Corporate law vs. company charter: shareholder protection and corporate governance in late 19th century Portugal

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In the last decade and a half, institutional economists have claimed that the development of equity markets is strongly conditioned by the protection that investors receive from the law and legal institutions. This is because investors face uncertainty owing to the "agency problems" they encounter in their relations with the corporations to which they subscribe. As a result "countries with poor investor protections have significantly smaller debt and equity markets" and they perform less well macro-economically (La Porta et al., 1998).

The question this raises is what happens when there is a laissez *faire regime* in which the state stands back from regulating these relationships. In this paper, we analyse the Portuguese corporate sector between 1867 and 1914, a time when legal safeguards were quite limited and shareholder protection was largely left to the stipulations of company charters.

Owing to its centrality in the corporate decision making process, we focus on the distribution of voting power within companies as determined by their charters and ownership patterns. We find that although share distribution in Portuguese corporations was very unequal, the majority of charters was designed to protect non-dominant interests. This was done by redistributing voting power from larger owners to lesser ones, a policy which was met by a favourable response from small and medium holders, who showed a preference for more "democratic" corporations. Our main conclusion is that weak regulation by the state did not mean weak protection for investors because companies were able instead to contractualize this with their shareholders. Effective investor protection in Portugal was not sufficient, however, to promote a strong growth of either the capital market or the economy. “Country characteristics” (Doidge et al, 2007) seem to have proved a stronger counter-influence.