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Study on Influence of Board Independency and Corporate Governance on Financial Performance of Banking Sector in Bengaluru

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Abstract: The process of decision making within and between the governing bodies of an organization is improved by good corporate governance practices. This helps in enhancing the efficiency of the business operations and the financial performance of the organization. The board of directors plays a vital role in maintaining organizational efficiency in terms of profit and financial growth. In this context, the banking sector still debates on corporate governance practices with respect to board composition, particularly, board independence and transparency. Even though there are guidelines in mandating number of independent directors, the association between board composition and performance are yet to be established. The purpose of this study is to examine corporate governance practices of selected public and private sector banks in Bengaluru and identifying how the board independency and transparency influence the financial performance of the banks.

Keywords: Corporate Governance, Board Independency, Board Transparency, Financial Performance, Banking sector.

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1. Introduction – The relevance of corporate governance to build confidence and exactness among stakeholders The Basel committee on Banking Supervision has framed ethical framework.[1]Financial organizations, being profoundly utilized, can evading certainty through an efficient corporate governance system (Gopinath et al., 2021a). Effective corporate governance enhances value in monitoring and management. In addition, sound corporate governance practice is a significant component in paving way for investors, and investors are happy to pay a premium of up to 25% for a well governed organization (Barton, Coombes and Wong, 2004)[2].

Indian economy believes on bank based system in the monetary development**.**The income of Indian banking has increased from 11.8 billion American dollars to 46.9 billion American dollars in the year 2010.

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[1]Basel Committee (2006), "Enhancing corporate governance for banking organization," February, Bank for International Settlements, Basel: Report. https://www.bis.org/publ/bcbsc138.pdf.

[2]Barton et al, 2004, D. Barton, P. Coombes, S.Y. Wong, Asia's governance challenge McKinsey Quarterly, 2 (2004), pp. 54-61

As the banking industry turns out to be increasingly intricate, competitive and lack transparency, the BOD's plays a relevant role in efficient corporate governance with effective management. The intricate nature of banking made banking guideline progressively rigid. Understanding the significance of board structure in banking sector for the best possible working of the banking system. Indian regulators underscored the significance of the board through an alternate administrative system (Gopinath et al., 2021b). The organisation structure in banking sector has been defined by RBI through "fit and proper" models. In addition, the market controller. The framework related to BOD has been given by SEBI under clause-49 and through that corporate governance practice has been made compulsory for every single listed organization in India. This research article shows the significance of board independency on financial performance of banking sector in Bengaluru.

1.1 Board Independence

The major factor for the board independence is getting adequate number of independent Bod's. The ability, eagerness and board environment may pave way for independent approach of every director (Gopinath, 2019a). In any firm, nearness of more non-official individuals in the boards, over the total number of directors, is relied upon to practice board's independence. These directors, who are not executives, are relied upon to head the review panel; subsequently such a role is considered to as intermediary to the investors and also indicates well in the governance index.

1.2 Independent Directors

The role of independent directors on the board of directors is to viably screen and control activities of firm in lessening deft administrative practices and apprehension of firm's assets. Nevertheless, challenges faced by independent directors in carrying out their responsibilities are not legitimately partnered with the management. There is proof to show that independent directors are esteemed for their capacity to prompt, to set business and individual connections, and to signify that the organization is doing well instead of just monitoring ability.

1.3 Importance of independent director

Independent directors have become a crucial instrument in indicating the stakeholders' interests extending to the minority investors from the expense power. As per Juan Ma and Tarun Khanna (2013) the resistance for minority investors are from the side of Independent directors. Outsider guidance and oversight in guaranteeing the correct governance of the organizations by the directors. The working performance and firm value are correlated with directors.. Likewise, independent directors fill in as operators of arranging irreconcilable situations among management and the board because of their autonomy from both (Gopinath, 2020a). In addition to mitigating conflicts, independent directors have different points of interest too. They evidently are more knowledgeable when compared to an executive director who has all the more firm-explicit knowledge (Gopinath, 2020b). Therefore they focused on external factors influencing the firm over a long term. The suggestions are received from independent directors without any prejudices. This suggests that independence is the core element that makes independent directors a successful device towards achieving better governance (Gopinath, 2019b).

1.4 Transparency

An effective Corporate Governance augments transparency and furthermore legitimacy of financial statement. Transparency governance suggests organization's activity revealing adequate as well as sufficient data to all the stakeholders. Facilitation of monitoring supports transparency to enhance accountability, and providing of incentive for agents supports accountability to enhance transparency so as to make sure that the activities of the agents are appropriately distributed and comprehended together (Gopinath, 2020c). Collectively accountability and transparency enforce a principle that improves the process of decision making. This thus builds the financial performance of the banking sector/ventures. Transparency in reporting of corporate financial additionally improves the decision making process in the capital market and the risk management quality by all market participants. It upgrades the nature of allocating resources and in this manner increments financial performance at the macro level (Bhattacharyya, 2003)[3].

