

Role of Corporate Governance Awareness in Shaping Investment Behaviour: A Mediation Analysis

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Abstract

With investor knowledge serving as a mediator, this research aims to comprehend the effect of corporate governance policies on investment choices. Financial reporting, auditing standards, disclosure procedures, and the board of directors' responsibilities are all parts of corporate governance that have an impact on investment choices. Firms' ESG information is vital in their financing choices, which further emphasizes the necessity for strong governance structures in light of the growing importance of ESG aspects. This research examines the characteristics impacting the investing behavior of 385 individual investors, chosen by purposive selection. A systematic online questionnaire was circulated using Google Forms to gather the main data. Respondents' knowledge of corporate governance procedures, views on ESG considerations, and methods of decision-making were all recorded in the questionnaire. The correlations between corporate governance procedures, degrees of awareness, and investment choices were investigated by using Structural Equation Modeling (SEM) in conjunction with regression data analysis. According to the results, investor knowledge mediates the relationship between corporate governance procedures and financial investment choices. To be more specific, investors' faith in investment options grows, their sense of investment risk diminishes, and they make better, more educated choices as they learn more about governance processes. Findings from this research stress the need of openness, board supervision, and thorough disclosure in attracting investors. In order to attract knowledgeable investors and promote long-term market development, these evident results highlight the need of realistic governance norms and investor education

Keywords:

Introduction:

Policy guidelines for corporate governance provide standards for audits, transparency, financial reporting, and board structure; these standards have a substantial impact on investment decisions (Shleifer & Vishny, 1997; OECD, 2015). Incorporating ESG (environmental, social, and governance) factors is a result of the rising tide of responsible investment. Investors are placing a greater emphasis on responsible investment, which has led to a rise in the importance of ESG factors (Gompers et al., 2003; Friede et al., 2015). Credible and transparent government reduces information asymmetry and boosts trust, which in turn influences investment decisions for the better (Healy & Palepu, 2001). Good corporate governance inspires trust among investors, but poor governance makes them wary of putting money into the business (La Porta et al., 2000). According to Black (1986), individual investors are vital to the market's stability, price discovery, and liquidity. Their investment decisions are impacted by both monetary and non-monetary factors, including market dynamics, personal risk preferences, and company governance systems (Barber & Odean, 2001). More and more individuals are paying attention to ESG (environmental, social, and governance) concerns, and that has led to an increase in socially responsible investing (Bollen, 2007). Financial reports, particularly certified financial records, serve as a roadmap for individual investors as they make investment decisions. We need transparent and reliable data in order to make informed decisions. Investors' responses to corporate governance rules and, therefore, their investment decisions are strongly correlated with their level of knowledge about these processes (Merton, 1987). Investing Decisions and Business Ethics Policies: How Familiarity Level Mediates the Correlation Investor knowledge mediates the relationship between governance practices and investment decisions (Yermack, 1996). One indicator of good governance is the degree to which shareholders and other interested parties are aware of a company's financial health, risk management practices, and ESG projects. Investors may better understand and assess the impact of governance on their investment decisions as their knowledge grows, say Fama and Jensen (1983). Companies that adhere strictly to governance standards, such as transparent reporting and reasonable auditing standards, are often seen as having a lower risk of loss by investors. Bebchuk et al. (2009) states that this perspective positively affects their investing decisions. On the other side, investors may make bad decisions due to a lack of understanding of governance signals caused by inadequate information (Bushee & Noe, 2000).

