CHAPTER III
REVIEW OF LITERATURE

3.1 Introduction

This chapter makes an effort to review the extant literature on corporate governance with reference to firm level governance in India and abroad. An effort would be made here to delineate the issues and formulate the structure for the present study. The academic literature on corporate governance examines the efficacy of alternative ownership structures and alternative structure for board of directors. While there is a mounting evidence of failure of certain governance structures to motivate managers to increase firm performance, the empirical evidence to date is mixed and gives little coherent evidence for the shape of an optimal structure of corporate governance.

The researcher’s endeavour in the chapter is to explore the literature on relationship between ownership patterns, different variables considered as favourable for good governance and firm performance. Various studies were conducted on the issues of corporate governance in general and its relationship with Disclosure & Transparency, Corporate Performance, Board of Directors, Role of Promoters and Role of Institutional Investors in particular. All these studies have been extensively reviewed in the chapter to show the relationship between corporate governance and these issues.

Accordingly, this chapter has been divided into six sections. The Section I is devoted for introducing the chapter and its objective. The Section II reviews the studies conducted in the area of role of ownership structure and its relationship with performance. The Section III is concerned with the review of studies conducted on construction of overall corporate governance index to measure compliance by firms and its effect on performance. Section IV has been devoted to review the studies focusing on role of board characteristics like structure, busyness, activity in corporate governance and enhancing
performance. Section V covers the studies undertaken specifically on the telecom sector. Finally, Section VI makes the concluding observations. Thereafter a synopsis of related research work in this chapter is given in a tabular format also.

### 3.2 Role of ownership structure

Theoretical and applied work on corporate governance systems point to the importance of the structure of ownership and control in setting the background for the corporate governance issues that can arise in reality. The connection between ownership structure and performance has been the subject of an important and ongoing debate in the corporate finance literature. The empirical studies about the relation between both variables seem to have yielded conflicting results.

Empirical research shows that share ownership and its structure can be important sources of incentives for managers, boards of directors and outside shareholders. However, despite these considerable research advances, the theory of optimal ownership structure still has a number of conceptual and empirical gaps that require to be filled. The ambiguity of theoretical predictions concerning the impact of ownership structure on firm performance is confirmed by the existing empirical evidence requiring further analysis especially in the context of Indian corporate sector. The present section reviews the extant literature on shareholding pattern and performance.

*Singh and Gaur (2009)* sought to understand how business group affiliation, within firm governance and external governance environment affect firm performance in top 500 Indian and Chinese firms and found that group affiliated firms performed worse than unaffiliated firms and the negative relationship was stronger in case of Indian firms than the Chinese firms. Ownership concentration was found to have a positive effect on firm performance while board independence had a negative effect of performance. They also concluded that group affiliation – firm performance relationship in a given country context was moderated by ownership concentration.¹
Chiang and Lin (2007) analysed the relationship between ownership structure and board of directors’ composition and their influence on the total factor productivity (TFP) of Taiwan’s firms and found that a curvilinear specification better captured the relationship between inside ownership and firm productivity. They also found that more collateralised shares by board decreased productivity of a firm but institutional shareholdings could alleviate this negative impact of collateralised shares on TFP and that the combined titles of CEO and chairman of the board of directors might be able to improve productivity. Conglomerate, high-tech and non-family-owned firms were more productive than their counterparts.  

Pant and Pattanayak (2007) examined the effect of insider ownership on corporate value in India for the period of 2001 – 2004; using 1833 (BSE) listed firms. They provide evidence that relationship between insider shareholding and firm value is non-linear in nature and there exists a significant non-monotonic relationship between the two. Tobin’s Q first increased, then declined and finally rose as ownership by insiders increased. The study also confirmed that foreign promoter /collaborator share holding has a significant positive Impact on the firm value. 

Douma, George and Kabir (2006) investigated the differential impact of foreign institutional and foreign corporate shareholders on the performance of 1005 emerging market firms using Capitaline 2000 database. They used OLS regression to estimate the relation between performance measured by ROA and Tobin’s Q and ownership variables to conclude that the effect of foreign ownership on performance is substantially attributable to foreign corporations and the impact of foreign institutional investors on performance is not clear cut. They documented the positive influence of corporations vis-a vis financial institutions with respect to domestic shareholdings as well.  

