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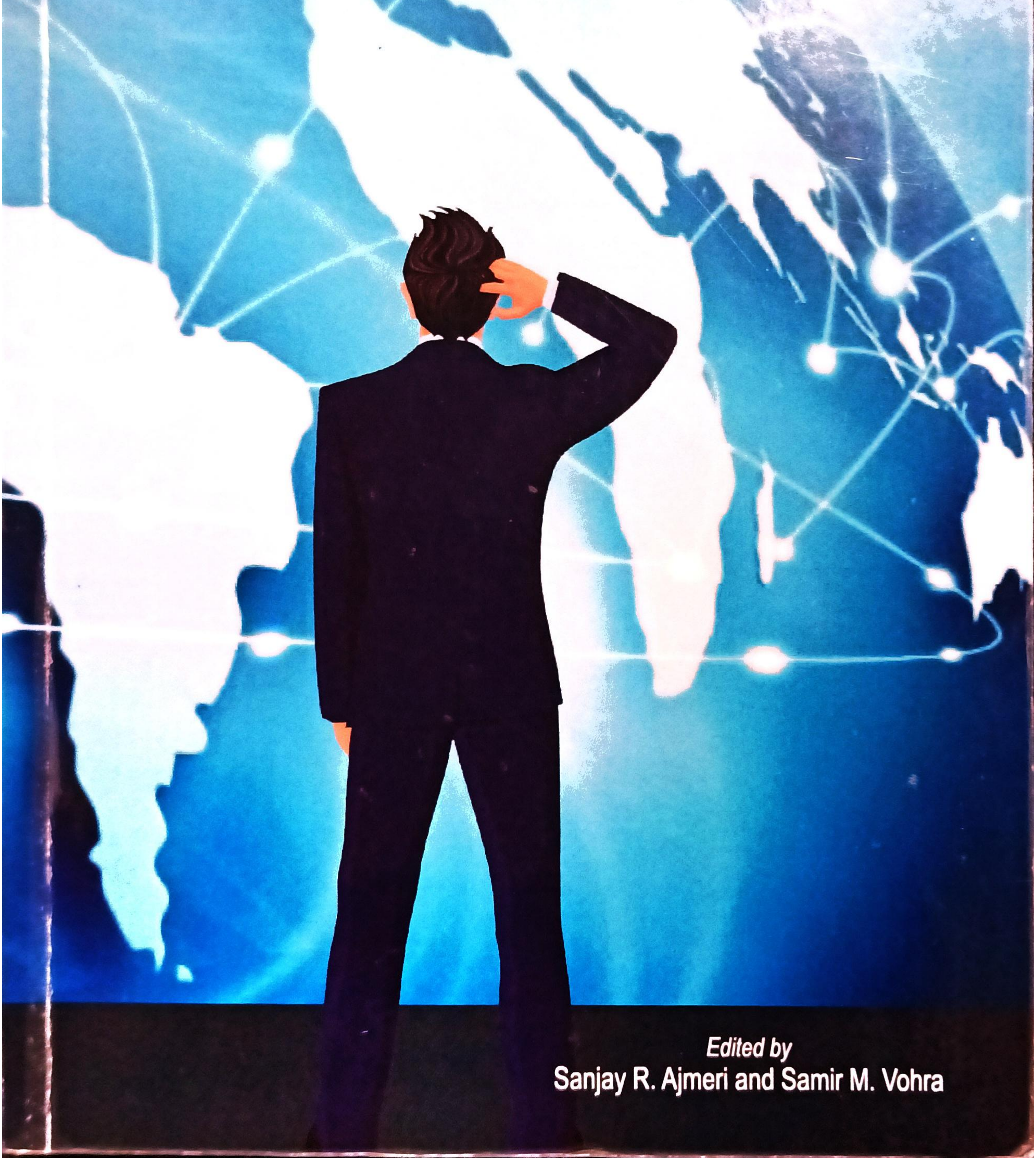

Edited by

Sanjay R. Ajmeri and Samir M. Vohra

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An Impact of Corporate Governance on the Profitability of Indian Textile Industry

Payal S. Jogani[1] and Rupal N. Patel[2]

INTRODUCTION

Corporate governance is a system of structuring, operating, and controlling a company with a view to achieve long-term strategic goals satisfy its shareholders, creditors, employees, customers and suppliers. Corporate governance plays an important role for enhancement of profitability. The improvement of firms profit is important to attain overall corporate goals. Durable corporate governance is needed for the all the business organizations because it plays an essential role in the management administrations in both developed and developing countries.

