HAWKAMAH
THE INSTITUTE FOR CORPORATE GOVERNANCE

A New Leaf for Corporate Governance for MENA
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A New Leaf for Corporate Governance for MENA

- ❑HAWKAMAH INSTITUTE FOR CORPORATE GOVERNANCE
- ❑CORPORATE GOVERNANCE IS SOURCE OF GREAT FINANCIAL CRISIS
- ❑CORPORATE GOVERNANCE REFORMS & IMPLICATIONS FOR MENA REGION
- ❑WHY DOES CORPORATE GOVERNANCE MATTER?
- ❑CORPORATE GOVERNANCE REQUIRED TO ATTRACT "PATIENT CAPITAL" TO MENA
- ❑ENVIRONMENT, CSR & CORPORATE GOVERNANCE IN MENA: S&P/HAWKAMAH ESG INDEX
- ❑WHAT WE NEED TO DO: NEXT STEPS

Hawkamah Institute for Corporate Governance

- **A "Think & Do Tank" Established in April 2006**
- **Bridge the "Corporate Governance gap"**
- **Assist the countries and companies of the region in developing sound, 'home grown' and globally well integrated CG frameworks & practices**:
  - **Advocate, Coordinate and Sequence the designing, and implementation of CG reforms**
  - **Monitor the outcomes of CG policies at the public and private sector level.**
  - **Provide Advisory services to Governments, Regulators & Private Companies**
  - **Build Capacity to implement CG best practices**

GCC Corporate Governance Reforms 2008-2011

Country	CG Developments 2008-2011
Bahrain	CG Code issued in 2010
UAE	CG Code mandatory from April 2010 (issued in 2007)
Qatar	CG Code issued in 2009
Oman	In 2010, The Capital Market Authority set up a corporate governance unit to ensure implementation of the CG Code (issued in 2002)
Saudi Arabia	In 2010, the Capital Market Authority set up a corporate governance unit to ensure implementation of the CG Code.
Kuwait	Capital Market Authority set up in 2010.

> *“The financial crisis was and is a failure of governance and executive management took excessive risk for corporations while risking almost nothing for themselves.” Robert Monks*

The recent global Great Financial Crisis has put corporate governance back on the policy agenda in the same way that the Asian crisis, the dotcom-bubble and the demise of Enron & WorldCom prompted responses.

Issues:

- **Boards: Composition & Competence of Directors**
- **Risk Management procedures, processes and implementation**
- **Alignment of Incentives**
- **Inefficient Regulations & Ineffective Regulators**

Avalanche of New Corporate Governance Guidelines

At least **40 countries** since the fall of Lehman Brothers have issued new or amended corporate governance codes

- **UK – Financial Reporting Council** corporate governance and Stewardship codes; Walker report on corporate governance in banks and other financial institutions
- **European Commission** Green Paper on corporate governance in financial institutions and corporate governance review
- **US Dodd-Frank** proposals on corporate governance, sequel to Sarbanes-Oxley
- **Basel Committee on Banking Supervision** have issued their Principles for Enhancing Corporate Governance

Required Responses

- Conduct: Accountability, Risk and Remuneration
- More competence, training, and authority in risk management
- Know risks, justify them, monitor and manage them
- Structure: Board Effectiveness
- Monitoring and Enforcement: Regulatory bodies, Shareholder Relations and Stewardship
- Regulators - Corporate Governance Risk should be dealt with as an integral part of managing Systemic Risk: CG failures at individual company level can generate failure of system, i.e. source of systemic risk

