



INTERNATIONAL FINANCE CORPORATION
WORLD BANK GROUP

Corporate Governance and the Financial Crisis

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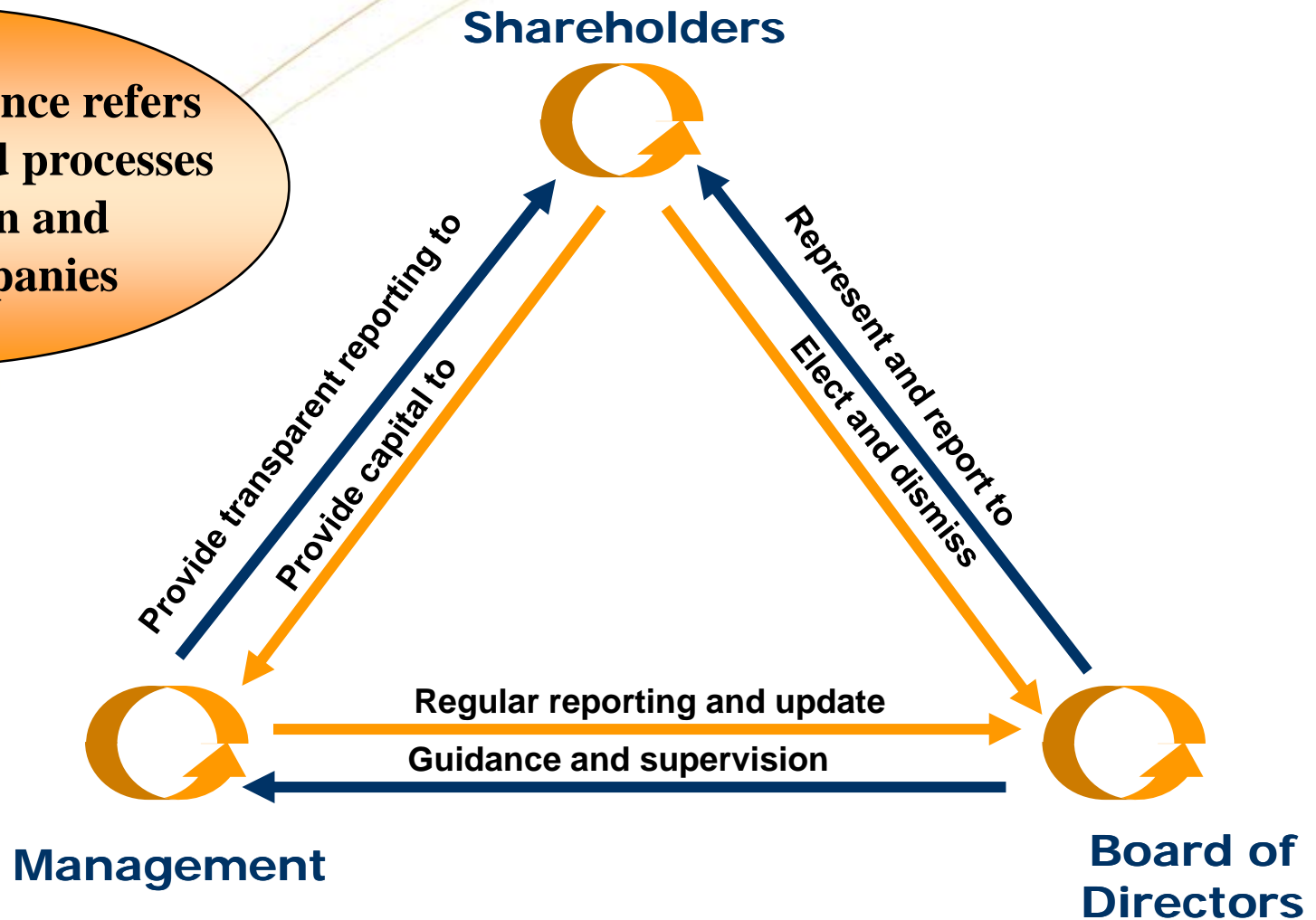
Program Manager

