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Theoretical Aspects and Methods of Evaluating the Economic Efficiency of Corporate Management in the Banking Sector of the Republic of Kazakhstan

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ABSTRACT
The aim of the work is to review the existing approaches of the economic efficiency valuation of the corporate governance in the banking sector and to develop on their basis the ways of improving the effectiveness of the corporate governance in credit organizations of the Republic of Kazakhstan. The authors describe the risk assessment method in corporate governance, methods based on the financial data analysis; present the features of two-factor and four-factor predictive models, etc. The study also found that the main aim of the corporate management in the banking sector of Kazakhstan is to increase the potential investor's confidence to the mechanisms of attracting investments. The practical value of the article is in presenting the promising directions of the corporate governance in Kazakhstan and in suggesting ways to improve the effectiveness of the corporate governance in the banking sector of the Republic, which may be acceptable to the other transition economies.

Introduction

Currently, the corporate management is the basis of the success of modern banks and of the entirely economy (Shpotov, 2000). In this regard, it becomes urgent to create an effective corporate management system, to achieve transparency of the operating structures and, as a result, to change of conditions for investment activity, with the following increase (Kalimullin, Youngblood & Khodyreva, 2016).

The unlimited opportunities of the corporatization led to the appearance of a plurality of integrated formations, which are using the new features and advantages of the corporate structures (Berger, Imbierowicz & Rauch, 2016). The

process of solving the corporate governance issues is coming to the fore and becomes the determining when the developed countries enter into the world economy in the conditions of proceeding global changes (Tricker, 2015).

It should be noted that the main purpose of the effective corporate management in the banking sector of the Republic of Kazakhstan (RK) is to increase the potential investor's confidence to the mechanisms of attracting investments and to enhance on this basis the capitalization of the entirely Kazakhstan economy (Haan & Vlahu, 2016; Macey & O'hara, 2003).

The level of the corporate governance is one of the processes, which directly determines the status of Republic in the world community, as it determines the Bank governance at the level of their integration (Estrin, 2002). The high rate of development of the corporate governance has being observed in Kazakhstan since 2002 (Choybecova, 2007). You could even say a certain experience on management and development of the corporations in market conditions has accumulated, based on international practice; has been developed a complex of the policy papers to bring the strategic directions of development of the corporate sector into the reality (Bank risks, 2007).

Following the adoption of the Corporate Governance Code in October 2006 by the Issuer Board (Yusupov, 2006) there was conducted the first study of the corporate governance condition in Kazakhstan, which shows that:

1. The corporate governance is principally accepted, but not uniformly in practice. While the companies, registered in KSE (Kazakhstan Stock Exchange), have the Corporate Governance Code, created on the model recommended by the KSE, the quality and the level of the operational detailed elaboration and efficiency vary in different organizations.

2. The organizations with the most advanced standards and practices of the corporate governance are larger structures (in terms of assets and number of employees), which shares are quoted on the stock exchange. These organizations are represented mainly by the financial services sector.

3. The company's current practice has significant drawbacks. Particularly noticeable drawback is the procedures inadequacy for disputes arising between the Board of Directors and the governing body; or the ensuring of an adequate protection of shareholders' rights, who do not own any controlling stake; and establishing of Committees of Board of Directors.

4. In many cases, companies solving the problematic issues in the absence of coherence in making decisions rely on informal procedures.

5. The effective implementation is also complicated by the lack of knowledge and experience on the practical introduction of the corporate governance standards.

6. The lack of the independent directors or their small number makes the transition to international standards more difficult (Kashyk, 2009).

We note that based on the place, role and importance of the corporate governance in people and state life, the corporate governance is a system, an effective tool for the formation and regulation of economic and social relations in

the process of production and distribution of public goods (Milvidov, 2007). So many subjects of these relationships are interested in its strengthening and development at the same time: the owners, managers, staff, suppliers of equipment and raw materials, customers, investors and lenders, banks, insurance companies, state, regional and local authorities (Beyakov, 2008).

From the position of the sources of funds for doing business in the corporate governance is necessary, first of all, to identify the following stakeholders with different abilities to impact on commercial bank management, and also pursuing different goals: the majority shareholders; minority shareholders; major lenders; small creditors; regulatory authorities (Yanivskaya & Nikifiriva, 2005).

