A Turkish Perspective of Islamic Corporate Governance for a Sustainable Financial Performance

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Abstract: This paper evaluates the role that integration of Islamic corporate governance has on the overall sustainable financial performance of a firm. Unlike the case with traditional corporate governance, Islamic institutions have a shariah supervisory board (SSB) which is tasked with the role of acting as the main supervisory, ensuring that the organization is observing the established shariah principles to guide its performance. The qualitative study methodology was adopted for the study to aid in comprehension of the underlying issues concerning adoption of Islamic corporate governance in a firm and the impact it has on sustainable financial performance. The study relied on qualitative research technique via sending questionnaires to 50 CEO and Board of director selected via snowball sampling. The questionnaires were meant to examine the concept of ICG and the impact it has on the sustainable financial performance of an organization in Turkey. The results indicate there is a strong positive relationship between ICG and sustainable financial performance of organizations in Turkey. The analysis further indicates that shariah governance and managerial ownership have a moderating role in the performance of the organization due to the confidence they offer to the shareholders. These findings will provide a roadmap to the Islamic firms when it comes to the integration of ICG in their operations to improve the sustainability of their financial performance. One limitation of this study is the limited nature of ICG in Turkey, whereby the concept of corporate governance is still in the developing stages.

Key words: Corporate Governance, Turkey, Islamic corporate governance, Sustainable financial performance, Shariah Supervisory Board, Firm’s financial performance.

I. Introduction

The model of Islamic banking which is characterized by the sharing of both profits and losses has been in existence for a long time in many parts of the world, whereby there is abhorrence on the imposition of interest. The core dissimilarity between Islamic banking and the other traditional forms of banking is not founded on the business practice but the principles guiding Islamic baking when it comes to the activities and reputation (Siswanti, et al., 2017). The values that are founded in Sharia are indicated not only in the activity of their transactions but also in the extent of its effect on the society. The additional way to differentiate between conventional and Islamic banking is the prevalence of sharia supervisory board (SSB) which is used as part of the internal governance structure of the entity while the traditional banking is deemed to only have a board of directors as the internal supervisory component (Siswani, et al., 2017). It thus becomes evident that reliable corporate governance in Islamic banking is vital to guarantee that the depositors will not suffer losses attributed to the fact it would be easier to “defraud” them than is the case with depositors in the conventional banks.

The realization of these attributes, therefore, makes it imperative to involve independent advisors, experts, and thorough supervision of the sharia related issues and their impact on the sustainable performance of an organization. Garas (2012) asserts that the fact Muslims do not exhibit the same authority on traditional financial entities, they sought to create the Islamic financial that are founded on sharia and that institutions are controlled by the SSB and BODs whose role is to guarantee their compliance with Sharia law. The presence of the SSB is deemed to be acting as the in-house religious council to ensure that the Islamic financial institutions become more sensitive towards all the activities linked to the social and environmental regulations (Jan, Marimuthu & Hassan, 2019).

According to Hashim, Mahadi & Amran, (2015), the fact that fact the term governance can be used to refer to the relationship existing between the government and its constituents could then lead to the assertion
that corporate governance relates to the corporations and its constituents. The definition, therefore, leads to the question of who is to be considered constituents of this corporation. Although numerous parties could support the position that a corporation should be having extensive corporate responsibility mandate, in most traditional conceptions of corporate governance the core relationships tend to be between the management and the shareholders.

In contrast, Islamic corporate governance predominantly has an extensive commission that has obligations that extend to customers, suppliers, employees, and competitors who embrace the spiritual and temporal needs of the Islamic community (Hashim, Mahadi & Amran, 2015). Corporate governance is among the fast emerging fields in the business sector that has a significant impact on the overall performance of an organization. It can be considered as cooperation between the top management, shareholders, and board of directors that exhibits an alignment towards the success of the organization (Siswanti, et al., 2017). Corporate governance could additionally be used to explain the existing relationship between the objective of the board of directors and shareholders.

