CHAPTER-III

CORPORATE GOVERNANCE AND
GLOBALIZATION
CHAPTER-III

CORPORATE GOVERNANCE AND GLOBALIZATION

The concept of corporate governance has been examined in the context of economic liberalization and globalization in India with a special emphasis on rule based and voluntarily based corporate governance. The subject of corporate governance received an unprecedented importance both in developed and developing countries owing to the assumed benefits of free market economy and the process of globalization sweeping the various economies the world over. The establishment of the World Trade Organization (WTO) in 1995 formalized the arrival of the open economy with free market forces. The new economy formalized the removal of built in protective measures in the development process.

Globalization became the new management theme in most of the developed and developing economies. The corporate sector has been compelled to adjust to the open economy by globalizing its business and reengineering its strategies, focus, and governance mechanisms. In the globalized economic environment, good corporate governance has become the necessity to establish a competitive and fair market to ensure a fair distribution of returns to the shareholders and honoring the contractual obligations of other stakeholders.

The corporate sector has been forced by the global business challenges and thrust for good governance to be the most competitive player in the national and global economies. The clarion call to the corporate sector in the globalized business environment is very clear to emerge in the new open economy by adopting improved, reorganized, and realigned business process to the free market realities or faces the consequences of retrograde business process resulting in low scale developments.
3.1 THREE CRITICAL ISSUES

Corporate governance stretches entire network of formal and informal structure of an organization. The governance of an organization requires a critical focus on issues of operations (profitability and growth), strategic decisions (long term vision and translation into annual operations), and managerial functions (accountability, transparency, and performance-oriented managerial practices). Corporate governance can be improved by focusing on these critical areas by the board. The ability to comprehend the three distinct roles and then to build a top management structure to reflect these quite distinctly and transparently assures shareholders and employees that management is clearly engaged in the legitimate business of maximizing rewards and the society in general that is being done in a socially and legally acceptable manner.

3.2 DIVERGENCE IN CAPITAL STRUCTURE (Debt and Equity Governance)

The level of governance of a corporation varies from different arrangements of corporate finance or capital structure. A significant difference between the financial structure of Corporates in developing countries and those in developed countries is that the former is far less dependent on internal finance than the latter. Indian firms depend far more heavily on external debt as a source of finance than do firms in advanced countries. Thus in India, debt governance plays a key role in a corporation.

The proportion of debt/equity is divergent under different conditions in different countries. In USA and UK, equity is dominant form of long term finance and commercial banks provide debt capital. In Japan and to a lesser extent German banks do contribute significantly towards equity stocks and part the same from parent company. A comparative proportion of financing of top 50 listed manufacturing companies in few countries reveals that there is a divergence in the financing pattern internal finance (Long term) external finance.
(equity) average external finance (long term debt) as could be seen from the following table

Table No 31 Financing of Top 50 Listed Manufacturing Companies

<table>
<thead>
<tr>
<th>Period</th>
<th>Country</th>
<th>IF (LT) %</th>
<th>EF (Equity) %</th>
<th>AVF (LTD) %</th>
<th>Change in IF %</th>
</tr>
</thead>
<tbody>
<tr>
<td>1980 87</td>
<td>Korea</td>
<td>12.8</td>
<td>40.3</td>
<td>45.4</td>
<td>7.6</td>
</tr>
<tr>
<td>1980 86</td>
<td>Pakistan</td>
<td>58.3</td>
<td>12.3</td>
<td>16.1</td>
<td>-4.6</td>
</tr>
<tr>
<td>1980 87</td>
<td>Jordan</td>
<td>5.8</td>
<td>84.1</td>
<td>16.4</td>
<td>24.1</td>
</tr>
<tr>
<td>1983 87</td>
<td>Thailand</td>
<td>17.3</td>
<td>NA</td>
<td>NA</td>
<td>23.1</td>
</tr>
<tr>
<td>1984 88</td>
<td>Mexico</td>
<td>17.1</td>
<td>76.0</td>
<td>2.9</td>
<td>14.9</td>
</tr>
<tr>
<td>1980 88</td>
<td>India</td>
<td>36.1</td>
<td>11.0</td>
<td>45.6</td>
<td>12.6</td>
</tr>
<tr>
<td>1982 87</td>
<td>Turkey</td>
<td>18.1</td>
<td>60.5</td>
<td>15.5</td>
<td>13.2</td>
</tr>
<tr>
<td>1983 87</td>
<td>Malaysia</td>
<td>42.4</td>
<td>31.4</td>
<td>2.1</td>
<td>7.7</td>
</tr>
<tr>
<td>1980 88</td>
<td>Zimbabwe</td>
<td>58.5</td>
<td>43.0</td>
<td>0</td>
<td>16.8</td>
</tr>
</tbody>
</table>


Note

a) Average values for the relevant period for each country

b) Percentage point changes from the average of the first two years to the Average of last two years of the period

IF = Internal Finance (Long Term)    EF = External Finance
AVF=Average External Finance    LTD = Long Term Debt

During 1991-99 periods the RBI data on Indian medium and large companies suggests that on an average internal finance contributed about 33% of total funds and external finance 67%. During 1981-1993 periods Indian companies financing pattern indicated that internal finance accounted at 37.6% external debt at 20.4% and external equity at 4.5% as against US companies financing pattern internal finance at 51% external debt at 9.8% and external equity at 4% during 1972-1992 period.

