

How Corporate Governance and Performance Affect Firm Valuation: Evidence from Indian Listed Firms

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Revised Research Paper with Firm Size and Firm Age as Control Variables

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Abstract

This paper examines the relationship between corporate governance, corporate performance signals and firm valuation using panel data for Indian listed firms over the period 2020–2024. Firm valuation is measured using Tobin's Q , a market-based indicator that reflects investors' expectations about a firm's future growth, profitability and risk. The main explanatory variables in the study are board size, percentage of independent directors and promoter ownership. Firm size and firm age are included as control variables because they may independently affect valuation through scale, maturity, reputation, growth opportunities and access to capital. The study estimates pooled ordinary least squares, fixed-effects and random-effects panel regression models. Diagnostic and model-selection tests are used to determine the most appropriate empirical specification. The Hausman test strongly rejects the random-effects model, indicating that unobserved firm-specific characteristics are correlated with the explanatory variables. Therefore, the fixed-effects model is preferred for inference. The results suggest that corporate governance characteristics are associated with firm valuation, though the relationship is not uniform across all variables. In the preferred fixed-effects model, board size has a positive and statistically significant relationship with Tobin's Q . Independent directors and promoter ownership show weaker and less stable effects across specifications. By treating firm size and firm age as control variables, the paper separates the impact of governance-related factors from basic firm characteristics. This distinction is important because larger or older firms may have different valuation patterns regardless of their governance structure. The findings suggest that investors in Indian capital markets respond to governance signals, but these effects must be interpreted after accounting for firm-level scale and maturity. The paper contributes to the literature on corporate governance and valuation in emerging markets and highlights the importance of panel-data methods when firm heterogeneity is present.

Keywords: corporate governance, corporate performance, firm valuation, Tobin's Q , board size, independent directors, promoter ownership, firm size, firm age, control variables, panel regression, India

Introduction

Firm valuation reflects the market's assessment of a company's current strength and future potential. Investors value firms not only on the basis of current earnings but also on the basis of expected cash flows, governance quality, risk management, ownership structure and growth opportunities. A firm with strong financial performance but weak governance may receive a lower valuation if investors fear agency problems, poor transparency or misuse of control. Similarly, a firm with moderate current performance may receive a higher valuation if investors believe that its governance structure supports long-term value creation.

The relationship between corporate governance and

valuation is especially important in emerging markets such as India. Indian listed firms often operate with concentrated ownership, promoter influence, business-group affiliations and varying levels of board independence. These features make the Indian corporate environment different from widely held corporations in developed markets. In such a setting, investors may pay close attention to board structure, promoter ownership and the role of independent directors when forming expectations about firm value.

This study examines how selected governance-related corporate performance indicators affect firm valuation among Indian listed firms. The main governance variables are board size, percentage of independent directors and promoter ownership.

These variables are chosen because they reflect the monitoring structure, independence and ownership incentives of the firm. Board size captures the scale and potential diversity of board oversight. Independent director percentage captures the extent of external monitoring. Promoter ownership captures the degree of controlling shareholder involvement.

Firm size and firm age are included in the model as control variables. This is a key feature of the revised paper. Firm size and age are not treated as the main variables of interest because they do not directly represent governance mechanisms. Instead, they are included to control for firm characteristics that may influence valuation independently of governance. Larger firms may have greater stability, better access to capital and stronger analyst coverage, but they may also have lower growth prospects. Older firms may benefit from reputation, experience and established stakeholder relationships, but they may also be more mature and less growth-oriented. Controlling for these factors allows the study to estimate the relationship between governance variables and valuation more clearly.

The study uses panel data for Indian listed firms from 2020 to 2024 and applies pooled OLS, fixed-effects and random-effects models. The panel-data approach is appropriate because it captures both differences across firms and changes within firms over time. It also allows the study to control for unobserved firm-specific characteristics that may affect valuation.

The main research question is:

How do corporate governance variables affect the valuation of Indian listed firms after controlling for firm size and firm age?

The contribution of this paper is threefold. First, it focuses on recent Indian firm-level data during a period marked by market volatility, regulatory change and post-pandemic recovery. Second, it distinguishes between main governance variables and control variables, thereby improving the conceptual clarity of the model.

