A STUDY ON CORPORATE GOVERNANCE AND FINANCIAL PERFORMAMCE OF SELECTED BANKS IN INDIA

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Abstract

Banking industry plays a very important role in the development of economy. Effective corporate governance is recognized as an important tool for the success of banks. Good governance strengthens the investor's confidence. The aim of this study is to analyze the board structure and financial performance of selected Indian banks listed in the stock exchange. The study aims to examine the relationship between the board independence, and women director in the board and their effect on financial performance. Return on Asset and Earnings per share are taken as financial variables. The study utilizes the secondary data from the annual reports and other web sources of selected public and private sector banks listed in the stock exchange for the period of 2015-2018.Data collected are analyzed by using Pearson's coefficient correlation and ordinary least square regression using SPSS.

Keywords: Return on Asset, Earnings per share, Board independence and corporate governance.

Introduction:

An effective system of corporate governance is considered as crucial in aligning the interest of board of directors with shareholders (Hemal Pandya, 2011). The directors have a very important role in the governance. . According to Fama and Jensen (June, 1983),"Board of directors are the common apex of the decision control system of organization". To improve the effectiveness of directors and corporate governance of banks, the Reserve bank of India and SEBI are the two important regulatory bodies empowered to regulate and maintain the required standards. RBI being a regulator of banking sector in India has an important role in formulating, implementing and promoting the standards of corporate governance (Dr.Nayantara Padhi and Dr. kamal Vagrchan, 2017). As per SEBI regulations, an optimum combination of executive and non-executive directors is required. The board comprises of not less than 50% of non-executive directors; at least one women director and one third of independent directors if the chairman of the board is regular non- executive director and one-half if the chairman is not a regular non-executive director.

In this paper, attempt is taken to analyze the relationship between board structure and financial performance of selected banks in India listed in stock exchange. The study focus on two aspects of composition of board , percentage of board independence and at least one women director in a board, as corporate governance variables. If the banks satisfy the SEBI norms then dichotomous 1 is used otherwise 0 and Return on asset and Earnings per share as a financial performance variable of the banks.

CORPORATE GOVERNANCE

An emerging issue in the area of management is the aspect of corporate governance and its impact on firm value and return for shareholders (Mishra et al., 2001; McConaughy et al., 1998; Black et al., 2003).According to Catherwood,"Corporate governance means that company manages its business in a manner that is accountable and responsible to the shareholders, in wider interpretation, corporate governance includes company's accountability to shareholders and other stakeholders such as employees, suppliers, customers and local community." Good governance practice leads to stability in financial and sustainable economy.

CORPORATE GOVERNANCE IN BANKS

Banks play a dominant role in the development and stability of an economy. In case of instability in the banking sector, the entire economic stability may impact adversely. Therefore effective corporate governance is needed for the economic stability. RBI plays major role in regulating the banking industry in India. RBI is continuously interacting with SEBI and Govt., to ensure the best practice of corporate governance in banking industry in India. Over decades, many amendments and revisions were made in banking sector with regards to corporate governance. In India, many committees are formed in regard to corporate governance. Dr. Bimal Jalan, Governor of Reserve Bank of India had made a first announcement in regard to corporate governance. A Standing committee on International Financial Standards and codes was set up under the chairman of Dr. R.H. Patil; the consultative group of director of banks/ financial institutions was set under the chairmanship of Dr. A.S. Ganguly; The Advisory group on banking supervision was set under the chairman of Shri. M.S.Verma; further committee was set up to review governance of boards of banks in India under the chairmanship of J.P.Nayak;

BOARD STRUCTURE

"The journey of creating conductive boardroom practices begins with composition of board." "The composition of board is combination of both dependent and independent directors."(Twinkle Prusty & Saurabh Kumar (2016). An independent, non- executive director doesn't have affiliation with the firm except directorship (Clifford and Evans, 1997). Fama and Jensen(1983) suggest that non-executive directors play a vital role in the decision making process and effective resolution in agency problem. According to revised clause 49 of Equity Listing Agreement, Securities Exchange Board of India (SEBI), The composition of Board should follow the following criteria:

1. "The Board shall have an optimum combination of Executive and Non-Executive directors with at least one women director and not less than fifty percent of the board of directors comprising non-executive directors"
2. "If the chairman of the board is a non-executive, one-third of the board should comprise of independent directors and if the board doesn't have regular non-executive chairman, at least half of the board should be independent directors.

   Where the regular non-executive chairman is a promoter of the company or is related to any promoter of the company or is related to any promoter or person occupying management position at the board level or at one level below the board, at least one-half of the board shall consist of independent director."