1.5 Association between Board Independence and Firm Performance

The organisations working process and activity is to be observed and requires changes if it is essential. Effective monitoring mechanism in the firm could lessen organizational issues. Therefore, the organization ought to name independent directors who could practice legitimate monitoring work in checking governance, risk management and internal control (Gopinath & Chitra, 2020a). For the growth and effective firm performance there is a need to have independent directors in the board. This is corresponding to the elements of the independent directors to expand the wealth of shareholders. Good corporate governance practice by the organizations is ensured by Board independence(Foo and Zain, 2010). The relevance of data depends upon the existence of board independency and transparency, It implies that the board would be more transparent when it was independent and distribution of information across the concerned individuals improves liquidity of the firm.

2. Review of literature

Renata Karkowska & Jan Acedański (2020)[4]intended to experimentally distinguish frame work of a bank and quality (experience, skills & background) influence its motivating forces. In particular, it examines whether banks' solvency and corporate governance nexus transformed after financial crisis from 2007 to 2009. The study employed both public and commercial banks for the purpose of study.

This outcome shows that in the repercussions of the market emergency, everything was needed to reinforce corporate governance practices which may reduce the undesirable impacts of the emergency on the banking sector.

Karim, Md. Rezaulet al (2020)[5]analyzed the determinants of board independence in the banking sector of Bangladesh. The study employs

a multivariate board relapse investigation for the thirty banks listed with DSE covering the period between 2006 and 2016. When directors provide significant expertise as needed by company's guidelines the result shows the independency of the directors. Moreover, this article exhibits the large scale firms are enjoying more independent than small scale firms. In addition, the boards of the turned firms will in general be increasingly independent since debt holders apply extreme strain to actualize severe monitoring techniques.

[3] Bhattacharyya, K Asish. (2003), „Corporate reporting for corporate governance: An introduction", Decision, 30: 1, 1-25.
[4] Renata Karkowska& Jan Acedański (2020) The effect of corporate board attributes on bank stability, Portuguese Economic Journal volume 19, pages99 137(2020)/ https://link.springer.com/article/10.1007/s10258-019-00162-3
[5] Karim, Md. Rezaul, Mitra, Ranjan Kumar, and Khan, Ibrahim. (2020), Determinants of Board Independence in the Banking Sector of Bangladesh. In: Journal of Economics and Business, Vol.3, No.1, 65-81

Ayodeji Ajibade et al (2019)[6] the current investigation plans to focus on the connection in the midst of financial performance of Deposit Money Banks and board independence as well as giving a similar view by emphasizing on Canada and Nigeria. The study tries to examine the relationship among the board independence and growth.

. From the findings, it is uncovered that there exists a noteworthy connection between board independence and profitability of deposit money banks in both the nations. Experimental outcomes uncovered that independent audit committee advanced monetary performance of the deposit money banks in Nigeria while in Canada it was certain and immaterial. Both independent directors and audit committee members are essential for the benefits of banks.

3. Research Gap

Existing studies on bank corporate governance intently revolve around a single facet of governance, such as the role of directors or of investors, while excluding different components and connections that might be significant inside the governance structure. Corporate governance has obtained a lot of consideration in the accounting literature, with studies revolving around the effect of corporate governance and the financial performance of the firm. Corporate governance are highly prioritized by policymakers, investors, financial establishments, organizations and academics. In the literature, various studies have tried to research on the board independency and transparency and its connection with financial performance. Most of the studies have demonstrated a mixed outcome without a definite association. Profitability of an organization is positively impacted by corporate governance practices, whileon the other hand, evidences show that board independency does not have any impact on financial performance. This present study accordingly tries to explore the relationship that exists between board transparency and independency and financial performance of banking sector in Bengaluru. There is a requirement for more grounded tests to perceive the impacts on a bank's financial performance with respect to board composition. Subsequently this study aims to address these gaps on board independency and transparency and its influence on financial performance among the banking sector in Bengaluru.