Third, it compares pooled OLS, fixed-effects and random-effects models and uses diagnostic tests to

select the appropriate specification.

1. Literature Review

1.1 Corporate Governance and Firm Valuation

Corporate governance refers to the system of rules, practices and processes through which firms are directed and controlled. It determines how decisions are made, how managers are monitored and how the interests of shareholders and other stakeholders are protected. Good governance can improve firm valuation by reducing agency costs, improving transparency, strengthening accountability and increasing investor confidence.

Agency theory provides the main theoretical foundation for this relationship. Jensen and Meckling (1976) argue that when ownership and control are separated, managers may not always act in the best interests of shareholders. This creates agency costs. Governance mechanisms such as boards of directors, independent directors and ownership concentration can reduce these costs by monitoring management and aligning incentives.

Firm valuation is influenced by both current performance and expected future performance. Market-based valuation measures such as Tobin's Q are particularly useful because they incorporate investor expectations. A higher Tobin's Q suggests that investors believe the firm has strong future prospects, valuable intangible assets or effective governance mechanisms. A lower Tobin's Q may indicate concerns about growth, risk, governance or capital allocation.

1.2 Board Size and Firm Valuation

Board size is an important governance variable because it affects the board's ability to monitor management and provide strategic advice. A larger board may offer more diverse knowledge, wider networks and greater expertise. This can be useful for complex firms that require advice across finance, law, technology, risk management, regulation and industry strategy. In emerging markets, larger boards may also improve legitimacy and compliance with governance expectations. However, larger boards can also create problems. Coordination may become more difficult, decision-making may slow down and

individual directors may contribute less actively. Yermack (1996) finds that smaller boards are associated with higher valuation in some developed-market settings. This suggests that the effect of board size is ambiguous and may depend on context. In India, the relationship may differ because many firms are promoter-led and operate in complex ownership and regulatory environments. A larger board may be valued positively if it increases monitoring capacity and brings external expertise. Therefore, board size is treated as a key explanatory variable in this study.

1.3 Independent Directors and Firm Valuation

Independent directors are expected to improve governance by providing objective oversight. They can protect minority shareholders, question management decisions and improve the credibility of board processes. A higher percentage of independent directors may therefore increase investor confidence and valuation.

However, the effectiveness of independent directors depends on more than their formal presence. Independent directors must have real autonomy, relevant expertise, access to information and willingness to challenge management. In some firms, independent directors may be appointed mainly to satisfy regulatory requirements. In such cases, board independence may not have a strong effect on valuation.

Hermalin and Weisbach (2003) argue that board composition is endogenous. This means that board structure may be shaped by firm performance, ownership structure and bargaining power. As a result, the relationship between independent directors and valuation may be unstable across empirical models.

1.4 Promoter Ownership and Firm Valuation

Promoter ownership is especially important in the Indian context. Promoters often play a central role in firm strategy, board appointments and capital allocation. Promoter ownership can affect valuation in two opposite ways. The first is the incentive-alignment effect. When promoters hold a large ownership stake, they have a direct financial interest in increasing firm value. Their wealth is tied to the

company's share price, which may encourage long-term decision-making and stronger performance.

The second is the entrenchment effect. If promoters have excessive control, they may influence decisions in ways that benefit themselves at the expense of minority shareholders. Investors may discount such firms if they fear related-party transactions, tunneling, weak oversight or limited board independence.

Demsetz and Lehn (1985) argue that ownership structure is partly determined by firm-specific characteristics. Therefore, promoter ownership may not have a simple linear effect on valuation. It may improve valuation at some levels but reduce valuation when control becomes excessive.

1.5 Firm Size and Firm Age as Control Variables

Firm size and firm age are widely used as control variables in corporate finance research. They are included because they affect valuation independently of governance mechanisms. Firm size may influence valuation in several ways. Larger firms usually have more stable operations, greater market visibility, better access to financing and stronger bargaining power. These features may support valuation. At the same time, larger firms may be more mature and may have fewer high-growth opportunities. Therefore, firm size must be controlled for when estimating governance effects. Firm age also affects valuation. Older firms may benefit from reputation, experience, established customer relationships and organizational learning. However, older firms may also be less dynamic than younger firms. Younger firms may receive higher valuation multiples if investors expect rapid growth. Because age may influence valuation regardless of governance quality, it is included as a control variable.

