

**THE IMPACT OF CORPORATE GOVERNANCE RATINGS ON FINANCIAL PERFORMANCE IN DEVELOPING COUNTRIES: A NEW EVIDENCE FROM TÜRKİYE**Assoc. Prof. Mustafa KEVSER (Ph.D.)<sup>\*</sup> Seda DOĐAN (Ph.D.)<sup>\*\*</sup> **ABSTRACT**

*The aim of this study is to analyze the impact of Corporate Governance Rating (CGR) on the Financial Performance (FP) of companies listed on the Borsa Istanbul Corporate Governance Index (BIST CG Index) in Türkiye. In this study, 16 firms traded in the BIST CG Index and having a CGR between 2009 and 2023 are evaluated. Return on Assets (ROA), Return on Equity (ROE), Earnings Per Share (EPS), Earnings Before Interest and Taxes (EBIT) and Financial Leverage (FIN-LEV) Ratios are the dependent variables, while the independent variable is CGR. Correlation and panel Granger causality analyses were applied to the 209 observation values obtained from the data. According to the results there is a significant and negative relationship between CGR and ROA, ROE, EBIT and FIN-LEV. Panel Granger causality test results shows the existence of a unidirectional causality relationship from CGR to EPS. There is no causality relationship between CGR and ROA, ROE, EBIT and FIN-LEV. Our findings suggest that, unlike prevailing literature, CGRs may impose structural costs on firm performance in Türkiye, especially in developing markets. The results are important as they show that compliance with CGR is a cost factor for Türkiye. Accordingly, policymakers in Türkiye should provide more support and incentives to businesses in terms of CG practices and make regulations that will remove the negative impact on their financial structures.*

**Keywords:** Corporate Governance Rating, Financial Performance, Profitability, Granger Causality.

**Jel Codes:** G30, G32, M14, O16.

\* Bandırma Onyedi Eylül University, Manyas Vocational School, Department of Finance, Banking and Insurance, Balıkesir/Türkiye, mkevser@bandirma.edu.tr.

\*\* Anadolu University, Institute of Social Sciences, Eskişehir/Türkiye, seddogan85@gmail.com.

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## 1. INTRODUCTION

The concept of CG emerged in response to the lack of effective oversight by management boards in the 1970s, aiming to address issues of poor performance (Lu and Lai, 2023). CG encompasses the entirety of relationships between firm managers and its owners, employees, and stakeholders while performing their duties (Ülgen and Mirze, 2004). The most general definition of this concept is known as ‘rule-based corporate management’ (Aktan, 2013). According to this notion, management decisions should adhere to established rules within the organization rather than relying solely on the discretion of managers. In this context, the concept embraces principles of fairness/equality, transparency, accountability, and responsibility in firm management. It also embodies a governance philosophy that prioritizes the will creating the most suitable balance among stakeholders and shareholders for the sustainable operation of the firm.

In 1997, numerous scandals in the Asian financial markets led to a financial crisis. In the United States (US), CG garnered significant attention following the Enron scandal in 2001 and the WorldCom scandal in 2002 (Lu and Lai, 2023). The US implemented the ‘CG Quality’ scoring system in 2002 to evaluate governance practices of its firms, which was later expanded in 2004 to include European and Asian firms (Lysandrou and Parker, 2011). In Türkiye, the CG Index (XKURY) was established on August 31, 2007, within the scope of the Istanbul Stock Exchange (IMKB). The practice of CGR began in 2007. The purpose of establishing the index was to recognize and publicize companies that adhere to CG principles and implement them correctly, gaining recognition from investors and the public. Additionally, the number of firms listed in the Türkiye CG Index increased from 7 in 2007 to 52 in 2014 (Gürarda, Özsös and Ateş, 2016). By 2024, the number of firms in the index had reached 73.

In the aftermath of these crises, academics have focused on the importance of CG, which comprises processes, practices, and policies that govern a firm’s formal decision-making and management. Consequently, CG has become a central theme in management and financial accounting literature over the past two decades, with a particular emphasis on its impact on performance (Lu and Lai, 2023).

Even though past FP is considered in predicting future FP, it is not the sole factor (Donker and Zahir, 2008). Major scandals resulting from the improper implementation of CG are among the factors that have shaken confidence in capital markets. As a result, CG has risen to the top of the agenda for business and political leaders (Hussainey and Al-Najjar, 2012).

CGRs have become increasingly influential and popular among stakeholders due to their role in monitoring management effectiveness, preventing irregular and inappropriate behavior, ensuring legal compliance, and serving as an important criterion for investors’ decision-making (Hussainey and Al-Najjar, 2012; Epps and Cereola, 2008). In this context, global institutions such as the Organisation for Economic Co-operation and Development (OECD), the International Finance Corporation (IFC), and

the World Bank (WB) have emphasized the development of various regulations, guidelines, and good governance codes (Epps and Cereola, 2008).

The primary purpose of a rating is to assess and compare companies' governance scores against standards within a specific corporate context (Al-Malkawi, Pillai and Bhatti, 2011). Accordingly, firms that develop responsible CG systems restrict managerial discretion, safeguard minority shareholder rights, and minimize the abuse of control power by majority shareholders (Donker and Zahir, 2008). In this regard, CGRs prepared by independent organizations are actively utilized by stakeholders for analyzing institutional risks (Waqar and Ma, 2023).

