DOES CORPORATE GOVERNANCE MATTER FOR INSTITUTIONAL INVESTORS? INSIGHTS FROM INTERNATIONAL EVIDENCE[1]

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ABSTRACT | We examine the impact of firms' board structure, as a significant provision of firm-level corporate governance mechanism, institutional investors' investment decisions. The results show that firms with independent board members, a higher representation of women on their boards, and a separation between CEO and chairman roles share characteristics that attract institutional investors, encouraging them to invest in these firms' shares. Furthermore, the number of board members does not have a effect on the investment decisions of institutional investors. Similar results are observed for domestic and foreign institutional investors, indicating that these sub-groups share common factors influencing their investment decisions, except for the factor of CEO duality. The findings are robust to several sensitivity tests, including alternative measures of firm-level corporate governance, controlling for country fixed effects, and including additional control variables.

Keywords: *Institutional investor, corporate governance, board structure*

JEL Codes: *G34, L25, M41*

Scope: *Bussiness administration*
Type: *Research*

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KURUMSAL YÖNETİM KURUMSAL YATIRIMCILAR İÇİN ÖNEMLİ Mİ? ULUSLARARASI KANITLARDAN ÇIKARIMLAR

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ÖZ | Bu çalışma, firmaların yönetim kurulu yapısının, kurumsal yönetim mekanizmasının önemli bir unsuru olarak, kurumsal yatırımcıların yatırım kararları üzerindeki etkisini incelemektedir. Bulgular, bağımsız yönetim kurulu üyelerine sahip olan, yönetim kurullarında kadın temsili daha yüksek olan ve CEO ile yönetim kurulu başkanı rollerinin ayrıldığı firmaların, kurumsal yatırımcıları çekme ve bu firmaların hisselerine yatırım yapmaya teşvik etme özelliklerine sahip olduğunu göstermektedir. Ek olarak, firma yönetim kurulu üye sayısının kurumsal yatırımcıların yatırım kararları üzerinde benzer bir etkisi bulunmamaktadır. Yerli ve yabancı kurumsal yatırımcılar için benzer sonuçlar gözlemlenmiş olup, CEO'nun çift rol üstlenmesi (CEO duality) faktörü dışında bu alt grupların yatırım kararlarını etkileyen ortak faktörlere sahip olduğu görülmüştür. Elde edilen bulgular firma düzeyinde kurumsal yönetimin alternatif ölçümlerini kullanarak, ülke sabit etkilerini kontrol ederek ve ek kontrol değişkenlerini dahil ederek güvenilirliği test edilmiştir.

Anahtar Kelimeler: *Kurumsal yatırımcı, kurumsal yönetim, yönetim kurulu yapısı*

JEL Kodları*: G34, L25, M41*

Alan: *İşletme*
Türü: *Araştırma*

1. INTRODUCTION

The number of shares held by groups of investors around the world has changed significantly in recent years. Specifically, institutional shareholdings has raised, while individual shareholdings has declined. This shift is particularly notable in the United Kingdom (UK). As of 2018, individual investors' shareholdings had declined to 13.5%, while institutional investors, such as insurance companies and pension funds, emerged as the dominant shareholders. Similarly, in Japan, the proportion of shares held directly by individual investors dropped from approximately 30% in 1980 to 18% in 2021. A comparable trend has been observed in the United States (US), where individual investors, who were dominant shareholders in publicly listed companies until the 1980s, have been increasingly replaced by institutional investors. In Turkey, by the end of 2020, institutional investors accounted for only 9% of corporate ownership structures (Medina, De La Cruz & Tang, 2022).

One of the reason of increasing shareholdings held by institutional investors lies in the imperfections of financial markets. In a perfect market, all information is freely accessible, securities can be traded in any desired quantity and volume, and transaction costs do not exist (Fama, 1970). However, in the real world, these ideal conditions are not met, and institutional investors can serve to mitigate the resulting market inefficiencies (Dağlar, 2007). For example, institutional investors play a crucial role in ensuring the proper functioning of the financial system. They are specialized financial institutions that raise savings from small investors and manage these funds with acceptable risk levels, aiming for return maximization and maturity matching (Aras, 2003). In addition, institutional investors play a pivotal role in shaping modern publicly traded companies through three core functions: acting as informed investors, monitoring management, and providing advisory services. Their ability to collect and utilize information significantly contributes to the development of capital markets by promoting efficient transactions, enabling accurate risk assessments, and supporting governance systems (Gillan & Starks, 2003; Gillan & Starks, 2007). Furthermore, institutional investors also play a significant role in capital markets through their substantial holdings. Their large shareholdings incentivize them to monitor and discipline corporate managers, actively gather information and counteract stock mispricing. As a result, firms with high proportions of institutional ownership often demonstrate improved information efficiency and a lower likelihood of stock mispricing (Boehmer & Kelley, 2009). Research suggests that companies with greater institutional investor participation are less likely to experience stock return irregularities, including those related to accrual-based anomalies (Collins, Gong & Hribar, 2003; Green, Hand & Soliman, 2011),

momentum effects (Hanson & Sunderam, 2013) and post-earnings announcement drift (Bartov, Radhakrishnan & Krinsky, 2000; Ali, Durtschi, Lev & Trombley 2004; Ke & Ramalingegowda, 2005). Previous studies also show that institutional ownership increases firm market value (Ferreira & Matos, 2008), reduces the cost of debt (Elyasiani, Jia & Mao, 2010), promotes better information disclosure (Bird & Karolyi, 2016), and improves governance standards in countries with weaker investor protections (Aggarwal, Erel & Matos, 2011).