The scientists say the market competition is an effective lever of influence on management - it encourages the companies to minimize their costs and to improve the corporate governance mechanism in order to find the cheap external funding sources (Janakiraman & Radhakrishnan, 2015; Chang et al., 2015). At the same time, some experts insist on that the market competition is unlikely to solve the problems of the corporate governance independently (Qian & Yeung, 2015).

Another form of manifestation of the competition – the possibility of the absorption by another company, and this factor in the economic life is conducive to the proper development of the corporate governance (Krinichansky, 2007). A company with poor management may receive an offer to sale their business and shareholders dissatisfied with the existing control condition, may take a decision to sale the company (Schwert, 1996; Berger et al., 1998). In this case, the new owner of the company is likely to replace the management measures (which often happens in practice). Thus, the M&A market stimulates the managers to act in the interests of shareholders, in order to avoid the dismissal in the case of the owner change (Lebedev et al., 2015).

We can summarize that the corporate governance issues are crucial for the Kazakhstan banks and companies, interested in attracting new shareholders. Good corporate governance reduces the investor's risk and may increase the shareholder value of companies (Yanivskaya & Nikifiriva, 2005).

Moreover, further transnational activities of Kazakhstan corporations and banks (with the usage of the joint enterprise mechanisms of the financial-industrial groups and multinational banks, their branches and subsidiaries abroad) is impossible without proper and adequate proceeding corporate governance (OECD Principles Corporate Governance, 2004).

Methods

In this work, we used the method of the theoretical research analysis of the corporate governance efficiency valuation.

The first stage of the study was the distribution of existing valuation methods for qualitative and quantitative. The second step involves the comparing results of model calculations by E. Altman (1968) and features of the four-factor predictive model by R. Taffler (1977).

The final stage of the work was to develop ways of improving the corporate governance effectiveness in credit organizations of the Republic of Kazakhstan.

It should be noted, that in the description of methods of the corporate management economic efficiency valuation in the banking sector, the authors have presented a typical model for the analysis of companies, which shares are quoted on the stock exchanges, have described the formula calculating the possibility of bankruptcy.

The method of the corporate governance risk assessment, developed by Brunswick UBS Warburg, was divided into categories and presented in a tabular form.

Data, Analysis, and Results

First, we can note the presence of a variety of methods of the corporate governance effectiveness valuation in the banking sector (Figure 1).
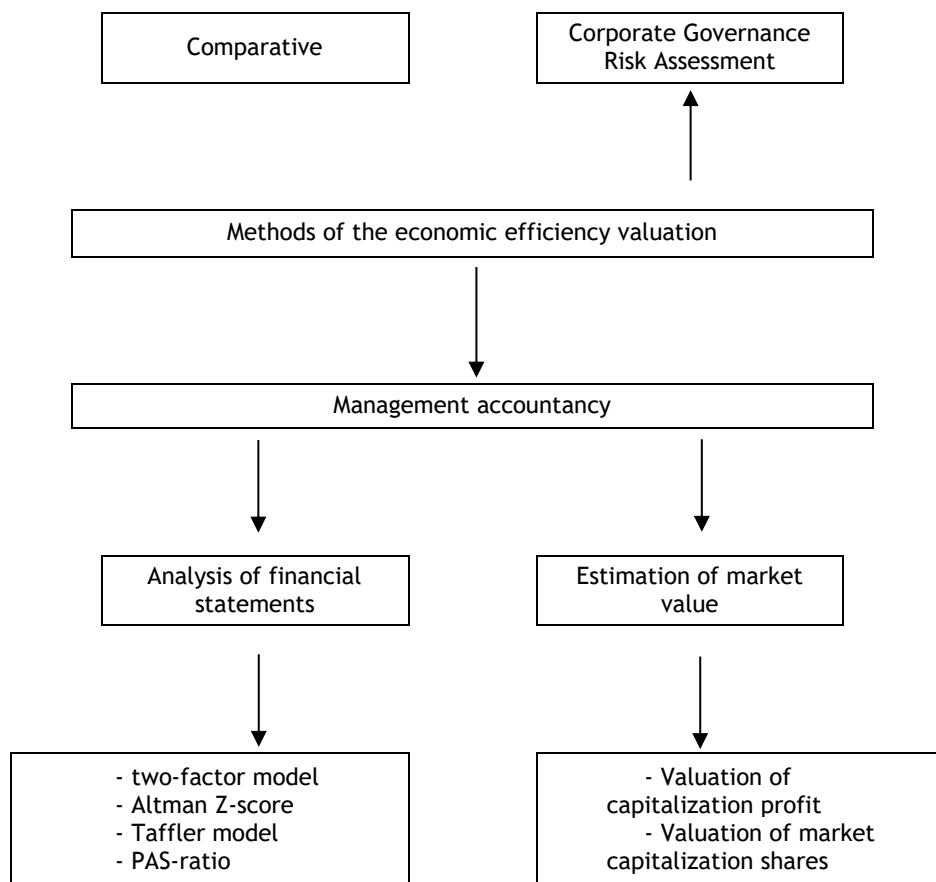

