

THE CORPORATE GOVERNANCE DRIVERS: WHAT RELATIONS WITH PERFORMANCE AND RISK? EMPIRICAL EVIDENCE FROM ITALIAN CONTEXT

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Abstract

Considering a sample of Italian firms and defining a good Governance index (gGI), we investigated if there is a relation between the gGI, the performance and the default risk and which governance determinants are most responsible of these effects. To deepen the analysis, the aforementioned relations are also observed by comparing family and non-family firms and the companies more or less active in M&A. We found that the Corporate Governance quality presents some correlations with performance and risk. The non-family companies are better structured, showing a positive correlation between some Corporate Governance drivers and performance and Z-score. Furthermore, the "well-advised" firms in external strategies are able to obtain a better correlation with performance and also a good relation with Z-score****.

Keywords: Corporate Governance; Good Governance Index; Performances; Bankruptcy Prediction; Family Business; Acquisitions

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1 Introduction

The issue of corporate governance has always been interesting for business economics. Several reasons have led scholars to address the above issue. In particular, in the context of management studies, corporate governance may prove to be an important determinant of various aspects of business dynamics. Such aspects can reconnect, for example, to the performance, to the default risk and, nevertheless, to the probability of the future survival of the company. Riskier financial conditions can be determined, in fact, both by inefficient internal dynamics and by general hostile economic conditions (Whitaker, 1999). In this context, the current economic and financial crisis has made companies more vulnerable and more exposed to situations of insolvency. The interest towards the relationship between corporate governance issues, performance and conditions of financial distress is emphasized also by recent cases of corporate governance failure, such as the scandal of Parmalat (Melis, 2005). In particular, this study focused on the mentioned issue researching some possible relationships between the main determinants of the corporate governance of the sampled companies, some performance and default risk indicators.

For this purpose, we proposed a synthetic indicator (good Governance Index-gGI) capable of providing a measure of the quality of corporate governance for companies listed on the Italian Stock Exchange (MTA segment) in 2005-2011, excluding pure financial companies and real estate services companies (Giovannini, 2010; Sraer and Tesmar, 2006; Favero et al., 2006). A more accurate analysis of the impact of governance systems, on one side, and performance and risk, on the other, has been conducted looking at the relationships between some of the parameters used to build the synthetic indicator and some performance and risk measures. The analysis reveals that some key factors of the governance profile – such as the existence of shareholders' agreements, of a Code of Ethics and the presence of non-executive directors – can positively bind with certain performance and business value measures. In particular, the performances were observed focusing on their accounting profile (ROI), on their market trends (CAR) and on the evaluation of the company's ability to create value (Tobin-Q). The financial risk, however, was measured looking at the level of indebtedness (Leverage), and at the Z-Score indicator, developed to classify the sampled firms into financially distressed and non-distressed groups (Altman, 1968).

In these years, the discussion is lively on what may be the best strategies to create value and to "react" to the crisis (Wan and Yiu, 2009; Cartwright and Schoenberg, 2006). Entrepreneurs and policy makers are debating on the real contribution that merger and acquisitions can play on the value creation process (Bigelli and Mengoli, 1999) and on the different factors of attractiveness that a market in recession can present, including the opportunity to deal underestimated targets (Granata and Chirico, 2010). Analyses that involve the observation of the economic system in general, but particularly in Italy, also cannot leave aside the study of family business that represents an essential component of the Italian economic structure. The family business is an "evergreen" research field concerning for example the definition of the "familiness", the relationships between the "familiness" and the performances, the implemented strategies and some other issues. One of the topics moving the debate among scholars regards its possible dynamics of growth of family firms. In this sense, our analysis is based on the evidence stemming from a sample of the Milan Stock Exchange listed companies which made acquisitions in the considered period.

In order to deepen the investigation and to better understand if the particular nature of the companies, or their capacity to pursue external growth strategies, could affect the above mentioned relationships, we analyzed the sampled companies distinguishing them on the basis of their "familiness" (Rutherford et al., 2008) and of their propensity towards the realization of active acquisitions. In this regard, we tried to verify the difference of effects of Corporate Governance variables on performance and risk for family businesses and for companies involved in active M&A deals.

Our major finding is that companies could improve their Corporate Governance quality, especially in the subsample of family business: they detected a lower value of the good governance index, although the index value could be influenced by some specific drivers connected to the "familiness" (i.e. Executive Independent, CEO). Moreover, we should point out that the non-family companies are better structured, demonstrating a greater protection of minorities and opening to the outside.

We can highlight a positive correlation of gGI values with Tobin Q in static analysis. For this reason, we can observe that the Tobin Q is the only parameter that manages to capture a relationship. The "well-advised" firms in external strategies are able to obtain a better correlation with performance and a less probability of default (Z-score).

Observing the aforementioned relationships for the identified subsamples, we can find that a greater acquisition activity⁸ is correlated with a lower probability of failure (Z-score) and with a positive sign of CAR. Among the other results, which will be discussed later, we mention that the non-family firms, that present a better gGI, show a lower probability of default.

⁸ It is important to underline that the more active in corporate acquisition companies feel the need to draw up a Code of Ethics.

The paper is structured as follows. After a definition of a theoretical framework, we illustrate our research hypotheses. Then, we describe the data collection process, the variables used in the empirical analysis and the statistical methodology. In the last parts, we discuss our findings and the limitations of our study. Again, we highlight that this work is a first step in the overall research, a work in progress: the study, in fact, is proceeding with an expansion of the sample, introducing a benchmark with the companies of other countries.