Worldwide the capital structure has contributed to the level of governance in the company. The expectations of the contributors of capital or their power mechanism over the company affairs varied from country to country. In USA and UK power is exercised through exit (i.e., withdrawing of funds even if there is a
liquidation of a company) In Japan banks are concerned to steer long term strategy of the organization and to use their power to have their voice heard. Foreign capital entered Korea for reasons of mobility and profit motivation fully aware that corporate governance in Korea was inadequate—and ultimately left for the same reasons When growth slowed and risks from poor corporate governance outweighed profitability foreign investors pulled out.

On the basis of data collected from sample companies in India the debt equity ratio is analyzed during the periods 1998-2002. The companies having no debt accounted at 18%. One hundred forty-eight companies (56.71%) were placed in debt equity ratio up to 1.00. Thirty-nine companies (15%) were placed in debt equity ratio between 1.2. Forty-four companies (17%) were placed in the debt equity ratio of 2.5 and thirty companies (11%) were placed above 5. The following table and graph indicate that 39% of small, 14% of medium and 19% of large companies were placed in debt equity ratio up to 2.00 accounting an aggregate of 72% of sample companies. This data is supporting the fact that the Indian companies depend heavily on debt financing.

Table No 3.2 Debt Equity Ratio of Sample Companies

<table>
<thead>
<tr>
<th>Ranges in Δ</th>
<th>Small</th>
<th>Medium</th>
<th>Large</th>
<th>Total</th>
<th>(%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Zero Debt</td>
<td>31 (11.88)</td>
<td>8 (3.07)</td>
<td>8 (3.07)</td>
<td>47 (18.01)</td>
<td></td>
</tr>
<tr>
<td>Up To 1</td>
<td>47 (18.01)</td>
<td>22 (8.43)</td>
<td>32 (12.26)</td>
<td>101 (38.70)</td>
<td></td>
</tr>
<tr>
<td>Between 1.01 To 2.00</td>
<td>23 (8.81)</td>
<td>6 (2.30)</td>
<td>10 (3.83)</td>
<td>39 (14.94)</td>
<td></td>
</tr>
<tr>
<td>Between 2.01 To 5.00</td>
<td>19 (7.28)</td>
<td>13 (4.98)</td>
<td>12 (4.60)</td>
<td>44 (16.86)</td>
<td></td>
</tr>
<tr>
<td>Above 5.00</td>
<td>11 (4.21)</td>
<td>6 (2.30)</td>
<td>13 (4.98)</td>
<td>30 (11.49)</td>
<td></td>
</tr>
<tr>
<td>TOTAL (%)</td>
<td>131 (48.28)</td>
<td>55 (21.07)</td>
<td>75 (30.65)</td>
<td>261 (100)</td>
<td></td>
</tr>
</tbody>
</table>
The effect of higher debt equity ratio is significant on the overall profitability accumulation of reserves and dividend paying capabilities of the company. High debt portion in a capital structure results in more outflow of borrowing cost which in turn reduces the profits of a company. The earnings to the ultimate risk takers of the corporate also get reduced as a consequence of high borrowing cost.

3.3 CORPORATE GOVERNANCE A DYNAMIC CONCEPT

Since there is a direct relation between the level of governance and capital structure of a company and falling in line with the objectives of this study, a close examination of multi-dimensional aspects of corporate governance concept is inevitable.

The concept of corporate governance is a dynamic one encompassing the changes taking place in economic environment, legislative framework and composition of the capital structure in the corporation. At the basic level corporate governance models are classified as the insider model which is found in OECD countries characterized by concentrated shareholdings that may help to keep the incumbent management in place and outsider model which prevails in US and the UK which predominantly relied on the equity market to finance enterprises.6
The Cadbury Committee (1992) defined corporate governance as *the system by which companies are directed and controlled*. The boards of directors are responsible for the governance of their companies. The shareholders' role in governance is to appoint the directors and the auditors and to satisfy themselves that an appropriate governance structure is in place. The responsibilities of the board include setting the company's strategic aims, providing leadership to put them into effect, supervising the management of the business, and reporting to the shareholders on their stewardship. The board's actions are subject to laws, regulations, and the shareholders in general meeting.

The analysis of this definition reveals that corporate governance is the system and therefore everyone forming a part of the system is in fact contributing to the corporate governance. The accounting profession is an important part of that system. The auditors forming an integral part of the accounting profession are not having an executive role in corporate governance except the role of oversight and attest function of examination of records and giving an assurance on the credibility of records of performance and financial information mainly to the shareholders of the company and other users of such information. The system referred to in the Cadbury Committee definition of corporate governance includes the board of directors, shareholders, supervisory management, regulators, and other external stakeholders as players of the company. The system contemplates the best interest of the company and the stakeholders by practicing good governance. In this endeavor, organizational structure and processes employed are very much significant. The corporate governance includes certain structural organizational aspects; the process that charts how things are done within such structure and organizational systems.