Patibandala (2006) separated large institutional investors into 2 groups – private foreign institutional investors and government owned local financial institutions in context of Indian economy as a developing country using firm level data of 12
Indian industries from 1989 – 2000 including 148 firms using CMIE database. He argued that government owned institutions had lower incentives in monitoring managers. Empirical results showed that increasing presence of foreign institutional investors has a positive effect on corporate performance in terms of profitability and firms that depend on government financial institutions for external finance show decline in performance.\(^5\)

**Selarka (2005)** contributed to the understanding of corporate governance issues in emerging economies by examining the role of blockholders in influencing firm value. Using a cross sectional sample of 1397 manufacturing firms traded on the Bombay Stock Exchange for the year 2001 she presented a deeper understanding of interaction between ownership structure and firm value in the following ways. She analyzed the role played by the shareholders with substantial voting power in situations when equity holding is less vis-à-vis more concentrated in the hands of promoters. She also attempted to see if these investors coordinate among themselves to constrain the insiders from expropriating corporate resources and found a significant curvilinear relationship between firm value and the fraction of voting rights owned by insiders. The curve slopes downward until the insider ownership reaches approximately between 45% and 63% and then slopes upward. Empirical results on ownership concentration by minority blockholders did not support the monitoring hypothesis of these investors.\(^6\)

**Miguel, Pindado and Torre (2003)** studied how the main institutional factors characterizing corporate governance systems around the world affect the relationship between ownership structure and firm value. They found that ownership concentration and inside ownership levels are determined by several institutional features such as investor protection development of capital markets, activity of market for corporate control, and effectiveness of boards. The relationship between ownership concentration was not directly affected by these institutional factors. There was a direct influence of corporate governance characteristics on the relationship between inside ownership and firm value. Their study included six countries: U.S, U.K, Australia, Japan, Germany, and
Spain. They also concluded that the factors which are more relevant or play an important role in explaining how ownership structure affects firm value were those embodied in the laws.  

*Mohanty (2002)* found that the basic objective of an institutional investor is to maximize its own shareholders' wealth and not to monitor the activities of the companies in which it has invested. However, they found that the development of financial institutions have lent money to companies with better corporate governance measures. They also find that mutual funds have invested money in companies with better corporate governance record. They found that corporate governance index is positively associated with financial performance measures like Tobin’s Q and industry-adjusted excess stock returns. Using a simultaneous equation approach, they find that this positive association is because of two reasons. Firstly, the development of financial institutions have invested in companies with good governance records, and secondly, their investment has caused the financial performance of the companies to improve. 

*Sarkar and Sarkar (2000)* looked into the role of large shareholders on corporate governance and found that block-holdings by directors increase company value after a certain level of holding and institutional investors; typically mutual funds were not active in governance and lending institutions start monitoring effectively once they have substantial equity holding in the company and this monitoring is reinforced by the extent of debt holdings by these institutions. Concentrated ownership was found to have a positive impact on company value providing support to ‘convergence of interest’ hypothesis rather than ‘entrenchment’ hypothesis. Their analysis also highlighted that foreign equity ownership has a beneficial effect on company value.  

*Khanna and Palepu (2000)* investigated the interaction between three different kinds of concentrated owners among 567 BSE listed companies in India; insider ownership, ownership held by domestic financial institutions and ownership by foreign financial institutions and their role as performance monitors. Their evidence suggested that domestic financial institutions in India were ineffective monitors, whereas foreign institutional investment had significant monitoring
benefits. Performance measured by Tobin’s Q was positively correlated with the presence of foreign institutional ownership and negatively correlated with the presence of domestic institutional ownership. Moreover, they did not find any evidence of a difference in this relationship between group affiliates and unaffiliated firms. However, when probed by further analysis it was found that foreign owners were indeed less likely to invest in group affiliates than unaffiliated firms and when they do invest in groups, they seek groups with lowest transparency problem.\(^{10}\)

**Sundaramurthy (1996)** examined the differential impact of institutional investors’ stockholding, managerial stock ownership, and corporate board characteristics on the rate of adoption of antitakeover provisions, including provisions which do and do not require stockholder approval. Institutional investment was found to reduce the rate of adoption of antitakeover amendments which require stockholder approval, whereas managerial stockholding reduces the rate of adoption of provisions which do not require stockholder approval.\(^{11}\)

