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The Impact of Corporate Governance on Firm's Performance-*A Case Study of Rashtriya Ispat Nigam Limited*

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Abstract

Corporate governance is one of the most discussed topics in the present corporate world and its economic systems and the term has become a dynamic word in India as well as the world over. Corporate governance is referred to as a system by which a firm is directed and controlled through a set of rules and principles to achieve its objectives and it has gained its attention with greater popularity in 1998 especially in India with the publication of the Voluntary Code by the Confederation of Indian Industry. Since a good corporate governance could significantly contribute to advance the interests and rights of stakeholders as it produces better management and fair allocation of the company's resources hence the concept of Corporate Governance has gained even more importance in its practice, implementation and impact on the performance of companies in the modern era thereby drawing attention of the researchers to research on its implications on firm's overall performance from time to time. However, the corporate governance practices have found to be slightly weaker in developing countries where in India is not an exception and the firms were often suggested for the implementation of good practices with a proactive approach and genuine interests of the stakeholders, the study on such grounds becomes even more significant. For this purpose, one such premier and oldest firm has been taken into consideration that is Rashtriya Ispat Nigam Limited with intent to study the impact of Corporate Governance on the Firm's Performance of selected Public Sector Undertakings.

The present study is a descriptive and empirical study based on secondary data intended to identify the extent to which Corporate Governance has an impact on the Firm's Performance. The result of this empirical study revealed that the components of corporate Governance plays an important role in the firm's performance. The correlation also shows that components of corporate Governance have a high level of positive association with the firm's performance.

Keywords: Corporate governance, practices, stakeholders, firm's performance, proactive approach, profit maximization public sector undertakings

Introduction

The Cadbury Report on Corporate Governance defined it as the "system by which businesses are directed and controlled" (Cadbury, 1992) [28]. Hence, corporate governance is the set of rules, and principles by which a firm is directed and controlled. The Corporate governance has received wide attention in both developed and developing countries in the last couple of decades due to failures and collapses of a number of well-known companies. The incidents have resulted in urgent demands for reform and improved corporate governance practices across various firms. Good corporate governance is a key to secure and maintain sustainable competitive advantage, which is one of the major tools to maximize shareholders wealth. It is also serves as a mechanism to protect the interests and welfares of other stakeholders of companies such as employees, investors, customers and suppliers. In fact, effective corporate governance derives satisfaction to all stakeholders of the firm. Company's competitive advantage emanates from unique competencies that a firm has already acquired on the other hand a weak corporate governance systems and practices are seen a contributing factor to financial crises (Tarraf, 2011) [2]. Therefore, efforts have been made worldwide to develop effective systems and practices of corporate governance in order to protect stakeholder's interests at the maximum level.

Review of Literature

In recent years corporate governance has attracted the attention of many academicians and research scholars. Various studies have been also conducted to study corporate governance from various perspectives to underline the hidden strengths and weaknesses and the reasons for weak corporate governance despite of various initiatives. A couple of studies have been put forth for a wider understanding.

Renu Hooda. (2021) [13] in her study has found a notable relationship between the components of the corporate governance and parameters of financial performance of CPSEs showing a impact on one another.

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Faozi *et al*. (2020) [7] in their review paper have observed that the corporate governance studies in India can be categorized into three streams according to this approach and data used by various studies which are

1. Based on primary data and indices,
2. Studies based on secondary data, and
3. Studies about concepts or reviews.

They observed that several researchers reported that government-controlled (owned) firms have a low level of compliance as compared to privately owned firms. Diriba and Basumatary (2019) [6] has interestingly identified no such noteworthy impact of corporate governance variables on the company performance of India's leading companies in the sample of 20 top companies selected. The outcome further showed that there is no fundamental effect of CEO duality, board size and board independence on company value.

Goel, (2018) [8] has concluded that better corporate governance performance leads to better financial performance in terms of revenue and growth.

Aswathy & Chandramohan (2018) [5] in their research have found an inverse relation of CEO duality on performance which indicates the need for firms to separate the post of CEO and Chair in order to ensure optimal performance. Further concluded that increasing the number of members up to a point will impact the performance positively, but very large boards have a tendency to negatively impact the performance. Diversity in board composition has been found to be helpful to bring in a variety of expertise to enrich performance.

Gugnani (2013) [9] investigated the corporate governance issues of 97 companies listed on the Bombay stock exchange and found that large board sizes had a negative impact on the company's performance. The study suggested that profit margin is the only financial performance measure which is related to internal governance structures significantly.