IFC MENA Corporate Governance

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Definition of Corporate Governance

Corporate governance refers to the structures and processes for the direction and control of companies



IFC's MENA CG Program - Initial Results Show Impact



For example, over the past four years:

- Trained ~4,000 directors and executives from ~1,600 firms and nearly 600 FIs
- 16 'best practice companies' improve CG
- 3 CG Institutes in Egypt, Pakistan & UAE launched with IFC support. 6 new initiatives existing in MENA
- Guided and supported launch of 14 CG Codes around region

Good Overall Progress Has Been Made in MENA

In Lebanon: Bank CG survey and legal review; CG Code for SMEs launched; LTA to found Institute of Directors and offer training courses

In Jordan: Model CG code for banks and listed companies launched; legal review of bank CG framework undertaken with IBRD

In Algeria: CG Code in preparation

In West Bank & Gaza: Bank CG awareness event; two CG Codes in final review process

In Syria: CG Guidelines for private sector banks being drafted

In Morocco: CG Code launched; workshop on CG for IFC MFI clients

In Pakistan: Pakistan CG Institute launched; training program; 13 TV episodes on CG with Business Plus; NUST university launched CG elective with 20 students

In Tunisia: CG Code in preparation

In Egypt:

- Egyptian Institute of Directors launched, training program
- Egyptian Banking Institute will launch training program for bank directors
- Two CG Codes published, listing rules strengthened

In Saudi Arabia: CG regulations launched; major bank CG conference being held; bank CG training with Institute of Banking

In Bahrain: CG Code being drafted

In Qatar: CG Code being drafted

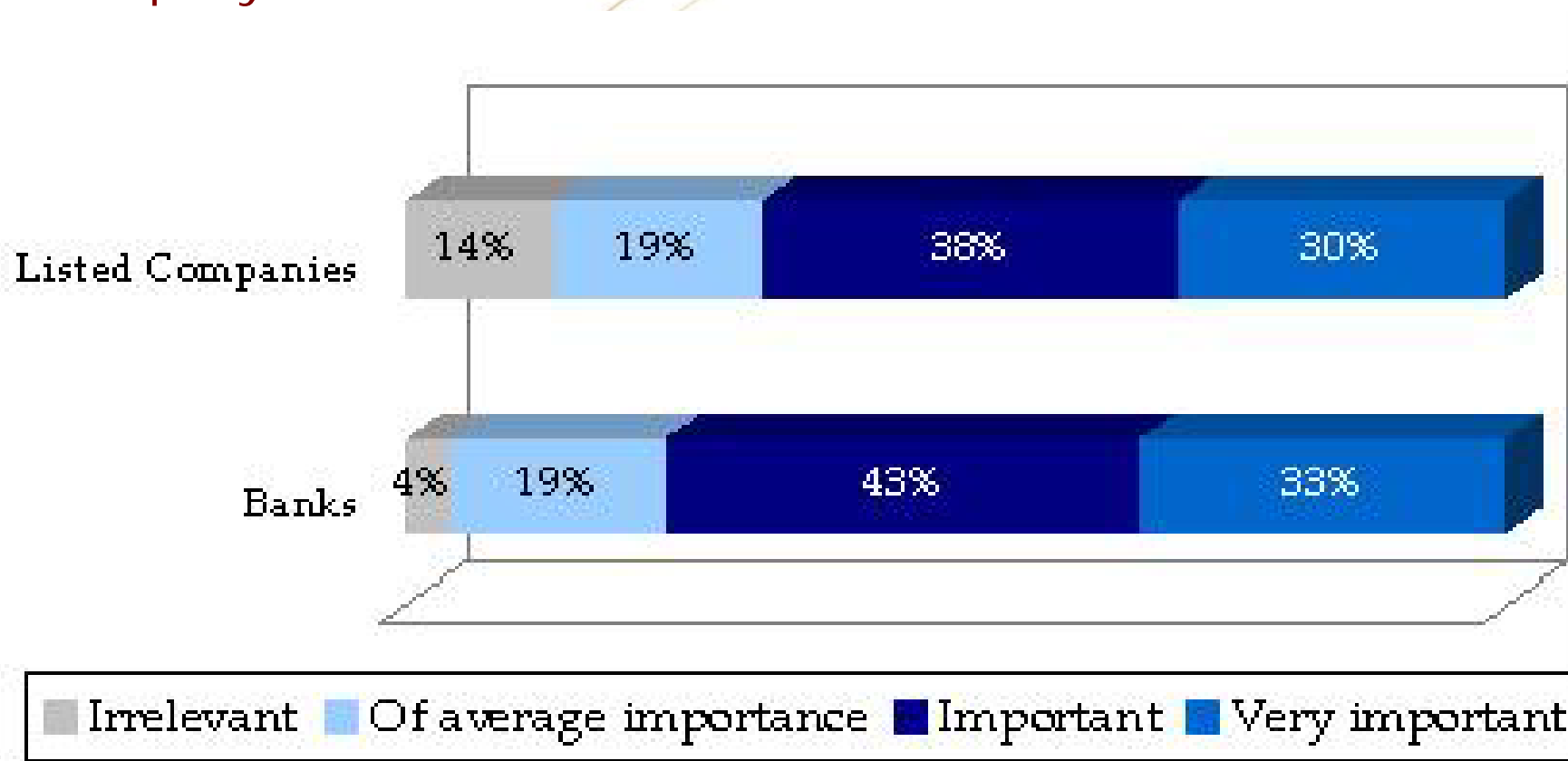
In UAE: Launch of Hawkamah and Mudara; training program and regional awareness raising events

