GAP iNTERDISCIPLINARITIES
A Global Journal of Interdisciplinary Studies
(ISSN – 2581-5628)
Impact Factor: SJIF - 5.363, IIFS - 4.875
Globally peer-reviewed and open access journal.

A STUDY ON IMPACT OF CORPORATE GOVERNANCE ON FINANCIAL PERFORMANCE OF THE SELECTED IT COMPANIES IN INDIA

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Abstract

The term "corporate governance" has recently gained popularity in the business world. It is regarded as a moral obligation. It entails promoting adherence to the law in letter and spirit and illustrating ethical behavior. Corporate governance is a critical procedure that influences an organization's financial performance. The main aim of this paper is to investigate the impact of corporate governance on the financial performance of the leading IT sector companies in India. For this purpose five leading IT sector companies (on the basis of market share) have been selected namely TCS, Wipro, Infosys, HCL Tech and Tech Mahindra. The present study is based on Secondary Data. Data of five years (from 2018-19 to 2022-23) have been analyzed through panel data regression. In this study, ROA and ROE are taken as performance indicators and Board Size, Board Composition, CEO Duality, Promoter's Holding, Size and Age have been selected as independent variables. The outcome of regression analysis showed that only promoters holding and Size have significant positive influence on the ROA and ROE whereas, Age is having significant negative impact on them. Further, it is also concluded that corporate governance variables such as board size, board composition and duality have no significant impact on the performance of the leading IT companies in India.

Keywords: *Financial Performance, Corporate Governance, IT Companies, Regression etc.*

INTRODUCTION:

To date, the world has witnessed numerous corporate scandals and frauds, which have harmed stakeholders' trust and faith in huge organizations' governance and control mechanisms. Some Indian MNCs, such as 'Satyam,' have also made investors nervous by portraying a truthful and unbiased perspective of huge corporations, which resulted in a scam and landed nowhere. Companies, like artificial humans, are unable to do or conduct things or activities on their own (Prusty & Kumar, 2016). Following the Satyam case, much has been said and done in India regarding board mechanisms. Following the adoption of Clause 49, it became mandatory to follow its suggestions. The emphasis was placed on board composition and strengthening the internal governance framework of at least listed enterprises. The article 49 listing agreement of independent directors for publicly traded firms was postponed for nine months, till December 31, 2005. Finally, it went into effect on January 1, 2006. As a result, numerous firms have restructured their boards. The question is whether these changes in corporate governance structures are linked to business performance metrics (Klein, 1998).

Corporate governance is a multifunctional governance strategy. It primarily focuses on enhancing corporate performance through the accountability of those involved in administration (Diriba & Basumatary, 2019). Corporate governance refers to the methods and structures that a company uses to manage itself while preserving the interests of its stakeholders. A good governance is based on the concepts of openness, accountability, fairness, and responsibility in corporate management. Good governance improves a company's performance and competitiveness, paving the way for it to achieve business excellence (Mohan & Chandramohan, 2018). The Cadbury Committee defined Corporate Governance as "the system by which companies are directed and controlled" in its 1992 report Financial Aspects of Corporate Governance. In general, Corporate Governance refers to the set of rules and regulations that regulate, control, and direct a company. It is carried out for the benefit of the company's stakeholders by the Board of Directors or the relevant committee (Cadbury, 1992).

A well-planned and operational Corporate Governance System aids in the attraction of new investments and strengthens the foundation for the firm's performance. According to (Dalton, Johnson, & Ellstrand, 2005), the relationship between corporate governance and performance has significant consequences for legislators who prescribe corporate governance methods. According to Johnson et al. (2000), poor corporate governance exacerbated the 1997 Asian currency crisis, emphasizing the relevance of corporate governance to business performance. Previous research has primarily focused on advanced countries, with a few new studies focusing on underdeveloped countries. In this backdrop, the purpose of this study is to present empirical evidence on the relationship between corporate governance and firm performance in India. Over a sample of 30 listed corporations, data from the Bombay Stock Exchange (hereafter ''BSE'') and other credible data sources were used. As a result, this study attempts to examine how CG proxies affect financial performance while taking firm-specific aspects into account. For this, board composition, board size, and CEO duality were used as proxies for corporate governance, and ROE and PB ratios were used to measure financial success, while firm-specific factors included asset turnover, financial leverage, and percentage of sales growth.

