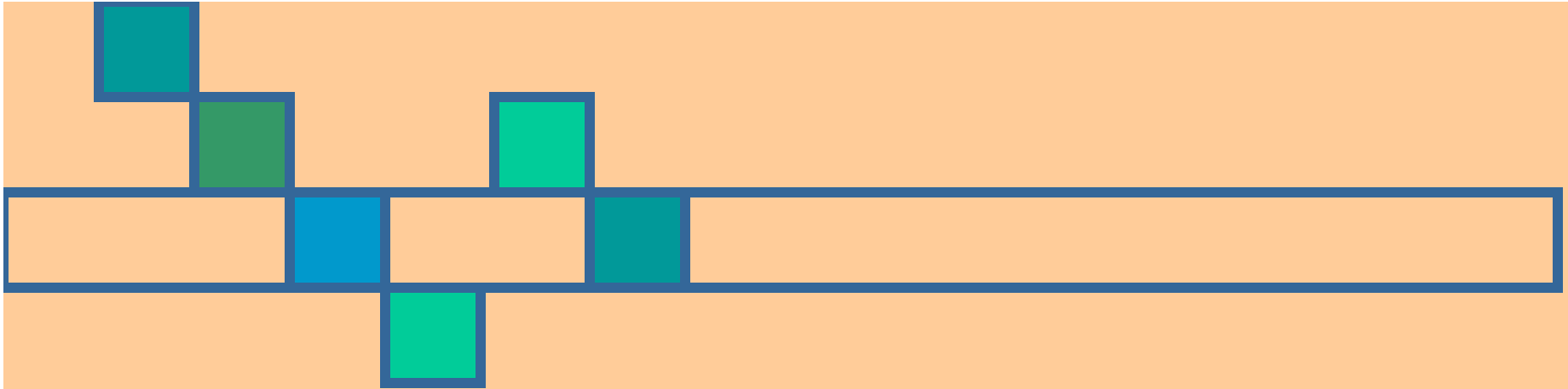




Corporate Control and Governance



Ram Kumar Kakani



The views expressed herein
are personal



FINANCIAL FOCUS

- ↪ 19th & 20th Century
- ↪ Company legislation
- ↪ Bottom line driven
- ↪ Destroy communities
- ↪ Create communities

