# Effectiveness Of Board and Its Impact On Financial Growth – A Study On Implications Of Corporate Governance In Selected Firm Of Bangalore

Malini M V
Assistant Professor –Department Of Commerce
Government First Grade College, Malur, Karnataka

**ABSTRACT**
The process of decision making within and between the governing bodies of an organization is improved by good corporate governance practices. This helps in enhancing the efficiency of the business operations and the financial performance of the organization. The board of directors plays a vital role in maintaining organizational efficiency in terms of profit and financial growth. In this context, the selected five companies still debates on corporate governance practices with respect to board composition, particularly, board independence and transparency. Even though there are guidelines in mandating number of independent directors, the association between board composition and performance are yet to be established. The purpose of this study is to examine corporate governance practices of selected companies and identifying how the effectiveness of board with respect to its independency and transparency influence the financial growth of selected companies of Bangalore.

**Keywords:** Corporate Governance, Board Independency, Board Transparency, Financial Growth, Board Effectiveness

## 1. INTRODUCTION

An organization's economic performance is determined not only by its productivity, creativity, and quality control, but also by its adherence to corporate governance standards. In developed economies, implementing corporate governance principles enhances a company's financial results and has a positive effect on internal productivity.[1] However, the efficacy of corporate governance mechanisms is harmed by a lack of accountability and inadequate disclosure practises. However, the global financial crisis and major corporate scandals have highlighted the importance of good corporate governance processes in improving long-term success and sustainability.[2]

### 1.1 CORPORATE GOVERNANCE - MEANING AND DEFINITION

Corporate governance is a set of rules, processes, procedures, and systems that an organisation uses to run its operations in order to meet its financial, organisational, and strategic objectives while also ensuring long-term viability. It requires balancing the needs of a number of stakeholders, including management, consumers, vendors, financiers, the government, and the general public. Corporate Governance is described by the Securities and Exchange Board of India Committee on Corporate Governance as "management's acceptance of the inalienable rights of shareholders as the true owners of the corporation and of their own position as trustees on behalf of the shareholders; it is about commitment to values, ethical business conduct, and making a distinction between personal and corporate interests." India is a developing economy, and corporate governance plays an important role in protecting investors' interests and clearly defining management roles.

According to Maier (2005),[3] corporate governance defines a set of relationships between a company's management, its board, its shareholders and its stakeholders. Good corporate governance "ensures that corporations take into account the interests of a wide range of constituencies, as well as the communities within which they operate, and that their boards are accountable to them." Corporate governance was created to protect the interests of shareholders, but it has increasingly gained significance for other stakeholders and society.[4]

The aim of corporate governance is to make it easier to track and manage business operations. Its core is based on operational fairness and accountability, as well as increased disclosures to protect the interests of various stakeholders.[5] Corporate governance systems are supposed to improve the firm's performance by allowing for better decision-making.[6]

### 1.2 COMPONENTS OF CORPORATE GOVERNANCE

- **Board Size:** The size of the board is considered to have a major effect on the firm's results, which is generally positive. Independent directors are generally thought to play an important role in overseeing and guiding the company's management. They are expected to the organization's and stakeholders' overall interest.

- **Separation of CEO and Chairman:** When the roles of CEO and Chairman of the Board are observed by the same person, there is typically a conflict of interest, a concentration of influence, and a lack of board independence.
- **Financial Expertise of Directors:** Directors should be financially literate in order to better understand the consequences of management decisions, resulting in better and more efficient control.
- **Number of Board Meetings:** Members of the board should meet often enough. Few meetings suggest a lack of interest on the part of the Board, while too many meetings indicate an issue within the company.
- **Role of External Auditors:** The external auditor should be knowledgeable and impartial enough to identify and investigate corporate report frauds and manipulations. External auditors that provide both audit and non-audit services at the same time reduce audit effectiveness. The amount of audit fees is also important to consider.
- **Committees of the Board:** Board committees improve the board's efficiency by exerting more influence over management decisions. There are some of them:
  - **Audit committee:** The need for an effective audit committee has increased as a result of high-profile corporate frauds. Daily meetings and the audit committee's independence will help ensure the integrity of corporate reports.
  - **Remuneration committee:** A board remuneration committee assists in determining the appropriate amount of remuneration for top executives such as the CEO.
  - **Nomination committee:** The nomination committee assesses the necessary qualifications, knowledge, and experience to become a director and selects the most qualified applicants.[7]

**1.3 GOOD CORPORATE GOVERNANCE**

Transparency and responsiveness to the rules and controls of the owners, directors, and officers are created by good corporate governance. Corporate Governance is all that companies aim for. Today's businesses prioritise social responsibility over profit, focusing on environmental awareness, ethical actions, and sound corporate governance practises. Strong governance has a positive effect on a company's success and long-term sustainability. Participation, rule of law, openness, responsiveness, consensus orientation, fairness, effective, quality, and accountability are eight characteristics of good governance.