2 Literature and research hypotheses

The quality of Corporate Governance models, imposed by a legal system or Auto Disciplinary Code, may be important for the proper functioning of the economic system (Roe, 2004). Some studies confirm that improvements in corporate governance practices and rules, as the awareness and active involvement of all components of the business community (Brown and Taylor, 2006), can increase the economic efficiency (World Bank, 2001). In the context of the different Corporate Governance definition, we mention the interpretation elaborated by Baghat et al. (2010: p. 1806) that put the rules of good governance first as an investment and therefore the importance of the measurement of its effects: "*Corporate governance is the set of processes that provides an assurance to outside investors of a fair return of their investment*".

Performance, accountability and supervision are interdependent dimensions: managers and Boards of Directors – being "measured" continuously for the results obtained by the company under their guidance – should improve their performance, helping the business to grow. There has been renewed interest in the Corporate Governance practices of modern corporations, particularly in relation to accountability, since the high-profile collapse of a number of large corporations during 2001-2002, most of which involved accounting fraud. In fact, many corporate crises were caused by deficiencies, or even the absence, of controls: the importance given to Corporate Governance issues by the owners and the managers, as well as by the market and the legislator, have grown considerably (Baghat and Bolton, 2008; Barontini and Caprio, 2006). In recent years the Corporate Governance issues are focusing on interest of scholars and practitioners, stimulating a cross-culture discussion, investing finance scholars, economists and jurists. A search for "Corporate Governance" found a lot of titles, that analyzed the different matters, but one of the most important issue is the need to "measure" the quality of firm's Corporate Governance and the effects that a good practice may have on performance and on the level of risk, especially on the default risk. In literature, there have been innumerable studies examining the Corporate Governance best practices (Black, 1999; Lipman and Lipman, 2006; Tarantino, 2008; Zaffron and Logan, 2009) and the impact on performance, using several parameters. The issue of measurement of Corporate Governance is still very delicate and discussed (Romano, 1996; Bhagat and Black, 2002). In fact, it is a matter of great importance for

academics and for investors. There is still not today a unique universally adopted methodology and a unique meaning of Corporate Governance (Bhagat et al., 2008; Colarossi et al., 2008). The studies of Gompers et al. (2003) have opened a new thread pointing to the creation of firm level Corporate governance indexes (G-Index), that can concentrate the contribution of different drivers of the Corporate Governance quality. The use of an index, as an aggregated measure of Corporate Governance quality, allows scholars and

professionals to enjoy a significant advantage, because they can relate the Corporate Governance with companies' performance indicators. After these studies there have been other contributions that have banked some simplification (Cremers and Viany, 2005; Bebchuk et al., 2009; Brown and Caylor, 2006) or to consider the country policy regulation (Bubbico et al., 2012) (Tab. 1).

Table 1. Most important Corporate Governance Indexes in literature

CORPORATE GOVERNANCE INDEXES	AUTHORS	NUMBER OF DRIVERS
Governance Index (G)	Gompers, Ishii and Metrick, 2003	24
Alternative Takeover Protection Index (ATI)	Cremers and Vinay, 2005	3
Gov-Score Index and Gov 7	Brown and Caylor, 2006	51 and 7
Entrenchment index (E) and Other Provision Index	Bebchuk, Cohen and Ferrel, 2009	6 and 18
Corporate Governance Index (CGI)	Bubbico, Giorgino and Monda, 2012	76

These indexes are similar but different at the same time, both in terms of number and of kind of included drivers. It is obvious that considering a wide range of factors a more indicative index and a more accurate firm's Governance measurement can be produced. On the other hand, it is also true, however, that adopting a more limited number of provisions makes the index far more practical, easier and faster to find all the information necessary for its construction. It will focus more attention on those few, but more reliable and relevant.

For this reason, in this work a Corporate Governance index (good Governance Index-gGI) was built and tested, adjusted to Italian enterprises, considering the peculiarities of the national context. The main cognitive goal is to evaluate the minority protection, as well as the level of openness towards investors, especially private equity funds, that have become an important partner for financial support to enterprises' strategies. Private equity funds can produce significant advantages for businesses, including credibility, improvement of rating, higher visibility and increasing corporate communications, better access to community and international contributions: in essence, they stimulate a well-structured governance (AIFI, 2013).

Another factor of interest is the study of the relation between the level of good governance with the performance and the financial risk. In academic empirical studies of the relationship between Corporate Governance and performance we can identify two research fields. In the first case, the analysis is centered in the study of Governance effects, such as unitary complex of choices of Government, for the creation of business value. The second group of studies, on the other hand, focused on the drivers of Corporate Governance (specifically the Ownership structure, the Size, Composition and Turnover of the Board of Directors and the Control System) and the performance (Romano, 1996; Baghat and Black, 2002). Despite widespread belief in the importance of governance mechanisms for resolving agency problems (Jensen, 1988), the empirical

literature, investigating the effect on corporate performance, has not been able to identify a unique effect. Although Gompers et al. (2010), Brown and Caylor (2006) and Bebchuk et al. (2009) found a positive associations between their indexes' rankings of governance quality and firm performance, correlations are obviously not causation. Subsequent works have even questioned whether a positive association truly exists (Cremers and Nair, 2006; Lehn et al., 2006; Core et al., 2006).

In addition to these studies, we considered further research that has occupied the theme of the relationship between good Governance practices and corporate performance.

A first example was a survey (McKinsey, 2000 and 2002) highlighting that about 80% of investors would be willing to pay a premium for well governed companies, with a majority of external, independent advisors. The amount of the premium, according to the survey, should be a minimum of 11% for Canadian companies, to a maximum of 40% for those companies operating in countries with a less strong State regulation.