The system referred in Cadbury Committee definition include laws, procedures, practices, and implicit rules that determine the company's ability to take managerial decisions vis-à-vis its stakeholders. The board and executive management are under an obligation to run the company with greater accountability, transparency, and fair disclosure with a view to determine the directions and attain desired level of business performance. While running the...
company, the board and executive management is duty bound to comply with the laws, standing orders, internal rules, governance codes to see that the ultimate interest of the risk takers of the company (the shareholders) and other stakeholders are protected. The board’s actions are subject to the approval of the shareholders in the annual general meeting. These aspects are the requirements of corporate governance in terms of the Cadbury Committee definition. Thus, the imperatives of corporate governance flow from the concept of accountability for the safety and performance of assets and resources entrusted to the operating team.

3.4 PROFESSIONAL MANAGEMENT

The ultimate requirement of the system of directing and controlling a company is to achieve long-term strategic goals to satisfy shareholders, suppliers, lenders, employees, customers, the regulators, and the society. When this requirement is practiced under a well-laid-out system, it leads to building of a legal, commercial, and institutional framework and demarcates the boundaries within which these functions are performed.

The function of direction and control underlines the need for professionalism in management. The right mix of people with right resources under a well-guarded governance mechanism with external checks by the auditors would lead to a better performance of the company. The achievement of long-term strategic goals to satisfy stakeholders requires professional managers over family-based managers in corporate governance. It has been proved globally that the professional management of a company does matter in ensuring better performance and thereby ensuring higher value to the shareholders. The analysis of secondary data reveals an interesting aspect of top 50 business families in India.

Business Today Magazine conducted an exhaustive study of top 50 business families in India to find out the strategic response from family managed business houses on the factors of core competence required to survive in the
next 50 years the competitiveness of family business to withstand global competition etc. The study revealed the perceptions on the quality of professional management in family managed business houses. The responses are family owned companies are the least preferred employers, career development is uncertain in family owned companies, business families strategize by lobbying for protection, the level of transparency in business house is below average and family businesses compare poorly on leadership qualities. This study also highlighted the significance of professional management in the top 50 business houses managed by family members with a view to survive in the next 50 years by redefining their strategies, technology, and leadership roles etc.

3.5 TRUSTEESHIP PRINCIPLE

Corporate governance in its widest sense is almost like a trusteeship. Corporate governance is not simply creating checks and balances; it is about creating an outperforming organization which leads to increasing customers satisfaction and shareholders value. Corporate governance is one of the principles of governance. The board and management are under trusteeship for the shareholders of the company. Breach of trusteeship has led to misgovernance on the part of the board and the management. Mahatma Gandhi propounded the principle of corporate governance in the early 20th century when he said that the businessmen are trustees of the wealth generated by business. Peter Ducker expanded this thought when he advocated that the company’s management is a trustee—accountable to no single group of shareholders or stockholders. They emphasized the concept of trusteeship in respect of management of fund of others. In a corporate structure where the ownership and the management is divorced, these principles apply with greater force and importance. The essence of good corporate governance is to achieve the right balance between the shareholders and management interests which also requires accountability, cordial relationship between the board and company’s stakeholders without distorting the function of trust and equity.
3.6 MAXIMUM GOVERNANCE TOOL – A VOLUNTARY CODE

The system of directing and controlling must be strong enough to consider the implicit need for humane governance in the form of more humane, more stable, more just ways of functioning, more of culture driven with credible means. The canons of good governance—accountability, transparency, trusteeship, fair disclosure, professional approach, balanced judgment towards stakeholders, etc.—underline the significance of ethical agenda of the board and chief executive officer while dealing with corporate responsibilities towards all the stakeholders more particularly the society at large. Any system without having deep root in ethical agenda would not last in the long run. The value system being the cornerstone of ethical agenda is very much significant in the governance mechanism. In management of a business successfully value system adopted is an important factor and plays a significant role according to the masters of the art of management.

Any extent of statute-based governance system would not result in maximizing governance value in the organization. The law states minimum standards of conduct. The maximum must come from the corporate organization itself, its players, management and leaders. Thus the implicit aspect of the Cadbury Committee definition is visible in the form of ethical agenda. Corporate governance is a way of life and not a set of rules. A way of life that necessitates taking into account the shareholders' interests in every business decision. The concept is against concentration of powers, wealth, and imbalanced approach towards the stakeholders of a company. Corporate governance sans entrepreneurial ethos, business ethics, and a perceptible attitudinal change.

Laws are not enough to guarantee good corporate governance. Human ingenuity is so phenomenal that people find ways to beat any system. What we need is an inner value system—a belief that translucence and deceit will not pay. We must know that knowledge economy has changed the world. Earlier companies made money by not informing people. Today you make money by
informing people. The answer is to have courage to own your failures and share them with shareholders. Transparency cannot be achieved without courage. In the innovative economy of today, you cannot have all the shots right succeed all the time. The problem is our education system and training does not prepare us to handle failures and turn them to our advantage. Owning failure is what gives you strength. Disowning failures is a recipe for disaster.

