A World Bank Group Flagship Report

WORLD BANK GROUP · 15TH YEAR · DOING BUSINESS

Doing Business 2018

Protecting Minority Investors

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May 2018

I. **Why does it matter?**
II. What does it measure – and what does it not?
III. What are the main findings in DB18?

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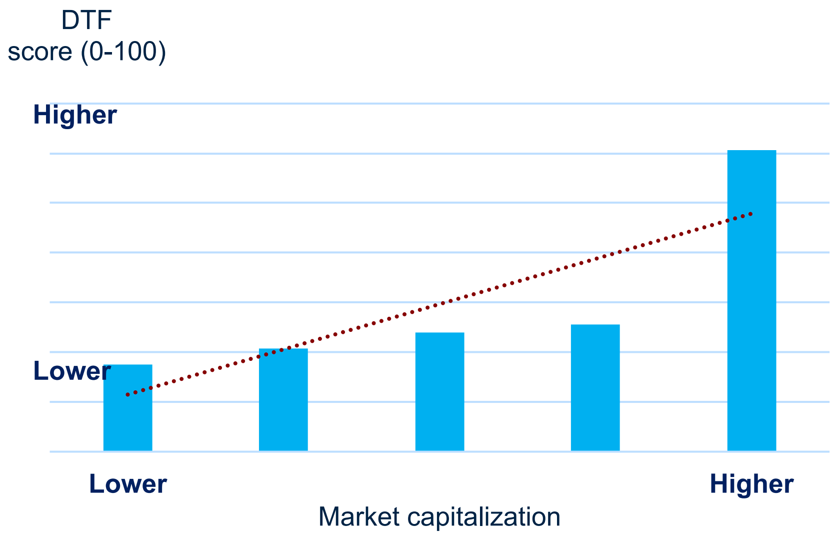
Why does Protecting Minority Investors matter?

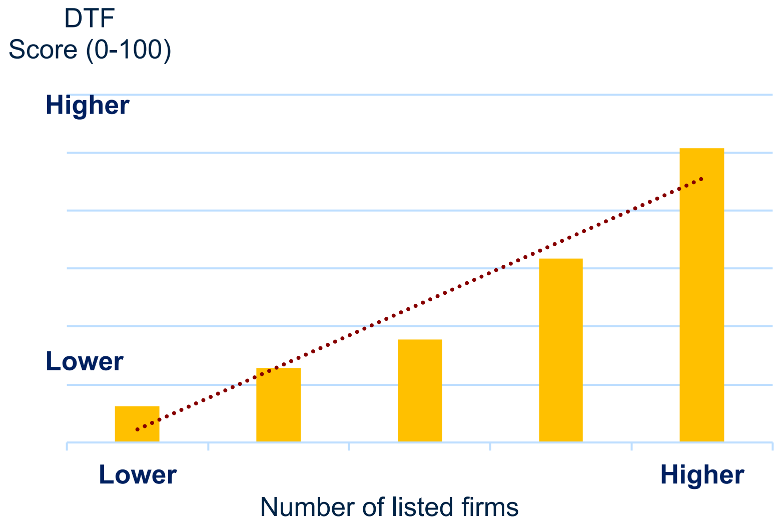
Stronger minority investor protection is associated with:

- ✓ **Higher market capitalization**
- ✓ **Higher entry level to capital markets**

Market capitalization to GDP



Number of listed firms



Source: Doing Business database, World Bank (2010).
Note: Relationships remain significant when controlling for income per capita. Higher values on the strength of investor protection index indicate greater protection.

Why does Protecting Minority Investors matter?

- Empirical research shows that stricter regulation of self-dealing is associated with greater equity investment and lower concentration of ownership.
- Research on 539 large firms in 27 economies shows that firm valuation is higher in economies with good investor protections than in those with poor protections.
- Other research shows that corporate risk-taking and firm growth rates are positively related to the quality of the system of investor protections.
- Most recently, a study found that in economies with stronger investor protections, investment in firms is less sensitive to financial constraints and leads to greater growth in revenue and profitability.
- Another study found that regulating conflicts of interest is essential to successfully empowering minority shareholders.

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What is not measured?

Protections for foreign direct investment (FDI)

Broad frameworks of rights for minority shareholders

Practical enforcement of laws

Fraud or violations of law

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What does Protecting Minority Investors measure?

