

Corporate Governance Practices in Indian Public Sector Banks: Evidence from the State Bank of India

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ABSTRACT

Governance refers to the rules, controls, policies, and resolutions to command corporate behavior. Corporate Governance stabilizes the interests of a company's many stakeholders, such as shareholders, senior management executives, customers, suppliers, financiers, the Government, and the community. Corporate governance in the banking sector refers to the stratagem by which managers are selected, inspired, and held responsible. Good corporate governance principles aim to achieve vigorous and transparent risk management, promote public confidence, and uphold the safety and soundness of the banks. In the light of the above, the paper is a modest attempt to evaluate the corporate governance practices of the State Bank of India. It assesses the corporate governance procedures implemented by the State Bank of India (SBI), showing a compliance rate of 79.06%. Prominent difficulties are identified in categories like Board Effectiveness (BE), Audit Function (AF), Risk Management (RM), and Remuneration (R). It's crucial to tackle these shortcomings to build trust and uphold regulatory standards in the banking domain. Future studies could delve into key factors influencing these challenges and devise novel approaches to address them, possibly by examining multiple banks simultaneously. Furthermore, conducting comparative studies across different sectors or global standards could provide useful strategies for strengthening corporate governance in banking.

Keywords: Corporate Governance, Public Sector Bank, SBI, Disclosure, Compliance

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1. INTRODUCTION

In the contemporary business world, which is becoming more interconnected globally, adherence to universal principles is imperative for companies striving to maintain competitiveness. Corporate governance, which ensures efficient decision-making and execution processes, has garnered substantial attention worldwide. This is particularly critical due to its dynamic nature, constantly evolving alongside market dynamics and regulatory frameworks (Gandhi & Raju, 2010; Seenivasan, 2014; Naushad & Malik, 2015). The agency delicate, stemming from the divergence of possession and management in large corporations, poses a central challenge that corporate governance aims to tackle.

Historical instances and early organizational structures attest to the longstanding recognition of governance's importance in directing and overseeing corporate operations.

Important events such as the Watergate scandal and the 2007-08 financial crisis underscored the necessity of regulating the corporate sector, leading to the formulation of various committees and recommendations internationally. In India, committees and reforms, including those by the Confederation of Indian Industries (CII), Securities and Exchange Board of India (SEBI), and Department of Corporate Affairs (DCA), have significantly shaped corporate governance practices (Dave & Pratapsinh, 2012; Shukla, 2009; Ministry of Finance and Company Affairs, 2002; SEBI, 2002; Government of India, 2013). Reports like the Kumar Mangalam Birla Committee and initiatives by Naresh Chandra and Narayana Murthy have influenced governance standards and revisions to the Companies Act.

Additionally, legislative changes such as the Companies Act 2013 have introduced provisions to enhance governance standards and safeguard minority shareholders' interests. In the banking sector, corporate governance is crucial in ensuring accountability, credibility, and transparency to protect stakeholders' interests and maintain economic stability (Khan, 2017; Kumar & Pavithra, 2017; Davis & Mathew, 2018; Padhi et al., 2017). The banking industry in India has witnessed continuous reforms, particularly post-independence, and following recommendations from committees like the Narshimham committee. These reforms, coupled with economic liberalization, have intensified competition, compelling banks to strengthen governance mechanisms to instil stakeholders' trust and prevent corporate failures.

2. REVIEW OF LITERATURE

Corporate governance practices are shaped by the environment in which banks and their managers operate, aiming to ensure healthy and clear risk management and administrative processes. Strong corporate governance is crucial for banking institutions as they bear the responsibility of maintaining public trust and safeguarding depositors' interests. Moreover, effective governance fosters public dignity and contributes to the stability and health of the banking system. Considering this backdrop, numerous studies have already explored various facets of corporate governance practices, with reviews conducted from both applied and methodological perspectives.

