

Shareholders' Perception towards Corporate Governance in India

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Abstract

Good corporate governance is a key component in enhancing the economic competence of a firm and it additionally serves to ensure that companies consider the interests of a broader range of communities, as well as society within which they operate. [N. R Narayana Murthy Committee, 2003]. This paper intends to study Shareholders' Expectations on Corporate Governance. The data used for this purpose is primary and was collected from a sample of 495 respondents through a well-structured questionnaire. The main statistical techniques used for subjecting the primary data include frequency distribution, mean, SD, t test, f test and Factor Analysis. Major findings of the study revealed that the sampled respondents consider five factors, namely, 'shareholders rights', 'timeliness and adequacy of disclosure', 'trustworthiness of financial intermediaries', 'fairness and independence of the legal system' and 'treatment of foreign investors as equal to local investors', quite satisfactory across all independent variables.

Keywords: Corporate Governance, Shareholder's Perception, India

Introduction

Cadbury Committee (1992) defined corporate governance as “the system by which companies are directed and controlled...”. It deals with laws, procedures, practices and inherent rules that determine a company's ability to take management decisions with regard to its stakeholders, specifically, the shareholders, creditors and employees. [*Confederation of Indian Industry Code*]. It involves an understanding of connections between an organization's management, board, shareholders and alternate partners. Also, it gives a structure through which the objectives of the organization are formed; the way of accomplishing those targets is determined and performance monitoring is facilitated. [*The OECD Principles of Corporate Governance, 2004*].

Review of Literature

For several years, researchers in the field of corporate governance studied its various aspects. Country level investor protection and firm level corporate governance practices are interrelated and highly important to investment decisions as institutional investors who are actively monitoring their portfolio holdings are prepared and willing to engage in shareholder activism and their investment decisions appear to be related to their preferences [*McCahery et al., 2009*]. A statistically significant relation between corporate disclosures and foreign share ownership is reported by *Bokpin* and his co-authors. They documented that foreign investors consider corporate governance and disclosure practices of firms too in making their investment decisions, and avoid investing in countries with a governance regime with poor

disclosure practices; thus, international capital mobility is affected by good governance and disclosure practices [Bokpin *et al.*, 2009]. Policy makers should also continue to reform corporate governance to improve transparency and accountability to adopt international standards and to attract foreign capital [Demirbas and Yukhanaev, 2011].

Although, Raithatha and Bapat argued that corporate governance state in India might not be an important factor for FFIs to decide on buying stakes in the company and the falsehood that usually small/medium market capitalization based companies do not have a very strong and sound corporate governance was proved false. The company attributes like size, profitability, market capitalization, leverage ratio, foreign ownership, etc. are not significantly related to Corporate Governance score [Raithatha and Bapat, 2012]. Affected by disclosure practices of various governance information and quality of financial reports, the groups of institutional and individual investors exhibit different levels of confidence [Lee and Shailer, 2005].

Research methodology

The present piece of work is an exploratory study. For this study, sampling elements comprised of five hundred shareholders. The total numbers of questionnaires administered to shareholders are around seven hundred, but around five hundred twenty are received back as filled up. Of which, twenty five could not be included in the final sample due to the inadequacy of the information provided by the respondents. Finally, the responses of 495 respondents were included in the study. Five point measurement scales have been developed with a view to gaining insights, on the governance issues. Both primary and secondary data is used in present study. Primary data were solicited with the help of a structured questionnaire administered to the sampled shareholders manually and electronically. Prior to finalizing the questionnaire, a pilot survey had been carried out and it involved fifty respondents. The primary data collected through sample survey are subjected to statistical analysis with the help of SPSS 13.0 software. The main statistical techniques used for subjecting the primary data include frequency distribution, mean, SD and Factor Analysis.

Objective of the study

The present study aims to reveal the factors of corporate governance considered by shareholders while taking investment decisions in India.

Reliability of the construct: Reliability of test refers to the degree to which a test is consistent and stable in measuring what it is intended to measure. The most widely used

reliability coefficient is Cronbach's alpha which can range from 0 to 1, with higher figures indicating a better reliability. The reliability of this construct is 0.90 which indicates data is highly reliable.

Result and Discussions

This aspect covers nineteen statements which were evaluated on a five point Likert scale encompassing very low, low, neutral, high and very high. Factor analysis is used on these nineteen statements to find out the major consideration factors of corporate governance for making investment decision. Principal components method is used to find out the major factors of consideration and only the factors with Eigen values greater than one were retained for analysis. Further, the varimax rotation method is used. In addition to this, factor ranking is assigned on the basis of the overall mean value of each factor.

