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The moderating effects of a board of directors on FDI's international diversification in Turkey

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Abstract

Purpose – This paper aims to investigate the moderating effects of a board of directors on foreign direct investment (FDI)'s international diversification in Turkey.

Design/methodology/approach – A sample of Turkish multinational firms with FDI was used. Two different aspects of international diversification were considered: the relationship between international diversification and financial performance and the moderating effect of board composition on the relationship between international diversification and the firm's financial performance. Firm-level data were obtained from the Istanbul Stock Exchange in Turkey.

Findings – The findings reveal that international diversification leads to better financial performance according to market-based measures. On the other hand, this study indicates that the board characteristics have a moderating effect on international diversification and financial performance.

Research limitations/implications – The study is based on a sample of publicly listed firms in Turkey, and this restriction limits the generalizability of the findings.

Practical implications – The internalization efforts of Turkish FDI have led to better financial performance in terms of market-based measures. The results have stated that the interest of independent outside directors is aligned with lower-risk investment decisions. Independence of independent outside directors in Turkey is interrogated by practitioners or the Capital Markets Board of Turkey. The larger board size which a moderator variable is provided, the wider shareholder value in Turkey is.

Social implications – One can understand that the development of market-supporting institutions provides the support for entry to an emerging economy which is inefficient or incomplete markets and highly concentrated family ownership.

Originality/value – These findings provide important implications for corporate governance and highlight the need for further research on the role of governance in firm internationalization. This study

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not only helps to understand how board characteristics affect the choice of international diversification decisions, but the results also allow to assess the performance implications of these choices for a particular period.

Keywords Corporate governance, International business, Emerging markets, Board of director

Paper type Research paper

1. Introduction

The emergence of a second wave of multinational enterprises (MNEs) is an important feature of globalization. These new MNEs have different characteristics and investment decisions from the multinational companies that emerge in developed countries. However, some authors describe these MNEs as second-wave, latecomer, southern or South-south foreign direct investment (FDI). These MNEs have demonstrated similar features such as investments close to their home country, familiarity through trade and ethnic and cultural ties (Bonaglia *et al.*, 2006; Aykut and Goldstein, 2006). Emerging MNEs internationalize rapidly, and this internationalization has been able to realize organizational innovations that are well-adapted to emergent global economic circumstances (Guillen and Garcai-Canal, 2009).

The improvement of the foreign investment environment in the emerging country context depends on political, economic and financial stability. On the other hand, foreign investment decision is affected by national governance models which provide a greater focus on long-term sustainability. Recently, some authors have investigated how corporate governance factors might affect the performance of overseas subsidiaries in which the MNE has invested (Luo *et al.*, 2009; Floyd and Summan, 2009; Aguilera and Yip, 2004). There has been a considerable amount of research on the effects of boards of directors on decisions to diversify internationally by means of FDI or entry mode selection (Rhoades and Rechner, 2001; Musteen *et al.*, 2009; Filatotchev *et al.*, 2007; Lien *et al.*, 2005), but there is little literature on whether different board compositions affect the relationship between internalization and firm performance, especially during financial crises in different markets (Berthon, 2010).

The improvement of the foreign investment environment in Turkey was a priority item particularly in the 2000s, but it was interrupted by the political instability and financial crisis (Kosekahyaoglu, 2006). The first was the year of 1994, and the second followed the 2001 political crisis, which led to a massive withdrawal of funds. The third crisis occurred in 2008 following the mortgage crisis in the USA (Rodrik, 2009). International capital seized an opportunity to invest in Turkey after the 2000-2001 crises. Net FDI increased significantly after the crisis (Dufour and Orhangazi, 2007). On the other hand, chronic macroeconomic and political instabilities lasting over more than three decades for larger Turkish companies have to account for developing ownership-specific assets and internalizing those specific assets through outward FDI (Erdilek, 2003).

Turkey not only actively invests regionally, particularly in West and Central Asia, but also in new markets in the European Union (EU), the USA, the Balkans, West Asia, North Africa, the Russian Federation and the newly independent Turkish republics in Central Asia (Erdilek, 2003). Especially after the liberalization period, most emerging MNEs have enhanced their operations in emerging economies and developed economies, as can be seen in the white goods sector. Mabe, Arçelik and Haier (from Mexico, Turkey and China, respectively) are examples of successful multinationals that managed to upgrade their operations, evolving from the production of simple goods to

new product lines developed through their own design, branding and marketing capabilities (Bonaglia *et al.*, 2006, p. 2). This study also provides meaningful insight into emerging multinationals and their management styles in different market contexts in Turkey.

Turkey's outward FDI gained momentum from 2003 to 2008. Corporate governance codes came into effect at the Istanbul Stock Exchange (ISE) in 2003. The codes of good governance provide protection for shareholders and other interests in terms of accountability and transparency. Therefore, this study focuses on 2004-2008 data which reflect post-financial crisis period. Using a sample of publicly listed Turkish companies after the period of financial crisis and the implementation of corporate governance codes, two different aspects of international diversification are considered in this study:

(1) the first one is the relationship between international diversification and financial performance; and

(2) the second one is the moderating effect of board composition on the relationship between international diversification and the firm's financial performance.

Consequently, our study enhances knowledge regarding multinational firms in emerging economies during periods of institutional change. This study helps to understand how board characteristics affect the choice of international diversification decisions, and the results allow us to assess the performance implications of these choices for a particular period.

This paper is organized into four sections. The first section provides an evaluation of the effects of financial crisis and corporate governance mechanisms in Turkey. The second one involves conceptual framework and hypotheses. The third section introduces the research method and analytical strategies used in this study and presents key descriptive statistics and empirical analyses. Finally, the fourth section summarizes the main findings and offers some practical and theoretical recommendations for future research.

2. FDI by Turkish firms: the effects of financial crisis and corporate governance

2.1 Institutional change and financial crisis in Turkey

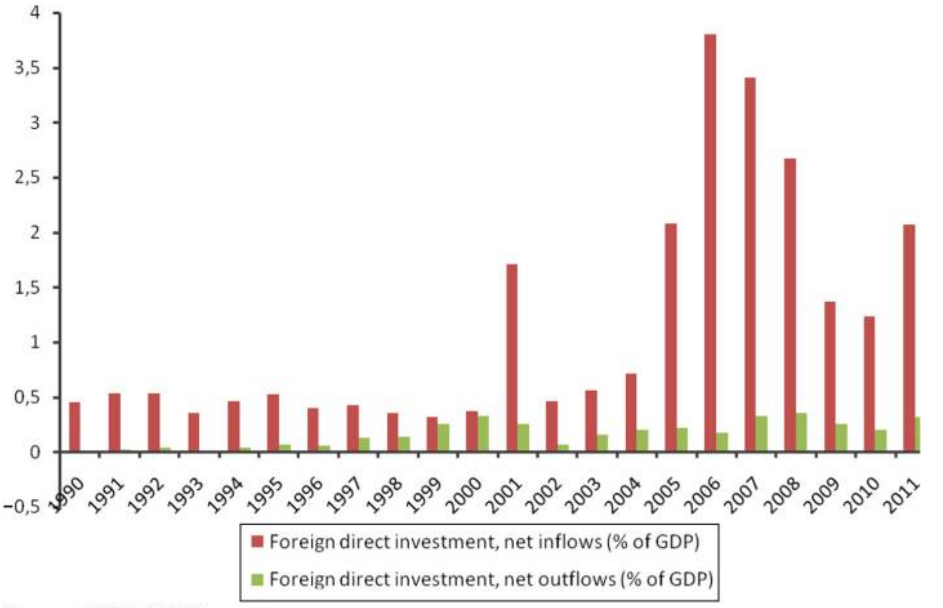
Turkey has experienced several crises for about two decades to secure economic growth and financial stability. The first important crisis was the year of 1994, which was a signal of the forthcoming economic turmoil. High interest, inflation rates and open capital account exacerbated volatility in financial markets. Therefore, the combination led to an important crisis in 1994. The second crisis followed the 2001 political crisis, which led to a massive withdrawal of funds. The November 2000 and February 2001 crises were experienced, although the International Monetary Fund's stand-by program was followed. The condition of the Turkish economy at that time could be defined with high regulation, interest rates, monitored foreign exchange operations, limited foreign asset ownership, barriers against foreign investment, insufficient liquidity, chronic inflation and trade deficit. Turkey began a new economic program in 2000, but that program failed in November 2000 as a result of a liquidity crisis that emerged as a sudden capital outflow. The cause of the crisis was the combination of a fragile banking sector and a set of triggering factors (Temiz, 2009; Özatay and Sak, 2002; Yeldan, 2004). The third crisis occurred in 2008 following the mortgage crisis in the USA (Rodrik,

2009). The third crisis began in the USA in the housing market with excessive lending to weak investors and spread through the rest of the world afterwards.