In Oman: Region's first CG Code launched, now being updated; local CG institute considered

MENA-wide: CG Survey in 11 countries conducted and launched; joint MENA Initiative with OECD on policy reform for banks and SOEs

State of Corporate Governance in MENA

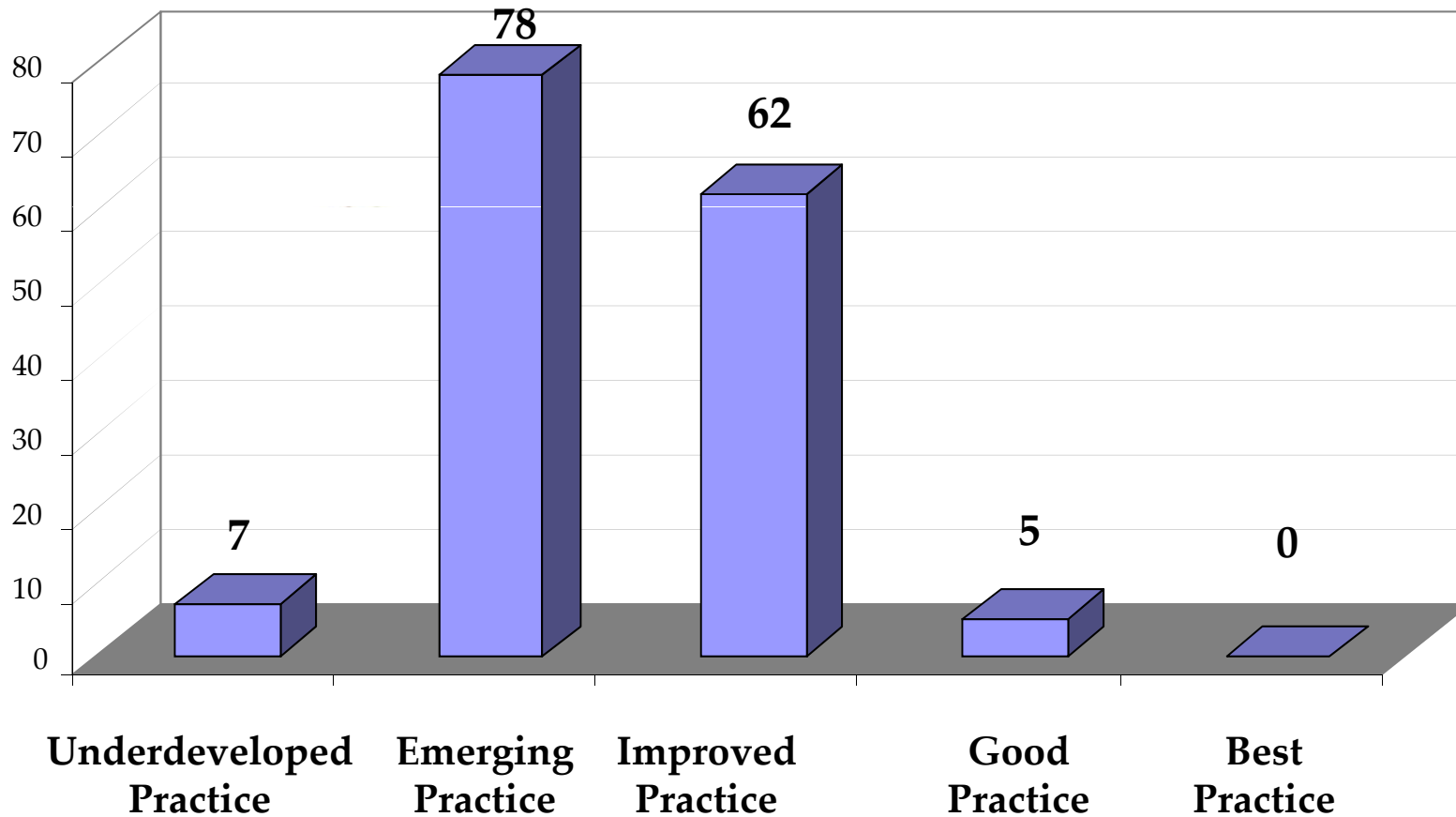
- MENA Survey: How important is Corporate Governance to your company?



2007 IFC/Hawkamah MENA CG Survey

State of Corporate Governance in MENA

➤ MENA Survey: How do you rate your current CG practices?



