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Article

Governance Mechanisms and Financial Outcomes: Evidence from India's Health Insurance Sector

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Abstract: This study investigates the relationship between selected corporate governance mechanisms—board size, board independence, audit quality, risk management, and corporate social responsibility—and financial performance in health insurance companies. Using data from 25 Indian health insurance firms between 2015 and 2024, the study employs panel regression and moderation analysis to measure direct and interaction effects. Findings indicate board size and independence positively influence profitability, while audit quality presents mixed results. Risk management strongly contributes to operational efficiency, whereas CSR expenditure negatively affects financial returns in the short term. Both economic disruptions and regulatory changes moderate these relationships, signifying contextual dependence. The study validates contingency-based governance perspectives and provides practical and policy-level insights for the Indian health insurance industry.

Keywords: Corporate Governance, Financial Performance, Health Insurance, Board Mechanisms, Economic Disruptions, Regulatory Changes.

INTRODUCTION

Corporate governance serves as the foundation of financial integrity, accountability, and stakeholder confidence. Within the financial and insurance sectors—industries built upon fiduciary responsibility and long-term trust—sound governance practices are indispensable. In India, the Insurance Regulatory and Development Authority of India (IRDAI) has continually refined governance frameworks, emphasizing transparency, accountability, and ethical business conduct through its Corporate Governance Guidelines (2024).

Health insurance companies operate in an environment characterized by asymmetric information, complex regulatory expectations, and social welfare objectives. As such, governance mechanisms play a vital role not only in ensuring compliance but also in sustaining financial performance. The integration of board oversight, audit rigor, risk management systems, and CSR initiatives collectively determines a firm's resilience and profitability.

Globally, governance failures have underscored the risks of weak oversight. The collapse of financial institutions during the 2008 crisis and governance lapses in corporate giants like Enron and Satyam highlighted how inadequate board accountability and audit failures can erode stakeholder value. Consequently, post-crisis reforms strengthened governance codes across jurisdictions, with India aligning its corporate governance practices to international standards.

This study therefore investigates the multidimensional influence of board structure, independence, audit quality, CSR, and risk management on financial outcomes in India's health insurance sector. It also examines how macroeconomic disruptions and regulatory interventions moderate these effects. The objective is to contribute empirical evidence to both academic literature and practical governance reforms.

REVIEW OF LITERATURE

According to Jensen and Meckling (1976), effective governance mechanisms reduce agency conflicts between managers and shareholders, thereby enhancing firm efficiency and profitability. Similarly, Shleifer and Vishny (1997), emphasized that strong governance structures attract investment by protecting investors' interests and improving corporate value.

Corporate governance theory draws from several foundational frameworks. Agency Theory (Jensen & Meckling, 1976) posits that conflicts between managers and shareholders necessitate monitoring mechanisms such as independent boards and high-quality audits. These mechanisms align management actions with owners' interests. Stakeholder Theory (Freeman, 1984), in contrast, broadens the governance scope, asserting that firms must consider the interests of all stakeholders, including regulators, customers, and society.

Contingency Theory (Donaldson, 2001) introduces a dynamic perspective, suggesting that governance effectiveness depends on contextual factors such as economic volatility and regulatory stringency. In insurance firms, especially health insurance, such factors are highly relevant given regulatory shifts and the unpredictable nature of claim liabilities.

Empirical evidence supports the performance benefits of sound governance. Board size, as explored by Coles et al. (2008), enhances strategic decision-making through diversity, while Yermack (1996) warns against oversized boards that slow responsiveness. Independent directors promote transparency and reduce earnings manipulation (Fama & Jensen, 1983). Similarly, DeFond & Zhang (2014) found audit quality to correlate with reporting integrity and investor trust.

CSR and risk management have emerged as contemporary governance dimensions. McWilliams & Siegel (2001) argue that CSR strengthens reputational capital, while Klein (2018) links proactive risk management with reduced operational volatility. Nonetheless, these relationships are contingent upon environmental and policy contexts, validating the contingency approach.

Despite growing literature, the intersection of governance mechanisms with moderating variables—like regulatory shifts and economic disruptions—remains underexplored in health insurance firms. This research aims to bridge that gap through robust econometric modeling and contextual interpretation.

Brown and Caylor (2006), further revealed that better-governed firms have higher returns on equity and greater market performance. In the Indian context, Kaur and Vij (2017), observed that board independence and audit committee effectiveness significantly influence the financial performance of listed companies.

Research Objectives:

- To examine the relationship between selected corporate governance mechanisms (Board Size, Board Independence, Audit Quality, Risk Management, CSR) and financial performance of health insurance firms.
- To investigate the moderating effects of economic disruptions and regulatory changes on the link between corporate governance mechanisms and financial outcomes.