The voluntary code of corporate governance overrides the statute based corporate governance code. The experts on the subject have come to a general opinion that voluntary code of corporate governance with minimal rule based governance is ideally suited to ensure effective governance to various stakeholders. It underlines the need for practicing corporate democracy by all the stakeholders and the corporate itself. The compliance with corporate governance practices must come from every individual and department as a way of life. The force of law must sparingly enforce it. Self governance by companies is highly acceptable as a credible mechanism to punish corporate bad behavior and little supplementation by external statutory regulations. An ideal combination of governance mechanism i.e., more by self governance and less by external statutory regulations in the changing economic environment is the requirement of the day in the corporate sector.

In order to develop long lasting vibrant self regulated company, the board of directors is required to give importance to self governance mechanism with high value system which is again implicit in the definition of corporate governance in terms of Cadbury Committee.

The data from the study points out that 63 respondents have preferred rule based governance module (24%). None of the respondents have suggested only voluntary based module of governance. 198 respondents out of 261 have preferred a combination of rule based and voluntary based module of governance. The analysis of this data indicates that the governance module should never be fully voluntary based. The respondents have indicated minimal extent of rule-based governance.
can be concluded that a combination of rule based and voluntary based governance module is preferred by the majority respondents (more than 75%).

3.7 WELL FUNCTIONING BOARD

Good governance is linked with the quality of governing organ i.e. the board of directors. The board's role in giving a credible value-based organization to maximize shareholders' value is important. The reviewed literature revealed that for ensuring well-functioning boards, a proper balance between members of executive board and non-executive board with independence of board members is critical. The committee structure of governance is also a key factor in ensuring well-functioning of the board. A well-functioning board will have insights and foresights about the company's performance and its timely review with utmost importance of highest executive responsibility in the company. The chairman's role in securing well-functioning boards and thereby assuring good corporate governance is very much crucial. Further, a well-functioning board must accept change as an opportunity for the growth of the company without any reservations.

The findings from the study reveal that suitable nature of board members must be from professional directors category. Further, it shows that Non-Executive Directors (NED) must be appointed purely on merit. More than 60% of the respondents clearly vouch this view and the same gets support from the result of statistical tool as significant. The data also reveals that the non-executive directors must be on rotation system over a period of 2 years. The threat of non-performance and losing the position at the end of fixed term would sensitize NED towards performance track. The ceiling on directorship in case of a director must be 5 companies at the most. Lesser companies' directorship would ensure timely involvement and evaluation of company's performance. This is another finding from the data collected. Further, the study showed an interesting aspect on the powers of the board. 74% of the respondents stated that power lies with the board as a collective body. By publication of director's...
responsibility statement in the annual reports the shareholders and other stakeholders would get a proper view on the directors responsibilities in the company. The study reveals the requirement for the well functioning of the board in the company.

3.8 FRAUD - FREE GOVERNANCE

The system of directing and control of a company must ensure fraud free governance. The board must not act as a destroyer of wealth as against the agenda of creators of wealth in terms of shareholders expectations. Recently some companies with mounting scandals and frauds have lost credibility in the minds of investors. The happening of corporate frauds has demoralized the investors community. This has halted further capital mobility to the development of a corporate sector. Thus fraud free governance is the top most agenda of every corporate in today’s context.

No system of corporate governance can be totally free from fraud or incompetence. The test is how such aberrations can be discouraged and how quickly they can be brought to light. Making the participants in the governance process as effectively accountable as possible can reduce the impact of risks. The key safeguards are properly constituted boards, separation of functions of chairman and of chief executive audit committee, vigilant shareholders, and sound financial reporting and auditing systems which provide full and timely disclosure to the stakeholders.

The American practice of corporate governance focused only on creation of shareholders wealth. This suited the CEOs eminently. It was so easy to emulate earnings and profits. It is not so easy to satisfy all stakeholders of the corporation. The practice of creating accounting is not novel. It dates back at least to the boom of 1990s. It is universally accepted that over a long period profits growth should be in line with GDP growth. Yet in the 1990s reported profits grew much faster than GDP growth. Indeed this was also a period when related earnings proportion was much higher than dividends. So CEOs had a lot...
more cash which went into mergers and acquisitions which in turn was used by CEOs to pay themselves large remunerations and stock options on the grounds they were bigger companies and bigger risks. Throughout the 1990s while average CEO's pay rose by almost 30% annually to several million dollars a year employee wages stagnated at less than 1% of this amount turning corporate governance to corporate greed. Our aim was to reverse the process. Make employees and other stakeholders part of the process in corporate governance and make decision making more transparent, accountable and equitable. Creation of wealth from the stakeholders viewpoint made sense in other ways too.

The recent survey conducted by the Invest India Economic Foundations (IIEF) reveals shocking results that only 6% of the respondents were confident that SEBI would protect them against frauds. The rest 94% obviously have no faith in SEBI. The survey contacted 1832 individuals from 106 districts across India. The IIEF however said that data does not represent India even as could at the best be an eye opener for the future.

3.9 CORPORATE SOCIAL RESPONSIBILITY

The society is one of principal stakeholders in the corporate. The Corporate is required to take various business decisions with a view to ensure social corporate governance. Social corporate governance requires adherence to good corporate governance which will help to reinforce the confidence of the investors and gradually supply stable flow of capital. The healthy economy is possible with healthy functioning of companies which contribute to the GDP in a sizeable manner.

