Corporate Governance Index And Its Determinants In Samsung Company

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ABSTRACT

The aim of this study is to examine the relationship between Corporate Governance Index and its dependents. This Samsung Company had been chosen as the focus of our studies. Five years of data were collected from Samsung’s annual reports and websites from the year 2014 until the year 2018. The data collected is used to calculate the descriptive analysis which will be shown in the reports. Based on our studies, the dependent variables were the Corporate Governance Index. And for the independent variables, We had chosen Return on Asset (ROA), Return On Equity (ROE), Tobin’s Q, and Altman Z as the Internal factors and for the data like GDP per capita, Unemployment rate, and Exchange rate had been chosen as the external factors. The Stepwise method is used to claiming the results for the Correlations, regression results and etc to observe the most significant with the corporate governance index. Only the unemployment rate shows the most influence on the Corporate Governance Index.

Keywords: Corporate Governance, Corporate Governance Index, ROA, ROE
Unemployment Rate, GDP per capita

1.0 INTRODUCTION

Lee Byung-Chul was founded Samsung in 1983. Samsung has separated into four company which one of them was Samsung Group after Lee’s death in year 1987. Since from 1990, Samsung is increasingly globalized its activities and electronics. (Wikipedia, 2019) Samsung’s most important source of income was mobile phones and semiconductors. Business Korea (2017) stated that in 2017, Samsung has become the top 10 highest global brand value. Samsung has already more than 80 companies until today. Samsung was a highly diversified
company in which the activities in the area are including construction, financial services, consumer electronics, etc.

The Board of Samsung is composed of 7 members. From the 7 members, there was 4 Outside Director Candidate Recommendation Committee. Samsung Electro websites state that ‘The governance of Samsung Electronic was consisting legal and transparent procedures’. The procedures were based on Commercial Art and Company’s Article of Association.

In 2016, after the few days the announcement of Galaxy Note 7, few explosion cases were reported in few countries (INDEPENDENT, 2016). INDEPENDENT9 (2016) mention that from the cases, Samsung was facing a few principles problem under scandal. Which were Accountability and Business Ethics principles? Samsung faces a huge loss as recalling millions of flammable Galaxy Note 7. More than $19 billion has been wiped off from the company’s share value since the recall. This has slump dragged total profits down by 30%. It had been reached their lowest level in two years. After the case of Note 7 caught fire during flight, many countries had banned Samsung Galaxy Note 7 in the airlines. From the ValueWalk websites in 2016, it stated that ‘more than 10 people suffered from the injuries and 47 people’s personal property was damageed’.

In this assignment, the study will be divided into 4 parts. First part will be the introduction. The second chapter will be a literature review which discussing the previous study done by researchers. Next will discuss the analysis and findings which discover how the incidents happen and how Samsung handling the case. The last chapter will be including some discussion, recommendation, and conclusion to Samsung

2.0 LITERATURE REVIEW

In this chapter, the objectives of this study are to observe the secondary records. The secondary record may be obtained from the magazine, article, or any possible methods. In this research will be talking about 5 items regarding corporate governance. According to Business Dictionary, they mentions that ‘Corporate Governance is the framework of rules and practices’. The framework is needed so that board of directors ensures the principles of corporate governance in a company's relationship with its all stakeholders’. In Marco Beach (2005) views, he states that ‘Corporate governance is one of the most relevant and debatable areas of business and finance’.
The first item we will be talking about is how corporate governance is related to scandals. ‘The Corporate Scandals was occurring on a frequent basis in the 1980’s – 1990’s, stated by The international Corporate Governance Review 2003. The ICAEW (Institute of Chartered Accounts for England and Wales 2002) discuss ‘the importance of Corporate Governance in more details’. They explain that because of the corporate scandals, ‘Corporate Governance begins to operate or it can also be said corporate scandals is the main driver for Corporate Governance as it highlights what can actually happen and also the devastating effects’. Ana Paula (2016) also mentioned that ‘corporate scandals open wide weaknesses on internal and external controls over companies, which should be detected by good practices of governance’.