Corporate governance is the means through which an organization is directed, controlled, and administered. The creation of corporate governance presents an overview of the distribution of roles as well as responsibilities and rights among the different stakeholders in an organization. They focus on the identification of the policies as well as practices and procedures that are meant to aid accurate decision making for the diverse corporate affair (Al-Suhaibani & Naifar, 2014). In this case, they offer the basis for an organization to use in developing its goals and adopting innovative methods that will be used in accomplishing the goals via the close assessment of the performance process.

Al-Suhaibani & Naifar, (2014), asserts that shareholders influence corporate governance since it suits their interests as employees, customers, creditors, government agencies, debtors, financial institutions, banks and the society at large. The main players when it comes to corporate governance include the shareholders, management as well as board of directors.

Globalization has encouraged an increase in competition, increasing the complexity and toughness of the business environment. It thus becomes evident that organizations are progressively working towards the improvement of performance that is reflected in their values. The values, in this case, are vital to the firm considering that the core objectives of organizations entail increasing their overall value. Every organization tends to focus on increasing its value which is seen in the overall prosperity of its stakeholders (Platonova, et al., 2018).

The fundamental aim of undertaking effective corporate oversight is to ensure that the management of an organization is acting in the best interests of the shareholders. It follows that corporate governance acts as a control mechanism, regulating and managing the company’s profile as a way of increasing their prosperity. It is additionally concerned with the perspectives of the investors concerning the benefits that are created by the organization’s leadership (Hasan, 2009).

II. Statement of the problem

In the contemporary business environment, corporate governance has become a major topic when examining the global corporate market. This research seeks to assess the overall impact of Islamic corporate governance on the performance of a firm, using the case study of Turkey. The rationale is informed by the fact that the Islamic banking sector exhibits an extensive scope in the Muslim nations as well as non-Muslim nations; an attribute that makes it imperative to examine the impact is Islamic corporate governance on the sustainable financial performance of organizations.

III. State of Corporate governance in Turkey

According to Akman, Mugan & Aksik, (2011), Turkey’s model of corporate governance along with the related reporting measures are in developing stage, there is very little literature of corporate governance and almost none relating to Islamic corporate governance in the country. This is the opposite of the case in the more industrialized countries that have more advanced corporate governance systems. The concept of Islamic corporate governance has been studied by a few researchers and scholars in Turkey yet there are no previous peer-reviewed studies on the impact of Islamic corporate governance on the sustainable financial performance of firms in Turkey (Akman, Mugan & Aksik, 2011). The attribute has been the major factors that shaped the present study, researching literature on the relationship between Islamic corporate governance and sustainable
financial performance of an organization to offer practitioners and authors foundation with which to base their policies and studies.

The underlying assertion in the contemporary business environment is the fact that Islamic banking institutions have responded extremely slowly to the modern idea of sustainability. The study is using Turkey to undertake an in-depth investigation since Turkey has some of the highest Islamic businesses and the results of this study could be generalized to other Islamic business institutions (Claessens & Yurtoglu, 2013). Additionally, the nature of the identified environmental, economic as well as social complexities that are faced by Islamic businesses in Turkey offers an indication that these businesses must improve on their sustainability practices and further adopt a sharia-based sustainability evaluation index (Claessens & Yurtoglu, 2013).

IV. Literature Review

Gürbüz, Aybars & Kutlu (2010) examined the effect of corporate governance on an organization’s financial performance in Turkey, considering the subject of institutional ownership. They relied on a sample of 164 annual observations of the real sector companies on the Istanbul stock exchange for 4 years between 2005 and 2008. They established that corporate governance measures served to enhance the performance of a firm in the course of the period under observation. Because of their analyses, institutional investors are deemed to focus on improving the financial performance of all organizations in cases where the effect on companies listed on the index is greater than the ones that have not been listed on the index.

Akman et al (2011) on the other hand sought to assess if foreign or family ownership impacts the performance of an organization differently in Turkey. They focused on the analysis of the prevalent association between the structure of ownership and performance of the firm for the publicly traded entities that are listed on the Istanbul stock exchange between 2005 and 2009. They determined that there is an adverse association between family ownership and the performance of a firm while foreign ownership exhibited a positive effect on the performance of the firm.