According to Erdilek (2003), Turkish outward FDI accelerated following the 1994 economic crisis and increased much faster than inward FDI. New external markets and the ability of the Turkish private sector are important motivations to invest abroad. Currently, Turkey's unattractive FDI environment, which has been caused by political and economic instability as well as historical and cultural biases, shows significant improvement. Figure 1 shows the changes of economic and political stability with changes in FDI for Turkey as a host and home country environment. Turkish inward FDI rose and fell until 2003; thereafter, the inflow of FDI accelerated until 2008. Demirbag *et al.* also (2009, p. 446) stated that "total FDI entries have increased dramatically because the start of the accession negotiations between Turkey and the EU (European Union) in December 2004". A similar trend has also been observed in Turkey's outward FDI. As can be seen from Figure 1, Turkey's outward FDI gained momentum from 2003 to 2008. Therefore, this study focuses on the post-financial crisis period and evaluates the firm's internalization performance through outward FDI decision related to financial crisis.

2.2 Corporate governance mechanism in Turkey

Investment flow is affected by a mix of legal factors and levels of corruption in both Eastern and Western countries. Despite the strong performance of China, for example, corruption still limits potential investments (Floyd and Summa, 2007). The host country should seek to control or regulate investment through foreign investment law. China has enacted foreign investment codes to screen foreign investment (Floyd and Summan,



Source: WDI (2012)

Figure 1.
The changes in stability with FDI inflows and outflows for Turkey, 1990-2011

2007). On the other hand, some regulations take into account the issue of corporate social responsibility and governance in the host country.

The main purpose of these codes is to protect shareholders and other interests in terms of accountability and transparency. As illustrated in Table I, corporate governance codes came into effect at the ISE in 2003. As in other emerging countries, the protection of minority shareholders is a weakness in Turkish governance (Ararat and Uğur, 2003). As can be seen in Table I, Korean, Taiwanese, Chinese and Turkish corporate governance models are similar to each other. China is different from Korea, Taiwan and Turkish in ownership structure. Especially, the government is a major shareholder, but family and social network ties are important relationships (Cheung *et al.*, 2008, 2010). Turkey has been labeled as an insider system due to large family-owned shareholdings (Demirağ and Serter, 2003; Kula and Tatoğlu, 2006; Gönençer, 2008) and due to the fact that most Turkish trade companies exhibit highly concentrated and centralized ownership structures (Yurtoglu, 2000).

Ownership is highly concentrated, and family ownerships are important features of the Turkish business system. Boards are dominated by insiders; however, outsider representation has tended to increase, especially after the financial crisis. Therefore, the chances in governance mechanism will have a positive effect on the internationalization–performance relationship. In the USA, for example, outsider and independent director ratios are usually high due to ownership concentration and dominant owners. In Korea, Taiwan and Turkey, chief executive officers (CEOs) are usually family members and close relatives, but professional managers tend to be CEOs in the American corporate governance mechanism. Japan's corporate governance mechanism lies between the USA and other emerging countries. Therefore, emerging multinationals tend to resemble each other in board composition after the financial crisis period. Our study investigates how corporate governance mechanisms affect outward investment decisions and performance on the national level in the emerging country context.

3. Literature review and research hypothesis

3.1 The effect of international diversification on financial performance

The relationship between international diversification and firm performance has received much more attention in international strategic management literature; however, findings have been mixed (Hitt *et al.*, 2009). Currently, researchers suggest a more complex relationship between international diversification and firm performance, resembling U-shaped (Capar and Kotabe, 2003; Ruigrok and Wagner, 2003; Lu and Beamish, 2004), inverted U-shaped (Hitt *et al.*, 1997) and S-shaped (Lu and Beamish, 2004; Contractor *et al.*, 2003; Riahi-Belkaoui, 1998) curves. In recent years, some researchers have stated that there are requirements for understanding the role of home country environments in the links between international diversification and firm performance (Wan, 2005; Wan and Hoskisson, 2003; Kim *et al.*, 2008; Hunya, 2000). Kim *et al.* (2008, p. 12) and Hitt *et al.* (1997) stated that "emerging economy firms may be less capable of overcoming the liability of foreignness", as they increase international diversification by entering into different geographical regions. Accordingly, they develop a hypothesis corresponding to a negative relationship between international diversification and firm performance. Therefore, findings between internalization and

Table I.
Comparison of corporate governance models for financial crisis

Dimensions of corporate governance models	Emerging countries				Advanced countries	
	Korea	Turkey	Taiwan	China	USA	Japan
Ownership concentration	High	High	High	High	Low	Moderate
Dominant owners	Family and affiliated group firms	Family and affiliated group firms	Family and affiliated group firms	Government major shareholder and family	Institutional investors	Main banks and affiliated groups firms
Board composition and board size	Inside directors and family member	Large (family members and associates)	Large (independent directors and shareholders)	Executive and non-executive directors	Outside and independent directors	Inside directors (employees and bank representatives)
Insider representation	Dominated by insiders (before the financial crisis	Dominated by insiders and non-executives (before the financial crisis	Dominated by insiders directors (family members and associates)	Dominated by insiders (executive directors)	Limited	Dominated by insiders (employees and bank representatives)
Outsider representation	Increasing outsider representation (after the financial crisis)	Increasing outsider representation (after the financial crisis)	Increasing outsider representation (after the financial crisis)	Moderate and high proportion of independent non-executive directors	Dominated by outsider and independent directors	Dominated by insiders (employees and bank representatives)
CEO (board chair) background	Family members and close relatives	Family members and close relatives	Family members and close relatives	Moderate (CEO duality)	Professional managers (CEO duality)	Long-term employees
Country of origin of legal system	Legal system of German origin (civil law)	Legal system of French origin (civil law)	Legal system of German origin (civil law)	Legal system a mixture of civil law and socialist law	Legal system of English origin (common law)	Legal system of German origin (civil law)
Year of adoption of worldwide code	1997 (first) 2004 (revised version)	2003 (first)	2002 (first)	2001 (first) 2004 (revised version)	1997 (first) 2007 (revised version)	1998 (first) 2008 (revised version)

Sources: ECGN (2008); World Bank (2008); La Porta *et al.* (1998); Litch *et al.* (2008), Sherman *et al.* (1998a), 1998b; Lien *et al.* (2005); Filatotchev *et al.* (2007); Musteen *et al.* (2009); Rhoades and Rechner (2001); Tihanyi *et al.* (2003); Luo *et al.* (2009); Kim *et al.* (2008); Ararat and Ügur (2003); Demirağ and Serter (2003); Yurtoglu (2000) and present study for Turkey, Cheung *et al.* (2008); Cheung *et al.* (2010); Klings and Weitzel (2011)

performance are inconclusive due to the selection of different industrial periods and motivations for international diversification in different studies (Hitt *et al.*, 2009).

Taking into consideration institutional context and internalization strategy as a latecomer for Turkey' FDI, we have to rely on various theoretical explanations. In particular, institutional theory explains the selection of investment location, as the existence of ethnic and cultural ties can play a significant role in the decision of MNEs to invest abroad (Amighini *et al.*, 2007; Aykut and Goldstein, 2006; Bonaglia *et al.*, 2006; Battat and Aykut, 2005). They tend to invest near their home country, especially where they have acquired a certain familiarity through trade or ethnic and cultural ties. For example, Russian investments abroad have primarily been in the countries of the former Soviet Union; Turkey has also been actively investing regionally, particularly in West and Central Asia, and companies from India and China have been particularly active in Asian countries. Also, institutional settings may be seen to affect all three parts of the eclectic paradigm. Institutional advantages should be separated from other ownership-specific advantages. The most direct link is location (L) advantages of the OLI (ownership-location-internalization) paradigm. The internalization (I) factor is already institutionalized at the micro level, but ownership-specific advantages are most difficult to deal with. As a result, institutions within the OLI paradigm can be an inclusive term under asset-based advantages as another form of organizational know-how (Dunning and Lundan, 2008, pp. 131-132).