Nathanson (2002) explains that ‘corporate scandals often have fundamentals of political blame’. Nathanson explains that ‘they made a drive for growth by taking the example of Heath’s Government in 1972’. Which mean that when the growing at around 5%, a high share price will be affected the economy. ‘Some companies such as Slater Walker went bankrupt’ stated by Nathanson in 2002. In ‘On-going Board Reforms: One-size-fits-all and Regulatory Capture’, Gérard Hertig argues that ‘the board reform has fast-tracked dramatically in current years. Which driven by runaway executive compensation in the United States during the 1990s and the corporate downturn and scandals at the turn of the twenty-first century’.

Next, we will be discussing how corporate governance related to bankruptcy or Altman Z. Based on Investopedia, in 2019, they tells that ‘Altman Z-score is a publicly traded manufacturing company's likelihood of bankruptcy by using the output of a credit-strength test that gauged’. In the article of ‘Corporate Governance In the Bankruptcy Reorganization of Large, Publicly Held Companies, 1993’ It pointing out that ‘after many years the Bankruptcy Code became effective in 1979, there were no empirical studies of corporate governance in the bankruptcy reorganization of large, publicly held companies’. Based on M. Adnan Aziz, Humayon A. Dar, (2006) ‘Prediction of bankruptcy is of increasing importance to corporate governance. M. Adnan Aziz states that ‘Global economies need to become alert of the risks involved in corporate liability, especially after the passing of huge organizations such as WorldCom and Enron’. M. Adnan Aziz also mentions that ‘Corporate bankruptcy prediction is inherently vulnerable to problems arising from small samples.

Based on Wu, Sean (2016) ‘bankruptcy is associated with several conditions including a firm’s fixed costs, sales sensitivity and the proportion of liquid assets’. Based on the article ‘Corporate Governance In the Bankruptcy Reorganization of Large, Publicly Held Companies,
‘The splitting of the risk of loss and the view of gain has deep implications for corporate governance of insolvent and marginally solvent companies’. Chron website tells that ‘the behavior of managers is giving a great impact on the performance and value of a company’. From the Deloitte research, they investigated that ‘the corporate performance have a scientifically proven relationship with governance variables, and it would helping the boards and directors decide on the right structures and mechanisms’. The results confirm that corporate governance standards are good predictors of firm performance, especially in emerging markets with weak legal institutions. According to William (1999), ‘another tactic to find out the possible effects of corporate governance on corporate performance is to compare measures of national economic performance while controlling for governance commissions’.

According to Investopedia 2019, ‘The Tobin’s Q ratio is the assets replacement cost which are divided from market value of a company’. Therefore, equilibrium is when the value of market replacement cost. The analysis is used to calculate an estimation of the magnitude of agency costs (AC) by comparing a firm’s actual Tobin’s Q with its best-performing benchmark Q (Chung et al., 2012). ‘If the manager prevented from maximizing firm value. Therefore, the firm’s actual Q lies beneath the frontier. It is smaller than its hypothetical benchmark Q*, the shortfall from the frontier (Q*-Q) suggests inefficiency and is a measure of agency costs’ (Habib and Ljungqvist, 2005; Chung et al., 2012).

Ficici, A., & Aybar, C. B. (2012) stated that ‘high volatility and pricing inefficiencies in emerging markets raise some questions about Tobin’s-Q as a performance measure’. Ficici, A. & Aybar, C. B. (2012) also found that ‘the result was supporting a positive correlation between total corporate governance scores of emerging market MNEs and Tobin’s Q’. In the report ‘What Corporate Governance Elements Predict Firm Value: Evidence from Brazil’ shows that ‘the disclosure and Shareholder Rights subindices are important. It was important to explain that the stronger association between BCGI and Tobin’s Q for non-manufacturing firms and high-growth firms’. They also founded that the association between BCGI and Tobin’s Q is existing for high profit firms. For firms with the high Tobin’s Q, which was proxies in part for growth opportunities

Lastly, we will be talking about how corporate governance-related with macroeconomics. Habib stated that while Skeel is supports the collapsed residual ownership theory for resolving corporate governance problems. He was acknowledges that the possibility that a corporation so governed was too risk-averse from a wealth maximization perspective’.
(Habib and Ljungqvist, 2005; Chung et al., 2012). From the studies, Chow (2018) finds that ‘the overall relationship between macroeconomic uncertainty on leverage among firms with the better governance quality is negative’. ‘In countries with strong corporate governance, I makes the supply and the demand curves shift to the right. Ceteris paribus more companies with strong corporate governance systems will find that selling equity is an attractive way to finance investment, that the stock market should be thicker and that holdings should be more fragmented’.

