Impact of Corporate Governance on Financial Performance during the Post Companies Act 2013 period: Evidence from Pharmaceutical Companies

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Abstract

The Companies Act 2013 was implemented with effect from 2015. The legislation was much sought after since many changes in the field of Corporate Governance were introduced in the Act. The stock exchange regulator SEBI also brought about momentous changes in the listing agreement in order to make Corporate Governance more effective.

The study has framed two sets of indexes, one for the phase before the implementation of the Companies Act. The index is based on the SEBI clause 49 agreement 2013, Voluntary Guidelines on Corporate Governance 2009 and literature on pharmaceutical companies. The other is index related to the period after the introduction of the Companies Act 2013. This index is based on SEBI (LODR) 2015 Voluntary Guidelines on Corporate Governance 2009 and literature on pharmaceutical companies. The study has identified four sets of variables which influence Corporate Governance. Mandatory, Non Mandatory, Voluntary and Industry specific variables. Corporate Governance scores of 92 pharmaceutical companies is computed on the basis of a five point scale. The scores for five years 2009-10 to 2013-14 and three years 2014-15 to 2016-17 have been separately found out and have been regressed against five financial ratios EVA, MVA, Tobin's Q, ROE and ROA. The aim is to study the impact of Corporate Governance on the financial performance before and after the introduction of the Companies Act, in order to see if any positive change has been noticed. The study could be helpful to know if the momentous changes made in the Corporate Governance has positively impacted the financial performance of pharmaceutical companies and also to help in future policy formulation.

Key Terms: Corporate Governance, CG Score, Mandatory variables, Non-Mandatory variables, Voluntary Variables, Industry Specific Variables.

Introduction

Ever since the adoption of market friendly policies by the Indian Government since 1991, India has witnessed a phenomenal growth in the Stock Market and the corporate sector. But, at the same time corporate scams and frauds, have also been witnessed in the Indian corporate scene. From being a set of voluntary suggestions to a code of mandatory requirements supported by legal and regulatory mechanisms, the journey of Corporate Governance in India has been interesting. The first effort towards better Corporate Governance was made by the industry itself. The Confederation of Indian Industry gave a voluntary code in 1998. This was followed by the Kumarmangalam Birla Report in 2000 which was sponsored by SEBI. Following this report SEBI enacted clause 49 amending the Listing agreement. SEBI further formed the Narayan Murthy committee report to bring about further improvement in Corporate Governance; consequently the clause 49 was further amended in 2006. The Ministry of corporate affairs also formed the Irani Committee in 2004 and the Naresh Chandra Committee in 2009. As a result the Ministry of corporate affairs brought about a set of voluntary guidelines in 2011 and also a number of amendments in the Companies Act. In 2013 the Parliament adopted the Companies Act which introduced far reaching changes in the field of Corporate Governance and Corporate Social Responsibility. The Companies Act finally became effective in 2015. The SEBI also introduced SEBI(Listing obligations, and disclosure requirements) replacing Clause 49 in September 2015 which aims to bring in new Corporate Governance norms in order to ensure that the corporate sector in India reaches a level that is much higher and which is in keeping with the best in the world.(SEBI chairman UK Sinha).

The pharmaceutical sector is considered to be one of the few sectors which can lead India to a place of eminence in the world export scene. The sector which was virtually 'nonexistent' in the 70's has become a pillar of India's growth. It is recording a growth of 8% to 9% annually and presently estimated to be worth $ 4.5 billion. There are about 20,000 registered a large number operating in the corporate form. The competition is fierce in the sector as reflected in the sphere of prices. At the same time government control on prices is high. The Indian government permits 100% foreign equity participation along with duty free imports of all inputs and products. India's pharmaceutical industry is about 3.1 to 3.6% of the world industry in terms of value and about 10 % in terms of volume. The Indian Brand Equity Foundation opines that the sector would grow to US $ 100 billion by 2025, in its report of 2017.

Such mammoth growth would necessitate that skilled scientists would be given key roles in organization structures in strategic processes both as decision makers and stockholders (Lacetra 2000). The Pharmaceutical corporates also need to invest heavily in R&D because there exists a strong and positive relationship between R&D costs and profitability of Pharmaceutical companies (Hajiheydari, Dastgir and Sultani 2011).Corporate Governance happens to be a 'key element' in R&D investment (Hillier, Pindado, Queiroz &Torre 2011).