As a result, there is a significant incentive to invest regionally for South-south FDI flows (Battat and Aykut, 2005). After the liberalization period, most MNEs have expanded their operations mainly within other emerging economies in the same region. For example, Turkey has increased its investments in emerging countries in the same region, particularly West and Central Asia and Russia (network or linkage advantage). Another important factor affecting international investing is the role of economic, ethnic and cultural ties (institutional-related advantage). On the other hand, new MNEs also invest beyond their immediate region, notably the white goods electronic sector in Turkey (learning advantage). Demirbağ *et al.* (2009, p. 458) provided strong support to the central argument that "emerging country MNEs use outward investment as a springboard to acquire strategic assets".

Therefore, emerging multinationals can overcome the liability of foreignness, as they increase international diversification by entering into similar geographical regions or cultural and ethnic ties. Accordingly, a positive relationship between international diversification and firm performance is hypothesized because Turkish multinational companies internalize for specific assets through outward FDI due to the chronic macroeconomic and political instability in the post-financial crisis period (Erdilek, 2003; Kosekahyaoglu, 2006; Dufour and Orhangazi, 2007).

H1. International diversification of a firm leads to better financial performance after the financial crisis period.

3.2 The moderating effects of a board of directors on FDI's international diversification and financial performance

There has been a considerable amount of literature published on the effects of boards of directors on FDI decisions or entry mode selections (Rhoades and Rechner, 2001; Musteen *et al.*, 2009; Filatotchev *et al.*, 2007; Lien *et al.*, 2005), but very little has been published on whether board composition affects the relationship between

internalization strategy and firm performance, especially in periods of financial crisis. For example, some emerging economies such as China and Eastern Europe transformed from planned economies to capitalist economies. Other emerging economies such as Korea that experienced the Asian financial crisis have liberalized their markets and adopted new corporate governance mechanisms that enhance corporate monitoring and transparency, and thereby have sought to improve their market-oriented institutions (Kim *et al.*, 2008). For example, before the financial crisis in Korea, boards were typically dominated by insiders and thus failed to play monitoring roles and to protect minority shareholders. Therefore, to increase independence and accountability, boards have been required to fill at least 25 per cent of their seats with outside directors. It is hypothesized:

H2. In the post-financial crisis period, corporate governance mechanisms positively moderate the relationship between international diversification and firm performance.

3.3 Independent outside directors

Dependent – independent directors in the board are widely held in different ways by researchers in corporate governance **(**Daily and Dalton, 1994; Davidson and Rowe, 2004). Daily and Dalton (1994, p. 1607) stated that "independent directors are outside directors who were appointed to board prior to a current CEO's appointment". Another description is made by Davidson and Rowe (2004) regarding "insiders and outsiders". Davidson and Rowe (2004, p. 52) described insiders as "inside directors who are also fund executives and serve in at least one of the following categories: management of the fund and management of the investment advisor" and outsiders as "outside directors who are not fund executives". Grey (1990) suggests the term "affiliated outsiders" for those "who have a close relationship with the firm or the CEO and have a required disclosure on the proxy statement of their relationship" (Tuggle, 2004, p. 19). Independent outsiders are described as an "independent outsider who has not any present direct business relationship with the corporation on whose board they serve" (Cohen, 1977, p. 837). Yildirim-Öktem and Üsdiken (2009) propose that "outsiderness" is an affiliated outsider director in a Turkish family holding. Also, the Corporate Governance Principles of Turkey (CGP) published by the Capital Board of Turkey state that the formation of the outside directors is independent outside directors. According to CGP, independent outside directors will be required to demonstrate independence of the board and recommended that "the board of directors be constituted from at least two independent members and that at least one third of the members fulfill the criteria for independence".

Board characteristics have been empirically linked to the decision to diversify internationally by means of FDI (Tihanyi *et al.*, 2003, 2000; Sanders and Carpenters, 1998). Finkelstein and Hambrick (1996) propose that the board makes important strategic decisions, such as acquisitions, divestitures and joint ventures. Most studies of corporate governance focus on the impact of board composition and on firm performance. These performance outcomes are also a function of the firm's strategic decisions, and it might be useful to consider moderator effects on internationalization and financial performance. Prior studies have indicated that outside directors affect diversification, corporate restructuring, FDI strategic choices and entry mode selection (Hill and Snell, 1988; Hoskisson *et al.*, 1994; Pearce and Zahra, 1992; Rhoades and Rechner, 2001; Musteen *et al.*, 2009; Filatotchev *et al.*,

2007; Lien *et al.*, 2005). Tihanyi *et al.* (2003) propose that outside and inside board members have moderator effects on institutional ownership and international diversification. Sherman *et al.* (1998a) predicted a positive relationship between the proportion of independent directors and a firm's degree of international activity, but they did not provide any significant support for this hypothesis. Sherman *et al.* (1998b, p. 32) stated that "inside board members were also significantly associated with increased internationalization", contrary to their expectations. Rhoades and Rechner (2001, p. 314) predicted "a positive relationship between the proportion of outside directors and selection of higher risk-higher performance modes of entry"; however, they found partial support for the effects of governance. As mentioned before, informational asymmetries and risks associated with international diversification strategy can cause potential conflicts between managers and owners, as predicted by agency theory. Lien *et al.* (2005, p. 746) propose that "a greater degree of the directors and supervisors in the large family have a positive effect upon decision to foreign direct investment"; however, they did not find any significant results in China. In the context of internationalization, some authors (Tihanyi *et al.*, 2003; Musteen *et al.*, 2009) observed that higher representation of independent outside directors in the board increases the odds of taking more risks in their international diversification efforts. Unfortunately, empirical evidence does not offer consistent findings in previous literature; higher risk creates a higher return, profitability and market prices. Thus, the next hypothesis is:

H2a. In the post-financial crisis period, independent outside directors moderate the relationship between international diversification and firm performance; the relationship will be stronger (positive) for firms with higher representation of independent outside directors on their boards.

3.4 Board size

Board size is one of the important dimensions of board composition in the current literature. Empirical evidence supports the idea that financial performance and board size are negatively correlated (Yermack, 1996; Eisenberg *et al.*, 1998; Cheng *et al.*, 2008; Andres *et al.*, 2005), but some results are contradictory (Dehaene *et al.*, 2001; Kaymak and Bektas, 2008; Kula, 2005). This negative correlation is confirmed by the agency theory, which has been a dominant theory in economic and finance literature (Hermalin and Weisbach, 2000). Social psychology literature proposes that larger board size leads to communication and coordination problems (Jensen, 1993). On the other hand, a large board decreases both the ability and incentives to control management (Cheng *et al.*, 2008). According to the resource dependence theory, a larger board leads to new resources and skills when a firm is faced with environmental uncertainty and turbulence (Zahra and Pearce, 1989; Peng, 2004; Filatotchev *et al.*, 2001). Sherman *et al.* (1998a, p. 321) predicted that a large board is positively associated with the degree of internalization in a turbulent environment, according to the resource dependence theory, but they do not provide any significant support for this hypothesis. Also, Lien *et al.* (2005) predicted that board size may have a positive effect on decisions regarding FDI and found only limited empirical support for undertaking FDI. Based on the literature, the next hypothesis is:

H2b. In the post-financial crisis period, board size moderates the relationship between international diversification and firm performance; the relationship will be stronger (positive) for firms with larger board sizes.

3.5 CEO turnover

The replacement of top executives is an important decision, as a large number of studies have predicted a positive relationship between CEO turnover and poor performance (Hermalin and Weisbach, 2000). CEO turnover can be voluntary or involuntary, but strategic change leads to CEO turnover. To better this understanding, Weisbach (1988) investigated board composition and firm performance in a CEO turnover equation. His results indicate that CEO turnover is more sensitive to firm performance in outsider-dominated boards, while smaller boards are more effective overseers of CEO turnover than larger boards (Hermalin and Weisbach, 2000, pp. 8-9). Therefore, a CEO who performs poorly is more likely to be replaced than one who performs well (Hermalin and Weisbach, 2000; Kim *et al.*, 2008). Therefore, the next hypothesis is:

H2c. In the post-financial crisis period, CEO turnover moderates the relationship between international diversification and firm performance; the relationship will be stronger (positive) for firms replacing a CEO.

As Figure 2 illustrates, the primary research focus of our paper is to investigate the moderating role of a board of directors on FDI's international diversification.