Significance of the Study

This study intends to investigate the impact of corporate governance on investment decisions by positing that investors' knowledge mediates this relationship. The main purpose of the study is to fill in the gaps in our understanding of how institutional investors' investment decisions are influenced by financial statements, auditing standards, disclosure mandates, and the incorporation of ESG factors (68% of whom rank governance factors as very important). Emphasis is placed on the role of the board of directors. This study's significance lies in the fact that improved corporate governance processes and information may lead to wiser investment choices. This research highlights the mediating function of awareness, which might encourage corporations to adopt more transparent and comprehensive governance procedures (Claessens & Yurtoglu, 2013). A wider range of well-informed investors could be interested as a result. Businesses and investors benefit from the study because it helps design regulations that promote a transparent and long-term investment environment (Gillan, 2006). The literature is replete with examples of how corporate governance affects investing decisions. Reducing information asymmetry and agency costs, there is evidence that good governance measures may attract institutional and individual investors. According to Healy and Palepu (2001) and La Porta et al. (2000), these standards include complete disclosures, impartial audits, and open and honest financial reporting. According to research (Gompers et al., 2003; Claessens & Yurtoglu, 2013), investors are more likely to put their money into companies that have strong governance systems. Both the number and quality of corporate governance procedures are taken into account when these judgments are being made. Recent studies have shown that individual investors are increasingly considering ESG factors when making investment decisions. A person's degree of knowledge usually determines their behavior as an investor, whether they prioritize short-term swings or seek for longer-term rewards. When investors have all the facts they need to understand the complex world of corporate governance, they can make more educated investment decisions. While it comes to environmental, social, and governance (ESG) issues, other studies have shown that investors could reduce the risks connected with certain governance practices (Friede et al., 2015; Claessens & Yurtoglu, 2013). This research found that investors' knowledge levels moderated the behaviors of investors with regard to corporate governance and their own investment decisions.

Objectives of the Study

- 1) To know the impact of CG practices on investment decisions among individual investors.
- 2) To understand the role of the board of directors in influencing CG practices and its effect on investment decisions.
- 3) To examine the mediating effect of investor awareness, particularly regarding ESG factors, on the relationship between corporate governance (CG) practices and individual investment decisions.
- 4) To analyse the extent to which individual investors' awareness and perception of ESG factors influence their investment choices.

Hypotheses of the study:

- H1: CG practices have a significant positive impact on investment decisions among individual investors, with ESG awareness acting as an influential mediating factor.
- H2: The board of directors significantly impacts CG practices and investment decisions.
- H3: Investor awareness levels mediate the relationship between CG practices and investment decisions.
- H4: Higher awareness of ESG factors positively influences individual investors' decisions to Invest in companies..

Sampling Design:

For this survey, we used a purposive sample strategy, which entails selecting individual investors with expertise who are also stock market participants and who are knowledgeable with auditing standards, ESG considerations, financial statements, and corporate governance procedures. In order to successfully satisfy investor expectations, this method makes sure that all parties involved are able to assess whether or not open and accountable governance processes are necessary. In keeping with the aims of the research, our method sought to collect a central dataset from participants themselves (Etikan et al., 2016). Following the recommendations for the survey, 385 individual investors were chosen as a sample size. This number is enough to reach a 95% confidence level with a 5% margin of error (Cochran, 1977). Findings on the individual's behavior may be obtained from this sample size.

Data Collection

An organized survey was designed to collect information on important factors like corporate governance practices (such as auditing standards, disclosure policies, and financial statements), investment choices (the dependent variable), ESG factors (environmental, social, and governance), the board of directors' function (the mediator), and the degree of knowledge about certain corporate governance practices (the mediating variable). Recent studies have used this methodology to study the effects of corporate governance frameworks that incorporate AI, the impact of boards of directors on individual investors, and ESG practices that are shared with seasoned investors. The convenience and efficacy of online data collecting has made it possible for respondents to provide insightful answers, which in turn has improved the quality of analysis (Dillman, 2011).

Data Analysis

Analyzing the collected data using statistical methods allows us to understand the relationships between CG practices, awareness levels, and investment decisions. The demographics of the Respondents were better understood by the computation of descriptive statistics, such as mean, median, mode, and standard deviation. The hypothesis that one's degree of knowledge mediates the connection between CG practices and investment decisions was examined using regression analysis (Baron & Kenny, 1986). Hair et al. (2010) used Structural Equation Modelling (SEM) to examine the direct and indirect effects of the board of directors on investment decisions via CG practices and levels of awareness. A literature review on CG practices and investment decisions reveals that investors' knowledge levels mediate the relationship between the two. This section of the research delves into the following topics: disclosure rules, auditing standards, financial statements, the board of directors, ESG issues, and investment alternatives. These problems were discovered all across the literature review. We polled investors on the relative importance of these traits across all attributes.