**1.4 BENEFITS OF GOOD CORPORATE GOVERNANCE PRACTICES**

In today's intensely competitive business climate, good governance is crucial in terms of raising money, securing debts, nominating skilled directors, managing talent, maintaining employee and stakeholder satisfaction, and growing and acquiring new companies. Corporate Governance is built on the law, which is focused on corporate regulation, securities laws and policies, security regulators, and court decisions. The company's directors are required to represent the company with loyalty, in the company's best interests, and in good faith. They also use data from the stock exchange, interest groups, the newspapers, and other outlets. Corporate governance assists directors in performing their roles and obligations to the company. The board of directors is responsible for directing, controlling, creating, managing, and achieving the organization's managerial objectives. Corporate Governance practises should be dependable and credible in order to draw investors, lower capital costs, and ensure proper functioning and financing.

**1.5 CORPORATE GOVERNANCE AND FINANCIAL PERFORMANCE**

Independent boards are seen as a proxy for good corporate governance and are cited as such. The presence of independent and non-executive directors on the board acts as a powerful oversight tool. The inclusion of outside directors on the board strengthens the firm's image by serving as a Good Governance activity. Independent Directors had a positive impact on the companies' financial performance. The number of directors on the board is referred to as the board size. Clause 49 does not mention the board's size, instead using the term "optimal combination." This means that the Board should be made up of a diverse group of people with a wide range of experience, knowledge, and skills.

Larger boards have a positive effect on a company's financial performance because they put in more experience, diverse viewpoints, and skills. The number of meetings held by the Board is used to assess its activity. Clause 49 stipulates that at least four meetings must be held each year, with no more than 120 days between them. A higher number of board meetings allows for more discussion of business problems, which increases financial results. The number of board meetings attended by the directors has a positive impact on the companies' financial performance. When directors attend meetings on a regular basis, there is a close oversight and control of the company's operations, which has a positive effect on the company's performance. The presence of a financial expert on the Audit Committee increases the reliability, accountability, and analysis of the company's financial results.[8]

**1.3 CORPORATE GOVERNANCE REFORMS AND IMPLICATIONS**

Corporate governance reforms are especially important for developing economies because they improve corporate structures, enable them to compete more effectively with multinational companies, and boost investor trust.[9] In order to keep up with global trends, India has seen a host of corporate governance reforms. The adoption of clause 49 of the listing agreement by the Security Exchange Board of India (SEBI), India's apex regulatory authority for the stock market, is one such reform. The corporate governance mechanisms for listed companies in India are outlined in this clause. It has had major consequences for independent board directors, increased transparency standards, and improved audit committees, among other items. Furthermore, the adoption of the amended Company Act, 2013, strengthens corporate governance initiatives. Corporate governance reforms are crucial for India, which is aiming for a more effective and transparent economic governance structure.[10] The Indian economy was liberalised and privatised after the fiscal crisis of 1991. Finance was needed by Indian businesses in order for them to develop and expand. Corporate governance reforms in India were necessitated by the need for foreign investment. Since then, SEBI has put a high priority on good capital market governance. SEBI's regular updates of guidelines, laws, and regulations to ensure transparency and accountability demonstrate this.[11] Clause 49 was adopted by SEBI in 1999 from the Confederation of Indian Industry's (CII) code of governance, which is an autonomous body that works with the government on policy issues. It has been updated on a regular basis to ensure better compliance.

**2 REVIEW OF LITERATURE**

**Phillip Cordwell James (2020)**[12] conducted a comprehensive review of previous research in order to provide some guidance and closure to the debate over the impact of board structure on firm results. According to the findings of the literature review, there are persuasive reasons on both sides to support or refute the hypothesis that board structure influences firm success. As a result, this study points the researcher in a new direction in his or her quest to address this decade-old query. According to **Prajakta Dhuru et al. (2019)**[13] Corporate Governance is a significant feature for the application of standards and codes that have a positive effect on firm success. The corporate governance system ensures meaningful interaction with all of the company's stakeholders, as well as accountability between the company's authority and its stakeholders. Corporate governance is a concept that is used in all sectors of the economy. The similarities and differences in good governance practises between various companies in the Fast-Moving Consumer Goods (FMCG) sector are presented in this report. FMCG is the economy's fourth largest market. This research aims to learn about the good governance principles used in this industry, as well as their main differentiation theory. **Akshita Arora and Shernaz Bodhanwala's (2018)**[14] observed if there was a correlation between CGI and firm results. We construct CGI using important governance criteria including board structure, ownership structure, corporate control market, and market competition. Our panel data set consists of publicly traded companies, and the estimation analysis was conducted using the random effects process. CGI and firm output indicators have a significant positive relationship, according to the report. In explaining firm results, CGI is a significant and causal factor. Investors will also have a positive impression of businesses that adhere to high governance standards, potentially lowering financing costs. **Puneeta Goel (2018)**[15] examined the efficacy of corporate governance reforms by reviewing the corporate governance practises of

