

Short-Selling Activism and Corporate Governance in India: A Qualitative Study of Market, Regulatory and Board Responses

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Abstract - Short-seller reports on Indian listed companies are often seen as either market abuse or shareholder activism. This paper instead explores them from a governance perspective. It reviews public documents (company statements, exchange filings, regulatory communications, and press coverage) around the Hindenburg Research report on the Adani Group, Eros International (Mangrove Partners and other short sellers, from about 2015), and asks what boards, institutional investors, and regulators did once the allegations surfaced. Three things stand out. Boards with credible independent directors and effective audit processes responded with evidence-based, procedural answers, while promoter-led boards leaned on denial and legal threats. Institutional investors asked harder questions, though mostly out of public view. The regulatory response counted for as much as the allegations: slow or mixed signals prolonged the uncertainty. The paper argues that an activist short report acts as an external stress test of a firm's disclosure and oversight, and that the quality of the response matters more than whether the report turns out to be right. Suggestions are made for boards, investors and regulators.

Key Words: short-selling activism, corporate governance, India, board oversight, shareholder activism, regulatory response.

1. INTRODUCTION

In January 2023, Hindenburg Research, a US-based short seller, published a report accusing the Adani Group of stock manipulation and aggressive accounting. Within days, the group's listed companies had lost a large share of their market value, its flagship company had pulled a follow-on public offer of roughly ₹20,000 crore, and the Supreme Court of India was setting up an expert committee. Very few governance episodes in India have drawn in so many institutions so quickly.

The Adani case is the best known, but it is not the only one. Activist short sellers, meaning funds or research outfits that take a short position and then publish claims about overvaluation, accounting irregularities, or governance failures, have targeted other Indian companies before and since. The public argument usually turns on two questions: is the report accurate, and is the seller acting in good faith? Both are fair questions. They also leave out something a governance researcher should want to know, which is what the company, its investors and its regulators actually do after the allegations become public.

India is an interesting place to ask this. Promoter ownership is concentrated in a large share of listed firms [6], and that weakens the usual market routes by which outsiders discipline management. At the same time, the rules have tightened. The Companies Act, 2013 and the SEBI listing regulations [9][10] put

heavier disclosure duties on companies and expect independent directors to do real oversight. A short report lands in the gap between those two facts.

This paper asks how short-selling activism shapes corporate governance in Indian listed firms, and what decides whether the result is better accountability or simply a long fight. It does three things. It describes the governance mechanisms a short report sets off. It shows how responses differ with ownership and board strength. And it suggests what boards, investors and regulators might do differently.

2. LITERATURE REVIEW

Research on short selling divides fairly cleanly. One group of studies finds that short sellers are good at spotting trouble. Karpoff and Lou [5] show that short interest builds up before financial misconduct is made public, and that this helps prices adjust sooner. The older theoretical work of Diamond and Verrecchia [3] points the same way: when short selling is constrained, private bad news reaches prices more slowly. On this view, short sellers do a monitoring job that nobody else is paid to do.

Others are less convinced. A public campaign can be timed around the seller's own trades, claims can be stretched, and markets can overreact before anyone has checked the facts. Aggarwal and Wu [1] show that manipulation tends to thrive where stocks are illiquid and information is hard to verify. The point carries over: a loud public claim can move a price whether or not it is true, and some Indian stocks fit that description.

Activism from the long side has been studied closely. Brav et al. [2] find that firms targeted by activist hedge funds tend to show better operating performance and positive announcement returns. Activism from the short side has had much less attention, and very little of it concerns India.

Indian governance research has mostly dealt with ownership, board composition, independent directors, audit quality and enforcement [6]. To our knowledge, little of it treats a hostile, public challenge from outside as a governance event in its own right. There are legal commentaries and a few market-reaction studies, but few that follow what happens inside and around the firm afterwards. That is the gap this paper tries to fill, in a modest way.

3. THEORETICAL FRAMEWORK

Three standard theories are used here as reading tools rather than as hypotheses to be tested.

Signaling theory [7] suggests that a short report tells the market something exists outside the company's own disclosures, whether

or not the claim is accurate. Stakeholders then have to decide how much to believe, and how the company reacts becomes a signal too. A prompt, specific answer says one thing. Silence or a vague statement of outrage says another.

Agency theory [4] explains why this matters. Managers know more than outsiders and may not volunteer bad news. A short seller adds external pressure and raises the cost of staying quiet. Whether that pressure improves oversight depends on whether the board is willing and able to use it, which is where independent directors and audit committees come in.

Stakeholder theory [8] reminds us that more than shareholders are watching. Lenders, auditors, regulators, employees, and rating agencies all read the same report, and each has its own reasons to act on it. The governance outcome comes out of how these groups interpret the event and respond to one another.

4. METHODOLOGY

The study is qualitative and interpretive, built around cases. An event-study design would show how prices moved, but it would say little about what boards decided, how investors engaged or how regulators reacted, and those are the questions here.

The material is public. It includes company filings and stock exchange disclosures, press releases and rebuttals, regulatory statements, court orders, and press coverage and commentary. The Hindenburg report on the Adani Group is the main case because its public record is the fullest. Other publicised short campaigns against Indian listed companies, and against foreign-listed firms with substantial Indian operations (Eros International and Ebix), were used to check whether the patterns held beyond one group.

Each episode was read in chronological order. The documents were then coded for board response, investor engagement, regulatory action, changes in disclosure and reputational effects, and the codes were compared across firms with different ownership structures.

The limits are plain. The evidence is the public record only, with no interviews. Press coverage is partial and sometimes partisan. Many of the allegations have not been proved or disproved, so the paper makes no claim about whether any report was correct. And because the number of episodes is small, the findings below are propositions to be tested, not general results.