By treating firm size and firm age as controls, this study avoids overstating the role of governance variables. The model estimates whether board size, independent directors and promoter ownership affect valuation after accounting for differences in firm scale and maturity.

2. Conceptual Framework and Hypotheses

The conceptual framework of this study links corporate governance variables to firm valuation while controlling for firm characteristics. The dependent variable is Tobin's Q. The main explanatory variables are board size, independent director percentage and promoter ownership. Firm size and firm age are control variables.

The logic of the model is that investors observe governance characteristics and use them as signals of monitoring quality, agency risk and managerial accountability. These governance signals may influence market valuation. However, investors also consider basic firm characteristics such as scale and maturity. Therefore, firm size and firm age must be included as controls.

The following hypotheses are developed:

H1: Board size has a significant relationship with firm valuation.

The expected direction is ambiguous. Larger boards may improve expertise and monitoring, but they may also reduce coordination efficiency.

H2: The percentage of independent directors has a positive relationship with firm valuation.

Independent directors are expected to improve monitoring and protect shareholder interests, although the effect may depend on the quality of independence.

H3: Promoter ownership has a significant relationship with firm valuation.

Promoter ownership may increase valuation through incentive alignment, but excessive control may reduce valuation through entrenchment.

3.3 Main Explanatory Variables

Control expectation 1: Firm size affects valuation and must be controlled for. Firm size may influence valuation through scale, stability, visibility and growth opportunities. Control expectation 2: Firm age affects valuation and must be controlled for. Firm age may influence valuation through reputation, maturity, experience and growth expectations.

3. Data and Variables

3.1 Data Description

The study uses firm-year panel data for Indian listed firms from 2020 to 2024. The dataset includes firm name, year, Tobin's Q, board size, percentage of independent directors, promoter ownership, firm size and log firm age. The sample contains approximately 468 firm-year observations. The visible extract includes firms such as ABB, Adani Energy Solutions, Adani Enterprises, Adani Green Energy, Adani Ports, Adani Power and Ambuja Cements, among others.

Panel data are suitable for this research because they allow the study to observe firms over time. This makes it possible to control for unobserved firm-specific factors that do not change quickly, such as business model, promoter identity, corporate culture, brand reputation and industry positioning.

3.2 Dependent Variable

The dependent variable is Tobin's Q, which measures firm valuation. Tobin's Q is a market-based measure and is commonly used in corporate governance research. It reflects how investors value a firm relative to its asset base. A higher Tobin's Q indicates stronger market expectations about future performance, growth and governance quality.

Variable	Role in Model	Definition	Expected Relationship with Valuation
Board Size	Main explanatory variable	Total number of directors on the board.	Ambiguous: a larger board may improve expertise and decision-making capacity but may reduce coordination efficiency.
Independent Directors (%)	Main explanatory variable	Percentage of independent directors on the board.	Expected positive, as greater board independence may improve monitoring, corporate governance, and investor confidence.

Promoter Ownership	Main explanatory variable	Percentage of shares held by promoters or controlling shareholders.	Ambiguous: promoter ownership may align managerial and shareholder interests but may also lead to entrenchment.
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4.4 Control Variables

Firm size and firm age are included as control variables to account for differences in firm characteristics that may influence firm valuation.

Variable	Role in Model	Definition	Reason for Inclusion
Firm Size	Control variable	Natural logarithm of total assets, used as a measure of firm scale.	Controls for differences in firm scale, stability, market visibility, and access to capital.
Firm Age	Control variable	Natural logarithm of the firm's age, measured in years since establishment.	Controls for differences in organizational maturity, reputation, business experience, and lifecycle effects.

Note: The exact operational definitions should be consistent with the variables used in the empirical analysis. If firm size is measured using total revenue or market capitalization rather than total assets, the definition should be revised accordingly.

