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AN IMPACT OF CORPORATE GOVERNANCE ON FINANCIAL PERFORMANCE OF SELECTED NON-FINANCIAL COMPANIES

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ABSTRACT

In corporate world, Corporate Governance is the new buzz in the present days. It is established as one of the moral duty, it involves the promotion of ethical law in letter and demonstrating and show such spirit in conduct. The association of Corporate Governance and Financial Performance has been widely discussed by the scholars and researchers from the last decade. So many researchers have put themselves in such exploration to examine the linkage between these two but not reached to the conclusive evidence. The outcome of the present study is mixed. In this study, it has been attempted to search out the impact of corporate governance on financial performance of corporate from Indian context, there has been collected 20 companies as sample, listed on S&P CNX Nifty 50 index. Number of various test like, correlation, regression, t-test and F-Test have been applied by using secondary data over a period of two years from financial year 2017 – 2018 to 2018 – 2019 to examine the said association. Size of firm has also been controlled in the study. It has been observed that rating of government has significant and positive impact on corporate financial performance. As observed in so many researches, there are also certain limitation in the present study, which should be discussed or considered at the time of using the result of this study and the future researchers should attempt to overcome these limitations.

KEYWORDS
corporate governance, financial performance, stakeholder relation, value creation.

JEL CODES
G30, G31, G32, G34.

INTRODUCTION
The term 'Corporate Governance', suggests the extent to which companies are govern in an honest and open manner. The committee from UK, named 'The Cadbury Committee' (2002) defined the corporate governance concept as the system by which firm are run, controlled and directed. The true corporate governance lies in promoting accountability and transparency and fulfilling the valid expectations of all the stakeholders. Corporate Governance is the procedure, system of tool that helps to accomplish such goals and to secure the objectives of the group of Stakeholders. It involves the promotion of ethical law in letter and demonstrating and show such spirit in conduct. Corporate Governance and its framework inspires effective application of resources and also demand accountability for the stewardship of those available resources.

There are three important key constituents of Corporate Governance are Management, Board of Directors and Shareholders of the company. Corporate Governance and its area has demanded very serious attention of the last decade because of various remarkable scandals of corporate and collapses such as WorldCom, Enron and Satyam etc. due to involvement of unethical practices in Business. It has been often remarked that value creation and corporate governance preserve hand in hand. If the corporate does not embrace and demonstrate ethical practices of conduct, it will not be able to get success. So many researchers have made study to examine the association between financial performance and corporate governance, but unfortunately the outcome inconclusive and mixed. In the present study, it has been attempted to examine and analyze the impact of corporate governance on financial performance of the firm from an Indian context.

COMPONENTS OF CORPORATE GOVERNANCE
A. SIZE OF BOARD: It is very strongly believed that size of the board has positive impact on firm performance; which is generally detected to be significant.
B. INDEPENDENCE OF BOARD FROM MANAGEMENT: The independent directors play as a guide to the company. It is believed that their role is important to governance standards and corporate credibility, and it helps in monitoring and advertising the company management.
C. DIFFERENTIATE ROLE OF CEO AND CHAIRMAN: Conflict of interest, concentration of power and reduced board independence are usually observed when the roles of CEO and Chairman of the board are exercised by the same individual.
D. DIRECTORS' FINANCIAL EXPERTISE: Director must acquire financial literacy, so that will help the director to better understand the implication of decisions which has been taken by the management and that will direct towards better and effective controlling.
E. BOARDS MEETINGS: It should be required that sufficient number of meetings were held in a year. Very hard to find lack of interest from the part of the Board in meeting, and on the other hand too frequent meeting in the company indicate some problems.
F. EXTERNAL AUDITORS' ROLE: The External Auditor should be competent and have enough independence to notice and report manipulations and frauds in corporate reports. Simultaneous establishment for both audit and non-audit services by external auditors affects effectiveness of audit. Fees amount of Audit is also relevant.
G. THE BOARD COMMITTEE: The Committee of Board add effectiveness to the board by performing and exercising healthy control over the decisions of management which includes:

- **Audit Committee:** The very remarkable Corporate Scandals have demanded the heightened effective audit committee. Audit committee and its independence and frequent meetings can ensure creditability of the report of Corporate.
- **Remuneration Committee:** A remuneration committee of board helps in taking decision the suitable remuneration for the higher level executives of the company like CEO.
- **Committee of nomination:** The Committee of nomination assesses the knowledge, skills and needed expertise to become a director and scrutinize the most suitable candidates.

REVIEW OF LITERATURE

I) THEORETICAL PERSPECTIVES

The huge number of research has examined the correlation between corporate governance and financial performance, in which many studies suggested positive relationship.

