Impact of Corporate Governance on Financial Performance: A Study on Selected Commercial Indian Banks

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Abstract: ***After 2008 global financial crisis, COVID-19 Crisis represented to be the most fundamental threat to the financial stability of a banking sector. Global Financial crunch made the Corporate Governance more prominent in banking sector. In India regulatory and supervisory standards with regards to appointment, roles and responsibility, remuneration, risk management, audit, evaluation of Board of Directors are the significant areas of good corporate governance which needs to be effectively enforced at individual level. The present study attempt to examine the impact of certain governance characteristics over the financial performance of selected 3 commercial public and private sectors banks over a time span of 2018-2022.Secondary data of 30 firm entries of banks collected on the basis of market capitalisation from their corporate governance report of banks which were analysed using panel regression through fixed effect model in which certain governance parameters like Board Size and No. of Independent directors having negative insignificant impact over the financial performance indicator i.e. ROE whereas the rest of variables like No. of female director, Board Meeting, and Executive director having positive significant impact over the financial performance indicator of the banks. Although with the constraints of time availability and sample present in study result will not be generalise for other categories but with more variability in governance variables and performance indicators research study will provide better insight to investors to take proper investment decision. Also not just regulation and code of conduct alone but risk management strategies and audit needs to be followed all the time by every directors to promote dynamic and stable financial sector.***

Keywords: Corporate Governance, Financial Performance, COVID-19, Risk management

1. Introduction

Corporate governance defined to be a process by which various activities in an organisation is regulated and controlled. It is a process by which firm frame various policies and the long term strategies and it help to govern the senior members and to monitor their plans, actions and decisions. It is a mechanism which govern the Board members to act in the interest of all the stakeholders (Customers, Creditors, managers, shareholders, auditors, regulators etc.).Corporate governance becomes a significant matter of policies and corporate practices and more prominent concept in today's complex environment where Indian market are highly complex in nature the role of corporate governance brings more transparency and financial viability and makes the Board of management powerful in decision making.

During Covid crisis we have seen a drastic change in an Indian Economy which not only affected the individuals at personal level but also various business firms got collapsed and faced bad financial crunch. COVID 19 put up various challenges and it forced businesses to reframe their strategies, to bring more financial viability, transparency in the system. Post COVID crisis stressed more on the aspect of corporate governance like accountability, communication, fairness etc. In order to bring sustainability in the business financial regulator like SEBI issues strict guidelines to improve the compliance of Corporate Governance. SEBI lay down various policies which comprehend and strengthen the internal management through their regulatory guidelines. In a banking sector RBI lay down various regulatory guidelines which improvise the financial performance of the business. Also Basel Committee norms in a banking sector sets high standards for maintaining transparency with their stakeholders. Good governance practices will enable to improve the financial performance and it provide fair return to investors and equal treatment of all the stakeholders and it help the management to achieve both individual interest and public interest.

Banking sector play a prominent role in Indian economy through their leaps and bounds in past years specifically during COVID crisis where the high inflation rates, government deficit, rigid monetary policies, low foreign reserves, unamortised liabilities and high rates of NPA becomes a major hurdles for the banking sector. However, with the passage of time role of board structure changed also strategic decision making, effective internal control system, sense of hierarchy and coordination between the management and the Board make this study more dynamic and comprehensive in nature.

To improve the financial performance of business no.of internal and external factors affects but Board of directors play a major role to maintain the financial viability and their significance become more crucial in financial sector after post covid crisis. The main function of Board of Directors is to appoint and supervise the activities of senior members, to give assistance to management, formulate a strategic plan, and to ensure its responsibility and accountability towards all the stakeholders. Board of directors structure consist of mainly two types of directors i.e. Independent Directors and the Executive Directors. Executive directors need to see the management of resources and the control of operations. Independent Directors influence the decisions of management and they have got expertise in their area of work, maintain transparency, improve the level of compliance and maintain the interest of the minority shareholders as well. Whereas the main objective of Executive directors is to protect the stakeholders interest considering the self -individual interest. Existence of both types of directors in a firm makes Internal Corporate Control more effective and efficient. Good governance is necessary is to maintain the economic sustainability and it will also improve the financial system of the country.