Table 1 Factor Analysis of Corporate Governance Variables of Consideration

Factors	Statements	Loading	Eigen values	Mean	SD	Factor Mean	Factor Rank
F ₁ : Board members' caliber and meeting schedule	Number and caliber of independent directors	0.51	7.03	2.83	1.10	2.73	4
	Caliber of members of audit committee	0.71		2.88	1.19		
	Powers given to the audit committee	0.66		2.73	1.15		
	Meeting schedule of audit committee	0.78		2.74	1.23		
	Caliber of the members of remuneration committee	0.78		2.43	1.19		
	Frequency of the board meetings held	0.61		2.88	1.10		
	Number of directorships held by directors	0.62		2.64	1.26		
F ₂ : Board's	Board effectiveness in	0.43	1.50	3.34	1.12	3.32	3

effectiveness and governance compliance status	discharging their duties and responsibilities						
	Content and quality of directors' reports	0.64		3.33	1.02		
	Effectiveness of shareholders/investors grievance committee	0.74		3.17	1.19		
	Disclosure range in corporate governance report	0.70		3.28	1.15		
	Compliance status of company to SEBI rules on corporate governance	0.71		3.58	1.14		
	Board composition	0.40		3.22	0.94		
F ₃ : Shareholders' privileges and communication means	Management profile	0.59	1.24	3.68	1.02	3.35	2
	Rights given to the shareholders	0.56		3.31	1.02		
	Shareholders' protection rules	0.67		3.39	1.15		
	Means of communication	0.67		3.01	1.07		
F ₄ : Ownership structure and shareholders' activism	Ownership structure	0.74	1.04	3.97	0.93	3.39	1
	Shareholders' activism level in AGMs	0.45		2.81	1.11		

Table 1 reveals the results of factor analysis and produces four major factors given as follows:

- i. Board members' caliber and meeting schedule (F₁)
- ii. Board's effectiveness and governance compliance status (F₂)
- iii. Shareholders' privileges and communication means (F₃)
- iv. Ownership structure and shareholders' activism (F₄)

➤ F_1 : Board members' caliber and meeting schedule:

Here, the first factor F_1 includes seven major issues, viz. the number and caliber of independent directors on board of company, caliber of the members of audit committee of company, powers given to the audit committee by the board of the company, meeting schedule of the audit committee on board of company, the caliber of the members of remuneration committee of company, the frequency of the board meetings held in a company and a number of directorships held by directors of the company.

The loading values of these factors worked out at 0.51, 0.71, 0.66, 0.78, 0.78, 0.61 and 0.62 respectively. The values of factor loadings present the correlation between the factor and variable. It implies that the factor F_1 "Board members' caliber and meeting schedule" and all seven variables are highly correlated. Keeping in view, the nature of these variables, the name for factor F_1 is considered as "Board members' caliber and meeting schedule".

➤ F_2 : Board's effectiveness and governance compliance status

The second factor F_2 , Board's effectiveness and governance compliance status, is a combination of six variables such as 'effectiveness of company's board in discharging their duties and responsibilities', 'content and quality of directors report of company', 'effectiveness of shareholders/investors grievance committee', 'disclosure range in the corporate governance report of company', 'compliance status of company with SEBI rules on corporate governance' and 'composition of board of the company'. The loading values of these variables are 0.43, 0.64, 0.74, 0.70, 0.71 and 0.40 respectively. This implies a high level of correlation between the second factor and its variables due to the high value of loading variables.

➤ F_3 : Shareholders' privileges and communication means

The third factor F_3 "Shareholders' privileges and communication means" comprises four aspects, 'management profile of the company', 'rights given to the shareholders of the company', 'shareholders' protection rules of the company' and 'means of communication used by the company to communicate its shareholders'. The loading values for these variables are 0.59, 0.56, 0.67 and 0.67 respectively. The higher loading values of variables present the high level of correlation between the factor and the variables. It implies that the third factor and its variables are highly correlated with each other.

F_4 : Ownership structure and shareholders' activism:

The fourth factor F_4 (Ownership structure and shareholders' activism) has only two sub factors 'ownership structure of the company' and 'shareholder activism level in annual general meeting of company'. The loading values of these two sub factors are 0.74 and 0.45 respectively. These values are good enough and present a high correlation between the factor and its variables.

Table 1 further discloses the value of loading, mean and SDs of variables, value of mean of factors and ranking of factors on the basis of afore-discussed mean values. It is noticed that factor F_4 (Ownership structure and shareholders' activism) having the highest mean value (3.39), falls in the first rank. The factors F_3 (Shareholders' privileges and communication means) and F_2 (Board's effectiveness and governance compliance status) obtained second and third rank with mean values of 3.35 and 3.32 respectively. The last rank goes to the factor F_1 (Board members' caliber and meeting schedule) with mean 2.73. The aforesaid rankings assigned to the factors are based on the concept that as the mean value of factors decreases, the corresponding values of their rank increases.

Conclusions and Suggestions

Shareholders are the main party who gets affected by failure of a corporate governance system. In a country like India, minority shareholders mainly invest for speculative purpose, but during the survey it was found that people who are aware of corporate governance mechanisms consider this aspect while investing their money in any company. The ownership structure and shareholders' activism is found the most considered variable by respondent shareholders. In addition, it was found that companies should also focus on its communication means because these are also considered important by respondents more than compliance status. Board members' calibre which seems important factor was not considered so much by minority shareholders.

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