Other studies have also found a link between the quality perception of the company and the stock returns. For example, in research on consolidated profit in five years, led by the American Magazine Fortune, it was shown that in "much admired" companies presented a consolidated profit of shares in five years equal to 125%, compared to the 80% of those "less experience".

In an economic situation in which there is a "struggle for existence" (Lee and Yeh, 2004; Hui and Jing-Jing, 2008) a strong debate began about the relationship between Corporate Governance and default risk. Among the many reasons that led a company to a crisis, a large literature highlighted the ineffective and inefficient management and control systems: the problems related to Corporate Governance as a bad "governum" (Mumford, 2003; Wright et al., 2002). The seriousness of the causes of decline is expressed by poor economic performance and often resulting in loss of value for the companies.

The outlook of the company is not favorable and the degree of risk is ever increasing (Mariani and Panaro, 2012). More attention has been given to the study of systems and instruments that can be adopted in the prevention, diagnosis of corporate crisis (Lappalainen and Niskanen, 2009). In literature on corporate finance there are numerous works on problem analysis and forecasting crisis (Altman, 1977, 2000, 2002; Altman and Hotchkiss, 2006; Beaver, 1966 and 1968; D'Annunzio and Falavigna, 2004; Friedman, 1977; Hui and Jing-Jing, 2008; Lee and Yeh, 2004; Mumford, 2003).

In this framework, we considered relevant to verify the existence of a relationship between the quality of corporate governance system – defining a Corporate Governance Index – and the corporate performances e the default risk (Altman, 2000; Platt and Platt, 2002). For this purpose has been formulated and tested the following research hypothesis:

H1: There is a relationship between the quality of Corporate Governance and performance and default risk.

A more in-depth analysis of the relationship above hypothesized, requires the identification of the different Corporate Governance drivers influence on performance and risk. In accordance with Agency Theory, we can highlight that a widespread share ownership could determine a reduction of involvement or even the difficulty for the owner to exercise effective control over the management (Jensen and Meckling, 1976). Studies in this area have shown, albeit with obvious simplifications and limits, a positive trend in support of the theory of the agency costs, highlighting how the presence of an active shareholder reduces the tendency of managers to pursue private interests and to promote value creation. Yet, Bhagat and Bolton (2008) found a significant positive relationship between performance and ownership. The decisive balance of studies found none between Directors independence and performance, shown by accounting parameters or stock return measures (Romano, 1996; Bhagat et al., 1999). In this sense, therefore, it would seem useful in terms of Good Governance to take an ownership structure that requires a principal owner and not an overly fragmented one (La Porta et al., 2000).

The relationship between voting rights and performance has not been as extensively studied as that of board composition. Not surprisingly, some studies showed that voting rights are economically quite valuable (Gompers et al., 2010; Zingales, 1994). Other researches (Forbes and Milliken, 1999) investigated the correlation between the size of the Board and the corporate performance, and not all had the same empirical results. In fact, there are studies claiming that the increasing of the numbers of members can determine new strategic opportunities, with advantages in terms of performance. Other studies showed that the benefits emerging from an increasing size of the Board produces lower costs due to major decision-making and organizational complexity of Corporate Governance (Lipton and Lorsh, 1992).

Further studies, concerning the relationship between the components of the Board of Directors turnover and business performance, went on to

analyze the optimum composition of it in relation to the number and the impact of the independent Directors in terms of value creation (Li and Harrison, 2008; Bhagat and Black, 2002; Mork, 1988).

Ample space is also occupied by studies and research relating to the issue of internal controls. The presence of an effective control system facilitates the convergence of different interests within the company. According to these studies, there is a positive correlation between higher level of independence and technical expertise of internal control bodies and value creation (Chan and Li, 2008). The studies of Bennedsen et al. (2009) provide direct evidence that CEO actions can have a meaningful impact on performance. In order to deepen the cited debate, we can define the second research hypothesis:

H2: There is a relation between the Corporate Governance quality drivers and performance and default risk.

Although in several countries, the most common large shareholder are families (Anderson and Reeb, 2003; Villalonga and Amit, 2006), it should be noted that in Italy the presence of family businesses has spread in a more marked way than in other countries (Corbetta and Salvato, 2004; Gnan and Songini, 2003; Gnan and Montemerlo, 2008). In recent years, the studies on this topic have multiplied, more often supported by empirical analysis, to deepen the “definition dilemma” (Rutherford et al., 2008; European Commission, 2009; Toma and Montanari, 2010) and the impact that the family role could express on performance and on corporate governance quality (Litz, 1997; Miller et al., 2007; Chrisman et al., 2010; Sharma, 2011; Pearson and Lumpkin, 2011). The first crucial question is what a family business is. The “definition dilemma” is somewhat debated and still able to produce controversy. As it is well known, it is not possible to find an unambiguous and generally shared definition of family business. Being a family firm depends on different aspects. Some studies define a firm as a family business considering the sole extent of interest owned by the family (Donckels and Frohlich, 1991). In a progressive evolution scholars have additionally considered the presence of family members also in management (Astrachan and Shanker, 2003; Babicky, 1987; Chrisma et al., 2004; Churchill and Hatten, 1987; Davis, 2007; Dreux, 1990; Donnelley 1964; Handler 1990; Holland and Boulton 1984; Holland and Oliver 1992; Lyman, 1991; Litz, 1995; Pratt and Davis, 1986). The development of a synthetic indicator capable of representing the degree of family involvement in the firm is a possible solution to understand the different aspects (Astrachan et al., 2002, Klein et al., 2005). The importance of family business has sparked a growing body of studies that focuses on the governance of these companies. Aside from defining problems, we must emphasize that family firms are unique because the corporate governance is largely determined by family control. In fact, in terms of governance, ownership concentration may alleviate the agency problems from dispersed shareholdings (Miller et al., 2010). The challenge is that families may steer firms towards decisions that favor them at the expense of minority

