

# Corporate governance in connection with performance and digital

Igor Dimitriev<sup>1</sup>, and Elena Krasilnikova<sup>2,\*</sup>

<sup>1</sup>GPB, Vvedenskogo Str.12.1, 117342 Moscow, Russia

<sup>2</sup>Central Economics and Mathematics Institute of the Russian Academy of Sciences, Nahimovsky Pr., 47, 117418 Moscow, Russia

**Abstract.** The article concerned issues, related to the characteristics of Corporate governance and performance. The characteristics of Corporate governance are pervasive: ownership structure, separation from control, Board of directors, protection of rights. For Russian companies traditional organizational characteristics of life cycle stages are not decisive. Currently there is a tendency for owners to get out from management and focus on social, environmental results. The ownership of private insiders is the highest at the stage of formation, and the foreign ownership rises at the stage of growth. Based on the model was estimated significant positive impact of companies' age on an increase in property rights, ownership and control, protecting minority investors encourages R&D. Results of estimation of 62 countries in 2020 represented significant positive relation Technology factors: adaptive attitudes, business agility, IT integration with performance and Corporate governance. An increase in digital is associated with a higher quality of Corporate governance.

## 1 Introduction: the Corporate Governance Features

The quality of Corporate governance (CG), first of all, is based on taking into account the interests of the company's stakeholders both in the short-term and long-term period. So it could be an internal central, like a system, stream of company's development. CG represents not only control and procedure measures, but also an institute, that provides a framework defines the rights, roles and responsibilities of various stakeholder groups. One of the challenges of CG is related to maintain balance and incentives, required to minimize and manage conflicts of interest. OECD Principles of Corporate governance are constantly improved, and the impact is referred not only on company performance. GC has a significant influence financial stability and economic growth. The resent tasks are associated with digital impact on stakeholder's relations.

Crucial principles of CG are protection rights, especially protecting minority investors. Positive trends are noted for Russian companies according to the Doing business study and Competitiveness report, conducted by the World Bank. Until 2018 year Russia's position in terms of Corporate governance was improving. But in 2019 Russia has worsened position: remains low «property rights» and «conflict of interest regulation» estimation. However,

---

\*Corresponding author: [krasilnikova\\_lena@list.ru](mailto:krasilnikova_lena@list.ru)

the last measure focuses on director's opportunism and behavior to personally use of firm assets. Traditionally, principal-agent relations have been studied under the owner-manager concept and the positive agency theory in the context of the ownership separation from the control. This is a natural step in the company's development, when the founders delegate their governance functions to professional management, as discussed by A.A. Berle and G.C. Means [1]. Most agent-principal models are aimed at investigating conflicts of interest between the management and the owners. This conflict results from opportunistic behavior in spending the company's resources for the managers' own needs, excessive growth of remunerations, misuse of the company's funds, unreasonably high benefits, payments and preferences to the managers. Such agency problems encourage an increase in agency costs of equity capital for monitoring, control, contribute to lose profit, reduce the effectiveness of strategic projects. Management opportunistic behavior could be solved due to increase in debt financing, which would impose obligations on managers. However, debt attraction as a disciplining factor leads to an increase in agency costs of debt, causes underinvestment, a decreases in free cash flow for shareholders [2-4].

However, there are two controversial cases for Russian companies. Agency models of the capital structure take into account the availability of debt resources, but for more, than 35% of companies in 2009 year, 14% in 2012, and 19,6% in 2011 limit in attraction finance is the main obstacle to doing business.

Studying Russian companies, researchers have found significant differences in specifics of principal-agent relations, a high concentration of ownership and its impact on corporate activities compared foreign firm in developed capital market. In particular, the classical manager-shareholder conflict (when the management demonstrates opportunistic behavior) is not typical for Russian companies. Many foreign studies conclude that ownership concentration has a negative impact on the company's financial and economic performance and value. But for Russian companies, accumulation of ownership has a different meaning. A high ownership concentration in Russia is a defensive measure due to the lack of protection both for the owners and the company itself. A major shareholder, as a rule, performs functions of the management that controls the company and makes strategic decisions, and is not considered only as an opportunistic hired manager. In companies with a low concentration, the goals of the owners differ mostly and agency contradictions are growing, the presence of a strong owner, who has a strong and predictable strategy, contradiction are mitigated, but an extremely high concentration can lead to discrimination.

