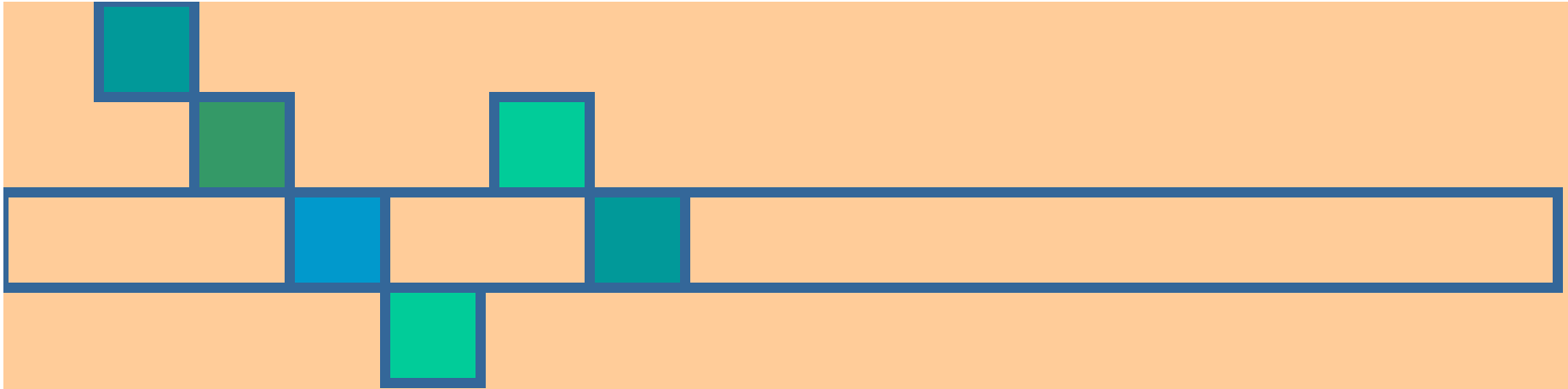




# Corporate Control and Governance



Ram Kumar Kakani



The views expressed herein  
are personal



# FINANCIAL FOCUS

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

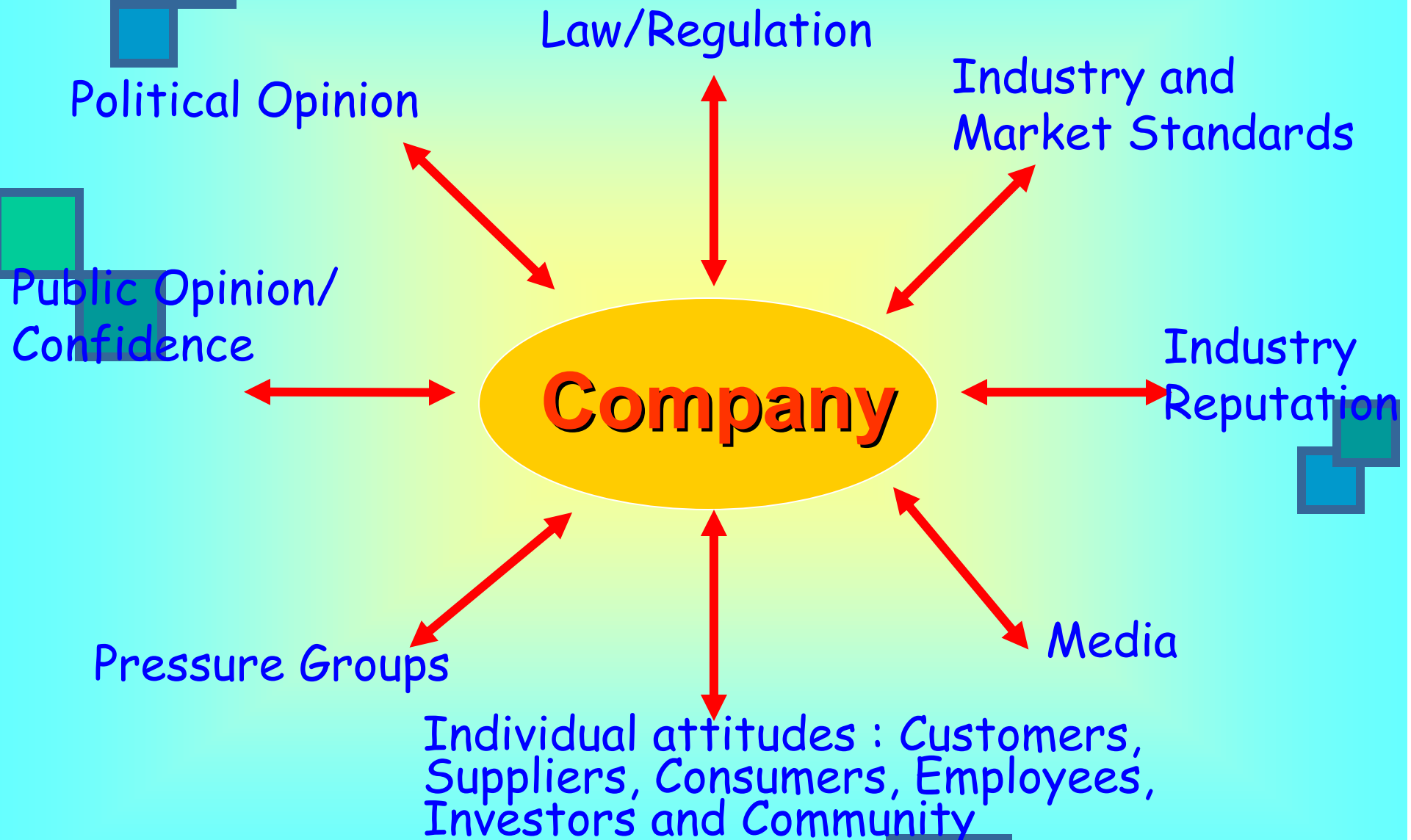


