

Business Groups and Corporate Governance Networks

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IEU,

April 27, 2014

Business Groups: The Big Players

- Business group is a collection of firms (listed or not) coordinated by a formal structure or by informal alliances.
- Apart from Anglo-Saxon countries, business groups are really the big players around the world.
- Keiretsu in Japan, Chaebol in South Korea, Konzerne in Germany, familiar business groups in Italy (ie. Berlusconi group)
- In Turkey they are really big. Top 15 business groups have more than %60 of the total market value in the stock exchange.

- Business groups are strange creatures that defy the logic of "the nature of the firm" (ie.Coase, Williamson)
- BGs have various flavors: Chilean business groups are very different than the Israeli ones
- Multidimensional space to locate a BG.
- Ownership and Control: Family, Families, Banks, State, Coops, Pension Funds
- Scope: How diversified are the BG firms in terms of economic sectors
- Depth: How are links among BG firms are maintained? Hierarchical or horizontal

- Conventional view on business groups emphasize the imperfect of missing markets.
- BGs substitute for missing or underdeveloped capital and managerial markets.
- BGs diversification is a way of portfolio diversification when insurance and risk markets are not developed.
- At the extreme, BGs are suspected for crony capitalism and abuse of minority shareholders

- Institutional or evolutionary scholars emphasize the endogenous growth of BGs.
- Alice Amsden favors BG firms as national champions.
- Institutional complementarities are underlined.
- BGs form and reproduce themselves in very different institutional settings, ie. South Korea versus Turkey

Corporate Governance of Business Groups

- A typical firm in an emerging economy is either a BG firm or an independent firm aspiring to become a BG firm.
- Thus BG firms' corporate governance principles and practices are extremely important
- By corporate governance we mean how a firm is run, generally by the board of directors.
- Although there have been a convergence expectation with respect to corporate governance due to globalization, there is still a huge diversity (Kogut 2012)
- The diversity will remain.

- The success of different corporate governance systems depend on many factors.
- We can nevertheless abstract those factors and classify into two main categories
- (1) Structures and (2) Practices
- However, we still have to consider interactions within and among these 2 main categories.
- Obligation to appoint independent directors: BGs handle by inviting members of other families or former managers into their boards.

- Government quality matters
- Existence and effectiveness of constraints on executive power
- Politically connected firms
- Rent-seeking
- Turkuaz Media example!

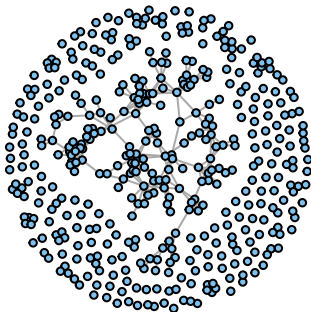
- Extent of state ownership matters
- How are the managers of SOEs controlled?
- Public-private partnerships
- Privatization

- Scale and scope of financial markets matter
- Is there a corporate bonds market?
- Does stock market work for IPOs?
- Private Equity? Hedge Funds?

Bist and Business Groups in Turkey

- We extract data for the listed firms in Turkey for the year 2013
- We construct a network in which two firms are connected if they share a common board member
- There are 435 firms 2635 board members some of whom connect some of these firms.
- There 536 links among firms.

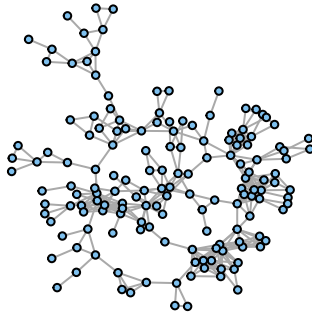
Firm Network in 2013



Firm Projection Statistics, Year: 2013.

Number of Components	177
Number of Edges	536
Number of Firms	435
Maximum degree	14
Mean Firm Projection Degree	2.46437
Mean / maximum possible degree	0.00567827

Giant Component in 2013



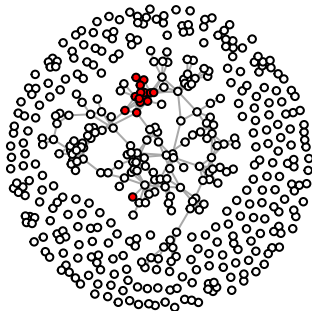
Giant Component

Number of Edges	382
Number of Firms	157
Maximum degree	14
Mean Firm Projection Degree	4.86624
Mean / maximum possible degree	0.0311939

KOÇ Business Group

- The biggest private business group in Turkey
- The origins go back to 1920s when the founder Vehbi Koç began as a trader and subcontractor for State.
- In 1963, the holding company is established.
- The third generation of the family is managing the BG.
- KOÇ BG firms operate in more than 25 sectors.
- KOÇ BG listed firms operate in 10 sectors.