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Indian companies during two reform cycles (FY 2012–13 as Period 1 and FY 2015–16 as Period 2). A corporate governance performance (CGP) index has been created to calculate corporate governance score of Indian companies, taking into account mandatory regulations as per clause 49 of the Listing Agreement with the Securities Exchange Board of India and governance norms in the new Company Act, 2013. Despite the fact that Indian companies' corporate governance systems have improved significantly, the number of independent directors inducted into the board has decreased after the reforms in period 2. Following corporate governance policies has improved significantly in all of the industries studied as a result of the reforms. Only in period 1 did the analysis find a significant connection between an integrated system of overall corporate social performance and financial performance. In period 2, corporate governance reforms have no impact on financial linkages in the Indian industry.

## 3 RESEARCH GAP

According to an analysis of the literature, previous research on board of directors has been conducted in a systematic manner in the field of management. On the one hand, some authors believe that board composition has little or no impact on a company's financial growth; while on the other hand, some authors believe that board composition has a substantial impact on a company's financial growth. Corporate governance has obtained a lot of consideration in the accounting literature, with studies revolving around the effect of corporate governance and the financial performance of the firm. Corporate governance is highly prioritized by policymakers, investors, financial establishments, organizations and academics. In the literature, various studies have tried to research on the board independency and transparency and its connection with financial performance. Most of the studies have demonstrated a mixed outcome without a definite association. Profitability of an organization is positively impacted by corporate governance practices, while on the other hand, evidences show that board independency does not have any impact on financial performance. This present study accordingly tries to explore the relationship that exists between board transparency and independency and financial growth and performance of selected five companies in Bangalore. There is a requirement for more grounded tests to perceive the impacts on financial performance of the companies with respect to board composition. Subsequently this study aims to address these gaps on board independency and transparency and its influence on financial performance among the selected companies in Bangalore.

## 4 STATEMENT OF THE PROBLEM

SEBI's corporate governance rules are primarily concerned with a company's board of directors. From determining board size to putting it into action, there are a number of criteria that businesses must follow for two reasons: to be legitimate and to expand their business. From a general viewpoint, it is evident that the board of directors has a huge effect on the success of businesses. The study's key concern is how important it would be. Shareholders own businesses, but the board of directors oversees and governs them. Any organization's Board of Directors is a unit that makes strategic decisions and requires active involvement from all of the directors that make up the board. The study focuses on board-related variables that are thought to have a major impact on its results.

## 5 OBJECTIVES OF THE STUDY

- To study the determinants of board composition in selected companies of Bangalore.
- To analyze the influence of board effectiveness and its impact on financial growth of selected companies of Bangalore.

## 6 RESEARCH METHODOLOGY

The present paper involves both descriptive and empirical analysis and has incorporated both primary and secondary data. The study's primary and secondary data were obtained in a systematic manner. **Primary Data:** A survey was conducted among the 151 respondents from the selected five companies (Hindustan Unilever Ltd, ITC Ltd, Sun Pharma, Dr Reddy's Labs, and Dabur India Ltd) in the study area Bangalore using a self-structured questionnaire and a simple random sampling process. The participants were asked to rate various items on a 5-point Likert Scale, with 5 representing Strongly Agree and 1 representing Strongly Disagree. Questions about board structure, financial performance and corporate governance were included in the survey. Except for the socio demographic questions, all questions were answered on a five-point Likert scale. Cronbach's Alpha was used to assess the questionnaire's reliability, with an estimate of 0.7 and above indicating that the data was reliable. **Secondary data** was gathered from journals, magazines, studies, books, newspapers, periodicals, working papers, research papers, blogs and business publications,. The participants in this study are members of the Board of Directors (Charman, Director, Audit Committee, and so on) as well as Executive Officers (president, CEO, vice president, finance executive officers etc.). Simple Random Sampling was adopted for the study. The Statistical Package for Social Sciences (SPSS) version 20.0 was used to analyse the results. Using the study variables Cash Flow, Profitability, Sales Growth, Liquidity Position, and Organisational Development, the SPSS analysis was used to measure Financial Growth of the selected firms. Statistical tools such as Factor analysis, Anova, Chi-square, and SEM were used in this analysis to determine the relationship between the study variables.

