Analysis in corporate governance

Abstract. Introduction. Corporate governance is a system shaping and modifying company’s management and control. Building-up a smart system of analytical support for corporate governance is a prerequisite to ensure corporate governance quality upgrading, fundraising and capitalization enforcement. Purpose. To provide evidence to the significance of economic analysis as a tool to ensure high standards of corporate governance, to design a system of analytical support to serve successful corporate governance and to specify its elements. Results. The article presents the specifics of corporate governance analysis. It covers the basic elements of an analytic support system for corporate governance, such as: reporting transparency assessment, dividend payout analysis, top management remuneration analysis, target value analysis. Conclusion. A system approach to developing analytic support for corporate governance is proposed. Its implementation is essential to improve investment attractiveness of a company, ensure achieving the company’s goals and enhance its competitiveness.

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1. Introduction. The growing interest to the issues of standards of corporate governance improving is caused, firstly, by the role of corporations in developed countries’ economies and, secondly, by the demand of major companies for financial assets along with the need to maintain and enhance their competitiveness. It seems clear that implementation of high standards of corporate governance so far has not been timely and appropriately conducted. We deem that economic analysis is instrumental to foster the promotion of corporate governance principles.


3. Purpose. To provide evidence to the significance of corporate economic analysis as a tool to improve corporate governance and design a system of analytical support for corporate governance specifying its elements.

4. Results. At present, economic prosperity of any nation is largely determined by the rate of corporate sector growth. For economically developed countries, corporations account for 80% of overall national output of goods and services.
Principles of Corporate Governance and the Commentary. Consequently, it is essential to follow the provisions of the document on corporate governance fixed in the corporate charter, and the double-duty for corporate governance. At that, consideration of methods for corporate economic activity analysis shows that specific aspects of joint-stock companies and the way they bear upon the content of the financial state of a company, investment attractiveness and efficiency analysis patterns is insufficiently addressed [20, p. 15].

From the opinion of analysts of business transparency, the main problems of remuneration and the management and the board of directors in Russian public companies are: 1) weak correspondence between the amount of remuneration and actual target values; 2) unsatisfactory disclosure of remuneration expenses [24, p. 101].

Only two thirds (126) of 182 companies surveyed by the RRIRN in 2015 explain their policy in terms of remuneration and the corporate management body and the Board. Most of the companies (137 of 182) disclose the amounts of remuneration to the Board members; 97 companies disclose the remuneration scheme, but only in 52 companies remuneration is correlated with key performance indicators (KPI). Information concerning remuneration to company director-general, or president, remains the least transparent: only 35 companies disclose the remuneration amounts, one third of the companies surveyed disclose the remuneration scheme, and 71 company correlates remuneration with the company KPI [22]. For example, in 2015 Public Joint-Stock Company «Novolipetsk Steel» (NLMC) from RAEX-600 and Top-100 lists is recognized in Russia by the amount of remuneration. For instance, in 2015 the company is one of the top ten companies as for the volume of sales and occupies the 17th position in terms of capitalization according to 2014 year end) [25]. NLMC annual reports [26] disclose the amount and the scheme of remuneration to the Board members for their participation in the activity of the corporate management body which made 72.6 million RUB in 2013 and 75.9 million RUB in 2014 (to nine Board members). Information on the amounts of individual remuneration is not disclosed. At present, NLMC is deploying a program of long-range key management motivation [26].

Element 3. Amount of dividend payouts and their consistency are characteristics of smart corporate governance. Corporate dividend policy is deemed to set up a proportion between the parts of net earnings to be consumed and to be reinvested with a purpose to benefit market value of the company assets and wealth of the shareholders. Dividend policy has an effect on company’s size by its market capitalization, and, in particular, on its stock prices.

Theoretical aspects of dividend policy and its key determinant are addressed in research works of V. Kovalev (2010) [9], D. Yendovitsky (2012) [7] and other authors. For successful dividend policy analysis, it is firstly necessary to check the existence of the corporate Rules and Regulations on Dividend Policy. The document availability conforms to the guidelines of high standard corporate governance practices and facilitates most full enjoyment of the shareholders’ rights to dividend payouts. It is intended to provide shareholders with information concerning corporate policy on amount, frequency and consistency of dividend payments.