Figure 1. Methods of the economic efficiency valuation.

Among them can be distinguish the qualitative and quantitative evaluation methods. In the group of high-quality techniques, we wanted to stay at the two of them, which are close in usage in today's market conditions. These are the Comparative method and the method of Corporate Governance Risk Assessment.

The quantitative methodology of the corporate governance efficiency is based on the analysis of economic activities of the corporation. And this group of methods

is also subdivided into two sets: methods of evaluating the financial condition and methods for estimation the market value.

Investors are wary of investing in Kazakh banks and companies, fearing the infringements of their rights by the Bank or company managements. In this regard, the establishment of an effective corporate governance system is one of the self-contradictory tasks.

Let us proceed to the consideration of these techniques.

The Comparative method of corporate governance efficiency valuation is to compare its mechanisms in different conditions of the managing the corporation (as a rule, the geographic distribution of the countries). This tactic is formalized and allows you to compare the conditions of the corporate governance in different countries. In such a case, is used an expert evaluation of development of the countries legislation of the corporate governance, the degree of its implementation, the development of the stock market (compared to the capitalization), the bankruptcy mechanism (compared to the degree of the bankruptcy proceedings simplicity and its frequency usage). It is known to be the outside mechanisms valuation of the corporate governance.

 In the internal mechanisms valuation, is evaluated the activity of the Board of Directors (the correlation of the internal and external directors, the number of the Board, the method of the manager's activity by the Board of Directors and other indicators, depending on the activity specifics of the Board of Directors in a certain country and the goal evaluation). The construction of the remuneration system of managers is also evaluated (the degree of the rapprochement between the manager's and owner's interests depending on the payment system).

A more exact look at the problem of the corporate governance efficiency valuation is reflected in the unlike tactic. The uniting link of these techniques is the understanding that the effective financial and economic activity of the corporation is the one confirmation of the corporate governance effectiveness you need. This tactic is implemented in the following basic methods. The first – is the estimation of the market value of the corporation, and the second - the estimation of the financial condition of the corporation, the key point of which is to calculate the possibility of bankruptcy. Recent methods have a certain relevance in Kazakhstan conditions.

Among the methods of valuation of the possibility of bankruptcy, is normal to distinguish the methods based on the financial data analysis, including the operation with rates: gaining popularity Altman Z-score (USA), the Taffler model (UK) and others, as well as the ability to "read a balance sheet." The methods for the data comparison on the bankrupt companies with the data of the relevant company.

Methods based on the analysis of financial statements are currently the most common. Although, according to the researchers, there are objective disadvantages of these techniques. Firstly, the companies, which are having trouble, delay the publication of its reports in every way, and thus, the certain data can be unavailable for years (Estrin, 2002). Secondly, even if the data is communicated they can be "creatively processed". In such circumstances, the

desire to whitewash the activities is inherent for the companies, which sometimes even falsify data. It takes a special skill to isolate the groups of edit data and to assess the degree of the falsification. A third difficulty is that some relationships, derived according to the company's activity data, may indicate the insolvency at the time, when the other ones – may provide conclusions about the stability or even a small improvement. In such conditions, it is difficult to judge about the real businesses situation (Lebedev et al., 2015). However, we could agree with the third statement only in condition of the static valuation instead of the dynamic. Speaking about the first two objections, we should note that the study of the requirements for the information disclosure on the corporate activities, undertaken in various countries, allows us to make a conclusion about the insolvency of these objections, since the requirements disclosure include an amount of important elements. This and the reporting on a quarterly basis (in the US and in the Republic of Kazakhstan), or every six months (in Germany) eliminates the possibility for corporations to delay the reporting. This and the mandatory audit of the financial statements what significantly reduces the risk of falsification (Lebedev, Yanivskaya & Nikifiriva, 2005; OECD Principles Corporate Governance, 2004).