Additionally, several theories influence CG. Among the most important are corporate theory, agency theory, stewardship theory, and stakeholder theory. Corporate theory integrates a broader understanding of the cultural dimensions and formal factors of a firm in a modern society (Davis, 2005). Therefore, CG can be significantly influenced by institutional factors such as culture, legal frameworks, and financial markets (Briano-Turrent and Rodriguez-Ariza, 2016). Agency theory highlights the conflict of interest between management and owners due to the separation of ownership and control. This theoretical approach suggests that firms should adopt internal and external mechanisms of CG to minimize differences and reduce agency costs (Tariq and Abbas, 2013; Haniffa and Hudaib, 2006). Stewardship theory presents positive views on the role of managerial ownership in reducing representation conflicts between managers and owners (Jensen and Meckling, 1976). Stakeholder theory is based on two principles. The first is to determine 'what the firm's purpose is,' while the second is to determine 'what responsibilities management has towards stakeholders.' Thus, the firm can improve its performance and relationships with stakeholders (Ertuğrul, 2008).

This article examines whether the CGR of companies listed on the Türkiye Borsa Istanbul CG Index affects FP. The study evaluates the period from 2009 to 2023 for 16 firms included in the CG index. Additionally, by covering a longer period than previous studies and including different variables such as Earnings Before Interest and Taxes (EBIT), this research provides new empirical evidence to the literature. In this context, the contributions of the research can be listed as follows: i) the research covered a longer period compared to previous studies, ii) the research focused on many FP indicators at the same time, iii) the research included different FP indicators such as EBIT in the analysis and made a versatile contribution to the literature. iv) Unlike previous studies, CGR was considered a single rating score calculated by integrating subcomponents and analysing the FP relationship. Correlation analysis and panel Granger causality analyses are applied to test the hypotheses. The primary aim of the study is to determine the relationship between CGR and FP and provide recommendations to policymakers.

The rest of the study is structured as follows: The first section begins with an introduction, emphasizing the importance of the subject. The second section includes a literature review and develops

the hypotheses of the study. The third section explains the methodology. The fourth section elaborates on the research findings in detail, while the fifth section presents the conclusion.

## **2. LITERATURE REVIEW AND HYPOTHESES DEVELOPMENT**

CGR have become extensively used in the governance-performance literature by many researchers. The main reason for that is many prior empirical researches have showed the effect of CG on FP (Kevser, Tunçel, Gürsoy and Zeren, 2023; Velte, 2017). At this point, we benefit from stakeholder theory and agency theory when explaining the nexus between CG and FP. Accordingly, the results obtained from the research are evaluated within the framework of these theories. Stakeholder theory suggests that the company should establish strong relationships with internal and external stakeholders who benefit from it for better FP. It claims that will be possible with successful corporate management (Freeman, 1984). Besides, agency theory states that conflicts of interest will arise between managers and partners in growing companies and that managers will prioritize their interests, and claims that conflicts of interest will be prevented. FP will be increased with good CG (Jensen and Meckling, 1976; Ross, 1973). Accordingly, while strong CG serves the purpose of better FP by reconciling the expectations and interests of many stakeholders, the CGR is also considered an indicator of good CG. Kumar and Singh (2013) showed a negative relationship between board size and firm value in their study conducted on 176 Indian firms listed on the BSE 200 Index. Verma (2022) examined the effects of factors on FP by considering CGRs as a single score and subcategories. While the findings didn't determine a significant relationship between economic performance and sub-dimensions, they showed a significant relationship with CGR. Hussainey and Al-Najjar (2012) analyzed nexus among the quality of CG practices and financial distress in UK firms. They found that profitability was associated with company's CGRs. Kaewkerd and Soonthonrot (2020) examined the relationship between FP and CG in Thailand Stock Exchange which they evaluated in five categories. The findings exhibited that only board size has a significant relationship with investor confidence rate and ROE. Chan, Watson, and Woodliff (2014) observed that research in corporate social responsibility increased CGRs and led to higher leverage as ratings improved. However, Dwivedi and Jain (2005) found a positive relationship between board size and market value for Indian firms in their study. Diwakar and Sahu (2023) examined whether there is a positive relationship between ROA, ROE and Return on Capital Employed (ROCE) and CGRs of Indian companies. Researchers have used firms' governance ratings for CG performance. The findings showed a strong positive correlation between FP and CGR. Mishra and Kapil (2017) concluded that board size, a category of CGR, had a positive impact on accounting-based performance indicators. Velte (2019) examined the impact of environmental, social and governance (ESG) dimensions on earnings management. The study concluded that ESG performance has a negative impact on accrual-based earnings management, however, the statistically significant negative impact on accrual-based earnings management belongs to governance performance. Using a sample of 300 companies from 14 European nations, Renders, Gaeremynck, and Sercu (2010) found that CGRs were positively correlated with

