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### Article information:

To cite this document:

Tarek Ibrahim Eldomiaty Chong Ju Choi, (2006), "Corporate governance and strategic transparency: East Asia in the international business systems", Corporate Governance: The international journal of business in society, Vol. 6 Iss 3 pp. 281 - 295

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# Corporate governance and strategic transparency: East Asia in the international business systems

Tarek Ibrahim Eldomiaty and Chong Ju Choi

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## Abstract

**Purpose** – This paper aims at discussing the determinants of strategic transparency and the governance structure of the East Asian firms. The relatively weak institutional infrastructure in East Asia raises the question about the adaptable governance structure and transparency in the East Asian firms.

**Design/methodology/approach** – The paper presents theoretical underpinnings of the literature on corporate governance, corporate strategy and international business. This paper argues that one of the common factors that determine the success of corporate governance structure is the extent to which it is transparent to the market forces within particular institutional arrangements.

**Findings** – When the institutional arrangements favor mandatory versus voluntary corporate disclosure, this study suggests a reform measure for the East Asian corporate governance system that relies, inter alia, on the percentages of long-term and short-term financing to total financing. The higher the percentage of long-term financing, the more we can infer the extent of outside investors' confidence in the future of the East Asian firms. When more active role of banks involvements with the firms' business is permitted and an effective banks' and firms' strategic transparency can be assured, the East Asian banks and stock market can both lead firms to long-term favorable achievements. This study also suggests that the protection of both shareholder's rights and creditors' rights can go in parallel lines with the latter is to be given first priority until the investors' confidence in the near and far future of East Asia corporate governance system is built.

**Originality/value** – This paper extends the value of corporate governance structure to the East Asian firms through advocating the determinants of strategic transparency in East Asia.

**Keywords** International business, Corporate governance

**Paper type** Research paper

The international business systems have undergone numerous radical changes in recent years due to the emergence of the new global economy. The catalysts of structural economic changes have led to an urgent need to reassess the traditional purely competition-driven frameworks such as Porter (1990). In the public policy domain, there has also been an intense debate on the role of state and national competitiveness in the age of global competition. Acknowledging the growing force of globalization, Porter (1990) and Dunning (1995) discuss the role of the state to enhance the competitiveness of national industries. This research has tended to view firms as black boxes competing through economics-driven frameworks of success. In contrast to economics-driven frameworks, the research on models of corporate social performance (Freeman, 1984; Aram, 1989; Jones, 1995; Donaldson and Preston, 1995) has provided another model of a relationship-based business system. As quoted in Donaldson and Preston (1995), the diversity of such business systems were highlighted in *The Economist* (1993, p. 52):

In America, for instance, shareholders have a comparatively big say in the running of the enterprise they own; workers ... have much less influence. In many European countries, shareholders have less say and workers more ... in Japan managers have been let alone to run their companies as they see fit – namely for the benefit of employees and of allied companies, as much as for shareholders.

The characteristics of the East Asian business system have emerged in the existence of another business systems that are quite different in terms of the underlying economic and social foundations[1]. The type of economics-driven model does not take into account the institutional infrastructure in Asia, which is another business system commonly characterized by relationship-based business framework. Within this framework, it has been realized that firms face constraints from various stakeholders in their home business systems. This issue is closely linked to corporate governance transparency East Asia. According to the World Bank (2000) report, the business system in East Asia has been characterized by the lack of corporate governance transparency, weak institutional arrangement to protect shareholders rights, inadequate financial supervision, high leverage of corporations, prolonged moral hazard, and ill-established capitalism. These were considered the major reasons behind the East Asia economic crisis in general and the massive corporate bankruptcies in particular. Compared to the Anglo-Saxon corporate governance system, the East Asian firms need to expand the financial-based corporate governance transparency to a more comprehensive strategic-based corporate governance transparency.