4. Statement of the Problem

In many of the developing countries, private ownership of banks are not allowed and there is huge intervention of government control. The association between the banks, large businesses and political or government circle contribute to the poor corporate governance practices. In India, rules and regulation of corporate governance are ineffective as the boards ignore these practices for reasons such as unproductive executive management or non-qualified directors who obtain unsecured loans just for themselves at the expense of depositors, failing to enforce good governance on bank management. This is not only due to lack of audit process at banks which has led to rapid deterioration of the economy, but also due to lack of board independency and transparency which affects the return on assets and leverage of the banks. These issues have pushed the researcher to address the concerns of this topic so as to find out the influence of board independency and transparency on financial performance of banks in Bengaluru.

[6] Ayodeji Ajibade, Richard Adeleye Okunade (2019) Board Independence and Financial Performance of Deposit Money Banks in Nigeria and CanadaMay 2019

5. Objectives

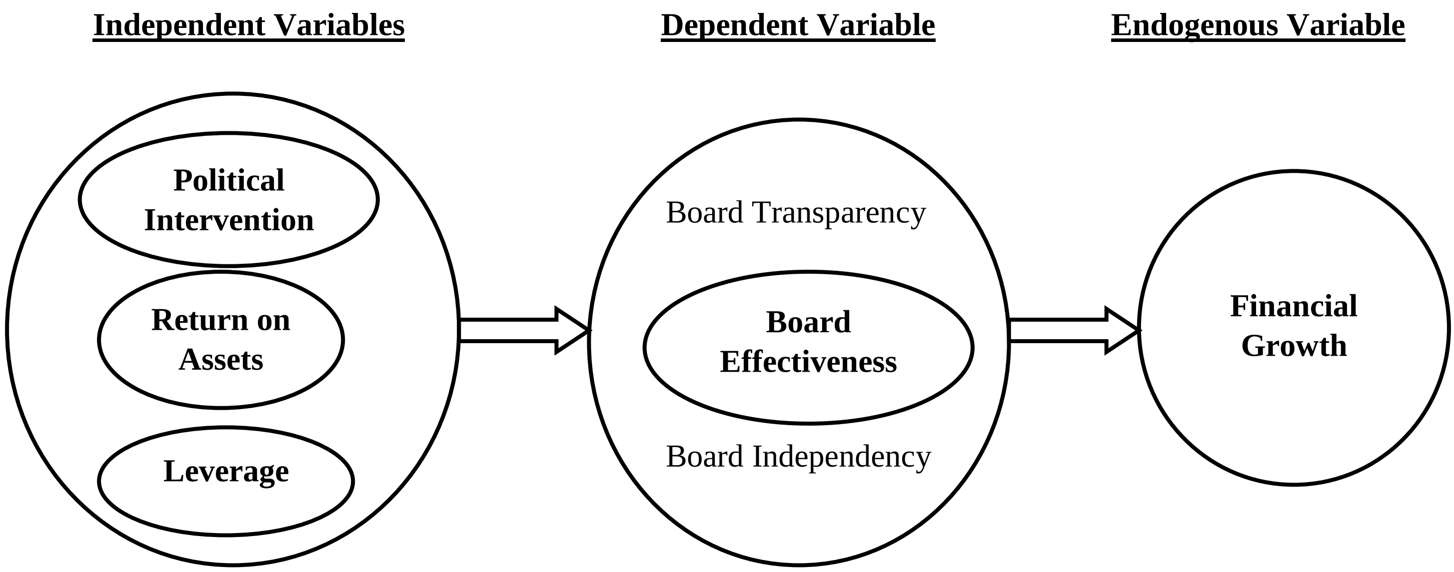
- To study the determinants of board composition in banking sector in Bengaluru
- To analyse the influence of board independency and corporate governance on financial performance of banking sector in Bengaluru

6. Research methodology

The methodology adopted for a study is a significant part in research asit discusses research design, samples and sampling method, hypotheses and data collection technique and methods for interpretation of the research data. The present study is explorative as it takes into consideration the influence of board independency and transparency on financial performance of banking sector.The study is also empirical because the study examines the relationship between the independent and dependent variables related to the board independency, transparency and financial performance.

6.1 Conceptual Framework

Figure 1.1



Selected banks for the present study

Table - 1

Selected Private and Public sector banks in Bengaluru

SL. No.	Nationalized banks	SL.No.	Private banks
1	Dena bank	4	Indus Ind bank
2	Canara bank	5	HDFC bank
3	Bank of Baroda	6	ING Vysya bank

Source: Self prepared by the researcher

6.2 Data collection:

The present study used **Primary Data** collection method by preparing a self-administered questionnaire related to the influence of board independency on financial performance and information about the Corporate Governance practices followed by the Bank selected for the present study. Questions were structured with both open and close ended questions based on the Self developed instrument on 5-point (1- strongly disagree to 5- strongly agree) Likert scale. **Secondary data** collection method was implemented in this study by gathering already existing information from journals, articles, annual reports of the banks, books, magazines, newspaper articles etc.

