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**EFFECT OF CORPORATE GOVERNANCE FACTORS AND MSWG ACTIVISM ON
CUMULATIVE ABNORMAL RETURNS INDUCED BY RELATED PARTY
TRANSACTION**

10 FEB 2016

By
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**Thesis Submitted to
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OTHMAN YEOP ABDULLAH GRADUATE SCHOOL OF BUSINESS
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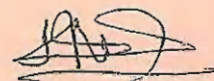
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ABSTRACT

This is an event study that examines the effects of related party transaction (RPT) and corporate governance factors in a firm's daily cumulative abnormal return of the stock price (CAR), using a sample of 422 RPTs engaged by 286 listed firms in the Main Market of Bursa Malaysia from 2008 to 2013. Univariate analysis (t-test) is used to determine the RPT's announcement effect on CAR in the short horizon window, and ordinary least squares (OLS) and logistic regression are employed to investigate the relationships between the firm's CAR and exogenous variables of RPT types and size, Minority Shareholder Watchdog Group (MSWG) activism, and corporate governance factors. The univariate result shows significant negative effects on CAR in the post-announcement of RPT, indicating governance discount of stock prices by the market in realizing the occurrence of expropriation, in particular asset acquisition and cash-payment types of RPT. The regression results show that cash ownership of the dominant owner and the divergence of control to cash right for the dominant owner and the directors have a significant negative relationship with CAR. This contributes to extant researches in emerging markets with findings that the problems of expropriation are mainly attributed to circumstances of high dominant family ownerships, which is further exacerbated by the entrenchment of the controlling shareholders and directors. This study also adds to the literature by showing evidence that MSWG activism, which results in higher firm's disclosure quality, has a significant positive effect on CAR in mitigating the expropriating behaviour of the controlling shareholders. Furthermore, the significant positive relationship between board independence and CAR also reinforces previous research findings that increasing the independence of the board enhances its effectiveness as an advocate for minority shareholders' interest. Finally, clear evidence was found that participation of the state's block holders or public investment fund contributes positively to the deterrence of expropriation by the dominant owner.

Keywords: Related party transaction, MSWG, CAR

ABSTRAK

Kajian ini dijalankan untuk menyelidik kesan urusan pihak berkaitan (RPT) dan faktor urus tadbir korporat ke atas pulangan abnormal kumulatif harian harga saham (CAR) dengan menggunakan sampel sebanyak 422 RPT yang melibatkan 286 buah syarikat yang tersenarai di Pasaran Utama Bursa Malaysia dari tahun 2008 hingga tahun 2013. Analisis univariat telah digunakan untuk menentukan sama ada pengumuman RPT memberi kesan terhadap CAR dalam tempoh masa yang singkat. Kuasa dua terkecil biasa (OLS) dan regresi logistik digunakan dalam kajian ini untuk meneliti hubungan antara CAR syarikat dengan pemboleh ubah eksogen, iaitu jenis dan saiz RPT, aktivisme Badan Pengawas Pemegang Saham Minoriti (MSWG), dan faktor urus tadbir korporat. Dapatan univariat menunjukkan RPT menyebabkan terdapat kesan negatif yang signifikan terhadap CAR semasa pascapengumuman RPT. Hal ini memperlihatkan bahawa terdapat diskaun urus tadbir ke atas harga saham dan kewujudan ekspropriasi. Hasil regresi pula memaparkan bahawa pemilikan tunai oleh pemegang saham yang dominan dan pemisahan kawalan dari tunai oleh pemegang saham yang dominan dan para pengarah mempunyai hubungan negatif yang signifikan terhadap CAR. Hasil kajian ini menyokong penyelidikan sedia ada yang membuktikan bahawa masalah ekspropriasi yang disebabkan oleh pemilikan keluarga yang dominan serta tinggi. Keadaan ini diburukkan lagi dengan penguasaan daripada pemegang saham majoriti dan para pengarah. Kajian ini turut menambah kosa ilmu sedia ada dengan memperlihatkan bahawa aktivisme MSWG yang menghasilkan kualiti pendedahan firma yang lebih tinggi memberikan kesan positif yang signifikan terhadap CAR. Ini menunjukkan bahawa MSWG dapat mengurangkan masalah ekspropriasi dalam kalangan pemegang saham majoriti. Di samping itu, hubungan positif yang signifikan antara CAR dengan kebebasan lembaga pengarah juga mengukuhkan hasil penyelidikan sebelum ini berhubung kepentingan kebebasan lembaga dalam meningkatkan keberkesanannya untuk melindungi kepentingan pemegang saham minoriti. Akhir sekali, terdapat bukti yang jelas bahawa penyertaan pemegang saham blok atau dana pelaburan awam dapat mengurangkan masalah ekspropriasi oleh pemilik yang dominan secara positif.