Tobin's Q, price-to-sales ratio, market-to-book value, return on equity, and return on assets. Better CG was associated with higher market-to-book value for European companies, according to Schauten, Van Dijk, and van der Waal (2013). Velte (2017) found a positive relationship between the profitability of German companies and CGRs. Mutairi, Tian, Hasan and Tan (2012) investigated the impact of the ownership of financial managers of companies operating on the Kuwait stock exchange within the framework of CG. The results showed that company managers try to maximize their profits and senior managers are the largest stakeholders. The results are remarkable in terms of supporting agency theory. Taliento, Favino, and Netti (2019) analyzed a sample of 150 firms from Belgium, France, Germany, Italy, and Spain in the same sector and found that only one firm's FP was positively affected by CGRs compared to other firms. Larcker, Richardson, and Tuna (2007), in their research using 2106 companies and 14 CG tools, determined that CG tools affect company performance and stock returns. Lu and Lai (2023) investigated the relationship between CGRs and firm performance in Taiwan from 2014 to 2018. They compared TWSE CG evaluations based on five sub-indices- Protecting Shareholders' Rights and Interests, Equal Treatment of Shareholders, Improving Board Formation and Operation, Enhancing Information Transparency, and Implementing Corporate Social Responsibility- with firms' profitability, return on equity, and earnings per share-based performance measures. The results showed that firms with higher CGRs performed better in Taiwan. Bai, Liu, Lu, Song, and Zhang (2006) examined the relationship between CG mechanisms and market values of publicly traded companies in China. Researchers created a CG index to summarize information on CG variables and found that the index has significant effects on market valuation. Additionally, the results suggest that investors pay a significant premium for well-managed firms in China. Berthelot, Morris, and Morrill (2010) examined whether investors considered CGRs published by "The Globe and Mail," a recognized Canadian newspaper, in their stock price evaluations. The research findings suggested that investors did take CGRs into account when evaluating stock prices and that certain components of CG were associated with accounting outcomes. In this context, the general consensus in the majority of studies is that there is a positive relationship between governance ratings and FP (Chen and Kao, 2010). Kevser and Doğan (2021) examined the relationship between CGR and stock returns in BIST and found a positive relationship between CGR and stock returns.

According to Briano-Turrent and Rodriguez-Ariza (2016), CGRs have been deemed beneficial in creating a rating or index and integrating various elements of a firm's governance system into a single score. Despite the generally positive and favorable implications of CG on performance, Donker and Zahir (2008) conducted research on the most popular CGR systems. They particularly focused on the methodology used by rating agencies to establish CG practices. Examining the categories and variables used in ratings, Donker and Zahir criticized the reduction of a complex CG process into a single score, suggesting its weakness in enhancing FP. In this study, considering Donker and Zahir's criticisms from 2008 alongside the consistent positive findings of all other studies, the research will proceed. However,

this study will treat CGRs, without disaggregating into subcomponents, following the research of Renders et al., (2010), Schauten et al., (2013), Taliento et al., (2019), and Velte (2017). Additionally, in line with Briano-Turrent and Rodriguez-Ariza's (2016) perspective, this study will treat CGRs as integrated representations of various elements into a single score. Furthermore, the study will incorporate the Earnings Before Interest and Taxes (EBIT) value, unlike previous research, following the studies of Hussainey and Al-Najjar (2012), Chan et al., (2014), Mishra and Kapil (2017), Renders et al., (2010), Velte (2017), and Lu and Lai (2023). Consequently, the study aims to investigate the impact of CGRs on FP among firms in Türkiye, a developing country. Therefore, the research aims to examine the relationship between CG and FP and analyze whether good CG leads to better performance in Türkiye. Granger causality analysis is conducted to test the hypotheses developed to explain the relationship between variables. Moreover, the study is significant for examining the relationship between FP and CGRs over the period from 2009 to 2023, adding new empirical evidence to past research. Finally, the study aims to contribute to the literature on Turkish CG by analyzing CGRs alongside Return on Assets (ROA), Return on Equity (ROE), Earnings Per Share (EPS), EBIT, and Financial Leverage (FIN-LEV) ratios within a single framework.

Due to the increasing complexity of the business world, both developed and developing countries are placing more trust in the private sector as the engine of growth. Consequently, investors expect CGRs to be incorporated into firm returns or values as these ratings provide information to investors (Lu and Lai, 2023). Numerous empirical studies have investigated the impact of CG and FP on developed markets. A significant portion of research indicates that having good CG practices leads to a substantial increase in economic value and firm value, higher productivity, and lower systematic financial failure risk for countries (Aydemir, 2012). Considering these studies and the existing literature, the following hypotheses have been formulated.

- ***ROA, ROE, EPS and EBIT variables***

It is argued that profitable firms disclose more information to investors to demonstrate positive outcomes of their performance (Schleicher, Hussainey and Walker, 2007). Therefore, it is believed that profitable firms are motivated to improve the quality of their CG practices (Hussainey and Al-Najjar, 2012).

Gompers, Ishii and Metrick (2003) and Mutairi et al. (2012) analyzed the relationship between CG and long-term return on equity, firm value, and accounting performance measures. Their analysis findings suggest that well-governed firms have higher equity returns, are more valuable, and exhibit better performance in accounting statements compared to poorly governed counterparts. These findings encouraged investors to consider CG in their investment decisions. Consequently, the increasing importance of CGRs prompted many researchers to establish a relationship between firms' CGRs and

profitability ratios (Wahyudin and Solikhah, 2017; Isiaka, 2014; Ben Amar, Boujenoui and Francoeur, 2011; Ertugrul and Hegde, 2009; Epps and Cereola, 2008; Brown and Caylor, 2006).

- **FIN-LEV Ratio variable**

In signaling theory, it is argued that firms with high financial leverage ratios incur higher monitoring costs. A possible response to reduce these costs for highly leveraged firms is to increase the level of disclosure regarding CG practices to meet the needs of creditors. This suggests a positive relationship between financial leverage and CGRs. Additionally, previous research indicates that a high-quality CG system lowers the cost of debt financing.

