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Exploring the Impact of Corporate Governance on the Financial Performance of Indian IT Industry

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ABSTRACT

This paper involves research into the interface between corporate governance and financial performance in the Indian IT sector from the angle of the role played by the governance mechanism of board size, board committees, and board meetings on ROE. This study is based on secondary data compiled from the annual financial reports of the seven IT companies listed during the period of 2022-2024. Utilizing a quantitative approach for this research, this research applies the use of descriptive statistics, correlation analyses, and regression analyses. Hence, the average model analysis gives a moderate correlation between corporate governance factors and ROE, with 54.3% of ROE variance explained by these predictors. Though, the correlation results are not significant, so a complex indirect link between governance and financial performance has been revealed. Although the regression model is highly significant, many other factors also affect ROE. Further, the research shows that it needs more corporate governance dynamics. Further, it concludes that the evolving economic and regulatory environment in IT industry should help governance practices move forward.

Keywords: Corporate Governance, Financial Performance, Return on Equity (ROE)

1. Introduction

Corporate governance can be described as the rules, practices, and standards governing corporate entities, boards of directors, executives, and other stakeholders about their behavior and decision-making. Its role is to balance the interest of shareholders, customers, regulators, and the broader economy, besides promoting responsible and ethical conduct, as well as protecting the interest of all the stakeholders. Corporate governance of the IT industry in India is an important framework that governs financial institutions and guides them on the aspects of transparency, accountability, and protection of various stakeholders' interests. The need for good corporate governance maintains stability and integrity within the IT industry while protecting the interest of various stakeholders and sustainable financial performance. Still, there is a pressing need to take the existing state of corporate governance in the IT industry into serious consideration. More importantly, there is a complex interrelation between the financial performance of IT firms and the practice of corporate governance and, thus it becomes necessary that policymakers, regulators, and industry participants be well apprised of this interrelation. The current paper aims at understanding the inter-link between the governance practices followed in the management and the subsequent financial performance; thereby, valuable insight will be drawn towards developing a more effective structure for governance for this critical sector. The purpose is to understand if a significant, statistically relevant relationship between the adopted corporate governance practices by IT firms and their respective financial performance actually exists. This would be establishing the actual mechanisms of governance through board composition and board committees as well as how they relate to financial metrics like ROE in this particular instance.

Corporate governance provides the very base of transparency, accountability, and ethical management practices within any organization. Effective corporate governance practices in the IT industry, which is the prime pillar of the nation's economy and a leader in technological innovation worldwide keeps respective stakeholder interests comfortable, regulatory requirements met, and ensures sustainable growth.

Corporate governance has proved significant, and at the same time, the study scopes open for a more in-depth investigation of how and to what level governance practices contribute toward performance in financial statements in the Indian IT sector. Such complexity results from an alteration in regulatory environment and increasing expectations by stakeholders with an ever-changing character of the IT industry. The aim of the paper is to understand how Indian IT companies and their financial performances are influenced by corporate governance. The findings of this study will give valuable insights into the role of corporate governance in enhancing financial outcomes, thereby contributing to a better understanding of best practices and areas for improvement within the Indian IT industry.

2. Review of Literature

In the study by **Pal and Patel, (2024) [5]** the financial performance of leading IT firms in India is studied. As part of key gauges related to profitability, liquidity, ROA, ROE, and market valuation of the IT sector, the performance analysis is also carried out here for evaluating financial health and stability.

The findings indicate that profitability and liquidity vary across firms, with the larger companies having more financial stability and higher market capitalization. Innovation, global demand, and operational efficiency are some of the key drivers of the financial performance of IT firms. Revenue growth and investment patterns in the sector are influenced by macroeconomic factors and regulatory policies. It therefore concludes that, for long-run sustainability, performance in the IT industry of India is critical in terms of finances. The work is of utmost value to the investor, policy maker, and corporate manager regarding strategic financial planning to enhance growth and competitiveness.

Corporate governance is very critical in terms of financial stability and long-term success. **Sarkar, (2022) [3]** the author explores the impact of corporate governance on the financial performance of Indian firms. The study examines key governance indicators such as board composition, ownership structure, transparency, and regulatory compliance to determine their influence on profitability, return on assets (ROA), and market valuation. The study results indicate that good corporate governance has a positive relationship with better financial performance. Firms that have independent boards, an efficient mechanism in the audit, and high transparencies in governance will be likely to achieve higher profitability and market credibility. The results of the study further reflect that firms which have better structures of governance attract higher investor confidence and incur fewer financial risks.