Modern business enterprise is considered as one of the instruments available to a country for material and social transformation of the society just as much as other sectors viz agriculture, mineral and infrastructure development. The planners in most democratic and developing countries have mentioned a variety of development objectives for the countries namely (a) Increase in per
capita income (b) improvement in quality of life (c) development of backward regions (d) increase in employment opportunities (e) maintaining price stability (f) reduction in inequalities of income and facilities (g) hold the deposit of adequate foreign exchange reserve. The company is considered as a guardian for the resources entrusted to it therefore good governance by the company with proper performance and accountability is the call from the society. The company's contribution to the society is increasing in the changed perception about the company by the society in general.

Corporate sector had contributed in different ways to social causes through philanthropic and charitable actions. While the motivations may have been varied, there appears to be an increasing tendency for the corporate sector to give back to the society through a social code for business.

3.10 GOOD CORPORATE GOVERNANCE

Corporate governance has many static and dynamic aspects. Successful corporate governance lies in balancing the various conflicting interests and interest groups known as multi stakeholders of the company.

Good corporate governance is an instrument for both economic and social transformation of a corporate. The board of directors ought to balance the interest of capital providers with those of other stakeholders and aim for a long term and sustained business success. As the Enron debacle indicates a good corporate code is no guarantee of good corporate governance. There must be strict monitoring and enforcement of law on the punishment of those who involve in corporate scams and violate public trust. The law must be amended to meet out swift and deterrent punishment to the offenders. Expeditious and cost-effective resolution of commercial dispute is an integral part of good corporate governance. A primary goal of good corporate governance ought to be to foster a culture of creativity, innovations, and entrepreneurship to protect the business from irrelevance and obsolescence. It should aim to leverage the intellectual capital to serve the unarticulated customers and untapped markets. Corporate governance is the market mechanism in protecting investors' rights most...
effectively it is also necessary to secure a stable supply of long term capital essential for sustained growth

The board and executive management is required to know the ill effects of poor corporate governance which not only inflates uncertainty but also hampers the application of appropriate remedies for the crisis

There is a global consensus about the objective of good corporate governance i.e. maximizing long term shareholders value. The corporate governance deals with an economic, legal and institutional environment that allows the companies to grow and restructure to do such other acts which will maximize long term shareholders value. Maximization of shareholders value ensures to maximization of returns to other stakeholders.

The success of good governance system reflects the efforts of top management in institutionalizing the corporate governance. The board is required to look beyond governance and take care of all the stakeholders in a friendly and receptive manner as a long term strategy. The attitudes of simplicity, responsiveness and high rate of empathy for others must be practiced by the corporate leaders as an opportunity to serve the society above self through a company which is being led by them. The human satisfaction is the utmost test of true performance which could be achieved only by service above self. One must inculcate and practice the popular saying Be in line for online services to the humanity through all your endeavors.
3.11 CORPORATE GOVERNANCE DEFINED

After analyzing the multi-dimensional aspects of the concept of corporate governance and in consideration of its core principles, a wider connotation to the concept is necessary. A comprehensive definition of corporate governance incorporating multi-dimensional aspects namely corporate objectives, well-functioning of the board, responsibility of the management, the foresight of wealth creation for the benefit of all, and creating balanced and long-lasting relationship of multi-stakeholders and other aspects of the company is as follows:

Corporate Governance postulates a framework of systems, strategy, structure, process, relationship, and ethical considerations of an organization with proper checks and balances in the corporate functioning towards pursuit of creating sustainable wealth and thereby maximizing the shareholders' value without compromising the balance of interests of other stakeholders. Good corporate governance ought to create value for all stakeholders including the society.

3.12 GLOBAL GOVERNANCE IN GLOBAL ECONOMY

Global governance has assumed a renewed urgency in the global economy. The corporate sector is no exception to this phenomenon. The study of globalization is imperative in view of internationalization of the subject of corporate governance. The Zeitgeist—The Spirit of Times today dictates liberalization and globalization. Globalization is a buzzword that has launched a thousand strategies. The borderless corporation is the new phenomenon of our times. The world today boasts of 40,000 transnational corporations. Globalization refers to the growing economic interdependence among the countries as reflected in increasing cross-border flows of goods, services, capital, and know-how. The extent of interlinkages between countries, economy and the rest of the world is the essence of globalization. The exports and imports as a ratio of GDP, inward and outward flows of foreign direct investment, royalty...
payments for technology transfer sharing of brand names decentralization of manufacturing facilities in different countries and more feasible and desirable marketing network worldwide are few of the instances of globalization process

There is a greater economic integration in terms of cross border trade finance and movement of manpower technology transfer etc during the last two decades The corporate sector mainly private enterprise has emerged as a major player in the globalization process The absorptive capacity of any corporate has gone up considerably as a consequence of globalization process

The yester-years buzz world protectionism wind has gone out considerably with the advent of globalization process We live in an increasingly global world The economic landscape is not the same as it was 20 years ago nor is the pace of global economic change expected to slacken in the next 20 years On the contrary change is likely to accelerate The Corporates must understand the effects of globalization on the corporate functioning and prepare to meet the challenging opportunities of globalization

The global trading system has become more open transparent more rule based and non discretionary There are global rights and national responsibilities creating new challenges for policy makers In the fast changing business environment Corporates have been forced to rediscover corporate governance and reengineer their governance to effectively compete in the global market