4. Research methods

4.1 Data sources and sample selection

A sample of Turkish multinational firms with FDI was used. Firm-level data were obtained from the ISE in Turkey. All companies listed on the ISE are required to submit annual reports to make reliable and comprehensive sources of data. The available series

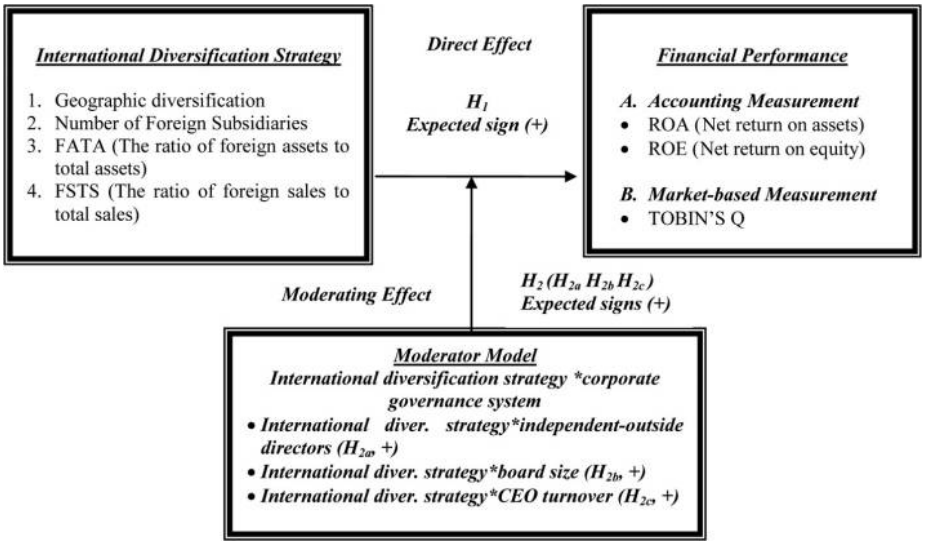


Figure 2.
Research model

include performance measures and financial accounting data as well as data on ownership, board structure and FDI. On the other hand, concerning board composition, data were obtained via corporate governance compliance reports, which are published by the ISE for listed companies. These reports are not mandatory for listed companies. The sample was selected from at least one minority joint venture in 2004 and samples selected from all listed MNEs. First, entry mode was coded (least to most risk) as follows: 1 = minority joint ventures; 2 = (50-50) equal joint ventures; 3 = majority joint ventures; 4 = acquisition, wholly owned and Greenfield operations. Partial acquisition was not considered in this study. Our sample consists of 59 firms, all of which possessed foreign operations in host countries after the corporate governance codes. However, only 51 firms had data on all independent and control variables. Therefore, data for all independent and control variables were collected from 2004 through 2008 for 51 FDIs. Table II reveals sample characteristics for 2008. It can be seen that the most invested-in countries are Holland, Germany and Russia. The most common type of entry mode selection is full ownership. The distribution of ownership is minority foreign-owned (20), co-ownership (8), majority foreign-owned (19) and full ownership (51). The number of foreign subsidiaries is 98 for the year 2008.

		The type of entry mode selection			
Host countries	The number of foreign subsidiary	< 50% (minority)	= 50% (equal)	> 50% (majority)	100% (whole)
Holland	16	2	1	2	11
Germany	15	7		1	7
Russia	12	2	3		7
USA	8	3		1	4
Cyprus	7	2	1	3	1
UK	6	1		2	3
Bulgaria	5		2	2	1
Romania	4			2	2
Ukraine	3				3
China	3			1	2
Spain	2	1			1
Sweden	2				2
Azerbaijan	2				2
Egypt	2	1		1	
Italy	2		1		1
Belgium	1			1	
Indonesia	1			1	
Dubai	1				1
Kazakhstan	1				1
Cayman Islands	1				1
Austria	1	1			
Bosnia Herzegovina	1			1	
Belarus	1			1	
India	1				1
Total	98	20	8	19	51

Table II. Sample characteristics

4.2 Operationalization of the variables

4.2.1 Dependent variables

4.2.1.1 Performance measurement. Accounting measures of performance have been criticized as too easily manipulated by managers (Cochran and Wood, 1984). In contrast, market-based measures are typically viewed as somewhat more robust, given that they are not subject to direct manipulation by the management (Muth and Donaldson, 1998). Therefore, this study used both accounting- and market-based measures. Net return on assets was calculated as the ratio of net profit to total assets (ROA: net return on assets). Similarly, measuring firm's efficiency at using investment funds to create increased earnings, return on equity was calculated as the ratio of net profit to equity (ROE: net return on equity). Market value was calculated as shown below:

Tobin's q = [market value (equity) + book value (assets) − book value (equity)]/ book value (assets) (Tobin's q: the market value of common stock shares outstanding; PS: the book value of the firm's outstanding preferred stock; DEBT: the book value of debt; TA: the book value of the total assets) (Kim *et al.*, 2008).

4.2.2 Explanatory variables. There has been no agreement as to the measure of international diversification (Hitt *et al.*, 2006). Therefore, several measurements were used in this study. Geographic diversification is defined as the number of geographic regions where a firm had foreign subsidiaries (Kim *et al.*, 2008). Regarding the Kim *et al.* (2008) study, host countries were categorized into the following regions: Asia and the Pacific, the Middle East, Europe, North America, South America and Africa. Another international diversification measure is the number of host countries or foreign subsidiaries (Lu and Beamish, 2004). Other multidimensional measures of the transnational index are composed of FATA, FSTS and FETE and are published annually by the World Investment Report. FETE, which is the ratio of foreign employees to total employees, is not calculated in this study due to the lack of data. Others were calculated in our study. FATA is the ratio of foreign assets to total assets, and FSTS is the ratio of foreign sales to total sales.

4.2.3 Control variables. Risk measurement (risk) is an index that is calculated by mode of entry/number of foreign subsidiaries (Rhoades and Rechner, 2001). Research and development intensity (R&D expenditures/total sales) was controlled to consider the effect of tangible assets on firm performance. Firm size (size of firm: captured by the logarithm of total sales) and firm age (age of firm: captured by the logarithm of firm's age) were also controlled to consider the effects of an organization's age and size on firm performance. Business group affiliation (affiliation) was created using a dummy variable.

4.2.4 Moderator variables (corporate governance variables). Board composition was measured with three different dimensions. Board size (board size) shows the number of people on the board. Following the CMBT (Capital Markets Board of Turkey) statements (2005, p. 49), the proportion of independent members (indepoutside) indicates the percentage of independent directors. Therefore, being an "independent or inside" member refers to the definition made by the CMBT. In the study, CEO turnover data were coded as a binary variable, meaning that if CEOs are changed by the board of directors, then it is accepted that there is a CEO turnover and coded with score of "one"; otherwise, a "zero" was recorded. The CEO duality concept is used in implying whether CEO and chairman roles were performed by different persons or not. If CEO and chairman functions are performed by the same person, then there is a CEO – chairman

duality, and this structure is also known as a one-tier board system. Following the CMBT statement, CEO and chairman roles should be separated. Therefore, we coded chairman position as a CEO turnover managing for operational process.

4.3 Model specification

To investigate the hypothesized moderating role of "corporate governance mechanism", an adapted version of the procedure described by Baron and Kenny (1986) was utilized (Fraizer *et al.*, 2004; Tepper and Taylor, 2003; Thwaites and Dagnan, 2004; Kim *et al.*, 2008). As can be seen from Table III, this procedure tests the existence of a moderating relationship via a hierarchical regression equation in which the following variables are regressed onto the target variable. The control variables are first entered to see effect on dependent variables. At the first level, the predictor (international diversification strategy) is entered. At the second level, the variable hypothesized to be a moderator is entered (corporate governance features), and finally, the product of the previous two variables (interaction effect) is entered. Baron and Kenny (1986) suggest that if the final step is significant once the previous two variables have been controlled, this supports the role of the variable in moderating the predictor and target variables.

Panel data analysis was used to test the above hypothesis. Panel data refer to data for N different entities such as countries, firms or households, observed at T different periods. Panel data methodology is typically applied when the sample of countries, firms or households N is typically and relatively large and when the number of periods T is generally short. A sample panel data equation can be shown as follows:

$$Y_{it} = \alpha_{it} + \beta_{kit} X_{kit} + \ldots + \beta_{Kit} X_{Kit} + \varepsilon_{it} \quad (1)$$

i= 1 …… N; t= 1 …… T; k= 1 …… K.