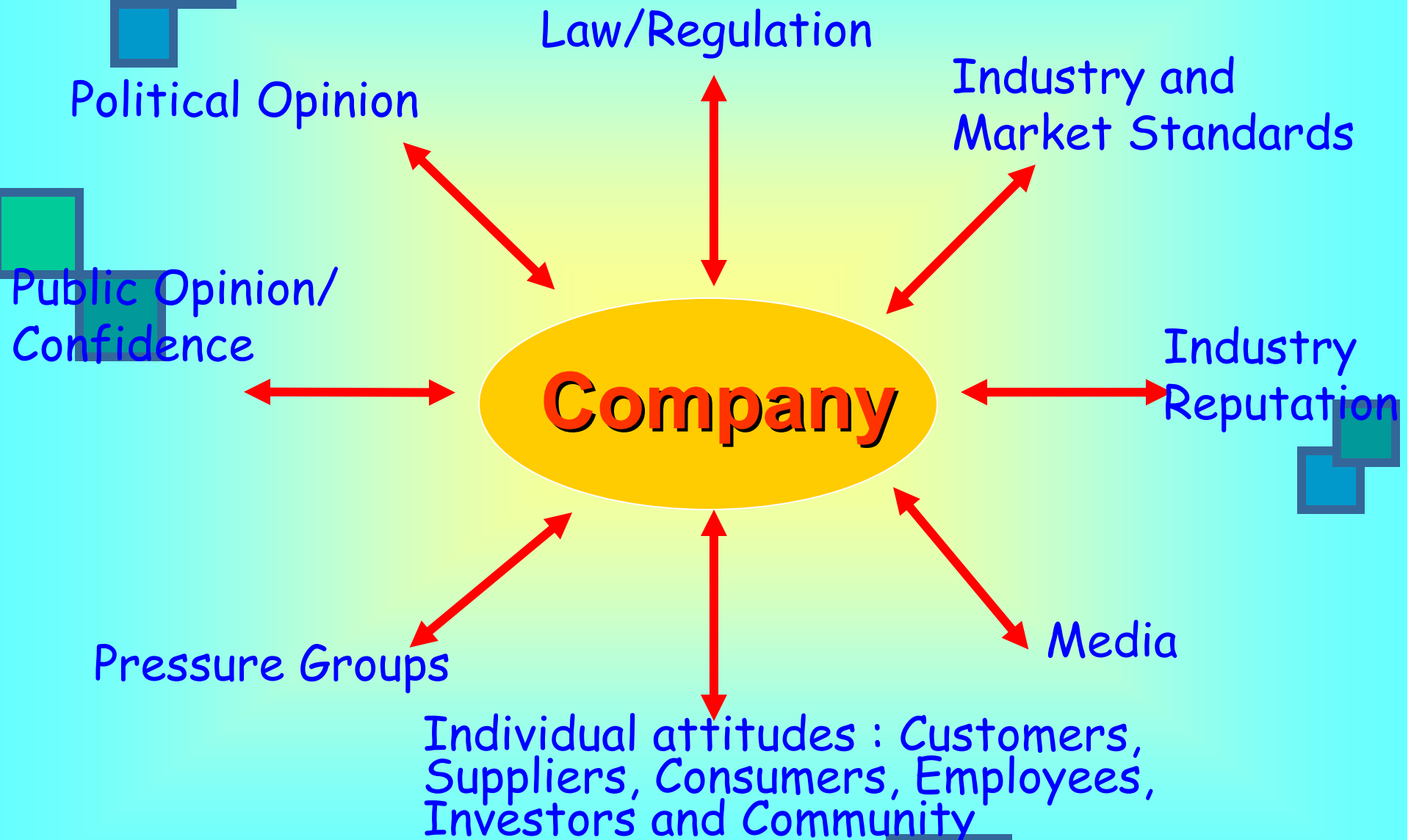


Power of Multinationals

- ↪ Open world economy - W.T.O.
- ↪ Only 25 Countries GDP > GM
- ↪ Denmark 25th - 5.2m
- ↪ GM supports 9 million people
- ↪ Shell > 40% of Holland market cap
- ↪ Wallenberg holds a major chunk of Sweden (> 64%)
- ↪ Main source of tax revenue
- ↪ Economic and political power

Source: www.corpgov.org (2001)

Licence to operate



Can we in 21st Century?

- ⇒ Have shareholder dominance
- ⇒ Exclude other stakeholders
- ⇒ Have financial measurements only