## **2 Methods: Corporate Governance Factors relation with Performance**

In the study of the problems of agency relations, it was traditionally assumed that the organization was at the stage of maturity and corporate characteristics at the previous stages were overlooked from the survey. The configuration of ownership and management is associated with the stage of life cycle in developed capital markets, when the founder-entrepreneur is the main initiator of the formation of the company. Moreover, the life cycle stage is mainly defined with management features and characters at various stages. The age and size of the company, its organizational structure, formalization, crises, and preferences of economic agents, agency relation and leadership are characteristics of the life cycle stages according to traditional approaches [5]. I.K. Adizes and L.E. Greiner investigated the stages of the life cycle and development of a company based on the modification of management types and management structure, the presence of entrepreneurial initiative in the founder [6-8]. The dominance of management styles and forms of interaction is primarily focused on solving internal developmental problems, in particular, the study of slowing development and quickly aging. They do not study the strong pressure of the

external environment, the weak protection of owners, the uncertain influence of state participation – such important problems typical for Russian companies [9]. For Russian companies, such combinations and types of management are not successful in the face of strong pressure from external threats and state participation. I.K. Adizes notes the condition of "silence" within a Russian companies (possibly due to the fear of public leadership qualities, autocracy and desires to control). For Russian companies, the use of the classical theory of the life cycle is complicated, since many companies were formed through privatization. According to the author, the weak protection of the rights and the inability to use market signals for better orientation led to the majority owners in management and a slower owner' delegation functions to management as compared to foreign companies with dispersed ownership. The owners prefer to control flows and holds the post of CEO [10].

## **2.1 Ownership Separation from Control, link with Board of Directors, Life Cycle and Performance**

Although recently there has been a tendency for owners to decrease involvement in management and attracting professional managers. Such changes according to early stages of life cycle in a developed capital market, are characteristic at the maturity stage in Russia. Now the management's interest in the long-term development of the enterprise is increasing. For example, the retail company Ltd. Lenta was established in 1993, and the founding owner was a director. As the company developed and foreign investors were attracted to the Board of directors (BD), the owner headed the BD. With the entry of foreign investors, the owner has stopped management functions, and after that, got out from the equity capital. The BD was chaired by a domestic minority shareholder, and a foreign representative of foreign funds was appointed as CEO.

For growing companies, the role and involvement of the BD is one of important force to sustainable development. At the early stages, in the BD includes those, who are most familiar with the industry and the market. Independent directors with significant knowledge could enforce environmental practices and mitigate agency conflicts [11]. Also Independent directors have a positive correlation with capital structure, owner rights protection, but a negative correlation with avoidance of unpredictability [12]. The Board diversity has a positive impact on sustainability in terms of ecological, social and governance performance. And the number of Independent directors doesn't encourage performance [13]. Not internal drivers stimulate Corporate governance changes, but also external factors like the level of stock exchange listing [14].

Controversial is the issue of development drivers. Within the life cycle concept, research is mainly aimed at changing the company's organizational characteristics related to management. The existing theoretical works are applicable to large companies with dispersed ownership, which makes it difficult to verify their applicability to Russian companies.

Recently, research has focused on fast-growing companies in emerging capital markets and identified a significant discrepancy between the actual situation and the conclusions from the agency theories, which caused the need for more detailed studies of behavioral characteristics of agents.

The preferences of interests affect the corporate strategies. Managers sometimes overestimate their characteristics, consider shares to be undervalued. Optimistic managers overestimate the likelihood of success and underestimate the risk, which leads to an increase in debt financing. From the one hand, in case of the opportunistic management behavior debt attracts to prevent ownership dispersion. From the other hand, debt capital is represented as internal governance, encourages performance and social responsibility [12]. The Corporate governance Index is higher at the growth stage. And debt-to-equity ratio has

a positive relation with CG at the slow growth stage. Companies with low CG have a tendency to decrease debt-to-equity, share of liquid assets is higher and they are more sensitive to market risk.

## 2.2 Digital relation with Corporate Governance

Digital technologies increase productivity, but change internal interactions. Responsibility of actors will increase through the introduction of Artificial Intelligence (AI), they will transfer from decision makers to agile leaders. And AI implementation will deepen Corporate culture in case of strong relations of human and machines [15]. One of the principles will be trust, openness and transparency. Moreover AI introduction will cause the crucial changes in the profit-maximizing concept. Sometimes less profitable strategies refer to an improvement in ecological, social performance [16].

## 3 Analysis: Key Factors and Some Results and Discussion

The author suggests that the characteristics and features of Corporate governance are related to the stages of the life cycle.

Hypothesis 1. Concentration of domestic ownership is the greatest at the stage of formation, and as the company transfers along life cycle, it decreases, and foreign owners get into the ownership structure. Based on regression model, it was revealed that the ownership of private insiders is the highest at the stage of formation, and the ownership of foreign owners rises at the stage of growth.