Where i denotes cross-sections such as countries, firms or households, and t denotes periods with i = 1, 2 …… N, and t = 1, 2 …… T. Y_{it} shows i^{th} economic unit's t period dependent variable's value, and X_{kit} shows i^{th} economic unit's t period k^{th} independent variable's value. The error terms ε_{it} are assumed to be independent and identically distributed. $N(0,\sigma_{\varepsilon}^2)$.

Static panel data estimation is performed by using fixed-effects and random-effects models in literature. Random-effects models were used because of data structure. The models we used in the study are as follows:

Model 1:

$$FP_{it} = \alpha_{it} + \beta_1 IDS_{it} + \beta_2 CGS_{it} + \beta_3 X_{it} + \varepsilon_{it} \quad (2)$$

Model 2:

$$FP_{it} = \alpha_{it} + \beta_1 IDS_{it} + \beta_2 CGS_{it} + \beta_3 IDS{*}CGS + \beta_4 X_{it} + \varepsilon_{it} \quad (3)$$

In the equations above, FP denotes financial performance, IDS is international diversification strategy, CGS is corporate governance system, IDS × CGS is international diversification strategy multiplied by corporate governance system, X is control variables (age of firm, size of firm, R&D, risk and affiliation) and ε_{it} are error terms.

Direct relationship: Test of *H1*	Step 1 Financial performance: $\beta_o + \beta_1$ international diversification strategy $+ \beta_2$ control variables
International diversification strategy and financial performance	
Moderating relationship: Test of *H2*	Step 1 Financial performance: $\beta_o + \beta_1$ international diversification strategy $+ \beta_2$ corporate governance $+ \beta_3$ control variables
Moderating effects of corporate governance	Step 2 Financial performance: $\beta_o + \beta_1$ international diversification strategy $+ \beta_2$ corporate governance $+ \beta_3$ control variables $+ \beta_4$ international diversification strategy*corporate governance system

Predictors	Dependent variables	Independent variables		
	Financial performance	International diversification strategy	Corporate governance system	Control variables
	ROA (net return on assets)	Geographic diversification	Board size (the number of people on the board)	Risk measurement (type of entry mode/number of foreign
	ROE (net return on equity	Number of foreign subsidiaries	Independent outside director (percentage of independent director)	Research and development intensity (R&D expenditures/ total sales)
	Tobin's q	FATA (the ratio of foreign assets to total assets)	CEO turnover	Size of firm (the logarithm of total sales)
		FSTS (the ratio of foreign sales to total sales)		Age of firm (the logarithm of firm's age)
				Business group's affiliation

Table III.
Research model

5. Findings

The correlation matrix provides the means, standard deviations and correlation matrix of the variables used in our analysis. The results show that board size averages approximately seven members. Our data indicated that the number of outside directors

is approximately one. Also, our sample has a 16 per cent turnover rate among firms. The ratio of foreign assets to total assets (FATA) is 1 per cent, while the ratio of foreign sales to total sales (FSTS) is 8 per cent, which means that these ratios are quite low. The mean geographic diversification of the firms is 1.7, while the mean number of host countries or foreign subsidiaries is approximately 1.3, indicating a lower level of international diversification. Sixty-nine per cent of firms were affiliated with a business group. The proportion of R&D is approximately 1 per cent, which means that R&D investment is considerably low. Descriptive statistics demonstrate that firms' profitability is low in terms of ROA and ROE, with approximately 1 per cent and −8 per cent, respectively. The mean of Tobin's q is about 6.8, indicating an above average level.

Table IV reveals a number of significant correlations among the variables. As can be seen, the highest Pearson correlation coefficient is between geographic diversification and the number of foreign subsidiaries (r: 0.786). On the other hand, none of the variables has a correlation coefficient exceeding 0.50. Gujarati (1995, p. 335) and Kennedy (1999, p. 187) suggested that co-linearity should not be considered harmful until the correlation coefficient exceeds 0.8 or 0.9. Because the highest Pearson correlation in this study is below the cutoff point of 0.8, multicollinearity does not appear to be a serious problem in interpreting the regression results.

An important significant finding, the size of the firm, depicted as a control variable for all models, is positively related to ROA ($p < 0.01$) and ROE ($p < 0.05$), implying that greater firm size leads to better financial performance in terms of ROA and ROE. Also, it is seen that the firm's age (age of firm, $p < 0.05$) exhibits a significantly negative relationship with Tobin's q, which means that higher firm age leads to lower market value.

As can be seen in Table V for Models 1, 4 and 7, international diversification (geographic diversification) was estimated against ROA, ROE and Tobin's q, and the results show that ROA, ROE and Tobin's q have no statistically positive relationship with international diversification (geographic diversification). This finding is not consistent with the predictions in *H1*. In addition, all variables used for interaction terms also provided moderating effects. Models 3, 6 and 9 were used to estimate the impact of international diversification on each of the proposed interactions. *H2a* suggests that adequate representation of independent outside directors will positively moderate the relationship between international diversification and a firm's financial performance. In Model 3, the interaction between international diversification (geographic diversification) and proportion of independent outside directors had a negative and statistically significant effect on ROA ($p < 0.10$). These results do not provide support for *H2a* in terms of geographic diversification and ROA. In Tables V and VI for Models 4 and 13, firm size (size of firm) is marginally positively related to ROE ($p < 0.1$), and in Tables VII and VIII, for Models 22 and 31, positively related to ROE ($p < 0.05$). This means that larger firm size (size of firm) at least partially increases ROE.

Similarly, in Table VI, in Models 10, 13 and 16, international diversification was estimated against ROA, and the results suggest that ROA has no statistically significant relationship with international diversification (the number of foreign subsidiaries); these results do not provide support for *H1*. Also, in Model 12, the interaction between international diversification (the number of foreign subsidiaries) and proportion of outside directors had a significantly negative relationship with ROA ($p < 0.01$). These results do not provide support for *H2a* in terms of the number of foreign subsidiaries and ROA. *H2b* suggests that board size will positively moderate the relationship between international

Table IV.
Descriptive statistics of variables

Variables	Mean	SD	Size of firm	CEO turnover	FATA	Age of firm	FSTS	Affiliation	Geographic diversification	Foreign subsidiaries	Outside director	R&D	Risk	ROA	ROE	Size of firm	Tobin's q
Size of board	6.990.476	1.722.329	1.000														
CEO turnover	0.161905	0.369244	0.078	1.000													
FATA	0.010897	0.036693	−0.253	0.130	1.000												
Age of firm	3.695.238	1.206.631	0.257	0.180	−0.096	1.000											
FSTS	0.088211	0.227204	−0.136	0.029	0.726	−0.014	1.000										
Affiliation	0.690476	0.463402	−0.052	0.071	−0.039	−0.011	−0.203	1.000									
Geographic diversification	1.766.667	1.665.247	0.346	0.077	−0.015	0.231	−0.090	0.098	1.000								
Foreign subsidiaries	1.295.238	0.805766	0.233	0.080	−0.030	0.250	−0.097	0.297	0.786	1.000							
Outside director	1.200.000	1.066.228	0.071	−0.010	0.085	−0.387	−0.011	−0.010	−0.173	−0.236	1.000						
R&D	0.014478	0.055097	0.147	0.028	0.065	0.264	0.070	−0.105	0.111	0.098	−0.010	1.000					
Risk	2.653.381	1.603.444	0.120	0.090	0.058	0.129	0.074	−0.087	0.511	0.454	0.139	0.088	1.000				
ROA	0.018060	0.118472	0.295	0.005	0.001	−0.045	0.114	0.092	0.112	0.091	−0.016	0.067	0.119	1.000			
ROE	−0.081672	1.245.876	0.138	0.042	−0.066	0.072	0.010	−0.062	0.071	0.062	−0.037	−0.013	0.061	0.302	1.000		
Size of firm	1.39E+09	2.52E+09	0.412	0.189	−0.023	0.409	0.053	0.093	0.400	0.376	−0.007	0.119	0.248	0.159	0.081	1.000	
Tobin's q	0.686616	0.492860	0.224	−0.020	0.050	0.004	0.110	−0.043	0.056	−0.071	0.008	−0.291	0.028	0.236	0.110	−0.052	1.000

