

Rise of Shareholders Activism in India

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Abstract:

Shareholders' Activism is on rise in India. As per our earlier paper we have found limited literature on Shareholders activism in India. We tried finding out various issues raised globally by the activist shareholders in our second paper which are broadly categorised in Idle Cash related issues, Financial Performance and Valuation related issues, Executive/Senior Management related issues and Board of directors' related issues. We tried understanding where activism in India stands and mapped the issues raised by the activist in India. For this purpose, we chose resolutions which were rejected by the shareholder's in last three financials years (starting from FY2017 to FY2019). As per our study most of the cases falls under Board of directors' related issues followed by Executive/Senior Management related issues. Related party transaction (miscellaneous issues) is found to be the key issue in these cases. We found only one resolution rejected for Financial Performance and Valuation related issue. As India is going through regulatory transformation along with increased institutional stake in Indian corporates, we expect rejection to increase Multifood going forward. This again depends on how effectively regulations gets implemented and executed.

Keywords: Shareholder Activism, Corporate Governance, Issues in Shareholder's activism, Shareholders Proposal.

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Introduction

Shareholders Activism is using ownership position to influence the company's policy and practices (Sjöström, 2008 and Clifford, 2008). Generally the term is associated activism by institutional shareholders and / or minority shareholders who are not satisfied with company management (Gillan & Starks, 2000).

Corporate governance is based on four key elements Aguilera et al. (2015) – protection of shareholders interest, mediation between internal stakeholders (management and employees), transparency in disclosures and providing strategic and ethical guidance to the company. They have focused on external environment for corporate governance which is legal and regulatory framework, market for corporate control (such as Merger and Acquisitions), Auditors, Rating agencies, activist

investors and media. La Porta (1999) reiterated that legal and regulatory framework is one of the most important factors for harvesting shareholder activism and in protecting shareholders right. India is experiencing the transformation in its corporate governance framework by bringing changes in legal and regulatory framework such as introduction of the companies act, 2013. There are multiple new initiatives taken by Indian regulators such as e-voting facility, appointing minimum number of independent directors, separation of Chairman and Managing Director (MD) role etc. India has over 5000 listed companies of which shares of around 4,000 companies are traded actively on stock exchanges. There are over 4.8 crore registered investors in India. Also Finance ministry has proposed to increase the Minimum Public Shareholding (MPS) to 35% from current level of 25%. In 2019, India is ranked 13th in global ranking on Protecting Minority Shareholders parameter.

As per our detailed literature review on issues raised by activist shareholders globally, Idle Cash related issues, Financial Performance and Valuation related issues, Executive/Senior Management related issues and Board of directors' related issues are the broad categories of concerned issues. We also have pointed out gaps in Indian literature on shareholders activism and its impact on the performance of the company (Shingade & Rastogi 2019). We also have pointed out that legal and regulatory framework and ownership concentration are some of the key enablers for shareholders activism.

In current paper we are mapping the issues raised by institutional shareholders in India. We limited ourselves to shareholder resolutions which are rejected by these shareholders. We have used three year data from financial year 2017 to 2019.

Paper is divided in three sections. It starts with discussion on various issues followed by section on Indian activism scenario. We conclude the paper

with our observation and scope of future research in the area.

Issues raised by Activist Shareholders

Activist shareholders have predefined objectives of targeting particular set of companies; these broadly fall either under financially motivated activism or socially motivated activism (Judge, W. Q., Gaur, A., & Muller-Kahle, M. I., 2010). Our work focuses primarily on financially motivated activism. Globally, shareholder activism is dominated by hedge funds (Klein & Zur 2009, Becht 2008), pension funds (Klein & Zur 2009) and other institutional investors such as mutual fund and insurance companies.

Financially motivated activists typically target companies having deteriorated financial performance (Richardson 2006, Brav 2008, Fama & Jensen 1983). Financial performance is measured using various accounting and market based ratios. Firms having sound financial health but having corporate governance issues (CG) are also targeted (Carleton 1998, Daily 1997, Baliga 1996, Bebchuk 2010, Del Guercio 2008) by activist investors. We have identified number of issues (both financial as well as non-financials), as per our understanding these issues falls in one of the category given below.