Aggarwal (2013) [3] has concluded that the governance rating of a company has a significant positive impact on its financial performance, and further found that the ratings of the company along employees-related and environmental dimensions also significantly influence corporate financial performance.

Gaeremynck and Sercu (2010) [4] found a significant positive relationship between corporate-governance ratings and performance that has been observed in a Cross-European study of 33, 667 firms across 14 countries in Europe by Renders.

Narayana Murthy Committee Report (2003) examined a range of corporate governance issues relating to audit committees and corporate boards and disclosure of shareholders. The Committee recommendations included independent directors, audit committees, audit reports, directorship and director compensation, codes of conduct, financial disclosures, related party transactions and risk management. In its present form, Clause 49, called "Corporate Governance", contains eight sections dealing with the Boards of Directors, Audit Committee, Remuneration of Directors, Board Procedure, Management, Shareholders; Report on Corporate Governance, and Compliance, respectively. The Firms which do not comply according to the Clause 49 may be de-listed and charged with financial penalties. Reforms in the area of Corporate Governance did not stop after adopting Clause 49 in India.

Naresh Chandra Committee (2002) was appointed to examine various corporate governance issues. This Committee has been entrusted to analyse and recommend changes if necessary, in diverse areas.

Kumar Mangalam Birla Committee on Corporate Governance (1999) the Committee was set up by SEBI to promote and raise the standards of Corporate Governance. The Committee's suggested suitable amendments to the listing agreement executed by the stock exchanges with the companies in order to enhance the corporate governance standards of listed companies and recommendations were incorporated in Clause 49 of this listing agreement of stock exchanges.

The reviews identified here under did focus on various aspects of corporate governance highlighting the good and the weaker side of the same but the studies pertaining to manufacturing industries and the contributions or impact of corporate governance in this segment are insufficient and are invisible which has drawn the attention of the researcher. Most of the studies on corporate governance in India have focused on listed companies, and there are very few studies that mentioned the effects of corporate governance practices on Firm's Performance of unlisted government-owned companies. Therefore, the study has been proposed to fill the gap by exploring this area through the case study of one unlisted Central Public Sector Enterprise (CPSE) named RINL-Visakhapatnam steel plant for the period of 219-20, 2020-21, and 2021-22 exclusively.

Statement of the Problem

Undoubtedly the concept of Corporate Governance is gaining much more importance in its practice, and implementation by companies globally in the modern era. Notable changes in the guidelines on cooperate governance practices are also being added all over the world but on the performance end the issue still exists. Specifically, this corporate governance issue is an inheriting problem of most of the Indian companies. Day by day the framework of corporate governance (CG) is changing gradually in India, but the compliance part reflects a low performance. Many companies are being collapsed in India. SEBI has taken several steps to mitigate these collapsed. Still more suggestions are required on the impact of cooperate governance practices to formulate effective cooperate governance practices. In the era of globalization, the implementation of good corporate governance principles is necessary for Public Sector Units like Rashtriya Ispat Nigam Limited. Therefore, the present study on Corporate Governance Practices and its impact on the firm's performance of Rashtriya Ispat Nigam Limited has required more concentration to keep great efforts for the study of this paper.

Objectives of the Study

- To study the corporate governance Practices in Rashtriya Ispat Nigam Limited
- To understand the Guidelines by The Department of Public Enterprises (DPE) on Corporate Governance for Central Public Sector Enterprises (CPSES)
- To examine the impact of corporate governance on the firm performance of the RINL

Hypothesis of the Study

H1: There is a significant relationship between corporate governance and profitability.

H0: There is no significant relationship between corporate governance and profitability.

H1: There is an impact of corporate governance on profitability position.
H0: There is no impact of corporate governance on profitability position.

Methodology of the Study
The present study has been intended to identify the corporate governance practices and its impact on the firm's performance in Rashtriya Ispat Nigam Limited. Efforts are kept to analyse the relationship between the components of the corporate governance practices and the firm's performance of The Rashtriya Ispat Nigam limited for the latest three as per the guidelines of DPE.
This study design uses quantitative methods of data collection and analysis to achieve the objectives including Hypothesis testing. The hypothesis will be tested true or false, by evaluating the correlation and regression of selected financial performance variables as dependent variables, with Corporate Governance Rating values as the independent variable.
This study is empirical and descriptive in nature based on the secondary data which is collected from the annual reports of Rashtriya Ispat Nigam Limited for the years 2019-20, 2020-21, and 2021-22, articles, periodicals, magazines, newspaper, research journals and websites were reviewed. The hypothesis will be tested true or false, by evaluating the correlation and regression of selected financial performance variables like Return on Net Worth, Return on Share Capital, and Return on Capital Employed (ROCE) considered as dependent variables. And the Rating values Corporate Governance components like the Board of directors, Audit Committee, Remuneration Committee, Boards of subsidiary companies, Disclosures, reports on Corp Governance and CEO duality taken as the independent variables.