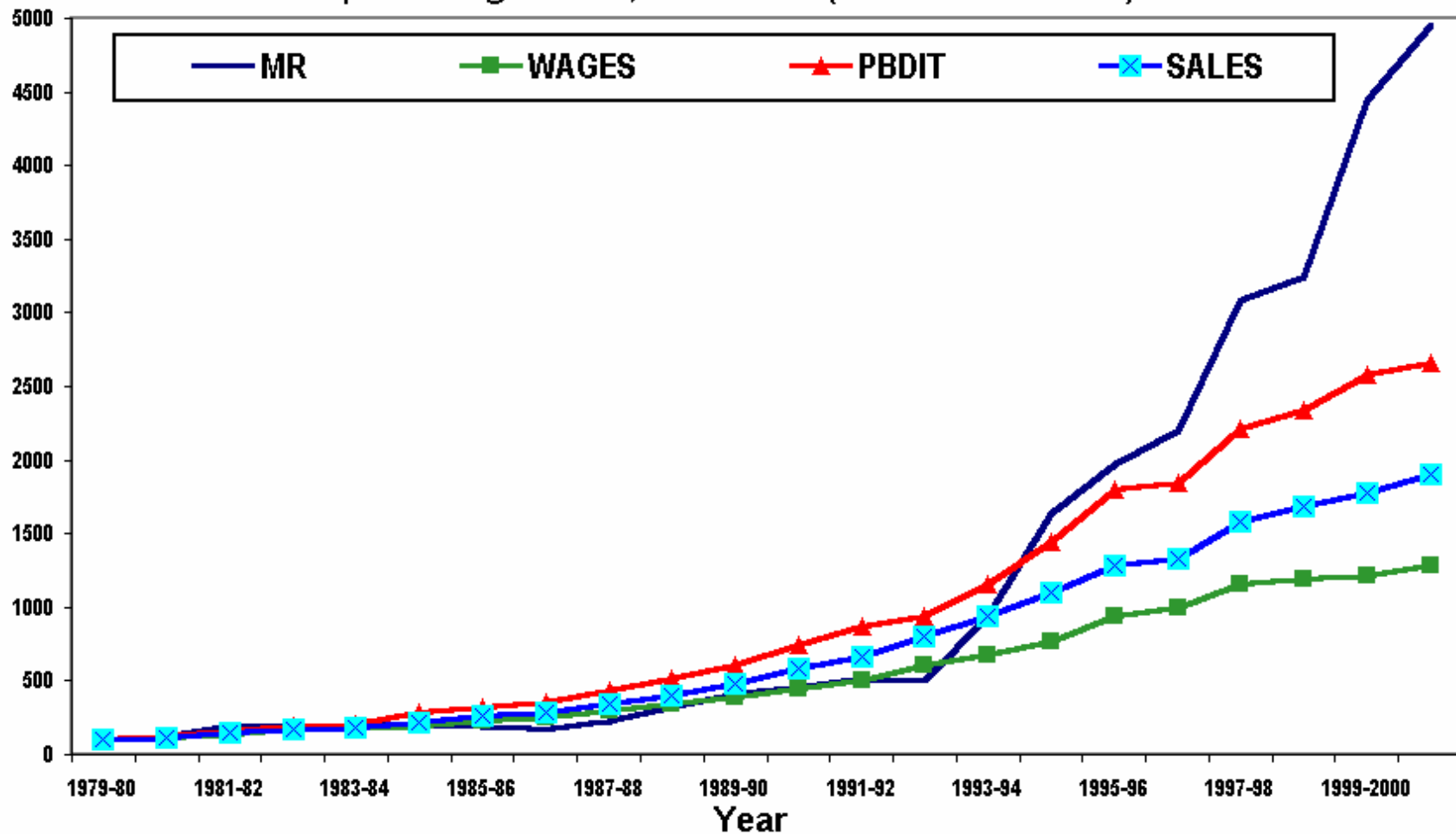
We need in 21st Century?

- ⇒ measurements for sustained business success
- ⇒ Responsibility towards stakeholders
- ⇒ Accountability to shareholders
- ⇒ Transparency

Corporate Governance Examples

- Corporate Governance is taking into account all stakeholders interest ...
- In other words ... not to misuse powers given by some others is the essence of corporate governance
- Example ...
- Wealth Transfer (C K Birla, P&G, Colgate)
and/or
- Managements Personal Agenda (Pfizer, Tata)
- Cross-Holdings Structure in Business Groups

Growth of Managerial Remuneration, Employee Wages, Operating Profit, & Sales (Base 1979-80)



Source: Ram Kumar Kakani & Pranabesh Ray, Managerial Remuneration: The Ballooning Issue, XLRI Working Paper, XLRI Jamshedpur: India, 2002

Governance: Indian Context

- ❖ Governance is different from Western Countries
- ❖ Ownership pattern is itself different
- ❖ 5 categories of owners –
 1. Indian Promoter(s)/Owner(s)
 2. Foreign Investor(s)
 3. Domestic Institutional Investor(s)
 4. Other Big Investor(s) incl. Private Mutual Funds
 5. Retail Investor(s) OR Public Shareholding

Indian Context

- ❖ Broadly 4 types of firms –
 1. Foreign Owned
 2. State Owned
 3. Indian Business Group Controlled
 4. Private Indian (non-business group)
- ❖ Question:

Does Ownership Pattern Influence Corporate Governance and Corporate Performance of a Firm?