In our earlier work (Shingade & Rastogi, 2020) we tried understanding the various issues raised by activist shareholders by going through existing literature. Typically these issues can be broadly classified as below,

- Board of directors related issues
- Executive / Senior Management related issues
- Financial Performance and Valuation related issues
- Idle Cash and Capital Structure related issues

- Miscellaneous issues (Other issues which are not part of any of the above category)

Table 1: List of Issues-

Sr. No.	Issues discussed in literature	Categories of Issues
1	Appointment of Board of directors	Board of directors related issues
2	Compensation of Board of directors	Board of directors related issues
3	Gender diversity in Board of directors	Board of directors related issues
4	Appointment of Executives / Senior Management	Executive / Senior Management related issues
5	Compensation of Executives / Senior Management	Executive / Senior Management related issues
6	CEO Duality	Executive / Senior Management related issues
7	Financial Performance of the company	Financial Performance and Valuation related issues
8	Strategy	Financial Performance and Valuation related issues
9	Growth	Financial Performance and Valuation related issues
10	Earning Management	Financial Performance and Valuation related issues
11	Dividend	Financial Performance and Valuation related issues
12	Liquidity	Financial Performance and Valuation related issues
13	Size of Firm	Financial Performance and Valuation related issues
14	Under Valuation	Financial Performance and Valuation related issues
15	Capital Structure of the company	Idle Cash and Capital Structure related issues
16	Capex plan	Idle Cash and Capital Structure related issues
17	Over-Investment	Idle Cash and Capital Structure related issues
18	Idle cash availability	Idle Cash and Capital Structure related issues
19	Ownership type	Miscellaneous issues
20	Auditor related issues	Miscellaneous issues
21	Poison Pill	Miscellaneous issues
22	Executive Behaviour	Miscellaneous issues
23	Policy	Miscellaneous issues
24	Regulation	Miscellaneous issues
25	Risk Taking ability of firm	Miscellaneous issues

Shareholders Activism in India

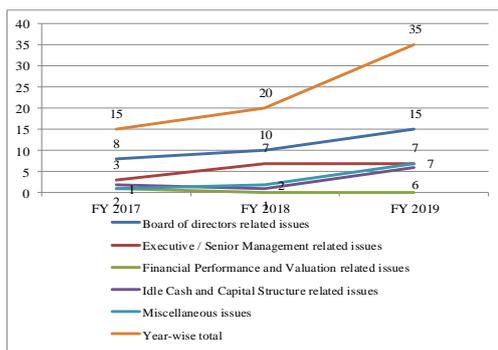
Promoters shareholding¹ in listed companies stood at 54.56% as of June 30 2019 compared to 61.34% as of June 30 2009. Over the period promoters holding in listed companies have declined by 6.78%. One reason for the said decline could be requirement of minimum 25% public shareholding for Indian listed companies. The trend is expected to continue as finance minister has proposed minimum public shareholding at 35% in budget 2019. Generally increase in institutional shareholding lead to activism.

Data and Observations

We would like to understand the extent of shareholder activism in India. For that we have gone through the shareholders proposal in India for listed companies for the period FY2017 to FY2019. We limited ourselves to proposals which are rejected by the shareholders. There are around 70 proposals in India which were rejected by the shareholders and numbers of rejected proposals are increasing over the years. As discussed earlier, we have mapped these issues with the categories we gave created.

¹ Source: Quarterly Shareholding Tracker June 2019_Detailed Report by Prime Database

Chart 1: Summary of Indian proposal mapping



Over the years the shareholders proposals rejected by shareholders are increasing. In FY2017, shareholders rejected 15 proposals; in FY2018 they rejected 20 proposals while in FY2019 total numbers of rejected proposals were 35. These proposals are spread across 40 companies. We understand that activism is not limited to any particular industry, these proposals are spread across 29 industries (industry classification as per BSE).