# Power of Multinationals

- ↪ 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](http://www.corpgov.org) (2001)

# Licence to operate



Source: [www.corpgov.org](http://www.corpgov.org)

# Can we in 21st Century?

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

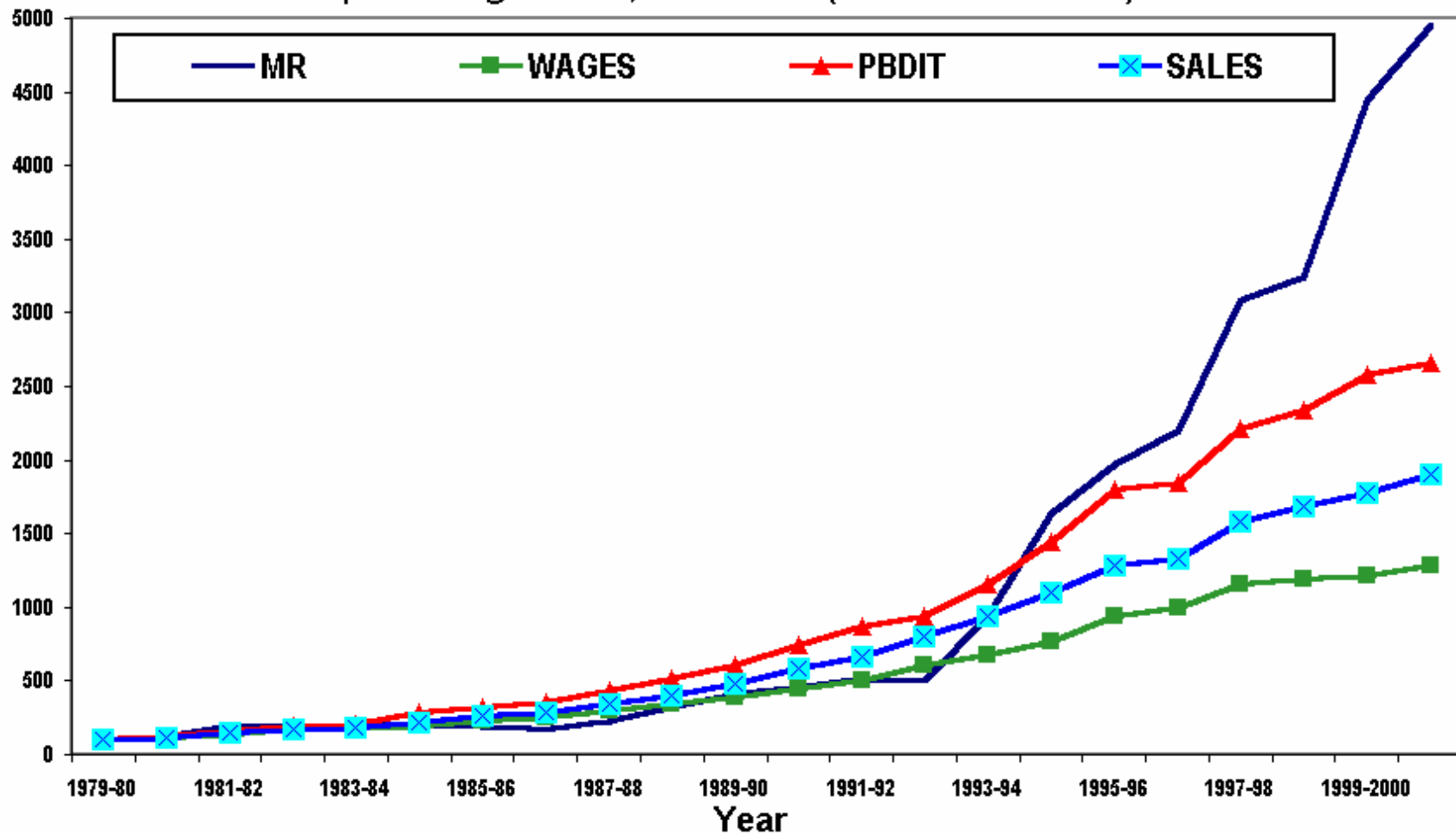
## We need in 21<sup>st</sup> Century?