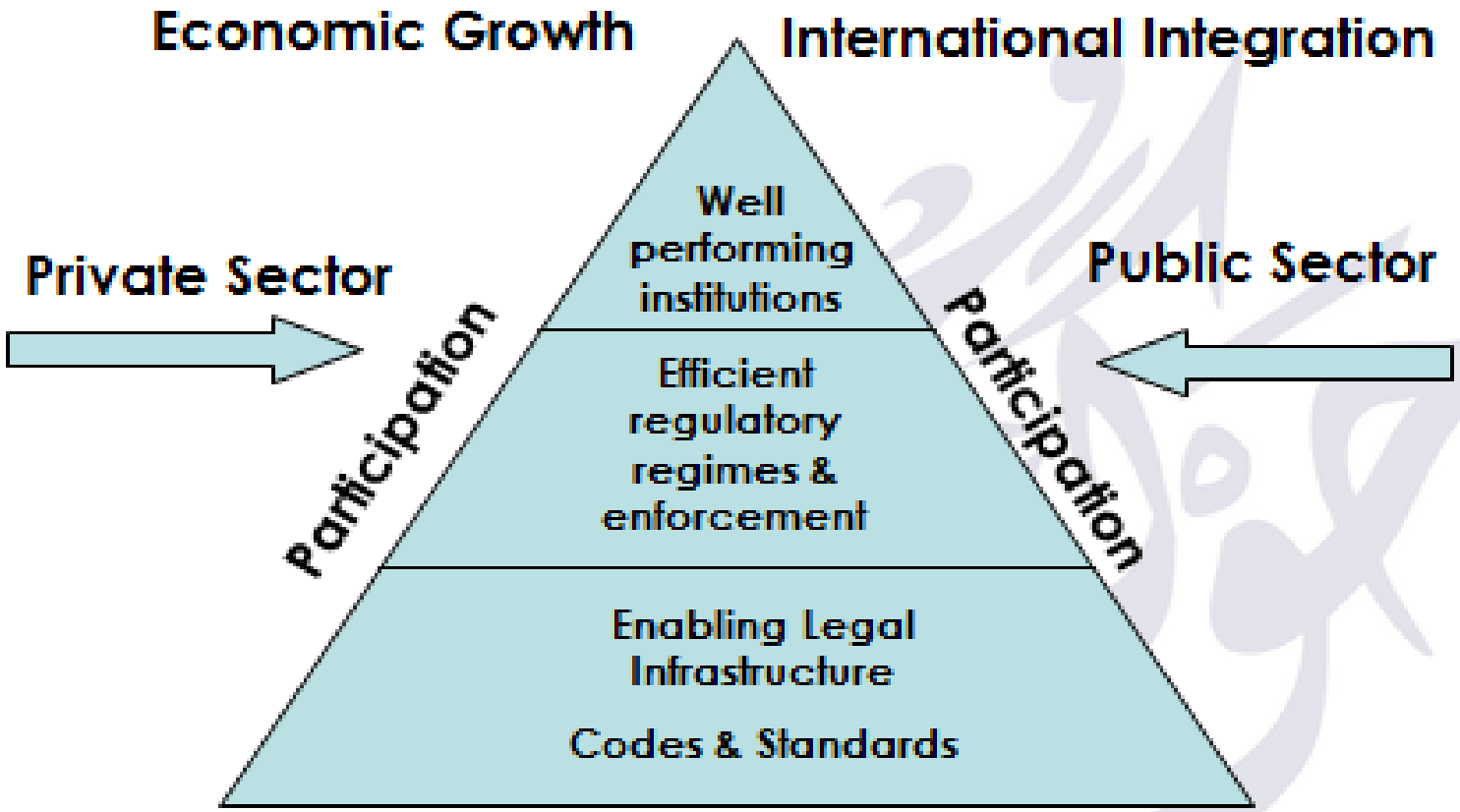
Implications for the MENA region

- International best practices on corporate governance are evolving. We must understand what these emerging practices mean for the MENA region, what we can learn & do about them, what is relevant to our markets & economies, and how the other emerging market economies have responded.
- **Revise the GCC CG Codes** (as they pre-date the crisis) to take account of developments in international best practices, especially in areas of Board competence and risk management.
- **Tighter CG standards are needed for financial institutions (Hawkamah Policy Brief) and listed companies.**
- **Extend CG frameworks beyond listed companies – SOEs & Banks**
- **Ensure Compliance** with CG standards & guidelines
- Establish a **GCC common Corporate Governance Standard**.

Why Does Corporate Governance matter?

- Economic development & growth require deepening the region's financial markets, changes in banking relations, and generalised openness towards trade & investment– these all require good corporate governance.
- Well performing institutions, enabling legal & physical infrastructure, regulatory regimes and enforcement, "good governance" are major contributors to economic growth & prosperity and accountability.
- Companies with good corporate governance outperform and survive crises- including family succession crises
- "Good governance" is required by both the public sector and the private sector in the MENA

Governance is integral element of sustainable economic growth & development: it is an imperative



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Investment in MENA

- The MENA region has been a significant capital exporter for decades, but we have not been very good at accommodating inward capital flows or retaining and deploying our own capital resources for economic development and sustaining economic growth.
- The region is overlooked by global investors despite its natural resource wealth, positive demographics and promising growth prospects.
- This **marginalization of MENA has much to do with a perceived lack of good corporate governance**, lack of transparency, disclosure and accountability .

