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Invisible Hands behind the Corporate Governance Practices in Malaysia

Sheila Nu Nu Htay[1], Syed Ahmed Salman[2] and Ibrahim Shaugee

The issues of corporate governance became very popular in the corporate world in UK, USA and Europe during the last two decades. With the opening up of economies and liberalization, the concern for corporate governance also spread to the developing world. Therefore, most of the developed and developing countries, including Malaysia have laid down corporate governance guidelines to enhance the current governance practices. Based on the analysis of the contents in the corporate governance codes, most of the recommendations are founded on the concept of agency theory. Unfortunately, the majority of the findings of researchers show that the results are not in line with the theoretical expectations. In Malaysia, Malaysian Code on Corporate Governance was introduced in 1998 and eventually; it has been amended in 2000 and 2007. However, some of the findings on corporate governance in Malaysia are not in line with the recommendations of the Code. Thus, this study examines the possible reasons that hinder current corporate governance system less effective in Malaysia. The main reasons for this problem are due to nature of ownership structure, political and culture background of Malaysia and the adoption of unsuitable foreign corporate governance template. The findings of this research will be useful for the regulators to develop future rules and regulations and implement them accordingly.

Field of Research: Agency theory, corporate governance, banks

1. Introduction

Corporate governance is recognized as a heart of the corporation since the board of directors is the top leaders of any company and mainly responsible to lay down the strategic planning. The issues of corporate governance became very popular in the corporate world in UK, USA and Europe during the last two decades. With the opening up of economies and liberalization, the concern for corporate governance also spread to the developing world. Thus, the researcher opines that the quality of corporate governance has become a critical success factor for the survival of businesses in any business sector. Dwived and Jain (2003) state that the quality of corporate governance has become a major factor in influencing the ability of a company to raise funds from capital markets, to narrow the gap between agents' and principals' interests, to recover faster from economic crises, and to build a stronger financial system and economy that will be less susceptible to further crises.

Due to the essential nature of effective corporate governance, many developed and developing countries have produced corporate governance guidelines and codes of best practice for their own countries. In Malaysia, the important role of corporate governance has been given attention due to the 1997/98 Asian financial crisis.

[1] Assistant Professor, IIUM Institute of Islamic Banking and Finance, International Islamic University Malaysia, (sheila@iium.edu.my or sheilay7@yahoo.ca)
[2] Syed Ahmed Salman is a PhD candidate, IIUM Institute of Islamic Banking and Finance , International Islamic University Malaysia, (salmaniium@gmail.com)

Although very strict regulations are gradually imposed on the board of directors, it seems that the loopholes of the unethical conducts of directors could not be hindered. It has been proven by corporate failures such as Enron, Swissair, the Worldcom, Global Crossing Ltd., Healthsouth, Pamalat, Jinro Ltd, and Tyco international companies. Furthermore, many countries have developed corporate governance guidelines mainly derived from the agency theory aspect, which is dominant theory in the corporate governance issues. However, the findings of many research are mixed, i.e. some are in line with theory while some are not, especially in the Malaysian banking sector. Therefore, we are motivated to examine to what extend the agency theory is applicable in Malaysian context since this theory is founded on Anglo-American business environment and examines what are the invisible hands behind board of directors that make current corporate governance system weak.

This research paper is organized in six sections. The second section mentions the important role of directors in corporate governance. The third section explains the agency theory and its concepts in corporate governance. The fourth section further elaborates corporate governance literature. The fifth section explores on the invisible situations behind corporate governance in Malaysia and the last section concludes.

2. Important Roles of Directors in Corporate Governance

Having a good corporate governance system in a company is a critical issue because poor corporate governance system may lead to corporate failure, which affects the wealth of the shareholders, in particular, as well as the welfare of other stakeholders, in general. This is demonstrated by the recent corporate failures, for instance, Enron, Swissair, the Worldcom, Global Crossing Ltd., Healthsouth, Pamalat, Jinro Ltd, and Tyco international companies (Spremann, 2002; Petra, 2005; Centre for Financial Market Integrity, 2005; Sang, 2005; Williams, Duncan, Ginter & Shewchuk, 2006). Practising good corporate governance is important to safeguard all parties and to ensure the sound economy of the country and this is the responsibility of directors.