Corporate governance would henceforth require greater awareness appreciation and sensitivity to the international culture and multi cultural market and also to the sensitivity of behavior of people India has no alternative but to make a decisive move towards a market oriented policy

The multinational company (MNC) is the key actor on the stage of international business It leads to globalization operating as a flagship for regional business clusters Multinational companies that produce or distribute in two or more countries dominate international production in major industries such as automobiles consumer durables chemicals pharmaceuticals electronics and
petroleum MNC can realize great economies of scale and build extensive production network globally

The world’s 500 largest MNCs are evenly scattered across the economic triad of US (162 No) the European Union (155 No) Japan (126 No) Switzerland (14 No) South Korea (13 No) and other countries (30) and compete in a wide variety of industrial sector and traded services for global market shares and profits. So global competition itself removes any possibility of sustainable excess profits. There has been an increase in standards of living and consumers have been offered a far greater choice of products and services as MNCs respond to the challenge of divergent taste with a wide range of niche products and services.

The presence of multinational companies in some countries has given impetus to operational efficiency and effective strategic decisions which to some extent are followed by other enterprises in those countries. The MNCs with their huge resource backup have followed strict norms of functioning and created their presence in the global landscape. India is one of the beneficiaries of attracting 1213 foreign companies as on 30.09.2001. The following Table & figure is indicative of increase in number of foreign companies in India during post globalization period.
Table No 3.3 Number of Foreign Companies at work in India

<table>
<thead>
<tr>
<th>As on</th>
<th>Number of Foreign Companies</th>
</tr>
</thead>
<tbody>
<tr>
<td>31 03 1994</td>
<td>565</td>
</tr>
<tr>
<td>31 03 1995</td>
<td>619</td>
</tr>
<tr>
<td>31 03 1996</td>
<td>679</td>
</tr>
<tr>
<td>31 03 1997</td>
<td>772</td>
</tr>
<tr>
<td>31 03 1998</td>
<td>871</td>
</tr>
<tr>
<td>31 03 1999</td>
<td>956</td>
</tr>
<tr>
<td>31 03 2000</td>
<td>1045</td>
</tr>
<tr>
<td>31 03 2001</td>
<td>1141</td>
</tr>
<tr>
<td>30 09 2001</td>
<td>1213</td>
</tr>
</tbody>
</table>

Source: Adapted from the website of the Department of Company Affairs, Ministry of Law and Company Affairs, Government of India, New Delhi. Data base updated as on 31 12 2001.

3.13 THE GLOBAL COMPETITION AND EMERGING MARKETS

The process of globalization resulted global level competition and creating a challenging landscape for the global players. The increased competition driven by globalization will always produce both winners and losers. It is therefore not surprising that some managers see current trends as a great threat while others view them as a challenge and an opportunity. Four forces are listed behind the
increase in global competition viz (1) Changing customers expectations (2) Preferences to technological changes (3) De regulation (4) Regional forces

External forces will continue to change the way we need to think about global competition. Technology will continue to change customers' expectations and will continue to increase and further de regulation seems to be the rule rather than exception. Successful companies will exploit the changing end user needs by keeping close contacts with a customer and understanding customer's needs is probably the best known and most repeated management mantra. Successful companies will also exploit revolutionary technologies. Although a good end user understanding is crucial to success, the process of turning market knowledge into new products is equally significant.

Global presence of the Corporates does not automatically ensure competitive advantages to them. Turning global presence into global competitive advantage requires a company to exploit the value creation opportunities generated by global presence and to meet related challenges with innovative practices and effective decisions.

To be globally competitive, a country must be blessed with two favorable factors—an unlimited reservoir of talented and skilled labour and an abundance of capital availability. A World Bank report indicated that India had both these factors in abundance. India has 5000 years of civilization behind her civilization which reached the summit of human thought in the words of Ralph Waldo Emerson. India inherited great skills and much splendor intelligence since the genes had evolved over five luminous millennia. The trader's instinct is innate in our ethos. An Indian can buy from a Jew and sell to a Scot and yet make a profit.

The international capital flows through foreign institutional investors both in Indian stock markets and industrial developments. Since the opening of Indian economy in July 1991, the corporate leaders started to look for foreign investors to reap the fruits of economic liberalization and globalization.
availability of cost effective and quality domestic labour and foreign direct investment together with transfer of technology enhanced the prospects of rapid economic growth of the Indian economy and thereby turning the Corporates as more privileged players in the emerging markets.

The FIls started to concentrate in emerging markets with increased flow of investment and placing their nominees on various company boards. The SEBI registered 225 FIls as portfolio related transaction investors as long back as 1994. The concessional taxation rates simplified registration formalities with Stock Exchange Control Boards removal of investment restrictions simplified repatriation and higher rate of return have prompted FIls to come in large number to emerging markets in a big way.

The Economies opened up are China, Indonesia, Taiwan, India, South Korea, Hong Kong, Singapore, Thailand, Poland, Portugal, and Brazil, etc. The rationale of selecting these emerging economies is a paradigm shift from the low yielding to high yielding returns on investments and assured markets. The higher rate of return in emerging economies have prompted American and Japanese investors to become active buyers in the emerging equity markets and securing better growth than that available in their own countries.

