The determinants and effects of corporate governance level: evidence from Istanbul stock exchange

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Abstract

This paper aims to investigate the determinants and effects of corporate governance level of the firms operating in Istanbul Stock Exchange. It was drawn that firm value was the most important determinant for corporate governance level to be enhanced. Moreover, it was found that firm value mediated corporate investor ratio on corporate governance level. On the other hand, there found a positive relationship between growing corporate governance implementations of the firms and the firm performance. The manifestation of the agency costs resulting from earnings management practices in direction decreasing earnings was seen as a variable that moderates this relationship. Lastly, it was concluded that rising corporate governance implementations had impact on foreign investor preference and that these investors chosen those firms whose corporate governance implementations were enhanced.

Keywords: Corporate Governance, Earnings Management, Firm Value, Corporate Investors

1. Introduction

World economy has been rapidly changed and developed since industrial revolution. Besides, the number of the parties increases every day and this leads to a substantially competitive environment. Firms willing to outperform in such an environment have intensely strived to specialize operationally and administratively, aiming to use production factors efficiently. This process brings about the professionalisation causing the ownership and the control to be polarized in the firms. The association

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between these two polarized groups seems to be directed by the mutual interest at first, whereas it turned into a conflict, owing to fact that the executives having expertise and the power of control chase their own interests. Similarly, there also exists a conflict between the majority and the minority shareholders, resulting from capital shares allocated imbalancedly for various reasons in aggregate corporations. The majority shareholders generate greater excess earnings because of the special knowledge.

These conflicts are called as agency problems in the literature. Agency costs largely damage firms’ survival, having impact on their financial structure. Bringing about the untrustable environment, this hinders market development. Various institutions have imposed some regulations to solve agency problems and hence to create a trustable environment by enhancing firms’ continuity. There also have been many studies which resonate with this crucial issue, proposing some precious solutions to the agency problems. The concept of corporate governance (henceforth CG) has been originated from these valuable efforts. Yet, those efforts bringing about CG do not incorporate coercive rules. Thus, firms display divergence regarding CG practices. In this context, a sample of the firms trading in Istanbul Stock Exchange (henceforth ISE) was employed to investigate the determinants of CG level and its influences on the firm performance.

2. Literature Review

They are not usually same who place funds and those who manage in the corporations. This distinction can be the most essential point that reveals the need of CG (Stuart, 2006). It is not always possible for both capital owners and those having control power to strive for common interests simultaneously. The self-interests of principal partners and senior executives may sometimes dominate the others. While senior executives serving their self-interests can manipulate earnings, shareholders and executives who have control can transfer the funds to other companies they own by means of transfer pricing or asset stripping (La Porta et al., 2000).

In that context, Aren (2009) in his empirical study on ISE provided evidence that several accounting practices known as earnings management (henceforth EM) have been appealed, succeeding the management change seen in the companies. Leuz et al. (2003) in their study, encompassing 31 countries, proposed that EM practices are less likely to be seen in the countries in which have developed stock markets, strong investor protection and more dispersed ownership. In their study conducted in 49 countries, La Porta et al. (1998) mentioned about the relationship between the legal investor protection and the law system in a country. Accordingly, there exists a strong investor protection in countries having common-law system such as UK and USA, and a weak investor protection in those having civil law system. Additionally, they added the ownership concentration (henceforth OC) is considerably high especially in countries that gave no investor protection.

Shleifer and Vishny (1997) manifested that OC was significantly effective in solving the problems suggested by agency theory. It is also pointed out that however highly OC minimized agency problems, principal partners who having control violated rights of minority shareholders by giving priority to their self-interests. La Porta et al. (1999) examined the ownership structure and the shareholders having control in large companies and stated that firms except those which had strong shareholder protection were mostly family or publicly owned. Also, it was seen that firms were not common whose equities were controlled by financial intermediaries. The studies conducted in Turkey, as another country which gave weaker investor protection (La Porta et al., 1998), also supported these findings. Demirag and Serter (2003) expressed that the OC was very high in Turkey and that firms were controlled by families. The same study drew the conclusion that pyramidal structure of ownership and big business group gave more
control to the firm shareholders than the cash flows did. Shinong et al. (2009) stated no relationship between ownership and legal investor protection in terms of firms controlled by the state and that the state has protected other investors’ rights by conducting monitoring activities on firms through its force.