Independent variables	Dependent variable: ROA				Dependent variable: ROE				Dependent variable: Tobin's q			
	Control variables coefficient	Model 1 coefficient	Model 2 coefficient	Model 3 coefficient	Control variables coefficient	Model 4 coefficient	Model 5 coefficient	Model 6 coefficient	Control variables coefficient	Model 7 coefficient	Model 8 coefficient	Model 9 coefficient
Age of firm	−0.030	−0.029	−0.051*	−0.046*	0.164	0.161	0.054	0.071	−0.279	−0.270**	−0.320**	−0.331**
	(−1.12)	(−1.070)	(−1.810)	(−1.630)	(0.834)	(0.816)	(0.248)	(0.319)	(−2.09)**	(−2.030)	(−2.390)	(−2.430)
Size of firm	0.019***	0.020***	0.017***	0.017***	0.095**	0.090*	0.072	0.071	−0.024	−0.022	−0.031	−0.033
	(3.44)	(3.460	(2.790)	(2.640)	(2.05)	(1.880)	(1.280)	(1.230)	(−0.957)	(−0.833)	(−1.160)	(−1.220)
R&D	0.142	0.137	0.150	0.136	−1.849	−1.842	−1.624	−1.834	−0.038	−0.114	−0.215	−0.196
	(0.836)	(0.796)	(0.875)	(0.798)	(−1.17)	(−1.170)	(−1.020)	(−1.140)	(−0.053)	(−0.157)	(−0.297)	(−0.270)
Risk	0.002	0.004	0.007	0.008	0.001	−0.009	0.010	−0.013	0.009	0.016	0.027	0.023
	(0.477)	(0.684)	(1.250)	(1.150)	(0.028)	(−0.163)	(0.167)	(−0.207)	(0.459)	(0.652)	(1.110)	(0.789)
Affiliation	0.010	0.012	0.016	0.021	−0.176	−0.186	−0.163	−0.174	−0.127	−0.122	−0.106	−0.122
	(0.463)	(0.526)	(0.762)	(0.983)	(−1.13)	(−1.180)	(−1.030)	(−1.040)	(−1.14)	(−1.090)	(−1.010)	(−1.120)
Geographic diversification		−0.003	−0.007	−0.006		0.019	0.0005	−0.015		−0.012	−0.019	−0.032
		(−0.539)	(−1.110)	(−0.839)		(0.377)	(0.010)	(−0.215)		(−0.478)	(−0.747)	(−1.010)
Size of board			0.080*	0.088**			0.364	0.329			0.343*	0.318*
			(1.910)	(2.020)			(0.982)	(0.832)			(1.880)	(1.660)
CEO turnover			0.0001	−0.022			0.069	0.110			0.034	−0.038
			(0.007)	(−0.780)			(0.354)	(0.351)			(0.527)	(−0.338)
Outside director			−0.018*	−0.007			−0.068	−0.036			−0.044	−0.058
			(−1.830)	(−0.572)			(−0.858)	(−0.379)			(−1.010)	(−1.080)
Geographic diversification* size of board				0.010 (0.649)				0.108 (0.743)				0.003 (0.042)
Geographic diversification * outside director				−0.026* (−1.680)				−0.057 (−0.413)				0.034 (0.504)
Geographic diversification * CEO turnover				0.025 (1.010)				−0.036 (−0.134)				0.075 (0.755)
Constant	−0.268*	−0.284*	−0.290**	−0.325**	−2.438	−2.337**	−2.242*	−2.331*	2.225***	2.137***	1.870***	2.018***
	(−1.88)	(−1.940)	(−1.980)	(−2.150)	(−2.18)**	(−2.030)	(−1.920)	(−1.870)	(3.28)	(3.130)	(2.730)	(2.850)
F-test (Wald-test)	20.78***	20.9***	27.8***	31.2***	7.0	7.2	8.9	9.5	7.5	7.7	12.1	13.1
R^2	0.08	0.08	0.10	0.12	0.2	0.03	0.04	0.04	0.03	0.03	0.05	0.05
Adj. R^2	0.06	0.06	0.07	0.08	0.18	0.01	0.004	0.01	0.01	0.01	0.02	0.002
Number of observations	255	255	255	255	255	255	255	255	255	255	255	255

Notes: ***; ** and * denote significance at 1, 5 and 10% levels, respectively. Figures in parentheses indicate *t*-statistics

Table V.
International diversification (geographic diversification) results for ROA, ROE and Tobin's q

Table VI.
International diversification (the number of foreign subsidiaries) results for ROA, ROE and Tobin's q

	Dependent variable: ROA				Dependent variable: ROE				Dependent variable: Tobin's q			
Independent variables	Control variables coefficient	Model 10 coefficient	Model 11 coefficient	Model 12 coefficient	Control variables coefficient	Model 13 coefficient	Model 14 coefficient	Model 15 coefficient	Control variables coefficient	Model 16 coefficient	Model 17 coefficient	Model 18 coefficient
Age of firm	−0.030	−0.027	−0.050*	−0.040	0.164	0.157	0.054	0.077	−0.279	−0.271**	−0.320**	−0.302**
	(−1.12)	(−1.00)	(−1.810)	(−1.50)	(0.834)	(0.791)	(0.250)	(0.352)	(−2.09)**	(−2.020)	(−2.400)	(−2.270)
Size of firm	0.019***	0.021***	0.020***	0.018***	0.095**	0.091*	0.072	0.071	−0.024	−0.019	−0.025	−0.026
	(3.44)	(3.620)	(3.030)	(2.90)	(2.05)	(1.870)	(1.240)	(1.230)	(−0.957)	(−0.706)	(−0.929)	(−0.942)
R&D	0.142	0.123	0.128	0.047	−1.849	−1.833	−1.622	−1.996	−0.038	−0.125	−0.304	−0.466
	(0.836)	(0.718)	(0.752)	(0.286)	(−1.17)	(−1.160)	(−1.020)	(−1.230)	(−0.053)	(−0.172)	(−0.420)	(−0.634)
Risk	0.002	0.006	0.009	0.009	0.001	−0.007	0.008	−0.005	0.009	0.022	0.035	0.027
	(0.477)	(0.984)	(1.560)	(1.390)	(0.028)	(−0.140)	(0.152)	(−0.091)	(0.459)	(0.898)	(1.410)	(0.971)
Affil.	0.010	0.018	0.026	0.030	−0.176	−0.199	−0.166	−0.164	−0.127	−0.096	−0.074	−0.074
	(0.463)	(0.804)	(1.170)	(1.360)	(−1.13)	(−1.180)	(−0.977)	(−0.958)	(−1.14)	(−0.826)	(−0.675)	(−0.685)
The number of foreign subsidiaries		−0.015	−0.024*	−0.035*		0.041	0.006	−0.068		−0.057	−0.077	−0.138
		(−1.16)	(−1.770)	(−1.650)		(0.355)	(0.051)	(−0.348)		(−0.992)	(−1.320)	(−1.460)
Size of board			0.078*	0.042			0.363	0.221			0.343*	0.290
			(1.890)	(1.000)			(0.994)	(0.560)			(1.900)	(1.490)
CEO turnover			−0.001c	−0.043			0.069	0.176			0.030	0.011
			(−0.070)	(−1.250)			(0.355)	(0.411)			(0.467)	(0.0794)
Outside dir.			−0.020**	0.024*			−0.066	0.035			−0.053	−0.035
			(−2.070)	(1.760)			(−0.830)	(0.270)			(−1.200)	(−0.551)
Foreign subsidiaries × size of board				0.054**				0.217				0.084
				(2.490)				(0.993)				(0.901)
Foreign subsidiaries × outside director				−0.10***				−0.237				−0.036
				(−4.270)				(−0.955)				(−0.363)
Foreign subsidiaries × CEO turnover				0.051				−0.131				0.025
				(1.340)				(−0.273)				(0.160)
Constant	−0.268*	−0.307**	−0.311**	−0.332**	−2.438	−2.335**	−2.232*	−2.303*	2.225***	2.010***	1.790***	1.767***
	(−1.88)	(−2.090)	(−2.140)	(−2.350)	(−2.18)**	(−2.020)	(−1.910)	(−1.910)	(3.28)	(3.030)	(2.630)	(2.600)
F-test (Wald-test)	20.78***	22.1***	30.1***	53.1***	7.0	7.2	8.9	10.3	7.5	8.5	13.5	14.7
R^2	0.08	0.08	0.11	0.18	0.2	0.03	0.04	0.04	0.03	0.03	0.05	0.06
Adj. R^2	0.06	0.06	0.08	0.14	0.18	0.01	0.004	0.01	0.01	0.01	0.02	0.01
Number of observations	255	255	255	255	255	255	255	255	255	255	255	255

Notes: ***, ** and * denote significance at 1, 5 and 10% levels, respectively. Figures in parentheses indicate *t*-statistics.