2.1. Review Related to Corporate Governance of Banks

Arun and Turner (2004) emphasized the distinct nature of banking institutions and argued for stronger corporate governance mechanisms, highlighting challenges in implementation due to factors like government ownership, distributional cartels, and restrictions on foreign bank entry. The study suggested that banking reforms should be accompanied by robust prudential regulatory systems, with privatization seen as integral, and corporate governance reforms considered essential for successful government divestiture. Additionally, the entry of foreign banks was viewed as beneficial for improving corporate governance practices. Adelegan (2005) examined the relationship between internal and external governance

mechanisms in Nigerian banking companies, utilizing secondary data from annual reports. The findings revealed a higher segment of non-executive directors and a tendency to separate the roles of chairman and CEO compared to other Nigerian quoted companies. They also noted the presence of audit committees with a significant proportion of non-executive directors in Nigerian banks. Som (2006) analyzed the corporate governance code in India, observing efforts to align it with international best practices while acknowledging challenges rooted in Indian cultural values. They identified widespread issues such as ownership concentration, lack of protection for minority shareholders, and non-compliance with disclosure norms hindering progress in corporate governance principles. Marcinkowska (2012) critically reviewed literature and regulations on corporate governance in banks, attributing weak and ineffective governance mechanisms as contributing factors to the financial crisis. They advocated for significant changes in areas such as board roles, risk management, management remuneration, and transparency. Deb (2013) investigated corporate governance practices in Indian banks, assessing adherence to attributes like transparency, accountability, disclosure, and share price movements. Their findings indicated a commitment to good corporate governance, with executives driving the mission forward, while emphasizing the importance of ethical responsibility beyond legal compliance. Ranju and Vineeth (2018) examined women's participation on Indian bank board's using a sample from the NIFTY Bank Index. They found that gender balance, particularly with women directors, often met only the minimum statutory requirement, with private banks leading in gender diversity. They recommended increased representation of women on boards beyond statutory measures. Sanchez et al. (2020) empirically analyzed how the global financial crisis of 2007-08 prompted changes in the corporate governance mechanisms of banks and improvements in efficiency, comparing the shareholder and stakeholder models. The study found that Anglo-American countries following the shareholder model maintained high governance effectiveness post-crisis, while Continental European banks adhering to the stakeholder model enhanced governance effectiveness by modifying practices such as board structure, executive compensation, and execution of CSR committees, leading to a convergence of governance systems.

2.2. Methodological Review

Hossain's study in 2008 investigated the compliance and disclosure practices regarding corporate governance among Indian banking companies. Analyzing mandatory disclosures recommended by SEBI for 38 banks listed on the Bombay Stock Exchange and the National Stock Exchange, the study recognized 46 mandatory disclosure items. It has also found that attributes such as size, ownership, board composition, and profitability significantly influenced the extent of corporate governance disclosure. Meanwhile, Kumar and Upadhaya's research in 2011 aimed to create a Corporate Governance Index (CGI) for assessing compliance in Nepalese commercial banks. They devised a methodology involving 110 questions distributed across categories such as board responsibility, structure, shareholder rights, transparency, and disclosures, with binary scoring. The resulting CGI

was a composite index derived by summing weighted values from each category. Tuteja and Nagpal (2013) sought to devise a corporate governance index tailored specifically for Indian banks. Their study synthesized existing literature to identify critical evaluation factors, culminating in the formulation of the Corporate Governance Index. This index incorporated benchmarks from Clause 49 of the Listing Agreement of the Indian Stock Exchanges, covering key aspects such as the board of directors, audit committee, remuneration committee, nomination committee, risk management, related party transactions, and disclosures, with further breakdowns into sub-elements. In a similar vein, Halder and Rao's study in 2013 crafted a corporate governance index for large listed Indian firms spanning 2008 to 2011. Utilizing six key governance mechanisms and encompassing 44 factors affecting governance, they developed sub-indices for each mechanism. The averaging of these sub-indices yielded an overall Corporate Governance Index, revealing an upward trend in governance levels among Indian companies. Additionally, their findings highlighted the positive impact of governance and promoter holdings on financial performance, while leverage was found to have a negative influence.

2.3. Research Gap

The literature review emphasizes the dynamic nature of corporate governance, especially in the banking sector, where research studies encompassing a wide range of governance variables is scarce. Most existing studies stem from foreign settings, leaving a significant gap in understanding the efficacy of governance frameworks designed specifically for banks. With regulatory changes moving towards global standards, there is an opportunity to explore the corporate governance practices specific to Indian banks. Hence, this research aims to fill these gaps by identifying and analyzing the corporate governance factors present within the Indian banking sector.

3. Objective of the study

The objective of the paper is to estimate the implementation of corporate governance practices in the State Bank of India.

4. Research Methodology

4.1. Population and sample

The research focuses on corporate governance within the Indian banking sector, with a special reference to State Bank of India (SBI) which is one of the listed public sector banks with the highest market capitalization as of March 2024. Secondary data from various reliable sources such as government websites, RBI data, banks' websites, and annual reports will be analyzed to investigate the corporate governance practices of the bank. The findings aim to provide insights into the governance frameworks of SBI in particular and contribute to understanding corporate governance in the Indian banking industry in general.