In the light of aforementioned benefits of institutional investors to both firm and capital markets, understanding their preferences is of critical importance. In other words, the questions to address are: which companies do institutional investors prefer, and what are the characteristics of these companies? Extant literature provides useful insights about these questions. For example, Velte (2023) highlights that institutional investors are heterogeneous, and differences in investor categories (e.g., long-term sustainable investors, foreign institutional investors, or independent institutions) can significantly influence investment decisions. Supporting this view, Drobetz, El Ghoul, Fu and Guedhami (2023) and Hong and Shore (2023) argue that long-term investors, such as pension funds and university endowments, often prioritize social norms. In contrast, hedge funds and other short-term-oriented institutional investors primarily focus on financial gains. Additionally, empirical evidence indicates that ESG (Environmental, Social, and Governance) factors matter for institutional investors in their portfolio management activities (Amel-Zadeh & Serafeim, 2017; Barko, Cremers, & Renneboog, 2018; Eccles, Serafeim, & Krzus, 2011; Hanson, Lyons, Bender, Bertocci & Lamy, 2017). Moreover, institutional investors can be grouped as domestic and foreign institutional investors and previous studies document that these two groups may have different preferences in their investment decision process, too. For example, Ferreira and Matos (2008) mentioned that foreign and domestic institutions exhibit differing stock preferences, with foreign institutions showing a preference for stocks that are both cross listed on U.S. exchanges and part of the Morgan Stanley Capital International All Country World Index (MSCI ACWI). Aggarwal et al. (2011) highlight that foreign institutional investors tend to favor firms with similar characteristics, such as strong governance. Yıldız, Karan and Ozkan (2019) observe that foreign institutional investors tend to favor firms with larger boards and lower insider ownership when making investment decisions. Conversely, domestic investors, utilizing their knowledge advantage, are more inclined to invest in smaller firms and companies operating within the local market (Coval & Moskowitz, 1999). Foreign institutional investors are expected to uphold strong corporate governance practices to secure their investments. Unlike domestic institutional investors, who often have close

business relationships with local companies, foreign institutional investors generally have fewer local connections (Ferreira & Matos, 2008). Wahab, How and Verhoeven (2008) mentioned that institutional investors investments are positively and significantly related to corporate governance. Al-Najjar (2010) suggests that institutional investors are more likely to invest in firms with good corporate governance. McCahery, Sautner and Starks (2016) observe that one of the most important factors for institutional investors' decision is corporate governance practices like board independence. Shahid and Abbas (2019) mentioned that good corporate governance practices positively effects investor confidence and investment decisions. Considering these differences, understanding how firms' corporate governance structures influence the preferences of foreign and domestic institutional investors represents a key focus for academic research.

This study investigates whether firms' board structure, as a significant provision of firm-level corporate governance mechanism, attracts institutional investors, using 12,252 firm-year observations from 44 countries. The results indicate that firms with more independent board members, more women members on their boards, and separated CEO and chairman positions attract institutional investors' attention and encourage them to invest in their shares. On the other hand, the number of board members in firms does not influence institutional investors' investment decisions. Similar results are observed for domestic and foreign institutional investors, except for the factor of CEO duality, suggesting that these sub-groups share common factors influencing their investment decisions. The findings are robust to several sensitivity tests. Specifically, we perform robustness checks using alternative measures of firm-level corporate governance, controlling for country fixed effects, and incorporating additional control variables.

This study contributes to literature in several ways. First, it differs from previous studies focusing on a single country context by providing international evidence based on a large data set. This provides a more comprehensive understanding of the relationship between firm-level corporate governance practices and institutional investors across countries. Second, the study employs three distinct measures to represent institutional investors: total institutional investors, domestic institutional investors, and foreign institutional investors. By focusing on these different institutional investor groups, this study provides useful insights about whether the impact of firm-level corporate governance differs between these institutional investor groups. Third, corporate governance is proxied and examined through firm' board structure, which is directly responsible for firm management, with four variables: board size, the rate of

independent directors among all directors, the rate of female directors among all directors and whether the CEO also serves as the board chair.

The structure of the study is as follows. In the second section, the relationship between corporate governance practices and institutional investor preferences is discussed and the hypotheses are presented. In section three, the data and methodology are explained. In section four, we provide the results of the analysis. The study concludes with section five.

2. LITERATURE REVIEW AND HYPOTHESIS DEVELOPMENT

Corporate governance provisions can enhance institutional investors' confidence, contributing to the sustainable success of firms. The relationship between firms' corporate governance provisions and institutional investors' attention to firms' shares can be discussed under several theoretical frameworks encompassing stakeholder theory, resource based view, and agency theory. Specifically, stakeholder theory suggests that effective corporate governance ensures the protection of all stakeholders' rights, including investors, thereby fostering long-term value creation. From the perspective of the resource based theory, a strong governance structure serves as a valuable internal resource that provides a competitive advantage. Similarly, agency theory suggests that strong corporate governance mechanisms mitigate agency conflicts by aligning the interests of managers and institutional investors, reducing opportunistic behavior, and enhancing accountability. Thus, by employing strong firm-level governance provisions, firms can attract more attention from institutional investors. Regarding board characteristics, board independence strengthens oversight and reduces agency conflicts, female board representation enhances diversity and decision-making quality, and CEO duality may either consolidate leadership efficiency or pose risks related to excessive power concentration.

Given that the corporate governance system provides protection for shareholders, effective governance can boost investor confidence, leading to an increase in stock prices. Consequently, firms can raise additional capital, providing more funds for corporate investments. In addition, strong corporate governance attracts cross-border investors to purchase shares in domestic companies (Shahid & Abbas, 2019). Since empirical findings demonstrate the significant influence of corporate governance practices on investment decisions, it is reasonable to expect institutional investors to place emphasis on firm corporate governance when making investment decisions. As stated in Leuz, Lins and Warnock (2009), corporate governance factors should be considered by institutional investors when making investment decisions. Similarly, Gillan and

Starks (2007) demonstrate that institutional investor activism in the US has concentrated on corporate governance matter since 2000, underscoring the importance of corporate governance on the firm-level to institutional investors. Furthermore, previous work shows that investors with a preference for growth tend to allocate their portfolios toward firms with "stronger" board features, highlighting that investors' perceptions of board-level governance provisions are essential for companies with significant growth prospects (Bushee, Carter & Gerakos, 2014). Relatedly, in a recent study, Feng et al. (2024) report that firms with enhanced governance mechanism regarding sustainability related issues attract more cross-border equity investment, suggesting foreign institutional investors take firms' sustainability related governance mechanisms into account. They underline that information asymmetry and corporate reputation are the two factors through which firms influence foreign institutional investors' decisions.