Sengur (2011) in her study assesses if effective integration of corporate governance tenets makes a difference when the performance of the business in Turkey. The outcomes of her study demonstrated that there is no significant difference when it comes to corporate governance index companies operating in Turkey when performance is evaluated based on return on investment as well as Tobin Q. further, her studies supported the assertion there is no significant difference in the context of the performance of corporate governance index when examining companies between the age of t0 to t1, whereby t0 is the preceding year of joining the corporate governance index while t1 is the first year being in the corporate governance index.

V. The importance of corporate governance

Effective corporate governance is essential when it comes to the creation of an environment that promotes efficiency as well as sustainable growth in all sectors of a company. The significance of corporate governance in Islamic institutions is characterized by the outcomes of a research that was undertaken by (Mollah & Zaman, (2015), which asserts that the implementation of corporate governance in Islamic institutions is meant to promote public confidence in these Islamic institutions. The execution of corporate governance in business institutions is therefore vital. The position is founded in the fact that corporate governance serves to not only create the presence of these business institutions alone but further preserve the reputation of the good name of these Islamic institutions in the eyes of the society considering there is no guarantee that an institution that has a name of sharia explicitly subject to and fully satisfies the principles of sharia (Safieddine, 2009). Thus for this objective to be realized, Islamic bans must guarantee the presence of excellent corporate governance structures as well as processes.

Numerous studies have signified the relevance of corporate governance when it comes to issues revolving around the performance of companies (Aggarwal, 2013), Haider et al., 2015). The implications of these studies have indicated that corporate governance exhibits a positive effect on the sustainable financial performance of a company. Sustainable financial performance is one of the most resourceful information sources for investors. A company’s profitability is one of the most reliable measures of sustainable financial performance. It follows that superior profitability coupled with strong long term development tends to impact the sustainability of the company. Further, according to Nawaiseh (2015), financial performance is indicated by the return of equity and return on investment since they exhibit a positive effect on the disclosures of an organization’s corporate social responsibility.
Islamic corporate governance sets its focus on the creation of the ways that economic agents, the legal systems besides the corporate governance could by social and moral values be founded on shariah laws. Proponents of ICG hold the position that all corporate, economic as well as business activities ought to be founded on an ethareligious model whose fundamental objective is the promotion of the wellbeing of individuals besides society as a whole (Hashim, Mahadi & Amran, 2015). In most ways, ICG advances that its objective is traditional corporate governance although embodying religious-based moral tenets of Islam.

Platonova, (2018) contend that financial performance is used about the financial condition of a company at a specific period and relates to the attributes of fundraising along with distribution of funds that are measured indicators of liquidity, capital adequacy, and long term value earned by the shareholders via integration of social, economic and environmental attributes in the business strategy. Sustainability on the other hand is seen to be the promotion of the triple bottom line of people-planet and profit.

When it comes to Islamic corporate governance, one of the common attributes is the fact that Islamic financial institutions tend to disclose more corporate sustainability disclosure’s in their annual financial reports that is the case with traditional businesses (Siswanti, et al., 2017). In ICG, the challenge imposed by the need to increasingly make disclosures of the company’s financial information is addressed by the organic participatory culture of the Shuratic process both in the context of the discursive body and the learning medium with the tenets of the world systems.

Islamic corporate governance is not significantly different from the traditional definition since it is used about the system by which organizations are directed and controlled with the sole objective of meeting the entity’s objective via protection of the rights and interests of the different stakeholders (Siswanti, et al., 2017). However, in the Islamic model, corporate governance introduces its unique attributes in comparison with the conventional model since it indicates a distinctive case of an extensive decision-making paradigm that employs the tenets of Islamic social scientific epistemology that is founded on the divine oneness of god. Further, examining corporate governance win this paradigm makes it very essential since it encourages integrity, honesty, accountability, transparency, and responsibility among all the stakeholders in an organization (Siswanti, et al., 2017)

When it comes to the Islamic banking sector, it is evident that the majority of the researchers have abided by the good management theory via dependence on the organization’s financial performance as the main dependent variable while business practices have been used as the independent variable (Hasan, 2009). Additionally, in the context of the effects, researchers have held the perspective of the stakeholder theory; assuming that there is a positive impact attributable to sustainable business practices on the performance of the organization in Islamic banking (Hasan, 2009).