**Table 1. Hypotheses Developed for Causality Analysis**

<b>H1:</b> <i>Hypotheses</i>	<b>H1a:</b> <i>There is a causal relationship between CGR and ROA.</i>
	<b>H1b:</b> <i>There is a causal relationship between CGR and ROE.</i>
	<b>H1c:</b> <i>There is a causal relationship between CGR and EPS.</i>
	<b>H1d:</b> <i>There is a causal relationship between CGR and EBIT.</i>
	<b>H1e:</b> <i>There is a causal relationship between CGR and FIN-LEV.</i>

### 3. DATASET, METHODOLOGY

#### 3.1. Dataset and Methodology

This study aims to analyze whether the CGR affects the FP of companies listed on the BIST CG Index. The main population of the study consists of 73 firms listed on the BIST CG Index, and the sample comprises 16 firms that regularly disclosed their CGRs between 2009 and 2023. The years during which these firms disclosed their CGRs to the public are indicated in Table 1. The data obtained from these firms provide a total of 209 observations for potential use in the study. However, banks, holdings, financial, and insurance companies were excluded from the sample due to their highly diversified and regulated financial statements. The data regarding the explanatory variable, CGR, were collected from sustainability and integrated reports published on the firms' websites. Financial indicators forming the dependent variables were sourced from financial statements available on isyatirim.com. To ensure objectivity and statistical reliability, quantitative analysis methods such as correlation and panel Granger causality analysis were applied to the structured dataset.

**Table 2. Companies Included in the Study**

	<b>CODES</b>	<b>FIRMS</b>	<b>YEARS</b>		<b>CODES</b>	<b>FIRMS</b>	<b>YEARS</b>
<b>1</b>	<b>AEFES</b>	Anadolu Efes	2009-2023	<b>9</b>	<b>MGROS</b>	Migros Ticaret	2015-2023
<b>2</b>	<b>AKSA</b>	Aksa Akrilik	2014-2023	<b>10</b>	<b>OTKAR</b>	Otokar Otomotiv	2009-2023
<b>3</b>	<b>ASELSAN</b>	Aselsan Elek.	2009-2023	<b>11</b>	<b>PGSUS</b>	Pegasus	2013-2023
<b>4</b>	<b>ARCLK</b>	Arçelik	2012-2023	<b>12</b>	<b>TOASO</b>	Tofaş Türk Otom.	2009-2023
<b>5</b>	<b>COLA</b>	Coca-Cola	2009-2023	<b>13</b>	<b>TTRAK</b>	Türk Traktör	2009-2023
<b>6</b>	<b>DOAS</b>	Doğuş Otom.	2013-2023	<b>14</b>	<b>TUPRS</b>	Türkiye Petrol	2009-2023
<b>7</b>	<b>ENKA</b>	Enka İnşaat	2012-2023	<b>15</b>	<b>TTKOM</b>	Türk Telekom.	2009-2023
<b>8</b>	<b>EREGL</b>	Ereğli Demir	2015-2023	<b>16</b>	<b>VESTL</b>	Vestel Elektronik	2009-2023

### 3.1.1. Correlation and Panel Granger Causality Analysis

Correlation analysis is frequently used in empirical research to reveal the existence and significance of the relationship between variables. In this research, correlation analysis was used to determine the strength and direction of the relationship between the variables. The correlation coefficient resulting from *correlation analysis* is used to interpret the strength or magnitude of the relationship between at least two variables. Additionally, the analysis is applied to determine the direction (positive/negative) and strength of the relationship identified between variables. Furthermore, the measurement values fall between “-1 and +1”. Nevertheless, correlation analysis does not demonstrate the causal relationship between variables (Doğan, 2024).

**The Panel Granger causality analysis** demonstrates whether at least two variables can be defined as dependent and independent variables in the linear relationship formed between them. Moreover, the analysis investigates whether the relationship between variables is unidirectional or bidirectional, or if there is no functional relationship between the variables. In other words, another method of investigating the relationship between two or more interacting variables is to examine their causal relationship. Granger (1969) designed a statistical analysis called the “Panel Granger causality test,” which uses F-tests and t-tests together. According to the assumption of this analysis,  $X_t$  and  $Y_t$  consist of two stationary series. In this regard, the formula for the analysis is as follows;

$$y_t = \alpha + \sum_{k=1}^K \gamma_k y_{t-k} + \sum_{k=1}^K \beta_k x_{t-k} + \varepsilon_t \quad (1)$$

**Source:** Lopez and Weber, 2017: 973.

Whether X causes Y can be analyzed using Formula 1. Even if the previous values of X, along with the previous values of Y, are added to the model, if the previous values of X are significant predictors of the current value of Y, then X has a causal effect on Y. Using Formula 1, the causality relationship can be investigated based on the F-test with the null hypothesis as indicated in Formula 2 (Lopez and Weber, 2017).

$$H_0: \beta_1 = \dots = \beta_K = 0 \quad (2)$$

**Source:** Lopez and Weber, 2017: 973.

If  $H_0$  is rejected, causality from X to Y can be inferred. It is possible to observe bidirectional causality through Granger causality analysis (Lopez and Weber, 2017). Additionally, the probability value in the analysis, if smaller than any predetermined “ $\alpha$ ” value (0.01, 0.05, or 0.10) chosen by the researcher, leads to the rejection of the  $H_1$  hypothesis at that level (Wei, 2016).

### 3.2. Description of the Variables

In this research, there are various FP metrics that will be used as dependent variables. These include:

#### ***Dependent variables***

ROA ratio is used to measure the relationship between profit or earnings and total assets. ROA is a performance metric that indicates to an investor how much profit a company generates from its invested capital in assets (Almazari, 2011). Managers are directly responsible for the firm's operations and thus the utilization of the firm's assets. Therefore, ROA enables investors to evaluate the effectiveness of a firm's CG system in ensuring efficient management of the firm (Lu and Lai, 2023).

$$\text{Return on Assets Ratio} = \frac{\text{Net Profit}}{\text{Average Assets}} \quad (3)$$

#### **Return on assets ratio formula**

ROE is a performance measure that shows investors how much profit a company generates from the money invested by its shareholders. ROE is defined as the ratio of a company's net income for a certain year, minus preferred dividends, to its beginning-of-year equity (common shares) book value. Therefore, ROE serves as a fundamental basis for evaluating a firm's performance (Lu and Lai, 2023).

$$\text{Return on Equity Ratio} = \frac{\text{Net Profit}}{\text{Average Equities}} \quad (4)$$

#### **Return on Equities Ratio formula**

EPS ratio is universally recognized as one of the most important measures and indicators of a company's FP. This ratio measures the overall profitability in terms of the equity stake contributed by owners. Essentially, it is calculated by dividing the 'earnings, i.e., net income attributable to equity shareholders' by the 'weighted average number of equity shares outstanding' (Lu and Lai, 2023).