'Does Ownership Pattern Influence Shareholder Value of a Firm'

Table 1

Category	Mean Holdings	Remarks
1. Indian Promoter(s)/ Owner(s) holding	37%	It also presents the indirect stake by owners i.e., the interest held by owner(s) in their firms by way of crossholdings.
2. Foreign Investor(s)	15%	This figure also includes the stake held by Foreign Institutional Investors.
3. Domestic Institutional Investor(s)	14%	This figure includes holdings of UTI, LIC, SBI, GIC, and IDBI, and their mutual funds.
4. Retail Investor(s)	27%	Also known as Public Shareholding.
5. Other(s)	07%	This figure also includes the interests of Private Mutual Funds
Total	100%	

Period: FY 2001

Monitor(s)

- Owner-Manager(s)

Agency Theory Vs Reputational Theory

- Foreign Institutional Investors & Private Mutual Funds

Formal Authority, Social Influence, Ruthless, Expertise to capture property rights

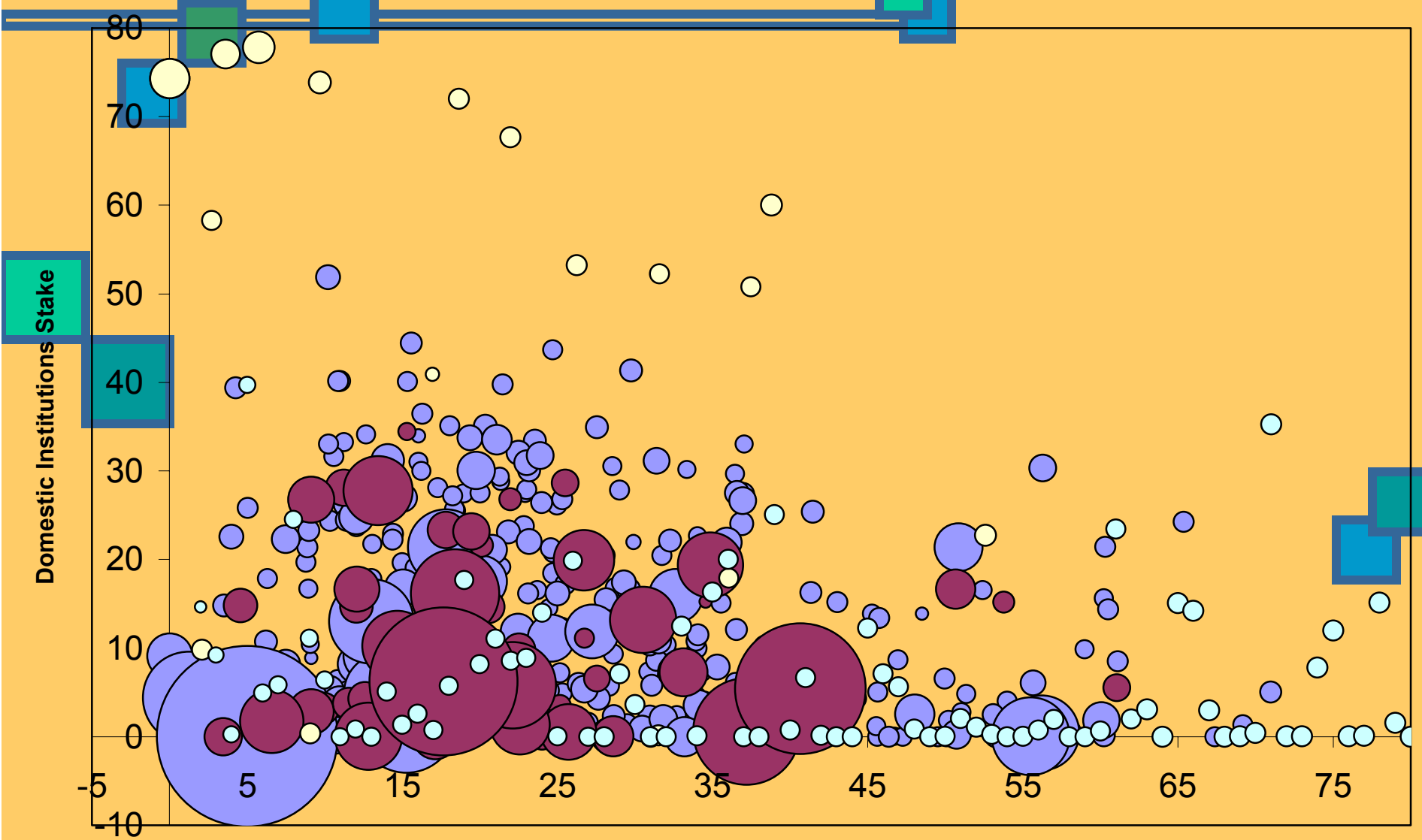
- Domestic Institutional Investors

Political pressures, economic factors, & legal issues

- Retail Investors

Lack Capability, No Incentives, Low Awareness, Poor Corporate Governance Norms


How Corporate India Performed?



- Business Group
- Foreign Owned (MNC)
- State Owned
- Private Indian



Results ...

- Foreign firms performed well, but
 - Private Indian firms performance was bad
 - State-Owned firms did not perform well, but ...
 - Performance of Indian Business Group Affiliates has been varied
- 

Possible Reasons ...

- Retail shareholders are usually very small and dispersed.
- Foreign Investors are operating in non-capital intensive value generating sectors
- Whereas, DIIS were investing in value destroying sectors.
- Another reason is, DIIS own equity due to subscription of devolved public/rights issues, underwritten IPOs, conversion of debt-to-equity in distressed companies.

Corporate Governance

An AGM of Grasim Industries, was held in a remote location. Of its 13 directors, just one showed up, while only a handful of the company's 300,000 minority shareholders attended. And they were employees who were unlikely to hold management accountable.

- Rahul Bajaj epitomized the problem. He said at a seminar on corporate governance in 1996 that:
- “All of us know what boards and managements should do, but are doing what we should not do. We have done things that are questionable – legal but questionable. Why should we need a committee to tell us what to do?”

Corporate Governance

- Strategy Guru Prof. K.R.S.Murthy, Ex-Director, IIM Bangalore summarizes the governance questions in Asia as
 - Why do business leaders do things they know should not be done?
 - What are the pressures or fears that force them to do so?
 - How can they be helped to be more integral to their own beings?
 - How can the board of directors play a more useful role?