Relatedly, Schnatterly and Johnson (2014) suggest that institutional investors assess a firm's governance characteristics to decide whether to add it to their portfolios, as these characteristics can significantly influence performance. McCahery et al. (2016) use a straightforward approach to investigate institutional investors' preferences by conducting a survey among long-term-focused institutional investors, examining corporate governance both perspectives from firm and country. Their results reveal that the most important factors for institutional investors include equity-based compensation, management equity ownership, accountability, high free float and board independence. De La Hoz, Pombo and Taborda (2018) suggest that institutional investors (like pension funds and insurance companies) prioritize corporate governance mechanisms that align with the agency theory perspective, whereas independent investors concentrate on business opportunities in accordance with the resource-based view of the board of directors. Bansal and Themnozhi (2019) indicates that institutional investors favor the norm of board independence and reward affected firms by increasing their investments during the post-mandate period. Therefore, results indicate a positive association between a higher presence of independent directors and greater institutional ownership. Pombo and De La Hoz (2021) investigates institutional investors' preferences for board attributes in emerging markets with low investor protection and finds that grey investors (e.g., pension funds, insurance companies) prefer directors with graduate degrees and diverse demographics, while independent investors (e.g., mutual funds, investment firms) place emphasis on managerial and entrepreneurial experience. The results highlight investor heterogeneity in board composition preferences.

In addition to these studies, previous work also focuses on different types of institutional investors (e.g. domestic vs foreign) and provides useful insights

to better understand the factors that may affect their investment decision. Domestic institutional investors have extensive knowledge of the local business environment, regulatory framework, cultural dynamics, local potential, and opportunities at the national level (Taran & Mironiuc, 2018). It is widely argued that domestic institutional investors have a strong motivation to recover their investments and earn dividend income (Iwasaki & Mizobata, 2018). Domestic institutional investors possess a significant information advantage over foreign investors in emerging markets. Unlike foreign institutional investors, domestic institutional investors experience lower monitoring costs because they are not hindered by the liabilities of foreignness. Moreover, domestic institutional investors benefit from informal networks that enable rapid information transmission, in contrast to the slower, formal channels such as analyst reports and business media (Caixe, Pavan, Maganini & Sheng, 2024). As for foreign institutional investors, extant literature shows that they tend to diversify their holdings across broad portfolios due to higher levels of information asymmetry (Cai, Lee, Xu & Zeng, 2019). To oversee managerial actions, they implement control measures like regular reporting systems and oversight mechanisms (Abor & Biekpe, 2007; Lu & Li, 2019). In addition, foreign institutional investors promote awareness of international corporate governance standards among managers (Nguyen, Pham, Dao, Nguyen & Tran, 2020), cultivating a culture of effective governance within the organization, which in turn, motivates managers to act ethically, make sound investment decisions, and ultimately improve the company's overall performance (Bhatia & Kumari, 2024).

There are two views in the literature regarding the differences between domestic and foreign institutional investors. On the one hand, it is argued that foreign institutional investors are more experienced compared to their domestic counterparts (Grinblatt & Keloharju, 2000). On the other hand, an alternative view suggests that both groups are equally experienced, though foreign investors may be less well-informed than domestic investors (Covrig, Lau & Ng, 2006). However, despite potential differences in information access, both types of investors may target companies with similar characteristics (Liu, Bredin, Wang & Yi, 2014). Specifically, previous studies suggest that foreign and domestic institutional investors may exhibit similar investment preferences (Kang & Stulz, 1997, Grinblatt & Keloharju, 2000, Covrig, et. al., 2006, Chang, 2010).

Another strand of the literature shows that domestic and foreign institutional investors share several common investment preferences, despite exhibiting some differences (Ferreira & Matos, 2008). For example, Aggarwal et al. (2011) suggest that foreign institutional investors possess greater experience in international markets compared to domestic institutional investors, making

them more informed and aware of the importance of stronger corporate governance practices. Also, Liu et. al., (2014) examines the differences in investment preferences between domestic and foreign institutional investors in China. The results indicate that domestic institutional funds prioritize basic financial indicators in their investment decisions, while foreign institutional investors focus more on corporate governance aspects, such as management compensation. In addition to the above literature, studies show that foreign and domestic institutional investors both play a role in monitoring investee firms, while foreign institutional investors are generally more active in demanding changes to corporate governance. This difference arises because domestic institutional investors often maintain stronger business relationships with investee firms, which can lead to a greater sense of loyalty to management (Ferreira & Matos 2008; Gillan & Starks, 2003).

In line with previous studies, therefore, we posit that institutional investors (and its sub-groups, namely domestic and foreign) place significant emphasis on firm corporate governance provisions, which is proxied by firm board structure. We formulate our testable hypotheses as follows:

H1: Institutional investors (total, domestic and foreign) prefer to invest in firms with strong board structure.

3. DATA AND METHODOLOGY

3.1. Data and Research Sample

We start with all publicly available non-financial firms available on Refinitiv. We use Refinitiv as the primary data source due to its comprehensive coverage of firm-level governance and financial information. The sample of the study covers the period from 2010 to 2020. Firms with missing values for total institutional investors, domestic institutional investors, or foreign institutional investors are excluded to ensure data completeness and consistency. After removing firms with incomplete or missing information, the final sample includes 12,252 firm-year observations from 44 countries (these are the countries with firms having information of the key variables of the study). Firm-level total institutional investors, domestic institutional investors, foreign institutional investors, corporate governance score and firm-level financial data is obtained from Refinitiv. Last, county-level GDP and GDP growth are obtained from the World Bank. The sample distribution by country is documented in Table 1.

Table 1: Distribution of Sample, Institutional Investors and Board Structure Measures