The importance of the role of board of directors has been discussed in the literature since aligning the interests of managers and shareholders requires vigilant, independent, and effective boards (Rezaee, 2003). Bai, Liu, Lu, Song, and Zhang (2004) state that “the board of directors is the first instrument through which shareholders can exert influence on the behavior of managers in order to ensure that the company is run in their interests.” Similarly, Whittington (1993) and Ruin (2001) assert that a group of directors, as a corporate control, is selected by the shareholders to monitor the performance of the management on their behalf. The directors become the agents of the shareholders to fulfill the interest of the principals (i.e. shareholders) and they are directly accountable to the shareholders. Accordingly, directors are responsible for supervising the activities of the management by providing proper and strategic instructions and then checking and monitoring how the management uses the assets to maximize the benefits of the shareholders (Lefort & Urzua, 2008). Hemraj (2003) also elaborates that directors are responsible to (a) safeguard the assets of the company, (b) prevent and detect fraud and other irregularities, and (c) maintain adequate accounting records. Hence, effective board is essential for the betterment of the companies. It is supported by

Weir (1997), Sharma (2004), Shamsul Nahar (2006), Sharma (2006), Wang and Deng (2006), and Charitou, Louca and Vafeas (2007).
Epstein and Roy (2004) state the core objectives of board are to provide superior strategic guidance in order to ensure the company's growth and prosperity, ensure accountability of the company to its stakeholders and ensure a highly qualified executive team in managing the company. Banaga, Ray and Tomkins (1995) and Tricker (2000) also mention that the directors should play their roles for the betterment of the company. They are the performance role (i.e. the board focuses on strategic and policy issues for the future and setting the corporate direction as well as contributing to the performance of the business) and the conformance role (i.e. the board ensures that the company is conforming to policies, procedures, and plans laid down by the board and is properly accountable for its activities).

Directors are still accountable for the integrity of financial reporting system, which limits top management's discretion, constraining top management to act in shareholders' interest, in particular, and stakeholders' interest, in general (Melis, 2004). Furthermore, the inclusion of board members in the audit committee puts more responsibility on the shoulders of the board of directors. According to Ruin (2001), the aim of this committee is to enhance effective corporate governance. Some of its functions are to monitor the integrity of companies' financial statements, review companies' internal audit functions, make recommendations to the board in relation to the appointment of the external auditor, and review the maintenance of accounting and operational systems and effective controls (Solomon & Solomon, 2004). Therefore, it could be summarized that this committee oversees financial reporting, internal control, and audit functions.

3. Agency Theory and Corporate Governance

According to Jensen and Meckling (1976), the agency relationship is defined as a contract under which one party (the principal) engages another party (the agent) to perform some services on the principal's behalf. The directors as agents are directly responsible for the smooth running of the company, which is in line with the interests of the shareholders who are the owners. However, due to the separation of ownership and control, agency problems, i.e. moral hazard and adverse selection, could occur and directors might maximize their own interests at the expense of the shareholders (Millson & Ward, 2005). Thus, the main issue from the agency theory is the existence of agency cost (Mueller, 2006; Williams et al., 2006). There should be some mechanisms that align the interests of principals and agents (Judge et al., 2003). The suggested mechanism is good corporate governance by which this conflict of interest can be resolved to a certain extent (Gursoy & Aydogan, 2002) since it promotes goal congruence (Conyon & Schwalbach, 2000; Cheung & Chan, 2004).

Among the mechanisms to reduce the agency conflict between the directors and the owners of the companies, the recommendations of the agency theory for the separate board leadership structure, involvement of independent non-executive directors in board composition, board size and ownership are discussed.

3.1 Board Leadership Structure: Agency Theory Perspective

The agency theory argues for a clear separation of the responsibilities of the CEO and the chairman of the board and seems to prefer to have the separate leadership structure (Jensen & Meckling, 1976; Fama & Jensen, 1983; Jensen, 1993). If the CEO and the chairman of the board is the same person, there would be no other individual to monitor CEO's actions and then CEO will be very powerful and may maximize his or her own interests at the expense of the shareholders. Therefore, the combined leadership structure promotes CEO entrenchment by reducing board monitoring effectiveness (Finkelstein & D' Aveni, 1994; Florackis & Ozkan, 2004; Dalton & Dalton, 2005; Nor Hashimah, Norman, Jaffar and Mohamat Sabri, 2007).

