

# Corporate governance and its impact on the performance of firms in emerging countries: The evidence from Vietnam

Dr. Nguyen Ngoc Thang\*

*Faculty of Business Administration, VNU University of Economics and Business,  
144 Xuan Thuy, Hanoi, Vietnam*

Received 17 August 2011

**Abstract.** Corporate governance has become an important issue for both Vietnamese firms and government. This study examines the effects of corporate governance on firm performance in Vietnam using the 2009 Survey of Corporate Governance Practices, which surveyed a sample of 100 large, publicly traded Vietnamese companies on the Hanoi Stock Exchange (HSE) and the Ho Chi Minh Stock Exchange (HOSE) on 1<sup>st</sup> January 2009. The research results show that corporate governance has an impact on firm performance. More specifically, corporate governance practices have impacted on firm profitability and market performance. The article concludes with some recommendations for management and directions for future research.

*Keywords:* Corporate governance, firm performance, emerging countries, Vietnam.

## 1. Introduction

Corporate governance has emerged as an important issue for both scholars and policy makers all over the world. There are many publications on the topic (Rajagopalan and Zhang, 2008; Singh and Gaur 2009; Lattemann et al., 2009; Shen and Lin, 2009; Renders et al., 2010). In Vietnam, after a decade of economic expansion and the growth of large corporations, corporate governance has become an important issue for Vietnamese firms as they increasingly interact with regulators and investors from developed markets. The recent corporate scandals - Bach Tuyet Cotton, Vinashin Group, and Vien Dong Pharmaceutical - reveal that the Vietnamese government needs to improve and promote good corporate governance to ensure

inflow of capital and the outflow of products. Furthermore, understanding corporate governance standards and issues in Vietnam is also important to both executives of local companies and foreign multinationals doing business in this country.

According to the Corporate Governance Regulations, the best practice of corporate governance suitable to the conditions in Vietnam would enhance market stability, increase investor confidence and trust, encourage investment into Vietnam from foreign sources and reduce the cost of capital for companies and, ensure a stable development

---

*“Corporate governance was first introduced in the Law on Enterprises in 2005 in Vietnam and introduced largely in the Corporate Governance Regulations in 2007.”*

\* Tel.: 84-946611417  
E-mail: thangnn@vnu.edu.vn

of the stock market and a transparent economy in Vietnam.

In the light of the both domestic and international attention paid to good corporate governance and its impact on firm performance, it is disturbing that the literature on this topic is so limited in the Vietnamese context. In this article, we use the data from the 2009 Survey of Corporate Governance Practices to examine the corporate governance practices in Vietnam and its impact on firm performance. At the end of the article we provide some recommendations for management and future research.

## 2. Why is corporate governance important

With the increasing integration of world economies, good corporate governance practices are essential for the development of a market based economy and a prosperous society. The perceptions of corporate governance have varied across different countries. For example, in Germany, large public companies tend to have two board systems including an executive board and a non-executive supervisory board which often includes employee representatives. In contrast, in the US and UK, companies have adopted a single board of directors system, which has the primary role of protecting the shareholders' interests. However, the boards of both corporate governance systems have a role and responsibility to oversee the actions of senior management in order to ensure that the running of the company serves the wishes and interests of shareholders (Aguilera and Jackson, 2003).

Corporate governance has become an important issue for companies. Where the managers and the owners of a company differ there is a possibility that their respective interests may become misaligned. Under these circumstances boards of directors and inspection/auditing committees, on the shareholders' behalf, can provide balance through examining and monitoring the actions of senior management. In addition, there are also other stakeholders that can influence a company, including employees and unions, suppliers, clients, and the government (OECD, 2004).

There is clear evidence that good corporate governance is an increasingly important factor for investment decisions, for reduction of risk related to its day-to-day operations, and to protect the firm from corrupt practices. Recent history is littered with high profile examples of corporate governance scandals and failures globally - such as Enron, Tyco International, Arthur Andersen, WorldCom, Bernard Madoff Investment Securities... The result is loss of investor confidence in financial markets and a fall in the market value of shares. The downturn in the domestic corporate sector performance may have also exposed further poor governance practices. In Vietnam, there have been a number of company scandals from corporate governance failures and malpractices. They have included some of the largest corporate names in the country, including Petroleum

---

*“Some studies show that investors are willing to pay more for shares in companies that are perceived as conforming to higher corporate governance standards. In contrast, investors will pay less, or may choose not to invest at all, in firms that display poor disclosure, transparency, and poor corporate governance practices (Mekong Capital, 2003).”*

---

Technical Service Company, Viet Hoa Bank, Bach Tuyet Cotton, Vinashin, and Vien Dong Pharmaceutical... This gives evidence that implies the need for major improvements in corporate governance practices in Vietnam.