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Kata kunci: Urusniaga pihak berkaitan, MSWG, CAR

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ACId	: Audit Committee Independence Dummy
AGM	: Annual General Meeting
ASRPTd	: Asset Sales Related Party Transaction Dummy
BIND	: Board independence
BMSB	: Bursa Malaysia Securities Berhad
BS	: Board Size
CAR	: Cumulative Abnormal Return of Stock Prices
CCM	: Company Commission Malaysia
CEO	: Chief Executive Officer
CEODd	: CEO Duality Dummy
CFO	: Chief Financial Officer
CG	: Corporate Governance
CMDf	: Capital Market Development Fund
COBH	: Cash Ownership of Block Holders
CODIR	: Cash Ownership of Directors
CODO	: Cash Ownership of Dominant Owner
COGLIC	: Cash Ownership of Government Linked Investor or State Government
CPRPTd	: Cash Payment Related Party Transaction Dummy
CRRPTd	: Cash Receipts Related Party Transaction Dummy
DCRDIR=1d	: Divergence of Control to Cash Right for Director = 1 Dummy
DCRDIR>1d	: Divergence of Control to Cash Right for Director > 1 Dummy
DCRDO	: Divergence of Control to Cash Right for Dominant Owner
DOviaUCd	: Share Held by Dominant Owner via Unlisted Company Dummy
EGM	: Extraordinary General Meeting
EPF	: Employee Provident Fund
ESRPTd	: Equity Sales Related Party Transaction Dummy
FBMEMAS	: FTSE - Bursa Malaysia Emas Index
FBMKLCI	: FTSE - Bursa Malaysia Kuala Lumpur Composite Index
FDC	: Family Director Concentration
FSIZE	: Firm Size
GLCs	: Government-Linked Corporations
GLICs	: Government-Linked Institutional Companies
IPO	: Initial Public Offering
ISS	: Institutional Shareholder Services
KWAP	: Kumpulan Wang Amanah Pencen (Civil Pension Fund)
LEV	: Leverage
LGRPTd	: Loan Guarantee Related Party Transaction Dummy
LVDRPTd	: Likelihood of Value-Destroying Related Party Transaction Dummy
MCCG	: Malaysian Code of Corporate Governance

MCG	: Malaysia Corporate Governance
MD	: Managing Director
MSWG	: Minority Shareholder Watchdog Group
MSWGd	: Minority Shareholder Watchdog Group Dummy
NCLS	: Non-Controlling Large Shareholders
NPV	: Net Present Value
OLS	: Ordinary Least Square
PNSBHd	: Presence of Non-State Block Holder Dummy
ROA	: Return on Assets
ROE	: Return on Equity
RPT	: Related Party Transaction
SOE	: State-Owned Enterprises
SRPT	: Size of Related Party Transaction
SRRPTd	: Subsidiary Relationship Related Party Transaction Dummy
SUBPRIMEd	: US Subprime Crisis Years (2008 & 2009) Dummy
SWF	: Sovereign Wealth Funds
TO&JVRPTd	: Takeover Offers & Joint Ventures Related Party Transaction Dummy
TRRPTd	: Trading Relationship Related Party Transaction Dummy
VIF	: Variance Inflation Factor



CHAPTER 1: INTRODUCTION

1.1 Introduction

What is minority interest protection quality, its significance and implication on a country's security market development?

A developed securities market in a country is related to the establishment of a credible governance and enforcement rules designed to protect the interest of the minority investors, (Crocì & Petmezas, 2010). From a macroeconomic perspective, poor corporate governance and legal enforcement will result in liquidity and turnover problems, which deprive firms from financing valuable growth opportunities (Modigliani & Perotti, 1997). Besides obtaining less financing, the firm will invest less in intangible assets, whereby Claessens and Laeven (2003) found such pattern will eventually have an adverse influence on the economic expansion of a country. Furthermore, Lemmon and Lins (2008) showed that a crisis or a negative shock in the weak market raises incentive of insiders or controlling shareholders to expropriate minority shareholders to compensate for their loss.

According to the classic *'The Modern Corporation & Private Property'* by Berle and Means (1932/1967), which is the foundational theory of corporate governance and institutional economics, dispersal shareholding ownership will result in management and directors managing the firm's assets and business to the owner's benefits with minimum oversight from investors:

“The property owner who invests in a modern corporation so far surrenders his wealth to those in control of the corporation that he has exchanged the position of independent owner of one in which he may become merely recipient of the wages of capital.. [Such owners] has surrendered the right that the corporation should be operated in their sole interest...” (p.355, 1932 edition)

“the owners most emphatically will not be served by a profit seeking controlling group” (p.114, 1967 edition)

The implication was they advocate embedded privileges of investors to vote, and a better

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