### 3.3 Role of overall Corporate Governance Index

The empirical work on corporate governance has been following either a unified approach whereby researchers have tried to gauge the overall corporate governance compliance of the sample under study or a fragmented approach of observing certain components of corporate governance like board characteristics, managerial remuneration, duality etc. While studying the overall compliance many scholars have constructed a corporate governance index to measure the quality of governance and its contribution in enhancing performance. Many indexes have been formulated by various agencies like stock exchanges of certain countries and various research bodies. So far empirical research has given varied results and no universal compliance index has been formulated. This section emphasises on studies relating to construction and evaluation of such indexes.

**Cheung, Jiang, Limpaphyom and Lu (2008)** assessed the quality of corporate governance practices of Chinese Listed firms. They constructed a corporate governance index (based on the OECD principles of corporate governance) to
measure the quality of corporate governance and disclosure practices of 100 largest Chinese listed firms. The study showed no significant relationship between market valuation and corporate governance practices as measured by CGI for the sample. However, it was found that there was significant difference in CGI of top 20 versus bottom 20 performing companies. Further overseas listed Chinese companies showed more regard for the role of stakeholders and disclosure and transparency than non-overseas listed Chinese companies.\(^{12}\)

**Shen and Chih (2007)** studied the impact of corporate governance on earnings management in nine Asian countries and found that firms with good corporate governance tended to conduct less earnings management. Also, large firms were prone to earnings smoothing but good corporate governance could mitigate the effect on average. Where the governance index was large, there was leverage effect, otherwise reverse leverage effect existed. Firms with higher growth were prone to engage in earning smoothing and earnings aggressiveness, but good corporate governance could mitigate the effect.\(^{13}\)

**Florou and Galarniotis (2007)** developed the governance rating for Greek listed companies by benchmarking their governance structures against three levels: the minimum requirements under Greek regulations (low level), recommendations of the Greek code (middle level) and the additional international best practices prescribed by UK combined code (higher level). They found that the average governance rating at the lower level was 65.5%, this reduced significantly as it moved to middle and higher level, the average rating being 44%. Moreover, governance scores increased with firm size. They documented a relatively high lack of transparency in relation to Greek governance practices.\(^{14}\)

**Goncharov, Werner and Zimmerman (2006)** examined the pricing effect connected to the declared degree of compliance with the German codes of governance and found that degree of compliance was consistently value relevant information for the capital market and higher compliance receives a premium on pricing suggesting the existence of capital market pressures for adoption of code’s recommendations.\(^{15}\)
**Klapper and Love (2004)** explored the differences in firm level governance mechanisms, their relationship with the country level legal environment, and correlations between governance and performance using data from a report by CLSA (Credit Lyonnais Securities Asia) that constructed corporate governance rankings for 495 firms across 25 emerging markets and 18 sectors. It was found that firms in countries with weak overall legal systems have on average lower governance rankings, firms that trade shares in the United States have higher governance rankings. Good governance is positively correlated with market valuation and operating performance and this relationship is stronger in countries with weak legal systems.  

**Brown and Caylor (2004)** related corporate governance to firm performance of 2327 firms to measure the strength of a firm’s governance, they created a 51 point governance code using data from Institutional Shareholder Services (ISS) and related it to operating performance, valuation and shareholder payout. Better governed firms were found to be relatively more profitable, more valuable and paid out more cash to their shareholders.  

**Black, Jang and Kim (2003)** reported evidence that corporate governance is an important factor in explaining the value of Korean Public Companies. They constructed a corporate governance index (on 100) for 531 of the 560 companies listed on the Korea Stock Exchange (KSE), relying primarily on the response to a survey conducted by the KSE during the first half of 2001. The index was based on six sub indices for shareholder rights, board of directors in general, outside directors, audit committee and internal auditor, disclosure to investors and ownership parity. They found a strong positive correlation between the overall corporate governance index and firm value, which was robust across OLS, 2LS and 3LS regressions, in subsamples, in alternate specifications of corporate governance index, and with alternate measures of firm value. A moderate 10 point increase in CGI predicted a 6% increase in Tobin’s q a 105% increase in market/book ratio.
Park (2003) tested empirically the impact of corporate governance issues on productivity and growth in Korea by surveying 38 firms listed in Korean stock exchange. A multivariate analysis framework was drawn consisting of four key areas; ownership, management, social responsibility and institutional interface. The empirical findings supported a positive relationship between firms’ performance measured by profitability measures like ROE, ROA, profit margin, sales growth rate and the four key areas chalked out for the purpose. 19