4. Methodology

4.1 Empirical Model

The empirical model estimates the effect of governance variables on firm valuation while controlling for firm size and firm age. The baseline panel regression is specified as follows:

$$[\text{TobinQ}_{\{it\}} = + 1 \text{ BoardSize}_{\{it\}} + 2 \text{ IndependentDirectors}_{\{it\}} + 3 \text{ PromoterOwnership}_{\{it\}} + 1 \text{ FirmSize}_{\{it\}} + 2 \text{ LogFirmAge}_{\{it\}} + i + \{it\}]$$

where (i) represents firms and (t) represents years. ($\text{TobinQ}_{\{it\}}$) is the dependent variable. ($\text{BoardSize}_{\{it\}}$), ($\text{IndependentDirectors}_{\{it\}}$) and ($\text{PromoterOwnership}_{\{it\}}$) are the main explanatory variables. ($\text{FirmSize}_{\{it\}}$) and ($\text{LogFirmAge}_{\{it\}}$) are control variables. (i) captures unobserved firm-specific effects and ($\{it\}$) is the error term.

This model structure allows the study to examine whether governance variables influence valuation after holding constant firm scale and maturity.

4.2 Pooled OLS Model

The pooled OLS model combines all firm-year observations and estimates a single regression. It assumes that unobserved firm-specific factors are not correlated with the explanatory variables. This assumption is often unrealistic in corporate

governance research because firms differ in persistent ways that affect both governance and valuation.

Pooled OLS is still useful as a baseline model because it provides an initial estimate of the relationships in the data. However, if firm-specific heterogeneity exists, pooled OLS may produce biased results.

4.3 Fixed-Effects Model

The fixed-effects model controls for all time-invariant firm-specific characteristics. It uses within-firm variation over time to estimate the relationship between governance variables and valuation. This is useful when unobserved firm characteristics are correlated with the regressors.

In this study, fixed effects are important because Indian firms differ in promoter identity, group affiliation, industry position, governance culture and brand strength. These factors may influence both governance structure and valuation. By controlling for them, the fixed-effects model provides a more reliable estimate of how changes in governance variables are associated with changes in valuation.

4.4 Random-Effects Model

The random-effects model assumes that firm-specific effects are uncorrelated with the explanatory variables. If this assumption holds, random effects can be efficient because it uses both

within-firm and between-firm variation. However, if the assumption is violated, the random-effects estimator becomes inconsistent.

The Hausman test is used to choose between fixed effects and random effects. A significant Hausman test indicates that fixed effects should be preferred.

4.5 Diagnostic Tests

The study reports diagnostic tests for model selection and reliability. The Hausman test compares fixed and random effects. The F-test for individual

effects checks whether firm-level effects are statistically significant. The Breusch-Godfrey/Wooldridge test checks for serial correlation. The Breusch-Pagan test checks for heteroskedasticity. The Pesaran CD test checks for cross-sectional dependence.

These tests are necessary because panel-data regressions may suffer from serial correlation, unequal error variance and common shocks across firms. If these issues are present, robust or clustered standard errors should be used in the final model.

5. Empirical Results

5.1 Regression Results

Main Regression Results

Variable	Role in Model	Pooled OLS	Fixed Effects	Random Effects
Board Size	Main explanatory variable	0.124 (0.134)	0.324**	—
Independent Directors (%)	Main explanatory variable	0.207* (0.025)	-0.056	0.099
Promoter Ownership	Main explanatory variable	3.460 (0.730)	6.691 (1.576)	3.380 (1.110)
Firm Size	Control variable	-1.322 (0.426)	1.706	-0.960
Log Firm Age	Control variable	0.156 (0.240)	3.505	0.623
Constant	—	3.071 (2.05)	—	1.192 (2.65)
Observations	—	468	468	468
R-squared	—	0.470	—	0.190
Adjusted R-squared	—	0.460	—	—
F-statistic	—	81.974 (df = 5, 462)	18.113	—

Notes: The table is based on the supplied regression output. Some standard errors and Random Effects entries were not fully legible in the original preview. Values in parentheses are reproduced as supplied; verify their interpretation against the original output.

Significance notation: * $(p < 0.10)$; ** $(p < 0.05)$.

5.2 Model Selection

The Hausman test reports a chi-square statistic of 112.56 with a p-value below $2.2e-16$. This strongly rejects the null hypothesis that the random-effects estimator is consistent. Therefore, the fixed-effects model is preferred for inference.