Table 2: Detailed mapping of proposals rejected by Indian Shareholders with categories of Issues

List of Issues	Date of Meeting	Board of directors related issues			Executive / Senior Management related issues			Financial Performance and Valuation related issues							Idle Cash and Capital Structure related issues				Miscellaneous issues								
		Appointment of Board of directors	Compensation of Board of directors	Gender diversity in Board of directors	Appointment of Executives / Senior Management	Compensation of Executives / Senior Management	CEO Duality	Financial Performance of the company	Stakeholder	Growth	Earnings Management	Dividend	Liquidity	Size of Firm	Under Valuation	Capital Structure of the company	Capex plan	Over-Investment	Idle cash availability	Ownership	Auditor related issues	Pollution	Executive Behaviour	Political	Regulation	Risk Taking ability of firm	
Equitas Holdings Ltd	28-Mar-19	✓																									
Lupin Ltd.	27-Mar-19	✓																									
Gufic Biosciences Ltd.	13-Dec-18																									✓	
Shriram Transport Finance Co. Ltd.	4-Dec-18																									✓	
Eclerx Services Ltd.	25-Oct-18	✓																									
TeamLease Services Ltd	6-Oct-18																										
TeamLease Services Ltd	6-Oct-18					✓																					
ITC Ltd	1-Oct-18					✓																					
ITC Ltd	1-Oct-18					✓																					
A P L Apollo Tubes Ltd.	29-Sep-18	✓	✓			✓																					
Elpro International Ltd.	29-Sep-18																								✓		
Elpro International Ltd.	29-Sep-18																✓								✓		
Gufic Biosciences Ltd.	28-Sep-18																✓								✓		
Atul Auto Ltd.	28-Sep-18																✓								✓		
Heidelberg	21-Sep																✓								✓		

List of Issues	Date of Meeting	Board of directors related issues			Executive / Senior Management related issues			Financial Performance and Valuation related issues								Idle Cash and Capital Structure related issues				Miscellaneous issues							
		Appointment of Board of directors	Compensation of Board of directors	Gender diversity in Board of directors	Appointment of Executives / Senior Management	Compensation of Executives / Senior Management	CEO Duality	Financial Performance of the company	Stability	Growth	Earnings Management	Dividend	Liquidity	Size of Firm	Under Valuation	Capital Structure of the company	Capex plan	Over-Investment	Idle cash availability	Ownership type	Auditor related issues	Pollution	Executive Behaviour	Policy	Regulation	Risk Taking ability of firm	
Cement India Ltd.	p-18																										
Advanced Enzymes Technologies Ltd	14-Sep-18	✓																									
Advanced Enzymes Technologies Ltd	14-Sep-18	✓																									
Apollo Tyres Ltd.	7-Sep-18	✓																									
J B F Industries Ltd.	3-Aug-18		✓																								
Akzo Nobel India Ltd.	2-Aug-18	✓																									
PNB Housing Finance Ltd	27-Jul-18	✓																									
Suzlon Energy Ltd.	27-Jul-18														✓												
Suzlon Energy Ltd.	27-Jul-18														✓												
Syngene International Ltd.	15-Jul-18					✓																					
Syngene International Ltd.	15-Jul-18					✓																					
Syngene International Ltd.	15-Jul-18					✓																					
Jammu & Kashmir Bank Ltd.	7-Jul-18	✓																									
Fortis Healthcare Ltd.	22-May-18	✓																									
Fortis Healthcare Ltd.	22-May-18	✓																									
Fortis Healthcare Ltd.	22-May-18	✓																									
Gammon India Ltd.	21-Mar-18		✓																								
Gammon India Ltd.	21-Mar-18		✓																								
Karur Vysya Bank Ltd.	1-Feb-18					✓																					
Dr. Reddy's Laboratories Ltd.	19-Jan-18					✓																					
Dr.	19-					✓																					