Several Studies have been conducted on the banking sectors with reference to pre and post effects on financial performance of Indian banking sector, opportunities and challenges in banking sector, considering factors like inflation, savings, investments, Basel 3 recommendations, financial crisis, NPA's, Risk management and the several initiatives of Government faced by the Indian Financial System. Present scenario of a banking sector where the NPA's and money laundering activities raised which posing a questions over the efficiency of banking operation and management and Board of directors are accountable to all strategic planning and policies and in majority of financial frauds happened around the globe in banking sector is due to inefficiency and malpractices done by Board Members. Thereby the present study attempts to define the effects of board constituents over the financial performance of the banks since over the period of 5 years. This research paper shows an extend research in the area of corporate governance in banking sector with reference to public and private sector banks and their impact over the financial performance.

Corporate Governance and Banks:

The banking sectors play a significant role in the recent economic times in a most emerging and complex Indian economy. The main function of the banking and financial institutions is to lend money and to protect the saving of investors and to keep on maintaining the trust and the confidence over the banking operations. Compare to other sectors banking sector having wide and different implications as they have strict guidelines from regulators. Banking firms shows significant difference in the nature of operations compared to other sectors. Because of their differences in their organisational structure and complexities in operations and a payment mechanism process it become noteworthy to follow a proper governance procedure. In a banking sector regulators play a stringent role to watchdog over the various activities like money laundering it is their responsibilities to keep investor vigilant about unfair means and protect them from credit risk, operational risk, market risk. Reserve bank of India play a significant role in framing the monetary policies, supervise the lending activities, make rules for maintain balances of reserve and generate various financial reports from banks to strengthen the financial system by developing various banking reforms. The major pros of this sector it's a regulated industry but still various factors like Inflation, Change in government policies, Current Fiscal deficit, Increased repo rates, Increasing NPA rates, Increasing Restructure Loans, Unstructured Loans, Increasing Interest rate in Saving deposit , Implementation of Basel III Norms etc are the important factors which are the barriers in growth of banks in Global market. Several comprehensive and intangibles roles of Board of directors like interdependency of board members for the planning and policy and decision making, quality of work, leadership and direction of Board members at a managerial level, Internal Control, Strategic planning play an equally important role in the success and the failure of the banks. These are the variables which are difficult to quantify but having significant impact over the performance of the banks. Several other factors are untouched and sometimes become a major hurdle in the progression of banks. Those few factors like High leveraging investments, delays in project implementation, Higher operating cost due to inefficiency in day to day activities of management and Drastic and sudden fluctuations in capital market stop them get equity access, Unamortised loans etc. The reason behind highlighting these major issues in Indian Banking Industry is to bring some stringent governance practices, improvisation in role of internal management and the board of directors, restructuring board composition etc to bring the quality functioning of the firms. Hence, The Board of Directors has to govern all the major activities of business, need to supervise the activities of managerial officers, to appoint executive officers, to comply with all companies laws, to look after internal control ,to deal with managerial affairs, implementation and execution of all strategic plans and policies, to built a transparent support system for their stakeholders. To communicate and aware them with the financial conditions of banks all these factors become a major concern for the governing body thereby board composition ,their role and activities towards management become a concern for the study. Hence this research study has been done to investigate the impact of governance variables over the bank performance through financial performance indicator.

2. Literature Reviews and Hypothesis Development

Dr. Pandya (2011) in her research work "Corporate Governance Structure and financial performance of selected banks" Board structure and CEO duality considered as a independent variables in which financial performance assesses using ROE and ROA. Sample consist of 8 public and private Sector banks. Study resulted that there is no significant relationship between proportion of Board Structure and Financial Performance.

Agarwal (2013) conducted a research study over "Impact of Corporate Governance over Financial Performance" Using a sample of 20 companies listed on S & P CNX Nifty 50 Index. Various test like regression. t-test, F-Test have used for a secondary data for the financial year 2010-11,2011-12. Study resulted that governance ratings have positive significance over the financial performance. Employee related and environmental dimensions also significantly influence the corporate financial performance. Also control variable shows firm size shows significant impact over the financial performance.

Kumar & Nihalani (2014) done a research study on "The Effects of Corporate Governance on performance on Indian Banks" They have shown the comprehensive effects of Board Characteristics (Which includes women directors, board size, number meeting and busy meetings). Performance Indicators like Return on Equity, Return on Assets, Return on long term funds, Earning per share used to see impact over financial performance. Board of directors play a significant role in return earned on long term funds.