Based on the results, Chow (2018) suggests that ‘When formulating financing policies, companies in the Asia-Pacific region take into account the volatility of the macroeconomic environment’. ‘The large pyramidal structures that arise in countries with weak corporate governance systems. It will affects the large blockholders which lead to improper allocation of capital and slowing economic growth’. Morck et al. (2000) present evidence that this occurs. Morck et al. in year 2000 also stated that ‘corporate integrity, strengthened market discipline, increased transparency through improved disclosure’. He also mentioned that ‘it was based on effective regulation and corporate social responsibility. These basic principles are the basis for healthy macroeconomic growth’.

3.0 METHODOLOGY

Introduction

Based on The Investopedia, methodology is the systematic, theoretical analysis of the methods applied to a field of study. Merriam-Webster described that ‘methodology is a body of methods, rules, and postulates employed by a discipline’. The purpose of this research is to understand how the Scandal is influencing to Samsung companies. The method that used is to collecting and analyzing data is from IBM Statistical Package for the Social Sciences (SPSS) Statistics version 25.

Sampling Technique

In this research, the company that is chosen was Samsung. Five years of analysis are taken to compare in order to conduct this research. The 5 years chosen are from the year 2014 until the year 2018. Most of the findings are from 5 years of Samsung’s annual reports and financial reports. The finding also consists of web-based research to get extra information from the companies. For example, Samsung website which some of their details are not including in the reports.
**Statistical Techniques**

This study focuses on the Samsung Company. To conduct this research, 5 years of data is extracted from Samsung’s annual reports and financial reports from the year 2014 until the year 2018. To evaluate the financial performance of Samsung, Income statement and balance sheet are used from each year of the annual report. Financial ratios such as Return on Asset (ROA), Return on Equity (ROE), Tobin’s Q and Altman Z-score is needed to evaluate financial performance. The data of Gross Domestic Product, unemployment rate and exchange rate from the year 2014 until the year 2018 are also collected. These data are used to analyze the economic condition from the year 2014 until the year 2018.

To complete the research, we are using Ordinary Least-Square (OLS) regression or known as linear regression as main technique. ‘Least-Squares method had been used to seek a line of best fit in order to explains the potential relationship between an independent variable and a dependent variable’ (Investopedia, 2018). OLS chooses the restrictions of a linear function of a set of explanatory variables by minimizing the sum of the squares of the difference between the dependent variable observed in a given data set and the dependent variable predicted by a linear function. The relationship is modeled using a linear prediction function, where the unknown model parameters are estimated from the data. Therefore, OLS is more user-friendly be used to valuing regression by comparing to other alternative techniques.

**Data Analysis**

In this research, one dependent variable (Corporate Governance Index) and two categories of the independent variable (internal and external factors) are used. The research framework is shown below:
The Regression Analysis (OLS) is conducted to research out for the relationship between a dependent variable and an independent variable. Overall, regression analysis helps to justify how the value of dependent variable ups and downs when the independent variables are different. Multiple regression analysis methods are used to determine the influence of independent variables on the dependent variable in this study.

**IBM Statistical Package for Social Sciences (SPSS Statistics)**

IBM SPSS Statistics version 25 had been used to compute data from the annual reports. In order to complete the research, this methods was used to acquire the result. Norman H. Nie, C. Hadlai (Tex) Hull and Dale H. Bent from University of Standford has been developed Statistical Package for the Social Sciences (SPSS) in a long time ago.

In 2015, SPSS was officially renamed as IBM SPSS Statistics after acquiring of IBM. It is now the most widely used programs for analyze the research statistically. It has a great multi-function such as data management, data documentation features and statistical analysis. These features would help in better to making the decision. IBM SPSS Statistics were used in this research. The features used to compute descriptive statistics, correlation, coefficient and etc between independent variables and dependent variable. The features was based on quantitative data collected from primary and secondary data.

