A Study on Corporate Governance Disclosures in Selected Housing Finance Companies in India

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Abstract

Every company across the globe today focuses on basic principles of good corporate governance for performing efficiently and to enhance their valuation in the market. A good corporate can generate the source of attracting capital, foreign investment, investors' trust, confidence, and also take advantage of the vibrant stock market. Corporate governance is a code of business conduct and ethics that would greatly benefit the companies to thrive and prosper. The outcome of the literature review was that even though the disclosures are made mandatory, there is a large variation in the quality of corporate governance disclosure practices adopted by companies listed in different countries. Empirical research done earlier has also proved that good corporate governance practices being followed enhances the firm value. Housing finance companies face unique corporate governance challenges due to myriad reasons like ownership structures, lack of transparency, and insufficient checks on inappropriate activities. Despite the 'corporate governance revolution', there exists no universal benchmark for the effective level of disclosure and transparency. Corporate governance practices followed in business firms are communicated through the corporate governance section of annual reports. clause 49 of the listing agreement sets a detailed corporate governance provision to be followed by listed companies in India. This study aimed at evaluating the governance practices in Housing Finance Companies against disclosure requirements of clause 49. Housing Finance companies that are listed in the NSE are taken into consideration as the sample for the study. Kendall's coefficient of concordance is used for determining the degree of association among several (k) sets of ranking of N objects or individuals.

Introduction

Corporate governance today, has become a subject of keen importance and attention in government policy circles, academia, and media throughout the world. Various reasons explain the current prominence of what many persons might otherwise consider an esoteric and technical topic. The financial scandals of recent times to name a few such as Enron, WorldCom, and the resulting loss of confidence by the investors in the stock market have impacted a dramatic decline in share prices and which led to substantial financial losses to millions of individual investors. The cause for such scandals and loss was due to the failed corporate governance.

In the words of Cadbury (1992) corporate governance is defined as the system by which companies are directed and controlled. According to Hampbel (1998) Corporate governance is the way in which the businesses of the corporate are handled by their corporate boards and officers. It was also observed that good governance confirms that constituents (stakeholders) with a relevant interest in the company's business are fully considered. Operational, financial and all material disclosures depict the health of an organization.

In order to achieve the objectives and there by effectively discharge their responsibilities, corporations must possess qualitative and effective leadership who should be responsive, transparent, and accountable and needs to have all the required intelligence in order to acquire & apply knowledge and

knowhow for the production and creation of wealth. Good corporate governance is considered to be the lifeblood of a prosperous society.

Globalization has broadened the operating business area of companies which in turn has been massively impacting investment. Likewise, investors are very particular on knowing whether the companies they intend to invest into is following a standard corporate management and a good reporting standard. The investor is also concerned with the correct implementation and monitoring mechanism companies are following in order to provide them their excepted returns. Likewise, transmission of relevant information on the actual events to the involved stakeholders is very important in order to avoid information irregularity. The collapse of than unique organizations globally like Enron(US), Maxwell Communications (UK), Vivendi (France) and as well as local cases like Satyam Computer services ltd., Café Coffee Day, Jet Airways and Yes Bank has proven the importance of the high quality of information in the company among stakeholders. Disclosure of information is a fundamental principle in the system of good governance in the company, namely transparency. With a good corporate governance, it is expected that disclosure of relevant information will increase and will decrease the information asymmetry, especially among agent and principal.

The annual report is one of the mediums of disclosure mechanism wherein the material matters are communicated to various users such as stakeholders (existing and prospective), creditors, suppliers, authorities, and public. One such part of the Annual report is the corporate governance report. A section on the corporate governance report is intended to include governance-related disclosures of an organization. The sequence and matters that are disclosed are based on clause 49 of the listing agreement of stock exchanges. Clause 49 of the listing agreement provides a framework for governance aspects. The provisions that are included in this clause have been broadly classified into two heads as a). Mandatory provisions and b). Non-mandatory provisions. All companies that are already listed and companies which are aspiring to get listed in stock exchanges are required to follow the listing requirements regularly. It is obligatory on part of companies to follow clause 49 provisions and to file the reports to exchanges on time. Recognizing the need for good corporate practices Securities Exchange Commission (SEC) introduced Sarbanes Oxley Act in United States. Following the path, Securities and Exchange Board of India (SEBI) introduced clause 49 to the listing agreement to enhance transparency and integrity to financial statements. Prof. Rajyalakshmi (2014), Corporate disclosure is a process through which a corporate entity communicates business and financial information to their stakeholders.