Literature Review

The extent of research on the issue of Corporate Governance has been phenomenal during the past two decades. This has resulted in the accumulation of a lot of literature on several aspects of Corporate Governance. Srinivasan Padmini and Srinivasan Vasanthi (2011) have concluded that top five themes emerge in international journals on Corporate Governance in India are on Performance, Corporate Social Responsibility, Governance origins and models, Disclosure, Regulatory mechanism and reforms. They further opine that of all the themes relating to Corporate Governance in International Journals, performance is the most sought after theme claiming 36.4% interest. Studies on the impact of Corporate Governance on financial performance have been carried all over the world in countries such as Nigeria, Canada, India, Pakistan, Greece, China, Hong Kong, Malaysia etc. Vintila and Gherghira (2012) found a negative relationship between Corporate Governance sub-indices and firm performance with some exceptions. Bagchi (2012) conducted an analysis of the relationship between the Corporate Governance of firms and their Corporate Market performance. He found that no abnormal returns were earned by different portfolios constructed on the basis of Corporate Governance Index. Mukhopadhyay, Malik and Dolly. (2012), conducted a study on 237 medium sized family companies. They concluded that Corporate Governance leads to improved financial performance. Md.Shamimul Hasan and Normah Omar (2015), concluded that a significant positive relation exists between board independence and market capitalization in the market. At the same time the research found that a negative relation exists between public ownership and market ownership. Akshita Arora, and Shernaz Bodhanwala (2018), support the view that compliance with good Corporate Governance practices leads to better accounting and market performance and reduction in agency costs. Virender S., Poonia, Vandana (2018), have studied the role of EVA as compared to other performance measures in analyzing the financial performance of selected pharmaceutical companies. They have established the relative importance of EVA. Jyotsna Ghildiyal Bijalwan, Dr. Pankaj Madan (2013), suggest a positive relation between the size and composition of the board and firm performance but indicate a negative relation between ownership structure and performance. Lian-fu Ma, De-qiu Chen, Yun-jia Zhong (2009), study the relationship between mandatory and voluntary Corporate Governance on firm performance. While it was found that mandatory governance has no major effect on firm performance, voluntary governance improves performance. Rajya Lakshmi Kandukuri Laila Memdani, P. Raja Babu, (2015), suggest an interdependent relationship among profitability measured by Tobins Q and Corporate Governance. Merugu Venugopal and M Ravindar Reddy (2016), conducted a study on 77 pharmaceutical companies during the period 2007-15.They conclude that investors prefer firms with positive EVA, while those with negative EVA are not able to cover cost. EVA based performance framework improves financial performance. Lorne N. Switzer and Tang Minguin (2010) made a comparative study of small cap and large cap companies during periods of boom and depression. The study suggests that small cap companies tend to exhibit a better performance as compared to large cap companies during the year subsequent to a period of depression but lag behind the large cap during the year before the boom phase. N.Sakthivel, (2011) made a study on 15 pharmaceutical companies to evaluate the trend and growth of shareholders' value in terms of Economic Value Added and MVA Market Value Added. The study supports the view that the sampled companies have been able to meet the shareholders expectations in terms of value creation. Santhosh Abraham Claire Marston Edward Jones, (2015), attempted to study levels of observance of mandatory and voluntary requirements in two periods–before and after the amendments to clause 49. It has been found that the extent of compliance of mandatory disclosures is high among the sampled companies. The disclosure levels have also shown a significant improvement after the amendments as a result of increased penalties suggested in the amendment. Laallam, A., Alom, F.,Mohamad, A. (2017), sought to study the impact of the various features of Corporate Governance and the Malaysian code amendments of 2012 on performance of 162 listed companies. The study reveals the existence of a positive relationship between 'Corporate Governance and firm performance' on the basis of both accounting and market based ratios. It also points out to a negative relationship between Corporate Governance amendment and accounting based performance measures.