### 4.0 ANALYSIS AND FINDING

**Descriptive Analysis**

<table>
<thead>
<tr>
<th>Year</th>
<th>Corporate Governance Index</th>
<th>ROA</th>
<th>ROE</th>
<th>Tobin's Q</th>
<th>Altman Z</th>
<th>GDP per cap (USD)</th>
<th>Unemployment rate</th>
<th>Exchange rate</th>
</tr>
</thead>
<tbody>
<tr>
<td>2014</td>
<td>0.51</td>
<td>0.10</td>
<td>0.14</td>
<td>0.11</td>
<td>5.21</td>
<td>27,815.00</td>
<td>3.50</td>
<td>1,099.00</td>
</tr>
<tr>
<td>2015</td>
<td>0.53</td>
<td>0.08</td>
<td>0.11</td>
<td>0.10</td>
<td>7.65</td>
<td>27,096.00</td>
<td>3.60</td>
<td>1,173.00</td>
</tr>
<tr>
<td>2016</td>
<td>0.53</td>
<td>0.09</td>
<td>0.12</td>
<td>0.09</td>
<td>3.38</td>
<td>27,608.00</td>
<td>3.70</td>
<td>1,208.00</td>
</tr>
<tr>
<td>2017</td>
<td>0.54</td>
<td>0.14</td>
<td>0.20</td>
<td>0.14</td>
<td>4.98</td>
<td>29,745.00</td>
<td>3.70</td>
<td>1,071.00</td>
</tr>
<tr>
<td>2018</td>
<td>0.54</td>
<td>0.13</td>
<td>0.05</td>
<td>0.14</td>
<td>8.03</td>
<td>29,743.00</td>
<td>3.80</td>
<td>1,081.00</td>
</tr>
</tbody>
</table>

Table 4.1: Descriptive Results
Based on the table above, Samsung’s Corporate Governance Index has increased from the year 2014 to the year 2018. The ROA (Return on Asset) and the ROE (Return on Equity) had decreased in the first few years from the year 2014 and increased back afterward. Tobin’s Q had decreased from the year 2014 and increased back in the year 2017. Altman Z shows an inconsistency grows, it increases from the year 2014 until the year 2015. Then it decreased during the year 2016 and finally increasing back in the year 2017 and the year 2018. In overall, GDP per capita had increased from the year 2014 to the year 2018, which from USD 27,815 to USD 29,743. The unemployment rate also had been increased from the year 2014 (3.5) to the year 2018 (3.8). The exchange rate increased from the year 2014 to the year 2016 and drop again in the year 2018.

**Descriptive Statistics**

<table>
<thead>
<tr>
<th></th>
<th>Mean</th>
<th>Std. Deviation</th>
<th>N</th>
</tr>
</thead>
<tbody>
<tr>
<td>Corporate Governance Index</td>
<td>.5328</td>
<td>.01379</td>
<td>5</td>
</tr>
<tr>
<td>ROA</td>
<td>.1075</td>
<td>.02683</td>
<td>5</td>
</tr>
<tr>
<td>ROE</td>
<td>.1218</td>
<td>.05363</td>
<td>5</td>
</tr>
<tr>
<td>Tobin's Q</td>
<td>.1138</td>
<td>.02218</td>
<td>5</td>
</tr>
<tr>
<td>Altman Z</td>
<td>5.8523</td>
<td>1.95292</td>
<td>5</td>
</tr>
<tr>
<td>GDP per capital (USD)</td>
<td>28401.4000</td>
<td>1253.25269</td>
<td>5</td>
</tr>
<tr>
<td>Unemployment rate</td>
<td>3.6600</td>
<td>.11402</td>
<td>5</td>
</tr>
<tr>
<td>Exchange rate</td>
<td>1126.4000</td>
<td>60.64487</td>
<td>5</td>
</tr>
</tbody>
</table>

**Table 4.2 Descriptive Statistics**

The table above is showing the Descriptive Statistic of Samsung Company. This table shows the results of the mean (average) and standard deviation of Samsung based on microeconomic and macroeconomic data in 5 years.