shareholders (Becht et al., 2003). The family organization can play a crucial role in decision making. At the most general level, family governance determines the type of interactions between the family and the firms (such as Ownership, Board of Directors, and Management). Bennedsen et al. (2007) provide stark evidence that the characteristics of the family behind the firm can affect succession decisions and performance. The existing literature provides few clues into the specific ways in which family firms use their characteristics or structure to affect value (Caprio et al., 2011). Direct tests on the effect of governance in family firms are rare in literature and it can be an attractive area of research for the future. In this discussion we can analyze the third research hypothesis.

H3: The relation between Corporate Governance quality drivers and performance and default risk is different for family and non-family firms.

As previously noted, the corporate governance quality can influence the company strategies and M&A activity is a fundamental strategy for growth, for value creation and sometimes for the enterprise survival (Bigelli and Mengoli, 1999; DePamphilis, 2012; Healy et al., 1992; Heron and Lie, 2002; Teece et al., 1997;). In fact, many multinational companies today are the result of M&A between two or more companies (Arnold, 2013). The high incidence and volume of mergers and acquisitions highlights their importance to the economic context of the firms operating in different countries. The literature on M&A is extensive. Several studies argue also that corporate acquisition is one of the mechanisms by which companies gain access to new resources through redeployment, increase revenues, efficiency and cost reduction. The realization of M&As, as known, promotes the achievement of market, operating and financial synergies (Sirower, 1997; Sirower and Sahni, 2006) by combining the resources of the two merging companies. Another kind of synergy discussed in the academic literature results from the improvement of the target firms' corporate governance. A hostile acquisition can be considered an important corporate mechanism to correct opportunistic managerial behavior. However, a "good governum" can influence the success of these operations. In fact, M&A activity is sometimes mentioned as the outgrowth of corporate governance failure. This is because numerous empirical studies showed that a substantial proportion of M&As destroy corporate value. The failure of an acquisition (Kalpic, 2008; Marafioti, 2005) is, in most cases, attributable to the managerial inability and lack of a strategic management. Murphy, Shleifer and Vishny (1991) cited agency problems between management and shareholders as the main driver of such value destroying acquisitions. Self-interested managers may engage in M&A activity to achieve their personal objectives, such as "building an empire", at the expense of shareholders value (Jensen, 2005). So the fourth research hypothesis:

H4: The relation between Corporate Governance quality drivers and performance and default risk may be different for companies with a higher or a lower propensity to M&A activity.

Since some transactions may result in value destruction if there is a conflict of interest between management and shareholders of the bidders, we can argue that the Corporate Governance quality is a crucial issue for institutional shareholders that are determined to finance M&As and to complete restructuring operations. Institutional shareholders generally agree on the core principles of corporate governance and what might be deemed to be good governance. The level of balance between the rights of shareholders and managers and the opening degree of management and control structures are important for institutional investors, who would be willing to recognize a premium for well governed companies (Mc Kinsey, 2002): in essence "*the need of openness*" (Gubitta and Gianecchini, 2011).

3 Methodology

3.1 Data collection

The analysis is based on the evidence stemming from a sample of the Milan Stock Exchange listed companies. The sample includes all the companies which were listed in each year from 2005 to 2011 and which realized at least one acquisition in the period, excluding pure financial companies and real estate services (Giovannini, 2010; Sraer and Tesmar, 2006; Favero et al., 2006). The sample dimension is of 98 units.

It was necessary to merge several data sources in order to build an exhaustive database to analyse different aspects:

- 1) to provide measures on the number of mergers and acquisitions operations;
- 2) to calculate performance indicators;
- 3) to identify family businesses;
- 4) to measure the market value of the company;
- 5) to assess the financial risk of the company.

Accounting data was drawn from the Financial Statements of the companies, the DataStream and AIDA databases and from the companies' web-sites. Information about corporate acquisition activity was taken from the Zephyr files. The Borsa Italiana and YahooFinance website provided data on the companies' share prices and Corporate Governance Relations. Gathering data on "familiness" was particularly demanding. Most of information was drawn from the companies' corporate governance reports and from the Consob files. In some cases, it was necessary to consult the company's web-site and/or journalistic data sources.

3.2 Variables description

We describe, below, the other variables used for the empirical analysis.

3.2.1 Familiness

In this paper, we distinguished the family firms from other companies, using variables well-suited to expose the characteristics of the Italian economic context and unambiguous in their definition (Astrachan et al., 2002). First, we introduced a criterion regarding ownership and management at the

same time, i.e. a dichotomous variable "familiness" (equal to 1 in the case of family businesses, 0 otherwise). According to this interpretation, the following were considered family businesses (see table 2):

- Companies where family members own a majority interest equal to at least 50% + 1 of the equity capital (family presence in the property).
- Companies where at least one member of the family (major owner) holds a business interest not smaller than 20% (Klasa, 2007: p. 346) and at least one member of the family is part of the Board of Directors (family presence in ownership and in administration).

The criterion "family presence in the property" includes in the group of family businesses all companies in which control is permanently held by the family (regardless of the fact that there are family members in the Board of Directors), for which there is no possibility of involuntary loss of control rights as a result of passive takeovers. The choice of a high threshold (absolute control) of the share capital is

based on the characteristics of Italian companies. The Italian context, is characterized by companies with more concentrated ownership with respect to the Anglo-Saxon benchmark, especially in the case of family businesses (Favero et al., 2006; Granata and Chirico, 2010).