At the country level, if countries are to attract long-term capital and full benefits of global capital market, corporate governance must be credible and consistent with internationally accepted principles. Even if local companies do not need foreign sources of capital, good corporate governance will help improve the belief of domestic investors and help improve the good conditions of financial markets. In addition, good corporate governance practices result in efficiency and productivity gains for individual companies and their investors, and the results then have positive impact on the overall economy (OECD, 2004).

Recognizing the importance of corporate governance, many countries have issued rules or guidelines to specifically address this issue. International agencies have produced documents in order to assist companies follow good corporate governance practice such as the OECD's Principles of Corporate Governance. In Vietnam, the legal and regulatory framework has changed considerably in recent years and it is recognized that there are still gaps and need for improvement. The following laws are part of major efforts to build good corporate governance:

(i) The Law on Foreign Investment in 1987, its amendments in 2000 and its later unification with the Law on Domestic Investment in 2005;

(ii) The Law on Enterprises in 1999, and its replacement in 2005;

(iii) The Law on the State Bank in 1997 and the Law on Credit Institutions of 1997, amendments to both laws in 2003 and 2004 respectively; the new Law on the State Bank of Vietnam 2010; and the new Law on Credit Institutions, 2010;

(iv) The Law on Insurance Business in 2000;

(v) The Competition Law in 2004;

(vi) The Law on Securities in 2006.

### 3. Data

Our data was obtained from the 2009 Survey of Corporate Governance Practices, International Finance Corporation (IFC), the Survey on Corporate Governance of 100 publicly listed companies in Vietnam, which was conducted in 2009 with support from the IFC. The sample was selected from a total of 100 listed companies on the Hanoi Stock Exchange (HNX) and the Ho Chi Minh Stock Exchange (HOSE), as at 1 January 2009, which together represent some 90% of the total market capitalization of these exchanges. The companies were assessed against the five key areas, which are recognized by the OECD Principles as the keys to good corporate governance: (i) The rights of shareholders; (ii) Equitable treatment of shareholders; (iii) Role of stakeholders in corporate governance; (iv) Disclosure and transparency; (v) The responsibilities of the board. More specifically, the questionnaire was allocated by areas and scored as follows:

Table 1. Questionnaire topic area and score allocation

<i>Category</i>	<i>Number of questions</i>	<i>Percentage of total score</i>
The rights of shareholders	21	15
Equitable treatment of shareholders	18	20
Role of stakeholders in corporate governance	8	5
Disclosure and transparency	32	30
The responsibilities of the board	31	30
<b>Total</b>	<b>110</b>	<b>100</b>

Source: The 2009 survey of corporate governance practices, IFC.

The OECD Corporate Governance Principles are the globally accepted benchmark for corporate governance.

However, the specific Vietnam questionnaire was constructed with questions that reflect the OECD Principles and specific corporate governance legal and

*According to international experience, the total score of a company considered practising good corporate governance is between 65% and 75%. Compared with the survey results, there were no Vietnamese companies in this survey who achieved the international standard for good corporate governance.*

regulatory frameworks in Vietnam, especially the Ministry of Finance’s Decision 12/2007/QD-BTC on corporate governance.

The data was collected from a wide variety of publicly available information in the company’s annual report and financial report as disclosed at 31 December 2009, HNX and HOSE filings, Securities Supervisory Commission filings, and other documents, especially the minutes and documents relating to the General Meeting of Shareholders, the company Articles of Association, and from the public media and other sources of public information such as the company website.

#### 4. Results and discussion

Figure 1 provides the overall mean results in corporate governance categories. The results show that the area of best compliance with global good practice was the equitable treatment of shareholders with an overall level of compliance of 65.1%. Other areas achieved a level of compliance of less than 50%. This may very well be the reason why there are many corporate governance scandals and failures in Vietnam in the past few years.

The area of least compliance with global good practice was that relating to the role of stakeholders with a level of compliance of just 29.2%. This result shows that the role of stakeholders in corporate governance may be a new concept in Vietnam. However, under international pressure, companies cannot ignore the adoption of good practices related to the environment, society and governance because this is a focus of investor attention and corporate social responsibility. Other areas of low compliance were the responsibilities of the board (35.3%) and disclosure and transparency (39.4%). It is clear that corporate governance is in its early stages in Vietnam. Society perceives that a commitment to good corporate governance is not yet established.