Dr. Maheshwari and Meena (2015) done analysis on "Corporate governance practices: A Comparative study of HDFC and SBI. The main objective of their study is to analyse the good corporate governance practices also to determine the financial and non-financial disclosures in SBI and HDFC. Secondary data collected from annual report of 2013-14.Overall it is observed that SBI is maintaining best practices with regards to Corporate governance large number of board of directors with reference to non-executive directors whereas negative aspects like whistle blower policy, review of chairman for various committee, dematerialisation of shares, director appointment or re-appointment etc.

Dr. Raja & Dr. Shah (2015) conducted a research work over the "Corporate Governance and Financial Performance: An empirical Study. Sample of Nifty 50 companies selected.ROA and ROE selected as a dependent variable and Board Structure, ownership, remuneration and Independent Directors consider as a Independent Variable. Block Holders and Duality found to have significant impact over financial performance while rest of variables have insignificant impact over profitability.

Handa (2018) done a research study over "Does Corporate Governance affect over the financial performance: A study of Selected Banks" By considering sample of 8 banks and taking ROE as a dependent variable. Using the panel regression model they found that Chairman, CEO Duality, average remuneration of directors, board committees, female directors place a significant role in the performance of the company.

Mandal & Al-Ahdal (2018) done a research study over the "Impact of Corporate governance on Financial performance of Indian Electronic Consumer Good Firms. For the study purpose sample of 7 active electronics consumers goods companies of India and he goods have been selected as per market Capitalisation. Independent variables like Audit Committee, Audit Committee meeting, Audit Committee Independence. The dependent variables ROA, ROCE. The result of their studies shows that there is significant relationship between board Size. audit committee, firm size having positive impact over the financial performance.

Dr. Kiradoo (2019) conducted a research study on "Impact of Corporate Governance on the Profitability and the financial performance of the Organisation". For this purpose, relationship between CEO Duality, Board Size and Ownership with Organisational Performance. Profitability is an important factor in all the corporate which increased with the organisational performance. Also they added on that Strategic Planning, Transparency and Accountability and their ethical decisions which place them on a advantageous position. Communication and the cyber security helps to maintain the proper Internal control and make the organisational structure effective.

Bezawada (2020) conducted research study on "Corporate Governance Practices and Bank Performance: Evidence from Indian Banks". Busy directors and the number of meetings have a positive significance on bank performance. Also they found that percentage of Independent directors and the Busy directors have a negative impact over the net non-performing assets ratio. Board size has a negative impact on the Tobin's Q and percentage of busy directors have a positive impact on Tobin's Q and Board Size have a negative impact on Bank Performance.

Hypothesis development:

All the previous research work pointed that the Board of Directors and their role in the management will tend to have a greater significance in determining the performance of banks. Information Asymmetry, Stringent government laws, compliance with company laws, frequent changes in governance practices makes more difficult for the investors to take a investments decision. Although regulators brings out stringent rules and laws and as they work as a interpose between the interest of society and the management and for the sake of their own benefit they perceived governance as an issue not a necessity. Significance of Board of directors not only found in Indian Context but also having corner in International Context. As per International Context researchers mainly focused on several factors in research study like Board meetings, Board Size, No. of Independent Directors, No. of Women Directors etc. Also the role of Board of directors in the overall functioning of the firm is unexplored in various aspect and in various other developed countries like USA. In this research study we mainly explore certain governance characteristics and their impact over the financial performance of the banks.

For this purpose, the main objective of this study is to validate the necessity of certain governance characteristics like Board Size, its structure, its composition, No. of Board Meetings No. of independent directors and their significant impact over the performance of the banks. We need to determine the positive and negative impact of those variables over the performance of the banks. Data will be analysed using the panel regression model to see the changes in the variables over the period of time and to check their impact over the performance indicator. In a simple words it can be written like, No. of meetings held in a year generate the positive impact over the ROE which shows that the higher the no. of meetings held of a Board of Directors results into higher return will be on investments.

Specifically, total five board Characteristics has been considered as a part of corporate governance to check their impact over the financial performance of the banks:

Board Size: Brahmaiah Bezawada (2020) shows the negative impact of Board Size over the TOBINS'Q model which shows a negative effect over financial performance. Also the larger the size of board result into improvement in the quality work, and it increase the operating efficiency and Capital of Business.