VI. Theoretical perspective

According to Harrison & Wicks, (2013), stakeholder’s theory created in 1984 by Freeman, seeks to deal with the issue of what or who matters. During the proposition of this theory, Freeman divided the stakeholder model into two core parts; the direct as well as the indirect stakeholders. According to the stakeholder’s theory, the value of an organization tends to increase as the different stakeholders of the company are taken into consideration and their needs satisfied. An organization’s stakeholders could include the individuals or groups impacted by the company’s actions (Harrison & Wicks, 2013). In most instances, it encompasses the employees, customers, suppliers, financiers, trade associations, government bodies, communities, political groups, and the environment among others.

Haider & Iqbal (2015), in their article, argue that organizations address these different stakeholders via efficient sustainable measures coupled with their subsequent reporting. For example, local communities, employees and suppliers of the organization are taken into consideration via economically sustainable business measures besides reporting, as the economically sustainable measures tend to advocate for reporting of the minimum wage that is to be paid to the employees, enhancing investment in communities and further promoting and emphasizing on purchases made from the local suppliers (Abu-Tapanjeh, 2009). The different stakeholders could be addressed via environmental sustainability measures like the economic sustainable business practices management tends to advocate for entity’s compliance with the environmental laws that are created by the government, further expounding on the issues of waste management, recycling, energy consumption among others (Abu-Tapanjeh, 2009). Measures introduced to address the stakeholders as well as the subsequent reporting target the communities as well as environmental observers.
In the same way, the different stakeholders could be addressed via the introduction of socially sustainable business processes and management. The assertion is based on the fact that socially sustainable business dealings focus on elaborating on decent work processes, protection of human rights, safety, and occupational health (Haider & Iqbal, 2015). Overall, efficient sustainable business practices along with the subsequent reporting could address the interest of different stakeholders (Aggarwal, 2013). Besides, the stakeholders’ theory assumes that when multiple stakeholders have been addressed, it ends up improving the performance of the company.

Ahamed, et al., (2014) proposed two theories that include the slack resources theory and the good management theory when arguing on the issue of direction of causality. In the slack resource model, the direction of causality tends to address sustainable business practices as the dependent variable while the financial performance of the firm is deemed to be the independent variable. The argument, in this case, is that the firm that has slack resources could choose to spend more finance on their sustainability interventions (Mollah & Zaman, 2015). Conversely, the good resource management theory asserts that the direction of causality tends to treat both sustainable business practices as an independent variable and the financial performance of the firm as the dependent variable (Kramar, 2014).

The model contends that a sustainability intervention that is undertaken by an organization serves to promote its reputation in the minds of the different stakeholders, an attribute that ultimately aids them to gain more financial rewards (Kramar, 2014). In the context of impact, the tradeoff theory assumes that the connection between sustainable business interventions and financial performance of a firm is negative although the model assumes a positive impact of sustainable business practices on the overall financial performance of the firm.

Concerning the Islamic banking industry, it is evident that most of the studies have relied on the good management theory whereby they use the bank’s financial performance is the dependent variable while sustainable business practices have been used as the independent variable (Kramar, 2014). Additionally, when it comes to the issue of impact, it is evident that researchers have been consistent with the perspective of the stakeholder’s theory and make the presumption that positive impact attributed to the sustainable business measures on an organization’s financial performance in the Islamic banking sector (Harrison & Wicks, 2013). Based on the available literature, the study abides by the tenets of the good performance model in the case of the direction of causality while borrowing from the stakeholder’s theory when addressing the issue of impact on the enduring relationship.
Theoretical model

Islamic corporate governance

Sustainable business practice

Shariah Governance

Managerial ownership

Firm’s sustainable financial performance

governance has on the sustainability of the financial performance of an organization, Turkey which is a state that has predominantly adopted governance laws being the case study. This study implies that management and practitioners are going to have a platform with which they can employ in safeguarding and expediting the established targeted sustainable business interventions that will serve to enhance the sustainability of their financial performance. Thus, the study will be valuable for the experts of the global Islamic sector on matters of policy formulation.

