous studies regarding the influence of institutional investors over corporate governance mechanisms (especially board's members' independence and composition) and financial and non-financial disclosure practices.

1. Introduction

Corporate governance is a concept that has begun to preoccupy more and more worldwide researchers, gaining a very important place in those companies whose main concern is business excellence. The subject of corporate governance has become of a great importance, especially after a series of economic scandals which have led the investors to lose their confidence in managers' ability to best lead the great corporations and public institutions (Cheffins, 2012).

Corporate governance has developed in the context of agency and informational problems which occur in all organisations. Agency problems arise when a part, usually the manager, stops acting in the interest of the investor, but in its own interest. Feleaga (2005) brings into discussion that a fragmented ownership and the increase of the companies have led to the reduction of the investors' power, allowing managers to act according to their interests and to control as they wish the policies of the companies, producing in this manner a concrete separation between ownership and control.

There are two views of what corporate governance means. In a shareholder view, corporate governance is the way how funds suppliers ensure that they will get proper remuneration for the investment made. On the other hand, in a stakeholder view, corporate governance represents a set of institutional and organisational mechanisms whose purpose is to separate power, influence managers' decisions and to reduce their discretionary space (Feleaga, 2010).

Corporate governance is an extremely rich field of study, situated between management, finances, accounting, law, generating a lot of interesting study themes. One of the most important research themes analyses the influence that institutional investors exert over the corporate governance companies choose to implement.

2. Institutional investors

Institutional investors are usually pension funds, insurance companies, banks whose purpose is best investing other persons' funds, having towards them the fiduciary obligation of closely monitoring the companies they invest in but also taking all the necessary measures to protect them against the loss of value but also to ensure this value follows an upward trend (Mallin et al., 2005).

Specialized foreign literature (Ertuna and Tukel 2013, Kirkpatrick and Jesover, 2005, Feleaga, 2005 Bushee, 2004) identifies a number of attitudes and processes through which institutional investors optimize corporate governance mechanisms. Some authors (Carcello et al., 2011, Bushee, 2004) point out that there is often a temptation to treat all investors as a 'homogeneous mass', although their attitudes are different depending on different situations.

For example, Carcello et al. (2011) tries to differentiate the attitude of the so called *blockholders,* who can be founders of companies or individuals who invest large amounts in one company, of the attitude an *institutional investor* - insurance company, pension fund, financial investment company, etc- must have in a company.

Over time, studies have shown that in contrast to individual investors, institutional investors often have another investment attitude, more sophisticated, protecting their investment in a more professional way, from this point of view being more important to study the influence they have on the corporate governance of companies they finance.

Moreover, specialists OECD (2011) noted that attitude towards risk and how institutional investors act is often influenced by the commitments they have made to those whose savings they manage, but it also depends on the industries in which companies operate. Feleagă (2005) mentions that in the case the investor is not satisfied with the way his investments are managed, his attitude may be an *exit* type one, for example to carry out the sale of its shares or to take a *voice* type action , trying to improve business practices, using his right to vote.

This idea is supported by Bushee (2004), which states that the so-called transient investors will be interested in short-term gains, avoiding encouraging management in supporting research and development projects, while long-term investors are tempted to use their influence to determine and intervene in optimizing the long-term business of the companies in which they invest in.

The first influence that institutional investors can have on companies is one slightly atypical, being a direct influence. Ertuna and Tukel (2013) shows that in an attempt to attract more institutional investors and thus attract additional capital, companies in countries with less developed governance principles have improved the quality of annual reports by increasing the information given voluntarily, and therefore the level of transparency.

Regarding the direct influence of the institutional investors in companies, while Scott (2011) suggests that institutional investors can improve research and development policies of the companies in which they invest, and remuneration policies of managers, Kirkpatrick and Jesover (2005) extend the area of influence of institutional investors to interventions in the company's strategic decisions, investments, sales of assets, remuneration of the managers and board composition by increasing the number of independent members, but also lobbying for legislative changes in areas such as procurement of companies.

Many of these studies, however, are placed in certain countries or institutional contexts, that is why it can be concluded that the level of knowledge is quite fragmented at an international level. Moreover, this issue is just recently being studied in Romania (by Feleagă, 2005). Corporate governance in our country appears conceptually and only regular in the early 2000s, the delay being motivated by delays in implementing effective reforms in the political, economic, legal and social environment (Feleaga et al., 2010). This is why researchers began to pay in increasingly more attention to understanding governance practices assimilated by Romanian companies, but also trying to identify the best means by which all stakeholders, especially investors, ensure that their interests were protected by those who lead companies.

That is why I tried to identify to what extent institutional investors in Romanian listed companies get involved in the companies they invest in, assessing to what extent they can ammeliorate corporate governance issues.

The next part of the paper will review previous studies I developed regarding various corporate governance and transparency issues and the influence institutional investors had over them.

3. Empirical results

First of all, analysing the 2012 annual reports disclosed by 15 non-financial companies listed in the first tier of Bucharest Stock Exchange it resulted that 88% of the analysed companies have institutional investors, in these companies the average percentage held by institutional investors in a company's equity being of 45%.