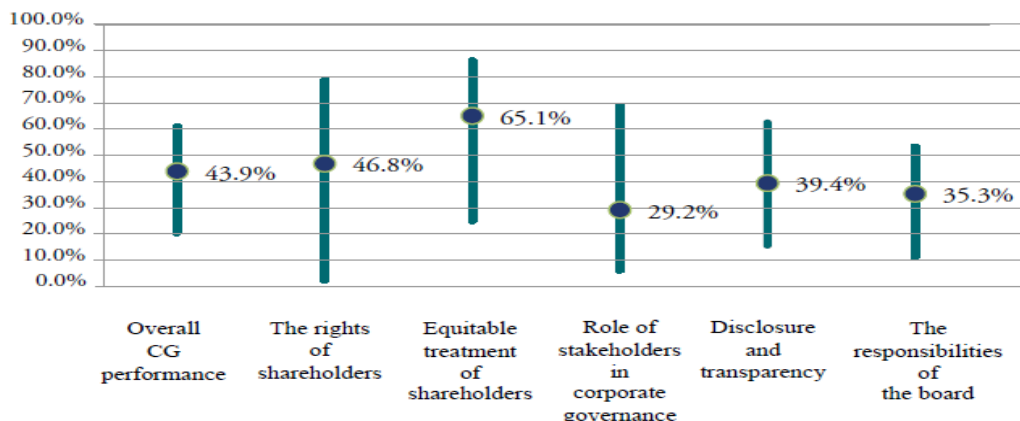


Figure 1. Overall results in corporate governance categories.  
 Source: The 2009 survey of corporate governance practices, IFC.

Based on the survey results, firms fall into three groups dependant on the corporate governance score: 25 percent of firms with a higher score, 50 percent of firms with a middle score, and 25 percent of firms with a lower score of corporate governance practices. Tobin's Q and Market to Book (M/B) ratio of

each group is calculated in order to compare corporate governance practices and the market performance of each group. Tobin's Q measures the ratio between the market value of equity plus firm debt divided by the book value of total assets.

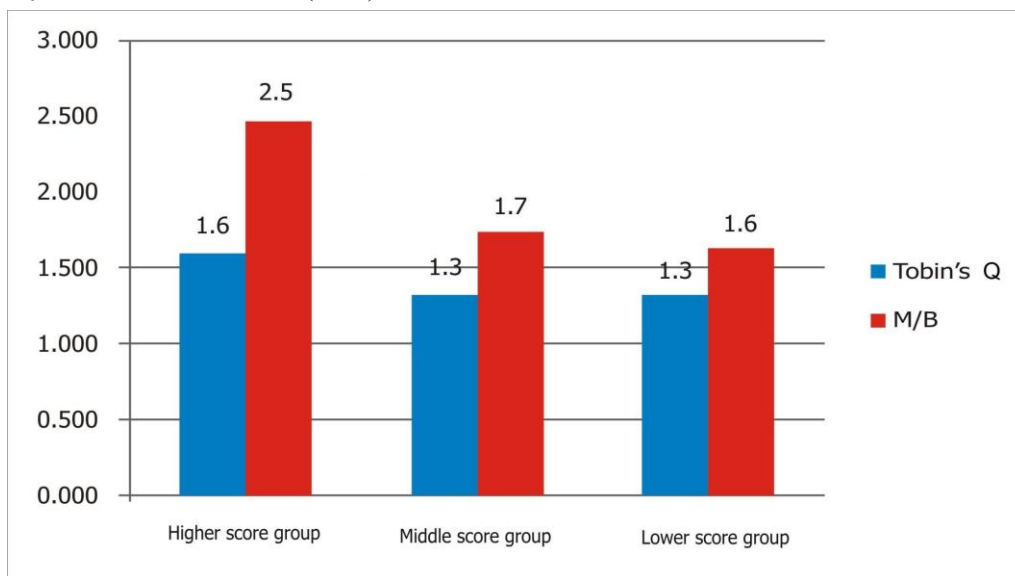


Figure 2. Corporate governance practices and market performance.

Source: The 2009 survey of corporate governance practices, IFC.

As shown in Figure 2, the Tobin's Q ratios are 1.6, 1.3, and 1.3 for the higher score group, the middle score group, and the lower score group of corporate governance practices respectively. M/B ratios of the higher score group, middle score group, and lower score group of corporate governance practices are 2.5, 1.7, and 1.6 respectively. Such findings indicated that the companies with better corporate governance scores have better market performance (as measured by Tobin's Q), even if the Vietnamese market is immature, inefficient or volatile. Unfortunately, the survey does not allow us to explore this phenomenon in more detail.