In corporate governance, Board of Director measured very useful factors which impact a whole business and all interested parties. The question is that "what is the characteristic of board of directors and how it impact on performance of the firm" has attracted significant attention from researcher and interested parties over the last so many years.

(**Zahra and Pearce) 1989,** in their research, it is explain that the role of board of director in company financial performance by producing and reviewing 4 perspectives.

A. agency theory B. class hegemony C. logistic and D. resource dependence.

II) EMPIRICAL STUDIES

Brown and Caylor (2004) has found composition of board was very important factor among all factors of Corporate Governance Quotient (CGO). In their research they found positive association between Corporate Governance Quotient (CGO) and financial performance measures like profitability, dividend payout, shareholder returns, and yield. **Van De Velde et al. (2005)** determine the relationship between corporate governance Rating and firm financial performance and found positive but not significant relationship between them. **Van De Velde** statement is consistent with the finding of **Gompers et al. (2003)** they determined that shareholder rights enjoy higher firm value, profit and sales growth because firm has strong governance structure. **Governance Metrics International and Byun (2006)** has investigated in their study about the association between financial performance and Corporate Governance and conclude that the companies which are rated the top 10% of GMI's global database achieved a best ROA, ROE and ROC (Return on Capital) than the companies which are in bottom of 10%. **Upton & Selvaggi, (2008)** has found that the firms which are better governed, yield higher return with risk adjusted. A strong point they have emphasized that enrichment of corporate governance is the reason behind the enrichment performance and not vice-versa. But somehow, **Statman & Gluskov** and **Core et Al. (2008)** failed to establish significant association between financial performance and corporate governance. 'Structural Equation Modeling' (SEM) has been used by **Azim (2012)** and analyzed that mechanism of some corporate governance have positive covariance whereas some other have negative co-variance. So that, he failed to find out the significant association between financial performance and mechanism of governance (as it is peroxided by ROA, ROE, Price Earnings Ratio, Market to Book value ration and Dividend Yield). So that, it has been observed that few existing studies suggest significant and positive association; and in some it has been found positive but irrelevant association; and some studies completely failed to established significant association between financial performance and corporate governance. Thus, present reviews clear mixed and inconclusive outcome, and so that, the topic need empirical inspection to be done in this context to reach at significant and conclusive outcome.

OBJECTIVES OF THE STUDY

This research paper focus on the following objectives:

- To provide an overview of various components of corporate governance;
- To provide literature review on the relationship between corporate governance and corporate financial performance; and
- To examine the impact of corporate governance on financial performance of firm in Indian context through multiple regression, correlation, t-test and F-test.

HYPOTHESIS

Based on above theoretical arguments and reviews of literature, the following hypothesis has been framed:

[Null Hypothesis] H_o: There is no impact of government rating on company's financial performance.

[Alternate Hypothesis] H_1: There is positive impact of government rating on company's financial performance.

RESEARCH METHODOLOGY

Several tests are conducted like – correlation, multiple regression, F- test and t-test have been implemented using IBM- SPSS statistic software to examine the impact of corporate governance and financial performance with the help of secondary and cross- sectional data. For examine, the impact average of two year data from 2017-2018 to 2018-2019 has been used for analysis.

SAMPLE SELECTION

There has been included sample of 20 Indian non-financial companies, which are listed on the NSE; companies have continuously been incorporated in NIFTY 50 Index during 1st April, 2017 to 31st March, 2019, with the help of data availability of required financial and governance ratings ; and which have minimum once issued CSR/Sustainability Report as per GRI guidelines.

DATA SOURCES & VARIABLE DESCRIPTION

There are four numbers of Accounting Based Measure, Return on Capital Employed (ROCE), Return on Equity (ROE), Return on Assets (ROA) and Profit before Tax (PBT) have been applied as proxies for financial performance. Such measures tools of financial performance has been selected due to the audited data of accounting tends to available fair and true view of company and it is not affected by perceptions of market and is thus considered less strident in comparison to market centered indicators like price of share, return of stock etc. **[Loez et Al – 2007]**. The companies' ratings of governance have been applied as proxy for the performance of corporate governance. There has been control for employee related, community related and environmental performance of companies which has been likely to influence companies' governance. There has also been control for size of company by using Natural Log of Total Assets. 'Moneycontrol.Com' website has helped to get the data for study. The community, governance, environmental ratings and employee data have been obtained from 'CSRHub Database', it has been titled to be one of the best largest corporate sustainability ratings database and principally adheres to the guidelines of GRI. The rating of company governance from CSRHub include mainly three indicators Leadership ethics, Board and Reporting & Transparency.

