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Modern corporate governance is influenced more by political atmosphere and economic conditions than by law

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ABSTRACT
In the context of the global business environment, this article explores the impact of political, economic, and legal factors on corporate governance. It argues that political factors, including regulations, government intervention, and political system differences, significantly influence corporate governance, both positively and negatively. Economic conditions, such as growth or recession, and global economic integration, also shape corporate decision - making and governance practices. Although law provides a fundamental framework for corporate governance, its effectiveness is subject to political and economic influences. In conclusion, political and economic factors have a broader impact on corporate governance than legal elements. Company managers should consider the integration of these three factors based on specific regional contexts to achieve effective corporate governance.

KEYWORDS
Corporate governance; Government regulations; Global economic integration; Economic conditions

1 Introduction

In today's global business environment, corporate governance has become a critical element of organisational success[1] Corporate governance encompasses a range of management and supervisory principles aimed at ensuring effective operation of the enterprise while protecting the interests of all stakeholders.[2] With the continued development and increasing complexity of global business relationships, a profound understanding of corporate governance has become crucial.

Corporate governance is not merely an organisational structure but rather a complex system of rights and responsibilities allocation. According to Roe, corporate governance is defined as "the process of ensuring that corporate decisions are made in a manner that maximises shareholder value and strategically plans for the sustainable success of the company."[3] This definition emphasises the direct relationship between corporate governance and shareholder interests, highlighting its pivotal role in safeguarding shareholder rights and enhancing company value.

As the global economy evolves, the concept of corporate governance has undergone continuous change. Shleifer and Vishny pointed out that the evolution of corporate governance is an adaptation to economic and market conditions to ensure companies maintain competitiveness in the fiercely competitive environment. [4] This reflects the inherent connection between corporate governance and the economic environment.

This article provides an analysis of the intricate interplay between politics, economics, and corporate governance, aiming to enhance our understanding of the impact of corporate governance. By delving into these, people can gain a more holistic understanding of how various political and economic factors shape and influence the corporate governance mechanisms.

2 The impact of politics on corporate governance

In any country or region, the influence of political factors is significant. This article asserts that the impact of political factors on corporate governance is primarily manifested in the realm of regulation. Political decisions and administrative resolutions have far-reaching effects on the formulation and implementation of corporate regulations. [5] As Santos contends, governmental legislation and regulatory agency provisions directly impact a company's operational activities and governance structure. [6] Governments may regulate corporate behaviour by enacting new laws and regulations, including requirements for disclosure, protection of shareholder rights, and composition of the board of directors. For instance, in the United States, the Sarbanes-Oxley Act of 2002 (Public Company Accounting Reform and Investor Protection Act of 2002) represented a major reform in corporate governance, mandating public companies to enhance internal controls and financial disclosures to increase transparency and safeguard investor interests. [7] It exemplifies the significant influence of political factors on corporate governance, where changes in the political environment may lead to the formulation and revision of corporate governance regulations, thereby exerting a profound impact on corporate governance. Moreover, governmental intervention also directly affects corporate governance. [8] Governments may influence corporate decision-making through incentive measures, tax policies, or subsidies. For example, the Chinese government's "13th Five-Year Plan" includes policies supporting the new energy vehicle industry, such as subsidies and tax incentives for new energy vehicle enterprises, directly impacting their decisions in technological development and market expansion.[9]

Political factors can also have an impact on corporate governance in other aspects, improper political intervention and existing corrupt practices can lead to corruption in corporate governance and loss of public trust.[10] Political factors can contribute to the existence of unfair and non-compliant behaviour. Research shows that corrupt practices by political officials have a negative impact on corporate governance, this negative impact can lead to non-compliance and corruption, which may put the company in ethical and legal dilemmas.[11] In her 2010 article, Duchin highlighted the negative consequences of inappropriate political intervention in undermining the fairness of a company's decision-making process and diminishing the influence of independent directors, ultimately impairing the overall effectiveness of corporate governance.[12] Additionally, unethical practices and corrupt behavior can trigger societal skepticism and public condemnation towards the company, resulting in detrimental effects on its business reputation and eroding public trust.[13]