The various studies on firm performance have made use of indexes based on rating methodology to measure the extent of Corporate Governance. The studies on the various indexes used reveal that one index cannot be used for all studies. Separate indexes based on the requirements of the study have to be built. Various financial measures have been used whic may be divided into market based such as MVA, Tobins Q, EVA etc and other measures such as turnover, total assets, Return on Equity, Return on Assets etc. Recently EVA has attracted a lot of attention from researchers. Despite the large volume of literature on firm performance and Corporate Governance, unanimity is lacking with regard to results.

Literature relating to Corporate Governance and Pharmaceutical industry

Baysinger et al. (1991) found that high insider representation on a Board and a concentration of equity among institutional investors positively affected corporate R&D spending. Casper and Matraves (1997) revealed that UK firms developed new competencies in biotechnology and other research areas in response to the structural changes. But German firms continued to strengthen competencies in traditional research methods based on organic chemistry. Lacetra (2001) has highlighted the increasing importance being placed in the pharmaceutical industry on biotechnology and life sciences which has led to emphasis being placed on innovative activity. The paper proposes industry specific variables for pharmaceuticals including internal settings as well as relations with external actors. Gray and Skogsvik (2004) empirically investigate voluntary disclosure practices of a few selected Swedish and UK Pharmaceutical companies. The paper finds some similarities in the Voluntary Disclosure practices of the companies of the two countries with regard to R&D activities whereas disclosures pertaining to business growth and forecasts of net incomes have been more prevalent in Swedish companies. The companies have not shown information relating to tangible and intangible assets to the expected levels. Cai, Keasey and Short (2006) highlight the impact of governance characteristics on information efficiency in the security market. The paper holds that lack of diversity in the composition of members in board of directors is directly proportional to information asymmetry in the market. Lee and Kohler (2010) study the increasing trend among Pharmaceutical companies to benchmark their Corporate Social Responsibility performance and its impact on increasing access to medicines. The paper demonstrates the importance of benchmarking and transparency in creating inter business competition and the translation of these responses to actual access to medicine practices.

An analytical study of the literature reveals that the work on Corporate Governance has undergone both a quantitative and qualitative improvement over the last 20 years or so. Research has been undertaken on a number of variables such as the impact of market efficiency, insider information, environmental performance, risk disclosures, equity holding pattern, R&D spending, human resource practices, etc. on Corporate Governance levels of companies. Most of the research has been undertaken in US and UK, some of the research is of cross national nature, few researches have been conducted in Indian conditions covering Indian regulatory framework. Even few researches have been conducted in industry specific conditions. While it is widely recognised that there is need for more empirical research in Indian context which explore the institutional contextual realities of India (Padmini Srinivasan 2011).

Research Gap

A review of literature reveals that despite the availability of so much work on the issue of Corporate Governance various issues remain unresolved or need more intense study to be useful to the policy makers. Most of the research still remains confined to developed countries, research in developing countries such as India is relatively less and much more needs to be done. Most of the research is general in nature but to be useful, research should be conducted for specific conditions (Lee and Kohler 2010). In India the promulgation of the Companies Act 2013 with a clear focus on Corporate Governance, has opened up new avenues for research. The various rating techniques have inherent limitations and one technique cannot be used for any other study. There is need to evolve an index which can satisfy the objectives of the study. Performance measures used in the various studies have been restricted to two or three measures. More performance measures need to be incorporated in the study. Very few studies have been conducted to study the impact of reforms such as the Companies Act or the SEBI (LODR) on the performance of companies. There is need to bridge this gap.

Rationale of the study

The literature leaves a lot of scope for future research. The study has been made on 92 pharmaceutical companies listed on the Bombay stock exchange. The pharmaceutical sector has been selected for the study in view of its strategic importance in the present day Indian Economy. The sector has certain peculiar Governance issues which need to be incorporated in the study. These issues are often overlooked in studies which not industry specific. The focus of the new Companies Act is Corporate Governance. Several changes have come about with an aim to make the corporate scene in India receptive to the demands of Corporate Governance and also to make India's corporate world meet the world standards. There is therefore need to study if the Act has made any tangible impact on the performance of companies and compare it with the period before the Act came into force.

Thus the study will revolve around the hypothesis

Ho1 There is no significant impact of Corporate Governance on financial performance of pharmaceutical companies during the Pre Companies Act phase.