EBIT is used to show the profitability resulting from a company's operations and to analyze profitability ratios. EBIT has a broad user base because it reflects a company's profit before taxes. This ratio is traditionally calculated based on net income or operating profit. Since a common formula for this ratio has not been established in the literature, it can be calculated differently depending on the purpose of use. In this study, the formula used is 'EBIT = Net Income + Tax Expense + Interest Expense' (Doğan, 2024; Aydeniz, 2009).

$$\text{EBIT} = \text{Net Income} + \text{Tax Expense} + \text{Interest Expense} \quad (5)$$

#### **EBIT value formula**

FIN-LEV is a calculation obtained by dividing a company's total debt by its total assets. The ratio provides information on how much of a company's total debt could be covered if all of its assets were liquidated.

$$\text{Financial Leverage Ratio} = \frac{\text{Short – term Liabilities} + \text{Long – term Liabilities}}{\text{Total Assets}} \quad (6)$$

### **Finansal leverage rasyon formülü**

#### ***Independent variable***

The independent variable, represented by CGR (CGR), was obtained from the sustainability and integrated reports published by the companies annually.

## **4. FINDINGS**

In this section of the article, the findings of the applied statistical analyses, their interpretation, and evaluation are presented. Results of the normality test conducted for the variables in the study is shown in Table 3.