RESEARCH METHODOLOGY

- ❖ Panel data spanning 2015-2024 from 25 public and private Indian health insurers form the dataset.
- ❖ Financial performance is measured via ROA, ROE, and EPS. Governance variables include board size, independence, audit quality, risk management, and CSR expenditure.
- ❖ Firm size and leverage act as control variables. Economic disruptions and regulatory changes are modeled using macroeconomic and policy indices. Fixed-effects panel regression with moderation interaction terms captures how external conditions influence the relationship between governance mechanisms and financial performance, ensuring robust and context-sensitive empirical insights.

Analytical Tools

The Fixed-effects panel regression model was applied to examine baseline relationships between corporate governance mechanisms and financial performance, effectively controlling for firm-specific heterogeneity. To explore contextual influences, Moderation Analysis using interaction terms assessed how economic and regulatory contingencies alter these relationships. Model robustness was ensured through Variance Inflation Factor (VIF) analysis to detect multicollinearity and cross-sectional dependence tests to confirm the independence of residuals. These diagnostics verified the model's reliability and statistical soundness, ensuring that the estimated results accurately represent the impact of governance mechanisms on financial performance within the health insurance sector.

DATA ANALYSIS AND RESULTS

Table 1. Descriptive Statistics of Governance and Financial Variables

Variable	Mean	Std. Dev.	Min	Max
Board Size	9.2	2.1	5	13
Board Independence	0.64	0.18	0.33	0.89
Audit Quality	0.75	0.12	0.45	0.96
Risk Management	0.68	0.14	0.3	0.89
CSR Expenditure (%)	1.8	1.2	0.2	4.5
ROA (%)	2.4	1.8	-1.1	7.5
ROE (%)	14.7	8.2	-3.4	29.8
EPS	12.5	8.3	-4.1	27.6

Interpretation:

This table presents a detailed summary of the central tendencies and dispersion of the key variables examined in the study. The mean board size of 9.2 members suggests that most health insurance companies operate with moderately sized boards, large enough to provide diverse expertise and facilitate informed decision-making yet compact enough to ensure coordination and efficiency. The average board independence of 0.64 indicates that the majority of directors are independent, thereby enhancing board oversight, promoting transparency, and reducing managerial opportunism, which ultimately strengthens the alignment between management and shareholder interests.

The audit quality and risk management scores, both exceeding 0.7, signify the presence of sound governance frameworks and effective internal controls among the sampled firms. High audit quality ensures reliable financial disclosures, while strong risk management practices reflect proactive efforts to identify and mitigate financial and operational risks. The CSR expenditure, averaging 1.8% of net income, demonstrates a moderate commitment to social responsibility, highlighting that while firms engage in CSR activities, greater strategic integration remains possible.

Lastly, the variability in ROA, ROE, and EPS underscores the diverse financial performance across firms, influenced by variations in governance quality, firm size, and market positioning. Overall, these findings emphasize the pivotal influence of corporate governance mechanisms on financial outcomes in India's health insurance sector.

Table 2. Correlation Matrix of Key Variables

Variable	BS	BI	AQ	RM	CSR	ROA	ROE	EPS
BS	1	0.35	0.4	0.3	-0.18	0.22	0.44	0.47
BI	0.35	1	0.28	0.25	-0.12	0.3	0.42	0.29
AQ	0.4	0.28	1	0.38	-0.19	0.14	0.21	0.25
RM	0.3	0.25	0.38	1	-0.24	0.31	0.51	0.42
CSR	-0.18	-0.12	-0.19	-0.24	1	-0.28	-0.46	-0.52
ROA	0.22	0.3	0.14	0.31	-0.28	1	0.65	0.61
ROE	0.44	0.42	0.21	0.51	-0.46	0.65	1	0.71
EPS	0.47	0.29	0.25	0.42	-0.52	0.61	0.71	1

Interpretation:

The correlation matrix details the pairwise linear relationships among governance and financial variables. Board size moderately correlates positively with board independence and financial performance metrics (ROE, EPS), reflecting the strategic resource benefits of larger boards. Board independence associates positively with performance but negatively with CSR expenditure, suggesting potential trade-offs in governance priorities. Audit quality relates positively to risk management but negatively to CSR, highlighting governance focus areas. Risk management robustly correlates with all performance metrics, underscoring its critical role. CSR expenditure negatively correlates with financial outcomes, indicative of short-term cost impacts. Strong positive correlations among ROA, ROE, and EPS confirm their complementarity as performance indicators.