No. of Board Meetings: More no. of meetings held in a year keep the management effective and it leads to increase the co-operation and co-ordination among the members. Direction can be give in a effective way. On the other hand more of meetings also result into more usage of resource in terms time and money. Anshuman Kumar & Yatin Nihalani (2014)in their study shows the positive impact over the financial performance of the firms.

No. of Women Directors: Female directorship concept has got more of significance in international context but now in India as well it has been mandatory to have atleast one women directors in a firm. Rekha Handa (2018) and Anshuman Kumar & Yatin Nihalani (2014) conducted a study in which they have shown a significant impact of women directorship over the financial performance but it is also true that their dominant behaviour can insignificantly affect performance too.

Executive Directors: Many a times this term is refer in similar to the role of CEO but the board is led by Executive directors. Executive directors act as a chief whip leading the opinion of the entire board. In case of financial institutions there may be no of executive directors and more number of human resource leads to create conflict in decision making.

Independent Directors: Role of independent directors is to safeguard interest of all the members who are directly connected to the firm .Since these directors have not any material relationship with the company so they do not have any undue influence from the Board management. Brahmaiah Bezawada (2020), Dr. Abhay Raja & Dr. Hitesh Shah (2015) in their study shows a negative significance of independent director over the financial performance which might be a result of information asymmetry.

Data Collection, Methodology and Variables:
The Present Study shows an attempt to identify the effects of Corporate Governance Variables over the Financial Performance of the banks. For this Purpose, we have used a sample of 6 Banks particularly 3 from Private Sector and 3 from Public Sector which have been chosen with the time duration of 5 years. The scope of the Study is limited to few Independent variables like Board Size, Board Committee, Board meetings, Executive directors etc have been selected as a factors affecting financial performance. Secondary data collected from the annual report of these sample banks. This research study covers a time period from 2016 to 2020.

Therefore, results based on total entries will be analysed using descriptive statistics and panel regression analysis. Because of having trend of time series and cross sectional analysis panel regression model has been used to analyse year wise as well individual group and it brings more of variability in the data

Variables: In order to analyse the effects of corporate governance over financial performance of selected banks the most common financial performance indicator have been used i.e. ROE. ROE is calculated by taking a ratio of EBIT and the average total equity at the end of each year. Independent directors, Board meetings, Board Size, Board Committee. Financial information were obtained from www.moneycontrol.com

Dependent Variables	Description
ROE	It's a ratio between net income and the total banks equity at the end of each year
Independent Variables	
Board Size	Total no.of Board of Directors
Board Meetings	No.of Board meetings held in a year
Executive Directors	No. of Executive Directors
Board Committee	No. of Board Committees
Independent Directors	No. of Independent Directors
Women Directors	No .of Women Directors

The above mentioned variables in Table 1 have been used as an Independent variable in the study. The assumption of Board size is that the larger no. of members in a board represent the efficient functioning but at a same time it does involve the complexity and delay in decision making process. With the observation that it may decrease the financial performance of the business because of miscommunication and low cooperation among the and higher cost of hiring and training for the board members. Another variable which has been covered is no. of female directors the presence of female directors in Board Committee is now made it mandatory as per Companies 2013.Board committee facilitates proper governance structure with the defined roles of board members and effective functioning of the board committee affect the financial performance of the banks. Frequent Board Meetings results in to consistency and active participation but at the same time it no. of meetings also affect productivity of the members. Board meeting helps in strategic decisions and monitoring and implementing all the decisions. An Executive director commonly referred as full time directors of the firm it act as a leader, implement policies and actively involve with the daily operations at managerial level and which may affect the financial performance positively or negatively. Independent directors look more after the creditability and improving the business standards and they do not have any material relationship with the board and they protect the interest of investors which also does affect the financial performance of business.

Thus, these governance parameters are found to be more feasible to examine their impact on the financial performance of the selected public and private sector banking firms.