Data Collection and Statistical Tools Used
secondary data method is used to collect data for a 3-year period from the most recent annual reports of 2019-20, 2020-21, and 2021-22, using statistical analysis to know if there is a positive correlation existing between independent and dependent variables. For the purpose of testing the hypothesis whether it is true or false, statistical tools like correlation and regression were considered for the purpose of analysis. The ratios of financial performance are taken as dependent variables, with rating values of Corporate Governance compensates as the independent variable.

Measures of Firm Performance
As figured above, three firm performance measures have been selected for the present study namely:
- Return on Net Worth
- Return on Share Capital
- Return on Capital Employed (ROCE) These are explained below

Return on Net Worth
Return on Net Worth is a measure of firm performance, which measures the ability of the management to earn a return by the use of resources however the firms which use their assets efficiently have higher returns. We have calculated the return on the net worth by Net Profit/Profit after tax (PAT) by Net worth. (Source: Annual Report of RINL)

$$\text{Return on Net Worth} = \frac{\text{NP/PAT}}{\text{Net Worth}} \times 100$$

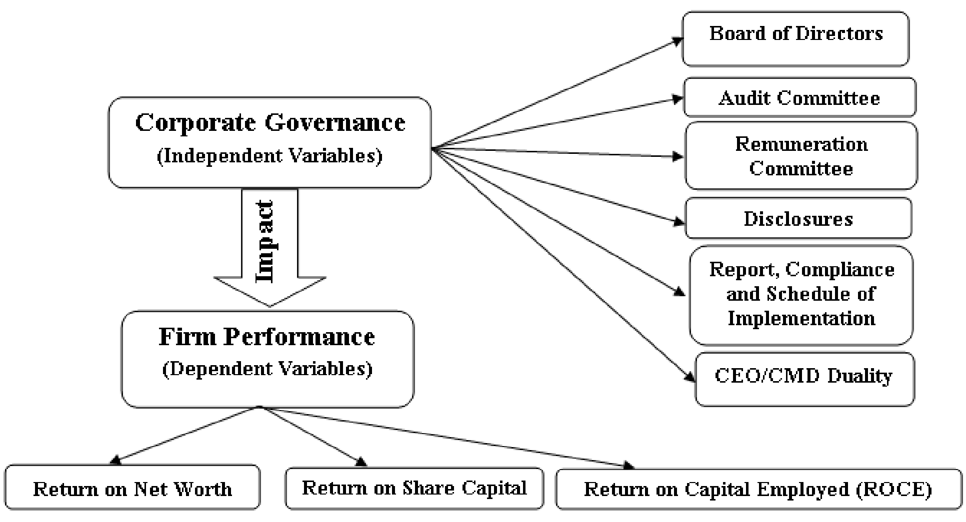
Return on Share Capital
Return on equity has been considered as another firm performance measure which explains the extent to which the objective of wealth maximization has been achieved by using the company's owner's resources. In the present study, we calculated Return on Share Capital by dividing Gross Profit/Profit before interest and tax (PBIT) by Share Capital. (Source: Annual Report of RINL)

$$\text{Return on Share Capital} = \frac{\text{GP/PBIT}}{\text{Share Capital}} \times 100$$

Return on Capital Employed (ROCE)
Return on Capital employed has been used as one of the measures of firm performance, which measures how efficiently a company generates profits by using its capital. Investors considered ROCE as one of the best profitability ratios to determine whether a company is suitable to invest in or not. In this study, we calculated ROE by dividing Net Profit/Profit after tax (PAT) by Capital Employed. (Source: Annual Report of RINL)

$$\text{Return on Capital Employed (ROCE)} = \frac{\text{NP/PAT}}{\text{Capital Employed}} \times 100$$

A glimpse of the study has been presented in the form of a diagram.