Apart from domestic politics, corporate governance in the era of globalization is profoundly influenced by multifaceted factors, including international trade conflicts and shifts in diplomatic policies.[14] These external dynamics cast a significant impact on the functioning and effectiveness of corporate governance mechanisms in a globalized setting. The most common one is international trade disputes, with the increasing interdependence of the global economy, international trade disputes have become more prominent.[15] When there are conflicts in trade behaviour between countries, it may have far-reaching implications for corporate governance, especially for companies involved in international trade. These factors require companies to adjust their governance mechanisms to adapt to the constantly changing environment. Furthermore, alterations in diplomatic policies, political tensions, and the implementation of trade sanctions are additional factors that can exert a significant influence on the intricacies of corporate governance.[16] These external circumstances possess the potential to shape and mold the effectiveness and dynamics within the realm of corporate governance.

Lastly, the differences in political systems among countries and regions have a significant impact on corporate governance and result in variations in corporate governance practices.[17] In democratic political systems, corporate governance tends to focus more on shareholder rights protection and democratic participation. On the other hand, in centralised political systems, the government has a more direct influence on corporate decision-making and governance.[18]

In a democratic political system, corporate governance places greater emphasis on protecting shareholder rights and democratic participation. It highlights fair and transparent decision-making processes, safeguards shareholder rights, and prevents conflicts of interest.[19] Furthermore, according to Lele's research, shareholder protection has been improving over the past thirty years.[20] Correspondingly, corporate governance under this political system tends to prioritise external supervision and internal controls.

Under a centralised political system, corporate governance may be more influenced by government intervention and guidance in corporate decision-making and governance. The government's direct intervention and guidance aim to achieve national interests and policy objectives. Therefore, compared to the interests of private shareholders, the government's interests and priorities have a greater influence on corporate governance.[21]

While corporate governance practices may vary across political systems, this article contends that the key determinant of success lies in the commitment to ensuring fairness, transparency, and effectiveness. The article argues that no method can be deemed universally superior or inferior in an absolute sense, as the suitability of specific approaches should be contingent upon the unique circumstances and contextual factors at play.

3 The impact of economic factors on corporate governance

Analysing the impact of the economy on corporate governance is a critical aspect. Economic conditions play a significant role in shaping the decision-making processes and governance practices within organisations.[22] In this section, we will begin by examining how economic conditions influence corporate governance. Subsequently, the article will delve into the effects of economic recessions or upturns on governance practices.

Macroeconomic conditions can have a significant impact on corporate governance.[23] During periods of economic growth, corporations are often presented with opportunities for expansion and investment. Economic prosperity tends to foster an environment conducive to innovation and market expansion.[24] As a result, companies may be more inclined to take calculated risks and engage in strategic investments to pursue higher returns. Conversely, economic downturns or increased uncertainty may prompt a more cautious approach, leading companies to adopt conservative financial strategies aimed at reducing costs and risks to ensure survival and stability. In such circumstances, companies may defer investments, reduce expenses, downsize, or consider mergers and acquisitions.[25]

Furthermore, economic recessions or upturns significantly impact governance practices within organisations.[26] During economic downturns, the focus of corporate governance often shifts towards stabilising the financial health of the enterprise. Boards of directors and executive teams may need to place greater emphasis on risk management and financial transparency to ensure the company's survival and stability during economic downturns. Conversely, during economic upturns, corporate governance may concentrate more on strategic development and long-term value creation. Boards of directors and executive teams may focus on innovation and market competitiveness to achieve sustained growth and value creation.[27]

This analysis underscores the profound impact of economic conditions on corporate governance. Companies must tailor their strategies and decisions to address the diverse challenges and opportunities presented by varying economic environments. Similarly, governance practices should be adjusted in response to changes in economic conditions to ensure the long-term development and stability of the organisation.