One of the simplest models of predicting the possibility of bankruptcy is the two-factor model. It is based on the two main indicators (such as the current liquidity and an indicator of leverage), that determine the possibility of bankruptcy. These figures are multiplied by the weighting coefficient values, found empirically, and then the results are combined with a constant (const), which was received the same way (experimental statistics). If the result (C1) is negative, the possibility of bankruptcy is low. A positive value of C1 indicates a high possibility of bankruptcy.

In American practice are identified and used such weighting factor values:
- For the current liquidness ratio (coverage) (R) – (-1.0736);
- For the leverage ratio in the liabilities enterprises (Ks) – (0.0579);
- Constant – (-0.3877).

Hence, the C1 calculating formula takes the following form:

$$C1 = -0.3877 + R * (- 1.0736) * 0.0579 + Ks \qquad (1)$$

The considered two-factor model does not provide of the full financial condition valuation of the enterprise, and therefore there may be too large deviations of the forecast from reality. To get a more accurate forecast the US practice recommends taking into account the level and trend of the profitability of sold products, as this figure significantly affect the company's financial stability. It allows you to compare the rate of bankruptcy risk (C1) and the level of sale profitability. If the first parameter is in safe limits and the level of production profitability is relatively high, the possibility of bankruptcy is very small.

Well-known Western economist Edward I. Altman proposed another quantitative method in 1968. The credit index is constructed using a multiplicative apparatus of discriminant analysis (Multiple-discriminant analysis

- MDA) and allows to divide the economic objects on the potential bankrupt and not bankrupt (Altman, 1968).

In the index formation, Altman examined 66 companies, half of which went bankrupt in the period between 1946 and 1965 and the other half worked well; and examined 22 analytical factors that could be useful for the prediction of possible bankruptcy. From these figures, he selected five of the most significant and built a multiple regression equation. Thus, Altman index is a function of several parameters, describing the economic potential of the company, and the results of his work during this period. In general, the credit index (Z - score) has the following form:

$$Z = 1.2X1 + 1.4X2 + 3.3X3 + 0.6X4 + X5 \qquad (2)$$

Where:

X1 - working capital / total assets;

X2 - retained profit / total assets;

X3 - operating profit / total assets;

X4 - the stock value / debt;

X5 - revenues / total assets.

The results of the calculations on a Altman model showed that general indicator Z can take values in the range of [-14, 22], and the enterprises, for which Z> 2.99, fall into the number of financially stable, but the enterprises, for which Z <1,81, are certainly untenable. The interval [1.81 - 2.99] has to be a zone of uncertainty.

Z-score is a common serious disadvantage: it can be used only in the case of large companies of which shares are quoted on the stock exchanges. For these companies, you can get an objective market valuation of the equity.

In 1983, Altman modified his formula for the companies, which shares are not quoted on the stock exchange:

$$K = 8,38X1 + X2 + 0.054X3 + 0.63X4 \qquad (3)$$

(X4 - the carrying value of the shares).

Altman ratio is one of the most common.

There are other similar criteria. Thus, in 1977 the British scientist R. Taffler proposed a four-factor forecast model, the development of which he used the following tactic:

Using the computer equipment on the first stage, are calculated 80 correlations according to the insolvent and the solvent companies. Then, using a statistical method, known as multivariate discriminant analysis, it is possible to create a model of solvency, identifying the particular ratios that are well distinguished by the two groups of companies and their coefficients (Taffler, 1977). Such a selective ratio counting is typical for the determination of some of the main measurements of the corporate activities, such as profitability, compliance with the working capital, financial risk and liquidity. Combining these indicators and bringing them together appropriately, the solvency model produces an accurate picture of the corporation's financial condition. A typical model of analysis of the

companies, which shares are quoted on the stock exchanges, takes the following form:

$$Z = C0 + C1X1 + C2X2 + C3X3 + C4X4 + ... \qquad (4)$$

Where:

x1 = pretax profit / current liabilities (53%);

x2 = current assets / total liabilities (13%);

x3 = current liabilities / total assets (18%);

x4 = the lack of credit range (16%);

c0, ..., c4 - ratios, the percentages in parentheses indicate the proportions of the model; x1 measures the profitability, x2 – the condition of the working capital, x3 – financial risk and x4 – the liquidity.

To enhance the predictive role of models the Z-score can be transformed into the PAS-ratio (Perfomans Analysys Score), tracking the company activities over time. Studying PAS-ratio (above and below the critical level), it is easy to determine the moments of company's demise and revival.

The PAS-ratio is just the relative level of the company's activity, based on its Z-score in a certain year and expressed as a percentage from 1 to 100. For example, the PAS-ratio of 50 indicates that the company's activity is acceptable, and then a PAS-ratio of 10 indicates that only 10% of companies are in the worst position (inacceptable situation). Thus, counting the company's Z-score, you can translate the absolute measure of financial position into a relative measure of financial performance. In other words, if the Z-score indicate that the company is in a dangerous position, the PAS-ratio reflects the historical tendency and the current activities in perspective.

The forte of this tactic is its ability to combine the main features of the income statement and balance sheet into a single representative ratio. That is why the company with large profits, but weak in balance terms, can be compared with the less profitable, which balance is stable. Thus, calculating the PAS-ratio, you can quickly valuate the financial risks, associated with the certain company to vary the terms of the transaction. In essence, the tactic based on the principle that the single unit is more valuable than the sum of its parts.

An extra feature of this tactic is to use a "risk rating" to identify the further hidden risks. This rating is determined only statistically, if a company has a negative Z-score, calculated because of the tendency of Z-score, the negative Z-score value and the number of years, during which the company was in a dangerous financial position. Using a five-point scale, where 1 indicates "the risk, but little possibility of immediate disaster" and 5 means "the absolute impossibility of preserving the last condition", the manager operates with ready means of the overall risk balance valuation, connected with the customer's credits (Choybecova, 2007).

The existing tactics of the management effectiveness valuation in terms of the market value of the corporation include various techniques. Among the main, one determines the market value, based on the valuation of the capitalization of the corporation income, and the other based on the share prices of the corporation.

In the first line, the enterprise value (V) is determined by the capitalization of profit:

$$V = P / K \quad (5)$$

Where:

P – Expected profit before taxes and the percent on credits and dividends;

K – Weighted average cost of liabilities (liabilities) of the company (the average percentage, showing the percent and dividends, which must be paid in accordance to the prevailing market conditions for debt and equity).

Reducing the price of the enterprise means a reduction in its profitability or increase in the average cost of liabilities (requirements of the banks, shareholders, depositors and other investor's requirements). The forecast of expected decline requires an analysis of the profitability prospects and percent rates.

It is wise to calculate the company price in the short and long term. The terms of the company's falling prices are usually formed currently and could be foreseen in a certain degree (but there is always some place for unpredictable shock waves in the economy).

Methods of the corporate governance risks assessment is designed by Brunswick UBS Warburg.

At the same time a variety of actual and potential risks, connected with the corporate governance, are divided into eight categories and 20 subcategories, each of which correspond to a clearly defined risk ratio and indication of its usage.

The awarding of drawback points produces the valuation of each risk types. Accordingly, the higher is the corporation rating with its scored points, the greater is the risk degree and, consequently, the lower is the level of the corporate governance. The awarding of drawback points by categories has the following feature (Table 1).

According to the model, the corporations, which receive more than 35 drawback points, are in the extreme danger and therefore can be characterized by a low level of the corporate governance, but companies with a rating, which is lower than 17, are considered to be relatively safe, with a high level of management.

Table 1. Methods of the corporate governance risk assessment.

