Can Media Reporting Shape Corporate Conduct?

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WASHINGTON—In developing countries—such as Russia and China—corruption is often treated as an unavoidable byproduct of doing business. Media scrutiny and revelation of misconduct have little effect, as courts, regulators and those in positions of authority are as corrupt as those they govern, according to a recently updated research report.

The report, titled "The Corporate Governance Role of the Media: Evidence from Russia," by Professor Alexander Dyck of University of Toronto, Natalya Volchkova of The New Economic School in Russia and Luigi Zingales of the University of Chicago offers some insight into the role of business media in influencing corporate conduct.

Businesses—some of which are state-owned—from such nations often employ underhanded business tactics and use their influence to exert pressure in their domestic markets. However, they are often forced to follow the international ethical and business standards outside their home country. They fear being embarrassed, lose face or what the professors called "shaming" by the international community. Therefore, international media exposures of their corruptive behavior are to be avoided.

"Shaming only works if the audience shares the same set of values," suggested the professors. "If diluting minority shareholders is not perceived as terrible by Russian businessmen, then shaming cannot work." So, even if the local press reports inappropriate business behavior, people usually just shrug it off.

Corruption Results in Far Reaching Repercussions

Negative press reporting in developing countries and countries that do not operate a market economy have only a negligible effect on management behavior, while coverage of the same misconduct by a foreign media outside the respective country could affect the offending parties significantly and result in firing and criminal charges.

In nations with a stable, regulated market economy, media exposure of corporate management wrongdoing by local or international media often leads to extensive investigations by regulators. The Securities and Exchange Commission (SEC) and Federal Trade Commission (FTC) serve such roles in the United States. Legal actions, resignations, firings, prison terms and large fines could result.

The professors explained that media coverage In the U.S. "of much milder violations [than those that would cause a stir in Russia] lead to immediate firing or resignations." One example was the firing of former New York Stock Exchange CEO Richard Grasso, who drew regulatory ire for pocketing excessive compensation.

International media coverage not only affects the respective corrupt business executives in emerging markets, but also their regulators because they neglected their oversight duties.

If such corrupt or fraudulent behavior becomes known abroad, these globally active may have trouble borrowing in foreign markets, lose lucrative sales contracts, or attract fewer investments. Western banks and multinational companies take political and legal risk seriously in considering alliances.

Business tycoons in emerging markets—especially Russia—face a complicated political environment. By keeping a clean image, they find it easier to receive refugee status if they run afoul on their home turf for political or other reasons.

One of the foremost reasons for having a clean track record is the desire to be accepted into international business community circles. One designation that businesses in emerging markets covet is an elevated status at the World Economic Forum in Davos.

"Negative news reported in international media can also have the effect of ostracizing the executives from these desired social circles," or they may not be offered an influential position on the board of a company, according t o the professors.

Oleg Deripaska, one of Russia's youngest billionaires and the Chairman of the Board of RUSAL, a Russian aluminum manufacturer, "was disinvited from participating in the [2001] Davos meeting, and was stripped of his designation as one of the global leaders of tomorrow, because of a lawsuit and unflattering media reports suggesting bribery, money laundering, paying bribes and other corrupt behavior," said the researchers.

Taking On Gazprom Through The Media

The above-cited report was partly funded by William Browder, founder and CEO of Hermitage Capital Management Ltd. and manager of a hedge fund holding mainly Russian stocks. Browder has opposed Gazprom's corrupt management through savvy use of the media.

Gazprom is a Moscow-based, partially state-owned oil and gas monopoly, and one of the world's largest producer and exporter of natural gas. Gazprom provides roughly a quarter of Russia's tax revenues. Recent reports claim that Gazprom engaged in strong arm tactics and used its connections with Russian officials to limit the presence of competing foreign energy companies seeking to operate in Russia.

Browder took on Gazprom because "it is hard to find a place where there was more high-profile abuse than Russia, and a lot of the abuse was evident and quantifiable," claimed Dyck in a recent Knowledge@Wharton (KW) article "Good News about Bad Press."

Browder sought to build a relationship with reporters. He was truthful when he admitted that he was in it for self-centered reasons and expected to profit in the long run.

Gazprom had little experience with the media. In 2001, Browder fed *The Wall Street Journal, Business Week* and *The Financial Times* with information about Gazprom's executives "shifting corporate assets to entities controlled by friends and relatives," according to the KW article.

Soon after, Gazprom CEO Rem Vyakhirev lost his job and corporate reforms were enacted to prevent abuses. The outcome of successfully using the foreign media was a big win for Browder's hedge fund—it grew from $150 million to $1.5 billion in asset under management. Because of his actions, however, Browder has now become a persona non-grata in Russia, as a result of causing Russian authorities to lose face internationally.

Local Media Coverage Has Negligible Effect

In Russia, even if the local business media is foreign owned, there is little negative fallout from news regarding corrupt business policies

A good example is Russia's Vedemosti, a Russian newspaper jointly owned by Dow Jones & Co. (publisher of *The Wall Street Journal*) and Pearson Plc (publisher of *The Financial Times*).

"Being in Russian [language], it only reaches Russian businessmen and politicians. Our finding that coverage by Vedemosti has no significant effect suggests that in Russia the only shaming that works is the one in front of the international business community," according to the professors.