Statement of The Problem.

Corporate scams or scandals past and in near times, was largely due to the lack of good corporate governance practice. These lapses were typically due to misusing or misdirecting funds, overstating of revenues, understating of expenses, overstating the value of corporate assets or underreporting the existence of liabilities, sometimes with the support of officials in other corporations or affiliates. India is no different though there exist legal and regulatory measures to have proper governance mechanisms in place. Security Exchange Board of India (SEBI) has laid down several provisions through listing

agreements that lead to a fair and transparent governance structure among organizations. Compliance with these provisions will be communicated to all shareholders, stock exchanges and, other stakeholders through disclosure. Annual reports, corporate governance reports and, other official releases by the companies are the prominent media of communication.

Why housing finance companies?

India is considered as one of the fastest growing economies of the world. After overtaking the United Kingdom and France, India has become world's fifth largest economy in 2019 in terms of nominal GDP. Housing is the fourth largest contributor to Indian GDP and the sector has the potential to become the engine of domestic growth for the Indian economy in the coming years. The home loan-to-GDP ratio in India is expected to grow significantly over the next few years as India has a low mortgage-to-GDP ratio at 9%, when compared to other developing countries. Non- Banking Financial Companies (NBFCs) and Housing Finance Companies (HFCs) have taken advantage of this potential and have been the biggest drivers of housing finance growth. The development of housing sector can have direct impact on employment generation, GDP growth and consumption pattern in the economy. The current estimated market size of the Real Estate industry is 12 lakh crores (USD 180 bn) for FY2020. By 2030, the Indian real estate industry is expected to touch 65 lakh crores (USD1 trillion), becoming the third largest globally. The residential segment in India contributes 80% of the entire real estate sector.

The housing finance market in India is a highly competitive segment in overall credit industry. The government, both at centre and states, is a facilitator and is assisted by two regulating authorities, Reserve Bank of India (RBI) and National Housing Bank (NHB). The Housing Finance sector has undergone a major transformation post DHFL and IL&FS crisis in 2018, followed by subsequent liquidity issues around the HFCs & NBFCs leading to a sharp deceleration in the growth of credit extended by HFCs. The major reason of defaults of these companies are lack of effective disclosure of information in their annual reports and lack of transparency and intentional frauds. As of January 2020, there were 100 HFCs, of which only 18 were deposit taking entities. From the Indian context point of view, it was noted that very few studies were carried out on the housing finance sector, probably this could be because formal housing financing system had only emerged very late in India. Majority of the studies carried out in the housing finance sector was largely focusing on the operational efficiency analysis. This study is an attempt to explore corporate governance practices in Housing Finance Companies as disclosed in Corporate Governance reports, clause 49 being taken as the benchmark.

The present standards of Corporate Governance Disclosures

First, shareholders need to have access to information about important matters to make decisions that are in their interests. Second, information disclosure is crucial in preventing managers and dominant shareholders from engaging in activities that are illegal or are detrimental to minority shareholders. Managers and dominant shareholders will be more reluctant to undertake such activities when they

expect that shareholders will find out about them and may act against them. (M. Subramanyam1, October 2014)

Clause 49 of the Listing Agreement

The term ‘Clause 49’ refers to clause number 49 of the Listing Agreement between a company and the Stock Exchanges on which it is listed. Listing agreement helps in free transferability, leads to transparency in disclosure of information, and ensures that official quotation is available. The Listing Agreement is identical for all Indian Stock Exchanges, including the NSE and BSE. The revised Clause 49 has suitably pushed forward the original intent of protecting the interests of investors through enhanced governance practices and disclosures. In this connection, Chakrabarti (2008) very aptly commented, “Similar in spirit and scope to the Sarbanes-Oxley measures in the USA, Clause 49 has been a milestone in the evolution of Corporate Governance practices in India.”

Literature Review

In the words of noted Economist and Noble Laureate Milton Friedman, “Corporate Governance refers to conduct of the business in harmony with owners or shareholders desires, while imitating to the basic rules of the society embodied in law and local customs” Economic Times, (2001).