VII. Participants

The participants in this were 50 CEO and members of board of directors for firms in Turkey who are directly responsible for the execution of corporate governance as well as financial performance of their firms. These participants had to have held these positions for not less than three years during the period 2015 and 2019. The underlying eligibility criteria employed in selection of these participants were having been a member of board of directors CEO, a manager having at least 3 years’ experience in these position that was attained in the course of the period 2015 and 2019. When it comes to selection of the participants the researchers make sure that the individuals are knowledgeable of the issue at hand.

VIII. Research Method and Design

During this qualitative multiple case study research, focus was to capture the accounts of human lived experiences from individual’s perspective. Babbie (2010) asserts that qualitative case study design was selected since it offers an examination of the phenomenon under study, thus allowing the researcher to investigate the specific as well as complex issue in its real world context. The qualitative research methodology was adopted for this study since it offers the researcher the process that is appropriate for gathering the relevant subjective description of an issue or event from their informed perspective (Merriam & Tisdell, 2015). The focus of this study was to examine the underlying impact of Islamic corporate governance on the sustainable financial performance of firms in Turkey. The method involved sending questionnaire to a small number of participants, in this case CEO and Directors of firms in Turkey that had operated in the country for more than 10 years. These participants were selected using snowball sampling since it ensured only the participants with sufficient information on the question at hand were sampled.
IX. The research method

The goal was to examine whether Islamic corporate governance contribute to the sustainable financial performance of a firm, using the case study of entities operating in Turkey. Therefore, a qualitative methodology was appropriate for gathering information, meanings as well as interpretations. Qualitative research has been defined as a method that is employed to aid comprehension of individual and groups perspective towards a specific human or social challenge (Merriam & Tisdell, 2015). Through qualitative research, researchers manage to explore the meanings of human experiences, revealing the qualitative instead of quantitative attributes in these human behaviors and experiences.

X. The sample

To get a clear picture of the state of Islamic governance and the impact it has on the sustainable performance of a firm, the researcher used purposive sampling to recruit sufficient participants with the required knowledge as well as expertise. Purposive sampling is one of the strategies by which samples collected include specific groups or parts of a population. The reasoning behind use of purposive sampling is the necessity to only use participants who had specific knowledge of Islamic corporate governance in Turkey. Further, these participants had to have specific experience and knowledge of ways of integrating Islamic corporate governance in an organization as well as its impact on the overall financial performance of their firm.

The method involved sending questionnaire to a small number of participants, in this case CEO and Directors of firms in Turkey that had operated in the country for more than 10 years. These participants were selected using snowball sampling since it ensured only the participants with sufficient information on the question at hand were sampled. In thus study 100 firms operating in Turkey were selected and through snowball sampling, 60 respondents who satisfied the eligibility criteria were selected.

XI. Results

The questionnaires that were sent to these respondents presented an assortment of themes and inclinations that are related to the rolling out of Islamic corporate governance in Turkey. The main themes that were under assessment in the questionnaire included:

XII. The concept of corporate governance

Analysis of the responses from these questions, the participants deemed corporate governance as the desire to ensure a balance has been created between a firms shareholder interest, those of the senior management executive, suppliers customers, the community among others. Additionally, it became apparent that the prevailing system of corporate governance that is adopted by firms in Turkey is dependent on the size of the organization whereby the small and medium size firms relied on the international governance system mechanism. Other sought to adopt internal mechanisms customized to their needs and created by experts and further approved by the board of governors on behalf of the stakeholders. Integration of corporate governance principles in a firms act was one of the attributes that was accepted by all the stakeholders whereby the firms declared in their annual report the degree of abiding of the governance principles.