Developed countries vary from developing countries in many ways. For developing countries like India, respectable corporate governance is a vital tool for globalization of business organizations. Good corporate governance consists of clearness principle, accountability principle, obligation principle, independence principle and fairness principle which have direct effect on corporate performance. Good corporate governance does not only enrich the profitability but also raises firm performance. By improving the overall presentation of companies and increasing their access to outside capital, good corporate governance pays toward economic stability that reduces the vulnerability of the monetary crises. It reduces cost of capital and transaction cost. Corporate governance concerns with the relationship among management, board of directors, controlling shareholders, monitoring shareholders and other stakeholders.

Poor corporate structure results indiscipline, both on the part of management and workers. Unwell governed corporations not only pose a risk to themselves, but they also cause barrier to others and could indeed pull down capital market. For instance, the poor governance of a systematically important firm would pose a threat to the economy. Irrespective of how

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sound macroeconomic policies are, if entities are not well governed, the macro-economic purposes may not be reached. Thus, corporate governance is significant for all types of business bodies.

2. LITERATURE REVIEW

Correctly applied corporate governance ethics in the organization may rise the profitability and returns, improve its effectiveness, credibility and improve relations with key stakeholders such as investors, business partners, employees, customers, etc.

Todorovic (2013) Kumar and Nihalani (2014) investigated the effect of corporate governance on the performance of Indian Banks and found that board of the directors has play important role in firm performance but the board meetings negatively impact on the financial performance.

Latif *et al.* (2013) found that board size and CEO duality had significant impact on firm performance while board composition had insignificant impact on performance. Todorovic (2013) found that if the company tightly follows principles of corporate governance then it results in higher net profit margin and earnings per share. Outside directors and managerial ownership are negatively related to the return on assets and earning per share.

VO and Phan (2013) examined fundamentals of corporate governance such as CEO duality, presence of female board members, the working experience of the board members and compensation of board members and found that all the elements had positive impact on the firm performance but board size had negative impact on the firm performance.

Sheikh *et al.* (2013) studied the impact of internal attributes of corporate governance on firm performance. The research study found that board size, CEO complement, and ownership concentration were confidently related to the firm performance but Nyamonogo and Temesgen (2013) analyzed the impact of corporate governance on firm performance and found that board size negatively impacts firm performance while independent board directors tend to enhance the firm performance.

Danoshana and Ravivathani (2013) found that board size and audit committee size exert positive influence on the firm performance while board meeting frequency has negative impact on the firm performance.

Mathur and Gill (2011) investigated impact of board size, CEO duality and corporate liquidity on the profitability. The study create CEO

...ability and corporate liquidity to be positively related to the profitability ...ile the board size had negative impact on the profitability.

Coleman and Biekpe (2006) studied the interrelationship between corporate governance and financial performance in Ghana and found that board size and CEO duality had no significant relation with performance while board composition had positive impact on the performance.

Jerdan and Szczepanska (2011) did a comparative analysis between director's remuneration and company's performance of listed companies in Poland and UK and the study showed positive relationship between the director's payments and the companies' size. The study also examines that directors remunerations and return on capital were positive associated.

Emmanuel and Hodo (2012) examined corporate governance impact on the bank performance by taking the sample of the Nigerian bank and found that the size of the board of directors and the number of the shareholders had positive impact on the return on equity and return on the assets. The study also showed that the quality of the assets, equity providers and managers also exert an influence on bank performance.

Abdullah (2006) calculated the association among directors' remuneration, firm performance and corporate governance in the Malaysian firms and the study displayed that directors remuneration was not connected with the profitability while the board independence and the extent of non-executive interests negatively influence the directors remuneration and also tough negative relationship was found between the return on assets and the directors remuneration.

Stephen and Olatunji (2011) studied the role of non-executive directors in the profitability and the study revealed that the non-executive directors and return on equity are negatively associated with each other. The findings show that more numbers of outside directors in board adversely impact the financial performance.

3. RESEARCH GAP

Corporate governance is the important factor in economic development. For business globalization economics, implementation of good corporate governance principle is necessary.

Many of studies are being conducted in the context of corporate governance but no study was found to analyze corporate governance impact on the profitability in context of Indian textile firms. On the basis of review of available literature in various national and international journals, a small number of study is found that focused over corporate governance components like audit committee members, non-executive directors and board meetings.

