Driving effective stewardship

Investor stewardship codes are becoming a feature of many jurisdictions across the world. Rita Benoy Bushon sets out the rationale – and the trials – of introducing Malaysia's first shareholder governance code.

Institutional investors are a major feature of many jurisdictions and are significant players in the global economy.

The publication of the UK and South African stewardship codes in 2010 and 2011, and similar stewardship codes in other jurisdictions thereafter, discussed the concept of institutional investor stewardship extensively – as well as its importance in the governance of listed companies.

The case for change in Malaysia

In Malaysia, it was recognised that ownership responsibilities among institutional investors can encourage best practices amongst corporates when properly instituted.

The Malaysian Corporate Governance Blueprint, published in 2011, provides a holistic view for reforms of corporate governance in Malaysia. It argues the case for more effective exercise of ownership rights by institutional investors.

The Blueprint acknowledged that responsible ownership requires high standards of transparency, probity and care on the part of the institutions. This may be met by adhering to a set of over-arching principles in the form of a code for institutional investors. The Blueprint highlighted the need for institutional investors to review their existing practices in light of the significance of their role, and heightened expectations to oversee their investee companies.

Thus, one of the recommendations of the Blueprint was the development of a code for institutional investors in Malaysia; this was realised in June 2014, when the Malaysian Code for Institutional Investors was launched.

The Code's principles

The Code defines stewardship as 'investor stewardship from the perspective of a long-term institutional investor'. It includes the responsible oversight of assets for the benefit of the institutional investors' ultimate beneficiaries or clients.

The core of the Code is a set of six principles intended to protect beneficiaries' interests.

The voluntary Code is directed at asset owners and asset managers with equity holdings in corporations listed on Bursa Malaysia. It exhorts institutional investors to become signatories and to engage in the following six principles:

1. Institutional investors should disclose the policies on their stewardship responsibilities.
2. Institutional investors should monitor their investee companies.
3. Institutional investors should engage with investee companies as appropriate.
4. Institutional investors should adopt a robust policy on managing conflicts of interest which should be publicly disclosed.
5. Institutional investors should incorporate corporate governance and sustainability considerations into the investment decision-making process.
6. Institutional investors should publish a voting policy.

The Code provides guidance on effective exercise of stewardship responsibilities under each principle towards the delivery of sustainable long-term value to the institutional investors' ultimate beneficiaries or clients. The Code also advocates the adoption of standards that go beyond the minimum prescribed by regulations.

Development of the Code

The development of the Code itself The Code's development was spearheaded by the independent Minority Shareholder Watchdog Group (MSWG), along with institutional investors, government and non-government retirement funds, and a number of other key stakeholders.

Expert and observer groups were also formed to provide input and expert opinion in the development of the code. These included representatives from ICGN, the UK Financial Reporting Council, PwC Malaysia, Governance for Owners, the Securities Commission Malaysia, Bursa Malaysia and the OECD.

The Code was benchmarked against the UK Stewardship Code, the ICGN Statement of Principles for Institutional Investor Responsibilities and the OECD guidelines. Further feedback was sought during a six-week consultation process in early 2014, which attracted valuable feedback from global governance organisations, industry players, institutions of higher learning and members of the public. The feedback was incorporated into the Code which was then modelled to fit the local scenario and level of readiness of the Malaysian investing industry.

"Adoption of the Stewardship Code among institutional investors in Malaysia is expected to take time."

Institutional investors are encouraged to be signatories to show their commitment to the Code and should explain how they have applied its principles, taking into account the guidance provided. Signatories are allowed to determine the best approach to adopting the principles, as it is acknowledged that there is no 'one size fits all' approach to stewardship. They are also encouraged to bring in their service providers where applicable to understand the principles of the Code.

Signatories of the Code are expected to report annually on their application of the principles of the Code in their website or annual report starting from year 2016.

Transparency is the cornerstone of the Code. One of the most important principles in the Code is that institutional investors should be transparent on voting policies. There have been many instances in the past where voting actions were not explained by institutional investors; coupled with the absence of transparent voting guidelines, this caused much confusion and distress among the boards of investee companies and minority shareholders.

Transparency on voting policies will also help to alleviate second-guessing by boards of the investee companies as to how institutional investors view company issues such as dividend distribution, diversity policies or even time commitment and re-election of directors.

Implementation and challenges

Adoption among institutional investors in Malaysia is expected to take time. Nine months after its launch, there were only six signatories to the Code.

Pushback against the Code included concerns about perceived additional cost and compliance burdens from a reporting perspective, while others requested an advocacy period to familiarise themselves with the Code's requirements. Some also claimed that differences in investment strategies and objectives posed challenges in adopting the Code.

Nevertheless, efforts are in the pipeline to encourage more signatories. The MSWG is leading this initiative, and is currently in the process of forming an umbrella body to represent the common interests of all institutional investors. We envisage this body will be a platform to shape and influence this wider sphere of corporate governance culture that can only come through an effective adoption of the Code.

This body will monitor the take-up and application of the Code, as well as promote understanding and adherence to the principles contained therein. It will also serve as a platform to discuss stewardship matters and corporate governance issues.

Conclusion

The potential benefits of the Code to the Malaysian investment industry is significant. Facilitating a collaborative relationship between shareholders and board members through active engagement, aligned to the company's best interests, will go a long way in unlocking value and consequently, long-term value creation of the company.

In addition, companies themselves will gain from having engaged shareholders, as these investors would be more likely understand their investee companies and carry out a more purposeful oversight – whilst at the same time reaping benefits in terms of sustainable long term performance from their investee companies.

About the author

Rita Benoy Bushon is the CEO of the Minority Shareholder Watchdog Group Malaysia. Prior to this, she served the Employees Provident Fund holding various senior positions in the investment division. She has also held board positions in several public listed companies.