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Corporate Governance and Bond Ratings in Malaysia

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Abstract

This paper examines the effects of corporate governance mechanisms on bond ratings of banking firms in Malaysia. This study scrutinises the link between institutional ownership, and independent directorship with bond ratings of Malaysian local banks, while holding the debt to equity and size of the firm as control variables. Our sample consists of Malaysian local banks from 2005 to 2017. This study employed the panel ordered logistic regression and found that independent directors and blockholders show an insignificant relationship with bond ratings. Leveraging debt to equity ratio also showed an insignificant relationship with bond ratings. However, a significant positive relationship has been found between firm size and bond ratings. Our insignificant result for corporate governance mechanism and bond ratings may be due to banking firms work closely with rating agencies as they are also part of the key underwriters of debt securities issuing and Sukuk for other cooperations; hence their bond ratings may be less influenced by their independent directors and blockholders. The study from this paper can be used as a guideline for bank management, current and potential investors, and policymakers in Malaysia by providing additional evidence of bond ratings in the Malaysian market.

Key words Corporate Governance, Bond Ratings, Institutional Ownership, independent Directorship

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1. Introduction

Managing business and company affairs require a process and structure in which generally known as corporate governance. Good corporate governance is known as the key to enhance business prosperity while taking into consideration of other stakeholders interests, and ensuring corporate accountability with the goal of realising long term shareholder wealth, as stated in the Report on Corporate Governance in Malaysia by the Finance Committee (2000). In Malaysia, after the Asian Financial Crisis back in 1997, corporate governance was introduced and started to gain attention. Amendment of the listing requirement by Bursa Malaysia in 2001 represents the evidence of corporate governance forte.

In Malaysia, the foundation of the development of the bond market involves the inclusive controlling framework and resilient groundwork, along with clear vision and mission, political stability, and comprehensive macroeconomic policies. Since the early days of bond introduction in Malaysia, Bank Negara Malaysia (BNM), a government agency is responsible for the compliance of corporate bond issuance. Two government agencies, namely the Malaysian Rating Corporation Berhad (MARC) and Rating Agency Malaysia Berhad (RAM) provide sovereign estimations and opinions on how a potential debt issuer