Category name	Max. rate
Transparency lack	14
- Financial Statements US GAAP / IAS (US / IFRS National standard)	6
- Transparency reputation	4
- ADR (Depositary provides services to depository receipts program)	2
- Notification of the shareholder's annual / extraordinary general meetings	2
Dilution of shareholding	13
- Declared but not issued shares	7
- The blocking stake of portfolio investors	3
- The presence of the protective measures in the charter	3
Dissipation of assets / transfer pricing	10
- Shareholders with a controlling stake	5
- Transfer pricing	5
Merger / restructuring	10
- Merger	5
- Restructuring	5
Bankruptcy	12
- Overdue accounts payable or problems with the arrears in settlements with the budget	5
- Debts	5
- Financial management	2
Limits on buying and holding of shares	3
The restriction on ownership of shares by foreigners, or on their part in the vote	3
Corporate Governance Initiatives	9
Membership of the Board of Directors	3
Corporate Governance Code	2
Presence of a foreign strategic partner	1
The Dividend policy	3
Registry holder	1
Quality	1
Total	**72**

Discussions

It is worth noting that scientists take different lines in the definition of the concepts of the corporate governance, disclosure of its value in the market conditions. As an example, M. Al Masum & L. Parker (2013) emphasize the most characteristic features, inherent to certain models of the corporate governance. A. Radygin, R. Entov & J. Mezheraups (2003) associated the concept of the corporate governance with its applying only in the shareholder structure, where is clearly seen the separation of the owner's interests and the management functions.

In the study, we have determined that the M&A market encourages managers to act in the interests of shareholders. However, the other works show that the manager's resistance and the presence of the illiquid stock market often delay the action of the M&A market (Tagiyeva & Paruhina, 2008). The exception,

perhaps, here are the US and the UK, where the stock market is more developed and sustained (Finance, Monetary Circulation, 2009).

It is established that for the companies from developed countries the corporate governance is particularly important, as international investors especially fear for the honesty and the business qualities of their management (Estrin, 2002).

As the international experience, the capitalization of companies with good corporate governance is significantly higher than the average on the market. Especially great difference is for the Arab countries, Latin America (except Chile), Turkey, Russia, Malaysia and Indonesia (Lebedev et al., 2015).

Conclusion

As a result, considered methodology of the corporate governance efficiency valuation submit a different tactic in studding the problem. Firstly, this is because, the corporate governance is a multi-faceted category and researchers in the efficiency valuation may have different purposes, which require the use of different techniques; Secondly, the presence of a technique variety shows that none of them is not a panacea for all the problems of the corporate governance.

The corporate governance is becoming important due to several factors:
- The active searching of opportunities to attract the foreign capital and investors to finance the future development;
- The increased interest in M&A between the Kazakhstani companies;
- The interest of the Kazakh business in achievements on foreign markets and, hence, the activity in a relatively unstable and uncertain business environment;
- The growing interest of the Kazakh companies to participate in the leading foreign stock exchanges, with high standards of the CG – LSE (London Stock Exchange), NYSE (New York Stock Exchange), TSE (Turkish Stock Exchange);
- The understanding that improving corporate standards affect the current ratings and increase the investor's confidence, in particular, the timely disclosure of financial information;
- The CG raising standards can facilitate the absorption of the local companies by foreign investors in the international market.

We can also conclude that the corporate governance needs improving, as it:
- Increases the investment attractiveness of the company;
- Helps to attract long-term investors;
- Reduses the cost of credit;
- Increases the market value of the company.

To improve the corporate governance effectiveness in Kazakhstan credit organizations, is necessary to carry out the following measures:

- The vertical integration;
- The quality and accuracy of the information disclosure (transparency);
- The creation of the independent s/c Boards of Directors;
- Appointment of professional managers;
- The corporate ethics and culture, respect for its principles by the top-managers;
- Audit and control;
- Risk assessment and management;
- The combat with corruption;
- The competition in the internal and external markets.

It is expected that in the near future the corporate governance in Kazakhstan will be developed in the following directions:

- Improving the protection of the shareholder's rights and interests and the ensuring of their equal rights;
- The improvement of the information disclosure system and ensure transparency of the company;
- The separation of powers between the company's management bodies;
- Consideration for the stakeholder's rightful interests (employees, management, creditors, etc.);
- The formation and development of an advanced, proven its civilized corporate governance culture.

Disclosure statement

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