This result indicates that unobserved firm-specific characteristics are correlated with the explanatory variables. In other words, firms with different governance structures also differ in deeper ways that affect valuation. For example, a firm's promoter background, business-group affiliation or

governance culture may influence both its board structure and its market value. The fixed-effects model controls for such time-invariant characteristics.

The F-test for individual effects reports $F = 22.705$, indicating significant firm-level effects. This further confirms that panel-data methods are necessary. A simple pooled model would ignore important firm-specific differences.

The diagnostic tests also indicate econometric concerns. The Breusch-Godfrey/Wooldridge test suggests serial correlation, with a reported statistic of 8.722 and p-value of approximately $1.512e-05$.

The studentized Breusch-Pagan test reports $BP = 49.21$ and p-value around $2.005e-09$, indicating heteroskedasticity. A Pesaran CD test is also reported, suggesting possible cross-sectional dependence. These issues imply that robust or clustered standard errors should be used in a final empirical version.

6. Interpretation of Results

6.1 Board Size

Board size is the most consistent governance variable in the results. It has a positive coefficient in the pooled OLS model and a positive, statistically significant coefficient in the fixed-effects model. The fixed-effects coefficient of 0.324 suggests that, within the same firm, increases in board size are associated with increases in Tobin's Q after controlling for firm size and firm age.

This finding suggests that the market may value larger boards in the Indian context when they improve board capacity, expertise and oversight. Indian listed firms often operate in complex environments involving promoter influence, regulatory requirements, diversified business activity and changing investor expectations. A larger board may help firms manage these complexities by bringing in directors with varied expertise.

However, the result should be interpreted carefully. It does not mean that increasing board size always improves valuation. Board effectiveness depends on the quality, independence, experience and participation of directors. A large board that lacks active oversight may not improve governance. The result simply suggests that, in this sample, increases in board size are positively associated with valuation after controlling for scale and age.

6.2 Independent Directors

The percentage of independent directors shows an unstable relationship with valuation. It is positive and weakly significant in pooled OLS, negative in fixed effects and positive in random effects. This suggests that board independence does not have a simple direct effect on valuation in the sample.

One explanation is that the percentage of independent directors may capture formal independence rather than actual independence.

Investors may not reward firms merely for having independent directors if those directors do not exercise meaningful oversight. The market may care more about director reputation, expertise, attendance, committee membership and willingness to challenge management.

Another explanation is that independent director percentage may not change much over time within firms. Since the fixed-effects model relies on within-firm variation, limited change in this variable can make its effect difficult to estimate precisely.

6.3 Promoter Ownership

Promoter ownership is positive across the reported specifications, although its statistical strength is not fully clear from the available output. A positive coefficient is consistent with the incentive-alignment argument. When promoters hold a significant ownership stake, they may be motivated to improve firm value because they directly benefit from share-price appreciation.

However, promoter ownership must be interpreted cautiously. In India, promoters often exercise substantial control over firms. This can support long-term commitment, but it can also raise concerns about entrenchment and minority shareholder protection. The relationship between promoter ownership and valuation may therefore be nonlinear. Moderate promoter ownership may increase valuation, while very high promoter control may reduce valuation if investors fear governance risks.

Future research could test this possibility by including squared promoter ownership or ownership-threshold variables.

6.4 Firm Size as a Control Variable

Firm size is included as a control variable rather than a main explanatory variable. Its purpose is to account for the fact that large and small firms may be valued differently regardless of governance structure.

The results show that firm size has a negative coefficient in pooled OLS and random effects but a positive coefficient in fixed effects. This difference suggests that firm size operates differently across firms and within firms. Across firms, larger firms

may have lower Tobin's Q because mature firms often trade at lower growth multiples. Within the same firm, however, growth in size may be valued positively if it reflects expansion, stronger operations or improved market position. Because firm size affects valuation independently, controlling for it is necessary. Without this control, the estimated effect of governance variables could partly reflect differences in firm scale.