The primary goal of any type of business is to maximize profit while also increasing the wealth of all stakeholders. The corporation must make a profit while not jeopardizing the interests of any person with a stake in the company. The firm's financial performance, as measured by profitability, must be enhanced through the process of corporate governance in order to safeguard the interests of all stakeholders. The interests of shareholders play a significant role in how a firm works. However, the board of directors is in charge of strategic management. As a result, proper harmony must be maintained between all stakeholders and the board of directors. Investing money in any company requires a significant level of confidence and faith. For shareholders to trust any firm, its operating procedures should be thoroughly revealed. Corporate governance can be viewed as a key tool for gauging the effectiveness of a company's board of directors (Kajananthan, 2012).

LITERATURE REVIEWS:

(Ghosh, 2006) investigated the association between financial performance and board parameters in Indian non-financial enterprises empirically. For the fiscal year 2003, data from 127 publicly traded manufacturing enterprises were used. The findings demonstrated that, after controlling for numerous business-specific factors, larger boards have a detrimental effect on firm performance, as measured by accounting or market-based performance indicators. The data also reveals that the salary of the CEO has a considerable impact on corporate performance.

(MOHAN & MARIMUTHU:, 2015) investigated the impact of corporate governance on the financial performance of BSE-listed Indian companies. Data on Return on Assets and Corporate Governance variables of Board Size (number of directors on the board), Duality (if the chairman and managing director are the same), Remuneration to the board of directors, independence (number of non-executive directors), and Board Ownership (Shareholding pattern of promoter and promoter's group) of these companies were collected from moneycontrol.com and CMIE data sources for the five-year period of 01/04/2009 to 31/03/2014. The findings demonstrated that the two Corporate Governance variables, Board Ownership and Duality, have a significant impact on ROA at the 5% level.

Between 2005 and 2012, (Gugnani, 2013) researched the relationship between corporate governance and financial performance of listed Indian manufacturing enterprises. In the contemporary Indian scenario, the impact of board size, board composition, duality in board leadership, and promoter ownership was evaluated in connection to two sets of financial performance. The survey of literature was utilized as a qualitative measure to investigate the relationship of sampled variables, and the ordinary least squares (OLS) method was employed as a quantitative instrument to investigate the relationship. The study postulated a negative relationship between board size and CEO status and financial success, as well as a positive relationship between corporate performance and board independence and insiders (promoters) holding. According to the data, profit margin is the only financial performance measure that is significantly related to internal governance frameworks.

(Danoshana & Ravivathani, 2014) did another study to investigate the effect of corporate governance on business performance of 25 listed financial institutions in Sri Lanka from 2008 to 2012. The study employed return on equity and return on assets as important variables to define business performance. The outcomes of the analysis demonstrate that corporate governance variables have a substantial effect on business performance, and the size of the board of directors and audit committee has a positive effect on business performance. Nonetheless, meeting frequency is inversely related to business performance.

(Griffin, Guedhami, Kwok, Li, & Shao, 2014) conducted a study to investigate the relationship between National Culture, Corporate Governance Practices, and Firm Performance. They discovered that the stock market-based financial system of a country has a negative impact with transparent disclosure and minority shareholder protection by using a new database from Governance Metrics International measures of corporate governance practices across a large number of countries for the sample period of 2006-2011.