Ho2 There is no significant impact of Corporate Governance on financial performance of pharmaceutical companies during the Post Companies Act phase.

Ho3 the level of impact of Corporate Governance on financial performance has not improved in the Post Companies Act 2013 period as compared to the earlier period.

Organization of the paper

The paper has been divided into five portions. The first portion relates to introduction, the second to theoretical perspectives and past research, third relates to research methodology, the fourth portion deals with analysis discussion and findings and finally the last portion relates to conclusion and directions for future research.

Research Methodology

Sample size and sampling method

The BSE lists companies on the basis of categories. The pharmaceutical sector showed a list of 163 companies on the active list on 21st January 2017. The website Report Junction which is a repository of Annual Reports was evaluated to search for annual reports of all the pharmaceutical companies for the period 2010 to 2017. Since the data was not available for all the companies only those companies were selected which had data for the entire period. The data finally consisted of 92 companies (736 observations). Since the study involves comparison of two time periods the data was grouped into Pre Companies Act 2013-five years 2010 to 2014 and Post Companies Act 2013-three years 2015 to 2017.

Index formation

Most of the previous studies have taken recourse to indexes based on various parameters to measure the extent of Corporate Governance. In the present study two indexes for the Pre Companies Act 2013 and Post Companies Act 2013 periods have been framed. The rationale is that since the Corporate Governance mechanism has undergone a huge change because of the promulgation of the Companies Act 2013 a single index would not be adequate to measure the level of Corporate Governance. Previous studies have selectively identified a few variables that impact Corporate Governance, the present study has taken into account all the variables mandatory and non-mandatory as mandated in the clause 49 of the listing agreement of SEBI for Pre Companies Act period and SEBI (LODR) 2015 provisions. In addition the present study has also included the voluntary variables as given in the Voluntary Guidelines on Corporate Governance 2009 because Corporate Governance is not restricted to legal provisions alone. Since the study is specific to pharmaceutical companies, certain Corporate Governance variables peculiar to pharmaceutical industry have been identified. The Pre Companies Act 2013 index contains 90 variables whereas the Post Companies Act 2013 contains 118 variables.

Scoring: Each of the variables within the sets have been evaluated on a five point scale. Various studies have used a two point (Yes or No) scale. But, such a methodology suffers from the drawback that the scale is quantitative rather in qualitative. For a scale to be qualitative five point scale becomes more relevant.

Each of the variables within the sub parts have been assigned equal weights whereas each of the sets of variables have been assigned weights.

1. Mandatory variables have been assigned 1 weight because such variables are required by the regulations and non-observance will result in penalties to the defaulting companies. Previous research shows that most companies have tended to observe these norms.
2. Non mandatory variables have been assigned 2 weight because although the variables are discretionary in nature but since the companies are required to disclose the extent of observance / non observance, the companies are obligated to disclose whether they have observed or not observed these variables in their Report on Corporate Governance.
3. Voluntary Variables have been assigned 3 weight because adoption of such norms is completely at the discretion of the company and it has been observed that companies have not shown an inclination to adopt such variables.
4. Industry specific variables are assigned the largest weight 4 because such variables reflect the commitment of the company towards disclosure of international best practices relevant to the pharmaceutical industry.

CG Score is calculated taking the total of the score generated by a company in a particular year and dividing it by the total maximum score.

Thus

Pre Companies Act 2013 CG Score = Total score /695

Post Companies Act 2013 CG Score = Total score / 800

To test the reliability of the index a study was conducted on 30 companies for two years of Pre Companies Act 2013 period and two years post Companies Act 2013.

Financial parameters

Various previous studies have employed different financial ratios to evaluate the performance of companies. Three approaches have been used

1. Accounting Ratios approach, Bayoud, Kavanagh and Slaughter, (2012),
2. Market Value Ratios approach, Arnold, Bassen and Frank, (2012) and
3. Mixture of accounting and market based approach, Mulyadi and Anwar, (2012).

In the present study the Value based ratios EVA, MVA and Tobins Q have been used along with accounting ratios ROA and ROE.
The financial data was accessed from the CMIE Prowess database.

1. EVA = NOPAT – WACC x (CE)

NOPAT = Net operating profit before interest after taxes = Net Profit +Interest (1-t).