Graph 1: Corporate governance Practices

Data Analysis

Table 1: Data related to Variables

Sl. No	Particulars	2019-20	2020-21	2021-22	Mean	Median	Standard Deviation
1	GP/PBIT	(2789)	493	2487			
2	NP/PAT	(3910)	(789)	913			
3	Net Worth	3272	2464	3175			
4	Capital Employed	8963	8446	20322			
5	Share Capital	4890	4890	4890			
6	Return on Net Worth	(119.5)	(32)	28.8	-40.9	-32	60.86942
7	Return on Share Capital	(57)	10.1	50.9	1.333333	10.1	44.48403
8	Return on Capital Employed	(43.6)	(9.3)	4.5	-16.1333	-9.3	20.22248
9	CG rating Score	77	82	90	83	82	5.354126

(Source: Annual Reports & Corporate Governance report for the years, 2019-20, 2020-21, 2021-22 of RINL)

The Above Table 1 shows the data collected from the annual Reports for the year 2019-20, 2020-21, and 2021-22 of RINL, from the above data it is observed that GP/PBIT, NP/PAT, Capital Employed, Return on Assets (ROA), Return on Equity (ROE), and Return on Capital Employed (ROCE) has been increasing as rating score on corporate governance is increasing respectively i.e. 77, 82, and 90 for the years of 2019-20, 2020-21, and 2021-22. However, the share capital stood constant but there is a slight fluctuation in the value of the net worth of the company.

For the purpose of this study the compliance score of corporate governance for the years 2019-20, 2020-21, and 2021-22 of RINL is obtained by giving the marks for each component as it complained as per the guidelines issued by DPE for the compliance score of corporate governance in the year 2010.

Table 2: Allotment of Grade for Corporate Governance Score

Grade	Annual CG Score	Year	Actual CG Score	Grade
Excellent	85 and above	2019-20	77	Very Good
Very Good	75-84	2020-21	82	Excellent
Good	60-74	2021-22	90	Excellent
Fair	50-59			
Poor	Below 50			

(**Source:** compiled from the data obtained from Annual Reports & Corporate Governance report for the years, 2019-20, 2020-21, 2021-22 of RINL as per guidelines issued by the DPE on compliance Corporate Governance report)

From the above table.2 it is observed that the compliance score of corporate governance of RINL has been increasing year by year gradually. It is also found that in the years 2020-21, and 2021-22, the company has a score of 82 and 90 respectively which comes under the grade of Excellent, but in the year 2019-20, the score was 77 which has come down to the grade of Very Good.

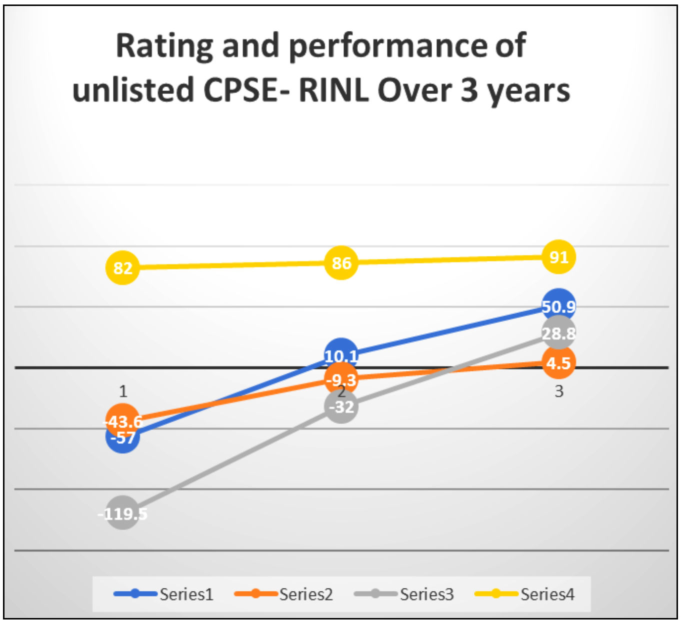


Fig 1: Data Visualisation for 3 years

Figure 1 shows data visualisation for the 3-year period for the years 2019-20, 2020-21 and 2021-22 respectively under study. It is observed that from the above graph, the curves of the three performance variables are moving upward, progressively corresponding to the respective CG Ratings score for the years 2019-20, 2020-21 and 2021-22. This is indicative of prima facie evidence that as the CG Rating score goes higher, performance parameters also raise.

