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Impact of Corporate Governance on the Financial Performance of Selected BSE30 Companies in India

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Abstract

Corporate governance is very important in modern times so here we conduct a detailed investigation on how corporate governance impact the financial performance of selected BSE30 companies in India. For that purpose, we selected a sample of 10 companies from the top 30 companies listed under the Bombay Stock Exchange(BSE30). The data for 3 years starting from 2020-21 to 2022-23 taken. For the corporate governance factors, we consider board size (BS), board independence (BI), CEO Duality and board meetings (BM) as a representative of corporate governance. And are turn on equity (ROE) and return on assets (ROA) as a representative of the financial performance of selected BSE30 companies of India. We use IBM SPSS as a data analysis tool. For the purpose of study, we collect secondary data from the financial statement and the annual reports of companies from their official website. For that purpose, we perform two different tests descriptive analysis and inferential analysis. In inferential analysis, we perform two tests Pearson correlation and linear regression. This study completes that there is no impact of selected corporate governance factors on the financial performance indicator. There are some drawback of this study takes a small sample size and a short period for the study. it's suggested to take a large sample size and a long period for the study.

Keywords: Corporate Governance, Financial Performance, Board Size, Board Independence, CEO Duality, Board Meeting, Return on Equity, Return on Assets, BSE 30 Companies.

Introduction

In today's world corporate governance is a crucial part of today's modern business. It's become very important that every company follow the corporate governance principle, which builds the trust of shareholders, investors, employees and customers toward the firm. In corporate governance, there are three pillars transparency, accountability and security. Transparency requires companies to disclose all related information publicly, in the early 2000s when financial scandals came out, transparency played a bigger role in preventing it. Accountability is something that if something wrong happens in a business firm who is liable for that and everything goes perfectly then whom to thank it creates trust among the

shareholders. After making transparency and accountability a firm's shareolders, investors, employees and third parties always feel secure about company operations.

In India, before 1991 India was characterized by a controlled economy, business run in a regulated environment. Corporate governance practices were not as well-defined, and there where limited emphasis on transparency and shareholder rights. 1991 Liberalization and Economic reform proved as a turning point. Due to increased foreign investment, increased competition, and a shift to market-oriented policies the need for improved corporate governance becomes apparent. several committees were formed to examine and recommend improvement in corporate governance. The Cadbury Committee (1997), the Kumar Mangalam Birla Committee (2000), and the Narayan Murthy Committee (2003) played crucial roles in formulating policies. Many acts and regulations are imposed in India, such as the Security and Exchange Board of India (SEBI), It is the regulatory authority for the security market in India and plays a very crucial role in shaping corporate governance norms. Other than that, the Companies Act 2013 was introduced. It imposed comprehensive provisions related to corporate governance, including the role of independent directors, and audit committees.

Literature Review

There are so many studies held in the field of the effect of corporate governance on financial performance, and most of the results of the study were positive but some of them are negative also here are a few reviews of the literature:

(aggarwal, 2013)on her research paper states that corporate governance is a moral duty and also a tool for prompting the compliance of low in letter and performing ethical conduct. A researcher investigates the relationship among corporate governance and financial performance in an Indian context, for the researcher used a sample size of 20 companies listed at S&P, CNX and Nifty50 Index and used secondary data from two years from 2010-2011 to 2011-2012. The researcher used various methods and various tests like regression correlation, t-test and F-test and also controlled the size of the firm. The researcher concludes that corporate governance and corporate financial performance are correlated and governance rating has a positive impact on a company's financial performance and also suggests improving their governance structure along indicators of good governance- Leadership ethics, Board Composition and Independence. However, this research has many limitations it has a very small size of the sample, took a short period of only 2 years, and the market measure and financial performance were not considered.

(Waleed M. AL-AHED, 2020) notes the significance of corporate governance in the modern era and gives a brief overview of the historical development of corporate governance mechanisms, legal frameworks, and monitoring policies in India and the Gulf Corporation Council (GCC) Countries in their research article, The study looks into the connection between the financial performance of listed companies in the GCC and India and their corporate governance. In order to do that, the researcher selected a sample of 53 non-financial enterprises from the GCC and 53 non-financial companies from India. Secondary data for the 2009–2016 period was obtained from online sources and annual reports. According to the study, audit committees and board accountability have little effect.