2007 IFC/Hawkamah MENA CG Survey



Key Dimensions of Corporate Governance

Commitment to Corporate Governance

Disclosure and Transparency

Shareholder & Stakeholder Relations

Family Governance

Board Functioning

Management Control Environment

Risk Management – Board Responsibility

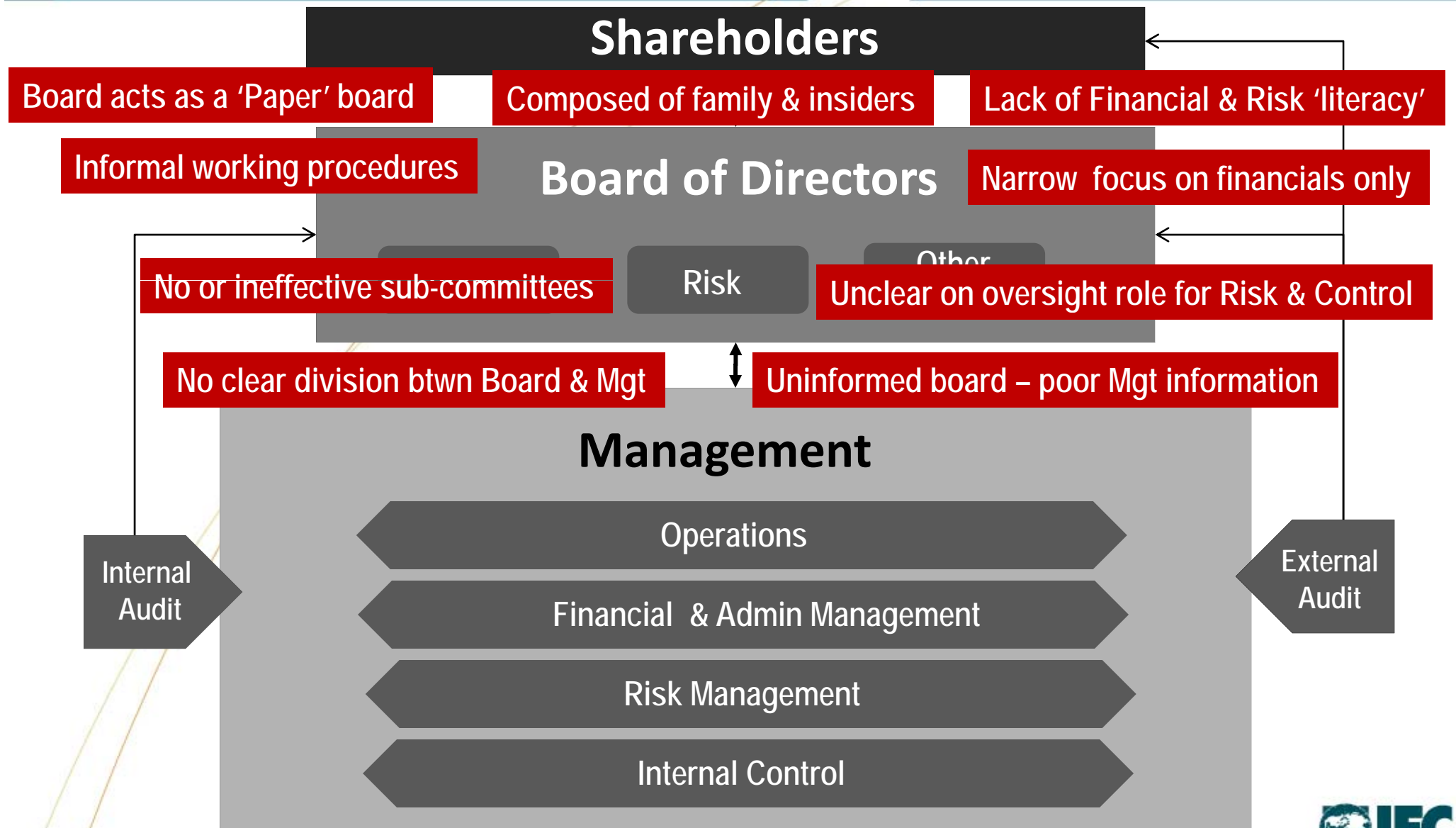
Basel Committee & Egypt Code of Governance

... the Committee has observed that boards and their individual members strengthen the corporate governance of a bank when they do the following:

- Understand and execute their oversight role, including understanding the bank's risk profile
- Approve the overall business strategy of the bank, including approval of the overall risk policy and risk management procedures

Source: 2006 Basel Committee on Banking Supervision, *Enhancing Corporate Governance for Banking Organisations*

What have we observed?



Board Functioning Principles To Encourage

Board Roles & Responsibilities

- ✓ Board's role is clearly defined vis-à-vis management
- ✓ Directors understand duties and responsibilities to the company and shareholders
- ✓ Board understands its oversight duties (esp. Risk & Control) and has appropriate processes in place