This is especially the case in companies in Europe and Asia which shareholders had more control because of pyramidal structure of ownership (Levy, 2007). Faccio and Lang (2002) drawn conclusion that controlling shareholders increased their control power in several ways. Dyck and Zingales (2004) and Leuz et al. (2003) provided evidence that having control power on a firm has provided some private benefits for shareholders.

Delgado-Garcia et al. (2010) stated that the presence of majority shareholders in firms inferred as a power of control and that this was perceived negatively by other shareholders in case of malicious handling. Moreover, some studies (Ruiz-Mallorquí & Santana-Martin, 2011) claimed a negative (positive) relationship between banking institutions (investment funds) as a dominant shareholder and firm value (henceforth FV). The reason for these effects was suggested that firm managers who made an agreement with bank managers might use firm's funds for their private goals and that investment funds took measures for activities which decrease the firm performance. Mizuno (2010) expressed that CG practices would be improved qualitatively when corporate investors (henceforth CI) are present.

Who owns control in a firm is very crucial issue for creditors. It can shift borrowing costs, based on firm risk. Hence, it can influence on firm performance. Anderson et al. (2003) found that in firms having founding family ownership structure, borrowing reduced agency costs. Similarily, they added that the presence of independent board of directors had same effect on these costs.

Kim et al. (2007) found a negative (positive) association between minority shareholder rights in a country and ownership structure (board independence in a firm). Also, they concluded that stronger legal protection of investor in a country was related to more independent board members in firms. Mangena and Tauringana (2007), in their research on Zimbabwe Stock Exchange, the second big stock market in Africa, they found that the ratio of CI ownership, the percentage of non-executive directors and the number of independent auditing members were positively related to shares owned by foreigners. Bae and Goyal (2010) stated that foreign shareholders are considerably high in firms whose CG is stronger. Linck et al. (2008) stressed that FV, debt ratios, financial performance and being operated in different fields are associated with the size of independent board and with the number of independent members. Further, Aren et al. (2012) displayed a negative relation between dept ratios and firm profitability in both Taiwan and also Turkey.

3. Methodology

In this study, it is aimed at investigating the effects of CI level, external financing needs and FV, all of which enhance CG level excluding legal regulations. On the other hand, it is intended to examine possible relations depending on whether the improvements in CG level have impact on firm’s financial performance and being preferred by foreign investors.

The study sample included 162 firms traded continuously on ISE on all indexes, excluding sportive and financial indexes. This research based on the secondary data relating firms. Relevant data such as FV, external financing needs, firm performance and EM were accessed through Finnet Analiz (Excel Add-In) Database while information about corporate and foreign investors were obtained from yearly statistical reports on MKK (MKK is the central securities depository for capital market instruments which are decided by Capital Markets Board of Turkey to be dematerialized). Lastly, CG data were acquired by compliance reports on firm websites.
3.1. Research Model and Hypotheses

CIIs aiming at securing their investment returns demand firms for improving CG level such as independent auditing boards (Mizuno, 2010). Additionally, CIIs make an effort to increase their auditing activities on firms in order to attain more investment return (Brav et al., 2008; Del Guercio and Hawkins, 1999, cited in Hadani et al., 2011; Mande et al., 2012). Thus, the hypothesis derived from here;

**H1: The presence of CIIs in the firm increases firm’s level of CG.**

Chen et al. (2010) found a negative relation between external financing needs and FV. Ruiz-Mallorquí and Sanatana-Martin (2011) determined a positive relation between FV and the presence of banks as controlling shareholders or the second/third big partner. Similarly, Baek et al. (2004) indicated a positive association between CIIs and FV. Accordingly, following hypothesis derived;

**H2: There is a positive relationship between no external financing needs and existence of CIIs and firm size.**

Mande et al. (2012) pointed out that small firms had lower CG levels owing to inadequate monitoring by the public. Aksu and Kosedag (2006) reported that large firms would improve their CGs since they were monitored especially by financial intermediaries. Linck et al. (2008) and Coles et al. (2008) stressed that firms with higher FV are more likely to enlarge their boards and to increase independent members in those boards. Thus, the hypothesis starting from this,

**H3: There is a positive relationship between firm size and CG level.**

Mizuno (2010) and Mande et al. (2012) indicated a positive relation between CI ratio and CG level. Linck et al. (2008) and Guest (2008) referred a positive relation between FV and CG. Ruiz-Mallorqui and Santana-Martin (2011) mentioned about a positive association between CI ratio and FV, known as the determinants of CG level. Additionally, Guest (2008) pointed that FV is a crucial determinant of CG level. Both these triple relations existed among them and FV being an important determinant of CG level raised doubts whether FV mediates CI ratio on CG level. Accordingly, the following hypothesis;