The relevance of corporate governance on a firm's financial performance is stated in (Muhammad Abdul Majid Makki, 2013) their study article states the purpose of this study is to

ascertain the structural relationship that exists between corporate governance and financial performance. To do this, the researcher first creates a model that connects the two variables, which is then verified using partial least square structural equation modeling. The sample is drawn at random from the listed companies on the Karachi Stock Exchange. For the study, the researcher used secondary data from the annual reports of particular companies. PLS graph software is a tool for data analysis used by researchers. This study suggests that corporate governance can improve financial performance rather than concluding that it always improves it.

According to the research paper of (Datta, 2018), corporate governance includes encouraging ethical behavior and adherence to the letter and spirit of the law. In order to better understand the relationship between corporate governance and insurance company financial performance, the researcher examined a number of corporate governance-related factors, including board size, composition, meetings, board audit committee, and financial performance. Ten insurance businesses that are listed on the DSE were selected by the researcher as a sample. Researchers employ IBM SPSS statistical tools for data analysis, and they perform a variety of tests, including statistical, multiple linear regression, Pearson correlation, and descriptive analyses. primarily utilized by researchers

Objectives of Study

This study wants to achieve the following objectives:

- To review the available literature about the impact of corporate governance on the financial performance of different firms.
- To find an impact of corporate governance on the financial performance of selected BSE30 companies.

Hypothesis

- **Hypothesis on Board Size**

H₀: there is no noteworthy relation among board size and the financial performance of a particular company.

H₁: there is a relation amongst board size and the financial performance of a selected company.

- **Hypothesis on Board Independence**

H₀: there is no momentous relation among board independence and the financial performance of a selected company.

H₁: there is a significant relationship between board independence and the firm financial performance.

- **Hypothesis on CEO Duality**

H₀: there is no noteworthy relation among CEO duality and the financial performance of a selected company.

H₁: there is a note worthy association between CEO duality and company financial performance.

- **Hypothesis on Board Meetings**

H₀: there is no momentous relation among board meetings and the company's financial performance.

H₁: there is a note worthy association between board meetings and the company's financial performance.

Corporate Governance Factor

- **Board Size**

Board size is considered as several board directors in a company, and here we assume that some board directors have an impact on a firm's financial performance.

- **Board Independence**

Independence directors are very vital for any company, so we are taking them as one of the corporate governance factors for our study.

- **CEO Duality**

It's become very important to know whether the CEO and MD of the company are the same or not, it is assumed that it will affect the firm's performance. And we are taking "1" as a CEO and MD of the company are same and "0" as a CEO and MD of a company are not same.

- **Board Meetings**

The number of meetings conducted during the year is considered a corporate governance factor and it is assumed that it affects the firm's financial performance.

Research Methodology

- **Data**

Data for the investigation of corporate governance practice on the financial performance of selected BSE30 companies is secondary data collected from the company's official website and the annual reports of the company.

- **Sample**

Sample size of 10 companies from the BSE30 company registered at Bombay Stock Exchange (BSE). Data for the 3 years has been taken for the period of 2020-21 to 2022-23. These companies are from different sectors like banking, technology, steel industry, pharma business and many more sectors.

- **Data Analysis Tools**

For the data analysis of corporate governance practices on the financial performance of the nominated BSE30 company, we perform two kinds of tests 1. Descriptive statistics and 2. Inferential analysis in the inferential analysis, we performed Pearson's correlation coefficient and linear regression method by using the IBM SPSS tool.

Research Model

For this study of corporate governance indicators on the financial performance of selected BSE30 companies we use the liner correlation method, for that, we use some dependent and some independent variables for the study.

$$ROE = a + b_1BS + b_2BODIND + b_3CEODUA + b_4BM$$

$$ROA = a + b_1BS + b_2BODIND + b_3CEODUA + b_4BM$$

Particular	Variable	Description
ROE	Depended	(net profit/shareholders equity)*100
ROA	Depended	(EBIT/total average assets)*100
BS	Independent	Total number of directorson the board
BODIND	Independent	Total number of independent directorsonthe board
CEODUA	Independent	Duality of CEO & MD
BM	independent	Total number of board meetings held in the year

Result & Discussion

This finding states the effect of corporate governance on the financial performance indicator of selected BSE30 companies, we took the sample size of 10 companies and collected the data for 3 years. For the analysis of this study, we perform three different tests descriptive analysis, Pearson correlation and linear regression.