Bauer, Giinster And Otten (2003) analyzed the effect of corporate governance on stock returns, firm value and performance in Europe. They used Deminor’s corporate governance ratings to rate around 250 firms included in Euro top 300 over the time period 2000 – 2001. They found a positive relationship between firm valuation and corporate governance but this relationship weakened substantially after adjusting for country differences. Firm performance measures were approximated by net profit margin and return on equity and the relationship turned out to be negative. 20

Sareen and Chander (2003) captured the glimpses of corporate voluntary disclosure practices of the private sector in India focussing on both the item-wise and corporate-wise disclosure of the selected companies belonging to different age groups, listing status, industries, sizes and profitability levels. They concluded that annual report is the most vital document to present information though style of presentation and method of accounting treatment and reporting vary. They were hopeful that with more and more companies trying to get listed in foreign countries; disclosure practices would improve to be in consonance with the international practices. 21

Bai, Liu, Lu, Song and Zhang (2002) identified a comprehensive set of internal and external governance mechanism for China’s listed companies and constructed relevant measures for each of them, they then created a rating index (the G index) to reflect the overall level of governance practice for China’s listed companies. They took a sample of 1006 firms listed in Shanghai and Shenzhen stock exchange. They found that better governed companies as per
their index were associated with higher market valuation as measured by TOBIN’s Q and ratio of market value and book value of total assets. They concluded that corporate governance matters greatly in China’s emerging market and China’s investors are willing to pay a significant premium for better governance standard.22

3.4 Role of board characteristics

Directors are one of the most important mechanisms of ensuring corporate governance practices. The role of board includes setting the company’s strategic aims, providing the leadership, supervising the management of business and reporting to the shareholders on their stewardship. Different committee reports have emphasised on their role and strengthening the norms for ensuring independence of the directors. Recently, by the efforts of different regulatory authorities, composition of directors has been drastically changed. This change is concerned with introducing more non-executive and independent directors, diversity of the directors, fixing their remuneration, their code of ethics and their entrepreneurial performance in Indian companies. Empirical work in the area has again given mixed results given the differences between the parameters studied and characteristics peculiar to the sample under study. The present section focuses on the studies relating to the different characteristics of board like composition, size, busyness, activity, leadership structure etc. for ensuring corporate governance.

Zattoni and Cuomo (2010) analyzed the recommendations of corporate governance scores developed worldwide by the end of 2005, about the independence, competencies and incentives of non-executive directors. Their results showed that non-executive directors’ independence is a commonly recommended governance practice “No-executive directors’ competencies and incentives are not considered a governance issue to be regulated in detail.23

Jackling and Johl (2009) studied the relationship between board structure an firm performance in the Indian context and provided some support to the agency theory as greater proportion on outside directors on boards were associated with
improved firm performance. However, agency theory’s notion that powerful CEOs have detrimental effect on performance was not supported. There was some support for resource dependency theory suggesting that a large board size have a positive impact on performance but at the same time there was found to be no support for the resource dependency theory in terms of association between frequency of board meetings and performance. They also found that outside directors with multiple appointments appeared to have a negative effect on performance.24

Sarkar and Sarkar (2009) Using a sample of 500 large firms and a measure of “busyness” that is more general in its applicability, found multiple directorships by independent directors to correlate positively with firm value. Independent directors with multiple positions were also found to attend more board meetings and were more likely to be present in a company’s annual general meeting. These findings were largely in contrast to the existing evidence from the US studies and lend support to the “quality hypothesis” that busy outside directors are likely to be better directors, and the “resource dependency hypothesis” that multiple directors may be better networked thereby helping the company to establish more linkages with its external environment. Multiple directorships by inside directors were, however, negatively related to firm performance. Their results suggested that the institutional specificities of emerging economies like India could work in favour of sustaining high levels of multiple directorships for independent directors without necessarily impairing the quality of corporate governance.25

