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Revision of the White Paper

(II) Developing Shareholder Engagement and Responsibility

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The views expressed in this paper are those of the author and do not necessarily represent the opinions of the OECD or its Member countries or the World Bank

White Paper on Corporate Governance in Asia 2003

- Priorities for Reform (relevant parts)
  - Priority 1: Public- and private-sector institutions should continue to raise awareness among companies, directors, shareholders and other interested parties of the value of good corporate governance
  - Priority 2: All jurisdictions should strive for effective implementation and enforcement of corporate-governance laws and regulations
  - (New) Priority 5B: Shareholder engagement should be encouraged and facilitated, in particular by institutional investors. Depending on their organization, institutional investors should be encouraged to accept their responsibilities toward portfolio companies by participating effectively at shareholder meetings. The exercise of voting rights should be facilitated and costs reduced.

＞Shareholder Engagement
[Case] Korea Corporate Governance Fund ("KCGF")

- Korea Corporate Governance Fund ("KCGF")
  - Nickname "Hasung Jang's Fund"
  - Successfully launched on April of 2006 with initial capital of approx. US$ 25 million (later grew to approx. US $ 50 million)
  - Key Players
    - Fund management: Lazard Asset Management
    - Adivisor: Professor Hasung Jang
    - CG Advisor: CGCG (Center for Good Corporate Governance)
  - First and the only "Activist Fund" in Korea (even today)
  - Objective of KCGF: ***Identify undervalued companies and realize profits through improving CG***

> Shareholder Engagement: [Case] "KCGF" (cont'd)

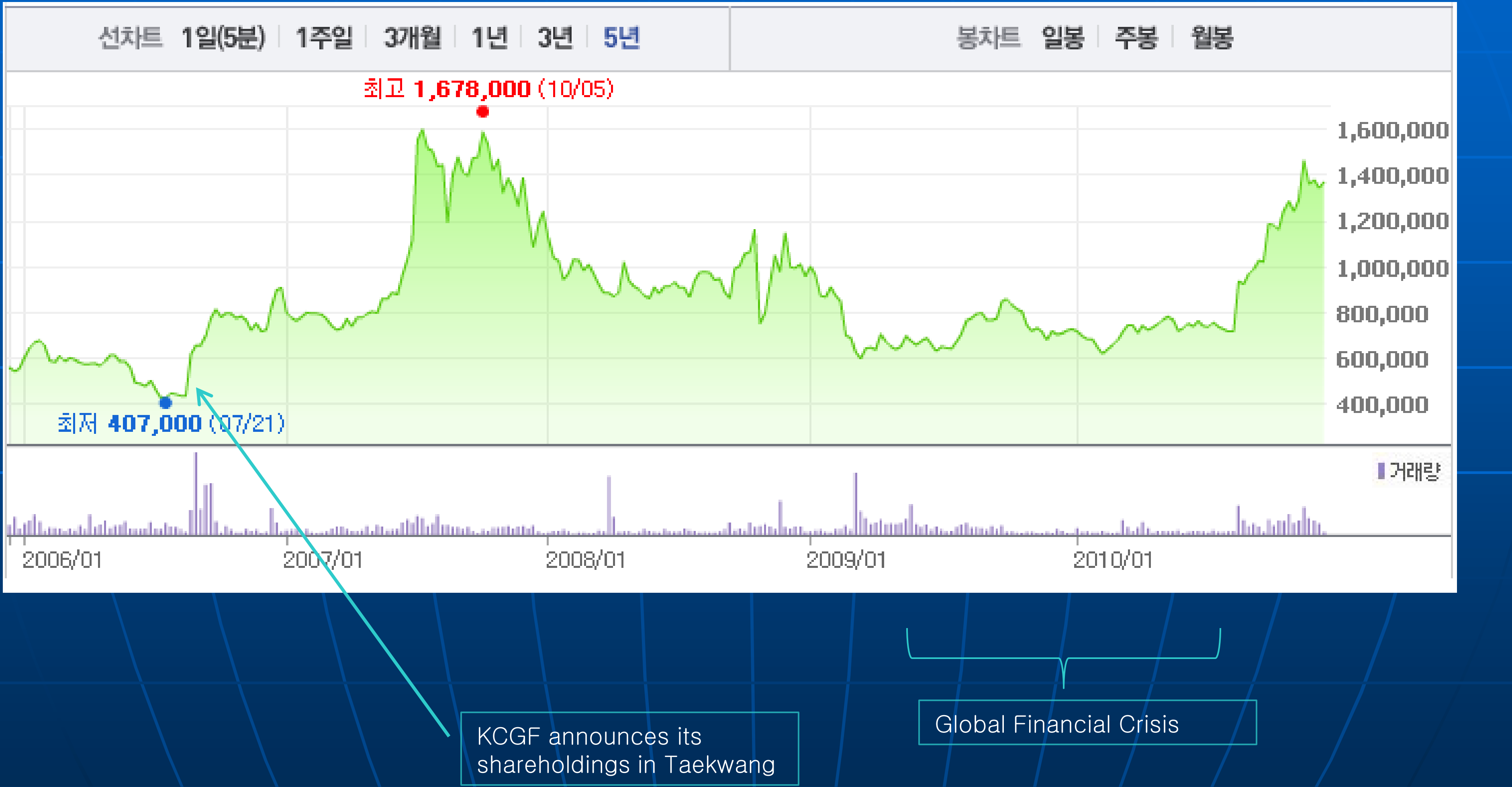
- Tactics
  - Target companies: mid and small cap stocks
    - 15 ~20 investee companies
  - Buy <u>legally</u> meaningful shares of the company (>3%)
    - Why 3%?
      - Korean law requires ownership of at least 3% to exercise certain shareholders' rights
      - Needed to show "commitment" to the market
  - After investment, the team would initiate full-fledged dialogue with the company's management suggesting implementation of CG best practices
  - Vowed to be "Long-term Investor" (at least 3~5 years)
  - Recommend independent director(s) or auditors
  - Required structural improvement (systematic approach)
  - Unwinding past irregular transactions by the controlling shareholder
  - Engage in proxy contest
  - Initiate civil actions (derivative suit) if needed