Corporate disclosure to stakeholders is the principal means by which companies can become transparent, Solomon and Solomon (2004). Investors get attracted by the relevant and reliable disclosure of the company's performance, Diamond and Verrecchia, (1991) and Kim and Verrecchia, (1994). Regulated disclosure provides new and relevant information for investors. which ultimately reflects the transparent system of the organization, Kothari, (2001) and Bushman and Smith, (2003). Karim (1996) argued that disclosures made by companies in their annual report should be considered as the most important source of information about a company. Holder-Webb et al. (2009) found a high degree of variability in the presentation of and reporting format choices.

Sarkar and Sarkar (2012) has made an analysis for 500 large listed companies for the period from 2003-2008, they used four important corporate governance mechanisms for calculating corporate governance index. through this index they found that companies with better corporate governance disclosures and structures earn substantially and higher rates of returns in the market.

Prof. Rajyalakshmi, (2014) made a comparative analysis on corporate governance disclosures between two industries (manufacturing and software) and drew a conclusion that even tough disclosures are made mandatory but there is a large variation in disclosure of corporate governance practices by different companies. She also emphasized that the value of the firm enhances only by following good governance practices.

A study undertaken by Subramanian, (2006), had identified the differences in disclosure pattern of financial information and governance attributes. A sample of 90 companies from BSE 100 index, NSE Nifty had been taken. The data was collected from the annual reports of the companies for the financial year 2003-04 and with respect to disclosure a score had been developed. The study followed the

Standard & Poor's "Transparency and Disclosure Survey Questionnaire" while collecting the data. The study finally concluded that "There were no differences in disclosure pattern of public/private sector companies with reference to their financial transparency and information were concerned."

Similarly, K.C. Gupta (2006) identified the differences in Corporate Governance practices of few local companies of an automobile industry. The data with respect to governance practices had been collected from the annual report of the companies for the year 2004-05. The study "did not observe any significant deviations of actual governance practices from Clause 49."

Brown &Caylor, (2004) stated that the most significant motivating force among the key variables of the Corporate Governance Quotient (CGQ) was board composition. Poor Corporate Governance practices by companies are prone to recession and as Corporate Governance deteriorate, the risk of dropping into financial difficulties continues to rise, Lee &Yeh, (2004). Gruszczynski, (2006) empirically evidenced that Corporate Governance of the polish companies do not have significant association with their financial performance. Ranti, (2011) emphasized that Corporate Governance disclosure practices are positively correlated with the Nigerian bank's performance. According to Aggarwal, (2013) Corporate Governance rating has a beneficial impact on the emerging Indian context through regression and correlation. Corporate Governance variables such as board size and non-executive members proportion positively associated with firm's performance, Lekaram, (2014).

Jayati Sarkar, Subrata Sarkar, (2010) have constructed a Corporate Governance Index for 500 large, listed firms in the Indian corporate sector for the period 2003 to 2008. The empirical analysis shows that good governance practices are rewarded by the market which provides an added incentive to companies to carry out governance reforms.

Arijit Sen, (2011) had determined the extent to which Indian listed companies disclose their corporate governance. He concluded that there is a substantial scope for improvement in the corporate governance disclosure practices and the size of the company is a significant determinant of disclosures.

Mehul Raithatha and Varadraj Bapat (2012), have developed a model to calculate the Corporate Governance Score of companies and then it is related to company attributes like size, profitability, leverage, foreign ownership etc.

Mita and Arti, (2012) have focused on the difference between governance regulations and implementation practices, and it was found that regulations have been followed to an extent which is mandatory and cannot be escaped. The study tried to highlight the areas of non- implementation.

Md. Shamimul Hasan et.al, (2013) investigated the influence of corporate governance on financial reporting disclosures. Their results show that corporate governance is significantly associated with the extent of financial reporting disclosures. External auditor, multi listing and profitability are significantly (5% level) associated with overall financial reporting disclosures index.

Over the thorough review of literature, it was understood that the concept of Corporate Governance is at the stage where there is every possible scope for development and improvement. This was the added motivation to further investigate the concept and to study corporate governance practices in Housing Finance Companies from the Indian context for a period of five years from 2015-16 to 2019-20.

