Corporate Governance and Value Creation: Indian Experience

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ABSTRACT

Corporate governance is a complex issue, the focal point of which is the exercise of power. The power has limits, however, imposed by both legislation and contracts. Also, even if the overarching power belongs to the shareholders, residual power cannot be exercised to the detriment of the rights of the other stakeholders. Because the governance system and resulting structures have a major influence on the decision-making processes within a company, financial analysts must understand the governance mechanisms. Moreover, in the business world today, corporate governance is a factor in competitiveness that is as important as the quality of a company’s human resources, its know-how, and its innovation capacity. Through in-depth literature review and contextual analysis the aim of this paper is to understand the corporate governance perspective and also to review for understanding the corporate governance and value creation experience from India.

KEYWORDS

Corporate, Government, India, Laws, Power, Shareholder, Stakeholders, Stock Exchange

INTRODUCTION

Corporate leaders should practice good corporate citizenship not merely for the sake of complying with rules and regulations in order to avoid fines—or worse, prison—but to create value for their shareholders (Baporikar, N., 2015a). The silver lining in the dark cloud of corporate misconduct is the intense focus on corporate governance by board members, corporate managers, policymakers, media and especially, investors. The well-publicized scandals at Enron Corporation, Tyco International, and WorldCom/MCI, latter Satyam and Shraddha Chit Funds together with transgressions within the asset management, insurance, and securities industries, have brought back the focus on the issue of corporate governance.

India, though not much adversely affected by the global financial crisis has been unnerved by the largest corporate accounting scandal at Satyam Computers Limited. According to an estimate shareholder and investors have lost not less than $2.8 billion (Tellis, 2009). It is now well understood that corporate misconduct has very unpleasant consequences, not only for those who perpetrate the misdeeds but also for employees and shareholders whose jobs and wealth are destroyed thereby leading to decline in value creation for the individual stakeholder and society at large. Hence, the term ‘corporate governance’ though only two decades old, has evolved with the incorporation of modern day business structure albeit in latent form (Singh & Kumar, 2009). Recent Satyam fraud further...
gives some evidence that dominant shareholders and some employees were involved in insider trading (Singh, Kumar & Uzma, 2010). Satyam-Maytas deal resulting in exposure of Satyam scandal is a typical example (Sharma, 2011) of not only poor corporate governance but also of negative value creation. Over the past two decades, there has been a sea change in Indian corporate governance. The chronological development can be seen below:

1996: Confederation of Indian Industry’ (CII) CG Task Force  
1998: CII Code  
1999: Security and Exchange Board of India (SEBI) Appointed Birla Committee  
2000: Enactment of Clause 49  
2002: SEBI Appointed Murthy Committee  
2002: MCA Appointed Chandra Committee  
2004: MCA Appointed Irani Committee and Clause 49 Amended  
2006: Clause 49 Amendments Implemented  
2009: Satyam Scandal, Companies Bill, Considered MCA Voluntary and CCI CG Guidelines  
2010: NASSCOM CG Recommendations and Listing Agreement Amended  
2013: Companies Act

When the Indian economy was liberalized in the 1990s, it created greater opportunities for private and foreign investment within the country. The needs of India’s expanding economy, including access to foreign direct investment, the increased presence of institutional investors (both domestic and foreign), and the growing desire of Indian companies to access global capital markets by being listed on stock exchanges outside of India, have spurred corporate governance laws (Black & Khanna, 2007). In this backdrop, of an expanding economy and an increasing level of domestic and foreign players, a need for regulation of economic activities was required. In this context, corporate governance reforms were seen to be as essential and mandatory requisites. However, whether corporate governance has led to value creation is still an enquiry at nascent stage. Through in-depth literature review and contextual analysis based on secondary data, policies and documents the aim of this paper is to under the corporate governance perspective and also to review the evolutionary understanding of the corporate governance and value creation experience from India. Thus this paper, examines whether and to what extent corporate governance linkage to value creation exists.

The term ‘Corporate Governance’ refers to a system that ensures the regulation of companies in India, for the benefit of its stakeholders, and aims in bringing about transparency and accountability in its performance. The element of transparency is usually with respect to information shared by the companies to its stakeholders. Accountability, on the other hand, ensures the precision of audits performed by such companies. India’s largest business association, the ‘Confederation of Indian Industry’ (CII) came up with a corporate governance code in the year 1998 for listed companies in the country. According to this code, “Indian companies, banks and financial authorities can no longer afford to ignore better corporate practices. As India gets integrated in the world market, Indian as well as international investors will demand greater disclosure, more transparent explanation for major decisions and better shareholder value”. (CII, 2008) Thus, with the increasing degree of integration of the Indian corporate sector with the global market, came about the need for higher accountability. However, this beneficial code was only adopted by a handful of companies and did not create a transformation with respect to corporate practices. With time, large corporate firms and industry groups in India lobbied for legislative changes that could bring forth a cumulative improvement in practices of investment.
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