Table 1: Research Model Estimations

Research Variables		Loading	AVE	CR	Alfa	rho_a
ID	<i>Investment Decisions</i>		0.568	0.867	0.807	0.814
ID1	Awareness regarding need & importance of corporate governance (N&I)	0.853				
ID2	Awareness regarding important financial statements of firms (FS)	0.754				
ID3	Awareness regarding the role of the board of directors in a firm (BoD)	0.730				
ID4	Awareness regarding the importance of internal & external audits (AUD)	0.762				
ID5	Awareness level with respect to ESG	0.667				
DR	<i>Disclosure Requirements</i>		0.606	0.860	0.787	0.814
DR1	Awareness regarding annual reports of firms.	0.827				
DR2	Awareness regarding the rights of investors.	0.827				
DR3	Awareness regarding important documents to be read before investing.	0.753				
DR4	Awareness regarding disclosure relating to corporate governance.	0.700				
FS	<i>Financial Statements</i>		0.585	0.876	0.823	0.825
FS1	Awareness regarding the sources of financial statements of firms.	0.755				
FS2	Awareness regarding financial reporting standards to be followed.	0.763				
FS3	Awareness regarding the financial reports of holding firms and subsidiaries.	0.748				
FS4	Awareness regarding important financial parameters to be examined.	0.788				
FS5	Awareness regarding tools to examine firms' financial performance.	0.771				
BOD	<i>Board of Directors</i>		0.635	0.874	0.808	0.814
BOD1	Awareness regarding board composition & its independence.	0.841				
BOD2	Awareness regarding shareholding guidelines for the board of directors.	0.811				
BOD3	Awareness regarding board meetings and their frequency.	0.741				
BOD4	Awareness regarding the performance measures of the board of directors.	0.785				
AR	<i>Auditing Requirements</i>		0.694	0.900	0.852	0.855
AR1	Awareness regarding the role of auditors (internal & external) in a firm.	0.858				
AR2	Awareness regarding the importance of the statutory audit of firms.	0.774				
AR3	Awareness regarding auditors' remuneration & benefits.	0.843				
AR4	Awareness regarding the components in an auditor's report.	0.853				
ESG	<i>Environment and Social Governance</i>		0.760	0.867	0.807	0.895
ESG1	Awareness regarding the importance of ESG.	0.883				
ESG2	Awareness regarding the impact of firms' operations on the environment.	0.846				
ESG3	Awareness regarding the impact of business operations on employees, customers, and society.	0.862				
ESG4	Awareness regarding steps taken by firms to mitigate ESG risks.	0.896				

Source: Primary Work

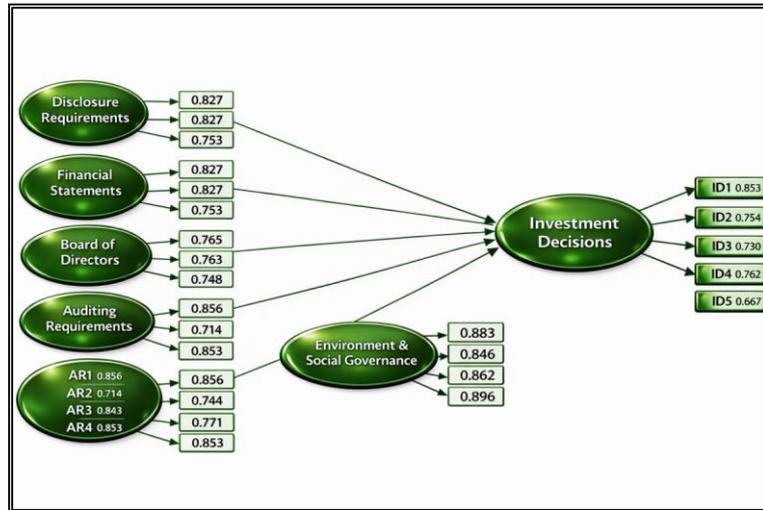


Figure 1, Value of rho_a Source: Smart PLS results

The above figure 1 and table 1, depicting the value of rho_a, serve as quality criteria that clearly indicate the variables' reliability and validity, with the minimum value of rho_a for all variables exceeding 0.7. The variables' rho_a values, i.e., investment decisions (0.815), environment, and social governance (0.895), board of directors (0.814), financial statements (0.825), auditing requirements (0.855) and disclosure requirements (0.814) are well above the minimum value of 0.7, which is a clear indication that variables are reliable and valid to proceed to the final prediction.