RESEARCH MODEL

Impact of Governance rating of firm (GOV- Independent Variable) has been studied on the financial performance of firm (ROE, ROA ROCE & PBT – Dependent Variable); at the time of controlling for size of firm (SIZE) and its performance along Environmental Dimensional (ENV), Employees Related (EMP) and Community Related (COM). In this study, four equations have been applied for analysis:

ROA = a + d1.GOV + d2.EMP + d3.ENV + d4.COM + d5.SIZE (I)

ROE = a + d1.GOV + d2.EMP + d3.ENV + d4.COM + d5.SIZE (II)

ROCE = a + d1.GOV + d2.EMP + d3.ENV + d4.COM + d5.SIZE (III)

PBT = a + d1.GOV + d2.EMP + d3.ENV + d4.COM + d5.SIZE (IV)

DATA ANALYSIS & INTERPRETATION

Used descriptive statistical variables have been shown in table no. 1 below.

TABLE 1: DESCRIPTIVE STATISTICS

Particulars	ROA (%)	ROE (%)	ROCE (%)	PBT (in Rs. Cr.)	GOV (%)
Mean	17.925	19.430	25.563	8135.417	49.83
Median	12.221	14.093	16.789	5557.093	50.75
Std. Dev.	11.036	16.517	24.029	8168.097	8.604
Observations	20	20	20	20	20

(**Source: researcher own calculation**)

From Table: 1, it has been observed that the mean value of Governance ratings is only about 49.83%, and it is less than 50%. It suggests the need to improve the governance structure of Indian companies, so as to make changes for achieving higher governance ratings.

The regression analysis and its outcome regarding impact of corporate governance ratings on financial performance of firm have been described in the following table no. 2:

TABLE 2: REGRESSION ANALYSIS

Particulars	R	R2	Adjusted R2	F	Significance of F	Beta Coefficient for GOV (b1)	p-value
ROA	.732	.535	.268	3.200	.038	1.381	.024*
ROE	.767	.588	.233	4.044	.017	1.926	.025*
ROCE	.762	.580	.426	3.824	.021	3.026	.018*
PBT	.829	.687	.570	6.035	.004	827.701	.026*

* At 5% level of Significance

(**Source: researcher own calculation**)

FINDINGS OF THE STUDY AND CONCLUSION

Following findings of the study and conclusion has been observed from the observation of given data in Table-2.

- The coefficients of determination [R2] values are found appropriately high (i.e. it is more than.50). Further, all impact of significance 'F' values are less than.05. And so the model is fit well.
- All Beta coefficients [B1] are found positive. And because of that ratings of corporate governance have positive impact on financial performance of firm.
- All values of 'p' are less than.05. And because of that ratings of corporate governance have positive impact on financial performance of firm.
- And on the basis of such outcome, here it rejected the said null hypothesis and granted the alternate hypothesis.

So, it can be indicated from the result of statistical data that governance rating of company has a significant impact on its financial performance. The present study outcome accordance with the other existing research result of Cremers and Nair (2005); Van de Velde et al. (2005); Governance Metrics International and Byun (2006); and Eisenhofer (2010). Above said studies comment good governance fosters good financial performance. Further it has been found the ratings of company along employees associated and environmental dimensions also significantly influence financial performance of corporate. The command over variable firm size also caught attention to have significant impact on corporate financial performance. This outcome is in consonance with the expectation and the outcome of the study of Patten and Guindry 2010.

RECOMMENDATIONS

In the study, it has been cleared that corporate financial performance and corporate governance are strongly associated and governance rating of company has significant remarkable impact on its financial performance. The present study outcome may help the company in its decision to improve its governance structure. Company should be sincere and strive to standardize its performance along indicators of good governance, Board Composition, Leadership Ethics, and Independence of Board, Executive Compensation, Reporting and Transparency, Engagement of Stakeholder and compliance with law in true spirit and letter. Company should have to know that improving sustainability and governance performance is as imperative as improving the financial performance.

LIMITATIONS OF THE STUDY

The current study has certain limitations.

- There has been selected only 20 companies for the study.
- The time period of present study is only 2 years.
- To measures the financial performance, market based variables have not been considered.
- Control variable like growth of firm, age of firm, leverage risk, intensity, R&D not considered in the study.

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In this age of Commerce, Economics, Computer, I.T. & Management and cut throat competition, a group of intellectuals felt the need to have some platform, where young and budding managers and academicians could express their views and discuss the problems among their peers. This journal was conceived with this noble intention in view. This journal has been introduced to give an opportunity for expressing refined and innovative ideas in this field. It is our humble endeavour to provide a springboard to the upcoming specialists and give a chance to know about the latest in the sphere of research and knowledge. We have taken a small step and we hope that with the active co-operation of like-minded scholars, we shall be able to serve the society with our humble efforts.

Our Other Journals