List of Issues	Date of Meeting	Board of directors related issues			Executive / Senior Management related issues			Financial Performance and Valuation related issues								Idle Cash and Capital Structure related issues				Miscellaneous issues						
		Appointment of Board of directors	Compensation of Board of directors	Gender diversity in Board of directors	Appointment of Executives / Senior Management	Compensation of Executives / Senior Management	CEO Duality	Financial Performance of the company	Stability	Growth	Earnings Management	Dividend	Liquidity	Size of Firm	Under Valuation	Capital Structure of the company	Cash expenditure	Over- Investment	Idle cash availability	Ownership type	Auditor related issues	Pension Plan	Executive Behaviour	Policy	Regulation	Risk Taking ability of firm
Reddy'S Laboratories Ltd.	Jan-18																									
Kolte Patil Developers Ltd.	28-Sep-17															✓									✓	
Finolex Cables Ltd.	28-Sep-17	✓																								
Finolex Cables Ltd.	28-Sep-17	✓																								
Finolex Cables Ltd.	28-Sep-17					✓																				
P T C India Ltd.	25-Sep-17	✓																								
Sintex Industries Ltd.	14-Sep-17	✓																								
Birlasoft Ltd.	23-Aug-17	✓																								
ZF Steering Gear (India) Ltd.	2-Aug-17	✓																								
Karnataka Bank Ltd.	17-Jul-17					✓																				
Hinduja Global Solutions Ltd.	11-Jul-17					✓																				
Hinduja Global Solutions Ltd.	11-Jul-17					✓																				
Gammone India Ltd.	29-Jun-17		✓																							
Jammu & Kashmir Bank Ltd.	17-Jun-17	✓																								
Raymond Ltd.	5-Jun-17																								✓	
U P L Ltd.	30-Mar-17					✓																				
U P L Ltd.	30-Mar-17					✓																				
Suzlon Energy Ltd.	30-Sep-16														✓											
Housing Development & Infrastructure Ltd.	29-Sep-16														✓											
D S Kulkarni Developers Ltd.	29-Sep-16											✓														
Multi Commo	19-Sep	✓																								

List of Issues	Date of Meeting	Board of directors related issues			Executive / Senior Management related issues			Financial Performance and Valuation related issues							Idle Cash and Capital Structure related issues				Miscellaneous issues								
		Appointment of Board of directors	Compensation of Board of directors	Gender diversity in Board of directors	Appointment of Executives / Senior Management	Compensation of Executives / Senior Management	CEO Duality	Financial Performance of the company	Stakeholder	Growth	Earnings Management	Dividend	Liquidity	Size of Firm	Under Valuation	Capital Structure of the company	Current	Over- Investment	Idle cash availability	Ownership	Auditor related issues	Provision	Executive Behaviour	Policy	Regulation	Risk Taking ability of firm	
Exchange Of India Ltd.	16-11																										
Mcleod Russel India Ltd.	8-Aug-16		✓																								
Ricoh India Ltd.	5-Aug-16	✓																									
Ricoh India Ltd.	5-Aug-16	✓																									
Ricoh India Ltd.	5-Aug-16	✓																									
Ricoh India Ltd.	5-Aug-16	✓																									
Aarti Drugs Ltd.	22-Jul-16	✓																								✓	
Jammu & Kashmir Bank Ltd.	20-Jul-16	✓																									
IDFC Ltd.	25-Jun-16					✓																					
Count		27	6	0	0	17	0	0	0	0	0	1	0	0	0	4	5	0	0	0	0	0	0	0	0	10	0

Size of the firms is important criteria for shareholder activism globally. Woidtke (2002) mentioned that companies having small scale are generally targeted by pension funds. Boyson and Mooradian (2007), also pointed out the same thing in case of hedge fund activism and reason behind this could be cost of associated with activism is on lower side for smaller firms. But as per our observation rejected proposals are spread across the size measured in terms of market cap. Largest company in this dataset is ITC which has market capitalization over Rs. 2 lakh crore while smallest company has market capitalization below Rs. 100 crore.