(Ahmed & Hamdan, 2015) investigated the impact of corporate governance features on business performance on the Bahrain Stock Exchange in their article "The Impact of Corporate Governance on Firm Performance: Evidence from Bahrain Stock Exchange." The study sample included 42 of the 48 Bahraini financial enterprises that were listed on the Bahrain Stock Exchange between 2007 and 2011. According to the empirical findings, performance measurements such as Return on Assets and Return on Equity are strongly associated to corporate governance in Bahrain. However, the Earnings Per Share performance indicator has no significant impact on corporate governance. Overall, this study discovered a favorable benefit of corporate governance procedures on overall firm performance on the Bahrain Stock Exchange.

RESEARCH METHODOLOGY:

Objective of the Study:
The prime objective of the study is to identify the corporate governance variable that affect the performance of the leading IT Companies in India and also to analyze the impact of corporate governance variables on company performance of the selected IT companies in India.

Research Design:
The present study is based on the ***Descriptive Research Design***.

Sampling Method and Sample Size:
A convenience sampling method is used for the purpose of the study. Top Five Indian IT sector companies based on market share have been selected namely TCS Ltd., Infosys Ltd., HCL Tech Ltd., Wipro Ltd. and Tech Mahindra Ltd.

Time Period of the Study:
The present study covers the time span of five years i.e. from the year 2018-19 to 2022-23.

Sources of Data:
The present study is based on the secondary sources of data. The data of five years have been collected from the annual reports of the sampled companies and moneycontrol website.

Tools & Techniques:
In order to examine the impact of corporate governance variables on the firm performance of the selected companies, data of the five years have analyzed through regression analysis. Here, The regression model used is as under:

Model – 1

$$\boldsymbol{ROAit = \beta 0 + \beta 1x1 + \beta 2x2 + \beta 3x3 + \beta 4x4 + \beta 5x5 + \beta 6x6 + \epsilon}$$

Model – 2

$$\boldsymbol{ROEit = \beta 0 + \beta 1x1 + \beta 2x2 + \beta 3x3 + \beta 4x4 + \beta 5x5 + \beta 6x6 + \epsilon}$$

Description of Variables used for Regression Analysis

Variable	**Label**	**Definition**
Dependent Variable		
Return on Asset	ROA	$\frac{Net\ Profits}{Total\ Assets}$
Return on Equity	ROE	$\frac{Net\ Profits}{Shareholder's\ Equity}$
Independent Variables		
Board Size	*X1*	*Total number of Directors*
Board Composition	X2	percentage of independent directors in a board
Duality	X3	Coded 0 if chairman and managing director are same Coded 1 if chairman and managing director are not same
Promoter's holding	X4	Percentage of share held by the promoters
Control Variables		

Size	X5	Natural log of total assets
Age	X6	Age of the company since its incorporation

Hypothesis of the Study:
H_0: There is no significant impact of Board Size, Board Composition, Duality, Promoter's Holding, Size and Age on the financial performance of the selected IT sector companies in India.
H_1: is no significant impact of Board Size, Board Composition, Duality, Promoter's Holding, Size and Age on the financial performance of the selected IT sector companies in India.

DATA ANALYSIS

TABLE 1: REGRESSION ANALYSIS OF MODEL 1

Model		Unstandardized Coefficients		T	Sig.	Collinearity Statistics	
		B	Std. Error			Tolerance	VIF
1	(Constant)	-116.844	20.058	-5.825	.000		
	Board Size	-0.332	.498	-.667	.513	.468	2.137
	Board Independence	-0.009	.083	-.102	.919	.801	1.249
	Promoters Holding	1.238*	.043	5.468	.000	.308	3.242
	Size	13.780*	1.646	8.371	.000	.589	1.698
	Age	-0.500*	.068	-7.364	.000	.341	2.935

(Source: Computed by the researcher in SPSS)
(* significant at 5% level of significance)

The above table shows the regression output of the model1. From the above table it can be observed that the promoters holding and size have significant positive impact on the dependent variable. While Age, has significant negative impact on the ROA. Board Size and Board Independence is negatively associated with the ROA. Further it is also observed that the Size followed by the promoters holding is the most contributing factor in the determination of ROA. There is no problem of multi-collinearity as it can be observed from the collinearity statistics.