3. Result Discussion and Analysis

Table 1: Descriptive Study for the variables of the study

Descriptive Analysis						
Variables	N	Mean	Median	Standard Deviation	Minimum	Maximum
ROE (%)	15	3.75	2.13	11.71	-32.85	16.91
Board Size	15	11.53	11	2.5	7	20
Board Meetings	15	12.6	13	4.04	7	22
Executive Directors	15	3.83	4	1.34	2	7
Independent Directors	15	6	5.5	1.85	4	12
No. of Women Directors	15	1.5	1	0.14	1	3

Source: Author Calculations

The Descriptive statistics have been used to describe or summarise the characteristics of a sample or data set. It help the data to be presented in a more understandable manner. It includes variables such as Mean, Median, Maximum, Minimum values. These variable all together help to understand the impact of governance characteristics over financial performance. Table 1 given a overview of change in pattern of various variables. Mean value of ROE 3.75 which indicates selected banks are taking more of financial leverage. It shows that overall the banks are generating more of its profits from its assets. Higher the ratio indicates better return on investments. With respect to ROE the maximum value recorded as 17%.The mean of Board Size seen to be 11.53 and the maximum value reported to be 20 which is higher than the statutory requirement 15 as per Companies Act 2013.As larger boards helps to resolve various issues and maintain an effective internal control. All banks fulfilling the mandatory requirement of atleast one women director and the maximum value derived is 3.The overall average percentage of female director is low of 1% which justifes that banks just fulfilling the statutory requirement and they least focused on managerial skills of women in a business. Also the average proportion of independent directors shows 6 which signify that banks are complying all the legal requirements with a lower value 4 and maximum value 12 and the mean value of Board meeting is 12.6 and it also exceeds the mandatory requirement of companies act of four meetings in a year which highlight the efficient n active board members participation and cooperation among them. The average proportion of full time directors in a banking business is 3.83 which signify that banks fulfilling the legal compliance of executive directors and maximum value is 7 which shows that banks are effectively carrying out their banking operations and decision making work and more of their contributions helps in business for strategic planning.

Table 2: Year wise mean value of variables

Year	2018	2019	2020	2021	2022
Observations	15	15	15	15	15
ROE(%)	-1.30	0.985	7.146	8.305	10.991
Board Size	10.66	13.33	11.33	13.33	10.66
Board Meetings	10.5	11.5	12.66	14.5	13.83
Executive Directors	3.66	4.16	3.83	3.66	3.83
Independent Directors	5.67	7	6.5	7	5.67
No. of Women Directors	1.5	1.5	1.5	1.5	1.5

Source: Author Calculation

Considering the Performance based measures the dependent variables ROE as mentioned in above table 2 shows a constant increase in the value of it over the period of last five years. A constant positive changes in a value of ROE states the clear picture of positive impact of board variables over the financial performance of the banks**.** Average of no. of women directors remain stable around 1.5.Also in a values of Independent Directors there is no major changes reported over the periods of the study. Minimum 4 meetings requirement of board meetings should held in year as per Companies Act 2013 fulfilled by all banks more than that frequent board meetings shows that board members are actively participating the in all strategic planning and discussion over the risk management and implementation of good governance practices. The average value of Board Size lies between 11 to 13 which signifies that the effective n efficient decision making but at a same time bring the conflict in their opinions which can hindrance the growth of the firm.

Panel Data Regression:

In order to analyse the objective of the study, characteristics of the variables, time period of the study cross sections panel data regression techniques have been used to show the impact of corporate governance variables over the financial performance of the banks. To analyse the impact of different time series with a dependent variables ROE over various Independent Variables like No. of Board Committee, Board Meetings, Executive Directors, Independent directors, women directors. Firstly, Pooled least square estimate techniques have been used with the assumptions that different sample for each time period intercept for all the variables are constant. By considering the effect of heterogeneity in a sample and to allow control for time-invariant unobserved individual characteristics correlation with observed independent variables fixed effect model to be used. Variability in dependent variables as well their correlation with other independent variables does not help to generalise and draw a random conclusion. To select the best fitted model redundant effect ratio applied from the pooled results to check the whether the dependent variables are significant or insignificant to independent variables.

With the results of redundant effect ratio models it is to be stated that the p value of both the cross section F and Cross section chi-square is 0.16 and 0.04 respectively which is less than 0.05 indicated the fixed effect model is the best fitted for the study.

