CHAPTER 7

FINDINGS, CONCLUSION AND RECOMMENDATIONS

INTRODUCTION
Corporate control, cash flow rights etc are spread across many stakeholders such as managers, shareholders, directors through legal, economic and institutional framework known as Corporate Governance. Corporate Governance has recently received much attention due to Enron, WorldCom, Satyam and other high profile scandals, serving as the impetus to recent U.S. regulations as the Sarbanes-Oxley Act of 2002, which is considered to be the most sweeping Corporate Governance regulation in the past 70 years (Byrnes et al., 2003). Not only in U.S but Corporate Governance legal reforms and voluntary Corporate Governance codes are proliferating around the world. In India, Securities Exchange Board of India (SEBI, India’s principal securities regulator) have come up with Clause 49 of the listing agreement. The share prices of large firms, to which the reform in regulations by SEBI were expected to apply, rose by roughly 4%, relative to smaller public firms. The overall effect of Corporate Governance on Firm Value or performance, however, remains unclear. Investor protection at the country level correlates with larger securities markets, less concentrated share ownership, and higher share prices (a higher value for minority shares) (e.g., La Porta, et al., 2005), (Levine, 1998). So
the question is whether the Corporate Governance practices of firms within a single country affects these firms' share prices and to what extent can a firm increase its market value by upgrading its Corporate Governance practices, and to what extent is it tied to its home country's rules and regulations? If better Corporate Governance is related to better firm performance, better-governed firms should perform better than worse-governed firms.

**OBJECTIVES:**

1. To study the impact of Corporate Governance on performance of S&P CNX Nifty index firms in India.

2. The objective of the study is to evaluate the impact of Board Composition of Central, state and Private owned listed Indian firms’ on market performance of the companies.

3. To study the impact of Corporate Governance scores on the performance of select public sectors companies.

**HYPOTHESES:**

$H_{0a}$: There is no relationship between firm performance proxied by three different variables i.e. Tobin’s q, MV/BV and market capitalization with Corporate Governance score of S&P CNX Nifty index.

$H_{0b}$: There is no impact of Board Composition of Central, state and Private owned listed Indian firms’ on market performance of the companies.
**H₀**: There is no impact of Corporate Governance Disclosure scores on the performance of select public sector companies.

**RESEARCH METHODOLOGY:**

The present study uses econometric modeling for examining the impact of Corporate Governance on the performance of S&P CNX Nifty companies. An attempt was also made to study the impact of Board Composition on performance of Central, Private, State owned companies and the level of Disclosure of PSUs using econometric model. The research methodology was adapted as per the objectives of the study and the extant review of literature.

**Sources of Data Collection**

The study was based on firm level data of all the companies across the various industries under consideration for the study. The data has been collected from Secondary sources. The secondary data has been collected mainly from the annual reports of the firms' under consideration for the study. The latest General Guidelines on Corporate Governance issued by Securities and Exchange Board of India (SEBI) was collected from SEBI website. Books on Corporate Governance, Journals, magazines and newspapers were also used as a secondary source for data collection. Prowess, a financial data base of Centre for Monitoring Indian Economy (CMIE) was also used for the study.
Sample Selection:-

The present study focuses on NSE S &P CNX Nifty 50 companies in Chapter 4, a comparative study of five Central, five Private and five State owned Companies in chapter 5 and five Public Sector Units in chapter 6. A sample of total 70 companies across the various industries covering almost 24 sectors of the Indian economy was taken in the entire thesis. The detailed selection of the sample for the respective chapter has been elaborated under each chapter.

Period of the Study

The period of the study was for 6 years that was from 2005-2011. The analysis of Chapter 4, Chapter 5 and Chapter 6 was based on 5 years database for a time period of 2004-2009.