### Research objectives

This study aims at achieving the objectives that follow:

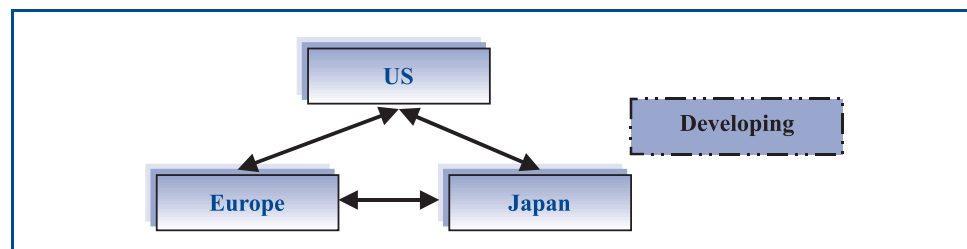
- Examine the institutional characteristics of the international business systems. This is to clear up the orientations of the corporate behavior and governance.
- Examine the institutional arrangements of the international corporate governance modes. This helps show the compatibility of corporate governance modes to the unique institutional arrangements in a particular business system.
- Explore the factors that can lead the East Asian corporate governance mode to become more transparent to its compatible institutional arrangements.

### Comparative business systems

The traditional definition of the international business environment (Ohmae, 1985; Porter, 1990; Thurow, 1992; Yoffie, 1996) argues that the increasing homogenization of demand, technology and income levels in the three triad markets (US, Western Europe and Japan) tend to shape managerial decision-making in global competition[2]. The traditional international comparative business system is shown in Figure 1.

The Anglo-Saxon business system, or capitalism (Albert, 1991) has been economically dominant in the nineteenth and twentieth centuries. Although the term West is often used to describe both North America and Western Europe as relatively homogenous group of countries in terms of economic and political systems, there is a significant difference between Anglo-Saxon countries such as the USA, Canada, and the UK and those of continental Europe. The communitarian business system includes the eastern and western European countries that differ from the Anglo-Saxon countries in term of their domestic business system that emphasizes the role of the government in economic and social affairs, the close linkages between banking and industry, and the group orientation of the society and communitarian values. In sum, the European stakeholders system is fundamentally

**Figure 1** Traditional models in international management: geography and wealth based



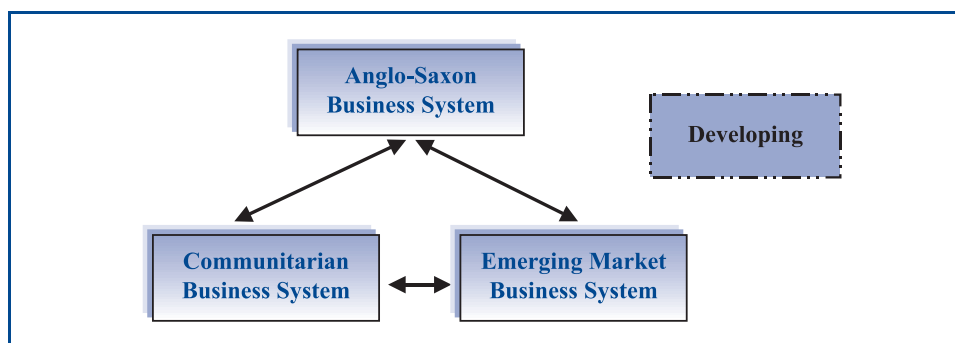
different. The emerging market business system refers to broad range of countries that are rapidly entering the world business system. These countries include most of the Asian countries, number of the Eastern European countries such as Russia, Hungary, Czech Republic and number of the Latin American countries such as Mexico, Chile, and Brazil. These countries are to be distinguished from the developing countries of the world. Figure 2 shows the home market institutions and constraints in international business systems.

### Institutions and corporate governance modes

Many studies in the literature discussed the importance of national institutions and capabilities. These studies include the business-government relations (Lodge, 1990; Doz and Prahalad, 1984), the role of economic institutions (North, 1990; Williamson, 1985), the role of technological capabilities and national systems of innovations (Kogut, 1991; Shan and Hamilton, 1991), and the comparative forms of business organizations and management systems (Whitley, 1990; Child and Monir, 1983). These studies, elaborating on the global standardization and local adaptation debate, have helped analyze the complex realities of institutional and organizational diversity that still persist in today's increasingly converging business environment. We further suggest that various institutional and cultural factors in a business system of a country or group of countries are to be considered crucial determinants when analyzing the differential modes of organization and strategy. Global competition can be seen from the viewpoint of what motivates and constrains firm strategy and behavior in today's global business environment. These constraints include national culture, legal and regulatory environment, business-government relationships, the role of financial institutions, and corporate governance systems in the home country as well as host countries of multinational firms. Accordingly, Stopford and Strange (1991), Kogut (1991) and Albert (1991) have shown that domestic institutions play as important role in determining corporate behavior as the pressures of globalization. For example, in many parts of Asia, it is not the financial markets but various government ministries that monitor corporate performance and control financial allocation. In many continental European countries such as Germany and Switzerland, the banking sector as institutional shareholders monitor corporate performance and investment decisions (Baums, 1992; Kim, 1995; Macey and Miller, 1995; Schmidt *et al.*, 1997). Therefore, firm behavior and strategy, especially investment decisions such as new market entry, diversification, and innovation and new product development can be significantly constrained by the differences of home market institutions.