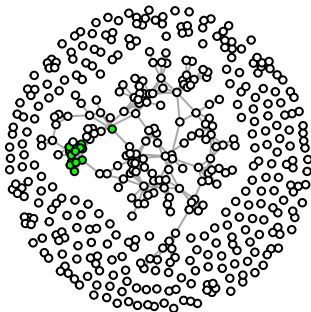
KOÇ BG



- There are 15 listed KOC BG firms
- KOC BG firms constitute %15 of the total market value in the stock market (BIST)
- KOC BG firms have important foreign partnerships
- with FIAT in TOFAS; with FORD in FORD OTOMOTIV, with UniCredit in YAPI KREDI BANKASI

- The second biggest private business group in Turkey
- The origins go back to 1930s when the founder Hacı Ömer Sabancı began as a trader and textile manufacturer.
- The holding company was established in 1967
- SABANCI BG listed firms operate in 9 different sectors.

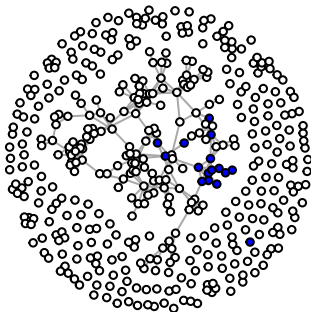
SABANCI BG



- There are 13 listed SABANCI BG firms
- SABANCI BG firms constitute %11 of the total market value in the stock market (BIST)
- SABANCI BG firms also have significant foreign partnerships
- with DuPont in SASA, with CitiBank in AKBANK

- ISBANK BG is a bank based business group. The main bank was established by the State in 1925.
- Currently the main bank is owned and controlled by the pension fund of the employees and retired employees.
- However, the Republican People's Party has also a stake of %28.
- ISBANK BG listed firms operate in 6 sectors but 10 of the 16 firms are concentrated in Finance and Glass production (6 in each)

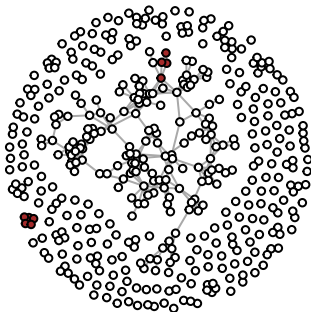
ISBANK BG



- ISBANK BG firms constitute % 6.7 of total market value in BIST.
- The main bank is critical in the development of other business groups.
- ISBANK BG is also a pioneer in venture capital projects.

- OYAK is a military-run business group.
- Although the formal owner is the pension fund of the military personnel the top generals have the last word
- The pension fund was established in 1961
- OYAK BG firms mainly operate in Cement, Auto and Finance

OYAK BG



BGs in the Giant Component

- The giant component provides the potential small world feature of the corporate governance networks
- High clustering and short average path lengths are important
- Enforcement depends on clustering
- Information and behaviour diffuse via short paths.

- Clustering coefficient is 0.57
- Average path length is 6.17
- There is a high clustering especially thanks to cliquishness of BG firms
- However the average path length is higher than other country networks as BGs have few links among each other.
- Either trust is lacking or there is no advantage to do so!

- Top 15 BGs in the giant component make up more than two thirds of the firms
- There are 157 firms and the total degree is 764 (which is twice the number of links)
- Top 10 BGs firms have % 74 all the degrees, that is they have 565 degrees collectively.
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- BG firms keep the small world of corporate governance networks through family members and loyal managers
- BGs collectively constrain the power of foreign capital
- BGs can stand against the excessive intervention of the executive power
- BGs incubate new start ups in new sectors

- The downside of the dominant BGs is the lack of entry
- Through their control of capital markets BGs enjoy a huge advantage
- There should be an optimal balance with BGs and independent/foreign firms.