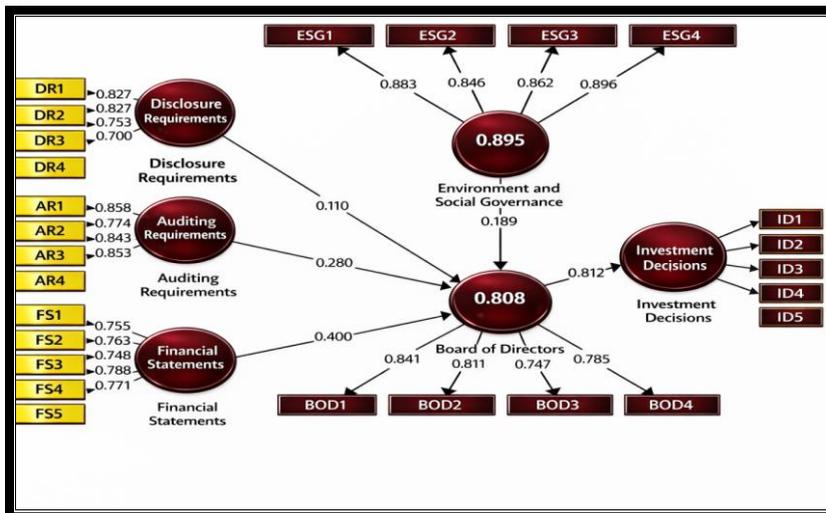


Figure 2: Value of Cronbach's Alpha (Source: Smart PLS results)

The above Figure 2 and Table 1, which depict the value of Cronbach's alpha, with the minimum value for all variables being greater than 0.7, estimate internal consistency, indicating that Awareness attributes are closely associated with their reflective qualities. The variables; Cronbach alpha values, i.e., investment decisions (0.807), environment and social governance (0.895), board of directors (0.808), financial statements (0.823), auditing requirements (0.852), and disclosure requirements (0.787) are well above the minimum value of 0.7, which is a clear indication that variables are reliable and valid to proceed with the final prediction.

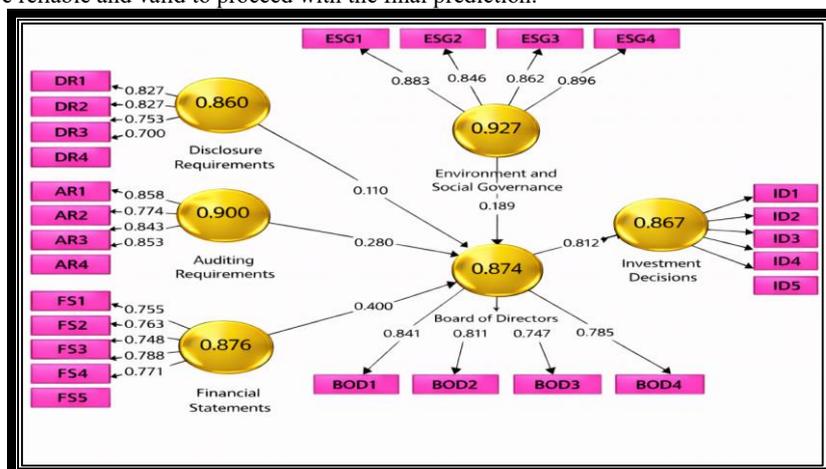


Figure 3, Value of Composite Reliability (Source: Smart PLS results)

Finally, the conclusion that awareness traits are closely matched to the structural equation model is supported by the composite reliability values shown in Figure 3 and Table 1, where all variables have minimum values larger than 0.7. associated. There is no doubt that the variables are valid and reliable to move forward with the final prediction because their composite reliability values 0.867 for investment decisions, 0.927 for environment and social governance, 0.874 for the board of directors, 0.876 for financial statements, 0.900 for auditing requirements, and 0.860 for disclosure requirements are significantly higher than the minimum value of 0.7.