   Source-(SEBI, circular, CIR/CFD/POLICY CELL/2/2014)"

REVIEW OF LITERATURE

Many papers are reviewed to know the previous research on the board structure and financial performance. Palaniappan Gurusamy (2017) "examined the relationship between board characteristics, audit committee and ownership structure on financial performance of the selected manufacturing firms listed in BSE and found that board size are positively and significantly have relation with financial performance but negative and significant with Tobin Q. Audit committee is negative and insignificant with ROE." Bonn (2004) " investigate the composition of board of directors in large Australian firms and analyze the board structure on financial performance and result showed outsider ratio and female ratio is positively associated with financial performance whereas board size and directors age is not having influence on firm performance." Kenneth A. Borokhovich, Robert Parrino, Teresa Trapani (1996),"document a strong positive relation between percentage of outsider and frequency of outsider CEO succession." Fitriya Fauzi and stuart Locke (2012), "examines the board structure role and its effect of ownership on firms performance in New Zealand listed firms and the results revealed that there is a significant impact ." Hemal Pandya (2011) studies the effect of board structure and CEO duality on performance in Indian Banks and result revealed that there is no significant relation."

OBJECTIVES

1. The aim of this study is analyze the relationship between corporate governance and financial performance in the selected public and private sector banks listed in the stock exchanges in India
2. To study about the effect of board structure on ROA and ROE.

STATEMENT OF HYPOTHESIS

H01: Proportion of Independent directors has no significant effect on ROA

H02: Proportion of Independent directors has no significant effect on EPS.

H03: There is no significant relationship between women director in board on ROA.

H04: There is no significant relationship between women director in board on EPS.

DATA COLLECTION

The study utilized the secondary data from the annual report and web source of concerned selected listed six public sector banks and six private sector banks in India.

Earnings per share and Return on Asset are used as financial performance variability and data of the same are collected from www.moneycontrol.com.

Board Independence and women director on the board are used as a corporate governance variability and data of the same are collected from annual report of concerned banks web portal and from www.bseindia.com.

SCOPE & LIMITATION OF STUDY

The study is limited to the randomly selected public and private sector banks listed in India for the three financial period of 2015-2018.

ANALYSIS & INTEPRETATION

The data collected percentage of independent directors, women directors, ROA and EPS, from different sources are analyzed by using Pearson correlation coefficient and ordinary least square regression to know whether there is a relationship with financial performance. SPSS package is used to analyze the data.

Corporate governance variable s, percentage of independent directors and women director in the composition of boards is taken as an independent variable. Corporate governance variable being dichotomous variable, 1 is given if the banks compliance with SEBI norms otherwise 0.

Return on Asset and Earnings per Share are used as dependent variable. Return on Asset is taken as a percentage and Earnings per Share is calculated with Net profit to outstanding share. The financial performance data are collected from www.money control.com.

Result on Correlation

Table 1 shows the result of Pearson's correlation coefficient of Return on Asset (ROA) with independent variables namely percentage of Independent directors (ID) and Women Directors (WD). ROA is negatively correlated with ID and WD and all are insignificant and the null hypothesis is accepted.

Correlations			
	ID	WD	ROA
ID	1	0.945	-0.439
WD	0.945	1	-0.122
ROA	-0.439	-0.122	1

Table 1: CORRELATION OF ROA, ID AND WD

Table 2 shows the result of Pearson's correlation coefficient of earning per Share (EPS) with independent variables namely percentage of Independent directors (ID) and Women Directors (WD). EPS is negatively correlated with ID and WD and all are insignificant and the null hypothesis is accepted.

Correlations			
	ID	WD	EPS
ID	1	0.945	-0.751
WD	0.945	1	-0.495
EPS	-.751	-0.495	1

Table 2: CORRELATION OF EPS, ID AND WD

Result on Regression Analysis

Regression Analysis on Return on Asset and Percentage of Independent directors:

Table 3, 4 & 5 show the results of Analysis of Variance and coefficient of the variables, ROA and ID. The value of F is 0.239 at significance of 0.711 which result that there is no significance between ROA and ID. The coefficient of ID is of -0.439 at significance of 0.711 and it shows a negative relationship between ROA and ID.