Diriba and Basumatary, (2019) [1] the authors studied how corporate governance practices affect the financial performance of the top Indian companies. The study uses empirical analysis to explore key governance factors such as board structure, ownership concentration, and transparency. The findings pointed out that firms with strong governance frameworks have higher profitability, better market valuation, and improved investor confidence. It hence depicts how corporate governance plays a key role in the sustainability of growth and thus turns into an important consideration for the policymakers, investors, and corporate managers within the Indian dynamic business environment.

Selarka, (2018) [4] had studied into the development, adoption, and effects of corporate governance in Indian firms, which aimed to study governance mechanisms that include board structure, ownership concentration, transparency, regulatory compliance, and shareholder rights to enhance accountability and stability within these firms.

Findings indicate the country has seen much improvement, although it's still not effective enough in firm performance and overall minority shareholder protection with independent boards in place with SEBI guidelines, and, to some extent, the reforms introduced by the Companies Act of 2013. The bottom line is firms that have in place a very good governance system has better performances financially, with greater investor confidence, and exhibit lesser corporate malpractices. Selarka concludes that it is strong governance that will catalyze Indian sustainable growth. The paper provides useful insights for the regulators, investors, and corporate managers toward constant improvement in governance, thus leading to better transparency and protection of stakeholder interests.

Kaura et al., (2019) [6] examine how corporate governance practices are associated with IT sector financial performance. The key governance factors assessed are board composition, ownership structure, transparency, and audit mechanisms with reference to their impacts on profitability, return on assets (ROA), return on equity (ROE), and market valuation.

It can therefore be concluded that there is a positive association between high corporate governance and company performance. Companies that have boards of independent directors, effective regulatory compliance, and shareholder-friendly policies will most likely display better profitability, financial stability, and investor confidence. It further stresses that governance is of prime importance as it will benefit in managing risks and resultant sustainable growth in a fast-changing technology environment. The study gives insights into the significance of corporate governance for improving financial performance in IT firms, which can be gainfully fruitful for investors, policymakers, and business leaders. The paper assumes a crucial role in continuous governance improvement while maintaining competitiveness and therefore achieving long-term financial success in the IT sector.

Reforms in corporate governance and social reporting are the core factors that make financial growth possible and bring confidence among investors to India. **Goel (2018) [7]**, in his study examines the relationship of corporate governance practices with financial performance in the Indian corporate sector. The study, therefore, is based on reforms in governance, regulatory frameworks, and social responsibility reporting about the changes in profitability, market valuation, and investor confidence.

The findings indicate that effective governance mechanisms, for example, transparency, independent board oversight, and stakeholder engagement have a positive impact on performance. Companies involved in governance reforms, as well as those complying with social reporting standards, are more capable of demonstrating financial solidity and having a solid reputation, thus increasing their opportunities to gain access to capital markets. The paper points out the evolution toward ethical business practices and sustainable long-term performance through mandated corporate social responsibility CSR disclosures.

Vennila and Chandru, (2021) [8] analyze the financial health of the leading IT firms in India. The study analyzes key financial indicators such as profitability, liquidity, return on assets (ROA), return on equity (ROE), earnings per share (EPS), and market valuation in order to understand the overall performance of the firms.

The study shows that Infosys and Tech Mahindra are companies with strong financial stability, profitability, and revenue growth and are ahead of the market leaders. Larsen & Toubro Infotech have stable growth trends while 3i Infotech have lower profitability and higher risks of financial impairment.

The growth of IT industry firms is driven by market and technological trends coupled with global demand, as revealed by the results. The paper concludes that the IT sector's sustainability is based on strategic financial planning, investment in innovation, and strong governance.

Aggarwal, (2013) [2] analyzes the impact that corporate governance practices have on financial performance in firms. The most vital factors have been researched here like board structure, ownership patterns, transparency, and regulatory compliance and whether these factors have an impact on profitability, return on assets (ROA), and market valuation.

Findings are that companies with strong corporate governance structures are better financially stable, more confident of investor confidence, and perform better over the long term. Companies that have more independent boards, active audit committees, and shareholder-friendly policies are perceived to have better profitability and lower financial risk.

Aggarwal has stressed the necessity of governance reforms to ensure transparency and protect shareholder interests. In conclusion, this study shows that robust corporate governance is necessary for sustainable financial success and provides valuable insights for policymakers, investors, and corporate leaders who seek to improve firm performance in a competitive business environment.