Investors need transparent markets

- There is a symbiotic relationship between **market information and market efficiency.**
- Better availability, timeliness & quality information to the market improves resource allocation and the economic efficiency of workers, consumers, and producers.
- **Transparency, disclosure and accountability are key elements in enhancing investor confidence** and improved credit ratings, in turn these result in: lower capital costs, improved access to and lower cost of finance, increased attractiveness to FDI, greater financial stability and long-term growth.

Drivers of Good Corporate Governance

- GCC is dominated by state-owned and close-family companies, which coupled with weak market & judiciary institutions means that there has never been an urgency to implement corporate governance.
- Investors, who often are the drivers of good corporate governance, shun the region because of lack of corporate governance.
- Therefore, corporate governance reform in the MENA must be government/regulatory driven.

What type of investors to attract: “Patient Capital”

- **Hedge funds** often own the shares for a very short period
- **Passive funds** or **index funds** hold stocks by certain criteria but can lead to ‘herd mentality’
- **Active managers** with 2-3 year holding patterns
- **Want Institutional Investors:**
- **Insurance companies** often have longer investment horizons
- **Pension funds** typically might hold a shares for several years.

Understanding the Needs of Long-Term Investors

- For pension funds & institutional investors, the debate has moved beyond just good corporate governance.
- They need not only know that the company is well-governed with strong internal controls and auditing processes, but that it is one that manages relationships with its employees, customers and the communities in which it operates, and has a strong regard for the environmental impacts of its business.
- It is becoming widely accepted among investors that **Environmental, Social and Corporate Governance** (ESG) factors have crucial impact on the bottom line & business sustainability.
- A recent IFC survey: 82% of surveyed asset owners say that ESG assessment will become significantly more important in their research, portfolio management and manager-selection process over the next three years.
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The Value of ESG & its Failure/Neglect

S&P/Hawkamah ESG Pan Arab Index

- Hawkamah in partnership with Standard & Poor's and with the support of the International Finance Corporation have launched an exchange tradable Environmental, Social and Corporate Governance (ESG) Index for the MENA region.
- Represents painstaking work undertaken over 18 months!
- The **S&P/Hawkamah ESG Pan Arab Index is the first Pan Arab Index of its kind**. It ranks and tracks the performance, transparency and disclosure of **50 regional companies** on ESG issues.
- The constituents of this Index are filtered/derived from 450 listed companies from 11 countries' stock exchanges: Bahrain, Egypt, Jordan, Lebanon, Kuwait, Morocco, Oman, Qatar, Saudi Arabia, Tunisia and the United Arab Emirates.
- Liquidity screen of a minimum average daily value traded of US$ 100,000, measured over one calendar year.

A Tool for Investors

- Addresses the ‘elephant’ in the room
- Provides an extra layer of assurance by using tried & tested ESG methodology
- Facilitates investment in the region by “patient capital” institutional investors such as pension funds
- Hawkamah-S&P Index helps investors who lack of resources or know-how to adopt a passive ESG policy.
- Indexing is a low cost strategy which requires relatively little monitoring and management on the part of the asset owner, and the use of specialised indices is seen as a relatively easy way to incorporate ESG factors into a passive mandate.

What the ESG Index means for companies

- An Index relates companies ESG performance to stock market performance
- Allows companies to compare themselves to ESG Index companies
- An Index can create incentives for companies to improve ESG performance
- An index has assets attached to it, raising the cost of capital for those that are not on the index
- An index creates a public list of leaders and therefore laggards, driving companies to be on “the list”
- A badge of honor, demonstrating leadership on ESG

THE NEXT STEPS

- **Revision & Strengthening of CG Codes**
- **Establishment by regulators of corporate governance compliance units**.
- **Board members should be accredited**: Supervisors should ensure that boards are staffed with competent individuals, who receive on-going professional development - Mudara Institute of Directors
- **Regulators need to embrace good governance themselves** – they need to have clear roles, mandates and lines of accountability, and staffed with competent personnel. Above all, they need to be effective, transparent and predictable.
- **Banks, SWFs, investment funds & asset managers should incorporate corporate governance/ESG criteria** into their investment and lending criteria. Banks can play a central role in instilling a culture of good corporate governance in the region.

THANK YOU FOR YOUR SUPPORT IN HELPING US BUILD INSTITUTIONS FOR THE REGION

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