Table 3

Table 3:**Model Summary**

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.439[a]	.193	-.614	.5161880
a. Predictors: (Constant), Independent director				
b. Dependent Variable: Return on Asset				

Table 4:**ANOVA**

Model		Sum of Squares	Df	Mean Square	F	Sig.
1	Regression	.064	1	.064	.239	.711[b]
	Residual	.266	1	.266		
	Total	.330	2			
a. Dependent Variable: Return on Asset						
b. Predictors: (Constant), Independent director						

Table 5: **Coefficients**

Model		Unstandardized Coefficients B	Unstandardized Coefficients Std. Error	Standardized Coefficients Beta	t	Sig.	95.0% Confidence Interval for B Lower Bound	95.0% Confidence Interval for B Upper Bound
1	(Constant)	1.674	2.977		.562	.674	-36.148	39.495
	Independent director	-1.861	3.808	-.439	-.489	.711	-50.252	46.529

a. Dependent Variable: Return on Asset

Regression Analysis on Return on Asset and Women director:

Table 6, 7 & 8 show the results of Analysis of Variance and coefficient of the variables, ROA and WD. The value of F is 0.015 at significance of 0.922 which result that there is no significance between ROA and WD. The coefficient of WD is of -0.122 at significance of 0.922 and it shows a negative relationship between ROA and WD.

Table 6: **Model Summary**

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.122[a]	.015	-.970	.5702318

a. Predictors: (Constant), Women director

b. Dependent Variable: Return on Asset

Table 7: **ANOVA**

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	.005	1	.005	.015	.922[b]
	Residual	.325	1	.325		
	Total	.330	2			

a. Dependent Variable: Return on Asset

b. Predictors: (Constant), Women director

Table 8: **Coefficients**

Model		Unstandardized Coefficients B	Unstandardized Coefficients Std. Error	Standardized Coefficients Beta	t	Sig.	95.0% Confidence Interval for B Lower Bound	95.0% Confidence Interval for B Upper Bound
1	(Constant)	.573	2.834		.202	.873	-35.441	36.587
	Women director	-.390	3.167	-.122	-.123	.922	-40.627	39.846

a. Dependent Variable: Return on Asset

Regression Analysis on Earnings per share and Women director:

Table 9, 10 & 11 show the results of Analysis of Variance and coefficient of the variables, EPS and WD. The value of F is 0.324 at significance of 0.671 which result that there is no significance between EPS and WD. The coefficient of WD is of -0.495 at significance of 0.671 and it shows a negative relationship between EPS and WD.

Table 9: **Model Summary**

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.495[a]	.245	-.510	7.7929083

a. Predictors: (Constant), Women director

b. Dependent Variable: Earnings per share

Table 10: **ANOVA**

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	19.686	1	19.686	.324	.671[b]
	Residual	60.729	1	60.729		
	Total	80.415	2			

a. Dependent Variable: Earnings per share

b. Predictors: (Constant), Women director

Table 11: **Coefficients**

Model		Unstandardized Coefficients B	Unstandardized Coefficients Std. Error	Standardized Coefficients Beta	t	Sig.	95.0% Confidence Interval for B Lower Bound	95.0% Confidence Interval for B Upper Bound
1	(Constant)	33.443	38.735		.863	.547	-458.733	525.618
	Women director	-24.639	43.277	-.495	-.569	.671	-574.520	525.242

a. Dependent Variable: Earnings per share

Regression Analysis on Earnings per share and Percentage of Independent director:

Table 9, 10 & 11 show the results of Analysis of Variance and coefficient of the variables, EPS and ID. The value of F is 1.294 at significance of 0.459 which result that there is no significance between EPS and ID. The coefficient of ID is of -0.751 at significance of 0.459 and it shows a negative relationship between EPS and ID.

Table 12: **Model Summary**

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.751[a]	.564	.128	5.9213122

a. Predictors: (Constant), Independent director

b. Dependent Variable: Earnings per share

Table 13: **ANOVA**

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	45.353	1	45.353	1.294	.459[b]
	Residual	35.062	1	35.062		
	Total	80.415	2			

a. Dependent Variable: Earnings per share

b. Predictors: (Constant), Independent director

Table 14: **Coefficients**

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.	95.0% Confidence Interval for B	
		B	Std. Error	Beta			Lower Bound	Upper Bound
1	(Constant)	50.178	34.146		1.470	.380	-383.685	484.041
	Independent director	-49.687	43.687	-.751	-1.137	.459	-604.787	505.413

a. Dependent Variable: Earnings per share

CONCLUSION

In this study, an attempt is taken to analyze the relationship between corporate governance and financial performance of banks in India, listed in the stock exchange. The study utilized the secondary data and Pearson's coefficient correlation and ordinary least square regression is used to analyze the data. The result showed a negative correlation between Independent directors, Women directors and ROA and EPS and there is no significant relationship. Therefore hypothesis is accepted. Many researches result a positive and significant relationship with corporate governance and financial performance and findings of this paper may differ as the sample size is small and need to consider other variables.

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