**H4: FV mediates CI ratio on CG level.**

Theoretically, the relationship between CG and financial performance depend upon agency problems among shareholders originating from information asymmetry (Jensen and Meckling, 1976). La Porta et al. (1999) reached findings that controlling shareholders with a motive to preserve their earnings can exploit firm’s resources, leading to a decrease in firm value. Beside, Gompers et al. (2003) expressed that CG level in firms related to stock return. Klapper and Love (2004) determined a relationship between CG level and firm’s both Tobin’s Q and ROA. Kula (2005) reported a relation between the separation of CEO and executers and firm performance. Starting from here, the hypothesis;

**H5a: When CG level increases, firm profitability (EBIT/Total Assets) increases too.**

**H5b: When CG level increases, firm’s Tobin’s Q ratio increases too.**

Lack of transparency in firms may leads to problems based on information asymmetry. These problems cause an increase of risk premium in calculation of return on investment. Hence, foreign investors would make their investment preferences on those firms with lower information asymmetry (Jiang ve Kim, 2004). Beside, Mangena and Tauringana (2007) and Barniv and Bao (2009) expressed that foreign investors took firms’ CG mechanisms into consideration while choosing their investments. Accordingly, the subsequent hypothesis;

**H6: When CG level increases in the firm, foreign investors in a country make more preferences on that firm.**

Klapper and Love (2004) and Gompers et al. (2003) stated that CG practices improved firm performance thereby reducing firm’s agency costs. Hazarika et al. (2012) and Hadani et al. (2011) pointed
out that EM practices in firms increased agency costs. Hence, agency costs were apparent in firms practicing EM and improving CG practices in these firms whose agency costs are apparent were more effective in enhancing firm performance than those having inapparent agency costs. Accordingly, the next hypotheses:

- **H7a**: EM activities in decreasing earnings way moderates CG on firm performance (EBIT/Tot.Ass.)
- **H7b**: EM activities in decreasing earnings way moderates CG on firm performance (Tobin’s Q).

The research model encompassing the hypotheses is depicted below.

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**Table 1: Variables in the Research Model**

<table>
<thead>
<tr>
<th>Variable</th>
<th>CALCULATION</th>
<th>REFERENCES</th>
<th>CITED BY</th>
</tr>
</thead>
<tbody>
<tr>
<td>Corp. Investor Ratio</td>
<td>Corporate Investor Stocks / Total Stocks</td>
<td>M KK and Finnet Analysis (Excel Add-In) Database</td>
<td>Mizuno, (2010)</td>
</tr>
</tbody>
</table>
| CG Level              | 1. ‘1’, if the number of board members of related firm greater than the sample, otherwise ‘0’  
2. ‘1’, if the number of non-executor members greater than executor members in related firm ‘1’, otherwise ‘0’  
3. ‘1’, if independent members having qualifications specified by Capital Market Board exist in related firm, otherwise, ‘0’  
4. ‘1’, related firm establish a corporate governance committee in their independence board, otherwise, ‘0’  
5. ‘1’, the same person does not hold director of both independent board and also executive board, otherwise ‘0’  
6. ‘1’, related firm gets the independence auditing service from Price Waterhouse Coopers, Deloitte Touche Tohmatsu, Ernst & Young and KPMG, known as the big four, otherwise, ‘0’  
 Max. 6 Points | Firms’ websites                                                               | Firms’ websites                                                          |
| EM                    | Modified Jones Model                                                        | Finnet Analysis (Excel Add-In) Database                                    | Aren (2003)                                                              |
| Firm Performance      | ROA and Tobin’s Q                                                           | Finnet Analysis (Excel Add-In) Database                                    | Klapper and Love, 2004                                                   |
| Foreign Investor      | Foreign investor shares / total foreign investor shares in the stock market | MKK                                                                        | Mangena and Tauringana, 2007                                             |
| Preference            |                                                                               |                                                                           |                                                                          |
3.2. Analysis

In this section, the research hypotheses will be tested successively in an effort to search their precision and the findings relating to validation of the model will be discussed.

**H1: The presence of CIs in the firm increases firm’s level of CG.**

To test this hypothesis, simple regression model is given below in equation (1).

\[
CGL_{it} = \beta_1(CIR)_{it-1} + \epsilon_{it-1}
\]  

(1)

In the regression model above, the subscripts t-1 and t represent years 2009 and 2010 respectively.