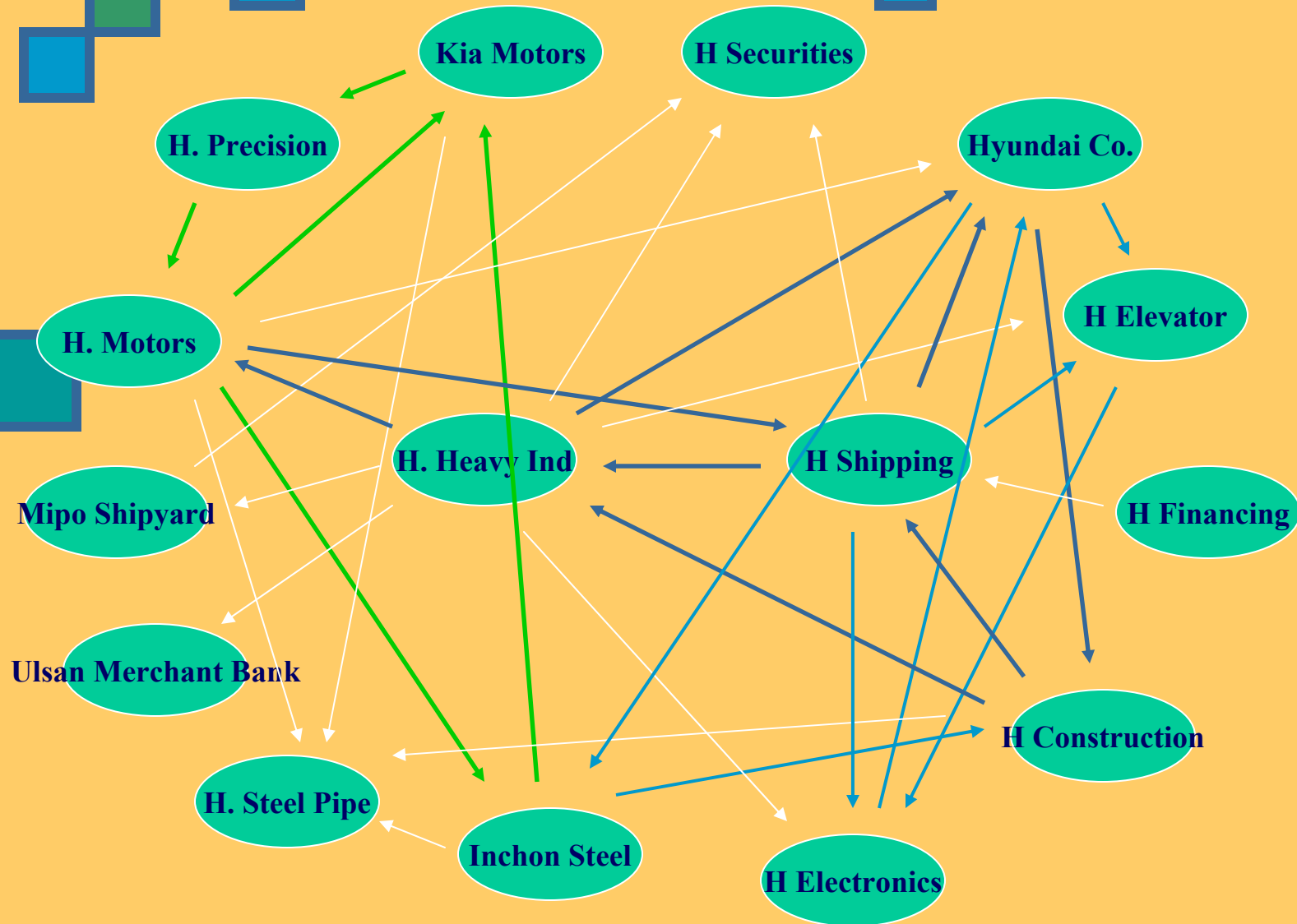
New Regulations

- Presentation of consolidated financial statements
- Presentation of segmental financial statements
- Stricter disclosure requirements be put in place
- Include outside (non-executive) representatives directors in the board representing minority (public) interests
- Audit Committee
- Remuneration and Nominations Committee
- Shareholders/Investors Grievance Committee

New Regulations

- Integrated supervision agency be established
- More regulation on related party transactions
- Stricter liability on accountant
- Improved accounting standards
- Duty of directors in legal codes
- Mandatory compliance officer
- Liability of controlling shareholder
- Cross debt guarantee prohibited
- Cross share ownership prohibited
- Strengthen minority shareholder rights
- Remove hostile takeover barriers
- Corporate Governance guidelines, etc be publicized