3.2 Board Composition: Agency Theory Perspective

According to Choe and Lee (2003), board composition is very important to effectively monitor the managers and reduce the agency cost. Although the executive directors have specialized skills, expertise and valuable knowledge of the firms' operating policies and day-to-day activities, there is a need for the independent persons to contribute the fresh ideas, objectivity and expertise gained from their own fields (Weir, 1997; Firth, Fung, and Rui, 2002; Cho, & Kim, 2003; Nathan, 2005; Hillier & McColgan, 2006; Nor Hashimah et al., 2007). In the Malaysian context, the independence of the directors means independence from management as well as from a significant shareholding (Seong, 2003). Agency theory recommends the involvement of independent non-executive directors to promote the independence of the board from management. The reason for this issue is that if the majority of the board members are executives of the company, the board will be more likely to be manipulated by managers and the decision made by the board might be biased and it might favor the interest of the management, not the shareholders (Le, Walters and Kroll, 2006). Thus, there should be a higher proportion of independent non-executive directors (Kiel & Nicholson, 2003; Florackis & Ozkan, 2004; Williams et al. 2006; Nor Hashimah et al., 2007).

3.3 Board Size: Agency Theory Perspective

Agency theory asks for the independence of the board from the management and hence, the board should have the optimal number of directors to monitor the management effectively and independently. According to Mak and Li (2001) by referring to Jensen (1983) and Florackis and Ozkan (2004), boards with more than about seven to eight members are unlikely to be effective. They further elaborate that large boards result in less effective coordination, communication, and decision making, and are more likely controlled by the CEO. Lipton and Lorsch (1992) in Yoshikawa and Phan (2003) also highlight that larger boards tend to be lesser cohesive and more difficult to coordinate because there might be the large number of potential interactions and conflicts among the group members. In sum, smaller boards seem to be more conducive for board member participation and thus would result in a positive impact on the monitoring function and the strategic decision-making capability of the board, and independence from the management (Huther, 1997).

3.4 Ownership: Agency Theory Perspective

The agency theory stresses the problems that could arise due to the separation of ownership and control. If the directors own the shares, the directors as the owners themselves are directly instructing and monitoring the management of the companies (Jensen & Meckling, 1976). Hence, there are likely to be fewer agency problems compared to the situation whereby the directors, who are not the owners, supervise the management of the company. It is also supported by Seifert, Gonenc and Wright (2005) who discuss the agency conflicts.

Regarding block ownership, if an individual has a substantial amount of interest in a particular company, he or she will be more interested in the performance of the company, compared to the shareholders who own a smaller number of shares because dispersed ownership may have less incentives to monitor management (Kang & Sorensen, 1999; Maher & Andersson, 1999; Kim & Lee, 2003). It is supported by Gorton and Schmid (1999), who study the relationship between corporate governance and ownership dispersion in the Austrian cooperative banking sector. They find that firm performance declines as the numbers of cooperative members increase, corresponding to a greater separation of ownership and control. The same result is found by Joh (2003) since his findings show that firms with low ownership concentration results in low firm profitability. Furthermore, Florackis and Ozkan (2008) find that ownership concentration seems to play an important role in mitigating agency cost. For this reason, block ownership might play an important role to monitor the management effectively.

Regarding the institutional investors, Salleh and Mallin (2002), Kim and Nofsinger (2004), Leng (2004), Soloman and Solomon (2004), Seifert et al. (2005) and Le et al. (2006) collectively agree institutional shareholders can play an important role in monitoring of firms' operations because institutional shareholders normally own substantial number of shares, the potential benefits from their activism is large enough to be worth their effort, they have less ability than individual shareholders to liquidate the shares without affecting the share price, as their influence on company management can be substantial and can be used to align management interests with those of the shareholder group, they seem to have a fiduciary responsibility towards the ultimate owners since they are the trustees of the beneficiaries and they are professionals and so they have ability to monitor executives.

4. Corporate Governance Literature

Based on the agency theory and corporate governance guidelines, corporate governance variables such as separate board leadership structure, higher proportion of independent directors, smaller board size and ownership variables such as higher ownership by directors, institutional shareholders and block shareholders are able to contribute positive impacts on the companies. However, when prior researchers examine on the impacts of the above-mentioned variables, findings are not in line with the expectation.

In the case of research examining the relationship between board leadership structure and performance of the firms, Coles, McWilliams and Sen (2001), Dehaene, Vuyst and Ooghe (2001), Bozec and Dia (2005), Leng and Shazaili (2005) and Htay (2009) find that combined leadership structure has significantly higher performance. Hence, their findings are not in line with the expectation from the agency theory as well as most of the codes.