	Number of obs.	Total Institutional İnvestors	Domestic Institutional İnvestors	Foreign Institutional İnvestors	Board size	Board independence	Board gender	CEO duality
Argentina	8	0.182	0.000	0.182	15.500	31.108	11.779	0.375
Australia	1535	0.129	0.027	0.102	6.371	59.896	13.539	0.130
Austria	56	0.115	0.022	0.094	12.286	58.372	18.996	0.000
Belgium	86	0.220	0.023	0.197	12.093	39.880	22.313	0.326
Brazil	100	0.192	0.060	0.132	10.110	29.941	6.407	0.220
Canada	338	0.341	0.143	0.198	8.456	71.444	10.421	0.432
Chile	12	0.094	0.013	0.081	8.250	27.539	0.000	0.167
China	625	0.073	0.058	0.015	9.426	38.269	13.375	0.214
Colombia	17	0.062	0.000	0.062	8.353	47.888	20.278	0.000
Denmark	44	0.315	0.034	0.281	10.273	56.115	26.219	0.068
Finland	11	0.245	0.049	0.196	6.636	98.990	26.843	0.000
France	292	0.250	0.057	0.192	13.195	53.537	33.598	0.640
Germany	191	0.254	0.046	0.208	13.770	44.065	23.430	0.115
Greece	7	0.429	0.005	0.424	8.286	39.886	25.566	0.000
Hong Kong	1020	0.140	0.015	0.125	10.798	38.103	11.059	0.377
India	469	0.178	0.053	0.125	11.143	51.189	10.186	0.299
Indonesia	126	0.119	0.005	0.114	6.603	40.386	4.935	0.119
Ireland	18	0.429	0.006	0.422	11.778	60.149	15.572	0.056
Israel	49	0.095	0.021	0.074	9.265	40.707	17.109	0.204
Italy	102	0.213	0.026	0.187	12.176	58.144	25.365	0.176
Japan	1474	0.168	0.058	0.109	12.593	17.878	3.447	0.349
Korea	490	0.135	0.008	0.127	9.606	52.539	1.364	0.396
Malaysia	325	0.090	0.010	0.080	9.068	48.650	15.995	0.138
Mexico	65	0.140	0.021	0.119	12.677	47.965	2.694	0.462
Netherlands	80	0.306	0.022	0.284	7.088	78.707	24.526	0.075
New Zealand	173	0.129	0.027	0.102	6.792	76.696	24.413	0.029
Norway	12	0.184	0.090	0.094	8.667	32.727	38.007	0.167
Peru	24	0.185	0.135	0.050	9.125	34.627	10.210	0.292
Philippines	125	0.134	0.001	0.133	9.832	27.618	7.290	0.552
Poland	20	0.185	0.126	0.059	8.600	29.274	22.291	0.000
Portugal	31	0.186	0.008	0.178	14.000	45.754	17.123	0.516
Qatar	14	0.032	0.001	0.031	9.000	22.277	0.000	0.000
Russia	108	0.109	0.001	0.109	11.481	32.669	5.970	0.222
Saudi Arabia	27	0.006	0.001	0.006	9.111	31.335	1.211	0.037
Singapore	228	0.129	0.028	0.101	9.868	60.759	11.014	0.162
South Africa	515	0.212	0.053	0.159	11.678	57.624	22.244	0.126
Spain	94	0.225	0.034	0.191	13.181	45.561	16.225	0.564
Sweden	21	0.386	0.192	0.194	8.429	77.793	28.589	0.286
Switzerland	158	0.267	0.086	0.180	8.044	41.734	11.167	0.209
Taiwan	398	0.120	0.009	0.112	10.440	21.470	12.115	0.324
Thailand	28	0.050	0.002	0.049	12.536	45.308	13.071	0.036
Türkiye	28	0.095	0.001	0.094	11.821	27.968	24.679	0.107
UK	1333	0.421	0.228	0.193	8.623	56.682	19.033	0.098
US	1375	0.609	0.533	0.076	8.233	73.891	12.908	0.508
Total	12,252							

Total 12,252

As reported in Table 1, Australia has the largest number of observations (1,535), followed by Japan (1,474), the UK (1,375), and the US (1,333) firm-year observations, respectively. Regarding total institutional investors, Greece and Ireland exhibit the highest values over the sample period. In terms of domestic institutional investors, the US records the highest value (0.533), while Greece has the highest foreign institutional investors values (0.424). Firms in Saudi Arabia

have the lowest value for total institutional investors (0.006). Argentina shows the lowest value for domestic institutional investors (0.000), followed closely by Qatar, Russia, Saudi Arabia, and Türkiye (0.001). Saudi Arabia (0.006) also records the lowest value for foreign institutional investors. Regarding the board structure, Argentina (15.500), Finland (98.990), Norway (38.007) and France (0.640) have the highest board size, board independence, board gender and CEO duality over the sample period, respectively. On the other hand, firms in Australia (6.371), Japan (17.878), Chile (and Qatar) (0.000) and Australia (and Colombia, Finland, Greece, Poland, Qatar) (0.000) have the lowest board size, board independence, board gender and CEO duality over the sample period, respectively.

3.2. Methodology

As the sample of the study consists of the observations with both a time dimension (2010–2020) and a cross-sectional dimension (firms from 44 countries), a panel data regression analysis is employed. This approach allows us to control for unobserved heterogeneity, capture both firm-specific and time-specific effects, and improve estimation efficiency compared to cross-sectional or time-series models. During the initial stage of our analysis, we test whether firm-level board structure affects institutional investors participation by using the following model:

$$Institutional\ Investors_{i,t} = Board\ Structure_{i,t} + X_{i,t} + Y_{i,t} + \varepsilon_{i,t} \quad (1)$$

In Equation 1, *X* and *Y* denote firm- and country-specific variables, respectively. Subscripts i and t represent the firm and year, respectively. In line with earlier studies, we control for firm size (*Firm size*), leverage (*Leverage*), tobin q (*Tobin Q*), foreign sales (*Foreign sales*), return on assets (*ROA*), dividend (*Dividend*) as firm-specific variables. Regarding the country-specific factors, we control GDP per capita (*GDP*) and GDP growth rate (*GDP growth*). We also include year and industry fixed effects in all estimations. To minimize the effects of outliers, we winsorize *firm-level financial variables* at the 1%and 99% levels. The standard errors are robust to heteroscedasticity and clustered at a firm level for autocorrelation (Chen, Han, Li, Megginson & Zhang, 2022).

3.3. Definitions of Variables

The variables included in the models used in the study, along with their definitions and sources, are presented in Table 2.