Tools of Analysis:

For the purpose of analysis, the present study use Econometric method. Panel data analysis or Pooled Cross Section Time Series Analysis was applied for analyzing the impact of Corporate Governance on firm performance in chapter 4. An attempt was also made to study the impact of Board Composition on performance of select Central, Private and State owned firms in chapter 5 and the affect of CG Disclosure on the firm performance of select public sector undertakings in chapter 6 by using panel data analysis. The detailed methodology for the respective chapter has been elaborated under each chapter.
REVIEW OF LITERATURE

In this thesis Chapter 2 presents the comprehensive review of literature pertaining to Corporate Governance and firm performance and highlighted the research gap in broad-spectrum, with special reference to India. The summary of research gap is as follows:

- Hitherto Corporate Governance standards of developed countries are more focused than developing countries like India.
- A vast survey of literature indicates that very few studies (Himmelberg, et al., (1999), (Lei, 2005), (Miguel and Pindado, 2001) have used panel data analysis to determine the association between Corporate Governance mechanisms and firm performance.
- So far no attempt was made to find out to what extent the companies in India are complying with the SEBI guidelines.
- Hitherto no study involves the manual computation of Corporate Governance index as per the SEBI guidelines.

CORPORATE GOVERNANCE IN INDIA

The managing agency system promoted dispersed equity ownership in the starting of Indian corporate development but at the same time it gave disproportionate control to management which was even greater than
their stock ownership which ended up into historic bankruptcy cases in India. Due to this situation most of the banks and their depositors' funds were flushed away, ultimately these banks decided that they will lend to only legally protected blue chip companies (S&P CNX NIFTY) and park their funds in government securities (PSUs).

Many changes were introduced in laws and regulations driving Corporate Governance after liberalization in India, perhaps the single most significant development in the field of Corporate Governance and investor protection was the establishment of the Securities and Exchange Board of India (SEBI) in 1992 and its regular empowerment since then.

An attempt is made to discuss about the various committees formed in India and how the recommendations of these committees have let to further enhancement of the SEBI guidelines and to study the updated Corporate Governance guidelines issued by Securities and Exchange Board of India (SEBI) under clause 49 of the listing agreement.

Corporate Governance in India came into picture by a spate of crises in the early 90's as well as opening up to the forces of competition and globalization. For development of Corporate Governance in India CII Committee and SEBI Committees such as Kumar Mangalam Birla committee and Narayana Murthy committee were formed. These committees provided recommendations for improving Corporate Governance in India on various issues such as Board of Directors, Audit
committee, Disclosure and Transparency and Other issues. These committee’s recommendations have had the maximum impact on changing the Corporate Governance situation in India.

SEBI implemented the recommendations of the Birla Committee through the enactment of Clause 49 of the Listing Agreements. Further these guidelines under clause 49 were improved by Mr Narayana Murthy during 2002-03. SEBI accepted the recommendations in August 2003 and asked the Stock Exchanges to revise Clause 49 of the Listing Agreement based on Murthy committee recommendations. This led to widespread protests in the Industry, and forced the Murthy committee to revise the recommendations. The committee, thereafter, considerably revised the earlier recommendations and the same was put up on SEBI website on 15th December 2003 for public comments. It was only on 29th October 2004 that SEBI finally announced revised Clause 49, which was implemented by the end of financial year 2004-05 till date. The clause 49 of the listing agreement provides guidelines on composition of Board of Directors, the Non executive directors’ compensation and Disclosures, other provisions as to Board and Committees and Code of Conduct. It also provides course of action for audit committee. What should be the Qualification of the Audit Committee, the number of Meeting of Audit Committee, Powers of Audit Committee, Role of Audit Committee, and Review of information by Audit Committee etc. The clause 49 also
provides rules for Subsidiary Companies and Disclosures of related party transactions, Disclosure of Accounting Treatment, Board Disclosures – Risk management, Proceeds from public issues, rights issues, preferential issues etc, Disclosure regarding Remuneration of Directors, Disclosure of Management and Shareholders. SEBI also demands for CEO/CFO certification, Report on Corporate Governance and Compliance from the listed companies in India under clause 49 of the listing agreement.