Similarly, Braga-Alves and Shastri (2011) find that smaller board size do not contribute to the better performance of the firms. When the impact of board composition on firm performance, Hermalin and Weisbach (1991), Vafeas and Theodorou (1998), Raja Azimah and Nor Liza (2002), Yoshikawa and Phan (2003), Shamsul Nahar (2004), Andres, Azofra, and Lopez (2005), Rose (2005), Vethanayagam, Sofri and Hasnah (2006), and Afzalur et.al (2010) find that board composition does not seem to have any relation or influence on firm performance. In addition, the findings of Coles et al. (2001), Evans, Evans and Loh (2002), Judge et al. (2003), Peng, Buck and Filatotchev (2003) and Htay (2009) do not support that firms with higher proportion of independent non-executive directors have better performance. Chiang (2005), Rose (2005) and Khaled and Mohamed (2007) find that board size has no significant impact on performance.

The studies conducted by Vafeas and Theodorou (1998) find that the percentage of stock ownership by executives is unrelated to performance. Similarly, Vethanayagam et al. (2006) found that the interaction between director ownership and performance is not significant. Empirical findings of Hirschey (1999), Coles et al. (2001), Evans et al. (2002), Hamadi (2002), Ho and Williams (2003), Seifert el al. (2005) and Barako Tower (2007) do not seem to be in line with theoretical expectation. This means that their results do not support that there is a positive relationship between director ownership and performance.

In the case of institutional ownership, the studies conducted by Xu and Wang (1999), Dwivedi and Jain (2003), Patibandla (2006), Barako Tower (2007) and Htay (2009) find that there is a negative relationship between government ownership and performance. Other studies conducted by Dwivedi and Jain (2003) and Chiang (2005) do not support the positive relationship between institutional ownership and performance.

Regarding block ownership, the studies conducted by Hovey, Li and Naughton (2003), and Lskavyan and Spatareanu (2006) show that there is no relationship between block ownership and performance. Moreover, Salim (2007), Htay (2009) and Alireza et al. (2011) find that there is a negative relationship between block ownership and market performance at ten percent significant level. He further provides the possible reason for this negative relationship is that the block holders may have strong incentives to divert the resources for their betterment at the expense of minority shareholders.

In sum, it can be concluded that findings in corporate governance area are not supporting the recommendations of governance codes, including the studies conducted in Malaysia. Therefore, the next section explores on why agency theory is not fully applicable in Malaysia and the current situations in Malaysia that make current MCCG (2001) less effective.

5. Invisible Situations behind Corporate Governance in Malaysia

5.1 Agency theory and Malaysian Market Situations

Agency theory represents an attractive platform for structuring corporate governance systems. This theory seems to be Anglo-American centric, grounded in capitalistic theory (Mccarthy & Puffer, 2008) and insensitive to non-economic forces that drive managerial choices in mixed (socialist/ capitalist) economies. It could be explained that corporate governance systems are not converging and (Yoshikawa & Phan, 2003) and consequently, local laws and local business environment might influence the governance system in its own country (Seifert et al., 2005). Therefore, it can be inferred that it is difficult to conclude governance system derived from the agency theory is the best since it depends on the needs and culture of the companies as well as local prevailing laws and business environment. The findings of Firth et al. (2002) seem to support above opinion since the results show that the corporate control mechanisms vary systematically across firms.

In addition, agency theory is Anglo-American centric where the market is efficient. In addition to the publicly available information, there are many financial analysts working for mutual funds, pension funds and other intermediaries who gather private information. The empirical evidence from efficient markets suggests that much of this information is reflected in stock price. On the contrary, Malaysian market is not efficient. Findings of Balkiz (2003) show that KLSE is inefficient when using daily composite index for the period of 1st January 1977 to 3rd May 2002. The results of the studies by Lim (1980), Lonjong (1983) and Laurence (1986) highlighted in Balkiz's (2003) paper show that KLSE is weak from efficient for active stocks. Moreover, unlike U.S., most media business in Malaysia are unlikely to disclose accurate, precise and controversial aspects of affiliated companies with media and so such constraint becomes another inadequacy in its corporate governance system (Singam, 2003).