Table 2. Regression Analysis Results of Corporate Investor Ratio on CG Level

<table>
<thead>
<tr>
<th>REGRESSION ANALYSIS</th>
<th>VARIABLES</th>
<th>β</th>
<th>P</th>
<th>R²</th>
<th>P</th>
</tr>
</thead>
<tbody>
<tr>
<td>Dependent Variable</td>
<td>CG Level</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Independent Variables</td>
<td>Corporate Investor Ratio</td>
<td>0.798</td>
<td>0.000</td>
<td>0.634</td>
<td>0.000</td>
</tr>
</tbody>
</table>

The regression results show a statistically significant relation between CI ratio and CG level. Beside, the model is significant overall and CI ratio is explaining nearly 64% of the total variation in CG level. An increase of one point in CI ratio causes an increase of 0.798 in CG. Thus, H1 is supported.

**H2: There is a positive relationship between no external financing needs and existence of CI and firm size.**

The simple regression model to test related hypothesis can be seen in equation (2) below.

\[
\ln(FV)_{it} = \beta_1(CIR)_{it-1} + \beta_2(EFN)_{it-1} + \epsilon_{it-1}
\]  

(2)

Table 3. Regression Analysis Results of Corporate Investor Ratio, External Financing Needs on Firm Value

<table>
<thead>
<tr>
<th>REGRESSION ANALYSIS</th>
<th>VARIABLES</th>
<th>β</th>
<th>P</th>
<th>R²</th>
<th>P</th>
</tr>
</thead>
<tbody>
<tr>
<td>Dependent Variable</td>
<td>Firm Value</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Independent Variables</td>
<td>Corporate Investor Ratio</td>
<td>0.632</td>
<td>0.000</td>
<td>0.430</td>
<td>0.000</td>
</tr>
<tr>
<td></td>
<td>External Financing Needs</td>
<td>-0.130</td>
<td>0.032</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Being significant at the 0.000 observed level, 43% of total variation in FV is explained by CI ratio and external financing needs. Individually, if CI ratio (external financing need) increases (decreases) by 1 unit, then FV increases by 0.63 (0.13) unit. CI ratio (external financing need) is significant at 0.000 (0.05) observed levels. As a result, the hypothesis H2 is supported.

**H3: There is a positive relationship between firm size and CG level.**

The simple regression model specified to test the related hypothesis is given in equation (3).

\[
CGL_{it} = \beta_1(\ln(FV))_{it-1} + \epsilon_{it-1}
\]  

(3)

Table 4. Regression Analysis Results of Firm Value on CG Level

<table>
<thead>
<tr>
<th>REGRESSION ANALYSIS</th>
<th>VARIABLES</th>
<th>β</th>
<th>P</th>
<th>R²</th>
<th>P</th>
</tr>
</thead>
<tbody>
<tr>
<td>Dependent Variable</td>
<td>CG Level</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Independent Variables</td>
<td>Firm Value</td>
<td>0.911</td>
<td>0.000</td>
<td>0.828</td>
<td>0.000</td>
</tr>
</tbody>
</table>

As seen on Table 4, nearly 83% of total variation in CG level is explained by FV. 1% change in FV causes a change of 0.911 in CG level. It can be seen that FV is a crucial determinant of CG level.

**H4: FV mediates CI ratio on CG level.**

As known, for the presence of any mediating variable, it is necessary that there must be relations denoted by I, II ve III in figure 2 and that the relation denoted by III must be decreasing or completely disappearant after the inclusion of the mediating variable (Demircan, 2003 cited in Alpkan et al., 2005).
Table 5. Results of Correlation Analysis Between Corporate Investor Ratio, Firm Value and Corporate Governance Level

<table>
<thead>
<tr>
<th>CORRELATION ANALYSIS</th>
<th>Corporate Investor</th>
<th>Firm Value</th>
<th>Corporate Governance Level</th>
</tr>
</thead>
<tbody>
<tr>
<td>Corporate Investor Ratio</td>
<td>1</td>
<td>0.648**</td>
<td>0.375**</td>
</tr>
<tr>
<td>Firm Value</td>
<td>0.648**</td>
<td>1</td>
<td>0.516**</td>
</tr>
<tr>
<td>Corporate Governance Level</td>
<td>0.375**</td>
<td>0.516**</td>
<td>1</td>
</tr>
</tbody>
</table>

** Correlation is significant at the 0.01 level.

On Table 5, it seems that, CI ratio, FV and CG level are significantly correlated at 99% level. Following this analysis, the regression results produced from equation (4) are reported below.