In East Asia, the relationship-based institutions have resulted in a business system that is characterized by concentration of ownership and control of corporations and banks by families. This governance mode is quite apparent in Indonesia, Philippines and Thailand, where the largest ten families control half of the corporate sector in terms of market capitalization (Claessens, Djankov and Lang, 1999). Hong Kong and Korea are behind these countries in rank that is about third of the corporate sector. Accordingly, the relatively high family-based concentration of corporate ownership and control have led to a governance structure that enables the dominant shareholding families to make key

**Figure 2** Shareholder versus stakeholder business systems



decisions on their own. For example, appointments of board members are almost entirely at the hands of those families in control of the firms (Nam *et al.*, 1999). Therefore, there is a possibility of conflict of interests between dominant shareholders, managers and the minority shareholders. This governance structure enabled expropriation of minority shareholders (Aoki and Kim, 1995a; Claessens, Djankov, Fan and Lang, 1999; Claessens *et al.*, 2000; Lehmann, 1996; Phan, 2001), which is less serious in Hong Kong, Malaysia and Singapore than in the rest of the region. Furthermore, the concentration of ownership by families has been supported by legal institutional arrangements that enabled the exercise of high degree of control over firms. These legal arrangements include the deviation from the one-share-one-vote rule that has led to more minority shareholders expropriation and the absence of mandatory disclosure of connected interests which is a fertile ground for self-dealing that resulted in expropriation.

The Anglo-Saxon (market-based) corporate governance literature links concentration of ownership to the role of institutional investors when monitoring and influencing firms' investment and financing decisions. In this concern, the picture in the East Asian region is different as evidence suggests that ownership by institutional investors is generally small compared to what is dominant in the Anglo-Saxon countries. Furthermore, institutional investors do not actively participate in the governance of firms even when they possess a significant proportion of shares. For example, the country reports for Hong Kong and Singapore all report limited institutional investors' participation in the governance of corporations, i.e. banks owned 10.2 percent of stock market capitalization. In Korea, institutional investors had been barred by law from exercising voting rights until recently, i.e. non-bank financial institutions owned 12.7 percent in 1997. The country report for Thailand in 1999 showed that domestic banks and other financial institutions own around 13 percent of the 150 largest listed companies (Nam *et al.*, 1999).

The inherited relationship-based corporate governance is one of the fundamental drivers of concentration of ownership and lack of transparency that have turned out to be the causes of the region's economic crisis. The East Asian region tried to liberalize its markets without having the proper required economic and legal institutions that enable an acceptable degree of corporate governance transparency. This is not to conclude that the Anglo-Saxon business system has to be a model for liberalization (Phan, 2001). As discussed earlier, the East Asian business system has its own institutional foundations that cannot be abandoned and, above all, that have led the economic progress in the region to a recognizable business system.

### Determinants of strategic transparency: perspectives from comparative business system

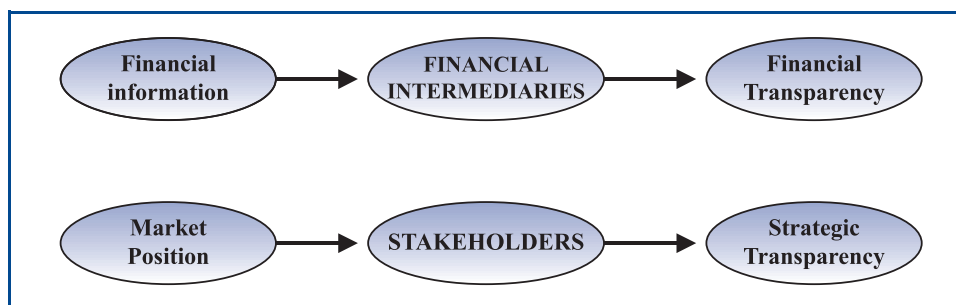
The realities of today's complex business environment, including the pressures from capital markets, principal-agent relationship and the importance of information flows, warrant a reexamination of the traditional models of corporate governance. This leads to the issue of "strategic transparency" in corporate information disclosure, which we define as follows:

Strategic transparency is the ability of firms to signal or provide adequate and relevant information timely and effectively to their shareholders, stakeholders or to other principal parties such as policy makers who motivate and constrain them to behave within the principal's interest and in an acceptable way to the society.

In stressing the importance of strategic transparency and accountability to the broader society and policy makers, it is important to take into account the constraints and motivations that drive firms' performance in different business systems. Figure 3 shows the catalysts of financial and strategic transparency.

The traditional market-based corporate governance models focus on the financial practices that aim at governing corporate performance (Williamson, 1988; Charkham, 1989; American Law Institute, 1982; Cadbury, 1993; Hart, 1995; Kay and Silberston, 1995; Lowenstein, 1996; Shleifer and Vishny, 1997). These models associate firm's strategic transparency with dissemination of financial information through the role played by the market intermediaries. Diamond (1984), Mayer (1988), Rajan (1992) and Von Thadden (1995) show the important

**Figure 3** Catalysts of financial and strategic transparency



role the financial intermediaries play with regard to information gathering and monitoring. Holmström and Tirole (1993) examined the market microstructure perspectives and concluded that decentralized market trading can support information collection. From the borrower's point-of-view, strategic transparency is associated with the extent to which information disclosure will affect firm's market position. On one hand, lenders prefer less information dissemination as long as it protects firms when in a weak competitive position. On the other hand, when the firm is in a strong market position, equity holders prefer more disclosure to maximize their profitability and capital gains (Perotti and von Thadden, 2001).

According to the theory of agency costs of debt and equity (Jensen and Meckling, 1976), the governing lenders will discourage transparency, as this would endogenously undermine the value of their claims. In contrast, firms governed by shareholders' interests prefer greater transparency, as information disclosure on average increases profitability as well as risk. The influence of banking finance on firm's financial disclosure has also been examined in the literature. Many studies showed that bank-dominated financing relationships are less transparent to external observers, thus discourage information gathering by investors (Bhattacharya and Chiesa, 1995; Boot and Thakor, 2001; Perotti and von Thadden, 2001; Hedge and McDermott, 2000). In contrast, market-based financing results in more corporate information disclosure to both investors and competitors (Perotti and von Thadden, 2001).

The discussion mentioned above suggests that the extent of strategic transparency is influenced by two factors:

1. The orientation of the institutional infrastructure in a certain economy.
2. The foundations of business system in a certain economy.

#### *Institutional orientation*

In the mature economies such as the USA and the UK, more disclosure is realized as long as the economic, political and social institutions permit and can cope with market pressures (Choi *et al.*, 1999). In the emerging economies, the institutional infrastructure is tied up to, among others, the degree of economic progress a country is targeting. Thus, a firm in an emerging or transitional economy can be strategically transparent to the extent to which its market position will not be impaired accordingly. This orientation is realized in transitional economies as banking finance and less transparency are relatively the dominant factors of corporate governance mode (Aoki and Kim, 1995b).

The issue of strategic transparency is very related to information dissemination and disclosure to firms' stakeholders. This calls for exploring whether firms are motivated by competitive reasons and/or legal obligations to be transparent to the market and disclose the relevant information to stakeholders. Recalling the global competitive pressures and the orientation of the East Asian region to conform to International Accounting Standards (IAS) regulations, it becomes clear that disclosure policies require prerequisite certain institutional arrangements. From legal point-of-view, some works have asserted on the necessity of having strong and effective laws and institutions as prerequisites for mandatory disclosure and for building strong capital markets (Levine and Zervos, 1996; Levine, 1998; Coffee, 1999; Pistor *et al.*,



2000; Black, 2001). To build a strong stock market, the aim of law is to protect minority shareholders' rights against insiders' self-dealing and to provide shareholders good information about the value of a firm's business (Black and Kraakman, 1996; La Porta *et al.*, 1997, 1998a, b, 1999). Black (1998) argues that controlling information asymmetry is essential for building strong stock market. Mauro (1995), Kumar (1996), Modigliani and Perotti (2000) and Ho (2001) studied the relationship between legal effectiveness and capital market developments and documented an inverse relationship between corruption and the strength of public securities markets in particular and economic growth in general.