Board Composition & Structure

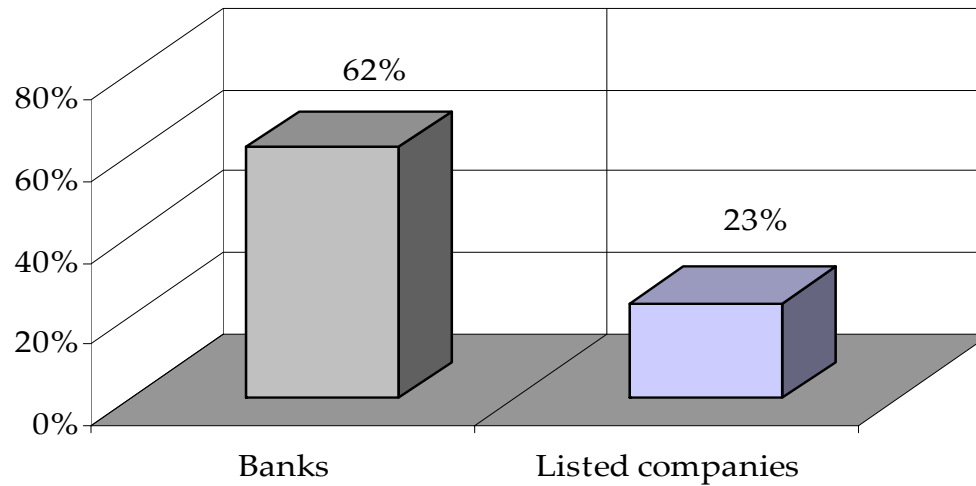
- ✓ Establish board committees: audit, remuneration, corporate governance and nomination, and/or others as necessary
- ✓ Directors should decide the optimal board size
- ✓ Boards to include appropriate mix of executive, non-executive and independent directors
- ✓ Directors should optimize the mix on the board, especially of skills

Board Practices

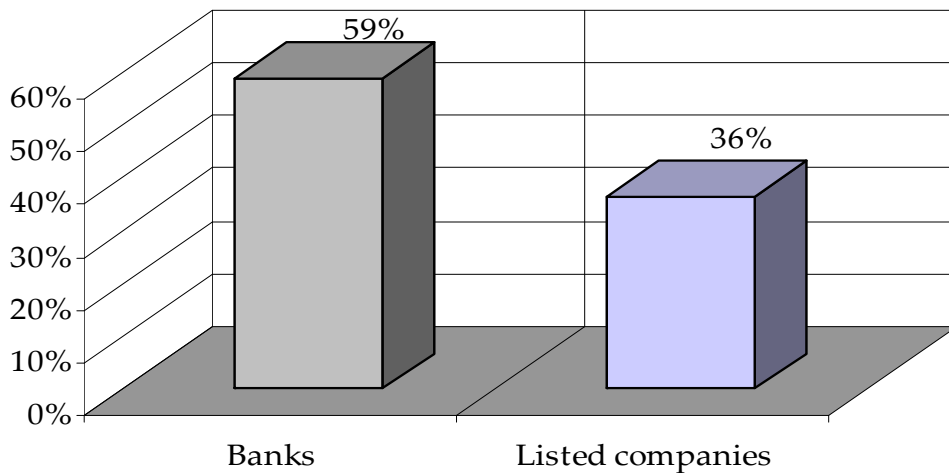
- ✓ Review board working procedures (e.g., meeting proceedings, frequency, formality)
- ✓ The board should be supported by a professional corporate secretary
- ✓ Board needs to establish executive and non-executive compensation policies and practices
- ✓ Board should conduct self-evaluations of performance
- ✓ Suggest that company offers training to directors