Next, to provide a more thorough understanding of the crucial dimensions and the effectiveness of corporate governance practices, a comparison of return on equity (ROE) and return

on assets (ROA) between the higher score, middle score, and lower score groups of corporate governance practices was conducted. The results in Figure 3 show that companies with better corporate governance practices also demonstrate better profitability. Companies in the higher score group of corporate governance practices have a higher return on equity and return on assets ratios than those in the lower score group of corporate governance practices. The ROE of companies with better corporate governance at an ROE of 23.5%, compare with the companies with lower corporate governance with ROE of 16.6%. The results of the ROA ratios revealed a similar picture with the ROE ratios.

In addition, the score of corporate governance practices varies across diverse industries. According to the survey, the healthcare industry, comprised of healthcare

equipment, pharmaceutical and biotechnology companies, achieved the highest mean score of 50.4. The second highest industry group, in the quality of its corporate governance, was the financial industry with mean score a 45.8. The oil and gas sector achieved the poorest result of all industry sectors with a mean score of 39.1.

However, when we compared the corporate governance practices score of the financials industry with those of all other nonfinancial industries, the financial industry (45.8) performed better in corporate governance practices than the mean of the other sectors (43.5). There are two possible reasons. First, given the important financial intermediation

role of the banking and financial services industry in an economy, there is a need to safeguard depositors' funds. Thus, government imposed tighter regulations for this sector in order to reduce the risks to the banking system - among other benefits. Second, in joining the World Trade Organization, Vietnam has been accepting increased competition, foreign banks have entered the Vietnamese market by opening their own operations through acquiring Vietnamese banks. Thus, they have been supported to improve corporate governance practices for local banks.

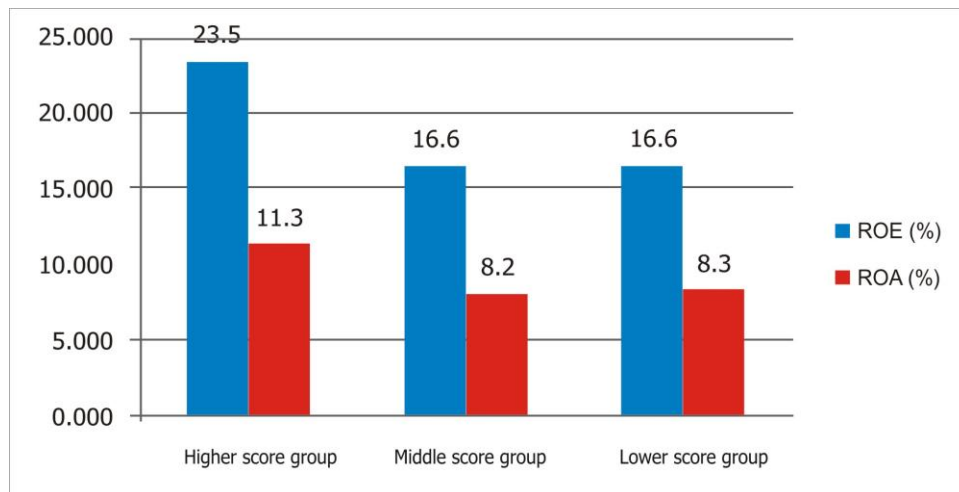


Figure 3. Corporate governance practices and profitability.  
Source: The 2009 survey of corporate governance practices, IFC.

## 5. Conclusion and recommendations

The results from the 2009 Survey of Corporate Governance Practices show clearly that there is a strong and positive relationship between company market performance and profitability which provides a good incentive for firms to improve their corporate governance practices in Vietnam. However, corporate governance in Vietnam is still at the beginning of a long journey and the commitment to good corporate governance is not yet established. This pursuit should comprise a central part of the

ongoing economic reform and business liberalization

process in Vietnam. Thus, Vietnam needs to improve corporate governance in order to reduce risk to companies. The study highlights another way in which corporate governance has emerged as

---

*"The pursuit of good corporate governance practices will be an important element in developing the next generation of domestic firms capable of competing at home and overseas."*

---

an important issue for scholars as well as policy makers and managers in Vietnam.