The second condition (family presence in ownership and in administration) is designed to include, in the sample of family companies, firms that are not completely controlled by the family capital. So we considered the presence of family members both as shareholders and as directors. In other words, if the family does not have absolute control, the family presence is required on the Board of Directors too. The aforementioned condition is also in line with Corbetta and Tommaselli (1996) and with Klein (2000). These authors stress that family participation in business can be inferred from the family control of the capital or, if the controlling stake is not held by the family, from the degree of influence of family members on the management.

Table 2. Family business identification criteria

		Ownership		
		family member = 0	family member = 1	family member > 1
Management	family member = 0	Non family	Non family	Family**
	family member = 1	Non family	Family*	Family*
	family member > 1	Non family	Family*	Family*

* if family stake is > 20%, ** if family stake is > 50%

3.2.2 Corporate governance index

The purpose of Good Governance Index (gGI) is to identify the level of openness to new shareholders and to measure the degree of protection to minority shareholders. We introduced the different elements of Governance that could contribute to this aim (tab. 3).

Each of these Corporate Governance variables, except those relating to the existence of shareholders' agreements and Auto Disciplinary Code, serves as a dummy variable — we can assign to it a value of 0 or 1. Since the purpose of the indicator of "good governance", as anticipated (to measure the degree of protection of minority shareholders and the company's opening level at the entrance of new members), assigning values to these variables follows this simple and logical policy: we will assign the value 1 to the variable object of analysis if it reflects a greater degree of openness to new members or input of greater protection of minorities. While, we assign the value 0 in the opposite case. With regard to shareholders, it was decided to assign the values 0 or 1, -1, while for the adhesion to the Auto Disciplinary Code has opted for assigning values 0, 1 or 2.

3.2.3 Performance

In order to assess the relationship between the quality of the corporate governance system and the performance, we considered two different performance indicators referred to the economic and financial status of the companies and to their market prices, as described below:

- ROI (Return On Investment) as accounting performance variables;

• CAR (Cumulative Abnormal Returns) used as market performance indicator (Masulis et al., 2007), obtained, on an annual basis, as the sum of monthly returns of stock prices compared with the FTSE-All Share Italy:

$$CAR = \sum_{t=1}^{12} \left[\frac{p_t - p_{(t-1)}}{p_{(t-1)}} - \frac{Ftse_t - Ftse_{(t-1)}}{Ftse_{(t-1)}} \right]$$

- Tobin-Q is the ratio of the market value to book value and it is calculated as follows: (total assets – equity book value + equity market value)/total assets. Where equity market value is represented by market cap.

Table 3. The Good Governance Index (gGI)

Corporate Governance Variables	SCORE
Administration Model	
Traditional	1
one-tier system	0
two-tier system	0
Auto Disciplinary Code	0 if not present 1 if partially present 2 if present
Code of ethics	1 if present; 0 if not present
Non-executive directors	1 independent; 0 dependent
Executive directors	1 no family member; 0 family member
Board of directors	1 if present; 0 if not present
Board audit committees	1 if present; 0 if not present
Compensation committees	1 if present; 0 if not present
Nomination Committee	1 if present; 0 if not present
Stockholders' agreement	0 if not present; 1 if for minority protection; -1 if for majority favor
Minority expressed Directors	1 if present; 0 if not present
Corporate Agreement or veto of Private Equity	1 if present; 0 if not present
Private Equity Directors	1 if present; 0 if not present
Nonvoting Stock	0 if present; 1 if not present
Chief Executive Officer (CEO)	1 external; 0 family member

3.2.4 Financial risk

We focused also on the company's risk profile. In this analysis, were considered indicators of financial risk represented below:

- Leverage (Debt/Equity) as financial risk indicator;
- Z-Score as default risk indicator. The Z-Score model consists in a linear analysis in that five measures are objectively weighted and summed up to define an overall score that represents the basis for measuring the risk of bankruptcy (Altman, 1968). We decided to use a revised version of Z-Score to represent the characteristics of Italian companies better (Bottani et al., 2004): $Z\text{-Score} = (1,981 \times \text{Working Capital/Assets}) + (9,841 \times \text{Retained Earnings/Assets}) + (1,951 \times \text{ROI}) + (3,206 \times \text{Equity/Assets}) + (4,037 \times \text{Return On Sales})$. The operating nature of the components described above, make the Z-Score more capable than other indicators to explain the risk linked to the operational aspect of the business.

- M&A: number of active operations concluded.

3.3 Statistical analyses and results

The aim of our analysis is to understand if and how corporate governance features can influence the performance and the risk of Italian listed companies. To do so, we collected a sample of 98 companies listed on the Italian Stock Exchange Market since 2005 to 2011, that had an active role in corporate acquisitions. For each of them we collected

information about corporate governance features, performance, risk and other data that we used to cluster the sample. Being aware of limitations due to this choice, we used a simple least square approach, in order to preserve easy and immediate understanding of results. First of all, we tried to build a synthetic index able to reflect corporate governance quality for each company. We listed 15 corporate governance features and built a matrix A_{mxn} ($m = 98$ is the number of companies and $n = 15$ is the number of corporate governance features considered). Each element of A , that is A_{ij} , is equal to 1, if company i has corporate governance feature j , otherwise if not present 0. The synthetic index of corporate governance is simply given by the row-wise sum of the matrix A . In the following Fig. 1 we displayed the distribution of gGI, that, as we can easily check, seems to be Gaussian. gGI index has a mean of 9.16 and a standard deviation of 1.72; the mode is 10 whereas the median is 9.