Objectives of the Study

The basic objectives for carrying out this study are as follows:

1. To study the existing corporate governance disclosure practices followed by Housing Finance Companies.

2. To Develop a Corporate Governance Disclosure Score.

Methodology Of The Study

Major five Housing finance companies listed in the national stock exchange under the equity segment with active status as of January 2020 was taken as a basis for the study. The study period was from 2015-16 to 2019-20.

Sample Selection: Non-probability (purposive) sampling procedure was followed. All the selected housing finance companies are listed in NSE. The criteria used for selection are deposit-taking companies.

The list of selected housing finance companies

1). CAN FIN HOMES

2). HDFC

3). REPCO

4). LICHFL

5). GIC HOUSING FINANCE COMPANY

Secondary data: The corporate governance sections were extracted from the annual reports of the respective housing finance company's website. The contents of the annual reports were analysed using the content analysis technique, a research tool used widely in social sciences, which objectively and quantitatively examines written or oral communication to make inferences about values, meanings, or understandings. An unweighted approach is employed for the study. According to the unweighted disclosure approach, a firm is scored 1 for disclosing an item in the annual report and 0 if it is not disclosed, Dr. S. Gayatri, (2015), The net score of a company was found by adding all the individual scores of various sub-dimensions. The maximum score a housing finance companies can obtaine would be 35 in case all the items are disclosed.

A corporate governance disclosure index (CGDI) was computed using the following formula which was used by Bhuiyan and Biswasiv (2007), Dr.laila (2014).

CGDI=Total Score of the Individual Company/ Maximum Possible Score*100

The CGDI disclosure index includes the core principles of sound corporate governance under the following headings amounting to a total score of 35. (Refer table no 4)

1.Disclosure of company's philosophy on corporate governance

2.Disclosure of board of directors

3.Disclosure of code of conduct

4.Disclosure of audit committee

5.Special disclosures

6.Management disclosures and analysis

7.Disclosures CFO/CEO certificates

8.Compliance of Corporate Governance and auditors reports

9.Disclosures of other committees

10. Disclosure of means of communication

11.Non- Mandatory Disclosures

The value of CGDI ranges between 0 and 100. Maximum score reflects best disclosure practices, and minimum score reflects weak practices. CGDI indicates the disclosure/presence of an item in the annual report.

Statistical tools

Kendall's coefficient of concordance is used for determining the degree of association among several (k) sets of ranking of N objects or individuals. When there is perfect agreement, w =1. When maximum disagreement exists, w = 0. The ranks of the five HFCs over the period five years was taken and tested for concordance.

Results, Interpretation And Discussion

Table-1 CGDI score for five years

SNO	Name of the HFC	CGDI score for five years	CGDI score percentage for five years	Ranks
1	CAN FIN HOMES	135	77.142	3
2	LICHFL	170	97.1	1
3	HDFC HOME	165	94.28	2
4	REPCO Home Finance	125	71.42	5
5	GIC Housing Finance	130	74.2	4

Source: computed from annual reports of selected HFCS

LICHFL is ranked first among 5 HFCs with a five years CGDI score of 97.14%. Followed by HDFC which is ranked 2 with average score of 94.28%, CAN FIN homes which is subsidiary of Canara bank is ranked number 3 with its average score of 77.142% for five years. GIC housing finance Ltd which was incorporated as GIC Grih Vitta Ltd stood with a rank of number 4 with average score 74.2%. lastly REPCO home finance was ranked at 5 with average score of 71.42%.

Table 2- Kendall's coefficient for ranking for five years

Year	Canara Fin	REPCO Home Finance	HDFC HOME	LICHFL	GIC Housing Finance	
Ranks in 15-16	3	4	2	1	4	
Ranks in 16-17	3	4	2	1	4	
Ranks in 17-18	3	4	2	1	4	
Ranks in 18-19	3	4	2	1	4	
Ranks in 19-20	3	4	2	1	4	
sum of ranks	15	20	10	5	20	14
S=(R-Rbar)^2	225	400	100	25	400	1150

Source –computed from secondary data'.

Null Hypothesis: There is no significant agreement in ranking of the sample HFCs over the five years.