6.3 Sample population

Executives were personally interviewed to seek their opinion on the influence of board independency on financial performance of banking sector. The target population for the present study are Vice Presidents, Company Secretaries, Top-Level Management and Financial experts in the area of Corporate Governance from the selected Private and Public banks in Bengaluru city.

6.4 Sampling Technique and Sample Size

For collecting the information convenience sampling method was chosen

. This method was particularly chosen because the sample taken from a group of people (respondents) are easy to reach or contact. .A sample of 117 respondents comprising of Company Secretaries, Vice Presidents, Financial experts and Top-Level Management in the area of corporate governance from the selected private and public banks in Bengaluru city.

6.5Statistical Tools

The collected data has been analysed using the statistical package AMOS and SPSS 20 and hypotheses were tested using the statistical tool like Regression, Chi-Square and SEM (Structural Equation Modelling).

7. Analysis and interpretation

Regression Analysis

H_{03} –There is no significant relationship between Leverage and Financial growth

H_{04}–There is no significant relationship between Return on Assets and Financial growth

Table - 2

Model Summary

Model	R	R Square	Adjusted R Square	Std.Error
	0.574	0.329	0.317	3.111

ANOVA

Model	Sum of Squares	df	Mean Square	F	Sig
Regression	540.620	2	270.310	27.936	0.000
Residual	1103.073	114	9.676		
Total	1643.692	116			

***5% Significant Level**

Co-efficient

Model	Unstandardized Coefficients		Standardized Coefficient	t	Sig.
	B	Std. Error	Beta		
(Constant)	8.318	2.026		4.106	0.000
Leverage	0.280	0.077	0.317	3.622	0.000
Return on Assets	0.388	0.097	0.350	4.003	0.000

***5% Significant Level**

Discussion:

The dependent variable is financial growth and leverage is an independent variable. The study shows financial growth is influenced by leverage. On the other hand Return on Assets is also a independent variable which also influences the financial growth. Null hypothesis is rejected because P value is lesser than significant value.

