The Impact of Corporate Governance on Investment Returns in Developed and Developing Countries

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Abstract:
We shed light on three conundrums in the literature on investment: why investments out of different sources of finance earn different returns, why different studies report different patterns of returns across sources of finance, and why companies in developing countries make greater use of external equity capital to finance their investment than do companies in developed countries. We show that the strength of corporate governance systems affects the preferred source of financing, which in turn helps to explain why investments financed in different ways exhibit significantly different rates of return. We find considerable differences between developed and developing countries in the effectiveness of corporate governance systems in aligning managers and shareholders' interests.