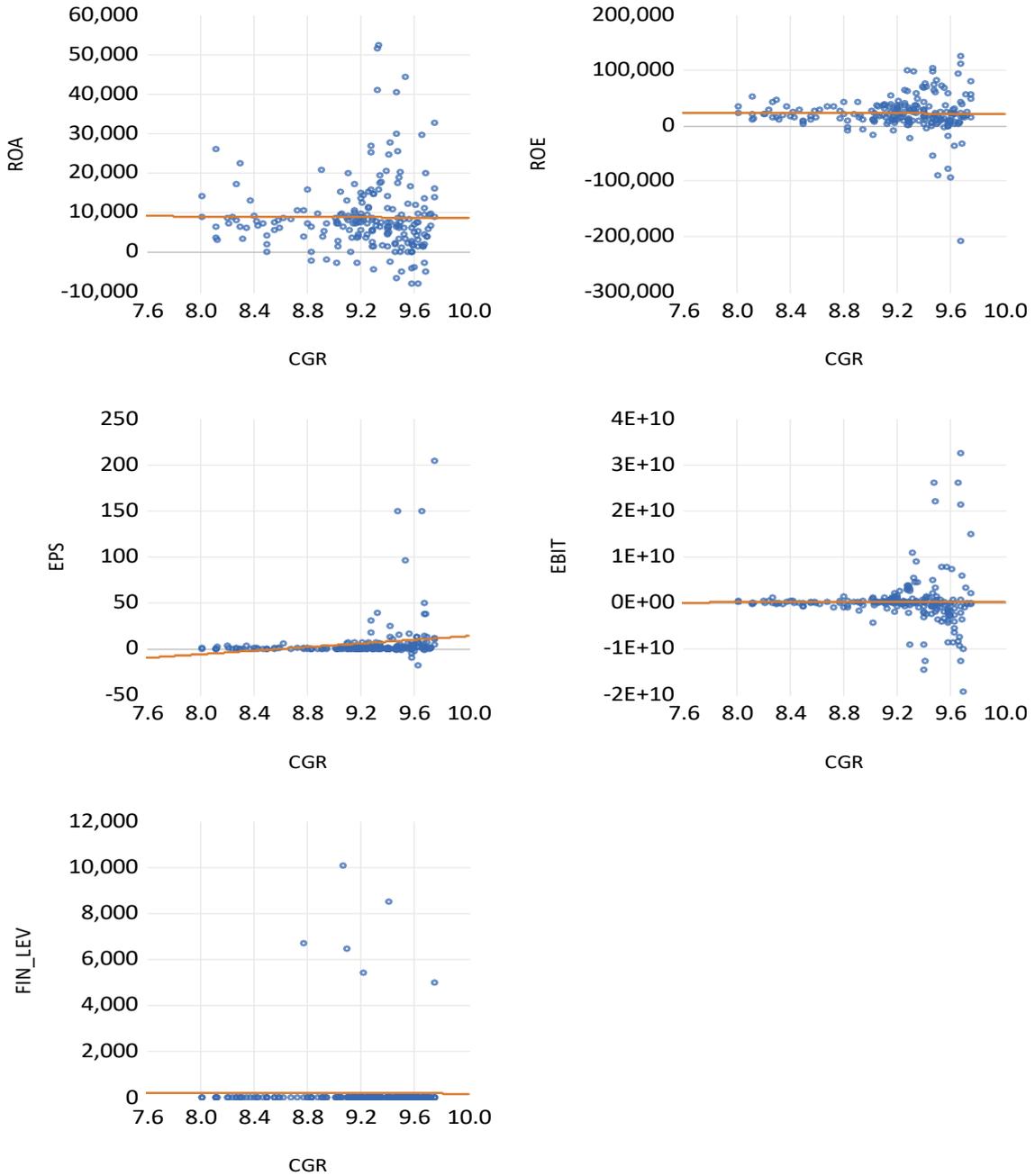
**Table 3. Normality Test**

	<b>ROA</b>	<b>ROE</b>	<b>EPS</b>	<b>EBIT</b>	<b>FIN-LEV</b>	<b>CGR</b>
<b>Skewness</b>	1.911697	-1.592441	6.651905	2.240311	6.212093	-1.125316
<b>Kurtosis</b>	8.717480	16.02564	51.29526	15.90554	41.89612	3.528762
<b>Jarque-Bera</b>	411.9731	1565.851	21852.89	1625.228	14519.13	46.54549
<b>Probability</b>	0.000000	0.000000	0.000000	0.000000	0.000000	0.000000
<b>Obs.</b>	209	209	209	209	209	209

To determine whether a series exhibits a normal distribution, skewness and kurtosis values of the variables are examined. Criteria indicating that the series exhibits a normal distribution require skewness to be “0” and kurtosis to be “3” (Doğan, 2024). Accordingly, based on the information in Table 3, both the skewness and kurtosis values of the variables indicate that the series does not exhibit a normal distribution. Additionally, the probability values provide insights into whether the series exhibits a normal distribution. A probability value greater than 0.05 suggests that the series exhibits a normal distribution, whereas a value less than 0.05 indicates otherwise. In this context, the probability values in the table are consistent with the skewness and kurtosis values, indicating that the series does not exhibit a normal distribution.

Scatter diagram provides a general overview of the direction and strength of the relationship between two variables (Doğan, 2024). Graph 1 illustrates the relationship between the variables showing a weak-strong, positive-negative correlation.

**Graph 1. Scatter Diagram**



Upon considering Graph 1, it is observed that an increase of one unit in the independent variable CGR does not lead to a proportional increase in the dependent variables; instead, it results in a ‘weak negative relationship’ in ROA and ROE, and a ‘strong negative relationship’ in EBIT and FIN-LEV. That is, an increase of one unit in CGR leads to a decrease in the ROA, ROE, EBIT, and FIN-LEV ratios. Between CGR and EPS, the initially negative effect gradually turns into a ‘weak positive relationship’ over time. However, an increase of one unit in ROA and CGR values significantly distorts the relationship between the two variables, with this distortion being lower in the ROE and EBIT variables and minimal in the EPS and FIN-LEV variables.

The scatter diagram illustrates the direction and strength of the relationship between two variables but does not indicate its intensity or significance level. The correlation analysis, as presented in Table 4, provides information on the direction, strength, and significance of the relationship between the variables in the study (Doğan, 2024).

**Table 4. Correlation analysis**

Correlation t-statistics Prob.	ROA	ROE	EPS	EBIT	FIN-LEV
<b>CGR</b>	-0.008227	-0.010199	0.188801	0.008113	-0.007371
	-0.118372	-0.146742	2.766117	0.116730	-0.106052
	0.9059	0.8835	<b>0.0062*</b>	0.9072	0.9156
<b>Observations</b>	209	209	209	209	209

\* The significance levels are indicated with (\*), (\*\*), and (\*\*\*) for values below 0.01, 0.05, and 0.10, respectively.

As observed in Table 4, there is a very weak negative correlation between the independent variable CGR and the variables ROA, ROE, and FIN-LEV. This means that a one-unit increase in CGR score leads to a decrease of -0.008 in ROA, -0.01 in ROE, and -0.007 in FIN-LEV. However, a weak but positive correlation is found between the independent variable CGR and the variables EPS and EBIT. Accordingly, a one-unit increase in CGR score results in an increase of 0.189 in EPS and 0.008 in EBIT. Moreover, examining the probability values between the variables, it is noted that the p-values for CGR with ROA, ROE, EBIT, and FIN-LEV variables are greater than the significance level of 0.10, indicating no significant correlation between these variables. Among these variables, only the p-value for EPS is less than 0.01, 0.05, and 0.10 significance levels, suggesting a significant correlation between CGR and EPS. In conclusion, there exists a statistically significant, predominantly negative correlation between CGR and FP indicators, except for EPS.

The impact of the CGR independent variable on the ROA, ROE, EPS, EBIT, and FIN-LEV dependent variables was examined using panel two-way Granger causality analysis method. An analysis was conducted to consider the possibility of a causal relationship between the variables with a 4-lag structure. The findings obtained as a result of these lags are presented in the tables below.

**Table 5. Granger causality analysis**

Binary Granger Causality Analyses					
Sample: 2009-2023					
Lags	H0: Null Hypothesis	Obs.	F-Statistics	Prob.	Results
<b>1</b>	CGR → ROA	193	0.11333	0.7368	<b>H0: ACCEPTED</b> <b>H1a: REJECTED</b> <i>(p&gt;0.01, 0.05 ve 0.10)</i>
	ROA → CGR		0.44577	0.5052	
<b>2</b>	CGR → ROA	177	0.55089	0.5775	
	ROA → CGR		0.45922	0.6325	
<b>3</b>	CGR → ROA	161	0.58836	0.6235	
	ROA → CGR		1.16227	0.3261	
<b>4</b>	CGR → ROA	145	0.64096	0.6342	
	ROA → CGR		0.99694	0.4116	
<b>1</b>	CGR → ROE	193	0.02374	0.8777	
	ROE → CGR		0.34977	0.5549	
<b>2</b>	CGR → ROE	177	0.36773	0.6928	<b>H0: ACCEPTED</b>