In order to discover if different corporate governance frameworks are responsible for different company performance and risk, we regressed companies performance indexes (ROI, CAR and Tobin Q) and companies risk indexes (Z-Score and leverage) versus our synthetic index gGI. We carried out two types of analysis: statical and dynamical. In the first one, we regressed the value of performance and risk indexes concerning the 2011 versus the gGI. In the latter, we analysed the correlation of the trend of performance and risk indexes of the last 6 years versus gGI. The static analysis highlighted a lower correlation (tabb. 4-5).

Figure 1. Distribution of Good Governance Index (gGI)

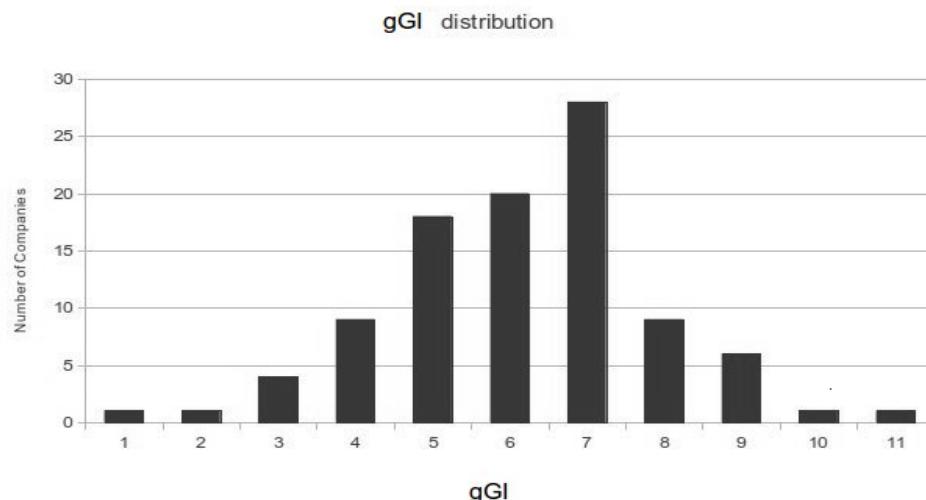


Table 4. Relation between Corporate Governance Index (cGI) and Performance. Static regression results

ROI vs. gGI	Beta	Standard Error	P-value
Const.	0,0254417	0,0460528	0,5823
gGI	-0,00423439	0,00494937	0,3950
Tobin Q vs. gGI	Beta	Standard Error	P-value
Const.	0,258493	0,143490	0,0758 *
gGI	0,0313410	0,0154371	0,0460 **

Table 5. Relation between Corporate Governance Index (cGI) and Risk. Static regression results

Leverage vs. gGI	Beta	Standard Error	P-value
Const.	1,21931	0,877316	0,1688
gGI	0,00937297	0,0943842	0,9212
CAR vs. gGI	Beta	Standard Error	P-value
Const.	-6,30081	7,24143	0,3864
gGI	0,541032	0,776819	0,4878

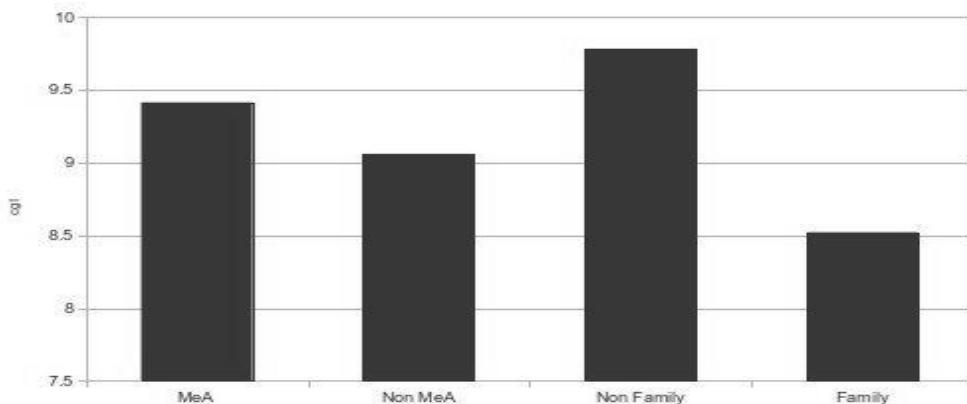
As we can see, only in the regression versus Tobin Q, gGI Beta is significantly different from 0 and shows a positive correlation between Tobin Q and gGI. Dynamical analysis shows insignificant correlations between performance/Risk indexes and gGI. We omit the results for brevity. The poor explaining power of our model can be due to the strong heterogeneity of the sample. To avoid this problem we clustered the sample using some a priori knowledge. More precisely, we separate companies whose number of merging and acquisition activities is under the mean from companies very active in M&As

and family from non-family business (Fig. 2).

Considering the number of M&A procedures, companies who are above the mean are 29, with an average gGI of 9.41 and gGI standard deviation of 1.59. Companies who did a number of M&A procedures smaller than the mean are 69 and have an average gGI of 9.05 and a standard deviation of 1.77.

Non-family business sub sample is composed of 50 companies with an average gGI of 9.78 and gGI standard deviation of 1.89; 48 companies composing of family business sub sample have an average gGI of 8.34 and gGI standard deviation of 1.72.

Figure 2. Value of gGI for different subsamples



In the following we show only significant results for the four subsamples.