Table 2: Variable Definitions and Data Sources

Variable	Definition	Source
Total Institutional Investors	The percentage of shares held by total institutional investors at time t	Refinitiv
Domestic Institutional Investors	The percentage of shares held by domestic institutional investors at time t	Refinitiv
Foreign Institutional Investors	The percentage of shares held by foreign institutional investors at time t	Refinitiv
Firm size	Natural logarithm of total assets	Refinitiv
Leverage	Total Debt divided by Total Assets.	Refinitiv
Tobin Q	The market value of assets divided by the book value of assets.	Refinitiv
Foreign sales	Foreign Sales divided by Total Sales.	Refinitiv
ROA	Net Income divided by Total Assets.	Refinitiv
Dividend	Dividends paid divided by Net Income.	Refinitiv
Board size	Total number of board members.	Refinitiv
Board independence	Independent Board Member/Total Board Member	Refinitiv
Board gender	Female Board Member/Total Board Member	Refinitiv
CEO duality	If the CEO is the Chairman of the Board, 1, otherwise 0	Refinitiv
Governance score	Refinitiv ESG's G-score	Refinitiv
Anti-self-dealing index	The measure shows legal protection of external and minority shareholders against expropriation by insiders. Higher values of the the index show stronger protection for outside investors.	Djankov et. al. (2008)
GDP	Gross domestic Product per capita.	World Bank
GDP growth	Annual percentage change in GDP per capita.	World Bank

4. RESULTS

4.1. Summary Statistics

Table 3 presents the summary statistics of the variables used in the analyses.

Table 3: Summary Statistics

Variable		Obs	Mean	Std. Dev.	Min	Max
Total Investors	Institutional	12,252	0.239	0.216	0.000	1.000
Domestic Investors	Institutional	12,252	0.115	0.197	0.000	0.998
Foreign Investors	Institutional	12,252	0.124	0.116	0.000	1.000
Firm size		12,252	9.426	0.754	4.623	12.024
Leverage		12,252	0.241	0.187	0.000	0.914
Tobin Q		12,252	1.688	1.867	0.309	13.773
Foreign sales		12,252	0.302	0.352	0.000	1.000
ROA		12,252	0.029	0.149	-1.081	0.326
Dividend		12,252	0.025	0.028	0.000	0.167
Board size		12,252	0.097	0.036	0.010	0.290

Board independence	12,252	0.491	0.241	0.000	1.000
Board gender	12,252	0.131	0.130	0.000	0.750
CEO duality	12,252	0.276	0.447	0.000	1.000
Governance score	12,252	0.468	0.222	0.003	0.985
Anti-self-dealing index	12,211	3.822	1.062	1.000	5.000
GDP	12,252	12.284	0.584	11.166	13.331
GDP growth	12,252	0.033	0.076	-0.338	0.399

As reported in Table 3, the mean values of the institutional investors indicators; total institutional investor, domestic institutional investors, and foreign institutional investors are 0.239, 0.115, and 0.124, respectively. Regarding the performance indicators, size, leverage, Tobin's Q, foreign sales, ROA and dividend have the mean value of 9.426, 0.241, 1.688, 0.302, 0.029 and 0.025, respectively. As for firms' board structure variables, the mean value of the variables board size, board independence, board gender, CEO duality, and governance score are 0.097, 0.491, 0.131, 0.276, and 0.468, respectively. Last, the country-level variables anti-self-dealing index, GDP and GDP growth have mean values of 3.822, 12.284 and 0.033, respectively.

4.2. Correlation Analysis

The relationships between the variables used in the study are presented, using correlation analysis. The results of the correlation analysis are presented in Table 4.

Table 4: Correlation Analysis

Variables	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)	(11)	(12)	(13)	(14)	(15)	(16)
(1) Total Institutional Investors	1.000															
(2) Domestic Institutional Investors	0.847**	1.000														
(3) Foreign Institutional Investors	0.425**	-0.120**	1.000													
(4) Firm size	-0.011	-0.120**	0.183**	1.000												
(5) Leverage	-0.047**	-0.031**	-0.035**	0.084**	1.000											
(6) Tobin Q	0.083**	0.073**	0.030**	0.025**	-0.211**	1.000										
(7) Foreign Sales	0.093*	-0.00	0.268*	0.151*	0.007	-0.00	1.000									

	**	55**	**	**		46**										
(8) ROA	-0.055**	-0.127**	0.114**	0.311**	-0.076**	-0.040**	0.079**	1.000								
(9) Dividend	-0.101**	-0.103**	0.013	0.094**	0.084**	-0.175**	0.027**	0.166**	1.000							
(10) Board Size	-0.102**	-0.141**	0.050**	0.387**	0.196**	-0.168**	0.065**	0.098**	0.045**	1.000						
(11) Board Independence	0.422**	0.373**	0.153**	-0.136**	-0.061**	0.101**	0.072**	-0.126**	-0.028**	-0.328**	1.000					
(12) Board Gender	0.131**	0.064**	0.135**	0.054**	0.029**	0.017*	0.105**	0.053**	0.131**	-0.002	0.281**	1.000				
(13) CEO Duality	0.074**	0.114**	-0.056**	0.009	0.008	0.001	-0.001	-0.003	-0.037**	0.051**	-0.044**	-0.086**	1.000			
(14) Governance Score	0.119**	-0.026**	0.267**	0.199**	0.053**	-0.089**	0.151**	0.098**	0.092**	0.018*	0.278**	0.260**	-0.163**	1.000		
(15) GDP	0.436**	0.563**	-0.144**	-0.073**	0.033**	0.120**	-0.144**	-0.186**	-0.162**	-0.029**	0.095**	-0.077**	0.131**	-0.123**	1.000	
(16) GDP Growth	-0.026**	0.000	-0.047**	0.075**	-0.026**	0.048**	-0.040**	0.061**	0.007	0.037**	0.038**	0.074**	0.019*	0.031**	0.025**	1.000

As reported in Table 4, there is a positive and significant relationship between total institutional investors and both domestic institutional investors and foreign institutional investors. Regarding the relationships between firms' institutional investors and corporate governance practices, it can generally be stated that there is a positive and significant relationship. These results indicate that as corporate governance indicators—such as board independence, board gender, CEO duality, and governance score—increase, the percentage of shares held by institutional investors also rises. Additionally, a positive relationship emerges between the corporate governance indicators board independence, board gender, CEO duality and domestic institutional investors. As these corporate governance practices increase, the percentage of shares held by domestic institutional investors also rises. Furthermore, as board size, board independence, board gender, and governance score improve, the percentage of shares held by foreign institutional investors investing in firms also increases.

4.3. Main Results

Table 5 documents the estimation results for the impact of firms' board structure on the level of institutional investors.