3.14 CORPORATE SECTOR AND GLOBALIZATION

Corporate sector in India is the biggest beneficiary of economic liberalization and globalization. The corporate sector being biggest beneficiary of fruits of economic liberalization and globalization cannot remain isolated in the global society. The corporate is expected to know awareness of global needs, objectives and changed business realities resulting from the process of globalization.

At the corporate level, the process of globalization and economic liberalization have redefined the mind set of corporate leaders. The strategies hitherto followed competitive edge drive for technology upgradation and
initiative to make their business on global platform with least cost of capital cost of time and transaction cost

The process of globalization at corporate sector level calls for an effective management since it is believed that the globalization results in benefits both monetary and non-monetary. It has the effect of increasing industrialization both at national and international level which in turn results in high growth.

The observation contained in the World Bank Report on global economic prospects and developing countries is worth quoting. The report establishes that globalization leads to high growth. Countries which took steps to integrate with international economy during the early 1980s and early 1990s experienced about 2% annual growth in their per capita income. Countries which were slow in integrating experienced a decline in per capita incomes.

3.15 PRE GLOBALIZATION ERA IN INDIA

The level of corporate governance was at poor state during pre-globalization period in India. The bureaucratic policy regime acted as a retrograde step in massive industrialization in India. The industry leaders were required to submit various applications to the government or competent authority for clearing the project, enhancement in capacity, change in location and product import of goods, joint venture participation, appointment of sole selling agents, broad basing manufacturing facilities for speedy distribution to the customers, etc. The process involved considerable time and cost. By the time the corporate leaders obtained clearance from the competent authority, the viability of the project was at stake. The agony of taking foreign participation for ownership and involvement of foreign institutional investors took considerable time during the pre-globalization period. The market economy was fully controlled both at entry and exit level, which demotivated specially foreign investors in taking a decisive role in Indian trade and industry. The presence of retrograde legislations for long period in India created misery for the Corporates in speedy implementation of their projects.
Due to rigid controls during pre globalization period the competitiveness of corporate sector got compromised to a great extent. The corporate sector restricted its operation mainly in domestic market excepting few companies in export and import business. The levels of transparency, fair disclosure, high technology orientation and professionalism in management were not on par with global standards which ultimately compromised the Indian corporate sectors growth in the global economy. The reforms introduced during this period did not motivate the foreign players and multinational companies to establish strategic relations with companies in India which also led to restricted area of operation for the Indian companies.

3.16 POST GLOBALIZATION ERA AND NEED FOR GOOD GOVERNANCE

The post economic liberalization and globalization policies from July 1991 revealed that the Indian companies have opted for International operations due to foreign markets flow of foreign direct investment, sharing technical know how, expansion of distribution network, formation of strategic alliance with multinational companies and internationalization of manufacturing facilities and brands etc. The protective shield which prevailed before July 1991 was pierced.

Developing global thinking which lays importance on sharing information, knowledge and experience across national, functional and business boundaries is a must in global mindset. Facilitating global leadership is also a key feature of global mindset.

The thrust for good governance assumed importance for the Corporates going for globalization of their economic activity and to be in the competitive edge over others. The Corporates have started to focus on competitive strategies with optimum utilization of economic resources and started to adopt value or cost based strategies with a view to maximize profit. Moreover, high risk of economic exposure started to receive top attention of the Corporates leaders. The engine of globalization has put the right track to the Corporates in garnering the

\[ t - 6475 \]
business activities in a more focused and professional way. Similarly, exposure to international laws, multi-trade practices, manner of conducting international trade, lessons from foreign trade, and consequences of breach of international trade laws, etc., have redefined the corporate business strategies in the post-globalization period.

The post-globalization period in India gave impetus to adopt and practice good corporate governance since leading Corporates began to source foreign capital by listing their stocks in international stock exchanges, acquire units in different countries out of foreign capital, etc. The corporate was compelled to alter the board composition, appoint professional managers, improvise disclosure requirements, disclose financial information as per the requirements of GAAP, and get the accounts audited by independent auditors to suit the global requirements of due diligence by the Foreign Institutional Investors (FII). The demanding complex and challenging globalization process has compelled the corporate sector in India to reorganize themselves on line with global governance standards.

The post-globalized economic activity of corporate sector in India attracted talented professional managers to take up the challenging tasks and convert the challenges of globalization into a real-time success story. The attitude towards openness, effective and efficient performance, transparency in business operations, and high rate of accountability has slowly changed the mindset of top professionals in the Corporates of emerging economies. The regime of takeovers and mergers has focused more on governance mechanism.

The most glaring technological innovation is the advent of information technology, which has created a virtual world. Advancement in cost-effective communication due to information technology has enabled the corporate sector in India to establish links for procurement of resources, technology, and manpower sourcing in no time. The integration of global economy has been at a faster rate during the IT revolution period, which again called for improved governance systems in the corporate functioning.
The globalization process paved a way for global consciousness in the minds of global people. The aspect of social responsibility of corporate came into forefront in the global environment. The corporate owes a responsibility towards the human race in protecting global environment, supply of need-based products and services, and playing a rightful role as a major beneficiary from the global society resources. The corporate should know very well that good health, good nutrition, good education, and good living conditions would go a long way in nurturing human race besides the requirement of peace. The corporate is under obligation to perform this extended role towards the community at large under the guise of community support from the leaders of the economic activity.

