

# Magni Client Commentary

## Talking Points on International Governance Research and Investing March 2016

### Country Ranking Trends

- Magni completed a review of key shareholder rights. As a result of the review, Turkey's score for protecting shareholder rights in distressed companies was reduced. Scores in all other countries are unchanged.
- As mentioned last month, Magni Country Scores on average increase over time. The pace of governance improvements around the world has temporarily stalled. Recent events in countries such as Malaysia, Poland, and Thailand have the potential for reductions in their respective Magni Country Scores (i.e., potential downgrades).

### Philippines

- Sophisticated cyber criminals stole key information from Bangladesh's central bank using malware previously inserted into the bank's computer systems. The information enabled the criminals to divert funds using the SWIFT messaging system from the bank's account at the New York Fed. The diversion funneled \$81M to personal bank accounts in the Philippines and another \$20M was directed to a bank in Sri Lanka. The Sri Lankan bank reported an unusual transaction to their central bank and authorities quickly returned the money to the Fed. However, gaps in the Philippine's anti-money laundering (AML) laws prevented quick identification of the unusual transactions. As a result, only \$68K of the stolen funds have been returned so far. Specifically, the perpetrators used a loophole where casinos are not covered by the Philippine's suspicious transaction reporting requirements to purchase at least \$40M in gambling chips. The Philippine Senate is now considering amendments to address this AML loophole.
- A country's ability to prevent money laundering is a good indicator of the integrity of the country's markets. Countries with low market integrity become riskier places to do business as supposedly routine transactions are not routine and companies have challenges operating honestly and efficiently. Further, less capital gets deployed (and less wealth is created) in these countries as the risk discount on investments is increased to reflect uncertainty and the potential for problems.
- Philippines has not demonstrated the ability to translate its intention to prevent money laundering into action and they get a relatively low score for Market Integrity. The theft is not a surprise given the already identified weaknesses in the country's laws and controls. Magni will be watching to see if effective enhancements are made to Philippine law and if the institutions of the country abide by the enhanced laws. This sort of progress would cause Magni to upgrade the country.

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### Brazil

- Impeachment proceedings against President Dilma Rousseff have accelerated amidst large protests. The long-running Petrobras scandal has most recently ensnared the former President Lula da Silva. Federal prosecutors are investigating whether millions of dollars Mr. da Silva and his foundation have received from companies linked to the scandal were actually bribes. Soon after prosecutors announced charges against Mr. da Silva, Ms. Rousseff named him her chief of staff. The move would largely shield him from prosecution because government ministers can only be investigated by the Supreme Court. Rousseff has insisted that the appointment was for his political abilities, but her opponents see it as political cronyism. A recent Supreme Court ruling against the appointment was accompanied by the release of recorded phone calls between Rousseff and Lula that the judge said showed evidence of their obstructing justice. Opponents are using this latest episode to reinvigorate impeachment efforts against Rousseff.
- The scandal and associated machinations are consistent with Magni's existing view of Brazil and its governance. Brazil ranks lower than roughly two thirds of the countries in the developed and emerging markets. If the scandal ultimately results in meaningful reforms and those reforms are successfully implemented, then Magni would consider Brazil for an upgrade.

### Thailand

- In the first vote since a coup two years ago, Thailand's military government has set August 7th as the date for a referendum on a constitution that was written since the coup. Thailand's military government is facing resistance over the creation of a 250-member non-elected senate and what opponents see as encroachments on individual rights. Politicians from Thailand's major parties have been critical, saying the draft constitution is too authoritarian and will weaken political parties and undermine democracy. At this stage the draft is not yet final and significant amendments have been discussed. The final draft becomes law if it obtains votes in the referendum from 50 per cent of all eligible voters (not just those who vote). The military has said it will relinquish power and hold elections in mid-2017, though it has not been specified what will happen if the constitution is rejected.
- Prior to and following the coup, Thailand had significant governance weaknesses. At this point, it is not clear that the resulting constitution and subsequently-elected government will finally put Thailand on a path of better governance.

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### Poland

- A stand-off over the powers of the Poland's top court has led to large protests and has been described as the potential start of a constitutional crisis. Poland's Constitutional Tribunal ruled as unconstitutional the recent legislation regarding changes to the court. The legislation was passed by the Law and Justice party after its election in November. The government has said it won't publish the court's ruling, a move Polish law requires for the decision to be binding. The government has said the ruling itself was illegal, effectively leaving the court order in legal limbo. The dispute has led to a "rule of law" probe by the Council of Europe's human rights body the Venice Commission. The commission ruled against the Law and Justice party and has called on the government to recognize the top court's verdict. The panel's opinion is nonbinding, and the Polish Constitution does not say what should happen if a government defies the high court. The government has said the commission's opinion would be sent to the parliament so all political sides could seek a resolution.
- This latest conflict within Polish government is yet another setback for a previously promising country. Several years ago Poland made significant progress in strengthening its governance. The election last fall of a populist party threatens to undo some, and perhaps most, progress. Magni will be assessing the resolution of these issues and the resulting impact on the country's environment for good governance.