The first step in dividend payout analysis is to assess the amount and dynamics of corporate earnings as the main source for dividend payouts. It is required to single out the part paid out as dividend and the part to plough back (or reinvest). The next step is to calculate Dividend Payout Ratio (dividends declared as dividend and the part to plough back, or reinvest. The next step is to calculate Dividend Payout Ratio (dividends declared to total net earnings of a company) and Reinvestment Ratio (plough-back earnings to total net earnings). Those should be calculated for a number of periods in order to expose the trends. After that, net earnings growth to dividend growth ratio analysis is conducted. Both the ratios are assessed and a reference pool of major Russian companies. Faster growth of dividend payouts compared to earnings is indicative of corporate governance improvement. Finally, common share dividend rates and growth is analyzed. For comparative dividend policy analysis, the following indices are commonly used: dividend yield, dividend payout and dividend cover [9, p. 389].

Remuneration directly depends on the amount of dividend policy was disclosed in 121 of 182 companies sur-
veyed (66%), which correspond the standards of the top three transparency levels (according to the RRIRN rating). Information on dividend amount, dividend per share and dividend yield was disclosed by 145 companies (80% of the companies surveyed). Dividend history was disclosed by 103 companies (57%). Corporate dividend information is best disclosed by the companies whose reports meet the requirements of the world business [22].

For example, NMLC (which is in the top 20 Russia’s most profitable companies [25]) follows a certain dividend policy and regularly brings it up to date. According to its new amendment, on the one hand, dividend payout ratio has been become 30-50% (compared to 50% before), on the other hand, dividend amount range has been made dependent on net debt by EBITDA ratio [26]. NMLC disclose their dividend per share par value: as of the end of the year 2014, it amounted to 2.44 RUB per share (0.67 RUB for the year 2013; 0.62 RUB for 2012; 2.00 RUB for 2011). The company dividend payout ran at 38% for 2014, 35% for 2013, 20% for 2012, 28% for 2011 [26].

Element 4. Corporate target value analysis. Such values as profit amount and profit growth rate, sales growth, market share gained on assets (ROA) and return on equity (ROE), market capitalization growth can be taken as the company’s target values. However, information concerning the goals and strategy of the company, which is essential for assessing its economic growth prospects, is far not always available for shareholders and investors. «Assessing the efficiency of a corporate strategy involves the diagnosis of the strategic targeting cost. That is assessed by means of comparing strategic thresholds achieved with strategic thresholds approved on each and every stage of the strategy implementation» [27, p.30].

Today, Russian companies start operating indices widely used in international corporate practice. Such indices as EVA, EBITDA and efficiency indices calculated on the basis of those mentioned above are critical for both assessing short-term results and achieving long-term goals, like SVA (Shareholder Value Added) and MVA (Market Value Added) growth.

Most of the biggest Russian companies (as of 2015) conform to relatively high transparency standards (182 companies). Their annual reports contain information which makes it possible to view the prospects for their further development. However, only 138 companies (75% of those surveyed) provide insight into their strategies. Only 72 companies (40%) provide the description of their corporate goals in quantitative terms [22]. As to the goal disclosure, such companies as «Vnesheconombank», PJSC «Federal Grid Company of United Energy System», «Sberbank of Russia», PJSC «RusHydro» and PJSC «Rosseti» occupy leading positions.

Element 5. Analysis of transaction costs. «Extension of economic relations among corporations caused considerable increase in transaction costs, which are incidental to market entry and exit, property rights protection, business relationship formation and servicing, ensuring resource access, business integration etc.» [11, p. 28]. Since for the time being economic transactions and costs incurred are not considered as separate accounting objects, the analysis is hindered enough. The need for organizing a set of cumulative data on transaction costs for making economic decisions prompted investigating into the issue with the purpose of designing a specific accounting model: typology and methods of assessing expenses, grouping the cost-related facts of corporate economic activity and recognition of them in company accounts [28, p. 49]. N. Sapozhnikova (2013) suggests the following «transaction cost typology: enforcing property rights; ensuring resource access; information retrieval; negotiating and contracting; resource quality assessment and monitoring; property rights and resource protection; protection against opportunist behaviour» [28, p. 52]. This solution seems to provide accountability of the expenses and, thus, facilitate the cost analysis.

Element 6. Analysis of a public company market activity includes calculation and assessment of the following indices: 1) Earnings Per Share (EPS); 2) Price/Earnings Ratio (P/E); 3) Dividend Yield; 4) Dividend Payout Ratio; 5) Tobin’s Q-ratio (9).

5. Conclusion. After careful consideration of modern approaches to corporate governance, a cumulative author technique in that field has been proposed. We singled out the problems with corporate governance practical assessment in Russia at the example of corporate analysis and summarising up ongoing practices. It is possible to conclude that corporate governance analysis is closely connected with strategic management and requires clear and full set of information for being conducted, which make it almost impossible for independent parties to realize. For the most Russian companies, developing a smart system of analytical support for corporate governance and its implementation in practice is deemed to ensure upgrading corporate governance quality, fund raising, capitalization growth and building up trust with international business community.

References