Further improvement of the model identifies the link between age, ownership structure and protection of rights. Due to the age increase company becomes more mature and acquires reputation.

$$CG_i = c + b_i * X_i + \varepsilon \quad (1)$$

$CG_i$  – corporate governance factors,  $X_i$  – age of companies.

The results presented significant positive impact of age on an increase in property rights (2,75 – estimated coefficient in the model) and ownership and control (2,08 – estimated coefficient in the model). Also protecting minority investors encourages R&D process, reflected in higher expenditures. Protecting minority contains several issues: disclosure information to shareholders, director liability, use shareholder capital, governance, Board structure and control.

Hypothesis 2. Digital strengthens agency relations. Growth of the quality of Corporate governance is positively related with the digital parameters. Based on Digital Competitiveness estimation of 62 countries and Doing Business ranking in 2020, was built model, reflected strong relation. Technology and companies' performance are actively highly correlated. So, ease to start business, register property, protecting minority investors have strong interrelation with Future Readiness. It reflects significant factors like Adaptive attitudes: E-Participation, Internet retailing, Tablet possession, Attitudes toward globalization. Russia remains low position except internet usage. The other factors – Business agility: Opportunities and threats, World robots distribution, Agility of companies, Use of big data and analytics, Knowledge transfer, Entrepreneurial fear of failure; and IT integration: E-Government, Public-private partnerships, Software piracy.

**Table 1.** Pearson correlation between Technology, Performance and Governance.

Technology factors	Performance		Corporate governance factors	
	Starting Business	Getting credit	Registry Property	Protecting Minority
Adaptive attitudes	0,48	0,05	0,39	0,14
Business agility	0,29	-0,15	0,31	0,1

## 4 Conclusion

The quality of Corporate governance directly affects the performance and strategies. This impact is not similar as in the country comparison, and for different stages of the life cycle. The characteristics of Corporate governance, based on ownership structure are different for Russian companies and companies in developed countries. For Russian companies, combinations of management types, according to I.K.Adizes, are not dominant in the development. The preferences of a large owner have recently being the main driver of development. Now they delegate functions to management and ecological, social, governance factors become more significant. According to the results of regression models, have found, that property rights and protecting minority investors are improving due to the higher stage of life cycle and age.

Digital also has a considerable impact on performance. It reflects changes in internal relations, modifies Corporate governance principles, referred to agency interaction. Based on empirical estimations of 62 countries in 2020 year, were identified significant correlations between Technology factors, companies performance and Corporate governance characteristics. So, an increase in Business agility, for example in case of use of big data and analytics or knowledge transfer, is associated with higher ownership protection. A decrease in Adaptive attitudes, presented by Attitudes toward globalization, deteriorates company's performance.

## 5. Acknowledgements

The article has been prepared with financial support of the Russian Fund for Fundamental Research. Grant of the RFFR № 18-010-01028 «a» (2018–2020).

## References

1. A.A. Berle, G.C. Means, *The Modern Corporation and Private Property* (1932)
2. M.C. Jensen, W.H. Meckling, *J. of Fin. Economic*, **3**, 305 (1976)
3. D.W. Diamond, *J. of Polit. Economy*, **97**, 828 (1989)
4. M. Harris, A. Raviv, *J.of Finance*, **46**, 297 (1991)
5. G.L. Lippitt, W.A. Schmidt, *Harv.Bus. Review*, **45**, 102 (1967)
6. I.K. Adizes, *Corporate Lifecycles How and Why Corporations Grow and Die and What To Do About It* (1989)
7. I.K. Adizes, *Organiz. Dynamics*, **9**, 3 (1979)
8. L.E Greiner, *Harv. Bus.Review*, **4**, 37 (1972)
9. E.V. Krasilnikova, *Ec. analyses: theory and practice*, **475**, 704 (2018)
10. T.G. Dolgopyatova, *Institutional problems of the Russian economy* (2015)
11. F. Haque, C. G. Ntim, *Bus. Strat. and the Environment*, **27**, 415 (2017)

12. J. Lu, J. Wang, *J. of Inter. Fin. Markets, Instit. & Money*, **4** (2020)
13. V. Naciti, *J. of Cl. Production*, **237**, 117727(2019)
14. O.A. Esqueda, T. O'Connor, *Res. in Inter. Bus. and Finance*, **51**, 101077(2020)
15. Official website of Accenture company, <https://www.accenture.com>
16. Official website of B the change, <https://bthechange.com>