The current literature covers a wide connection between corporate governance and financial performance of Indian firms, mainly in the IT sector. There exist studies by Sarkar (2022), Diriba and Basumatary (2019), Kaura et al. (2019), Aggarwal (2013), to establish a positive correlation between structures of governance with profitability and investor confidence. Selarka (2018) and Goel (2018) also found governance reforms and their consequences on financial stability. The works by Pal and Patel (2024) and Vennila and Chandru (2021) analyze the ROA, ROE, market valuation of an organization in its financial performance using macroeconomic variables and innovation variables. But so far, an important gap of research remains within the interaction of governance mechanisms that affect the time-series performance for financial sustainability for the IT industry, particularly when digital transformation with regulatory changes shape the new waves of strategies after the pandemic era.Moreover, there exists a dearth of well-tested empirical support with regard to how governance practices may influence the firm's decisions concerning long-term investment and risk management in the context of IT firms. After delineating future research directions, sector-specific governance frameworks combined with longitudinal studies would probably be more illuminating of sustainable financial performance within the Indian IT industry.

3. Research Methodology

To determine the relationship between Corporate Governance and Financial Performance of IT companies in India, that is, to examine and analyze the possible link between two delicate aspects within the IT sector: corporate governance practices and the financial performance of IT companies in India.

This particular research is an empirical study which utilizes secondary source of data. It is employed to assess the financial performance of IT companies, drawing from pre-existing financial reports and data sources extracted from Capitaline Databases. This study took a sample size of 7 IT companies which are publicly listed in India. The data is taken for 3 years i.e., 2022 to 2024. It covers specific governance mechanisms, for instance, board size, board committees and number of board meetings in a year and measuring the outcome on financial metrics i.e. Return on Equity (ROE). While computing the data for analysis different tools of analytics are used. Quantitative methods of analysis include descriptive statistics, correlation and regression analyses to determine the strength and significance of relationships between corporate governance variables, such as board composition, and financial performance metrics, for example, return on equity (ROE).

4. Analysis and Interpretation

The independent variables examined are- Board Size: Refers to the structure and nature of a company's board of directors, e.g., the ratio of executive and non-executive directors, their background, and diversity; Board Committees: Special committees of a company's board of directors that take care of certain functions or fields, e.g., audit, compensation, and governance; and Number of meetings held in a year: Number of times a company's board of directors meet to discuss and make decisions regarding company issues. These 3 independent variables account for the corporate governance structure of the IT firms. The Dependent variable here is Return on Equity or ROE which is a financial indicator that accounts for the profitability of a company by measuring its net income as a percentage of the shareholders' equity, indicating the efficiency with which the company generates returns on the capital of the investors. It is an indicator of financial performance of these firms.

The analysis of the variables is given below:

- Descriptive Statistics- The descriptive statistics provide insights into the central tendency, variability, and distribution of the variables in the dataset.

Table-1 (Descriptive Statistics of variables- ROE, Board Size, Board Committees, Board Meetings

	N	Minimum	Maximum	Mean	Std. Deviation	Variance
ROE (Dependent variable)	21	18.60	59.40	30.23	10.58	111.85
Board Size	21	6.0	15.0	10.62	2.42	5.85
Board Committees	21	5.0	9.0	6.62	1.40	1.95

Board Meetings	21	4.0	9.0	6.57	1.47	2.16

Source: Authors' compilation

The descriptive statistics are of interest in revealing the distribution and variability of the most important variables: Return on Equity (ROE), Board Size, Board Committees, and Board Meetings. The mean ROE is 30.23%, with a range that varies from a low of 18.6% to a high of 59.4%, indicating significant variation in financial performance among various firms. The high variance of 111.85 indicates that some firms perform significantly better than others, perhaps indicating variations in governance structures, strategic choices, or external market conditions. The number of board members ranges from 6 to 15, and the average size is 10.62 members, with a moderate standard deviation of 2.42. This suggests that most firms have relatively similar compositions. The Board Committees are within a pretty uniform range of 5 and 9 with an average of 6.62 and with very low variance at 1.95 indicating standard governance practice in firms. Likewise, the Board Meetings have ranged between 4 and 9 with an average of 6.57 which indicates most firms have a systemic approach toward involving the board. This implies that governance variables have a relatively low variation, while the high variation of ROE means that board structures are likely to influence financial performance but external and internal factors follow the significance of these.

- Correlation and Regression Analysis- Correlation analysis is a statistical technique used to examine the nature and the strength and direction of a linear relationship between two or more variables. While regression analysis extends the understanding gained from correlation by modelling the relationship between a dependent variable, for example, ROE and one or more independent variables, for instance, Board size, Board committees and No. of board meetings.