5. FINDINGS

5.1 The first shock falls on the board

A short report puts the board under immediate pressure to say something. In the Adani case the group answered within days with a long rebuttal, described the report as an attack on India and its institutions, and spoke of legal action. It then withdrew its share offer even though the offer had been fully subscribed, saying it did so to protect investors from market volatility. The reply defended the company, but it did not do much to settle the specific accounting and ownership questions the report had raised.

In the other episodes reviewed, the boards that handled the first weeks better tended to share certain features: an audit committee that could act independently, a record of detailed disclosure, and a willingness to say what was being checked and by whom. Their first response was procedural. The audit committee would look at the claims, sometimes with an outside firm, and a line-by-line reply would follow. Boards with weaker oversight were slower,

and their statements leaned on denial, on the seller's motives and on litigation.

5.2 Investors ask more questions, mostly in private

Institutional investors rarely said much in public. What the record suggests is that they asked for explanatory calls, pressed for independent verification and watched the board's behaviour closely. Even investors who did not accept the seller's claims had reason to want better answers, because the report had changed how others would value the company.

This is the weakest of the four findings, because engagement of this kind mostly happens out of sight and the documents show only fragments of it. It is consistent with the idea that a short report can sharpen stewardship, but it does not prove it.

5.3 Regulators and courts shape what comes next

After the Adani report, SEBI began an investigation, and the Supreme Court appointed an expert committee. In January 2024 the Court declined to hand the matter to a special investigation team and directed SEBI to complete its work. That is a long timeline. Through all of it the company's credibility stayed in question, partly because no authoritative finding arrived to settle the facts.

Matters grew more complicated in August 2024, when Hindenburg made allegations touching the SEBI chairperson, which she denied. Whatever their merit, they pulled the regulator itself into the dispute. A regulator whose independence is being questioned has a harder time turning a market controversy into governance accountability. The pattern here is that quick, consistent regulatory signals help a firm and its investors resolve the question, and slow or contested ones leave it hanging.

5.4 Ownership and board quality change the outcome

The outcome was not the same across firms. Firms with dispersed ownership, effective independent directors, and good disclosure habits were better able to absorb the pressure and respond in a constructive way. Promoter-controlled firms, especially where promoters have a strong hand in what gets disclosed, were more likely to respond defensively and to frame the report as an attack on the company or the country. Table -1 sets out the pattern. It is our interpretive summary of the documents, not a measured result.

Table -1: Governance response patterns by firm type (interpretive summary)

Firm type	Typical first response	Governance outcome observed
Widely held, strong independent board	Audit committee review, detailed reply, updated disclosure	Quicker correction, more accountability
Promoter-controlled	Public denial, legal threats, appeal to reputation or national interest	Slower and mixed; uncertainty lasts longer
Firms under a sector regulator	Coordination with the regulator, supervisory disclosure	Faster reporting, but depends on the regulator

The firm's governance structure largely decides the result. Two firms can face similar allegations and end up in very different places, depending on who controls the board and how far the company's disclosures can be trusted to start with.

6. DISCUSSION

The findings support a fairly simple reading. In India, a short report can work as an external governance mechanism, and its main effect is not the first-day fall in the share price. It is the pressure it puts on disclosure, on board accountability and on investor attention. Where the institutions are sound, that pressure can speed up review and correction. Where they are weak, the usual results are conflict, delay and reputational damage.

The debate over short selling is often set up as a choice between good activism and bad manipulation. The Indian record does not fit that neatly. Some campaigns may well carry exaggerated claims or commercial motives. Even so, they show how sensitive a firm's governance is to outside challenge, and the way a firm handles an unfair attack tells investors as much as the way it handles a fair one. Blanket suppression would be the wrong response. So would taking every report at face value.

There are costs on both sides. If short reports are brushed aside, firms miss a chance to fix real weaknesses. If everyone overreacts, the result is panic and litigation before the facts are known. The aim for Indian markets should be to keep what is useful in activism, which is information that formal disclosure missed, while making abuse costly.

7. IMPLICATIONS FOR BOARDS, INVESTORS AND REGULATORS

Boards. The main lesson is to prepare before a report arrives. A listed company should have a written protocol covering who verifies the claims, who speaks, what the audit committee reviews and where independent directors sit in the process. Ad hoc replies and long silences both feed suspicion.

Institutional investors. Stewardship cannot stay passive when a governance controversy is public. Investors should read the allegations on their merits, engage the company early and ask for verified answers where the questions are serious. This matters most in promoter-dominated firms, where outside monitoring has less competition.

Regulators. The task is one of balance. Legitimate research needs room, and so does the market's right to hear it. Manipulative or reckless campaigns need to be deterred. Clearer expectations on disclosure, better surveillance of trading around publication, and a standard process for asking companies to clarify in good time would serve both goals. Regulators also need to protect their own credibility, since it becomes part of the story when a dispute drags on.

8. CONCLUSIONS

Short-selling activism has real consequences for corporate governance in India. When institutions respond well, it can improve transparency, sharpen monitoring and prompt correction. When they respond poorly, it breeds uncertainty and reputational harm.

The paper's main argument is that an activist short report is best seen as a stress test of a firm's governance, whatever its accuracy. How the board, investors and regulators respond decides whether the episode ends in better accountability or in a prolonged quarrel. The study has clear limits: it rests on public documents, a small number of episodes and interpretive coding. Later work could add interviews with directors and investors, systematic coding of a larger set of campaigns, and comparison with other markets where ownership is also concentrated.

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