**IMPACT OF CORPORATE GOVERNANCE OF NIFTY 50 COMPANIES ON FIRM PERFORMANCE**

In chapter 4 the impact of Corporate Governance (CG) practices on firm performance in India was studied. CG scores were computed from the annual reports of S&P CNX Nifty companies as per the Clause 49 of listing agreements issued by Securities and Exchange Board of India for a period of five years from 2004 to 2009. In India, Clause 49 requires, in addition to other things, audit committee, a minimum number of independent directors, and CEO/CFO certification of financial statements and internal control. Firm performance is measured in multiple ways like Market Capitalization, Tobin’s q and Market Value/Book Value ratio. The research hypotheses have been constructed to prove that CG scores have positive influence on firm performance. In this regard, pooled cross sectional time series analysis was used to test
the hypotheses. It is evident from the analysis that overall CG scores are sub-grouped into various components like Board Composition, Audit Committee, Ownership Component and Compliances. The results proved that overall CG practices in India have positive relationship with firm performance. Subsidiary companies and compliance was positive in case of Market Capitalization, Tobin’s q/Firm Value and negative in case of Market Value/Book Value. Return on equity was positive for all dependent variables. Leverage was found to be positive in all cases and statistically significant in case of Tobin’s q. Thus these results were statistically significant and survive a variety of robustness checks. A comparison was also made between the top ten scoring companies on the CG framework with the least ten scoring companies based on their financial characteristics such as Firm Value, Market Value/Book Value, Debt, Sales Growth, Net Profit Margin etc and it was found that most of the important financial characteristics are superior incase of top ten scoring companies in comparison with least ten scoring companies for example top ten scoring companies have high Firm Value in comparison to least ten scoring companies. This study provides evidence to support the relationship between CG and firm performance. Thus suggests that properly designed quality Corporate Governance can increase firm performance in an emerging market like India.
IMPACT OF BOARD COMPOSITION ON PERFORMANCE OF INDIAN FIRMS

In chapter 5 an attempt was made to capture the significant relationship between performance of select Central, Private and State owned companies across the industries in India. The hypotheses of the study were that the Board Composition has a positive influence on the performance of the companies belonging to three types of ownership pattern in India. Based on the panel data analysis method, it may be concluded that only one component of Board Composition i.e. Board Independence has positive impact on performance of the select Private owned firms across the industries, whereas the total Board Composition has no influence on performance of the select Central and State owned firms across the industries. The present study support the results of (Faber, 2005) that the firm with more outside directors i.e. Board Independence has fewer propensities to commit fraud especially in case of Private sectors firms there by supporting the report by blue ribbon committee(1999) in the US which stressed on the role of independent directors. The results of the present study are useful to investors, management, regulators and policy makers. Further, similar kind of
studies can be carried out with a larger data set and across the various
types of companies across countries.

IMPACT OF CG DISCLOSURE SCORES ON THE PERFORMANCE OF
SELECT PSUs IN INDIA

In chapter 6, an attempt was made to capture the significant
relationship between CG Disclosure scores and the market performance
of select public sector companies in India. It has been hypothesized that
CG Disclosure scores has a positive impact on the performance of
companies. The sample is drawn from Bombay Stock Exchange (BSE). In
India, it is mandatory to all the listed companies to present their Annual
Reports as per the Disclosure norms given by SEBI’s Corporate
Governance provisions under Clause 49 of the Listing Agreements. The
study was covered for a period of five years that was from 2004-05 to
2007-09. Based on the pooled cross section time series analysis, it was
proved that CG score has positive impact on Market Capitalization of
select public sector companies in India. The hypothesis is proved but
statistically insignificant. It is evident from the results and analysis that
better Corporate Governance Disclosures result into better performance
of the companies. This study provides evidence to support the
relationship between CG Disclosure and firm performance. This suggests
that properly designed mandatory CG Disclosures can increase in firm
performance in an emerging market like India. The present study
supports the results of (Meek et.al., 1995), (Ettredge et al., 2002), (Haniffa and Cooke, 2002) that Corporate Governance Disclosure practices have positive influence on the firm performance. The results of the present study are useful to investors, management, regulators and policy makers. Further, similar kind of studies can be carried out with a larger data set and across the various types of companies.