In the Microeconomic or internal factor indicators for Samsung, we can see that the Corporate Governance Index was 53.28% among 5 years. Next would be the return on assets (ROA), every 1 dollar of the asset will be generating 10 cents of profit. Based on the return on equity (ROE), every 1 dollar of equity will be generating 12 cents of the profits. Based on the Tobin’s Q Ratio, averages of 1 dollar from the asset value of the firm the market value was 11
cents. In Altman Z the averages value was 5.85, which mean that Altman Z-score of Samsung was in a safe zone. The reason was the Zone of discrimination was more than 2.6.

Next would be the Macroeconomic or external factors indicators for Samsung. GDP is on average 28,401 dollars from the year 2014 to the year 2018. The unemployment rate was 3.66% 5 years and lastly, the exchange rate was 1126.4 South Korean Won for each 1 dollar

From the standard deviation tell us how volatile that Samsung is. We can know how unpredictable are the Samsung is. Based on the results, we can see that most of the internal factor indicator was near 0. That means Samsung is a volatile company. The reason is that Samsung’s ROA, ROE and Tobin’s Q was very near to the zero.

Correlations

<table>
<thead>
<tr>
<th>Size of correlation</th>
<th>Interpretation</th>
</tr>
</thead>
<tbody>
<tr>
<td>0.90 to 1.00</td>
<td>Very high positive correlation</td>
</tr>
<tr>
<td>0.70 to 0.90</td>
<td>High positive correlation</td>
</tr>
<tr>
<td>0.50 to 0.70</td>
<td>Moderate positive correlation</td>
</tr>
<tr>
<td>0.30 to 0.50</td>
<td>Low positive correlation</td>
</tr>
</tbody>
</table>

Table 4.3 Table of Correlation
Table A4.3B Table of Correlation Benchmark

Table 4.3 above is showings that the correlation of Samsung. Pearson Correlation is used to decide the relationship between the dependent variable (Corporate Governance Index) and independent variables (Internal Factor Indicator and External Factor Indicator). And Table 4.3B shows the determination of the relationship between the dependent variables and independent variables.

Based on Table 4.3, we can see that the unemployment rate is a very high positive related to the corporate governance index because the size was 0.934. It shows that when the unemployment rate decrease, the corporate governance index is also decreased. In other words, if the unemployment rate increase, the corporate governance index will be increased. The second high positive correlation that we can see from Table 4.3 was GDP per capita. The GDP per capita can be considered as a high positive correlated with corporate governance index because the result shows the size was 0.701.

For the moderate positive correlations. We found that the ROA is 0.588 size of correlation with corporate governance index. For other variables, the correlation was lower than 0.50 size of correlations. The result also shows that there are 2 variables which low negative correlation with corporate governance index. The two low negative variables were ROA (-0.101) and Exchange rate (-0.200) The negative correlation means that when either ROA or exchange rate is increased, the corporate governance index will be decreased.

We can say that GDP per capital and Unemployment rate are a significant correlation with corporate governance index. This is because the p values of GDP per capita is 0.094 which is less than 0.10 and the unemployment rate has a higher significant level because it is lower than 0.05. Based on the results based on Table 4.3, we can be concluded that the corporate governance index has a higher correlation with the macroeconomic or external factor indicators.

Variable

Variables Entered/Removed

<table>
<thead>
<tr>
<th>Correlation Range</th>
<th>Type of Correlation</th>
</tr>
</thead>
<tbody>
<tr>
<td>0.00 to 0.30</td>
<td>Negligible correlation</td>
</tr>
<tr>
<td>(0.00 to -0.30)</td>
<td>Negligible correlation</td>
</tr>
<tr>
<td>(-0.30 to -0.50)</td>
<td>Low negative correlation</td>
</tr>
</tbody>
</table>
Model Summary

Model Summary<sup>b</sup>

<table>
<thead>
<tr>
<th>Model</th>
<th>R</th>
<th>R Square</th>
<th>Std. Error of the Estimate</th>
<th>Durbin-Watson</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>.934&lt;sup&gt;a&lt;/sup&gt;</td>
<td>.872</td>
<td>.00570</td>
<td>3.125</td>
</tr>
</tbody>
</table>