Table VII.
International diversification (FATA) results for ROA, ROE and Tobin's q

Independent variables Indep.VaR.	Dependent variable: ROA Control variables coefficient	Model 19 coefficient	Model 20 coefficient	Model 21 coefficient	Dependent variable: ROE Control variables coefficient	Model 22 coefficient	Model 23 coefficient	Model 24 coefficient	Dependent variable: Tobin's q Control variables coefficient	Model 25 coefficient	Model 26 coefficient	Model 27 coefficient
Age of firm	−0.030	−0.030	−0.050*	−0.053*	0.164	0.141	0.043	0.048	−0.279	−0.270**	−0.324**	−0.300**
	(−1.12)	(−1.100)	(−1.780)	(−1.910)	(0.834)	(0.718)	(0.198)	(0.218)	(−2.09)**	(−2.020)	(−2.46)	(−2.250)
Size of firm	0.019***	0.019***	0.016***	0.015**	0.095**	0.094**	0.078	0.064	−0.024	−0.021	−0.035	−0.042
	(3.44)	(3.440)	(2.600)	(2.390)	(2.05)	(2.040)	(1.400)	(1.110)	(−0.957)	(−0.820)	(−1.320)	(−1.560)
R&D	0.142	0.140	0.157	0.165	−1.849	−1.724	−1.560	−1.313	−0.038	−0.089	−0.248	−0.219
	(0.836)	(0.819)	(0.920)	(0.977)	(−1.17)	(−1.100)	(−0.984)	(−0.827)	(−0.053)	(−0.123)	(−0.348)	(−0.305)
Risk	0.002	0.002	0.004	0.003	0.001	0.005	0.010	−0.006	0.009	0.005	0.014	0.016
	(0.477)	(0.448)	(0.724)	(0.548)	(0.028)	(0.112)	(0.218)	(−0.124)	(0.459)	(0.225)	(0.685)	(0.756)
Affil.	0.010	0.010	0.014	0.017	−0.176	−0.180	−0.170	−0.130	−0.127	−0.124*	−0.105	−0.096
	(0.463)	(0.466)	(0.647)	0.836	(−1.13)	(−1.170)	(−1.090)	(−0.830)	(−1.14)	(−1.110)	(−1.02)	(−0.931)
FATA		0.043	0.203	1.898*		−2.171	−1.798	8.972		1.610*	2.331**	0.686
		(0.195)	(0.879)	(1.700)		(−1.030)	(−0.802)	(0.880)		(1.790)	(2.450)	(0.140)
Size of board			0.084*	0.094**			0.269	0.302			0.463**	0.451**
			(1.930)	(2.170)			(0.703)	(0.783)			(2.480)	(2.370)
CEOTurn.			−0.002	0.005			0.093	0.084			0.017	0.037
			(−0.108)	(0.285)			(0.472)	(0.400)			(0.272)	(0.540)
Outside dir.			−0.017*	−0.013			−0.064	−0.015			−0.055	−0.040
			(−1.740)	(−1.320)			(−0.851)	(−0.180)			(−1.280)	(−0.875)
FATA*size of board				(−0.950)				(−0.328)				(0.790)
				−0.248				−0.742				0.918
			(−0.950)				(−0.328)				(0.790)	
			(−1.570)				(−2.000)				(−0.746)	
FATA*CEO turnover				−0.358				1.365				−1.139
				(−0.927)				(0.288)				(−0.769)
Constant	−0.268*	−0.272*	−0.277*	−0.268*	−2.438	−2.318**	−2.125*	−1.970*	2.225***	2.114***	1.715***	1.753***
	(−1.88)	(−1.89)	(−1.890)	(−1.890)	(−2.18)**	(−2.080)	(−1.850)	(−1.700)	(3.28)	(3.110)	(2.560)	(2.630)
F-test (Wald-test)	20.78***	20.8***	27.2***	32.1***	7.0	8.2	9.6	13.8	7.5	10.7*	18**	20.1**
R^2	0.08	0.08	0.10	0.12	0.2	0.03	0.04	0.05	0.03	0.04	0.07	0.08
Adj. R^2	0.06	0.13	0.07	0.03	0.18	0.01	0.004	0.002	0.01	0.02	0.04	0.03
Number of observations	255	255	255	255	255	255	255	255	255	255	255	255

Notes: ***; ** and * denote significance at 1, 5 and 10% levels, respectively. Figures in parentheses indicate *t*-statistics

Table VIII.
International diversification (FSTS) results for ROA, ROE and Tobin's q

	Dependent variable: ROA				Dependent variable: ROE				Dependent variable: Tobin's q			
Independent variables Indep.VaR.	Control variables coefficient	Model 28 coefficient	Model 29 coefficient	Model 30 coefficient	Control variables coefficient	Model 31 coefficient	Model 32 coefficient	Model 33 coefficient	Control variables coefficient	Model 34 coefficient	Model 35 coefficient	Model 36 coefficient
Age of firm	−0.030	−0.030	−0.051*	−0.051*	0.164	0.161	0.054	0.043	−0.279	−0.279**	−0.330**	−0.332**
	(−1.12)	(−1.110)	(−1.820)	(−1.830)	(0.834)	(0.815)	(0.248)	(0.197)	(−2.09)**	(−2.080)	(−2.480)	(−2.450)
Size of firm	0.019***	0.019***	0.016**	0.015**	0.095**	0.097**	0.074	0.074	−0.024	−0.025	−0.040	−0.041
	(3.44)	(3.420)	(2.480)	(2.390)	(2.05)	(2.070)	(1.300)	(1.250)	(−0.957)	(−0.971)	(−1.460)	(−1.500)
R&D	0.142	0.142	0.164	0.166	−1.849	−1.840	−1.628	−1.537	−0.038	−0.037	−0.157	−0.121
	(0.836)	(0.832)	(0.962)	(0.978)	(−1.17)	(−1.170)	(−1.030)	(−0.965)	(−0.053)	(−0.051)	(−0.219)	(−0.168)
Risk	0.002	0.002	0.004	0.003	0.001	0.003	0.010	0.0006	0.009	0.006	0.014	0.014
	(0.477)	(0.451)	(0.706)	(0.588)	(0.028)	(0.064)	(0.207)	(0.013)	(0.459)	(0.308)	(0.691)	(0.640)
Affil.	0.010	0.010	0.015	0.017	−0.176	−0.183	−0.165	−0.158	−0.127	−0.119	−0.096	−0.093
	(0.463)	(0.474)	(0.707)	(0.785)	(−1.13)	(−1.170)	(−1.050)	(−1.000)	(−1.14)	(−1.060)	(−0.920)	(−0.881)
FSTS		0.005	0.030	0.167		−0.123	−0.043	0.949		0.143	0.264	0.742
		(0.142)	(0.801)	(1.090)		(−0.382)	(−0.130)	(0.698)		(0.891)	(1.570)	(1.090)
Size of board			0.083*	0.079*			0.351	0.304			0.423**	0.418**
			(1.910)	(1.820)			(0.925)	(0.793)			(2.220)	(2.160)
CEOTurn.			−0.001	0.004			0.070	0.089			0.024	0.034
			(−0.068)	(0.215)			(0.357)	(0.410)			0.024	0.034
Outside dir.			−0.016*	−0.011			−0.068	−0.029			−0.047	−0.028
			(−1.710)	(−1.050)			(−0.890)	(−0.345)			(−1.100)	(−0.573)
FSTS × size of board				−0.014				−0.089				−0.058
				(−0.237)				(−0.169)				(−0.218)
FSTS × outside director				−0.110				−0.873				−0.397
				(−1.310)				(−1.250)				(−1.030)
FSTS × CEO turnover				−0.058				−0.141				−0.110
				(−0.606)				(−0.128)				(−0.291)
Constant	−0.268*	−0.268*	−0.263*	−0.254*	−2.438	−2.449**	−2.247**	−2.142*	2.225***	2.219***	1.886***	1.914***
	(−1.88)	(−1.890)	(−1.830)	(−1.780)	(−2.18)**	(−2.180)	(−1.970)	(−1.850)	(3.28)	(3.270)	(2.820)	(2.840)
F-test (Wald-test)	20.78***	20.7***	27.2***	30.0***	7.0	7.2	8.9	10.6	7.5	8.3	14.3*	15.5*
R^2	0.08	0.08	0.10	0.11	0.2	0.03	0.4	0.04	0.03	0.03	0.06	0.06
Adj. R^2	0.06	0.06	0.07	0.07	0.18	0.01	0.4	0.01	0.1	0.01	0.03	0.01
Number of observations	255	255	255	255	255	255	255	255	255	255	255	255

Notes: ***; ** and * denote significance at 1, 5 and 10% levels, respectively. Figures in parentheses indicate *t*-statistics

diversification and firm performance. The statistically significant and positive coefficient for the interaction between these variables ($p < 0.05$) in Model 12 indicates support for *H2b*.