In practice, we provide some following policy-oriented recommendations to promote better corporate governance practices in Vietnam. First, the Vietnamese government needs to improve existing and future laws and regulations that deal with corporate governance issues, standards and practices. These include (i) disclosure and transparency requirements for Board of Management members and senior executives of firms; ii) clarification of the legal roles and responsibilities of Board of Management members and senior executives of firms; iii) improve the role of the Inspection Committees so that they can better perform their assigned duties; iv) better protect shareholders' rights and ensure equitable treatment, particularly for minority shareholders.

Second, it is necessary to raise awareness of the benefits of corporate governance, to increase public awareness programs and collaboration with other market participants to explain the importance of shareholder participation in company activities and to facilitate participation. This should be done through extensive training for all stakeholders in corporate governance.

Third, integrating corporate governance improvements with broader reforms is recommended. It should be recognized that making corporate governance improvements can not be done in isolation from other efforts. Therefore, if we expect better corporate governance practices, we need to integrate it with wider economic reform. For example, it is difficult to envisage how companies will make major strides to improve the quality of their financial reporting without a marked improvement in the corporate income tax system. Consequently, any efforts to improve corporate governance practices in Vietnam would need to be integrated with other related issues.

Although our study provides interesting insights about the relationship between corporate governance practices and firm

performance, several limitations of this study should be emphasized and recommendations made for future research. First, this study tried to span most of the corporate governance issues that one finds in the existing literature. Future research needs to focus on examining the relationship of each corporate governance practice with firm performance. Second, future research needs to identify the more specific corporate governance problems faced by both the SOE and non-state sector, such as potential conflicts of interest, or related party transactions. Third, future research also needs to find a way to help companies to overcome the overlap that exists between senior executives and Boards of Management as well as improve the role of Inspection Committees in many private firms.

## References

- [1] Aguilera, R. V. and Jackson, G. (2003). The Cross national Diversity of Corporate Governance: Dimensions and Determinants. *Academy of Management Review*, 28, 447-465.
- [2] Lattemann, C., Fetscherin, M., Alon, I., Li, S., & Schneider, A. (2009). CSR communications intensity in Chinese and Indian multinational companies. *Corporate Governance: An International Review*, 17: 426-442.
- [3] Mekong Capital. (2003). Recommendations on Corporate Governance Practices in Vietnam. [www.mekongcapital.com/html/downloads.htm]
- [4] OECD. (2004). OECD Principles of Corporate Governance 2004. OECD Publishing.
- [5] Rajagopalan, N. & Zhang, Y. (2008). Corporate governance reforms in China and India: Challenges and opportunities. *Business Horizons*, 51: 55-64.
- [6] Renders, A., Gaeremynck, A. Sercu, P. (2010). Corporate-governance ratings and company performance: a cross-European study. *Corporate Governance*, vol. 18, no. 2, pp. 87-106.
- [7] Shen, W. & Lin, C. (2009). Firm profitability, state ownership, and top management turnover at the listed firms in China: A behavioral perspective. *Corporate Governance: An International Review*, 17: 443-456.

[8] Singh, D. A. & Gaur, A. (2009). Business group affiliation, firm governance and firm performance:

Evidence from China and India. *Corporate Governance: An International Review*, 17: 411-425.

## Quản trị công ty và ảnh hưởng đối với hoạt động của các doanh nghiệp ở những nền kinh tế mới nổi: Minh chứng từ Việt Nam

TS. Nguyễn Ngọc Thắng

*Khoa Quản trị Kinh doanh, Trường Đại học Kinh tế,  
Đại học Quốc gia Hà Nội, 144 Xuân Thủy, Hà Nội, Việt Nam*

**Tóm tắt.** Quản trị công ty là một trong những vấn đề quan trọng đối với doanh nghiệp và chính phủ Việt Nam. Bài viết này kiểm chứng sự ảnh hưởng của quản trị công ty đến kết quả hoạt động của doanh nghiệp Việt Nam thông qua số liệu thu thập từ cuộc khảo sát về quản trị công ty của 100 công ty đại chúng lớn nhất đang giao dịch trên sàn giao dịch chứng khoán Hà Nội và Thành phố Hồ Chí Minh tháng 1 năm 2009. Kết quả nghiên cứu chỉ ra rằng, quản trị công ty có ảnh hưởng đến kết quả hoạt động của doanh nghiệp Việt Nam. Cụ thể, quản trị công ty ảnh hưởng đến lợi nhuận và giá trị thị trường của công ty. Nghiên cứu cũng đưa ra một số khuyến nghị cho các nhà quản lý và gợi ý những định hướng cho nghiên cứu trong tương lai về chủ đề này.