- ⇒ 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
<b>Total</b>	<b>100%</b>	

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

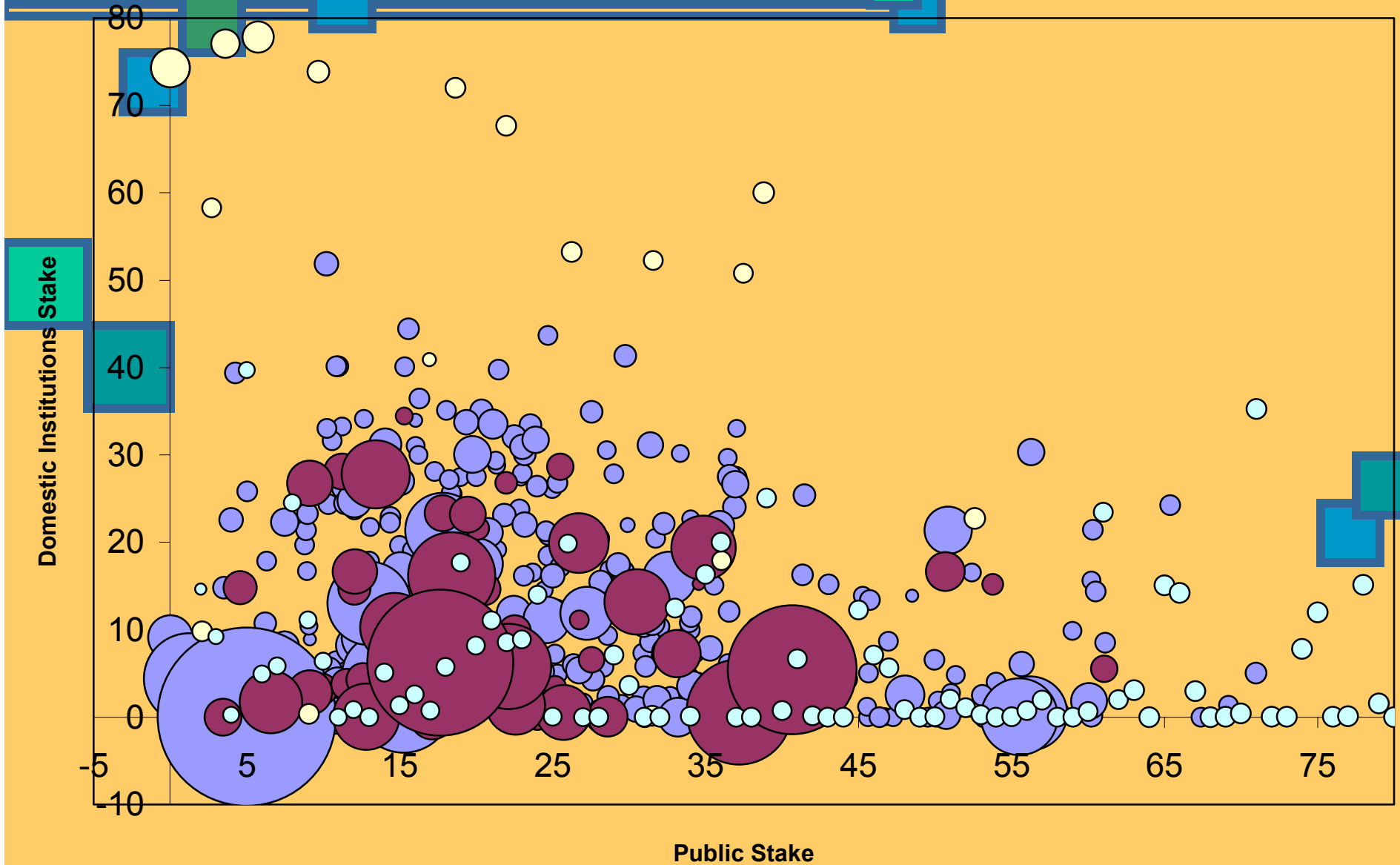
- Domestic Institutional Investors

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

2003