6.5 Firm Age as a Control Variable

Firm age is also included as a control variable. Older firms may have stronger reputation, more experience, better stakeholder relationships and greater organizational stability. These factors may support valuation. However, younger firms may have stronger growth opportunities and may receive higher valuation multiples. Log firm age is positive across the reported specifications. This suggests that older firms in the sample may benefit from reputation and maturity. However, the result should be interpreted cautiously because age changes mechanically over time and may be correlated with time trends. Including firm age as a control helps ensure that the estimated governance effects are not simply capturing the difference between younger and older firms.

7. Discussion

The results show that governance variables matter for firm valuation, but their effects are complex. Board size appears to have the clearest positive relationship with valuation in the preferred fixed-effects model. This may reflect the value of board expertise and monitoring capacity in Indian listed firms. Independent directors and promoter ownership show less stable effects. This does not mean that they are unimportant. Rather, it suggests that simple quantitative measures may not fully capture governance quality. The percentage of independent directors does not reveal whether directors are truly independent, experienced or influential. Similarly, promoter ownership can represent either commitment or control risk depending on the context. The treatment of firm size and firm age as control variables improves the clarity of the analysis. These variables are not the main focus of the study, but they are necessary

because valuation is influenced by firm scale and maturity. A large, mature firm may naturally have a different valuation profile from a smaller, younger firm. By controlling for firm size and age, the study provides a cleaner estimate of the relationship between governance variables and valuation. The diagnostic tests also show that corporate panel data require careful econometric treatment. Serial correlation, heteroskedasticity and cross-sectional dependence can affect standard errors and significance levels. Therefore, future versions of the paper should use robust or firm-clustered standard errors.

8. Managerial, Investor and Policy Implications

The findings have implications for managers, investors and regulators. For managers and boards, the study suggests that governance structure should be designed for effectiveness rather than mere compliance. Board size may matter when it improves expertise, oversight and strategic guidance. Firms should focus not only on the number of directors but also on board quality, diversity, independence and engagement. For investors, the results suggest that governance variables can provide useful information about valuation, but they should not be interpreted mechanically. Investors should examine whether independent directors are genuinely effective and whether promoter ownership reflects commitment or excessive control. Investors should also compare firms after accounting for size and age because valuation naturally differs across firms at different stages of development. For regulators, the findings suggest that formal governance requirements are useful but insufficient. Regulations should encourage not only board independence on paper but also meaningful director accountability, transparent disclosures and protection of minority shareholders.

9. Limitations and Future Research

This study has several limitations. First, the sample period from 2020 to 2024 is relatively short. A longer panel would allow stronger conclusions about long-term governance effects. Second, the study focuses on selected governance variables and does not include profitability measures such as

return on assets, return on equity or operating margin. Including these variables would provide a broader view of corporate performance. Third, the regression output indicates serial correlation, heteroskedasticity and possible cross-sectional dependence. Future research should report robust or clustered standard errors. Fourth, the independent director variable measures formal board independence but does not capture director quality, attendance, expertise or influence. Future studies could extend the model by including board diversity, audit committee strength, institutional ownership, leverage, profitability and ESG disclosure. They could also test nonlinear promoter ownership effects and compare results across industries.

10. Conclusion

This paper examined how corporate governance variables affect firm valuation among Indian listed firms from 2020 to 2024. Tobin's Q was used as the measure of firm valuation. The main explanatory variables were board size, percentage of independent directors and promoter ownership. Firm size and firm age were included as control variables to account for differences in scale and maturity.

The Hausman test strongly supports the fixed-effects model, indicating that unobserved firm-specific characteristics are correlated with the explanatory variables. In the preferred fixed-effects model, board size has a positive and statistically significant relationship with valuation. This suggests that increases in board size are associated with higher Tobin's Q after controlling for firm size, firm age and time-invariant firm characteristics.

The effects of independent directors and promoter ownership are less stable across specifications. This highlights the complexity of governance in India, where formal governance indicators may not fully capture actual governance quality and promoter ownership may reflect both incentive alignment and entrenchment risk. Overall, the study finds that governance characteristics are associated with valuation, but these effects must be evaluated after controlling for firm size and firm age. The results support the view that Indian investors price governance signals, while also considering firm

scale, maturity and unobserved firm-specific characteristics.

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