Table 5: Regression Analysis of Main Model

Variables	(1) Total Institutional Investors	(2) Domestic Institutional Investors	(3) Foreign Institutional Investors
Firm size	0.005*	-0.004**	0.009***
	(0.003)	(0.002)	(0.003)
Leverage	-0.012	0.010	-0.022**
	(0.019)	(0.017)	(0.011)
Tobin Q	-0.000	-0.002	0.002
	(0.002)	(0.002)	(0.002)
Foreign Sales	0.066***	-0.000	0.066***
	(0.010)	(0.008)	(0.008)
ROA	0.075**	0.035	0.040***
	(0.029)	(0.028)	(0.015)
Dividend	-0.265**	-0.088	-0.177***
	(0.106)	(0.092)	(0.059)
Board size	**0.009**	**-0.104**	**0.112**
	(0.115)	**(0.087)**	**(0.098)**
Board independence	**0.340*****	**0.256*****	**0.085*****
	(0.018)	**(0.015)**	**(0.012)**
Board gender	**0.102*****	**0.043****	**0.059*****
	(0.026)	**(0.022)**	**(0.017)**
CEO duality	**0.018****	**0.027*****	**-0.009***
	(0.007)	**(0.007)**	**(0.005)**
GDP	0.161***	0.180***	-0.019***
	(0.007)	(0.007)	(0.005)
GDP growth	-0.150***	0.009	-0.159***
	(0.027)	(0.021)	(0.018)
Constant	-1.993***	-2.124***	0.131*
	(0.105)	(0.099)	(0.078)
Observations	12,252	12,252	12,252
R-squared	0.368	0.429	0.154
Year FE	Yes	Yes	Yes
Industry FE	Yes	Yes	Yes

As reported in Table 5, the results demonstrate that firms' board structure variables are positively related to the level of institutional investors (except for board size), supporting H1. Specifically, in Column 1, the results suggest that board independence *(β=0.340, p<0.01)*, board gender diversity *(β=0.102, p<0.01)* and CEO duality *(β=0.018, p<0.05)* have significant effects on the level of total institutional investors, which is evident by positive and significant coefficients. In other words, institutional investors are more likely to invest in firms with more independent and women members on their board and with CEO is the chairman of the board. These results show that board-level governance provisions are important factors in explaining the investment preference of institutional investors. The insignificant coefficient of board size on institutional ownership suggests that increasing the number of directors does not necessarily

enhance perceived governance effectiveness by institutional investors. This may be due to potential coordination challenges, slower decision-making, or the presence of free-riding among board members, which can dilute the board's overall impact on firm performance and investor perceptions. Regarding firm-level control variables, firm size, the ratio of foreign sales to total sales, and return on asset have positive and significant impact on the level of total institutional investors, while dividend ratio has negative and significant effect on the level of total institutional investors. As for country level control variables, GDP per capita has positive and significant impact on the level of total institutional investors, while its growth rate has negative and significant effects. The same inferences are valid for the level of domestic and foreign institutional investors (except for CEO duality), demonstrating that sub-groups of total institutional investors share similarities regarding the factors affecting their investment decisions. Overall, our results support our hypothesis arguing that firms' board structure has significant effects on the level of total institutional investors (except or board size). In addition, it should be noted that CEO duality has different impact on total and domestic institutional investors than foreign institutional investors, showing that domestic and foreign institutional investors have different preferences regarding the CEO and chairman positions. As documented in previous literature, the separation of CEO and chairman positions is seen as a strong governance provision as the separation of these positions enhances the monitoring role of the firms' board of directors (Finkelstein & D'aveni, 1994). In line with this, the negative coefficient of CEO duality (in column 3) is consistent with the expectation and previous studies. On the other hand, institutional investors may perceive a dual CEO-Chair structure as a sign of strong leadership and decisive governance, leading to greater investment stability and commitment.

4.4. Robustness Checks

The results reported in Table 5 show that firm-level board structure matters for institutional investors. To test the sensitivity of our results, we employ several robustness checks including one year lagged models, controlling for country fixed effects, alternative measure of firms-level governance quality, and controlling for country-level governance environment.

4.4.1. One-year lagged model results

So far, we examine the relationship between firms' board structure and the level of institutional investors in order to the effects of firms' board structure on the level of institutional investors. However, the effects of firms' board structure on the level of institutional investors may be observed in the following

years, suggesting a delayed effect. In addition, previous work suggests that the use of lagged firms' board structure variables is a way to mitigate potential reverse causality problem (Gull, Hussain, Akbar Khan, Nadeem, & Mansour Zalata, 2023). Considering the delayed effects of firms' board structure on the level of institutional investors and to mitigate the reverse causality, following previous studies (Harjoto, Jo & Kim, 2017), we use one-year lagged values of the independent variables introduced in Equation 1. Table 6 reports the estimation results.

Table 6: One-Year Lagged Estimation Results

Variables	(1) Total Institutional Investors	(2) Domestic Institutional Investors	(3) Foreign Institutional Investors
Firm size	0.006**	-0.004*	0.009***
	(0.003)	(0.002)	(0.003)
Leverage	-0.006	0.018	-0.023**
	(0.020)	(0.018)	(0.012)
Tobin Q	0.003	-0.001	0.004**
	(0.002)	(0.002)	(0.002)
Foreign Sales	0.066***	-0.002	0.068***
	(0.011)	(0.009)	(0.008)
ROA	0.094***	0.038	0.056***
	(0.032)	(0.030)	(0.017)
Dividend	-0.197*	0.007	-0.205***
	(0.111)	(0.096)	(0.065)
Board size	**-0.108**	**-0.151***	**0.043**
	(0.117)	**(0.090)**	**(0.097)**
Board independence	**0.315*****	**0.235*****	**0.079*****
	(0.018)	**(0.015)**	**(0.012)**
Board gender	**0.098*****	**0.038***	**0.059*****
	(0.028)	**(0.020)**	**(0.018)**
CEO duality	**0.013***	**0.024*****	**-0.011****
	(0.008)	**(0.007)**	**(0.005)**
GDP	0.174***	0.185***	-0.011**
	(0.008)	(0.007)	(0.005)
GDP growth	-0.189***	-0.030	-0.159***
	(0.027)	(0.021)	(0.018)
Observations	10,124	10,124	10,124
R-squared	0.388	0.432	0.148
Year FE	Yes	Yes	Yes
Industry FE	Yes	Yes	Yes

As in Table 5, Table 6 documents the estimation results of total institutional investors in column 1, while column 2 and 3 reports the estimation

results of domestic and foreign institutional investors, respectively. As reported in Table 6, the results are qualitatively the same as those in Table 5, supporting our hypothesis. These results give us further confidence that our results are not driven by delayed effects of firms' board structure on the level of institutional investors and reverse causality.