As can be seen in Table VII and VIII, FATA and FSTS do not lead to better financial performance (ROA and ROE), which does not support *H1* and *H2*. As shown in Tables V-VIII, international diversification measures (geographic diversification, foreign subsidiaries, FATA and FSTS) were estimated against ROE, and the results show that ROE has no statistical relationship with international diversification measures for all models. This finding is inconsistent with our predictions (*H1*). Also, in Table VII for Model 24, the interaction between international diversification (FATA) and proportion of outside directors had a significantly negative relationship with ROE ($p < 0.05$). These results do not provide support for *H2a* in terms of FATA and ROE. Furthermore, these results are consistent with not only geographic diversification and ROA but also foreign subsidiaries and ROA.

Results of Models 19, 20, 21, 28, 29 and 30 in Tables VII and VIII reveal that ROA is positively associated with firm size (size of firm, $p < 0.01$ and 0.05), while ROA is negatively associated with the firm's age in Models 21 and 30, as depicted by control variables in terms of ROA, FATA and FSTS. Tables V-VIII also present test results of the Tobin's q as a market-based dependent variable. Our results revealed that in Table VII for Model 25, Tobin's q has a statistically marginally positive relationship to international diversification (FATA, $p < 0.10$), consistent with our expectations in *H1*. Therefore, increasing a firm's international diversification strategy leads to higher Tobin's q, which translates to better market value.

As a result, *H1* predicts that international diversification will exhibit a positive relationship with a firm's financial performance, marginally consistent with our prediction; this relationship supports *H1* in terms of Tobin's q and FATA. *H2a* predicts that higher independent outside director ratios will moderate the relationship between international diversification and financial performance. The interaction between FATA, geographic diversification and outside directors has a negative and statistically significant effect on ROA and ROE. On the other hand, the interaction between the number of foreign subsidiaries and outside directors also has a negative and statistically significant effect on ROA, which means that *H2a* is not supported in terms of the number of foreign subsidiaries, geographic diversification and FATA. Also, *H2b* predicts that a larger board size will moderate the relationship between international diversification and financial performance, consistent with our predictions; this finding supports *H2b* in terms of the number of foreign subsidiaries and ROA.

H3b regarding CEO turnover moderating effects and the relationship between international diversification and financial performance do not support any model. As mentioned, control variables size and age of firm impact the relationship between international diversification and firm financial performance. Size of firm has a positive relationship between international diversification and financial performance. Age of firm has a negative relationship between international diversification and financial performance for all models.

6. Discussion and conclusion

Much of current research on the roles of the board has only been able to establish a relationship between board characteristics and choices of entry modes (Musteen *et al.*, 2009; Filatotchev *et al.*, 2007; Rhoades and Rechner, 2001; Lien *et al.*, 2005; Datta *et al.*,

2009). In the current study, strong support was found to indicate that board characteristics have a moderator effect on international diversification and a firm's financial performance. In terms of independent outside directors on the relationship between international diversification and a firm's financial performance, the results clearly indicate that international diversification has a negative effect on financial performance using measures for FATA, number of foreign subsidiaries and geographic diversification. Our results showed that increasing geographic diversification leads to worse financial performance when independent outside director representation is high. These results suggest that the interest of outside board members is aligned with a limited scope for geographic diversification. Similarly, increasing the ratio of foreign assets over total assets (FATA) leads to poor financial performance when independent outside director representation is high. Increasing the number of foreign subsidiaries also leads to worse financial performance when numbers of independent outside directors are high. In terms of board size, our results indicate that the number of foreign subsidiaries leads to better financial performance when board size is high. These findings are consistent with resource-based arguments, which propose that a larger board leads to better financial performance (Zahra and Pearce, 1989; Peng, 2004; Filatotchev *et al.*, 2001; Sherman *et al.*, 1998a; Lien *et al.*, 2005).

Two main theoretical contributions emerge from the empirical results. The findings of this study do not correspond with some researchers' findings, which propose that emerging multinationals do not provide better financial performance due to the liability of foreignness (Kim *et al.*, 2008; Hitt *et al.*, 1997). According to the findings of this study, international diversification leads to better financial performance according to market-based measures, but the effect is only marginally significant. It can be said that greater international diversification leads to better market value. Turkish multinational companies internalize for specific assets through outward FDI to decrease the effect of financial crisis. Therefore, the internalization efforts of Turkish FDI led to better financial performance.

The sample characteristics of the study reveal that most invested-in countries are Holland, Germany and Russia, contrary to the fact that emerging multinationals have expanded their operations more than other emerging economies in the same region. Turkey has given migration to some EU countries, especially Holland, Germany and UK. Ilhan-Nas *et al.* (2011) stated that China and Turkey are important home countries that are a source of immigration to developed economies. Therefore, Turkey's internationalization strategy may reveal characteristics of ethnic entrepreneurship. Turkey's outward FDIs may be expanded to not only cultural and ethnic ties but also Turkey's EU membership.

6.1 Implications

Our results reveal some important practical implications for managers in firms seeking to internationalize their operations. The internalization efforts of Turkish FDI have led to better financial performance in terms of market-based measures. As mentioned above, it can be said that the internalization efforts of FDI have had a solution for decreasing the effect of financial crisis.

International diversification has a negative effect on financial performance when independent outside directors' representation is high. Some researchers (Sherman *et al.*, 1998b; Baysinger and Hoskisson, 1990) suggested that outsiders do not have the experience and knowledge to effectively evaluate strategic alternatives and dedicate a little amount of time concerning the firm's strategic issue. Another perspective is the

managerialism perspective (Barle and Means, 1932), which proposed that decision-making control of the firm lies in the hands of the executive team or a powerful CEO; consequently, outside member's influence on the strategic decision of firm internationalization is limited. Tihanyi *et al.* (2003) and Musteen *et al.* (2009) stated that higher representation of independent outside directors in the board increases the odds of taking more risks in their international diversification efforts. Independent outside directors are even more interested in a firm's international strategy regarding the monitoring role of the board of directors.

Our results have stated that the interest of independent outside directors is aligned with lower-risk investment decisions. Unfortunately, the environmental turbulence and financial crisis may affect board of directors' composition and firm's internationalization decision. However, the strategic decision of firm internalization is rather in the hands of the family control in the Turkish context. Yildirim-Öktem and Üsdiken (2009) stated that independence practices in the board of firms affiliated to family business groups are perceived as "affiliated outside directors". Therefore, independence of independent outside directors in Turkey is interrogated by practitioners or CMBT. In the current study, the internalization of FDI leads to better financial performance when the board size is large. The larger board size which a moderator variable is provided, the wider shareholder value in Turkey is.

Implications for society: we can understand that the development of market-supporting institutions provides the support for entry to an emerging economy which is inefficient or incomplete markets and highly concentrated family ownership. The current study has investigated Turkish FDI flows between emerging economies or from emerging economies in developed economies.

6.2 Future studies

Our study is based on a sample of publicly listed firms in Turkey, and this restriction limits the generalizability of the findings. Future research using different samples should provide important additional insight and understanding on this topic. Although prior research has emphasized the role of boards of directors in an international context (Sanders and Carpenter, 1998), future research should further examine the interactive effects of these different governance mechanisms. These findings provide important implications for corporate governance and highlight the need for further research on the role of governance in firm internationalization. This study not only helps to understand how board characteristics affect the choice of international diversification decisions, but the results also allow to assess the performance implications of these choices for a particular period.

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