4. RESEARCH OBJECTIVE AND HYPOTHESIS

The main objective of this study is to examine the impact of corporate governance on the profitability on the India textile industries. Further, study also attempt to describe the corporate governance and relationship of corporate governance with the profitability.

For achieving the research objective, following hypothesis has been testing.

H1: There is significantly positive association between board size and profitability.

H2: There is significantly positive association between audit committee members and profitability.

H3: There is significantly positive association between director's remuneration and profitability.

H4: There is significantly positive association between board meetings and profitability.

H5: There is significantly positive association between non-executive directors and profitability.

Theoretical Model to achieve research objective, a theoretical model (inspired from Achchhuthan and Kajananthan, 2013) has been constructed which highlights the various corporate governance variables impacting profitability.

Table 1: Theoretical Model

Corporate Governance	
NED DR BM ACM	→ PAT

BS : Board size
NED : Non-executive directors in the board
DR : Directors remuneration
BM : Board meetings
ACM : Audit committee members
PAT : Profitability

RESEARCH METHODOLOGY

here are number of variables which are used to analyze the impact of porate governance on profitability. Table 1 describes the different pendent and independent variables, used to analyze impact of corporate vernance over profitability, and their measurement. Independent ariables are the BS, NED, DR, BM and ACM which are measure the orporate governance. Dependent variable is the PAT which is measure the profitability.

ample selection, data collection and analysis Kothari (2004) stated that empirical study takes place when some variables affect another variable one way or another. In this study, efforts have been made to explain the impact of corporate governance on the profitability of textiles firms in India. Therefore, this study is empirical in nature. Secondary data has been used for the research purpose. Data has been collected from annual reports of the textiles industries. Five Textile companies which are listed in both Bombay Stock Exchange and National Stock Exchange have been selected as sample size. The data has been collected from annual report of five years ranging from 2012–2013 to 2016–2017.

Table 2: Descriptive Statistics of the Study

	PAT	*BS*	*ACM*	*DR*	*NED*	*BM*
Mean	215.787	8.8	3.641	3.974	5.528	5.656
Medium	48.78	9	3	2.32.	5	5
Maximum	3880.4	14	6	25.225	11	24
Minimum	–1637.61	5	3	0.015	1	4
Std. Dev.	690.146	2.306	0.789	4.675	2.150	2.951
Observations	195	195	195	195	195	195

Table 2 shows that the total observations are 195. Size is 8.8 and the average of the nine. Table 2 shows that total observations are 195. Presence of more than three members is essential to build a qualified and independent audit committee (Khan & Jain, 2011). Present study found that the presence of at least three members in audit committee in companies under sample. Whereas the board of directors meets at least four times in the year while the mean of the board directors meet more than five times. The part of non-executive directors in the board should be at least 50 percent (Khan & Jain, 2011). According to this sample the average of board size is 8.8 and the average of the non-executive directors is 5.528, it means non-executive directors in board is more than

50 percent. The average of director's remuneration (DR) is ₹ 3.97crore and director's remuneration is ₹ 25.225 crore to maximum extent. The minimum of the director's remuneration is the ₹ 1.45 lakh. The maximum profit is ₹ 3880.4 crore and minimum amount of profit shows negative representing loss amounts to ₹ 1637.61 crore.

Table 3: Correlation Matrix for All Variables

	PAT	*BS*	*ACM*	*DR*	*NED*	*BM*
PAT	1					
BS	0.182**	1				
ACM	–0.081	0.317	1			
DR	0.511	0.520	0.247*	1		
NED	0.002	0.582	0.282*	0.116	1	
BM	–0.057	–0.189	0.122**	0.186*	0.142**	1

Note: *, ** and *** show that the levels of significance 1%, 5% and 10% respectively.

Table 3 displays the correlation matrix between the dependent and independent variables. Accordingly, the Table 3 shows that board size plays important role in the profitability because the board size positively associated with the profitability (at 5% significance) its means that if the increasing the numbers of directors then increasing the profitability. Directors remuneration is also positively associated with the Profitability (at 1% significance). Means that directors remunerations is also playing an important role in the profitability. If increasing the director's remuneration then also enhanced the profitability. Director's remuneration is also positive associated with the board size. Means that if the increasing the numbers of directors in the board than the increasing the directors remuneration. If board size increasing than the audit committee members is also increasing because board size and audit committee members is positive associated but the board size has negative associated with the board meetings. Audit committee members and non-executive directors do not play any role for enhanced the profitability because the profitability is negative associated with the board meetings and audit committee members.