4.4.2. Controlling for country-fixed effects

Existing studies suggest that the effects of firms' board structure on firms' outcomes are contingent on country-level factors (Abu Alia et al., 2024). Our second robustness test aims to control for unobserved country-level factors that may affect our results. Specifically, we incorporate country-fixed effects to mitigate the effects of unobserved country-level factors. Table 7 presents the results of the estimation.

Table 7: Controlling for Country-Fixed Effects

Variables	(1) Total Institutional Investors	(2) Domestic Institutional Investors	(3) Foreign Institutional Investors
Firm size	0.005*	-0.005**	0.009***
	(0.003)	(0.002)	(0.003)
Leverage	-0.006	0.010	-0.015
	(0.020)	(0.017)	(0.011)
Tobin Q	-0.001	-0.003**	0.002
	(0.002)	(0.002)	(0.002)
Foreign Sales	0.064***	0.001	0.063***
	(0.011)	(0.009)	(0.008)
ROA	0.070**	0.035	0.036**
	(0.029)	(0.027)	(0.015)
Dividend	-0.251**	-0.086	-0.165***
	(0.105)	**(0.091)**	**(0.059)**
Board size	**0.050**	**-0.097**	**0.146**
	(0.116)	**(0.089)**	**(0.099)**
Board independence	**0.344*** **	**0.257*** **	**0.087*** **
	(0.017)	**(0.015)**	**(0.011)**
Board gender	**0.099*** **	**0.036***	**0.063*** **
	(0.025)	**(0.021)**	**(0.017)**
CEO duality	**0.016** **	**0.025*** **	**-0.009** **
	(0.007)	**(0.007)**	**(0.005)**
GDP	0.160***	0.178***	-0.017***
	(0.007)	(0.007)	(0.005)
GDP growth	-0.149***	0.009	-0.157***
	(0.027)	(0.021)	(0.018)
Constant	-2.001***	-2.089***	0.088
	(0.107)	(0.099)	(0.080)

Observations	12,252	12,252	12,252
R-squared	0.371	0.434	0.166
Year FE	Yes	Yes	Yes
Industry FE	Yes	Yes	Yes
Country FE	Yes	Yes	Yes

As reported in Table 7, firms' boar structure appears to play a prominent and significant role in attracting institutional investors' participation, which is evident by significant coefficients reported in column 1 to 3. These results give us further confidence that our main results are not driven by unobserved country-level factors.

4.4.3. Alternative measure of firm-level governance quality

Our third robustness check aims to test the sensitivity of our main results in terms of alternative measures of firm-level corporate governance. To do this, we use firms' governance score, which is a pillar of firms' aggregate ESG score, from Refinitiv. The higher the governance score the stronger the firm level governance. Table 8 presents the results of this analysis.

Table 8: Alternative Measure of Firm-Level Governance

Variables	(1) Total Institutional Investors	(2) Domestic Institutional Investors	(3) Foreign Institutional Investors
Firm size	-0.003	-0.010***	0.007**
	(0.002)	(0.002)	(0.003)
Leverage	-0.020	-0.001	-0.018*
	(0.022)	(0.019)	(0.011)
Tobin Q	0.003*	-0.000	0.004**
	(0.002)	(0.002)	(0.001)
Foreign Sales	0.084***	0.018**	0.066***
	(0.011)	(0.009)	(0.008)
ROA	0.037	0.012	0.025*
	(0.030)	(0.028)	(0.015)
Dividend	-0.198*	-0.034	-0.164***
	(0.112)	(0.094)	(0.060)
Governance score	**0.168*** **	**0.057*** **	**0.111*** **
	(0.017)	**(0.015)**	**(0.011)**
GDP	0.172***	0.186***	-0.014***
	(0.008)	(0.008)	(0.005)
GDP growth	-0.015	0.108***	-0.123***
	(0.030)	(0.024)	(0.018)
Constant	-1.906***	-2.007***	0.100
	(0.119)	(0.112)	(0.073)

Observations	12,252	12,252	12,252
R-squared	0.252	0.341	0.168
Year FE	Yes	Yes	Yes
Industry FE	Yes	Yes	Yes
Country FE	Yes	Yes	Yes

As documented in Table 8, firms' governance score has positive and significant coefficients through column1 to 3, demonstrating that institutional investors (total, domestic and foreign) tend to weigh more firms with higher governance score. Overall, this result demonstrates that our main results remain the same when using alternative measures of firm-level governance.

4.4.4. Controlling for country-level governance environment

Previous studies show that whether the country has investor-friendly environment matters for institutional investors (Döring, Drobetz, El Ghoul, Guedhami & Schröder, 2021). Thus, our last robustness check investigates whether the nexus between firm-level corporate governance and institutional investors is impacted by country-level governance (investor protection) environment because institutional investors tend to invest more in countries with strong governance environment. To control country-level governance environment, we include an additional control variable, namely *Anti-self-dealing index*, which measures the quality of country-level governance environment (Djankov, La Porta, Lopez-de-Silanes & Shleifer, 2008). The results are reported in Table 9.

Table 9: Controlling for Country-Level Governance Environment

Variables	(1) Total Institutional Investors	(2) Domestic Institutional Investors	(3) Foreign Institutional Investors	(1) Total Institutional Investors	(2) Domestic Institutional Investors	(3) Foreign Institutional Investors
Firm size	0.007**	-0.003	0.010***	-0.000	-0.008***	0.007***
	(0.003)	(0.002)	(0.003)	(0.002)	(0.002)	(0.003)
Leverage	-0.007	0.013	-0.020*	-0.023	-0.000	-0.023**
	(0.019)	(0.017)	(0.011)	(0.021)	(0.018)	(0.011)
Tobin Q	-0.001	-0.003**	0.002	0.003	-0.000	0.003**
	(0.002)	(0.002)	(0.002)	(0.002)	(0.002)	(0.001)
Foreign Sales	0.065***	-0.001	0.065***	0.082***	0.016*	0.066***
	(0.010)	(0.008)	(0.008)	(0.011)	(0.009)	(0.008)
ROA	0.062**	0.026	0.036**	0.021	-0.003	0.024
	(0.029)	(0.027)	(0.015)	(0.031)	(0.029)	(0.015)
Dividend	-0.155	-0.008	-0.147**	-0.070	0.068	-0.138**
	(0.102)	(0.089)	(0.060)	(0.107)	(0.091)	(0.060)
Board size	**-0.028**	**-0.121**	**0.094**			
	(0.118)	**(0.087)**	**(0.100)**			
Board	**0.305*** **	**0.231*** **	**0.074*** **			