WACC = Weighted Average Cost of Capital

CE = Capital Employed

2. MVA(market value added) = Market capitalization – Equity

Market capitalization = (Mkt price highest + Mkt price lowest)/2 X No. Of Equity shares

3. Tobin’s Q = (Mkt value of Equity + Mkt value of Debt)/(Book value of Equity +Book value of Debt)

It is assumed that market value of debt is equal to its book value

4. Return on Assets = Net Income/Average Total Assets

5. Return on Equity = Net Income/Shareholders’ Equity

Linear Regression Model

Linear Regression models have been developed to understand the relationship of the overall CG score (independent variable) and financial performance – EVA, MVA, Tobin’s Q, ROA and ROE (dependent variables). The model also helps to predict the quantum of impact of independent variables on the dependent variables.

Five Regression models that shall be tested in this study are

$EVA = \beta 0 + \beta 1\ CG\ Score + \varepsilon$
$MVA = \beta 0 + \beta 1\ CG\ Score + \varepsilon$
$Tobin's\ Q = \beta 0 + \beta 1\ CG\ Score + \varepsilon$
$ROA = \beta 0 + \beta 1\ CG\ Score + \varepsilon$
$ROE = \beta 0 + \beta 1\ CG\ Score + \varepsilon$

Data analysis and interpretation

A. Comparison of Corporate governance levels during the Pre Companies Act 2013 and Post.

A paired sample t test has been carried out after evaluating normality of the data, to evaluate if the levels of corporate governance have improved during the post phase or not.

Table 1 **Paired Samples Statistics**

		Mean	N	Std. Deviation	Std. Error Mean
Pair 1	Pre CG Score	.4584	92	.05722	.00597
	Post CG Score	.5448	92	.08374	.00873
Pair 2	Pre MV	.6146	92	.07188	.00749
	Post MV	.6369	92	.08326	.00868
Pair 3	Pre NMV	.3924	92	.07846	.00818
	Post NMV	.4064	92	.10243	.01068
Pair 4	Pre VV	.3231	92	.04930	.00514
	Post VV	.4935	92	.07717	.00805
Pair 5	Pre ISV	.2745	92	.09978	.01040
	Post ISV	.2920	92	.17657	.01841

Source: Author's calculations

Table 1 reveals that Mean values across all dimension have improved in the Post Companies Phase

Table 2 **Paired Samples Correlations**

		N	Correlation	Sig.
Pair 1	Pre CG Score & Post CG Score	92	.566	.000
Pair 2	Pre MV & Post MV	92	.609	.000
Pair 3	Pre NMV & Post NMV	92	.225	.031
Pair 4	Pre VV & Post VV	92	.430	.000
Pair 5	Pre ISV & Post ISV	92	.574	.000

Source: Author's calculations

The above table shows that correlation during the pre and post phases is weak but positive across all dimensions.

Table 3

Paired Samples Test

		Paired Differences					t	df	Sig. (2-tailed)
		Mean	Std. Deviation	Std. Error Mean	95% Confidence Interval of the Difference				
					Lower	Upper			
Pair 1	Pre CG Score - Post CG Score	-.08634	.06977	.00727	-.10079	-.07190	-11.871	91	.000
Pair 2	Pre MV - Post MV	-.02230	.06935	.00723	-.03666	-.00794	-3.084	91	.003
Pair 3	Pre NMV - Post NMV	-.01399	.11419	.01190	-.03763	.00966	-1.175	91	.243
Pair 4	Pre VV - Post VV	-.17048	.07153	.00746	-.18529	-.15566	-22.859	91	.000
Pair 5	Pre ISV - Post ISV	-.01754	.14463	.01508	-.04749	.01242	-1.163	91	.248

Source: Author's calculations

The study shows that overall CG Score, Mandatory variables, and voluntary variables have significantly improved during the Post phase whereas the Non mandatory variables and industry specific variables have improved but not significantly

B. Impact of Corporate Governance on financial performance during the Pre Companies Act 2013 Phase

Table 4 has been constructed as a summary of the five models during the Pre Companies Act 2013