Adjaond, Zeghal and Andleeb (2007) tested the link between the board’s quality and corporate performance. Board’s quality was determined by using a scoring mechanism used by McFarland(2002) to rank a sample of boards of Canadian firms on four criteria of board composition, compensation, shareholder rights and disclosure. Firm performance was based on accounting based measures ROI, ROE, EPS and market–to–book ratio and measures of value creation like economic value added and market value added. The empirical results showed, when performance was based on accounting income based measure, the
differences between the best and the worst boards was not significant. However when performance was defined in terms of value added, statistically significant differences were found between higher ranked and lower ranked firms. These results suggest that performance measure adjusting for risk and cost of equity lead to a better correlation with governance. Their regression results indicate that compensation and shareholders rights are significant variables in value creation.\textsuperscript{26}

\textit{Nicholson and Kiel (2007)} examined hypothesized links between the board of directors and firm performance as predicted by three predominant theories in corporate governance research, namely agency theory, stewardship theory and resource dependence theory. They used a case based approach to link board demography and firm performance under each theory for seven companies as case studies. They found that though each theory can explain a particular case, no single theory explains the general pattern of results.\textsuperscript{27}

\textit{Choi, Park and Yoo (2007)} examined the role of outside directors and foreign investors in Korea. Empirical results indicated that outside directors had a significant and positive effect on firm performance. They also found that institutional equity ownership especially by foreign investors had a positive effect on board and firm performance. In contrast to this, family ownership was found to be interfering with board independence and was coming out as a hindrance to firm performance in Korea. The effects of Chaebols were statistically insignificant.\textsuperscript{28}

\textit{Zang (2007)} in a bid to evaluate the Chinese government’s recent market-oriented efforts to promote good corporate governance conducted a re-examination of the working mechanics for market competition and other market-based governance mechanisms to ensure good corporate governance. He concluded that utility of market mechanisms may have been exaggerated, and they are not effective in disciplining serious managerial misbehaviour. He advocated legal sanction as fundamental to good corporate governance by combating serious misbehaviour and curbing illegitimate enrichment.\textsuperscript{29}
Garca and Anson (2007) analysed the effect of the Spanish privatisation process on the performance and corporate governance of the firms that were privatised through offerings over the period 1985-2003 and did not find any significant improvements in privatised firms’ profitability and efficiency. However, their results did suggest a change in firms’ ownership structure and in the characteristics of board of directors after privatisation. The ownership concentration decreased with the relinquishment of control by the state and board of directors were restructured with the creation of new specialised committees and incorporation of new executives.\(^{30}\)

Barako, Hancock and Izan (2006) suggested that the extent of voluntary disclosure by firms is influenced by its corporate governance attributes, ownership structure and company characteristics. Presence of audit committee, proportion of non-executive directors on board, institutional or foreign ownership were found to have a significant impact on level of disclosure whereas board leadership structure, liquidity, profitability and type of external audit firm did not have a significant influence on the level of voluntary disclosure by companies in Kenya.\(^{31}\)

Mak and Kusnady (2005) in their study examined the impact of corporate governance mechanisms measured by board composition, board size, independence and ownership variables on the firm value as measured by Tobin’s Q of Singapore and Malaysia firms with a sample of 230 firms listed on the SGX and 230 firms listed on the KLSE for the financial year 1999-2000. They found little evidence of relationships between most corporate governance mechanisms and Tobin’s Q. They found that there was an inverse relationship between board size and firm value in both countries. This suggests that the negative relationship between board size and firm value transcends different corporate governance systems.\(^{32}\)

Dwivedi and Jain (2005) investigated the relationship between corporate governance and firm performance in the Indian context, taking into account the endogeneity in the relationship. Governance parameters included board size,
directors’ shareholding, institutional and foreign shareholding, while the fragmentation in shareholding was captured by public shareholding. A simultaneous equation regression model for Tobin’s Q, as a measure of firm performance, was attempted using these variables, while controlling for industry effects and other non-governance variables. The data corresponded to a panel of 340 large, listed Indian firms for the period 1997–2001 spread across 24 industry groups. Their study provided evidence that a higher proportion of foreign shareholding was associated with increase in market value of the firm, while the Indian institutional shareholders’ association was not statistically significant. A weak positive association was also found between board size and firm value. Directors’ shareholding had a non-linear negative relationship with firm value, while the public shareholding had a linear negative association.  