In sum, firms with good news prefer more or less disclosure depending on the nature of the private information. When it concerns their own strength, better firms may want to enhance visibility, e.g. by an IPO as a mean to commit to more disclosure (Stoughton *et al.*, 2001; Stoughton and Zechner, 1998). When good information concerns the profitability of the market, which may encourage more competitors to enter the industry, firms with better information prefer less disclosure and thus private, bilateral financing (Gertner *et al.*, 1988; Yosha, 1995). This is linked to the issue of the changing state of economic progress and adaptable corporate governance. That is, in a stage of transition, weak firms can be less transparent until the firm's market position is improved, then greater transparency will result in greater profitability and risks as well. As bank-dominated financial system is observed in transitional economies, Perotti and von Thadden (2001) conclude that firms in such financial systems are less transparent than firms in shareholder-dominated financial systems.

We can conclude that mandatory disclosure is constrained by two factors. First, the evolution of the East Asian business system, which favors family and concentrated ownership. Second, the legal infrastructure that does not provide adequate protection to minority shareholders' rights[3]. Firms need to explore the effects of voluntary disclosure on their relative market position. Furthermore, firms need to avoid being stuck between mandatory law-based disclosure and the voluntary competitive-based disclosure. The criterion in this case is to adopt the disclosure approach (mandatory and/or voluntary) that positively affects the firm's market value. Gonedes (1980) and Verrecchia (1982) conclude that as mandatory reporting requirements become more detailed, voluntary disclosure may decline. As the law-based disclosure policies and mechanisms are not well established yet in the East Asian region, this provides an opportunity for voluntary disclosure to play the replacement role to affect firms' market value. In this regard, Dye (1986) developed a relationship between mandatory and voluntary disclosure and value-maximizing policies. Dye (1990) developed another model showing that when the two types of disclosure coincide, it is possible to economize in the process of setting mandatory disclosures. Holland (1998) concludes that private corporate voluntary disclosure is associated with the desire to create favorable institutional and market states with external benchmarks and pressures on companies for high quality communications. This shows how important is the voluntary disclosure that firms in the East Asian region are to explore in order to strengthen their relative position in the market as long as the law-based mandatory disclosure is not well established yet.

As low transparency is realized in the East Asian region, some of the law scholars tried to solve the problem of low disclosure and weak protection of shareholders' rights in transition economies. Coffee (1999) and Black (2001) suggest that firms can piggyback on the securities markets of developed countries by listing their shares on stock exchanges in those countries. In fact, this suggestion may solve the problem of low disclosure in the short-run, but certainly does not help improve the weak securities law in the long-run[4]. In addition, when taking the securities-related laws in developed countries as a model to follow does not guarantee real sustained improvements in the legal environment in East Asia. The East Asian region has adopted a wide range of western-oriented legal reform, which has been moving on according to the pace of globalization. What matters is the effectiveness of the legal institutions for improving the quality of legal actions. Pistor *et al.* (2000) concludes that, in the case of transition economies, good laws cannot substitute for weak institutions.

### Foundations of business system

We realize that although the concept of strategic transparency is required to a certain degree in all countries, the principles differ depending on the historical development of business system in each country. In fact, the different corporate governance modes and information disclosure can have important influences on firms' strategic behavior. Table I summarizes the requirements of strategic transparency in each business system.

The above discussion shows that the degree of strategic transparency is to be associated with firms' market position and degree of competitiveness. More generally, as certain economy is achieving a degree of economic progress, and the mode of corporate governance changes accordingly, firms have to adapt their degree of strategic transparency.