Table 3: Company details-

Company name	Market Capital in Rs. crore As of April 18, 2020	Industry as per BSE
ITC Ltd	2,31,216.87	Cigarettes, Tobacco Products
Dr. Reddy'S Laboratories Ltd.	65,331	Pharmaceuticals
Lupin Ltd.	37,295	Pharmaceuticals
U P L Ltd.	27,750	Agrochemicals
Shriram Transport Finance Co. Ltd.	18,215	Finance (including NBFCs)
Aarti Drugs Ltd.	16,447	Specialty Chemicals
Syngene International Ltd.	11,464	Pharmaceuticals
Akzo Nobel India Ltd.	10,554	Furniture, Furnishing, Paints
Fortis Healthcare Ltd.	8,942	Healthcare Facilities
Multi Commodity Exchange Of India Ltd.	5,676	Investment Companies
Apollo Tyres Ltd.	5,609	Auto Tyres & Rubber

Company name	Market Capital in Rs. crore As of April 18, 2020	Industry as per BSE
		Products
Finolex Cables Ltd.	3,758	Other Elect.Equip./ Prod.
Heidelberg Cement India Ltd.	3,554	Cement & Cement Products
A P L Apollo Tubes Ltd.	3,126	Iron & Steel Products
PNB Housing Finance Ltd	3,117	Housing Finance
TeamLease Services Ltd	2,778	Sp.Consumer Services
I D F C Ltd.	2,701	Finance (including NBFCs)
Karur Vysya Bank Ltd.	2,190	Banks
Birlasoft Ltd.	1,926	IT Consulting & Software
Advanced Enzymes Technologies Ltd	1,794	Other Agricultural Products
Raymond Ltd.	1,772	Textiles
Equitas Holdings Ltd	1,733	Holding Companies
Eclerx Services Ltd.	1,733	BPO/KPO
Suzlon Energy Ltd.	1,628	Heavy Electrical Equipment
Karnataka Bank Ltd.	1,369	Banks
P T C India Ltd.	1,257	Electric Utilities
Kolte Patil Developers Ltd.	1,245	Realty
Hinduja Global Solutions Ltd.	1,146	BPO/KPO
Jammu & Kashmir Bank Ltd.	800	Banks
Elpro International Ltd.	589	Other Elect.Equip./ Prod.
Gufic Biosciences Ltd.	488	Pharmaceuticals
Atul Auto Ltd.	371	2/3 Wheelers
Z F Steering Gear (India) Ltd.	251	Auto Parts & Equipment
Housing Development & Infrastructure Ltd.	94	Realty
J B F Industries Ltd.	74	Fibres & Plastics
Gammon India Ltd.	53	Construction & Engineering
Sintex Industries Ltd.	49	Textiles
D S Kulkarni Developers Ltd.	35	Realty
McLeod Russel India Ltd.	33	Tea & Coffee
Ricoh India Ltd.		

Berle & Means (1932) discussed three tier structures (Jensen & Meckling 1976, Fama & Jensen 1983) of Modern Corporation where shareholders are owners of the corporation, managers' controls the operation and board of

directors are monitoring agents. Board of directors and their compensation related issues forms large part of activist proposals. In detailed study of shareholders proxy proposals, Renneboog & Szilagyi (2011) found that these proxy proposals target firms with weak financial performance and weak corporate governance practices. Cziraki et al. (2010) studied proxy proposals in European countries where they are legally binding in nature (in most of the countries), most of the proposals were asking for change in board.

We also found this to be true in proposals which we studied. There are 33 proposals in Board of Director category of which 27 proposals related to appointment of directors; in some instances they rejected appointment of owner / founder of the company as director of the company and other 6 proposals are related to compensation of the directors. We see increasing trend of proposals in this category. Other large category is executive and their compensation, again all the issues falling under this are related to compensation of executives. Some of the proposals were related to issuing ESOPs (Employee Stock Options).

Third large category consists of 9 Idle cash and capital structure proposals. Of these 5 proposals are about capex whereas 4 are about capital structure. Under Miscellaneous issues large number of issues were related party transactions. There was only one proposal related to financial performance, reason for the same could be overlapping of issues between Idle Cash and Financial Performance.

Conclusion and Scope for future research

Our understanding is that activism is still evolving in India and as the concept gets rooted over the years, activist shareholders will also focus on financial performance and cash flow related issues. Globally Hedge Funds and Pension funds are most active investors. In India we are still lagging in such initiative from pension funds and hedge funds. Though there are instances of foreign pension fund taking dig at large Indian companies but we are yet

to see large scale activism in India from these investors.

As an extension to this, one can check characteristics of the companies where the proposals were rejected in terms of state of corporate governance, ownership structure, financial performance, free cash flows etc.

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