Kula Veysal (2005) had made an attempt to find the effect of roles, structure and process of the board of directors on the performance of Turkish companies. Drawing on the data obtained from a sample of 386 mostly small and non-listed stock ownership companies, it was found that the separation of chairman and general manager positions has significant positive impact on firm’s performance. From the board roles of control, service and resource acquisition firm performance was found to be positively related only to the level of adoption of resource acquisition role. It was also found that the effectiveness, information access and performance evaluation attributes of boards are positively and significantly associated with firm’s performance.  

Mudhaki and Joshi (2004) examined the composition, focus and functions of audit committees, the effects of meetings and criteria used in the selection of members by Indian listed companies and concluded that the concept of audit committee was not new in India but their formation was slow and their composition lacked independence. Also audit committee functions were concentrated in the traditional areas of accounting and their role was not changing fast enough to make corporate governance more effective.
Aggarwal and Fuloria (2004) studied the perceived connection between competitive credibility and corporate governance from two different perspectives; companies and consumers. They covered Indian IT sector for their study and concluded that corporate governance was not a necessity for successful competition in Indian IT sector but a requirement for global competitiveness. Though companies agreed that consumers wanted to see corporate information but consumer expectation was not a key incentive to disclosure.36

Solomon et al. (2003) studied the attitudes of Taiwanese companies’ directors towards the role and function of the board of directors in corporate governance. Their findings endorsed the importance of outside directors in corporate governance system in Taiwan. They also suggested that remuneration policies were not sophisticated. Moreover, it was found that directors were dissatisfied with the influence of founding families on the corporate governance of listed companies and also they wanted international harmonization of corporate governance standards and viewed corporate governance reforms as means of attracting foreign funds in Taiwan.37

Weir, Laing and McKnight (2001) addressed the issue of effectiveness of internal and external governance mechanisms. Internal mechanism comprised of non-executive or outside directors and board sub-committees; and market for corporate control being the external factor. They studied 312 U.K. quoted companies and found no significant relation between internal governance structures and performance or between quality of directors and performance. However, there was some evidence of a weak relationship between performance and internal governance structures while differentiating between the best and worst deciles performers. They also found some evidence that the internal and external control mechanisms may be regarded as substitutes when differentiating between best and worst performers.38

Coulton, James and Taylor (2001) investigated the transparency of CEO compensation disclosures by Australian firms and found it to be negatively
related to the level of size-adjusted compensation, also, transparency increased with firm size and (weakly) with performance. However, they could not find any evidence of specific corporate governance attributes being associated with more transparent disclosures nor did they find any evidence of transparency being associated with the mix of cash and stock-based compensation.  

**Mak and Li (2001)** examined the determinants and interrelationships among corporate ownership and board structure characteristics using a sample of 147 firms listed in Singapore Stock Exchange. Board composition, board leadership structure and board size were used to capture monitoring ability of the board along with two ownership characteristics namely managerial ownership and blockholder ownership. They used 2SLS regression to estimate the determinants of board and ownership characteristics and found that both are related. The proportion of outside directors was found to be negatively related to managerial ownership and board size, dual leadership structure was positively related to blockholders ownership and negatively related to regulation and CEO tenure.  

**McGuire (2000)** investigated the influence of growth potential on corporate governance mechanisms. He used managerial incentives, both short term and long term, board composition and monitoring and ownership pattern as areas of governance and used Tobin’s q as a measure of growth potential for 323 firms. Results suggested that firms with high growth potential make greater use of managerial equity ownership and long term incentives and higher proportions of insiders on their boards. The findings were congruent with the argument that firms with high growth potential make use of more flexible, future-oriented mechanism of corporate governance.  