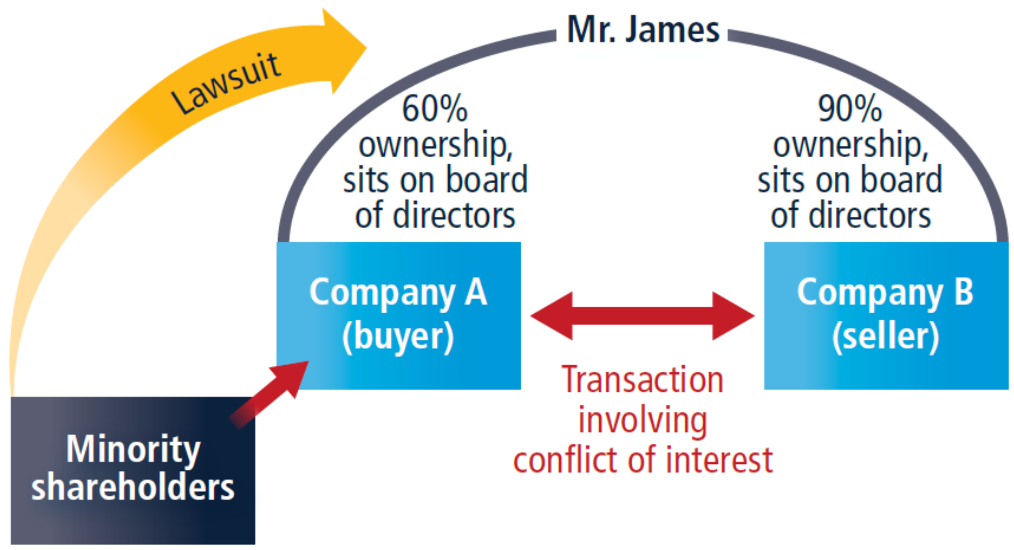
Extent of disclosure index (0–10)	**Extent of shareholder rights index (0–10)**
Review and approval requirements for related-party transactions	Shareholders’ rights and role in major corporate decisions
Internal, immediate and periodic disclosure requirements for related-party transactions	
Extent of director liability index (0–10)	**Extent of ownership and control index (0–10)**
Minority shareholders’ ability to sue and hold interested directors liable for prejudicial related-party transactions	Governance safeguards protecting shareholders from undue board control and entrenchment
Available legal remedies (damages, disgorgement of profits, fines, imprisonment, rescission of transactions)	
Ease of shareholder suits index (0–10)	**Extent of corporate transparency index (0–10)**
Access to internal corporate documents	Corporate transparency on ownership stakes, compensation, audits and financial prospects
Evidence obtainable during trial	
Allocation of legal expenses	
Extent of conflict of interest regulation index (0–10)	**Extent of shareholder governance index (0–10)**
Simple average of the extent of disclosure, extent of director liability and ease of shareholder suits indices	Simple average of the extent of shareholder rights, extent of ownership and control and extent of corporate transparency indices
Strength of minority investor protection index (0–10)	
Simple average of the extent of conflict of interest regulation and extent of shareholder governance indices	

How does Protecting Minority Investors measure conflict of interest?

Extent of disclosure
Disclosure and approval requirements

Extent of director liability
Ability to sue directors for damages

Ease of shareholder suits
Access by shareholders to documents plus other evidence for trial



- Transaction priced above market-value;
- Clear conflict of interest, but possible business purpose;
- Legal requirements met, but not exceeded;
- The transaction is not fraudulent.

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Where are minority investors more protected in 2016/17?

Top 10 performers:

- Kazakhstan
- Georgia
- New Zealand
- India
- Macedonia, FYR
- Malaysia
- Singapore
- Canada
- Hong Kong SAR, China
- United Kingdom

Top 10 improvers:

- Djibouti
- Rwanda
- Saudi Arabia
- Costa Rica
- Brunei Darussalam
- Azerbaijan
- Thailand
- Kazakhstan
- Georgia
- Indonesia

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How and where did economies strengthen minority investor protection in 2016/2017

Feature	Economies	Some highlights of global good practices
Expanded shareholders' role in company management	Azerbaijan; Bhutan; Brunei Darussalam; Djibouti; Arab Republic of Egypt; France; Georgia; Indonesia; Kazakhstan; Lithuania; Malaysia; Nepal; Rwanda; Saudi Arabia; Thailand; Uzbekistan.	Lithuania enacted a law requiring the disclosure of information about board members' other directorships as well as basic information on their primary employment.
Enhanced access to information in shareholder actions	Costa Rica; Djibouti; Georgia; Kazakhstan; Luxembourg; Rwanda; Thailand.	Luxembourg adopted legislation allowing shareholders that represent at least 10% of the share capital to inspect transactions documents before filing a suit.
Increased disclosure requirements for related-party transactions	Costa Rica; Djibouti; India; Saudi Arabia; Ukraine.	Costa Rica adopted a law requiring board members who have a personal interest in a proposed transaction to clearly disclose it and not participate in the decision.
Increased director liability	Djibouti; India; Luxembourg; Pakistan.	Djibouti adopted a law allowing shareholders to hold interested directors (as well as other board members) liable when a transaction with interested parties is unfair or prejudicial to the company and to have them repay profits made from the transaction upon a successful claim.

21 economies strengthen minority investor protection in 2016/2017

Number	Economies	
13	Azerbaijan, Brunei Darussalam, Djibouti, Egypt, France, Indonesia, Kazakhstan, Lithuania, Malaysia, Nepal, Rwanda, Saudi Arabia and Uzbekistan.	Promoted greater corporate transparency
9	Azerbaijan, Brunei Darussalam, Djibouti, Egypt, Georgia, Indonesia, Kazakhstan, Saudi Arabia and Thailand.	Expanded shareholders' role in the management of the company
9	Azerbaijan, Brunei Darussalam, Bhutan, Djibouti, Georgia, Kazakhstan, Rwanda, Saudi Arabia and Thailand.	Improved the governance safeguards protecting shareholders from undue board control and entrenchment
7	Costa Rica, Djibouti, Georgia, Kazakhstan, Luxembourg, Rwanda and Thailand.	Enhanced power of shareholders in shareholder suits
5	Costa Rica, Djibouti, India, Saudi Arabia and Ukraine.	Broadened disclosure requirements for related-party transactions
4	Djibouti, India, Luxembourg and Pakistan.	Increased director liability
	TOTAL: 21	

Of the 21 economies:

- ✓ **8** are in Europe & Central Asia
- ✓ **4** in East Asia & Pacific
- ✓ **4** in South Asia
- ✓ **3** in the Middle East & North Africa
- ✓ **1** in Sub-Saharan Africa

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THANK YOU!

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