Descriptive Statistics					
	N	Minimum	Maximum	Mean	Std. Deviation
Return on Equity	30	-.40	31.20	17.3603	7.75747
Return on Assets	30	-.24	23.69	8.8357	6.90496
Board Size	30	9	16	11.63	1.884
Board Independence	30	4	12	6.90	1.845
Ceo Duality	30	0	1	.60	.498
Board Meeting	30	4	5	4.27	.450
Valid N (Listwise)	30				

The mean board size is 11.63, and a minimum of 9 and a maximum of 16 directors are there. According to the Indian Companies Act, 2013 section 149(1) a public company must have a minimum of 3 directors, a private company shall have a minimum of 2 directors and a person's company have a minimum of 1 director. The mean of board independence is 6.90 with a minimum of 4 and a maximum of 12 independent directors. As per the Indian Company Act, of 2013, a public company with a paid-up share capital of INR 100 should contain at least 2 independent directors. The mean of CEO Duality is .60 so it clearly states that 60% of companies have the same CEO and managing director. The mean of board meetings is 4.27 with a minimum of 4 and a maximum of 5 board meetings, and as per section 173(1) company should conduct a minimum of 4 board meetings every year.

Correlations							
		Return on equity	Return on assets	Board size	Board independence	CEO duality	Board meeting
Return on equity	Pearson Correlation	1	.799**	.507**	.410*	.140	-.174
	Sig. (2-tailed)		.000	.004	.024	.459	.358
	N	30	30	30	30	30	30
Return on assets	Pearson Correlation	.799**	1	.375*	.305	-.050	-.121
	Sig. (2-tailed)	.000		.041	.101	.793	.525

	N	30	30	30	30	30	30
Board size	Pearson Correlation	.507**	.375*	1	.703**	.206	-.003
	Sig. (2-tailed)	.004	.041		.000	.276	.989
	N	30	30	30	30	30	30
Board independence	Pearson Correlation	.410*	.305	.703**	1	.068	-.133
	Sig. (2-tailed)	.024	.101	.000		.723	.484
	N	30	30	30	30	30	30
CEO duality	Pearson Correlation	.140	-.050	.206	.068	1	.031
	Sig. (2-tailed)	.459	.793	.276	.723		.872
	N	30	30	30	30	30	30
Board meeting	Pearson Correlation	-.174	-.121	-.003	-.133	.031	1
	Sig. (2-tailed)	.358	.525	.989	.484	.872	
	N	30	30	30	30	30	30

** . Correlation is significant at the 0.01 level (2-tailed).

ANOVA ^b						
	Model	Sum of Squares	df	Mean Square	F	Sig.
1	Regression	508.179	4	127.045	2.568	.063 ^a
	Residual	1236.992	25	49.480		
	Total	1745.171	29			
a. Predictors: (Constant), BM, BOARD SIZE, CEO DUALITY, BOARD INDEPENDENCE						
b. Dependent Variable: RETURN ON EQUITY						

This table shows the relation among the variables, as per the result the impact of board size, board independence and CEO Duality have a positive relation with the return on equity (ROE), while board meeting has a negative impact on the return on equity (ROE) which is -0.174. the impact of board size and board independence have a positive impact on the return on assets (ROA) which is .375 and .305, while CEO Duality and board meeting have a negative impact on the return on assets (ROA). The relation between return on assets (ROA) and return on equity (ROE) has a positive impact which is 0.799 which is very good. The relation between board size and board independence is positive and Its value is 0.703, CEO Duality is also positively correlated to board size with a value of 0.206 while the board meeting is negatively correlated to board size. Board independence and CEO Duality are positively correlated to each other at a of value 0.068 while board independence and board meetings are negatively correlated to each other at a value of -0.133 level. CEO Duality and board meetings are positively correlated to each other at a value of 0.031 level

Model Summary				
Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.540 ^a	.291	.178	7.03418
a. Predictors: (Constant, RETURN ON EQUITY), BM, BOARD SIZE, CEO DUALITY, BOARD INDEPENDENCE				

This analysis shows the model summary of the dependent variable return on equity on the independent variables board size, board independence, CEO Duality and board meetings of the study. Here the R, R² and adjusted R² are 54%, 29.1% and 17.8%. it's concluded that the correlation between independent factors and return on equity is 54%, so we take it as a

further study. A good ratio is always 70% but if it's above 40% we take that for further study. 29.1% return on equity can be explained by the independent variable and its generalized result by 17.8% level.