	ROE → CGR		0.33422	0.7164	<b>H1b: REJECTED</b> <b>(p&gt;0.01, 0.05 and 0.10)</b>
3	CGR → ROE	161	0.26230	0.8525	
	ROE → CGR		1.30185	0.2759	
4	CGR → ROE	145	0.74885	0.5604	
	ROE → CGR		1.06212	0.3778	
1	<b>CGR → EPS</b>	193	5.00216	<b>0.0265**</b>	
	<b>EPS → CGR</b>		0.10744	0.7434	<b>H1c: ACCEPTED</b> <b>(p&lt; 0.05)</b>
1	CGR → EBIT	193	0.07753	0.7810	
	EBIT → CGR		0.16917	0.6813	
2	CGR → EBIT	177	0.15842	0.8536	
	EBIT → CGR		0.28516	0.7523	<b>H1d: REJECTED</b>
3	CGR → EBIT	161	0.09593	0.9622	<b>(p&gt;0.01, 0.05 and 0.10)</b>
	EBIT → CGR		0.62979	0.5968	
4	CGR → EBIT	145	0.19892	0.9386	
	EBIT → CGR		0.11356	0.9776	
1	CGR → FIN-LEV	193	0.12163	0.7277	
	FIN-LEV → CGR		0.08337	0.7731	
2	CGR → FIN-LEV	177	0.47843	0.6206	
	FIN-LEV → CGR		0.21033	0.8105	<b>H1e: REJECTED</b>
3	CGR → FIN-LEV	161	0.39685	0.7554	<b>(p&gt;0.01, 0.05 and 0.10)</b>
	FIN-LEV → CGR		0.98082	0.4035	
4	CGR → FIN-LEV	145	0.38327	0.8203	
	FIN-LEV → CGR		0.30157	0.8765	

\* Significance levels are indicated by (\*) for values below 0.01, (\*\*) for values below 0.05, and (\*\*\*) for values below 0.10. Based on these values in the table, the rejection of the null hypothesis (H0) is demonstrated.

As a result of the analysis, the probability (p) values indicating causality from CGR to ROA, ROE, EBIT, and FIN-LEV, as well as from ROA, ROE, EBIT, and FIN-LEV to CGR, were found to be greater than the significance levels of 0.01, 0.05, and 0.10. Therefore, no statistically significant causality relationship was found between these variables. However, the probability (p) value indicating causality from CGR to EPS was found to be less than the significance level of 0.05, indicating a statistically significant one-way causality relationship between these two variables. Conversely, the probability (p) value indicating causality from EPS to CGR was found to be greater than the significance levels of 0.01, 0.05, and 0.10, indicating no statistically significant causality relationship between these two variables.

## 5. DISCUSSIONS

According to the correlation results obtained in the study, there is a negative relationship between CGR and ROA, ROE and FIN-LEV. These results align with those of Verma (2022). Additionally, a positive correlation was observed between CGR and EBIT. These findings are consistent with previous research by Chen and Koa (2010) and Mutairi et al. (2012). However, a positive correlation was found between CGR and EPS, but this relationship was not statistically significant. In this context the results appear to be consistent with Kevser and Doğan (2021), Larcker et al. (2007), Bai et al. (2006) in terms of correlation analysis. Accordingly, the results show that the correlation between the variables is weak.

The findings of the panel Granger causality analysis conducted in the study support other research indicating that CGR does not have a predicted effect on FP. In summary, the empirical relationship

between CGR and FP indicators, except for the hypothesis regarding EPS, was rejected. This implies that CGR does not have a causal effect on firms' return on assets, return on equity, earnings before interest and taxes, or financial leverage. It was observed that CGR affects EPS. This result is consistent with the findings of Kevser and Doğan (2021). The similarity in findings is due to multiple factors. First of all, our research was conducted in the context of Türkiye, like Kevser and Doğan (2021). Moreover, the method used and the period subject to analysis are parallel to each other. Therefore, the consistency of the results obtained also shows the consistency of the results obtained in the context of Türkiye. In addition, in the application of the causality analysis, four lags were taken to establish a relationship between variables. As a result of these lags, only a one-way relationship from CGR to EPS was established, while no relationship was found from EPS and other independent variables to CGR.

In the study, despite the corporate rating scores of the analyzed firms increasing over the years, the significant but negative correlation between variables and the inability to establish causality could be attributed to several reasons.

- First, these systems simplify a complex CG process and related performance into a single score. Such results cannot accurately reflect the true nature or performance of CG. Rankings, if necessary, should be carefully interpreted and should not be used as a simple measure of good or bad CG practices, as criticized by Donker and Zahir (2008). Reducing a complex CG process to a single scoring system may fall short in improving FP.
- Second, the CGR industry is still in its developmental stages and undoubtedly flawed in structure, but CGR systems will continue to evolve in the coming years. Therefore, investors need to educate themselves on what a "rating" actually signifies. The findings of this research underscore the importance for investors to remember that a "good governance rating" does not necessarily mean "good FP."
- Third, the results may suggest the necessity of simultaneously controlling for both sample selection bias and endogeneity. The CGR coefficient may exhibit a highly significant positive effect on performance after both issues are addressed.
- Fourth, the motive driving firms to obtain a CGR may be more about gaining reputation or establishing legitimacy within the market rather than guiding investors towards improving FP.
- Fifth, firms in developing countries may struggle to publicize these rating scores. Conversely, investors in developing countries may not trust these rating scores despite understanding their significance when evaluating firms, due to a lack of confidence in the market in which they operate.