**Selected Companies For The Present Study**

The study is focused on companies in non-financial sectors that must adhere to SEBI clause 49. The financial sector is exempt from the study due to the fact that businesses must follow various rules and regulations. The companies for the current study were chosen based on this criterion. Hindustan Unilever Ltd, ITC Ltd, Sun Pharma, Dr Reddys Labs, and Dabur India Ltd., all based in Bangalore, were chosen for their strong corporate governance strategies.

**Statistical Tools**

The collected data has been analyzed using the statistical package AMOS and SPSS 20 and hypotheses were tested using the statistical tool like Regression, Chi-Square and SEM (Structural Equation Modelling).

**7. ANALYSIS AND INTERPRETATION**

**Regression Analysis**

**$H_{01}$ –** There is no significant relationship between Leverage and Financial growth

**$H_{02}$ –** There is no significant relationship between Return on Assets and Financial growth

**Table - 1**

**Model Summary**

| Model | R | R Square | Adjusted R Square | Std.Error |
|---|---|---|---|---|
| | 0.574 | 0.329 | 0.317 | 3.111 |

**ANOVA**

| Model | Sum of Squares | df | Mean Square | F | Sig |
|---|---|---|---|---|---|
| Regression | 540.620 | 2 | 270.310 | 27.936 | 0.000 |
| Residual | 1103.073 | 114 | 9.676 | | |
| Total | 1643.692 | 116 | | | |

***5% Significant Level**

**Co-efficient**

| Model | Unstandardized Coefficients | | Standardized Coefficient | t | Sig. |
|---|---|---|---|---|---|
| | B | Std.Error | Beta | | |
| (Constant) | 8.318 | 2.026 | | 4.106 | 0.000 |
| Leverage | 0.280 | 0.077 | 0.317 | 3.622 | 0.000 |
| Return on Assets | 0.388 | 0.097 | 0.350 | 4.003 | 0.000 |

***5% Significant Level**

**Discussion:**

Leverage is an independent variable and Financial Growth is a dependent variable. From the table - 1 it is found that the P Value is 0.000, Therefore it is found that leverage influence the financial growth, as the P value is lesser than significant valve (5%). Hence null hypothesis is rejected. Return on Assets is an independent variable and Financial Growth is a dependent variable. From the table - 1 it is found that the P Value is 0.000, Therefore it is found that return on assets influence the financial growth, as the P value is lesser than significant valve (5%). Hence null hypothesis is rejected.

**SEM Path Analysis**

**Figure – 1**

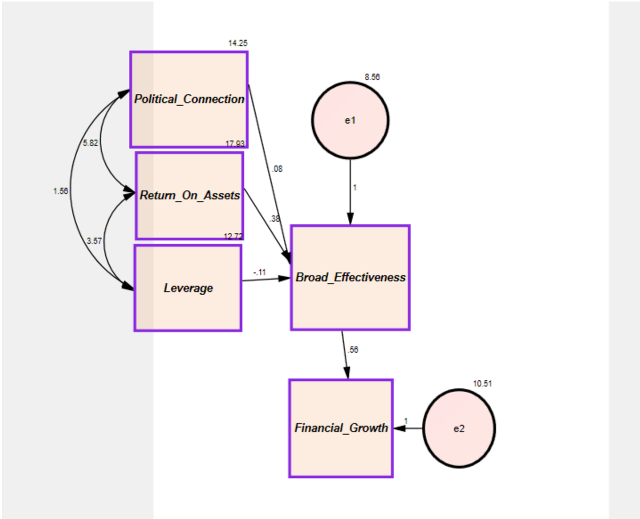


**Table - 2**
**Testing of Hypothesis**

| Hypothesis | Relationship | SE | P-Value | Result |
|---|---|---|---|---|
| $H_{03}$ | Political Connection has no influence on Board Effectiveness | 0.077 | 0.314 | Not Significant |
| $H_{04}$ | Return on Assets has no impact on Board Effectiveness | 0.070 | 0.000 | Significant |
| $H_{05}$ | Leverage has no impact on Board Effectiveness | 0.078 | 0.144 | Not Significant |
| $H_{06}$ | Board Effectiveness has no influence on Financial Growth | 0.089 | 0.000 | Significant |