\[
CGL_{it} = \beta_1 \ln(FV)_{it-1} + \beta_2 CIR_{it-1} + \epsilon_{it-1}
\]  

Table 6. Regression Analysis Results of Corporate Investor, Firm Value on CG Level

<table>
<thead>
<tr>
<th>REGRESSION ANALYSIS</th>
<th>VARIABLES</th>
<th>( \beta )</th>
<th>P</th>
<th>( R^2 )</th>
<th>P</th>
</tr>
</thead>
<tbody>
<tr>
<td>Dependent Variable</td>
<td>CG Level</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Independent Variables</td>
<td>Corporate Investor Ratio</td>
<td>0.07</td>
<td>0.433</td>
<td>0.259</td>
<td>0.000</td>
</tr>
<tr>
<td></td>
<td>Firm Value</td>
<td>0.47</td>
<td>0.000</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Although CI ratio was significant at the model in context of the hypothesis H1, it is not significant at nearly 0.5 observed level because FV mediates this relation. Summarizing the analyses in order to determine CG level, however FV is a substantial determinant of CG level and so is CI ratio individually. FV mediates CI ratio on CG level. Yet, CI ratio and external financing needs have effect on CG level through FV.

\( H5a: \) When CG level increases, firm profitability (EBIT/Total Assets) increases too.

\( H5b: \) When CG level increases, firm’s Tobins Q ratio increases too.

To test the hypotheses H5a and H5b, simple regression models below are specified.

\[
\frac{EBIT}{TA_{it}} = \beta_1 (CGL)_{it} + \epsilon_{it}
\]

\[
Q_{it} = \beta_1 (CGL)_{it} + \epsilon_{it}
\]

Table 7. Regression Analysis Results of Corporate Governance Level on EBIT/Tot. Ass.

<table>
<thead>
<tr>
<th>REGRESSION ANALYSIS</th>
<th>VARIABLES</th>
<th>( \beta )</th>
<th>P</th>
<th>( R^2 )</th>
<th>P</th>
</tr>
</thead>
<tbody>
<tr>
<td>Dependent Variable</td>
<td>EBIT/ Tot. Ass.</td>
<td></td>
<td></td>
<td>0.384</td>
<td>0.000</td>
</tr>
<tr>
<td>Independent Variables</td>
<td>Corporate Governance Level</td>
<td>0.623</td>
<td>0.000</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Table 7 shows the results of testing the hypothesis H5a. 38.4% of total variation in EBIT/Tot. Ass. is explained by CG level, with 0.000 observed or exact level of significance. Hence, H5a is supported.

Table 8. Regression Analysis Results of CG Level on Tobin’s Q

<table>
<thead>
<tr>
<th>REGRESSION ANALYSIS</th>
<th>VARIABLES</th>
<th>( \beta )</th>
<th>P</th>
<th>( R^2 )</th>
<th>P</th>
</tr>
</thead>
<tbody>
<tr>
<td>Dependent Variable</td>
<td>Tobin’s Q</td>
<td></td>
<td></td>
<td>0.275</td>
<td>0.000</td>
</tr>
<tr>
<td>Independent Variables</td>
<td>CG Level</td>
<td>0.529</td>
<td>0.000</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Similarly, CG level explains 28% of total variation in Tobin’s Q with 0.000 observed level of significance. Hence, the hypothesis H5b is supported.

\( H6: \) When CG level increases in the firm, foreign investors in a country make more preferences on that firm.

Table 9. Regression Analysis Results of CG Level on Total Foreign Investor Share

<table>
<thead>
<tr>
<th>REGRESSION ANALYSIS</th>
<th>VARIABLES</th>
<th>( \beta )</th>
<th>P</th>
<th>( R^2 )</th>
<th>P</th>
</tr>
</thead>
<tbody>
<tr>
<td>Dependent Variable</td>
<td>Total Foreign Investor Share</td>
<td>0.355</td>
<td>0.000</td>
<td>0.121</td>
<td>0.000</td>
</tr>
<tr>
<td>Independent Variables</td>
<td>CG Level</td>
<td>0.355</td>
<td>0.000</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
As seen above, the effect of CG level in a firm on preferences of foreign investors in a country is significant at 0.000 observed level of significance. Moreover, CG level explains 12.1% of total variation in total foreign investor ratio.

H7a: EM activities in decreasing earnings way moderates CG on firm performance (EBIT/Tot.Ass.)
H7b: EM activities in decreasing earnings way moderates CG on firm performance (Tobin’s Q).