> Shareholder Engagement: [Case] "KCGF" (cont'd)

- Impact to the market
  - First investee disclosed – Taekwang Industries (TK)
  - Stock price of TK: KRW 400,000/share (7/21)
  - After KCGF's disclosure: soared to KRW 1,678,000 (10/5)
  - Six consecutive days of "daily-high (limit) of 14.99%" (still holds the record)
  - When the negotiation broke down → stock price went down to KRW 600,000
  - Currently, it is traded around KRW 1,400,000 and the battle goes on against the management
  - After the successful story with TK, Corporate Governance Fund became one of the major "themes" of the market

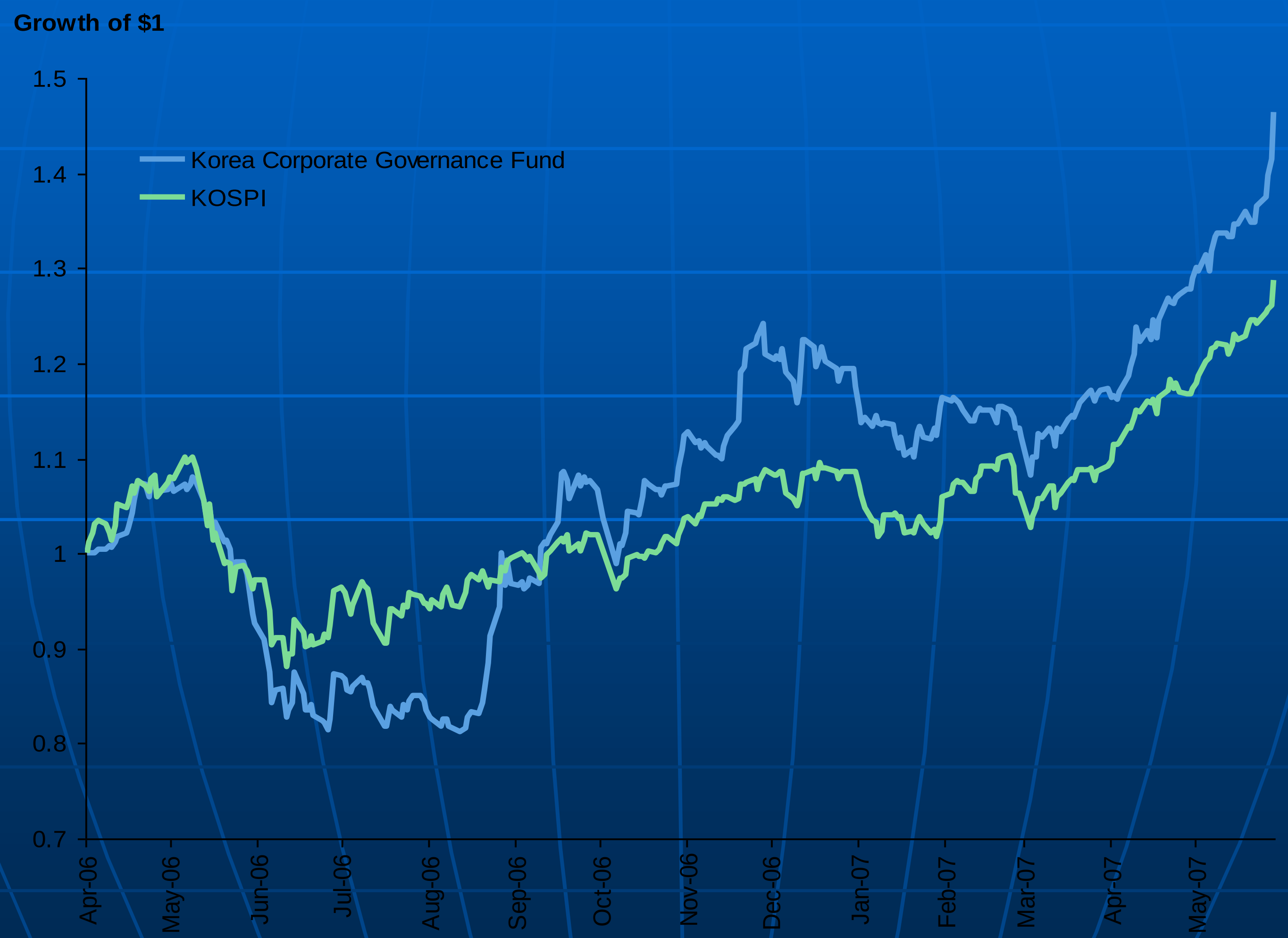
> Shareholder Engagement: [Case] "KCGF" (cont'd)

- Movement of Taekwang's Stock Price



> Shareholder Engagement: [Case] “KCGF” (cont’d)

- KCGF Performance (until 2007)



> Shareholder Engagement: [Case] "KCGF" (cont'd)

- Obstacles
  - The company often does not realize "win-win" situation
  - Strong resistance ("How dare you intervene with my company's affair")
  - Lack of understanding by the public, market, government and even the media
    - Media coverage depicting as "hedge funds" "foreign invasion" "short-term players"
  - Free-rider problem
  - Lack of good "exit" plan → difficult to cash-out
  - Courts were not friendly to "active shareholders"
  - In 2008, global financial crisis hit the market
    - → Companies with bad CG were hit harder than those with good CG

> Shareholder Engagement: [Case] "KCGF" (cont'd)

- Lessons from KCGF
  - Need to communicate with the management and market more effectively
  - Need to set up a good "exit" plan
  - Company, market and public still do not understand "CG Best Practices"
  - Still on-going experiment
  - It is yet too early to assess whether this experiment was successful or a failure

- More obstacles in the future
  - "Poison Pill" will be adopted in Korea
  - Lack of "discovery" in the civil proceedings
  - Lee Administration: "CG is not a priority (CG Watch 2010)"

Thank you