**Significant at 1% Level**

**Model Fit**
**Table – 3**

| S.No | Model Fit Indices | Calculated Value | Acceptable Threshold Levels |
|---|---|---|---|
| 1. | Goodness of Fit Index (GFI) | 0.957 | 0 – 1 |
| 2. | Comparative Fit Index (CFI) | 0.984 | 0 – 1 |
| 3. | Adjusted Goodness of Fit Index (AGFI) | 0.942 | 0 – 1 |
| 5. | Tucker Lewis Index | 0.914 | 0 – 1 |
| 6. | Root Mean Squared Error of Approximation (RMSEA) | 0.022 | 0.05 or lesser |

**Discussion:**

To estimate the appropriateness of the overall model, the study assessed the measures representing the overall fit, absolute goodness of fit (GFI = 0.957) incremental fit indices (CFI=0.984), Tuker Lewis index (TLI=0.915) and root mean square error of approximation (RMSEA= 0.022). Based on literature it was found that, GFI, CFI and TLI measures can be greater than 0.90, and RMSEA can be less than 0.08 preferably. Hence the above value shows the model is good fit.

**Chi-Square Test**

**Table - 4**

$H_{07}$ - There is no relationship between education and Monthly Income of the respondents

| Factor | Value | Df | Symp. Sig. (2-sided) | Statistical Inference |
|---|---|---|---|---|
| Pearson Chi-Square | 91.703 | 3 | 0.000 | **Significant** |
| Likelihood Ratio | 111.178 | 3 | 0.000 | |
| Linear-by-Linear Association | 6.428 | 1 | 0.011 | |
| N of Valid Cases | 117 | | | |

***Significant at 5% level**

**Result and Discussion**

From the above table, it is evident that the P value is lesser than Significant at = 5% levels, the null hypothesis is rejected. The value of Pearson Chi-square is 91.703, at 3 degrees of freedom and 5% level of significance therefore the Null Hypothesis "There is no relationship between education and monthly income" is rejected; and it is concluded that there is an association between education and monthly income factors.

**8. FINDINGS**

From the regression analysis it is found that leverage is an independent variable and Financial Growth is a dependent variable. From the table - 1 it is found that the P Value is 0.000, Therefore it is found that leverage influence the financial growth, as the P value is lesser than significant valve (5%). Hence null hypothesis is rejected. Return on Assets is an independent variable and Financial Growth is a dependent variable. From the table - 1 it is found that the P Value is 0.000, Therefore it is found that return on assets influence the financial growth, as the P value is lesser than significant valve (5%). Hence null hypothesis is rejected.

SEM is done to estimate the appropriateness of the overall model, the study assessed the measures representing the overall fit, absolute goodness of fit (GFI = 0.957) incremental fit indices (CFI=0.984), Tuker Lewis index (TLI=0.915) and root mean square error of approximation (RMSEA= 0.022). Based on literature it was found that, GFI, CFI and TLI measures can be greater than 0.90, and RMSEA can be less than 0.08 preferably. Hence the above value shows the model is good fit.

Chi-square test shows that the P value is lesser than Significant at = 5% levels, the null hypothesis is rejected. The value of Pearson Chi-square is 91.703, at 3 degrees of freedom and 5% level of significance therefore the Null Hypothesis "There is no relationship between education and monthly income" is rejected; and it is concluded that there is an association between education and monthly income factors. **SUGGESTIONS**

- In order to foster good corporate governance practises within organisations, the regulatory processes governing board effectiveness must be improved.
- Shareholders can advocate for board independence, diversity, and the creation of independent audit committees.
- Regulators of the selected companies should develop strategies to improve business practises, paving the way for financial profitability.

- Increasing the size of the board of directors may have an impact on the organization's success. As a result, the number of directors on the board must be transparent.

## 10. CONCLUSION

In light of previous literature reviews, the research concludes that board governance has an important effect on the financial growth and performance of the companies examined. It has been noted that almost all selected organisations have disclosed and adopted their corporate governance codes, although the approaches used to do so vary. Many organisations are currently using corporate governance practises as a benchmark. Aside from the mandatory provisions set out in SEBI clause 49, the company has concentrated on revealing the majority of the non-mandatory provisions.

The study also claims that the board transparency and board independency have a strong relationship with Return on Assets (ROA) and Leverage. This is effective in demonstrating its effect on financial growth. As a result, it is reasonable to conclude that the board governance index and the board committee as a whole have a direct effect on company financial results and hence, the board's position cannot be neglected.

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