Table 6. Relation between Corporate Governance Index (cGI) and Performance in companies more active in M&A

CAR vs. gGI	Beta	Standard Error	P-value
Const.	0,373989	0,222303	0,1040
gGI	-0,0435213	0,0232948	0,0726 *

Table 7. Relation between Corporate Governance Index (cGI) and Performance in companies less active in M&A

Tobin Q vs. gGI	Beta	Standard Error	P-value
Const.	0,201879	0,182826	0,2747
gGI	0,0371954	0,0197842	0,0658 *

As we can see, correlation between gGI and Tobin Q seems confirmed for companies who made fewer M&As, whereas, for the more active companies this correlation disappears, it is replaced by a small negative correlation between CAR and gGI.

Family/Non-family subs samples do not show significant results.

To understand better which Corporate

Governance component influences performances and risk, we regressed each single component of gGI versus both static and dynamical performance and risk indexes. We carried out the analysis for the whole sample and for four sub samples as before: high M&A/low M&A and Family/Non-family business.

We summarized significant results in table 8.

Table 8. Relation between different drivers of Corporate Governance Index (cGI) and Performance in the whole sample (Delta before index name indicates the trend of the index in last six years)

Parameters	Corporate Governance drivers	Beta	Standard Error	P-Value
Tobin Q	Shareholders' agreements	0,120926	0,0558514	0,0336**
Z Score	Executive directors	18,0959	9,69341	0,0659*
CAR	Board audit committees	8,14818	3,53234	0,0232**
Delta Tobin Q	Non-executive directors	-6,86202	3,55479	0,0565*
Delta Z Score	Shareholders' agreements	3,85124	1,87267	0,0425**
Delta CAR	Code of ethics	-0,281618	0,0969400	0,0046***

Results for the whole sample show that six corporate governance drivers seem to affect performance\risk indexes, two of which with a negative beta (Non-executive directors, Code of

ethics). It is interesting to highlight that same dependent variables are affected by different corporate governance drivers if we consider static or dynamic variables.

Table 9. Relation between different drivers of Corporate Governance Index and Performance in family business
(Delta before index name indicates the trend of the index in last six years)

Parameters	Corporate Governance driver	Beta	Standard Error	P-Value
ROI	Executive directors	-0,0559147	0,0250111	0,0310**
Tobin Q	Auto Disciplinary Code	0,115830	0,0598827	0,0602*
Tobin Q	Non-executive directors	0,133420	0,0713513	0,0688*
Z Score	Board audit committees	-9,22987	2,38871	0,0004***
Z Score	Non-executive directors	5,26496	2,35149	0,0308**
Delta CAR	Code of ethics	-0,196581	0,116047	0,0970*
Delta CAR	Traditional System	-0,957447	0,294817	0,0022***

Subsample composed by family business companies shows seven significant correlations, four of which with negative beta. Differently from the whole sample ROI seems to be affected, negatively, by the presence of executive directors (tab. 9).

Table 10. Relation between different drivers of Corporate Governance Index and Performance in non-family business (Delta before index name indicates the trend of the index in last six years)

Parameters	Corporate Governance driver	Beta	Standard Error	P-Value
Tobin Q	Board audit committees	0,546132	0,295181	0,0738*
Tobin Q	Non-executive directors	-0,197454	0,103201	0,0650*
Leverage	Nonvoting Stock	1,22048	0,680538	0,0827*
CAR	Board audit committees	10,9823	5,94454	0,0708*
Delta CAR	Code of ethics	0,0251763	0,0104901	0,0203**
Delta Z Score	Shareholders' agreements	2,92516	1,05114	0,0077***

Non-family business companies sub sample shows six significant correlations, one of which with negative beta. Considering this sub sample, ROI seems not to be affected by a corporate governance driver (tab. 10).

Table 11. Relation between different drivers of Corporate Governance Index and Performance in more active in M&A companies (Delta before index name indicates the trend of the index in last six years)

Parameters	Corporate Governance driver	Beta	Standard Error	P-Value
ROI	Auto Disciplinary Code	0,0754722	0,0354757	0,0460**
Tobin Q	Nonvoting Stock	0,135082	0,0703351	0,0692*
Tobin Q	Non-executive directors	-0,173214	0,0709145	0,0240**
Z Score	Auto Disciplinary Code	9,31618	3,85258	0,0253**
Z Score	Code of ethics	7,82869	4,01466	0,0653*
Leverage	Minority expressed Directors	1,08297	0,563582	0,0690*
Leverage	Nonvoting Stock	1,09867	0,526613	0,0500**
CAR	Board audit committees	-0,179935	0,0794669	0,0318**
Delta ROI	Shareholders' agreements	3,43056	1,48887	0,0291**
Delta ROI	Nonvoting Stock	-3,34444	1,66399	0,0545*
Delta ROI	Board audit committees	4,44928	1,84898	0,0232**
Delta Tobin Q	Code of ethics	3,75000	2,07814	0,0823*
Delta Tobin Q	Board audit committees	4,07246	1,89579	0,0408**
Delta Tobin Q	Non-executive directors	-3,25325	1,83822	0,0881*

Table 11. Relation between different drivers of Corporate Governance Index and Performance in more active in M&A companies (Delta before index name indicates the trend of the index in last six years) - continued

Parameters	Corporate Governance driver	Beta	Standard Error	P-Value
Delta Tobin Q	Nonvoting Stock	-3,39444	1,67320	0,0525*
Delta Z Score	Code of ethics	3,25000	1,88386	0,0959*
Delta Leverage	Executive directors	-1,76842	0,885866	0,0561*
Delta CAR	Shareholders' agreements	0,0233113	0,0132149	0,0890*
Delta CAR	Code of ethics	0,0402820	0,0170433	0,0256**

Sub samples composed of active companies in merging and acquisition activity seems to be the most affected by corporate governance drivers showing nineteen significant correlations, six of which with a

negative beta. It is interesting to highlight as same corporate governance drivers (e.g. presence of Auto Disciplinary Code) have effects on different performance\risk indexes (tab. 11).