In total the empirical studies that analyze the relationship between CGR and FP represent mix and contradictory results (Cho, Chung and Young, 2019; Orlitzky and Benjamin, 2003). The main reason for this is that majority of the previous studies deal with the issue on a country-by-country basis and use

different FP indicators (Kevser et al., 2023). Previous studies on the subject show that Türkiye-based studies are extremely limited. This research examines the relationship between CGR and FP holistically from the perspective of Türkiye. In this context, the research differs from existing studies, fills an important gap in the literature and provides new evidence from a macro perspective.

## 6. CONCLUSION AND SUGGESTIONS

Following the scandals in the Asian markets in 1997 and in the U.S. markets in 2001-2002, the concept and subject of CG gained significant attention. In this context, CGR scores largely represent the quality of CG practices. Moreover, investors perceive CG as an important criterion when making investment decisions, and they are willing to pay higher costs for firms with well-governed boards. Therefore, investors expect the incorporation of rating information into firm returns or values.

The motivation of the study lies in the idea that improved CG practices and ratings change into enhance FP, leading investors to invest in more profitable projects. In this context, the research examines whether CGR scores affect the FP of companies listed on the BIST CG Index. Contrary to previous assumptions widely accepted in literature indicating a positive effect, this study, in line with other research, suggests that CGR scores have limited effect on FP.

While evaluating the results obtained in the context of Türkiye reveals the managerial dimension and contribution of the research, evaluating the results in terms of stakeholder and representation theories stated in the literature contributes to the theoretical dimension of the research.

First of all, the concept of CGR is a new approach for Türkiye, which is in the developing country category (Ararat and Uğur, 2023; Kevser and Doğan, 2021; Poroy Arsoy and Crowther, 2008). Türkiye has experienced and is experiencing significant macroeconomic fluctuations in recent times. In this context, businesses have not yet clearly understood the importance of CG practices. Therefore, it provides limited resources for CG practices and therefore the impact is limited. Companies operating in Türkiye should invest in good CG practices for strong and sustainable FP in the long term, and should not consider these investments as a cost element. On the other hand, in the context of Türkiye, policy makers and legislators should encourage businesses to transition to CG practices and implement compelling legal regulations. In Türkiye, good CG practices should not be left to the choice of businesses. The limited impact of CG scores on FP in Türkiye indicates that stakeholders' trust and expectations are not managed at an optimal level. For this reason, companies in Türkiye must strengthen their CG practices to ensure the participation of stakeholders in business management and to ensure that new investors invest in the business. It has been proven many times that strong and sustainable FP will be achieved in the long term in companies where stakeholder expectations are managed correctly and conflicts of interest between managers and business owners are eliminated, and this constitutes the theoretical contribution of the research in terms of stakeholder and agency theory.

We can conclude that although CGR compliance increases structural costs of the firms in Türkiye, the firms can improve their financial market performance by adopting the right corporate governance mechanisms.

According to this; the study, firstly, provides new empirical evidence to past research by examining the relationship between FP and CGR scores during the period of 2009-2023. Secondly, it contributes to the current CG literature in Türkiye by investigating the relationship between CGR scores and variables such as Return on Assets, Return on Equity, Earnings Per Share, Earnings Before Interest and Taxes, and Financial Leverage. Thus, with this research, the relationship between CGR and FP was investigated with the causality dimension within the framework of Türkiye and an significant gap in the literature was filled. This gap also constitutes our main motivation for the research.

The firms included in the analysis did not equally distribute their CGR scores between 2009 and 2023. Additionally, sectoral differences were not considered among the 16 firms. Lastly, banks, holdings, financial, and insurance companies were not included in the sample due to their highly diversified and regulated financial statements.

One aspect of future research studies would involve focusing on a specific sector and examining relevant CG factors that may be more applicable to that particular industry. Additionally, conducting analyses on a sector-by-sector basis would allow for comparisons of results between two or more groups.

The empirical design of the study focused solely on Türkiye and firms listed on the Borsa Istanbul CG Index. One potential avenue for future research could involve expanding this analysis to include different countries, allowing for comparisons of results between cross-border and domestic examples.

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<b>KATKI ORANI / CONTRIBUTION RATE</b>	<b>AÇIKLAMA / EXPLANATION</b>	<b>KATKIDA BULUNANLAR / CONTRIBUTORS</b>
Fikir veya Kavram / <i>Idea or Notion</i>	Araştırma hipotezini veya fikrini oluşturmak / <i>Form the research hypothesis or idea</i>	Assoc. Prof. Mustafa KEVSER (Ph.D.) Seda DOĞAN (Ph.D.)
Tasarım / <i>Design</i>	Yöntemi, ölçeği ve deseni tasarlamak / <i>Designing method, scale and pattern</i>	Assoc. Prof. Mustafa KEVSER (Ph.D.) Seda DOĞAN (Ph.D.)
Veri Toplama ve İşleme / <i>Data Collecting and Processing</i>	Verileri toplamak, düzenlenmek ve raporlamak / <i>Collecting, organizing and reporting data</i>	Assoc. Prof. Mustafa KEVSER (Ph.D.) Seda DOĞAN (Ph.D.)
Tartışma ve Yorum / <i>Discussion and Interpretation</i>	Bulguların değerlendirilmesinde ve sonuçlandırılmasında sorumluluk almak / <i>Taking responsibility in evaluating and finalizing the findings</i>	Assoc. Prof. Mustafa KEVSER (Ph.D.) Seda DOĞAN (Ph.D.)
Literatür Taraması / <i>Literature Review</i>	Çalışma için gerekli literatürü taramak / <i>Review the literature required for the study</i>	Assoc. Prof. Mustafa KEVSER (Ph.D.) Seda DOĞAN (Ph.D.)

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