### East Asia corporate governance mode

Although the findings mentioned above have actually resulted from market-based business systems, similar findings have also been realized in the East Asian business system. Since the early days of economic development when the East Asian firms were largely financed by bank loans under government influence, close links among firms, their banks, and the government have been developed through a business system of family ties and political deal making (Nam *et al.*, 1999). Both firms and banks within this relationship-based system felt little need to develop corporate governance mechanisms, since firms were able to rely on banks to continue financing their projects and banks felt comfortable under the explicit or implicit government guarantee. In addition, governments adopted some policies that have resulted in less transparency to market forces and eventually have contributed to the witnessed economic crisis in the region. That is, one of the underlying aspects of the East Asian relationship-based corporate governance is the governments' orientation towards providing subsidized credit to firms in targeted industrial sectors and implicitly sharing their investment risk. In this sense, subsidies acted against strategic transparency as long as subsidized firms did not have to face market mechanisms and competition which both require adequate disclosure to outside investors. On the other hand, outside investors had little incentive to heavily invest into a new relationship given the weak legal infrastructure that protects their rights and the resulted lack of corporate transparency (Rajan and Zingales, 1998; Hirakawa, 2001). Given the East Asian market imperfection, expropriation of outside shareholders was an inevitable outcome that could have been avoided by being more transparent to market forces.

Furthermore, it is obvious that the relationship-based corporate governance system has resulted in the problem of resource misallocation since it does not use price signals, lacks monitoring and discipline from the market (Hoshi *et al.*, 1991; Weinstein and Yafeh, 1998; Peek and Rosengren, 1997; Calomiris and Rammirez, 1996). This comes in contrast to the market-based corporate governance that allocates financial resources through explicit contracts and associated prices. To the extent that contracts are inevitably incomplete, investors who supply funds to a firm are better protected if the firm is equipped with better corporate governance mechanisms with a higher level of transparency. This has very important implications to the East Asian countries that, as an economy moves from the

**Table I** Business systems, stakeholders and strategic transparency

| <i>Types of business systems</i> | <i>Stakeholder strategic transparency</i>   |
|----------------------------------|---|
| Anglo-Saxon system               | Shareholders and the dynamics of financial markets<br>High degree of information disclosure                                 |
| Communitarian system             | Stakeholders: employees, suppliers, government, and the community<br>Limited information disclosure                         |
| Emerging system                  | Family owners, government ministries<br>Lack of disclosure, transparency<br>Mix of both shareholder and stakeholder systems |



relationship-based to well-functioning market-based system, requires substantial improvements on its corporate governance system to become strategically transparent.

It is worth to note that we are not trying to stereotype the above mentioned characteristics of the relationship-based corporate governance over all East Asian countries. In fact, there exist significant differences between two groups of countries in terms of the overall quality of corporate governance systems and their legal infrastructure for property rights protection (Nam *et al.*, 1999). Hong Kong, Singapore and Malaysia appear to maintain significantly higher standards in corporate governance and have developed more sophisticated and adequate legal systems to protect property rights than the rest of the countries. A low level of property right protection, weak enforcement, loose operations of lending institutions and ineffective regulation of the financial sector are characteristics shared by Indonesia, Korea, Thailand, and Philippines.

### *The role of banks in East Asia corporate governance*

As the East Asian business system is characterized by family-based and concentrated ownership coupled with weak legal infrastructure, it will take much longer time and less incentives to protect minority shareholders' rights. Banks, therefore, are considered the other financial institutions that can provide an alternative and complementary source of financing (Levine, 1998). Here, the role of the East Asian banks in corporate governance transparency can be assessed by looking at the extent to which they are allowed to provide financing and investing to the non-financial business sector. In general, East Asian banks are not behaving as western institutional shareholders. What follows summarizes the banks' role (Nam *et al.*, 1999). The focus is on whether banks can act as intermediaries whose role is to monitor and disclose information about the firms to which they are lending, thus to show the extent to which banks can play a role in strategic transparency:

- *Singapore.* The Banking Act limits the investments of banks in other non-financial businesses to a maximum of 20 percent of their capital base. Banks are constrained when investing in large equity shares in a single firm even though if it is less than 20 percent. The exception is when a bank invests in firms setup to promote development, which have to be approved by the Monetary Authority in Singapore (MAS).
- *Hong Kong.* Under the Banking Ordinance of 1986, most banks belong to financial groups and the approval of the Hong Kong Monetary Authority (HKMA) is required in order to acquire 10 percent or more shares. Banks are only allowed to have equity shares in non-financial businesses of up to 25 percent of their capital base. Therefore, the banking sector was not allowed to play an important role in corporate governance.
- *Malaysia.* Most of banks are controlled by conglomerates. But the central bank prohibits banks from providing loans to related firms.
- *Korea.* Despite financial liberalization and deregulation, the government influences bank management primarily through appointing CEOs. In 1982, when the privatization of the banking sector was pursued, a ceiling of 8 percent was imposed on individual ownership of nationwide commercial banks. In 1994, this ceiling was even lowered to 4 percent to prevent any single shareholder from exerting excessive influence and control over a bank's management. In 1998, the ceiling was relaxed to 15 percent and commercial banks increased their shareholdings of non-financial firms in their asset portfolios, although this increase has been for achieving capital gains rather than management control. Consequently, 15 years after their privatization, banks still function like state-owned institutions.
- *Philippines.* Many financial institutions and non-financial corporations are under common family-based ownership. Accordingly, regulatory frameworks have been established for preventing banks from heavily involvement with firms.
- *Thailand.* Thai banks were able to hold a controlling share in listed companies through their equity shares in holding companies, which are not subject to any investment restrictions. Nevertheless, Thai banks were restricted in directly holding shares of listed non-financial firms and 10 percent ceiling was imposed on equity shares.

- *Taiwan*. Banks were strictly regulated in their equity shares of listed companies, and recently were allowed up to 15 percent of bank's net worth, which allowed banks to play a minor role in corporate governance.

The history of the East Asian business system tells that banks were playing more viable role in financing firms in the early stages of economic development in the region. Carlin and Mayer (1999) conclude that bank financing may be more appropriate for capital-intensive industries and low levels of economic development. These two characteristics are observed in the East Asian region. In addition, the western corporate governance literature states that bank-centered capital markets may be stronger than stock market-centered capital markets when ensuring that firms are not only honestly run, but also well run (Black, 2001). This suggests a priority of creditors' rights over shareholders' rights in the process of legal reform. In general, for firms in East Asia to grow in a global competitive environment, they need external finance rapidly enough not to wait until new legal requirements help build minority shareholders' confidence. Strong confidence requires enough time, good experience, and benchmarking. Here, banks can become a reliable source of financing and more patient capital suppliers, which is a common characteristic among banks in different business systems (Eldomiaty, 1998, 2001).

### Importance of strategic transparency to the East Asian corporate governance

Market liberalization in East Asia required firms to follow the IAS and the disclosure regulations of the leading international financial centers in the Anglo-Saxon business system. Nevertheless, the weak legal infrastructure did not permit adequate disclosure as many cases of fraudulent accounting and violations of disclosure rules were detected. The main areas of low or absent disclosure were asset valuation, disclosure of off-balance sheet items and transactions with the parties related to controlling shareholders.

In fact, although the IAS is unifying the disclosure rules, that norm of disclosure focuses only on the financial aspects of disclosure that, in fact, have been realized easy to violate. As the East Asian business system is integrating into global economic environment, it requires firms to become more transparent to market forces and to disclose the relevant financial and non-financial information that concerns the involved stakeholders.

Strategic transparency, therefore, requires bringing about structural changes into the East Asian corporate governance system in order to become more transparent. The importance of strategic transparency can be outlined as follows:

- The economic integration will gradually lead the East Asian market to be more liberalized which requires more disclosure to outside investors.
- The stage of economic transition in East Asia requires low-cost long-term financing which cannot be guaranteed unless financiers are fairly sure about the near and far future of the East Asian firms. In this regard, East Asia is considered in a good position to reach a reduced transaction costs by utilizing the technological information advantage and become more transparent to the existing and potential investors and stakeholders (Phan, 2001). Evidence in the field supports the positive relationship between firm disclosure, reducing cost of equity, cost of debt and performance in the product market (Bhattacharya and Ritter, 1982; Gertner *et al.*, 1988; Botosan, 1997, 2000; Sengupta, 1998).
- The economic integration requires the East Asian financial institutions (securities markets, banks, ... etc.) to focus on the long-run performance and avoid the problems of short-termism which is very common in the Anglo-Saxon market-based system. The role of East Asian banks, or even the subsidized debt, is not the only cause to blame for the economic downward witnessed at the region. In fact, to analyze the situation from practical point-of-view, bank loans are considered in the literature of corporate finance as very viable source of financing especially when certain type of investment does not appeal to the trends in the stock market. This active role of debt has been realized through the evolution of the Anglo-Saxon corporate governance system (Black, 1975; Campbell, 1979; Fama, 1985; Scott, 1986; Booth, 1992; Triantis and Daniels, 1995). The point of