XIII. Nature and purpose of the organizations

While some respondents indicated that their firms were emphasizing on the integration of ICG in their operations, 90% indicated they had not explicitly indicated their corporate governance mechanisms as being based on Islamic corporate governance although it has been informed on ICG tenets as they sought to protect and safeguard diversity in their workforce and environment. Additionally, 85% of the respondents indicated that considering that most of their employees are Muslim and that they are working in a predominantly Muslim nation, their overall working environment and social tenets allow them to become increasingly proactive, practical as well as efficient in delivering their objectives by observing ICG tenets.

XIV. The Islamic role of shareholders

On the role that is exerted by stakeholders when it comes to application of ICG, the respondents indicated that as is the case in Turkey, all companies have been integrating the principles of governance that have been established by the capital market board since it is very clear of the fact that shareholders possess the
right of information and can make follow-up of its application. The board of directors that is selected on behalf of the shareholders plays an integral role when it comes to application of governance policies. Transparency as well as accountability of the ICG has been indicated as the main ways in which the interests of the shareholders are advanced towards integration of ICG.

XV. The composition and role of Islamic based boards

When it comes to the assessment of whether the board is attaining the tasks founded on ICG, the respondents were in agreements that the boards of their firms were realizing the set objectives. On the question of whether the respondents felt that the board had an optimal balance of experts needed for creation of an Islamic cultural-based successful organization, they indicated that their firms were working with experts in the field and ensuring they remained updated on the changes in the industry.

XVI. Discussion

The paper assessed the responses from managers and members of the board of directors of firms in Turkey, evaluating their understanding of the role of adoption of Islamic corporate governance and the sustainable financial performance of a firm. The analysis of questionnaire responses reveals there is a positive relationship between the adoption of sustainable practices and the overall financial performance of the firm, an indication that the management, as well as stakeholder performance, is essential. The themes are in line with the assertion that the performance of the management as well as shareholders is vital for the success of a company. The management as well as shareholders has accepted the fact that the creation of sustainable business practices by their firms adds financial returns to their portfolios.

Conversely, the relationship between sustainable business measures and the financial performance of the firm shows that market performance is not significant. Further examination seeking to comprehend why the market is reluctant for their firms investing in sustainable practices, the study sought to analyses the moderating role of managerial ownership and shariah governance. Overall, it has been established that entrenchment of the management, as well as shariah governance supervision, exerts a positive impact on the market shareholders of Islamic banks for their sensitivity to the issue if sustainable business practices and the overall performance of the firm.

The attribute has been occasioned by the high management entrenchment that guarantees the integration of sustainable practices that positively impact the financial performance of the business. Further, it has been established that shariah corporate governance gives confidence to the market shareholders in obtaining superior financial returns via strong governance. This is occasioned by the fact that the shariah governance based on the SSB sizes allows professionals like economists even without much religious knowledge to sit on the board and offer expert perspectives on technical issues like sustainable financial performance.

XVII. Conclusion

The study commenced with the sole objective of examining the impact that Islamic corporate governance has on the sustainability of a firm's financial performance, using Turkey as a case study. Overall, the corporate governance model result in an organization engaging in more sustainable practices when the SSB has more scholars as well as people on its board. The study highlights the fact that the entrenchment of ICG in an organization tends to improve its overall financial performance.

XVIII. Recommendations

Islamic corporate governance is an integral component for the emerging world as well as the corporate structure of an organization in facilitating the transfer skills, training, controlling as well as financial management that will strengthen the monitoring, regulations and evaluation. Through assessment of integration of ICG, it will promote the reputation of corporate as well as help the employees and management of the firm since it established the rules and procedures that protect both the employee and employer.

XIX. Contributions

The results of this study will offer insight to diverse stakeholders and policymakers of the Islamic organization to integrate the necessary sustainability measures in their business models and further addressing
the balanced role that ICG acts as a connection between sustainable business practices and the overall financial performance of an organization.

**Limitations and Suggestions for Future studies**

The study used Turkey as the core case study for studying the existing relationship between ICG and sustainable financial performance of a firm from an Islamic perspective. It however follows that comprehensive understanding of this connection would be better realized if other countries that have increasingly entrenched the ICG model in their operations are used. This because the concept of corporate governance is a novel approach in Turkey that is still developing and thus does not offer reliable information to be used and integrated by other stakeholders.

**References**


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