			ANOVA		Coefficients			Model
S.No		R^2	F	Sig	β	t	Sig	
1	**Constant** **Pre EVA**	.048	4.570	.035b	.220	-1.828 2.138	.071 .035	Pre EVA = -3392.167 + 8586.444
2	**Constant** **Pre MVA**	.118	12.078	.001b	.344	-3.056 3.475	.003 .001	Pre MVA = -189817.261+ 467254.983
3	**Constant** **Pre Tobin's Q**	.137	14.301	.000b	.370	-2.791 3.782	.006 .000	Pre Tobin's q = -6.675 + 19.577
4	**Constant** **Pre ROA**	.091	8.973	.004b	.301	-2.145 2.995	.035 .004	Pre ROA = -.130 + .394
5	**Constant** **Pre ROE**	.032	2.937	.090b	.178	-1.218 1.714	.226 .090	Pre ROE = -0.305 + 0.930

Source: Author's calculations

Predictors: (Constant), Pre CG Score

Dependent variables: Pre EVA, Pre MVA, Pre Tobin's Q, Pre ROA, Pre ROE.

The data has been subjected to Durbin Watson test to know the extent of autocorrelation. Since the values are near 2 in all cases, the test is satisfied.

Table 4 reveals that for Pre EVA, Pre MVA, Pre Tobin's Q, Pre ROA the regression model statistically predicts the outcome since p<0.05. Hence the fitness of good criteria is met. However in the case of Pre ROE p>0.05 which indicates that the data is not a good fit. The R^2 values are less than 1 in all the situations which proves the association between the predictor and dependent variables is low. One unit of CG Score results in 8586.444 increase in Pre Eva. One unit of CG Score leads to an increase in Pre MVA by 467254.983. Similarly Pre Tobin's Q increases by 19.577 and Pre ROA by .394 respectively. The Pre ROE also increases by .930 for every unit change in Pre CG Score.

Thus the null hypothesis that the financial ratios do not depend on Pre CG scores will be rejected for Pre EVA, Pre MVA, Pre Tobin's Q and Pre ROA. The null hypothesis that Pre ROE does not depend on Pre CG score is accepted. .

C. Impact of Corporate Governance on financial performance during the Post Companies Act 2013 Phase

Table 5 has been constructed as a summary of the five models during the Post Companies Act 2013

			ANOVA		**Coefficients**			**Model**
S.No.		R^2	F	Sig	β	t	Sig	
1	**Constant** **Post EVA**	.034	3.152	.079^b	.184	-1.451 1.775	.150 .079	Post EVA = -3840.714 + 8528.318
2	**Constant** **Post MVA**	.082	8.092	.006^b	.287	-2.329 2.845	.022 .006	Post MVA = -311384.356 + 689950.969
3	**Constant** **Post Tobin's Q**	.006	.539	.465^b	.077	.172 .734	.864 .465	Post Tobin's Q = 0.908 + 7.043
4	**Constant** **Post ROA**	.107	10.798	.001^b	.327	-2.457 3.286	.016 .001	Post ROA = -0.147 + 0.357
5	**Constant** **Post ROE**	.037	3.503	.065^b	.194	-2.014 1.872	.047 .065	Post ROE = -3.558 + 6.000

Source: Author's calculations

Predictors: (Constant), Post CG Score

Dependent variables: Post EVA, Post MVA, Post Tobin's Q, Post ROA, Post ROE.

The data satisfied the Durbin Watson test to determine the extent of autocorrelation as the values in all cases were near 2.

Table 5 reveals that the R^2 values for all financial ratios are too low which explains that the association between Corporate Governance in financial performance is low. The significance values are greater than .05 for Post EVA, Post Tobin's Q, and Post ROE which explains that Post CG does not impact these ratios of financial performance. However in the case of Post MVA and Post ROA p < .o5, which explains that the data is a good fit and these financial ratios are dependent on Post CG.

One unit increase in Post CG score results in increase in Post EVA to the extent of 8528.318, Post MVA by 689950.969, Post Tobin's Q by 7.043, Post ROA by 0.357, and by 6.000 in the case of Post ROE.

Thus the null hypothesis that the financial ratios do not depend on Pre CG scores will be rejected for Post MVA, and Post ROA. The null hypothesis that Post EVA, Post Tobin's Q and Post ROE does not depend on Pre CG score is accepted.