Table 3: Result of Fixed Effect model

Independent Variables Dependent Variables: ROE	Output
Constant	-0.094979 (0.9253)
Board Size	-0.455552 (0.6539)
Board Meeting	0.324689 (0.7490)
No. of Female Directors	0.455521 (0.6594)
No. of Independent Directors	-0.392211 (0.6993)
Executive Director	0.917682 (0.3703)
R^2	0.697654

Adjusted R^2	0.538524
Number of Observation	30
F Statistics	4.384183 (0.002767)

Source: Author Calculation (Results obtained from E-Views)

The above values indicate the results of redundant effect of Fixed Effect model with the significance of F ratio as a good fit. The Adjusted R^2 value represent that around 54 percent of the financial performance of the sample banks effected by the ROE. Also the value of R shows the influence of the independent variables over the dependent variable. Prob F statistics shows the p value of F test is 0.0002 which is less than 0.5 which indicate rejection of H0 with a specification that there is strong significance of Independent variables of corporate governance over the dependent variables of financial performance i.e ROE. Board Size shows lack of significance and also shows negative influence over the financial performance which justifies the results of prior studies conducted Brahmaiah Bezawada (2020), Dr. Meenu Maheshwari and Sapna Meena (2015), Hemal Pandya (2011).Overall the variables found to be statistically insignificant .Board size found to be statistically insignificant that too evidences by the panel result of fixed effect model. Negative p value of it indicate that the large board size is not enough in making good strategic planning and policies which can impact the financial performance. Larger the size of board results in to differences over the views and conflict in strategic decision which affect the co-ordination and co-operation among the members which results in lowering the financial performance. The more of board meeting in a year indicate that the board members are consistently and effectively improvising over strategic planning more of communication resulted into better decision making process and Internal control. In study it indicates a positive significant relation with the financial performance of selected banks. Presence of female directors positively affects the banks financial performance and this relationship stands on test of significance. The explanations to this direction of relationship can possibly emerge from the more number of women directors on the Indian boards promote the culture of gender diversity and equality but at a same time it also raises the issues of domination in decision making process and thus in long term it may affect the financial performance of the board. Independent directors is a member of a board of who does have any pecuniary relationship with the company except sitting fee. They improve the creditability and the governance standards of the firm and also helps in managing risk. In a study it resulted a negative and insignificant relation with the financial performance. Many a times it has been observes the interference of the independent director in the day to day operation hindrance the financial performance of the banks. The role of Executive director is significant and shows the positive impact in preparing policies, long terms goals and to implement various strategic decision. They are full time directors responsible for Steering the organisations and managing its operations. The above result indicates the positive significant relation of executive directors and the financial performance which indicate that their effective skills of managing resources, banking operations, leading and motivating employees which scale up the overall banking business.

4. Conclusion

Financial Institutions having major role in NPA, credit risk management and to ensures proper utilisation of different resources, profitable investment and to maintain enough liquidity in business. Corporate Governance got prominent space in Global financial market after world biggest corporate scam like Enron and in India it got more of significance after 1990. Complexities of banking operations, Changing Paradigm over the period and cutthroat competitions across the globe, increasing up share of financial scams all over the country become a vital factor for the bringing up stringent governance practices and fair disclosures by regulatory authorities. Post Pandemic resulted into Global market recession and inter dependency of financial market of different countries on each other which give rise to formation of rigid policies by regulatory authorities make this study more relevant. At a primary stage of the study secondary data collected over a period of 5 years from the corporate governance reports to see the effects of corporate governance variables over the financial performance of the study. Corporate governance variables like Board Size, Board Meeting, No. of Independent directors, female directors and Executive directors etc considered as an Independent variable to see the financial viability over Dependent variables i.e. ROE. Data of 3 private and 3 public sector banks collected based on their market capitalisation which was analysed using Panel Regression Model. This test is specifically conducted to check the interdependency of variables over the different time period. Study resulted a insignificant and negative impact of Board Size and No. of Independent directors over the financial performance of selected banks. Rest all Independent variables like Board Meeting, No. of female directors, and the Executive Directors having a positive significant impact over the financial performance of the banks.

The study shows an evidence of Board Attributes over the financial performance but limitation of sample under this study requires more of descriptive study to generalise the result on a large database. Also there is scope of further more research in same area by focusing on some additional measures of performance indicators and governance variables which can give deep insight and new dimensions to the existing study.It will be helpful to the investors to take better investment decisions. Also it will help the academicians and the researcher to go for further research in same domain.

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