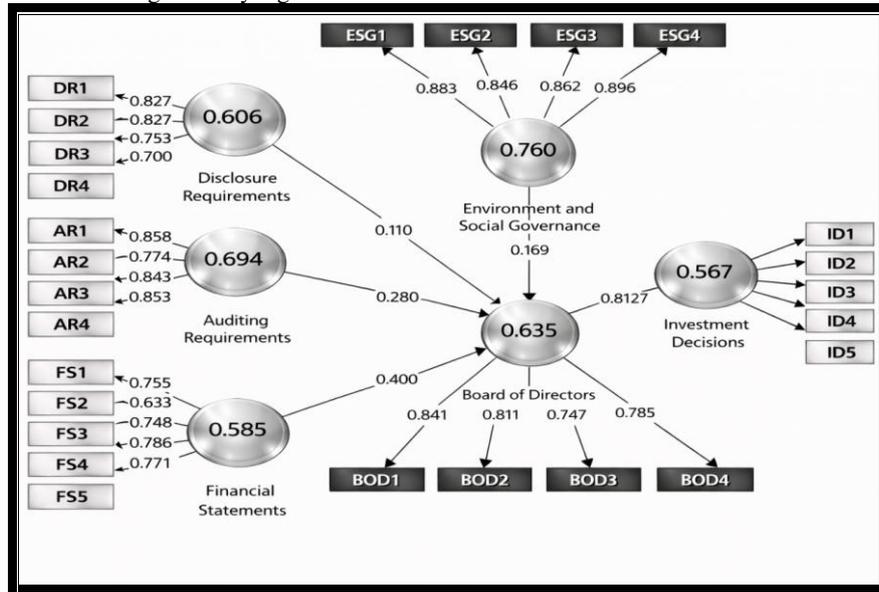


Figure 4: Value of Average Variance Explained
Source: Smart PLS results

Figure 4 and table 1 show the average variance explained, with all variables having a minimum value greater than 0.5. This provides an estimate of how well the research constructs capture the amount of variance explained relative to the degree of measurement error variance. With individual variable items/statements loadings above 0.5, it is evident that the variables are reliable and valid for final prediction. The variables with average variance explained values, such as investment decisions (0.567), environment and social governance (0.760), board of directors (0.635), financial statements (0.585), auditing requirements (0.694), and disclosure requirements (0.600), are well above the minimum value of 0.5.

Table 2: Research Model Estimations

Research Variables		Outer VIF	Effect Size	R ²
ID	Investment Decisions			0.654
ID1	Awareness regarding need & importance of corporate governance (N&I)	2.073		
ID2	Awareness regarding important financial statements of firms (FS)	1.533		
ID3	Awareness regarding the role of the board of directors in a firm (BoD)	1.565		
ID4	Awareness regarding the importance of internal & external audits (AUD)	1.764		
ID5	Awareness level with respect to ESG	1.395		
DR	Disclosure Requirements		0.159	
DR1	Awareness regarding annual reports of firms.	1.691		
DR2	Awareness regarding the rights of investors.	1.667		
DR3	Awareness regarding important documents to be read before investing.	1.665		
DR4	Awareness regarding disclosure relating to corporate governance.	1.475		
FS	Financial Statements		0.175	
FS1	Awareness regarding the sources of financial statements of firms.	1.712		
FS2	Awareness regarding financial reporting standards to be followed.	1.741		
FS3	Awareness regarding the financial reports of holding firms and subsidiaries.	1.661		
FS4	Awareness regarding important financial parameters to be examined.	1.870		
FS5	Awareness regarding tools to examine firms' financial performance.	1.687		
BOD	Board of Directors		0.216	0.750
BOD1	Awareness regarding board composition & its independence.	1.883		
BOD2	Awareness regarding shareholding guidelines for the board of directors.	1.900		
BOD3	Awareness regarding board meetings and their frequency.	1.637		
BOD4	Awareness regarding the performance measures of the board of directors.	1.830		
AR	Auditing Requirements		0.315	
AR1	Awareness regarding the role of auditors (internal & external) in a firm.	2.214		
AR2	Awareness regarding the importance of the statutory audit of firms.	1.648		
AR3	Awareness regarding auditors' remuneration & benefits.	2.093		
AR4	Awareness regarding the components in an auditor's report.	2.068		
ESG	Environment and Social Governance		0.201	
ESG1	Awareness regarding the importance of ESG.	2.684		
ESG2	Awareness regarding the impact of firms' operations on the environment.	2.205		
ESG3	Awareness regarding the impact of business operations on employees, customers, and society.	2.482		
ESG4	Awareness regarding steps taken by firms to mitigate ESG risks.	2.941		

Source: Primary work

There does not seem to be any multicollinearity among the variables, as seen in Table 2 above, where the lowest outer VIF (variance inflation factor) is 1.395 and the maximum is 2.941.

Investment Decisions is the dependent variable in this study, while the independent variables are the things that influence it. This further implies that there is no standard-method bias in the study model and that the items for all independent variables are strong. The fitness independent research factors also shown moderate to substantial impacts, with values ranging from 0.31 to 0.15 when analyzed using effect size (f^2).