Insert table 1 here

Even though the largest percentage held by institutional investors in a company's equity is of 88,42%, the large value of standard deviation has led us to the conclusion that there are great disparities among these companies, being obvious that diverse number of institutional investors exert different types of influence over corporate governance practices and mechanisms.

Even though these results confirm the fact that institutional investments are just beginning to develop in our country, in-depth analysis have more promising results, as follows.

In another study (Albu et al., 2013), we discovered the fact that the presence of institutional investors has a positive impact on segment disclosure practices. Even though companies in our country have recently implemented IFRS, it seems that the expertise institutional investors have and the importance they give to sound segment information influenced companies they invest in to disclose high quality segment information.

Insert table 2 here

Another study we developed (Albu et al, 2014) has confirmed the results obtained in Turkey bu Ertuna and Tukel (2013), namely that institutional investors have a positive impact on the quality of the financial statements and the annual report disclosed by the companies they invest in.

Insert table 3 here

In a more in-depth analysis, we discovered the fact that in Romanian listed companies, institutional investors have a positive impact especially on the disclosure of voluntary non-financial information (subsidiaries, impact on the environment, intellectual capital, CSR) and, as we expected, they exert a positive influence over corporate governance issues, such as presentation of corporate governance information, shareholders rights, the existence of a company corporate governance code, the disclosure of the Comply or Explain statement and others.

Insert table 4 here

Even though we expected to seize a positive relation between the presence of institutional investors and the size and composition of the companies' boards, the Pearson correlation showed no connecction between those indicators, being a sign that there are more changes to be done regarding the influence institutional investors should and really exert over the companies' boards, as the importance of an independent board is increasing more and more nowadays.

4. Conclusions

The issue of corporate governance has become of a great importance nowadays, especially in those companies whose objective is business excellence. Given that the influence of institutional investors is increasing in those companies they invest in, it is of a great importance to exactly understand in which areas do they have the power and expertise to intervene in.

Several empirical studies previously developed by us regarding the institutional investors' influence in Romanian listed companies have shown that they are interested in building a sound financial and non-financial disclosure system, paying great attention to segment reporting, but also to disclosing high-quality non-financial information, especially to presenting useful information regarding the corporate governance mechanisms implemented in the companies they invest in.

It is very important to continue studying the behaviour of institutional investors especially in emerging countries, as the institutional investments are growing day by day.

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APPENDIX

Table 1
Descriptive statistics for institutional investors' presence

	Min	Max	Average	Median	StDev
Institutional investors	0	88,42	45,10	54,81	31,41

Source: Author's research

Table 2
Regression results

	IFRS 8 compliance level
Size	-0,457
Auditor	1,436*
Growth	0,37
Ownership diffusion	-1,728**
Institutional investors	1,021*
Leverage	-0,43
Profitability	-1,107
F-value	4,034**
Adjusted R-square	0,603

Source: Albu, C.N, Albu, N., Mateescu, R., "Analiza practicilor de raportare pe segmente – cazul societatilor cotate la BVB" [Segment reporting practices analysis- The case of BSE listed companies]

Table 3
Correlation results between general scores and firm-level factors

Variables	auditor	size	growth	ownership	institutional investors	leverage	profitability	international sales	TRANSP
auditor	**1**								
size	**0.716*****	**1**							
growth	0.000	0.028	**1**						
ownership	-0.431	**-0.502***	0.107	**1**					
institutional investors	0.111	0.422	0.289	-0.185	**1**				
leverage	0.345	-0.137	-0.239	-0.255	**-0.518****	**1**			
profitability	-0.272	-0.116	0.354	0.075	0.272	-0.423	**1**		
international sales	0.389	0.433	-0.067	-0.431	0.324	-0.242	0.079	**1**	
TRANSP	0.346	**0.675***	0.252	-0.256	0.298	-0.223	-0.095	0.042	**1**
QUALITY	**0.602****	**0.552****	0.201	**-0.543****	**0.495***	0.249	0.232	0.432	0.371

*, **, *** Denotes significance at the 10%, 5% and 1% levels.

Source: Albu, C.N., Albu, N., Vasile, L., Mateescu, R., "Transparency and quality of financial disclosures. The case of Romanian listed companies"

Table 4
Correlation results between transparency sub-scores and firm-level factors

Variables	COMPLY	VOLUNT FIN	**VOLUNT NONFIN**	GENERAL	**CORP GOV**	PRESENT
Auditor	0.035	0.307	0.237	0.298	0.437	0.283
Size	0.412	**0.517****	**0.580****	0.424	**0.582****	**0.642*****
Growth	-0.136	0.177	**0.471***	0.092	**0.441***	0.055
Ownership	-0.397	-0.186	0.016	-0.335	-0.255	0.023
institutional investors	0.075	0.024	**0.559****	0.049	**0.493***	0.099
Leverage	-0.073	-0.160	**-0.571****	0.155	-0.113	-0.298
profitability	-0.132	-0.048	-0.106	-0.081	-0.094	0.061
international sales	-0.046	0.033	0.311	-0.227	0.078	0.029

*, **, *** Denotes significance at the 10%, 5% and 1% levels.

Source: Albu, C.N., Albu, N., Vasile, L., Mateescu, R., “Transparency and quality of financial disclosures. The case of Romanian listed companies”