TABLE 2: Model Summary OF MODEL 1

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	Change Statistics					Durbin-Watson
					R Square Change	F Change	df1	df2	Sig. F Change	
1	.931[a]	.867	.832	2.80977	.867	24.737*	5	19	.000	2.135
a. Predictors: (Constant), Age, Board Independence, Board Size, Size, Promoters Holding										
b. Dependent Variable: ROA										

(Source: Computed by the researcher in SPSS)
(* significant at 5% level of significance)

The table 2 depicts the model summary of the model 1. The value of R square in the above table is 0.867 which means around 86.70% variance is explained by this model and hence it can be said that the explanatory power of the model is good. The F value and Significant F Value is 24.737 and 0.00 respectively. The significant F value is less than the 0.05 which indicates that the model 1is statistically significant.

TABLE 3: REGRESSION ANALYSIS OF MODEL 2

Model		Unstandardized Coefficients		t	Sig.	Collinearity Statistics	
		B	Std. Error			Tolerance	VIF
2	(Constant)	-169.436	33.949	-4.991	.000		
	Board Size	-0.792	.843	-.940	.359	.468	2.137
	Board Independence	-0.107	.141	-.757	.459	.801	1.249
	Promoters Holding	1.353*	.074	4.807	.000	.308	3.242
	Size	20.592*	2.786	7.391	.000	.589	1.698
	Age	-0.705*	.115	-6.132	.000	.341	2.935

(Source: Computed by the researcher in SPSS)
(* significant at 5% level of significance)

The above table 3 represents the output of regression analysis of the model 2. From the above it can be seen that Board Size and Board Size and Board Independence are negatively correlated with the dependent variable i.e. ROE. Promoters holding and Size have significant positive influence on the ROE and Age is having significant negative impacts on the ROE. The contribution of Size and promoters holding is comparatively higher for the determination of the dependent variable i.e. ROE. The tolerance and VIF are within the limit so the multicollinearity does not exist.

TABLE 4: Model SUMMARY OF MODEL 2

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	Change Statistics					Durbin-Watson
					R Square Change	F Change	df1	df2	Sig. F Change	
2	.918[a]	.842	.801	4.75558	.842	20.325*	5	19	.000	2.041

a. Predictors: (Constant), Age, Board Independence, Board Size, Size, Promoters Holding
b. Dependent Variable: ROE

(Source: Computed by the researcher in SPSS)
(* significant at 5% level of significance)

From the table 4 it can be observed that the value of R Square is 0.842 which indicates that the around 84.20% variations in the ROE is explained by the all these independents variables. And therefore, it can be said the explanatory power of the model good. The F value and significant F value in the above table is 20.325 and 0.00 respectively. The significant F value is lower than the 5% level of significance which means that the model is statistically significant.

CONCLUSION

The prime objective of the study was to measure the impact of corporate governance variables on the financial performance of leading IT sector companies in India. Five leading IT sector companies based on the market share had been selected. The financial data of five years (2018-19 to 2022-23) were taken for the purpose of the study. Data of five years were analyzed by applying multiple regression. ROA and ROE were taken as dependent variables and Board Size, Board Composition, Duality, Promoter's Holding, Size and Age were taken as independent variables. The study revealed that promoters holding and Size have significant positive impact on the financial performance of the sampled companies. And Age has significant negative impact on the dependent variables i.e. ROA and ROE. Further, the outcome of regression also showed that Board Size, Board Composition and Duality have no fundamental effects on the company performance. So it can be concluded that most of the corporate governance variables (such as board size, board independence or board composition and CEO duality) have no significant influence on the financial performance of the Indian leading IT sector companies.

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