To determine firm’s EM activities, Modified Jones Model is employed. In the light of this model, discretionary accruals of each firm were calculated, searching for EM activities’ direction. It is expected that the activities in the direction of reducing earnings (negative discretionary accruals) in t-1 period-one year before when CG level calculated- would increase earnings together with the CG level in t period. Firstly, firms were divided in two groups: whose discretionary accruals is smaller than zero and greater than zero.

Table 10. One Sample T Test Results

<table>
<thead>
<tr>
<th></th>
<th>Mean</th>
<th>Test Value</th>
<th>t</th>
<th>p</th>
</tr>
</thead>
<tbody>
<tr>
<td>Firms whose discretionary accruals are below than “0”</td>
<td>-0.0341910</td>
<td>0</td>
<td>1.901</td>
<td>0.074</td>
</tr>
</tbody>
</table>

As seen, at 0.10 exact significance level, discretionary accruals mean is different from ‘0’, the mean in case of no EM activities. This finding leads to analyzing the relationship between CG level and both EBIT/Tot. Ass. and also Tobin’s Q in firms having EM facilities in earning reducing way in 2009.

Table 11. Regression Analysis Results of CG Level on EBIT/ Tot.Ass.

<table>
<thead>
<tr>
<th>REGRESSION ANALYSIS VARIABLES</th>
<th>β</th>
<th>P</th>
<th>R²</th>
<th>P</th>
</tr>
</thead>
<tbody>
<tr>
<td>Dependent Variable</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>EBIT/ Tot.Ass.</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Independent Variables</td>
<td>CG Level</td>
<td>0.871</td>
<td>0.000</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>0.745</td>
<td>0.000</td>
</tr>
</tbody>
</table>

As seen on Table 11, the coefficient of CG level in the context of the model encompassing H5a increased to 0.871 from 0.623. Last, H7a is supported. Below, Table 12 shows H7b is supported as well.

Table 12. Regression Analysis Results of Corporate Governance on Tobin’s Q

<table>
<thead>
<tr>
<th>REGRESSION ANALYSIS VARIABLES</th>
<th>β</th>
<th>P</th>
<th>R²</th>
<th>P</th>
</tr>
</thead>
<tbody>
<tr>
<td>Dependent Variable</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Tobin’s Q</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Independent Variables</td>
<td>Corporate Governance Level</td>
<td>0.823</td>
<td>0.000</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>0.658</td>
<td>0.000</td>
</tr>
</tbody>
</table>

4. Conclusion

Currently, the structures of the ownership and the control diverge from each other owing to fact both that firms have been growing and also that the need of senior executives is increasing. This divergency grounding on mutual benefits at first leads to the conflict of interest in several ways in the firm since senior executives with controlling power exploit their private knowledge for their self interests. Agency problems originated from this discrimination between the ownership and the control causes serious damages to firms. To reduce the costs stemmed from these problems, a variety of individuals and institutions gave some suggestions and made arrangements, all of which created the concept of CG.

In our study, the determinants and the effects of CG has been investigated on a sample of firms traded on ISE. In this direction, study’s theoretical model has formed in line with the relationships in extant literature. In the research model, CI ratio, firm size, external financing needs are supposed as the determinants of CG level and an array of tests has been made in searching for these presuppositions to be supported or not. On the other side, the effects of CG level have been identified through the analyses of
the relationships between CG level, firm performance and foreign investor preferences. Hence, it was found that FV-hence firm size- is the most crucial determinant of CG in firms. Parallel with literature, this finding can be interpreted in way that firms choose improving their CG level in order not to damage their institutional reputation. Moreover, it is seen that CI ratio is another major determinant of CG level. The indirect effect of CI ratio on CG level is conveyed through FV since it mediates this relation. Namely, CI ratio together with external financing needs can effect CG level only through FV. The results also exhibited that CG level enhances firm performance. Beside, this effect was moderated by appearance of agency costs after EM facilities in last year. Firms can improve their financial performance via CG practices in the same way which they eliminate the costs stemmed from interest conflicts related asymmetric information. Last, it is also concluded that foreign investors take the firm’s CG level into account on their firm preferences.

This study remained limited with the firms only traded on ISE regarding both the access to financial statements, the information about independence board structure of firms and also acquisition of the knowledge on their foreign investors’ share. Turkish Commercial Code newly enacted by 2012 necessitates all firms to report their financial statements. This enables working with larger samples in the future, giving way to reach more generalizable results. Future studies can carry our study furher if they take this change into account.

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