**ORIGINAL/SIGNIFICANT FINDINGS OF THE RESEARCH WORK**

1. All the dependent variables such as Firm Value/Tobin’s q, Market Value/Book Value and Market capitalization were positively correlated with Corporate Governance score of nifty 50 companies.

2. It was found that most of the important financial characteristics were superior incase of top ten CG scoring companies in comparison with least ten CG scoring companies on Corporate Governance framework for example top ten scoring companies have high Firm Value in comparison to least ten scoring companies.

3. It was found that a single component/variable doesn’t have much impact on dependent variables, but when all these single components/variables combines together which forms the total Corporate Governance have high impact on the performance of the companies. Hence, it is clear that companies cannot achieve quality Corporate Governance by complying only with one or two components but by complying with all the variables can help companies to maintain quality Corporate Governance which impacts on
performance. Among these lists of CG components some components such as Disclosure, audit committee, board of directors, subsidiary committees solely impacts the performance variables.

4. The results proved that CG Disclosure practices in India have positive relationship with firm performance. This suggests that properly designed mandatory CG Disclosures can increase in firm performance in an emerging market like India. Thus it was found that Corporate Governance Disclosures facilitate the investors in making more informed decisions.

5. Based on the panel data analysis method, it was found that Board Independence has positive impact on performance of the select Private owned firms across the industries, whereas the Board Composition had no influence on performance of the select Central and State owned firms across the industries. This findings support the results of (Faber, 2005) that the firm with more outside directors i.e. Board Independence has fewer propensities to commit fraud especially in case of Private sectors firms there by supporting the report by blue ribbon committee (1999) in the US which stressed on the role of independent directors.

6. According to the general theory of finance, leverage helps in increasing the shareholder’s returns i.e. the sign of leverage is expected to be positive. Among the control variables in the study it was found that the dividend payout, leverage and growth in sales
indicate positive sign but statistically not significant. Whereas, the Firm Value and net profit margin were found to be positive and statistically significant with Corporate Governance.

**CONCLUSIONS:**

Thus it may be concluded that quality Corporate Governance practice is related to firm performance in the Indian market. The following conclusions were also made:

1. A set of scattered diagrams proof that single Corporate Governance component/variable does not have much impact on dependent variables, but when all these single Corporate Governance components/variables are combined together which forms the total Corporate Governance have high impact on the performance of the companies.

2. All the dependent variables such as Firm Value/Tobin’s q, MV/BV and Market Capitalization were positively correlated with Corporate Governance score of select public sector undertakings and nifty 50 companies.

3. Top scoring companies were superior in financial characteristics in comparison to least scoring companies on Corporate Governance framework.

4. Board Independence has positive impact on performance of the select Private owned firms across the industries, whereas the Board
Composition has no influence on performance of the select Central and State owned firms across the industries.

RECOMMENDATIONS:

1. There should be double blind auditing to avoid the chance of juggling up of financial statements.

2. Apart from internal auditors at least two different external auditors should check the financial statement.

3. There should be strong internal control as it plays an important role in preventing and detecting fraud.

4. The board of directors should not be given full authority to make any investment decisions without showing the genuine proof of getting benefited from the investment to shareholders.

5. There should be strong implementation of risk management.

6. Very strict punishment should be given to the people involved in fraud.
FUTURE RESEARCH DIRECTIONS

The following are the future research directions:-

1. Similar kind of future research can be carried out to examine the impact of Corporate Governance on firm performance of listed companies focusing different type of industries.

2. Future studies can be undertaken to examine the impact of Corporate Governance on economy of a country.

3. Different Corporate Governance guidelines or international Corporate Governance standards and its impact on firm performance and country economy can be studied.

4. Based on this study, further, there is need to examine whether CG scores truly reflects firm performance with larger data set.

5. Future research should examine the role of CG scores in credit ratings of the companies.

6. There is a need for policy oriented study to further streamline the discloser practices across the industries.