5.2 Foreign Template MCCG (2007) and Law Reforms in Malaysia

MCCG (2007) is the code issued to help the companies recover faster from the crisis, to build a stronger financial system and economy that will be less susceptible to further crises and to re-invent the corporate enterprise in order to efficiently meet emerging global competition. Unfortunately, the code seems to be the British template which is not wholly appropriate for Malaysia's governance problems. It is because there are differences between U.K. and Malaysia in terms of shareholding structure as well as economic, political and cultural differences. Additionally, unlike U.K, in Malaysia, the biggest agency problem is between the controlling shareholders and minority shareholders, not between directors and shareholders since real control of Malaysian companies is exercised by majority or controlling shareholders and not directors. And hence, a code which mainly focuses on the shareholder-director agency conflict may not be wholly appropriate in a corporate environment. Therefore, the transplanted system which has as its focus the agency problem of directors-shareholders conflict is inappropriate for the concentrated nature of Malaysia's companies (Mohammad Rizal, 2006). Similarly, Liew (2006) also discusses that the promotion of corporate governance reform in Malaysia does not seem to provide the solutions for the specific local problems in the country. There is a need for a different approach to corporate governance reform if the processes adopted are to be applicable and suitable for Malaysia.

A few researchers such as Shamsul Nahar (2004), Norman et al. (2005) and Mohammad Rizal (2006) mention about the problems of the existing code. According to Shamsul Nahar (2004), among Malaysian companies, it is very difficult to find outside directors who are truly independent as Malaysian companies are very closely held and are mostly family controlled. He further states that evidence in Malaysia on effectiveness of the board in discharging their duties with regard to financial reporting is very limited and role of independent directors and their effectiveness in carrying out the duties is not clear. Norman et al. (2005) also assert in their paper that the code needs to be more specific about the characteristics of independent directors that may have a strong influence on the actions of CEO-Chairman. Mohammad Rizal (2006) also highlights some important problems of the existing code. The code acknowledges the difficulties posed by ownership concentration and by the presence of significant shareholder but does not propose any recommendations to overcome these difficulties or a plan to tackle the issue. The concept of independent non-executive directors which is borrowed from the Anglo-American should expand its concept of independence by including specific clause such as independent from significant shareholder as well as from management.

According to Ponnu and Ramthandin (2008), there should be stricter securities regulations, reforms in company law, stringent accounting practices and auditing standards, tighter bankruptcy law and stronger judicial enforcement in order to bring better corporate governance system in Malaysia.

5.3 Situations that Make Corporate Governance System less Effective in Malaysia

Some of the situations that make corporate governance system less effective in Malaysia are political problems, ownership problems as well as culture. They are discussed in the following paragraphs.

5.3.1 Political Problems

Regarding the political problems, Liew (2006) points out that political nepotism, cronyism and corruption are common in Malaysia since political leaders are constantly able to maneuver and transfer corporate assets into the hands of their allies. He further discusses that the regulatory institutions can be used as tools by powerful politicians for their own vested interests and to ensure that the regulatory bodies do not act against favored businessmen. Mohammad Rizal (2006) discusses further that the largest listed companies in Malaysia may be blocked into three main types: state-controlled, Chinese controlled and Malay controlled companies. State-controlled listed companies are in the main privatized companies in which the state retains majority shares and are controlled by the bureaucrats or dominant personalities within the ruling government. This control is exercised not only through the appointment of directors, but also by decision-making on policies and strategies. As to large Chinese and Malays-controlled companies, many are politically connected which creates governance problems as a result of political or state involvement in these companies. Based on the current scenario, the politics and the business are jointly connected and cannot be separated (The Asian Productivity Organization, 2007) and to implement the corporate governance system effectively in Malaysia, it is necessary to have the policies that strictly limit or eliminate the power and influence of bureaucrats and dominant owner-managers or top management in businesses as well as the policies that ensure the independence of regulators.

5.3.2 Ownership Problems

The ownership problems make the governance system less effective in Malaysia. Some of the problems, i.e. (a) ownership concentration, (b) family ownership, (c) the characteristics of ownership composition, (d) Chinese business culture related to ownership structure and their norms and (e) the nature of insider control firms are discussed in the following paragraphs.

5.3.2.1 Ownership Concentration

The first problem is ownership concentration in Malaysia. According to Allen and Gale (2001), their findings show that there is a negative correlation between the extent of minority shareholder protection and concentrated equity ownership. Furthermore, Lai (2004) asserts that in Malaysia, the agency problem might be between the minority and majority shareholders.

According to Singam (2003), the fundamental problem of ownership concentration is the potential expropriation of minority shareholders' rights by the controlling shareholders such as paying themselves special dividends, committing the company into disadvantages business relationship with other companies on which they can control and taking on excessively risky projects. Lefort and Urzua (2008) also mention that board of companies with high ownership concentration will tend to be mostly comprised of directors who represent the owner-managers' interests and thus it might not be in line with the interest of minority shareholders. Similarly, Zulkarnain (2007) asserts in his paper that due to ownership concentration, separation of management from ownership control is rare in Malaysia and that results in weak corporate governance system.