The sole objective of profit maximization of an economic activity should not be achieved at the cost of social objective of ensuring social accountability towards the human race. The profit maximization and social accountability are just two faces of the same coin which should be properly devised and performed in a balanced manner. Thus, the corporate is required to ensure good governance and equity in the global society with well-thought-out and practiced values in an objective manner and with social consciousness. It is said that social concern should also be the hallmark of an economic activity. The emergence of a global society is a process which cannot be reversed and will indeed gather momentum and move progressively towards a global consciousness.

The expectations of the stakeholders from the corporate underwent a sea change owing to globalized economic activity. The global stakeholders namely FIIs, foreign banks, venture capitalists, foreign governments, foreign regulatory bodies, including Ambassadors/Diplomats, and foreign companies, world economic forums, Human Rights Commission, and others started to become active players in globalized Corporates. The board and executive management's role of accountability and transparency in dealings have got extended to the...
global horizon as a result of globalized economic activity. This has led to the improvement in governance systems to a reasonable extent.

3.18 GLOBAL BUSINESS CHALLENGES

The advent of global economic activity has thrown open new challenges to the business and industry run by corporate sector in emerging economies including India. The changes in the form of technology management practices, supply chain and deliver mechanism, innovative ways of funding the business activity, business process outsourcing on cost effective considerations, etc. have forced the corporate leaders to redefine their corporate strategies to suit international practices.

The new challenges are increased customers' focus of demanding proven quality goods and services at a competitive rate, increased role of private initiative over slashed control regime of the government and thereby calling for sizeable financial resources to meet the expectations of globalized economic activity demanding increased investment on technological upgradation including information technology under the pressure of cost competitiveness and vanishing opportunities in the event delayed or failure to act quickly. Emergence of global players from Asian region purely on the parameters of low cost of labour, high skilled man power and hard working attitude, the availability of global finance only to competitive, good governed and well performing corporate players to finance their ambitious takeovers, mergers and strategic alliances, etc. changed paradigm of shifting domestic competition to the global competitive positioning with pressure on higher productivity and adhering to schedules of delivery of goods and increased presence of world renowned tech management and institutions calling for a sizeable investment from corporate sector with the objective of developing the human capital.

These new challenges clearly call for good corporate governance practices by corporate sector in India to withstand the global economic activity requirements and global governance practices in the long run. It appears that the
process of globalization has at least brought about rethinking on good corporate governance in corporate sector in India. The initiatives of CII and SEBI have just started a long marching journey towards good corporate governance practices in India.

3.19 RESPONSE TO CHANGES

The Corporates are required to respond to the changes effectively and redefine their strategies both at national and at international levels. The Corporates are bound to adopt the cannons of good governance in right earnest if at all the changes in the global environment are to be used as an opportunity. The business virtues of imagination, flair, ingenuity, and boldness are required to be practiced by the corporate leaders to be on the forefront in the global economy. The Corporates are required to steer towards further excellence in standards of governance by improving competitiveness. The complex environment of today is full of changes restructuring, reorganizing, and realignment to make a corporate a versatile in its functioning. The corporate leaders must read the change and lead the change for the better of today and tomorrow. They must accept the fact that change is inevitable in the changed economic conditions.

---
### End Notes And References

1. Business India (1997) *IC Chairman’s Statement in the AGM held on 24 07 1997
7. Iyer L V V (1997) *Corporate Governance Some Thoughts* *The Hindu dated 12th February*
14. Mathur S B (1997) *Corporate Governance Concept and Issues* *Chartered Secretary* May pp 120 121
15. Parekh D (1997) *Corporate Governance and Business Ethics* All India Management Assn New Delhi p 15


20 Deccan Herald dtd 25 10 2002 p 13


22 Corporate Social Responsibility (2001) South Asian Conference Material organized by CII at New Delhi on 11 12 Sept 2001 published by SAARC News Letter Sept Oct 2001 p 8 Social code demanding business people to act with sense of responsibility and take carefull account of the social moral and environmental consequences of the enterprise and the effect that it has on the safety and well being of the community It was providing goods and services to the community beyond the call of booty and profit


26 Narang S P (1997) Evolution of Corporate governance in India Chartered Secretary New Delhi May pp 135 141


31 Private sector investment in India during April 1998 accounted at 57.6% of investment in all industries 51.5% in April 1999 48.6% in April 2000 47.7% in April 2001 and 46.8% in October 2001 – Survey of investment projects published by CMIE Foreign collaborations approved increased from 528 in 1980 to 950 in 1991 from 1520 in 1992 to 2144 during 2000 In terms of foreign investment from Rs 9 Cr in 1980 to Rs 534 Cr in 1991 Rs 3888 Cr in 1992 to Rs 37040 Cr in 2000 Out of these investments corporate sector in India has emerged as major player during post economic liberalization and globalization period Employment generated during 1981 has gone up from 73.95 lakhs to 89.98 lakhs during 1999 owing to increased investment activity Department of Economics and Statistics Statistical Outline of India (2001 02) Tata Services Ltd Mumbai pp 165 172