Table 12. Relation between different drivers of Corporate Governance Index and Performance in less active in M&A companies (Delta before index name indicates the trend of the index in last six years)

Parameters	Corporate Governance driver	Beta	Standard Error	P-Value
Tobin Q	Shareholders' agreements	0,151405	0,0718986	0,0402**
Tobin Q	Code of ethics	0,162469	0,0868637	0,0672*
Z Score	Non-executive directors	25,0033	13,8506	0,0769*
Leverage	Non-executive directors	0,857166	0,458856	0,0675 *
CAR	Board audit committees	16,4651	5,57805	0,0044***
Delta Tobin Q	Code of ethics	-6,43421	3,82473	0,0972*
Delta Z Score	Shareholders' agreements	2,72052	1,33850	0,0461**
Delta CAR	Traditional System	-0,470149	0,184731	0,0132**
Delta CAR	Code of ethics	-0,149123	0,0836652	0,0792*
Delta CAR	Board audit committees	-0,303030	0,154782	0,0544*

The Last sub sample considered, is composed of companies who did few merging and acquisition procedures, showing ten significant correlations, four of which with a negative beta. The parameter that seems to be more affected by corporate governance drivers is delta CAR that is negatively correlated to three different corporate governance drivers Traditional System, Code of ethics, Board audit committees).

4 Discussion and conclusion

This paper is a first step in our work in progress. In fact, we aim to introduce a deeper analysis to test the gGI on other samples and in companies of other countries. In this direction, we can refine the Corporate Governance Index and test on other situations, such as Polish listed companies, that we are studying.

Our first results, however, could enlighten some interesting constructs.

Regarding the gGI we can observe that it can assume value between 4-13 and it presents an average value of 9.1 for the whole sample. Our companies could improve their Corporate Governance quality, especially in the sub sample of family businesses that detect a lower value (8.5), although in the index there

are drivers that specifically regard family firms (Executive Independent, CEO).

Moreover, we should point out that the non-family companies are better structured (9.8), demonstrating a greater minority protection and good opening to the outside.

The Corporate Governance quality presents some correlation with performance and risk parameters (Switzer and Wang, 2013). We can highlight a positive correlation of gGI values with Tobin Q (tab. 4), observed in a static analysis. For this reason we can observe that the Tobin Q is the only parameter able to capture a relationship, confirming its usefulness to detect market performance, as shown in literature (Gompers et al., 2003).

Looking at the sub-samples, only the companies less active in M&A present a positive correlation between a "good governum" and Tobin Q; while the more active firms have a negative relation with the performance, expressed by CAR. We can observe that the "well-advised" firms in external strategies are able to obtain a better correlation with performance.

Concerning the different contribution of Corporate Governance drivers, we can observe that Shareholders' Agreements and Board Audit Committee have an important correlation on performance. Shareholders' Agreements present a

positive relation on market performance (Tobin Q and CAR) for the whole sample (tab. 8) and for less active companies (Tobin Q-tab 12). Also on risk parameters Shareholders' Agreements show a correlation for the whole sample, for the companies less active in M&A and for non-family firms (tab. 10). We can observe that for these companies a better Corporate Governance is correlated with a lower probability of default. We can highlight that Shareholders' Agreements may represent an important minority instrument. The results show that the aforementioned agreements are more present especially in non-family companies, according to the part of literature that outlined that in more concentrated ownership the minority protection is lower (La Porta et al., 2000).

The variable "Non Executive Directors" presents a negative sign for the whole sample and for the non-family companies; it shows a good relation with Tobin Q for family firms in which Independent non executive directors are more present, demonstrating a particular attention to this important driver of Corporate Governance quality. Also on risk parameters the family businesses (tab. 9) present a positive relation with cGI level and Z-score, while less active in M&A companies show a positive relation with Z-score and leverage (tab. 12).

The companies, in which the Non Executive Directors are more present, demonstrate a greater openness to external subjects, with important management activities (Overhue and Cotter, 2010).

On the whole sample it is the Executive Directors presence that produces a very positive correlation with Z-score (tab. 8). Another important aspect is the role of the Code of Ethics, that explains the attention of the companies to stakeholders interests (in the broadest sense).

We can find that the more active companies in corporate acquisitions feel the need to draw up a Code of Ethics. The presence of the aforementioned Code is correlated with a lower probability of failure (Z-score) and with a positive sign for CAR. We can observe that a Code of Ethics can produce an improving in reputation, especially if we consider the investors and the other stakeholders (i.e.: Unions, employers), more important for the success of M&A operations. In fact, the Code of Ethics has become a tool for ensuring fair and efficient management of transactions and human relations, supporting the reputation of the enterprise, in order to create confidence. Creating a Code of Ethics can prove the good faith of the company, in cases of dispute, reducing the sanctions (Jensen, 2002).

According to Jensen and Meckling (1976), our analysis highlights that the non-family firms present a better gGI, showing a lower probability of default.

The classification adopted in this work for the identification of family businesses shows the presence of CEO "familiar" and family members on the board. In this connection, we can see that the presence of external managers, a future of non families sub sample, may guarantee a higher professionalization (Stewart and Hitt, 2012; Sciascia and Mazzola, 2008), with positive effects on performance and less risk of critical situations, especially in financial stability and working capital management.

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