criticism has come from the relatively heavy reliance on the stock market short-term financing that has led Anglo-Saxon firms to plan their financing and investment decisions to satisfy the short-term interests of their myopic shareholders (Porter, 1992; Bhidé, 1994; Lavery, 1996). For the East Asian business system to focus on the long-run performance, it is required to strengthen the legal infrastructure to enable more active role of bank financing. According to the preceding discussion, it has been realized that the East Asian banks cannot play the promised active role in corporate governance. In fact, low firms' equity holdings in banks institutions goes against the foundations of the relationship-based business system, which is unique to the region. The legal constraints on banks equity holdings have led to many unfavorable consequences such as banks lost their job in the economy as guardians to firms, turning banks into weak institutional investors looking at short-term profits and the problem of market-based "short-termism" is back again. Therefore, *inter alia*, if more active role of banks' involvements with firms' business is permitted and an effective banks' and firms' strategic transparency can be assured, the East Asian banks and stock market can both lead to longer-term favorable achievements.

- Transparency will lead to better financing and investment decisions as the market-based mechanisms use price signals to efficiently allocate resources and monitor market returns. In this regard, we can suggest a reform measure for the East Asian corporate governance system that relies, *inter alia*, on the percentages of long-term and short-term financing to total financing. The higher the percentage of long-term financing, the more we can infer the extent of outside investors' confidence in the future of the East Asian firms. The long-term perspective is crucial to a sustained competitive corporate governance system in East Asia as long as the Anglo-Saxon corporate governance system has resulted in short-termism in both financing and investment decisions which have negatively affected the competitiveness of the Anglo-Saxon corporate governance (Porter, 1992; Bhidé, 1994; Lavery, 1996).

## Conclusions and further research

This paper presents a redefinition of the comparative business systems framework that includes the pure economic competition among the global economic triad of the USA, Western Europe and Japan. Our research cleared up the influences of the comparative business systems on corporate governance orientations. Transparency is considered one of the determinants of corporate governance success in comparative business systems. Strategic transparency is closely related to the information disclosed to firm's stakeholders that are, in turn, affected by the structure of corporate ownership. Moreover, information disclosure and transparency are affected by the institutional arrangements in a certain business system, among which is the effectiveness of legal institutions that sets boundaries between mandatory and voluntary information disclosure. The global competitive pressures call firms not to wait for new disclosure laws to tell what, where, why, how, and when to disclose the relevant information to the involved stakeholders.

We can suggest that protection of both shareholder's rights and creditors' rights can go in parallel lines with the latter is to be given first priority until the investors' confidence in the near and far future of emerging countries and/or emerging firms is built. By that time, shareholders' confidence will happen accordingly. Further research can be developed on the determinants of firm strategic and financial transparency and their association with firm value.

## Notes

1. The East Asian countries referred to in this study include seven countries: Singapore, Hong Kong, Malaysia, Korea, Indonesia, Thailand, and Philippines.
2. This view is often extended to the argument that globalization of markets and the convergence of demand under this triad framework allow firms to allocate their resources and activities freely across these three regions, thus leading to increased economies of scale and scope by standardization of products and services, minimization of costs, and the formation of flexible organizational structures.

3. This conclusion comes in contrast with some law scholars who advocate the idea of forcing firms to disclose information. For further readings, see Coffee (1984), Easterbrook and Fischel (1991), Mahoney (1995) and Admati and Pfleiderer (1998).
4. Black (1990) argues that American corporate law is mostly and perhaps entirely trivial, in the sense that it does not significantly constrain any private contractual arrangements that a company's shareholders want to choose for themselves.

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