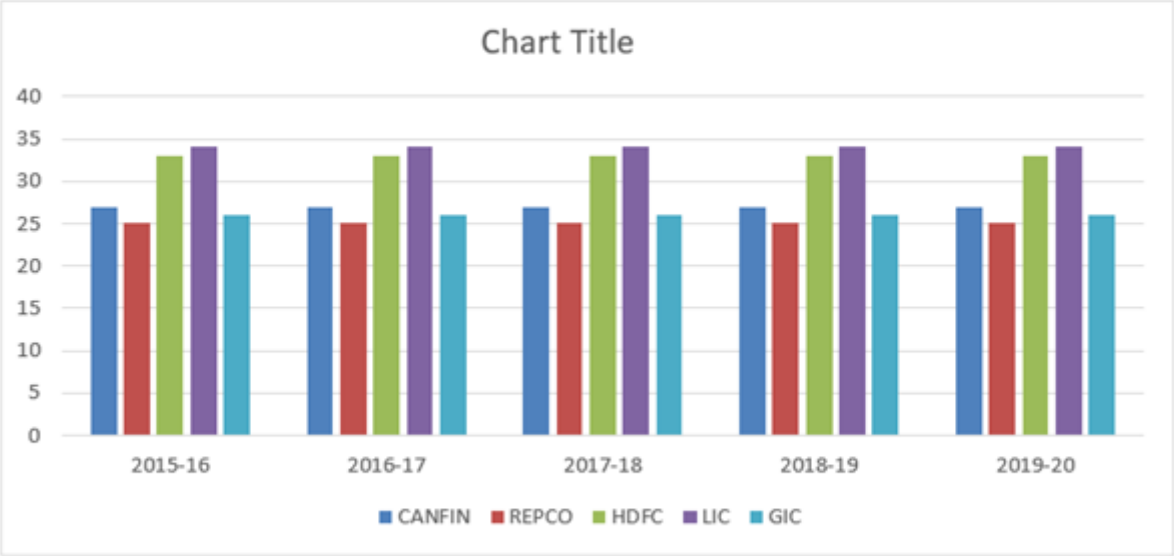
Alternate Hypothesis: There is significant agreement in ranking of the sample HFCs over the five years.

Kendall's coefficient w=12s/(m^2(n^3-n)-mT

(Here n denotes number of housing finance companies and m denotes number of years and s denotes sum of squared deviations S=∑(Ri-Rbar)2 with w value 0.68. chi-square =13.6,DF=4(n-1),P value=0.009.)

Since p value 0.009 which is less than 5% level of significance, the null hypothesis was rejected, and alternate hypothesis is accepted. There is a significant agreement in the ranking over the five years as the five set of ranking are independent. The lowest value observed among the sum of ranks is 5 which corresponds to LICHFL hence the best estimate of true ranking in this case is LICHFL.

Table no 3 CGI SCORE



(*Computed by the authors*)

From the table-3, we can clearly analyse that LICHFL is disclosing all the information of corporate governance standards according to clause 49 of listing agreement consistently all the 5 years and stood top and REPCO HOME Finance stood the last with least score in disclosing the information. The audit committee and composition of board of directors and means of communication is seen as a key fulcrum for any company. Companies which are ranked from 1 to 5 have 100% disclosed information with reference to the three corporate governance parameters. It was noted that the Information on participation of head of finance chief internal auditor in the meetings is not furnished by 90 % of the companies. only LICHFL housing finance company has furnished this detail for all the five years. Audit committees are the bodies which are really independent, transparent, competent and have authorities to get the required performance, any non-compliance in audit committee could lead to severe consequences in governance. A score above 90 is desirable and anything below it signifies its ineffectiveness. Through this study it was observed that the disclosures on audit committee of the different HFCs have been showing improvement during the five years period.

Conclusion

With the introduction of clause 49 of listing agreement it was observed that the housing finance companies have been disclosing cooperate governance in more systematic manner. From this study it is noted that corporate governance and disclosure practices followed by the Major five Housing finance companies listed in the national stock exchange under the equity segment and very interesting to note from among the five major housing companies LICHFL is ranked first among five HFCs with a five years CGDI score of 97.14%. while REPCO home finance ranked five with average score of 71.42%. The analysis also reveals that there lies a significant agreement in the ranking over the five years as the five set of ranking were independent. Another important observation from this study was apart from HDFC housing finance company the other major housing financing companies did not furnish information on the participation of their chief internal auditor and details of the meeting is not furnished.

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- Annexure.docx