With the deepening of global economic integration, multinational corporations are investors, shareholders, and stakeholders from different countries, which requires them to adhere to facing more standardised and internationalised corporate governance standards to ensure transparency and compliance in their operations.[28] Therefore, globalisation has far-reaching implications for the development of corporate governance standards. Globalisation has driven the convergence and enhancement of corporate governance standards.[29] According to Hermalin's article, we can understand that international organisations such as the International Monetary Fund (IMF) and the World Bank have promoted the standardisation and enhancement of corporate governance standards globally by issuing documents such as the "Corporate Governance Principles."[30]

On the other hand, globalisation has also accelerated the internationalisation of corporate governance standards.[31] Multinational corporations need to conduct business in different countries' markets, thus they must comply with each country's corporate governance regulations and standards. This requires multinational corporations to consider the differences in laws, cultures, and business environments of different countries when formulating corporate governance policies and practices, in order to ensure compliance and sustainable development on a global scale. In addition, globalisation has also promoted the more transparent and sustainable development of corporate governance standards, as multinational corporations need to provide clearer and more credible governance information to global investors, shareholders, and stakeholders in order to gain their support and trust.

The dynamics of the international economy have a significant impact on corporate behaviour. Factors such as international trade, fluctuations in the foreign exchange market, and global economic downturns can directly affect corporate governance. Multinational corporations need to closely monitor the dynamics of the international economy to address various risks and opportunities. For example, a global economic recession can reduce a company's sales and profits, leading to adjustments in its strategies and business plans. Additionally, exchange rate fluctuations can affect a company's costs and revenues, thus impacting its internationalisation strategy and capital management strategy.[32]

Therefore, economic globalisation has an undeniable impact on corporate governance, and the dynamics of the international economy have a significant influence on corporate behaviour. These factors require close attention from company managers and decision-makers in order to develop appropriate strategies and governance measures to adapt to the challenges and opportunities brought about by globalisation and the dynamics of the international economy.

4 The impact of law on corporate governance

Law plays a crucial role in corporate governance and business behaviour.[33] It provides the fundamental rules and systems for corporate governance, regulating the internal and external behaviour and relationships of companies.[34] Legal documents such as company law, securities law, and articles of association provide clear legal basis and norms for corporate governance, constraining and regulating the behaviours of the board of directors, shareholders, executives, and other stakeholders. These laws stipulate provisions regarding corporate governance structure, shareholder rights, board responsibilities, providing the basic framework and rules for governance.

However, it is important to note that the role of law in corporate governance may be influenced by political and economic factors.[35] Political factors may affect the formulation and enforcement of laws, while economic factors may affect the applicability and effectiveness of laws. For instance, the political stance and policy orientation of the government may influence the formulation and amendment of company laws, and political forces may have an impact on the establishment and revision of corporate governance regulations.[36] Additionally, economic conditions and market environments may also affect the applicability and effectiveness of laws. Factors such as economic recession, financial crises, etc., may lead to an impact on the effectiveness of law enforcement, thereby affecting the actual impact of corporate governance.

Therefore, while the legal framework plays an important role in corporate governance, its effectiveness is still subject to the influence of political and economic factors. Political factors may affect the formulation and amendment of corporate governance regulations, while economic factors may affect the applicability and effectiveness of laws. Corporate governance not only relies on law but also needs to consider the influence of political and economic factors on the legal framework and the potential impact during practical enforcement, in order to ensure the effectiveness and compliance of corporate governance.

5 Conclusion

When discussing issues related to corporate governance, it is inevitable to consider the impact of non-legal factors on corporate governance. Political factors may pose significant challenges to corporate governance, as changes in government policies can lead to legal uncertainties for companies and the instability of the political environment can affect long-term governance. Moreover, direct political intervention can expose companies to risks, such as government interference in corporate ownership and operations, which can have a negative impact on corporate governance. On the other hand, economic factors also present challenges to corporate governance. Fluctuations in economic cycles, instability in financial markets, and changes in the global trade landscape can all have significant impacts on corporate governance. Moreover, intensified global market competition and technological advancements can pose challenges to corporate governance, requiring companies to continuously adapt their governance approaches to the rapidly changing economic environment.

In conclusion, although the legal framework plays an important role in regulating and constraining corporate behaviour, political and economic factors have a broader influence, surpassing legal elements in corporate governance. To achieve effective corporate governance, it is not only necessary to have the support and regulation of laws, but also to consider the impact of the political and economic environment, and formulate corresponding strategies and measures to address challenges. However, the political and economic environment varies across different countries and regions. Therefore, it is crucial for company managers to focus on studying and discussing how to effectively integrate the influence of political, economic, and legal factors according to specific regional contexts, in order to promote more effective corporate governance.

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