Non-Technical Summary

Project no. RRC V-19:
"Corporate Governance, Minority Shareholders and Shares Prices on Emerging Capital Markets: the Case of Romania"

The final results of this research project have been comprised within three main studies, which are mentioned below:

- Dragotă, Victor, "Minority shareholders' protection in Romanian capital markets: evidence on dividends", published in *Euro-Mediterranean Economics and Finance Review*, January 2006, Vol. 1, No.1, pp. 76-89.
- Dragotă, Victor; Dumitrescu, Dalina; Ruxanda, Gheorghe; Ciobanu, Anamaria; Braşoveanu, Iulian; Stoian, Andreea; Lipară, Carmen, "Control premium for Romanian listed companies", submitted to Journal of Corporate Finance.
- Dragotă, Victor; Căruntu, Mihai; Stoian, Andreea, "Market informational efficiency and investors' rationality: some evidence on Romanian capital market".

The main results are presented below.

1. Minority shareholders' protection in Romanian capital markets: evidence on dividends

Recent studies in Finance suggest dividends' role as monitoring mechanisms, which allows minority shareholders to control the managers or larger shareholders' decisions. This paper tests this hypothesis on listed companies at Bucharest Stock Exchange, in 2000-2003 period, from the legislation perspective, but, also, using dividend ratios. Even the regulations and the enforcement of the law seem to guarantee an effective protection for minority shareholders, dividend policy is different from company to company, depending on shareholders structure. However, companies can fund their operations by banks, which could explain the relative indifference for minority shareholders proper treatment.

This paper concludes the dividend ratio for companies detained in more than 50% by minority shareholders are significantly greater than the dividend ratio for the other companies. The results seem to be in accordance with the hypothesis that the power of larger shareholders could be proven by low dividend ratios. One possible explanation could be, unfortunately, that larger shareholders could obtain benefits from other sources, more or less visible from outside.

This minor concerning on minority shareholders protection could cause difficulties for companies' financing decision because the new shares issues will become unattractive for them. However, even this fact creates great difficulties for companies which operate in Anglo-Saxon financial systems, is less visible in financial markets like Romanian one, where shares issues are not very important as financing mechanisms. The general accepted argument is that the low dividend ratios are a result of better growth opportunities after liberalisation: they may choose to distribute fewer dividends and invest more. Another explanation could be that a large investor might be rich enough that to prefer to maximise private benefits of control rather than wealth. On the other side, this reality implies a very slowly development for capital markets.

2. Control premium for Romanian listed companies

Control premium valuation is one of the main issues in Corporate Finance, strongly related to Corporate Governance principles and minority shareholders' protection.. Control premium for Romanian listed companies was estimated as the abnormal return at the moment of tender bid announcements. The median value for control premium is 44.62% and the mean value is 79.96%. There were, also, recorded 6 cases of negative control premium out of 44 observations (the sample spanned over 2002-2004). This particular evidence seems to be related to an informational asymmetry on the Romanian capital market. One explanation could be that operators simply do not know when a tender bid is launched. The large size of control premium could be an evidence for the lack of minority shareholders protection. However, it could be noticed that there are some anomalies which are very difficult to be explained in a rational behaviour hypothesis (in some cases, transactions are made at a price below tender bid price). For instance, the level for control premium reached a maximal level of 566.7%, which is obvious a case of over-valuation for offer price or an under-valuation case for price before this offer. This high level for control premium could, also, be explained by the general feeling the minority shareholders interests are not respected. For this reason, investors are interested to pay almost more half than shares prices in order to take control over the company (in this context, see, also, the maximum control premium – 567%). Another possible argument is the large difference between share prices and intrinsic values, which could be explained by a lack of informational efficiency or, more a lack of rationality for Romanian capital markets.

Concluding, the level of control premium for Romanian listed companies could be the result of two opposite causes. On the one hand, larger control premium could be the result of the lack of minority shareholders protection: investors are interested to take the control over companies because they know it is the only solution for defend their interests. On the other hand, smaller control premiums could be the result of a lack of information or of the lack of protection: how time minority shareholders are not protected, they have not the instruments to defend their rights. For this reason, they are disposed to accept very small control premiums (or, even, negative levels for them).

3. Market informational efficiency and investors' rationality: some evidence on Romanian capital market

Most of the studies concerning informational market efficiency focus on the fact that assets' returns follow a random walk and, as result, investors have no ability in predicting future returns, and, therefore, they could not obtain abnormal returns. This paper aimed in revealing the fact that even if econometric tests confirm the random walk hypothesis for some financial markets (e.g. emerging markets), this is not sufficient for capital markets to be informational efficient. The evidence on Romanian capital market shows there are large differences between market capitalisation and present market value of institutional investors' portfolios, and even though, empirical tests confirmed weak form on informational efficiency, this aspect could be rejected, and investors' rationality could be questioned. The methodology used in order to reveal the lack of informational efficiency of Romanian capital market is based on the fact that shares' price does not reflect available information.

This paper revealed that it is not necessary that a market is informational efficient only if prices follow a random walk. In other words, this is a necessary condition, but not a sufficient one. For example, on Romanian capital markets, some studies reveal a random walk evolution of prices. However, our study proved that there is a significant difference between price and an intrinsic value for some assets, which represents a major feature of Romanian capital markets, because that anomaly is persistent in time. Basically, the results of our study put in question investors' rationality on Romanian capital markets. It is not a paradox for emerging capital markets, how time Romanian capital markets history, even theoretically, has less by 10 years. Moreover, even if the econometric tests based on impossibility of obtaining abnormal systematic returns can not reject efficient market hypothesis, financial market could be inefficient due to the large difference between price paid and fair market value of shares.