Table 3: HTMT Discriminant Validity

Research Variables	(ID)	(DR)	(FS)	(BOD)	(AR)	(ESG)
Investment Decisions (ID)						
Disclosure Requirements (DR)	0.347					
Financial Statements (FS)	0.501	0.387				
Board of Directors (BOD)	0.601	0.429	0.467			
Auditing Requirements (AR)	0.741	0.745	0.301	0.502		
Environment and Social Governance (ESG)	0.713	0.623	0.457	0.605	0.531	

Source: Smart PLS results

Discriminant validity (HTMT), as shown in Table 3 above, guarantees that the reflective concept of the research interacts optimally with its own items. In addition, with all values below 0.9, the awareness variables' interval values show that they are highly connected and predict investment choices.

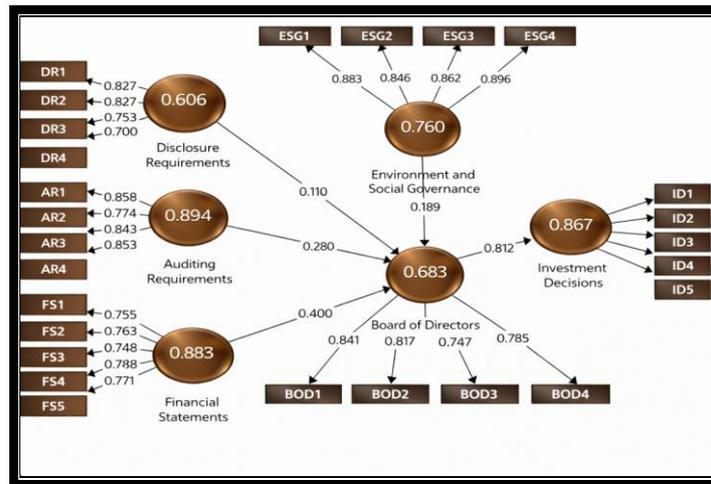


Figure 5: Value of R Square Adjusted Source: Smart PLS results

Table 4: Research Variables Associations

Confirmed Hypothesis	Coefficients	p-value	Observation
H: Disclosure Requirements → Board of Directors	0.110	0.091**	Accepted
H: Financial Statements → Board of Directors	0.400	0.004*	Accepted
H: Auditing Requirements → Board of Directors	0.280	0.055**	Accepted
H: Environment and Social Governance → Board of Directors	0.189	0.040*	Accepted
Mediation Variable	Coefficients	p-value	Observation
H: Board of Directors → Investment Decisions	0.805	0.000*	Full Effect

Source: Smart PLS results, $p^* < 0.05$, $p^{**} < 0.1$

Figures 5, 6, and 7 along with Table 2 clearly show that the proposed model was evaluated and found to fit the research. The research shows that the extracted independent variables—environmental and social governance, board of directors, financial statements, auditing requirements, and disclosure requirements—have a direct binding effect on investors' awareness level when it comes to making final decision-making. Figures 5, 6, and 7 as well as Table 2 indicate that there were quantifiable positive direct and indirect effects of model fitness, with $t > 1.96$ and $p < 0.05$ and 0.1 for all the independently produced constructs and hypotheses. The following factors have been determined to have a direct influence on the Board of Directors: Disclosure Requirements ($t = 2.859$; $p = 0.091^{**}$), Financial Statements ($t = 2.905$; $p = 0.004^*$), Auditing Requirements ($t = 1.925$; $p = 0.055^*$), and Environment and Social Governance ($t = 2.056$; $p = 0.040^*$). Lastly, the Board of Directors functions as a mediator for investment decisions, with a maximum described variance of ($R^2, 0.654$).

Conclusion

While "importance" means being able to predict which independent constructions have been very effective in regard to dependent constructs, "performance" is the average score in this context. The board of directors is the most important part, followed by auditing requirements, financial statements, disclosure statements, ESG, and social and environmental governance. We developed an awareness model for investment decisions using this IPMA technique (figure), which clearly indicates the individual components. A comprehensive dataset was acquired from 385 individual investors using a targeted sampling technique and a well-structured questionnaire. The study's validity and reliability were enhanced by this methodological technique, which ensured that educated respondents supplied meaningful insights. Factors like corporate governance processes and levels of knowledge may be better understood by examining the data, which could impact investment decisions.

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