5.3.2.2 Family Ownership

The second problem is related to family ownership. There is a substantial family corporate holding which is common in Malaysia, whereby ownership is achieved through holding or nominee companies (Singam (2003)). Furthermore, Mohammad Rizal (2006) states that Chinese family companies are tightly controlled by individual or family members even though the company is publicly listed. In these companies, there is no real separation between family and company interests, and results in a management culture which is biased towards the families' interests rather than that of the companies.

5.3.2.3 Characteristics of Ownership Composition

The third problem is the character of ownership composition which creates a unique problem in the Malaysian corporate governance system. The implementation of the New Economic Policy or Bumiputra Policy results in a significant shift in the balance of ownership towards the bumiputra ownership and hence, composition of shareholdings is changed. This policy makes the current corporate governance system more difficult to achieve a sound system in Malaysia. It is because the implementation of this policy increases the involvement of governmental and political influence into the business environment in Malaysia by including prominent bumiputras such as ex-bareaucrats or politicians, on their boards, in many Chinese companies and conglomerates (Singam (2003).

5.3.2.4 Chinese Family Business Culture

The fourth problem is related to the culture of Chinese family business since it has high economic influence and it is the back bone of the Malaysian economy since Chinese control sixty percent of the private, corporate and domestic share capital of the nation's economy (Singam, 2003; Lai, 2004; Mohammad Rizal, 2006). Some of the problems arising from the culture of Chinese family business are related to their corporate structure and their beliefs and norms. They are discussed in the following paragraphs.

According to the discussion by Singam (2003), the two problematic characteristics in the structures of Malaysian conglomerates, i.e. cross-shareholdings and the adoption of the pyramid model, discourage corporate sector in Malaysia from having an efficient corporate governance system. It is because of the following reasons. (a) The assets might be passed among the groups by ignoring the accepted principles of bookkeeping and accounting. (b) Majority conglomerates in Malaysia usually adopt the pyramid model in their corporate structure, whereby private holding company is at the apex of the structure and the second tier has the most valuable assets that are privately held and the third tier comprises the publicly listed companies. Shares are sold to the public, and proceeds are passed up the pyramid through a myriad of internal transactions and the less desirable assets are passed down the pyramid.

The second main problem of Chinese owned companies is due to their beliefs and norms. Usually, Chinese trade with people that they know and thus, these beliefs and norms in Chinese business network significantly lead to ownership concentration, which contributes to the inefficiency of the corporate governance system in Malaysia. According to Lai (2004), since the Chinese business culture has its own unique characteristics of leadership and ownership structure, decision making process and guanxi (relationship) as a form of business networking, the prescribed board structure under the code may not align with the Chinese business culture.

5.3.2.5 The Nature of Insider Control Firm

The fifth problem is due to insider control firms, which make the corporate governance system weak (Lai, 2004; Mohammad Rizal, 2006; Vethanayagam et al., 2006; Lefort & Urzua, 2008; Zulkarnain, 2007). In the family owned firms, especially Chinese owned firms, they do not have to rely on public disclosure and report to monitor their investments, since they have greater access to more comprehensive internal information. It is because the key persons who are managing the business are trusted insiders (Lai, 2004; Mohammad Rizal, 2006). According to Vethanayagam et al. (2006), Malaysia has concentrated managerial ownership, whereby 85 percent of the public listed companies have owner-managers in the post of CEO, Board chairman or vice chairman who is a member of the controlling family or an employee drawn from the ranks of the controlling shareholders.

5.3.3 Culture

Malaysian culture also influences the effectiveness of corporate governance system. According to Mohammad Rizal (2006), in Malaysia, there is no real market for takeovers and a negligible risk of being sued by shareholders to discipline directors and senior managers. The effectiveness of independent director provisions would be severely compromised in an environment where companies are run by autocratic leaders and in a culture where confrontations are generally avoided. Hence, a Western-style board may not work well within a Malaysian culture.

6. Conclusion

Since corporate governance becomes an important issue in the corporate world nowadays, this study explores on the effectiveness of corporate governance codes and applicability of agency theory in Malaysia. After critically reviewing the corporate governance literature, this study highlights that in Malaysia, the implementation of current corporate governance system is not effective and application of agency theory in Malaysia is very slim. Therefore, this study suggests the researcher to conduct future research by interviewing the financial analysts to find out their perception towards the effectiveness of the prevailing corporate governance codes in Malaysia.

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