Here we took the 95% confidence interval so the significant level is 5% so the significant value should be less than 0.05. in the above table, the significant value is 0.063. this concludes that the result is not significant to the study.

In the above analysis, the significant value is above the tolerance limit so there is a possibility of accepting the null hypothesis.

Coefficients ^a						
Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	5.580	14.911		.374	.711
	BOARD SIZE	1.842	1.008	.447	1.827	.080
	BOARD INDEPENDENCE	.295	1.019	.070	.290	.774
	CEO DUALITY	.758	2.696	.049	.281	.781
	BOARD MEETING	-2.844	2.955	-.165	-.963	.345
a. Dependent Variable: RETURN ON EQUITY						

So as per the above table, the significant values of the board size, board independence, CEO Duality and board meeting are 0.080, 0.774, 0.781, 0.345 and the constant value significant value is 0.711 and for the rejecting the null hypothesis the significant value should be less than 0.05. and hear all the factor values are greater than 0.05, so the null hypothesis is accepted.

Model Summary				
Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.414 ^a	.172	.039	6.76866
a. Predictors: (Constant), BM, BOARD SIZE, CEO DUALITY, BOARD INDEPENDENCE				

This is the modal summary of the dependent factor return on assets on the autonomous factors. The R, R² and adjusted R² are 0.414, 0.172 and 0.039, which show that independent factors and return on assets correlate 41.4%. and 17.2% return on assets explained by independent factors. This result generalized at 3.9%.

ANOVA ^b						
Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	237.306	4	59.327	1.295	.299 ^a
	Residual	1145.368	25	45.815		
	Total	1382.674	29			
a. Predictors: (Constant), BM, BOARD SIZE, CEO DUALITY, BOARD INDEPENDENCE						
b. Dependent Variable: RETURN ON ASSETS						

Here we take a 95% value confidence interval, so the significant level is 5%. if the significant value is less than 0.05 then the result is significant. But hear the significant value is 0.299 so this result is not significant for the study.

Coefficients ^a						
Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	.238	14.348		.017	.987
	BOARD SIZE	1.383	.970	.378	1.426	.166
	BOARD INDEPENDENCE	.125	.981	.033	.127	.900
	CEO DUALITY	-1.753	2.594	-.126	-.676	.505
	BM	-1.712	2.843	-.112	-.602	.553
a. Dependent Variable: RETURN ON ASSETS						

As per the above value, the significant values of board size, board independence, CEO Duality and board meeting are 0.166, 0.900, 0.505, 0.553 and the constant significant value is 0.987. and for rejecting the null hypothesis significant value should be less than 0.05. and the all four factors value are greater than 0.05 so the null hypothesis of all four independent factors was accepted.

Conclusion

Corporate governance is one of the important aspects of the firm so we conduct a study on the impact of corporate governance on the financial performance of selected BSE30 companies. As per the study it's found that there is no significant impact between the corporate governance factor of board size, board independence, CEO Duality, board meeting and the financial performance of a firm. To find out the impact of corporate governance on financial performance we make a null hypothesis that there is no significant impact of corporate governance on financial performance. As per the significant value of the regression analysis, the null hypothesis was accepted. Corporate governance factors board size, board independence, CEO Duality and board meetings have no impact on the financial performance indicator return on equity (ROE) and return on assets (ROA).

Limitations

This study comprises many confines. The study takes a small sample size which is only 10 BSE30 companies. A part from them, the time period of the company is very short term only 3 years of data from 2020-2021 to 2022-2023 taken, which is a very short period. This study took only four variables for the study board size, board independence, CEO Duality and board meeting, which are less. Also financial performance indicators are only two. other vital factors that are important for the study, are not considered into the study.

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