**Klien (1998)** demonstrated a linkage between firm performance and board composition by examining the committee structure of boards and the directors’ roles within these committees. He found little association between firm performance and overall board composition. However, by going into the inner workings of the board via board committee composition, he was able to find significant ties between firm performance and how boards are structured. First, a
positive relation was found between the percentage of inside directors on finance and investment committees and accounting and stock market performance measures. Next, firms significantly increasing inside director representation on these two committees experience significantly higher contemporaneous stock returns and return on investments than firms decreasing the percentage of inside directors on these committees.\(^{42}\)

**Yermack (1996)** presented evidence consistent with theories that small boards of directors are more effective, Using Tobin’s Q as an approximation of market valuation, he found an inverse association between board size and firm value in a sample of 452 large U.S. industrial corporations between 1984 and 1991. The result was robust to numerous controls for company size, industry membership, inside stock ownership, growth opportunities, and alternative corporate governance structures. Companies with small boards also exhibited more favourable values for financial ratios, and provided stronger CEO performance incentives from compensation and the threat of dismissal.\(^{43}\)

### 3.5 Studies on telecom sector

While there have been a large number of studies that have examined various aspects of corporate governance of industrial sector but very less empirical work has been done on governance of specific sectors, especially the telecom sector. The previous work too is inclined towards regulation of telecom rather than corporate governance. The researcher did not come across any study covering corporate governance in telecom. Previous work which did cover some sectors in certain countries had mostly excluded telecom from their sample. This section focuses on studies which covered some related aspects on the sector.

**Basant, Chandra and Mytelaka (2001)** looked into inter-firm linkages in the Indian telecom software sector. They found that about 58% of these linkages were between MNC’s and domestic firms and remaining involved only domestic firms. The linkages among domestic firms involves provision of equipment and infrastructure and distribution arrangements whereas the links between MNC’s and domestic firms were more varied and involved financial collaboration, joint production and accessing of marketing and distribution channels.\(^{44}\)
Cai and Tylecote (2008) set forth two frameworks, one for measuring static and dynamic technological capability in developing countries and other for predicting effects finance and corporate governance characteristics on the first and applied them together to Chinese mobile telecommunication manufacturing industry. It was found that ownership type matters but government’s influence over management selection matters more. Technological capability varied among types and levels in its visibility, and that state ownership and control was likely to make corporate governance less able to cope with low visibility technological capability. At the same time, it was likely to improve access to finance. However, semi-privatised firms were most dynamic.45

Gutierrez (2004) tried to integrate the available data in a more comprehensive institutional index of regulatory trend in telecommunications for a sample of Latin American and Carribbean countries. He took a sample of 25 countries in the region for the period 1980-2001 and tried to construct an index based on: autonomy, accountability, clarity of roles and objectives, transparency and participation, and the type of legal mandate that creates a regulatory body. The study showed that, in general, most countries embraced strong regulatory reforms along the lines recommended by experts and practitioners though their pace and scope has varied.46

Nestor (2005) stressed on a well defined corporate governance regime as an important tool to make the transition period for privatisation of telecom sector shorter and less painful. After reviewing the partially or wholly privatized European Telecom Sector, he proposes seven lessons for policy makers in charge for designing privatization. Where the state remains an important owner after partial privatization it should organize its shareholdings to pursue exclusively shareholders value objectives. If there are any privatization related asymmetries between control and cash flow rights, then shareholding should be limited in time and scope. While some minority shareholding powers, direct shareholder nomination and cumulative voting are welcome, the board needs to maintain its own cohesiveness and culture. The board should be actively and effectively involved in the development and validation of the company’s strengths and
control the major transactions. The privatized firms should strive to list in markets with high and credible disclosure requirements. Privatized firms should focus on developing a disclosure culture, especially as regards financial disclosures. Board should conduct a regular, thorough and independent evaluation of the CEO based on a set of criteria and yearly objectives agreed at the beginning of each year.\textsuperscript{47}

\textit{Wallsten (2002)} attempted to test the effects of establishing a regulatory authority prior to privatizing incumbent telecom firms. He found that countries that established separate regulatory authorities prior to privatization saw increased telecom investment, fixed telephone penetration and cellular penetration compared to countries that did not. Moreover, he found that investors were willing to pay more for telecom firms in countries that established a regulatory authority prior to privatization. This increased willingness to pay was consistent with the hypothesis that investors require a risk premium to invest where regulatory rules remain unclear.\textsuperscript{48}