<sup>a</sup> Predictors: (Constant), Unemployment rate

<sup>b</sup> Dependent Variable: Corporate Governance Index

Table 4.5 Model Summary Result

ANOVA<sup>a</sup>

<table>
<thead>
<tr>
<th>Model</th>
<th>Sum of Squares</th>
<th>df</th>
<th>Mean Square</th>
<th>F</th>
<th>Sig.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Regression</td>
<td>.001</td>
<td>1</td>
<td>.001</td>
<td>20.392</td>
<td>.020&lt;sup&gt;b&lt;/sup&gt;</td>
</tr>
<tr>
<td>Residual</td>
<td>.000</td>
<td>3</td>
<td>.000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>.001</td>
<td>4</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

<sup>a</sup> Dependent Variable: Corporate Governance Index

<sup>b</sup> Predictors: (Constant), Unemployment rate
Table 4.6 ANOVA Results

The Table 4.5 shows how much of the independent variable explains the dependent variable. So based on the results, we can tell that the model 1 (unemployment rate) can explain a very high of the corporate governance index. The R relationship coefficient R=0.93.

According to Table 4.5, adjusted R-Squared is equal to 82.9%. This represents that if using the Unemployment Rate in Model 1, it is showing that the variables used are able to explain about 82.9% of the average of corporate governance index of Samsung. The remaining of the 17.1% of the adjusted R-Square remain unknown. This implies that the average corporate governance index of Samsung is unable to be explained from the unemployment rates.

From Table 4.6, the ANOVA table shows that the significant values of 0.020 which is not below the alpha value (p < 0.001). This means that the variables are not perfectly significant to represent the model.

Coefficients

Coefficients\textsuperscript{a}

<table>
<thead>
<tr>
<th>Model</th>
<th>B</th>
<th>Std. Error</th>
<th>Beta</th>
<th>t</th>
<th>Sig.</th>
<th>95.0% Confidence Interval for B</th>
<th>Collinearity Statistics</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>Lower Bound</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>Upper Bound</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>Tolerance</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>VIF</td>
<td></td>
</tr>
<tr>
<td>1</td>
<td>(Constant)</td>
<td>.119</td>
<td>.092</td>
<td>1.305</td>
<td>.283</td>
<td>-.172</td>
<td>.411</td>
</tr>
<tr>
<td></td>
<td>Unemployment rate</td>
<td>.113</td>
<td>.025</td>
<td>.934</td>
<td>4.516</td>
<td>.020</td>
<td>.033</td>
</tr>
</tbody>
</table>

\textsuperscript{a} Dependent Variable: Corporate Governance Index

Table 4.7 Table of Regression Coefficients

The analysis of coefficients is showing how was the independent variable that influences on the corporate governance index can be determined through the identification of a p-value with the significant level of 5%. P-value of 0.000 showings explained that the independent variables
have most substantial on dependent variables, P-value lesser than 0.001 explainings that the independent variables have a strong influence on dependent variables. The p-value that less than 0.05 explaining that a moderate influence of independent variable on the dependent variable and the least significant influence was the p-value is lesser than 0.10.

Based on Table 4.7, it shows that the unemployment rate has a moderate on influencing the corporate governance index with p-value < 0.05. We also can be said that the unemployment rate is positively influenced with corporate governance index. This means that when the unemployment rate increase, corporate governance will be increased.

5.0 CONCLUSION

In conclusion, from the findings, the unemployment rate shows the most significant relationship with the corporate governance index. Unemployment rate defines as the percentage of unemployment of labor in the total labor force. Hence, Samsung main business was selling the smartphone. So if most of the people have a job, they are able to spend their money to purchase Samsung products. From the earning that is gained from the people, they would be able to improve the company structure. It will bring Samsung to be a good company which Samsung’s corporate governance index will be increased. In other words, if the unemployment rate was decreased, the earnings of Samsung will be decreased. And then lastly, there will be a high chance for Samsung’s corporate governance index to drop.

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