Legend
Series 1: 22021-22
Series 2: 2020-21
Series 3: 2019-20
Series 4: Computed Rating per cent Encouraged by the result from the data visualisation, for the purpose of the statistical tool of CORREL from the EXCEL Analysis is used, to determine extent of relation between the independent variables and dependent variables the coefficient of correlation is used.

Correlation Coefficient

In statistics, the Pearson correlation coefficient-also known as Pearson's r, the Pearson product-moment correlation coefficient, the bi-variate correlation, or simply stated as the correlation coefficient-is a measure of linear correlation between two sets of data.

Table 3: The result of the correlation analysis &Coefficients of the correlation

	Coefficient of Correlation		
Return on Net Worth (NP: NW)	0.9722742	Strong	Positive
Return on Share Capita (GP ShC)	0.9631650	strong	"
Return on Capital Employed (NP: CE)	0.9309737	strong	"

(**Source:** compiled from the data obtained from Annual Reports & Corporate Governance report for the years, 2019-20, 2020-21, 2021-22 of RINL as per guidelines issued by the DPE on compliance Corporate Governance report)

The present study in the above table-3 reveals that the coefficients of Correlation for all the three dependent variables are seen to be more than 0.9, which reveals a strong positive correlation between Corporate governance and a firm's financial performance parameters.

For further confirmation of the result, Regression analysis of the EXCEL data analysis programme has been used and the summary output for all 3 parameters is given.

Regression Analysis

Table 4: Regression Analysis

Sl. No	Regression Statistics	Dependent Variable		
		Return on Net Worth	Return on Share Capita	Return on Capital Employed
1	Multiple R	0.972274	0.963165	0.994857
2	R Square	0.945317	0.927687	0.989741
3	Adjusted R Square	-3	-3	-3
4	Standard Error	24.65388	20.71922	7.804184
5	Observations	1	1	1

(**Source:** compiled from the data obtained from Annual Reports & Corporate Governance report for the years, 2019-20, 2020-21, 2021-22 of RINL as per guidelines issued by the DPE on compliance Corporate Governance report)

For the present study in the above table – 4 shows that, the "Multiple R" is the correlation coefficient. It reflects how strong the linear relationship is. The value of 1 indicates a strong positive relationship among the variables and a value of zero means no relationship at all. It is the square root of r squared and Multiple R is a measure of the goodness of fit of the regression model. If the value of R squared is above 0.7 considered as a high level of correlation between the variables. In this study it is observed that the value of R squared for all dependent variables is above 0.9, hence it reveals high level of correlation among the variables.

Results Analysis and Interpretation

The statistical tools Coefficient of Correlation is a measure of linear correlation between two sets of data which belongs to the variables. In this case, the coefficients of correlation are 0.97,0.95 and 0.97 respectively of the three dependent variables with respect to the independent variable which is the computed Corporate Governance (CG) Rating, indicating a very strong positive relationship, supporting the hypothesis that the higher the CG Rating the better are the financial performance results. The regression analysis also resulted in R statistic of 1 which supports the hypothesis.

From the study it has been observed from the results that the CG Rating scale devised for this study has been found to be easy to understand and use in quantifying the CG guideline elements. There is, of course, a need for some judgement to be exercised in assigning Rating points in a few sections of the scale appropriately, a task that can be successfully accomplished after thoroughly reading the Annual Reports, again and again, looking for relevant information and interpret it relevantly.

Conclusion

The theory of corporate governance in India has been observed only after liberalization, globalization and privatization. Since India is a developing country Corporate governance concepts are very important to compete with both developed and developing countries in the era of Globalization. This study evaluated the corporate governance impact on the firm's performance of Rashtriya Ispat Nigam Limited. The regression model was applied to the data extracted from the Annual Reports of three years of the Rashtriya Ispat Nigam as samples respectively as independent and dependent variables. The result of this empirical study revealed that the components of corporate Governance plays an important role in the firm's performance. The correlation also shows that components of corporate Governance have a high level of positive association with the firm's performance. The present study was conducted only for the academic interest to find the relationship between the corporate governance variables and the firm's performance indicators and finds how extent the corporate governance ratings can be good predictors of corporate financial performance and the study is unbiased because the study was not connected to RINL Rashtriya Ispat Nigam Limited or its employees in any way. This case study offers important clues for further research using the CG Rating scale with data from a greater number of companies and more years and a comparative study could also be made between the companies for a better understanding of the impact of corporative governance and practices implemented by the firms for its growth and competitive advantage.

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