MENA Corporate Governance Survey

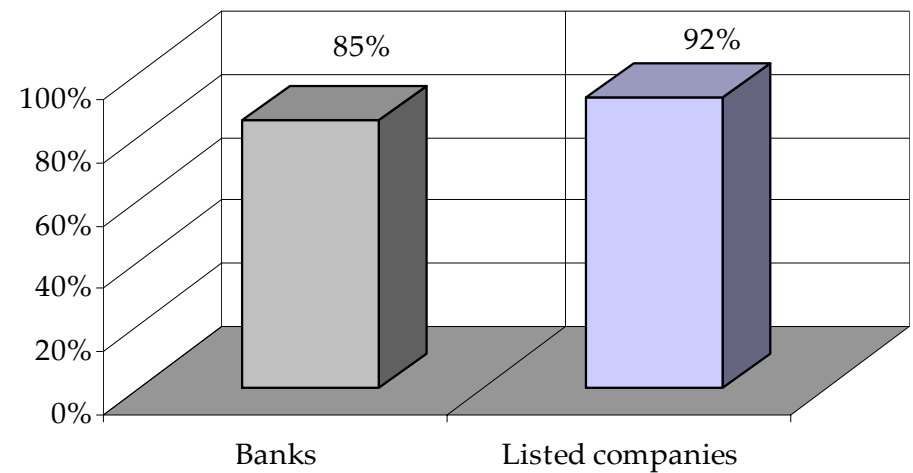
Risk Management



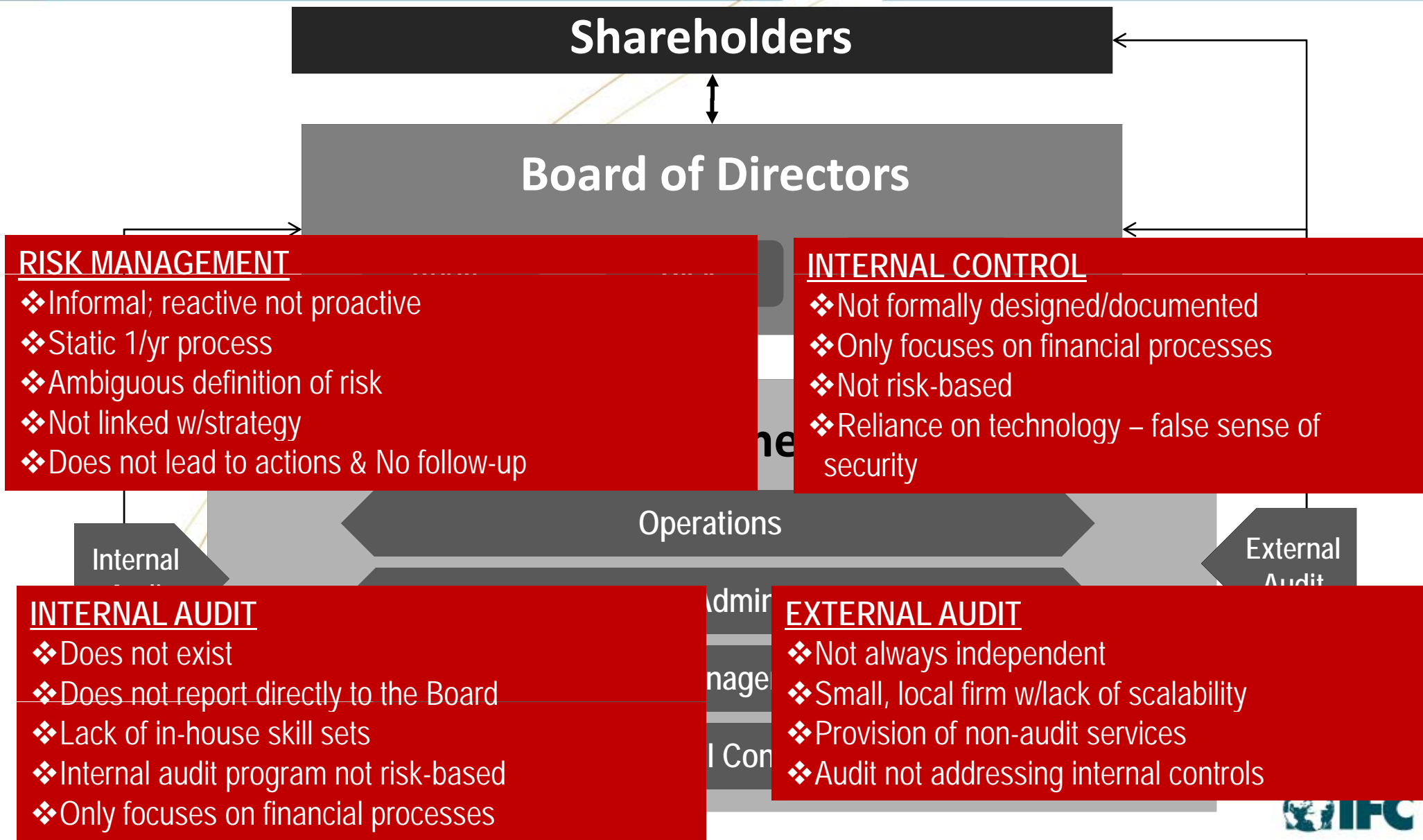
Internal Control



Internal Audit



What have we observed?



Management Control Environment Principles to Encourage

Management Control Environment

- ✓ **Risk management** framework/structure working effectively with ample 'Risk Dialogue'
- ✓ **Internal control** framework is structured, formal, risk-based, and established and working effectively
- ✓ **Internal audit** has broad mandate(not just financials) and reports independently to the Board
- ✓ Independent **external auditor** is independent, reputable, and conducts no other advisory services
- ✓ Business **planning and monitoring** functions are structured, well-understood, and effective (e.g., strategic planning, budgeting, and performance monitoring)
- ✓ **Information and communication** within the organization flows adequately to support transparency and timely control
- ✓ There is effective **compliance** (internal & external) oversight in the organization.
- ✓ **Board** is playing effective oversight role for the control functions.

Financial Crisis, Banks, and Corporate Governance

- Since the financial crisis, two rigorous studies have taken place exploring why banks have failed in the manner that they did, in comparison to those that survived
- Studies have shown that failures are mainly due to the *'rather limited understanding by bank boards of increasingly complex and geographically diverse businesses that is responsible for poor strategic choices'**
- Time and time again, failures in specific corporate governance aspects are mentioned:
 - Director Competence and Board Composition
 - Risk Oversight by the Board
 - Alignment and Incentives

Financial Crisis, Banks, and Corporate Governance – Failures were due to...