Table-2 (Correlation of ROE with Board Size, Board Committees, Board Meetings)

	Model 1
R	.737[a]
R Square	.543
Adjusted R Square	.462
Std. Error of the Estimate	7.75%
Sig. F Change	.003
Durbin-Watson	2.305

Source: Authors' compilation

The correlation analysis for IT firms reveals interesting findings about the linkage between financial performance, measured through Return on Equity (ROE), and the most critical variables of corporate governance. The negative measure of the correlation (-0.351) between ROE and Board Size indicates a very weak inverse correlation, which is that bigger boards are related with lower ROE. The degree of negative correlation between ROE and Board Committees is (-0.373). This means there is a very weak inverse correlation, and presence and effectiveness of specialized committees at the board do not positively correlate with ROE. However, the correlation between ROE and Board Meetings stands at (-0.259). This is a negative correlation. It could show that fewer board meetings have been associated with better ROE. These findings give initial insights into how the interplay between corporate governance structures and financial performance is relatively subtle in the case of IT companies, therefore opening avenues for further investigation in the factors behind these relationships.

Table-2 (Regression of ROE with Board Size, Board Committees, Board Meetings)

a. Predictors: (Constant), Board Meetings, Board Committees, Board Size
b. Dependent Variable: ROE

Variables		ROE
ROE (Dependent Variable)	Pearson Correlation	1
	N	21
Board Size	Pearson Correlation	-.351
	Sig. (2-tailed)	.119
	N	21
Board Committees	Pearson Correlation	-.373
	Sig. (2-tailed)	.096
	N	21
Board Meetings	Pearson Correlation	-.259
	Sig. (2-tailed)	.257
	N	21

Source: Authors' compilation

The model summary gives insight into how well Board Size, Board Committees, and Board Meetings predict Return on Equity (ROE). The R value of 0.737 indicates a strong positive correlation between the independent variables and ROE. The R Square value is 0.543, indicating that 54.3% of the variation in ROE can be explained by the board governance variables. Value of Adjusted R Square is 0.462 with an observation of the number of predictors in the model. F-statistic is 6.720, p-value is 0.003 and which is statistically significant that means at least one of the independent variables has some meaningful impact on the ROE. The Durbin-Watson statistic is 2.305, which suggests that there is no significant autocorrelation in the residuals. That is, the model does not suffer from serial correlation problems. Overall, this model has a moderate to strong explanatory power, suggesting that board structure has something to do with financial performance but is unlikely to be the sole determinant of ROE.

5. Conclusion

Overall, the analyses yield a panoramic view of the relationships between corporate governance factors, more specifically Board Size, Board Committees, and Board Meetings, and Return on Equity (ROE). The regression model suggests a moderate correlation between governance variables and ROE; with 54.3% of the variance in ROE accounted for by predictors. However, a lack of statistically significant correlations in the correlation analysis implies that even though governance structures affect financial performance, their direct effect is not particularly strong on this sample. Negative correlations between ROE and governance variables indicate a more complicated relationship, and therefore, that it is possible for larger boards or more committees not to produce higher ROE. There are also other areas like the moderate explanatory power of the model (Adjusted R Square = 0.462) and the statistical significance of the F-statistic in asserting that governance factors do play a role, but other external and internal factors likely contribute to the variation in ROE. The Durbin-Watson statistic also approves the reliability of the regression model due to the fact that there is no major autocorrelation in the residuals. In summary, although corporate governance is a critical consideration, it is one of the many factors that determine a firm's financial performance.

Several limitations, which the current study explicitly declares, will most likely impair its robustness and generalization power. For the main constraints of fairly small samples and only 7 IT companies sampled, a problem of lower representativeness and statistical power exists. Only focus on the relevance of findings related to the global context has limitations, making a comparative research agenda across diverse countries necessary. Data availability and quality issues, a very limited time frame, and a possible mismatch with evolving governance practices pose even more challenges. Nevertheless, these constraints notwithstanding, the paper provides an opportunity for more detailed research in the future and calls for researching the complexities of corporate governance in IT companies. Potential studies could address changing governance opportunities in the context of dynamic economic and regulatory change, looking into complex interplay between governance structures, board compositions, and barriers to financial performance. More or less, the similarity in studies could be interesting to scholars and practitioners, even for policymakers, financial institutions, and investors, in furthering their understanding and practice improvement in governance within the IT sector.

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