\textbf{3.6 Conclusion}

An attempt has been made to provide the literature review on the corporate governance and related issues in this chapter. Reviews show that the focuses of the studies have been on the issues of ownership, overall governance compliance and variables of board characteristics. Most of the studies reviewed in the present chapter are based on the secondary data and pertain to samples outside India. None of the works pertain to assessing the governance and performance of any specific sector in any country including the telecom sector which has been chosen by the researcher for the study. Previous empirical work has given varied results on the relationships studied, this may be because of differences in sample characteristics, time frame of study, socio-legal environment and market efficiency of the country from which sample is drawn. Peculiarities of any specific sector have been by and large ignored. On the basis of framework proposed, an attempt has been made to fill the gap uncovered by existing literature.
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<td>Park et al.</td>
<td>2003</td>
<td>There is a positive relationship between firm performance and corporate governance</td>
<td>38 Korean firms listed in Korean stock exchange</td>
<td>ROE, ROA, profit margin, sales growth rate and asset growth rate</td>
<td>Measures of corporate governance, Multivariate analysis</td>
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<td>Bai et al.</td>
<td>2002</td>
<td>Better governed companies as per index have higher market value</td>
<td>1006 Chinese firms</td>
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<td>Brown et al.</td>
<td>2004</td>
<td>Better governed firms are relatively more profitable</td>
<td>2327 firms</td>
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<td>51 corporate governance provisions, OLS</td>
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<td>Gupta et al.</td>
<td>2006</td>
<td>On an average 70% companies complied with 80% codes on corporate governance</td>
<td>1245 Indian companies</td>
<td>Rate of compliance</td>
<td>21 measures of corporate governance, averages</td>
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<td>Bauer et al.</td>
<td>2003</td>
<td>Weak positive relation between firm valuation and corporate governance, and negative relation between profitability and governance</td>
<td>250 Eurotop firms for 2000-01</td>
<td>Net profit margin, ROE and Tobin’s Q</td>
<td>Governance score, OLS</td>
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<td>Cheung et al</td>
<td>2008</td>
<td>No relationship between market valuation and corporate governance practices. But there was difference between top 20 and bottom 20 firms.</td>
<td>100 largest Chinese firms</td>
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<td>Khanna et al</td>
<td>2000</td>
<td>Foreign investment is positively associated with firm performance.</td>
<td>567 BSE listed companies.</td>
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<td>Sarkar and Sarkar</td>
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<td>Concentrated ownership has a positive relationship with performance.</td>
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<td>Miguel et al</td>
<td>2003</td>
<td>Insider ownership does affect firm performance &amp; domestic financial institutions are ineffective.</td>
<td>Data from 6 countries</td>
<td>Ownership patterns, board composition ratios</td>
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<td>Pant and Pattanayak</td>
<td>2007</td>
<td>Insider ownership has non-linear relationship with</td>
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<td>Douma et al.</td>
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<td>Jackling et al.</td>
<td>2009</td>
<td>Greater proportion of independent directors improve firm performance.</td>
<td>Indian companies</td>
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<td>Mak et al.</td>
<td>2001</td>
<td>Significant relationship between board composition, size and firm value.</td>
<td>147 companies listed in Singapore stock exchange</td>
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<td>Board composition, leadership and size.</td>
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<td>Nicholson et al.</td>
<td>2003</td>
<td>Board size and proportion of inside directors is positively associated with firm performance.</td>
<td>348 Australian companies.</td>
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<td>Bhagat</td>
<td>2000</td>
<td>Greater board independence does not improve firm performance.</td>
<td>928 US firms for yrs 1985-93</td>
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<td>Dwivedi et al.</td>
<td>2005</td>
<td>Larger boards have positive effect on performance;</td>
<td>340 firms</td>
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<td>Ownership pattern significantly affects firm performance.</td>
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<td>Multiple directorships by independent directors correlate positively with firm value</td>
<td>500 large Indian Firms</td>
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<td>Accounting based measures not associated with board characteristics but market based measures showed significant difference between high ranked and low ranked firms on basis of board characteristics.</td>
<td>Adjaond et.al 2007</td>
<td>Large Canadian firms</td>
<td>ROI, ROE, EPS, MVA,EVA</td>
<td>Board composition, compensation, disclosures and shareholder rights.</td>
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<td>Inverse relationship between board size and firm performance.</td>
<td>Mak et.al 2005</td>
<td>230 firms listed in KLSE and 230 firms listed on SGX</td>
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Endnotes:


