

Role of Institutional Investors in the Corporate Governance of their Portfolio Companies

On 17 December 2005, a Round Table conference on 'Role of Institutional Investors in the Corporate Governance of their Portfolio Companies' was organised by the National Foundation for Corporate Governance with Confederation of Indian Industry (CII) and the World Bank

The Chief Guest, Mr. Prem Chand Gupta, Minister of State (Independent Charge) for Company Affairs announced that the Government of India is undertaking a major revision of the Companies Act which is at an advanced stage to improve the image of Corporate Governance in the country.

Mr. Gupta stated that this was one of the several initiatives taken by the Government for furthering and promoting good corporate governance. The setting up of the National Foundation for Corporate Governance in partnership with the CII and Institute of Chartered Accountants of India (ICAI), he said, was a reflection of this Government's commitment.

"We have recently introduced Amendment Bills for reforming laws governing professional institutes: The Institute of Chartered Accountants of India, The Institute of Company Secretaries of India and Institute of Cost and Works Accountants of India. We know the importance of the role, these professional institutions play in promoting good governance practices, he stated.

The Minister pointed out that the role of institutional investors was recognized as far back as the 1950 s. At that time the State Bank Of India, LIC and UTI were the major investors and mobilised substantial funds and provided them to the private sector.

But times have changed and today India has a large number of institutional investors both from within and outside the country, he said. For this the role of good Corporate Governance has been highlighted by the McKinsey and the World Bank report, which shows that the international investors do not mind paying premium to invest in companies with good governance. In Germany this premium was 13% while in Russia the premium was 38 %.

"We must remember that good governance cannot be brought by law alone. It has to be a collaborative approach involving the promoters and other direct and indirect stakeholders," he asserted.

Ms. Komal Anand, Secretary, Ministry of Company Affairs, in her keynote address said that institutional investors like the Mutual funds, insurance companies, and foreign investors had a substantial presence in India. In view of their increasing role, she said that there was need for a debate on the duties and obligations that these institutions should have with regard to Corporate

Governance, in terms of disclosure policies and management of their voting rights.

She said that statistics had shown that in India Banks held 52 % of all investments held by institutional investors and despite this 80% of their investment were in Government and other approved securities and commercial banks did not have much equity stake in companies.

“The Indian securities markets are fairly integrated with the global markets. They have undergone a transformation during the last decade resulting in significant improvements in their efficiency, transparency and safety. But they would be able to participate fully in this rally only if the investor was confident regarding participation in the financial markets”, she said.

Mr. Michael Carter, Country Director India, World Bank, in his address said that the 2004 Corporate Governance assessment conducted by the World Bank had benchmarked India’s Corporate Governance framework to the globally accepted OECD principles of Corporate Governance. This assessment, he said, had found that a series of legal and other reforms taken by India in the last few years, had transformed Indian Corporate Governance framework and proved responsibility and accountability. However, he mentioned that implementation and enforcement of these amendments remained major challenges for India.

Mr. Carter pointed out that based on the experience of countries where shareholders activism was significant such as countries like Australia, France, UK and USA, it was expected that Indian institutional investors could enhance the value of their portfolio by undertaking analysis and using their ownership rights more actively.

Mr. Rajnikant Patel, Managing Director and CEO, Bombay Stock Exchange Ltd said that the extent of institutional shareholding in the leading companies was growing and this was evident from a survey of the non-PSU companies which were listed on the Stock Exchange where their range of holding was between 28% and 72%.

Prof. Sanjai Bhagat, Baughn Distinguished Scholar, Professor of Finance, University of Colorado, said that in countries with strong stock markets it was mandatory that shareholders received information on large self- dealing transactions and the power to act on it was used both by voting and litigation.