4.2. Period of the Study

The present study embraces 7 financial years from 2015-16 to 2020-21. The aforesaid period has been chosen by looking at mainly two important regulatory guidelines as envisaged at-

1. The Companies Act, 2013 and
2. The Securities and Exchange Board of India (Listing Obligations and Disclosure Requirements) Regulations, 2015.

4.3. Variables Considered

Corporate governance includes internal and external dimensions. For this research study, only internal corporate governance dimensions/mechanisms have been considered based on literature review and committee recommendations. Internal parameters have been considered because of the fact that corporate governance is the scheme of guidelines, practices, and procedures by which a banking organisation is focused and measured. The creation and implementation of these practices involves balancing the interests of bank stakeholders. The variables (corporate governance dimensions) considered for this study are Board Effectiveness (BE), Audit Function (AF), Risk Management (RM), Remuneration (R), Shareholder Rights and Information (SRI), and Disclosure and Transparency (DT). In addition to incorporating various sub-variables, norms, and indicators derived from previous research, a corporate governance index is developed.

4.4. Measuring Technique

The qualitative traits can be measured based on the existence and non-existence of the concerned traits. Nonetheless, academic researchers have put substantial effort towards the development of models to measure governance quality. The representative model takes the form of a Corporate Governance Index that aggregates several input variables to a single metric. To construct an index, researchers selected governance features (in the form of variables and sub-variables) that are deemed to be important. These variables are quantified while using a Dichotomous Approach (Generally through the assignment of two numerical values i.e. 0 or 1) and compiled into a Single Unweighted Index that is said to replicate complete governance quality. A bank's corporate governance score can be keenly compared against those of others to measure its comparative usefulness.

Corporate Governance Index (CGI) will be developed after thoroughly studying the different Acts and Laws prevailing in India which is applicable to the Indian banking sector especially the Companies Act 2013 and the Securities and Exchange Board of India (Listing Obligations and Disclosure Requirements) Regulations, 2015 of the SEBI Act, 1992, Recommendations from different national and international committees, Reports of Corporate governance rating agencies and other literature on corporate governance index. The construction of CGI will carry the key variables and subsequently the sub-variables.

The formula to be used to calculate the CGI:

$$CGI = \frac{\text{Actual Score}}{\text{Expected Score}} \times 100$$

5. ANALYSIS AND INTERPRETATION

This section begins with descriptive statistics of the collected data. Descriptive statistics refer to the summarization of data and the representation of raw data employed in analysis. These statistical measurements, according to Stock and Watson (2008), help to understand the average, range, standard deviation, dispersion or variation, and other properties in data collection. To comprehend each data set in this study, the analysis of mean, standard deviation, minimum, and maximum are used. For this purpose, aforesaid corporate governance variables have been considered. The descriptive statistical analysis of corporate governance variables is presented in table 1.

Table 1: Descriptive Statistics of Corporate Governance Variables

Variables	Obs	Mean	Std. Dev.	Min	Max
BE	84	74.40	7.70	55.00	90
AF	84	80.03	11.41	55.56	100
RM	84	78.57	17.23	40.00	100
R	84	77.86	27.77	20.00	100
SRI	84	97.52	4.25	83.33	100
DT	84	91.67	9.46	71.43	100

Source: Self-calculated by the present researchers

The analysis shows that the Board Effectiveness (BE) has a mean of 74.4 (SD = 7.7), Audit Function (AF) 80.03 (SD = 11.41), Risk Management (RM) 78.57 (SD = 17.23), and Remuneration (R) 77.86 (SD = 27.77). Shareholder Rights and Information (SRI) scores highest at 97.52 (SD = 4.25), and Disclosure and Transparency (DT) at 91.67 (SD = 9.46). The descriptive statistical analysis of corporate governance variables reveals that the State Bank of India generally has higher mean scores and lower variability, indicating a consistent governance practice.

Having analyzed the descriptive statistics of the corporate governance variables, the study proceeded with the analysis of the corporate governance of the selected bank on selected parameters. In this connection, the compliance level of each of the parameters based on the Actual Corporate Governance Score (ACGS) and also the Expected Corporate Governance Score (ECGS) have been analyzed for the State Bank of India.

The analysis and interpretation provide a detailed examination of the data collected, uncovering patterns, and their implications. Through careful analysis of the data, we aim to reveal key findings and their significance. The interpretation phase goes beyond the data to offer explanations and insights, contextualizing the results within existing literature and theoretical frameworks. This section presents an assessment of the corporate governance practices of selected banks considered for the study based on the abovementioned selected variables. Table 2 details the Corporate Governance analysis of the State Bank of India.

Table 2: Corporate Governance Practices of State Bank of India

Sl No.	Variables/ Years	2015-16	2016-17	2017-18	2018-19	2019-20	2020-21	2021-22	ACGS	ECGS	%
1	BE (20)	12	13	14	16	15	15	14	99	140	70.71
2	AF (9)	7	7	7	8	7	8	8	52	63	82.54
3	RM (5)	3	4	4	5	5	5	5	31	35	88.57
4	R (5)	2	3	2	2	3	3	3	18	35	51.43
5	SRI (12)	12	12	12	12	12	12	12	84	84	100.00
6	DT (7)	6	5	5	6	5	5	5	37	49	75.51
	ACGS:	42	44	44	49	47	48	47	321	406	79.00
	ECGS	58	58	58	58	58	58	58			
	%	72.41	75.86	75.86	84.48	81.03	82.76	81.03			

Note: (BE) is for Board Effectiveness, (AF) is for Audit Function, (RM) is for Risk Management, (R) is for Remuneration, (SRI) is for Shareholder Rights and Information and (DT) is for Disclosure and Transparency, (ACGS) is for Actual Corporate Governance Score and (ECGS) is for Expected Corporate Governance Score.

Source: *Self-calculated by the researchers*

The above table offers a comprehensive analysis of the State Bank of India's Corporate Governance disclosures from the fiscal year 2015-16 to 2021-22, showcasing scores and compliance percentages for each year. Over this period, the bank demonstrated varying levels of compliance, culminating in an overall compliance level of 79.06%. A deeper examination through content analysis of cumulative Corporate Governance disclosures from 2015-16 to 2021-22 reveals areas of concern where the bank appears to fall short. Notably, in dimensions such as Board Effectiveness (BE), Audit Function (AF), Risk Management (RM), Remuneration (R), and Disclosure & Transparency (DT), there are noticeable gaps in compliance. Specifically, in Board Effectiveness (BE), the bank achieved a compliance rate of 70.71%, indicating opportunities for enhancing governance practices related to board functions. Similarly, in Audit Function (AF), the bank met only 82.54% of

the criteria, highlighting room for improvement in audit-related processes. Furthermore, while the bank demonstrated relatively better performance in Risk Management (RM) with an 88.57% compliance rate, there are still areas for refinement. Similarly, compliance rates for Remuneration (R) and Disclosure & Transparency (DT) stood at 51.43% and 75.52% respectively, indicating areas where the bank can strengthen its practices. These findings underline the importance for the State Bank of India to focus on improving corporate governance practices in dimensions like Board Effectiveness (BE), Audit Function (AF), Risk Management (RM), Remuneration (R), and Disclosure & Transparency (DT) which will enhance transparency, accountability, and advance overall governance within the organization, developing trust and confidence among stakeholders.

6. COMPLIANCE LEVEL AND IMPLICATIONS

The analysis of results from the selected public sector bank i.e. State Bank of India (SBI) demonstrates very good performance in corporate governance practices, upholding findings from notable studies by Shukla (2009) and Das (2013). These studies categorize corporate governance scores into five ranges: Below 41, 41-55, 56-70, 71-85, and 86-100, representing Poor, Average, Good, Very Good, and Excellent respectively. This consistency highlights the strength of our findings and confirms that the bank exhibits a relatively high level of commitment to effective corporate governance practices, placing it significantly within the spectrum of governance performance. While the bank exhibits strengths in certain areas, such as risk management and shareholder rights, there are consistent challenges in dimensions like Board Effectiveness (BE), Audit Function (AF), and especially Remuneration (R). Addressing these deficiencies is crucial for enhancing trust, stability, and regulatory compliance within the banking sector, ensuring sustained growth and resilience across the industry.

7. DIRECTION FOR FUTURE RESEARCH

The present study represents an initial exploration into the corporate governance practices of State Bank of India (SBI), focusing on six specific variables. However, Future studies could delve into key factors influencing these challenges and devise novel approaches to address them, possibly by examining multiple banks simultaneously. Furthermore, conducting comparative studies across different sectors or global standards could provide useful strategies for strengthening corporate governance in banking.

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