independence						
	(0.018)	**(0.015)**	**(0.012)**			
Board gender	**0.108*** **	**0.050** **	**0.058*** **			
	(0.025)	**(0.021)**	**(0.016)**			
CEO duality	**0.022*** **	**0.030*** **	**-0.009***			
	(0.007)	**(0.007)**	**(0.005)**			
Governance score				**0.142*** **	**0.036** **	**0.106*** **
				(0.017)	**(0.015)**	**(0.011)**
Anti-self-dealing index	0.050***	0.036***	0.014***	0.061***	0.046***	0.015***
	(0.004)	(0.003)	(0.003)	(0.004)	(0.003)	(0.003)
GDP	0.208***	0.215***	-0.007	0.230***	0.232***	-0.002
	(0.009)	(0.008)	(0.006)	(0.010)	(0.009)	(0.005)
GDP growth	-0.091***	0.052**	-0.143***	0.040	0.150***	-0.109***
	(0.026)	(0.020)	(0.018)	(0.030)	(0.024)	(0.018)
Constant	-2.809***	-2.718***	-0.091	-2.915***	-2.804***	-0.111
	(0.136)	(0.119)	(0.098)	(0.146)	(0.134)	(0.091)
Observations	12,211	12,211	12,211	12,211	12,211	12,211
R-squared	0.407	0.454	0.165	0.307	0.373	0.172
Year FE	Yes	Yes	Yes	Yes	Yes	Yes
Industry FE	Yes	Yes	Yes	Yes	Yes	Yes

We document the estimation results of the effects of firms' board structure on the level of institutional investors (through column 1 to 3), while column 4 to 6 report the results of the estimations using alternative measure of firm-level governance. Controlling for country-level governance environment, our reported results in Table 9 (through column 4 to 6) are qualitatively similar to those reported in Table 5, suggesting that our main results are robust when we control for country-level governance environment. Importantly, country-level governance environment (Anti-self-dealing index) has positive and significant impact on the level of institutional investors, which is in line with the previous studies and suggest that institutional investors place emphasis on countries' governance environment (Saona & Martin, 2016, Matemilola, Bany-Ariffin & Nassir, 2018, Wu, 2021, Ghabri, 2022, Phan, 2024). Overall, the results reported in Table 9 show that our main findings are held after controlling for country-level governance environment and using alternative measure of firm-level governance.

5. CONCLUSION

Given the benefits that can be derived from institutional investors' participation in capital markets and firms, scholars have devoted much effort to better understanding the preferences and factors that influence institutional investors' investment decisions (Park & Jang, 2021; Lotto, 2023). Corporate governance, which is seen as a significant performance indicator in developed

markets, has also gained prominence in emerging markets in recent years. This study investigates how corporate governance influences institutional investors' decisions using an international large dataset. The aim of the study is to provide useful insights for firms on how to attract institutional investment by strengthening their internal governance mechanisms.

Considering the types of institutional investors, the study classifies institutional investors as total, domestic, and foreign institutional investors. Our main model examines the impact of firms' board structures on the decision-making processes of institutional investors. Controlling for other factors that might influence total institutional investors' decisions, the findings reveal that companies with a higher proportion of independent and female board members, and where the CEO also serves as the board chair, are more likely to attract institutional investments. In addition, these results, except for the CEO duality, are valid for both domestic and foreign institutional investors. Furthermore, the results highlight differences in preferences regarding the CEO-chair duality: domestic institutional investors tend to prefer firms where the CEO and board chair are the same individual, whereas foreign institutional investors favor a separation of these roles. Importantly, our results are robust for a battery of tests. Overall, the findings confirm the hypothesis that board structures, excluding board size, significantly impact the total level of institutional investment. These results align with prior studies, including those by Bushee et al. (2014), McCahery et al. (2016), and Pombo and Hoz (2021).

The results offer several implications for firms, managers, and regulatory bodies. First, firms aiming to attract institutional investors should optimize their board structures and strengthen their internal governance mechanism through board of directors as firms' strong internal governance mechanism matters for institutional investors. Second, the results are useful for corporate managers aiming to attract more institutional investor participation. Third, the study provides useful insights for regulatory bodies of countries that want to attract more equity capital from institutional investors. Specifically, countries with firms having relatively weak internal governance provisions can benefit from the results of this study in strengthening firms' internal governance provisions, which in turn attract more institutional investors' attention. Last but not least, as institutional investors become increasingly sensitive to ESG factors, firms should adopt transparent and proactive sustainability strategies to align with investor expectations and enhance long-term investment appeal.

The study is not free from limitations like other studies and leaves room that future studies may address. The sample of the study, which is subject to data availability, is the main limitation of the study. Future studies may employ

different sample structures and approaches to better understand the factors influencing institutional investors' decisions. More precisely, detailed analyses of specific subgroups of institutional investors (e.g., hedge funds, pension funds) would shed more light on the issue. In addition, industry-specific analyses could explore the importance of board structures across various sectors. Cultural and regional differences in institutional investors' preferences could also be investigated in detail. Such research would not only enrich the theoretical literature but also help firms and investors shape more effective strategies.

6. CONFLICT OF INTEREST STATEMENT

There is no conflict of interest between the authors.

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No funding or support was used in this study.

8. AUTHOR CONTRIBUTIONS

HT: Idea.
HT, İHU: Design.
HT: Supervision.
İHU, HT: Collection and/or processing of sources.
HT: Analysis and/or interpretation.
İHU: Literature review.
İHU, HT: Writing the manuscript.
HT: Critical review.

9. ETHICS COMMITTEE STATEMENT AND INTELLECTUAL PROPERTY COPYRIGHTS

The ethics committee principles were followed in the study and the necessary permissions were obtained in accordance with the intellectual property and copyright principles.

10. REFERENCE

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