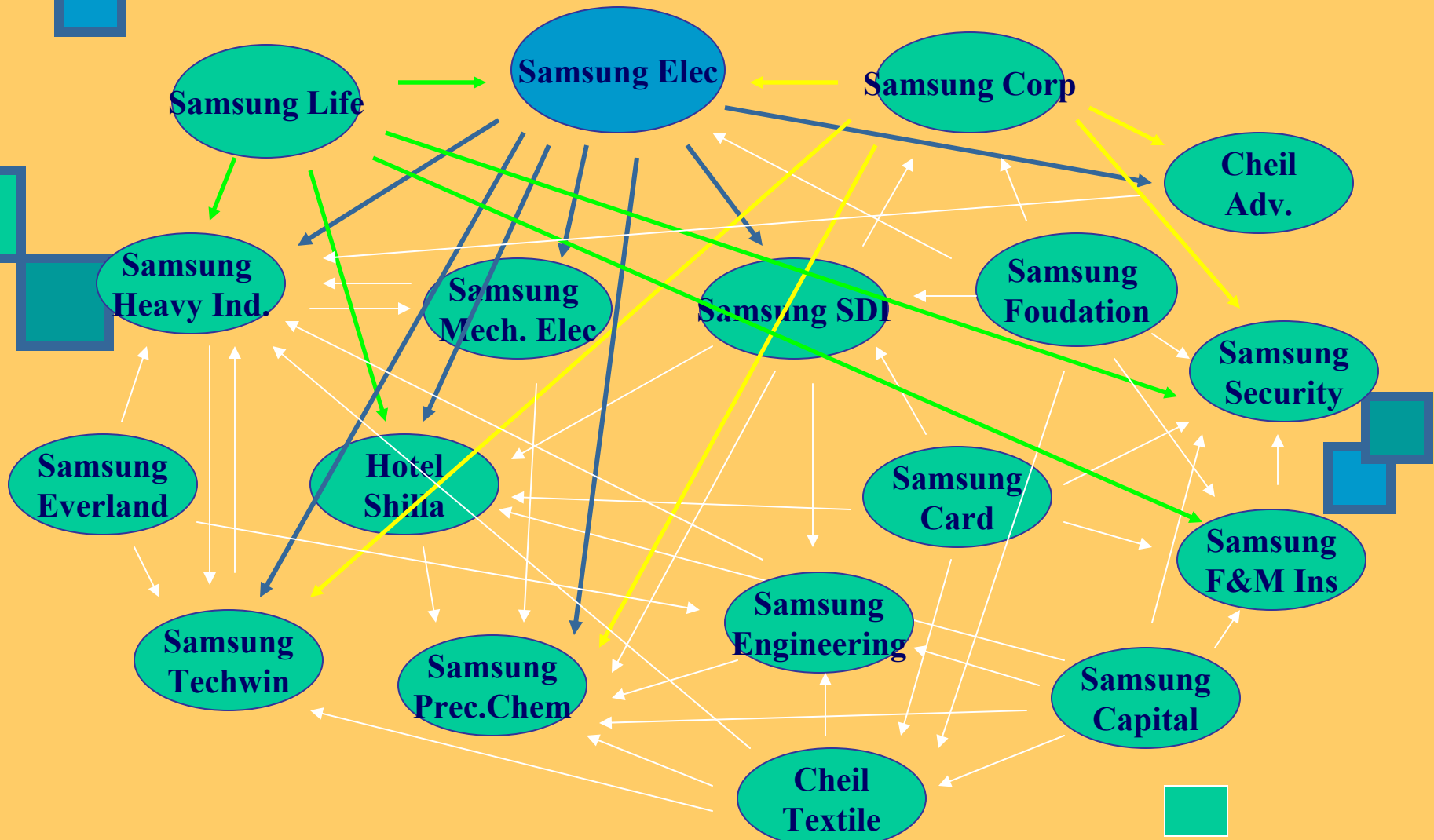
Circular Equity Ownership: Hyundai Group



Source: Hasung Jang, Korea University

Ram Kumar Kakani, XLRI Jamshedpur

Pyramidal Equity Ownership: Samsung Group



Source: Hasung Jang, Korea University

Ram Kumar Kakani, XLRI Jamshedpur

Some more ways to evade

- Off balance sheet transaction
- Off shore paper company operation
- Issue cheap equity/debt with warrants to promoters
- Hidden debt guarantees
- Import/Export/Re-export/Forex Dealings
- Evade Tax/Duty Obligations