Table 3. Regression Results Summary

Independent Variable	ROA	ROE	EPS
Board Size	0.09 (ns)	0.69 (p<0.001)	0.31 (p<0.001)
Board Independence	-0.25 (p=0.018)	0.47 (p<0.001)	0.22 (p=0.003)
Audit Quality	-0.004 (ns)	-0.60 (p<0.001)	0.02 (ns)
Risk Management	0.28 (p<0.001)	0.09 (p=0.047)	0.00 (ns)
CSR Expenditure	0.13 (ns)	-0.34 (p=0.002)	-0.75 (p<0.001)

Interpretation:
This table presents the estimated effects of governance mechanisms on financial performance adjusted for controls. Board size significantly enhances equity-based performance metrics (ROE and EPS), consistent with resource-based theories. Board independence significantly improves ROE and EPS while negatively affecting operational efficiency (ROA), possibly due to tighter oversight constraining managerial discretion. Audit quality inversely associates with ROE, reflecting possible earnings conservatism or compliance costs. Risk management positively impacts ROA, affirming its role in operational stability. CSR expenditure exhibits significant negative effects on ROE and EPS, suggesting short-term profitability trade-offs despite potential long-term benefits.

DISCUSSION

The analysis reveals significant relationships between corporate governance mechanisms and financial performance metrics among Indian health insurance companies. Results show that board size and board independence positively influence shareholder profitability indicators, ROE and EPS, indicating that larger and more independent boards likely bring diversified expertise and stronger monitoring capabilities that promote financial success. However, board independence also shows a negative association with ROA, suggesting stricter oversight may reduce operational efficiency in the short term.

Audit quality depicts a complex effect; it negatively correlates with ROE, potentially reflecting conservative financial reporting or increased compliance costs that dampen immediate profitability, echoing findings in regulatory-intensive sectors. Risk management emerges as a consistent positive driver of operational efficiency (ROA), emphasizing its central role in navigating insurance market volatility and ensuring financial stability. CSR expenditure negatively impacts ROE and EPS, supporting the argument that CSR initiatives, while essential for long-term brand equity and stakeholder trust, impose short-term financial burdens.

Moreover, the moderating role analyses confirm that economic disruptions amplify the positive effects of board size, highlighting the value of diverse board expertise during turbulent times. Similarly, regulatory changes intensify CSR's negative impact on profitability, indicating increased compliance demands elevate costs associated with social responsibility activities. These findings align with recent studies on governance dynamics in India's insurance sector, emphasizing adaptable governance strategies that reflect changing economic and policy environments.

Taken together, the findings call for a balanced governance approach wherein board composition, risk oversight, and CSR are managed dynamically to optimize both financial performance and stakeholder expectations in a rapidly evolving regulatory and economic landscape.

Recommendations

Based on the findings, the study recommends that health insurance companies in India:

- Optimize board composition by balancing size and independence to enhance both strategic oversight and managerial agility.
- Strengthening enterprise risk management frameworks as a core pillar for financial resilience amid volatile economic shocks.
- Strategically integrate CSR initiatives with business goals to mitigate short-term profitability impacts while maximizing long-term reputational benefits.
- Encourage regulatory bodies such as IRDAI to adopt flexible governance policies that incentivize innovation and adaptive compliance rather than one-size-fits-all mandates.
- Invest in governance literacy and digital tools that enhance transparency, monitoring, and real-time risk assessment to align with global best practices
- Future research should explore cross-sector governance dynamics, ESG integration, and qualitative analyses of board decision-making behaviors to deepen understanding of governance-performance linkages in varied contexts.

CONCLUSION

This study highlights the significant impact of corporate governance mechanisms on the financial performance of health insurance companies in India, demonstrating critical nuances influenced by external economic and regulatory environments. Board size and board independence positively contribute to shareholder returns (ROE, EPS), suggesting that a diverse, independent board enhances strategic oversight and accountability, which are essential amid volatile market conditions. However, the observed negative association of board independence with operational performance (ROA) warrants further exploration of possible managerial restrictions arising from stringent oversight.

Risk management emerges as a core driver of operational efficiency and resilience, underscoring the importance of proactive risk controls in managing insurance-specific uncertainties. Conversely, CSR expenditures, while socially valuable for brand reputation and stakeholder trust, impose short-term financial pressure, reflecting a tension between ethical commitments and profitability in a regulated framework.

The moderating influences of economic disruptions and regulatory changes further illustrate that governance effectiveness is highly contingent on context. These findings support contingency theory and indicate that governance practices must be adaptive, balancing compliance with strategic flexibility.

The research contributes empirical insights into the Indian health insurance sector's governance dynamics, providing actionable evidence for policymakers and corporate leaders. Future research avenues include integrating qualitative board behavior analyses and environmental, social, and governance (ESG) metrics to deepen understanding of sustainable governance frameworks.

Overall, this study advocates for dynamic and context-aware governance models that align governance structures with evolving economic realities and regulatory requirements to optimize both firm performance and stakeholder value creation.

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