SEM Path Analysis

Figure – 1

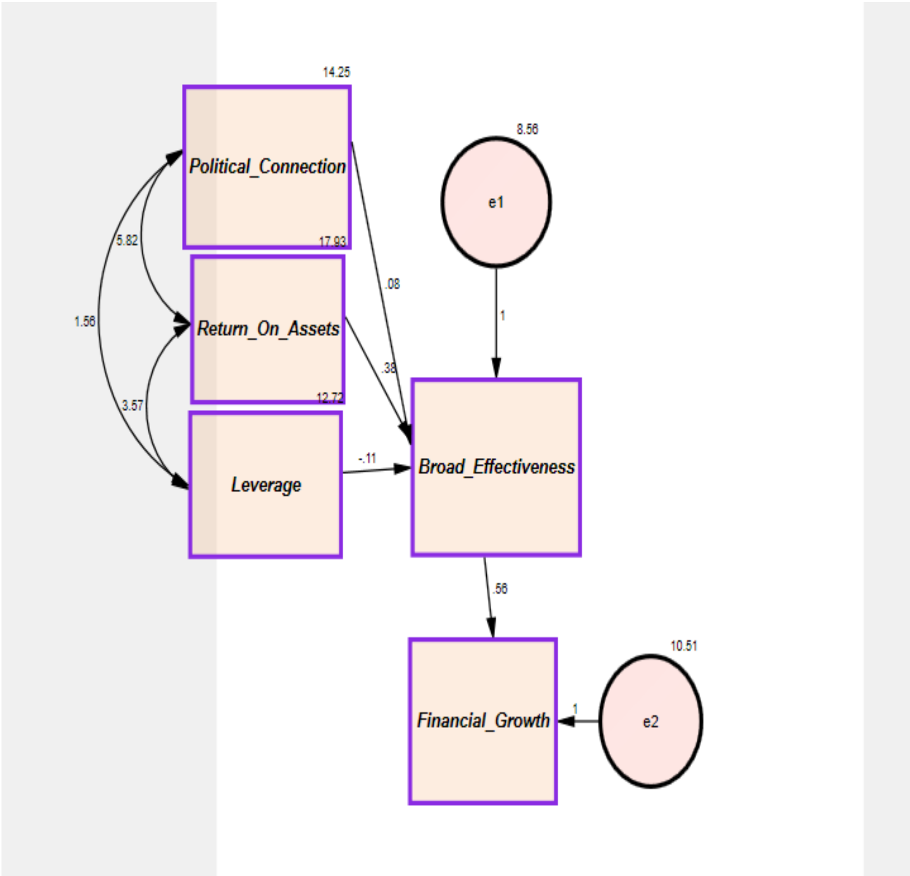


Table -3

Testing of Hypothesis

Hypothesis	Relationship	SE	P-Value	Result
H_{03}	Political Connection has no influence on Board Effectiveness	0.077	0.314	Not Significant
H_{04}	Return on Assets has no impact on Board Effectiveness	0.070	0.000	Significant
H_{05}	Leverage has no impact on Board Effectiveness	0.078	0.144	Not Significant
H_{06}	Board Effectiveness has no influence on Financial Growth	0.089	0.000	Significant

Significant at 1% Level

Model Fit

Table – 4

S.No	Model Fit Indices	Calculated Value	Acceptable Threshold Levels
1.	Goodness of Fit Index (GFI)	0.957	0 - 1
2.	Comparative Fit Index (CFI)	0.984	0 - 1
3.	Adjusted Goodness of Fit Index (AGFI)	0.942	0 - 1
5.	Tucker Lewis Index	0.914	0 - 1
6.	Root Mean Squared Error of Approximation (RMSEA)	0.022	0.05 or lesser

Discussion:

To estimate the appropriateness of the overall model, the study assessed the measures representing the overall fit, absolute goodness of fit (GFI = 0.957) incremental fit indices (CFI=0.984), Tuker Lewis index (TLI=0.915) and root mean square error of approximation (RMSEA= 0.022). The model proved as a good fit because based on data analysis FGI CFI & TLI measures shows greater than 0.90 .

Chi-Square Test

Table - 5

H_{07} - There is no relationship between education and Monthly Income of the respondents

Factor	Value	Df	Symp. Sig. (2-sided)	Statistical Inference
Karl Pearson Chi-Square test	91.703	3	0.000	**Significant**
Likelihood Ratio	111.178	3	0.000	
Linear-by-Linear Association	6.428	1	0.011	
No. of Valid Cases	117			

***Significant at 5% level**

Result and Discussion

The table shows the null hypothesis is rejected as P value is below the significant level. "There is no relationship between education and monthly income" is rejected; and it is proved that there is an correlation between monthly income factors and education.

8. Findings

- From the study it is found that financial growth is a dependent variable and leverage is an independent variable.. From the table - 1 it is found that thePValueis0.000,AstheP value shows lesser than a significant level of 5% it is concluded that leverage influence the financial growth.
- In this study null hypothesis is rejected because P value is lesser than significant value that is five percent and also shows that return on assets influence the financial growth.
- The study shows the model is fit because it was proved that GFI, CFI and TLI is greater than 0.90 and the appropriate tool used is SEM analysis.
- Another findings of the study is that there is an association between education and monthly income factors which has been proved through chi-square test, having value of 91.703 at three level degrees.

9. Suggestions

- The banks must strengthen the regulatory mechanisms with respect to board effectiveness in order to promote good corporate governance practices within the organizations.
- The shareholders should promote board independence, board diversity and allocate independent audit committees. This will increase the frequency of board meetings paving way for board transparency.
- Regulatory bodies of private banks should set up policies to enhance corporate practices paving way for achieving financial profitability.
- Increase in board size can also affect the performance of the organization. Hence, there must be transparency in number of directors in the board.

10. Limitation and future scope

Few respondents were reluctant to share data identified with the corporate governance process, referring to the sensitive nature of the issue. They consented to do so just on the state of confidentiality. The findings of this paper cannot be generalized since the corporate governance practice in the banks has been concentrated from the perspective of the banks as it were. It has not been workable for the researcher to consider the real impact that the corporate governance process on both the external and internal stakeholders. This area could give more scope for further research regarding this topic. There is likewise scope for contemplating the board structure and bank performance with more financial parameters.

11. Conclusion

The motive behind governance is not only concentrating on benefits to the firm but also improving more corporate social responsibility and accountability. In the stakeholder value, organizations should practice its corporate responsibility to stake holders of different organizations (Gopinath & Chitra, 2020b). The existence of number of independent directors will have more social relevance and benefits to the firm.

The ongoing financial crisis and from there on the breakdown of enormous banks have raised concerns about the board independency of banks. The study also recommends provisions for board structure in the banking sector (Subhashini et al., 2020).It is apparent from this investigation that the board independency of the bank is significant in banks' financial performance. An ideal board structure and independency and transparency will to a great extent add to the prudent performance of banks in India particularly in the study area Bengaluru.

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