## 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?

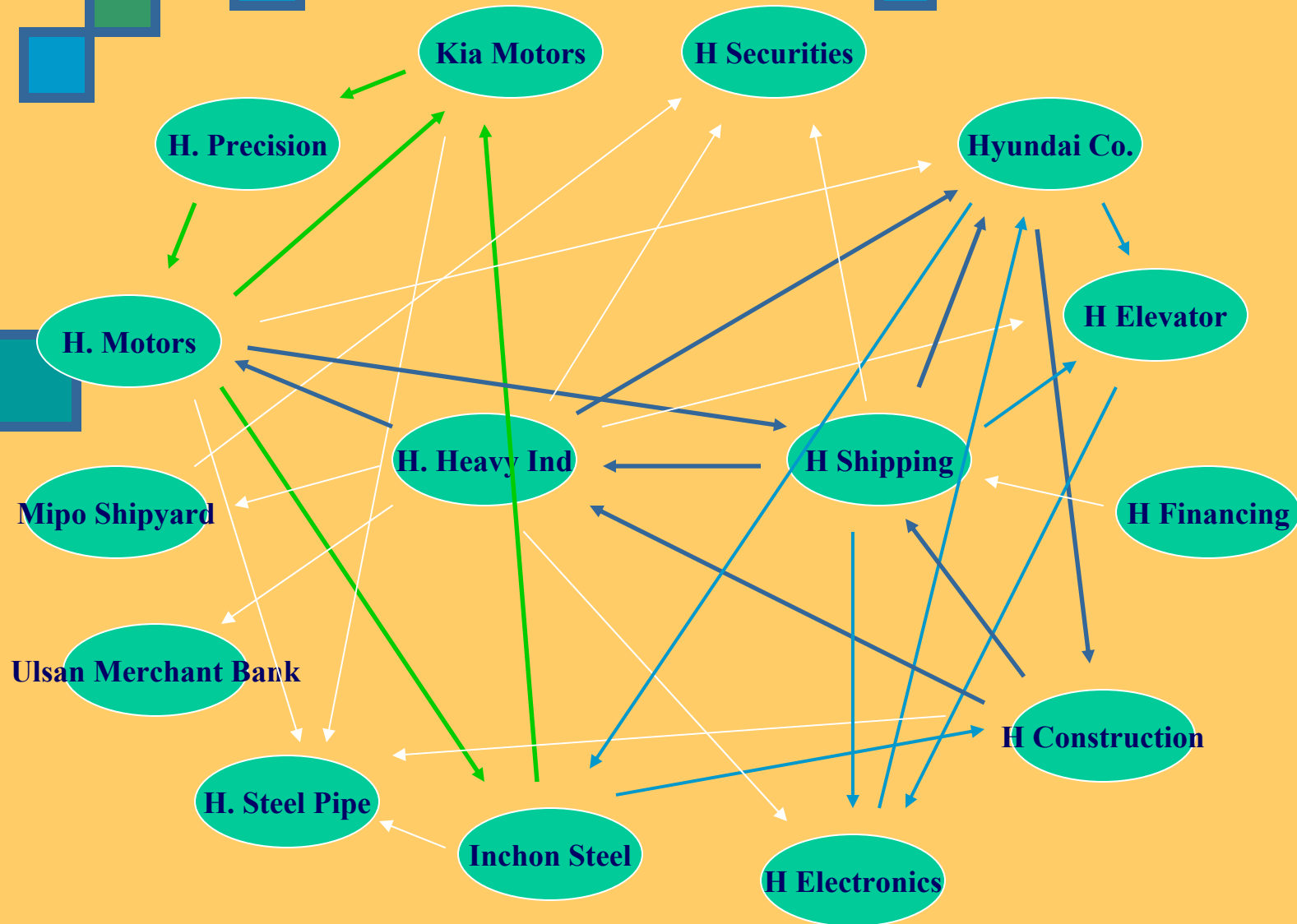
# New Regulations

- 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

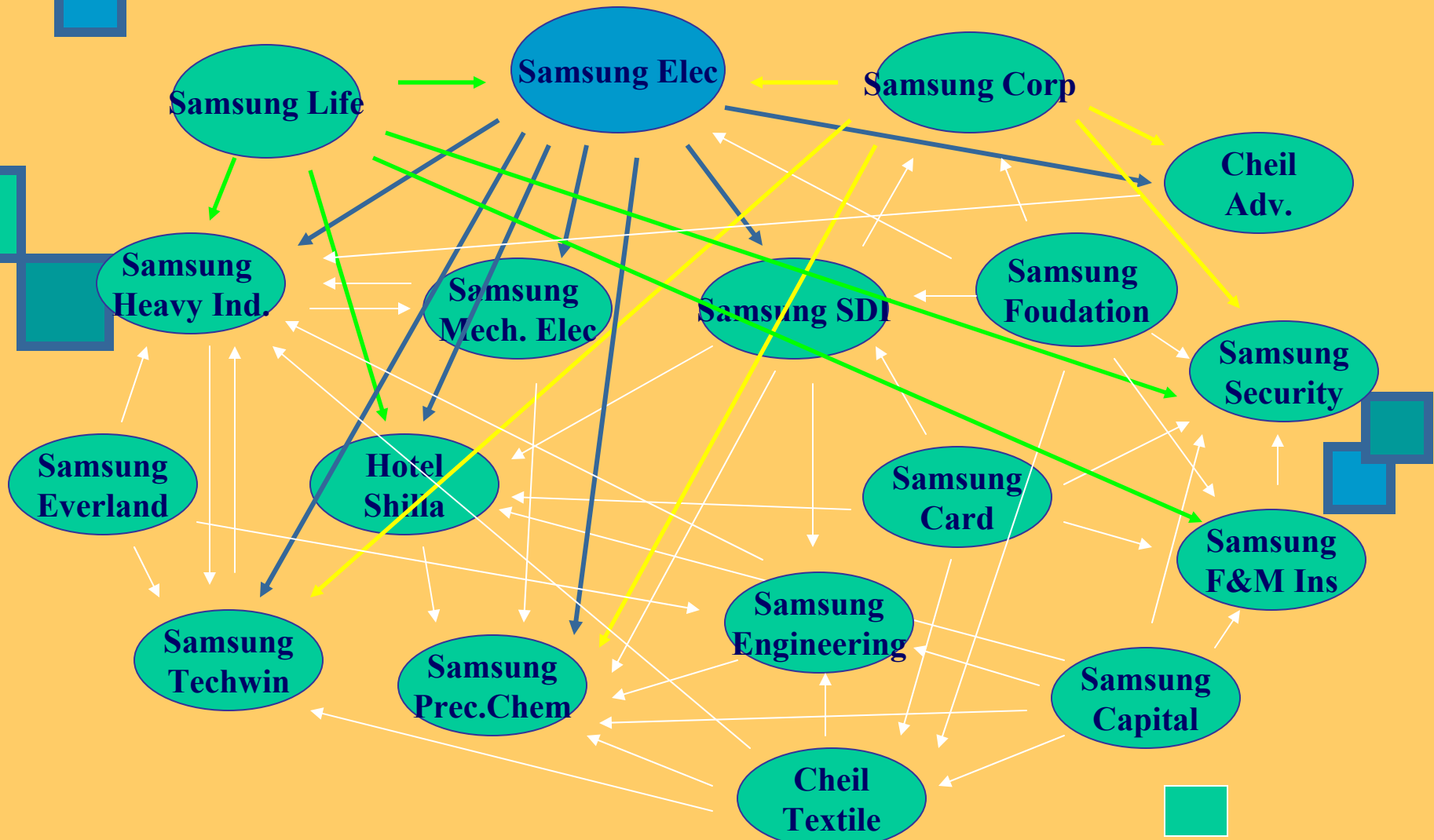
- Integrated supervision agency be established
- More regulation on related party transactions
- Stricter liability on accountant
- Improved accounting standards
- Duty of directors in legal codes
- Mandatory compliance officer
- Liability of controlling shareholder
- Cross debt guarantee prohibited
- 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

# 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