- **Lack of Director Competence and Bad Board Composition:**
 - **Independence of the Board:** Long tenure of CEOs/Chairmen and of non-executive directors on the board, making long total board tenure
 - **Adequate/Relevant Expertise on the Board:** Lack of financial industry expertise, especially that of non-executive directors
 - **Executive Presence on the Board:** Lack of executive presence on the board
 - **Age of Board Members:** Ageing board, lack of age limits on board members
 - Indicates highly influential CEO/Chairman with unbalanced power, no ‘independence of mind’, lack of informational flow regarding regular business into board, low variation on perspectives, outdated approach to a highly dynamic and complex business

Financial Crisis, Banks, and Corporate Governance – Failures were due to...

- **Lack of Risk Oversight by the Board:**
 - **Bank's Risk Appetite: Defining the risk appetite not a top board priority, or oversight of risk management and setting of risk appetite not a core board responsibility**
 - **Risk Committee: Low number of yearly meetings, no distinct risk committee, or no risk committee at all**
 - **Indicates unresponsiveness to imminent risks**

'Poor risk management practices represent the most compromising business and reputational threat to a financial institution.'*

Financial Crisis, Banks, and Corporate Governance – Failures were due to...

- **Alignment and Incentives**

- **Difference between CEO/Chairman and Senior Executive Officers Compensation: Large variance between chief executive and senior executive pay**
- **Full alignment with shareholder interests: Alignment with long-term shareholder value and CEO/Chairman's personal wealth**

→ **Indicates concentration of executive power within the bank and its team culture**



Thank You.

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