D. Comparison of Pre and Post Companies Act 2013 positions

A comparison of Table 4 and Table 5 has been made to understand the extent of improvement in the impact of Corporate Governance on financial performance. On making a paired comparison of the various values it is observed that the association between Corporate Governance and the financial performance has gone down as observed in R^2 values of the post companies act phase. Similarly the values corresponding to per unit of Post MVA and Post ROE has improved as compared to Pre MVA and Pre ROE. In all cases the values have gone down, which indicates that Corporate Governance significantly impacts only MVA and ROE significantly during the Post Companies phase while in the case of all other financial performance measures there is no relation with Corporate Governance during the Post Companies Act Phase.

During the Pre Companies the significant relation between Corporate Governance and financial performance was observed in case of all measures except ROE, but during the Post Companies Act phase the significant relation did not exist in case of three ratios EVA, Tobin's Q and ROE.

Thus it can be concluded that the relation between Corporate Governance and financial performance has become weak during the Post Companies Act phase as compared to the Pre Companies Act phase.

Findings

The study finds that the pharmaceutical companies have shown improvement in overall CG score which indicates that the new Companies Act has propelled the Companies to implement the Corporate Governance provisions in a better manner. However this is true in case of mandatory variables and not in case of Non Mandatory and industry specific variables. These results are in tune with an earlier study conducted by Avtar Singh, Dr Sukhdev Singh (2018). The reason seems to be that noncompliance of mandatory variables entails heavy penalties, whereas the companies merely have to show which non mandatory variables they have adopted and which they have not adopted. These results are in tune with earlier studies such as Ntim et al., (2012) and Krambia –Kapardis and Psaros (2006). The relationship between Corporate Governance and financial performance has been the subject of debate in recent years and the results have not been clear enough to give direction to the managers or policy makers. But it is expected that there should be a positive impact of Corporate Governance on financial performance and vice versa. Akshita Arora and Chandan Sharma (2016) have in their study concluded that the relationship between Corporate Governance and financial performance does not seem to be very strong in Indian companies. Similarly Goel, Puneeta (2018) holds that the reforms in the sphere of Corporate Governance have not impacted financial performance during the reform period. Our study is more or less on similar lines. Although it would not be correct to say that there is absence of relationship but it has become, to some extent weak in the Post companies Act phase in the Pharmaceutical sector. This phenomenon is disturbing as it is considered desirable that improvement in Corporate Governance should lead to an improvement in the financial performance of the company especially after reforms, in the field.

Managerial Implications

Our study holds immense importance for the policy makers and managers as it suggests that mere reforms cannot produce desired results in the face of poor implementation of the laws. The Indian legal system is slow and violations are not checked effectively as can be made out from the recent cases of corporate frauds including the those involving Vijay Mallya (Business Today March 14, 2019) and Nirav Modi (Business Today March 9, 2018). There is need to increase penalties manifold along with a check on bureaucratic and political interference.

Limitations

It is necessary to consider the limitations confronting the present study. The CG scores are based on indexes which have taken recourse to a rating methodology involving a five point scale. Although the Annual reports have been scanned multiple times and the indexes have been tested for consistency but the element of subjectivity remains. The study is limited to the study of the impact of Corporate Governance on financial performance, it is felt that a reverse study should also be made to see to what extent financial performance impacts the Corporate Governance of firms. Another area which can be explored is the unlisted firms since the study is confined only to listed pharmaceutical firms. The comparison of pre and post periods can be made taking into account a larger period for the Post companies act period since the study has taken only three years into consideration. Reforms generally take a longer time to show an impact. It would be desirable if a study involves at least five years for the post companies act phase..

Conclusion

Corporate Governance levels have been studied during the Pre and Post Company Act 2013 phases and a comparison has also been made. The Pharmaceutical companies as revealed in previous studies have improved their Corporate Governance levels as reflected in their overall CG Scores. They have also improved in disclosing Mandatory Variables and Voluntary Variables. They have not significantly improved disclosures in the matter of Non mandatory and industry specific variables. As far as the impact of Corporate Governance on financial performance is concerned it is observed that the relationship has not gone down but has weakened during the Post Companies Act 2013 phase.

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