6. OLS REGRESSION MODEL

Since the data is of panel in nature consisting of both time series and cross sectional data, so that the ordinary least square panel regression is used for the purpose of analysis. The following regression equation is estimation:

$$PAT_{it} = \alpha_{it} + \beta_1 BS_{it} + \beta_2 ACM_{it} + \beta_3 DR_{it} + \beta_4 NED_{it} + \beta_5 BM_{it} + \mu_{it}$$

In the above regression equation, PAT_{it} represents the profitability of firm i at time t. BS_{it}, ACM_{it}, DR_{it}, NED_{it} and BM_{it} represents corporate governance variables of firm i at time t. α_{it} and μ_{it} stand for the intercept and error term respectively. β_1 to β_5 are the slope of the coefficients which influence the dependent and independent variables.

Table 4: Ordinary Least Square Regression Result

	Coefficient	*Standardized*	*T-Statistics*
C	667.390		2.560072
BS	-27.834	-0.092986	-1.032104
ACM	-186.837	-0.213689	-3.292531
DR	0.900	0.610139	8.170755
NED	15.962	0.049723	0.635205
BM	4.842	0.020709	0.333666
N	195		
Adjusted R-Squared	0.292827		
F-Statistic	17.06637		
Prob (F-Statistic)	0		

Table 4 represents the result of ordinary least square model. The adjusted R2 0.293 for the model implies that more than 29 percent of the variance in profitability can be explained by the variances of independent variables. It is observed that the model is good fit because the Prob (probability) (F-statistic) is less than 0.05. The study found that director's remuneration (DR) has significant positive impact on the profitability of the companies. In the light of above result, it implies remuneration of directors positive impact on the profitability at 0.610139 that is why hypothesis (H3) is accepted But Abdullah (2006) revealed that directors remuneration were not positive associated with profitability. Whereas audit committee members (ACM) has significantly negative impact on the profitability so that the hypothesis (H2) is not accepted. Board size has also insignificant negative impact the profitability so that hypothesis (H1) is not accepted but Danoshana and Ravivathani (2013) found that board size and audit committee size exert positive influence on the firm performance. Non-executive directors and board meetings positively influence the profitability but there is no significant relationship with profitability so that hypothesis (H4) and hypothesis (H5) is not accepted.

Stephen and Olatunji (2011) found that the non-executive directors were negatively associated with the return on equity. Kumar and Nihalani (2014) found that board meeting negative on the financial performance.

7. SUMMARY AND CONCLUSION

The wave of corporate governance in India has only been observed after liberalization, globalization and privatization. India is developing country and Corporate governance concepts more important both develop and developing country because they faced more competition in Globalization of business.

The aim of this study is to evaluate that corporate governance impact on the profitability of Indian textile firms. The regression model was applied on the sample of five textiles companies. The empirical result showed that the director's remuneration plays important role in the profitability. The correlation matrix also shows that director's remuneration has significant positive association with the profitability.

More audit committee members are significantly negative to the profitability of different textile firms. Large board size may not be in favor of Indian textiles firms because they do not increase the profitability. Board meetings also have a positive impact on the profitability but result is not statistically significant. It is observed that if the Indian firms apply the good corporate governance principles then firm achievement, the firm objectives and also the Indian firms raising all over the world.

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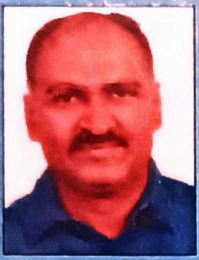
About the Book

This book is a compendium of papers presented in the International Conference on **Emerging Global Economic Situation: Impact on Trade and Agribusiness in India** jointly organised by Agro-Economic Research Centre (AERC) of Sardar Patel University, Vallabh Vidyanagar, Anand (Gujarat) and Bhikhabhai Jivabhai Vanijya Mahavidyalaya (BJVM), Vallabh Vidyanagar during September 28-29, 2018 with [illegible] of Mi[illegible] Agriculture and Farmers Welfare, Government of India [illegible] and Rural Development (NABARD), Ahmedabad. Th[illegible] [illegible]se interested in issues related to international business and com[illegible]

About the Editors



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